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

FORM 10-Q

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

For the quarterly period ended **November 30, 2019**

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

For the transition period from _______ to _______

SEC File No. 024-10557

SHIFTPIXY, INC.

(Exact name of registrant as specified in its charter)

Wyoming	**47-4211438**
(State of incorporation or organization)	(I.R.S. Employer Identification No.)
1 Venture Suite 150, Irvine CA	**92618**
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number: **(888) 798-9100**

N/A
(Former name, former address and former three months, if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer", "accelerated filer", "non-accelerated filer", "smaller reporting company", and "emerging growth company" in Rule 12b-2 of the Exchange Act.

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

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

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

The number of shares of the registrant's only class of common stock issued and outstanding as of January 20, 2020, was 1,020,050.

TABLE OF CONTENTS

Table of Contents

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS AND INFORMATION

This Quarterly Report on Form 10-Q, the other reports, statements, and information that we have previously filed or that we may subsequently file with the Securities and Exchange Commission ("SEC"), and public announcements that we have previously made or may subsequently make include, may include, incorporate by reference or may incorporate by reference certain statements that may be deemed to be "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995 and are intended to enjoy the benefits of that act. Unless the context is otherwise, the forward-looking statements included or incorporated by reference in this Form 10-Q and those reports, statements, information and announcements address activities, events or developments that ShiftPixy, Inc. (hereinafter referred to as "we," "us," "our," "our Company" or "ShiftPixy") expects or anticipates, will or may occur in the future. Any statements in this document about expectations, beliefs, plans, objectives, assumptions or future events or performance are not historical facts and are forward-looking statements. These statements are often, but not always, made through the use of words or phrases such as "may," "should," "could," "predict," "potential," "believe," "will likely result," "expect," "will continue," "anticipate," "seek," "estimate," "intend," "plan," "projection," "would" and "outlook," and similar expressions. Accordingly, these statements involve estimates, assumptions and uncertainties, which could cause actual results to differ materially from those expressed in them. Any forward-looking statements are qualified in their entirety by reference to the factors discussed throughout this document. All forward-looking statements concerning economic conditions, rates of growth, rates of income or values as may be included in this document are based on information available to us on the dates noted, and we assume no obligation to update any such forward-looking statements. It is important to note that our actual results may differ materially from those in such forward-looking statements due to fluctuations in interest rates, inflation, government regulations, economic conditions and competitive product and pricing pressures in the geographic and business areas in which we conduct operations, including our plans, objectives, expectations and intentions and other factors discussed elsewhere in this Report.

Certain risk factors could materially and adversely affect our business, financial conditions and results of operations and cause actual results or outcomes to differ materially from those expressed in any forward-looking statements made by us, and you should not place undue reliance on any such forward-looking statements. Any forward-looking statement speaks only as of the date on which it is made and we do not undertake any obligation to update any forward-looking statement or statements to reflect events or circumstances after the date on which such statement is made or to reflect the occurrence of unanticipated events. The risks and uncertainties we currently face are not the only ones we face. New factors emerge from time to time, and it is not possible for us to predict which will arise. There may be additional risks not presently known to us or that we currently believe are immaterial to our business. In addition, we cannot assess the impact of each factor on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements. If any such risks occur, our business, operating results, liquidity and financial condition could be materially affected in an adverse manner. Under such circumstances, you may lose all or part of your investment.

The industry and market data contained in this report are based either on our management's own estimates or, where indicated, independent industry publications, reports by governmental agencies or market research firms or other published independent sources and, in each case, are believed by our management to be reasonable estimates. However, industry and market data is subject to change and cannot always be verified with complete certainty due to limits on the availability and reliability of raw data, the voluntary nature of the data gathering process and other limitations and uncertainties inherent in any statistical survey of market shares. We have not independently verified market and industry data from third-party sources. In addition, consumption patterns and customer preferences can and do change. As a result, you should be aware that market share, ranking and other similar data set forth herein, and estimates and beliefs based on such data, may not be verifiable or reliable.

Our Management's Discussion & Analysis of Financial Condition and Results of Operations (MD&A) includes references to our performance measures presented in accordance with U.S. Generally Accepted Accounting Principles (GAAP) and other non-GAAP financial measures that we use to manage our business, make planning decisions and allocate resources. Refer to the Non-GAAP Financial Measures within our MD&A for definitions and reconciliations from GAAP measures.

PART I — FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

ShiftPixy, Inc.
Condensed Consolidated Balance Sheets

	November 30, 2019 (Unaudited)	August 31, 2019
ASSETS		
Current assets		
Cash	$ 49,000	$ 1,561,000
Accounts receivable	1,822,000	272,000
Unbilled accounts receivable	11,347,000	9,478,000
Deposit – workers' compensation	1,987,000	1,957,000
Prepaid expenses	371,000	519,000
Other current assets	164,000	244,000
Total current assets	15,740,000	14,031,000
Fixed assets, net	3,136,000	3,360,000
Deposits – workers' compensation	6,167,000	6,281,000
Deposits and other assets	124,000	124,000
Total assets	$ 25,167,000	$ 23,796,000
LIABILITIES AND STOCKHOLDERS' DEFICIT		
Current liabilities		
Accounts payable and other current liabilities	$ 5,911,000	$ 4,911,000
Payroll related liabilities	17,469,000	16,412,000
Convertible notes, net	3,426,000	3,351,000
Accrued workers' compensation costs	1,987,000	1,957,000
Default penalties accrual	1,800,000	1,800,000
Derivative Liability	2,814,000	3,756,000
Total current liabilities	33,407,000	32,187,000
Non-current liabilities		
Accrued workers' compensation costs	6,194,000	4,379,000
Convertible notes, net	778,000	-
Total liabilities	40,379,000	36,566,000
Commitments and contingencies		
Stockholders' deficit		
Preferred stock, 50,000,000 authorized shares; $0.0001 par value	-	-
Common stock, 750,000,000 authorized shares; $0.0001 par value; 907,047 shares issued as of November 30, 2019 and August 31, 2019	-	-
Additional paid-in capital	32,619,000	32,505,000
Treasury stock, at cost-13,953 shares as of November 30, 2019 and August 31, 2019	(325,000)	(325,000)
Accumulated deficit	(47,506,000)	(44,950,000)
Total stockholders' deficit	(15,212,000)	(12,770,000)
Total liabilities and stockholders' deficit	$ 25,167,000	$ 23,796,000

See accompanying notes to the unaudited interim condensed consolidated financial statements.

ShiftPixy Inc.
Condensed Consolidated Statements of Operations
(Unaudited)

	For the Three Months Ended November 30, 2019	2018
Revenues (gross billings of $110.7 million and $70.9 million less worksite employee payroll cost of $94.8 million and $60.4 million, respectively)	$ 15,866,000	$ 10,520,000
Cost of revenue	12,552,000	7,134,000
Gross profit	3,314,000	3,386,000
Operating expenses:		
Salaries, wages and payroll taxes	2,283,000	1,872,000
Commissions	774,000	553,000
Professional fees	840,000	624,000
External Software development	353,000	310,000
General and administrative	1,401,000	1,316,000
Total operating expenses	5,651,000	4,675,000
Operating Loss	(2,337,000)	(1,289,000)
Other income (expense)		
Interest expense	(1,161,000)	(957,000)
Change in fair value of derivative liability	942,000	-
Total other income (expense)	(219,000)	(957,000)
Net Loss	$ (2,556,000)	$ (2,246,000)
Net loss per common share		
Basic and diluted	$ (2.86)	$ (3.11)
Weighted average number of common shares		
Basic and diluted	893,094	723,033

See accompanying notes to the unaudited interim condensed consolidated financial statements.

ShiftPixy Inc.
Condensed Consolidated Statements of Stockholders' Deficit
For the Three Months Ended November 30, 2019 and 2018 (Unaudited)

	Common Stock Issued		Additional Paid-In Capital	Treasury Stock	Accumulated Deficit	Total Stockholders' Deficit
	Shares	Amount				
Balance, September 1, 2019	907,047	$ -	$ 32,505,000	(325,000)	$ (44,950,000)	$ (12,770,000)
Stock-based compensation expense	-	-	114,000	-	-	114,000
Net Loss	-	-	-	-	(2,556,000)	(2,556,000)
Balance, November 30, 2019	907,047	$ -	$ 32,619,000	(325,000)	$ (47,506,000)	$ (15,212,000)

	Common Stock Issued		Additional Paid-In Capital	Accumulated Deficit	Total Stockholders' Deficit
	Shares	Amount			
Balance, September 1, 2018	721,295	$ -	$ 18,468,000	$ (26,223,000)	$ (7,755,000)
Warrants exercised for cash	6,688	-	660,000	-	660,000
Common stock issued for services rendered	966	-	113,000	-	113,000
Stock-based compensation expense	-	-	77,000	-	77,000
Common shares issued upon conversion of convertible notes and interest	16,624	-	1,645,000	-	1,645,000
Net Loss	-	-	-	(2,246,000)	(2,246,000)
Balance, November 30, 2018	745,573	$ -	$ 20,963,000	$ (28,469,000)	$ (7,506,000)

See accompanying notes to the unaudited interim condensed consolidated financial statements.

Table of Contents

ShiftPixy, Inc.
Condensed Consolidated Statements of Cash Flows
(Unaudited)

	For the Three Months Ended November 30, 2019	For the Three Months Ended November 30, 2018
OPERATING ACTIVITIES		
Net Loss	$ (2,556,000)	$ (2,246,000)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	241,000	188,000
Amortization debt discount, debt issuance cost	854,000	1,044,000
Share based compensation	114,000	190,000
Gain on fair value of derivative liabilities	(942,000)	-
Changes in operating assets and liabilities		
Accounts receivable	(1,550,000)	(19,000)
Unbilled accounts receivable	(4,469,000)	1,434,000
Prepaid expenses	148,000	184,000
Other current assets	81,000	(93,000)
Deposits – workers' compensation	82,000	(892,000)
Deposits and other assets	-	26,000
Accounts payable	739,000	240,000
Payroll related liabilities	3,656,000	(1,988,000)
Accrued workers' compensation	1,847,000	1,068,000
Other current liabilities	260,000	(726,000)
Net cash used in operating activities	(1,495,000)	(1,590,000)
INVESTING ACTIVITIES		
Purchase of fixed assets	(17,000)	(493,000)
Net cash used in investing activities	(17,000)	(493,000)
FINANCING ACTIVITIES		
Proceeds from exercise of warrants	-	660,000
Net cash provided by financing activities	-	660,000
Net decrease in cash	(1,512,000)	(1,423,000)
Cash - Beginning of Period	1,561,000	1,650,000
Cash - End of Period	$ 49,000	$ 227,000
Supplemental Disclosure of Cash Flows Information:		
Cash paid for interest	-	133,000

Non-cash Investing and Financing Activities:		
Conversion of debt and accrued interest into common stock	-	1,645,000

See accompanying notes to the unaudited interim condensed consolidated financial statements.

ShiftPixy, Inc.
Notes to the Condensed Consolidated Financial Statements
(Unaudited)

Note 1: Nature of Operations

ShiftPixy, Inc. (the "Company") was incorporated on June 3, 2015. The Company is a specialized staffing service provider that provides solutions for large contingent part-time workforce demands, primarily in the restaurant, hospitality and maintenance service trades. The Company's focus is on the restaurant industry in Southern California.

Both ShiftPixy, Inc and its wholly-owned subsidiary, Shift Human Capital Management Inc. ("SHCM"), function as an employment administrative services ("EAS") provider including services such as administrative and processing services, performing functions in the nature of a payroll processor, human resources consultant, administrator of workers' compensation coverages and claims and provides workers compensation coverage written in the names of the clients (as may be required by some states). The Company has built a human resources information systems platform to assist in customer acquisition and hopes that this mechanism may become a way to onboard new clients into the ShiftPixy Ecosystem when eligible clients recognize the value of the services provided by the parent Company.

The Company is currently operating in one reportable segment.

Note 2: Summary of significant accounting policies

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") and the rules of the Securities and Exchange Commission ("SEC") applicable to interim reports of companies filing as a smaller reporting company. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for fair presentation have been included. The results of operations for the three months ended November 30, 2019, are not necessarily indicative of the results that may be expected for the year ending August 31, 2020.

For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's annual report on Form 10-K for the year ended August 31, 2019, filed with the SEC on December 13, 2019.

Principles of Consolidation

The Company and its wholly-owned subsidiary have been consolidated in the accompanying unaudited condensed consolidated financial statements. All intercompany balances have been eliminated in consolidation.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires the Company to make estimates and assumptions that affect certain reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates include:

- Liability for legal contingencies;
- Useful lives of property and equipment;
- Assumptions made in valuing embedded derivatives and freestanding equity-linked instruments classified as liabilities;
- Deferred income taxes and related valuation allowance; and
- Projected development of workers' compensation claims.

Revenue and Direct Cost Recognition

The Company provides an array of human resources and business solutions designed to help improve business performance.

The Company accounts for its EAS revenues in accordance with Accounting Standards Codification ("ASC") 605-45,*Revenue Recognition, Principal Agent Considerations*. EAS solutions revenue is primarily derived from the Company's gross billings, which are based on (i) the payroll cost of the Company's worksite employees and (ii) a mark-up computed as a percentage of payroll costs for payroll taxes and workers compensation premiums.

The Company's revenues are primarily attributable to fees for providing staffing solutions and EAS/HCM ("Employment Administration Services"/ "Human Capital Management") services. The Company recognizes revenue when all of the following criteria are met: (i) persuasive evidence of an arrangement exists; (ii) the services have been rendered to the customer; (iii) the sales price is fixed or determinable, and (iv) collectability is reasonably assured. The Company enters into contracts with its clients for EAS services based on a stated rate and price in the contract. Contracts generally have a term of 12 months but are cancellable at any time by either party with 30 days' notice. Contract performance obligations are satisfied as services are rendered and the term between invoicing and when the performance obligations are satisfied is not significant. The Company does not have significant financing components or significant payment terms for its customers and consequently has no material credit losses.

Gross billings are invoiced to each client concurrently with each periodic payroll of the Company's worksite employees which coincides with the services provided and which is typically a fixed percentage of the payroll processed. Revenues, which exclude the payroll cost component of gross billings and therefore consist solely of markup are recognized ratably over the payroll period as worksite employees perform their service at the client worksite. Revenues that have been recognized but not invoiced are included in unbilled accounts receivable on the Company's consolidated balance sheets and were $11,347,000 and $9,478,000 as of November 30, 2019 and August 31, 2019, respectively.

Consistent with the Company's revenue recognition policy, direct costs do not include the payroll cost of its worksite employees. The cost of revenue associated with the Company's revenue generating activities is primarily comprised of all other costs related to its worksite employees, such as the employer portion of payroll-related taxes, employee benefit plan premiums and workers' compensation insurance costs.

The Company has evaluated its revenue recognition policies in conjunction with its future expected business which may be migrating to a staffing business model. For fiscal years 2020 and 2019, there were no revenues which should have been evaluated under a staffing business model. Such a staffing business model would have included the payroll costs in revenues with a corresponding increase to cost of revenues for payroll costs associated with staffing services.

The Company reviewed the costs associated with acquiring its customers under ASC 340-10 *Other Assets and Deferred Costs* and determined that no such costs should be capitalized. Costs relating to its customers are typically commissions paid as a percentage of some of the Company's revenue components and are expensed as they are incurred because the terms of its contracts generally are cancellable by either party with a 30-day notice. These costs are recorded in commissions in the Consolidated Statement of Operations.

Concentration of Credit Risk

The Company considers all highly liquid investments with an original maturity of three months or less when purchased as cash equivalents. The Company maintains cash with a commercial bank and from time to time exceed the federally insured limits. The Company has not experienced losses from these deposits.

No one individual client represents more than 10% of revenues for the three months ended November 30, 2019, and 2018, respectively. However, four clients represent 92% of total accounts receivable both at November 30, 2019 and August 31, 2019.

Impairment and Disposal of Long-Lived Assets

The Company periodically evaluates its long-lived assets for impairment in accordance with ASC 360-10, *Property, Plant, and Equipment*. ASC 360-10 requires that an impairment loss be recognized for assets to be disposed of or held-for-use when the carrying amount of an asset is deemed to not be recoverable. If events or circumstances were to indicate that any of our long-lived assets might be impaired, the Company would assess recoverability based on the estimated undiscounted future cash flows to be generated from the applicable asset. In addition, the Company may record an impairment loss to the extent that the carrying value of the asset exceeded the fair value of the asset. Fair value is generally determined using an estimate of discounted future net cash flows from operating activities or upon disposal of the asset. There were no impairments recognized for the periods ended November 30, 2019, and 2018.

[Table of Contents](#)

Workers' compensation

Everest Program

Up to July 2018, a portion of the Company's workers' compensation risk was covered by a retrospective rated policy, which calculates the final policy premium based on the Company's loss experience during the term of the policy and the stipulated formula set forth in the policy. The Company funds the policy premium based on standard premium rates on a monthly basis and based on the gross payroll applicable to workers covered by the policy. During the policy term and thereafter, periodic adjustments may involve either a return of previously paid premiums or a payment of additional premiums by the Company or a combination of both. If the Company's losses under that policy exceed the expected losses under that policy, then the Company could receive a demand for additional premium payments.

The Company utilizes a third-party to estimate its loss development rate, which is based primarily upon the nature of worksite employees' job responsibilities, the location of worksite employees, the historical frequency and severity of workers' compensation claims, and an estimate of future cost trends. Each reporting period, changes in the assumptions resulting from changes in actual claims experience and other trends are incorporated into its workers' compensation claims cost estimates. As of November 30, 2019, the Company classified \$0.2 million in short term accrued workers' compensation and \$0.3 million in long term accrued workers' compensation in the Company's consolidated balance sheets.

Sunz Program

Starting in July 2018, the Company's workers' compensation program for its worksite employees has been provided through an arrangement with United Wisconsin Insurance Company ("UWIC") and administered by Sunz. Under this program, the Company has financial responsibility for the first \$0.5 million of claims per occurrence. The Company provides and maintains a loss fund that will be used to pay claims and claim related expenses. The workers' compensation insurance carrier established monthly funding requirements comprised of premium costs and funds to be set aside for payment of future claims ("claim loss funds"). The level of claim loss funds is primarily based upon anticipated worksite employee payroll levels and expected worker's compensation loss rates, as determined by the insurance carrier. Monies funded into the program for incurred claims expected to be paid within one year are recorded as Deposit - workers' compensation, a short-term asset, while the remainder of claim funds are included in deposits- workers' compensation, a long-term asset in its consolidated balance sheets.

As of November 30, 2019, the Company had \$2.0 million in deposit – workers' compensation classified as a short-term asset and \$6.2 million classified as a long-term asset.

The Company's estimate of incurred claim costs expected to be paid within one year is included in short-term liabilities, while its estimate of incurred claim costs expected to be paid beyond one year is included in long-term liabilities on its consolidated balance sheets. As of November 30, 2019, the

Company had short term accrued workers' compensation costs of $1.8 million and long term accrued workers' compensation costs of $5.9 million.

Because the Company bears the financial responsibility for claims up to the level noted above, such claims, which are the primary component of its workers' compensation costs, are recorded in the period incurred. Workers' compensation insurance includes ongoing health care and indemnity coverage whereby claims are paid over numerous years following the date of injury. Accordingly, the accrual of related incurred costs in each reporting period includes estimates, which takes into account the ongoing development of claims and therefore requires a significant level of judgment. In estimating ultimate loss rates, the Company utilizes historical loss experience, exposure data, and actuarial judgment, together with a range of inputs which are primarily based upon the worksite employee's job responsibilities, their location, the historical frequency and severity of workers' compensation claims, and an estimate of future cost trends. For each reporting period, changes in the actuarial assumptions resulting from changes in actual claims experience and other trends are incorporated into its workers' compensation claims cost estimates. The estimated incurred claims are based upon: (i) the level of claims processed during each quarter; (ii) estimated completion rates based upon recent claim development patterns under the plan; and (iii) the number of participants in the plan.

Fair Value of Financial Instruments

FASB ASC 825, "Financial Instruments," requires entities to disclose the fair value of financial instruments, both assets and liabilities recognized and not recognized on the balance sheet, for which it is practical to estimate fair value. FASB 825 defines fair value of a financial instrument as the amount at which the instrument could be exchanged in a current transaction between willing parties. At November 30, 2019 and August 31, 2019, the carrying value of certain financial instruments (cash, accounts receivable and payable, and other financial instruments) approximates fair value due to the short-term nature of the instruments. Convertible notes approximate fair value based on comparison of terms from similar instruments in the marketplace.

The Company measures fair value under a framework that utilizes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements). The three levels of inputs which prioritize the inputs used in measuring fair value are:

- Level 1: Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Company has the ability to access.

- Level 2: Inputs to the valuation methodology include:

  - Quoted prices for similar assets or liabilities in active markets;

  - Quoted prices for identical or similar assets or liabilities in inactive markets

  - Inputs other than quoted prices that are observable for the asset or liability;

  - Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

  - If the asset or liability has a specified (contractual) term, the level 2 input must be observable for substantially the full term of the asset or liability

- Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The Company did not have any Level 1 or Level 2 assets and liabilities at November 30, 2019 or August 31, 2019. The derivative liabilities associated with its March 2019 Convertible Notes (see Note 4), consisted of conversion feature derivatives and warrants, are Level 3 fair value measurements.

The table below sets forth a summary of the changes in the fair value of the Company's derivative liabilities classified as Level 3 as of November 30, 2019:

	March 2019 Conversion Feature	March 2019 Warrant Liability	Total
Balance at August 31, 2019	$ 2,852,000	904,000	$ 3,756,000
Change in fair value	(340,000)	(602,000)	(942,000)
Balance at November 30, 2019 (unaudited)	$ 2,512,000	302,000	$ 2,814,000

At November 30, 2019 and August 31, 2019, the Company estimated the fair value of the conversion feature derivatives embedded in the convertible debentures and the fair value of the warrant liabilities based on weighted probabilities of assumptions used in the Lattice-based option valuation model. The key valuation assumptions used consists, in part, of the price of the Company's common stock, a risk free interest rate based on the average yield of a Treasury note and expected volatility of the Company's common stock all as of the measurement dates, and the various estimated reset exercise prices weighted by probability.

The Company used the following assumptions to estimate fair value of the derivatives as of November 30, 2019, using the default rate of 75% of market price as a conversion price:

	March 2019 Conversion Feature (unaudited)	March 2019 Warrant Liability (unaudited)
Risk free rate	1.60%	1.62%
Market price per share	$ 10.20	$ 10.20
Life of instrument in years	0.79	4.28
Volatility	91%	102%
Dividend yield	0%	0%

When the Company changes its valuation inputs for measuring financial assets and liabilities at fair value, either due to changes in current market conditions or other factors, it may need to transfer those assets or liabilities to another level in the hierarchy based on the new inputs used. The Company recognizes these transfers at the end of the reporting period that the transfers occur. For the periods ended November 30, 2019 or 2018, there were no transfers of financial assets or financial liabilities between the hierarchy levels.

Research and Development

During the three months ended November 30, 2019 and 2018 the Company incurred research and development costs of approximately $0.9 million and $0.4 million, respectively. All costs were related to internally developed or externally contracted software and related technology for the Company's HRIS system and related mobile application. In addition, $0 and $0.4 million of software costs were capitalized for the three months ended November 30, 2019 and 2018, respectively.

Advertising Costs

The Company expenses all advertising as incurred. The Company incurred advertising costs totaling $304,000 and $379,000 for the three months ended November 30, 2019, and 2018, respectively.

Reverse Stock Split

On December 17, 2019 the Company implemented a 1 for 40 reverse stock split for all common share and common share equivalents including, options, warrants, and convertible notes. All common shares and common share equivalents are presented retroactively to reflect the reverse split.

Earnings (Loss) Per Share

The Company utilizes Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 260, "Earnings per Share." Basic earnings (loss) per share is computed by dividing earnings (loss) attributable to common stockholders by the weighted-average number of common shares outstanding during the reporting period. Diluted earnings (loss) per share is computed similar to basic earnings (loss) per share except that the denominator is increased to include additional common share equivalents available upon exercise of stock options and warrants using the treasury stock method. Dilutive common share equivalents include the dilutive effect of in-the-money share equivalents, which are calculated based on the average share price for each period using the treasury stock method, excluding any common share equivalents if their effect would be anti-dilutive.

Securities that are excluded from the calculation of weighted average dilutive common shares, because their inclusion would have been antidilutive are:

	For the Three Months Ended November 30, 2019	For the Three Months Ended November 30, 2018
Options	45,463	37,271
Senior Secured Convertible Notes	889,935	84,756
Warrants	107,416	87,783
Total potentially dilutive shares	1,042,814	209,810

Stock-Based Compensation

At November 30, 2019, the Company has one stock-based compensation plan under which the Company may issue awards. The Company accounts for this plan under the recognition and measurement principles of ASC 718, *Compensation- Stock Compensation*, which requires all share-based payments to employees, including grants of employee stock options, to be recognized in the condensed consolidated statements of operations on their fair values.

The grant date fair value is determined using the Black-Scholes-Merton ("Black-Scholes") pricing model. For all employee stock options, the Company recognizes expense over the requisite service period on an accelerated basis over the employee's requisite service period (generally the vesting period of the equity grant).

The Company's option pricing model requires the input of highly subjective assumptions, including the expected stock price volatility and expected term. The expected volatility is based on the historical volatility of the Company since our Initial Public Offering. Any changes in these highly subjective assumptions significantly impact stock-based compensation expense.

The Company elected to account for forfeitures as they occur, as such, compensation cost previously recognized for an unvested award that is forfeited because of the failure to satisfy a service condition is revised in the period of forfeiture.

Treasury Stock

Treasury stock represents shares of common stock provided to the company in satisfaction of the related party advance, described in Note 13. Shares provided are recorded at cost as treasury stock. The Company intends to retire all of its treasury stock outstanding as of November 30, 2019 and August 31, 2019 in fiscal 2020. Any treasury stock retired is recorded to additional paid-in capital, limited to the amount previously credited to additional paid-in capital, if any. Any excess is charged to accumulated deficit.

Reclassifications

Certain reclassifications have been made to prior year's data to confirm to the current year's presentation. Such reclassifications had no impact on the Company's financial condition, operating results, cash flows or stockholder's equity.

Revision of Financial Statements

During the preparation of the restated condensed consolidated financial statements for the three and six months ended February 28, 2019, the Company determined that it had improperly calculated the volatility of the Company's common stock, which had been used to calculate the relative fair value of the warrants issued in connection with the June 2018 convertible notes. This resulted in an overstatement of the net carrying amount of the convertible note by the understatement of the corresponding debt discount with the offset to additional paid-in capital as of February 28, 2019. The Company assessed the materiality of the misstatements in accordance with Staff Accounting Bulletin No.99, "Materiality" and No. 108, "Quantifying Misstatements", and concluded that this error was not qualitatively material on the Company's condensed consolidated balance sheet, statements of operations, statements of cash flows, statement of stockholders' deficit and net loss for the periods then ended.

The effect of this revision on the line items within the Company's condensed financial statements as of and for the three months ended November 30, 2018, was as follows:

	November 30, 2018		
	As Previously Reported	Adjustments	As Restated
Convertible note, net	$ 6,309,000	(739,000)	$ 5,570,000
Additional Paid-In Capital	19,729,000	1,232,000	20,961,000
Accumulated deficit	(27,977,000)	(493,000)	(28,470,000)
Net Loss	(2,000,000)	(246,000)	(2,246,000)
Net loss per share – Basic and diluted	(2.77)	(0.34)	(3.11)

Recent Accounting Standards

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606), which outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The core principle of the revenue model is that "an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services." The standard provides enhancements to the quality and consistency of how revenue is reported by companies, while also improving comparability in the financial statements of companies reporting using International Financial Reporting Standards or U.S. GAAP. The new standard also will require enhanced revenue disclosures, provide guidance for transactions that were not previously addressed comprehensively, and improve guidance for multiple-element arrangements. This accounting standard becomes effective for the Company for reporting periods beginning after December 15, 2018, and interim reporting periods within annual reporting periods beginning after December 15, 2019. Early adoption is permitted for annual reporting periods (including interim periods) beginning after December 15, 2016. This new standard permits the use of either the retrospective or cumulative effect transition method.

In March 2016, the FASB issued ASU No. 2016-08, Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations. The purpose of this standard is to clarify the implementation of guidance on principal versus agent considerations related to ASU 2014-09. The standard has the same effective date as ASU 2014-09 described above.

In April 2016, the FASB issued ASU No. 2016-10, Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing, which provides clarity related to ASU 2014-09 regarding identifying performance obligations and licensing implementation. The standard has the same effective date as ASU 2014-09 described above.

In May 2016, the FASB issued ASU 2016-12: Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients, which provides narrow scope improvements and practical expedients related to ASU 2014-09. The purpose of this standard is to clarify certain narrow aspects of ASU 2014-09, such as assessing the collectability criterion, presentation of sales taxes, and other similar taxes collected from customers, noncash considerations, contract modifications at transition, completed contracts are transition, and technical correction. The standard has the same effective date as ASU 2014-09 described above.

In December 2016, the FASB issued ASU 2016-20: Technical Corrections and Improvements to Topic 606, Revenue from Contracts with Customers. The amendments in this standard affect narrow aspects of guidance issued in ASU 2014-09. The standard has the same effective date as ASU 2014-09 described above. Topic 606 is effective for the company beginning with the fiscal year ending August 31, 2020.

The Company is evaluating the effect of adopting this new accounting guidance and is currently finalizing its analysis of the financial impact of the adoption. The Company expects to adopt the guidance using the modified retrospective method.

Note 3: Going Concern

As of November 30, 2019, the Company had cash of $0.1 million and a working capital deficiency of $18.5 million. During the quarter ended November 30, 2019, the Company used approximately $1.5 million of cash in its operations, consisting of a net loss of $2.6 million, reduced by net non-cash charges and gains of $0.3 million and working capital changes of $0.8 million. During the year ended August 31, 2019, the Company used approximately $2.1 million of cash in its operations, consisting of a net loss of $18.7 million, reduced by net non-cash charges and gains of $10.8 million and working capital changes of $6.0 million. The Company has incurred recurring losses resulted in an accumulated deficit of $48 million as of November 30, 2019. These conditions raise substantial doubt as to the Company's ability to continue as going concern within one year from issuance date of the financial statements.

The ability of the Company to continue as a going concern is dependent upon generating profitable operations in the future and obtaining additional funds by way of public or private offering to meet the Company's obligations and repay its liabilities when they become due. The Company has a recurring revenue business model that generated $12.4 million of gross profit for the year ended August 31, 2019 and $3.3 million for the quarter ended November 30, 2019.

The Company's plans and expectations for the next 12 months include raising additional capital to help fund expansion of its operations, including the continued development and support of its IT and HR platform and settling its outstanding debt as it comes due. The Company engaged an investment banking firm to assist the Company in (i) preparing information materials, (ii) advising the Company concerning the structure, price and conditions and (iii) organizing the marketing efforts with potential investors in connection with a financing transaction.

Historically, the Company's principal source of financing has come through the sale of its common stock and issuance of convertible notes. The Company successfully completed an Initial Public Offering (IPO) on NASDAQ on June 29, 2017, raising a total of $12 million ($10.9 million net of costs). In June 2018, the Company completed a private placement of 8% senior secured convertible notes to institutional investors raising $9 million of gross proceeds ($8.4 million net of costs). In March 2019, the Company completed a private placement of senior secured notes to institutional investors raising $3.75 million ($3.3 million net of costs). As of November 30, 2019 all of the $6.8 million of principal was in default. Subsequent to November 30, 2019, approximately $2.7 million of the notes in default were exchanged for new convertible notes payable. See Notes 4 and 9 for additional information.

Subsequent to November 30, 2019 and as described in Note 9 below, in January 2020, the Company assigned approximately 60% of its customer contracts representing approximately 50% of its recurring gross profit in exchange for $9.7 million in cash and expects to receive $9.5 million ratably over the four years following the transaction close, subject to certain closing conditions. The Company will transfer $1.7 million of working capital after closing the transaction and approximately $6 million of the Company's annualized gross profit.

The Company believes that its current cash position, after collection of the proceeds from the January 2020 customer assignment transaction, along with its revenue growth and the financing from potential institutional investors will be sufficient to fund its operations for at least a year from the date these financials are available. If these sources do not provide the capital necessary to fund the Company's operations during the next twelve months from the date of this report, the Company may need to curtail certain aspects of its operations or expansion activities, consider the sale of its assets, or consider other means of financing. The Company can give no assurance that it will be successful in implementing its business plan and obtaining financing on terms advantageous to the Company or that any such additional financing would be available to the Company. As such, these conditions raise substantial doubt as to its ability to continue as a going concern within one year from the issuance date of the financial statements. These consolidated financial statements do not include any adjustments from this uncertainty.

Note 4: Senior Secured Convertible Notes Payable (in default)

The Company has issued three series of senior secured convertible notes payable. In general, each series is convertible into common shares of the Company. Senior Secured Convertible Notes Payable consist of the following:

	November 30, 2019	August 31, 2019
	(unaudited)	
Senior Secured Convertible notes, Principal	$ 6,808,000	$ 6,808,000
Less debt discount and deferred financing costs	(2,604,000)	(3,457,000)
Total outstanding convertible notes, net	$ 4,204,000	$ 3,351,000
Less current portion of convertible notes payable	(3,426,000)	(3,351,000)
Long-term convertible notes payable	$ 778,000	$ -

The following table rolls forward the Convertible Notes Payable balances from August 31, 2019 to November 30, 2019:

	Gross Principal	Deferred Financing Costs	Note Discount	Net
Balance at August 31, 2019	$ 6,808,000	(344,000)	(3,113,000)	$ 3,351,000
Amortization of Interest Expense	-	80,000	773,000	853,000
Balance at November 30, 2019	$ 6,808,000	(264,000)	(2,340,000)	$ 4,204,000
Less Current Amount	(5,141,000)	174,000	1,541,000	(3,426,000)
Long Term Balance at November 30, 2019	1,667,000	(90,000)	(799,000)	$ 778,000

The following table outlines the gross principal balance rollforward for each series from August 31, 2019 to November 30, 2019. Each series is described in further detail below.

	June 2018 Notes	December 2018 Notes	March 2019 Notes	Total
Gross Balance at August 31, 2019	$ 1,466,000	867,000	4,475,000	$ 6,808,000
Less Discount and Debt Issuance Costs:				
Debt Issuance Costs	-	-	(264,000)	(264,000)
Deferred Financing Costs	-	-	(2,340,000)	(2,340,000)
Carrying Balance at November 30, 2019	$ 1,466,000	867,000	1,871,000	$ 4,204,000
Less Current Amount	(1,466,000)	(728,000)	(1,232,000)	(3,426,000)
Long Term Balance at November 30, 2019	$ -	139,000	639,000	$ 778,000

During the quarters ended November 30, 2019 and 2018 the Company amortized $853,000 and $798,000, respectively, to interest expense from the combined amortization of deferred financing costs and note discounts recorded at issuance for the June 2018 and March 2019 Notes.

To date, the holders of the June Notes have converted $8,534,000 of principal, holders of December 2018 Notes have converted $22,000 of principal, and holders of March 2019 Notes have converted $275,000 of principal into common shares of the Company. There were no conversions of convertible notes during the fiscal quarter ending November 30, 2019.

On June 3, 2019, one of its institutional investors filed a claim in the United States District Court, Southern District of New York seeking preliminary injunctive relief against the Company to immediately deliver one million shares of the Company's common stock and to honor all future conversion requests duly submitted in accordance with the terms of the notes.

On June 7, 2019, and June 10, 2019, the Company received notices from two of its institutional investors that the Company was in default due to missed principal and interest payments under the terms of the Notes. On June 27, 2019, the Company reported that is has informed its convertible note holders that it will cease honoring conversion requests of the 2018 and 2019 Notes forcing a voluntary default of these instruments. The Company is pursuing a renegotiation and amendment of these instruments in an effort to avoid litigation. The Company is requesting to amend the terms of the notes to remove the conversion features and revise the cash amortization, among other items.

On December 5, 2019, the Company entered into an exchange agreement with the holder of a majority of its March 2019 Convertible Notes. The exchange agreement and the related revised March 2019 note agreement revised the conversion price to $40.00 per share, extended the term of the March 2019 notes to March 1, 2022, provided for a revised quarterly amortization schedule beginning April 1, 2020, and removed certain anti-dilution terms of the related March 2019 warrants. The holder also exchanged $222,000 of December 2018 Notes by extending the term to coincide with the revised term of the March 2019 notes and for the revised amortization schedule. The Company agreed to issue an additional $200,000 of consideration to the holder, payable in common stock, as consideration for this exchange and agreed to increase the principal outstanding on the notes exchanged by 10% from $222,000 for the December 2018 notes to $244,000 and from $2,445,000 for the March 2019 notes to $2,890,000. On December 11, 2019, the Company issued 21,750 shares of common stock to the holder in satisfaction of the additional $200,000 of consideration. As of November 30, 2019, after the exchange as described in Note 9, the Company classified $778,000 of the $1,245,000 carrying value of the notes exchanged as long-term liabilities.

See also Note 8 for litigation related to the Convertible Notes Payable.

From June 10, 2019 until November 30, 2019, the Company has accrued interest at the default interest rate for all note series representing approximately $0.6 million of additional interest payable of which $0.3 million is attributable to the quarter ending November 30, 2019. The Company has accrued an additional $1.8 million to accrued default liabilities as of November 30, 2019 and August 31, 2019, representing potential liability associated with the default of the notes payable for default premium, potential liquidating damages, and other costs associated with the notes in default.

June 2018 Senior Convertible Notes (in default)

On June 4, 2018, the Company issued $10 million of senior convertible notes ("June 2018 Notes") to institutional investors with an original issue discount of $1 million for a purchase price of $9 million. The notes bear interest at a rate of 8%, with one year's interest guaranteed, and have a maturity date of September 4, 2019. The Notes remain outstanding as of November 22, 2019. The company received cash proceeds of $8.4 million representing the $9 million purchase price, reduced by approximately $0.6 million of financing costs directly related to the issuance of the June 2018 Notes.

Concurrent with the sale of the June 2018 Notes, the Company granted warrants to purchase 25,101 shares of common stock to its institutional investors and warrants to purchase 5,422 shares of common stock to its investment banker as placement fees, at an exercise price of $99.60, subject to down round price protection adjustment, as defined in the agreements. The warrants were valued at the date of issuance using the lattice-based option pricing model at $86.80 per warrant. Both the June 2018 Notes and the related warrants were issued with registration rights, whereby the Company was obligated to register the shares underlying the June 2018 Notes or was subject to registration rights penalties.

The terms of June 2018 notes are summarized as follows:

- Term: September 4, 2019;
- Coupon: 8%; Default interest rate: 18%;
- Convertible at the option of the holder at any time;
- Conversion price is initially set at $99.60 but subject to down round price protection. After maturity, the conversion price will be set subsequently at the lesser of the then conversion price and 85% of the volume weighted average price for the trading date immediately prior to the application conversion date; and
- Monthly amortization of principal either in cash at a 10% premium or in stock, subject to equity conditions, at a 15% discount to the lowest volume weighted average price, at the option of the Company.

December 2018 Notes (in default)

On December 20, 2018, the Company entered into settlement agreements with its institutional investors, which resolved all disputes relating to technical defaults by the Company in failing to meet deadlines for filing a registration statement and for having a registration statement effective by the SEC. As a result of such settlement, the Company issued additional notes ("December 2018 Notes" in the amount of $889,000 on substantially the same terms as the June 2018 Notes except that the stated interest rate was 0% and the term of the December 2018 Notes was December 31, 2019. There was no recorded discount or deferred financing costs for the December 2018 Notes issued.

March 2019 Bridge Financing (in default)

On March 12, 2019, the Company issued convertible notes in the principal amount of $4,750,000 with an original issue discount of $1 million for a purchase price of $3,750,000 to certain of its existing institutional investors (“March 2019 Notes”) and mature on September 12, 2020. The Company received net cash proceeds of $3.3 million to be used for mobile application development and working capital. The Company incurred approximately $0.5 million of debt issuance costs that are incremental costs directly related to the issuance of the bridge financing senior convertible notes payable.

The terms of the March 2019 convertible notes are summarized as follows:

- Term: September 12, 2020;
- Coupon: 0%;
- Default interest rate: 18%;
- Original issue discount: $1,000,000;
- Convertible at the option of the holder at any time;
- Initial conversion price is set at $1.67 but subject to down round price protection;
- Alternate conversion price at the greater of the floor price of $0.31 and the lower of the conversion price in effect and alternate conversion percentage of the lowest VWAP of the common share during the 10 consecutive trading day prior to the applicable conversion date;
- Alternate conversion percentage is 75% if the alternate conversion is an alternate conversion event of default as a result of bankruptcy or 80% for all alternate event of default conversion or 85% is such alternate conversion is an alternate optional conversion;
- Redemption at the option of the Company at 15% premium at any time after 45 days from March 12, 2019.

In connection with the note, the Company issued 74,387 warrants (“March 2019 Warrants”), exercisable at $70, with a five-year term. The Company evaluated the warrants issued and determined that they were derivative liabilities. The Company estimated the fair value of the warrants using the Lattice pricing model. The key valuation assumptions used consist, in part, of the price of the Company’s common stock of $63.60, a risk-free interest rate of 2.49% and expected volatility of the Company’s common stock of 122%, resulting in a fair value of $3,917,000.

The Company estimated the aggregate fair value of the conversion feature derivative embedded in the debenture (“March 2019 Conversion Feature”) at issuance at $2,421,000 based on weighted probabilities of assumptions using the Lattice pricing model. The key valuation assumptions used consist, in part, of the price of the Company’s common stock of $63.60, a risk-free interest rate of 2.49% and expected volatility of the Company’s common stock of 122%, and the various estimated reset exercise prices weighted by probability.

This resulted in the calculated fair value of the debt discount resulted from bifurcating the warrants and the conversion feature being greater than the face amount of the debt and the original issue discount, and the excess amount of $2.6 million was immediately expensed as financing costs.

[Table of Contents](#)

Note 5: Stockholders' Equity

Common Stock and Warrants

The Company issued no common shares or common stock warrants during the quarter ended November 30, 2019. No warrants were exercised, expired, or cancelled during the quarter ended November 30, 2019.

The following tables summarize our warrants outstanding as of November 30, 2019:

	Exercise price	Warrants Outstanding	Weighted average life of outstanding warrants in years
March 2019 Notes Warrants	$ 70.00	74,390	4.3
June 2018 Notes Warrants	$ 70.00	30,526	3.5
2017 PIPE Warrants	$ 276.00	2,500	2.6
		107,416	4.0

All warrants outstanding and exercise prices have been adjusted to reflect the 1:40 reverse split.

Table of Contents

Note 6: Share based Compensation

In March 2017, the Company adopted the 2017 Stock Option / Stock Issuance Plan (the “Plan”). The Plan provides incentives to eligible employees, officers, directors and consultants in the form of incentive stock options (“ISOs”), non-qualified stock options (“NQs”), each of which is exercisable into shares of common stock (“Options”) or shares of common stock (“share grants”). The Company has reserved a total of 250,000 shares of common stock for issuance under the Plan as of November 30, 2019.

Of these shares, as of November 30, 2019, approximately 83,000 options and 7,000 shares have been designated by the Board of Directors for issuance and approximately 38,000 of the options have been forfeited and returned to the option pool under the Plan due to employment terminations. As of November 30, 2019, approximately 200,000 shares remain issuable of which 167,000 are eligible to be issued as ISOs and 200,000 are eligible to be issued as either share grants or NQ stock options.

No options or shares were granted during the quarter ended November 30, 2019.

For all options granted thus far to November 30, 2019, each option is immediately exercisable and has a term of service vesting provision over a period of time as follows: 25% vest after a 12-month service period following the award, and the balance vest in equal monthly installments over the next 36 months of service. All options granted to date have a ten-year term.

Share grants are issued at fair value, considered to be the market price on the grant date. The fair value of option awards is estimated on the grant date using the Black-Scholes stock option pricing model.

Following the adoption of Accounting Standards Update ASU 2016-09, the Company elected to account for forfeitures as they occur. Any compensation cost previously recognized for an unvested award that is forfeited because of a failure to satisfy a service condition is reversed in the period of the forfeiture.

Share based compensation expense consisted of employee stock option compensation expense of $114,000 and $77,000 for the quarters ended November 30, 2019 and 2018, respectively.

At November 30, 2019, the total unrecognized deferred share-based compensation expected to be recognized over the remaining weighted average vesting periods of 2.1 years for outstanding grants was $1.4 million.

A summary of option activity was as follows:

	Options Outstanding and Exercisable		
	Number of Options	Weighted Average Remaining Contractual Life (In years)	Weighted Average Exercise Price
Balance, August 31, 2019	50,749	8.95	$ 95.20
Granted	–	–	$ –
Exercised	–	–	$ –
Forfeited	(5,286)	8.44	$ 69.01
Balance at November 30, 2019	45,463	8.67	$ 98.30

Options outstanding as of November 30, 2019 had aggregate intrinsic value of $0.

Option vesting activity was as follows:

Options Vested	Number of Options	Weighted Remaining Contractual Life (In years)	Weighted Average Exercise Price
Balance, August 31, 2019	10,291	8.04	$ 152.80
Vested	2,232	8.44	$ 146.82
Exercised	–	–	$ –
Forfeited	(488)	0.08	$ 116.32
Balance at November 30, 2019	12,035	7.87	$ 153.19

The following table summarizes information about stock options outstanding and vested at November 30, 2019:

	Options Outstanding and Exercisable			Options Vested		
Exercise Prices	Number of Options	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number of Options	Weighted Remaining Contractual Life	Weighted Average Exercise Price
		(In years)			(In years)	
$18.80-$40.00	6,625	9.52	$ 23.31	–	–	$ –
$40.01–$80.00	13,729	9.34	$ 51.21	–	–	$ –
$80.01–$120.00	11,224	8.45	$ 103.15	4,384	8.41	$ 103.53
$120.01–$160.00	12,625	7.79	$ 157.71	6.860	7.56	$ 157.41
$160.01-$391.60	1,260	7.63	$ 391.60	791	7.63	$ 391.60
	45,463	8.67	$ 98.30	12,035	7.87	$ 153.19

The number of options and exercise prices have been presented retroactively for the 1 for 40 December 17, 2019 reverse split.

Note 7: Related Parties

J. Stephen Holmes, our Sales Manager is an advisor to and significant shareholder of the Company. The Company incurred $180,000 and $180,000 in professional fees for management consulting services in the three months ended November 30, 2019, and 2018, respectively.

[Table of Contents](#)

Note 8: Contingencies

Certain conditions may exist as of the date the financial statements are issued, which may result in a loss to the Company, but which will be resolved only when one or more future events occur or fail to occur. The Company's management, in consultation with its legal counsel as appropriate, assesses such contingent liabilities, and such assessment inherently involves an exercise of judgment.

During the ordinary course of business, the Company is subject to various claims and litigation. Management believes that the outcome of such claims or litigation will not have a material adverse effect on the Company's financial position, results of operations or cash flow.

Convertible Note related litigation:

During 2019, three of the Company's note holders have filed complaints:

Alpha Capital v. ShiftPixy, Inc.

On July 3, 2019 ShiftPixy was served with a complaint filing by Alpha Capital Anstalt (ACA) in the United States District Court, Southern District of New York alleging breach of contract in refusing to honor the conversion of certain convertible notes, specifically one for $310,000 submitted on June 20, 2019. ACA sought an injunction requiring the Company to issue 25,000 common shares, damages for the claimed breaches, and attorney's fees. In August 2019, the court denied the motion for a preliminary injunction but granted accelerated discovery which was completed in September 2019. As of November 30, 2019, the Company had convertible notes outstanding with ACA for approximately $1.7 million consisting of $0.3 million of the June 2018 series, $0.2 million of the December 2018 series and $1.2 million of the March 2019 series. In January 2020, Alpha was awarded a judgement for $500,000 consisting of the $310,000 notes and $190,000 of damages. The damages are fully accrued for as of November 30, 2019 in the default penalty accrual as described in Note 4 above. On January 16, 2020 Alpha Capital converted all remaining June and December 2018 Note balances at $12.20 per share. On January 20, 2020 the Company paid the damages award in cash.

Dominion Capital LLC v. ShiftPixy, Inc.;

On July 18, 2019 ShiftPixy was served with a complaint filing by Dominion Capital LLC in the United States District Court, Southern District of New York alleging breach of contract in refusing to honor the conversion of certain convertible notes. Dominion sought injunctive relief, injunction to prohibit buyback, breach of contract on the June 2018, December 2018, and March 2019 notes, and declaratory judgment. In August 2019, the court denied the motion for a preliminary injunction but granted accelerated discovery which was completed in September 2019. As of November 30, 2019, the Company had convertible notes outstanding with Dominion for approximately $1.5 million consisting of $0.7 million of the June 2018 series, $0.2 million of the December 2018 series and $0.6 million of the March 2019 series. The Company expects to have a judgment awarded to Dominion later in January 2020 and is in discussions to settle the litigation.

MEF I, LP v. ShiftPixy, Inc.;

On August 27, 2019 MEF filed a complaint in the United States District Court, Southern District of New York. MEF seeks monetary relief of $2.1 million and seeks to appoint themselves as receiver of the Company. As of November 30, 2019 the Company had convertible notes outstanding to MEF at approximately $0.7 million face value consisting of approximately $0.5 million and $0.2 million for the June 2018 and December 2018 notes respectively. In November 2019 the Company filed a motion in response to the receiver request. On January 17, 2020 the Company and MEF I settled all claims and repaid all note principal remaining, accrued damages, and accrued interest and with issuance of 20,000 shares of common stock and payment of $725,000 in cash. The total of $969,000 was fully accrued for as of November 30, 2019.

Kadima Ventures

The Company is in dispute with its software developer, Kadima Ventures, over incomplete but paid for software development work. In May 2016, the Company entered into a contract with Kadima Ventures for the development and deployment of user features that were proposed by Kadima for an original build cost of $8.5 million to complete. As of the date of this filing, the Company has spent approximately $11 million but has not received the majority of certain software modules. In addition to the non-delivery of the paid for user features, Kadima Ventures asserts that it is owed additional funds to turn over the work completed. The Company initiated litigation to force the delivery of the software modules paid for through fiscal 2019 and exit the development engagement. In April 2019, Kadima filed a complaint against ShiftPixy in the County of Maricopa, AZ alleging breach of contract, promissory estoppel and unjust enrichment and has demands for an additional $10 million prior to releasing the remaining features. The parties agreed to a transfer of the matter to an Arizona Commercial Court with the expectation that the matter would be sent to arbitration or mediation. In October 2019, Kadima provided the software code to a third party for technical evaluation of the software in question. The Company expects to enter into mediation once the technical evaluation is completed later in fiscal 2020. An answer to the Complaint is due January 31, 2020.

Splond Litigation

On April 8, 2019, claimant, Corey Splond, filed a class action lawsuit, naming ShiftPixy, Inc. and its client as defendants, claiming that he was scheduled to work for more than 8 hours during 24-hour periods without being paid overtime, to which he was entitled. In addition, claimant is seeking waiting time penalties for the delay in payment. This lawsuit is in the initial stages; the financial impact to the Company, if any, cannot be estimated. No liability has been recorded for this matter at this time. In the event of an unfavorable outcome the Company's client is contractually obligated to indemnify the Company for misreported hours and portions of the claim would be covered under the Company's employment practices liability insurance.

Note 9: Subsequent Events

On December 5, 2019, the Company entered into an exchange agreement with the holder of a majority of its March 2019 Convertible Notes. The exchange agreement and the related revised March 2019 note agreement revised the conversion price to $40.00 per share, extended the term of the March 2019 notes to March 1, 2022, provided for a revised quarterly amortization schedule beginning April 1, 2020, and removed certain anti-dilution terms of the related March 2019 warrants. The holder also exchanged $222,000 of December 2018 Notes by extending the term to coincide with the revised term of the March 2019 notes and for the revised amortization schedule. The Company agreed to issue an additional $200,000 of consideration to the holder, payable in common stock, as consideration for this exchange and agreed to increase the principal outstanding on the notes exchanged by 10% from $222,000 for the December 2018 notes to $244,000 and from $2,445,000 for the March 2019 notes to $2,890,000. On December 11, 2019, the Company issued 21,750 shares of common stock to the holder in satisfaction of the additional $200,000 of consideration. As of November 30, 2019, the Company classified $778,000 of the $1,245,000 carrying value of the notes exchanged as long-term liabilities.

On December 17, 2019 the Company effected a 1 for 40 reverse stock split. All common shares, common share warrants, common share options, and convertible note conversion prices have been retroactively adjusted.

On December 23, 2019, the Company issued 428 shares to each of Messrs. Higgins and White, both Directors of the Company, in settlement of shares promised in December 2018 but not issued. The fair value on the date issued for the combined issuance of 856 shares was $7,000.

On January 6, 2020 the Company entered into an asset purchase agreement with a third party that assigned client contracts representing approximately 60% of the recurring business as of November 30, 2019 and certain operating assets in exchange for up to approximately $19.2 million of consideration. The Company received $9.7 million upon closing and expects to receive additional proceeds of approximately $2.4 million per year, payable monthly, for the next four years after certain transaction conditions are met. The Company evaluated the transaction and determined that as of November 30, 2019 the criteria were not met to designate any assets as assets held for sale.

In January 2020, the Company paid the damages claim with Alpha Capital as described in Note 8 above.

On January 17, 2020, the Company settled all claims with MEF I, LP as described in Note 8 above.

Management has evaluated subsequent events pursuant to the issuance of the interim unaudited consolidated financial statements and has determined that other than listed above, no other subsequent events exist through the date of this filing.

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

The following discussion of our financial condition and results of operations should be read in conjunction with our financial statements and the related notes, and other financial information included in this Form 10-Q.

Our Management's Discussion and Analysis contains not only statements that are historical facts, but also statements that are forward-looking. Forward-looking statements are, by their very nature, uncertain and risky. These risks and uncertainties include international, national, and local general economic and market conditions; our ability to sustain, manage, or forecast growth; our ability to successfully make and integrate acquisitions; new product development and introduction; existing government regulations and changes in, or the failure to comply with, government regulations; adverse publicity; competition; the loss of significant customers or suppliers; fluctuations and difficulty in forecasting operating results; change in business strategy or development plans; business disruptions; the ability to attract and retain qualified personnel; the ability to protect technology; the risk of foreign currency exchange rate; and other risks that might be detailed from time to time in our filings with the Securities and Exchange Commission.

Although the forward-looking statements in this Report reflect the good faith judgment of our management, such statements can only be based on facts and factors currently known by them. Consequently, and because forward-looking statements are inherently subject to risks and uncertainties, the actual results and outcomes may differ materially from the results and outcomes discussed in the forward-looking statements. You are urged to carefully review and consider the various disclosures made by us in this report as we attempt to advise interested parties of the risks and factors that may affect our business, financial condition, and results of operations and prospects.

Our Management's Discussion & Analysis of Financial Condition and Results of Operations (MD&A) includes references to our performance measures presented in accordance with U.S. Generally Accepted Accounting Principles (GAAP) and other non-GAAP financial measures that we use to manage our business, make planning decisions and allocate resources. Refer to the Non-GAAP Financial Measures within our MD&A for definitions and reconciliations from GAAP measures.

Overview

Our current business, and the primary source of our revenues to date, has been under a traditional staffing services business model. Our initial market focus is to use this traditional approach, coupled with developed technology, and address an underserved market containing predominately lower wage employees with high turnover, in light industrial, services, and food and hospitality. The Company provides Human Resources, employment compliance, insurance, payroll, and operational employment services solutions for our business clients ("clients") and shift work or "gig" opportunities for worksite employees ("WSEs"). We receive admin or processing fees as a percentage of a business client's gross payroll, process and file payroll taxes and payroll tax returns, provide workers compensation insurance, and provide employee benefits. We have built a substantial business on a recurring revenue model since our inception in 2015 and for the quarter ended November 30, 2019 we processed in excess of $400 million of annualized payroll billings. Our business grew in both billings and billable worksite employees in excess of 50% year over year for each year since inception and is expected to continue a high degree of growth. We have experienced losses to date as we have invested in both our technology solutions as well as the back-office operations required to service a large employee base under a traditional staffing model.

We provide services to businesses and we define a "client" as any business paying us to provide employee related services. We are currently focused on clients in the restaurant and hospitality industries, traditionally market segments with high employee turnover and low pay rates; however, we have clients in a variety of other industries as well. All have written client service agreements. The basic client agreement is substantially similar for all clients, with minor modifications to fit each client's specific situation, and some differences to account for whether the engagement is with ShiftPixy or its wholly owned subsidiary, Shift Human Capital Management Inc.

Our founders' initial goal was to bring Employment Administration Services ("EAS") and traditional staffing services ("Staffing") to an underserved segment of the market; namely small businesses who lack HR and Payroll infrastructure and therefore struggle with the HR compliance requirements and high turnover that is prevalent for many businesses who employ lower income and part time workers. Since our inception in 2015, we have built a client employee pool of over 25,000 persons that is populated by lower wage employees, averaging approximately $22,000 per year and for personnel typically under 35 years of age. We believe that by accumulating together a large number of low-wage and younger employee population, we will obtain a competitive advantage and increase revenues and profits through increased services over and above our base service offering to better serve the younger demographic through our technology solution.

Beginning in 2015, our core business model is to provide payroll services and to facilitate workers compensation insurance to small businesses in exchange for an administration fee calculated as a percentage of their gross payroll. We provide such services by employing an operations team consisting of taxation, customer service, HR Compliance, benefits, and workers compensation specialists and which allows us to deliver "best practices" HR, tax compliance, workers compensation insurance, and payroll services at a lower cost than it would cost our clients to provide on their own.

Table of Contents

Our revenues through the first quarter of fiscal 2020 primarily consist of admin fees calculated as a percentage of gross payroll processed, payroll taxes due on worksite employees billed to the client and remitted to the taxation authority, and workers compensation premiums billed to the client for which we facilitate workers compensation coverage. Our costs of revenues consist of the accrued and paid payroll taxes and our costs to provide the workers compensation coverage including premiums and loss reserves. A significant portion of our assets and liabilities is for our workers compensation reserves, carried as cash balances, and our estimates of projected workers compensation claims, carried as liabilities. We provide a self-funded workers compensation policy up to $500,000 and purchase reinsurance for claims in excess of $500,000. As of November 30, 2019, we have workers compensation related assets that are approximately $1.9 million higher than our projected workers compensation losses, or approximately 25% of the asset total as of November 30, 2019. We also actively and closely monitor and manage our clients and worksite employees' workers compensation claims which allow us to provide a lower cost option for our clients than they would otherwise be able to purchase on their own. We believe that our customer value proposition is to provide the combination of overall net cost savings to the client as follows:

- Payroll tax compliance and management services
- Governmental HR compliance such as for the Affordable Care Act compliance requirements
- Reduced client workers compensation premiums or enhanced coverage
- Access to an employee pool of potential applicants to reduce turnover costs
- Offset by increased administrative fee cost to the client payable to ShiftPixy

We see our technology platform as a key competitive advantage and differentiator to our market competitors. Our founders believed that providing this baseline business, coupled with a technology solution to address additional concerns such as employee scheduling and turnover, would provide a unique, cost effective solution to the HR compliance, staffing, and scheduling problems that faced these businesses. Our next goal, currently underway, is to match the small business needs of companies with paying “gigs” with a fully compliant and lower cost staffing solution. For this, we need to acquire a significant number of worksite employees (“WSE”) to provide our paying clients with a variety of solutions for their unique staffing needs and facilitate the employment relationship. We further believe that our pool of WSEs will provide an opportunity to be highly competitive in “last mile” delivery solutions using gig employees within our technology solution.

Over the past four years, the Company has invested heavily in a robust, cloud-based Human Resources Information System (HRIS) platform in order to:

- reduce WSE management costs,
- automate new WSE and client onboarding, and
- provide additional value-add services for our business clients resulting in additional revenue streams to the Company

As of August 31, 2019, the initial launch of onboarding and scheduling was completed and we began to provide some of the HRIS and application services to selected legacy customers on a test basis. During the first quarter of fiscal 2020, we continued working to implement additional mobile application and HRIS functionality in delivery, “gig” intermediation services, and scheduling which were launched in the first quarter of 2020 to selected customers on a no-fee basis. We see these technology-based services as multiple potential revenue drivers with limited additional costs.

Table of Contents

Our cloud-based HRIS platform captures, holds, and processes HR and payroll information for the clients and WSEs through an easy to use customized front end interface coupled with a secure, remotely hosted database. The HRIS system can be accessed by either a desktop computer or an easy to use electronic mobile phone application designed with legally binding HR workflows in mind. Once fully implemented, we expect to reduce the time, expense, and error rate for on boarding our client employees into our HRIS ecosystem and thereby have created a technological solution for employers and their workers. Once onboarded, the client employees are included as our worksite employees and who are available for shift work within our business ecosystem. This allows our HRIS platform to serve as a “gig” marketplace for WSEs and clients and allows for client businesses to better manage their staffing needs.

As of November 30, 2018, ShiftableHR and ShiftPixy had a combined client list of 192 clients with approximately 9,300 worksite employees. As of November 30, 2019, we had 247 clients with approximately 13,400 active WSEs and processed payroll of over $110 million ($440 million annualized) during our fiscal quarter ending November 30, 2019, an increase of nearly 60% from November 2018. Of these WSEs, approximately 60% represent workers in the restaurant industry. We have an additional 13,000 WSEs as of November 30, 2019 that were retained in our HRIS system that were not active WSEs but which are available for “gig” opportunities.

Our Services:

Our core EAS services are provided via standard legal contracts with our business clients, customized for each client’s specific needs and that are typically one year in length and are cancelable with 30 days’ notice. Through November 30, 2019, we have not had any material revenues or billings generated within our HRIS from additional value-added services. We consider our future service offering to be the future of the company and which will provide for additional revenue streams and support cost reductions for existing and future business clients. Future services, including technology based services provided through our HRIS system and mobile application will be through "a la carte" pricing via customizable on-line contracts.

We provide our solution in the developing nextGEN or "gig" economy primarily by absorbing our clients' workers, who we call worksite employees (WSEs) but may also be called "shift workers," "shifters," "gig workers," or "assigned employees." WSEs are carried under a ShiftPixy corporate employee umbrella and we shoulder certain employment-related compliance responsibilities for our business clients as part of our services provided. This arrangement benefits the WSEs by opening additional work opportunities through access to other shift work with other ShiftPixy clients. The WSE further benefits from employee status benefits through ShiftPixy's benefit plan offerings, including minimum essential health insurance coverage plans and a 401(k) plan while enjoying the protections of workers' compensation coverage and employment laws.

At the heart of ShiftPixy's employment service solutions is the secure, cloud-based HRIS database accessible by a desktop or mobile device through which ShiftPixy worksite employees will be enabled to find available shift work at ShiftPixy client locations. This solution solves a problem of finding available shift work for both the shifters looking for additional shift work and business clients looking to fill open shifts. For new WSEs, the mobile platform includes an easy to use WSE onboarding functionality which we believe will increase our WSE pool of workers that will provide a deep bench of worker talent for our business clients. The onboarding feature of our software enables us to capture all application process related data regarding our assigned employees and to introduce employees to and integrate them into the ShiftPixy Ecosystem. The mobile platform features a Pixy chatbot that leverages artificial intelligence to aid in gathering the data from workers via a series of questions designing to capture all required information, including customer specific and governmental information. Final onboarding steps requiring signatures can also be prepared from the HRIS onboarding module

In 2019, we implemented additional functionality to provide a scheduling component of our software, which enables each client worksite to schedule workers and to identify shift gaps that need to be filled. We utilize computer algorithms to maintain schedules and fulfillment, using an active methodology to engage and move people to action. We began using this functionality at the end of fiscal 2019 on a test basis and had additional deployments in the first fiscal quarter.

The final phase of our initial platform now beginning to be deployed, consists of our "shift intermediation" functionality, which is designed to enable our WSE shift workers to receive information regarding and to accept available shift work opportunities. The intermediation functionality becomes useful only to the extent that we have meaningful numbers of available workers and client shift opportunities in the same geographic region. We reached geographical concentration in Southern California during 2019 and we activated these key features in August 2019 to a limited group of customers on a test basis. These test basis deployment efforts have generated significant business knowledge and allowed our marketing and engineering teams to develop key enhancements and process flow improvements during the November 2019 quarter and these key feature enhancements are critical for our expected growth beginning January 1, 2020 after the end of the 2019 tax year.

Our goal is to have a mature and robust hosted cloud based HRIS platform coupled with a seamless and technically sophisticated mobile phone application ("App") that will act as both a revenue generation system as well as a "viral" customer acquisition engine through the combination of the scheduling, delivery, and intermediation features and interactions. We believe that once a critical mass of clients and WSEs is achieved, additional shift opportunities will be created pulling in additional WSEs and additional client businesses in food service and hospitality industries. Our approach to achieving this critical mass is to market our services to restaurant owners and franchisees, focusing on specific brands and geographical locations. We expect critical mass to be a function of both geography, such as in Southern California for viral adoption by WSEs and clients, or by adoption within franchise brands for viral adoption by clients.

Our initial market focus was chosen based on our understanding of the issues and challenges facing "Quick Service Restaurants" ("QSRs"), including fast food franchises and local restaurants. We have chosen to invest in two key features of our mobile application to this end consisting of: i) scheduling functionality, designed to enhance the client's experience through scheduling of employees and reducing the impact of turnover and ii) delivery functionality, designed to increase revenues through delivery fulfillment as well as to bring "in house" the delivery fulfillment and thereby reducing delivery costs.

One of the most recent developments in the food and hospitality industry is the rapid rise of third-party restaurant delivery providers such as Uber Eats, GrubHub, and DoorDash. These providers have successfully increased QSR revenue in many local markets by providing food delivery to a wide-scale audience using contract delivery drivers. We have observed two significant issues with our clients and third-party delivery providers which is increasingly being reported in the news media with companies like Dominos Pizza and Jimmy Johns franchises providing their own delivery services and avoiding third party delivery services. The first issue is the very large revenue share typically being paid to many of these third-party delivery providers as delivery fees. These additional costs erode the profit for the QSRs from those additional sales made through this delivery channel. The second is that our QSR customers have encountered problematic deliveries of their food products - late deliveries, cold food, missing accessories, and unfriendly delivery people. This in turn has caused significant "brand erosion" in many cases and has caused these clients to reconsider third-party delivery.

We provide a solution to the third-party delivery issues. We designed our HRIS platform to manage food deliveries by the QSRs using internal personnel and a customized "white label" smart phone App. Our recently released delivery feature links this "white label" delivery ordering system to our delivery solution, thereby freeing the QSR to have their own brand showcasing an ordering APP but retaining similar back-office delivery technology including scheduling, ordering, and delivery status pushed to a customer's smart phone. Our technology and approach to human capital management allows the company a unique window into the daily demands of QSR operators and the ability to extend our technology and engagement to enable this unique self-delivery proposition. ShiftPixy's new driver management layer for operators in the ShiftPixy ecosystem will now allow clients to use their own team members to deliver a brand intended customer experience. ShiftPixy's mobile platform now provides the HR compliance, management and insurance solutions necessary to the support of a delivery option and created a turnkey self-delivery opportunity for the individual QSR operator. Our solution saves delivery costs to the QSR client and allows them to retain the customer information and quality control over the food delivery.

The first phase of this component of our platform is the driver onboarding, which was completed in 2019. The enhanced features will also “micro meter” the essential commercial insurance coverages required by our operator clients on a delivery-by-delivery basis (workers’ compensation and auto coverages) which has been a significant barrier for some QSRs to provide their own delivery services. We began using the “delivery features” of our mobile platform for selected customers on a trial basis in the fourth quarter of fiscal 2019 into the first quarter of 2020 and is currently active in the Southern California area. We expect to launch the solution in fiscal 2020.

ShiftPixy’s headquarters is currently situated in Irvine, California, from which it can reach the Southern California market and has a geographical presence via sales offices in New York, Austin, Texas, Chicago and the Orlando area from which its local sales/services representatives will secure and service clients in those areas, and it plans to open additional physical offices in San Francisco and Miami. Through these office locations, we plan to engage more actively with clients through sales, marketing, employee onboarding, training and payroll processing, in each instance as necessary and appropriate to the applicable market. These markets collectively account for or allow us to cover approximately 53% of our target market in the restaurant/hospitality sectors. (U.S. Department of Labor. Bureau of Labor Statistics. May 2015. Occupational Employment and Wages.).

[Table of Contents](#)

We believe ShiftPixy will experience business and revenue growth in the nextGEN Gig Economy from the following key factors:

- **Large Potential Market.** Current statistics show that there are over 14.7 million employees working in our current target market--the restaurant and hospitality industries representing over $300 billion of annual revenues. (U.S. Department of Labor. Bureau of Labor Statistics. February 2018). Compared to the total workforce in all industries, workers in the restaurant industry have a notably higher percentage of part-time workers. (National Restaurant Association. "News & Research: Restaurant middle class job growth 4x stronger than overall economy." 13 January 2016). At our current monetization rate per employee, this represents an annual revenue opportunity of over $9 billion per year for the United States. Our current geographic presence in California, New York City and parts of Texas, Illinois, and Florida provides coverage of over 50% of this opportunity. Our intention is to expand both our geographic footprint and our service offerings into other industries, particularly where part-time work is a significant component of the applicable labor force, including the retail and health care sectors.

- **Positive External Market Forces.** A significant problem for small businesses and in particular businesses in the food service industry such as QSRs, involve compliance with employment related regulations imposed by federal, state and local governments. These regulations include the provisions of the Affordable Care Act and recent developments in California for Gig Economy companies such as Uber and Lyft under California SB5 which requires these companies to treat their workers as employees rather than independent contractors. We foresaw this change and provide a viable solution to convert contract workers into employees under our HRIS platform. We see significant business traction from this development.

- **Rapid Rise of Independent Workers**. The number of independent workers, totaling approximately 41 million in 2018, is expected to increase to 40% of the private, non-farm U.S. workforce by 2021. (MBO Partners. "America's Independents / A Rising Economic Force / 2016 State of Independence in America Report / Sixth Annual." 2016.). As of early 2019, approximately 48% of the U.S. workforce has worked as an independent employee as either part time or on a contract basis (Source: http://www.mbopartners.com/state-of-independence).

- **Technology Affecting and Attitudes towards Employment Related Engagements**. Gig-economy platforms have changed the way part-time workers can identify and connect to work opportunities, and Millennials and others have embraced such technologies as a means to secure short-term employment related engagements. The significant increase in the adoption of smart phone devices has provided the "last mile" platform to enable technology solutions such as ours to provide a gig economy platform. Most importantly, for our target audience of 18-35 year old workers as of February 2019, 92% of these workers regularly use a smart phone (Source: Pew Research Center).

- **New ShiftPixy Mobile App is Designed to Provide Additional Benefits to Employers and NextGen Shift Workers.** Millennials represent approximately 40% of the independent workforce who are over the age of 21 and who work 15 hours or more each week. (MBO Partners. "America's Independents / A Rising Economic Force / 2016 State of Independence in America Report / Sixth Annual." 2016.) Mindful that most of its shifters will be Millennials who connect with the outside world primarily through a mobile device, ShiftPixy is poised to significantly expand its business through the ShiftPixy mobile app. The ShiftPixy mobile app is a proprietary application downloaded to mobile devices, allowing ShiftPixy's shifters to access shift work opportunities at all of ShiftPixy's clients, not just their current restaurant or hospitality provider, and with an added feature, anticipated to be available in the first calendar quarter of 2020, also allowing shift employees not working at its clients to access shift work opportunities at all of its clients.

ShiftPixy and its subsidiary collectively serve, as of November 30, 2019, an aggregate of 247 clients with an aggregate of approximately 13,400 employees, including 8,700 employees of ShiftPixy and ShiftableHR that we provide to our clients and 4,700 employees of our clients for whom we provide only payroll administration services. None of these clients represents more than 10% of our revenues for the three months period ending November 30, 2019.

Significant Developments in Q1 2020

Revised customer focus

Beginning in June 2019 we refocused our sales efforts towards clients that were better suited to take advantage of our HRIS and mobile application benefits including the functions we believe will result in additional revenues, gross margins, and carry a reduced cost of operations to support both from our internal customer support team and from sales commissions. We hired additional internal sales personnel to focus on those client opportunities and we are moving away from our prior sales model which utilized highly commissioned sales personnel paid on a recurring percentage of customer billings. Those personnel were fully trained in September 2019 and their efforts began to bear positive results shortly thereafter resulting in customer wins in October with expected onboarding to begin in calendar 2020.

We believe our new sales model is better served to incentivize our sales and marketing personnel to acquire those customers that benefit from the HRIS value proposition and will result in both increased revenues and profitability. We also reviewed our legacy customers after this refocus as well as during the due diligence process for the assignment transaction that closed in January 2020 and identified those customers with limited potential to benefit from our "upsell" HRIS model. Those customers who did not fit our revised profile were typically selected to be included in the assignment transaction and the average revenue and gross profit per employee for the transferred contracts was approximately 35% lower than the averages for the retained contracts.

As a result, our customer acquisition, compared to historical customer acquisition, was not comparable. The "legacy" business consisting of clients in industries such as landscaping and construction has historically driven a large part of our growth but has lower gross margins and less upsell opportunity. We saw a reduction of approximately 200 billable employees, resulting from two customers that were acquired and changed service providers from the legacy customer group as compared to August 31, 2019. Our revised sales focus resulted in no new "legacy" clients under contract to offset this reduction as was experienced in past reporting periods. However, the food related business that we retained showed both increases in billed worksite employees as well as increases in per employee billing and gross profit per billed employee. We expect to add further business clients, each reflecting higher average profits and revenue per billed employee, as compared to our averages in past reporting periods. Our expectation is that we will be onboarding approximately $100 million of new customer payroll billings during the second quarter of fiscal 2020 with additional business likely, but as yet not fully contracted or considered backlog.

Software Development

Prior to March 2019, we primarily used turnkey contract software development firms to build the software code, mobile application, and license integrations required to build the functional solution and our internal personnel had a primarily oversight role. Beginning in March 2019 we hired an internal development team for cost-cutting and for better feature and implementation control.

The Company began building its internal software development team and transitioned away from its current software development vendor to expedite the Company's technology deployment. The tardy delivery of the user features from the Company's previous software development vendor and related on-going litigation slowed down the pace of the Company's growth. The completion of our technology and the deployment of these features would further accelerate the growth of the Company. Under licensing agreement, the Company launched version 2.0 of its app and enhanced user features (onboarding, scheduling and intermediation) during the fourth calendar quarter with all user features as well as the driver management. The release of these features will further accelerate the growth of our business and move the Company closer to its financial breakeven point.

We continued our software development internally in the first quarter of 2020 primarily feature enhancements such as delivery, scheduling, and onboarding functionality improvement, and better integration and more seamless process flow improvements resulting in an improved user experience, reduced internal staff time required for onboarding, and increased trials of our future revenue generation features such as delivery and scheduling.

From inception of the project in 2017 through November 30, 2019, we spent approximately $16.7 million consisting of outsourced research and development, IT related expenses, development contractors and employee costs and marketing spending consisting of advertising, trade shows, and marketing personnel costs.

The following table shows the technology and marketing spending for each period reported:

Development spending (in $ millions)	**Three months ending November 30, 2019**	**Three months ending November 30, 2018**
	(unaudited)	**(unaudited)**
Contract development and licenses	$ 0.4	$ 0.8
Internal personnel costs	0.4	0.1
Total Development spending	$ 0.8	$ 0.9
Marketing spending		
Advertising and Outside Marketing	$ 0.3	$ 0.4
Internal personnel costs	0.1	0.1
Subtotal, Marketing costs	$ 0.4	$ 0.5
Total, HRIS platform and mobile application spending	$ 1.2	$ 1.4
Cumulative Investment	$ 16.7	10.6
Portion of investment capitalized as fixed assets	$ 3.7	0.4
Portion of investment expensed	$ 13.0	10.2

For the quarters ended November 30, 2019 and 2018, and included in the table above as development spending, we capitalized $0 and $0.4 million, respectively, of development spending into fixed assets.

Prior to March 2019, we primarily used turnkey contract software development firms to build the software code, mobile application, and license integrations required to build the functional solution and our internal personnel had a primarily oversight role. However, the tardy delivery of the user features from the Company's previous software development vendor and related on-going litigation slowed down the pace of the Company's growth in fiscal 2019. Beginning in March 2019 we hired an internal development team for cost-cutting and for better feature and implementation control. Our development team was fully in place by August 2019 and focused on delivering a version of our mobile app and software solution using a combination of third-party licensed software and internally developed software.

Under these licensing agreements, the Company launched version 2.0 of its app and enhanced user features (onboarding, scheduling and intermediation) during the fourth calendar quarter of 2019 with all user features as well as the driver management to selected customers on a test basis. The development team used the experience from these real-world test cases to further enhance the process flows, usability, and user experience for the mobile app and accompanying desktop application software during the first quarter of 2020. The feature enhancements such as delivery, scheduling, and onboarding functionality improvement, and better integration and more seamless process flow improvements resulted in an improved user experience, reduced internal staff time required for onboarding, and increased trials of our future revenue generation features such as delivery and scheduling. We are currently preparing additional test activities in advance of a full commercial rollout later in fiscal 2020.

The mobile app is one of the software components of what we call the mobile platform, and together with the ShiftPixy "Command Hub" and the client portal, is being developed, tested and released in stages. We have released and are using the onboarding feature of our software, which enables us to capture all application process related data regarding our assigned employees and to introduce employees to and integrate them into the ShiftPixy Ecosystem. Our new employees no longer have to fill out the burdensome pile of required new employee paperwork. By leveraging advanced algorithm capabilities, new hires are guided by a conversation with a "Pixy" chatbot that asks the necessary questions and generates the required employment documents in a highly personal and engaging way.

Following completion of the questions, applicable onboarding paperwork is prepopulated with the data and prepared for the employee's signature to be affixed digitally via the app as well. We use the app to gather required compliance documents such as I-9 required documentation.

Table of Contents

Key Developments subsequent to November 30, 2019:

Nasdaq delisting notice:

On June 6, 2019, ShiftPixy, Inc. (the "Company") received two letters from the NASDAQ Listing Qualifications Associate Director notifying the Company of the failure of the Company's security to meet the listing rules of NASDAQ.

The first letter noted that the Company's security had filed to maintain a minimum bid price of $1 per share for the prior 30 consecutive business days. The letter noted that the Company would have an additional 180 calendar days to come into compliance with the Listing Rule.

The second letter noted that the Company's security had filed to maintain one of the other listing requirements, either: i) a minimum Market Value of Listed Securities of $35 million for the prior 30 consecutive business days, ii) a minimum shareholders' equity of $2.5 million, or iii) $0.5 million of income from continuing operations. The letter noted that the Company would have an additional 180 calendar days to come into compliance with the

Listing Rule**.** To maintain the Listing Requirements, the Company must meet one of these three criteria.

On December 4, 2019, the Company received a letter from NASDAQ Regulation notifying the Company of its intent to schedule the Company's securities for delisting from NASDAQ at the opening of business on December 13, 2019 and its intent of filing a Form 25-NSE with the Securities and Exchange Commission. This was subject to the Company's right to file an appeal and present its Plan of Compliance at a hearing in front of the NASDAQ Hearings Panel. At that time, the Company requested a Hearing. On December 10, 2019, the Company received a letter from NASDAQ Listing Qualification notifying it that The Hearing had been scheduled for January 23, 2020.

On December 17, 2019, the Company received a letter from NASDAQ Listing Qualifications that the Company no longer met the minimum of 500,000 of publicly held shares.

We have provided a response to the NASDAQ regulatory body of our plans. We believe that we have satisfied the first two letters by way of our 1 for 40 reverse for the minimum share price requirement. With our recent gain on the assignment transaction and note settlements described below, we will have in excess of $2.5 million of shareholders equity to satisfy the second letter. We have several options available to be in compliance with the third letter regarding the minimum publicly held share requirement and we expect to satisfy this requirement prior to the hearing date.

March 2019 Note Exchange:

On December 5, 2019, the Company entered into an exchange agreement with the holder of a majority of its March 2019 Convertible Notes. The exchange agreement and the related revised March 2019 note agreement revised the conversion price to $40.00 per share, extended the term of the March 2019 notes to March 1, 2022, provided for a revised quarterly amortization schedule beginning April 1, 2020, and removed certain anti-dilution terms of the related March 2019 warrants. The holder also exchanged $222,000 of December 2018 Notes by extending the term to coincide with the revised term of the March 2019 notes and for the revised amortization schedule. The Company agreed to issue an additional $200,000 of consideration to the holder, payable in common stock, as consideration for this exchange. We are currently in discussion with other noteholders to resolve our remaining note litigation.

January 6, 2020 contract assignment:

On January 6, 2020 the Company entered into an asset purchase agreement with a third party that assigned client contracts representing approximately 60% of the recurring business as of November 30, 2019 and certain operating assets in exchange for approximately $19.2 million of consideration. The Company received $9.7 million upon closing and expects to receive additional proceeds of approximately $2.4 million per year, payable monthly, for the next four years after certain transaction conditions are met. The exact figures for the recurring business transferred is not available as of the date of this filing.

Convertible Note Settlements and Litigation Settlements:

In January 2020, the Company settled or resolved a portion of its convertible note litigation as follows:

In January 2020, the Alpha Capital received a judgment of $500,000 plus accrued interest on their litigation claim representing March 2019 Note principal of $310,000 plus $190,000 of damages. The Company resolved the Alpha litigation by converting their remaining balance of the June 2018 and December 2018 notes in full by issuing 45,211 shares and paying the damages in cash. All balances were fully accrued for as of November 30, 2019.

On January 17, 2020, the Company and MEF I settled all claims and repaid all note principal remaining, accrued damages, and accrued interest with the conversion of $244,000 of June 2018 Note Principal and payment of $725,000 in cash. The total of $969,000 was fully accrued for as of November 30, 2019.

Performance Highlights

Q1 FYE 2019 vs. Q1 FYE 2018

- Served approximately 270 clients and co-employed average 13,400 worksite employees, a 49% increase in average worksite employees compared to the same period in FYE 2019, and
- Processed approximately $110.5 million in gross billings, an increase of 55.9% over the same period in 2018.

Table of Contents

Our financial performance for the first quarter ended November 30, 2019, compared to the same quarterly period ended November 30, 2018, included:

Revenues increased 50.8% to $15.9 million resulting from increased number of worksite employees the Company is currently servicing and improvements to the average revenue per worksite employee. Average billed employees increased 44% over the fiscal 2019 quarter and the average revenue per worksite employee increased approximately 6% as the company shifts towards higher revenue, higher margin clients geared more towards our HRIS system.

Cost of Revenue increased 75.9% to $12.6 million due to increased number of worksite employees and a non-recurring credit of $1.0 million in the November 30 2018 quarter related to a reduction in cost of revenue attributable to taxes since the credit reduction for the state of California was waived in November 2018.

Gross profit decreased 5.0% to $3.2 million or 20.4% of revenues for the quarter ended November 30, 2019 from $3.4 million or 32.2% of revenues for the quarter ended November 30, 2018. Excluding the non-recurring tax related credit from fiscal 2019, gross profit increased 34.8% on a comparable basis.

Operating expenses increased by 18.8% to $5.6 million in the quarter ended November 30, 2019, from $4.7 million in the quarter ended November 30, 2018. Payroll related expenses, commissions and general and administrative expenses increased due to increased volume of operation and the addition of our in-house technical team, legal expenses in fiscal 2020 for increased litigation, offset by a decrease in external software development and marketing expenses.

Other expense, net decreased by 77% to $0.2 million resulting from the net effect of $0.2 million higher interest expense on our convertible notes, offset by a $0.9 million gain on the change in fair value of our debt related derivative liabilities.

Net Loss increased to $2.6 million or $2.86 per diluted share, from $2.2 million or $3.11 per diluted share.

Results of Operations

The following table summarizes the condensed consolidated results of our operations for the three months ended November 30, 2019, and 2018 (Unaudited).

	For the Three Months Ended November 30,	
	2019	2018
		(Restated)
Revenues (gross billings of $110.7 million and $70.9 million less worksite employee payroll cost of $94.8 million and $60.4 million, respectively)	$ 15,866,000	$ 10,520,000
Cost of revenue	12,552,000	7,134,000
Gross profit	3,314,000	3,386,000
Operating expenses:		
Salaries, wages and payroll taxes	2,283,000	1,872,000
Commissions	774,000	553,000
Professional fees	840,000	624,000
External Software development	353,000	310,000
General and administrative	1,401,000	1,316,000
Total operating expenses	5,651,000	4,675,000
Operating Loss	(2,337,000)	(1,289,000)
Other income (expense)		
Interest expense	(1,161,000)	(957,000)
Change in fair value of derivative liability	942,000	-

Total other income (expense)	(219,000)	(957,000)
Net Loss	$ (2,556,000)	$ (2,246,000)
Net loss per common share		
Basic and diluted	$ (2.86)	$ (3.11)
Weighted average number of common shares		
Basic and diluted	893,094	723,033

Revenue for the three months ended November 30, 2019, increased by $5.3 million or 50.8% to $15.9 million compared to $10.5 million for the three months ended November 30, 2018.

Gross billings are a non-GAAP measurement and are the metric in which we currently earn our revenue. Gross billings for the three months ended November 30, 2019, were earned from billings to clients to whom we provide HR and payroll services and consist of gross payroll, employer taxes, admin fees, and workers comp insurance premiums. Gross billings for the three months ended November 31, 2019, increased by 39.8 million or 56.1% to $110.7 million compared to $70.9 million for the three months ended November 30, 2018.

The gross payroll costs of our worksite employees account for 85.7 % and 85.2% of our gross billings for the three months ended November 30, 2019, and 2018, respectively. As such, the mark- up components of gross billings account for approximately 16.7% and 17.4% for the three months ended November 30, 2019, and 2018, respectively.

Revenues' increase was primarily due to the increase in worksite employee by an average of 3,521 to an average of 8,990 employees, compared to 5,470 employees in the three months ended November 30, 2017. Revenues are recognized ratably over the payroll period as worksite employees perform their service at the client worksite.

Cost of Revenues mainly includes the costs of employer-side taxes and workers' compensation insurance coverage. Our cost of revenues for the three months ended November 30, 2019, increased by $5.5 million or 75.9% to $12.6 million, compared to $7.1 million for the three months ended November 30, 2018. The above increase was impacted by the reversal of approximately $1.0 million of California Federal unemployment Tax during the three months ended November 30, 2018 and which did not recur in the fiscal 2020 quarter. Excluding this credit, the cost of revenues increase attributable to the increase in worksite employees is $4.5 million, or 55% of adjusted fiscal 2019 cost of revenues and is consistent with the increase in revenues and gross billings increases.

Approximately $3.4 million is attributed to the additional worksite employees the Company is servicing, which increased by 3,521 from an average of 5,470 employees for the three months ended November 30, 2017, to an average of 8,990 employees for the three months ended November 30, 2018.

Gross Profit for the three months ended November 30, 2019, decreased by $0.1 million or 2.1% to $3.3 million, compared to $3.4 million for the three months ended November 30, 2018. The November 2018 quarter had two non-recurring events that resulted in $1.1 million of non-recurring year over year gross profit differences including the $1.0 million tax credit mentioned above. Excluding the non-recurring items for fiscal 2019 described above, the first quarter fiscal 2020 gross profit increased $1.0 million or 43.7% from the recurring gross margin of the quarter ended November 30, 2018.

Operating Expenses

The following table presents certain information related to our operating expenses (unaudited)

	Three months ended November 30,		
	2019	**2018**	**% Change**
	(in thousands)	**(in thousands)**	
Salaries, wages and payroll taxes	$ 2,283	$ 1,872	21.9%
Commissions	774	553	40.0%
Professional fees	840	624	34.6%
External Software development	353	310	13.9%
General and Administrative	1,401	1,316	6.5%
Total operating expenses	$ 5,651	$ 4,675	20.9%

Operating expenses increased $1.0 million or 20.9% to $5.7 million for the three months ended November 30, 2019 from $4.7 million for the three months ended November 30, 2018. The components of operating expenses changed as follows:

Salaries, wages and payroll taxes consist of gross salaries, benefits, and payroll taxes associated with our executive management team and corporate employees and share based compensation and increased by $0.4 million or 21.9% from $1.9 million for the quarter ended November 30, 2018. The increase is due to the increase in corporate employees including the addition of our technical team hired to replace outside software developers at a higher average salary than previously hired corporate employees.

Table of Contents

Commissions consist of commissions payments made to third party brokers and inside sales personnel. Commissions increased by $0.2 million or 40.0% to $0.8 million, from $0.6 million in the quarter ended November 30, 2018. Commissions are primarily associated with compensation to our sales force for sales as well as to our property and casualty agents. Commission expenses approximates 0.71% and 0.78% of our gross billings for the quarters ended November 30, 2019 and 2018, respectively.

Professional fees consist of legal fees, accounting and public company costs, board fees, and consulting fees. Professional fees for the quarter ended November 30, 2019, increased by $0.2 million or 34.6% to $0.8 million, from $0.6 million for the quarter ended November 30, 2018. The increase is due to increased legal fees related to our note default and product development litigation.

External software development consists of payments to third party contractors for licenses, software development, IT related spending for the development of our HRIS platform and mobile application. External software development increased by $0.1 million, or 13.9% to $0.4 million from $0.3 million. The increase was due to increased license spending in the fiscal 2020 quarter and reduced contracted software development from the fiscal 2019 levels.

General and Administrative expenses consist of office rent and related overhead, marketing, insurance, penalties, business taxes, travel and entertainment, depreciation and amortization and other general business expenses. General and administrative expenses for the quarter ended November 30, 2019 increased by $0.1 million or 6.5% from $1.3 million for the quarter ended November 30, 2018. The increase is primarily due to higher depreciation and overhead offset by lower marketing spending.

Other expenses represented in the table below decreased from $0.9 million for the quarter ended November 30, 2018 to $0.2 million for the quarter ended November 30, 2019:

(unaudited)	**For the three months ended November 30,**	
	2019	**2018**
		(Restated)
Interest expense	(1,161,000)	(947,000)
Change in fair value of derivative liability	942,000	-
Total other income (expense)	(219,000)	(947,000)

Interest Expense consists of cash interest on interest bearing notes, financing charges for the excess of fair value over carrying amounts of notes issued during any reporting period, amortization of recorded discount and associated deferred financing costs, and acceleration of discounts and deferred financing costs due to early conversions on notes payable. Interest expense increased by $0.2 million to $1.2 million for the quarter ended November 30, 2019 from $0.9 million in the quarter ended November 30, 2018. The increase is due to the increased interest expense and financing costs associated with our March 2019 convertible notes offset by a reduction in the similar expenses for our June 2018 notes and $0.3 million of default interest accrued on the remaining notes payable.

Change in fair value of derivative: The balance for the quarter ended November 30, 2019 represents the reduction in fair value of the derivative liabilities recorded with the March 2019 Notes payable. No such derivative existed during the quarter ended November 30, 2018.

Net loss. As a result of the explanations described above, the net loss for the fiscal quarter ended November 30, 2019, was $2.6 million, compared to a net loss of $2.2 million in the prior quarter representing an increase of $0.4 million or 13.8%. The increase in net loss was due to $1.1 million of additional operating losses consisting of $0.2 million lower gross margins resulting from a one time tax credit in the November 2018 quarter of $1.0 million offset by additional gross margin from revenue increases, and a $0.9 million increase in the operating expenses. The increase in operating losses were reduced by

$0.5 million decrease in other expenses.

Liquidity and Capital Resources

As of November 30, 2019, the Company had cash of $0.1 million and a working capital deficiency of $18.5 million. During the quarter ended November 30, 2019, the Company used approximately $1.5 million of cash in its operations, consisting of a net loss of $2.6 million, reduced by net non-cash charges and gains of $0.3 million and working capital changes of $0.8 million. During the year ended August 31, 2019, the Company used approximately $2.1 million of cash in its operations, consisting of a net loss of $18.7 million, reduced by net non-cash charges and gains of $10.8 million and working capital changes of $6.0 million. The Company has incurred recurring losses resulted in an accumulated deficit of $48 million as of November 30, 2019. These conditions raise substantial doubt as to the Company's ability to continue as going concern within one year from issuance date of the financial statements.

The ability of the Company to continue as a going concern is dependent upon generating profitable operations in the future and obtaining additional funds by way of public or private offering to meet the Company's obligations and repay its liabilities when they become due. The Company has a recurring revenue business model that generated $12.4 million of gross profit for the year ended August 31, 2019 and $3.3 million for the quarter ended November 30, 2019..

The Company's plans and expectations for the next 12 months include raising additional capital to help fund expansion of its operations, including the continued development and support of its IT and HR platform and settling its outstanding debt as it comes due. The Company engaged an investment banking firm to assist the Company in (i) preparing information materials, (ii) advising the Company concerning the structure, price and conditions and (iii) organizing the marketing efforts with potential investors in connection with a financing transaction.

Historically, the Company's principal source of financing has come through the sale of its common stock and issuance of convertible notes. The Company successfully completed an Initial Public Offering (IPO) on NASDAQ on June 29, 2017, raising a total of $12 million ($10.9 million net of costs). In June 2018, the Company completed a private placement of 8% senior secured convertible notes to institutional investors raising $9 million of gross proceeds ($8.4 million net of costs). In March 2019, the Company completed a private placement of senior secured notes to institutional investors raising $3.75 million ($3.3 million net of costs). As of November 30, 2019, all of the $6.8 million of principal was in default. Subsequent to November 30, 2019, approximately $2.7 million of the notes in default were exchanged for new convertible notes payable. See Notes 4 and 9 for additional information.

Subsequent to November 30, 2019 and as described in Note 9, in January 2020, the Company assigned approximately 60% of its customer contracts representing approximately 50% of its recurring gross profit in exchange for $9.7 million in cash and expects to receive $9.5 million ratably over the four years following the transaction close, subject to certain closing conditions. The Company will transfer $1.7 million of working capital after closing the transaction and approximately $6 million of the Company's annualized gross profit.

The Company's management believes that the Company's current cash position, along with its revenue growth and the financing from potential institutional investors will be sufficient to fund its operations for at least a year from the date these financials are available. If these sources do not provide the capital necessary to fund the Company's operations during the next twelve months from the date of this report, the Company may need to curtail certain aspects of its operations or expansion activities, consider the sale of its assets, or consider other means of financing. The Company can give no assurance that it will be successful in implementing its business plan and obtaining financing on terms advantageous to the Company or that any such additional financing would be available to the Company. These condensed consolidated financial statements do not include any adjustments from this uncertainty.

Non-GAAP Financial Measures

In addition to financial measures presented in accordance with GAAP, we monitor other non-GAAP measures that we use to manage our business, make planning decisions and allocate resources. These key financial measures provide an additional view of our operational performance over the long term and provide useful information that we use to maintain and grow our business. The presentation of these non-GAAP financial measures is used to enhance the understanding of certain aspects of our financial performance. It is not meant to be considered in isolation, superior to, or as a substitute for the directly comparable financial measures presented in accordance with GAAP.

We report our revenues as gross billings, net of related direct labor costs, for our EAS clients and revenues without reduction of labor costs for staffing services clients. For the years ended August 31, 2019 and 2018, we had no revenues associated with staffing services or generated through our technology services. Gross billings represent billings to our business clients and include WSE gross wages, employer payroll taxes, and workers compensation premiums as well as admin fees for our value-added services and other charges for workforce management support. Gross billings are a non-GAAP measurement and represent a key operating metric for management along with number of WSEs and number of clients. Gross billings and the number of active worksite employees represent the primary drivers of our business operations. Active worksite employees (WSEs) are defined as an employee in our HRIS ecosystem that has provided services for at least one of our client customers for any reported period. Our primary profitability metrics are gross profit, gross profit per WSE, and gross profit percentage of gross billings.

Reconciliation of GAAP to Non-GAAP Measure: Gross Billings to Net Revenues

	For the quarter Ended November 30,	
	2019	**2018**
Gross Billings in millions	$ 110.7	$ 70.9
Less: Adjustment to gross billings	94.8	60.4
Revenues, in millions	$ 15.9	$ 10.5

	November 30, 2019	**August 31, 2019**	**November 30, 2018**
Active worksite employees (unaudited)	13,400	13,100	9,000

Material Commitments

We do not have any contractual obligations for ongoing capital expenditures at this time. We do, however, purchase equipment and software necessary to conduct our operations on an as needed basis.

Off-Balance Sheet Arrangements

We did not have during the periods presented, and we do not currently have, any off-balance sheet arrangements.

Contingencies

Certain conditions may exist as of the date the financial statements are issued, which may result in a loss to the Company, but which will be resolved only when one or more future events occur or fail to occur. The Company's management, in consultation with its legal counsel as appropriate, assesses such contingent liabilities, and such assessment inherently involves an exercise of judgment. In assessing loss contingencies related to legal proceedings that are pending against the Company or unasserted claims that may result in such proceedings, the Company, in consultation with legal counsel, evaluates the perceived merits of any legal proceedings or unasserted claims, as well as the perceived merits of the amount of relief sought or expected to be sought therein. If the assessment of a contingency indicates it is probable that a material loss has been incurred and the amount of the liability can be estimated, then the estimated liability would be accrued in the Company's financial statements. If the assessment indicates a potentially material loss contingency is not probable, but is reasonably possible, or is probable, but cannot be estimated, then the nature of the contingent liability, together with an estimate of the range of possible loss, if determinable and material, would be disclosed. Loss contingencies considered remote are generally not disclosed unless they involve guarantees, in which case the guarantees would be disclosed.

New and Recently Adopted Accounting Standards

For a listing of our new and recently adopted accounting standards, see note 2, Summary of significant accounting policies, of the Condensed Notes to the Consolidated Financial Statements in "Part I, Item 1. Condensed Consolidated Financial Statements (unaudited)" of this report.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Not applicable.

Item 4. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures

The Company has established disclosure controls and procedures to ensure that information required to be disclosed in this quarterly report on Form 10-Q was properly recorded, processed, summarized and reported within the time periods specified in the Commission's rules and forms. The Company's controls and procedures are designed to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Act is accumulated and communicated to the Company's management, including its principal executive and principal financial officers to allow timely decisions regarding required disclosure.

We carried out an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) at November 30, 2019, based on the evaluation of these controls and procedures required by paragraph (b) of Rule 13a-15 or Rule 15d-15 under the Exchange Act. This evaluation was carried out under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, at November 30, 2019, our disclosure controls and procedures are not effective.

Management's Updated Report on Internal Control Over Financial Reporting

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we conducted an updated evaluation as of November 30, 2019, of the evaluation of effectiveness of our internal control over financial reporting as of August 31, 2019, based on the framework stated by the Committee of Sponsoring Organizations of the Treadway Commission.

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rules 13a-15(f) and 15d-15(f) of the Exchange Act. Our internal control system was designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes, in accordance with generally accepted accounting principles. Because of inherent limitations, a system of internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate due to change in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Based on its updated evaluation as of November 30, 2019, our management concluded that our internal controls over financial reporting were not effective as of November 30, 2019. A material weakness is a deficiency, or a combination of control deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of the Company's annual or interim financial statements will not be prevented or detected on a timely basis.

The material weaknesses at November 30, 2019, relate to the following:

1. Lack of Adequate Finance and Accounting Personnel – The Company's current accounting staff is small, and during the first fiscal quarter of 2020 we did not have the required infrastructure or accounting staff expertise to adequately prepare financial statements in accordance with U.S. GAAP as well as meeting the higher demands of being a U.S. public company. We also lack adequate written policies and procedures for accounting and financial reporting with respect to the requirements and application of GAAP and SEC disclosure requirements. The lack of sufficient personnel creates inadequate segregation of duties, which makes the reporting process susceptible to errors, omissions, and inadequate review procedures. During 2019, the Company began to implement a plan to develop its accounting and finance staff to meet the needs of its growing business, including but not limited to the hiring of a new staff, departmental training and the development of entity level controls and mitigating activity level controls to reduce the risk of management override resulting from inadequate segregation of duties. The Company is in the process of finalizing written policies and procedures to formalize the requirements of GAAP and SEC disclosure requirements.

The Company did not perform an effective risk assessment or monitor internal controls over financial reporting including completing the documentation and procedures surrounding its IT environment, controls over cut-off procedures, a related party transaction, accounting for certain default penalty accruals, segregation of duties, and corporate oversight functions. The Company will continue its assessment on a quarterly basis. During the reporting of the third quarter of fiscal 2019, we discovered a material misstatement in the calculation and reporting of its derivative financial instruments, resulting in amended SEC filings. During the reporting of the fiscal year ending August 31, 2019 we also discovered issues surrounding the accounting of our senior notes, including the note discount, amortization of the note discount, default penalty accrual, and for related party transactions, all of which could have resulted in significant adjustments to our financial statements. We have reviewed and addressed the control inadequacies that resulted in this misstatement by hiring a new Chief Financial Officer with experience in the financial instruments that give rise to the complex accounting requirements and providing for additional accounting resources to enhance the internal control structure. The Company plans to hire additional personnel and external resources to further mitigate these material weaknesses.

Changes in Internal Control Over Financial Reporting

During the quarter ended November 30, 2019, there have been no changes in the Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Table of Contents

PART II — OTHER INFORMATION

Item 1. Legal Proceedings and Risk Factors.

(a) Legal Proceedings.

The Company is a party to various legal actions arising in the ordinary course of business which, in the opinion of the Company, are not material in that management either expects that the Company will be successful on the merits of the pending cases or that any liabilities resulting from such cases will be substantially covered by insurance. While it is impossible to estimate with certainty the ultimate legal and financial liability with respect to these actions, management believes that the aggregate amount of such liabilities will not be material to the results of operations, financial position or cash flows of the Company. There have been no material developments to the litigations disclosed in our Annual Report in Form 10-K except as noted in Note 7 to the financial statements

(b) Risk Factors.

Not required.

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

None

Item 3. Defaults Upon Senior Securities.

On June 4, 2018, the Company issued convertible notes in the principal amount of $10 million for a purchase price of $9 million to institutional investors, bearing interest at a rate of 8%, with maturity date of September 4, 2019, for cash proceeds of $8.4million. The Company executed registration rights agreements with each of its institutional investors. These registrations rights agreements required, among other things, that the initial registration statement should be (a) filed within 30 days of June 4, 2018 and (b) declared effective within 90 days of June 4, 2018. Our registration statement was filed on October 1, 2018, and it was declared effective on October 29, 2018.

Item 4. Mine Safety Disclosures.

Not applicable.

Item 5. Other Information.

Not applicable.

Table of Contents

Item 6. Exhibits.

(a) Exhibits.

Exhibit No.	Document Description
31.1	CERTIFICATION OF CHIEF EXECUTIVE OFFICER PURSUANT TO EXCHANGE ACT RULE 13a-14(a), AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002.
31.2	CERTIFICATION OF CHIEF FINANCIAL OFFICER PURSUANT TO EXCHANGE ACT RULE 13a-14(a), AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002.
32.1*	CERTIFICATION OF CHIEF EXECUTIVE OFFICER PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEYACT OF 2002.
32.2*	CERTIFICATION OF CHIEF FINANCIAL OFFICER PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEYACT OF 2002.
Exhibit 101	Interactive data files formatted in XBRL (eXtensible Business Reporting Language): (i) the Condensed Consolidated Balance Sheets, (ii) the Condensed Consolidated Statements of Operations, (iii) the Condensed Consolidated Statements of Cash Flows, and (iv) the Notes to the Condensed Consolidated Financial Statements.**
101.INS	XBRL Instance Document**
101.SCH	XBRL Taxonomy Extension Schema Document**
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document**
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document**
101.LAB	XBRL Taxonomy Extension Label Linkbase Document**
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document**

* This exhibit shall not be deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934 or otherwise subject to the liabilities of that section, nor shall it be deemed incorporated by reference in any filing under the Securities Act of 1933 of the Securities Exchange Act of 1934, whether made before or after the date hereof and irrespective of any general incorporation language in any filings.

** XBRL (Extensible Business Reporting Language) information is furnished and not filed or a part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, is deemed not filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and otherwise is not subject to liability under these sections.

Table of Contents

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.

ShiftPixy, Inc.,
a Wyoming corporation

DATE: January 21, 2020

By: */s/ Scott W. Absher*
Scott W. Absher
Principal Executive Officer

In accordance with the Exchange Act, this Report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

SIGNATURE	NAME	TITLE	DATE
/s/ Scott W. Absher	Scott W. Absher	Principal Executive Officer and Director	January 21, 2020
/s/ Domonic J. Carney	Domonic J. Carney	Principal Financial Officer	January 21, 2020

Table of Contents

EXHIBIT INDEX

Exhibit No.	Document Description
31.1	CERTIFICATION OF CHIEF EXECUTIVE OFFICER PURSUANT TO EXCHANGE ACT RULE 13a-14(a), AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002.
31.2	CERTIFICATION OF CHIEF FINANCIAL OFFICER PURSUANT TO EXCHANGE ACT RULE 13a-14(a), AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002
32.1 *	CERTIFICATION OF CHIEF EXECUTIVE OFFICER PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEYACT OF 2002.
32.2 *	CERTIFICATION OF CHIEF FINANCIAL OFFICER PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEYACT OF 2002.
Exhibit 101	Interactive data files formatted in XBRL (eXtensible Business Reporting Language): (i) the Condensed Consolidated Balance Sheets, (ii) the Condensed Consolidated Statements of Operations, (iii) the Condensed Consolidated Statements of Cash Flows, and (iv) the Notes to the Condensed Consolidated Financial Statements.**
101.INS	XBRL Instance Document**
101.SCH	XBRL Taxonomy Extension Schema Document**
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document**
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document**
101.LAB	XBRL Taxonomy Extension Label Linkbase Document**
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document**

* This exhibit shall not be deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934 or otherwise subject to the liabilities of that section, nor shall it be deemed incorporated by reference in any filing under the Securities Act of 1933 of the Securities Exchange Act of 1934, whether made before or after the date hereof and irrespective of any general incorporation language in any filings.

** XBRL (Extensible Business Reporting Language) information is furnished and not filed or a part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, is deemed not filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and otherwise is not subject to liability under these sections.

EXHIBIT 31.1

CERTIFICATION

I, Scott W. Absher, certify that:

1. I have reviewed this report on Form 10-Q of ShiftPixy, Inc.;

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

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

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

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

   b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

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

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

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

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

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

ShiftPixy, Inc.

DATE: January 21, 2020

By: */s/ Scott W. Absher*
Scott W. Absher
Chief Executive Officer

EXHIBIT 31.2

CERTIFICATION

I, Domonic J. Carney, certify that:

1. I have reviewed this report on Form 10-Q of ShiftPixy, Inc.;

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

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

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

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

   b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

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

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

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

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

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

DATE: January 21, 2020

By: */s/ Domonic J. Carney*
Domonic J. Carney
Chief Financial Officer

EXHIBIT 32.1

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

Pursuant to 18 U.S.C. § 1350, as adopted pursuant to Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned hereby certifies that the Quarterly Report on Form 10-Q for the period ended November 30, 2019, of ShiftPixy, Inc. (the "Company") fully complies with the requirements of Section 13(a) or Section 15(d) of the Securities Exchange Act of 1934 and that the information contained in such Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

ShiftPixy, Inc.

DATE: January 21, 2020

By: */s/ Scott W. Absher*
Scott W. Absher
Chief Executive Officer

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement required by Section 906, has been provided to ShiftPixy, Inc., and will be retained by ShiftPixy, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.

EXHIBIT 32.2

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

Pursuant to 18 U.S.C. § 1350, as adopted pursuant to Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned hereby certifies that the Quarterly Report on Form 10-Q for the period ended November 30, 2019, of ShiftPixy, Inc. (the "Company") fully complies with the requirements of Section 13(a) or Section 15(d) of the Securities Exchange Act of 1934 and that the information contained in such Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

DATE: January 21, 2020

By: */s/ Domonic J. Carney*
Domonic J. Carney
Chief Financial Officer

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement required by Section 906, has been provided to ShiftPixy, Inc. and will be retained by ShiftPixy, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.