FRANKLY INC.

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PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

Frankly Inc. and Subsidiaries
Condensed Consolidated Balance Sheets

	March 31, 2018 (Unaudited)	December 31, 2017
Assets		
Current Assets		
Cash and cash equivalents	$ 757,673	$ 1,254,886
Restricted cash	634,115	634,115
Accounts receivable, net	2,214,409	3,483,347
Prepaid expenses and other current assets	489,984	535,111
Total Current Assets	**4,096,181**	**5,907,459**
Property & equipment, net	851,351	985,321
Software development costs, net	6,872,693	6,972,741
Intangible assets, net	6,543,882	6,762,216
Other assets	299,651	311,046
Total Assets	**$ 18,663,758**	$ **20,938,783**
Liabilities and Shareholders' Deficit		
Current Liabilities		
Accounts payable	$ 5,852,024	$ 5,740,788
Accrued expenses	2,224,133	1,717,030
Capital leases, current portion	-	40,449
Deferred revenue	36,103	92,279
Due to related parties	4,443,931	5,090,358
Total Current Liabilities	**12,556,191**	**12,680,904**
Non-revolving credit facility, net	13,672,478	12,155,573
Deferred rent	34,146	35,882
Other liabilities	743,234	840,973
Total Liabilities	**27,006,049**	**25,713,332**
Commitments and Contingencies (Note 10)		
Shareholders' Deficit		
Common shares, no par value, unlimited shares authorized, 2,304,834 and 2,226,861 shares outstanding as of March 31, 2018 and December 31, 2017, respectively	-	-
Class A restricted voting shares, no par value, unlimited shares authorized, 0 shares outstanding as of March 31, 2018 and December 31, 2017	-	-
Additional paid-in capital	66,362,525	66,127,485
Accumulated deficit	(74,645,823)	(70,836,330)
Accumulated other comprehensive loss	(58,993)	(65,704)
Total Shareholders' Deficit	**(8,342,291)**	**(4,774,549)**
Total Liabilities and Shareholders' Deficit	**$ 18,663,758**	**$ 20,938,783**

See accompanying notes to the condensed consolidated financial statements.

Frankly Inc. and Subsidiaries
Condensed Consolidated Statements of
Operations and Comprehensive Loss – Unaudited

	Three Months Ended March 31,	
	2018	2017
Total Revenue	$ **5,761,858**	$ **6,359,154**
Costs and operating expenses:		
Cost of revenue (excluding depreciation and amortization)	2,725,279	2,760,414
General and administrative (excluding depreciation and amortization)	2,475,698	1,892,983
Selling and marketing	462,020	663,684
Research and development (excluding depreciation and amortization)	1,079,772	848,415
Depreciation and amortization	1,147,245	1,066,731
Transaction costs	24,673	-
Restructuring expense	460,960	-
Retention expense	588,099	-
Other expense	-	27,017
Loss from operations	**(3,201,888)**	**(900,090)**
Foreign exchange loss (gain)	10,509	(6,476)
Interest expense, net	597,096	610,205
Loss before income tax expense	**(3,809,493)**	**(1,503,819)**
Income tax expense	-	-
Net Loss	$ **(3,809,493)**	$ **(1,503,819)**
Other Comprehensive Net Loss		
Foreign currency translation	6,711	(3,876)
Comprehensive Net Loss	$ **(3,802,782)**	$ **(1,507,695)**
Basic and Diluted Net Loss Per Share	$ **(1.70)**	$ **(0.71)**
Basic and Diluted Weighted-Average Common and Class A Restricted Voting Shares Outstanding	**2,236,209**	**2,129,464**

See accompanying notes to the condensed consolidated financial statements.

Frankly Inc. and Subsidiaries
Condensed Consolidated Statements of
Shareholders' Equity (Deficit) – Unaudited

	Common Shares	Class A Restricted Voting Shares	Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity (Deficit)
Balance, December 31, 2017	**2,226,861**	**-**	**$66,127,485**	**$ (70,836,330)**	**$ (65,704)**	**$ (4,774,549)**
Vesting of restricted share units	77,973	-	-	-	-	-
Stock-based compensation	-	-	235,040	-	-	235,040
Net loss	-	-	-	(3,809,493)	-	(3,809,493)
Other comprehensive loss	-	-	-	-	6,711	6,711
Balance, March 31, 2018	**2,304,834**	**-**	**$66,362,525**	**$ (74,645,823)**	**$ (58,993)**	**$ (8,342,291)**
Balance, December 31, 2016	**2,030,800**	**97,674**	**$64,986,368**	**$ (53,642,691)**	**$ (39,466)**	**$ 11,304,211**
Vesting of restricted share units	5,038	-	-	-	-	-
Stock-based compensation	-	-	228,166	-	-	228,166
Net loss	-	-	-	(1,503,819)	-	(1,503,819)
Other comprehensive loss	-	-	-	-	(3,876)	(3,876)
Balance, March 31, 2017	**2,035,838**	**97,674**	**$65,214,534**	**$ (55,146,510)**	**$ (43,342)**	**$ 10,024,682**

See accompanying notes to the condensed consolidated financial statements.

Frankly Inc. and Subsidiaries
Condensed Consolidated Statements of
Cash Flows – Unaudited

	Three Months Ended March 31,	
	2018	**2017**
Cash flows from operating activities		
Net loss	**$ (3,809,493)**	**$ (1,503,819)**
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	1,147,245	1,066,731
Amortization of debt discount	144,099	145,436
Amortization of deferred financing costs	10,340	26,534
Stock-based compensation expense	235,040	228,166
Deferred interest	362,466	-
Provision for bad debt expense	687,806	-
Changes in assets and liabilities:		
Accounts receivable	581,132	(140,550)
Prepaid expenses and other current assets	41,835	(421,396)
Other assets	11,395	43,402
Accounts payable	114,515	(1,854,889)
Accrued expenses	503,091	(127,277)
Deferred revenue	(56,176)	(7,154)
Due to related parties	(646,427)	1,167,749
Deferred rent and other liabilities	(99,475)	(51,302)
Net cash used in operating activities	**(772,607)**	**(1,428,369)**
Cash flows from investing activities		
Capitalized software costs	(694,892)	(636,863)
Purchases of property & equipment	-	(9,582)
Net cash used in investing activities	**(694,892)**	**(646,445)**
Cash flows from financing activities		
Revolving credit facility payments	-	(56,225)
Capital lease payments	(40,449)	(48,887)
Proceeds from issuance of debt	1,000,000	-
Net cash provided by (used in) financing activities	**959,551**	**(105,112)**
Effect of exchange rate changes on cash	10,735	4,662
Net change in cash and cash equivalents	**(497,213)**	**(2,175,264)**
Cash and cash equivalents at beginning of period	1,254,886	6,053,203
Cash and cash equivalents at end of period	**$ 757,673**	**$ 3,877,939**
Supplemental cash flow disclosure		
Cash paid for interest	$ 123,430	$ 380,237
Cash paid for income taxes	-	-

See accompanying notes to the condensed consolidated financial statements.

1. Description of Business and Going Concern

Description of Business

Frankly Inc. ("Frankly") has been operating since the incorporation of its predecessor, TicToc Planet Inc., on September 10, 2012. These consolidated financial statements include Frankly and its subsidiaries (Frankly Co. and Frankly Media LLC), together referred to as the "Company."

The Company helps TV broadcasters and media companies transform their traditional business from just delivering content over-the-air via broadcast television to distributing content in multi-platform, digital formats on new platforms such as mobile, tablets, desktop and other connected devices. The Company's core product is a white-labeled software platform that enables media companies to publish their official content onto multiscreen devices, increase social interaction on those multiscreen experiences, and enable digital advertising. The platform consists of a content management system ("CMS") platform, native mobile and over-the-top ("OTT") applications, responsive web framework, digital video solutions and digital advertising solutions. The Company generates revenues by charging monthly recurring software licensing fees, variable usage fees for our platform and sharing digital advertising revenue with our customers.

Going Concern

These condensed consolidated financial statements have been prepared on the assumption that the Company is a going concern, which contemplates the realization of its assets and the settlement of its liabilities in the normal course of operations.

As of March 31, 2018, the Company has an accumulated deficit of $74.6 million, representative of recurring losses since inception. Additionally, the Company has not generated positive cash flow from operations since inception when excluding changes in working capital. Beginning January 1, 2018, the billing for all services provided to Raycom are being applied to the advance agreement balance as of December 31, 2017 in the amount of $4,896,585 ($3,805,278 as of March 31, 2018) and Raycom will not be required to make cash payments for services provided by the Company until the balance has been fully repaid. These conditions raise substantial doubt about the Company's ability to continue as a going concern within one year after the issuance of its financial statements.

To reduce its operating cash needs, in February 2018, the Company executed a reduction-in-force that removed approximately 20 full-time employees from its headcount. In addition, the Company subleased its remaining office space in San Francisco, CA and is pursuing other areas where operating expenses can be reduced. On March 13, 2018, the Company received $1 million under the existing credit agreement with Raycom, bringing the total outstanding principal balance under the credit agreement to $15.5 million. On May 8, 2018, the Company entered into an amendment of the 2016 credit agreement, whereby Raycom will provide the Company with an additional $7.5 million of funding, to be paid in installments over a six-month period, subject to the Company's achievement of certain operational milestones. The $1.0 million advanced to the Company on March 13, 2018 is included in the additional $7.5 million funding noted above. Upon the Company's receipt of all of the additional funding under the amended credit agreement, the total outstanding principal balance under the amended credit agreement would be $22.0 million. The additional credit facility will be primarily used to get the Company current with its vendor and customer national revenue share payables as well as offset the operational cash outflow associated with the utilization of the $3.8 million advance agreement balance as of March 31, 2018 discussed above. There can be no assurance that the Company will achieve the operational milestones to obtain the additional advances from Raycom, or that those advances, if obtained, will provide adequate funding to sustain the Company's operations and execute its business plan through the next 12 months from the date of this filing.

2. Summary of Significant Accounting Policies

Basis of Presentation and Use of Estimates

The unaudited interim condensed consolidated financial statements and accompanying notes have been prepared in accordance with United States generally accepted accounting principles ("U.S. GAAP") and include the accounts of Frankly Inc. and its wholly-owned subsidiaries Frankly Co. and Frankly Media LLC. All intercompany balances and transactions have been eliminated in consolidation. In the opinion of the Company's management, the unaudited interim condensed consolidated financial statements include all adjustments, which include only normal recurring adjustments, necessary for the fair presentation of the Company's financial position for the periods presented. These unaudited interim condensed consolidated financial statements are not necessarily indicative of the results expected for the full fiscal year or for any subsequent period.

The accompanying condensed consolidated balance sheet as of December 31, 2017 was derived from the audited financial statements as of that date, but does not include all the information and footnotes required by U.S. GAAP. These unaudited interim condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes for the year ended December 31, 2017, included within the Company's Form 10-K as filed with the U.S. Securities and Exchange Commission on April 2, 2018.

Accounting Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates, judgments and assumptions that affect the amounts reported and disclosed in the condensed consolidated financial statements and the accompanying notes. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable, the results of which form the basis for making judgments about the carrying values of assets and liabilities. Such estimates primarily relate to unsettled transactions and events as of the date of the condensed consolidated financial statements. Accordingly, actual results may differ from estimated amounts.

Accounts Receivable and Concentrations of Risk

Accounts receivable are subject to credit risk and as of March 31, 2018 and December 31, 2017, two customers each accounted for greater than 10% of the Company's accounts receivable balance. In total, these customers accounted for 40% and 26% of the Company's accounts receivable balance as of March 31, 2018 and December 31, 2017, respectively. Additionally, approximately 42% and 38% of the Company's revenue for the three months ended March 31, 2018 and 2017, respectively, was generated from two customers, that each accounted for greater than 10% of the Company's total revenue. In addition, the allowance for doubtful accounts was $757,806 and $70,000 as of March 31, 2018 and December 31, 2017, respectively.

Recently Issued Accounting Pronouncements

The Company is an "emerging growth company" ("EGC") as defined by the Jumpstart Our Business Startups ("JOBS") Act of 2012. The JOBS Act provides that an emerging growth company can take advantage of the extended transition period provided in Section 7(a)(2)(B) of the Securities Act for complying with new or revised accounting standards. In other words, an emerging growth company can selectively delay the adoption of certain accounting standards until those standards would otherwise apply to private companies. The Company has elected to avail itself of this exemption and, as a result, its financial statements may not be comparable to the financial statements of issuers that are required to comply with the effective dates for new or revised accounting standards that are applicable to public companies. Section 107 of the JOBS Act provides that the Company can elect to opt out of the extended transition period at any time, which election is irrevocable.

ASU 2014-09: Revenue from Contracts with Customers (Topic 606) — In May 2014, the Financial Accounting Standards Board ("FASB"), issued Accounting Standards Update ("ASU") 2014-09, "Revenue from Contracts with Customers." The new topic will replace Topic 605, "Revenue Recognition," and creates modifications to various other revenue accounting standards for specialized transactions and industries. The topic is intended to conform revenue accounting principles with a concurrently issued International Financial Reporting Standards to reconcile previously differing treatment between U.S. practices and those of the rest of the world and to enhance disclosures related to disaggregated revenue information. The updated guidance is effective for interim and annual reporting periods beginning on or after December 15, 2018, for private companies; this effective date is applicable for the Company due to the JOBS Act exemption described above. Therefore, the Company plans to adopt this ASU on January 1, 2019 and plans to use the modified retrospective method. The Company will further evaluate during 2018, the anticipated impact of the adoption of this updated guidance on its consolidated financial statements.

ASU 2016-02: Leases (Topic 842) — In February 2016, the FASB issued ASU 2016-02, which requires a lessee to recognize assets and liabilities on its consolidated balance sheet for leases with accounting lease terms of more than 12 months. ASU 2016-02 will replace most existing lease accounting guidance in U.S. GAAP when it becomes effective. The new standard states that a lessee will recognize a lease liability for the obligation to make lease payments and a right-of-use asset for the right to use the underlying asset for the lease term. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the consolidated statements of operations. ASU 2016-02 will be effective for the Company as an EGC in 2020 and requires the modified retrospective method of adoption. Although the Company is currently evaluating the effect that ASU 2016-02 will have on its consolidated financial statements and related disclosures, the Company expects that most of its operating lease commitments will be subject to the new standard and recognized as operating lease liabilities and right-of-use assets upon adoption.

ASU 2016-18: Statement of Cash Flows (Topic 230), Restricted Cash — In November 2016, the FASB issued ASU 2016-18, which requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. ASU 2016-18 will be effective for the Company as an EGC in 2019. Early adoption is permitted, including adoption in an interim period. The adoption of this ASU will not have a significant impact on the consolidated financial statements.

Recently Adopted

ASU 2016-15: Statement of Cash Flows (Topic 230), Classification of Certain Cash Receipts and Cash Payments — In August 2016, the FASB issued ASU 2016-15, which provides guidance related to cash flows presentation and is effective for annual reporting periods beginning after December 15, 2017, subject to early adoption, which is permitted using a retrospective transition approach. ASU 2016-15 is intended to standardize the classification of certain cash receipts and cash payments in the Statement of Cash Flows, and was effective for the Company in its first quarter of fiscal 2018. The adoption of this ASU did not have a significant impact on the Company's consolidated financial statements.

3. Acquisition of Worldnow

On July 28, 2015, the Company signed an agreement (the "Purchase Agreement") to purchase all of the outstanding units of Gannaway Web Holdings LLC, operating as Worldnow, for total consideration of $45,000,000. On August 25, 2015 (the "Closing Date"), the Company completed the acquisition of Worldnow. Subsequent to the acquisition, Worldnow changed its name to Frankly Media LLC. The acquisition of Worldnow was made primarily to extend the reach of Frankly to Worldnow's existing customer base within the local broadcast marketplace.

Under the terms of the Purchase Agreement, the Company paid $10,000,000 in cash, issued $20,000,000 in Class A restricted voting shares of the Company (the "Share Consideration") and executed promissory notes to two shareholders of Worldnow bearing simple interest at a rate of 5 percent per year and agreed to pay $15,000,000 on August 31, 2016 (Note 7).

4. Restructuring Expense

Following an extensive process to explore and evaluate strategic alternatives, the Company's Board of Directors, led by the Strategic Committee, determined the best path for the Company at that time was to pursue internal growth opportunities and focus on further optimizing its operations. In an effort to reduce its operating cash needs, in February 2018, the Company executed a reduction-in-force that removed approximately 20 full-time employees from its headcount. In addition, the Company subleased its remaining office space in San Francisco, CA and is pursuing other areas where operating expenses can be reduced. The restructuring also included a reorganization of the senior management team. Effective April 12, 2018, the Company's CEO resigned and was succeeded by the Company's former COO and CFO. A number of other senior management changes were implemented on the same date. The restructuring plan is expected to be completed by the end of the second quarter of 2018. The Company accounted for the one-time termination benefits and certain contract costs in accordance with ASC 420 – Exit or Disposal Cost Obligations.

The following table summarizes the changes in the restructuring liability (included in accrued expenses) for the periods presented, by each major type of cost associated with the restructuring activity:

	One-time Termination Benefits	Contract Costs	Total
Balance, December 31, 2017	$ -	$ -	$ -
Restructuring expense	361,884	99,076	460,960
Payments	(134,150)	-	(134,150)
Adjustments	-	-	-
Balance, March 31, 2018	$ 227,734	$ 99,076	$ 326,810

5. Related Party Transactions and Balances

The Company has several significant shareholders as follows: Raycom Media Inc. ("Raycom"), SKP America LLC ("SKP America") and Gannaway Entertainment Inc. ("GEI") which each owned approximately 23.7%, 23.7% and 7.7%, respectively, as of March 31, 2018 and 24.6%, 24.5% and 8.0%, respectively, as of December 31, 2017 of the aggregate common shares and Class A restricted voting shares.

The following table summarizes related party balances in the condensed consolidated balance sheets for the periods presented:

Amounts Due (to) from Related Parties	**March 31, 2018**	**December 31, 2017**
	(Unaudited)	
Non-revolving credit facility, net		
Raycom	$ 13,672,478	$ 12,155,573
Due (to) from Raycom:		
Accounts receivable, net	-	427,489
Accounts payable	(307,422)	(275,960)
Accrued expenses	(389,564)	(432,802)
Deferred revenue	(3,805,278)	(4,896,585)
Total due to Raycom	(4,502,264)	(5,177,858)
Due from Mobdub:		
Prepaid expenses and other current assets	58,333	87,500
Total due from Mobdub	58,333	87,500
Total due (to) from related parties	$ (4,443,931)	$ (5,090,358)

The following table summarizes related party transactions in the condensed consolidated statements of operations and comprehensive loss for the periods presented:

	Three Months Ended March 31,	
Revenue (Expense) from Related Parties	**2018**	**2017**
	(Unaudited)	(Unaudited)
Raycom:		
Revenue	$ 1,222,065	$ 1,361,884
Interest on non-revolving credit facility	(516,904)	(510,080)
Interest on the Advance Agreement	(79,913)	(57,998)
	625,248	793,806
Mobdub:		
License fees	(29,167)	(29,167)
	(29,167)	(29,167)
	$ 596,081	$ 764,639

Raycom

As partial consideration for the acquisition of Worldnow on August 25, 2015, the Company issued a $4,000,000 promissory note to Raycom and 397,126 Class A restricted voting shares (Note 3). The note bore interest at 5% per annum and was due on August 31, 2016 (Note 7). Raycom was a customer and significant shareholder of Worldnow and, subsequent to the acquisition of Worldnow, remains a customer and significant shareholder of Frankly. Accordingly, during the three months ended March 31, 2018 and 2017, revenue-related transactions and balances with Raycom arose in the ordinary course of business.

On September 1, 2016, the Company completed the closing of its financing with Raycom (Note 7). The Company received a non-revolving term line of credit from Raycom in the principal amount of $14.5 million and, subject to approval of Raycom, an additional available $1.5 million non-revolving line of credit (collectively, the "Loan"). The proceeds were used to pay down $14 million of the $15 million outstanding promissory notes. In addition, Raycom converted the remaining $1.0 million of its existing $4.0 million promissory note from the Company into 150,200 common shares of the Company and the Company issued 871,160 common share purchase warrants to Raycom. The Loan was recorded at fair value of $11,578,593 with the remaining $2,921,407 being allocated to the warrants. On March 13, 2018, the Company received $1 million of the additional $1.5 million available under the Loan, bringing the total outstanding principal balance to $15.5 million. The carrying value of the Loan at March 31, 2018 and December 31, 2017, net of debt discount and deferred financing costs, was $13,672,478 and $12,155,573, respectively. Interest expense on the Loan for the three months ended March 31, 2018 and 2017, respectively, amounted to $516,904 and $510,080 and is presented within interest expense, net on the consolidated statements of operations and comprehensive loss.

On December 22, 2016, Raycom pre-paid $3 million of future fees for services to be provided by the Company (the "Advance Agreement"). On March 30, 2017, the Company entered into an amendment to the Advance Agreement pursuant to which Raycom pre-paid an additional $2 million of future fees for services to be provided by the Company. In connection with the Advance Agreement, the Company recognized interest expense of $79,913 and $57,998, for the three months ended March 31, 2018 and 2017, respectively. All services provided by the Company to Raycom since January 1, 2018 are being applied to the Advance Agreement balance.

Mobdub

The Company has a license agreement with a company that is owned by an officer of the Company. The agreement is for licensing of mobile applications and has a total contract value of $350,000. The period of the agreement is three years and commenced on October 14, 2015.

6. Long-Lived Assets

All of the Company's long-lived assets are domiciled in the U.S. Depreciation and amortization expense for long-lived assets was as follows for the periods presented:

	Three Months Ended March 31,	
	2018	**2017**
	(Unaudited)	(Unaudited)
Depreciation of property and equipment	$ 133,971	$ 154,849
Amortization of capitalized software	794,940	693,548
Amortization of other intangibles	218,334	218,334
Total depreciation and amortization	$ 1,147,245	$ 1,066,731

Property and Equipment, Net

The following table summarizes property and equipment, net, including assets held under capital lease:

	March 31, 2018	**December 31, 2017**
	(Unaudited)	
Cost:		
Office and computer equipment and software	$ 2,064,675	$ 2,064,676
Leasehold improvements	603,978	603,978
	2,668,653	2,668,654
Accumulated depreciation and amortization:		
Office and computer equipment and software	(1,520,897)	(1,416,140)
Leasehold improvements	(296,405)	(267,193)
	(1,817,302)	(1,683,333)
	$ 851,351	$ 985,321

Depreciation expense for assets held under capital lease for the three months ended March 31, 2018 and 2017, respectively, was $0 and $35,950. The net carrying value of assets held under capital lease was $0 and $262,747 as of March 31, 2018 and December 31, 2017, respectively.

Software Development Costs, Net

The following table summarizes software development costs, net for the periods presented:

	March 31, 2018 (Unaudited)	December 31, 2017
Cost	$ 12,815,681	$ 12,120,789
Accumulated amortization	(5,942,988)	(5,148,048)
	$ 6,872,693	$ 6,972,741

During the three months ended March 31, 2018 and 2017, the Company capitalized software development costs of $694,892 and $636,863, respectively.

Intangible Assets, Net

The following table summarizes intangible assets, net for the periods presented:

	March 31, 2018 (Unaudited)	December 31, 2017
Cost:		
Broadcast relationships, 12-year useful life	$ 7,600,000	$ 7,600,000
Advertiser relationships, 5-year useful life	1,200,000	1,200,000
	8,800,000	8,800,000
Accumulated amortization:		
Broadcast relationships	(1,636,118)	(1,477,784)
Advertiser relationships	(620,000)	(560,000)
	(2,256,118)	(2,037,784)
	$ 6,543,882	$ 6,762,216

7. Debt

Non-revolving Credit Facility

On September 1, 2016, the Company completed the closing of its financing with Raycom, a related party (Note 5). The Company received a non-revolving term line of credit from Raycom in the principal amount of $14.5 million and, subject to approval of Raycom, an additional available $1.5 million non-revolving line of credit. In addition, Raycom converted $1.0 million of its existing $4.0 million promissory note from the Company into 150,200 common shares of the Company and the Company issued 871,160 warrants to Raycom entitling the holder of each warrant to acquire one common share of the Company upon exercise of each warrant at a price per common share equal to CDN$8.50 ($6.63 based on the exchange rate at August 18, 2016). The warrants will expire on the earlier of: (i) the repayment of the Loan in accordance with its terms; and (ii) 5 years. To the extent that there is a mandatory repayment of any portion of the principal balance of the Loan, a proportionate number of the warrants will have their term reduced to the later of one year from issuance and 30 days from the date of such repayment. On March 13, 2018, the Company received $1 million of the additional $1.5 million available under the Loan, bringing the total outstanding principal balance to $15.5 million.

The warrants were recorded within shareholders' equity (deficit) in accordance with ASC 470-20 - *Debt With Conversion and Other Options*. Proceeds from the sale of the debt instrument with stock purchase warrants (detachable call options) were allocated to the two elements based on the relative fair values of the debt instrument without the warrants and of the warrants themselves at time of issuance. The value allocated to the Loan with Raycom was $11,578,593 with the remaining $2,921,407 being allocated to the warrants. The fair value of the 871,160 warrants issued were estimated based on the Black-Scholes pricing model, using the following assumptions: 1) Dividend yield of 0%, 2) Risk free rate of 0.66% for 751,000 warrants and 0.56% for 120,160 warrants, 3) Volatility of 71.14%, 4) Expected term of 5 years for 751,000 warrants and 7 months for 120,160 warrants, and 5) Forfeiture rate of 0%.

The debt discount of $2,921,407 is being amortized to interest expense, net on the consolidated statement of operations and comprehensive loss using the effective-interest method. Amortization of debt discount included in interest expense, net for the three months ended March 31, 2018 and 2017 amounted to $144,099 and $145,436, respectively. In accordance with ASC 470-50 - *Debt Modifications and Extinguishments*, the Company accounted for the refinancing transaction as an extinguishment of debt. The Company incurred legal fees directly related to the refinancing of $206,805, which were recorded as deferred financing costs and recorded against the carrying value of the Loan. Amortization of deferred financing costs included in interest expense, net for the three months ended March 31, 2018 and 2017 amounted to $10,340 and $7,110, respectively.

Prior to the completion of the financing arrangements, Raycom held 397,125 voting shares of the Company, which represented approximately 21% of the issued and outstanding voting shares of the Company. Immediately following the completion of the financing transactions, Raycom held 547,325 voting shares of the Company and 871,160 warrants, which collectively represented approximately 27% of the issued and outstanding voting shares of the Company on a non-diluted basis.

The proceeds of the Loan were used to pay off the outstanding $15.0 million of promissory notes issued by the Company in connection with the 2015 acquisition of Worldnow, including $3.0 million of the $4.0 million of such notes issued to Raycom, with the remaining $1.0 million promissory note balance owed to Raycom being converted to common shares of the Company as described above.

The Loan has a five-year term and is secured by the grant of a security interest in the Company's assets, a pledge of shares of the Company's subsidiaries and a guarantee by the Company's subsidiaries secured by their assets. Simultaneously, the Company and Raycom also entered into a software code escrow agreement. The software code escrow agreement required the Company to provide source code of its software products with a third party escrow agent.

Interest on outstanding balances of the Loan will accrue at a rate of 10% per annum, with a default interest rate of 12% per annum. The Loan is subject to certain scheduled mandatory principal repayments, with additional mandatory repayments occurring upon the Company's raising of additional financing, sales of assets and excess cash flow.

In addition, the Company must maintain certain leverage ratios and interest coverage ratios beginning with the fiscal quarter ending December 31, 2017. The Company is also subject to certain covenants relating to, among others, indebtedness, fundamental corporate changes, dispositions, acquisitions and distributions. On December 27, 2017, the Loan was amended to extend the period for commencement of the leverage ratio and interest coverage ratio covenants from the calendar quarter ending December 31, 2017 to the calendar quarter ending March 31, 2018. On March 28, 2018, the Loan was amended to extend the period for commencement of the leverage ratio and interest coverage ratio covenants from the calendar quarter ending March 31, 2018 to the calendar quarter ending June 30, 2019 and agreed that interest payments on the outstanding Loan balance for the period commencing on January 1, 2018 and continuing thereafter will be suspended, and each such suspended interest payment will be added to the principal balance of the Loan, and the 12% rate for overdue interest will not apply to such suspended interest. In connection with the above, during the three months ended March 31, 2018, the Company accrued interest expense of $362,466, which is presented within non-revolving credit facility, net on the condensed consolidated balance sheet as of March 31, 2018 as these amounts will not be paid within one year from the condensed consolidated balance sheet date.

Upon an event of default, Raycom may by written notice terminate the facility immediately and declare all obligations under the Loan, whether matured or not, to be immediately due and payable. Raycom may also as and by way of collateral security, deposit and retain in an interest bearing account, amounts received by Raycom from the Company under the Loan and realize upon the security interest agreements, guaranty agreements and pledge agreement.

Letter of Credit – Western Alliance Bank

On August 31, 2016, in lieu of a security deposit under the lease dated October 26, 2010, with Metropolitan Life Insurance Company, for real property located at 27-01 Queens Plaza North, Long Island City, NY, Frankly Media LLC entered into a standby letter of credit with Western Alliance Bank for an amount of $500,000 (the "Letter of Credit"). For each advance, interest will accrue at a rate equal to the sum of (i) the Base Rate (as defined below), plus (ii) 3.50%, provided that such interest rate will change from time to time as the Base Rate changes. The "Base Rate" means the rate of interest used as the reference or base rate to establish the actual rates charged on commercial loans and which is publicly announced or reported from time to time by the Wall Street Journal as the "prime rate". Interest will accrue from the date of the advance until such advance is paid in full. The Company has granted Western Alliance Bank a security interest in a $524,115 controlled cash deposit account together with (i) all interest, whether now accrued or hereafter accruing; (ii) all additional deposits hereafter made to the account; (iii) any and all proceeds from the account; and (iv) all renewals, replacements and substitutions for any of the foregoing. As of March 31, 2018 and December 31, 2017, no advances were made under the Letter of Credit. The cash security interest of $524,115 is presented within restricted cash on the consolidated balance sheets.

8. Shareholders' Equity

Common Shares and Class A Restricted Voting Shares

All common and Class A restricted voting shares and related stock-based grants have been denominated in Canadian dollars and have been translated to U.S. dollars using the exchange rate in effect at the date of transaction or grant, as applicable.

The Class A restricted voting shares have the same voting rights as common shares except for voting for the election and removal of directors of the Company. The Class A restricted voting shares participate in dividends and liquidation events in the same manner as common shares. In terms of restrictions on transfer, no Class A restricted voting shares shall be transferred to another party unless an offer to acquire common shares is concurrently made that is identical to the offer for the Class A restricted voting shares in terms of price per share, percentage of outstanding shares to be transferred and in all other material respects.

Shares Issued During the Three Months Ended March 31, 2018

During the three months ended March 31, 2018, the Company issued a total of 77,973 common shares for employee and director restricted stock units ("RSUs") that vested.

Stock-Based Compensation

Description of the Plan

On October 20, 2017, the Company adopted an amended and restated equity incentive plan (the "Restated Plan"). The Restated Plan amends the equity incentive plan, effective as of October 1, 2017, by replacing the compensation plan limit with a fixed total limit of 435,000 common shares that may be granted under option and RSU awards.

Options may be exercised over periods of up to 10 years as determined by the Company's Board of Directors ("Board") and the exercise price shall not be less than the closing price of the shares on the day preceding the award date. Option awards generally vest over four years with one year cliff vesting.

The Restated Plan allows the Company to award RSUs to officers, employees, directors and consultants of Frankly and its subsidiaries upon such conditions as the Board may establish, including the attainment of performance goals recommended by the Company's compensation committee. The purchase price for common shares of the Company issuable under each RSU award, if any, shall be established by the Board at its discretion. Shares issued pursuant to any RSU award may be made subject to vesting conditions based upon the satisfaction of service requirements, conditions, restrictions, time periods or performance goals established by the Board.

Based on the number of outstanding options and RSUs as of March 31, 2018 and RSUs vested through March 31, 2018, the Company had 44,095 options or RSUs remaining for issuance under the Restated Plan.

Total stock-based compensation expense was $235,040 and $228,166 for the three months ended March 31, 2018 and 2017, respectively. The Company did not recognize any tax benefits for stock-based compensation during any of the periods presented.

Stock Options

The following table sets forth the activity for the Company's stock options during the periods presented:

		Weighted Average		
	Shares	Exercise Price	Grant Date Fair Value	Remaining Contractual Term (Years)
Balance, December 31, 2016	245,762	$ 19.52	$ 9.10	8.71
Adjustment - Balance, December 31, 2016	(53)	-	-	
Granted	74,327	5.48	2.81	
Exercised	-	-	-	
Forfeited or canceled	(50,431)	18.21	9.30	
Canceled (Option Replacement)	(193,339)	19.90	9.11	
Granted (Option Replacement)	113,677	5.30	9.11	
Balance, December 31, 2017	189,943	$ 5.47	$ 6.58	8.22
Vested and expected to vest, December 31, 2017	183,924	$ 5.48	$ 6.65	8.20
Exercisable, December 31, 2017	69,567	$ 5.73	$ 10.17	7.33
Unaudited interim activity:				
Balance, December 31, 2017	189,943	$ 5.47	$ 6.58	8.22
Granted	-	-	-	
Exercised	-	-	-	
Forfeited or canceled	(20,301)	5.36	4.64	
Balance, March 31, 2018	169,642	$ 5.49	$ 6.81	7.92
Vested and expected to vest, March 31, 2018	165,383	$ 5.49	$ 6.87	7.90
Exercisable, March 31, 2018	84,454	$ 5.65	$ 9.03	7.39

The aggregate intrinsic value of outstanding and exercisable stock options as of September 30, 2017 is $0.

Restricted Share Units

The following table sets forth the activity for the Company's RSUs for the periods presented:

	Shares	Weighted-Average Grant Date Fair Value
Balance, December 31, 2016	76,731	$ 7.31
Adjustment - Balance, December 31, 2016	(7)	-
Granted	201,507	3.11
Vested	(98,387)	5.04
Forfeited or canceled	(754)	6.44
Balance, December 31, 2017	179,090	$ 3.84
Unaudited interim activity:		
Balance, December 31, 2017	179,090	$ 3.84
Granted	-	-
Vested	(77,973)	3.78
Forfeited or canceled	(1,617)	5.22
Balance, March 31, 2018	99,500	$ 3.86

Unrecognized compensation cost related to the Company's non-vested RSUs was $223,159 as of March 31, 2018, which is expected to be recognized from 2018 through 2020.

9. Income Taxes

The Company had $0 income tax expense for all periods presented. Deferred tax assets have been fully reserved given the Company's history of losses.

10. Commitments and Contingencies

Legal Proceedings

On July 21, 2017, a complaint was filed by GEI, Albert C. Gannaway III, and Samantha Gannaway, and was served on August 4, 2017, captioned Gannaway Entertainment, Inc., Albert C. Gannaway III, Samantha Gannaway V.S. Frankly Inc., Steve Chung, SKP America, LLC, JJR Private Capital Limited Partnership, Ron Schmeichel, Louis Schwartz in the U.S. District Court for the Northern District of California against the Company, the Company's Chief Executive Officer, Chief Financial Officer and Chief Operating Officer and others alleging violations of U.S. securities laws, fraud and breach of fiduciary duties, and seeking in excess of $15 million in damages, arising out of the Company's acquisition of Gannaway Web Holdings, LLC from GEI and other parties in 2015.

On September 30, 2017, the defendants filed a motion to dismiss the complaint. On October 11, 2017 the plaintiffs filed an amended complaint. On October 31, 2017 the defendants filed a motion to dismiss the amended complaint. On March 12, 2018, the plaintiffs in the GEI complaint voluntarily terminated their case. On March 15, 2018, the plaintiffs in the GEI complaint re-filed their complaint in state court. The Company is reviewing the complaint with its counsel and believes that the claims are without merit. The Company intends to defend the claims vigorously.

Operating Lease Commitments

The Company is obligated under multiple non-cancellable operating leases for office space, expiring in 2019 through 2023. The Company has two subleases for its excess office space as of December 31, 2017.

The future aggregate minimum lease payments under these non-cancellable operating leases, without regard to subleases, are payable as follows as of March 31, 2018:

Payments Due During the Years Ending March 31,	Total
2019	1,592,079
2020	1,152,891
2021	852,908
2022	852,908
2023	781,833
Thereafter	-
Total	$ 5,232,619

Employee Benefit Plan

The Company's subsidiaries, Frankly Co. and Frankly Media, have a 401(k) plan (the "Plan"), which covers all eligible employees. Under the Plan, employees may contribute from their gross salaries on a before tax basis up to annual statutory limits determined each year.

11. Subsequent Events

The Company has evaluated subsequent events through May 15, 2018 which is the date these unaudited interim condensed consolidated financial statements were available to be issued, and determined that there have been no events that have occurred that would require adjustments to or disclosure in the unaudited interim condensed consolidated financial statements except for the transactions described below.

Amendment to the Non-revolving Credit Facility

On May 8, 2018 the Company entered into an amendment of the 2016 credit agreement between the Company and Raycom, whereby Raycom will provide the Company with an additional $7.5 million of funding, to be paid in installments over a six-month period, subject to the Company's achievement of certain operational milestones. The $1.0 million Raycom advanced to the Company under the credit agreement on March 13, 2018 is included in the additional $7.5 million funding. Upon the Company's receipt of all of the additional funding under the amended credit agreement, the total outstanding principal balance under the amended credit agreement would be $22.0 million.