

Quadrant 4 System Corp  
Form 10-Q  
September 18, 2015

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

\_\_\_\_\_  
FORM 10-Q  
\_\_\_\_\_

(Mark One)

QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2015

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE EXCHANGE ACT

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 33-42498

QUADRANT 4 SYSTEM CORPORATION  
(Exact name of registrant as specified in its charter)

Illinois  
(State or other jurisdiction of  
incorporation or organization)

65-0254624  
(IRS Employer  
Identification No.)

1501 E. Woodfield Road, Suite 205 S, Schaumburg, IL 60173  
(Address of principal executive offices)

(855) 995-QFOR  
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-Q or any amendment to this Form 10-Q.

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

Indicate by checkmark whether the registrant is a shell company (as defined in Rule 126.2 of the Exchange Act). Yes  No

The number of shares of common stock outstanding as of September 18, 2015 was 103,011,773.

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## PART I. FINANCIAL INFORMATION

## Item 1. Financial Statements

QUADRANT 4 SYSTEM CORPORATION  
Condensed Consolidated Balance Sheets

|  | June 30, 2015<br>(Unaudited) | December 31,<br>2014<br>(Audited) |
|--|------------------------------|-----------------------------------|
| <b>ASSETS</b>  |                              |                                   |
| Current Assets   |                              |                                   |
| Cash   | \$ 634,722                   | \$ 2,285,557                      |
| Accounts and unbilled receivables (net of allowance for doubtful accounts of \$866,365 and \$810,000 at June 30, 2015 and December 31, 2014, respectively) | 12,651,433                   | 10,118,816                        |
| Inventory  | 118,596                      | -                                 |
| Other current assets   | 269,691                      | 233,789                           |
| <b>Total current assets</b>  | <b>13,674,442</b>            | <b>12,638,162</b>                 |
| Intangible assets, customer lists and technology stacks – net  | 12,129,580                   | 12,479,737                        |
| Equipment under capital lease, net   | 412,831                      | -                                 |
| Equipment – net  | 49,298                       | 35,931                            |
| Long-term assets   |                              |                                   |
| Software development costs   | 8,556,615                    | 5,146,047                         |
| Deferred financing costs – net   | 478,781                      | 600,583                           |
| Deferred licensing and royalty fees  | 1,080,000                    | 1,200,000                         |
| Other assets   | 395,736                      | 361,464                           |
| <b>TOTAL ASSETS</b>  | <b>\$ 36,777,283</b>         | <b>\$ 32,461,924</b>              |

## LIABILITIES AND STOCKHOLDERS' EQUITY

|   |                   |                   |
|---|-------------------|-------------------|
| Current Liabilities   |                   |                   |
| Accounts payable and accrued expenses                                     | \$ 6,245,598      | \$ 4,413,094      |
| Note payable – Revolver   | 7,136,796         | 6,750,050         |
| Earnouts payable  | 400,000           | -                 |
| Current obligation under capital lease                                    | 148,214           | -                 |
| Current maturities - long term debt, net of debt discount of \$356,333    | 1,505,274         | 650,810           |
| <b>Total current liabilities</b>  | <b>15,435,882</b> | <b>11,813,954</b> |
| Non-current obligation under capital lease                                | 239,591           | -                 |
| Long-term debt, less current maturities, net of debt discount of \$51,111 | 5,854,820         | 5,834,688         |
| <b>Total liabilities</b>  | <b>21,530,293</b> | <b>17,648,642</b> |
| Commitments and contingencies   |                   |                   |

Stockholders' Equity

Common stock - \$0.001 par value; authorized: 200,000,000 shares: issued and outstanding

103,011,773 and 102,661,774 at June 30, 2015 and December 31, 2014, respectively

|                            |              |              |
|----------------------------|--------------|--------------|
|                            | 103,012      | 102,662      |
| Additional paid-in capital | 33,452,453   | 33,231,980   |
| Accumulated deficit        | (18,308,475) | (18,521,360) |
| Total stockholders' equity | 15,246,990   | 14,813,282   |

|  |               |               |
|--|---------------|---------------|
| TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY | \$ 36,777,283 | \$ 32,461,924 |
|--|---------------|---------------|

See notes to the condensed consolidated financial statements

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QUADRANT 4 SYSTEM CORPORATION  
Condensed Consolidated Statements of Operations  
(Unaudited)

|  | Three Months Ending June 30, |              | Six Months Ending June 30, |              |
|--|------------------------------|--------------|----------------------------|--------------|
|  | 2015                         | 2014         | 2015                       | 2014         |
| Revenue                                    | \$13,069,754                 | \$11,917,170 | \$26,708,400               | \$22,201,314 |
| Cost of revenue                            | 7,684,286                    | 7,885,487    | 16,030,599                 | 14,718,265   |
| Gross Margin                               | 5,385,468                    | 4,031,683    | 10,677,801                 | 7,483,049    |
| <b>Operating expenses:</b>                 |                              |              |                            |              |
| General and administrative expenses        | (3,246,518 )                 | (1,790,455 ) | (6,045,858 )               | (3,514,626 ) |
| Research & Development                     | (469,795 )                   | (537,995 )   | (1,040,023 )               | (1,051,490 ) |
| Amortization and depreciation expense      | (1,020,357 )                 | (1,397,461 ) | (2,341,616 )               | (2,722,255 ) |
| Interest expense                           | (522,190 )                   | (282,242 )   | (1,037,419 )               | (675,454 )   |
| Total                                      | (5,258,860 )                 | (4,008,153 ) | (10,464,916 )              | (7,963,825 ) |
| Net Income / (loss) before income taxes    | 126,608                      | 23,530       | 212,885                    | (480,776 )   |
| Provision for Income taxes                 | -                            | -            | -                          | -            |
| Net Income/(loss)                          | \$126,608                    | \$23,530     | \$212,885                  | \$(480,776 ) |
| <b>Net Income/ (loss) per common share</b> |                              |              |                            |              |
| - Basic                                    | \$*                          | \$*          | \$*                        | \$(0.01 )    |
| - Fully diluted                            | \$*                          | \$*          | \$*                        | \$(0.01 )    |
| <b>Weighted average common shares</b>      |                              |              |                            |              |
| - Basic                                    | 102,956,279                  | 93,856,144   | 102,809,840                | 93,427,813   |
| - Fully diluted                            | 107,552,461                  | 96,772,909   | 107,406,023                | 93,427,813   |

\*Less than \$0.01, per share

See notes to the condensed consolidated financial statements

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QUADRANT 4 SYSTEM CORPORATION  
Condensed Consolidated Statements of Cash Flows  
(Unaudited)

|  | For the Six Months Ending<br>June 30, |              |
|--|---------------------------------------|--------------|
|  | 2015                                  | 2014         |
| Cash flows from operating activities:  |                                       |              |
| Net Income/(loss)  | \$ 212,885                            | \$ (480,776) |
| Adjustments to reconcile net income/(loss) to net cash used in operating activities:   |                                       |              |
| Amortization, impairment and depreciation expense  | 2,341,616                             | 2,722,255    |
| Provision for doubtful accounts  | 56,365                                | -            |
| Issuance of Stock for services and interest  | 52,500                                | 75,000       |
| Issuance of Warrants for services  | 25,823                                | -            |
| Changes in assets and liabilities, net of the effect of the acquisitions   |                                       |              |
| Accounts and unbilled receivables  | (2,467,267)                           | (1,649,514)  |
| Inventory  | (118,596)                             | -            |
| Other current assets   | (190,766)                             | (178,983)    |
| Software development costs   | (3,410,568)                           | (720,000)    |
| Deferred finance costs   | 121,802                               | -            |
| Deferred license cost  | 120,000                               | -            |
| Other assets   | 213,035                               | (64,986)     |
| Obligation under capital lease   | 387,805                               | -            |
| Accounts payable and accrued expenses  | 1,680,729                             | (256,223)    |
| Net cash used in operating activities  | (974,637)                             | (553,227)    |
| Cash flows from investing activities:  |                                       |              |
| Purchase of fixed assets   | (467,812)                             | (13,920)     |
| Acquisition of assets (net of assets assumed of \$104,700, notes payable assumed of \$1,000,000, contingent payments of \$400,000 and issuance of common stock of \$142,500) | (469,728)                             | -            |
| Net cash used in investing activities  | (937,540)                             | (13,920)     |
| Cash flows from financing activities:  |                                       |              |
| Proceeds from sales of common stock  | -                                     | 1,124,750    |
| Borrowings on revolver   | 23,413,786                            | 8,147,085    |
| Repayments of revolver   | (23,027,040)                          | (9,179,572)  |
| Payments of long-term debt   | (125,404)                             | (152,501)    |
| Net cash provided by/(used in) financing activities  | 261,342                               | (60,238)     |
| Net decrease in cash   | (1,650,835)                           | (627,385)    |
| Cash - beginning of year   | 2,285,557                             | 897,215      |
| Cash - end of year   | \$ 634,722                            | \$ 269,830   |
| Supplemental disclosure of cash flow information   |                                       |              |
| Cash paid for:   |                                       |              |
| Interest   | \$ 466,980                            | \$ 700,998   |

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|  |    |         |    |           |
|--|----|---------|----|-----------|
| Income taxes   | \$ | -       | \$ | -         |
| Noncash transactions   |    |         |    |           |
| Acquisition of technology platform utilizing common stock & warrants | \$ | -       | \$ | 3,075,649 |
| Noncash consideration for acquisitions                               | \$ | 142,500 | \$ | -         |

See notes to the condensed consolidated financial statements



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QUADRANT 4 SYSTEM CORPORATION  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)

NOTE 1 – ORGANIZATION AND OPERATIONS

Organization

Quadrant 4 System Corporation (sometimes referred to herein as “Quadrant 4” or the “Company”) was incorporated by the Florida Department of State on May 9, 1990 as Sun Express Group, Inc. and changed its name on March 31, 2011. The Company changed its domicile to Illinois on April 25, 2014. The Company generates revenue from clients located mostly in North America and operates out of six different office locations throughout the United States.

Operations

The Company is engaged in the Information Technology sector as a provider of Platform-as-a-Service (PaaS) and Software-as-a-Service (SaaS) systems to the health insurance (QHIX), media (QBLITZ) and education (QEDX) verticals. Along with these platforms, we also provide relevant services that leverage on our proprietary Social Media, Mobility, Analytics and Cloud (SMAC) technology stack. Our core services include Consulting, Application Life Cycle Management, Enterprise Applications & Data Management, Mobility Applications and Business Analytics (collectively “Consulting”). We blend these services with our technology platforms to offer client specific and industry specific solutions to Healthcare, Media, Education, Retail and Manufacturing industry segments (collectively “Solutions”).

The Company generates revenues principally from two broad segments, namely Services and Platforms (PaaS/SaaS). The Services component includes consulting services that bills on a time & material basis; projects that bill on a predominantly time & material basis with a small mile-stone component; and managed services that bill fixed fees that provide pre-determined SLA based services. The Platform segment bills on transaction basis such as per member per month enrolled for the QHIX; per bandwidth consumed for the QBLITZ; and per student per month for the QEDX platforms. The Company anticipates to start delivering Platform based revenues in 2016.

NOTE 2 – BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements and related notes have been prepared in accordance with the United States generally accepted accounting principles (“GAAP”) and with the applicable rules and regulations of the Securities and Exchange Commission. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements presentation. In the opinion of the management, all adjustments (consisting of normal recurring accruals) considered necessary to present fairly the financial position, results of operations and cash flows for interim financial statements have been included. This form 10-Q should be read in conjunction with the Company’s Annual Report on Form 10-K for the year ended December 31, 2014. Interim results are not necessarily indicative of the results for the fiscal year ending December 31, 2015.

Consolidated Financial Statements

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America and include all the accounts of the Company. As of January 1, 2015, all subsidiaries have been merged with Quadrant 4 System Corporation and all intercompany transactions have been eliminated.

NOTE 3 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reclassifications

Certain amounts for the prior period have been revised or reclassified to conform to 2015 presentation.

Estimates

The preparation of the Company's consolidated financial statements in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP") requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Significant estimates include the allowance for uncollectible accounts receivable, depreciation and amortization, intangible assets, including customer lists and technology stacks, capitalization, fair value and useful lives, accruals, contingencies, impairment and valuation of stock warrants and options. These estimates may be adjusted as more current information becomes available, and any adjustment could have a significant impact on recorded amounts. Accordingly, actual results could differ from those estimates.

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### Fair Value of Financial Instruments

The Company considers the carrying amounts of financial instruments, including cash, accounts receivable, accounts payable, accrued expenses and notes payable to approximate their fair values because of their relatively short maturities.

### Accounts and Unbilled Receivables

Accounts and unbilled receivables consist of amounts due from customers which are presented net of the allowance for doubtful accounts at the amount the Company expects to collect. The Company records a provision for doubtful receivables, if necessary, to allow for any amounts which may be unrecoverable, which is based upon an analysis of the Company's prior collection experience, customer creditworthiness, past transaction history with the customers, current economic trends, and changes in customer repayment terms.

Unbilled receivables are established when revenue is deemed to be recognized based on the Company's revenue recognition policy, but due to contractual restraints over the timing of invoicing, the Company does not have the right to invoice the customer by the balance sheet date.

### Inventory

Inventory consists primarily of manufactured and preassembled units ready for distribution. Inventory is stated at the lower of cost (first-in, first-out) or market. In evaluating whether inventory is stated lower of cost or market, management considers such factors as the amount of inventory on hand and the distribution channel, the estimated time to sell such inventory, and the current market conditions. Adjustments to reduce inventory to its net realizable value are charged to cost of goods sold.

### Vendors and Contractors

The Company outsources portions of its work to third party service providers. These providers can be captive suppliers that undertake software development, research & development and custom platform development. Some vendors may provide specific consultants or resources (often called Corp to Corp) or independent contractors (often designated as 1099) to satisfy agreed upon deliverables to its clients.

### Equipment

Equipment is recorded at cost and depreciated for financial statement purpose using the straight line method over estimated useful lives of five to fifteen years. Maintenance and repairs are charged to operating expenses as they are incurred. Improvements and betterments, which extend the lives of the assets, are capitalized. The cost and accumulated depreciation of assets retired or otherwise disposed of are removed from the appropriate amounts and any profit or loss on the sale or disposition of each assets is credited or charged to income.

### Intangible Assets

Intangible assets, consisting of customer lists and technology stacks, are recorded at fair value and amortized on the straight-line method over the estimated useful lives of the related assets.

The carrying value of intangible assets are reviewed for impairment by management of the Company at least annually or upon the occurrence of an event which may indicate that the carrying amount may be greater than its fair value. Management of the Company has decided to perform its impairment testing on a quarterly basis starting in fiscal year

2015. If impaired, the Company will write-down such impairment. In addition, the useful life of the intangible assets will be evaluated by management at least annually or upon the occurrence of an event which may indicate that the useful life may have changed.

Customer lists are valued based on management's forecast of expected future net cash flows, with revenues based on projected revenues from customers acquired and are being amortized over five years.

Technology stacks are valued based on management's forecast of expected future net cash flows, with revenues based on projected sales of these technologies and are amortized over five to seven years.

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### Software Development Costs

Costs that are related to the conceptual formulation and design of licensed software programs are expensed as incurred to research, development engineering and other administrative support expenses; costs that are incurred to produce the finished product after technological feasibility has been established and after all research and development activities for any other component of the product or process have been completed are capitalized as software development costs. Capitalized amounts will be amortized on a straight-line basis over periods ranging up to five years which will be recorded in amortization expense starting in year 2016 commencing when the platforms first become offered for sale. The Company performs periodic reviews to ensure that unamortized software development costs remain recoverable from future revenue. Cost to support or service licensed program are charged to cost of revenue as incurred.

### Pre-paid Expenses

The Company incurs certain costs that are deemed as prepaid expenses. The fees that are paid to the Department of Homeland Security for processing H1 visa fees for its international employees are amortized over 36 months, typically the life of the visa. One third of these pre-paid expenses are included in other current assets and two thirds in other assets.

### Deferred Financing Costs

Financing costs incurred in connection with the Company's notes payable and revolving credit facilities are capitalized and amortized into expense using the straight-line method over the life of the respective facility.

### Deferred Licensing and Royalty Fees

The Company licenses software, platforms and/or content on a needed basis and enters into market driven licensing and royalty fee arrangements. If no consumption or usage of such licenses happen during the reporting period, the Company has no obligation for any minimum fees or royalties and no accruals are posted. The deferred licensing fee is being amortized over five years.

### Leases

The Company has operating lease agreements for its offices some of which contain provisions for future rent increases or periods in which rent payments are abated. Operating leases which provide for lease payments that vary materially from the straight-line basis are adjusted for financial accounting purposes to reflect rental income or expense on the straight-line basis in accordance with the authoritative guidance issued by the Financial Accounting Standards Board ("FASB"). No such material difference existed as of June 30, 2015.

### Capitalized Lease

Capital leases are measured and recorded at present value as an asset and obligation. The asset is depreciated on a straight line over its estimated useful life and the obligation is paid using an effective interest rate.

### Financial Instruments

The Company does not use derivative instruments to hedge exposures to cash flow, market or foreign currency risks.

The Company reviews the terms of convertible debt and equity instruments it issues to determine whether there are embedded derivative instruments, including the embedded conversion option, that are required to be bifurcated and

accounted for separately as a derivative financial instrument. In connection with the sale of convertible debt and equity instruments, the Company may issue freestanding warrants that may, depending on their terms, be accounted for as derivative instrument liabilities, rather than as equity.

Bifurcated embedded derivatives are initially recorded at fair value and are then revalued at each reporting date with changes in the fair value reported as non-operating income or expense. When the convertible debt or equity instruments contain embedded derivative instruments that are to be bifurcated and accounted for as liabilities, the total proceeds allocated to the convertible host instruments are first allocated to the fair value of all the bifurcated derivative instruments. The remaining proceeds, if any, are then allocated to the convertible instruments themselves, usually resulting in those instruments being recorded at a discount from their face amount.

The discount from the face value of the convertible debt, together with the stated interest on the instrument, is amortized over the life of the instrument through periodic charges to interest expense, using the effective interest method.

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### Revenue Recognition

Revenue is recognized when there is persuasive evidence of an arrangement, the fee is fixed and determinable, performance of service has occurred and collection is reasonably assured. Revenue is recognized in the period the services are provided on which service ranges from approximately 2 months to over 1 year.

For time & material engagements, the Company recognizes revenues when the client signs and approves the time sheet of a consultant(s) assigned to the engagement. For projects, the Company recognizes the revenues when the client acknowledges or accepts the delivery of the defined deliverables. For managed services engagements, the Company bills the contracted amount per billing period with no further acknowledgement from the client since such contracts have service level agreements and any service deficiencies are addressed within the normal course of engagement. The hosting revenues are recognized in the beginning of the period and are amortized over the term of the engagement since the client has no recourse and such fees are non-refundable. Platform revenues are recognized at the end of the period using the starting and ending average of the billing period and is generated by the platform with no further statement of work or purchase orders or approvals.

### Income Taxes

Deferred income taxes have been provided for temporary differences between financial statement and income tax reporting under the liability method, using expected tax rates and laws that are expected to be in effect when the differences are expected to reverse. A valuation allowance is provided when realization is not considered more likely than not.

The Company's policy is to classify income tax assessments, if any, for interest expense and for penalties in general and administrative expenses. The Company's income tax returns for the years 2012, 2013 and 2014 are subject to examination by the IRS and corresponding states.

As of June 30, 2015, management has evaluated and concluded that there are no significant uncertain tax positions requiring recognition in the Company's condensed consolidated financial statements.

### Income (Loss) per Common Share

Basic income (loss) per share is calculated using the weighted-average number of common shares outstanding. Diluted income per share includes potentially dilutive securities such as outstanding options and warrants outstanding during each period.

For the six months ended June 30, 2015 there were 4,596,182 potentially dilutive securities that were included in the calculation of weighted-average common shares outstanding. For the six months ended June 30, 2014, there were 15,285,427 potentially dilutive securities that were not included in the calculation of weighted-average common shares outstanding since they would be anti-dilutive.

### Derivatives

We account for derivatives pursuant to ASC 815, Accounting for Derivative Instruments and Hedging Activities. All derivative instruments are recognized in the consolidated financial statements and measured at fair value regardless of the purpose or intent for holding them. We record our interest rate and foreign currency swaps at fair value based on discounted cash flow analysis and for warrants and other option type instruments based on option pricing models. The changes in fair value of these instruments are recorded in income or expense.

## Share based compensation

The Company recognizes compensation expense for all share-based payment awards made to employees, directors and others based on the estimated fair values on the date of the grant. Common stock equivalents are valued using the Black-Scholes model using the market price of our common stock on the date of valuation, an expected dividend yield of zero, the remaining period or maturity date of the common stock equivalent and the expected volatility of our common stock.

The Company determines the fair value of the share-based compensation awards granted as either the fair value of the consideration received or the fair value of the equity instruments issued, whichever is more reliably measurable. If the fair value of the equity instruments issued is used, it is measured using the stock price and other measurement assumptions as of the earlier of either the date at which a commitment for performance to earn the equity instrument is reached or the date the performance is complete.

The Company recognizes compensation expense for stock awards with service conditions on a straight-line basis over the requisite service period, which is included in operations.



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### Concentrations of Credit Risk

The Company maintains cash at various financial institutions, which at times, may be in excess of insured limits. The Company has not experienced any losses to date as a result of this policy and, in assessing its risk, the Companies' policy is to maintain cash only with reputable financial institutions.

The Company currently banks at two national institutions with one being the primary and the other for petty cash purposes. The Company does not maintain large balances in its lockbox account due to the daily automatic sweeping arrangement with its lenders that credits its debts on a daily basis. As of June 30, 2015 no operating accounts had cash value that exceeded the FDIC insurance limit of \$250,000.

The Company's largest customer represented 16% and 15% of consolidated revenues and 20.7% and 9% of accounts receivable as of and for the six months ended June 30, 2015 and 2014, respectively. The Company had two customers that represented 20.7% and 13.4% of the total accounts receivable as of June 30, 2015, while one customer had 15% of the total accounts receivable as of June 30, 2014. The Company's largest vendor represented 25.1% and 25.3% of total vendor payments for the six months ended June 30, 2015 and 2014, respectively.

### Advertising costs

Advertising costs are expensed as incurred. Total advertising was \$9,115 and \$12,821 for the six months ended June 30, 2015 and 2014 respectively; \$3,653 and \$9,133 for the three months ended June 30, 2015 and 2014, respectively.

### Recent Accounting Pronouncements

In May 2014, the FASB issued guidance creating Accounting Standards Codification ("ASC") Section 606, "Revenue from Contracts with Customers". The new section will replace Section 605, "Revenue Recognition" and creates modifications to various other revenue accounting standards for specialized transactions and industries. The section is intended to conform revenue accounting principles with a concurrently issued International financial Reporting Standards with previously differing treatment between United States practice and those of much of the rest of the world, as well as, to enhance disclosures related to disaggregated revenue information. The updated guidance is effective for annual reporting periods beginning on or after December 15, 2016, and interim periods within those annual periods. The Company will adopt the new provisions of this accounting standard at the beginning of fiscal year 2017, given that early adoption is not an option. The Company will further study the implications of this statement in order to evaluate the expected impact on its financial statements.

In August 2014, the FASB issued ASU No. 2014-15 "Presentation of Financial Statements-Going Concern." The provisions of ASU No.2014-15 require management to assess an entity's liability to continue as a going concern by incorporating and expanding upon certain principles that are currently in U.S. audit standards. Specifically, the amendments (1) provide a definition of the term substantial doubt, (2) require evaluation of every reporting period including interim periods, (3) provide principles for considering the mitigating effect of management's plans, (4) require certain disclosures when substantial doubt is alleviated as a result of consideration of management's plans, (5) require an express statement and other disclosures when substantial doubt is not alleviated, and (6) require an assessment for a period of one year after the date that the financial statements are issued (or available to be issued). The amendments in this ASU are effective for the annual period ending after December 15, 2016, and for annual periods and interim periods thereafter. The Company is currently assessing the impact of ASU No. 2014-15 on the Company's consolidated financial statements.

Management does not believe that any other recently issued, but not yet effective accounting pronouncements, if adopted, would have a material effect on the accompanying consolidated financial statements.

NOTE 4 – ACQUISITIONS

On January 1, 2015, the Company completed the acquisition of 100% of the outstanding stock of Brainchild Corporation ("Brainchild"). Brainchild based in Naples, Florida is a leading provider of web-based and mobile learning solutions for kindergarten through high school, grades K-12. The acquisition of Brainchild includes technology, staffing and software solutions developed for providing its educational solutions.

This acquisition represents the Company's entry into its newest vertical. This will not change the Company's business model since the Company intends to leverage its experience in building and operating cloud-based exchanges for healthcare and media to the education market. The Company believes there is a growing demand for platforms that will bring together the delivery of digital instructional content, assessments and analysis of student information and performance data by educators in K-12 schools throughout the US.

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The Company paid; \$500,000 in cash, less certain loan balances at closing; 250,000 shares of the Company's common stock with a buy back at thirty-six months at a guaranteed valuation of \$2.00, per share, and a note for \$1,000,000 for thirty-six months with interest at 8%, per annum. In addition, the Agreement calls for a performance based earn-out of up to \$400,000, as defined, to be paid on a semi-annual basis on January 1 and July 1 each year based on actual cash received from the sale of units during the period. The Seller has the option to receive any or all of the earn-out payment in common stock of the Company priced at a five trading day average price, as defined.

The following table summarizes the allocation of the purchase price of the acquisition over the estimated fair values of the assets acquired and liabilities assumed.

Fair value of consideration transferred:

|   |              |
|---|--------------|
| Cash  | \$ 500,000   |
| Subordinated debt   | 1,000,000    |
| Common stock, 250,000 shares (at \$0.57, per share)                         | 142,500      |
| Contingent earn-out payments  | 400,000      |
|   |              |
| Total consideration   | \$ 2,042,500 |
|   |              |
| Recognized amounts of identifiable assets acquired and liabilities assumed: |              |
|   |              |
| Cash  | \$ 31,164    |
| Customer lists/Technology intangibles, net                                  | 649,265      |
| Inventory   | 90,442       |
| Deposits  | 2,000        |
| Accounts receivable   | 121,715      |
| Fixed assets  | 12,045       |
| Accounts payable and accrued liabilities                                    | (151,774)    |
| Long-term debt  | (199,438)    |
|   |              |
| Sub-Total   | 555,419      |
| Excess of purchase price allocated to intangible assets                     | 1,487,081    |
|   |              |
| Total   | \$ 2,042,500 |

The following unaudited proforma summary presents consolidated information of the Company as if this business combination occurred on January 1, 2014 and includes the amortization of acquired intangibles.

|              |                |
|--------------|----------------|
|              | 2014           |
| Gross Sales: | \$ 50,482,572  |
|              |                |
| Net Loss:    | \$ (2,119,398) |

The Company repaid the long-term debt of \$199,438 on January 23, 2015 through advances of the Note payable – Revolver.

On January 20, 2015, the Company merged Brainchild with its parent.

NOTE 5 – INTANGIBLE ASSETS OF CUSTOMER LISTS AND TECHNOLOGY STACKS

On May 1, 2014, the Company acquired certain technology assets specific to media platforms for a total consideration of 4,444,445 shares priced at \$0.45/share aggregating to \$2,000,000 which was capitalized in 2014 as part of the technology stacks, and 2 million warrants exercisable over 3 years, with an exercise prices of \$0.50 and \$0.10, per share. The value of the warrants, using Black Scholes model is \$977,171 which was capitalized in 2014 as part of the technology stacks. These assets are critical to executing the long-term sales contract that the Company signed effective May 1, 2014 to provide media platform services valued up to \$50,000,000 over five years to an existing client.

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As of June 30, 2015 and December 31, 2014, intangible assets consisted of the following:

|                         | June 30, 2015        |                          |                   | December 31, 2014    |                          |                      |
|-------------------------|----------------------|--------------------------|-------------------|----------------------|--------------------------|----------------------|
|                         | Gross                | Accumulated amortization | Balance           | Gross                | Accumulated amortization | Balance              |
| <b>Customer list</b>    |                      |                          |                   |                      |                          |                      |
| Consulting              | \$ 7,131,196         | (7,131,196)              | -                 | \$ 7,131,196         | \$ (6,831,295)           | \$ 299,900           |
| Solutions               | 8,500,000            | (8,216,181)              | 283,819           | 8,500,000            | (8,003,313)              | 496,688              |
| Cloud                   | 7,650,000            | (4,852,090)              | 2,797,910         | 7,650,000            | (4,310,560)              | 3,339,440            |
| Media                   | 1,639,750            | (933,408)                | 706,342           | 1,639,750            | (797,808)                | 841,942              |
|                         | 24,920,946           | (21,132,875)             | 3,788,071         | 24,920,946           | (19,942,976)             | 4,977,970            |
| <b>Technology stack</b> |                      |                          |                   |                      |                          |                      |
| Solutions               | \$ 5,775,000         | (4,102,075)              | 1,672,925         | \$ 5,775,000         | \$ (3,614,665)           | \$ 2,160,335         |
| Cloud                   | 850,000              | (293,451)                | 556,549           | 850,000              | (232,737)                | 617,263              |
| Media                   | 5,642,171            | (1,321,016)              | 4,321,155         | 5,642,171            | (918,002)                | 4,724,169            |
| Education               | 2,934,931            | (1,144,051)              | 1,790,881         | -                    | -                        | -                    |
|                         | 15,202,102           | (6,860,593)              | 8,341,509         | 12,267,171           | (4,765,404)              | 7,501,767            |
| <b>Total</b>            | <b>\$ 40,123,058</b> | <b>(27,993,468)</b>      | <b>12,129,580</b> | <b>\$ 37,188,117</b> | <b>\$ (24,708,380)</b>   | <b>\$ 12,479,737</b> |

For the Six months ending June 30, 2015, the change in intangible assets was as follows:

|                      |               |
|----------------------|---------------|
| Balance, January 1,  | \$ 12,479,737 |
| Additions            | 1,937,800     |
| Impairment of assets | -             |
| Amortization         | (2,287,957)   |
| Balance, June 30,    | \$ 12,129,580 |

For three months ending June 30, 2015 and 2014, amortization expense was \$994,027 and \$1,395,963, respectively.

**NOTE 6 – SOFTWARE DEVELOPMENT COSTS**

The Company specifically recognizes capitalized software costs by its product platforms as follows:

| Description of Cost | June 30, 2015 | December 31, 2014 |
|---------------------|---------------|-------------------|
| <b>Platforms:</b>   |               |                   |
| QHIX                | \$ 3,935,634  | \$ 3,121,313      |
| QBIX                | 1,527,060     | 1,427,485         |
| QBLITZ              | 2,340,536     | 597,249           |
| QEDX                | 753,385       | -                 |
|                     | \$ 8,556,615  | \$ 5,146,047      |

**NOTE 7 – INVENTORY**

Inventory consists of the following:

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| Description                           | June 30, 2015 |
|---------------------------------------|---------------|
| Hardware Assessment Devices           | \$ 94,500     |
| Display Devices                       | 7,434         |
| Accessories – Power adaptors & Cables | 16,662        |
|                                       | \$ 118,596    |

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## NOTE 8 – PROPERTY &amp; EQUIPMENT

Property and equipment consists of the following:

| Description of Cost            | June 30, 2015 | December 31,<br>2014 |
|--------------------------------|---------------|----------------------|
| Furniture & fixtures           | \$ 10,294     | \$ 5,000             |
| Computing equipment            | 518,995       | 44,431               |
| Total                          | 529,289       | 49,431               |
| Less: Accumulated depreciation | (67,160)      | (13,500)             |
| Balance                        | \$ 462,129    | \$ 35,931            |

Depreciation expense was \$53,659 and \$1,500 for the six months ended June 30, 2015 and 2014, respectively; \$26,330 and \$1,250 for the three months ended June 30, 2015 and 2014, respectively.

## NOTE 9 – NOTE PAYABLE - REVOLVER

In October 2014, the Company refinanced its factoring facility and replaced it with a new Asset Based Lending (ABL) revolver bank facility that has a term of 36 months and a maximum line of \$10,000,000. The ABL was priced at 4.5% over 30-day LIBOR (with a minimum floor of 2%) plus an administrative fee of 0.1% per month on the outstanding balance and 0.084% per month on the unused portion of the revolver. As of June 30, 2015 and December 31, 2014, the Company has borrowed the maximum based on the borrowing base calculations and has borrowings of \$7,136,796 and \$6,750,050, respectively, on the Revolver.

In addition, the Company entered into a term loan commitment with the lender for \$3,000,000 (Note 10).

All borrowings under this revolving line of credit are collateralized by the accounts receivable and substantially all other assets of the Company.

In connection with the financing, the Company incurred legal, loan origination and advisory expenses totaling \$600,583 which has been recorded as deferred financing costs and are being amortized over three years as interest expense. Amortization for the six months ending June 30, 2015 on the deferred financing costs is \$70,692.

## NOTE 10 – LONG-TERM DEBT

Long-term debt consisted of the following:

|  | June 30, 2015 | December 31,<br>2014 |
|--|---------------|----------------------|
| Note payable due December 31, 2017, as extended, plus interest at 6.5% per annum (a) | \$ 3,117,538  | \$ 3,117,538         |
| Note payable due October 1, 2017, plus interest at approximately 10% per annum (b)   | 2,350,000     | 2,853,571            |
| Note payable due July 1, 2016, plus interest at 8% per annum (c)                     | 1,100,000     | 1,100,000            |
| Note payable due Jan 1, 2018, plus interest at 8% per annum (d)                      | 1,000,000     | -                    |
| Note payable due September 30, 2015, plus interest at 8% per annum (e)               | 200,000       | -                    |
| Less: Discounts  | (407,444)     | (585,611)            |
| Total  | 7,360,094     | 6,485,498            |

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|                          |             |              |
|--------------------------|-------------|--------------|
| Less: Current maturities | (1,505,274) | (650,810)    |
| Total long-term debt     | \$5,854,820 | \$ 5,834,688 |

(a) In December 2013, \$2 million of the original \$5,000,000 Promissory note was converted to 3,333,334 shares of common stock (at \$0.60/share) with 1,666,667 warrants exercisable at \$1/share through December 31, 2018. The warrant was valued using the Black Scholes Option Pricing model and the Company recorded additional interest related to the conversion of debt and grant of warrants of \$1,350,000. In March 2014, the note was extended to December 31, 2015 without any further considerations. On October 1, 2014, the note was extended to December 31, 2017 with the new interest rate at 6.5%. Additionally, 350,000 shares of common stock was granted as consideration for the extension valued at \$140,000.

(b) In October 2014, the Company entered into a term loan for \$3,000,000. The term loan was priced at 8% over 30-day LIBOR (with a minimum floor of 2%) with a term of 36 months. The term loan, as amended, is payable over three years, \$83,928.57/month from January 1, 2015 through and including December 1, 2015, and \$104,910.71/month from January 1, 2016 through maturity. The Company also issued 250,000 warrants, exercisable at \$0.60/share for five years.



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The Company calculated the fair value of the warrant as \$119,991, based on a Black-Scholes Option Pricing Model using the market price of the Company's stock on the date of grant of \$0.48, per share; volatility of 355%; a risk-free interest rate of 1.64%; a term of five years and zero dividend and has allocated the value of the warrant over the term note. The allocated value of the warrant of \$115,000 has been recorded as a discount on the term note payable and will be amortized over three years as interest expense.

(c) In December 2014, the Company entered into a securities purchase agreement for a senior debenture in the amount of \$1,100,000 at 8%. Interest is payable on October 1, 2015 with principal payments of 25% on 1/1/2016, 25% on 4/1/2016 and the remaining 50% on 7/1/2016. The Company issued 2,053,333 warrants priced at \$0.60/share. The Company is obligated to issue additional 2,053,333 warrants priced at \$0.60/share in the event of a default.

The Company calculated the fair value of the warrant as \$841,771, based on a Black-Scholes Option Pricing Model using the market price of the Company's stock on the date of grant of \$0.41, per share; volatility of 349%; a risk-free interest rate of 1.64%; a term of five years and zero dividend and has allocated the value of the warrant over the note payable. The allocated value of the warrant of \$477,000 has been recorded as a discount on the note payable and will be amortized over eighteen months as interest expense.

(d) In January 2015, the Company issued a seller note for \$1,000,000 in connection with the Brainchild acquisition at an interest rate of 8% per annum, payable over 36 months beginning the third quarter of 2016.

(e) On April 17, 2015, the Company issued a short term note for \$200,000 at an interest rate of 12%, payable October 16, 2015.

NOTE 11 – STOCKHOLDERS' EQUITY

Preferred Stock

The Company's board of directors may designate preferred stock with preferences, participations, rights, qualifications, limitations, restrictions, etc., as required. No preferred shares are presently designated.

On April 28, 2015, the Company issued 50,000 shares of its common stock for services related to investor relations valued at \$24,500.

On April 28, 2015, the Company issued 50,000 shares of its common stock for services to a Board member for consulting services valued at \$28,000.

In January 2015, the Company issued a warrant to purchase 50,000 of its common stock to one of its Directors valued at \$25,823 using the Black-Scholes Option Pricing Model.

NOTE 12 – COMMITMENTS AND CONTINGENCIES

Operating Leases:

In September 2012, the Company entered into a five year lease agreement for its Cranbury, New Jersey facility, which expires on September 8, 2016. In June 2013, the Company entered into a five year lease agreement for its Southfield, Michigan facility, which expires on October 31, 2018. In February 2013 the Company took over the lease agreement of its Irvine, California facility, which expires on April 12, 2015. In July 2014, the Company entered into a three year sub-lease agreement for its Alpharetta, Georgia facility, which expires on September 8, 2017. In December 2014, the Company entered into a one year lease agreement for its El Segundo, California facility, which expires on December

31, 2015. The Company also added certain facilities as a month to month basis. In December 2014, the Company entered into a four year sub-lease agreement for its Irvine, California facility, which expires on April 30, 2019.

Capital Lease:

Effective February 1, 2015, the Company entered into a business lease agreement for computer hardware equipment with monthly payments of \$13,926 for a term of three years with a \$1.00 end-of-term purchase option.

In accordance with FASB ASC 840, Leases, the Company has recorded this capital lease asset and capital lease obligation initially at an amount equal to the present value at the beginning of the lease term of minimum lease payments.

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The following is a schedule of future minimum lease payments as of June 30, 2015.

|   |             |
|---|-------------|
| Year ending June 30,  |             |
| 2016  | \$ 167,114  |
| 2017  | \$ 167,114  |
| 2018  | \$ 83,557   |
| Total minimum lease payments  | \$417,785   |
| Less: amount representing interest  | \$ (29,980) |
| Present value of net minimum lease payments,<br>presented as current and non-current obligations<br>under capital leases of \$148,214 and \$239,591,<br>respectively. | \$ 387,805  |

Rent Expense for the six months ended June 30, 2015 and 2014 were \$173,936 and \$67,207, respectively, and for three months ending June 30, 2015 and 2014 were \$95,392 and \$1,332, respectively.

## Legal:

On May 13, 2014, a claim was filed against the Company in the Superior Court of California, County of Santa Clara arising from a collections dispute related to vendors of an acquisition target of the Company. All Plaintiffs were vendors of the target and are seeking recovery of approximately \$222,000. The Company is vigorously defending their position and it is expected that the court case will remain stayed until the earliest being fall 2015. In response to the claim, as of December 31, 2014 the Company has recorded an accrual in the event of legal settlement in the amount of \$123,000.

In the normal course of business, the Company may become subject to claims or assessments. Such matters are subject to many uncertainties, and outcomes, which are not readily predictable with assurance.

## Investor relations consulting Agreement:

On January 14, 2015 Company entered into an Investor Relations Consulting Agreement (Agreement) with an investor relations firm to provide consulting services regarding markets and exchanges, competitors, business acquisitions and other aspects of or concerning the Company's business. The Agreement is for the term of twelve months in exchange for 50,000 shares of the Company's restricted stock, valued at \$24,500.

## NOTE 13 – FOREIGN OPERATIONS

The Company's headquarters and operations are located in the United States. However, the Company does have a key supplier and subcontractor located in India. The Company has no ownership, directly or indirectly, in the key supplier and subcontractor. The India based supplier billed the Company \$6,749,000 and \$5,031,300 for the years ended December 31, 2014 and 2013, respectively. For the India based supplier the Company owed \$630,000 and \$384,000 as of June 30, 2015 and 2014, respectively.

The Company has entered into a long term master services agreement with its Indian vendor that ends on December 31, 2020 with customary options for termination with a 30 day notice. The Indian vendor provides captive services to the Company and is paid on a cost plus basis. The Company paid following amounts to the Indian vendor for providing different classes of services:

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| Description of Cost         | Three Months<br>Ending<br>June 30, 2015 | Three Months<br>Ending<br>June 30, 2014 |
|-----------------------------|---|---|
| Client delivery and support | \$ 660,860                              | 808,557                                 |
| Platform development        | 585,000                                 | 360,000                                 |
| Sales support               | 43,250                                  | 38,294                                  |
| Back office support         | 522,870                                 | 388,833                                 |
| Research & Development      | 93,020                                  | 94,316                                  |
|                             | \$ 1,905,000                            | 1,690,000                               |

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### Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operation

The following discussion should be read in conjunction with our financial statements and notes thereto appearing elsewhere in this report.

#### CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION

This Form 10-Q for the quarter ending June 30, 2015 contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amending, and Section 21E of the Securities Exchange Act of 1934, as amending. Forward-looking statements may be identified by the use of forward-looking terminology, such as “may”, “shall”, “could”, “expect”, “estimate”, “anticipate”, “predict”, “probable”, “possible”, “should”, “continue”, or similar terms those terms or the negative of those terms. The forward-looking statements specified in the following information have been compiled by our management on the basis of assumptions made by management and are considered by management to be reasonable. Our future operating results, however, are impossible to predict and no representation, guaranty, or warranty is to be inferred from those forward-looking statements.

The assumptions used for purposes of the forward-looking statements specified in the following information represent estimates of future events and are subject to uncertainty as to possible changes in economic, legislative, industry, and other circumstances. As a result, the identification and interpretation of data and other information and their use in developing and selecting assumptions from and among reasonable alternatives require the exercise of judgment. To the extent that the assumed events do not occur, the outcome may vary substantially from anticipated or projected results, and, accordingly, no opinion is expressed on the achievability of those forward-looking statements. No assurance can be given that any of the assumptions relating to the forward-looking statements specified in the following information are accurate, and we assume no obligation to update any such forward-looking statements.

#### Overview

Quadrant 4 is a leading provider of cloud based Platform-as-a-Service (PaaS) and Software-as-a-Service (SaaS) products to the health insurance, media and education verticals. In addition, the Company provides expertise and relevant services that leverage our proprietary Social Media, Mobility, Analytics and Cloud (SMAC) technology stack. Our clients engage us to help them build more efficient operations; provide solutions to critical business and technology problems, and to help them drive technology-based innovation and growth. Our revenue is primarily generated from the sale and licensing of our PaaS and SaaS systems as well as from a wide range of technology oriented services and solutions. Our core platforms include QHIX, a cloud based health insurance exchange platform; QBLITZ, a cloud based digital media platform and QEDX, a cloud based education platform for K-12 students each of which incorporates our proprietary SMAC technologies. Our core services include Consulting, Application Life Cycle Management, Enterprise Applications & Data Management, Mobility Applications and Business Analytics. We blend these services with our technology platforms to offer client and industry specific solutions to the Healthcare, Media and Education industries.

#### Corporate History

Quadrant 4 System Corporation (sometimes referred to herein as “Quadrant 4” or the “Company”) was incorporated by the Florida Department of State on May 9, 1990 as Sun Express Group, Inc. and changed its name on March 31, 2011. The Company changed its domicile to Illinois on April 25, 2014.

#### Principal Business

The Company is engaged in the Information Technology sector as a provider of Platform-as-a-Service (PaaS) and Software-as-a-Service (SaaS) systems to the health insurance, media and education verticals. Along with these platforms, the company also provides relevant services that leverage our proprietary Social Media, Mobility, Analytics and Cloud (SMAC) technology stack. Our core services include Consulting, Application Life Cycle Management, Enterprise Applications & Data Management, Mobility Applications and Business Analytics. The Company blends these services with our technology platforms to offer client and industry specific solutions to the Healthcare, Media, and Education verticals.

#### Management's Discussion and Analysis of Financial Condition and Results of Operations

The nature of our model involves engaging employees and consultants to provide services to our customers with billing accrued and due in normal billing cycles. We also enter into subscription contracts for our software platforms that clients pay a fixed amount every month. We incur debt to meet payroll obligations, the largest component of our expenses, and service debt with the payments received from our customers. Many of our employees and consultants are assisted in the immigration process which is an expense component. The Company utilizes few major capital items in the delivery of its services and requires no significant plant expenses beyond ordinary commercial office space for both use by the employees on a limited basis and the back-office support for those employees.

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## Results of Operations

The revenues and expenses reflect the assets acquired and new businesses acquired during the past two years.

|                                     | Three months ending June 30, |               | Change       | Percent |
|-------------------------------------|------------------------------|---------------|--------------|---------|
|                                     | 2015                         | 2014          |              |         |
| Revenue                             | \$ 13,069,754                | \$ 11,917,170 | \$ 1,152,584 | 10%     |
| Cost of Revenue                     | (7,684,286)                  | (7,885,487)   | 201,201      | 3%      |
| Gross Margin                        | 5,385,468                    | 4,031,683     | 1,353,785    | 34%     |
| General and administrative expenses | (3,246,518)                  | (1,790,455)   | (1,456,063)  | (81%)   |
| Research & Development              | (469,795)                    | (537,995)     | 68,200       | 13%     |
| Amortization of intangible assets   | (1,020,357)                  | (1,397,461)   | 377,104      | 27%     |
| Interest and derivative expense     | (522,190)                    | (282,242)     | (239,948)    | (85%)   |
| Net Income/(loss)                   | \$ 126,608                   | \$ 23,530     | \$ 103,078   | 438%    |

|                                     | Six months ending June 30, |               | Change       | Percent |
|-------------------------------------|----------------------------|---------------|--------------|---------|
|                                     | 2015                       | 2014          |              |         |
| Revenue                             | \$ 26,708,400              | \$ 22,201,314 | \$ 4,507,086 | 20 %    |
| Cost of Revenue                     | (16,030,599)               | (14,718,265)  | (1,312,334)  | (9%)    |
| Gross Margin                        | 10,677,801                 | 7,483,049     | 3,194,752    | 43%     |
| General and administrative expenses | (6,045,858)                | (3,514,626)   | (2,531,232)  | (72%)   |
| Research & Development              | (1,040,023)                | (1,051,490)   | 11,467       | 1%      |
| Amortization of intangible assets   | (2,341,616)                | (2,722,255)   | 380,639      | 14%     |
| Interest and derivative expense     | (1,037,419)                | (675,454)     | (361,965)    | (54%)   |
| Net Income/(loss)                   | \$ 212,885                 | \$ (480,776)  | \$ 693,661   | 144%    |

## Comparison of Three Months and Six Months Ending June 30, 2015 and 2014

## REVENUES

Revenues for the three months ending June 30, 2015 totaled \$13,069,754 compared to \$11,917,170 during the same period in 2014. The increase in revenues of \$1,152,584 or 10% over the previous period was due to an increase in sales in the media group and as a result of the Brainchild acquisition. Revenues were comprised of service-related sales of software programming, consulting, subscriptions and development services.

Revenues for the six months ending June 30, 2015 totaled \$26,708,400 compared to \$22,201,314 during the same period in 2014. The increase in revenues of \$4,507,086 or 20% over the previous period was due to an increase in sales in the media group and as result of the Brainchild acquisition. Revenues were comprised of service-related sales of software programming, consulting, subscriptions and development services.

## COST OF REVENUES

Cost of revenue for the three months ending June 30, 2015 totaled \$7,684,286 compared to \$7,885,487 during the same period in 2014. The marginal decrease in cost of revenue of \$201,201 or 3% over the previous period was due to increased utilization and reduction of resources. Cost of revenue is comprised primarily of the direct costs of employee and contract labor and related expenses.

Cost of revenue for the six months ending June 30, 2015 totaled \$16,030,599 compared to cost of revenue of \$14,718,265 during the same period in 2014. The increase in cost of revenue of \$1,312,334 or 9% over the previous period was due to corresponding increase in revenues and the impact of the Brainchild acquisition during the first quarter of 2015. Cost of revenue is comprised primarily of the direct costs of employee and contract labor and related expenses.



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GROSS MARGIN

The increase in gross margin of \$1,353,785 or 34% for the three months ending June 30, 2015 over the previous three month period ending June 30, 2014 resulted primarily from increased revenues. The gross margin percentage increased to approximately 41% in the second quarter of 2015 from 34% in the same period of 2014 as a result of increased utilization of employees and sub-contractors.

The increase in gross margin of \$3,194,752 or 43% over the previous six month period ending June 30, 2014 resulted primarily from increased revenues. The gross margin percentage increased to approximately 40% in the six months ending June 30, 2015 from 34% in the same period of 2014

GENERAL AND ADMINISTRATIVE EXPENSES

General & administrative expenses for the three months ending June 30, 2015 totaled \$3,246,598 compared to general & administrative expenses of \$1,790,455 during the same period in 2014. The increase in general & administrative expenses of \$1,456,063 or 81% over the previous period was due to increased costs of building new vertical sales force during this period.

General & administrative expenses for the six months ending June 30, 2015 totaled \$6,045,858 compared to general & administrative expenses of \$3,514,626 during the same period in 2014. The increase in general & administrative expenses of \$2,531,232 or 72% over the previous six month period, was due to increased costs of building new vertical sales force during the six months ending June 30, 2015.

RESEARCH & DEVELOPMENT

Research & Development expenses for the three months ending June 30, 2015 totaled \$469,795 compared to Research & Development expenses of \$537,995 during the same period in 2014. The decrease in Research & Development expenses of \$68,200 or 13% over the previous second quarter was due to conversion of certain expenses to capitalized software development related to media units.

Research & Development expenses for the six months ending June 30, 2015 totaled \$1,040,023 compared to Research & Development expenses of \$1,051,490 during the same period in 2014. The decrease in Research & Development expenses of \$11,467 or 1% over the previous six month period, was due to conversion of certain expenses to capitalized software development related to media units.

AMORTIZATION AND WRITE-DOWN OF INTANGIBLE ASSETS

Amortization expense for the three months ending June 30, 2015 totaled \$1,020,357 compared to \$1,397,461 during the same period in 2014. The decrease in amortization expense of \$377,104 was due to completion of amortization of certain customer lists in the 2014 period. Amortization periods on the acquired intangibles range from 5 – 7 years.

Amortization expense for the six months ending June 30, 2015 totaled \$2,341,616 compared to \$2,722,255 during the same period in 2014. The decrease in amortization expense of \$380,639 was due to completion of amortization of certain customer lists in the 2014 period. Amortization periods on the acquired intangibles range from 5 – 7 years.

INTEREST EXPENSE

Interest expenses for the second quarter ending June 30, 2015 totaled \$522,190 compared to \$282,242 during the same period in 2014. The increase in interest expenses of \$239,948 or 85% over the previous second quarter was due to the

increase in notes payable and financing under the Revolver.

Interest expenses for the six months ending June 30, 2015 totaled \$1,037,419 compared to \$675,454 during the same period in 2014. The increase of \$361,965 or 54% over the previous six month period was due to the increase in notes payable and financing under the Revolver.

#### NET INCOME

The Company reported net income of \$126,608 for the three months ending June 30, 2015 compared to net income of \$23,530 for the same period in 2014. The increase of \$103,078 or 438 % over the previous period was the result of increased revenues and increased gross margins.

The Company reported net income of \$212,885 for the six months ending June 30, 2015 compared to net loss of \$480,776 for the same period in 2014. The increase in profit of \$740,162 or 154% over the previous six month period, was the result of increased revenues and increased gross margins.

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## EBITDA

Earnings before interest, taxes, depreciation and amortization (“EBITDA”) for the three month periods ending June 30, 2015 and June 30, 2014 is calculated as follows:

|                                       | June 30, 2015 | June 30, 2014 |
|---------------------------------------|---------------|---------------|
| Net Income (GAAP Basis)               | \$ 126,608    | \$ (23,530)   |
| Interest expense                      | 522,190       | 282,242       |
| Amortization and depreciation expense | 1,020,357     | 1,397,461     |
| Income Taxes                          | -             | -             |
| EBITDA                                | \$ 1,669,155  | \$ 1,703,233  |

Earnings before interest, taxes, depreciation and amortization (“EBITDA”) for the six months ending June 30, 2015 and June 30, 2014 is calculated as follows:

|                                       | June 30, 2015 | June 30, 2014 |
|---------------------------------------|---------------|---------------|
| Net Income/(Loss) (GAAP Basis)        | \$ 212,885    | \$ (480,776)  |
| Interest expense                      | 1,037,419     | 675,454       |
| Amortization and depreciation expense | 2,341,616     | 2,722,255     |
| Income Taxes                          | -             | -             |
| EBITDA                                | \$ 3,591,920  | \$ 2,916,933  |

Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA) for the three months ending June 30, 2015 decreased by \$34,078 or 2% over the previous three months and EBITDA for six months period ending June 30, 2015 increased by \$674,987 or 23% over the previous six-month period.

## LIQUIDITY AND CAPITAL RESOURCES

At June 30, 2015, we had an accumulated deficit of \$18,308,475 as compared to \$18,521,360 at December 31, 2014. As of June 30, 2015, we had a working capital deficit of \$1,761,440 as compared to working capital surplus of \$824,208 at December 31, 2014.

Net cash used by operations for the six months ending June 30, 2015 was \$974,637 as compared to \$553,227 primarily relating to the increases in Accounts receivable and software development costs, offset in part of by the increase in accounts payable.

Net cash used in investing activity for the six months ending June 30, 2015 was \$937,540 as compared to \$13,920 during the prior six months ending June 30, 2014. The increase was primarily due to acquisition of assets and purchase of computer assets during the first quarter of 2015.

Net cash provided in financing activities for the six months ending June 30, 2015 was \$261,342 as compared to \$60,238 primarily due to reduction of sales of common stock in the 2015 period.

Liquidity. The Company is continuing to expand its IT business operations through acquisitions and organic internal growth. Acquisitions of target company assets will require additional financing. Currently the Company anticipates that additional financing to fund these acquisitions of assets will be provided by sales of stock or borrowings. Also, the Company is exploring alternatives for its trade receivable factoring which carries a very high interest rate. Refinancing of this receivable factoring financing will reduce the Company’s interest expenses thereby increasing the Company’s liquidity position.

The Company is currently discussing with the lenders whose loans are coming due within the next year to extend their terms. The Company believes its resources are adequate to fund its current operations for the next 12 months.

#### Off Balance Sheet Arrangements

There are no off balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that are material to investors.

#### Impact of Inflation

We believe that inflation has not had a material impact on our results of operations for the six months ending June 30, 2015. We cannot assure you that future inflation will not have an adverse impact on our operating results and financial condition.

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Item 3. Quantitative and Qualitative Disclosures about Market Risk

Not required.

Item 4. Controls and Procedures

Disclosure Controls and Procedures

The Company's management, with the participation of the Company's principal executive officer and principal financial officer, respectively, has evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this report which is June 30, 2015. Based on such evaluation, the Company's principal executive officer and principal financial officer, respectively, have concluded that, as of the end of such period, the Company's disclosure controls and procedures specific to certain transactions were not effective. Rapid growth and inadequate staffing were the main reasons for such ineffective controls. Management has identified an action plan to remedy any ineffective controls that include additional staffing, realignment of existing staff, a search to hire a Chief Financial Officer, hiring of an outside consultant to assist with internal controls and creating a well-defined financial and accounting control matrix and procedures document which is in the process of being implemented.

Management's Report on Internal Control Over Financial Reporting

The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is defined in Rule 13a-15(f) and 15d-15(f) under the 1934 Act as a process designed by, or under the supervision of, the Company's principal executive officer and principal financial officer, respectively, and effected by the Company's management and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that:

- pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of assets;
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of consolidated financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures are being made only in accordance with authorizations of the Company's management; and
  - provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of assets that could have a material effect on the consolidated financial statements

Management is committed to continuous improvement in all areas of controls and procedures. The Company has instituted additional procedures to review its interim financial statements and significant transactions with the audit committee on a regular basis.

Based on this evaluation, our management concluded that our internal controls over financial reporting were not operating effectively as of June 30, 2015.

Changes in Internal Control Over Financial Reporting.

In order to address certain separation of duties and governance issues the Company has added additional human resources as well as a realignment of existing staff in its accounting and finance departments and instituted additional

procedures to review its interim financial statements and significant transactions with the audit committee on a regular basis in the spirit of continuing to improve internally.

These additions have improved accountability and created segregation of responsibilities across additional people which has resulted in improvement in the Company's internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the 1934 Act) subsequent to the year ending December 31, 2014.

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PART II. OTHER INFORMATION

Item 1. Legal Proceedings

On May 13, 2014, a claim was filed against the Company in the Superior Court of California, County of Santa Clara arising from a collections dispute related to vendors of an acquisition target of the Company. All Plaintiffs were vendors of the target and are seeking recovery of approximately \$222,000. The Company is vigorously defending their position and it is expected that the court case will remain stayed until the earliest being fall 2015. In response to the claim, as of December 31, 2014 the Company has recorded an accrual in the event of legal settlement in the amount of \$123,000.

Item 1A. Risk Factors

Not required.

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

None

Item 3. Defaults Upon Senior Securities

None

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None

Item 6. Exhibits

Item 601 of Regulation S-K

| Exhibit No.: | Exhibit   |
|--------------|---|
| 31.1         | <u>Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer of the Company</u>   |
| 31.2         | <u>Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer of the Company</u>   |
| 32.1         | <u>Section 1350 Certification by Chief Executive Officer and Chief Financial Officer</u>  |
| 101          | The following financial information from Quadrant 4 System Corporation's Quarterly Report on Form 10-Q for the quarter ending June 30, 2015, formatted in XBRL (eXtensible Business Reporting Language): (i) Consolidated Balance Sheets at June 30, 2015 |

(unaudited) and December 31, 2014; (ii) Consolidated Statements of Income (Unaudited) for the three and six months ending June 30, 2015 and 2014, (iii) Consolidated Statements of Cash Flows (Unaudited) for the six months ending June 30, 2015 and 2014.



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SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

QUADRANT 4 SYSTEM CORPORATION

September 18, 2015

By:

/s/ Dhru Desai

Dhru Desai  
Chief Financial Officer and Director

