

FALCONSTOR SOFTWARE, INC.

111 Congress Avenue, Suite 500, Austin, TX 78701
(631) 777-5188
www.falconstor.com
www.falconstor.com/contact
SIC – 7372

Quarterly Report

For the period ended, March 31, 2025 (the “Reporting Period”)

Outstanding Shares

The number of shares outstanding of our Common Stock was:

7,145,393 as of March 31, 2025
7,143,978 as of December 31, 2024

Shell Status

Indicate by check mark whether the company is a shell company (as defined in Rule 405 of the Securities Act of 1933, Rule 12b-2 of the Exchange Act of 1934 and Rule 15c2-11 of the Exchange Act of 1934):

Yes: ☐ No: ☒

Indicate by check mark whether the company’s shell status has changed since the previous reporting period:

Yes: ☐ No: ☒

Change in Control

Indicate by check mark whether a Change in Control of the company has occurred over this reporting period:

Yes: ☐ No: ☒

1) Name and address of the issuer and its predecessors:

The exact name of the issuer is FalconStor Software, Inc.

The issuer was incorporated in the State of Delaware in 1994 and is active and in good standing. The issuer was originally incorporated as Network Peripherals Inc. and changed its name to FalconStor Software, Inc. in 2001 through the completion of a reverse merger.

There have been no trading suspension orders issued by the SEC concerning the issuer since inception.

The issuer does not currently anticipate any stock split, stock dividend, recapitalization, merger, acquisition, spin-off, or reorganization and none have occurred in the past 12 months.

The address of the issuer's principal executive office:

111 Congress Avenue, Suite 500
Austin, TX 78701

The address of the issuer's principal place of business:

Check if principal executive office and principal place of business are the same address: ☐

Has the issuer or any of its predecessors been in bankruptcy, receivership, or any similar proceeding in the past five years?

No: ☒ Yes: ☐ If Yes, provide additional details below:

2) Security Information

Transfer Agent

Name: Computershare Investor Services
Address: 150 Royall Street, Canton MA 02021
Email: danielle.mann@computershare.com
Phone: (781) 575-2427

Publicly Quoted or Traded Securities:

Trading symbol: FALC

Exact title and class of securities outstanding: Common Stock and Series A redeemable convertible preferred stock

CUSIP: 306137209

Par or stated value: \$0.001 common stock and \$0.001 preferred stock

Total shares authorized: 30,000,000 common stock as of March 31, 2025

Total shares authorized: 2,000,000 preferred stock as of March 31, 2025

Total shares outstanding: 7,145,393 common stock as of March 31, 2025

Total shares outstanding: 900,000 preferred stock as of March 31, 2025

Total number of shareholders of record: 35 common stock as of March 31, 2025

Total number of shareholders of record: 5 preferred stock as of March 31, 2025

Security Description:

1. For common equity, describe any dividend, voting and preemption rights.

Subject to the Amended and Restated By-Laws (the "Bylaws") of FalconStor Software, Inc. (the "Company" or "FalconStor") holders of the Common Stock of the Company (the "Common Stock") are entitled to one vote for every share of such stock that is registered in his or her name on the record date of the applicable shareholders meeting.

2. For preferred stock, describe the dividend, voting, conversion, and liquidation rights as well as redemption or sinking fund provisions.

Dividend

Subject to the Amended and Restated Certificate of Designations, Preferences and Rights of Series A Convertible Preferred Stock of the Company, dated as of June 24, 2021 (as amended, the "Certificate of Designations"), the holders of the Company's Series A Redeemable Convertible Preferred Stock (the "Series A Preferred Stock") are entitled to receive cumulative dividends at the rate (as a percentage of the stated value per share) equal to the lesser of (x) the prime corporate rate announced from time to time at the end of each calendar month by the Wall Street Journal plus 5% and (y) 10%, per annum, accruing on a daily basis and compounding monthly (collectively, "Series A Preferred

Dividends”), except that the Company is not permitted to pay such dividends in cash while any indebtedness under the Amended and Restated Term Loan Credit Agreement, dated as of February 23, 2018 (the “Amended and Restated Loan Agreement”), by and among the Company, the other loan parties thereto, as guarantors, the various financial institutions party thereto, as lenders, and HCP-FVA, LLC (“HCP-FVA”) remains outstanding without the consent of the Required Holders (as defined in the Amended and Restated Loan Agreement). In addition, the declaration and payment of dividends is subject to compliance with applicable law and unpaid dividends will accrue. A holder’s right to convert its shares of Series A Preferred Stock and receive dividends in the form of Common Stock is subject to certain limitations including, among other things, that the shares of Common Stock issuable upon conversion or as dividends will not, prior to receipt of stockholder approval, result in any holder beneficially owning greater than 9.99% of the Company’s currently outstanding shares of Common Stock.

Voting

Each holder of Series A Preferred Stock has a vote equal to the number of shares of Common Stock into which its Series A Preferred Stock would be convertible as of the record date assuming a conversion price equal to \$123.00 (subject to adjustment from time to time for stock splits, stock dividends, stock combinations and similar events, as applicable, with respect to the Common Stock). In addition, the holders of a majority of the Series A Preferred Stock must approve certain actions, including any amendments to the Company’s Restated Certificate of Incorporation, as amended, or the Bylaws, in each case, that adversely affects the voting powers, preferences or other rights of the Series A Preferred Stock; payment of dividends or distributions; any liquidation, capitalization, reorganization or any other fundamental transaction of the Company; issuance of any equity security senior to or on parity with the Series A Preferred Stock as to dividend rights, redemption rights, liquidation preference and other rights; issuances of equity below the conversion price; any liens or borrowings other than non-convertible indebtedness from standard commercial lenders which does not exceed 80% of the Company’s accounts receivable; and the redemption or purchase of any of the capital stock of the Company.

Conversion

Pursuant to the Certificate of Designations, each share of Series A Preferred Stock can be converted into shares of the Company’s Common Stock, at an initial conversion price of \$102.488 per share, subject to appropriate adjustments for any stock dividend, stock split, stock combination, reclassification or similar transaction, (i) at any time at the option of the holder or (ii) by the Company if, following the first anniversary of the issuance of the Series A Preferred Stock (subject to extension under certain circumstances), the volume weighted average trading price per share of the Company’s common stock for sixty (60) consecutive trading days exceeds 250% of the conversion price and continues to exceed 225% of the conversion price through the conversion date, subject at all times to the satisfaction of, and the limitations imposed by, the equity conditions set forth in the Certificate of Designations (including, without limitation, the volume limitations set forth therein).

Liquidation

Upon the occurrence of any liquidation, dissolution or winding up of the Company, either voluntary or involuntary (“Liquidation Event”), the holders of Series A Preferred Stock are entitled to receive, prior and in preference to any distribution of any of the assets or funds of the Company to the holders of junior securities by reason of their ownership thereof, an amount per share in cash equal to the sum of (i) one hundred percent (100%) of the stated value per share of Series A Preferred Stock then held by them (as adjusted for any stock split, stock dividend, stock combination or other similar transactions with respect to the Series A Preferred Stock), plus (ii) 100% of all declared but unpaid dividends, and all accrued but unpaid dividends on each such share of Series A Preferred Stock (including, for the avoidance of doubt, any Series A Preferred Dividends applicable to such share of Series A Preferred Stock that the Company has elected to accrue pursuant to Section 3(b) of the Certificate of Designations and any Series A Preferred Dividends that have accrued thereon), in each case as of the date of such Liquidation Event (clauses (i) and (ii) together, the “Series A Preferred Stock Liquidation Preference”).

Redemption

Upon certain triggering events, such as bankruptcy, insolvency or a material adverse effect or failure of the Company to issue shares of Common Stock upon conversion of the Series A Preferred Stock in accordance with its obligations, the holders of the Series A Preferred Stock may require the Company to redeem all or some of the Series A Preferred Stock at a price per share equal to the greater of (i) the Series A Preferred Stock Liquidation Preference, and (ii) the product of the number of shares of Common Stock underlying a share of Series A Preferred Stock (and accrued and unpaid dividends with respect thereto) and the closing price as of the occurrence of the triggering event. On February 12, 2024, the Company entered into letter agreement with Hale Capital to further extend the redemption date of the Series A Preferred Stock to June 30, 2025. On January 10, 2025, the Company entered into another letter agreement with Hale Capital to further extend the redemption date of the Series A Preferred Stock to June 30, 2026. On or after June 30, 2026, subject to the approval of HCP-FVA, each holder of Series A Preferred Stock can also require the Company to redeem its Series A Preferred Stock in cash at a per share price equal to 100% of the stated value of a share of Series A Preferred Stock plus accrued and unpaid dividends with respect thereto. Notwithstanding the

forgoing, no holder of Series A Preferred Stock is permitted to exercise any rights or remedies upon a Breach Event (as defined in the Certificate of Designations) or to exercise any redemption rights under the Certificate of Designations, unless approved by the holders of a majority of the then-outstanding shares of Series A Preferred Stock.

Upon consummation of a fundamental sale transaction, the Series A Preferred Stock will be redeemed at a per share redemption price equal to the greater of (y) 250% of the stated value of the Series A Preferred Stock and (z) the price payable in respect of such share of Series A Preferred Stock if such share of Series A Preferred Stock had been converted into such number of shares of common stock in accordance with the Certificate of Designations (but without giving effect to any limitations or restrictions contained therein) immediately prior to such fundamental sale transaction; provided however that the 250% threshold is changed to 100% if the fundamental sale transaction is approved by the two Series A Directors (as defined in the Certificate of Designations). In addition, if the Company consummates an equity or debt financing that results in more than \$5.0 million of net proceeds to the Company and/or its subsidiaries, the holders of Series A Preferred Stock will have the right, but not the obligation, to require the Company to use the net proceeds in excess of \$5.0 million to repurchase all or a portion of the Series A Preferred Stock at a per share price equal to the greater of (i) the sum of 100% of the stated value of such share of Series A Preferred Stock plus accrued and unpaid dividends with respect thereto, and (ii) the number of shares of common stock into which such share of Series A Preferred Stock is then convertible multiplied by the greater of (y) the closing price of the Common Stock on the date of announcement of such financing or (z) the closing price of the Common Stock on the date of consummation of such financing.

3. Describe any other material rights of common or preferred stockholders.

N/A

4. Describe any material modifications to rights of holders of the company's securities that have occurred over the reporting period covered by this report.

N/A

3) Issuance History

A. Changes to the Number of Outstanding Shares

Indicate by check mark whether there were any changes to the number of outstanding shares within the past two completed fiscal years:

No: ☐ Yes: ☒ (If yes, you must complete the table below)

Shares Outstanding as of Second Most Recent Fiscal Year End: Opening Balance: Date: <u>December 31, 2022</u> Common: <u>7,118,609</u> Preferred: <u>900,000</u>									
Date of Transaction	Transaction type (e.g., new issuance, cancellation, shares returned to treasury)	Number of Shares Issued (or cancelled)	Class of Securities	Value of shares issued (\$/per share) at Issuance	Were the shares issued at a discount to market price at the time of issuance? (Yes/No)	Individual/ Entity Shares were issued to. *You must disclose the control person(s) for any entities listed.	Reason for share issuance (e.g. for cash or debt conversion) -OR- Nature of Services Provided	Restricted or Unrestricted as of this filing.	Exemption or Registration Type.
February 17, 2023	New Issuance	1,415	Common	\$1.39	No	Vincent Sita	Executive Compensation - Shares issued pursuant to vesting of restricted stock units	Unrestricted	Exemption – Section 4a2 of Securities Act
March 6, 2023	New Issuance	925	Common	\$1.99	No	Non-Executive Employee	Employee Compensation - Shares issued pursuant to vesting of restricted stock units	Unrestricted	Exemption – Section 4a2 of Securities Act
March 16, 2023	New Issuance	1,250	Common	\$1.75	No	Non-Executive Employee	Employee Compensation - Shares issued pursuant to vesting of restricted stock units	Unrestricted	Exemption – Section 4a2 of Securities Act
September 22, 2023	New Issuance	2,832	Common	\$1.00	No	Non-Executive Employee	Employee Compensation - Shares issued pursuant to vesting of restricted stock units	Unrestricted	Exemption – Section 4a2 of Securities Act
October 5, 2023	New Issuance	6,808	Common	\$1.00	No	Non-Executive Employee	Employee Compensation - Shares issued pursuant to vesting of restricted stock units	Unrestricted	Exemption – Section 4a2 of Securities Act
December 15, 2023	New Issuance	1,250	Common	\$1.50	No	Non-Executive Employee	Employee Compensation - Shares issued pursuant to vesting of	Unrestricted	Exemption – Section 4a2 of Securities Act

							restricted stock units		
February 17, 2024	New Issuance	1,415	Common	\$1.33	No	Vincent Sita	Executive Compensation - Shares issued pursuant to vesting of restricted stock units	Unrestricted	Exemption – Section 4a2 of Securities Act
September 22, 2024	New Issuance	1,416	Common	\$1.25	No	Non-Executive Employee	Employee Compensation - Shares issued pursuant to vesting of restricted stock units	Unrestricted	Exemption – Section 4a2 of Securities Act
October 2, 2024	New Issuance	1,840	Common	\$1.39	No	Michael Kelly	Director Compensation - Shares issued pursuant to vesting of restricted stock units	Unrestricted	Exemption – Section 4a2 of Securities Act
October 2, 2024	New Issuance	1,840	Common	\$1.39	No	Barry Rudolph	Director Compensation - Shares issued pursuant to vesting of restricted stock units	Unrestricted	Exemption – Section 4a2 of Securities Act
October 2, 2024	New Issuance	1,840	Common	\$1.39	No	William Miller	Director Compensation - Shares issued pursuant to vesting of restricted stock units	Unrestricted	Exemption – Section 4a2 of Securities Act
October 2, 2024	New Issuance	1,288	Common	\$1.39	No	Non-Executive Employee	Employee Compensation - Shares issued pursuant to vesting of restricted stock units	Unrestricted	Exemption – Section 4a2 of Securities Act
December 10, 2024	New Issuance	1,250	Common	\$1.35	No	Doug Balog	Executive Compensation - Shares issued pursuant to vesting of restricted stock units	Unrestricted	Exemption – Section 4a2 of Securities Act
February 17, 2025	New Issuance	1,415	Common	\$1.90	No	Vincent Sita	Executive Compensation - Shares issued pursuant to vesting of restricted stock units	Unrestricted	Exemption – Section 4a2 of Securities Act
Shares Outstanding on March 31, 2025	Ending Balance: Common: <u>7,145,393</u> Preferred: <u>900,000</u>								

B. Convertible Debt

The following is a complete list of the Company's Convertible Debt which includes all promissory notes, convertible notes, convertible debentures, or any other debt instruments convertible into a class of the issuer's equity securities. The table includes all issued or outstanding convertible debt at any time during the last complete fiscal year and any interim period between the last fiscal year end and the date of this Certification.

☐ Check this box to confirm the Company had no Convertible Debt issued or outstanding at any point during this period

Date of Note Issuance	Principal Amount at Issuance (\$)	Outstanding Balance (\$) (including accrued interest)	Maturity Date	Conversion Terms	# Shares Converted to Date	# of Potential Shares to be Issued Upon Conversion	Name of Noteholder	Reason for Issuance
February 23, 2018	\$3,000,000	\$2,174,924*	June 30, 2026	N/A	None	None	Hale Capital Partners, LP	Loan

* Interest is paid monthly on the Loan; therefore Accrued Interest is \$0.

4) Business, Products and Services

A. Business operations:

FalconStor is the trusted data protection software leader modernizing disaster recovery and backup operations for the hybrid cloud world. The Company enables enterprise customers and managed service providers to secure, migrate, and protect their data while reducing data storage and long-term retention costs by up to 95%. More than 1,000 organizations and managed service providers worldwide standardize on FalconStor as the foundation for their cloud first data protection future. Our products are offered through and supported by a worldwide network of leading original equipment manufacturers, managed service providers ("MSPs"), systems integrators, and resellers.

B. Subsidiaries:

Domestic Subsidiaries:

FalconStor, Inc. (Delaware)
FalconStor AC, Inc. (Delaware)

Foreign Subsidiaries:

FalconStor Software, Inc. (Korea)
FalconStor, Inc. (Taiwan)

C. Principal products or services.

Our products address the increasing demand for hybrid-cloud data protection for multiple devices, networks and platforms across enterprise on-premises data centers, and private and public clouds. Our products are utilized by enterprises and MSPs to address two key areas of enterprise data protection: (i) long-term data retention and recovery, and (ii) data replication to preserve business continuity. As enterprises increasingly look to focus their core IT staffs on application development and refresh, MSPs are increasingly assuming responsibility for cloud integration and data protection. Our integration with modern cloud-based data storage environments, such as IBM Cloud, Amazon Web Services and Microsoft Azure, enables our enterprise customers to significantly reduce costs and improve the portability, security and accessibility of their enterprise data and enables MSPs to serve their customers with their cloud of choice. We believe this accessibility is key in our modern world, where data must be protected and intelligently leveraged to facilitate learning, improve product design and drive competitive advantage. Our products can be used regardless of the underlying hardware, cloud, and source-data, which enables our enterprise customers to leverage their existing hardware and software investments.

5) Facilities

Since the Covid-19 pandemic, we have been essentially operating fully remotely. We maintain a mailing address and rent virtual office facilities at 111 Congress Avenue, Suite 500, Austin, Texas 78701. Our telephone number is (631) 777-5188. We also rent physical office space in Taiwan, and virtual offices in Germany, France, Malaysia, China, Korea, and Japan.

<u>Location</u>	<u>Own/Lease</u>	<u>Description</u>
Taiwan	Lease	Office Space

6) Officers, Directors, and Control Persons

The following tables show the number of shares of common stock beneficially owned by directors, executive officers, by directors and executive officers as a group, and by persons known to the Company to beneficially own more than five percent of the outstanding shares of common stock as of March 31, 2025. For the purposes of computing a person's beneficial ownership, shares of common stock issuable upon the exercise of securities exercisable within 60 days of March 31, 2025, are deemed outstanding for the purposes of computing the share ownership and percentage ownership of the person holding such securities, but are not deemed outstanding for the purposes of computing the percentage ownership of any other person.

Percentage of beneficial ownership is calculated assuming 7,145,393 shares of the Company's stock that were outstanding as of March 31, 2025. Except as otherwise indicated, known to the Company, the beneficial owners of common stock listed below have sole or shared investment and voting power with respect to such shares.

Individual Name or Entity Name⁽¹⁾	Names of Control Person(s) for Entities	Affiliation with Company (e.g. Officer Title /Director/Owner of more than 5%)	City and State	Number of Shares Owned	Class of Shares Owned	Percentage of Class of Shares Owned (undiluted)⁽²⁾
Martin Hale, Hale Fund Management, LLC Hale Capital Management, LP, Hale Capital Partners, LP, HCP-FVA, LLC ⁽³⁾	Martin Hale	Director and Control Person	New York, NY	3,653,377	Common	50.8%
Nantahala Capital Management, LLC ⁽⁴⁾	Wilmot B. Harkey and Daniel Mack	Control Person	Darien, CT	638,151	Common	8.9%
ESW Capital, LLC ⁽⁵⁾	Joseph A. Liemandt	Control Person	Austin, TX	1,308,068	Common	18.3%
Bard Associates ⁽⁶⁾	Timothy B. Johnson	Control Person	Chicago, IL	500,090	Common	7.0%
Michael P. Kelly ⁽⁷⁾		Director	Scottsdale, AZ	20,691	Common	*
Barry Rudolph ⁽⁸⁾		Director	Estes Park, CO	20,636	Common	*
William Miller ⁽⁹⁾		Director	Colorado Springs, CO	12,129	Common	*
Todd Brooks ⁽¹⁰⁾		Director and Executive Officer	Punta Gorda, FL	87,146	Common	1.2%
Vincent Sita ⁽¹¹⁾		Executive Officer	Mont Royal, Quebec, Canada	5,660	Common	*
Martin Hale, Hale Fund Management, LLC Hale Capital Management, LP, Hale	Martin Hale	Director and Control Person	New York, NY	558,000	Preferred	62.0%

Capital Partners, LP, HCP-FVA, LLC ⁽³⁾						
Nantahala Capital Management, LLC ⁽⁴⁾	Wilmot B. Harkey and Daniel Mack	Control Person	Darien, CT	99,807	Preferred	11.1%
ESW Capital, LLC ⁽⁵⁾	Joseph A. Liemandt	Control Person	Austin, TX	224,786	Preferred	25.0%
Michael P. Kelly ⁽⁷⁾		Director	Scottsdale, AZ	1,405	Preferred	*

* Less than 1% of the Company's outstanding common stock.

- (1) A person is deemed to be the beneficial owner of voting securities over which the person has voting power or that can be acquired by such person within 60 days after March 31, 2025 upon the exercise of options or convertible securities, or upon the lapse or the removal of all restrictions on shares of restricted stock. Each beneficial owner's percentage ownership is determined by assuming that options or convertible securities that are held by such person (but not those held by any other person) and that are currently exercisable (i.e., that are exercisable within 60 days from March 31, 2025) have been exercised. Unless otherwise noted, we believe that all persons named in the table have sole voting and investment power with respect to all shares beneficially owned by them.
- (2) Based upon 7,145,393 shares of common stock outstanding as of March 31, 2025.
- (3) Based on information contained in Forms 4 and a report on Schedule 13D/A filed by Mr. Hale, Hale Fund Management, LLC ("Fund Management"), Hale Capital Management, LP ("Capital Management"), Hale Capital Partners, LP ("Hale Capital"), and HCP-FVA on May 22, 2019 and December 31, 2018. Consists of (i) 3,598,932 shares of common stock held by Hale Capital and HCP-FVA which includes 708 shares held by Mr. Hale for the benefit of Hale Capital, and (ii) 558,000 shares of Series A Preferred Stock held by HCP-FVA, which equates to 54,445 shares of common stock on an as-converted basis (without giving effect to the 9.99% blocker contained in the Certificate of Designations), held by HCP-FVA. Each of Mr. Hale, Fund Management, Capital Management and Hale Capital disclaims beneficial ownership of such shares of common stock except to the extent of his or its pecuniary interest.
- (4) Based on information contained in a report on Schedule 13G/A filed by Nantahala Capital Management, LLC ("Nantahala"), Wilmot B. Harkey and Daniel Mack on February 14, 2023. Consists of (i) 628,415 shares of common stock and (ii) 99,807 shares of Series A Preferred Stock that may be converted for 9,736 shares of common stock within 60 days of March 31, 2025. Messrs. Harkey and Mack are the managing members of Nantahala and disclaim beneficial ownership of such shares of common stock except to the extent of their pecuniary interest.
- (5) Based on information contained in a report on Schedule 13D/A filed by ESW Capital, LLC and Joseph A. Liemandt on December 31, 2018. Consists of (i) 1,286,135 shares of common stock and (ii) 224,786 shares of Series A Preferred Stock that may be converted for 21,933 shares of common stock within 60 days of March 31, 2025. ESW Capital, LLC and Mr. Liemandt disclaim Section 13(d) beneficial ownership with respect to 21,933 shares of common stock issuable upon conversion of Series A Preferred Stock as a result of the application of the 9.99% blocker contained in the Certificate of Designations. Mr. Liemandt is the sole voting member of ESW Capital, LLC and disclaims beneficial ownership of such shares of common stock except to the extent of his pecuniary interest.
- (6) Based on information contained in a report on Schedule 13G filed by Bard Associates, Inc. on January 4, 2024. Consists of 500,090 shares of common stock.
- (7) Based on information contained in Forms 3 and 4 filed by Mr. Kelly and certain other information. Consists of (i) 20,554 shares of common stock and (ii) 1,405 shares of Series A Preferred Stock held by Mr. Kelly, which equates to 137 shares of common stock on an as-converted basis (without giving effect to the 9.99% blocker contained in the Certificate of Designations) held by Mr. Kelly.
- (8) Based on information contained in Forms 3, 4 and 5 filed by Mr. Rudolph and certain other information. Consists of 20,636 shares of common stock held by Mr. Rudolph.

- (9) Based on information contained in Forms 3, 4 and 5 filed by Mr. Miller and certain other information. Consists of 12,129 shares of common stock held by Mr. Miller which includes 26 shares of common stock held by PV Strategies LLC, a hedge fund managed by Miller Investment Management LLC, a registered investment adviser of which Mr. Miller is a principal. Mr. Miller, as the principal of Miller Investment Management LLC, may be deemed the beneficial owner of shares owned by PV Strategies LLC. Mr. Miller disclaims beneficial ownership of such shares except to the extent of his pecuniary interest therein.
- (10) Based on information contained in Forms 3, 4 and 5 filed by Mr. Brooks and certain other information. Consists of 87,146 shares of common stock.
- (11) Based on information contained in Forms 3 and 4 filed by Mr. Sita and certain other information. Consists of 5,660 shares of common stock.

7) Legal/Disciplinary History

A. Identify whether any of the persons or entities listed above have, in the past 10 years, been the subject of:

- 1. Been the subject of an indictment or conviction in a criminal proceeding or plea agreement or named as a defendant in a pending criminal proceeding (excluding minor traffic violations);

N/A

- 2. Been the subject of the entry of an order, judgment, or decree, not subsequently reversed, suspended or vacated, by a court of competent jurisdiction that permanently or temporarily enjoined, barred, suspended or otherwise limited such person's involvement in any type of business, securities, commodities, financial- or investment-related, insurance or banking activities;

N/A

- 3. Been the subject of a finding, disciplinary order or judgment by a court of competent jurisdiction (in a civil action), the Securities and Exchange Commission, the Commodity Futures Trading Commission, a state securities regulator of a violation of federal or state securities or commodities law, or a foreign regulatory body or court, which finding or judgment has not been reversed, suspended, or vacated;

N/A

- 4. Named as a defendant or a respondent in a regulatory complaint or proceeding that could result in a "yes" answer to part 3 above; or

N/A

- 5. Been the subject of an order by a self-regulatory organization that permanently or temporarily barred, suspended, or otherwise limited such person's involvement in any type of business or securities activities.

N/A

- 6. Been the subject of a U.S Postal Service false representation order, or a temporary restraining order, or preliminary injunction with respect to conduct alleged to have violated the false representation statute that applies to U.S mail.

N/A

B. Material pending legal proceedings: None

8) Third Party Service Providers

Securities Counsel:

Name: Olshan Frome Wolosky LLP
Address: 1325 Avenue of the Americas
New York, NY 10019
Phone: (212)-451-2252
Email: KSchlesinger@olshanlaw.com

Auditor:

Name: Weaver & Tidwell, LLP
Address: 1601 South MoPac Expressway, Suite D250,
Austin, TX 78746
Phone: (512) 609-1900

All other means of Investor Communication:

Website: <https://www.falconstor.com/investors/>
X (Twitter): <https://x.com/FalconStor/status/1547135867600474112>
LinkedIn: <https://www.linkedin.com/company/falconstor-software/>
Facebook: <https://www.facebook.com/falconstorsoftwareinc/>

Other Service Providers:

Firm: Bridgepoint Consulting
Nature of Services: Financial Reporting
Address: 8310 N. Capital of Texas Highway, Bldg. 1, Ste. 420
Austin, Texas 78731
Phone: 512-437-7900

Firm: Pope, Shamsie & Dooley LLP
Nature of Services: Tax Services
Address: 5332 Thunder Creek Road
Austin, Texas 78759
Phone: 512-836-5855

9) Disclosure & Financial Information

A. This Disclosure Statement was prepared by:

Name: Vincent Sita
Title: CFO
Relationship to Issuer: Employee and Officer

B. The following financial statements were prepared in accordance with:

- ☐ IFRS
☒ U.S. GAAP

C. The following financial statements were prepared by:

Name: Vincent Sita
Title: CFO
Relationship to Issuer: Employee and Officer
Qualifications of the person who prepared the financial statements: CFO, Professional Accountant, 25+ years experience in financial management.

The following consolidated financial statements are attached for the three months ended March 31, 2025 and are hereby incorporated by reference:

- a. Consolidated Balance Sheets at March 31, 2025, and December 31, 2024 (unaudited)
- b. Consolidated Statements of Operations for the three months ended March 31, 2025, and 2024 (unaudited)
- c. Consolidated Statements of Cash Flows for the three months ended March 31, 2025, and 2024 (unaudited)
- d. Consolidated Statements of Comprehensive Income (Loss) for the three months ended March 31, 2025, and 2024 (unaudited)
- e. Consolidated Statements of Stockholders' Deficit for the three months ended March 31, 2025, and 2024 (unaudited)
- f. Notes to the Consolidated Financial Statements

10) Issuer Certification

I, Todd Brooks, certify that:

1. I have reviewed this Quarterly Disclosure Statement for FalconStor Software, Inc.;
2. Based on my knowledge, this disclosure statement 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 disclosure statement; and
3. Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this disclosure statement, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this disclosure statement.

/s/ Todd Brooks

Todd Brooks
Chief Executive Officer

May 7, 2025

Date

Principal Financial Officer:

I, Vincent Sita, certify that:

1. I have reviewed this Quarterly Disclosure Statement for FalconStor Software, Inc.;
2. Based on my knowledge, this disclosure statement 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 disclosure statement; and
3. Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this disclosure statement, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this disclosure statement.

/s/ Vincent Sita

Vincent Sita
Chief Financial Officer

May 7, 2025

Date

FALCONSTOR SOFTWARE, INC. AND SUBSIDIARIES
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FALCONSTOR SOFTWARE, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(UNAUDITED)

	<u>March 31, 2025</u>	<u>December 31, 2024</u>
Assets		
Current assets:		
Cash and cash equivalents	\$ 3,323,078	\$ 2,487,773
Accounts receivable, net	1,794,414	3,415,510
Prepaid expenses and other current assets	964,457	800,269
Contract assets, net	486,168	435,051
Total current assets	<u>6,568,117</u>	<u>7,138,603</u>
Property and equipment, net	105,586	48,436
Operating lease right-of-use assets, net	16,411	33,180
Deferred tax assets	40	—
Software development costs, net	—	3,611
Other assets	15,005	15,145
Goodwill	4,150,339	4,150,339
Other intangible assets, net	68	320
Long-term contract assets, net	314,069	369,686
Total assets	<u>\$ 11,169,635</u>	<u>\$ 11,759,320</u>
Liabilities and Stockholders' Deficit		
Current liabilities:		
Accounts payable	\$ 624,160	\$ 585,060
Accrued expenses	1,264,497	1,577,687
Current portion of lease liabilities	16,411	33,180
Deferred revenue	3,196,487	3,391,269
Total current liabilities	<u>5,101,555</u>	<u>5,587,196</u>
Other long-term liabilities	1,003,760	966,817
Notes payable, net of debt issuance costs and discounts	2,175,192	2,174,924
Deferred tax liabilities	480,612	480,796
Deferred revenue, net of current portion	1,375,759	1,582,450
Total liabilities	<u>\$ 10,136,878</u>	<u>\$ 10,792,183</u>
Commitments and contingencies (Note 10):		
Series A redeemable convertible preferred stock, \$.001 par value, 2,000,000 shares authorized, 900,000 shares issued and outstanding, redemption value of \$19,891,818 and \$19,402,697, respectively	19,883,708	19,393,205
Stockholders' deficit:		
Common stock, \$.001 par value, 30,000,000 shares authorized, 7,145,393 shares and 7,143,978 shares issued and outstanding, respectively	7,145	7,144
Additional paid-in capital	106,910,367	107,399,398
Accumulated deficit	(123,755,961)	(123,834,888)
Accumulated other comprehensive loss	(2,012,502)	(1,997,722)
Total stockholders' deficit	<u>\$ (18,850,951)</u>	<u>\$ (18,426,068)</u>
Total liabilities and stockholders' deficit	<u>\$ 11,169,635</u>	<u>\$ 11,759,320</u>

See accompanying notes to unaudited consolidated financial statements.

FALCONSTOR SOFTWARE, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

	Three Months Ended March 31,	
	2025	2024
Revenue:		
Product revenue	\$ 1,302,732	\$ 797,357
Support and services revenue	1,177,539	1,498,855
Total revenue	<u>2,480,271</u>	<u>2,296,212</u>
Cost of revenue:		
Product	9,174	19,183
Support and service	358,803	400,090
Total cost of revenue	<u>367,977</u>	<u>419,273</u>
Gross profit	\$ 2,112,294	\$ 1,876,939
Operating expenses:		
Research and development costs	653,076	570,537
Selling and marketing	826,660	725,056
General and administrative	605,006	572,882
Total operating expenses	<u>2,084,742</u>	<u>1,868,475</u>
Operating income	27,552	8,464
Interest and other income (expense)	63,835	(145,763)
Income (loss) before income taxes	91,387	(137,299)
Income tax expense (benefit)	12,460	(16,247)
Net income (loss)	<u>\$ 78,927</u>	<u>\$ (121,052)</u>
Less: Accrual of Series A redeemable convertible preferred stock dividends	489,121	442,758
Less: Accretion to redemption value of Series A redeemable convertible preferred stock	1,382	2,918
Net loss attributable to common stockholders	<u>\$ (411,576)</u>	<u>\$ (566,728)</u>
Basic net income (loss) per share attributable to common stockholders	<u>\$ (0.06)</u>	<u>\$ (0.08)</u>
Diluted net income (loss) per share attributable to common stockholders	<u>\$ (0.06)</u>	<u>\$ (0.08)</u>
Weighted average basic shares outstanding	<u>7,144,733</u>	<u>7,133,758</u>
Weighted average diluted shares outstanding	<u>7,144,733</u>	<u>7,133,758</u>

See accompanying notes to unaudited consolidated financial statements.

FALCONSTOR SOFTWARE, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(UNAUDITED)

	Three Months Ended March 31,	
	2025	2024
Net income (loss)	\$ 78,927	\$ (121,052)
Other comprehensive income (loss), net of applicable taxes		
Foreign currency translation	(14,781)	60,623
Total other comprehensive income (loss), net of applicable taxes:	(14,781)	60,623
Total comprehensive income (loss)	\$ 64,146	\$ (60,429)
Less: Accrual of Series A redeemable convertible preferred stock dividends	489,121	442,758
Less: Accretion to redemption value of Series A redeemable convertible preferred stock	1,382	2,918
Total comprehensive income (loss) attributable to common stockholders	\$ (426,357)	\$ (506,105)

See accompanying notes to unaudited consolidated financial statements.

FALCONSTOR SOFTWARE, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' DEFICIT
(UNAUDITED)

	Common Stock Outstanding	Common Stock	Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss, Net	Total Stockholders' Deficit
Balance at January 1, 2025	7,143,978	\$ 7,144	\$ 107,399,398	\$ (123,834,888)	\$ (1,997,722)	\$ (18,426,068)
Net income (loss)				78,927		78,927
Share-based compensation to employees			1,473			1,473
Shares issued in connection with vesting of restricted stock	1,415	1	(1)			—
Accretion of Series A redeemable convertible preferred stock			(1,382)			(1,382)
Dividends on Series A redeemable convertible preferred stock			(489,121)			(489,121)
Foreign currency translation					(14,780)	(14,780)
Balance at March 31, 2025	7,145,393	7,145	106,910,367	(123,755,961)	(2,012,502)	(18,850,951)

See accompanying notes to unaudited consolidated financial statements.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' DEFICIT
(UNAUDITED)

	Common Stock Outstanding	Common Stock	Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss, Net	Total Stockholders' Deficit
Balance at January 1, 2024	7,133,089	\$ 7,133	\$ 109,240,183	\$ (124,528,795)	\$ (1,689,874)	\$ (16,971,353)
Net income (loss)				(121,052)		(121,052)
Share-based compensation to employees			2,361			2,361
Shares issued in connection with vesting of restricted stock	1,415	1	(1)			—
Accretion of Series A redeemable convertible preferred stock			(2,918)			(2,918)
Dividends on Series A redeemable convertible preferred stock			(442,758)			(442,758)
Foreign currency translation					60,623	60,623
Balance at March 31, 2024	7,134,504	7,134	108,796,867	(124,649,847)	(1,629,251)	(17,475,097)

See accompanying notes to unaudited consolidated financial statements.

FALCONSTOR SOFTWARE, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

	Three Months Ended March 31,	
	2025	2024
Cash flows from operating activities:		
Net income (loss)	\$ 78,927	\$ (121,052)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	8,047	17,830
Amortization of debt discount on notes payable	268	1,081
Amortization of right of use assets	16,769	20,541
Share-based payment compensation	1,473	2,361
Provision for credit losses	(48,386)	47,720
Deferred income taxes	(21)	(53,066)
Changes in operating assets and liabilities:		
Accounts receivable	1,667,526	871,600
Prepaid expenses and other current assets	(144,495)	16,486
Contract assets	4,500	29,821
Other assets	3,093	(12,720)
Accounts payable	(31,947)	40,286
Accrued expenses and other long-term liabilities	(298,614)	(647,601)
Operating lease liabilities	(16,769)	(20,540)
Deferred revenue	(404,877)	(666,500)
Net cash provided by (used in) operating activities	835,494	(473,753)
Cash flows from investing activities:		
Purchases of property and equipment	(62,323)	—
Net cash provided by (used in) investing activities	(62,323)	—
Cash flows from financing activities:		
Payments of short-term debt	—	(39,239)
Net cash provided by (used in) financing activities	—	(39,239)
Effect of exchange rate changes on cash and cash equivalents	62,134	(18,505)
Net increase (decrease) in cash and cash equivalents	835,305	(531,497)
Cash and cash equivalents, beginning of period	2,487,773	3,409,120
Cash and cash equivalents, end of period	\$ 3,323,078	\$ 2,877,623
Supplemental disclosures:		
Cash paid for interest	\$ 44,277	\$ 52,341
Non-cash investing and financing activities:		
Undistributed Series A redeemable convertible preferred stock dividends	\$ 489,121	\$ 442,758
Accretion of Series A redeemable convertible preferred stock	\$ 1,382	\$ 2,918

See accompanying notes to unaudited consolidated financial statements.

FALCONSTOR SOFTWARE, INC. AND SUBSIDIARIES
Notes to Unaudited Consolidated Financial Statements

(1) Summary of Significant Accounting Policies

The Company and Nature of Operations

FalconStor Software, Inc., a Delaware corporation ("we", the "Company" or "FalconStor"), is a trusted data protection software leader modernizing disaster recovery and backup operations for the hybrid cloud world. The Company enables enterprise customers and managed service providers to secure, migrate, and protect their data while reducing data storage and long-term retention costs by up to 95%. More than 1,000 organizations and managed service providers worldwide standardize on FalconStor as the foundation for their cloud first data protection future.

Liquidity

As of March 31, 2025, the Company had a working capital surplus of \$1.5 million, which is inclusive of current deferred revenue of \$3.2 million, and a stockholders' deficit of \$18.9 million. During the three months ended March 31, 2025, the Company had a net income of \$0.1 million and positive cash flow from operations of \$0.8 million. The Company's total cash balance at March 31, 2025 was \$3.3 million, an increase of \$0.8 million compared to \$2.5 million on December 31, 2024.

The Company's principal sources of liquidity at March 31, 2025 consisted of cash and future cash anticipated to be generated from operations. The Company generated net income and positive cash flows from operations during the three months ended March 31, 2025, and it reported positive working capital as of March 31, 2025.

As described further in Note (8) Notes Payable, the Company is currently party to an Amended and Restated Term Loan Credit Agreement, dated as of February 23, 2018, as amended December 27, 2019, by and between the Company and HCP-FVA, LLC ("HCP-FVA"), (the "Amended and Restated Loan Agreement"). Subsequent amendments extended the maturity of the Amended and Restated Loan Agreement through December 31, 2023. On February 10, 2023, the Company entered into a letter agreement with Hale Capital to extend the maturity date of the senior secured debt to June 30, 2024. On February 12, 2024, the Company entered into a letter agreement with Hale Capital to further extend the maturity date of the senior secured debt to June 30, 2025. On January 10, 2025, the Company entered into a letter agreement with Hale Capital to further extend the maturity date of the senior secured debt to June 30, 2026. See Note (8) Notes Payable for more information.

Also, as described further in Note (11) Series A Redeemable Convertible Preferred Stock, the effective date of the mandatory redemption right of the Company's Series A Redeemable Convertible Preferred Stock (the "Series A Preferred Stock") held by HCP-FVA and Hale Capital is June 30, 2026 pursuant to that certain Amendment No. 1 to the Amended and Restated Certificate of Designations, Preferences and Rights of Series A Convertible Preferred Stock of the Company, dated as of June 24, 2021 (as amended, the "Certificate of Designations") and subsequent letter agreements in which Hale Capital agreed not to exercise or permit the exercise of the mandatory redemption right of the Series A Preferred Stock on or prior to the mandatory redemption date unless the redemption is in accordance with Section 8(e)(z) of the Certificate of Designations or in accordance with a Breach Event (as defined in the Certificate of Designations). On February 10, 2023, the Company entered into a letter agreement with Hale Capital to extend the redemption date of the Series A Preferred Stock to June 30, 2024. On February 12, 2024, the Company entered into letter agreement with Hale Capital to further extend the redemption date of the Series A Preferred Stock to June 30, 2025. On January 10, 2025, the Company entered into another letter agreement with Hale Capital to further extend the redemption date of the Series A Preferred Stock to June 30, 2026. If such Series A Preferred Stock was redeemed on March 31, 2025, the Company would have been required to pay the holders of the Series A Preferred Stock \$19.9 million.

The Company believes its current cash balances together with anticipated cash flows from operating activities will be sufficient to meet its working capital requirements for at least one year from the date the consolidated financial statements were issued.

Actual or threatened public health pandemics or outbreaks may adversely impact on our business, operations and the markets and communities in which we, our partners and customers operate.

Actual or threatened public health pandemics or outbreaks may adversely impact our business, operations and the markets and communities in which we, our partners and customers operate. For example, the COVID-19 pandemic and actions taken to slow its spread had an adverse impact on our operations, including disruptions in our and our partners' supply chains, increased foreign exchange rate volatility, reduced in-person sales interactions, and other disruptions which affected our results and financial condition. We cannot predict if or when other similar disease outbreaks will emerge that cause similar disruptions. The extent to which future pandemics may impact our operations will depend on future developments, which are highly uncertain and cannot be predicted with confidence, such as the timing and duration of future pandemics, the transmissibility and severity of illness caused by future pandemics, the efforts by governments and businesses to contain the spread of future pandemics, business closures or business disruptions and the impact on the economy and capital markets. Similar disruptions or disease outbreaks could delay or reduce our ability to recognize revenues within a particular fiscal period and harm our results of operations.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America ("GAAP") 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. The Company's significant estimates include those related to revenue recognition, accounts receivable allowances, valuation of derivatives, valuation of goodwill and income taxes. Actual results could differ from those estimates.

The financial market volatility in many countries where the Company operates has impacted and may continue to impact the Company's business. Such conditions could have a material impact on the Company's significant accounting estimates discussed above.

Unaudited Interim Financial Information

The accompanying condensed consolidated financial statements have been prepared in accordance with GAAP for interim financial information and in accordance with the requirements of Quarterly Reporting of the OTC Markets. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. The interim financial information is unaudited, but reflects all normal adjustments and accruals which are, in the Company's opinion, considered necessary to provide a fair presentation for the interim periods presented. The consolidated financial statements included herein should be read in conjunction with the reported consolidated financial statements and the footnotes thereto included within the Company's latest OTC Markets Annual Reporting for the fiscal year ended December 31, 2024.

Revenue from Contracts with Customers and Associated Balances

Nature of Products and Services

Licenses for on-premises software provide the customer with a right to use the software as it exists when made available to the customer. Customers may purchase perpetual licenses or subscribe to licenses, which provide customers with the same functionality and differ mainly in the duration over which the customer benefits from the software. Revenue from distinct on-

premises licenses is recognized upfront at the point in time when the software is made available to the customer. Revenue allocated to software maintenance and support services is recognized ratably over the contractual support period.

Hardware products consist primarily of servers and associated components and function independently of the software products and as such are accounted for as separate performance obligations. Revenue allocated to hardware maintenance and support services is recognized ratably over the contractual support period. We have largely exited this business, other than supporting past customers who previously purchased hardware from us.

Professional services are primarily related to software implementation services and associated revenue is recognized upon customer acceptance.

Contract Balances

The timing of revenue recognition may differ from the timing of invoicing to customers. The Company records a contract asset when revenue is recognized prior to invoicing, or unearned revenue when revenue is recognized subsequent to invoicing. For perpetual licenses with multi-year maintenance agreements, the Company invoices the license and generally one year of maintenance with future maintenance generally invoiced annually. For multi-year subscription licenses, the Company generally invoices customers annually at the beginning of each annual coverage period. The Company records a contract asset related to revenue recognized for multi-year on-premises licenses as its right to payment is conditioned upon providing product support and services in future years.

As of March 31, 2025 and December 31, 2024, accounts receivable, net of allowance for doubtful accounts, was \$1.8 million and \$3.4 million, respectively. A provision for expected credit losses for accounts receivables and contract assets that share similar risk characteristics is recorded based on an evaluation of historical loss experience, current conditions, and reasonable and supportable forecasts. Accounts are written off when it becomes apparent that such amounts will not be collected, generally when amounts are past due by greater than nine months. Our provision for credit loss on accounts receivable was \$30,008 as of March 31, 2025 and \$78,622 as of December 31, 2024, respectively. As of March 31, 2025 and December 31, 2024, short and long-term contract assets, net of provision for credit loss, was \$0.8 million and \$0.8 million, respectively. Our provision for credit loss on contract assets was \$8,002 and \$8,047 as of March 31, 2025 and December 31, 2024, respectively.

Deferred revenue is comprised mainly of unearned revenue related to maintenance and technical support on term and perpetual licenses. Maintenance and technical support revenue is recognized ratably over the coverage period. Deferred revenue also includes contracts for professional services to be performed in the future which are recognized as revenue when the Company delivers the related service pursuant to the terms of the customer arrangement.

Changes in deferred revenue were as follows:

Balance at January 1, 2025	\$	4,973,719
Deferral of revenue		2,079,558
Recognition of revenue		(2,480,271)
Change in reserves		(760)
Balance at March 31, 2025	\$	<u>4,572,246</u>

During the three months ended March 31, 2025 and 2024, revenue of \$1.0 million and \$1.2 million respectively, was recognized from the deferred revenue balance at the beginning of each period.

Deferred revenue includes invoiced revenue allocated to remaining performance obligations that has not yet been recognized and will be recognized as revenue in future periods. Deferred revenue was \$4.6 million as of March 31, 2025, of which the Company expects to recognize approximately 70% of such amount as revenue over the next 12 months and the remainder thereafter.

Approximately \$1.8 million of revenue is expected to be recognized from remaining performance obligations for unbilled support and services as of March 31, 2025. We expect to recognize revenue on approximately 44% of these remaining performance obligations over the next twelve months, with the balance recognized thereafter.

Payment terms and conditions vary by contract type, although terms generally include a requirement of payment within 30 to 90 days. In instances where the timing of revenue recognition differs from the timing of invoicing, the Company has determined that its contracts generally do not include a significant financing component. The primary purpose of the Company's invoicing terms is to provide customers with simplified and predictable ways of purchasing its products and services, and not to receive financing from our customers or to provide customers with financing. Examples include invoicing at the beginning of a subscription term with maintenance and support revenue recognized ratably over the contract period, and multi-year, on-premises licenses that are invoiced annually with product revenue recognized upon delivery.

Significant Judgments

The Company's contracts with customers often include promises to transfer multiple products and services to a customer. Determining whether products and services are considered distinct performance obligations that should be accounted for separately versus together may require significant judgment.

Judgment is required to determine the standalone selling price ("SSP") for each distinct performance obligation. For products and services aside from maintenance and support, the Company estimates SSP by adjusting the list price by historical discount percentages. SSP for software and hardware maintenance and support fees is based on the stated percentages of the fees charged for the respective products.

The Company's perpetual and term software licenses have significant standalone functionality and therefore revenue allocated to these performance obligations are recognized at a point in time upon electronic delivery of the download link and the license keys.

Product maintenance and support services are satisfied over time as they are stand-ready obligations throughout the support period. As a result, revenues associated with maintenance services are deferred and recognized as revenue ratably over the term of the contract.

Revenues associated with professional services are recognized at a point in time upon customer acceptance.

Disaggregation of Revenue

Please refer to the condensed consolidated statements of operations and Note (15) *Segment Reporting and Concentrations* for discussion on revenue disaggregation by product type and by geography. The Company believes this level of disaggregation sufficiently depicts how the nature, amount, timing and uncertainty of our revenue and cash flows are affected by economic factors.

Assets Recognized from Costs to Obtain a Contract with a Customer

The Company recognizes an asset for the incremental costs of obtaining a contract with a customer if it expects the benefit of those costs to be longer than one year. The Company has determined that its sales commission program meets the requirements for cost capitalization. Total capitalized costs to obtain a contract were immaterial during the periods presented and are included in other current and long-term assets on our consolidated balance sheets. The Company applies a practical expedient to expense costs as incurred for costs to obtain a contract with a customer when the amortization period would have been one year or less.

Leases

We have entered into operating leases for our various facilities. We determine if an arrangement is a lease at inception. Operating leases are included in Right-of-Use ("ROU") assets, and lease liability obligations in our condensed consolidated balance sheets. ROU assets represent our right to use an underlying asset for the lease term and lease liability obligations represent

our obligation to make lease payments arising from the lease. ROU assets and liabilities are recognized at commencement date based on the present value of lease payments over the lease term. We have lease agreements with lease and non-lease components and account for such components as a single lease component. As most of our leases do not provide an implicit rate, we estimated our incremental borrowing rate based on the information available at commencement date in determining the present value of lease payments. We use the implicit rate when readily determinable. The ROU asset also includes any lease payments made and excludes lease incentives and lease direct costs. Our lease terms may include options to extend or terminate the lease. Such extended terms have been considered in determining the ROU assets and lease liability obligations when it is reasonably certain that we will exercise that option. Lease expense is recognized on a straight-line basis over the lease term.

Right of Use Assets and Liabilities

We have various operating leases for office facilities that are expected to continue through 2025. Below is a summary of our ROU assets and liabilities as of March 31, 2025.

Right of use assets	\$	16,411
Lease liability obligations, current		16,411
Lease liability obligations, less current portion		—
Total lease liability obligations	\$	16,411
Weighted-average remaining lease term		0.25
Weighted-average discount rate		3.25 %

	Three Months Ended March 31,	
	2025	2024
Components of lease expense:		
Operating lease cost	\$ 34,588	\$ 35,588

During the three months ended March 31, 2025 and 2024, operating cash flows from operating leases was \$16,935.

Approximate future minimum lease payments for our ROU assets over the remaining lease periods as of March 31, 2025, are as follows:

Lease payments 2025 (remaining)	\$	14,113
Less interest		(2,298)
Present value of lease liabilities	\$	16,411

Recently Issued Accounting Pronouncements

In December 2023, the FASB issued ASU 2023-09, “Income Taxes (Topic 740): Improvements to Income Tax Disclosures.” The amendments in this update are intended to enhance the transparency and decision usefulness of income tax disclosures primarily through changes to the rate reconciliation and income taxes paid information. This update is effective for annual periods beginning after December 15, 2024, with early adoption permitted. We are currently evaluating the ASU to determine its impact on our consolidated financial statements and related disclosures.

In November 2024, the FASB issued ASU 2024-03, Income Statement—Reporting Comprehensive Income—Expense Disaggregation Disclosures (Subtopic 220-40): Disaggregation of Income Statement Expenses, which requires disclosure about the types of costs and expenses included in certain expense captions presented on the income statement. The new disclosure requirements are effective for the Company’s annual periods beginning after December 15, 2026, and interim periods beginning after December 15, 2027, with early adoption permitted. The Company will evaluate the impact of this pronouncement on our related disclosures.

Recently Adopted Accounting Pronouncements

In August 2020, the Financial Accounting Standards Board, or FASB, issued ASU 2020-06, regarding ASC Topic 470 “Debt” and ASC Topic 815 “Derivatives and Hedging,” which reduces the number of accounting models for convertible instruments and amends the calculation of diluted earnings per share for convertible instruments, among other changes. The guidance is effective for smaller reporting companies as defined by the SEC, for annual reporting periods beginning after December 15, 2023, including interim periods within that reporting period. We adopted the standard on January 1, 2024 and there was no impact on our consolidated financial statements.

In November 2023, the FASB issued Accounting Standards Update (ASU) 2023-07, Segment Reporting (Topic 280): Improvements to Reportable Segment Disclosures. The new standard requires enhanced disclosures about significant segment expenses and other segment items and requires companies to provide all annual disclosures about segments in interim periods. All disclosure requirements under ASU 2023-07 are also required for public entities with a single reportable segment. The ASU is effective for the Company’s Annual Report for the fiscal year ending December 31, 2024, and subsequent interim periods. The Company adopted Topic 280 effective December 31, 2024.

(2) Earnings Per Share

Basic earnings per share ("EPS") is computed based on the weighted average number of shares of common stock outstanding. Diluted EPS is computed based on the weighted average number of common shares outstanding increased by dilutive common stock equivalents, attributable to stock option awards, restricted stock awards, warrants and the Series A Preferred Stock outstanding.

The following represents the common stock equivalents that were excluded from the computation of diluted shares outstanding because their effect would have been anti-dilutive for the three months ended March 31, 2025 and 2024:

	Three Months Ended March 31,	
	2025	2024
Stock options	2,825	2,825
Restricted stock	8,326	13,549
Series A redeemable convertible preferred stock	194,089	175,692
Total anti-dilutive common stock equivalents	205,240	192,066

(3) Property and Equipment

The gross carrying amount and accumulated depreciation of property and equipment as of March 31, 2025 and December 31, 2024 are as follows:

	March 31, 2025	December 31, 2024
Gross carrying amount	\$ 1,327,715	\$ 1,269,789
Accumulated depreciation	(1,222,129)	(1,221,353)
Property and Equipment, net	\$ 105,586	\$ 48,436

For the three months ended March 31, 2025 and 2024, depreciation expense was \$4,184 and \$11,308, respectively.

(4) Software Development Costs

The gross carrying amount and accumulated amortization of software development costs as of March 31, 2025 and December 31, 2024 are as follows:

	March 31, 2025	December 31, 2024
Gross carrying amount	\$ 3,015,132	\$ 3,015,132
Accumulated amortization	(3,015,132)	(3,011,521)
Software development costs, net	\$ —	\$ 3,611

During the three months ended March 31, 2025 and 2024, the Company recorded \$3,611 and \$5,417, respectively, of amortization expense related to capitalized software costs.

(5) Goodwill and Other Intangible Assets

The gross carrying amount and accumulated amortization of goodwill and other intangible assets as of March 31, 2025 and December 31, 2024 are as follows:

	March 31, 2025	December 31, 2024
Goodwill	\$ 4,150,339	\$ 4,150,339
Other intangible assets:		
Gross carrying amount	\$ 4,041,216	\$ 4,041,216
Accumulated amortization	(4,041,148)	(4,040,896)
Net carrying amount	\$ 68	\$ 320

For the three months ended March 31, 2025 and 2024, amortization expense was \$252 and \$1,105, respectively.

(6) Share-Based Payment Arrangements

On June 22, 2018, the Company's stockholders adopted the FalconStor Software, Inc. 2018 Incentive Stock Plan (the "2018 Plan"). The 2018 Plan is administered by the Compensation Committee (the "Compensation Committee") of the Company's Board of Directors (the "Board") and initially provided for the issuance of up to 1,471,997 shares of the Company's common stock upon the grant of shares with such restrictions as determined by the Compensation Committee to the employees and directors of, and consultants providing services to, the Company or its affiliates. In June 2021, the Company's stockholders approved an amendment to increase the number of shares of our common stock authorized and reserved for issuance under the 2018 Plan by 220,800 shares to a total of 1,692,797 shares. Exercise prices of the options are determined by the Compensation Committee, subject to the consent of Hale Capital. The vesting terms are performance based and determined by the Compensation Committee, subject to the consent of Hale Capital, based on various factors, including (i) the return of capital to the holders of the Series A Preferred Stock and the Company's common stock in the event of a change of control, (ii) the repayment of the Company's obligations under its senior secured debt, and (iii) the Company's free cash flow.

The following table summarizes the 2018 Plan, which was the only plan under which the Company was able to grant equity compensation as of March 31, 2025:

Name of Plan	Shares Authorized	Shares Available for Grant	Shares Outstanding
FalconStor Software, Inc. 2018 Incentive Stock Plan	1,692,797	239,069	1,292,489

The following table summarizes the Company's equity plans that have terminated or expired but that still have equity awards outstanding as of March 31, 2025:

Name of Plan	Shares Available for Grant	Shares Outstanding
FalconStor Software, Inc., 2016 Incentive Stock Plan	—	2,000
FalconStor Software, Inc., 2006 Incentive Stock Plan	—	825

A summary of the Company's restricted stock activity for the three months ended March 31, 2025 is below. Such restricted stock did not bestow any voting or dispositive power and is not deemed outstanding until they vest.

	Number of Restricted Stock Awards
Non-Vested at January 1, 2025	1,293,904
Granted	—
Vested	(1,415)
Forfeited	—
Non-Vested at March 31, 2025	1,292,489

The following table summarizes the share-based compensation expense for all awards issued under the Company's stock equity plans in the following line items in the condensed consolidated statements of operations for the three months ended March 31, 2025 and 2024:

	Three Months Ended March 31,	
	2025	2024
Cost of revenue - support and service	909	80
Research and development costs	225	531
Selling and marketing	199	549
General and administrative	140	1,201
	<u>\$ 1,473</u>	<u>\$ 2,361</u>

(7) Income Taxes

The Company's provision for income taxes consists principally of state and local, and foreign taxes, as applicable, in amounts necessary to align the Company's year-to-date tax provision with the effective rate that it expects to achieve for the full year.

For the three months ended March 31, 2025, the Company recorded an income tax provision expense of \$12,860. The effective tax rate for the three months ended March 31, 2025 was 11.2%. The effective tax rate differs from the statutory rate of 21% due to the mix of foreign and domestic earnings, foreign withholding taxes and the application of valuation allowances. As of March 31, 2025, the Company's conclusion did not change with respect to the realizability of its domestic deferred tax assets and therefore, the Company has not recorded any income tax benefit as such amounts are fully offset with a valuation allowance.

For the three months ended March 31, 2024, the Company recorded an income tax provision benefit of \$16,247. The effective tax rate for the three months ended March 31, 2024 was 11.8%. The effective tax rate differs from the statutory rate of 21% due to the mix of foreign and domestic earnings and the application of valuation allowances. As of March 31, 2024, the Company's conclusion did not change with respect to the realizability of its domestic deferred tax assets and therefore, the Company has not recorded any income tax benefit as such amounts are fully offset with a valuation allowance.

The Company's total unrecognized tax benefits, excluding interest, March 31, 2025 and March 31, 2024 were none and \$51,552, respectively. As of March 31, 2025 and March 31, 2024, the Company had none and \$44,959, respectively, of accrued

interest reflected in accrued expenses. The Company expects all of its remaining unrecognized tax benefits to be released during the next twelve months due to expiring statute of limitations, which will impact the Company's effective tax rate.

(8) Notes Payable

The long-term note payable balance consists of the following:

Long-term note payable, net at January 1, 2025	\$	2,174,924
Accretion of discount		268
Long-term note payable, net at March 31, 2025	\$	<u>2,175,192</u>

Senior Secured Debt

The Company is currently a party to the Amended and Restated Loan Agreement. The senior secured debt bears interest at prime plus 0.75%. Subsequent amendments extended the maturity of the Amended and Restated Loan Agreement through December 31, 2023. On February 10, 2023, the Company entered into a letter agreement with Hale Capital to extend the maturity date of the senior secured debt to June 30, 2024. On February 12, 2024, the Company entered into a letter agreement with Hale Capital to further extend the maturity date of the senior secured debt to June 30, 2025. On January 10, 2025, the Company entered into a letter agreement with Hale Capital to further extend the maturity date of the senior secured debt to June 30, 2026. The Company concluded the extensions under the January 2025 Loan Extension Letter Agreement resulted in a debt modification under ASC 470-50, Modifications and Extinguishments, and therefore no gain or loss was required to be recognized. The changes were accounted for prospectively using the new effective interest rate of the loan.

In the event the term notes issued pursuant to the Amended and Restated Loan Agreement (the "Term Loan") are prepaid for any reason, such prepayment will be subject to the payment of a premium in an amount equal to 5% of the principal amount prepaid. The Term Loan is required to be prepaid upon the occurrence of certain events, including but not limited to certain asset dispositions, the incurrence of additional indebtedness, the receipt of insurance proceeds, and a change of control, subject to certain exceptions.

The Amended and Restated Loan Agreement has customary representations, warranties and affirmative and negative covenants. The negative covenants include financial covenants relating to in-force annual contract value. The Amended and Restated Loan Agreement also contains customary events of default, including but not limited to payment defaults, cross defaults with certain other indebtedness, breaches of covenants, bankruptcy events and a change of control. In the case of an event of default, as administrative agent under the Amended and Restated Loan Agreement, HCP-FVA, an affiliate of Hale Capital may (and upon the written request of lenders holding in excess of 50% of the term loans, which must include HCP-FVA, is required to) accelerate payment of all obligations under the Amended and Restated Loan Agreement, and seek other available remedies.

As of March 31, 2025, the Company was in compliance with the financial covenants contained in the Amended and Restated Loan Agreement.

(9) Fair Value Measurements

The Company measures its cash equivalents and derivative instruments at fair value. Fair value is an exit price, representing the amount that would be received on the sale of an asset or that would be paid to transfer a liability in an orderly transaction between market participants. As a basis for considering such assumptions, the Company utilizes a three-tier fair value hierarchy, which prioritizes the inputs used in the valuation methodologies in measuring fair value.

Fair Value Hierarchy

The methodology for measuring fair value specifies a hierarchy of valuation techniques based upon whether the inputs to those valuation techniques reflect assumptions other market participants would use based upon market data obtained from independent sources (observable inputs) or reflect the Company's own assumptions of market participant valuation (unobservable inputs). As a result, observable and unobservable inputs have created the following fair value hierarchy:

- *Level 1* – Quoted prices in active markets that are unadjusted and accessible at the measurement date for identical, unrestricted assets or liabilities. The Company had no Level 1 securities at March 31, 2025 and December 31, 2024.
- *Level 2* – Quoted prices for identical assets and liabilities in markets that are not active, quoted prices for similar assets and liabilities in active markets or financial instruments for which significant inputs are observable, either directly or indirectly. At March 31, 2025 and December 31, 2024, the Company did not have any Level 2 category assets included in the condensed consolidated balance sheets.
- *Level 3* – Prices or valuations that require inputs that are both significant to the fair value measurement and unobservable. At March 31, 2025 and December 31, 2024, the Level 3 category included derivatives. The Company did not hold any cash and cash equivalents categorized as Level 3 as of March 31, 2025 or December 31, 2024.

The following table presents the Company's assets and liabilities that are measured at fair value on a recurring basis at March 31, 2025:

		Fair Value Measurements at Reporting Date Using		
		Quoted Prices		
		in		
		Active		
		Markets for		
		Identical		
		Assets		
		(Level 1)		
	Total	Significant	other Inputs	Significant
		(Level 2)	Inputs	Unobservable
				Inputs
				(Level 3)
Derivative liabilities:				
Derivative Instruments	\$ 988,383	\$ —	\$ —	\$ 988,383
Total derivative liabilities	988,383	—	—	988,383
Total assets and liabilities measured at fair value	\$ 988,383	\$ —	\$ —	\$ 988,383

The following table presents the Company's assets and liabilities that are measured at fair value on a recurring basis at December 31, 2024:

		Fair Value Measurements at Reporting Date Using		
		Quoted Prices		
		in		
		Active		
		Markets for		
		Identical		
		Assets		
		(Level 1)		
	Total	Significant	other Inputs	Significant
		(Level 2)	Inputs	Unobservable
				Inputs
				(Level 3)
Derivative liabilities:				
Derivative Instruments	\$ 948,710	\$ —	\$ —	\$ 948,710
Total derivative liabilities	948,710	—	—	948,710
Total assets and liabilities measured at fair value	\$ 948,710	\$ —	\$ —	\$ 948,710

Measurement of Fair Value

The fair value of the Company's derivatives were valued using the Black-Scholes pricing model adjusted for probability assumptions, with all significant inputs, except for the probability and volatility assumptions, derived from or corroborated by observable market data such as stock price and interest rates. The probability and volatility assumptions are both significant to the fair value measurement and unobservable. These embedded derivatives are included in Level 3 of the fair value hierarchy. The derivatives are included in other long-term liabilities on our consolidated balance sheets.

The Company's Series A Preferred Stock and notes payable are measured at amortized cost using an effective interest rate of 10.0% and 8.3% yield, respectively.

The following table presents a reconciliation of the beginning and ending balances of the Company's liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the three months ended March 31, 2025 and 2024:

	Three Months Ended March 31,	
	2025	2024
Beginning Balance	\$ 948,710	\$ 846,041
Total loss recognized in earnings	39,673	30,910
Ending Balance	<u>\$ 988,383</u>	<u>\$ 876,951</u>

The Company's derivatives were valued using the Black-Scholes pricing model adjusted for probability assumptions, with all significant inputs, except for the probability and volatility assumptions, derived from or corroborated by observable market data such as stock price and interest rates. The probability and volatility assumptions are as follows:

Probability of redemption as part of a fundamental sale transaction	0.5 %
Probability of redemption absent a fundamental sale transaction	4.75 %
Annual volatility	65 %

(10) Commitments and Contingencies

The Company typically provides its customers a warranty on its software products for a period of no more than 90 days. Such warranties are accounted for in accordance with the authoritative guidance issued by the FASB on contingencies. For the three months ended March 31, 2025, the Company has not incurred any costs related to warranty obligations.

Under the terms of substantially all of its software license agreements, the Company indemnifies its customers for all costs and damages arising from claims against such customers based on, among other things, allegations that the Company's software infringes on the intellectual property rights of a third party. In most cases, in the event of an infringement claim, the Company retains the right to (i) procure for the customer the right to continue using the software; (ii) replace or modify the software to eliminate the infringement while providing substantially equivalent functionality; or (iii) if neither (i) nor (ii) can be reasonably achieved, the Company may terminate the license agreement and refund to the customer a pro-rata portion of the license fee paid to the Company. Such indemnification provisions are accounted for in accordance with the authoritative guidance issued by the FASB on guarantees. From time to time, in the ordinary course of business, the Company receives claims for indemnification, typically from original equipment manufacturers. The Company is not currently aware of any material claims for indemnification.

As described under Note (11) *Series A Redeemable Convertible Preferred Stock* the holders of the Series A Preferred Stock have redemption rights upon certain triggering events. As of March 31, 2025, the Company did not fail any non-financial covenants related to the Company's Series A Preferred Stock.

In connection with the appointment of Todd Brooks as Chief Executive Officer, the Board approved an offer letter to Mr. Brooks (the "Brooks Agreement"), which was executed on August 14, 2017. The Brooks Agreement provides that Mr. Brooks is entitled to receive an annualized base salary of \$350,000, payable in regular installments in accordance with the Company's general payroll practices. Mr. Brooks will also be eligible for a cash bonus of \$17,500 for any quarter that is free cash flow

positive on an operating basis and additional incentive compensation of an annual bonus of up to \$200,000, subject to attainment of performance objectives to be mutually agreed upon and established. Mr. Brooks' employment can be terminated at will. Pursuant to the Brooks Agreement and the 2018 Plan, Mr. Brooks received 735,973 shares of restricted stock. If Mr. Brooks' employment is terminated by the Company other than for cause, he is entitled to receive severance equal to 12 months of his base salary if (i) he has been employed by the Company for at least 12 months at the time of termination or (ii) a change of control has occurred within six months of Mr. Brooks' employment. Except as set forth in the preceding sentence, Mr. Brooks is entitled to receive severance equal to six months of his base salary if he has been employed by the Company for less than six months and his employment was terminated by the Company without cause. Mr. Brooks is also entitled to vacation and other employee benefits in accordance with the Company's policies as well as reimbursement for an apartment.

In connection with Mr. Sita's appointment as Chief Financial Officer, the Board approved an Independent Contractor Services Agreement with Alucra Consulting, Inc. ("Alucra"), an entity owned by Mr. Sita (the "Sita Agreement"), which was executed on February 11, 2022, and amended on November 26, 2024. The Sita Agreement provides that Alucra is entitled to receive a fee of \$22,500 per month. Alucra will also be eligible for an additional payment of up to \$120,000 annually, based upon the achievement of goals determined by the Company, to be paid quarterly in accordance with standard Company policies. The agreement also provided that Mr. Sita received a grant of shares of the Company's common stock, to be governed by the Company's 2018 Stock Incentive Plan and subject to specific vesting conditions.

The Sita Agreement initially expired on July 1, 2023 and automatically renews for additional one year terms pursuant to the terms set forth therein.

(11) Series A Redeemable Convertible Preferred Stock

The Company has 900,000 shares of Series A Preferred Stock outstanding with a par value \$0.001 per share and a stated value of \$10 per share. Pursuant to the Certificate of Designations, each share of Series A Preferred Stock can be converted into shares of the Company's common stock, at an initial conversion price of \$102.488 per share, subject to appropriate adjustments for any stock dividend, stock split, stock combination, reclassification or similar transaction, (i) at any time at the option of the holder or (ii) by the Company if, following the first anniversary of the issuance of the Series A Preferred Stock (subject to extension under certain circumstances), the volume weighted average trading price per share of the Company's common stock for sixty (60) consecutive trading days exceeds 250% of the conversion price and continues to exceed 225% of the conversion price through the conversion date, subject at all times to the satisfaction of, and the limitations imposed by, the equity conditions set forth in the Certificate of Designations (including, without limitation, the volume limitations set forth therein).

Pursuant to the Certificate of Designations, the holders of the Series A Preferred Stock are entitled to receive quarterly dividends at the prime rate (provided in the Wall Street Journal Eastern Edition) plus 5% (up to a maximum dividend rate of 10%), payable in cash or in kind (i.e., through the issuance of additional shares of Series A Preferred Stock), except that the Company is not permitted to pay such dividends in cash while any indebtedness under the Amended and Restated Loan Agreement remains outstanding without the consent of the holders of the Series A Preferred Stock. In addition, the declaration and payment of dividends is subject to compliance with applicable law and unpaid dividends will accrue. A holder's right to convert its shares of Series A Preferred Stock and receive dividends in the form of common stock is subject to certain limitations including, among other things, that the shares of common stock issuable upon conversion or as dividends will not, prior to receipt of stockholder approval, result in any holder beneficially owning greater than 9.99% of the Company's currently outstanding shares of common stock.

The Series A Preferred Stock dividends shall accrue whether or not the declaration or payment of such Series A Preferred Stock dividends are prohibited by applicable law, whether or not the Company has earnings, whether or not there are funds legally available for the payment of such dividends and whether or not such dividends are authorized or declared.

Upon certain triggering events, such as bankruptcy, insolvency or a material adverse effect or failure of the Company to issue shares of common stock upon conversion of the Series A Preferred Stock in accordance with its obligations, the holders may

require the Company to redeem all or some of the Series A Preferred Stock at a price per share equal to the greater of (i) the sum of 100% of the stated value of a share of Series A Preferred Stock plus accrued and unpaid dividends with respect thereto, and (ii) the product of the number of shares of common stock underlying a share of Series A Preferred Stock (and accrued and unpaid dividends with respect thereto) and the closing price as of the occurrence of the triggering event. On or after June 30, 2025, subject to the approval of HCP-FVA, each holder of Series A Preferred Stock can also require the Company to redeem its Series A Preferred Stock in cash at a per share price equal to 100% of the stated value of a share of Series A Preferred Stock plus accrued and unpaid dividends with respect thereto. Notwithstanding the forgoing, no holder of Series A Preferred Stock is permitted to exercise any rights or remedies upon a Breach Event (as defined in the Certificate of Designations) or to exercise any redemption rights under the Certificate of Designations, unless approved by the holders of a majority of the then-outstanding shares of Series A Preferred Stock.

Upon consummation of a fundamental sale transaction, the Series A Preferred Stock will be redeemed at a per share redemption price equal to the greater of (y) 250% of the stated value of Series A Preferred Stock and (z) the price payable in respect of such share of Series A Preferred Stock if such share of Series A Preferred Stock had been converted into such number of shares of common stock in accordance with the Certificate of Designations (but without giving effect to any limitations or restrictions contained therein) immediately prior to such fundamental sale transaction; provided however that the 250% threshold is changed to 100% if the fundamental sale transaction is approved by the two Series A Directors (as defined in the Certificate of Designations). In addition, if the Company consummates an equity or debt financing that results in more than \$5.0 million of net proceeds to the Company and/or its subsidiaries, the holders of Series A Preferred Stock will have the right, but not the obligation, to require the Company to use the net proceeds in excess of \$5.0 million to repurchase all or a portion of the Series A Preferred Stock at a per share price equal to the greater of (i) the sum of 100% of the stated value of such share of Series A Preferred Stock plus accrued and unpaid dividends with respect thereto, and (ii) the number of shares of common stock into which such share of Series A Preferred Stock is then convertible multiplied by the greater of (y) the closing price of the common stock on the date of announcement of such financing or (z) the closing price of the common stock on the date of consummation of such financing.

Each holder of Series A Preferred Stock has a vote equal to the number of shares of common stock into which its Series A Preferred Stock would be convertible as of the record date. In addition, the holders of a majority of the Series A Preferred Stock must approve certain actions, including approving any amendments to the Company's Restated Certificate of Incorporation as amended or Amended and Restated Bylaws that adversely affects the voting powers, preferences or other rights of the Series A Preferred Stock; payment of dividends or distributions; any liquidation, capitalization, reorganization or any other fundamental transaction of the Company; issuance of any equity security senior to or on parity with the Series A Preferred Stock as to dividend rights, redemption rights, liquidation preference and other rights; issuances of equity below the conversion price; any liens or borrowings other than non-convertible indebtedness from standard commercial lenders which does not exceed 80% of the Company's accounts receivable; and the redemption or purchase of any of the capital stock of the Company.

The holders of our outstanding Series A Preferred Stock have a mandatory redemption right that may be exercised only with the approval of HCP-FVA and Hale Capital. The effective date of such redemption right is June 30, 2025 pursuant to an amendment to the Certificate of Designations, dated as of June 24, 2021 and subsequent letter agreements in which Hale Capital agreed not to exercise or to permit the exercise of the mandatory redemption right of the Series A Preferred Stock on or prior to the mandatory redemption date unless the redemption is in accordance with Section 8(e)(z) of the Certificate of Designations or in accordance with a Breach Event (as defined in the Certificate of Designations). On February 10, 2023, the Company entered into a letter agreement with Hale Capital to extend the redemption date of the Series A Preferred Stock to June 30, 2024. On February 12, 2024, the Company entered into a letter agreement with Hale Capital to further extend the redemption date of the Series A Preferred Stock to June 30, 2025. On January 10, 2025, the Company entered into a letter agreement with Hale Capital to further extend the redemption date of the Series A Preferred Stock to June 30, 2026. The Company concluded the extensions resulted in a debt modification under ASC 470-50, Modifications and Extinguishments, and therefore no gain or loss was required to be recognized. The changes were accounted for prospectively using the new effective interest rate of the preferred stock.

The Company has classified the Series A Preferred Stock as temporary equity in the financial statements as it is subject to redemption at the option of the holder under certain circumstances. As a result of the Company's analysis of all the embedded conversion and put features within the Series A Preferred Stock, the contingent redemption put options in the Series A Preferred

Stock were determined to not be clearly and closely related to the debt-type host and also did not meet any other scope exceptions for derivative accounting. Therefore, the contingent redemption put options are being accounted for as derivative instruments and the fair value of these derivative instruments was bifurcated from the Series A Preferred Stock and recorded as a liability.

As of March 31, 2025 and December 31, 2024, the fair value of these derivative instruments were included in other long-term liabilities within the consolidated balance sheets. The loss on the change in fair value of these derivative instruments for the three months ended March 31, 2025 and 2024 was included in interest and other expense within the consolidated statement of operations.

At the time of issuance, the Company recorded transaction costs, a beneficial conversion feature and the fair value allocated to the embedded derivatives as discounts to the Series A Preferred Stock. These costs were being accreted to the Series A Preferred Stock using the effective interest method through the stated redemption date of August 5, 2017, which represents the earliest redemption date of the instrument. This accretion was accelerated as of December 31, 2016 due to the failure of the financial covenants and the redemption right of the holders at that time. In connection with the public offering of the Company as described in the Company's Registration Statement on Form S-1, as amended, originally filed on June 3, 2021, Hale Capital Partners, which was the sole holder of the Series A Preferred Stock, agreed to the extension of the mandatory redemption right and waived prior breaches of the terms of the Series A Preferred Stock. The Company included deductions for accretion, deemed and accrued dividends on the Series A Preferred Stock as adjustments to net loss attributable to common stockholders on the statement of operations and in determining loss per share for the three months ended March 31, 2025 and 2024, respectively.

The Series A Preferred Stock consists of the following:

Total Series A redeemable convertible preferred stock, net at January 1, 2025	\$	19,393,205
Accrued dividends		489,121
Accretion of preferred stock		1,382
Total Series A redeemable convertible preferred stock, net at March 31, 2025	\$	<u>19,883,708</u>

(12) Accumulated Other Comprehensive Loss

The changes in Accumulated Other Comprehensive Loss, net of tax, for the three months ended March 31, 2025 are as follows:

	Foreign Currency Translation	Net Minimum Pension Liability	Total
Accumulated other comprehensive income (loss) at January 1, 2025	<u>\$ (1,977,666)</u>	<u>\$ (20,056)</u>	<u>\$ (1,997,722)</u>
Other comprehensive income (loss)			
Other comprehensive income (loss) before reclassifications	<u>(14,780)</u>	<u>—</u>	<u>(14,780)</u>
Total other comprehensive income (loss)	<u>(14,780)</u>	<u>—</u>	<u>(14,780)</u>
Accumulated other comprehensive income (loss) at March 31, 2025	<u>\$ (1,992,446)</u>	<u>\$ (20,056)</u>	<u>\$ (2,012,502)</u>

The changes in Accumulated Other Comprehensive Loss, net of tax, for the three months ended March 31, 2024 are as follows:

	Foreign Currency Translation	Net Minimum Pension Liability	Total
Accumulated other comprehensive income (loss) at January 1, 2024	<u>\$ (1,680,258)</u>	<u>\$ (9,616)</u>	<u>\$ (1,689,874)</u>
Other comprehensive income (loss)			
Other comprehensive income (loss) before reclassifications	<u>60,623</u>	<u>—</u>	<u>60,623</u>
Total other comprehensive income (loss)	<u>60,623</u>	<u>—</u>	<u>60,623</u>
Accumulated other comprehensive income (loss) at March 31, 2024	<u>\$ (1,619,635)</u>	<u>\$ (9,616)</u>	<u>\$ (1,629,251)</u>

(13) Stockholders' Equity

Stock Repurchase Activity

During the three months ended March 31, 2025 and 2024, the Company did not repurchase any shares of its common stock.

(14) Litigation

In view of the inherent difficulty of predicting the outcome of litigation, particularly where the claimants seek very large or indeterminate damages, the Company generally cannot predict what the eventual outcome of the pending matters will be, what the timing of the ultimate resolution of these matters will be, or what the eventual loss, fines or penalties related to each pending matter may be.

In accordance with the authoritative guidance issued by the FASB on contingencies, the Company accrues anticipated costs of settlement, damages and losses for claims to the extent specific losses are probable and estimable. The Company records a receivable for insurance recoveries when such amounts are probable and collectable. In such cases, there may be an exposure to loss in excess of any amounts accrued. If, at the time of evaluation, the loss contingency related to a litigation is not both probable and estimable, the matter will continue to be monitored for further developments that would make such loss contingency both probable and estimable and, the Company will expense these costs as incurred. If the estimate of a probable loss is a range and no amount within the range is more likely, the Company will accrue the minimum amount of the range.

The Company is subject to various legal proceedings and claims, asserted or unasserted, which arise in the ordinary course of business. While the outcome of any such matters cannot be predicted with certainty, such matters are not expected to have a material adverse effect on the Company's financial condition or operating results.

The Company continues to assess certain litigation and claims to determine the amounts, if any, that the Company believes may be paid as a result of such claims and litigation and, therefore, additional losses may be accrued and paid in the future, which could materially adversely impact the Company's financial results, its cash flows and its cash reserves.

(15) Segment Reporting and Concentrations

The Company is organized in a single operating segment for purposes of making operating decisions and assessing performance. Revenue to customers in the following geographical areas for the three months ended March 31, 2025 and 2024, and the location of long-lived assets as of March 31, 2025 and December 31, 2024, are summarized as follows:

	Three Months Ended March 31,	
	2025	2024
Revenue:		
Americas	\$ 1,668,157	\$ 1,349,095
Europe, Middle East, Africa and Other	526,565	595,836
Asia Pacific	285,549	351,281
Total Revenue	\$ 2,480,271	\$ 2,296,212
	March 31, 2025	December 31, 2024
Long-lived assets:		
Americas	\$ 316,893	\$ 376,122
Asia Pacific	131,854	91,521
Europe, Middle East, Africa and Other	2,364	2,415
Total long-lived assets	\$ 451,111	\$ 470,058

For the three months ended March 31, 2025, the Company had two customers that accounted for 10% or more of total revenue. For the three months ended March 31, 2024, the Company had one customer that accounted for 10% or more of total revenue.

As of March 31, 2025, the Company had two customers that accounted for 10% or more of the gross accounts receivable balance. As of December 31, 2024, the Company had two customers that accounted for 10% or more of the gross accounts receivable balance.

Segment expenses for a single operating segment are included in the Company's consolidated statements of operations. Detailed disclosure of significant segment expenses by function, which are not individually shown in the consolidated statements of operations for the three months ended March 31, 2025 and 2024, are provided below:

	Three Months Ended March 31,	
	2025	2024
Revenue	\$ 2,480,271	\$ 2,296,212
Expenses:		
Employee & Contractor expense	\$ 1,676,585	\$ 1,538,196
Professional expense	343,123	319,376
Office and General expense	139,465	142,031
Software and Support expense	198,459	230,692
Marketing expense	74,353	21,887
Depreciation and amortization	8,047	17,830
Net Interest expense	36,979	40,700
Income tax expense	12,460	(16,247)
Other expense*	(88,127)	122,799
Total Expenses	\$ 2,401,344	\$ 2,417,264
Net Income	\$ 78,927	\$ (121,052)

(*) Other expenses included in Segment net income includes marketing expenses, foreign currency exchange gains and losses and other overhead expenses.