UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

(Mark One)

☒ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended March 31, 2021

OR

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from __________ to ________________

Commission File Number: 001-38371

One Stop Systems, Inc.
(Exact Name of Registrant as Specified in its Charter)

Delaware	**33-0885351**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

2235 Enterprise Street #110

Escondido, California 92029

(Address of principal executive offices including Zip Code

(760) 745-9883

(Registrant's telephone number, including area code)

(Former Name, former address and former fiscal year, if changed since last report)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading symbol	Name of exchange on which registered
Common Stock, $0.0001 par value per share	OSS	The Nasdaq Capital Market

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes ☒ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	☐	Accelerated filer	☐
Non-accelerated filer	☒	Smaller reporting company	☒
		Emerging growth company	☒

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

As of April 30, 2021, the registrant had 18,510,415 shares of common stock (par value $0.0001) outstanding.

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PART 1 – FINANCIAL INFORMATION

Item 1. Financial Statements.

ONE STOP SYSTEMS, INC. (OSS)

UNAUDITED CONSOLIDATED BALANCE SHEETS

	Unaudited March 31, 2021	December 31, 2020
ASSETS		
Current assets		
Cash and cash equivalents	$ 19,614,315	$ 6,316,921
Accounts receivable, net	5,733,675	7,458,383
Inventories, net	9,548,960	9,647,504
Prepaid expenses and other current assets	889,043	655,708
Total current assets	35,785,993	24,078,516
Property and equipment, net	3,368,959	3,487,178
Deposits and other	45,136	81,709
Deferred tax assets, net	3,638,073	3,698,593
Goodwill	7,120,510	7,120,510
Intangible assets, net	498,357	662,257
	$ 50,457,028	$ 39,128,763
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable	$ 2,735,695	$ 976,420
Accrued expenses and other liabilities	3,585,102	3,481,444
Current portion of notes payable, net of debt discount of $292 and $2,047, respectively (Note 7)	1,190,065	1,365,204
Current portion of related party notes payable, net of debt discount of $962 and $6,726, respectively (Note 7)	50,685	199,943
Current portion of senior secured convertible note, net of debt discounts of $165,731 and $256,242, respectively (Note 7)	2,288,814	1,789,212
Total current liabilities	9,850,361	7,812,223
Senior secured convertible note, net of current portion and debt discounts of $0 and $14,107 (Note 7)	136,364	531,347
Paycheck protection program note payable (Note 7)	1,499,360	1,499,360
Total liabilities	11,486,085	9,842,930
Commitments and contingencies (Note 9)		
Stockholders' equity		
Common stock, $.0001 par value; 50,000,000 shares authorized; 18,502,902 and 16,684,424 shares issued and outstanding, respectively	1,850	1,668
Additional paid-in capital	40,652,472	30,758,354
Accumulated other comprehensive income	37,159	287,547
Accumulated deficit	(1,720,538)	(1,761,736)
Total stockholders' equity	38,970,943	29,285,833
	$ 50,457,028	$ 39,128,763

See accompanying notes to consolidated financial statements

ONE STOP SYSTEMS, INC. (OSS)

UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS

	For the Three Months Ended March 31,	
	2021	**2020**
Revenue	$ 13,315,752	$ 13,359,637
Cost of revenue	8,882,968	9,963,950
Gross profit	4,432,784	3,395,687
Operating expenses:		
General and administrative	2,157,619	2,514,065
Marketing and selling	1,167,901	1,189,351
Research and development	832,233	1,203,425
Total operating expenses	4,157,753	4,906,841
Income (loss) from operations	275,031	(1,511,154)
Other income (expense), net:		
Interest income	5,300	24,637
Interest expense	(149,982)	(68,784)
Other income (expense), net	(28,629)	(8,029)
Total other income (expense), net	(173,311)	(52,176)
Income (loss) before income taxes	101,720	(1,563,330)
Provision (benefit) for income taxes	60,522	(467,298)
Net income (loss)	$ 41,198	$ (1,096,032)
Net income (loss) per share:		
Basic	$ 0.00	$ (0.07)
Diluted	$ 0.00	$ (0.07)
Weighted average common shares outstanding:		
Basic	17,348,164	16,332,898
Diluted	18,642,061	16,332,898

See accompanying notes to consolidated financial statements

ONE STOP SYSTEMS, INC. (OSS)

UNAUDITED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

	For the Three Months Ended March 31, 2021	2020
Net income (loss)	$ 41,198	$ (1,096,032)
Other comprehensive loss:		
Currency translation adjustment	(250,388)	(55,567)
Total other comprehensive loss	(250,388)	(55,567)
Comprehensive loss	$ (209,190)	$ (1,151,599)

See accompanying notes to consolidated financial statements

ONE STOP SYSTEMS, INC. (OSS)

UNAUDITED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

For the Three Month Period Ended March 31, 2021

	Common Stock						
	Shares	Amount	Additional Paid-in-Capital	Noncontrolling Interest	Accumulated Other Comprehensive income	Accumulated Deficit	Total Stockholders' Equity
Balance, January 1, 2021	16,684,424	$ 1,668	$ 30,758,354	$ -	$ 287,547	$ (1,761,736)	$ 29,285,833
Stock-based compensation	-	-	438,394	-	-	-	438,394
Exercise of stock options, RSU's and warrants	321,472	32	278,936	-	-	-	278,968
Proceeds from issuance of stock, net of issuance costs of $778,810	1,497,006	150	9,221,040	-	-	-	9,221,190
Taxes paid on net issuance of employee stock options	-	-	(44,252)	-	-	-	(44,252)
Currency translation adjustment	-	-	-	-	(250,388)	-	(250,388)
Net Income	-	-	-	-	-	41,198	41,198
Balance, March 31, 2021	18,502,902	$ 1,850	$ 40,652,472	$ -	$ 37,159	$ (1,720,538)	$ 38,970,943

See accompanying notes to consolidated financial statements

ONE STOP SYSTEMS, INC. (OSS)

UNAUDITED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

For the Three Month Period Ended March 31, 2020

	Common Stock				Accumulated Other		Total
	Shares	Amount	Additional Paid-in-Capital	Noncontrolling Interest	Comprehensive loss	Accumulated Deficit	Stockholders' Equity
Balance, January 1, 2020	16,121,747	$ 1,612	$ 30,537,015	$ 500	$ (17,773)	$ (1,755,192)	$ 28,766,162
Stock-based compensation	-	-	207,761	-	-	-	207,761
Exercise of stock options	354,914	35	56,965	-	-	-	57,000
Return of capital upon dissolution of SkyScale				(500)			(500)
Taxes paid on net issuance of employee stock options	-	-	(656,845)	-	-	-	(656,845)
Currency translation adjustment	-	-	-	-	(55,567)	-	(55,567)
Net loss	-	-	-			(1,096,032)	(1,096,032)
Balance, March 31, 2020	16,476,661	$ 1,647	$ 30,144,896	$ -	$ (73,340)	$ (2,851,224)	$ 27,221,979

See accompanying notes to consolidated financial statements

ONE STOP SYSTEMS, INC. (OSS)

UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS

	For the Three Months Ended March 31, 2021	2020
Cash flows from operating activities:		
Net income (loss)	$ 41,198	$ (1,096,032)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Deferred benefit for income taxes	(59,290)	(441,282)
(Gain) on disposal of property and equipment	-	(1,542)
Provision for bad debt	(16,590)	(2,405)
Warranty reserves	13,944	5,075
Amortization of deferred gain	-	(41,479)
Amortization of intangibles	163,900	174,525
Depreciation	216,878	221,300
Inventory reserves	154,335	148,418
Amortization of debt discount	61,210	7,520
Stock-based compensation expense	438,394	207,761
Changes in operating assets and liabilities:		
Accounts receivable	1,697,901	2,530,072
Inventories	(223,160)	(1,826,564)
Prepaid expenses and other current assets	(152,561)	(386,005)
Accounts payable	1,795,141	(275,428)
Accrued expenses and other liabilities	159,766	54,293
Net cash provided by (used in) operating activities	4,291,066	(721,773)
Cash flows from investing activities:		
Purchases of property and equipment, including capitalization of labor costs for test equipment and ERP	(121,759)	(200,049)
Proceeds from sales of property and equipment	-	1,542
Net cash used in investing activities	(121,759)	(198,507)
Cash flows from financing activities:		
Proceeds from exercise of stock options and warrants	278,968	57,000
Payment of payroll taxes on net issuance of employee stock options	(44,252)	(656,845)
Proceeds from issuance of stock	10,000,000	-
Stock issuance costs	(778,810)	-
Net (repayment) borrowings on bank lines of credit	(80,117)	(430,313)
Net repayments on related-party notes payable	(155,022)	(141,042)
Net repayments on notes payable	(47,174)	(42,919)
Net cash provided by (used in) financing activities	9,173,593	(1,214,119)
Net change in cash and cash equivalents	13,342,900	(2,134,399)
Effect of exchange rates on cash	(45,506)	(12,916)
Cash and cash equivalents, beginning of period	6,316,921	5,185,321
Cash and cash equivalents, end of period	$ 19,614,315	$ 3,038,006

See accompanying notes to consolidated financial statements

ONE STOP SYSTEMS, INC. (OSS)

UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS - CONTINUED

	For the Three Months Ended March 31,	
	2021	2020
Supplemental disclosure of cash flow information:		
Cash paid during the period for interest	$ 83,392	$ 22,369
Cash paid during the period for income taxes	$ 80,629	$ -

See accompanying notes to consolidated financial statements

NOTE 1 – THE COMPANY AND BASIS OF PRESENTATION

Nature of Operations

One Stop Systems, Inc. ("we," "our," "OSS," or the "Company") was originally incorporated as a California corporation in 1999 after initially being formed as a California limited liability company in 1998. On December 14, 2017, the Company was reincorporated as a Delaware corporation in connection with its initial public offering. The Company designs, manufactures, and markets industrial grade computer systems and components that are based on industry standard computer architectures. The Company markets its products to manufacturers of automated equipment used for media and entertainment, medical, industrial, and military applications.

During the year ended December 31, 2015, the Company formed a wholly owned subsidiary in Germany, One Stop Systems, GmbH ("OSS GmbH"). During July 2016, the Company acquired Mission Technologies Group, Inc. ("Magma") and its operations.

In April 2017, the Company and a related entity formed a joint venture named SkyScale, LLC in the State of California ("SkyScale"). In accordance with the Contribution Agreement, each member contributed $750,000 and received a 50% interest in the joint venture. The purpose of SkyScale was to engage in the business of providing high performance computing capabilities as cloud services. As a result of changes in the competitive landscape and downward pressure on pricing from large competitors, the members of the SkyScale joint venture agreement agreed to dissolve SkyScale and ceased operations as of December 31, 2018.

On August 31, 2018, the Company acquired Concept Development Inc. ("CDI") located in Irvine, California. CDI specializes in the design and manufacture of custom high-performance computing systems for airborne in-flight entertainment and networking systems. CDI has been fully integrated into the core operations of OSS as of June 1, 2020.

On October 31, 2018, OSS GmbH acquired 100% of the outstanding stock of Bressner Technology GmbH, a Germany limited liability company located near Munich, Germany ("Bressner"). Bressner provides standard and customized servers, panel PCs, and PCIe expansion systems. Bressner also provides manufacturing, test, and sales and marketing services for customers throughout Europe.

Liquidity, Going Concern Considerations and Management Plans

Given our recurring operating losses, the Company's primary sources of liquidity have been provided by (i) the Company's February 2018 initial public offering (net proceeds were approximately $16,100,000); (ii) March 2019 notes payable from members of the Board of Directors and others of $1,500,000; (iii) the July 2019 sale of 1,554,546 shares of the Company's common stock for net cash proceeds of $2,488,148; (iv) the April 24, 2020 sale of $3,000,000 of Senior Secured Convertible Promissory Notes issued at a 10% original issue discount; (v) receipt of approximately $1,500,000 on April 28, 2020 of government loan proceeds under the Paycheck Protection Program, and (vi) a receipt of approximately $9,221,000 on March 3, 2021 in a registered direct offering.

As of March 31, 2021, the Company's cash and cash equivalents were $19,614,315 and working capital was $25,935,632. Cash and cash equivalents held by Bressner totaled $1,263,430 (USD) at March 31, 2021. Bressner's debt covenants do not permit the use of these funds by its parent company.

During the three month period ended March 31, 2021, the Company experienced an operating income of $275,031, with cash generated by operating activities of $4,291,066. During the year ended December 31, 2020, the Company experienced an operating loss of $424,281, with cash used in operating activities of $250,173.

The Company's revenue growth during the prior year slowed due to the effects of COVID-19. However, resulting from a reduction in force and strict cost containment, the Company has been able to mitigate the effects, to some degree, of the reduced revenue attributable to the economic impact of COVID-19.

In March 2020, the World Health Organization declared the outbreak of COVID-19, a global pandemic and the United States federal government declared it a national emergency. COVID-19 continues to impact worldwide economic activity. A public health pandemic, including COVID-19, poses the risk that we or our employees, contractors, customers, suppliers, and other partners may be prevented from conducting business activities for an indefinite period of time, including due to shutdowns that may be requested or mandated by governmental authorities.

More generally, COVID-19 raises the possibility of an extended global economic downturn, which could affect demand for our products and services, and impact our results and financial condition even after the pandemic is contained and remediation/restriction measures are lifted. For example, we may be unable to collect receivables from customers that are significantly impacted by COVID-19. Also, a decrease in orders in a given period could negatively affect our revenues in future periods. COVID-19 may also have the effect of heightening many of the other risks described in the "Risk Factors" section of our December 31, 2020 Annual Report on Form 10-K filed March 25, 2021, including risks associated with our customers and supply chain. We will continue to evaluate the nature and extent of the impact of COVID-19 to our business.

Presently, it is clear the global economy has been negatively impacted by COVID-19, and demand for some of our products and services have been reduced due to uncertainty and the economic impact of COVID-19. In particular, in the media and entertainment industry, demand for the use of outdoor media equipment has been impacted due to restrictions on public gatherings. Until such restrictions improve, we expect that demand for certain of our clients' products and services will be limited, and may not return to prior levels, and thus, may impact our financial results and operations.

Specifically, our business has also begun to be negatively affected by a range of external factors related to COVID-19 that are not within our control. For example, numerous measures have been implemented by governmental authorities across the globe to contain the virus, including travel bans and restrictions, quarantines, shelter-in-place orders, restrictions and limitations of public gatherings, and business limitations and shutdowns. Many of our customers' businesses have been severely impacted by these measures and some have been required to reduce employee headcount as a result. If a significant number of our customers are unable to continue as a going concern, this would have an adverse impact on our business and financial condition. In addition, many of our customers are working remotely, which may delay the timing of new business and implementations of our services. If COVID-19 continues to have a substantial impact on our partners, customers, or suppliers, our results of operations and overall financial performance will be harmed.

Though management has been proactively managing through the current known impacts, if the situation further deteriorates or the outbreak results in further restriction on supply and demand factors, our cash flows, financial position and operating results for year 2021 and beyond will be negatively impacted. Neither the length of time nor the magnitude of the negative impacts can be presently determined.

The longer the COVID-19 pandemic persists, the greater the potential for significant adverse impact to our business operations. Quarantines, travel restrictions, prohibitions on non-essential gatherings, shelter-in-place orders and other similar directives and policies intended to reduce the spread of the disease, may reduce our productivity and that of the third parties on which we rely and may disrupt and delay many aspects of our business.

The Company is complying with state mandated requirements for safety in the workplace to ensure the health, safety and welling-being of our employees. These measures included personal protective equipment, social distancing, and cleanliness of the facilities and daily monitoring of the health of employees in our facilities. We have not developed a specific and comprehensive contingency plan designed to address the challenges and risks presented by the COVID-19 pandemic, even if and when we do develop such a plan, there can be no assurance that such plan will be effective in mitigating the potential adverse effects on our business, financial condition and results of operations.

Management's plans with respect to the above is to continue its efforts towards responding to the changing economic landscape attributable to COVID-19, to continue to reduce costs, conserve cash, strengthen margins, and improve company-wide execution. Specific actions already implemented by management include a reduction in force, a limited freeze on hiring, reduced work week, minimizing overtime, travel and entertainment, and contractor costs. On April 7, 2020, the Company implemented a cost reduction plan which included the termination of certain employees and elimination of certain costs. Savings from this effort are estimated to be $2.5 million on an annual basis.

While management expects these actions to result in prospective cost reductions, management is also committed to securing debt and/or equity financing to ensure that liquidity will be sufficient to meet the Company's cash requirements through at least a period of the next twelve months. Management believes potential sources of liquidity include at least the following:

- In May 2019, the Company filed a Form S-3 prospectus with the Securities and Exchange Commission which became effective on June 19, 2019, and allows the Company to offer up to $100,000,000 aggregate dollar amount of shares of its common stock, preferred stock, debt securities, warrants to purchase its common stock, preferred stock or debt securities, subscription rights to purchase its common stock, preferred stock or debt securities and\or units consisting of some or all of these securities, in any combination, together or separately, in one or more offerings, in amounts, at prices and on the terms that the Company will determine at the time of the offering and which will be set forth in a prospectus supplement and any related free writing prospectus.
- On April 24, 2020, the Company completed a $6.0 million debt financing on a non-interest bearing convertible note with a 10% original issue discount. The first tranche of $3.0 million was received on April 27, 2020, with an additional $3.0 million available seven months from the date of closing at the option of the Company conditioned upon meeting certain requirements which have been satisfied. The note is repayable in twenty-two installments beginning three months after closing in cash or shares of the Company's common stock.
- On March 1, 2021, the Company entered into a Securities Purchase Agreement with an accredited investor, pursuant to which the Company agreed to issue and sell, in a registered direct offering, 1,497,006 shares of the Company's common stock, par value $0.0001 per share, to the purchaser at an offering price of $6.68 per share. The registered offering was conducted pursuant to the Company's effective shelf registration statement on Form S-3 (Registration No. 333-231513), which was initially filed with the Securities and Exchange Commission on May 15, 2019; and was declared effective on June 19, 2019. As compensation for their services, the Company paid to the placement agents a fee equal to 7% of the gross proceeds received by the Company as a result of the registered offering, and reimbursed the placement agents for certain expenses incurred in connection with such offering. The net proceeds from the registered offering are approximately $9.2 million after deducting certain fees due to the placement agents' and the Company's transaction expenses. The net proceeds received by the Company will be used for general corporate and working capital purposes.

As a result of management's cost reduction plans, the Company's sources of liquidity and management's most recent cash flow forecasts, management believes that the Company has sufficient liquidity to satisfy its anticipated cash requirements for at least the next twelve months. However, there can be no assurance that management's cost reduction efforts will be effective, the forecasted cash flows will be achieved, or that external sources of financing, including the issuance of debt and/or equity securities, will be available at times and on terms acceptable to the Company, or at all.

Basis of Presentation

The accompanying consolidated financial statements have been prepared on an accrual basis of accounting in accordance with United States Generally Accepted Accounting Principles ("U.S. GAAP"), as set forth in the Financial Accounting Standards Board's ("FASB") Accounting Standards Codification ("ASC").

The unaudited consolidated financial statements herein have been prepared by the Company pursuant to the rules and regulations of the United States Securities Exchange Commission ("SEC"). The accompanying interim unaudited consolidated financial statements have been prepared under the presumption that users of the interim financial information have either read or have access to the audited consolidated financial statements for the latest year ended December 31, 2020. Accordingly, note disclosures which would substantially duplicate the disclosures contained in the December 31, 2020 audited consolidated financial statements have been omitted from these interim unaudited consolidated financial statements. The Company evaluated all subsequent events and transactions through the date of filing this report.

In the opinion of management, all adjustments considered necessary for a fair presentation have been included in the accompanying condensed financial statements. Operating results for the three months ended March 31, 2021, are not necessarily indicative of the results that may be expected for the year ending December 31, 2021. For further information, refer to the audited consolidated financial statements and notes for the year ended December 31, 2020 included in the Company's Annual Report on Form 10-K filed with the SEC on March 25, 2021.

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of OSS, which include the acquisition of Concept Development Inc., its wholly owned subsidiary, OSS GmbH, which also includes the acquisition of Bressner Technology GmbH. Intercompany balances and transactions have been eliminated in consolidation.

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES

There have been no changes to our accounting policies disclosed in our audited consolidated financial statements and the related notes for the year ended December 31, 2020.

Use of Estimates

The preparation of condensed consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent liabilities at the date of the condensed consolidated financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from these estimates and assumptions.

On an ongoing basis, our management evaluates these estimates and assumptions, including those related to determination of standalone selling prices of our products and services, allowance for doubtful account and sales reserves, income tax valuations, stock-based compensation, goodwill, intangible assets and inventory valuations and recoverability. We base our estimates on historical data and experience, as well as various other factors that our management believes to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities.

As of March 31, 2021, we had approximately $3.6 million in net deferred tax assets (DTAs). These DTAs include approximately $5.1 million related to net operating loss carryforwards that can be used to offset taxable income in future periods and reduce our income taxes payable in those future periods. At this time, we consider it more likely than not that we will have sufficient taxable income in the future that will allow us to realize these DTAs. However, it is possible that economic conditions may decrease the likelihood that we will have sufficient taxable income in the future. Therefore, unless we are able to generate sufficient taxable income from our operations, a substantial valuation allowance to reduce our U.S. DTAs may be required, which would materially increase our expenses in the period the allowance is recognized and materially adversely affect our results of operations and statement of financial condition.

On March 11, 2021, Congress passed, and the President signed into law, the American Rescue Plan Act, 2021 (the "ARP"), which includes certain business tax provisions. At this point we do not believe that these changes will have a material impact on our income tax provision for 2021. We will continue to evaluate the impact of new legislation on our financial position, results of operations, and cash flows.

Due to the COVID-19 pandemic, there has been uncertainty and disruption in the global economy and financial markets.We are not aware of any specific event or circumstance that would require an update to our estimates or assumptions or a revision of the carrying value of our assets or liabilities as of the date of this Quarterly Report on Form 10-Q. These estimates and assumptions may change as new events occur and additional information is obtained. As a result, actual results could differ materially from these estimates and assumptions.

Recent Accounting Pronouncements

In February 2016, the FASB issued ASU No. 2016-02,*Leases* ("ASU 2016-02"). Under ASU 2016-02, lessees will be required to recognize the following for all leases (with the exception of short-term leases) at the commencement date: a lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis; and a right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. ASU 2016-02 is effective for the Company for fiscal years beginning after December 15, 2021, and interim periods within fiscal year 2023. Early application is permitted. Lessees must apply a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. The modified retrospective approach would not require any transition accounting for leases that expired before the earliest comparative period presented. Lessees may not apply a full retrospective transition approach. The Company is currently evaluating the impact of adopting ASU 2016-02 on its consolidated financial statements and disclosures. Based on our preliminary analysis, management expects the Company's assets and liabilities to increase by the present value of the lease payments.

In June 2016, the FASB issued ASU 2016-13,*Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments.* ASU 2016-13 amends the guidance on the impairment of financial instruments. This update adds an impairment model (known as the current expected credit losses model) that is based on expected losses rather than incurred losses. Under the new guidance, an entity recognizes, as an allowance, its estimate of expected credit losses. In November 2019, ASU 2016-13 was amended by ASU 2019-10 that changed the effective date of ASU 2016-13 to fiscal years beginning after December 15, 2022, with early adoption permitted. Further, the ASU clarifies that operating lease receivables are not within the scope of ASC Subtopic 326-20 and should instead be accounted for under the new leasing standard, ASC 842. The Company is currently evaluating the impact of adopting ASU 2016-13 on its consolidated financial statements and related disclosures.

Recently Implemented Accounting Pronouncements

In September 2018, the FASB issued ASU No. 2018-07,*Stock-based Compensation: Improvements to Nonemployee Share-based Payment Accounting* which amends the existing accounting standards for share-based payments to nonemployees. This ASU aligns much of the guidance on measuring and classifying nonemployee awards with that of awards to employees. Under the new guidance, the measurement of nonemployee equity awards is fixed on the grant date. This ASU became effective for the year ended December 31, 2020 (and interim periods in 2021). ASU 2018-07 did not materially impact the Company's consolidated financial statements.

In May 2014, the FASB issued Accounting Standards Update ("ASU") No. 2014-09,*Revenue from Contracts with Customers* ("ASU 2014-09"). ASU 2014-09 supersedes the revenue recognition requirements in FASB Topic 605, *Revenue Recognition*. ASU 2014-09 implements a five-step process for customer contract revenue recognition that focuses on transfer of control, as opposed to transfer of risk and rewards. This guidance provides a single, comprehensive accounting model for revenue arising from contracts with customers. This guidance supersedes most of the existing revenue recognition guidance, including industry-specific guidance. Under this model, revenue is recognized at an amount that a company expects to be entitled to upon transferring control of goods or services to a customer, as opposed to when risks and rewards transfer to a customer. The new guidance also requires additional disclosures about the nature, timing and uncertainty of revenue and cash flow arising from customer contracts, including significant judgments and changes in judgments. We adopted this standard beginning January 1, 2019 and used the modified retrospective method of adoption. Under the new guidance, based on the nature of our contracts, we continued to recognize revenue in a similar manner as with the former guidance. Accordingly, the adoption of this standard did not significantly impact our revenues.

In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments* ("ASU 2016-15"), which is intended to reduce the existing diversity in practice in how certain cash receipts and cash payments are classified in the statement of cash flows. ASU 2016-15 is effective for fiscal years beginning after December 15, 2018, with early adoption permitted, provided that all of the amendments are adopted in the same period. The Company's adoption of this guideline did not have a material effect on the Company's consolidated financial statements.

In July 2017, the FASB issued Accounting Standards Update No. 2017-11, *Accounting for financial instruments with down rounds features* ("ASU 2017-11"), which addressed (i) accounting for certain financial instruments with down round features, and (ii) replacement of the indefinite deferral for mandatorily redeemable financial instruments of certain nonpublic entities and certain mandatorily redeemable non-controlling interests with a scope exception. The main provisions of Part I of ASU 2017-11 are to change the classification analysis of certain equity-linked financial instruments and embedded features with down round features. When determining whether certain financial instruments should be classified as liabilities or equity instruments, a down round feature no longer precludes equity classification when assessing whether the instrument is indexed to an entity's own stock. The amendments also clarify existing disclosure requirements for equity-classified instruments. As a result, a freestanding equity-linked financial instrument or embedded conversion option no longer would be accounted for as a derivative liability at fair value as a result of the existence of a down round feature. For freestanding equity classified financial instruments, the amendments require entities that present earnings per share (EPS) to recognize the effect of the down round feature when it is triggered. That effect is treated as a dividend and as a reduction of income available to common shareholders in basic EPS. Under previous US GAAP, the existence of down round features often result in an accounting conclusion that the evaluated feature or instrument is not indexed to the entity's own stock, which results in classification as a derivative liability. ASU 2017-11 was adopted early by the Company on April 1, 2020, with no adjustments. The Company's April 2020 convertible note payable described in Note 7 possesses down round features.

In December 2019, the FASB issued ASU 2019-12, *Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes* ("ASU 2019-12"), an amendment to the guidance on income taxes, which is intended to simplify the accounting for income taxes. The amendment eliminates certain exceptions related to the methodology for calculating income taxes on an interim period, the approach for intra-period tax allocation, and the recognition of deferred tax liabilities for outside basis differences. The amendment also clarifies existing guidance related to the recognition of franchise tax, the evaluation of a step up in the tax basis of goodwill, and the effects of enacted changes in tax laws or rates in the effective tax rate computation, among other clarifications. The effective date of the standard is annual periods beginning after December 15, 2021, and interim periods within fiscal years beginning after December 15, 2022, with early adoption permitted. The Company elected to early adopt ASU 2019-12 prospectively as of July 1, 2020, which did not have a material impact on the consolidated financial statements, except for the elimination of the rule that limited the interim tax benefit to the tax benefit expected for the year. The early adoption resulted in the Company recording an additional interim tax benefit of $446,099 for the three months ended September 30, 2020. The adoption did not impact the Company's annual income tax benefit or expense for the year ended December 31, 2020 or the amount of net deferred income tax assets as of March 31, 2021. The Company made the election to early adopt because, consistent with the FASB, it believes that it will reduce the time and cost associated with income tax accounting and reporting, while not adversely altering the information provided to stakeholders on an interim basis.

NOTE 3 – ACCOUNTS RECEIVABLE

Accounts receivable, net consists of the following:

	March 31, 2021	December 31, 2020
Accounts receivable	$ 5,749,660	$ 7,491,397
Unbilled receivables	4	106
	5,749,664	7,491,503
Less: allowance for doubtful accounts	(15,989)	(33,120)
	$ 5,733,675	$ 7,458,383

Unbilled receivables include amounts associated with percentage of completion and milestone billing accounting, which includes cost and gross profit earned in excess of billing, not currently billable due to contractual provisions. Provision for bad debt expense related to accounts receivable was ($16,590) and ($2,405) for the three month periods ended March 31, 2021 and 2020, respectively.

NOTE 4 – INVENTORIES

Inventories, net consist of the following:

	March 31, 2021	December 31, 2020
Raw materials	$ 4,014,408	$ 5,210,327
Sub-assemblies	208,453	255,699
Work-in-process	768,473	407,328
Finished goods	5,218,864	4,424,603
	10,210,198	10,297,957
Less: reserves for obsolete and slow-moving inventories	(661,238)	(650,453)
	$ 9,548,960	$ 9,647,504

NOTE 5 – LONG LIVED INTANGILE ASSETS

Definite lived intangible assets related to acquisition are as follows, as of March 31, 2021:

	Expected Life	Remaining Months	Gross Intangible Assets	Accumulated Amortization	Net Intangible Assets
Customer lists and relationships	36 to 60 months	7 to 29 months	$ 2,084,515	$ (1,695,302)	$ 389,213
Drawings and technology	36 months	0 months	760,207	(760,207)	-
Trade name, trademarks & other	24 to 36 months	7 months	447,274	(383,202)	64,072
Non-compete	36 months	7 months	246,797	(201,725)	45,072
			$ 3,538,793	$ (3,040,436)	$ 498,357

Definite lived intangibles assets related to acquisitions are as follows, as of December 31, 2020:

	Expected Life	Remaining Months	Gross Intangible Assets	Accumulated Amortization	Net Intangible Assets
Customer lists and relationships	36 to 60 months	10 to 32 months	$ 2,084,515	$ (1,578,178)	$ 506,337
Drawings and technology	36 months	0 months	760,207	(760,207)	-
Trade name, trademarks & other	24 to 36 months	10 months	447,274	(355,742)	91,532
Non-compete	36 months	10 months	246,797	(182,409)	64,388
			$ 3,538,793	$ (2,876,536)	$ 662,257

As of March 31, 2021, amortization expense of the definite lived intangible assets for the years remaining is as follows:

2021	2022	2023	Total
$ 392,972	$ 63,231	$ 42,154	$ 498,357

Amortization expense recognized during the three months ended March 31, 2021 and 2020 was $163,900 and $174,525, respectively.

NOTE 6 – ACCRUED EXPENSES AND OTHER LIABILITIES

Accrued expenses and other liabilities consist of the following:

	March 31, 2021	December 31, 2020
Accrued compensation and related liabilities	$ 992,810	$ 932,988
Deferred revenue and customer deposits	1,281,663	1,096,672
Warranty reserve	425,377	425,636
Deferred rent	292,890	312,909
Other accrued expenses	592,362	713,239
	$ 3,585,102	$ 3,481,444

NOTE 7 – DEBT

Bank Lines of Credit

Bressner Technology GmbH has two revolving lines of credit with German institutions totaling €2,200,000 (US$2,578,904). Borrowing under the lines of credit bear interest at a variable rate of Euribor plus a stated rate. The current rates for the lines of credit are 3.89% and 4.0%. One million euros of the credit line expires in January 2024, with the remaining balance being open indefinitely or until occurrence of a defined change of control event. There were no outstanding lines of credit balances as of March 31, 2021 and December 31, 2020.

Foreign Debt Obligations

Bressner Technology GmbH has two term loans outstanding as of March 31, 2021 with a total balance outstanding of €1,000,000 (US$1,174,343) as follows:

On April 9, 2020, Bressner converted €500,000 of its line of credit from UniCredit Bank to a one-year term loan at 1.9% interest with a balloon payment of principal and interest due upon maturity. The balance outstanding as of March 31, 2021 and December 31, 2020 is €500,000 (US$587,171, $611,406, respectively);

Bressner entered into a note payable in June 2019 in the amount of €500,000 (US$586,189) which bears interest at 1.70% and matured on June 25, 2020 with a balloon payment of principal and interest. This loan was subsequently extended to June 18, 2021, with an interest rate of 1.87% The amount outstanding as of March 31, 2021 and December 31, 2020 is €500,000 (US$587,172, $611,406, respectively);

Bressner entered into a note payable in April 2019 in the amount of €500,000 (US$586,189) which bears interest at 2.25% and matures on March 30, 2021 with monthly payments of principal and interest of €22,232 (US$24,960). The balance outstanding as of March 31, 2021 and December 31, 2020 is €0 (US$0) and €66,446 (US$81,251), respectively;

Bressner entered into a note payable in September 2019 in the amount of €300,000 (US$336,810) which bore interest at 1.65% and matured on March 24, 2020, with a balloon payment of principal and interest. The outstanding balance was paid in full as of March 31, 2020; and

Bressner entered into a note payable in September 2017, in the amount of €400,000 (US$436,272) which bore interest at 2.125% and matured on January 31, 2020 and has been paid in full.

Notes Payable

In April 2019, the Company borrowed $350,000 from three individuals for a two-year period at an interest rate of 9.5% which requires the Company to make monthly principal and interest payments of $16,100 per month. These loans are secured by the assets of the Company. In connection with these loans, the Company issued to the noteholders warrants to purchase shares of the Company's common stock equal to 10% of the original principal at a price per share equal to $2.15 per share. Accordingly, the Company issued to the noteholders warrants to purchase 16,276 shares of the Company's common stock at an exercise price of $2.15 per share. The relative fair value of each warrant was $0.90. The relative fair value of warrants was estimated using Black-Scholes with the following weighted-average assumptions: fair value of the Company's common stock at issuance of $2.15 per share; five year contractual term; 44.60% volatility; 0.0% dividend rate; and a risk-free interest rate of 2.307%. The total relative fair value of the warrants issued is $14,037. The balance outstanding as of March 31, 2021 and December 31, 2020 is $16,014 and $63,188, respectively.

Notes Payable – Related Parties

In April 2019, the Company borrowed $1,150,000 from three individuals who serve on the Company's board of directors for a two-year period at an interest rate of 9.5% which requires the Company to make monthly principal and interest payments of $52,900 per month. These loans are secured by the assets of the Company. In connection with these loans, the Company issued to the noteholders warrants to purchase shares of the Company's common stock equal to 10% of the original principal at a price per share equal to $2.15 per share. Accordingly, the Company issued to the noteholders warrants to purchase 53,490 shares of the Company's common stock at an exercise price of $2.15 per share. The relative fair value of each warrant was $0.90. The relative fair value of warrants was estimated using Black-Scholes with the following weighted-average assumptions: fair value of the Company's common stock at issuance of $2.15 per share; five year contractual term; 42.60% volatility; 0.0% dividend rate; and a risk-free interest rate of 2.3067%. The relative fair value of warrants issued is $46,121. The balance outstanding as of March 31, 2021 and December 31, 2020 is $51,647 and $206,669, respectively.

Paycheck Protection Program Loan

On April 28, 2020, One Stop Systems, Inc. received authorization pursuant to the Paycheck Protection Program (PPP) of the Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act") as administered by the U.S. Small Business Administration (the "SBA") for a "PPP" loan. On May 11, 2020, the Loan was funded, and the Company received proceeds in the amount of $1,499,360 (the "PPP Loan").

The PPP Loan, which took the form of a two-year promissory note (the "PPP Note"), matures on April 28, 2022 and bears interest at a rate of 1.0% per annum. Monthly principal and interest payments, less the amount of any potential forgiveness (discussed below), was initially to commence on October 28, 2020. The Company did not provide any collateral or guarantees for the PPP Loan, nor did the Company pay any facility charge to obtain the PPP Loan. The PPP Note provides for customary events of default, including, among others, those relating to failure to make payment, breaches of any term, obligation, covenant, or condition contained in the PPP Note and payment of unauthorized expenses or use of proceeds contrary to CARES Act rules. The Company may prepay the principal of the PPP Loan at any time without incurring any prepayment charges.

Under the original rules, all or a portion of the PPP Loan may be forgiven by the SBA and lender upon application by the Company beginning 60 days but not later than 120 days after loan approval and upon documentation of expenditures in accordance with the SBA requirements. Under the CARES Act, loan forgiveness is available for the sum of documented payroll costs, covered rent payments, and covered utilities during the eight-week period beginning on the date of loan approval. For purposes of the CARES Act, payroll costs exclude compensation of an individual employee in excess of $100,000, prorated annually. Not more than 25% of the forgiven amount may be for non-payroll costs. Forgiveness is reduced if full-time headcount declines, or if salaries and wages for employees with salaries of $100,000 or less annually are reduced by more than 25%. In the event the PPP Loan, or any portion thereof, is forgiven pursuant to the PPP, the amount forgiven is applied to outstanding principal.

However, the Paycheck Protection Program Flexibility Act of 2020 (the "PPP Flexibility Act"), enacted on June 5, 2020, amended the original rules governing loans granted under the PPP, among others, as follows: (i) the time period to spend the received funds was extended from the original eight weeks to twenty-four weeks from the date the PPP Loan was originated, during which PPP funds need to be expended in order to be forgiven; (ii) at least 60% of PPP funds must be spent on payroll costs, with the remaining 40% available to spend on other eligible expenses; (iii) payments are deferred until the date on which the amount of forgiveness determined is remitted to the lender, and if a borrower fails to seek forgiveness within 10 months after the last day of its covered period, then payments will begin on the date that is 10 months after the last day of the covered period; and (iv) the PPP Flexibility Act modified the CARES Act by increasing the maturity date for loans made after the effective date from two years to a minimum maturity of five years from the date on which the borrower applies for loan forgiveness. Existing PPP loans made before the new legislation retain their original two-year term, but may be renegotiated between a lender and a borrower to match the 5-year term permitted under the PPP Flexibility Act.

The Company has submitted an application with the lender to forgive the PPP Loan, in accordance with SBA Procedural Notice, Control No. 5000-20057, effective as of October 2, 2020. Because the Company expects the PPP loan to be forgiven in full, all related amounts have been presented as noncurrent liabilities (See Note 13).

Senior Secured Convertible Note:

On April 20, 2020, the Company entered into a Securities Purchase Agreement with an institutional investor, providing for the issuance of the Company's Senior Secured Convertible Promissory Notes with a principal face amount of up to $6,000,000. The notes are, subject to certain conditions, convertible into shares of the Company's common stock, par value $0.0001 per share, at an initial conversion price per share of $2.50. The notes will be issued with a 10% original issue discount.

At the initial closing of this offering, the Company issued notes of $3,000,000, and can consummate additional closings of up to $3,000,000, subject to the prior satisfaction of certain closing conditions which have been satisfied. The initial investor purchased the notes for an aggregate purchase price of $2,700,000 at the initial closing. The notes bear no interest rate (except upon event of default) and, unless earlier converted or redeemed, will mature on April 1, 2022.

The Notes are convertible at any time, in whole or in part, at the option of the investors, into shares of common stock at the initial conversion price of $2.50 per share. The conversion price is subject to adjustment for issuances of securities below the conversion price then in effect and for stock splits, combinations or similar events. If immediately following the close of business on the six month anniversary of the issuance date of each note, the conversion price then in effect exceeds 135% of the volume weighted average price VWAP (the "Market Price"), the initial conversion price under any such note will be automatically lowered to the Market Price.

Commencing July 1, 2020, the Company has made monthly amortization payments equal to 1/22nd of the initial principal, any accrued and unpaid interest and late charges and any deferred or accelerated amount, of such note, which may be satisfied in cash at a redemption price equal to 105% of such installment amount (110% of such installment amount on notes issued at additional closings). As of March 31, 2021, the holder has elected to defer receipt of three installment payments as allowed per the agreement.

Subject to the satisfaction of certain equity conditions set forth in the notes, installment amounts may be satisfied in shares of our common stock, with such installment conversion at a conversion price equal to the lower of (i) the conversion price then in effect; and (ii) the greater of (x) the floor price of $1.00 (80% of the Nasdaq market price at date of purchase agreement) and (y) the lower of (I) 82.5% the volume weighted average price of our common stock on the trading day immediately before the applicable installment date and (II) 82.5% of the quotient of (A) the sum of the volume weighted average price of our common stock for each of the three (3) trading days with the lowest volume weighted average price of our common stock during the twenty (20) consecutive trading day period ending and including the trading day immediately prior to the applicable installment date, divided by (B) three (3). Shares of our common stock to be issued with respect to any such installment will be pre-delivered on the second trading day after the applicable installment notice date (as defined in the notes) with a true-up on the applicable installment date. The market value of any installment amount below the floor price will be cash settled on the applicable installment date.

Management evaluated the embedded conversion feature to determine whether bifurcation was required as a separate derivative liability. Management first determined that the conversion feature was not within the scope of ASC 480. It then determined that the embedded derivative should be separated from the host instrument and accounted for as a derivative instrument because it met the criteria of ASC 815-15-25-1, primarily because the contract provides for delivery of an asset that puts the recipient in substantially the same position as net settlement. However, in part due to the Company's adoption of ASC 2017-11 on April 1, 2020, which allowed management to disregard the down round provisions of the conversion feature, management determined that a scope exception to derivative accounting existed by satisfying the additional conditions necessary for equity classification specified by ASC 815-10-15-74 and ASC 815-40-25. As a result of management's analysis, the conversion feature was not accounted for separately from the debt instrument and the Company will recognize the contingent beneficial conversion feature when, or if, such is triggered.

The original issue discount of 10% on the Senior Secured Convertible Note was recorded as a debt discount, decreasing the note payable. This debt discount is amortized to interest expense using the effective interest rate method over the term of the loan. For the three months ended March 31, 2021, total debt discount amortization was $50,928, and such amount is included in interest expense in the accompanying consolidated statements of operations.

Debt issuance costs in the amount of $316,274 related to this indebtedness were deducted from the face value of the note. Such costs are amortized to interest expense using the effective interest rate method over the term of the loan. Total debt issuance costs amortized during the three months ended March 31, 2021 was $53,690, and such amount is included in interest expense in the accompanying consolidated statements of operations.

Debt Discount

The relative fair value of warrants issued in connection with the notes payable described above were recorded as debt discount, decreasing notes payable and related-party notes payable and increasing additional paid-in-capital on the accompanying consolidated balance sheets. The debt discounts are being amortized to interest expense over the term of the corresponding notes payable using the straight-line method which approximates the effective interest method.

For the three month periods ended March 31, 2021 and 2020, total debt discount amortization was $7,519 and $7,520, respectively, and such amounts are included in interest expense in the accompanying consolidated statements of operations.

A summary of outstanding debt obligations as of March 31, 2021 is as follows:

Loan Description	Current Interest Rate	Maturity Date	Balance (Euro)	Balance ($)	Current Portion	Long-term Portion
Domestic:						
Notes payable - third party	9.50%	April-21	€ -	$ 16,014	$ 16,014	$ -
Related party notes payable	9.50%	April-21	-	51,647	51,647	-
Convertible senior secured note	10% OID	April-22	-	2,590,909	2,454,545	136,364
PPP loan	1.00%	April-22	-	1,499,360	-	1,499,360
			€ -	$ 4,157,930	$ 2,522,206	$ 1,635,724
Foreign:						
Uni Credit Bank AG	1.87%	June-21	€ 500,000	$ 587,171	$ 587,171	$ -
Uni Credit Bank AG	1.90%	April-21	500,000	587,172	587,172	-
			€ 1,000,000	$ 1,174,343	$ 1,174,343	$ -
				$ 5,332,273	$ 3,696,549	$ 1,635,724

Outstanding debt obligations as of March 31, 2021 consist of the following:

Period Ended March 31, 2021	Related Parties	Third Parties	Convertible Note	PPP Loan	Foreign	Total
Current portion:						
Principal	$ 51,647	$ 16,014	$ 2,454,545	$ -	$ 1,174,343	$ 3,696,549
Less discount	(962)	(292)	(80,677)	-	-	(81,931)
Less loan origination costs	-	-	(85,054)	-	-	(85,054)
Net liability	$ 50,685	$ 15,722	$ 2,288,814	$ -	$ 1,174,343	$ 3,529,564
Long-term portion:						
Principal	$ -	$ -	$ 136,364	$ 1,499,360	$ -	$ 1,635,724
Less discount	-	-	-	-	-	-
Less loan origination costs	-	-	-	-	-	-
Net liability	$ -	$ -	$ 136,364	$ 1,499,360	$ -	$ 1,635,724
Total:						
Principal	$ 51,647	$ 16,014	$ 2,590,909	$ 1,499,360	$ 1,174,343	$ 5,332,273
Less discount	(962)	(292)	(80,677)	-	-	(81,931)
Less loan origination costs	-	-	(85,054)	-	-	(85,054)
Net liability	$ 50,685	$ 15,722	$ 2,425,178	$ 1,499,360	$ 1,174,343	$ 5,165,288

Total future principal payments under notes payable and related party notes payable as of March 31, 2021 are as follows:

Period Ending March 31,	Related Parties	Third Parties	Convertible Note	PPP Loan	Foreign	Total	Discount / Loan Original Costs
2022	$ 51,647	$ 16,014	$ 2,454,545	$ -	$ 1,174,343	$ 3,696,549	$ (166,985)
2023	-	-	136,364	1,499,360	-	1,635,724	-
Total minimum payments	51,647	16,014	2,590,909	1,499,360	1,174,343	5,332,273	(166,985)
Current portion of notes payable	(51,647)	(16,014)	(2,454,545)	-	(1,174,343)	(3,696,549)	166,985
Notes payable, net of current portion	$ -	$ -	$ 136,364	$ 1,499,360	$ -	$ 1,635,724	$ -

NOTE 8 – STOCKHOLDERS' EQUITY

The Company's amended and restated certificate of incorporation filed on December 14, 2017, authorizes the Company to issue 10,000,000 shares of preferred stock and 50,000,000 shares of common stock.

Stock Options

Effective June 24, 2020, the Company entered into an employment agreement with Mr. Raun to serve as the Company's president and chief executive officer. Pursuant to the terms of the employment agreement, Mr. Raun is entitled to receive 412,125 restricted stock units ("RSUs") that shall vest over three years, with one third of the RSUs vesting following the one-year anniversary of the date of grant, and the remaining RSUs vesting in four equal installments, commencing six months after the one-year anniversary of the date of grant and every six months thereafter until fully vested; and 412,125 Incentive Stock Options ("ISOs") pursuant to the Company's 2017 Equity Incentive Plan, whereby the exercise price for the ISOs shall be no less than the fair market value of the Company's common stock at the date of grant, ($2.14).

The ISOs shall vest at the end of each of the second and fourth quarters, the price of the Company's common stock as of the end of quarter two or quarter four, as applicable, shall be determined using the ten-day trailing volume weighted average price ("VWAP") after reporting of quarter two and quarter four earnings, as applicable. The date of each such determination shall be referred to as a "Determination Date." If on any Determination Date the Company's stock price has increased from the prior Determination Date, then a portion of the ISOs shall become vested. The number of ISOs that shall become vested on a Determinate Date is determined as follows: ((Price at Determination Date – Price at prior Determination Date) x 100) * 1,177.52 = Vested ISOs. If on any Determination Date the Company's stock price is $5.50 per share, all ISOs shall immediately become vested.

In the event that Mr. Raun's employment agreement is terminated for a reason other than "good cause" or for "good reason", Mr. Raun, upon executing an effective waiver and release of claims, unvested RSUs shall accelerate so that an additional twelve (12) months of RSUs shall vest from the termination date.

A summary of stock option activity under each of the Company's stock option plans during the three month period ended March 31, 2021:

	Stock Options Outstanding			
	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (in years)	Aggregate Intrinsic Value
Outstanding at January 1, 2021	1,320,267	$ 1.81	6.43	$ 2,889,274
Granted	-	-	-	-
Forfeited / Cancelled	1,113	$ 1.95	6.28	$ 4,886
Exercised	(198,891)	$ 1.08	3.17	$ 1,047,002
Outstanding at March 31, 2021	1,122,489	$ 1.95	6.72	$ 4,932,363
Exercisable at March 31, 2021	663,265	$ 1.75	5.08	$ 3,044,253
Vested and expected to vest at March 31, 2021	1,108,712	$ 1.94	6.69	$ 4,875,720

The following table presents details of the assumptions used to calculate the weighted-average grant date fair value of common stock options granted by the Company. There were no options granted during the three month period ended March 31, 2021:

	For the Three Months Ended March 31,	
	2021	2020
Expected term (in years)	0	5.87
Expected volatility	0.00 %	43. - 47.8%
Risk-free interest rate	0.00 %	1.41 %
Weighted average grant date fair value per share	$ -	$ 2.70
Grant date fair value of options vested	$ 1,160,847	$ 720,095
Intrinsic value of options exercised	$ 1,047,002	$ 463,800

As of March 31, 2021, the amount of unearned stock-based compensation estimated to be expensed from 2021 through 2025 related to unvested common stock options is $49,012, net of estimated forfeitures. The weighted-average period over which the unearned stock-based compensation is expected to be recognized is 0.93 years.

If there are any modifications or cancellations of the underlying unvested awards, the Company may be required to accelerate, increase, or cancel any remaining unearned stock-based compensation expense or calculate and record additional expense. Future stock-based compensation expense and unearned stock-based compensation will increase to the extent that the Company grants additional common stock options or other stock-based awards.

Restricted Stock Units

Restricted stock units may be granted at the discretion of the compensation committee of the Board of Directors under the Company's 2017 Equity Incentive Plan that was adopted on October 10, 2017 (the "2017 Plan") in connection with the hiring and retention of personnel and are subject to certain conditions. Restricted stock units generally vest quarterly or semi-annually over a period of one to three years and are typically forfeited if employment is terminated before the restricted stock unit vest. The compensation expense related to the restricted stock units is calculated as the fair value of the common stock on the grant date and is amortized to expense over the vesting period and is adjusted for estimated forfeitures.

The Company's restricted stock unit activity for the three month period ended March 31, 2021 is as follows:

	Restricted Stock Units	
	Number of Shares	Weighted Average Grant Date Fair Value
Unvested at January 1, 2021	575,922	$ 2.65
Granted	-	$ -
Vested	(93,793)	$ 2.37
Cancelled	-	$ 2.70
Unvested at March 31, 2021	482,129	$ 2.70

As of March 31, 2021, there was $786,901 of unrecognized compensation cost related to unvested restricted stock units which is expected to be recognized over a weighted average period of 2.07 years.

Stock-based compensation expense for the three month periods ended March 31, 2021 and 2020 was comprised of the following:

	For the Three Months Ended March 31,	
Stock-based compensation classified as:	2021	2020
General and administrative	$ 401,000	$ 159,680
Production	14,659	17,969
Marketing and selling	15,397	17,292
Research and development	7,338	12,820
	$ 438,394	$ 207,761

Warrants

The following table summarizes the Company's warrant activity during the three month period ended March 31, 2021:

	Number of Warrants	Weighted Average Exercise Price
Warrants outstanding – January 1, 2021	505,946	$ 5.00
Warrants granted	-	$ -
Warrants exercised	(35,067)	$ 1.85
Warrants outstanding – March 31, 2021	470,879	$ 5.23

NOTE 9 – COMMITMENTS AND CONTINGENCIES

Legal

We are subject to litigation, claims, investigations, and audits arising from time to time in the ordinary course of our business.

On September 29, 2020, the Company's former Chief Executive Officer, Stephen D. Cooper, commenced an action entitled Stephen D. Cooper v. One Stop Systems, Inc. et al, in San Diego County Superior Court, Case No. 37-2020-00034492-CU-BC-CTL Mr. Cooper alleges claims for (1) breach of written contract and (2) violation of California Labor Code Sections 201 and 203 in connection with the Company's alleged failure to pay unpaid wages and an earned bonus following the Company's termination of Mr. Cooper's employment with the Company in February 2020. Mr. Cooper seeks unspecified compensatory damages and statutory penalties.

The Company has denied Mr. Cooper's allegations. On December 8, 2020, the Company filed a cross-complaint ("Cross Complaint") against Mr. Cooper for (1) breach of contract (in connection with a binding commitment letter and Mr. Cooper's employment agreement), (2) intentional misrepresentation, (3) negligent misrepresentation, and (4) breach of fiduciary duty. The Company is seeking compensatory damages, punitive damages, pre-judgment interest, attorneys' fees, and the cost of suit incurred in connection with Mr. Cooper's complaint and the Cross Complaint. The Company intends to vigorously defend all allegations.

Guarantees and Indemnities

The Company has made certain indemnities, under which it may be required to make payments to an indemnified party, in relation to certain transactions. The Company indemnifies its directors, officers, employees, and agents to the maximum extent permitted under the laws of the State of Delaware. In connection with its facility lease, the Company has indemnified its lessor for certain claims arising from the use of the facilities. Also, in connection with its Credit Agreement, the Company has agreed to indemnify its lender and others related to the use of the proceeds and other matters. The duration of the indemnities varies, and in many cases is indefinite. These indemnities do not provide for any limitation of the maximum potential future payments the Company could be obligated to make. Historically, the Company has not been obligated to make any payments for these obligations and no liabilities have been recorded for these indemnities in the accompanying consolidated balance sheets.

Leases

The Company leases its offices, manufacturing, and warehouse facility in San Diego County under a non-cancelable operating lease. Our corporate headquarters are in a leased space comprising of approximately 29,342 square feet in Escondido, California under a lease that was modified in February 2019 and expires in August 2024. The Company also leases a 3,208 square foot facility in Salt Lake City, Utah that houses our Ion software development team. The Company is the lessee of a leased space comprising approximately 12,880 square feet located in Irvine, California with the lease expiring in June 2021. Bressner Technology GmbH, leases space comprising of 8,073 square feet on a month-to-month basis.

For the three month periods ended March 31, 2021 and 2020, rent expense was $251,130 and $189,417, respectively.

Purchase Commitments

In the normal course of business, the Company enters into purchase commitments for inventory components to be delivered based upon pre-established delivery schedules over a period that may exceed one year.

Customer Concentration

During the three month periods ended March 31, 2021 and 2020, the Company had two customers and in 2020, one customer that had approximately 38%, and 27%, respectively of revenue for which each represented greater than 10% of our consolidated annual revenue.

As of March 31, 2021, the Company had three customers and as of December 31, 2020, one customers that had approximately 58% and 41%, respectively of trade accounts receivables for which each customer's balances represented greater than 10% of our consolidated trade accounts receivable balance.

During the three month periods ended March 31, 2021 and 2020, the Company had approximately 22%, and 18%, respectively of purchases from vendors/suppliers for which each represents greater than 10% of our consolidated purchases.

NOTE 10 – RELATED PARTY TRANSACTIONS

In April 2019, certain members of the Company's Board of Directors executed definitive agreements to commit funds of up to $4,000,000 as a credit facility. The Company initially borrowed $1,150,000 from members of the Board of Directors and $350,000 from other shareholders for a two-year period at an interest rate of 9.5% which requires the Company to make monthly principal and interest payment of $69,000 per month. In connection with these loans, the Company issued to these note holders warrants to purchase shares of the Company's common stock equal to 10% of the original principal at a price per share equal to $2.15 per share. Accordingly, the Company issued to these note holders warrants to purchase 69,766 shares of the Company's common stock. The relative fair value of the warrants issued was $60,158. Interest expense on all related-party notes payable for the three months ended March 31, 2021 and 2020 totaled $3,678 and $17,156, respectively. The remaining unfunded commitments expired as of April 1, 2020, and the Company has not received any additional funding commitments from members of the Board of Directors as of the date of filing of the Quarterly Report on Form 10-Q.

NOTE 11 – NET INCOME (LOSS) PER SHARE

Basic and diluted net loss per share was calculated as follows for the three month periods ended March 31, 2021 and 2020:

	For the Three Months Ended March 31, 2021	2020
Basic and diluted net income (loss) per share:		
Numerator:		
Net income (loss)	$ 41,198	$ (1,096,032)
Denominator:		
Weighted average common shares outstanding - basic	17,348,164	16,332,898
Effect of dilutive securities	1,293,897	-
Weighted average common shares outstanding - diluted	18,642,061	16,332,898
Net income (loss) per common share:		
Basic	$ 0.00	$ (0.07)
Diluted	$ 0.00	$ (0.07)

NOTE 12 – REVENUE, SEGMENT AND GEOGRAPHIC INFORMATION

The Company operates in two reportable segments: the design and manufacture of high-performance customized computers and flash arrays, which is inclusive of in-flight entertainment & connectivity, and value-added reseller with minimal customization. The Company evaluates financial performance on a company-wide basis. As of June 1, 2020, CDI's operations became fully integrated and combined with the operation of OSS' core business operations located in Escondido, California. It is the Company's intention to dissolve CDI as a standalone entity upon resolution of certain outstanding items.

Segment detail for the three month periods ended March 31, 2021 and 2020 is as follows:

	For the Three Months Ended March 31, 2021			For the Three Months Ended March 31, 2020		
	OSS	Bressner	Total	OSS	Bressner	Total
Revenues	$ 8,601,971	$ 4,713,781	$ 13,315,752	$ 8,440,224	$ 4,919,413	$ 13,359,637
Cost of revenues	(5,341,362)	(3,541,606)	(8,882,968)	(6,120,909)	(3,843,041)	(9,963,950)
Gross profit	3,260,609	1,172,175	4,432,784	2,319,315	1,076,372	3,395,687
Gross margin %	37.9%	24.9%	33.3%	27.5%	21.9%	25.4%
Total operating expenses	(3,251,785)	(905,968)	(4,157,753)	(3,986,209)	(920,632)	(4,906,841)
Income from operations	$ 8,824	$ 266,207	$ 275,031	$ (1,666,894)	$ 155,740	$ (1,511,154)

Revenue from customers with non-U.S. billing addresses represented approximately 66% and 50%, of the Company's revenue during the three month periods ended March 31, 2021 and 2020, respectively.

As of March 31, 2021, substantially all the Company's long-lived assets were located in the United States of America with the exception of assets of $215,961 located in Germany.

NOTE 13 – SUBSEQUENT EVENTS

The Company has evaluated subsequent events after the consolidated balance sheet dated as of March 31, 2021 through the date of filing of this quarterly report. Based upon the Company's evaluation, management has determined that, other than as disclosed in the accompanying notes, no subsequent events have occurred that would require recognition in the accompanying consolidated financial statements or disclosure in the notes thereto, other than as disclosed in the accompanying notes and as set forth below.

On April 7, 2021, Bressner Technologies, Inc. received a short-term loan of €500,000 at an interest rate of 1.6% due September 30, 2021.

On May 3, 2021, the Company received notification from the Small Business Administration (SBA) that its Paycheck Protection Program (PPP) Loan of $1,499,360 plus accrued interest had been fully forgiven.

ITEM 2 . MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion and analysis of our financial condition and operating results together with our financial statements and related notes included elsewhere in this Quarterly Report. This discussion and analysis contains forward-looking statements based upon current beliefs, plans and expectations that involve risks, uncertainties and assumptions. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of various factors, including those set forth under "Risk Factors" or in other parts of this Quarterly Report.

Overview

One Stop Systems (OSS) designs, manufactures, and markets specialized high-performance computing modules and systems targeting edge deployments. These specialized computers and storage products incorporate state-of-the art components and allow our customers to offer high-end computing capabilities (often embedded within their equipment) to their target markets. Edge computing is when data is processed/analyzed on devices, that is, at the edge of the network, rather than in the cloud itself. Factors such as increase in load on the cloud infrastructure globally and rises in artificial intelligence (AI) applications, are the major factors driving the growth of the edge computing market. Our customer applications often require connection to a wide array of data sources and sensors, ultra-fast processing power and the ability to quickly access and store large and ever-growing data sets at their location not in the cloud. This equipment requires datacenter class performance optimized for deployment at the edge in challenging environments. Unlike the controlled air-conditioned data center, many of these edge applications have unique requirements including special and compact form factors ruggedized for harsh conditions. We are uniquely positioned as a specialized provider for the high-end of this marketplace providing custom servers, data acquisition platforms, compute accelerators, solid-state storage arrays, system IO expansion systems as well as edge optimized industrial and panel PCs, tablets and handheld compute devices. Our systems also offer industry leading capabilities that occupy less physical space and power consumption. We deliver this high-end technology to our customers through the sale of equipment and embedded software.

We were originally organized as One Stop Systems, LLC, a California limited liability company in 1998 before converting into One Stop Systems, Inc., a California corporation in 1999. On July 6, 2016, we entered into a Merger Agreement and Plan of Reorganization with Mission Technology Group, Inc. ("Magma") whereby Magma merged with and into OSS with OSS continuing as the surviving corporation. We reincorporated as a Delaware corporation on December 14, 2017 and began trading as a public company on the Nasdaq Capital Markets on February 1, 2018.

On August 31, 2018, we acquired Concept Development Inc. ("CDI"), a provider of specialty in-flight entertainment, networking and other aerospace technology located in Irvine, California. As of June 1, CDI has been fully integrated into the core operations of OSS.

On October 31, 2018, we acquired Bressner Technology GmbH ("Bressner") located near Munich, Germany. Bressner provides manufacturing, test, sales and marketing services for customers throughout Europe. Furthermore, Bressner is a valued-added reseller of high technology hardware which expanded the company's high-performance computing product lines to include industrial and panel PCs, tablets and handheld compute devices while also opening up new markets in Europe.

Recent Developments

In March 2020, the World Health Organization declared the outbreak of Coronavirus, or COVID-19, a global pandemic and the United States federal government declared it a national emergency. COVID-19 continues to impact worldwide economic activity. A public health pandemic, including COVID-19, poses the risk that we or our employees, contractors, customers, suppliers, and other partners may be prevented from conducting business activities for an indefinite period of time, including due to shutdowns that may be requested or mandated by governmental authorities.

More generally, COVID-19 raises the possibility of an extended global economic downturn, which could affect demand for our products and services and impact our results and financial condition even after the pandemic is contained and remediation/restriction measures are lifted. For example, we may be unable to collect receivables from customers that are significantly impacted by COVID-19. Also, a decrease in orders in a given period could negatively affect our revenues in future periods. COVID-19 may also have the effect of heightening many of the other risks described in the "Risk Factors" section of our Annual Report on Form 10-K filed on March 25, 2021, including risks associated with our customers and supply chain. We will continue to evaluate the nature and extent of the impact of COVID-19 to our business.

At present, it is clear the global economy has been negatively impacted by COVID-19, and demand for some of our products and services have been reduced due to uncertainty and the economic impact of COVID-19. Specifically, our business has been negatively affected by a range of external factors related to COVID-19 that are not within our control. For example, numerous measures have been implemented by governmental authorities across the globe to contain the virus, including travel bans and restrictions, quarantines, shelter-in-place orders, restrictions and limitations of public gatherings, and business limitations and shutdowns. Many of our customers' businesses have been severely impacted by these measures and some have been required to reduce employee headcount as a result. If a significant number of our customers are unable to continue as a going concern, this would have an adverse impact on our business and financial condition. In addition, many of our customers are working remotely, which may delay the timing of new business and implementations of our services. If COVID-19 continues to have a substantial impact on our partners, customers, or suppliers, our results of operations and overall financial performance will be harmed.

Though management has been proactively managing through the current known impacts, if the situation further deteriorates or the outbreak results in further restriction on both supply and demand factors, our cash flows, financial position and operating results for 2021 and beyond will be negatively impacted. Neither the length of time nor the magnitude of the negative impacts can be presently determined.

The longer the COVID-19 pandemic persists, the greater the potential for significant adverse impact to our business operations. Quarantines, travel restrictions, prohibitions on non-essential gatherings, shelter-in-place orders and other similar directives and policies intended to reduce the spread of the disease, may reduce our productivity and that of the third parties on which we rely and may disrupt and delay many aspects of our business.

The Company is complying with state mandated requirements for safety in the workplace to ensure the health, safety and welling-being of our employees. These measures included personal protective equipment, social distancing, and cleanliness of the facilities and daily monitoring of the health of employees in our facilities. We have not developed a specific and comprehensive contingency plan designed to address the challenges and risks presented by the COVID-19 pandemic and, even if and when we do develop such a plan, there can be no assurance that such plan will be effective in mitigating the potential adverse effects on our business, financial condition and results of operations.

On February 15, 2020, Steve Cooper was terminated as President and CEO of One Stop Systems, Inc., and was replaced by David Raun who is now the president and CEO of the Company.

On April 7, 2020, the Company implemented a cost reduction plan which included the termination of certain employees and elimination of certain costs. Savings from this effort are estimated to be approximately $2.5 million on an annual basis.

On April 24, 2020, the Company completed a $6.0 million debt financing on a non-interest bearing convertible note with a 10% original issue discount. The first tranche of $3.0 million was received on April 27, 2020, with an additional $3.0 million available seven months from the date of closing at the option of the Company conditioned upon meeting certain requirements which have been satisfied. The note is repayable in twenty-two installments beginning three months after closing in cash or shares of the Company's common stock.

On March 1, 2021, the Company entered into a Securities Purchase Agreement with an accredited investor, pursuant to which the Company agreed to issue and sell, in a registered direct offering, 1,497,006 shares of the Company's common stock, par value $0.0001 per share, to the purchaser at an offering price of $6.68 per share. The registered offering was conducted pursuant to the Company's effective shelf registration statement on Form S-3 (Registration No. 333-231513), which was initially filed with the Securities and Exchange Commission on May 15, 2019 and was declared effective on June 19, 2019. As compensation for their services, the Company paid to the placement agents a fee equal to 7% of the gross proceeds received by the Company as a result of the registered offering, and reimbursed the placement agents for certain expenses incurred in connection with such offering. The net proceeds from the registered offering are approximately $9.2 million after deducting certain fees due to the placement agents' and the Company's transaction expenses. The net proceeds received by the Company will be used for general corporate and working capital purposes.

Components of Results of Operations

Revenue

The Company recognizes revenue under accounting standard ASC 606. Revenue is primarily generated from the sale of computer hardware and engineering services and to some extent the sale of software, and sales of software maintenance and support contracts. The Company's performance obligations are satisfied over time as work is performed or at a point in time. The majority of the Company's revenue is recognized at a point in time when products ship and control is transferred to the customer. The Company determines revenue recognition through the following steps: (1) identification of the contract with a customer; (2) identification of the performance obligations in the contract; (3) determination of the transaction price; (4) allocation of the transaction price to the performance obligations in the contract; and (5) recognition of revenue when, or as, a performance obligation is satisfied.

Cost of revenue

Cost of revenue primarily consists of costs of materials, costs paid to third-party contract manufacturers (which may include the costs of components), and personnel costs associated with manufacturing and support operations. Personnel costs consist of wages, bonuses, benefits, stock-based compensation expenses. Cost of revenue also includes freight, allocated overhead costs and inventory write-offs and changes to our inventory and warranty reserves. Allocated overhead costs consist of certain facilities and utility costs. We expect cost of revenue to increase in absolute dollars with an improvement in margin, as product revenue increases.

Operating expenses

Our operating expenses consist of general and administrative, marketing and sales and research and development expenses. Salaries and personnel-related costs, benefits, and stock-based compensation expense, are the most significant components of each category of operating expenses. Operating expenses also include allocated overhead costs for facilities and utility costs.

General and Administrative - General and administrative expense consists primarily of employee compensation and related expenses for administrative functions including finance, legal, human resources, and fees for third-party professional services, as well as allocated overhead. We expect our general and administrative expense to increase in absolute dollars as we continue to invest in growing the business.

Marketing and Selling – Marketing and Selling expense consists primarily of employee compensation and related expenses, sales commissions, marketing programs, travel, and entertainment expenses as well as allocated overhead. Marketing programs consist of advertising, tradeshows, events, corporate communications, and brand-building activities. We expect marketing and selling expenses to increase in absolute dollars as we expand our sales force, increase marketing resources, and further develop sales channels.

Research and Development - Research and development expense consists primarily of employee compensation and related expenses, prototype expenses, depreciation associated with assets acquired for research and development, third-party engineering, and contractor support costs, as well as allocated overhead. We expect our research and development expenses to increase in absolute dollars as we continue to invest in new and existing products.

Other Income (Expense), net

Other income consists of miscellaneous income and income received for activities outside of our core business. Other expense includes expenses for activities outside of our core business.

Provision for Income Taxes

Provision for income taxes consists of estimated income taxes due to the United States and German governments as well as state tax authorities in jurisdictions in which we conduct business, along with the change in our deferred income tax assets and liabilities.

Results of Operations

The following tables set forth our results of operations forthe three month periods ended March 31, 2021 and 2020, presented in dollars and as a percentage of revenue, respectively.

	For the Three Months Ended March 31,	
	2021	2020
Revenue	$ 13,315,752	$ 13,359,637
Cost of revenue	8,882,968	9,963,950
Gross profit	4,432,784	3,395,687
Operating expenses:		
General and administrative	2,157,619	2,514,065
Marketing and selling	1,167,901	1,189,351
Research and development	832,233	1,203,425
Total operating expenses	4,157,753	4,906,841
Income (loss) from operations	275,031	(1,511,154)
Other income (expense), net:		
Interest income	5,300	24,637
Interest expense	(149,982)	(68,784)
Other income (expense), net	(28,629)	(8,029)
Total other income (expense), net	(173,311)	(52,176)
Income (loss) before income taxes	101,720	(1,563,330)
Provision (benefit) for income taxes	60,522	(467,298)
Net income (loss)	$ 41,198	$ (1,096,032)

	For the Three Months Ended March 31,	
	2021	2020
Revenue	100 %	100 %
Cost of revenue	67 %	75 %
Gross profit	33 %	25 %
Operating expenses:		
General and administrative	16 %	19 %
Marketing and selling	9 %	9 %
Research and development	6 %	9 %
Total operating expenses	31 %	37 %
Income (loss) from operations	2 %	-11 %
Other income (expense), net:		
Interest income	0 %	0 %
Interest expense	-1 %	-1 %
Other income (expense), net	0 %	0 %
Total other income (expense), net	-1 %	0 %
Income (loss) before income taxes	1 %	-12 %
Provision (benefit) for income taxes	0 %	-3 %
Net income (loss)	0 %	-8 %

Comparison of the three months ended March 31, 2021 and 2020:

Revenue, cost of revenue and gross profit:

	For the Three Months Ended March 31, 2021				For the Three Months Ended March 31, 2020			
Entity:	Revenue	Cost of Revenue	Gross Profit	Gross Margin %	Revenue	Cost of Revenue	Gross Profit	Gross Margin %
OSS	$ 8,601,971	$ (5,341,362)	$ 3,260,609	37.9 %	$ 8,440,224	$ (6,120,909)	$ 2,319,315	27.5 %
Bressner Technology GmbH	4,713,781	(3,541,606)	1,172,175	24.9 %	4,919,413	(3,843,041)	1,076,372	21.9 %
	$ 13,315,752	$ (8,882,968)	$ 4,432,784	33.3 %	$ 13,359,637	$ (9,963,950)	$ 3,395,687	25.4 %

Revenue

For the three month period ended March 31, 2021, total revenue decreased $43,885 or 0.33%, as compared to the same period in 2020. OSS saw an increase in revenue of $161,747 or 1.21 percentage points as compared to the prior year. The majority of this increase is attributable to an increase in shipments of product to government OEM suppliers creating a change in mix of distributed products as compared to the prior year which was dominated by product shipment to our largest media and entertainment customer. Bressner experienced a decrease of $205,632 or a decrease of 1.54 percentage points. This decrease is mainly due to a general slow-down in Europe attributable to the COVID-19 pandemic.

Cost of revenue and gross profit

Cost of revenue decreased by $1,080,982 or 10.8%, for the three month period ended March 31, 2021 as compared to the prior year in 2020. The decrease in cost of revenue was mainly attributable to our reduced sales in the media and entertainment industry that is a lower margin business as compared to product sales to OEMs engaged in government contracts, thus driving a significant change in products shipped during the quarter. OSS saw a decrease in cost of revenue of $779,547 or 7.8 percentage points as compared to the prior year. Bressner's cost of revenue decrease $301,435 or 3.0 percentage points on lower sales and changes in product mix.

The overall gross margin percentage improved from 25.4% for the three month period March 31, 2020 to 33.3% for the same period ended March 31, 2021, an increase of 7.9 percentage points. OSS' gross margin percentage for the three months ended March 31, 2021 was 37.9%, an increase of 10.5 percentage points as compared to the prior year period of 27.5% attributable to changes in product mix. Bressner contributed gross margin at a rate of 24.9% as compared to the same prior year period in 2020 of 21.9%, an increase of 3.0 percentage points which was attributable to a change in product mix.

Operating expenses

General and administrative expense

General and administrative expense decreased $356,446 or 14.2%, for the three months period ended March 31, 2021 as compared to the same prior year period in 2020. OSS experienced a decrease of $369,625 which was offset by an increase at Bressner of $13,179. The decrease in general and administrative expense was primarily attributable to cost containment efforts initially implemented in April 2020. Overall, total general and administrative expense decreased as a percentage of revenue to 16.2% during the three month period ended March 31, 2021 as compared to 18.8% during the same period in 2020.

Marketing and selling expense

Marketing and selling expense decreased $21,450 or 1.8% during the three month period ended March 31, 2021 as compared to the same prior year period 2020. OSS had a modest increase of $18,433 which was offset by a decrease at Bressner of $39,883 due to less travel associated with COVID-19 restrictions. Overall, total marketing and selling expense decreased as a percentage of revenue to 8.8% during the three month period ended March 31, 2021 as compared to 8.9% during the same period in 2020.

Research and development expense

Research and development expense decreased $371,192 or 30.8% during the three month period ended March 31, 2021 as compared to the same prior year period 2020. OSS saw a decrease of $383,231 or 103.2% of the decrease. The decrease was largely driven by engineering resources being deployed on billable projects for which their costs are reclassified as cost of revenue or classified as work in process labor. This reduction was offset by a modest increase of $12,039 or 3.2% at Bressner. Overall, total research and development expense as a percentage of revenue decreased as a percentage of revenue to 6.2% during the three month period ended March 31, 2021 as compared to 9.0% during the same period in 2020.

Interest income

Interest income decreased $19,337 for the three month period ended March 31, 2021 as compared to the same prior year period in 2020. The decrease is attributable to reduced finance charges on outstanding accounts receivable balances from our largest customer in the media and entertainment industry which has brought their account current.

Interest expense

Interest expense increased $81,198 for the three month period ended March 31, 2021 as compared to same period in 2020. On April 24, 2020, the Company borrowed $3,000,000 through a senior secured convertible debt offering issued with a 10% original issue discount and incurred legal costs associated with this debt offering. The interest and the professional fees incurred on securing the debt are being amortized on an effective interest rate basis to interest expense.

Other income (expense), net

Other income (expense), for the three month period ended March 31, 2021 resulted in net expenses of $28,629 as compared to net other expenses of $8,029 in the same prior year period in 2020, for a net change of $20,600. The majority of the increase is an increase in foreign currency transactions gains and losses.

(Benefit) provision for income taxes

We have recorded an income tax provision (benefit) of $60,522 and $(467,298), respectively, for the three month periods ended March 31, 2021 and 2020. The effective tax rate for the years ended March 31, 2021 and 2020 differs from the statutory rate mainly due to permanent non-deductible goodwill amortization for Bressner Technology GmbH, deductions related to expenses of OSS stock options, as well as projecting federal, foreign and state tax liabilities for the year. The effective tax rate for 2021 is 76.4% as compared to 28.2% in the prior year 2020.

Liquidity and capital resources

Given our prior year operating losses, the Company's primary sources of liquidity have been provided by (i) the Company's February 2018 initial public offering (net proceeds were approximately $16,100,000); (ii) March 2019 notes payable from members of the Board of Directors and others of $1,500,000; (iii) the July 2019 sale of 1,554,546 shares of the Company's common stock for net cash proceeds of $2,488,148; (iv) the April 24, 2020 sale of $3,000,000 of Senior Secured Convertible Promissory Notes issued at a 10% original issue discount; (v) receipt of approximately $1,500,000 on April 28, 2020 of government loan proceeds under the Paycheck Protection Program; and (vi) a receipt of approximately $9,221,000 on March 3, 2021 in a registered direct offering.

As of March 31, 2021, the Company's cash and cash equivalents were $19,614,315 and working capital was $22,935,632. Cash and cash equivalents held by Bressner totaled $1,263,439 (USD) on March 31, 2021, and Bressner's debt covenants do not permit the use of those funds by its parent company. During the three month period ended March 31, 2021, the Company experienced an operating income of $275,031, with cash generated by operating activities of $4,291,066. During the year ended December 31, 2020, the Company experienced an operating loss of $424,281, with cash used in operating activities of $250,173.

Our sources of liquidity and cash flows are used to fund ongoing operations, research and development projects for new products and technologies, and provide ongoing support services for our customers. Over the next year, we anticipate that we will use our liquidity and cash flows from our operations to fund our growth. In addition, as part of our business strategy, we occasionally evaluate potential acquisitions of businesses and products and technologies. Accordingly, a portion of our available cash may be used at any time for the acquisition of complementary products or businesses. Such potential transactions may require substantial capital resources, which may require us to seek additional debt or equity financing. We cannot assure you that we will be able to successfully identify suitable acquisition candidates, complete acquisitions, integrate acquired businesses into our current operations, or expand into new markets. Furthermore, we cannot provide assurances that additional financing will be available to us in any required time frame and on commercially reasonable terms, if at all.

The Company's revenue growth during the year 2020 slowed due to the effects of COVID-19. However, resulting from a reduction in force and strict cost containment, the Company has been able to mitigate the effects, to some degree, of the reduced revenue. For a further description and risk factors associated with COVID-19, please see Part 1A of the December 31, 2020 Annual Report on Form 10-K filed March 25, 2021.

Management's plans are to continue its efforts towards responding to the changing economic landscape attributable to COVID-19, to restructure the Company with the primary objectives of reducing costs, conserving cash, strengthening margins, and improving company-wide execution. Specific actions already implemented by management include a reduction in force, a limited freeze on hiring, reduced work week, minimizing overtime, travel and entertainment, and contractor costs. On April 7, 2020, the Company implemented a cost reduction plan which included the termination of certain employees and elimination of certain costs.

While management expects these actions to result in prospective cost reductions, management is also committed to securing debt and/or equity financing to ensure that liquidity will be sufficient to meet the Company's cash requirements through at least a period of the next twelve months. Management believes potential sources of liquidity include at least the following:

- In May 2019, the Company filed a Form S-3 prospectus with the Securities and Exchange Commission which became effective on June 19, 2019, and allows the Company to offer up to $100,000,000 aggregate dollar amount of shares of its common stock, preferred stock, debt securities, warrants to purchase its common stock, preferred stock or debt securities, subscription rights to purchase its common stock, preferred stock or debt securities and\or units consisting of some or all of these securities, in any combination, together or separately, in one or more offerings, in amounts, at prices and on the terms that the Company will determine at the time of the offering and which will be set forth in a prospectus supplement and any related free writing prospectus.
- On April 24, 2020, the Company completed a $6.0 million debt financing on a non-interest bearing convertible note with a 10% original issue discount. The first tranche of $3.0 million was received on April 27, 2020, with an additional $3.0 million available seven months from the date of closing at the option of the Company conditioned upon meeting certain requirements which have been satisfied. The note is repayable in twenty-two installments beginning three months after closing in cash or shares of the Company's common stock.
- On March 1, 2021, the Company entered into a Securities Purchase Agreement with an accredited investor, pursuant to which the Company agreed to issue and sell, in a registered direct offering, 1,497,006 shares of the Company's common stock, par value $0.0001 per share, to the purchaser at an offering price of $6.68 per share. The registered offering was conducted pursuant to the Company's effective shelf registration statement on Form S-3 (Registration No. 333-231513), which was initially filed with the Securities and Exchange Commission on May 15, 2019; and was declared effective on June 19, 2019. As compensation for their services, the Company paid to the placement agents a fee equal to 7% of the gross proceeds received by the Company as a result of the registered offering, and reimbursed the placement agents for certain expenses incurred in connection with such offering. The net proceeds from the registered offering are approximately $9.22 million after deducting certain fees due to the placement agents' and the Company's transaction expenses. The net proceeds received by the Company will be used for general corporate and working capital purposes.

As a result of management's cost reduction plans, the Company's potential sources of liquidity and management's most recent cash flow forecasts, management believes that the Company has sufficient liquidity to satisfy its anticipated working capital requirements for its ongoing operations and obligations for at least the next twelve months. However, there can be no assurance that management's cost reduction efforts will be effective or the forecasted cash flows will be achieved. Furthermore, the Company shall continue to evaluate its capital expenditure needs based upon factors including but not limited to the Company's sales from operations, growth rate, the timing and extent of spending to support development efforts, the expansion of the Company's sales and marketing, the timing of new product introductions, and the continuing market acceptance of the Company's products and services. If cash generated from operations is insufficient to satisfy the Company's capital requirements, the Company may open a revolving line of credit with a bank, or it may have to sell additional equity or debt securities or obtain expanded credit facilities to fund its operating expenses, pay its obligations, diversify its geographical reach, and grow the Company. In the event such financing is needed in the future, there can be no assurance that such financing will be available to the Company, or, if available, that it will be in amounts and on terms acceptable to the Company. If the Company cannot raise additional funds when it needs or wants them, the Company's operations and prospects could be negatively affected. However, if cash flows from operations become insufficient to continue operations at the current level, and if no additional financing were obtained, then management would restructure the Company in a way to preserve its business while maintaining expenses within operating cash flows.

The following table summarizes our cash flows forthe three month periods ended March 31, 2021 and 2020:

Cash flows:	For the Three Months Ended March 31, 2021	2020
Net cash provided by (used in) operating activities	$ 4,291,066	$ (721,773)
Net cash used in investing activities	$ (121,759)	$ (198,507)
Net cash provided by (used in) financing activities	$ 9,173,593	$ (1,214,119)

Operating Activities

During the three month period ended March 31, 2021, the Company generated$4,291,066 in cash from operating activities, an increase of $5,012,839 when compared to the cash used in operating activities of $721,773 during the same three month period year in 2020. This improvement in operating cash flow is mainly attributable to better earnings resulting from improved gross margins, a reduction in expenses, and reduction in working capital requirement resulting in better collections from customers.

The improvement in cash generated by operating activities was primarily a result of a decrease in working capital requirements of $3,180,719, an improvement in net loss of $1,137,230, and an increase in non-cash adjustments of $694,890. Non-cash adjustments include increases of $794,122 attributable to deferred taxes; gain on disposal of property and equipment, warranty reserves, amortization of deferred gain, inventory reserves, amortization of debt discount and stock-based compensation expense. These increases were offset by $29,232 in decreases in non-cash adjustments attributable to the provision for bad debt depreciation, and amortization.

Working capital requirements were reduced overall by $3,180,719. The sources of working capital of $4,012,890 were attributable to changes inventory levels, prepaid and other current assets and accounts payable and accrued expenses and other liabilities for the comparable period. These sources were offset by reductions in working capital of $832,171 attributable to accounts receivable.

Our ability to generate cash from operations in future periods will depend in large part on our profitability, the rate and timing of collections of our accounts receivable, our inventory turns and our ability to manage other areas of working capital including accounts payable and accrued expenses.

Investing Activities

During the three month period ended March 31, 2021, the Company used cash of $121,759 in investing activities as compared to $198,507 used during the prior year period in 2020, a decrease of $76,748. The main projects for the three months ended March 31, 2021 and 2020 were the continued enhancement of our ERP system, and the purchase of test equipment for the engineering department. We currently do not anticipate any other significant purchases of equipment or expansion of our ERP system beyond completion of phase II of the project, which is the integration of certain sales functions.

Financing Activities

Given the economic and financial hardships operating in a COVID-19 environment, the Company believed it to be imperative to secure additional financial resources to ensure financial stability during trying economic times. During the three month period ended March 31, 2021, the Companygenerated $9,173,593 in cash from financing activities, as compared to the cash used in financing activities of $1,214,119 during the same three month period year in 2020.

During the three month periods ended March 31, 2021and 2020, the Company received proceeds of $278,968 and $57,000, respectively, from the exercise of warrants and stock options which was offset by payment for taxes of $44,252 and $656,845, respectively that was paid on behalf of those that exercised options and RSU’s on a net cashless basis.

On March 1, 2021, the Company entered into a Securities Purchase Agreement with an accredited investor, pursuant to which the Company agreed to issue and sell, in a registered direct offering, 1,497,006 shares of the Company's common stock, par value $0.0001 per share, to the purchaser at an offering price of $6.68 per share. The net proceeds from the registered offering were approximately $9.22 million after deducting certain fees due to the placement agents' and the Company's transaction expenses.

Off balance sheet arrangements

Other than lease commitments incurred in the normal course of business and certain indemnification provisions, we do not have any off-balance sheet financing arrangements or liabilities, guarantee contracts, retained or contingent interests in transferred assets, or any obligation arising out of a material variable interest in an unconsolidated entity.

We do not have any majority-owned subsidiaries that are not consolidated in the financial statements. Additionally, we do not have an interest in, or relationships with, any special purpose entities.

Stockholder transactions

In April 2019, certain members of the Company's Board of Directors executed definitive agreements to commit funds of up to $4,000,000 as a credit facility. The Company initially borrowed $1,150,000 from members of the Board of Directors and $350,000 from other shareholders for a two-year period at an interest rate of 9.5% which requires the Company to make monthly principal and interest payment of $69,000 per month. In connection with these loans, the Company issued to the note holders warrants to purchase shares of the Company's common stock equal to 10% of the original principal at a price per share equal to $2.15 per share. Accordingly, the Company issued to the note holders warrants to purchase 69,766 shares of the Company's common stock. The relative fair value of the warrants issued was $60,158. The remaining unfunded loan commitments expired as of April 1, 2020, and the Company has not received any additional funding commitments from members of the Board of Directors. These are now fully paid as of April 2021.

Critical accounting policies and estimates

In preparing our consolidated financial statements in conformity with U.S. generally accepted accounting principles, management must make a variety of decisions which impact the reported amounts and the related disclosures. These decisions include the selection of the appropriate accounting principles to be applied and the assumptions on which to base accounting estimates. In making these decisions, management applies its judgment based on its understanding and analysis of the relevant circumstances and our historical experience.

Our accounting policies and estimates that are most critical to the presentation of our results of operations and financial condition, and which require the greatest use of judgments and estimates by management, are designated as our critical accounting policies. See further discussion of our critical accounting policies under Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations," in our Annual Report on Form 10-K for year ended December 31, 2020. We periodically re-evaluate and adjust our critical accounting policies as circumstances change. There were no significant changes to our critical accounting policies during the three month period ended March 31, 2021.

Recently implemented accounting pronouncements

Per the Company's consolidated financial statements Note 2 – Significant Accounting Policies, we have implemented a number of changes, as required by FASB. See Note 2 of the accompanying financial statements for further details.

Interest rate risk

Our exposure to interest rate risk is primarily associated with borrowing on revolving lines of credit denominated in both U.S. dollars and Euros. We are exposed to the impact of interest rate changes primarily through our borrowing activities for our variable rate borrowings.

Concentration of credit risk

Financial instruments that potentially expose us to concentrations of credit risk consist principally of cash, cash equivalents, and accounts receivable. We place our cash and cash equivalents with financial institutions with high credit quality. On March 31, 2021 and December 31, 2020, we had $19,614,315 and $6,316,921, respectively, of cash and cash equivalents on deposit or invested with our financial and lending institutions. We provide credit to our customers in the normal course of business. We perform ongoing credit evaluations of our customers' financial condition and limit the amount of credit extended when deemed necessary.

Foreign currency risk

We operate primarily in the United States. Foreign sales of products and services are primarily denominated in U.S. dollars. We also conduct business outside the United States through our foreign subsidiary in Germany, where business is largely transacted in non-U.S. dollar currencies particularly the Euro, which is subject to fluctuations due to changes in foreign currency exchange rates. Accordingly, we are subject to exposure from changes in the exchange rates of local currencies. Foreign currency transaction gains and losses are recorded in other income (expense), net in the consolidated statements of operations.

OSS GmbH operates as an extension of OSS' domestic operations and acquired Bressner Technology GmbH in October 2018. The functional currency of OSS GmbH is the Euro. Transactions denominated in currencies other than the functional currency are remeasured to the functional currency at the average exchange rate in effect during the period. At the end of each reporting period, monetary assets and liabilities are translated using exchange rates in effect at the balance sheet date. Non-monetary assets and liabilities are remeasured at historical exchange rates. Consequently, changes in the exchange rates of the currencies may impact the translation of the foreign subsidiaries' statements of operations into U.S. dollars, which may in turn affect our consolidated statement of operations. The resulting foreign currency translation adjustments are recorded as a separate component of accumulated other comprehensive income in the consolidated statement of comprehensive income.

Derivative Financial Instruments

We employ derivatives on a periodic basis to manage certain market risks through the use of foreign exchange forward contracts. We do not use derivatives for trading or speculative purposes. Our derivatives are designated as a hedge of a forecasted transaction or of the variability of cash flows to be received or paid related to a recognized asset or liability (cash flow hedge). We hedge a portion of the exchange risk involved in anticipation of highly probable foreign currency-denominated transactions. In anticipation of these transactions, we may enter into foreign exchange contracts to provide currency at a fixed rate.

Non-GAAP Financial Measures

Adjusted EBITDA

We believe that the use of adjusted earnings before interest, taxes, depreciation and amortization, or adjusted EBITDA, is helpful for an investor to assess the performance of the Company. The Company defines adjusted EBITDA as income (loss) before interest, taxes, depreciation, amortization, acquisition expenses, impairment of long-lived assets, financing costs, fair value adjustments from purchase accounting, stock-based compensation expense and expenses related to discontinued operations.

Adjusted EBITDA is not a measurement of financial performance under generally accepted accounting principles in the United States, or GAAP. Because of varying available valuation methodologies, subjective assumptions and the variety of equity instruments that can impact a company's non-cash operating expenses, we believe that providing a non-GAAP financial measure that excludes non-cash and non-recurring expenses allows for meaningful comparisons between our core business operating results and those of other companies, as well as providing us with an important tool for financial and operational decision making and for evaluating our own core business operating results over different periods of time.

Our adjusted EBITDA measure may not provide information that is directly comparable to that provided by other companies in our industry, as other companies in our industry may calculate non-GAAP financial results differently, particularly related to non-recurring, unusual items. Our adjusted EBITDA is not a measurement of financial performance under GAAP, and should not be considered as an alternative to operating income or as an indication of operating performance or any other measure of performance derived in accordance with GAAP. We do not consider adjusted EBITDA to be a substitute for, or superior to, the information provided by GAAP financial results.

	For the Three Months Ended March 31,	
	2021	2020
Net income (loss)	$ 41,198	$ (1,096,032)
Depreciation and amortization	380,778	395,825
Amortization of deferred gain	-	(41,479)
Stock-based compensation expense	438,394	207,761
Interest expense	149,982	68,784
Interest income	(5,300)	(24,637)
Provision (benefit) for income taxes	60,522	(467,298)
Adjusted EBITDA	$ 1,065,574	$ (957,076)

Adjusted EPS

Adjusted EPS excludes the impact of certain items and therefore, has not been calculated in accordance with GAAP. We believe that exclusion of certain selected items assists in providing a more complete understanding of our underlying results and trends and allows for comparability with our peer company index and industry. We use this measure along with the corresponding GAAP financial measures to manage our business and to evaluate our performance compared to prior periods and the marketplace. The Company defines Non-GAAP (loss) income as (loss) or income before amortization, stock-based compensation, expenses related to discontinued operations, impairment of long-lived assets and non-recurring acquisition costs. Adjusted EPS expresses adjusted (loss) income on a per share basis using weighted average diluted shares outstanding.

Adjusted EPS is a non-GAAP financial measure and should not be considered in isolation or as a substitute for financial information provided in accordance with GAAP. These non-GAAP financial measures may not be computed in the same manner as similarly titled measures used by other companies. We expect to continue to incur expenses similar to the adjusted income from continuing operations and adjusted EPS financial adjustments described above, and investors should not infer from our presentation of these non-GAAP financial measures that these costs are unusual, infrequent or non-recurring.

The following table reconciles Non-GAAP net income and basic and diluted earnings per share:

	For the Three Months Ended March 31,	
	2021	2020
Net income (loss)	$ 41,198	$ (1,096,032)
Amortization of intangibles	163,900	174,525
Stock-based compensation expense	438,394	207,761
Non-GAAP net income (loss)	$ 643,492	$ (713,746)
Non-GAAP net income (loss) per share:		
Basic	$ 0.04	$ (0.04)
Diluted	$ 0.03	$ (0.04)
Weighted average common shares outstanding:		
Basic	17,348,164	16,332,898
Diluted	18,642,061	16,332,898

Free Cash Flow

Free cash flow, a non-GAAP measure for reporting cash flow, is defined as cash provided by or used in operating activities less capital expenditures for property and equipment, which includes capitalized software development costs for the implementation of the Company's ERP system. We believe free cash flow provides investors with an important perspective on cash available for investments and acquisitions after making capital investments required to support ongoing business operations and long-term value creation. We believe that trends in our free cash flow can be valuable indicators of our operating performance and liquidity.

Free cash flow is a non-GAAP financial measure and should not be considered in isolation or as a substitute for financial information provided in accordance with GAAP. This non-GAAP financial measure may not be computed in the same manner as similarly titled measures used by other companies.

We expect to continue to incur expenditures similar to the free cash flow adjustments described above, and investors should not infer from our presentation of this non-GAAP financial measure that these expenditures reflect all of our obligations which require cash. The following table reconciles cash provided by or used in operating activities, the most directly comparable GAAP financial measure, to free cash flow:

	For the Three Months Ended March 31,	
Cash flow:	**2021**	**2020**
Cash provided by (used in) operating activities	$ 4,291,066	$ (721,773)
Capital expenditures	(121,759)	(200,049)
Free cash flow	$ 4,169,307	$ (921,822)

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Not Applicable.

Item 4. Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our periodic and current reports that we file with the SEC is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms; and that such information is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure.

Limitation on Effectiveness of Controls

The design of any control system is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals. The inherent limitations in any control system include the realities that judgments related to decision-making can be faulty, and that reduced effectiveness in controls can occur because of simple errors or mistakes. Due to the inherent limitations in a cost-effective control system, misstatements due to error may occur and may not be detected.

Evaluation of Disclosure Controls and Procedures

Management is required to evaluate our disclosure controls and procedures, as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 (the "Exchange Act"). Disclosure controls and procedures are controls and other procedures designed to provide reasonable assurance that information required to be disclosed in our reports filed under the Exchange Act, such as this Quarterly Report on Form 10-Q, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include controls and procedures designed to provide reasonable assurance that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. Based on our management's evaluation (with the participation of our principal executive officer and principal financial officer), our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) were effective at a reasonable assurance level as of the end of the period covered by this report.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting during the quarter ended March 31, 2021, which were identified in connection with management's evaluation required by paragraph (d) of Rules 13a-15 and 15d-15 under the Exchange Act, that have materially affected or are reasonably likely to materially affect our internal control over financial reporting.

PART II—OTHER INFORMATION

Item 1. Legal Proceedings.

For a description of our material pending legal proceeding, please see Note 9, Commitments and Contingencies, to our condensed consolidated financial statements included in Part I, Item 1 of this Quarterly Report on Form 10-Q.

Item 1A. Risk Factors.

Please carefully consider the information set forth in this Quarterly Report on Form 10-Q and the risk factors discussed in Part I, Item IA. of our Annual Report on Form 10-K for the year ended December 31, 2020, which could materially affect our business, financial condition, or future results. In evaluating our business, you should carefully consider the risk factors discussed in our Annual Report on Form 10-K, as updated by our subsequent filings under the Exchange Act. The occurrence of any of the risks discussed in such filings, or other events that we do not currently anticipate or that we currently deem immaterial, could harm our business, prospects, financial condition and results of operations. In that case, the trading price of our common stock could decline, and you may lose all or part of your investment.

We must successfully navigate the demand, supply and operational challenges associated with the ongoing coronavirus (COVID-19) pandemic.

Our business has been negatively affected by a range of external factors related to COVID-19 that are not within our control. For example, numerous measures have been implemented by governmental authorities across the globe to contain the virus, including travel bans and restrictions, quarantines, shelter-in-place orders, restrictions and limitations of public gatherings, and business limitations and shutdowns. Many of our customers' businesses have been severely impacted by these measures and some have been required to reduce employee headcount as a result. If a significant number of our customers are unable to continue as a going concern, this would have an adverse impact on our business and financial condition. In addition, many of our customers are working remotely, which may delay the timing of new business and implementations of our services. If COVID-19 continues to have a substantial impact on our partners, customers, or suppliers, our results of operations and overall financial performance will be harmed.

The impacts of COVID-19 on our business, customers, partners, suppliers, employees, markets and financial results and condition are uncertain, evolving and dependent on numerous unpredictable factors outside of our control, including:

- the spread, duration and severity of COVID-19 as a public health matter and its impact on governments, businesses and society generally and our clients, partners, suppliers and our business more specifically;
- the measures being taken by governments, businesses and society in response to COVID-19 and the effectiveness of those measures, including our suppliers in China experiencing delays due to the Chinese government's response to COVID-19;
- the scope and effectiveness of fiscal and monetary stimulus programs and other legislative and regulatory measures being implemented by federal, state and local governments in response to COVID-19;
- the duration and impact of the numerous measures implemented by governmental authorities throughout the country to contain COVID-19, including travel bans and restrictions, quarantines, shelter-in-place orders, restrictions and limitations on public gatherings, and business limitations and shutdowns;
- the increase in business failures or slowdowns among our customers, suppliers, and other businesses;
- the pace and extent to which our customers and other businesses are able to operate and/or reduce their number of employees and other compensated individual; the willingness of current and prospective clients to invest in our products and services; and
- the satisfaction of customers with product and service remote delivery and support

If we are not able to respond to and manage the impact of such events effectively, our business will be harmed.

It is clear the global economy has been negatively impacted by COVID-19, and demand for some of our products and services has been reduced due to uncertainty and the economic impact of COVID-19. In particular, in the media and entertainment and commercial airlines industries, demand for the use of outdoor media equipment has been impacted due to restrictions on public gatherings and the airlines industry has been impacted by reduced travel. Until such restrictions improve, we expect that demand for certain of our clients' products and services will be limited, and thus, may impact our financial results and operations.

More generally, COVID-19 raises the possibility of an extended global economic downturn, which could affect demand for our products and services and impact our results and financial condition even after the pandemic is contained and remediation/restriction measures are lifted. For example, we may be unable to collect receivables from customers that are significantly impacted by COVID-19. Also, a decrease in orders in a given period could negatively affect our revenues in future periods. COVID-19 may also have the effect of heightening many of the other risks described in the "Risk Factors" section of our Annual Report on Form 10-K, including risks associated with our customers and supply chain. We will continue to evaluate the nature and extent of the impact of COVID-19 to our business.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

The information set forth below relates to our issuances of securities without registration under the Securities Act of 1933 during the reporting period which were not previously included in an Annual Report on Form 10-K, Quarterly Report on Form 10-Q, or Current Report on Form 8-K:

During the three months ended March 31, 2021, the Company issued 35,067 shares of common stock upon the exercise of warrants for total proceeds of $65,000.

These securities were issued pursuant to Section 4(a)(2) of the Securities Act and/or Rule 506 promulgated thereunder. The holders represented their intention to acquire the securities for investment only and not with a view towards distribution. The investors were given adequate information about us to make an informed investment decision. We did not engage in any general solicitation or advertising.

Item 3. Defaults Upon Senior Securities.

None.

Item 4. Mine Safety Disclosures.

Not Applicable.

Item 5. Other Information.

None.

Item 6. Exhibits.

Exhibit Index

Exhibit Number	Description
2.1 (1)	Agreement and Plan of Merger and Reorganization, dated August 22, 2018, with Concept Development Inc.
2.2 (2)	Share Purchase Agreement, dated October 31, 2018, with Bressner Technology GmbH.
3.1 (3)	Amended and Restated Certificate of Incorporation (currently in effect).
3.2 (4)	Bylaws, as amended (currently in effect).
4.1 (5)	Second Amended and Restated Investors' Rights Agreement, dated January 2007.
4.2 (5)	Common Shareholder Piggyback Registration Rights Agreement, dated July 15, 2016.
10.1+ (6)	Form of Indemnification Agreement between One Stop Systems, Inc. and each its directors and executive officers.
10.2+ (5)	One Stop Systems, Inc. 2000 Stock Option Plan and related form agreements.
10.3+ (5)	One Stop Systems, Inc. 2011 Stock Option Plan and related form agreements.
10.4+ (5)	One Stop Systems, Inc. 2015 Stock Option Plan and related form agreements.
10.5+ (5)	One Stop Systems, Inc. 2017 Stock Equity Incentive Plan and related form agreements.
10.6 (12)	Amendment No. 1 to the 2017 Stock Equity Incentive Plan.
10.7 (6)	Lease Agreement dated October 21, 2004, as amended.
10.8 (1)	Piggyback Registration Rights Agreement by and between One Stop Systems, Inc. and James M. Reardon, dated August 31, 2018.
10.9 (7)	Form of Binding Commitment Letter.
10.10 (8)	Executive Employment Agreement between One Stop Systems, Inc., and David Raun, dated March 24, 2020.
10.11 (9)	Form of Senior Secured Convertible Promissory Note.
10.12 (9)	Form of Securities Purchase Agreement, dated April 20, 2020, by and between the Company and the investors
10.13 (9)	Form of Security Agreement, dated April 20, 2020, by and between the Company, certain of its subsidiaries and the investors
10.14 (9)	Form of Intercreditor Agreement, dated April 20, 2020, by and between the Company, the investors and certain secured parties
10.15 (10)	Senior Secured Convertible Promissory Note, dated April 24, 2020, by and between the Company and the investor
10.16 (11)	Promissory Note, dated as of April 28, 2020, by and between One Stop Systems, Inc., as Borrower, and Cache Valley Bank, as Lender.
10.17 (12)	Employment Agreement between One Stop Systems, Inc., and David Raun, dated June 24, 2020.
10.18 (13)	Form of Securities Purchase Agreement
10.19 (13)	Form of Placement Agency Agreement

Exhibit Index

31.1*	Certification of Principal Executive Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.**
31.2*	Certification of Principal Financial Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.**
32.1*	Certification of Principal Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.**
32.2*	Certification of Principal Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.**
101.INS*	XBRL Instance Document
101.SCH*	XBRL Taxonomy Extension Schema Document
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF*	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB*	XBRL Taxonomy Extension Label Linkbase Document
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase Document

(1) Incorporated by reference to Amendment No.1 to the Registrant's Current Report on Form 8-K filed with the SEC on March 21, 2019.
(2) Incorporated by reference to the Registrant's Current Report on Form 8-K filed with the SEC on February 6, 2019.
(3) Incorporated by reference to the Registrant's Registration Statement on Form S-1 (Registration No. 333-222121) filed with the SEC on December 18, 2017.
(4) Incorporated by reference to Amendment No. 1 to the Registrant's Registration Statement on Form S-1 (Registration No. 333-222121) filed with the SEC on January 16, 2019.
(5) Incorporated by reference to the Registrant's Current Report on Form 8-K filed with the SEC on February 1, 2019.
(6) Incorporated by reference to the Registrant's Current Report on Form 8-K filed with the SEC on August 3, 2019.
(7) Incorporated by reference to the Registrant's Current Report on Form 8-K filed with the SEC on September 6, 2019.
(8) Incorporated by reference to the Registrant's Current Report on Form 8-K filed with the SEC on November 6, 2019.
(9) Incorporated by reference to the Registrant's Quarterly Report on Form 10-Q filed with the SEC on May 9, 2020.
(10) Incorporated by reference to the Registrant's Current Report on Form 8-K filed with the SEC on June 26, 2020.
(11) Incorporated by reference to the Registrant's Current Report on Form 8-K filed with the SEC on August 8, 2020.
(12) Incorporated by reference to the Registrant's Quarterly Report on Form 10-Q filed with the SEC on August 8, 2020.
(13) Incorporated by reference to the Registrant's Current Report on Form 8-K filed with the SEC on March 3, 2021.
+ Indicates management contract or compensatory plan.

* Filed herewith.

** These certifications are being furnished solely to accompany this quarterly report pursuant to 18 U.S.C. Section 1350, and are not being filed for purposes of Section 18 of the Securities Exchange Act of 1934 and are not to be incorporated by reference into any filing of the Registrant, whether made before or after the date hereof, regardless of any general incorporation language in such filing.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

ONE STOP SYSTEMS, INC.

Date: May 13, 2021	By:	/s/ David Raun
		David Raun
		President and Chief Executive Officer
		(Principal Executive Officer)
Date: May 13, 2021	By:	/s/ John W. Morrison Jr.
		John W. Morrison Jr.
		Chief Financial Officer
		(Principal Financial and Accounting Officer)

Exhibit 31.1

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER PURSUANT TO RULES 13a-14(a) AND 15d-14(a) UNDER THE SECURITIES EXCHANGE ACT OF 1934, AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, David Raun, certify that:

1. I have reviewed this quarterly report on Form 10-Q of One Stop Systems, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) [paragraph omitted in accordance with Exchange Act Rule 13a-14(a)];

   (c) evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):

   (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 13, 2021

By: /s/ David Raun
David Raun
President and Chief Executive Officer
(Principal Executive Officer)

Exhibit 31.2

CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER PURSUANT TO RULES 13a-14(a) AND 15d-14(a) UNDER THE SECURITIES EXCHANGE ACT OF 1934, AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, John W. Morrison Jr., certify that:

1. I have reviewed this quarterly report on Form 10-Q of One Stop Systems, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) [paragraph omitted in accordance with Exchange Act Rule 13a-14(a)];

   (c) evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):

   (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 13, 2021

By: /s/ John W. Morrison Jr.

John W. Morrison Jr.
Chief Financial Officer
(Principal Financial and Accounting Officer)

Exhibit 32.1

**CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER PURSUANT TO
18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of One Stop Systems, Inc. (the "Company") on Form 10-Q for the period ending March 31, 2021, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, David Raun, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

Date: May 13, 2021

By: /s/ David Raun
David Raun
President and Chief Executive Officer
(Principal Executive Officer)

Exhibit 32.2

**CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER PURSUANT TO
18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of One Stop Systems, Inc. (the "Company") on Form 10-Q for the period ending March 31, 2021 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, John W. Morrison Jr., Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

Date: May 13, 2021

By: /s/ John W. Morrison Jr.
John W. Morrison Jr.
Chief Financial Officer
(Principal Accounting and Financial Officer)