

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (D) OF THE SECURITIES AND EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2020

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (D) OF THE SECURITIES AND EXCHANGE ACT OF 1934

For the transition period from _____ to _____

QUEST PATENT RESEARCH CORPORATION

(Exact Name of Registrant as Specified in Charter)

Delaware (State or other jurisdiction of incorporation)	33-18099-NY (Commission File Number)	11-2873662 (IRS Employer Identification No.)
411 Theodore Fremd Ave., Suite 206S, Rye, NY (Address of principal executive offices)		10580-1411 (Zip Code)

Registrant's telephone number, including area code: **(888) 743-7577**

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	<input type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input checked="" type="checkbox"/>	Smaller reporting company	<input checked="" type="checkbox"/>
		Emerging growth company	<input type="checkbox"/>

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

Securities registered pursuant to Section 12(b) of the Act: None

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. 383,038,334 shares of common stock are issued and outstanding as of November 16, 2020.

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This report contains forward-looking statements regarding our business, financial condition, results of operations and prospects. Words such as “expects,” “anticipates,” “intends,” “plans,” “believes,” “seeks,” “estimates” and similar expressions or variations of such words are intended to identify forward-looking statements, but are not deemed to represent an all-inclusive means of identifying forward-looking statements as denoted in this report. Additionally, statements concerning future matters are forward-looking statements.

Although forward-looking statements in this report reflect the good faith judgment of our management, such statements can only be based on facts and factors currently known by us. Consequently, forward-looking statements are inherently subject to risks and uncertainties and actual results and outcomes may differ materially from the results and outcomes discussed in or anticipated by the forward-looking statements. Factors that could cause or contribute to such differences in results and outcomes include, without limitation, those specifically addressed under the headings “Risks Factors” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in our report on Form 10-K for the year ended December 31, 2019, in “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in this Form 10-Q and in other reports that we file with the SEC. You are urged not to place undue reliance on these forward-looking statements, which speak only as of the date of this report.

We file reports with the SEC. The SEC maintains a website (www.sec.gov) that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC, including us. You can also read and copy any materials we file with the SEC at the SEC’s Public Reference Room at 100 F Street, NE, Washington, DC 20549. You can obtain additional information about the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330.

We undertake no obligation to revise or update any forward-looking statements in order to reflect any event or circumstance that may arise after the date of this report, except as required by law. Readers are urged to carefully review and consider the various disclosures made throughout the entirety of this quarterly report, which are designed to advise interested parties of the risks and factors that may affect our business, financial condition, results of operations and prospects.

OTHER PERTINENT INFORMATION

Unless specifically set forth to the contrary, “Quest”, “Company”, “we,” “us,” “our” and similar terms refer to Quest Patent Research Corporation, and its subsidiaries, unless the context indicates otherwise.

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

QUEST PATENT RESEARCH CORPORATION AND SUBSIDIARIES UNAUDITED CONSOLIDATED BALANCE SHEETS

	<u>September 30,</u> <u>2020</u>	<u>December 31,</u> <u>2019</u>
ASSETS		
Current assets		
Cash and cash equivalents	\$ 91,879	\$ 537,198
Accounts receivable	1,850,667	1,850,375
Other current assets	9,647	17,180
Total current assets	<u>1,952,193</u>	<u>2,404,753</u>
Patents, net of accumulated amortization of \$2,127,530 and \$1,617,762 respectively	2,339,586	2,754,354
Total assets	<u>\$ 4,291,779</u>	<u>\$ 5,159,107</u>
LIABILITIES AND STOCKHOLDERS’ DEFICIT		
Liabilities		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 2,714,721	\$ 3,362,932
Accrued liabilities – related party	564,050	-
Loans payable – third party	147,000	147,000
Purchase price of patents, current portion, net of unamortized discount of \$0	975,000	569,386
Loan payable – related party, net of unamortized discount and debt issuance costs of \$0 and \$189,705, respectively	4,672,810	4,483,105
Accrued interest – loan payable related party	117,780	117,780
Accrued interest - loans payable third party	281,210	270,185
Derivative liability	-	595,000
Total current liabilities	<u>9,472,571</u>	<u>9,545,388</u>
Non-current liabilities		
Contingent funding liabilities	20,378	20,378
Loans payable – SBA	172,974	-
Purchase price of patents, net of unamortized discount of \$155,019 and \$282,503, respectively	1,159,981	1,442,497
Total liabilities	<u>10,825,904</u>	<u>11,008,263</u>
Stockholders’ deficit:		
Preferred stock – par value \$.00003 per share – authorized 10,000,000 Shares – no shares issued and outstanding	-	-
Common stock, par value \$0.00003 per share; authorized 10,000,000,000 shares and 10,000,000,000 at September 30, 2020 and December 31, 2019; shares issued and outstanding 383,038,334 at September 30, 2020 and December 31, 2019	11,491	11,491
Additional paid-in capital	14,427,782	14,107,782
Accumulated deficit	(20,973,631)	(19,968,668)
Total Quest Patent Research Corporation deficit	<u>(6,534,358)</u>	<u>(5,849,395)</u>
Non-controlling interest in subsidiary	233	239
Total stockholders’ deficit	<u>(6,534,125)</u>	<u>(5,849,156)</u>
Total liabilities and stockholders’ deficit	<u>\$ 4,291,779</u>	<u>\$ 5,159,107</u>

See accompanying notes to unaudited consolidated financial statements.

QUEST PATENT RESEARCH CORPORATION AND SUBSIDIARIES
UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS

	FOR THE THREE MONTHS ENDED SEPTEMBER 30,		FOR THE NINE MONTHS ENDED SEPTEMBER 30,	
	2020	2019	2020	2019
	Revenues			
Patent licensing fees	\$ 3,404,985	\$ 640,000	\$ 5,488,088	\$ 2,002,418
Licensed packaging sales	-	-	-	25,274
	<u>3,404,985</u>	<u>640,000</u>	<u>5,488,088</u>	<u>2,027,692</u>
Operating expenses				
Cost of revenue:				
Cost of sales	-	-	-	4,520
Litigation and licensing expenses	2,996,416	555,474	4,714,406	1,400,003
Management support services	-	150	-	1,793
Selling, general and administrative expenses	301,853	302,574	1,213,151	945,601
Total operating expenses	<u>3,298,269</u>	<u>858,198</u>	<u>5,927,557</u>	<u>2,351,917</u>
Income/(loss) from operations	106,716	(218,198)	(439,469)	(324,225)
Other Income and (expenses)				
Gain/(loss) on derivative liability	175,000	290,000	275,000	(270,000)
Other income	1,000	-	1,000	-
Interest expense	(233,101)	(216,336)	(776,137)	(590,828)
Total other income (expenses)	<u>(57,101)</u>	<u>73,664</u>	<u>(500,137)</u>	<u>(860,828)</u>
Net income (loss) before income tax	49,615	(144,534)	(939,606)	(1,185,053)
Income tax	-	-	(65,363)	(225)
Net income/(loss)	49,615	(144,534)	(1,004,969)	(1,185,278)
Net (income)/loss attributable to non-controlling interest in subsidiaries	6	(347)	6	1,558
Net income/(loss) attributable to Quest Patent Research Corporation	<u>\$ 49,621</u>	<u>\$ (144,881)</u>	<u>\$ (1,004,963)</u>	<u>\$ (1,183,720)</u>
Income (loss) per share basic and diluted	<u>\$ 0.00</u>	<u>\$ (0.00)</u>	<u>\$ (0.00)</u>	<u>\$ (0.00)</u>
Weighted average shares outstanding – basic and diluted	<u>383,038,334</u>	<u>383,038,334</u>	<u>383,038,334</u>	<u>383,038,334</u>

See accompanying notes to unaudited consolidated financial statements.

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QUEST PATENT RESEARCH CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' DEFICIT

	Common Stock		Additional Paid-in Capital	Deficit	Non- controlling Interest in Subsidiaries	Total Stockholders' Deficit
	Shares	Amount				
Balances as of December 31, 2018	383,038,334	11,491	14,107,782	(18,659,892)	1,758	(4,538,861)
Net loss	-	-	-	(539,809)	(259)	(540,068)
Balance as of March 31, 2019	383,038,334	11,491	14,107,782	(19,199,701)	1,499	(5,078,929)
Net loss	-	-	-	(499,030)	(1,646)	(500,676)
Balance as of June 30, 2019	383,038,334	11,491	14,107,782	(19,698,731)	(147)	(5,579,605)
Net income (loss)	-	-	-	(144,881)	347	(144,534)
Balances as of September 30, 2019	<u>383,038,334</u>	<u>\$ 11,491</u>	<u>\$ 14,107,782</u>	<u>\$ (19,843,612)</u>	<u>\$ 200</u>	<u>\$ (5,724,139)</u>

	Common Stock		Additional Paid-in Capital	Deficit	Non- controlling Interest in Subsidiaries	Total Stockholders' Deficit
	Shares	Amount				
Balances as of December 31, 2019	383,038,334	11,491	14,107,782	(19,968,668)	239	(5,849,156)
Net loss	-	-	-	(682,798)	-	(682,798)
Balance as of March 31, 2020	383,038,334	11,491	14,107,782	(20,651,466)	239	(6,531,954)
Net loss	-	-	-	(371,786)	-	(371,786)
Balance as of June 30, 2020	383,038,334	11,491	14,107,782	(21,023,252)	239	(6,903,740)
Resolution of derivative liability	-	-	320,000	-	-	320,000
Net income/(loss)	-	-	-	49,621	(6)	49,615
Balances as of September 30, 2020	<u>383,038,334</u>	<u>\$ 11,491</u>	<u>\$ 14,427,782</u>	<u>\$ (20,973,631)</u>	<u>\$ 233</u>	<u>\$ (6,534,125)</u>

See accompanying notes to unaudited consolidated financial statements.

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QUEST PATENT RESEARCH CORPORATION AND SUBSIDIARIES
UNAUDITED CONSOLIDATED STATEMENT OF CASH FLOWS

For the
Nine Months Ended
September 30,

	2020	2019
Cash flows from operating activities:		
Net loss	\$ (1,004,969)	\$ (1,185,278)
Adjustments to reconcile net loss to net cash provided by/(used in) operating activities:		
Amortization of debt discount	412,189	254,133
(Gain)/loss on derivative liability	(275,000)	270,000
Depreciation and amortization	509,768	388,402
Changes in operating assets and liabilities:		
Accounts receivable	(292)	(524,897)
Accrued interest – loans payable related party	-	(25,000)
Accrued interest – loans payable third party	12,267	12,225
Other current assets	7,533	(17,467)
Accounts payable and accrued expenses	(84,161)	1,235,971
Net cash provided by/(used in) operating activities	(422,665)	408,089
Cash flows from investing activities:		
Purchase of patents	(95,000)	(75,000)
Net cash used in investing activities	(95,000)	(75,000)
Cash flows from financing activities:		
Proceeds from sale of future revenue	95,000	-
Proceeds from SBA loans	171,732	-
Repayment of purchase price of patents	(194,386)	(155,614)
Net cash provided by/(used in) financing activities	72,346	(155,614)
Net increase (decrease) in cash and cash equivalents	(445,319)	177,475
Cash and cash equivalents at beginning of period	537,198	166,911
Cash and cash equivalents at end of period	\$ 91,879	\$ 344,386
Non-cash investing and financing activities		
Accounts payable for patent purchase, net of imputed interest of \$336,781	-	1,238,219
Resolution of derivative liability	320,000	-
Supplemental disclosure of cash flow information:		
Cash paid during the period for:		
Income taxes, including foreign taxing authorities withheld taxes of \$65,363 and \$225 during the periods ended September 30, 2020, and 2019 respectively.	65,363	225
Interest	350,000	349,500

See accompanying notes to unaudited consolidated financial statements.

QUEST PATENT RESEARCH CORPORATION
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2020

NOTE 1 – DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

The Company is a Delaware corporation, incorporated on July 17, 1987 and has been engaged in the intellectual property monetization business since 2008.

As used herein, the “Company” refers to Quest Patent Research Corporation and its wholly-owned and majority-owned and controlled operating subsidiaries unless the context indicates otherwise. All intellectual property acquisition, development, licensing and enforcement activities are conducted by the Company’s operating subsidiaries.

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the US (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, these interim financial statements do not include all of the information and notes required by GAAP for complete financial statements. All adjustments (consisting of normal recurring items) necessary to present fairly the Company’s consolidated financial position have been included. These interim financial statements should be read in conjunction with the consolidated financial statements and accompanying notes included in our Annual Report on Form 10-K for the year ended December 31, 2019. Operating results for the interim periods presented herein are not necessarily indicative of the results that may be expected for any other interim period or for the entire year. Reclassifications have been made to conform with the current year presentation.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of consolidation and financial statement presentation

The consolidated financial statements are prepared in accordance with U.S. generally accepted accounting principles (“US GAAP”) and present the consolidated financial statements of the Company and its wholly-owned and majority-owned subsidiaries as of September 30, 2020.

The consolidated financial statements include the accounts and operations of:

Quest Patent Research Corporation (“the Company”)

Quest Licensing Corporation (NY) (wholly owned)

Quest Licensing Corporation (DE) (wholly owned)

Quest Packaging Solutions Corporation (90% owned)

Quest Nettech Corporation (65% owned)

Semcon IP, Inc. (wholly owned)

Mariner IC, Inc. (wholly owned)

IC Kinetics, Inc. (wholly owned)

CXT Systems, Inc. (wholly owned)

Photonic Imaging Solutions Inc. (wholly owned)

M-RED Inc. (wholly owned)

Prior to April 2019, the operations of Wynn Technologies, Inc. were not included in the Company's consolidated financial statements as there were significant contingencies related to its control of Wynn Technologies, Inc. The sole asset of Wynn Technologies, Inc. was US Patent No. RE38,137E. Wynn Technologies, Inc. could not transfer, assign, sell, hypothecate or otherwise encumber US Patent No. RE38,137E without the express written consent of the owner of 35% of Wynn Technologies, Inc., unless, as of the date of such transfer, assignment, sale, hypothecation or other encumbrance, the owner had received a total of at least \$250,000. US Patent No. RE38,137E expired on September 28, 2015. The Company accounted for its 65% interest in Wynn Technologies, Inc. under the equity method whereby the investment accounts were increased for contributions by the Company plus its 60% share of income pursuant to the contractual agreement which provides that the holder of 35% of the stock of Wynn Technologies, Inc. retained 40% of the income, and reduced for distributions and its 60% share of losses incurred, respectively, with the restriction whereby the account balances cannot go below zero. On April 11, 2019, Wynn Technologies, Inc. merged into Quest NetTech Corporation with Quest NetTech Corporation being the surviving entity. Pursuant to the merger agreement, Quest NetTech Corporation issued a 35% interest to the former 35% stockholder of Wynn Technologies, Inc.

Significant intercompany transaction and balances have been eliminated in consolidation.

Use of Estimates

In preparing financial statements in conformity with accounting principles generally accepted in the United States of America, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and revenue and expenses during the reporting period. Actual results could differ from those estimates.

Intangible Assets

Intangible assets consist of patents which are amortized using the straight-line method over their estimated useful lives or statutory lives whichever is shorter and are reviewed for impairment upon any triggering event that may give rise to the assets ultimate recoverability as prescribed under the guidance related to impairment of long-lived assets. Costs incurred to acquire patents, including legal costs, are also capitalized as long-lived assets and amortized on a straight-line basis with the associated patent.

Patents include the cost of patents or patent rights (hereinafter, collectively "patents") acquired from third-parties or acquired in connection with business combinations. Patent acquisition costs are amortized utilizing the straight-line method over their remaining economic useful lives, ranging from one to ten years. Certain patent application and prosecution costs incurred to secure additional patent claims that, based on management's estimates are deemed to be recoverable, are capitalized and amortized over the remaining estimated economic useful life of the related patent portfolio.

Derivative Financial Instruments

The Company evaluates the embedded conversion feature within its convertible debt instruments under ASC 815-15 and ASC 815-40 to determine if the conversion feature meets the definition of a liability and, if so, whether to bifurcate the conversion feature and account for it as a separate derivative liability. For derivative financial instruments that are accounted for as liabilities, the derivative instrument is initially recorded at its fair value and is then re-valued at each reporting date, with changes in the fair value reported in the statements of operations. For stock-based derivative financial instruments, the Company uses a Black Scholes model, in accordance with ASC 815-15 "Derivative and Hedging" to value the derivative instruments at inception and on subsequent valuation dates. The classification of derivative instruments, including whether such instruments should be recorded as liabilities or as equity, is evaluated at the end of each reporting period. Derivative instrument liabilities are classified in the balance sheet as current or non-current based on whether net-cash settlement of the derivative instrument could be required within 12 months after the balance sheet date.

Fair value of financial instruments

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. A fair value hierarchy is used which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. See Note 4 for information about derivative liabilities.

The fair value hierarchy based on the three levels of inputs that may be used to measure fair value are as follows:

Level 1 – Quoted prices in active markets for identical assets or liabilities.

Level 2 – Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 – Unobservable inputs that are supported by little or no market activity and that are financial instruments whose values are determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant judgment or estimation.

The carrying value reflected in the consolidated balance sheets for cash and cash equivalents, accounts receivable, accounts payable and accrued expenses and short-term borrowings approximate fair value due to the short-term nature of these items.

Income Tax

The Company records revenues on a gross basis, before deduction for income taxes. The Company incurred foreign income tax expenses of approximately \$0 and \$65,000 for the three and nine months ended September 30, 2020, respectively, and approximately \$0 and approximately \$225 for the three and nine months ended September 30, 2019, respectively.

Inventor/Former Owner Royalties and Contingent Legal/Litigation Finance Expenses

In connection with the investment in certain patents and patent rights, certain of the Company's operating subsidiaries may execute related agreements which grant to the inventors and/or former owners of the respective patents or patent rights, the right to receive a percentage of future net revenues (as defined in the respective agreements) generated as a result of licensing and otherwise enforcing the respective patents or patent portfolios.

The Company's operating subsidiaries may retain the services of law firms that specialize in patent licensing and enforcement and patent law in connection with their licensing and enforcement activities. These law firms may be retained on a contingent fee basis whereby such law firms are paid a percentage of any negotiated fees, settlements or judgments awarded.

The Company's operating subsidiaries may engage with funding sources that provide financing for patent licensing and enforcement. These litigation finance firms may be engaged on a non-recourse basis whereby such litigation finance firms are paid a percentage of any negotiated fees, settlements or judgments awarded in exchange for providing funding for legal fees and out of pocket expenses incurred as a result of the licensing and enforcement activities.

The economic terms of the inventor agreements, operating agreements, contingent legal fee arrangements and litigation financing agreements associated with the patent portfolios owned or controlled by the Company's operating subsidiaries, if any, including royalty rates, contingent fee rates and other terms, vary across the patent portfolios owned or controlled by such operating subsidiaries. Inventor/former owner royalties, payments to non-controlling interests, contingent legal fees expenses and litigation finance expenses fluctuate period to period, based on the amount of revenues recognized each period, the terms and conditions of revenue agreements executed each period and the mix of specific patent portfolios with varying economic terms and obligations generating revenues each period. Inventor/former owner royalties, contingent legal fees expenses and litigation finance expenses will continue to fluctuate and may continue to vary significantly period to period, based primarily on these factors.

Revenue Recognition

The Company recognizes revenue in accordance with ASC Topic 606, "Revenue from Contracts with Customers". Revenue is recognized when control of the promised goods or services is transferred to customers at an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods or services. Under Topic 606, revenue is recognized when there is a contract which has commercial substance which is approved by both parties and identifies the rights of the parties and the payment terms. The Company adopted Topic 606 as of January 1, 2018 using the modified retrospective transition method, with no impact on the consolidated financial position or results of operations.

Recent Accounting Pronouncements

Management does not believe that there are any recently issued, but not effective, accounting standards which, if currently adopted, would have a material effect on the Company's financial statements.

Going Concern

As shown in the accompanying financial statements, the Company has an accumulated deficit of approximately \$20,974,000 and negative working capital of approximately \$7,520,000 as of September 30, 2020. Because of the Company's continuing losses, its working capital deficiency, the uncertainty of future revenue, the Company's obligations to Intellectual Ventures and Intelligent Partners, as transferee of United Wireless, the Company's low stock price and the absence of a trading market in its common stock, the ability of the Company to raise funds in equity market or from lenders is severely impaired. These conditions, together with the effects of the COVID-19 pandemic and the steps taken by the states to slow the spread of the virus and its effect on its business raise substantial doubt as to the Company's ability to continue as a going concern. Although the Company may seek to raise funds and to obtain third party funding for litigation to enforce its intellectual property rights, the availability of such funds, particularly in view of the COVID-19 pandemic, is uncertain. The financial statements do not include any adjustments that might result from the outcome of this uncertainty. The Company is in default on payment of principal and interest on its convertible notes due September 30, 2020 in the principal amount of \$4,672,812. Accrued interest on the notes was \$117,780. The Company has obtained a standstill agreement of the noteholder until November 13, 2020. In connection with the standstill agreement, the Company paid the \$117,780 interest accrued at September 30, 2020, and, in connection with an extension of the standstill to November 13, 2020, the Company paid additional interest through the standstill period of \$20,000. Although the Company is in negotiations with the noteholder with respect to a restructure of the note and other payment agreements between the noteholder and the Company, it can give no assurance that the negotiations will result in a revised agreement. The failure of the Company to negotiate an acceptable restructure of the agreement could materially and adversely affect the ability of the Company to continue in business, and it may be necessary for the Company to seek protection under the Bankruptcy Act.

NOTE 3 – SHORT-TERM DEBT AND LONG-TERM LIABILITIES

The following table shows the Company's short-term and long-term debt at September 30, 2020 and December 31, 2019.

	<u>September 30, 2020</u>	<u>December 31, 2019</u>
Short-term debt:		
Loans payable – third party	\$ 147,000	\$ 147,000
Purchase price of patents – current portion	975,000	569,386
Net short-term debt	<u>1,122,000</u>	<u>716,386</u>
Loan payable – related party		
Gross	4,672,810	4,672,810
Accrued Interest	117,780	117,780
Unamortized discount	-	(189,705)
Net loans payable – related party	<u>\$ 4,790,590</u>	<u>\$ 4,600,885</u>
Long-term liabilities:		
Loans payable - SBA		
Gross	\$ 170,832	-
Accrued Interest	2,142	-
Net loans payable SBA	<u>172,974</u>	<u>-</u>
Purchase price of patents		
Gross	1,315,000	1,725,000
Unamortized discount	(155,019)	(282,503)
Net purchase price of patents – long-term	<u>\$ 1,159,981</u>	<u>\$ 1,442,497</u>

Contingent funding liabilities:

Gross	20,378	20,378
Net contingent funding liabilities	<u>\$ 20,378</u>	<u>\$ 20,378</u>

Loan payables:

The loan payable – third party represents unsecured demand loans made by former officers and directors, who are unrelated third parties at September 30, 2020, and December 31, 2019, in the amount of \$147,000. The loans are payable on demand plus accrued interest at 10% per annum. These third parties are also stockholders, but their stockholdings are not significant.

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The loan payable – related party at September 30, 2020 represents the principal amount of the Company’s 10% secured convertible note to Intelligent Partners, LLC (“Intelligent Partners”) as transferee of the secured convertible notes issued to United Wireless Holdings, Inc. (“United Wireless”), in the amount of \$4,672,810 pursuant to securities purchase agreement dated October 22, 2015 between the Company and United Wireless, as more fully described in the Company’s financial statements for the year ended December 31, 2019. The notes payable to Intelligent Partners, as transferee of United Wireless, are classified as a current liability as of September 30, 2020 and December 31, 2019. The notes became due by their terms on September 30, 2020, and the Company did not make any payment on account of principal of and interest on the notes on that date. See Note 10 for information with respect to current status of the notes payable to Intelligent Partners.

Interest on all notes issued pursuant to the securities purchase agreement, accrued through September 30, 2018, with accrued interest being added to principal on September 30, 2016, 2017 and 2018. On September 30, 2018, approximately \$395,459 of accrued interest was added to principal. Since September 30, 2018, the Company has been required to pay interest quarterly. For the three and nine months ended September 30, 2020, the Company paid approximately \$117,000 and \$30,000 in interest, respectively, on these loans.

Because of its right to elect a director of the Company, United Wireless is treated as a related party. Prior to the securities purchase agreement with United Wireless, the Company had no relationship with United Wireless.

Long term liabilities

The loans payable-SBA at September 30, 2020 represents:

- An unsecured loan from JPMorgan Chase Bank, N.A. in the aggregate amount of \$20,832, pursuant to the Paycheck Protection Program (the “PPP”) under Division A, Title I of the Coronavirus Aid, Relief, and Economic Security Act, also known as the CARES Act, which was enacted March 27, 2020. The loan, which was taken down on April 23, 2020, matures on April 23, 2022 and bears interest at a rate of 0.98% per annum, with interest payable monthly commencing on November 23, 2020. The loan may be prepaid by the Company at any time prior to maturity with no prepayment penalties. Funds from the loan may only be used for payroll costs, costs used to continue group health care benefits, mortgage payments, rent, utilities, and interest on other debt obligations incurred before February 15, 2020. The Company has used the entire loan amount for qualifying expenses. Under the terms of the PPP, certain amounts of the loan may be forgiven if they are used for qualifying expenses as described in the CARES Act.
- A secured Economic Injury Disaster Loan from the U.S. Small Business Association (“SBA”) in the aggregate amount of \$150,000, pursuant to Section 7(b) of the Small Business Act as part of the COVID-19 relief effort. The Company’s obligations on the loan are set forth in the Company’s note dated May 14, 2020 which matures on May 14, 2050 and bears interest at a rate of 3.75% per annum, payable monthly commencing on May 14, 2021. The Note may be prepaid by the Company at any time prior to maturity with no prepayment penalties. Funds from the Loan may be used solely as working capital to alleviate economic injury caused by disaster occurring in the month of January 31, 2020 and continuing thereafter and to pay Uniform Commercial Code (UCC) lien filing fees and a third-party UCC handling charge of \$100 which were deducted from the loan amount stated above. In addition to the loan, as part of the COVID-19 relief effort, the Company obtained an Emergency EIDL Grant from the SBA in the amount of \$1,000. The Company is not required to repay the grant.

The purchase price of patents at September 30, 2020 represents:

- the minimum payments due under the agreement between CXT Systems, Inc. (“CXT”), a wholly owned subsidiary, and IV 34/37 pursuant to which at closing CXT acquired by assignment all right, title, and interest in a portfolio of fourteen United States patents, five foreign patents and six related applications (the “CXT Portfolio”). Under the agreement, CXT will distribute 50% of net recoveries, as defined, to IV 34/37. CXT advanced \$25,000 to IV 34/37 at closing, and agreed that in the event that, on December 31, 2018, December 31, 2019 and December 31, 2020, cumulative distributions to IV 34/37 total less than \$100,000, \$375,000 and \$975,000, respectively, CXT shall pay the difference necessary to achieve the applicable minimum payment amount within ten days after the applicable date; with any advances being credited toward future distributions to IV 34/36. As of September 30, 2020, \$600,000 of the minimum future cumulative distributions were presented as short-term debt based on the payment due date. No affiliate of CXT has guaranteed the minimum payments. CXT’s obligations under the agreement are secured by a security interest in the proceeds (from litigation or otherwise) from the CXT Portfolio. During the nine-months ended September 30, 2020, the Company paid the \$194,386 liability that was classified as a short-term liability as of December 31, 2019.

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- The non-current portion of minimum payments due under the agreement between M-RED Inc. (“M-RED”), a wholly owned subsidiary and Intellectual Ventures Assets 113 LLC and Intellectual Ventures Assets 108 LLC (“IV 113/108”) pursuant to which M-RED paid IV 113/108 \$75,000 and IV 113/108 transferred to M-RED all right, title and interest in a portfolio of sixty United States patents and eight foreign patents (the “M-RED Portfolio”). Under the agreement, M-RED is to distribute 50% of net proceeds, as defined, to IV 113/108, as long as the Company generates revenue from the M-RED Portfolio. The agreement with IV 113/108 provides that if, on September 30, 2020, September 30, 2021 and September 30, 2022, cumulative distributions to IV 113/108 total less than \$450,000, \$975,000 and \$1,575,000, respectively, M-RED shall pay the difference between such cumulative amounts and the amount paid to IV 113/108 within ten days after the applicable date. The \$75,000 initial payment is treated as an advance against the first distributions of net proceeds payable to IV 113/108. As of September 30, 2020, \$1,125,000 and \$375,000 of the minimum future cumulative distributions were presented as long-term and short-term debt, respectively, based on payment due dates. Neither the Company nor any of its affiliates has guaranteed the minimum payments. M-RED’s obligations under the agreement with IV 113/108 are secured by a security interest in the proceeds (from litigation or otherwise) from the M-RED Portfolio.
- The non-current portion of our obligations under the unsecured non-recourse funding agreement with a third-party funder entered into in May 2020 whereby the third-party agreed to provide acquisition funding in the amount of \$95,000 for the Company’s acquisition of the audio messaging portfolio. Under the funding agreement, the third party funder is entitled to a priority return of funds advanced from net proceeds. as defined, recovered until the funder has received \$190,000. The Company has no other obligation to the third party and has no liability to the funder in the event that the Company does not generate net proceeds. Pursuant to ASC 470, the company recorded this monetization obligation as debt and the difference between the purchase price and total obligation as a discount to the debt and fully expensed to interest during the period.

The contingent funding liabilities at September 30, 2020 represents:

- the non-current portion of our obligations under the unsecured non-recourse litigation funding agreement with a third-party litigation funder entered into in

December 2018 whereby the third-party agreed to provide litigation funding in the amount of \$150,000 to the Company, and the Company has no other obligation to the third party.

The Company's relationship with the funding source meets the criteria in ASC 470-10-25 - Sales of Future Revenues or Various Other Measures of Income ("ASC 470"), which relates to cash received from a funding source in exchange for a specified percentage or amount of revenue or other measure of income of a particular product line, business segment, trademark, patent, or contractual right for a defined period. Under this guidance, the Company recognized the fair value of its contingent obligation to the funding source, as of the acquisition date, as long-term debt in its consolidated balance sheet. This initial fair value measurement is based on the perspective of a market participant and includes significant unobservable inputs which are classified as Level 3 inputs within the fair value hierarchy and are discussed further within Note 2. At each subsequent reporting period, the Company will measure the long-term debt at fair value based on the discounted expected future cash flows over the life of the obligation. The Company's repayment obligations are contingent upon future patent licensing fee revenues generated from the licensing programs.

Under ASC 470, amounts recorded as debt shall be amortized under the interest method. The Company made an accounting policy election to utilize the prospective method when there is a change in the estimated future cash flows, whereby a new effective interest rate is determined based on the revised estimate of remaining cash flows. The new rate is the discount rate that equates the present value of the revised estimate of remaining cash flows with the carrying amount of the debt, and it will be used to recognize interest expense for the remaining periods. Under this method, the effective interest rate is not constant, and any change in expected cash flows is recognized prospectively as an adjustment to the effective yield. As of September 30, 2020, the total contingent funding liability was approximately \$20,000, and the effective interest rate was approximately 8.5%. This rate represents the discount rate that equates the estimated future cash flows with the fair value of the debt and is used to compute the amount of interest to be recognized each period. Any future payments made to the funding source will decrease the long-term debt balance accordingly. For the period ended September 30, 2020, the amortization amount is deemed immaterial.

NOTE 4—DERIVATIVE LIABILITIES

Because there is not a fixed conversion price, remaining compliant with the authorized share requirement under the notes to Intelligent Partners is outside of the control of the Company. Because there is no set limit on the number of shares issuable under the notes if the notes become convertible, absent an increase in the stock price or an increase in authorized shares, there are potentially not enough authorized shares of common stock to satisfy the exercise of the Company's options, thus the Company determined that certain options qualify as derivative liabilities under ASC Topic 815. On January 22, 2016, the Company reclassified all non-employee warrants and options as derivative liabilities and revalued them at their fair values at each balance sheet date. Any change in fair value was recorded as other income (expense) for each reporting period at each balance sheet date.

As of September 30, 2020, and December 31, 2019, the aggregate fair value of the outstanding derivative liability was approximately \$0 and \$595,000, respectively. The underlying derivative expired unexercised on September 30, 2020, the derivative liability was resolved and credited back to additional paid in capital.

The Company estimated the fair value of the derivative liability using the Black-Scholes option pricing model using the following key assumptions during the period ended September 30, 2020 and December 31, 2019:

	Period Ended	
	September 30, 2020	December 31, 2019
Volatility	261%	207-426%
Risk-free interest rate	0.20%	0.24%
Expected dividends	-%	-%
Expected term	-	1.75-4.70

The following schedule summarizes the valuation of financial instruments at fair value in the balance sheets as of September 30, 2020 and December 31, 2019:

	Fair Value Measurements as of					
	September 30, 2020			December 31, 2019		
	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
Assets						
None	-	-	-	-	-	-
Total assets	-	-	-	-	-	-
Liabilities						
Option derivative liability	-	-	-	-	-	595,000
Total liabilities	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 595,000

The following table sets forth a reconciliation of changes in the fair value of derivative liabilities classified as Level 3 in the fair value hierarchy:

	Significant Unobservable Inputs (Level 3) as of September 30, 2020
Beginning balance	\$ 595,000
Change in fair value	(275,000)
Resolution of derivative liability	(320,000)
Ending balance	\$ 0

NOTE 5—STOCKHOLDERS' EQUITY

No options were granted during the nine months ended September 30, 2020.

A summary of the status of the Company's stock options and changes is set forth below:

	Number of Options (#)	Weighted Average Exercise Price (\$)	Weighted Average Remaining Contractual Life (Years)
Balance - December 31, 2019	50,000,000	0.03	0.75
Granted	-	-	-
Exercised	-	-	-
Expired	(50,000,000)	0.03	-
Cancelled	-	-	-
Balance - September 30, 2020	-	-	-

NOTE 6 – INTANGIBLE ASSETS

Intangible assets include patents purchased and are recorded based at their acquisition cost. Intangible assets consisted of the following:

	September 30, 2020	December 31, 2019	Weighted average amortization period (years)
Patents	\$ 5,690,000	\$ 5,595,000	6.50
Less: net monetization obligations	(509,811)	(509,811)	
Imputed interest	(713,073)	(713,073)	
Subtotal	4,467,116	4,372,116	
Less: accumulated amortization	(2,127,530)	(1,617,762)	
Net value of intangible assets	<u>\$ 2,339,586</u>	<u>\$ 2,754,354</u>	6.38

Intangible assets are comprised of patents with estimated useful lives. The intangible assets at September 30, 2020 represent:

- patents acquired in October 2015 for a purchase price of \$3,000,000, the useful lives of the patents, at the date of purchase, was 6-10 years;
- patents acquired in July 2017 pursuant to an obligation to distribute 50% of net revenues to IV 34/37, against which \$25,000 was advanced at closing and provided that in the event that, on December 31, 2018, December 31, 2019 and December 31, 2020, cumulative distributions of 50% of net revenues to IV 34/37 total less than \$100,000, \$375,000 and \$975,000, respectively, CXT shall pay the difference necessary to achieve the applicable minimum payment amount within ten days after the applicable date; with any advances being credited toward future distributions to IV 34/36; the useful lives of the patents, at the date of acquisition, was 5-6 years;
- patents (which were fully depreciated at the date of acquisition) acquired in January 2018 pursuant to an agreement with Intellectual Ventures Assets 62 LLC and Intellectual Ventures Assets 71 LLC (“IV 62/71”), pursuant to which CXT has an obligation to distribute 50% of net revenues to IV 62/71 against which CXT advanced \$10,000 at closing;

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- patents acquired in January 2018 by Photonic Imaging Solutions Inc. (“PIS”) from Intellectual Ventures Assets 64 LLC (“IV 64”) pursuant to which PIS is to pay IV 64 (a) 70% of the first \$1,500,000 of net revenue, (b) 30% of the next \$1,500,000 of net revenue and (c) 50% of net revenue in excess of \$3,000,000, against which PIS advanced \$10,000 at closing; and
- patents acquired in March 2019 by M-Red Inc. (“M-Red”) from Intellectual Ventures Assets 113 LLC and Intellectual Ventures 108 LLC (“IV 113/108”) pursuant to which M-Red is obligated to distribute 50% of net revenues to IV 113/108, against which \$75,000 was advanced at closing and provided that in the event that, on September 30, 2020, September 30, 2021 and September 30, 2022, cumulative distributions of 50% of net revenues to IV 113/108 total less than \$450,000, \$975,000 and \$1,575,000, respectively, M-Red shall pay the difference necessary to achieve the applicable minimum payment amount within ten days after the applicable date; with any advances being credited toward future distributions to IV 113/108; the useful lives of the patents, at the date of acquisition, was approximately nine years; and
- patents (which were fully depreciated at the date of acquisition) acquired in May 2020 for a purchase price of \$95,000 pursuant to an agreement with Texas Technology Ventures 2, LLP (“TTV”), pursuant to which of the Company retains the first \$230,000 of net proceeds, as defined in the agreement, after which the company has an obligation to distribute 50% of net proceeds to TTV.

The Company amortizes the costs of intangible assets over their estimated useful lives on a straight-line basis. Costs incurred to acquire patents, including legal costs, are also capitalized as long-lived assets and amortized on a straight-line basis with the associated patent. Amortization of patents is included as a selling, general and administrative expense in the accompanying consolidated statements of operations.

The Company assesses intangible assets for any impairment to the carrying values. As of September 30, 2020, and December 31, 2019, management concluded that there was no impairment to the acquired assets. At September 30, 2020 and December 31, 2019, the book value of the Company’s intellectual property was \$2,339,586 and \$2,754,354, respectively.

Amortization expense for patents comprised \$509,768 and \$529,486 for the nine months ended September 30, 2020 and the year ended December 31, 2019, respectively. Future amortization of intangible assets is as follows:

Year ended December 31,	
Remainder of 2020	\$ 135,350
2021	549,345
2022	495,742
2023	323,070
2024 and thereafter	836,079
Total	<u>\$ 2,339,586</u>

Pursuant to the securities purchase agreement dated October 22, 2015 between the Company and United Wireless, more fully described in the Company’s Annual Report on Form 10-K for the year ended December 31, 2019, 15% of the net monetization proceeds from the patents acquired in October 2015 will be paid to Intelligent Partners, as transferee of United Wireless. This monetization obligation was recognized as a discount to the loan and amortized over the life of the loan using the effective interest method. In addition, the Company entered into a monetization agreement with United Wireless pursuant to which the Company agreed to pay United Wireless 7.5% of the net monetization proceeds from the patents acquired by CXT in July 2017. This obligation was recorded as an expense and is reflected in interest expense during the third quarter of 2017.

The Company granted Intellectual Ventures a security interest in the patents assigned to the Company as security for the payment of the balance of the purchase price. The security interest of Intellectual Ventures is senior to the security interest of Intelligent Partners, as successor to United Wireless, in the proceeds derived from such patents.

Pursuant to the funding agreement dated May 29, 2019 between the Company and the funding source, 100% of the net monetization proceeds due to the company from the audio messaging patents acquired in May 2020 will be paid to the funding source until the funding source receives \$190,000. The monetization obligation, net of the \$95,000 provided by the funding source, was recognized as a discount to the debt and fully amortized to interest expense during the period.

The balance of the purchase price of the patents is reflected as follows:

	<u>September 30,</u> <u>2020</u>	<u>December 31,</u> <u>2019</u>
Current Liabilities:		
Purchase price of patents, current portion	975,000	\$ 569,386
Unamortized discount	-	
Non-current liabilities:		
Purchase price of patents, long term	1,315,000	\$ 1,725,000
Unamortized discount	(155,019)	(282,503)
Total current and non-current	2,134,981	2,011,883
Effective interest rate of Amortized over 2-3 years	9.35%-14.45%	9.6-12.5%

Because the non-current minimum payment obligations are due over the next three years, the Company imputed interest at 10% per annum and the interest will be accreted up to the maturity date.

NOTE 7 – NON-CONTROLLING INTEREST

The following table reconciles equity attributable to the non-controlling interest related to Quest Packaging Solutions Corporation.

Balance as of December 31, 2019	\$ 239
Net loss income attributable to non-controlling interest	\$ (6)
Balance as of September 30, 2020	\$ 233

NOTE 8 – RELATED PARTY TRANSACTIONS

The Company has at various times entered into transactions with related parties, including officers, directors and major stockholders, wherein these parties have provided services, advanced or loaned money, or both, to the Company which was needed to support its daily operations. The Company discloses all related party transactions.

See Notes 3 and 6 in connection with transactions with United Wireless. During periods ended September 30, 2020 and 2019, the Company incurred interest expense on the Company's 10% notes issued to United Wireless pursuant to the securities purchase agreement dated October 22, 2015 more fully described in the Company's financial statements for the year ended December 31, 2019. On each of September 30, 2017 and 2018, accrued interest was added to the principal amount of the note. Subsequent to September 30, 2018, the Company is to pay interest quarterly. During the three and nine months ended September 30, 2020 the Company paid the amounts due of approximately \$117,000 and 350,000 in interest, respectively, and the amounts due of approximately \$117,000 and 350,000 for the three and nine months ended September 30, 2019, respectively.

See Note 9 with respect to the employment agreement with the Company's president and chief executive officer.

During the three and nine months ended September 30, 2020 and 2019, the Company contracted with an entity owned by the chief technology officer for the provision of information technology services to the Company. The cost of such services was approximately \$115 and \$320 for the three and nine months ended September 30, 2020, respectively, and approximately \$115 and \$350 for the three and nine months ended September 30, 2019, respectively.

During the three and nine months ended September 30, 2020, the Company contracted with a law firm more than 10 percent owned, but not controlled, by the father-in-law of the chief executive officer. The firm is engaged on a contingent fee basis and serves as escrow agent for the Company in connection with monetization of the Company's intellectual property rights. As of September 30, 2020 the Company recorded an accrued liability of approximately \$564,000 in connection with the engagement. In prior periods, the Company engaged a firm at which the father-in-law of the chief executive was formerly a partner. Because his interest in the prior firm was less than 10%, the prior firm was not considered a related party in prior periods.

NOTE 9 – COMMITMENTS AND CONTINGENCIES

Employment Agreements

Pursuant to a restated employment agreement, dated November 30, 2014, with the Company's president and chief executive officer, the Company agreed to employ him as president and chief executive officer for a term of three years, commencing January 1, 2014, and continuing on a year-to-year basis unless terminated by either party on not less than 90 days' notice prior to the expiration of the initial term or any one-year extension. The agreement provides for an initial annual salary of \$252,000, which may be increased, but not decreased, by the board or the compensation committee. In March 2016, the Company's board of directors increased the chief executive officer's annual salary to \$300,000, effective January 1, 2016. The chief executive officer is entitled to a bonus if the Company meets or exceeds performance criteria established by the compensation committee. In August 2016, the Company's board of directors approved annual bonus compensation equal to 30% of the amount by which the Company's consolidated income before income taxes exceeds \$500,000, but, if the Company is subject to the limitation on deductibility of executive compensation pursuant to Section 162(m) of the Internal Revenue Code, the bonus cannot exceed the amount which would be deductible pursuant to Section 162(m). The chief executive officer is also eligible to participate in any executive incentive plans which the Company may adopt.

On May 11, 2020, the board of directors adopted a Simplified Employee Pension – Individual Retirement Accounts Contribution Agreement for its employees pursuant to which the Company deposits to a SEP IRA account of its employees a percentage of the employee's compensation, subject to statutory limitations on the amount of the contribution. For 2020, the percentage was set at 19%. The Company has only one employee, its chief executive officer.

Inventor Royalties, Contingent Litigation Funding Fees and Contingent Legal Expenses

In connection with the investment in certain patents and patent rights, certain of the Company's operating subsidiaries executed agreements which grant to the former owners of the respective patents or patent rights, the right to receive inventor royalties based on future net revenues (as defined in the respective agreements) generated as a result of licensing and otherwise enforcing the respective patents or patent portfolios.

The Company's operating subsidiaries may engage third party funding sources to provide funding for patent licensing and enforcement. The agreements with the third party funding sources may provide that the funding source receive a portion of any negotiated fees, settlements or judgments. In certain instances, these third party funding sources are entitled to receive a significant percentage of any proceeds realized until the third party funder has recouped agreed upon amounts based on formulas set forth in the underlying funding agreement, which may reduce or delay and proceeds due to the Company.

The Company's operating subsidiaries may retain the services of law firms in connection with their licensing and enforcement activities. These law firms may be retained on a contingent fee basis whereby the law firms are paid on a scaled percentage of any negotiated fees, settlements or judgments awarded based on how and when the fees, settlements or judgments are obtained.

Depending on the amount of any recovery, it is possible that all the proceeds from a specific settlement may be paid to the funding source and legal counsel.

The economic terms of the inventor agreements, funding agreements and contingent legal fee arrangements associated with the patent portfolios owned or controlled by the Company's operating subsidiaries, if any, including royalty rates, proceeds sharing rates, contingent fee rates and other terms, vary across the patent portfolios owned or controlled by the operating subsidiaries. Inventor royalties, payments to noncontrolling interests, payments to third party funding providers and contingent legal fees expenses fluctuate period to period, based on the amount of revenues recognized each period, the terms and conditions of revenue agreements executed each period and the mix of specific patent portfolios with varying economic terms and obligations generating revenues each period. Inventor royalties, payments to third party funding sources and contingent legal fees expenses will continue to fluctuate and may continue to vary significantly period to period, based primarily on these factors.

In December 2018, the Company entered into an unsecured non-recourse funding agreement whereby a third party agreed to provide funds to the Company to enable the Company to support its structured licensing programs for the CMOS and M-RED portfolios. Under the funding agreement, the third party receives an interest in the proceeds from the programs, and the Company has no other obligation to the third party. As of September 30, 2020, the Company paid the third party approximately \$130,000 under the agreement.

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In May 2020, the Company entered into an unsecured non-recourse funding agreement whereby a third party agreed to provide funds for the acquisition of the audio messaging portfolio. Under the funding agreement, the third party receives a priority interest in the net proceeds, as defined in the agreement, from the program up to \$190,000 and the Company has no other obligation to the third party and has no liability to the funder in the event that the Company does not generate net proceeds. See Note 3 for information with respect to the funding agreement.

Patent Enforcement and Other Litigation

Certain of the Company's operating subsidiaries are engaged in litigation to enforce their patents and patent rights. In connection with these patent enforcement actions, it is possible that a defendant may request and/or a court may rule that an operating subsidiary has violated statutory authority, regulatory authority, federal rules, local court rules, or governing standards relating to the substantive or procedural aspects of such enforcement actions. In such event, a court may issue monetary sanctions against the Company or its operating subsidiaries or award attorney's fees and/or expenses to a defendant(s), which could be material, and if required to be paid by the Company or its operating subsidiaries, could materially harm the Company's operating results and financial position and could result in a default under the Company's notes to Intelligent Partners, which are already in default as a result of the Company's failure to pay the notes on the September 30, 2020 maturity date. Since the operating subsidiaries do not have any assets other than the patents, and the Company does not have any available financial resources to pay any judgment which a defendant may obtain against a subsidiary, such a judgement may result in the bankruptcy of the subsidiary and/or the loss of the patents, which are the subsidiaries' only assets.

On January 19, 2017, the court in the Mobile Data Portfolio litigation granted the defendants' motion for summary judgment of non-infringement. On January 31, 2017, Quest Licensing Corporation filed a notice of appeal with the United States Court of Appeals for the Federal Circuit. Following the court's decision granting the defendant's motion for summary judgment, the defendants moved for an award of attorneys' fees under Section 285 of the Patent Act which provides that "the court in exceptional cases may award reasonable attorney fees to the prevailing party." On June 29, 2017, the defendants' motion for attorney fees in the Mobile Data litigation was denied, without prejudice and with leave to renew their motion thirty days from the decision of the appellate court on Quest Licensing Corporation's appeal. On June 8, 2018 the appellate court affirmed the lower court's decision. On June 9, 2018 Quest Licensing Corporation filed a petition for rehearing with the appellate court. On July 30, 2018 the appellate court denied Quest Licensing Corporations petition for rehearing. On March 27, 2019 the court in the Mobile Data Portfolio litigation denied the defendants' motion for attorney fees under Section 285 of the Patent Act.

In May 2018, CXT brought patent infringement suits in the United States District Court for the Eastern District of Texas against Stage Stores, Inc. In February 2020, Specialty Retailers, Inc. ("Specialty"), the parent company of Stage Stores, Inc., failed to make the final installment payment pursuant to the Settlement and License Agreement between Specialty and CXT. On March 31, 2020, CXT made a sealed motion with the Court to Reopen the Action and Enforce the Settlement Agreement. On May 1, 2020, CXT filed a sealed motion with the Court seeking Summary Judgment to Enforce the Settlement Agreement. On May 4, 2020, the Court granted the motion. On May 10, 2020 Specialty filed voluntary petitions under Chapter 11 of the Bankruptcy Code in the U.S. Bankruptcy Court for the Southern District of Texas, Houston Division. On May 16, 2020, CXT filed a proof of claim with the Bankruptcy Court. On May 20, 2020, the reopened District Court action was stayed automatically pending the outcome of the bankruptcy action.

In May 2018 CXT Systems brought patent infringement suits in the United States District Court for the Eastern District of Texas against J.C. Penney Company, Inc. ("JCP"). On April 20, 2020 the parties entered into a settlement and license agreement and the case was dismissed. On May 15, 2020 JCP filed voluntary petitions under Chapter 11 of the Bankruptcy Code in the U.S. Bankruptcy Court for the Southern District of Texas, Houston Division. On June 4, 2020, the CXT notified JCP of material breach of the settlement and license agreement for failure to make payment pursuant to the agreement. On May 16, 2020, CXT filed a proof of claim with the Bankruptcy Court.

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NOTE 10 – SUBSEQUENT EVENTS

At September 30, 2020, promissory notes in the aggregate principal amount of \$4,672,810 payable to Intelligent Partners became due. At September 30, 2020, accrued interest on the notes was \$117,780. The notes became due by their terms on September 30, 2020, and the Company did not make any payment on account of principal of and interest on the notes on that date.

On October 1, 2020, the Company entered into a standstill agreement with Intelligent Partners pursuant to which:

- Intelligent Partners agreed that, provided that the Company pays Intelligent Partners \$117,780 of accrued interest on the note by October 2, 2020, for a period commencing on October 1, 2020 until the earlier of (i) October 22, 2020 or (ii) the date of any action by any person (other than Intelligent Partners and its affiliates) relating to the assertion of a breach or default by the Company or any of its subsidiaries under any agreement to which the Company or any of its subsidiaries is a party (the "Standstill Period"), Intelligent Partners and any person acting on behalf of Intelligent Partners will forbear from taking any action to enforce any of the rights they have or may have under the Agreements between the Company and Intelligent Partners or under applicable law or otherwise in respect of or arising out of the failure by the Company to pay the principal on the notes on the maturity date thereof or as a result of any defaults or alleged defaults by the Company or any subsidiary of the Company under any of the agreement between the Company and Intelligent Partners or under any applicable law or otherwise.

- During the Standstill Period, the Company and Intelligent Partners will seek to negotiate a mutually agreeable restructure agreement which provides for restructure of the Company's obligations under the notes and a modification of its obligations under the Company's Agreements with Intelligent Partners.

On October 1, 2020, the Company made the \$117,780 payment to Intelligent Partners. Pursuant to amendments to the standstill agreement, the Standstill Period was extended to October 27, 2020, October 31, 2020 and November 13, 2020. In connection with the third extension, the Company made a payment of \$20,000 in full satisfaction of any interest accrued during the Standstill Period on the Company's note to Intelligent Partners.

The Company intends to negotiate in good faith with respect to a restructuring of its obligations to Intelligent Partners. However, the Company cannot give any assurance that it will be successful in negotiating a restructure. In the event the Company is not able to negotiate a restructure, it may not be able to continue in business and may be necessary for the Company to seek protection under the Bankruptcy Act.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Overview

Our principal operations include the development, acquisition, licensing and enforcement of intellectual property rights that are either owned or controlled by us or one of our wholly owned or majority-owned subsidiaries. We currently own, control or manage eleven intellectual property portfolios, which principally consist of patent rights. As part of our intellectual property asset management activities and in the ordinary course of our business, it has been necessary for either us or the intellectual property owner who we represent to initiate, and it is likely to continue to be necessary to initiate patent infringement lawsuits and engage in patent infringement litigation. We anticipate that our primary source of revenue will come from the grant of licenses to use our intellectual property, including licenses granted as part of the settlement of patent infringement lawsuits.

Our business, like all businesses at the present time, are affected by the COVID-19 pandemic and the steps taken by states to seek to reduce the spread of the virus. Although we do not manufacture or sell products, the COVID-19 pandemic and the work shutdown imposed in the United States and other countries to limit the spread of the virus can have a negative impact on our business. Our revenue is generated almost exclusively from license fees generated from litigation seeking damages for infringement of our intellectual property rights. The work shutdown has affected the court system, with courts operating on a reduced schedule. As a result, patent infringement actions are likely to be lower priority items in allocation of court resources, with the effect that deadlines are likely to be postponed which delays may give defendants an incentive to delay negotiations or offer a lower amount than they might otherwise accept. In addition, the effect of the COVID-19 and the public response may adversely affect the financial condition and prospects of defendants and potential defendants, which would make it less likely that they would be willing to settle our claim. A number of defendants and potential defendants have filed to take advantage of the Bankruptcy Act or have announced that they may consider such action. If any defendant files for protection under the Bankruptcy Act, the action would be stayed and we may not be able to obtain a judgment or recover on any judgment.

The COVID-19 pandemic and the response to limit the spread of the infection may affect the financial condition of financing sources and the willingness of potential financing sources to provide funding for our litigation. In addition, these factors may affect a law firms' ability and willingness to provide us with legal services on a contingent or partial contingent. The possibility that a defendant may seek protection under the Bankruptcy Act may make it less likely that a financing source would finance the litigation or that a law firm would work on a contingency or modified contingency basis.

Further, to the extent that holders of intellectual property rights see these factors impacting our ability to generate revenue from their intellectual property, they may be reluctant to sell intellectual property to us on terms which are acceptable to us, if at all.

We seek to generate revenue from two sources:

- Patent licensing fees relating to our intellectual property portfolio, which includes fees from the licensing of our intellectual property, primarily from litigation relating to enforcement of our intellectual property rights. All of the revenue for the three and nine months ended September 30, 2020 resulted from patent licensing fees, of which approximately 88% and 86%, respectively, was paid to funding sources, legal counsel and prior owners of the respective patents. Approximately all of the revenue for the three and nine months ended September 30, 2019 were from patent licensing fees, of which approximately 87% and 70%, respectively, was paid to funding sources and legal counsel pursuant to our agreements with funding sources, legal counsel and prior owners of the respective patents. Timing and amount of revenue is dependent upon the results of litigation and, depending on the terms of the engagement with counsel, total fees payable across all our portfolio enforcement actions may exceed total settlement recoveries as of a specific date as the settlements do not occur simultaneously.
- Licensed packaging sales, which relate to the sale of licensed products, although we did not generate revenue from these sales during the three or nine months ended September 30, 2020.

In previous periods, we also generated revenue from management fees, which we received for managing structured licensing programs, including litigation, related to our intellectual property rights. We do not currently receive these fees and do not have any agreements that provide for such payments.

Because of the nature of our business transactions to date, we recognize revenues from licensing upon execution of a license agreement following settlement of litigation and not over the life of the patent. Thus, we would recognize revenue when we receive the license fee or settlement payment. Although we intend to seek to develop portfolios of intellectual property rights that provide us for a continuing stream of revenue, to date we have not been successful in doing so, and we do not anticipate that we will be able to generate any significant revenue from licenses that provide a continuing stream of revenue. Thus, to the extent that we continue to generate cash from single payment licenses, our revenue can, and is likely to, vary significantly from quarter to quarter and year to year. Our gross profit from license fees reflects any royalties which we pay in connection with our license.

It is generally necessary for us to commence litigation in order to obtain a recovery for past infringement of, or to license the use of, our intellectual property rights. Intellectual property litigation is very expensive, with no certainty of any recovery. To the extent possible we seek to engage counsel on a contingent fee or partial contingent fee basis, which significantly reduces our litigation cost, but which also reduces the value of the recovery to us. We do not have the resources to enable us to fund the cost of litigation. To the extent that we cannot fund litigation ourselves, we may enter into an agreement with a third-party funding source. Our agreements with the funding sources typically provide that the funding source pays the litigation costs and that the funding source receives a percentage of the recovery, thus reducing our recovery in connection with any settlement of the litigation. In view of our limited cash and our working capital deficiency, we are not able to institute any monetization program that may require litigation unless we engage counsel on a fully contingent basis or we obtain funding from third party funding sources. In these cases, counsel may be afforded a greater participation in the recovery and the third party that funds the litigation would be entitled to participate in any recovery. To the extent that we have agreements with counsel and/or litigation funding sources pursuant to which payments made to them represent a portion of the gross recovery, and such payment is contingent upon a recovery, our revenue from litigation reflects the gross recovery from litigation as licensing fees, and payments to counsel and/or litigation funding sources are reflected as cost of revenue.

To a significantly lesser extent, we generate revenue from sale of packaging materials based on our TurtlePakTM technology. Our gross profit from sales reflects the cost of contract manufacturing and labor. We did not generate any revenue from the TurtlePakTM Portfolio other than from the sale of products using our technology.

In May 2018, Semcon brought patent infringement actions in the United States District Court for the Eastern District of Texas against TCT Mobile International Limited et. al. and Shenzhen OnePlus Science & Technology Co., Ltd. These actions were settled and our revenue for the three and nine month periods ended September 30, 2020 includes revenue from these settlements. We did not generate revenue from any other litigation in the three or nine months ended September 30, 2020.

On April 23, 2020, we borrowed \$20,832 from JPMorgan Chase Bank, N.A. pursuant to the Paycheck Protection Program (the "PPP") under Division A, Title I of the Coronavirus Aid, Relief, and Economic Security Act, also known as the CARES Act. The loan matures on April 6, 2022 and bears interest at a rate of 0.98% per annum, payable monthly commencing on November 23, 2020. We may prepay the loan at any time prior to maturity with no prepayment penalties. Funds from the loan may only be used for payroll costs, costs used to continue group health care benefits, mortgage payments, rent, utilities, and interest on other debt obligations incurred before February 15, 2020. We intend to use the entire loan amount for qualifying expenses. Under the terms of the PPP, certain amounts of the loan may be forgiven if they are used for qualifying expenses as described in the CARES Act.

On May 14, 2020, we took out a secured Economic Injury Disaster Loan from the U.S. Small Business Association ("SBA") in the amount of \$150,000, pursuant to Section 7(b) of the Small Business Act as part of the COVID-19 relief effort, as amended. Our obligations on the loan are set forth in our note which matures on May 14, 2050 and bears interest at a rate of 3.75% per annum, payable monthly commencing on May 14, 2021. We may prepay this note at any time prior to maturity with no prepayment penalties. Proceeds from the loan may be used solely as working capital to alleviate economic injury caused by disaster occurring in the month of January 31, 2020 and continuing thereafter and to pay Uniform Commercial Code (UCC) lien filing fees and a third-party UCC handling charge of \$100 which were deducted from the loan amount. In addition to the loan, as part of the COVID-19 relief effort, we obtained an Emergency EIDL Grant from the SBA in the amount of \$1,000. We are not required to repay the grant.

Results of Operations

Three and nine months ended September 30, 2020 and 2019

Revenues for the three months ended September 30, 2020 were approximately \$3,405,000, an increase of approximately \$2,765,000, or 432%, from the comparable period of 2019, which were approximately \$640,000. Revenues for the nine months ended September 30, 2020 were approximately \$5,488,000, an increase of approximately \$3,486,000, or 174%, from the comparable period of 2019, which was approximately \$2,002,000. We generated revenue from patent fees of approximately \$3,405,000 and \$5,488,000 for the three and nine months ended September 30, 2020, respectively, from licenses to the CXT, M-RED and power management portfolios. Our revenue, in the near future if not longer, is likely to be affected by factors relating to the COVID-19 pandemic as described under "Overview". We generated revenue from patent fees of approximately \$640,000 and approximately \$2,002,000 for the three and nine months ended September 30, 2019, respectively, from settlements in the CXT portfolio actions, anchor structure portfolio actions, power management/bus controller portfolio actions and CMOS portfolio actions. The total settlement recovery is included in revenue and the associated costs are deducted as cost of revenue. As discussed above, the timing and amount of our revenue is dependent upon the results of litigation seeking to enforce our intellectual property rights, and we cannot predict when or whether we will have a recovery and how much of the recovery will be received by us after payments to legal counsel, to our funding sources, or to inventors/former patent owners who have an interest in our share of the recovery from certain patent portfolios after deducting payments due to counsel and the litigation funding source. Since our revenue is dependent upon our success in litigation, the timing of revenue is dependent upon the timing of litigation and our success in the litigation as well as the ability of defendants to make any agreed-upon payments. As a result, we expect that our revenue will continue to be subject to significant changes from quarter to quarter.

Operating expenses for the three months ended September 30, 2020 increased by approximately \$2,440,000, or 284%, compared to the three months ended September 30, 2019. Operating expenses for the nine months ended September 30, 2020 increased by approximately \$3,576,000, or 152%, compared to the nine months ended September 30, 2019. Our principal operating expense for both the three and nine months ended September 30, 2020 was litigation and licensing expenses of approximately \$2,996,000 and \$4,714,000, respectively, which represent fees payable to attorneys, third-party funding sources and inventors/former patent owners associated with the CXT, M-RED and power management portfolio licenses and are reflected as cost of revenues. These fees became payable as a result of license agreements. The total licensing fee is included in revenue and the associated costs are treated as cost of revenue. When the licensing fee funds are disbursed we receive the net amount due us after deducting the associated settlement costs. We had settlement costs of approximately \$555,000 and approximately \$1,400,000 for the three and nine months ended September 30, 2019, respectively. As discussed above, the timing and amount of revenue is dependent upon the results of litigation seeking to enforce our intellectual property rights. Depending on the terms of the engagement with counsel, total fees payable across all our portfolio enforcement actions may exceed total settlement recoveries as of a specific date as the settlements do not occur simultaneously.

Other income (expense) for the three and nine months ended September 30, 2020 included a gain on the derivative liability associated with the options granted pursuant to our agreement with Intelligent Partners of \$175,000 and \$275,000, respectively. We realized a gain of \$290,000 and incurred a loss of \$270,000 on derivative liability for the three and nine months ended September 30, 2019, respectively. Other income (expense) reflects interest expense of approximately \$233,000 and approximately \$776,000 for the three and nine months ended September 30, 2020, respectively, and approximately \$216,000 and approximately \$591,000 for the three and nine months ended September 30, 2019. The increase in interest expense reflects the interest accrued on our note to Intelligent Partners.

We incurred income tax expense of approximately \$0 and \$65,000 for the three and nine months ended September 30, 2020, respectively, compared to approximately \$0 and \$225 for the three and nine months ended September 30, 2019. The increase in income tax expense primarily reflect foreign income taxes related to foreign source patent licensing fees. We did not incur foreign income tax expenses in the three and nine months ended September 30, 2019.

As a result of the foregoing, we realized net income of approximately \$50,000, or \$0.00 per share (basic and diluted) and a net loss of approximately \$1,005,000, or \$0.00 per share (basic and diluted), for the three and nine months ended September 30, 2020, respectively, compared to net loss of approximately \$145,000, or \$0.00 per share (basic and diluted), and approximately \$1,185,000, or \$0.00 per share (basic and diluted) for the three and nine months ended September 30, 2019, respectively.

Liquidity and Capital Resources

At September 30, 2020, we had current assets of approximately \$1,952,000, and current liabilities of approximately \$9,473,000. Our current liabilities include approximately \$975,000, payable to Intellectual Ventures, loans payable of approximately \$4,673,000, and accrued interest of approximately \$118,000 payable to Intelligent Partners, as transferee of the notes initially issued to United Wireless, and which are in default as a result of our failure to make payment on the September 30, 2020 maturity date, and loans payable of \$147,000 and accrued interest of approximately \$281,000 due to former directors and minority stockholders. As of September 30, 2020, we have an accumulated deficit of approximately \$20,974,000 and a negative working capital of approximately \$7,520,000. Other than salary to our chief executive officer, we do not contemplate any other material operating expense in the near future other than normal general and administrative expenses, including expenses relating to our status as a public company filing reports with the SEC.

We cannot assure you that we will be successful in generating future revenues, in obtaining additional debt or equity financing or that such additional debt or equity financing will be available on terms acceptable to us, if at all, or that we will be able to obtain any third party funding in connection with any of our intellectual property portfolios. We have no credit facilities. The timing of any recovery may be affected by the court schedules, which have been affected by court closures or reduced court scheduled as a result of the COVID 19 pandemic and the steps taken by states to address the pandemic.

We cannot predict the success of any pending or future litigation. Our obligations to Intelligent Partners are not contingent upon the success of any litigation. If we fail to generate a sufficient recovery in these actions (net of any portion of any recovery payable to the funding source or our legal counsel) in a timely manner to enable us to pay Intelligent Partners on the present loans we would be in default under our agreements with Intelligent Partners which could result in Intelligent Partners obtaining ownership of the three subsidiaries which own the patent rights we acquired from Intellectual Ventures. Our agreements with the funding sources provide that the funding sources will participate in any recovery which is generated. We believe that our financial condition, our history of losses and negative cash flow from operations, and our low stock price make it difficult for us to raise funds in the debt or equity markets.

As noted below, there is a substantial doubt about our ability to continue as a going concern.

Significant Accounting Policies and Estimates

The discussion and analysis of our financial condition and results of operations is based upon our financial statements that have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets and liabilities. On an on-going basis, we evaluate our estimates including the allowance for doubtful accounts, the salability and recoverability of our products, income taxes and contingencies. We base our estimates on historical experience and on other assumptions that we believe to be reasonable under the circumstances, the results of which form our basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Management believes the following critical accounting policies affect the significant judgments and estimates used in the preparation of the financial statements.

Principles of Consolidation

The consolidated financial statements are prepared in accordance with US GAAP and Rule 8-03 of Regulation S-X of the SEC, and present our financial statements and those of our wholly-owned and majority-owned subsidiaries. In the preparation of our consolidated financial statements, intercompany transactions and balances are eliminated.

Use of Estimates and Assumptions

The preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Fair Value of Financial Instruments

We adopted Financial Accounting Standards Board (“FASB”) ASC 820, “Fair Value Measurements and Disclosures”, for assets and liabilities measured at fair value on a recurring basis. ASC 820 establishes a common definition for fair value to be applied to existing US GAAP that require the use of fair value measurements which establishes a framework for measuring fair value and expands disclosure about such fair value measurements.

ASC 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Additionally, ASC 820 requires the use of valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. These inputs are prioritized below:

- Level 1: Observable inputs such as quoted market prices in active markets for identical assets or liabilities
- Level 2: Observable market-based inputs or unobservable inputs that are corroborated by market data
- Level 3: Unobservable inputs for which there is little or no market data, which require the use of the reporting entity’s own assumptions.

In addition, FASB ASC 825-10-25 “Fair Value Option” was effective for January 1, 2008. ASC 825-10-25 expands opportunities to use fair value measurements in financial reporting and permits entities to choose to measure many financial instruments and certain other items at fair value.

Income Tax

We record revenues on a gross basis, before deduction for income taxes. We incurred foreign income tax expenses of approximately \$0 and \$65,000 for the three and nine months ended September 30, 2020 and approximately \$0 and \$225 for the three and nine months ended September 30, 2019, respectively.

Long-Lived Assets

We review for impairment whenever events or circumstances indicate that the carrying amount of assets may not be recoverable, pursuant to guidance established in ASC 360-10-35-15, “Impairment or Disposal of Long-Lived Assets.” We recognize an impairment loss when the sum of expected undiscounted future cash flows is less than the carrying amount of the asset. The amount of impairment is measured as the difference between the asset’s estimated fair value and its book value.

Revenue Recognition

We recognize revenue in accordance with ASC Topic 606, “Revenue from Contracts with Customers.” Revenue is recognized when control of the promised goods or services is transferred to customers at an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods or services. Under Topic 606, revenue is recognized when there is a contract which has commercial substance which is approved by both parties and identifies the rights of the parties and the payment terms. We adopted Topic 606 as of January 1, 2018, using the modified retrospective transition method, with no impact on the consolidated financial position or results of operations.

Cost of Revenue

Cost of revenues mainly includes expenses incurred in connection with our patent enforcement activities, such as legal fees, consulting costs, patent maintenance, royalty fees for acquired patents and other related expenses. Cost of revenue does not include expenses related to product development, patent amortization, integration or support, as these are included in general and administrative expenses.

Inventor/Former Owner Royalties and Contingent Legal/Litigation Finance Expenses

In connection with the investment in certain patents and patent rights, certain of our operating subsidiaries may execute related agreements which grant to the inventors and/or former owners of the respective patents or patent rights, the right to receive a percentage of future net revenues (as defined in the respective agreements) generated as a result of licensing and otherwise enforcing the respective patents or patent portfolios.

Our operating subsidiaries may retain the services of law firms that specialize in patent licensing and enforcement and patent law in connection with their licensing and enforcement activities. These law firms may be retained on a contingent fee basis whereby such law firms are paid a percentage of any negotiated fees, settlements or judgments awarded.

Our operating subsidiaries may engage with funding sources that specialize in providing financing for patent licensing and enforcement. These litigation finance firms may be engaged on a non-recourse basis whereby such litigation finance firms are paid a percentage of any negotiated fees, settlements or judgments awarded in exchange for providing funding for legal fees and out of pocket expenses incurred as a result of the licensing and enforcement activities.

The economic terms of the inventor agreements, operating agreements, contingent legal fee arrangements and litigation financing agreements associated with the patent portfolios owned or controlled by our operating subsidiaries, if any, including royalty rates, contingent fee rates and other terms, vary across the patent portfolios owned or controlled by such operating subsidiaries. Inventor/former owner royalties, payments to non-controlling interests, contingent legal fees expenses and litigation finance expenses fluctuate period to period, based on the amount of revenues recognized each period, the terms and conditions of revenue agreements executed each period and the mix of specific patent portfolios with varying economic terms and obligations generating revenues each period. Inventor/former owner royalties, contingent legal fees expenses and litigation finance expenses will continue to fluctuate and may continue to vary significantly period to period, based primarily on these factors.

Recent Accounting Pronouncements

Management does not believe that there are any recently issued, but not effective, accounting standards which, if currently adopted, would have a material effect on our financial statements.

Going Concern

We have an accumulated deficit of approximately \$20,974,000 and negative working capital of approximately \$7,520,000 as of September 30, 2020. Because of our continuing losses, our working capital deficiency, the uncertainty of future revenue, our obligations to Intellectual Ventures and Intelligent Partners, as transferee of United Wireless, our low stock price and the absence of a trading market in our common stock, our ability to raise funds in equity market or from lenders is severely impaired. These conditions together with the effects of the COVID-19 pandemic and the steps taken by the state to slow the spread of the virus and its effects on our business raise substantial doubt as to our ability to continue as a going concern. Although we may seek to raise funds and to obtain third party funding for litigation to enforce our intellectual property rights, the availability of such funds, particularly in view of the COVID-19 pandemic, is uncertain. Our financial statements do not include any adjustments that might result from the outcome of this uncertainty. We are in default on payment of principal and interest on our convertible notes due September 30, 2020 in the principal amount of \$4,672,812. Accrued interest on the notes was \$117,780. We obtained a standstill agreement of the noteholder until November 13, 2020. In connection with the standstill agreement, we paid the \$117,780 interest accrued at September 30, 2020, and, in connection with an extension of the standstill to November 13, 2020, we paid additional interest through the standstill period of \$20,000. Although we are in negotiation with the noteholder with respect to a restructure of the note and other payment agreements between the noteholder and us, we can give no assurance that the negotiations will result in a revised agreement. Our failure to negotiate an acceptable restructure of the agreement could materially and adversely affect our ability to continue in business and it may be necessary to seek protection under the Bankruptcy Act.

Off-balance Sheet Arrangements

We have not entered into any other financial guarantees or other commitments to guarantee the payment obligations of any third parties. We have not entered into any derivative contracts that are indexed to our shares and classified as stockholder's equity or that are not reflected in our consolidated financial statements. Furthermore, we do not have any retained or contingent interest in assets transferred to an unconsolidated entity that serves as credit, liquidity or market risk support to such entity.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

We are a smaller reporting company as defined by Rule 12b-2 of the Securities Exchange Act of 1934 and are not required to provide the information under this item.

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Item 4. Controls and Procedures.

Management's Conclusions Regarding Effectiveness of Disclosure Controls and Procedures

We conducted an evaluation of the effectiveness of our "disclosure controls and procedures" ("Disclosure Controls"), as defined by Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), as of September 30, 2020, the end of the period covered by this Quarterly Report on Form 10-Q. The Disclosure Controls evaluation was done under the supervision and with the participation of management, including our chief executive officer and chief financial officer, which positions are held by the same person. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives. Based upon this evaluation, our chief executive officer and chief financial officer concluded that, due to the inadequacy of our internal controls over financial reporting and our limited internal audit function, our disclosure controls were not effective as of September 30, 2020, such that the information required to be disclosed by us in reports filed under the Securities Exchange Act of 1934 is (i) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and (ii) accumulated and communicated to the president and treasurer, as appropriate to allow timely decisions regarding disclosure.

Changes in Internal Control over Financial Reporting.

As reported in our annual report on Form 10-K for the year ended December 31, 2019, management has determined that our internal audit our internal controls contains material weaknesses due to lack of segregation of duties within accounting functions as well as lack of qualified accounting personnel and excessive reliance on third party consultants for accounting, financial reporting and related activities. These problems continue to affect us as we only have on full-time executive officer, who is our only full-time employee and who serves as chief executive officer and chief financial officer.

During the period ended September 30, 2020, there was no change in our internal control over financial reporting (as such term is defined in Rule 13a-15(f) under the Exchange Act) that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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PART II - OTHER INFORMATION

Item 6. Exhibits.

10.1	SBA Economic Injury Disaster Loan Note and Security Agreement dated May 14, 2020
31.1	Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.ins	XBRL Instance Document

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.

Date: November 16, 2020

QUEST PATENT RESEARCH CORPORATION

By: /s/ Jon C. Scahill
 Jon C. Scahill
 Chief Executive Officer and
 Acting Chief Financial Officer

EX-10.1 2 f10q0920ex10-1_questpatent.htm SBA ECONOMIC INJURY DISASTER LOAN NOTE AND SECURITY AGREEMENT DATED MAY 14, 2020

Exhibit 10.1

DocuSign Envelope ID: C8907BDC-4F3B-47B6-B4A3-198EB576CE74

Doc # L-01-0233279-01

SBA Loan #6317357403

Application #3300070808

 <p style="text-align: center;">U.S. Small Business Administration</p> <p style="text-align: center;">NOTE</p> <p style="text-align: center;">(SECURED DISASTER LOANS)</p>	Date: 05.14.2020
	Loan Amount: \$150,000.00
	Annual Interest Rate: 3.75%

SBA Loan # 6317357403

Application #3300070808

- PROMISE TO PAY:** In return for a loan, Borrower promises to pay to the order of SBA the amount of **one hundred and fifty thousand and 00/100 Dollars (\$150,000.00)**, interest on the unpaid principal balance, and all other amounts required by this Note.
- DEFINITIONS:** **A)** "Collateral" means any property taken as security for payment of this Note or any guarantee of this Note. **B)** "Guarantor" means each person or entity that signs a guarantee of payment of this Note. **C)** "Loan Documents" means the documents related to this loan signed by Borrower, any Guarantor, or anyone who pledges collateral.
- PAYMENT TERMS:** Borrower must make all payments at the place SBA designates. Borrower may prepay this Note in part or in full at any time, without notice or penalty. Borrower must pay principal and interest payments of **\$731.00** every **month** beginning **Twelve (12)** months from the date of the Note. SBA will apply each installment payment first to pay interest accrued to the day SBA receives the payment and will then apply any remaining balance to reduce principal. All remaining principal and accrued interest is due and payable **Thirty (30) years** from the date of the Note.
- DEFAULT:** Borrower is in default under this Note if Borrower does not make a payment when due under this Note, or if Borrower: **A)** Fails to comply with any provision of this Note, the Loan Authorization and Agreement, or other Loan Documents; **B)** Defaults on any other SBA loan; **C)** Sells or otherwise transfers, or does not preserve or account to SBA's satisfaction for, any of the Collateral or its proceeds; **D)** Does not disclose, or anyone acting on their behalf does not disclose, any material fact to SBA; **E)** Makes, or anyone acting on their behalf makes, a materially false or misleading representation to SBA; **F)** Defaults on any loan or agreement with another creditor, if SBA believes the default may materially affect Borrower's ability to pay this Note; **G)** Fails to pay any taxes when due; **H)** Becomes the subject of a proceeding under any bankruptcy or insolvency law; **I)** Has a receiver or liquidator appointed for any part of their business or property; **J)** Makes an assignment for the benefit of creditors; **K)** Has any adverse change in financial condition or business operation that SBA believes may materially affect Borrower's ability to pay this Note; **L)** Dies; **M)** Reorganizes, merges, consolidates, or otherwise changes ownership or business structure without SBA's prior written consent; or, **N)** Becomes the subject of a civil or criminal action that SBA believes may materially affect Borrower's ability to pay this Note.
- SBA'S RIGHTS IF THERE IS A DEFAULT:** Without notice or demand and without giving up any of its rights, SBA may: **A)** Require immediate payment of all amounts owing under this Note; **B)** Have recourse to collect all amounts owing from any Borrower or Guarantor (if any); **C)** File suit and obtain judgment; **D)** Take possession of any Collateral; or **E)** Sell, lease, or otherwise dispose of, any Collateral at public or private sale, with or without advertisement.
- SBA'S GENERAL POWERS:** Without notice and without Borrower's consent, SBA may: **A)** Bid on or buy the Collateral at its sale or the sale of another lienholder, at any price it chooses; **B)** Collect amounts due under this Note, enforce the terms of this Note or any other Loan Document, and preserve or dispose of the Collateral. Among other things, the expenses may include payments for property taxes, prior liens, insurance, appraisals, environmental remediation costs, and reasonable attorney's fees and costs. If SBA incurs such expenses, it may demand immediate reimbursement from Borrower or add the expenses to the principal balance; **C)** Release anyone obligated to pay this Note; **D)** Compromise, release, renew, extend or substitute any of the Collateral; and **E)** Take any action necessary to protect the Collateral or collect amounts owing on this Note.

- FEDERAL LAW APPLIES:** When SBA is the holder, this Note will be interpreted and enforced under federal law, including SBA regulations. SBA may use state or local procedures for filing papers, recording documents, giving notice, foreclosing liens, and other purposes. By using such procedures, SBA does not waive any federal immunity from state or local control, penalty, tax, or liability. As to this Note, Borrower may not claim or assert against SBA any local

- 8. **GENERAL PROVISIONS:** **A)** All individuals and entities signing this Note are jointly and severally liable. **B)** Borrower waives all suretyship defenses. **C)** Borrower must sign all documents required at any time to comply with the Loan Documents and to enable SBA to acquire, perfect, or maintain SBA’s liens on Collateral. **D)** SBA may exercise any of its rights separately or together, as many times and in any order it chooses. SBA may delay or forgo enforcing any of its rights without giving up any of them. **E)** Borrower may not use an oral statement of SBA to contradict or alter the written terms of this Note. **F)** If any part of this Note is unenforceable, all other parts remain in effect. **G)** To the extent allowed by law, Borrower waives all demands and notices in connection with this Note, including presentment, demand, protest, and notice of dishonor. Borrower also waives any defenses based upon any claim that SBA did not obtain any guarantee; did not obtain, perfect, or maintain a lien upon Collateral; impaired Collateral; or did not obtain the fair market value of Collateral at a sale. **H)** SBA may sell or otherwise transfer this Note.
- 9. **MISUSE OF LOAN FUNDS:** Anyone who wrongfully misapplies any proceeds of the loan will be civilly liable to SBA for one and one-half times the proceeds disbursed, in addition to other remedies allowed by law.
- 10. **BORROWER’S NAME(S) AND SIGNATURE(S):** By signing below, each individual or entity acknowledges and accepts personal obligation and full liability under the Note as Borrower.

Quest Patent Research Corporation

/s/ Jon C. Scahill
Jon C. Scahill, Owner/Officer

DocuSign Envelope ID: C8907BDC-4F3B-47B6-B4A3-198EB576CE74

Doc # L-01-0233279-01

SBA Loan #6317357403

Application #3300070808



U.S. Small Business Administration
SECURITY AGREEMENT

SBA Loan #:	6317357403
Borrower:	Quest Patent Research Corporation
Secured Party:	The Small Business Administration, an Agency of the U.S. Government
Date:	05.14.2020
Note Amount:	\$150,000.00

1. DEFINITIONS.

Unless otherwise specified, all terms used in this Agreement will have the meanings ascribed to them under the Official Text of the Uniform Commercial Code, as it may be amended from time to time, (“UCC”). “SBA” means the Small Business Administration, an Agency of the U.S. Government.

2. GRANT OF SECURITY INTEREST.

For value received, the Borrower grants to the Secured Party a security interest in the property described below in paragraph 4 (the “Collateral”).

3. OBLIGATIONS SECURED.

This Agreement secures the payment and performance of: (a) all obligations under a Note dated 05.14.2020, made by Quest Patent Research Corporation, made payable to Secured Lender, in the amount of \$150,000.00 (“Note”), including all costs and expenses (including reasonable attorney’s fees), incurred by Secured Party in the disbursement, administration and collection of the loan evidenced by the Note; (b) all costs and expenses (including reasonable attorney’s fees), incurred by Secured Party in the protection, maintenance and enforcement of the security interest hereby granted; (c) all obligations of the Borrower in any other agreement relating to the Note; and (d) any modifications, renewals, refinancings, or extensions of the foregoing obligations.

4. COLLATERAL DESCRIPTION.

The Collateral in which this security interest is granted includes the following property that Borrower now owns or shall acquire or create immediately upon the acquisition or creation thereof: all tangible and intangible personal property, including, but not limited to: (a) inventory, (b) equipment, (c) instruments, including promissory notes (d) chattel paper, including tangible chattel paper and electronic chattel paper, (e) documents, (f) letter of credit rights, (g) accounts, including health-care insurance receivables and credit card receivables, (h) deposit accounts, (i) commercial tort claims, (j) general intangibles, including payment intangibles and software and (k) as-extracted collateral as such terms may from time to time be defined in the Uniform Commercial Code. The security interest Borrower grants includes all accessions, attachments, accessories, parts, supplies and replacements for the Collateral, all products, proceeds and collections thereof and all records and data relating thereto.

5. RESTRICTIONS ON COLLATERAL TRANSFER.

Borrower will not sell, lease, license or otherwise transfer (including by granting security interests, liens, or other encumbrances in) all or any part of the Collateral or Borrower's interest in the Collateral without Secured Party's written or electronically communicated approval, except that Borrower may sell inventory in the ordinary course of business on customary terms. Borrower may collect and use amounts due on accounts and other rights to payment arising or created in the ordinary course of business, until notified otherwise by Secured Party in writing or by electronic communication.

6. MAINTENANCE AND LOCATION OF COLLATERAL; INSPECTION; INSURANCE.

Borrower must promptly notify Secured Party by written or electronic communication of any change in location of the Collateral, specifying the new location. Borrower hereby grants to Secured Party the right to inspect the Collateral at all reasonable times and upon reasonable notice. Borrower must: (a) maintain the Collateral in good condition; (b) pay promptly all taxes, judgments, or charges of any kind levied or assessed thereon; (c) keep current all rent or mortgage payments due, if any, on premises where the Collateral is located; and (d) maintain hazard insurance on the Collateral, with an insurance company and in an amount approved by Secured Party (but in no event less than the replacement cost of that Collateral), and including such terms as Secured Party may require including a Lender's Loss Payable Clause in favor of Secured Party. Borrower hereby assigns to Secured Party any proceeds of such policies and all unearned premiums thereon and authorizes and empowers Secured Party to collect such sums and to execute and endorse in Borrower's name all proofs of loss, drafts, checks and any other documents necessary for Secured Party to obtain such payments.

7. CHANGES TO BORROWER'S LEGAL STRUCTURE, PLACE OF BUSINESS, JURISDICTION OF ORGANIZATION, OR NAME.

Borrower must notify Secured Party by written or electronic communication not less than 30 days before taking any of the following actions: (a) changing or reorganizing the type of organization or form under which it does business; (b) moving, changing its place of business or adding a place of business; (c) changing its jurisdiction of organization; or (d) changing its name. Borrower will pay for the preparation and filing of all documents Secured Party deems necessary to maintain, perfect and continue the perfection of Secured Party's security interest in the event of any such change.

8. PERFECTION OF SECURITY INTEREST.

Borrower consents, without further notice, to Secured Party's filing or recording of any documents necessary to perfect, continue, amend or terminate its security interest. Upon request of Secured Party, Borrower must sign or otherwise authenticate all documents that Secured Party deems necessary at any time to allow Secured Party to acquire, perfect, continue or amend its security interest in the Collateral. Borrower will pay the filing and recording costs of any documents relating to Secured Party's security interest. Borrower ratifies all previous filings and recordings, including financing statements and notations on certificates of title. Borrower will cooperate with Secured Party in obtaining a Control Agreement satisfactory to Secured Party with respect to any Deposit Accounts or Investment Property, or in otherwise obtaining control or possession of that or any other Collateral.

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Doc # L-01-0233279-01

SBA Loan #6317357403

Application #3300070808

9. DEFAULT.

Borrower is in default under this Agreement if: (a) Borrower fails to pay, perform or otherwise comply with any provision of this Agreement; (b) Borrower makes any materially false representation, warranty or certification in, or in connection with, this Agreement, the Note, or any other agreement related to the Note or this Agreement; (c) another secured party or judgment creditor exercises its rights against the Collateral; or (d) an event defined as a "default" under the Obligations occurs. In the event of default and if Secured Party requests, Borrower must assemble and make available all Collateral at a place and time designated by Secured Party. Upon default and at any time thereafter, Secured Party may declare all Obligations secured hereby immediately due and payable, and, in its sole discretion, may proceed to enforce payment of same and exercise any of the rights and remedies available to a secured party by law including those available to it under Article 9 of the UCC that is in effect in the jurisdiction where Borrower or the Collateral is located. Unless otherwise required under applicable law, Secured Party has no obligation to clean or otherwise prepare the Collateral for sale or other disposition and Borrower waives any right it may have to require Secured Party to enforce the security interest or payment or performance of the Obligations against any other person.

10. FEDERAL RIGHTS.

When SBA is the holder of the Note, this Agreement will be construed and enforced under federal law, including SBA regulations. Secured Party or SBA may use state or local procedures for filing papers, recording documents, giving notice, enforcing security interests or liens, and for any other purposes. By using such procedures, SBA does not waive any federal immunity from state or local control, penalty, tax or liability. As to this Agreement, Borrower may not claim or assert any local or state law against SBA to deny any obligation, defeat any claim of SBA, or preempt federal law.

11. GOVERNING LAW.

Unless SBA is the holder of the Note, in which case federal law will govern, Borrower and Secured Party agree that this Agreement will be governed by the laws of the jurisdiction where the Borrower is located, including the UCC as in effect in such jurisdiction and without reference to its conflicts of laws principles.

12. SECURED PARTY RIGHTS.

All rights conferred in this Agreement on Secured Party are in addition to those granted to it by law, and all rights are cumulative and may be exercised simultaneously. Failure of Secured Party to enforce any rights or remedies will not constitute an estoppel or waiver of Secured Party's ability to exercise such rights or remedies. Unless otherwise required under applicable law, Secured Party is not liable for any loss or damage to Collateral in its possession or under its control, nor will such loss or damage reduce or discharge the Obligations that are due, even if Secured Party's actions or inactions caused or in any way contributed to such loss or damage.

13. SEVERABILITY.

If any provision of this Agreement is unenforceable, all other provisions remain in effect.

SBA Form 1059 (09-19) Previous Editions are obsolete.

14. BORROWER CERTIFICATIONS.

Borrower certifies that: (a) its Name (or Names) as stated above is correct; (b) all Collateral is owned or titled in the Borrower's name and not in the name of any other organization or individual; (c) Borrower has the legal authority to grant the security interest in the Collateral; (d) Borrower's ownership in or title to the Collateral is free of all adverse claims, liens, or security interests (unless expressly permitted by Secured Party); (e) none of the Obligations are or will be primarily for personal, family or household purposes; (f) none of the Collateral is or will be used, or has been or will be bought primarily for personal, family or household purposes; (g) Borrower has read and understands the meaning and effect of all terms of this Agreement.

15. BORROWER NAME(S) AND SIGNATURE(S).

By signing or otherwise authenticating below, each individual and each organization becomes jointly and severally obligated as a Borrower under this Agreement.

Quest Patent Research Corporation

/s/ Jon C. Scahill

Jon C. Scahill, Owner/Officer

Date: 5/14/2020

SBA Form 1059 (09-19) Previous Editions are obsolete.

EX-31.1 3 f10q0920ex31-1_questpatent.htm CERTIFICATION

Exhibit 31.1

**CERTIFICATION OF PRINCIPAL EXECUTIVE AND FINANCIAL OFFICER
PURSUANT TO SECTION 302 OF THE
SARBANES-OXLEY ACT OF 2002**

I, Jon C. Scahill, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Quest Patent Research Corporation;
2. Based on my knowledge, this quarterly 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 quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly 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 quarterly report;
4. The registrant's other certifying officer 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 controls 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 quarterly report is being prepared;
 - b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - 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;
 - 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 that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent function):
 - a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

Dated: November 16, 2020

By: /s/ Jon C. Scahill

Chief Executive Officer and
Acting Chief Financial Officer
(Principal Executive and Accounting Officer)

EX-32.1 4 f10q0920ex32-1_questpatent.htm CERTIFICATION

Exhibit 32.1

**CERTIFICATION 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 Quest Patent Research Corporation (the "Company") on Form 10-Q for the period ended September 30, 2020 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Jon C. Scahill, chief executive officer and acting chief financial officer of the Company, certify, pursuant to 18 U.S.C. section 1350 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 results of operations of the Company.

Dated: November 16, 2020

By: /s/ Jon C. Scahill
Jon C. Scahill
Chief Executive Officer and
Acting Chief Financial Officer
(Principal Executive and Accounting Officer)

