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

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2023

or

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from ___________ to ___________

Commission File Number 001-33169

Creative Realities, Inc.
(Exact Name of Registrant as Specified in its Charter)

Minnesota	**41-1967918**
State or Other Jurisdiction of Incorporation or Organization	I.R.S. Employer Identification No.
13100 Magisterial Drive, Suite 100, Louisville KY	**40223**
Address of Principal Executive Offices	Zip Code

(502) 791-8800
Registrant's Telephone Number, Including Area Code

Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, par value $0.01 per share	CREX	The Nasdaq Stock Market LLC
Warrants to purchase Common Stock	CREXW	The Nasdaq Stock Market LLC

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes ☒ No ☐

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

Large accelerated filer	☐	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 period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

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

APPLICABLE ONLY TO CORPORATE ISSUERS

As of August 4, 2023, the registrant had 7,409,027 shares of common stock outstanding.

PART 1. FINANCIAL INFORMATION

Item 1. Financial Statements

CREATIVE REALITIES, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except per share amounts)
(Unaudited)

	June 30, 2023	December 31, 2022
	(unaudited)	
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 3,264	$ 1,633
Accounts receivable, net	6,496	8,263
Work-in-process and inventories, net	1,148	2,267
Prepaid expenses and other current assets	784	1,819
Total current assets	$ 11,692	$ 13,982
Property and equipment, net	453	201
Operating lease right-of-use assets	1,356	1,584
Intangibles, net	23,936	23,752
Goodwill	26,453	26,453
Other assets	44	43
TOTAL ASSETS	$ 63,934	$ 66,015
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable	$ 2,892	$ 3,757
Accrued expenses	3,217	3,828
Deferred revenues	2,827	1,223
Customer deposits	3,985	2,478
Current maturities of operating leases	645	711
Short-term portion of Secured Promissory Note	833	1,248
Short-term portion of related party Consolidation Term Loan, net of $747 and $745 discount, respectively	3,245	1,251
Short-term related party Term Loan (2022)	119	2,000
Total current liabilities	17,763	16,496
Long-term Secured Promissory Note	-	208
Long-term related party Acquisition Term Loan, net of $1,139 and $1,484 discount, respectively	8,861	8,516
Long-term related party Consolidation Term Loan, net of $469 and $840 discount, respectively	2,724	4,349
Long-term obligations under operating leases	711	873
Contingent acquisition consideration, at fair value	9,881	9,789
Other liabilities	136	205
TOTAL LIABILITIES	40,076	40,436
SHAREHOLDERS' EQUITY		
Common stock, $0.01 par value, 66,666 shares authorized; 7,409 and 7,266 shares issued and outstanding, respectively	74	72
Additional paid-in capital	76,618	75,916
Accumulated deficit	(52,834)	(50,409)
Total shareholders' equity	23,858	25,579
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 63,934	$ 66,015

See accompanying notes to condensed consolidated financial statements

CREATIVE REALITIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share amounts)
(Unaudited)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2023	2022	2023	2022
Sales				
Hardware	$ 3,437	$ 5,667	$ 7,759	$ 12,126
Services and other	5,759	5,256	11,381	9,554
Total sales	9,196	10,923	19,140	21,680
Cost of sales				
Hardware	2,724	4,610	5,930	9,992
Services and other	2,174	1,651	3,823	3,134
Total cost of sales	4,898	6,261	9,753	13,126
Gross profit	4,298	4,662	9,387	8,554
Operating expenses:				
Sales and marketing expenses	1,229	1,147	2,365	1,854
Research and development expenses	377	418	743	659
General and administrative expenses	2,595	2,562	5,493	5,422
Depreciation and amortization expense	797	468	1,576	1,175
Deal and transaction expenses	-	37	-	428
Total operating expenses	4,998	4,632	10,177	9,538
Operating income/(loss)	(700)	30	(790)	(984)
Other income (expenses):				
Interest expense, including amortization of debt discount	(787)	(750)	(1,590)	(1,199)
Change in fair value of warrant liability	-	2,433	-	7,902
Change in fair value of equity guarantee	(16)	(73)	(92)	(73)
Loss on debt waiver consent	-	-	-	(1,212)
Loss on warrant amendment	-	(345)	-	(345)
Gain/(loss) on settlement of obligations	-	21	-	(274)
Other income (expense)	123	(1)	135	5
Total other income (expense)	(680)	1,285	(1,547)	4,804
Net (loss) income before income taxes	(1,380)	1,315	(2,337)	3,820
Provision for income taxes	(45)	(53)	(88)	(56)
Net (loss) income	$ (1,425)	$ 1,262	$ (2,425)	$ 3,764
Basic (loss) earnings per common share	$ (0.19)	$ 0.17	$ (0.33)	$ 0.62
Diluted (loss) earnings per common share	$ (0.19)	$ 0.17	$ (0.33)	$ 0.62
Weighted average shares outstanding - basic	7,406	7,234	7,379	6,060
Weighted average shares outstanding - diluted	7,406	7,234	7,379	6,060

See accompanying notes to condensed consolidated financial statements.

CREATIVE REALITIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Six Months Ended June 30,	
	2023	**2022**
Operating Activities:		
Net (loss) income	$ (2,425)	$ 3,764
Adjustments to reconcile net (loss) income to net cash provided by operating activities		
Depreciation and amortization	1,576	1,175
Amortization of debt discount	714	541
Amortization of stock-based compensation	493	1,014
Loss on debt waiver consent	-	1,212
Loss on warrant amendment	-	345
Change on change in fair value of warrants	-	274
Bad debt expense	309	106
Gain on change in fair value of warrants	-	(7,902)
Loss on change in fair value of contingent consideration	92	73
Deferred income taxes	46	-
Changes to operating assets and liabilities:		
Accounts receivable	1,458	(4,035)
Work-in-process and inventories	1,119	(562)
Prepaid expenses and other current assets	1,035	(811)
Accounts payable	(585)	2,487
Accrued expenses	(559)	229
Deferred revenues	1,604	1,178
Customer deposits	1,507	809
Other	(40)	40
Net cash provided by (used in) operating activities	6,344	(63)
Investing activities		
Acquisition of business, net of cash acquired	-	(17,186)
Purchases of property and equipment	(219)	(32)
Capitalization of labor for software development	(1,984)	(2,328)
Net cash used in investing activities	(2,203)	(19,546)
Financing activities		
Principal payments on finance leases	(6)	-
Proceeds from sale of common stock in PIPE, net of offering expenses	-	1,814
Proceeds from sale & exercise of pre-funded warrants in PIPE, net of offering expenses	-	8,295
Proceeds from Acquisition Loan, net of offering expenses	-	9,868
Repayment of Term Loan (2022)	(1,881)	-
Repayment of Secured Promissory Note	(623)	(411)
Net cash (used in) provided by financing activities	(2,510)	19,566
Increase (decrease) in Cash and Cash Equivalents	1,631	(43)
Cash and Cash Equivalents, beginning of period	1,633	2,883
Cash and Cash Equivalents, end of period	$ 3,264	$ 2,840

See accompanying notes to condensed consolidated financial statements.

CREATIVE REALITIES, INC.
CONSOLIDATED STATEMENTS OF SHAREHOLDERS’ EQUITY
(in thousands, except shares)
(Unaudited)

	Common Stock		Additional paid in capital	Accumulated Deficit	Total
	Shares	Amount			
Three Months Ended June 30, 2023					
Balance as of March 31, 2023	7,394,407	$ 74	$ 76,417	$ (51,409)	$ 25,082
Stock-based compensation	-	-	171	-	171
Stock-based compensation issued to vendors	14,620	-	30	-	30
Net loss	-	-	-	(1,425)	(1,425)
Balance as of June 30, 2023	7,409,027	$ 74	$ 76,618	$ (52,834)	$ 23,858

	Common Stock		Additional paid in capital	Accumulated Deficit	Total
	Shares	Amount			
Six Months Ended June 30, 2023					
Balance as of December 31, 2022	7,266,382	$ 72	$ 75,916	$ (50,409)	$ 25,579
Stock-based compensation	-	-	414	-	414
Shares issued to directors as compensation	51,616	1	95	-	96
Shares issued to vendors as compensation	28,554	-	55	-	55
Shares issued to employees pursuant to the Retention Bonus Plan	62,475	1	138	-	139
Net loss	-	-	-	(2,425)	(2,425)
Balance as of June 30, 2023	7,409,027	$ 74	$ 76,618	$ (52,834)	$ 23,858

	Common Stock		Additional paid in capital	Accumulated (Deficit)	Total
	Shares	Amount			
Three Months Ended June 30, 2022					
Balance as of March 31, 2022	7,225,012	$ 72	$ 68,771	$ (49,783)	$ 19,060
Stock-based compensation	-	-	341	-	341
Stock-based compensation issued to vendors	22,943	-	65	-	65
Warrant amendment	-	-	5,709	-	5,709
Net income	-	-	-	1,262	1,262
Balance as of June 30, 2022	7,247,955	$ 72	$ 74,886	$ (48,521)	$ 26,437

	Common Stock		Additional paid in capital	Accumulated (Deficit)	Total
	Shares	Amount			
Six Months Ended June 30, 2022					
Balance as of December 31, 2021	4,002,843	$ 40	$ 60,943	$ (52,254)	$ 8,729
Stock-based compensation	-	-	892	-	892
Shares issued to vendors as compensation	22,943	-	65	-	65
Shares issued and warrants exercised in private investment in public entity ("PIPE")	2,388,835	24	2,254	-	2,278
Shares issued in Reflect Systems, Inc. Merger	833,334	8	4,992	-	5,000
Warrant repricing events	-	-	31	(31)	-
Warrant amendment	-	-	5,709	-	5,709
Net income	-	-	-	3,764	3,764
Balance as of June 30, 2022	7,247,955	$ 72	$ 74,886	$ (48,521)	$ 26,437

See accompanying notes to condensed consolidated financial statements.

NOTE 1: NATURE OF ORGANIZATION AND OPERATIONS

Unless the context otherwise indicates, references in these Notes to the accompanying Condensed Consolidated Financial Statements to "we," "us," "our" and "the Company" refer to Creative Realities, Inc. and its subsidiaries.

Nature of the Company's Business

Creative Realities, Inc. is a Minnesota corporation that provides innovative digital marketing technology and solutions to retail companies, individual retail brands, enterprises and organizations throughout the United States and in certain international markets. The Company has expertise in a broad range of existing and emerging digital marketing technologies, as well as the related media management and distribution software platforms and networks, device management, product management, customized software service layers, systems, experiences, workflows, and integrated solutions. Our technology and solutions include: digital merchandising systems and omni-channel customer engagement systems, interactive digital shopping assistants, advisors and kiosks, and other interactive marketing technologies such as mobile, social media, point-of-sale transactions, beaconing and web-based media that enable our customers to transform how they engage with consumers. We have expertise in a broad range of existing and emerging digital marketing technologies, as well as the following related aspects of our business: content, network management, and connected device software and firmware platforms; customized software service layers; hardware platforms; digital media workflows; and proprietary processes and automation tools.

Our main operations are conducted directly through Creative Realities, Inc., and under our wholly owned subsidiaries Allure Global Solutions, Inc. ("Allure), a Georgia corporation, Creative Realities Canada, Inc., a Canadian corporation, and Reflect Systems, Inc. ("Reflect"), a Delaware corporation.

Reverse stock split

On March 23, 2023, the Company filed Articles of Amendment with the Secretary of State of the State of Minnesota to effectuate, effective March 27, 2023, a 1-for-3 reverse stock split of the shares of the Company's common stock, par value $0.01 per share. All share and per share information (including share and per share information related to share-based compensation) has been retroactively adjusted to reflect the reverse stock split within this Quarterly Report on Form 10-Q.

As a result of the reverse stock split, effective 12:01 am on March 27, 2023, every three shares of common stock then-issued and outstanding automatically combined into one share of common stock, with no change in par value per share. No fractional shares were outstanding following the reverse stock split and any fractional shares resulting from the reverse split were rounded up to the nearest whole share of common stock. In connection with the reverse stock split, the total number of shares of common stock authorized for issuance was reduced from 200,000,000 shares to 66,666,666 shares in proportion to the reverse stock split.

Effective as of the same time as the reverse stock split, the number of shares of common stock available for issuance under the Company's equity compensation plans were reduced in proportion to the reverse stock split. The reverse stock split also resulted in reductions in the number of shares of common stock issuable upon exercising or vesting of equity awards in proportion to the reverse stock split and proportionate increases in exercise price or share-based performance criteria, if any, applicable to such awards. Similarly, the number of shares of common stock issuable upon exercise of outstanding warrants were reduced in proportion to the reverse stock split, and the exercise prices of outstanding warrants were proportionately increased.

Liquidity and Financial Condition

In accordance with Accounting Standards Update ("ASU") No. 2014-15, *Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern (Subtopic 205-40) ("ASU 205-40")*, the Company has evaluated whether there are certain conditions and events, considered in the aggregate, that raise substantial doubt about the Company's ability to continue as a going concern within one year after the date that the Condensed Consolidated Financial Statements are issued.

At June 30, 2023, the Company has an accumulated deficit of $52,834, negative working capital of $6,071, including current debt obligations of $4,197, and cash of $3,264. For the six months ended June 30, 2023, the Company incurred an operating loss of $790 and generated positive net cash flows from operations of $6,344. In addition, pursuant to the Second Amended and Restated Credit and Security Agreement (the "Credit Agreement") made between the Company and Slipstream Communications ("Slipstream") the Company is required to make monthly repayments of principal on the Consolidation Term Loan beginning on September 1, 2023 and on the first day of each month thereafter until the Maturity Date on February 17, 2025. The monthly principal payment beginning on September 1, 2023 is approximately $399, or total principal repayments for the twelve months subsequent to the reporting date of these Condensed Consolidated Financial Statements of $4,389. As a result of the principal debt service payments required to be paid on account of the Consolidation Term Loan, the Company does not currently have cash on hand or committed available liquidity to repay all of its outstanding debt due within one year after the date that these financial statements are issued. These conditions and events raise substantial doubt about the Company's ability to continue as a going concern under the technical framework within ASU 205-40.

In response to these conditions, management plans to either refinance or recapitalize the debt. However, these plans have not been finalized and are not completely within the Company's control, and therefore cannot be deemed probable under ASU 205-40. We have been unable to obtain a continuing support letter from Slipstream beyond the period ending May 31, 2024. Obtaining a continuing support letter from Slipstream beyond one year of the date our financial statements were issued was a factor that previously alleviated the substantial doubt about our ability to continue as a going concern. As a result, the Company has concluded that management's plans do not alleviate substantial doubt about the Company's ability to continue as a going concern.

The Condensed Consolidated Financial Statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or the amounts and classification of liabilities that might result from the outcome of this uncertainty.

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A summary of the significant accounting policies consistently applied in the preparation of the accompanying Condensed Consolidated Financial Statements follows:

1. Basis of Presentation

The accompanying unaudited Condensed Consolidated Financial Statements have been prepared in accordance with the applicable instructions to Form 10-Q and Article 10 of Regulation S-X and include all of the information and disclosures required by generally accepted accounting principles in the United States of America (“GAAP”) for interim financial reporting. These unaudited Condensed Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements of the Company and related footnotes for the year ended December 31, 2022, included in the Company’s Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 30, 2023.

The results of operations for the interim periods are not necessarily indicative of results of operations for a full year. Management believes the accompanying unaudited Condensed Consolidated Financial Statements reflect all adjustments, including normal recurring items, considered necessary for a fair statement of results for the interim periods presented.

2. Recently Issued and Adopted Accounting Pronouncements

Credit Losses. In June 2016, the Financial Accounting Standards Board (“FASB”) issued ASU No. 2016-13, *Financial Instruments—Credit Losses*, which requires entities to estimate expected lifetime credit losses on financial assets and provide expanded disclosures. The ASU replaced the incurred loss methodology with one that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. We adopted ASU No. 2016-13 on January 1, 2023. The adoption of this guidance did not have a material impact on the Company's Condensed Consolidated Financial Statements, as the Company's primary financial assets are its trade accounts receivable, which are short-term financings under industry standard credit and trade terms.

Debt. In August 2020, the FASB issued Accounting Standards Update No. 2020-06, *Debt—Debt with Conversion and Other Options (Subtopic 470-20) and Derivatives and Hedging—Contracts in Entity’s Own Equity (Subtopic 815-40): Accounting for Convertible Instruments and Contracts in an Entity’s Own Equity (ASU 2020-06)*, which simplifies the accounting for convertible instruments by reducing the number of accounting models available for convertible debt instruments. This guidance also eliminates the treasury stock method to calculate diluted earnings per share for convertible instruments and requires the use of the if-converted method. This guidance will be effective for us in the first quarter of 2024 on a full or modified retrospective basis, with early adoption permitted. We do not intend to early adopt this standard, nor do we expect the adoption of this guidance to have a material impact on our Consolidated Financial Statements.

3. Revenue Recognition

We recognize revenue in accordance with ASC 606, *Revenue from Contracts with Customers*, applying the five-step model.

If an arrangement involves multiple performance obligations, the items are analyzed to determine the separate units of accounting, whether the items have value on a standalone basis and whether there is objective and reliable evidence of their standalone selling price. The total contract transaction price is allocated to the identified performance obligations based upon the relative standalone selling prices of the performance obligations. The standalone selling price is based on an observable price for services sold to other comparable customers, when available, or an estimated selling price using a cost plus margin approach.

The Company estimates the amount of total contract consideration it expects to receive for variable arrangements by determining the most likely amount it expects to earn from the arrangement based on the expected quantities of services it expects to provide and the contractual pricing based on those quantities. The Company only includes some or a portion of variable consideration in the transaction price when it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur when the uncertainty associated with the variable consideration is subsequently resolved. The Company considers the sensitivity of the estimate, its relationship and experience with the client and variable services being performed, the range of possible revenue amounts and the magnitude of the variable consideration to the overall arrangement. The Company receives variable consideration in very few instances.

Revenue is recognized when a customer obtains control of promised goods or services under the terms of a contract and is measured as the amount of consideration the Company expects to receive in exchange for transferring goods or providing services. The Company does not have any material extended payment terms as payment is due at or shortly after the time of the sale, ranging between thirty and ninety days. Observable prices are used to determine the standalone selling price of separate performance obligations or a cost plus margin approach when one is not available. Sales, value-added and other taxes collected concurrently with revenue producing activities are excluded from revenue.

The Company recognizes contract assets or unbilled receivables related to revenue recognized for services completed but not yet invoiced to the clients. A contract liability is recognized as deferred revenue when the Company invoices clients in advance of performing the related services under the terms of a contract. Deferred revenue is recognized as revenue when the Company has satisfied the related performance obligation.

The Company uses the practical expedient for recording an immediate expense for incremental costs of obtaining contracts, including certain design/engineering services, commissions, incentives and payroll taxes, as these incremental and recoverable costs have terms that do not exceed one year.

4. Allowance for Credit Losses

The allowance for credit losses is the Company's best estimate of the amount of expected lifetime credit losses in the Company's accounts receivable. The Company regularly reviews the adequacy of its allowance for credit losses. The Company estimates losses over the contractual life using assumptions to capture the risk of loss, even if remote, based principally on how long a receivable has been outstanding. Account balances are charged off against the allowance for credit losses after all reasonable means of collection have been exhausted and the potential for recovery is considered remote. Other factors considered include historical write-off experience, current economic conditions, customer credit, and past transaction history with the customer. The allowance for credit losses is included in accounts receivable, net in the accompanying Condensed Consolidated Balance Sheets.

The Company had the following activity for its allowance for credit losses from December 31, 2022 to June 30, 2023:

Balance as of December 31, 2022	$	984
Amounts accrued		309
Write-offs charged against the allowance		(179)
Balance as of June 30, 2023	$	1,114

5. Inventories

Inventories are stated at the lower of cost or net realizable value, determined by the first-in, first-out (FIFO) method, and consist of the following:

	June 30, 2023	December 31, 2022
Raw materials, net of reserve	$ 551	$ 1,671
Work-in-process	597	596
Total inventories	$ 1,148	$ 2,267

The reserve for obsolete inventory at June 30, 2023 and December 31, 2022 was $1,895 and $1,777, respectively, of which $1,707 related to Safe Space Solutions. The Company is no longer actively promoting the sale of our Safe Space Solutions or purchasing inventory to support such solutions.

6. Impairment of Long-Lived Assets

We review the carrying value of all long-lived assets, including property and equipment, for impairment annually as of September 30 in accordance with ASC 360, *Accounting for the Impairment or Disposal of Long-Lived Assets*. Under ASC 360, impairment losses are recorded whenever events or changes in circumstances indicate the carrying value of an asset may not be recoverable.

If the impairment tests indicate that the carrying value of the asset is greater than the expected undiscounted cash flows to be generated by such asset, an impairment loss would be recognized. The impairment loss is determined as the amount by which the carrying value of such asset exceeds its fair value. We generally measure fair value by considering sale prices for similar assets or by discounting estimated future cash flows from such assets using an appropriate discount rate. Assets to be disposed of are carried at the lower of their carrying value or fair value less costs to sell. Considerable management judgment is necessary to estimate the fair value of assets, and accordingly, actual results could vary significantly from such estimates.

7. Basic and Diluted (Loss)/Earnings per Common Share

Basic and diluted (loss)/earnings per common share for all periods presented is computed using the weighted average number of common shares outstanding. Basic weighted average shares outstanding includes only outstanding common shares. Diluted weighted average shares outstanding includes outstanding common shares and potential dilutive common shares outstanding in accordance with the treasury stock method.

Shares reserved for outstanding stock options, including stock options with performance restricted vesting, and warrants totaling approximately 7,391,651 and 7,490,962 at June 30, 2023 and 2022, respectively, were excluded from the computation of (loss)/earnings per share as the strike price on the options and warrants were higher than the Company's market price and therefore anti-dilutive.

8. Income Taxes

Deferred income taxes are recognized in the financial statements for the tax consequences in future years of differences between the tax basis of assets and liabilities and their financial reporting amounts based on enacted tax laws and statutory tax rates. Temporary differences arise from a number of matters including, but not limited to, net operating losses, differences in basis of intangibles, stock-based compensation, reserves for uncollectible accounts receivable and inventory, differences in depreciation methods, and accrued expenses. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized. The Company accounts for uncertain tax positions utilizing an established recognition threshold and measurement attributes for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. We had no uncertain tax positions as of June 30, 2023 and December 31, 2022.

9. Goodwill and Intangible Assets

We follow the provisions of ASC 350, Goodwill and Other Intangible Assets. Pursuant to ASC 350, goodwill acquired in a purchase business combination is not amortized, but instead tested for impairment at least annually. The Company uses an annual measurement date of September 30 to assess impairment of goodwill and indefinite-lived intangible assets, or as indicators are identified.

Definite-lived intangible assets are amortized straight-line in accordance with their identified useful lives.

10. Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Our significant estimates include: contingent purchase consideration valuation, allowance for credit losses, valuation allowances related to deferred taxes, the fair value of acquired assets and liabilities, the fair value of liabilities reliant upon the appraised fair value of the Company, valuation of stock-based compensation awards and other assumptions and estimates used to evaluate the recoverability of long-lived assets, goodwill and other intangible assets and the related amortization methods and periods. Actual results could differ from those estimates.

11. Business Combinations

Accounting for acquisitions requires us to recognize separately from goodwill the assets acquired and the liabilities assumed at their acquisition date fair values. Goodwill as of the acquisition date is measured as the excess of consideration transferred over the net acquisition date fair values of the assets acquired and the liabilities assumed. While we use our best estimates and assumptions to accurately value assets acquired and liabilities assumed at the acquisition date as well as contingent consideration, where applicable, our estimates are inherently uncertain and subject to refinement. As a result, during the measurement period, which may be up to one year from the acquisition date, we may record adjustments to the assets acquired and liabilities assumed with the corresponding offset to goodwill. Upon the conclusion of the measurement period or final determination of the values of assets acquired or liabilities assumed, whichever comes first, any subsequent adjustments are recorded to our consolidated statements of operations.

12. Contingent Consideration

The Company has contingent consideration arrangements related to certain acquisitions to potentially pay additional cash amounts in future periods based on the lack of achievement of certain share price performance goals of our common stock. Such contingent consideration arrangements are recorded at fair value and are classified as liabilities on the acquisition date and are remeasured at each reporting period in accordance with ASC 805-30-35-1 using a Monte Carlo simulation model.

NOTE 3: FAIR VALUE MEASUREMENT

We measure certain financial assets, including cash equivalents, at fair value on a recurring basis. In accordance with ASC 820-10-30, fair value is a market-based measurement that should be determined based on the assumptions that market participants would use in pricing an asset or liability. As a basis for considering such assumptions, ASC 820-10-35 establishes a three-level hierarchy that prioritizes the inputs used in measuring fair value. The three hierarchy levels are defined as follows:

Level 1 — Valuations based on unadjusted quoted prices in active markets for identical assets.

Level 2 — Valuations based on observable inputs (other than Level 1 prices), such as quoted prices for similar assets at the measurement date; quoted prices in markets that are not active; or other inputs that are observable, either directly or indirectly.

Level 3 — Valuations based on inputs that are unobservable and involve management judgment and the reporting entity's own assumptions about market participants and pricing.

The calculation of the fair value of the contingent consideration contains inputs which are unobservable and involve management judgment and are considered Level 3 estimates. Additionally, the separately identifiable intangible assets rely on a discounted cash flow model which utilizes inputs including the calculation of the weighted average cost of capital and management's forecast of future financial performance which are unobservable and involve management judgment and are considered Level 3 estimates.

The calculation of the weighted average cost of capital and management's forecast of future financial performance utilized within our discounted cash flow model for the impairment of goodwill contains inputs which are unobservable and involve management judgment and are considered Level 3 estimates.

The calculation of the fair value of the warrant liability contains valuation inputs which are based on observable inputs (other than Level 1 prices) and are considered Level 2 estimates. The liability warrants were converted to equity warrants effective June 30, 2022.

NOTE 4: REVENUE RECOGNITION

The Company applies ASC 606 for revenue recognition. The following table disaggregates the Company's revenue by major source for the three and six months ended June 30, 2023 and 2022:

(in thousands)	Three Months Ended June 30, 2023	Three Months Ended June 30, 2022	Six Months Ended June 30, 2023	Six Months Ended June 30, 2022
Hardware	$ 3,437	$ 5,667	$ 7,759	$ 12,126
Services:				
Installation Services	1,168	903	2,115	2,242
Software Development Services	289	109	820	300
Managed Services	3,835	3,832	7,907	6,535
Media Sales	467	412	539	477
Total Services	5,759	5,256	11,381	9,554
Total Hardware and Services	$ 9,196	$ 10,923	$ 19,140	$ 21,680

System hardware sales

System hardware revenue is recognized generally upon shipment of the product or customer acceptance depending upon contractual arrangements with the customer in instances in which the sale of hardware is the sole performance obligation. Shipping charges billed to customers are included in hardware sales and the related shipping costs are included in hardware cost of sales. The cost of freight and shipping to the customer is recognized in cost of sales at the time of transfer of control to the customer. System hardware revenues are classified as “Hardware” within our disaggregated revenue.

Installation services

The Company performs outsourced installation services for customers and recognizes revenue upon completion of the installations. Installation services also includes engineering services performed as part of an installation project.

When system hardware sales include installation services to be performed by the Company, the goods and services in the contract are not distinct, so the arrangement is accounted for as a single performance obligation. Our customers control the work-in-process and can make changes to the design specifications over the contract term. Revenues are recognized over time as the installation services are completed based on the relative portion of labor hours completed as a percentage of the budgeted hours for the installation. Installation services revenues are classified as “Installation Services” within our disaggregated revenue.

Software design and development services

Software and software license sales are revenue when a fixed fee order has been received and delivery has occurred to the customer. Revenue is recognized generally upon customer acceptance (point-in-time) of the software product and verification that it meets the required specifications. Software is delivered to customers electronically. Software design and development revenues are classified as “Software Development Services” within our disaggregated revenue.

Software as a service

Software as a service includes revenue from software licensing and delivery in which software is licensed on a subscription basis and is centrally hosted by the Company. These services often include software updates which provide customers with rights to unspecified software product upgrades and maintenance releases and patches released during the term of the support period. Contracts for these services are generally 12-36 months in length. We account for revenue from these services in accordance with ASC 985-20-15-5 and recognize revenue ratably over the performance period. Software as a service revenue are classified as “Managed Services” within our disaggregated revenue.

Maintenance and support services

The Company sells support services which include access to technical support personnel for software and hardware troubleshooting. The Company offers a hosting service through our network operations center, or NOC, allowing the ability to monitor and support its customers’ networks 7 days a week, 24 hours a day. These contracts are generally 12-36 months in length. Revenue is recognized over the term of the agreement in proportion to the costs incurred in fulfilling performance obligations under the contract. Maintenance and Support revenues are classified as “Managed Services” within our disaggregated revenue.

Maintenance and support fees are based on the level of service provided to end customers, which can range from monitoring the health of a customer’s network to supporting a sophisticated web-portal to managing the end-to-end hardware and software of a digital marketing system. These agreements are renewable by the customer. Rates for maintenance and support, including subsequent renewal rates, are typically established based upon a fee per location, per device, or a specified percentage of net software license fees as set forth in the arrangement. These contracts are generally 12-36 months in length. Revenue is recognized ratably and evenly over the service period.

The Company also performs time and materials-based maintenance and repair work for customers. Revenue is recognized at a point in time when the performance obligation has been fully satisfied.

Media sales

Media revenues are derived from selling (i) sponsorship packages, including mobile takeover or physical presence, or (ii) advertising space to customers on digital displays or other outdoor structures, each within physical venues. We generally do not own the physical structures on which we display advertising for our customers but instead sell advertising or sponsorship opportunities on behalf of our media network owners to our brand customers. Media revenue services are recognized either on a straight-line basis over the available hours of advertising during the contracted period, or at the time of an event in the case of sponsorships.

Our media revenue contracts with customers range from four weeks to three years and billing commences at the beginning of the contract term, with payment generally due within ninety (90) days of billing. For the majority of our contracts, transaction prices are explicitly stated. Any contracts with transaction prices that contain multiple performance obligations are allocated primarily based on a relative standalone selling price basis. Any deferred revenues primarily consist of revenues paid in advance of being earned.

On a contract-by-contract basis, we evaluate whether we should be considered the principal (i.e., report revenues on a gross basis) or an agent (i.e., report revenues on a net basis). We are considered the principal in our arrangements and report revenues on a gross basis, wherein the amounts billed to customers are recorded as revenues and amounts paid to network owners are recorded as expenses. We are considered the principal because we control the advertising space before and after the contract term, are primarily responsible to our customers, and have discretion in pricing. For revenues generated through the use of a subcontracted advertising agency, commissions are calculated based on a stated percentage of gross advertising revenue and reported in the Consolidated Statement of Operations within Sales and Marketing expenses.

NOTE 5: BUSINESS COMBINATION

On November 12, 2021, the Company and Reflect, entered into an Agreement and Plan of Merger (as amended on February 8, 2022 and February 11, 2023, the “Merger Agreement") pursuant to which a direct, wholly owned subsidiary of Creative Realities, CRI Acquisition Corporation, or “Merger Sub,” would merge with and into Reflect, with Reflect surviving the merger and becoming our wholly owned subsidiary, which transaction is referred to herein as the “Merger.” On February 17, 2022, the parties consummated the Merger (the "Closing").

Reflect provides digital signage solutions, including software, strategic and media services to a wide range of companies across the retail, financial, hospitality and entertainment, healthcare, and employee communications industries in North America. Reflect offers digital signage platforms, including ReflectView, a platform used by companies to power hundreds of thousands of active digital displays. Through its strategic services, Reflect assists its customers with designing, deploying and optimizing their digital signage networks, and through its media services, Reflect assists customers with monetizing their digital advertising networks.

Subject to the terms and conditions of the Merger Agreement, at the Closing, Reflect stockholders as of the effective time of the Merger collectively received from the Company, in the aggregate, the following Merger consideration: (i) $16,166 in cash, (ii) 777,778 shares of common stock of Creative Realities (valued based on an issuance price of $6 per share) (the “CREX Shares”), (iii) the Secured Promissory Note (as described below), and (iv) supplemental cash payments (the “Guaranteed Consideration”), if any, payable on or after February 17, 2025 (subject to the Extension Option described below, the “Guarantee Date”), in an amount by which the value of the CREX Shares on such anniversary is less than $19.20 per share, or if certain customers of Reflect collectively achieve over 85,000 billable devices online at any time on or before December 31, 2022, is less than $21.60 per share (such applicable amount, the “Guaranteed Price”), multiplied by the amount of CREX Shares held by the Reflect stockholders on the Guarantee Date (subject to the Extension Option described below). At or before December 31, 2022, the condition of certain customers of Reflect collectively to achieve over 85,000 billable devices online was not met. Accordingly, the contingent cash payment amount was reduced at December 31, 2022 from $21.60 per share to $19.20 per share, a reduction of $2.40 per share.

The Company may exercise an extension option (the “Extension Option”) to extend the Guarantee Date by six (6) months, from February 17, 2025 to August 17, 2025, if (i) the Extension Threshold Price is greater than or equal to 70% of the Guaranteed Price described above, and (ii) the Company provides written notice of its election to exercise the Extension Option no later than February 7, 2025. The “Extension Threshold Price” means the average closing price per share of Creative Realities common stock as reported on the Nasdaq Capital Market (or NYSE) in the fifteen (15) consecutive trading day period ending February 2, 2025. If the Extension Threshold Price is less than 80% of the Guaranteed Price, then the Guaranteed Price will be increased by $3.00 per share.

In connection with the Merger, the Company adopted a Retention Bonus Plan and raised capital to, among other things, pay the cash portion of the Merger consideration. The Retention Bonus Plan is described below.

Retention Bonus Plan

On February 17, 2022, in connection with the Closing, the Company adopted a Retention Bonus Plan, pursuant to which the Company is required to pay to key members of Reflect’s management team an aggregate of $1,334 in cash, which was paid 50% at the Closing, and subject to continuous employment with Reflect or Creative Realities, 25% was paid on February 17, 2023 (the one-year anniversary of Closing) and 25% will be paid on February 17, 2024 (the two-year anniversary of the Closing). In connection with the closing of the Merger, the future cash payments due on the one-year and two-year anniversaries of the Closing were deposited into an escrow agreement. The Retention Bonus Plan also requires the Company to issue Common Stock having an aggregate value of $667 to the plan participants as follows: 50% of the value of such shares were issued at the Closing, and subject to continuous employment with Reflect or Creative Realities, 25% of the value of such shares was issued on February 17, 2023 (the one-year anniversary of Closing) and the remaining 25% of the value of such shares will be issued on February 17, 2024 (the two-year anniversary of the Closing). The shares issued on the Closing were valued at $6.00 per share. The shares issued on the one-year anniversary were valued at $2.22 based on the value of shares issuable divided by the trailing 10-day volume weighted average price ("VWAP") of the shares as of February 17, 2023 as reported on the Nasdaq Capital Market. The Company issued 62,475 shares to key members of Reflect's management team pursuant to the Retention Bonus Plan. Certain participants made an election to have stock withheld to cover applicable withholding taxes. In such cases, the Company reduced the stock award issued to the employee and settled the employees tax liability by remitting cash to the applicable taxing authorities. The shares to be issued on the two-year anniversary will be determined based on the value of shares issuable divided by the trailing 10-day VWAP of the shares as of February 17, 2024 as reported on the Nasdaq Capital Market.

Upon the resignation of a participant’s employment for “good reason,” or termination of the employment of a participant without “cause,” each as defined in the Retention Bonus Plan, the participant will be fully vested and will receive all cash and shares allocated to such participant under the Retention Bonus Plan. Any amounts unpaid by reason of a lapse in continuous employment or otherwise will be reallocated among the remaining Retention Bonus Plan participants.

Purchase price

The preliminary purchase price of Reflect consisted of the following items:

(in thousands)	Consideration	
Cash consideration for Reflect stock	$ 16,664	(1)
Cash consideration for Retention Bonus Plan	1,334	(2)
Common stock issued to Reflect stockholders	4,667	(3)
Common stock issued to Retention Bonus Plan	333	(4)
Secured Promissory Note	2,500	(5)
Earnout liability	10,862	(6)
Total consideration	36,360	
Vendor deposit with the Company	(818)	(7)
Cash acquired	(812)	(8)
Net consideration transferred	$ 34,730	

(1) Cash consideration for outstanding shares of Reflect capital stock per Merger Agreement.

(2) Cash consideration utilized to fund the Retention Bonus Plan per Merger Agreement.

(3) Company common stock issued in exchange for outstanding shares of Reflect capital stock per Merger Agreement.

(4) Company common stock issued to fund initial issuances under the Retention Bonus Plan per Merger Agreement.

(5) The Secured Promissory Note accrued interest at 0.59% (the applicable federal rate at the time of issuance of the Secured Promissory Note) and required the Company and Reflect to collectively pay equal monthly principal installments of $104 on the fifteenth (15th) day of each month, commencing on March 15, 2022. On February 11, 2023, the Company and the Stockholders' Representative executed an amendment (the "Note Amendment") to the Secured Promissory Note. The Note Amendment eliminated the balloon payment, extending the maturity date for a one-year period, to February 17, 2024. During the extended period, the Company will continue to make monthly principal payments of $104, and the annual interest rate on the outstanding principal increased from 0.59% to 4.60%, which will accrue and is payable in full on the new maturity date.

(6) Represents an estimate of the fair value of the Guaranteed Consideration as of the Merger, which, if any, is payable on or after February 17, 2025 (subject to the Extension Option), in an amount by which the value of the CREX Shares on such anniversary is less than $19.20 per share, multiplied by the amount of CREX Shares held by the Reflect stockholders on the Guarantee Date (subject to the Extension Option), subject to the terms of the Merger Agreement.

(7) Prior to the Merger, Reflect had engaged the Company on a project and paid the Company a deposit of $818. These amounts reduced consideration paid by the Company in accordance with ASC 805.

(8) Represents the Reflect cash balance acquired at Closing.

The Company incurred $37 and $428 of direct transaction costs for the three and six months ended June 30, 2022, respectively. These costs are included in deal and transaction expense in the accompanying Condensed Consolidated Statement of Operations.

The Company accounted for the Merger using the acquisition method of accounting. The final allocation of the purchase price is based on the fair value of assets acquired and liabilities assumed as of February 17, 2022, which included the following:

(in thousands)	**Total**
Accounts receivable	$ 1,359
Inventory	190
Prepaid expenses & other current assets	666
Property and equipment	96
Operating right of use assets	555
Other assets	36
Identified intangible assets:	
Definite-lived trade names	960
Definite-lived Developed technology	5,130
Definite-lived Customer relationships	11,040
Definite-lived Noncompete agreements	30
Goodwill	18,935
Accounts payable	(104)
Accrued expenses	(483)
Customer deposits	(1,661)
Deferred revenues	(1,259)
Current maturities of operating leases	(277)
Long-term obligations under operating leases	(278)
Other liabilities	(205)
Net consideration transferred	$ 34,730

The Company engaged a third-party valuation specialist to assist in the identification and calculation of the fair value of those separately identifiable intangible assets.

The Company completed its valuation procedures by asset utilizing the following approaches:

- Customer relationship asset was estimated using the income approach through a discounted cash flow analysis wherein the cash flows will be based on estimates used to price the Merger. Discount rates were benchmarked with reference to the implied rate of return from the Company’s pricing model and the weighted average cost of capital.

- Trade name asset represents the Reflect brand name as marketed primarily as a full services digital software solution, marketed in numerous verticals with the exception of food service. The Company applied the income approach through an excess earnings analysis to determine the fair value of the trade name asset. The Company applied the income approach through a relief-from-royalty analysis to determine the fair value of this asset.

- The developed technology assets are primarily comprised of know-how and functionality embedded in Reflect’s proprietary content management applications, which drive currently marketed products and services. The Company applied the income approach through a relief-from-royalty analysis to determine the preliminary fair value of this asset.

The Company is amortizing the identifiable intangible assets on a straight-line basis over the weighted average lives ranging from 2 to 10 years as outlined in the table below.

The table below sets forth the valuation and amortization period of identifiable intangible assets:

(in thousands)	**Valuation**	**Amortization Period (in years)**
Identifiable definite-lived intangible assets:		
Trade names	$ 960	5
Developed technology	5,130	10
Noncompete	30	2
Customer relationships	11,040	10
Total	$ 17,160	

The Company estimated the preliminary fair value of the acquired property and equipment using a combination of the cost and market approaches, depending on the component. The fair value of such property and equipment is $96.

The excess of the purchase price over the fair value of the tangible net assets and identifiable intangible assets acquired was recorded as goodwill. The factors contributing to the recognition of the amount of goodwill are based on several strategic and synergistic benefits that are expected to be realized from the Merger. These benefits include a comprehensive portfolio of iconic customer brands, complementary product offerings, enhanced national footprint, and attractive synergy opportunities and value creation. None of the goodwill is expected to be deductible for income tax purposes.

NOTE 6: SUPPLEMENTAL CASH FLOW STATEMENT INFORMATION

	Six Months Ended June 30,	
	2023	**2022**
Supplemental non-cash investing activities		
Capitalized software in accounts payable	$ 264	$ -
Property and equipment in accounts payable	$ 23	$ -
Right-of-use assets obtained in exchange for new finance lease liabilities	$ 89	$ -
Supplemental non-cash financing activities		
Conversion of liability warrant to equity warrants	$ -	$ 5,709
Supplemental disclosure information for cash flow		
Cash paid during the period for:		
Interest	$ 1,040	$ 656
Operating leases	$ 377	$ 252
Income taxes, net	$ 44	$ 44

NOTE 7: INTANGIBLE ASSETS, INCLUDING GOODWILL

Intangible Assets

Intangible assets consisted of the following at June 30, 2023 and December 31, 2022:

	June 30, 2023		December 31, 2022	
	Gross Carrying Amount	**Accumulated Amortization**	**Gross Carrying Amount**	**Accumulated Amortization**
Technology platform	$ 9,765	$ 4,737	$ 9,765	$ 4,354
Purchased and developed software	5,336	3,748	4,682	3,375
In-Process internally developed software platform	5,112	-	4,074	-
Customer relationships	15,000	3,497	15,000	2,849
Trademarks and trade names	1,600	904	1,600	808
Non-compete	30	21	30	13
	36,843	12,907	35,151	11,399
Accumulated amortization	12,907		11,399	
Net book value of amortizable intangible assets	$ 23,936		$ 23,752	

For the three months ended June 30, 2023 and 2022, amortization of intangible assets charged to operations was $755 and $431, respectively. For the six months ended June 30, 2023 and 2022 amortization of intangible assets charged to operations was $1,508 and $1,111, respectively.

Goodwill

Goodwill represents the excess of the purchase price over the fair value of net assets acquired. Goodwill is subject to an impairment review at a reporting unit level, on an annual basis at September 30th each fiscal year, when an event occurs, or circumstances change that would indicate potential impairment. The Company has only one reporting unit, and therefore the entire goodwill is allocated to that reporting unit.

The Company assessed the carrying value of goodwill at the reporting unit level based on an estimate of the fair value of its reporting unit. Fair value of the reporting unit was estimated using both (1) a market approach, leveraging recent industry merger and acquisition activity as well as comparable public company information, and (2) a discounted cash flow analyses consisting of various assumptions, including expectations of future cash flows based on projections or forecasts derived from analysis of business prospects and economic or market trends that may occur, specifically, the Company gave significant consideration to actual historic financial results, including revenue growth rates in the current and preceding three years, further informed by known backlog and customer acquisitions. Based on the Company's assessment, we determined that the fair value of our reporting unit exceeds its carrying value, and accordingly, the goodwill associated with the reporting unit is not considered to be impaired at September 30, 2022.

At December 31, 2022, we concluded the decline in our market value represented an interim indicator of potential impairment. Based on a quantitative assessment of our fair value performed at December 31, 2022, using the same approach as our annual impairment performed at September 30, described above, we concluded that the carrying value of our goodwill did not exceed the reporting unit fair value. No indicators of impairment were identified as of June 30, 2023. The Company recognizes that any differences between our actual and projected future results, or changes in our projected future results, could potentially have a material impact on our assessment of goodwill impairment. The Company will continue to monitor the actual performance of its operations against expectations and assess further indicators of possible impairment. The valuation of goodwill and intangible assets is subject to a high degree of judgment, uncertainty and complexity. Should any indicators of impairment occur in subsequent periods, the Company will be required to perform an analysis in order to determine whether goodwill is impaired.

NOTE 8: LOANS PAYABLE

The outstanding debt with detachable warrants, as applicable, are shown in the table below. Further discussion of the debt follows.

As of June 30, 2023

Debt Type	Issuance Date		Principal	Maturity Date	Warrants	Interest Rate Information
A	2/17/2022	$	10,000	2/15/2025	833,334	8.0% interest(1)
B	2/17/2022		833	2/17/2024	-	4.6% interest(2)
C	2/17/2022		7,185	2/15/2025	898,165	10.0% interest(3)
D	10/31/2022		119	9/1/2023	-	12.5% interest(4)
	Total debt, gross		18,137		1,731,499	
	Debt discount		(2,355)			
	Total debt, net	$	15,782			
	Less current maturities		(4,197)			
	Long term debt	$	11,585			

As of December 31, 2022

Debt Type	Issuance Date		Principal	Maturity Date	Warrants	Interest Rate Information
A	2/17/2022	$	10,000	2/15/2025	833,334	8.0% interest(1)
B	2/17/2022		1,456	2/17/2024	-	0.59% interest(2)
C	2/17/2022		7,185	2/15/2025	898,165	10.0% interest(3)
D	10/31/2022		2,000	9/1/2023	-	12.5% interest(4)
	Total debt, gross		20,641		1,731,499	
	Debt discount		(3,069)			
	Total debt, net	$	17,572			
	Less current maturities		(4,499)			
	Long term debt	$	13,073			

A – Acquisition Term Loan with related party
B – Secured Promissory Note
C – Consolidation Term Loan with related party
D – Term Loan (2022) with related party

(1) 8.0% cash interest per annum through maturity at February 15, 2025.
(2) Annual interest rate on the outstanding principal increased from 0.59% to 4.60% per annum effective February 17, 2023 through maturity at February 17, 2024. Annual interest rate was 0.59% cash interest per annum (the applicable federal rate) through February 17, 2023.
(3) 10.0% cash interest per annum through maturity date at February 15, 2025.
(4) 12.5% cash interest per annum through maturity at September 1, 2023.

Secured Promissory Note

On February 17, 2022, in connection with the Closing, the Company issued to RSI Exit Corporation (“Stockholders’ Representative”), the representative of Reflect stockholders, a $2,500 Note and Security Agreement (the “Secured Promissory Note”).

The Secured Promissory Note accrued interest at 0.59% per annum (the applicable federal rate on the date of issuance of the Secured Promissory Note) and required the Company and Reflect to collectively pay equal monthly principal installments of $104 on the fifteenth (15th) day of each month, commencing on March 15, 2022. Any remaining or unpaid principal was due and payable on February 17, 2023. All payments under the Secured Promissory Note are paid to the escrow agent in the Merger Agreement to be placed into the escrow account to secure the Reflect stockholders’ indemnification obligations until released on February 17, 2023 (the one-year anniversary of the Closing), at which time any remaining proceeds not subject to a pending indemnification claim would be paid to the exchange agent for payment to the Reflect stockholders pursuant to the Merger Agreement. The Secured Promissory Note is secured by a first-lien security interest in certain contracts of Reflect, including obligations arising out of those certain contracts. The Company has the right to offset amounts payable under the Secured Promissory Note upon a final, non-appealable decision of a court that entitles the Company or its affiliates to any damages for indemnification under the Merger Agreement, or the Stockholders’ Representative’s agreement in writing to such damages.

On February 11, 2023, the Company and the Stockholders’ Representative executed an amendment (the “Note Amendment”) to the Secured Promissory Note. The Note Amendment eliminates the balloon payment, extending the maturity date for a one-year period, to February 17, 2024. During the extended period, the Company will continue to make monthly principal payments of $104, and the annual interest rate on the outstanding principal increased from 0.59% to 4.60%, which will accrue and is payable in full on the new maturity date.

Second Amended and Restated Loan and Security Agreement

On February 17, 2022, the Company and its subsidiaries (collectively, the “Borrowers”) refinanced their debt facilities with Slipstream, pursuant to a Second Amended and Restated Credit and Security Agreement (the “Credit Agreement”). The Borrowers include Reflect, which became a wholly owned subsidiary of the Company as a result of the Closing on February 17, 2022. The debt facilities continue to be fully secured by all assets of the Borrowers.

The Credit Agreement also provides that the Company’s outstanding loans from Slipstream at December 31, 2021, consisting of its pre-existing $4,767 senior secured term loan and $2,418 secured convertible loan, with an aggregate of $7,185 in outstanding principal and accrued and unpaid interest under such loans, were consolidated into a term loan (the “Consolidation Term Loan”). The Consolidation Term Loan has an interest rate of 10.0%, with 75.0% warrant coverage (or 898,165 warrants). On the first day of each month, commencing March 1, 2022 through February 1, 2025, the Borrowers will make interest-only payments on the Consolidation Term Loan. Commencing on September 1, 2023, and on the first day of each month thereafter until the Maturity Date, the Borrowers will make a payment on the Consolidation Term Loan, in an equal monthly installment of principal sufficient to fully amortize the Consolidation Term Loan in eighteen equal installments. The Company assessed the combination of the pre-existing senior secured term loan and secured convertible loan in accordance with ASC 470 *Debt* and determined the transaction should be accounted for as an extinguishment, in part as the Consolidation Term Loan eliminated a substantive conversion feature. In aggregate the Company recorded a loss on extinguishment of $295 during the six month period ending June 30, 2022, primarily associated with the write-off of pre-existing debt discounts.

In addition to refinancing the existing debt with Slipstream, the Company issued to Slipstream a $10,000, 36-month senior secured term loan (the “Acquisition Term Loan”) resulting in $10,000 in gross proceeds, or $9,950 in net proceeds. The Acquisition Term Loan matures on February 17, 2025 (the “Maturity Date”) and has an interest rate of 8.0%, with 50.0% warrant coverage (or 833,334 warrants). On the first day of each month, commencing March 1, 2022 through February 1, 2025, the Borrowers will make interest-only payments on the Acquisition Term Loan. No principal payments on the Acquisition Term Loan are payable until the Maturity Date.

In connection with the Acquisition Term Loan and Consolidation Term Loan warrant coverage, the Company issued to Slipstream a warrant to purchase an aggregate of 1,731,499 shares of Company common stock (the “Lender Warrant”). The Lender Warrant has a five-year term, an initial exercise price of $6.00 per share, subject to adjustments in the Lender Warrant, and was not exercisable until August 17, 2022. The warrants were assessed in accordance with ASC 470 and ASC 815 *Derivatives* and were deemed to represent bifurcated derivative instruments that should be recorded as liabilities in the Condensed Consolidated Balance Sheets. The Company performed a Black-Scholes valuation of the warrants as of the issuance date, resulting in a fair value of $2.4387 per warrant. In recording the warrant liability, the Company recorded a debt discount associated with each of the Acquisition and Consolidation Term Loans in an amount of $2,032 and $2,190, respectively. These amounts are being amortized straight-line through interest expense over the life of the loans, resulting in incremental interest expense of $358 and $714 for the three and six months ended June 30, 2023, respectively. The Company has deemed straight-line amortization to be materially consistent with the effective interest method.

In certain circumstances, upon a fundamental transaction of the Company (e.g., a disposal or sale of all or the greater part of the assets or undertaking of the Company, an amalgamation or merger with another company, or implementation of a scheme of arrangement), the holder of the Lender Warrant will have the right to require the Company to repurchase the Lender Warrant at its fair value using a Black Scholes option pricing formula; provided that such holder may not require the Company or its successor entity to repurchase the Lender Warrant for the Black Scholes value in connection with a fundamental transaction that is not approved by the Company’s Board of Directors, and therefore not within the Company’s control.

Effective June 30, 2022, the Company amended the terms of the Lender Warrant to remove the holder’s option to exercise such warrant on a cashless basis utilizing the VWAP of the Company’s common stock on the trading day immediately preceding the date of a notice of cashless exercise in certain circumstances, and remove the condition to exercising such warrant that the Company’s shareholders approve the exercise thereof (which had already been obtained). The amendments to the Lender Warrant also extend the term of such warrants for an additional one year, such that the Lender Warrant will expire on February 17, 2028. The foregoing amendments to the Lender Warrant caused such warrants to be accounted for as equity instruments in the Company’s Consolidated Financial Statements.

On October 31, 2022, the Borrowers and Slipstream amended the Credit Agreement to provide the Borrowers with a $2,000 term loan ("Term Loan (2022)"), the net proceeds of which were used by the Company to accelerate an active software development project with potential to expand SaaS revenues associated with an existing customer. The Term Loan (2022) has an annual interest rate of 12.5% and matures on September 1, 2023. Commencing on February 1, 2023, the Borrowers will make monthly installment payments of approximately $270 until the maturity date, consisting of principal and interest sufficient to fully amortize the Term Loan (2022) through the maturity date.

NOTE 9: COMMITMENTS AND CONTINGENCIES

On August 2, 2019, the Company filed suit in Jefferson Circuit Court, Kentucky, against a supplier of the Company’s wholly owned subsidiary, Allure, for breach of contract, breach of warranty, and negligence with respect to equipment installations performed by such supplier for an Allure customer. On October 10, 2019, the Allure customer that is the basis of our claim above sent a demand to the Company for payment of $3,200 as settlement for an alleged breach of contract related to hardware failures of equipment installations performed by Allure between November 2017 and August 2018. On March 10, 2023, the Company, the supplier and the Allure customer reached a Settlement Agreement and Release of Claims ("Settlement Agreement"). Pursuant to the Settlement Agreement, the Company is obligated to pay $733; however, its insurer agreed to pay $700 of that amount. Thus, the Company paid $33 of the settlement amount in April 2023.

Except as noted above, the Company is not party to any other material legal proceedings, other than ordinary routine litigation incidental to the business, and there were no other such proceedings pending during the period covered by this Report.

NOTE 10: INCOME TAXES

Our deferred tax assets are primarily related to net federal and state operating loss carryforwards (NOLs). We have substantial NOLs that are limited in usage by IRC Section 382. IRC Section 382 generally imposes an annual limitation on the amount of NOLs that may be used to offset taxable income when a corporation has undergone significant changes in stock ownership within a statutory testing period. We have performed a preliminary analysis of the annual NOL carryforwards and limitations that are available to be used against taxable income. Based on the history of losses of the Company, there continues to be a full valuation allowance against the net deferred tax assets of the Company with a definite life.

For the three and six months ended June 30, 2023, we reported tax liability of $45 and $88, respectively. As of June 30, 2023, the net deferred tax liabilities totaled $75 after valuation allowance, compared to net tax liabilities of $28 at December 31, 2022.

NOTE 11: WARRANTS

A summary of outstanding warrants is included below:

	Warrants		
	Amount	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life
Balance December 31, 2022	5,824,027	$ 6.56	4.21
Warrants expired	(68,508)	10.40	-
Balance June 30, 2023	5,755,519	$ 6.51	3.76

On February 3, 2022, the Company entered into a Securities Purchase Agreement with a purchaser (the “Purchaser”), pursuant to which the Company agreed to issue and sell to the Purchaser, in a private placement priced at-the-market under Nasdaq rules, (i) 438,334 shares (the “Shares”) of the Company’s common stock, par value $0.01 per share (the “Common Stock”) and accompanying warrants to purchase an aggregate of 438,334 shares of Common Stock, and (ii) pre-funded warrants to purchase up to an aggregate of 1,950,502 shares of Common Stock (the “Pre-Funded Warrants”) and accompanying warrants to purchase an aggregate of 1,950,502 shares of Common Stock (collectively, the “Private Placement”). The accompanying warrants to purchase Common Stock are referred to herein collectively as the “Common Stock Warrants.” Under the Securities Purchase Agreement, each Share and accompanying warrants to purchase Common Stock were sold together at a combined price of $4.605, and each Pre-Funded Warrant and accompanying warrants to purchase Common Stock were sold together at a combined price of $4.6047, for gross proceeds of approximately $11,000, before deducting placement agent fees and estimated offering expenses payable by the Company. During the six months ended June 30, 2022, each of the Pre-Funded Warrants were exercised. The Common Stock Warrants expire five years from the date of issuance. The Company evaluated the Pre-Funded Warrants and concluded that they met the criteria to be classified within stockholders’ equity, with proceeds recorded as common stock and additional paid-in-capital. The Company evaluated the Common Stock Warrants and concluded they do not meet the criteria to be classified within stockholders’ equity. The Common Stock Warrants include provisions which could result in a different settlement value for the Common Stock Warrants depending on the registration status of the underlying shares. Because these conditions were not an input into the pricing of a fixed-for-fixed option on the Company’s ordinary shares, the Common Stock Warrants are not considered to be indexed to the Company’s own stock. The Company recorded these warrants as liabilities on the Condensed Consolidated Balance Sheets at fair value, with subsequent changes in their respective fair values recognized in the Condensed Consolidated Statements of Operations at each reporting date. At the date of issuance, the Company performed a Black-Scholes valuation of the warrants, resulting in a fair value of $3.2781 per warrant. At June 30, 2022, the Company reassessed the fair value of these warrants via Black Scholes valuation methodology and determined that the fair value of these warrants was $1.2057 per warrant, resulting in the Company recording a gain on the fair value of these warrants of $1,287 and $4,950 in the Condensed Consolidated Statement of Operations for the three and six months ended June 30, 2022.

On February 17, 2022, in connection with the Credit Agreement with Slipstream, the Company issued to Slipstream 1,731,499 warrants with an exercise price of $6.00 per share which expire five years from the date of issuance (the “Lender Warrant”). These warrants are not exercisable until 180 days after the issuance date. The common shares underlying these warrants have not yet been registered for resale under the Securities Act of 1933, which provides Slipstream with an option for cashless exercise once the warrant becomes exercisable until such time as such registration occurs. The Lender Warrants expire five years from the date of issuance. The Company evaluated the Lender Warrant and concluded that it does not meet the criteria to be classified within stockholders’ equity. The Lender Warrant includes provisions which could result in a different settlement value, for the Lender Warrant depending on the registration status of the underlying shares. Because these conditions are not an input into the pricing of a fixed-for-fixed option on the Company’s ordinary shares, the Lender Warrant is not considered to be indexed to the Company’s own stock. The Company recorded these warrants as liabilities on the consolidated balance sheets at fair value, with subsequent changes in their respective fair values recognized in the Condensed Consolidated Statements of Operations at each reporting date. At the date of issuance, the Company performed a Black-Scholes valuation of the warrants, resulting in a fair value of $2.4387 per warrant. In recording the warrant liability, the Company recorded an increase in debt discount in the Condensed Consolidated Balance Sheet associated with the issuance of the warrants of $4,223, which is being amortized through interest expense in the Condensed Consolidated Statement of Operations over the life of the Acquisition Term Loan and Consolidation Term Loans. At June 30, 2022, the Company reassessed the fair value of these warrants via Black Scholes valuation methodology and determined that the fair value of these warrants was $1.1097 per warrant, resulting in the Company recording a gain on the fair value of these warrants of $894 and $2,302 in the Condensed Consolidated Statement of Operations for the three and six months ended June 30, 2022.

On February 17, 2022, in connection with obtaining a waiver of certain restrictions in investment documents between an investor and the Company in order to consummate the financing contemplated by the Credit Agreement, the Company paid consideration to such investor in the form of a warrant (the "Purchaser Warrant") to purchase 466,667 shares of Company common stock in an at-the-market offering under Nasdaq rules. The number of shares of Company common stock subject to the Purchaser Warrant is equal to the waiver fee ($175) divided by $0.375 per share. The exercise price of the Purchaser Warrant is $4.23 per share, and the Purchaser Warrant is not exercisable until August 17, 2022. The Purchaser Warrant expires five years from the date of issuance. The Company evaluated the Purchaser Warrant and concluded that it does not meet the criteria to be classified within stockholders' equity. The Purchaser Warrant includes provisions which could result in a different settlement value, for the Purchaser Warrant depending on the registration status of the underlying shares. Because these conditions were not an input into the pricing of a fixed-for-fixed option on the Company's ordinary shares, the Purchaser Warrant is not considered to be indexed to the Company's own stock. The Company recorded these warrants as liabilities on the Condensed Consolidated Balance Sheets at fair value, with subsequent changes in their respective fair values recognized in the Condensed Consolidated Statements of Operations at each reporting date. At the date of issuance, the Company performed a Black-Scholes valuation of the Purchaser Warrant, resulting in a fair value of $2.5968 per warrant. In recording the warrant liability, the Company recorded an expense in the Condensed Consolidated Statement of Operations associated with the issuance of the Purchaser Warrant of $1,211. At June 30, 2022, the Company reassessed the fair value of the Purchase Warrant via Black Scholes valuation methodology and determined that the fair value of the Purchaser Warrant was $1.2051 per warrant, resulting in the Company recording a gain on the fair value of the Purchaser Warrant of $252 and $650 in the Condensed Consolidated Statement of Operations for the three and six months ended June 30, 2022.

Effective June 30, 2022, the Company amended the terms of the Common Stock Warrant (2,388,836 warrants), Lender Warrant (1,731,499 warrants) and Purchaser Warrant (466,667 warrants). The amendments to such warrants removes the holder's option to determine the value of such warrants utilizing the VWAP of the Company's common stock on the trading day immediately preceding the date of a notice in a cashless exercise, and removes the condition to exercising such warrants that the Company's shareholders approve the exercise thereof (which had already been obtained). The amendments to the warrants also extend the term of such warrants for an additional one year, such that the Common Stock Warrant will expire on February 3, 2028, and the Lender Warrant and Purchaser Warrant will expire on February 17, 2028.

The foregoing amendments to the warrants resulted in such warrants to be accounted for as equity instruments on the Company's Condensed Consolidated Financial Statements as of June 30, 2022. As such, the Company reclassified the warrant liability from noncurrent liabilities to additional paid-in-capital as of June 30, 2022. These amounts are reflected as additional paid-in-capital in the Condensed Consolidated Balance Sheet as of December 31, 2022.

NOTE 12: STOCK-BASED COMPENSATION

A summary of outstanding options is included below:

Time Vesting Options

Range of Exercise Prices between	Number Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Options Exercisable	Weighted Average Exercise Price
$4.01 - $8.00	566,673	7.14	$ 7.42	538,340	$ 7.46
$8.01+	96,125	2.53	25.22	96,125	$ 25.22
	662,798	6.47	$ 10.00	634,465	

Performance Vesting Options

Range of Exercise Prices between	Number Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Options Exercisable	Weighted Average Exercise Price
$4.01 - $8.00	240,000	6.93	$ 7.59	240,000	$ 7.59
	240,000	6.93	$ 7.59	240,000	

Market Vesting Options

Range of Exercise Prices between	Number Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Options Exercisable	Weighted Average Exercise Price
$0.01 - $4.00	733,334	1.64	$ 3.00	-	$ -
	733,334	1.64	$ 3.00	-	

	Market Vesting Options		***Time Vesting Options***		***Performance Vesting Options***	
Date/Activity	**Options Outstanding**	**Weighted Average Exercise Price**	**Options Outstanding**	**Weighted Average Exercise Price**	**Options Outstanding**	**Weighted Average Exercise Price**
Balance, December 31, 2022	633,334	3.00	662,910	$ 10.02	240,000	$ 7.59
Granted	100,000	3.00	-	-	-	-
Forfeited or expired	-	-	(112)	162.00	-	-
Balance, June 30, 2023	733,334	3.00	662,798	10.00	240,000	$ 7.59

The weighted average remaining contractual life for options exercisable is 6.53 years as of June 30, 2023.

Valuation Information for Stock-Based Compensation

For purposes of determining estimated fair value under FASB ASC 718-10, *Stock Compensation*, the Company computed the estimated fair values of stock options using the Black-Scholes model.

Amendment to Performance Options

On June 1, 2020, Rick Mills, CEO, and Will Logan, CFO, were issued ten-year options to purchase 160,000 and 80,000 shares of common stock (the “Performance Options”), respectively, which vest in equal installments over a three-year period (2020-2022), subject to satisfying the Company revenue targets and EBITDA (earnings before interest, taxes, depreciation and amortization) targets for the applicable year. In each of calendar years 2020, 2021 and 2022, one-third of the total shares may vest (if the revenue and EBITDA targets are met), and the shares that are subject to vesting each year are allocated equally to each of the revenue and EBITDA targets for such year. The Performance Options include a catch-up provision, where any options that did not vest during a prior year due to the Company’s failure to meet a prior revenue or EBITDA target may vest in a subsequent vesting year if the revenue or EBITDA target, as applicable, is met in the future year.

On June 15, 2022, the Board approved of an amendment to the Performance Options to provide that the revenue target for the calendar year 2022 set forth therein ($38,000) was eliminated, and the remaining shares that are available for vesting under the Performance Options (106,667 unvested shares for Mr. Mills and 53,334 for Mr. Logan) (including the unvested portions of shares based on the satisfaction of the revenue targets for 2020 and 2021 by virtue of the catch-up provisions in the Performance Options) will fully vest upon the achievement of an updated EBITDA target for calendar year 2022 of $3,600.

The Performance Options state that the calculation of EBITDA set forth in the Performance Options shall be calculated in a form consistent with the Company’s 2022 approved budget, which

(i) excludes any impact on EBITDA of:

(a) the accounting treatment (including any “mark-to-market accounting”) of the Company’s warrants or the Guaranteed Consideration (as defined in the Merger Agreement),

(b) non-recurring transaction expenses associated with the Merger and the capital raising financing activities of the Company to effectuate the Merger, and

(c) any write-down or write-off of any Company inventory of Safe Space Solutions products.

(ii) includes deductions related to any cash or stock bonuses paid or payable to any employees of the Company for services provided in calendar year 2022 (even if such bonuses are actually paid after calendar year 2022), including bonuses paid pursuant to the terms of the 2022 Cash Bonus Plan (as described below) (collectively, the “EBITDA Calculations”).

The unvested portion of the Performance Options as of December 31, 2022 vested in full effective March 30, 2023 upon confirmation by the Board of Directors of achievement of the performance metrics for the year ended December 31, 2022.

The exercise price of the foregoing options is $7.59 per share, the closing price of the Company’s common stock on the date of issuance (as adjusted by the Company's 1-for-3 reverse stock split in March 2023). The options were issued from the 2014 Stock Incentive Plan.

Issuance of Options

On June 15, 2022, Messrs. Mills and Logan received ten-year options to purchase 333,334 and 200,000 shares of common stock, respectively (the “New Options”). The New Options are eligible to vest at any time on or prior to February 17, 2025 if the trailing 10-trading day VWAP of the Company’s common stock, as reported on the Nasdaq Capital Market, exceeds the share price targets below, subject to such executive serving the Company as a director, officer, employee or consultant at such time:

	Share Price Target						
Executive	**$6.00**	**$9.00**	**$12.00**	**$15.00**	**$18.00**	**Guaranteed Price**	**Total Shares**
Mills Shares Vested	16,667	33,334	50,000	66,667	83,333	83,333	333,334
Logan Shares Vested	10,000	20,000	30,000	40,000	50,000	50,000	200,000
Percentage of Shares Vested	5%	10%	15%	20%	25%	25%	

The “Guaranteed Price” has the meaning ascribed to such term in the Merger Agreement, which currently means $19.20 per share.

The exercise price of the New Options is $3.00 per share, which exceeded the closing price of the Company’s common stock on the date of issuance (as adjusted by the Company's 1-for-3 reverse stock split in March 2023). The New Options are issued from the Company’s 2014 Stock Incentive Plan, as amended. An additional 100,000 options with identical market vesting restrictions were issued to non-executives.

The fair value of the options on the grant date varied between $0.63 and $1.11 per award as determined using the Monte Carlo model. These values were calculated using the following weighted average assumptions:

Risk-free interest rate	3.30%
Expected term (in years)	2.68
Expected price volatility	123.53%
Dividend yield	0%

At June 30, 2023, the Company evaluated the probability of achieving the share price targets in each tranche based, in part, on work performed by the Company’s third party valuation specialist in conjunction with evaluating the equity guarantee contingent liability. As a result of that evaluation of probability, during the three and six month period ending June 30, 2023 the Company recorded $4 and $7 of compensation expense, respectively. These awards have not yet vested and are subject to actual share price performance through February 2025.

Stock Compensation Expense Information

ASC 718-10, *Stock Compensation*, requires measurement and recognition of compensation expense for all stock-based payments including warrants, stock options, restricted stock grants and stock bonuses based on estimated fair values. Under the Amended and Restated 2006 Equity Incentive Plan, the Company reserved 573,334 shares for purchase by the Company’s employees and under the Amended and Restated 2006 Non-Employee Director Stock Option Plan the Company reserved 233,334 shares for purchase by the Company’s employees. There are 3,890 options outstanding under the 2006 Equity Incentive Plan.

In October 2014, the Company’s shareholders approved the 2014 Stock Incentive Plan, under which 7,390,355 shares were reserved for purchase by the Company’s employees. In August 2018, a special meeting of shareholders was held in which the shareholders voted to amend the Company’s 2014 Stock Incentive Plan to increase the reserve of shares authorized for issuance thereunder, from 7,390,355 shares to 18,000,000 shares. Following a 1-for-30 reverse stock split, the shares authorized for issuance under the Company’s 2014 Stock Incentive Plan was reduced to 600,000. On July 10, 2020, the Company’s shareholders approved an amendment to the Company’s 2014 Stock Incentive Plan to increase the reserve of authorized for issuance thereunder to 6,000,000. Following a 1-for-3 reverse stock split, the shares authorized for issuance under the Company's 2014 Stock Incentive Plan was reduced to 2,000,000. There are 1,632,242 options outstanding under the 2014 Stock Incentive Plan.

Employee Awards

Compensation expense recognized for the issuance of stock options to employees for the three and six months ended June 30, 2023 of $152 and $377, respectively, was included in general and administrative expense in the Condensed Consolidated Financial Statements. Compensation expense recognized for the issuance of stock options to employees for the three and six months ended June 30, 2022 of $398 and $948, respectively, was included in general and administrative expense in the Condensed Consolidated Financial Statements

At June 30, 2023, there was $498 of total unrecognized compensation expense related to unvested share-based awards with performance vesting criteria for employees. Compensation expense related to performance vesting options will be recognized if it becomes probable that the Company will achieve the identified performance metrics.

Non-Employee Awards

Compensation expense recognized for the issuance of stock options to our Board of Directors, for the three and six month period ended June 30, 2023 of $43 and $86, was included in general and administrative expense in the Condensed Consolidated Financial Statements. Compensation expense recognized for the issuance of stock options to our Board of Directors, for the three and six month period ended June 30, 2022 of $356 and $895, was included in general and administrative expenses in the Condensed Consolidated Financial Statements.

At June 30, 2023, there was approximately $65 of total unrecognized compensation expense related to unvested share-based awards with time vesting criteria for non-employee directors. Generally, expense related to the time vesting options will be recognized over the next year and will be adjusted for any future forfeitures as they occur.

The Company engages certain consultants to perform services in exchange for Company common stock. Shares issued for services were calculated based on the ten (10) day VWAP for the last ten (10) days during the month of service provided.

During the three and six months ended June 30, 2023, the Company issued shares issuable in exchange for services in the amount of $30 and $55, respectively. During the three and six months ended June 30, 2022, the Company issued shares issuable in exchange for services in the amount of $45 and $70, respectively.

NOTE 13: SIGNIFICANT CUSTOMERS/VENDORS

Significant Customers

We had two customers that in the aggregate accounted for 28.3% of accounts receivable at June 30, 2023 and three customers that in the aggregate accounted for 49.2% of accounts receivable at December 31, 2022.

We had three customers that in the aggregate accounted for 33.5% of revenue for the three months ended June 30, 2023, compared to two customers that in the aggregate accounted for 37.5% of revenue for the three months ended June 30, 2022.

We had two customers that in the aggregate accounted for 29.7% of revenue for the six months ended June 30, 2023, compared to three customers that in the aggregate accounted for 54.3% of revenue for the six months ended June 30, 2022.

Significant Vendors

We had one vendor that in the aggregate accounted for 36.1% of outstanding accounts payable at June 30, 2023, and one vendor that accounted for 30.1% of outstanding accounts payable at December 31, 2022.

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

The following discussion contains various forward-looking statements within the meaning of Section 21E of the Exchange Act. Although we believe that, in making any such statement, our expectations are based on reasonable assumptions, any such statement may be influenced by factors that could cause actual outcomes and results to be materially different from those projected. When used in the following discussion, the words "anticipates," "believes," "expects," "intends," "plans," "estimates," "projects," should," "may," "propose," and similar expressions (or the negative versions of such words or expressions), as they relate to us or our management, are intended to identify such forward-looking statements. These forward-looking statements are subject to numerous risks and uncertainties that could cause actual results to differ materially from those anticipated, and many of which are beyond our control. Factors that could cause actual results to differ materially from those anticipated are set forth under the caption "Risk Factors" in the Company's Form 10-K for the year ended December 31, 2022 as filed with the Securities and Exchange Commission on March 30, 2023.

Our actual results, performance or achievements could differ materially from those expressed in, or implied by, forward-looking statements. Accordingly, we cannot be certain that any of the events anticipated by forward-looking statements will occur or, if any of them do occur, what impact they will have on us. We caution you to keep in mind the cautions and risks described in this document and to refrain from attributing undue certainty to any forward-looking statements, which speak only as of the date of the document in which they appear. We do not undertake to update any forward-looking statement.

Overview

Creative Realities, Inc. (“Creative Realities,” “we,” “us,” or the “Company”) transforms environments through digital solutions by providing innovative digital signage solutions for key market segments and use cases, including:

- Retail
- Entertainment and Sports Venues
- Restaurants, including quick-serve restaurants (“QSR”)
- Convenience Stores
- Financial Services
- Automotive
- Medical and Healthcare Facilities
- Mixed Use Developments
- Corporate Communications, Employee Experience
- Digital out of Home (DOOH) Advertising Networks

We serve market-leading companies, so there is a good chance that if you leave your home today to shop, work, eat or play, you will encounter one or more of our digital signage experiences. Our solutions are increasingly visible because we help our enterprise customers achieve a range of business objectives including:

- Increased brand awareness
- Improved customer support
- Enhanced employee productivity and satisfaction
- Increased revenue and profitability
- Improved guest experience
- Increased customer/guest engagement

Through a combination of organically grown platforms and a series of strategic acquisitions, including our acquisition of Reflect in February 2022, the Company assists clients to design, deploy, manage, and monetize their digital signage networks. The Company sources leads and opportunities for its solutions through its digital and content marketing initiatives, close relationships with key industry partners, specifically equipment manufacturers, and the direct efforts of its in-house industry sales experts. Client engagements focus on consultative conversations that ensure the Company’s solutions are positioned to help clients achieve their business objectives in the most cost-effective manner possible.

When comparing Creative Realities to other digital signage providers, our customers value the following competitive advantages:

- **Breadth of solutions** – Creative Realities is one of only a few companies in the industry capable of providing the full portfolio of products and services required to implement and run an effective digital signage network. We leverage a 'single vendor' approach, providing clients with a one-stop-shop for sourcing digital signage solutions from design through day two services.

- **Managed labor pool** – Unlike most companies in our industry, we have a curated labor pool including thousands of qualified and vetted field technicians available to service clients quickly nationwide. We can meet tight schedules even in exceptionally large deployments and still ensure quality and consistency.

- **In-house creative resources** – We assist clients in repurposing existing content for digital signage experiences or creating new content, an activity for which the Company has won several design awards in recent years. In each instance, our services can be essential in helping clients develop an effective content program.

- **Network scalability and reliability** – Our software as a service ("SaaS") content management platforms power some of the largest and most complex digital signage networks in North America evidencing our ability to manage enterprise scale projects. This also provides us purchasing power to source products and services for our customers, enabling us to deliver cost effective, reliable and powerful solutions to small and medium size business clients.

- **Ad management platform** – Our customers are increasingly interested in monetizing their digital signage networks through advertising content. However, efficiently scheduling advertising content into digital signage playlists to meet campaign objectives can be a challenging and labor-intensive process. AdLogic, our home-grown, content management-agnostic platform, automates this process, allowing network owners to capture more revenue with less expense.

- **Media sales** – Few, if any other digital signage solution providers, can offer their clients media sales as a service. We have in-house media sales expertise to elevate conversations with clients interested in better understanding network monetization. We believe this meaningful differentiation in the sales process provides an additional revenue stream to Creative Realities compared to our competitors.

- **Market sector expertise** – Creative Realities has in-house experts in key market segments such as automotive, retail, quick-serve restaurants (QSR), convenience stores, and Digital Out of Home (DOOH) advertising. Our expertise in these business segments enables our teams to provide meaningful business conversations and offer tailored solutions with prospects and customers to their unique business objectives. These experts build industry relationships and create thought leadership that drives lead flow and new opportunities for our business.

- **Logistics** – Implementing a large digital signage project can be a logistics nightmare that can stall an initiative even before deployment. Our expertise in logistics improves deployment efficiency, reduces delays and problems, and saves customers time and money.

- **Technical support** – Digital signage networks present unique challenges for corporate IT departments. Creative Realities helps simplify and improve end user support by leveraging our own Network Operations Center ("NOC") in Louisville, Kentucky. The NOC resolves many issues remotely and when field support is required, it can be dispatched from the NOC, leveraging our managed labor pool to resolve customer issues quickly and effectively.

- **Integrations and Application Development** – The future of digital signage is not still images and videos on a screen. Interactive applications and integrations with other data sources will dominate the future. From social media feeds to corporate data stores to Point of Sale ("POS") systems, our proven ability to build scalable applications and integrations is a key advantage clients can leverage to deliver more compelling and engaging experiences for their customers.

- **Hardware support** – A number of digital signage providers sell a proprietary media player or align themselves with just one operating system. We utilize a range of media players including Windows, Android and BrightSign to provide clients the flexibility they need to select the appropriate hardware for any application knowing the entire network can still be served by a single digital signage platform, reducing complexity and improving the productivity of their teams.

The three primary sources of revenue for the Company are:

- Hardware sales from reselling digital signage hardware from original equipment manufacturers such as Samsung and BrightSign.

- Services revenue from helping customers design, deploy and manage their digital signage network, including:

  - Hardware system design/engineering

  - Hardware installation

  - Content development

  - Content scheduling

  - Post-deployment network and field support

  - Media sales

- Recurring subscription licensing and support revenue from our digital signage software platforms, which are generally sold via a SaaS model. These include:

  - **ReflectView**, the Company's core digital signage platform for most applications, scalable and cost effective from 10 to 100,000+ devices

  - **Reflect Xperience**, a web-based interface that allows customers to give content scheduling access to local users via the web or mobile devices, while still maintaining centralized programming control

  - **Reflect AdLogic**, the Company's ad management platform for digital signage networks, which presently delivers approximately 50 million ads daily

  - **Reflect Clarity**, the Company's menu board solution, which has become a market leader for a range of restaurant and convenience store applications

  - **Reflect Zero Touch**, which allows customers to turn any screen into an interactive experience by allowing guests to engage using their mobile device

  - **iShowroomProX**, an omni-channel digital sales support platform targeted at original equipment manufacturers in the transportation sector, which integrates with dozens of key data services including dealer inventory at the VIN level

  - **OSx+**, a digital VIN-level checklist used to assist in the tracking and delivery of new vehicles in the transportation sector, providing measurable lift in customer satisfaction scores and connected vehicle enrollments and subscription activations.

While hardware sales and support services revenues can fluctuate more significantly year over year based on new, large-scale network deployments, the Company expects to see continuous growth in recurring SaaS revenue for the foreseeable future as digital signage adoption/utilization continues to expand across the vertical markets we serve.

Our Expenses

Our expenses are primarily comprised of three categories: sales and marketing, research and development, and general and administrative. Sales and marketing expenses include salaries and benefits for our sales, business development solution management and marketing personnel, and commissions paid on sales. This category also includes amounts spent on marketing networking events, promotional materials, hardware and software to prospective new customers, including those expenses incurred in trade shows and product demonstrations, and other related expenses. Our research and development expenses represent the salaries and benefits of those individuals who develop and maintain our proprietary software platforms and other software applications we design and sell to our customers. Our general and administrative expenses consist of corporate overhead, including administrative salaries, real property lease payments, salaries and benefits for our corporate officers and other expenses such as legal and accounting fees.

Recent Developments

Reverse stock split

On March 23, 2023, the Company filed Articles of Amendment with the Secretary of State of the State of Minnesota to effectuate, effective March 27, 2023, a 1-for-3 stock split of the shares of the Company's common stock, par value $0.01 per share.

As a result of the reverse stock split, effective 12:01 am on March 27, 2023, every three shares of common stock then-issued and outstanding automatically combined into one share of common stock, with no change in par value per share. No fractional shares were outstanding following the reverse stock split and any fractional shares resulting from the reverse split were rounded up to the nearest whole share of common stock. In connection with the reverse stock split, the total number of shares of common stock authorized for issuance was reduced from 200,000,000 shares to 66,666,666 shares in proportion to the reverse stock split.

Effective as of the same time as the reverse stock split, the number of shares of common stock available for issuance under the Company's equity compensation plans were reduced in proportion to the reverse stock split. The reverse stock split also resulted in the number of shares of shares of common stock issuable upon exercise of outstanding warrants, or the exercise or vesting of equity awards, in proportion to the reverse stock split and caused a proportionate increase in exercise price or share-based performance criteria, where applicable.

Rejection of unsolicited offer

On February 2, 2023, we received an unsolicited proposal from Pegasus Capital Advisors, L.P., on behalf of itself and certain of its affiliates, including Slipstream (collectively, “Pegasus”), to acquire all of the outstanding shares of common stock of the Company that are not owned by Pegasus for a purchase price of $0.83 per share (or, as a result of our recent reverse stock split, $2.49 per share) in cash. Pegasus is the beneficial owner of our common stock owned of record by Slipstream. The Special Committee of the Company’s Board of Directors (the “Special Committee”) has concluded that such proposal undervalues the Company based on the Special Committee’s views of the intrinsic value of the Company’s existing business and current and future prospects, and is not in the best interests of the Company’s existing shareholders. Consequently, the Special Committee has advised Pegasus that it has rejected the proposal.

On May 1, 2023, we received a subsequent unsolicited proposal from Pegasus to acquire all of the outstanding shares of common stock of the Company that are not owned by Pegasus for a purchase price of $2.85 per share in cash. The Special Committee has concluded that such proposal undervalues the Company based on the Special Committee’s views of the intrinsic value of the Company’s existing business and current and future prospects, and is not in the best interests of the Company’s existing shareholders. Consequently, the Special Committee has advised Pegasus that it has rejected the proposal.

Please see Note 5 *Business Combinations*, Note 8 *Loans Payable*, Note 11 *Warrants*, and Note 12 *Stock-based Compensation* to the Company’s Condensed Consolidated Financial Statements contained in this Report for a description of recent developments of the Company that occurred during, and subsequent to, the three and six months ended June 30, 2023.

Critical Accounting Policies and Estimates

The Company's significant accounting policies are described in Note 2 *Summary of Significant Accounting Policies* of the Company's Condensed Consolidated Financial Statements included elsewhere in this Report. The Company's Condensed Consolidated Financial Statements are prepared in conformity with accounting principles generally accepted in the United States. Certain accounting policies involve significant judgments, assumptions, and estimates by management that could have a material impact on the carrying value of certain assets and liabilities and disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Our actual results could differ from those estimates.

Results of Operations

Note: All dollar amounts reported in Results of Operations are in thousands, except share and per-share information.

Three Months Ended June 30, 2023 Compared to Three Months Ended June 30, 2022

The tables presented below compare our results of operations and present the results for each period and the change in those results from one period to another in both dollars and percentage change.

	For the three months ended June 30,		Change	
	2023	2022	$	%
Sales	$ 9,196	$ 10,923	$ (1,727)	16%
Cost of sales	4,898	6,261	$ (1,363)	22%
Gross profit	4,298	4,662	(364)	8%
Sales and marketing expenses	1,229	1,147	82	7%
Research and development expenses	377	418	(41)	10%
General and administrative expenses	2,595	2,562	33	1%
Depreciation and amortization expense	797	468	329	70%
Deal and transaction expense	-	37	(37)	100%
Total operating expenses	4,998	4,632	366	8%
Operating (loss) income	(700)	30	(730)	2433%
Other income/(expenses):				
Interest expense	(787)	(750)	(37)	5%
Change in fair value of warrant liability	-	2,433	(2,433)	100%
Change in fair value of equity guarantee	(16)	(73)	57	100%
Loss on warrant amendment	-	(345)	345	100%
Gain on settlement of obligations	-	21	(21)	100%
Other income/(expense)	123	(1)	124	12400%
Total other income/(expenses)	(680)	1,285	(1,965)	153%
Net (loss) income before income taxes	(1,380)	1,315	(2,695)	205%
Provision for income taxes	(45)	(53)	8	15%
Net (loss) income	$ (1,425)	$ 1,262	(2,687)	213%

Sales

Sales were $9,196, representing a decrease of $1,727, or 16%, as compared to the same period in 2022. Hardware revenues were $3,437 for the three month period ended June 30, 2023, a decrease of $2,230, or 39%, as compared to the prior year. Hardware revenues generated during the three month period ended June 30, 2022 were driven by two customers which refreshed their digital hardware throughout their entire geographic footprint. These refresh activities are cyclical in nature and no current customer executed a similar large scale refresh during the three months ended June 30, 2023. Those refresh activities represented $2,418 in incremental hardware revenue during the three months ended June 30, 2022. Services and other revenues were $5,759 for the three month period ended June 30, 2023, an increase of $503, or 10%, driven primarily by increases in installation services revenue.

Gross Profit

Gross profit decreased by $364, or 8% during the three months ended June 30, 2023 as compared to the same period in 2022 driven by an increase in installation services revenue.

Gross profit margin increased to 47% during the three months ended June 30, 2023, from 43% in the same period in 2022 driven by (1) favorable revenue mix during the three months ended June 30, 2023 as managed services, which includes higher margin SaaS and other services revenues, increased to 42% of total revenue as compared to 35% of total revenues in the three months ended June 30, 2022, and (2) margin expansion in hardware, partially offset by reduced revenue in the current year.

Sales and Marketing Expenses

Sales and marketing expenses generally include the salaries, taxes, and benefits of our sales and marketing personnel, as well as trade show activities, travel, and other related sales and marketing costs. Sales and marketing expenses increased by $82, or 7%, driven primarily by the Company's enhanced investments into sales and marketing activities. Following the Merger, the Company adopted certain tools, technology, and processes – particularly with respect to lead generation and brand marketing – that were historically undercapitalized by the Company and have since accelerated new customer acquisition. Through completion of the Merger, the Company also acquired a media sales business unit that serves to monetize customer networks via the direct sale of advertising to be displayed on digital advertising networks owned by those customers. This business utilizes internal and third-party sales agents - the salaries and commissions of which are included within Sales and Marketing Expense within the Condensed Consolidated Statement of Operations. We expect the sales and marketing expenses of the Company for the three months ended June 30, 2023 to adequately reflect normal spend in these areas in future reporting periods.

Research and Development Expenses

Research and development expenses generally include personnel and development tools costs associated with the continued development of the Company's content management systems and other related application development. The Company capitalizes certain of these expenses and amortizes those costs through the Condensed Consolidated Statement of Operations on a straight-line basis over the economic useful life of the software feature or functionality. Research and development expenses decreased by $41, or 10%, for the three month period ended June 30, 2023 as compared to the same period in 2022 driven primarily by an elevated level of capitalized activity during the current quarter associated with a customer-facing opportunity.

General and Administrative Expenses

General and administrative expenses were effectively flat, increasing $33, or 1%. Compared to the three months ended June 30, 2022, the Company experienced decreases of (1) $203 in stock compensation expense as outstanding performance awards were fully expensed as of December 31, 2022, and (2) reductions in certain expenses following completion of integration activities/projects completed during 2022 following the Merger (including but not limited to consolidation of CMS tools, cloud hosting environments, IT tools) that materialized through the balance of 2022. These decreases were offset by increases of $278 in increased personnel costs as a result of higher headcount following the Merger and scaled up operations in response to an increase in customer acquisitions.

Depreciation and Amortization Expenses

Depreciation and amortization expenses increased $329, or 70%, in the three months ended June 30, 2023 compared to the same period in 2022, driven by incremental amortization expense generated from the addition of $17,160 in amortizing intangible assets on February 17, 2022, as a result of the Merger, and a measurement period adjustment recorded during the three months ended June 30, 2022 which artificially reduced the total depreciation and amortization expense. The Company current expects depreciation and amortization expense to be approximately $800 per quarter for the remainder of 2023.

Interest Expense

See Note 8 *Loans Payable* to the Condensed Consolidated Financial Statements for a discussion of the Company’s debt and related interest expense obligations.

Changes in Fair Value of Warrant Liability

During the three month period ended June 30, 2022, the Company recorded a gain of $2,433 as the result of assessing the fair value of warrant liabilities associated with the Company’s issuance of warrants in its debt and equity offerings completed in February 2022 to finance the Merger. These warrants were initially assessed at fair value through Black Scholes calculation, with changes in fair value recognized at each period end.

Loss on Warrant Amendment

Effective June 30, 2022, the Company amended the terms of certain warrants previously issued to its creditor and an investor, which removed the holder’s option to exercise such warrants on a cashless basis utilizing the VWAP of the Company’s common stock on the trading day immediately preceding the date of a notice of cashless exercise in certain circumstances, and removed the condition to exercising such warrants that the Company’s shareholders approve the exercise thereof (which had already been obtained). The amendments to the warrants extended the term of such warrants for an additional one year. As a result of the extension in term provided in exchange for the amendment, the Company reassessed the fair value of those warrants, resulting in the Company recording a loss on the fair value of these warrants of $345. The foregoing amendments to the warrants resulted in such warrants to be accounted for as equity instruments on the Company’s Condensed Consolidated Financial Statements as of June 30, 2022.

Six Months Ended June 30, 2023 Compared to Six Months Ended June 30, 2022

The tables presented below compare our results of operations and present the results for each period and the change in those results from one period to another in both dollars and percentage change.

	For the Six Months Ended June 30,		Change	
	2023	2022	$	%
Sales	$ 19,140	$ 21,680	$ (2,540)	12%
Cost of sales	9,753	13,126	(3,373)	26%
Gross profit	9,387	8,554	833	10%
Sales and marketing expenses	2,365	1,854	511	28%
Research and development expenses	743	659	84	13%
General and administrative expenses	5,493	5,422	71	1%
Depreciation and amortization expense	1,576	1,175	401	34%
Deal and transaction expenses	-	428	(428)	100%
Total operating expenses	10,177	9,538	639	7%
Operating loss	(790)	(984)	194	20%
Other income/(expenses):				
Interest expense	(1,590)	(1,199)	(391)	33%
Change in fair value of warrant liability	-	7,902	(7,902)	100%
Change in fair value of equity guarantee	(92)	(73)	(19)	26%
Loss on debt waiver consent	-	(1,212)	1,212	100%
Loss on warrant amendment	-	(345)	345	100%
Loss on settlement of debt	-	(274)	274	100%
Other income	135	5	130	2600%
Total other income/(expenses)	(1,547)	4,804	(6,351)	132%
Net (loss) income before income taxes	(2,337)	3,820	(6,157)	161%
Provision from income taxes	(88)	(56)	(32)	57%
Net (loss) income	$ (2,425)	$ 3,764	(6,189)	164%

Sales

Sales were $19,140, representing a decrease of $2,540, or 12%, as compared to the same period in 2022. Hardware revenues were $7,759 for the six month period ended June 30, 2023 as compared to $12,126 for the six month period ended June 30, 2022, a decrease of $4,367, or 36%. Hardware revenues generated during the six month period ended June 30, 2023 were driven by two customers which refreshed their digital hardware throughout their entire geographic footprint . These refresh activities are cyclical in nature and no current customer executed a similar large scale refresh during the six months ended June 30, 2023. Those refresh activities represented $4,418 in incremental hardware revenue during the six months ended June 30, 2022.

Services and other revenues were $11,381 for the six month period ended June 30, 2023, an increase of $1,827, or 19%, driven by growth in managed services revenue. Managed services revenue, which includes both SaaS and help desk technical subscription services, as well as non-contracted recurring content management services, were $7,907 in the six months ended June 30, 2023 as compared to $6,535 in the same period in 2022, driven by expansion in the Company's SaaS revenue and the inclusion of Reflect revenue for a full six months in the current year as compared to approximately four and one half months during the six months ended June 30, 2022 as a result of the Merger closing on February 17, 2022. This represents a year-over-year growth rate of 21% in our higher margin, primarily subscription-based, managed services revenue.

Gross Profit

Gross profit increased by $833, or 10% during the six months ended June 30, 2023 as compared to the same period in 2022 driven by improvements in hardware gross margins as a result of a significant deployment with gross margin of approximately 25%.

Gross profit margin increased to 49% during the six months ended June 30, 2023, from 39% in the same period in 2022 driven by (1) favorable revenue mix as managed services revenue, which includes higher margin SaaS and other services revenues, increased to 41% of total revenue for the six months ended June 30, 2023 as compared to 30% of total revenues in the six months ended June 30, 2022 and (2) margin expansion in hardware partially offset by reduced revenue in the current year.

Sales and Marketing Expenses

Sales and marketing expenses generally include the salaries, taxes, and benefits of our sales and marketing personnel, as well as trade show activities, travel, and other related sales and marketing costs. Sales and marketing expenses increased by $511, or 28%, driven primarily by (1) the acquisition of Reflect via the Merger on February 17, 2022, and (2) the Company's enhanced investments into sales and marketing activities. Following the Merger, the Company adopted certain tools, technology, and processes – particularly with respect to lead generation and brand marketing – that were historically undercapitalized by the Company and have since accelerated new customer acquisition. Through completion of the Merger, the Company also acquired a media sales business unit that serves to monetize customer networks via the direct sale of advertising to be displayed on digital advertising networks owned by those customers. This business utilizes internal and third party sales agents - the salaries and commissions of which are included within Sales and Marketing Expense within the Condensed Consolidated Statement of Operations. We expect the sales and marketing expenses of the Company for the six months ended June 30, 2023 to adequately reflect the normal spend in these areas in future reporting periods.

Research and Development Expenses

Research and development expenses generally include personnel and development tools costs associated with the continued development of the Company's content management systems and other related application development. The Company capitalizes certain of these expenses and amortizes those costs through the Condensed Consolidated Statement of Operations on a straight-line basis over the economic useful life of the software feature or functionality. Research and development expenses increased by $84, or 13%, for the six month period ended June 30, 2023 as compared to the same period in 2022 driven primarily by incremental headcount added via completion of the Merger on February 17, 2022. Through the Merger, we acquired a fully staffed, experienced software development team and elected to keep that team in-tact, particularly given current competitive employment market conditions with respect to talented software engineers. We integrated the development teams which has enhanced speed to market on new feature and functionality development activities. We expect a continued elevated level of expenditure and capitalized activity through the third quarter of 2023 associated with a customer-facing opportunity, followed by a return to spending levels consistent with the Company's results for the second quarter of 2022, which adequately reflect the pace for spend in these areas in future reporting periods.

General and Administrative Expenses

General and administrative expenses were effectively flat, increasing $71, or 1%. As compared to the six months ended June 30, 2022, the Company experienced decreases of (1) $456 in stock compensation expense as outstanding performance awards were fully expensed as of December 31, 2022, and (2) reductions in certain expenses following completion of integration activities/projects completed during 2022 following the Reflect Merger (including but not limited to consolidation of CMS tools, cloud hosting environments, IT tools) that materialized through the balance of 2022. These decreases were partially offset by increases of (1) $313 in increased personnel costs as the Company scaled up operations in response to an increase in customer acquisitions, (2) $133 in legal expenses associated with the Company's establishment of a Special Committee of the Board of Directors to consider and respond to an unsolicited proposal of a Company shareholder to acquire certain outstanding shares of common stock of the Company, as well as settlement of two open litigation matters during the period, and (3) other operating costs, each primarily associated with the consolidation of Reflect for six months in 2023, as compared to reporting consolidation of Reflect for only 134 days during the six months ended June 30, 2022 as a result of completion of the Reflect Merger on February 17, 2022.

Depreciation and amortization expenses

Depreciation and amortization expenses increased $401, or 34%, in the six months ended June 30, 2023 compared to the same period in 2022, driven primarily by incremental amortization expense generated from the addition of $17,160 in amortizing intangible assets on February 17, 2022, as a result of the Merger.

Interest expense

See Note 8 *Loans Payable* to the Condensed Consolidated Financial Statements for a discussion of the Company’s debt and related interest expense obligations.

Changes in fair value of warrant liability; Loss on warrant amendment

During the six month period ended June 30, 2022, the Company recorded a gain of $7,902 as the result of assessing the fair value of warrant liabilities associated with the Company’s issuance of warrants in its debt and equity offerings completed in February 2022 to finance the Merger. These warrants were initially assessed at fair value through Black Scholes calculation, with changes in fair value recognized at each period end.

Effective June 30, 2022, the Company amended the terms of certain warrants previously issued to its creditor and an investor, which removed the holder’s option to exercise such warrants on a cashless basis utilizing the VWAP of the Company’s common stock on the trading day immediately preceding the date of a notice of cashless exercise in certain circumstances, and removed the condition to exercising such warrants that the Company’s shareholders approve the exercise thereof (which had already been obtained). The amendments to the warrants extended the term of such warrants for an additional one year (collectively, the "Warrant Amendment"). The foregoing amendments to the warrants resulted in such warrants to be accounted for as equity instruments in the Company’s Condensed Consolidated Financial Statements.

Changes in fair value of equity guarantee

The Company has contingent consideration arrangements related to the Merger to potentially pay additional cash amounts in future periods based on the lack of achievement of certain share price performance goals of our common stock. Such contingent consideration arrangements are recorded at fair value and are classified as liabilities on the acquisition date and are remeasured at each reporting period in accordance with ASC 805-30-35-1 using a Monte Carlo simulation model. The change in the period represents the mark-to-market adjustment as of the balance sheet dates.

Loss on debt waiver consent

During the six months ended June 30, 2022, in connection with obtaining a waiver of certain restrictions in investment documents between an investor and the Company in order to consummate the financing contemplated by the Company's credit agreement with Slipstream, the Company paid consideration to such investor in the form of the Purchaser Warrant to purchase 466,667 shares of Company common stock in an at-the-market offering under Nasdaq rules. The number of shares of Company common stock subject to the Purchaser Warrant was equal to the waiver fee ($175) divided by $0.375 per share. The exercise price of the Purchaser Warrant is $4.23 per share, and the Purchaser Warrant became exercisable on August 17, 2022. The Purchaser Warrant expires six years from the date of issuance following execution of the Warrant Amendment. At the date of issuance, the Company performed a Black-Scholes valuation of the Purchaser Warrant, resulting in a fair value of $2.5968 per warrant. In recording the warrant liability, the Company recorded an expense in the Condensed Consolidated Statement of Operations associated with the issuance of the Purchaser Warrant of $1,212 for the six months ended June 30, 20222. No such transactions occurred in the current period.

Loss on extinguishment of debt

During the six months ended June 30, 2022, the Company refinanced its debt facilities with Slipstream. The Company assessed the combination of the pre-existing senior secured term loan and secured convertible loan in accordance with ASC 470 *Debt* and determined the transaction should be accounted for as an extinguishment, in part as the Consolidation Term Loan eliminated a substantive conversion feature. In aggregate the Company recorded a loss on extinguishment of $295, primarily associated with the write-off of pre-existing debt discounts. No such transactions occurred in the current period.

Summary Unaudited Quarterly Financial Information

The following represents unaudited financial information derived from the Company's quarterly financial statements:

	Quarters Ended				
Quarters ended	**June 30 2023**	**March 31 2023**	**December 31 2022**	**September 30 2022**	**June 30 2022**
GAAP net income (loss)	$ (1,425)	$ (1,000)	$ (1,334)	$ (554)	$ 1,262
Interest expense:					
Amortization of debt discount	358	356	364	363	360
Other interest, net	429	447	423	394	390
Depreciation/amortization:					
Amortization of intangible assets	754	754	743	848	431
Amortization of employee share-based awards	151	225	448	456	316
Depreciation of property & equipment	43	25	30	37	37
Income tax expense/(benefit)	45	43	33	(10)	53
EBITDA	$ 355	$ 850	$ 707	$ 1,534	$ 2,849
Adjustments					
Gain on fair value of warrant liability	-	-	-	-	(2,433)
Gain on settlement of obligations	-	-	-	(37)	(21)
Loss on warrant amendment	-	-	-	-	345
(Gain)/loss on fair value of equity guarantee	16	76	(705)	(442)	73
Disposal of Safe Space Solutions inventory	-	-	909	-	-
Deal and transaction expenses	-	-	54	110	37
Other (income)/expense	(123)	(12)	7	2	1
Stock-based compensation – Director grants	43	43	56	82	82
Adjusted EBITDA	$ 291	957	1,028	1,249	933

Liquidity and Capital Resources

See Note 1 *Nature of Organization and Operations* to the accompanying Condensed Consolidated Financial Statements for a discussion of liquidity and financial resources.

Operating Activities

The net cash provided by operating activities during the six months ended June 30, 2023 was $6,344 compared to net cash used in operating activities of $63 for the same period in 2022. Cash provided by operating activities in the six month period ending June 30, 2023, was driven by a reduction in accounts receivable, inventory and prepaid assets of $1,458, $1,119 and $1,035, respectively. In addition, deferred revenue and customer deposits increased $1,604 and $1,507 respectively.

Investing Activities

Net cash used in investing activities during the six months ended June 30, 2023 was $2,203 compared to $19,546 during the same period in 2022. The use of cash in the prior year was driven by completion of the Merger. We currently do not have any material commitments for capital expenditures as of June 30, 2023; however, we anticipate continued elevated capital expenditures in excess of historical trends through third quarter of 2023 as we complete the modernization and internationalization of our automotive platform in an effort to capture incremental SaaS-based revenue contracts.

Financing Activities

Net cash used in financing activities during the six months ended June 30, 2023 was $2,510 compared to net cash provided by financing activities of $19,566 for the same period in 2022. The change is the result of the Company's completion of equity and debt financing in the first quarter of 2022 to facilitate the Merger, which provided net cash of $10,109 and $9,868, respectively. Net cash used in financing activities during the six month period ended June 30, 2023, primarily represents repayments made on the Secured Promissory Note and Term Loan (2022) of $623 and $1,881, respectively.

Off-Balance Sheet Arrangements

During the three and six months ended June 30, 2023, we did not engage in any off-balance sheet arrangements set forth in Item 303(a)(4) of Regulation S-K.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

An evaluation was performed under the supervision and with the participation of our management, including our Chief Executive Officer (principal executive officer) and Chief Financial Officer (principal financial officer), of the effectiveness of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended ("Exchange Act"), as of the end of the period covered by this report. Based on that evaluation, our management, including our Chief Executive Officer and Chief Financial Officer, concluded that our disclosure controls and procedures were effective as of June 30, 2023, and designed to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act, is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting that occurred during the quarter ended June 30, 2023 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

None.

Item 1A. Risk Factors

As a smaller reporting company, we are not required to provide the information required by this Item; however, the discussion of our business and operations should be read together with the Risk Factors set forth in our Annual Report on Form 10-K filed with the SEC on March 30, 2023 and subsequent filings made with the SEC. Such risks and uncertainties have the potential to affect our business, financial condition, results of operations, cash flow, strategies or prospects in a material and adverse manner. In addition, below is an additional risk factor for which you should be aware:

If we are unable to extend the maturity or replace our existing financing agreements in the future, our plans to operate our business may be adversely affected and we could be required to curtail our activities significantly and/or cease operating.

As of August 4, 2023, our largest shareholder and investor, Slipstream Communications LLC (“Slipstream”) is the holder of 96% of our outstanding debt instruments, including three term loans, and has beneficial ownership of approximately 38% of our common stock (on an as-converted, fully diluted basis including conversion of outstanding warrants, and assuming no other convertible securities, options and warrants are converted or exercised by other parties). Historically, we have been able to obtain a continuing support letter from Slipstream, a factor that has previously alleviated the substantial doubt about our ability to continue as a going concern.

Pursuant to the Second Amended and Restated Credit and Security Agreement (the "Credit Agreement") made between the Company and Slipstream Communications ("Slipstream") the Company is required to make monthly repayments of principal on the Consolidation Term Loan beginning on September 1, 2023 and on the first day of each month thereafter until the Maturity Date on February 17, 2025. The monthly principal payment beginning on September 1, 2023 is approximately $399, or total principal repayments for the twelve months subsequent to the reporting date of these Condensed Consolidated Financial Statements of $4,389. As a result of the principal debt service payments required to be paid on account of the Consolidation Term Loan, the Company does not currently have cash on hand or committed available liquidity to repay all of its outstanding debt due within one year after the date that these financial statements are issued. These conditions and events raise substantial doubt about the Company's ability to continue as a going concern under the technical framework within ASU 205-40.

In response to these conditions, management plans to either refinance or recapitalize the debt should the Company not produce sufficient cash flows to continue to make repayments of principal. However, these plans have not been finalized and are not completely within the Company's control, and therefore cannot be deemed probable under ASU 205-40. We have been unable to obtain a continuing support letter from Slipstream beyond the period ending May 31, 2024. Obtaining a continuing support letter from Slipstream beyond one year of our report date was a factor that previously alleviated the substantial doubt about our ability to continue as a going concern. As a result, the Company has concluded that management's plans do not alleviate substantial doubt about the Company's ability to continue as a going concern.

If we are unable to extend the maturity or replace our existing financing agreements in the future, our plans to operate our business may be adversely affected and we could be required to curtail our activities significantly and/or cease operating.

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

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

Rule 10b5-1 Trading Plans

During the quarter ended June 30, 2023, none of the Company’s directors or executive officers adopted or terminated any contract, instruction or written plan for the purchase or sale of Company securities that was intended to satisfy the affirmative defense conditions of Rule 10b5-1(c) or any “non-Rule 10b5-1 trading arrangement."

Earnings Release

On August 4, 2023, the Company issued a press release announcing its financial condition and results of operations for the three and six months ended June 30, 2023. A copy of the press release is furnished as Exhibit 99.1 and is incorporated by reference into this Item 5 in lieu of separately furnishing such press release under Item 2.02 of Form 8-K. This disclosure, including Exhibit 99.1 hereto, shall not be deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), or otherwise subject to the liabilities of that section, nor shall it be deemed incorporated by reference into any of the Company’s filings under the Securities Act of 1933, as amended, or the Exchange Act, except as expressly set forth by specific reference in such filing.

Item 6. Exhibits

Exhibit No.	Description
31.1	Chief Executive Officer Certification pursuant to Exchange Act Rule 13a-14(a).
31.2	Chief Financial Officer Certification pursuant to Exchange Act Rule 13a-14(a).
32.1	Chief Executive Officer Certification pursuant to 18 U.S.C. Section 1350.
32.2	Chief Financial Officer Certification pursuant to 18 U.S.C. Section 1350.
99.1	Press Release dated August 4, 2023
101.INS	Inline XBRL Instance Document
101.SCH	Inline XBRL Taxonomy Extension Schema.
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase.
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase.
101.LAB	Inline XBRL Taxonomy Extension Label Linkbase.
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase.
104	Cover Page Interactive Data File (formatted as inline XBRL and contained in Exhibit 101).

* Filed herewith

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Creative Realities, Inc.

Date: August 4, 2023

By /s/ Richard Mills
Richard Mills
Chief Executive Officer

By /s/ Will Logan
Will Logan
Chief Financial Officer

EXHIBIT 31.1

CHIEF EXECUTIVE OFFICER CERTIFICATION
PURSUANT TO EXCHANGE ACT RULE 13a-14(a)

I, Richard Mills, certify that:

1. I have reviewed this quarterly report on Form 10-Q for the three and six months ended June 30, 2023, of Creative Realities, 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(s) 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(s) 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 functions):

   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.

Dated: August 4, 2023

By: /s/ Richard Mills
Richard Mills
Chief Executive Officer

EXHIBIT 31.2

CHIEF FINANCIAL OFFICER CERTIFICATION
PURSUANT TO EXCHANGE ACT RULE 13a-14(a)

I, Will Logan, certify that:

1. I have reviewed this quarterly report on Form 10-Q for the three and six months ended June 30, 2023, of Creative Realities, 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(s) 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(s) 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 functions):

   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.

Dated: August 4, 2023

By: /s/ Will Logan
Will Logan
Chief Financial Officer

EXHIBIT 32.1

CHIEF EXECUTIVE OFFICER CERTIFICATION
PURSUANT TO 18 U.S.C. SECTION 1350

In connection with the Quarterly Report of Creative Realities, Inc. (the “Company”) on Form 10-Q for the three and six months ended June 30, 2023, as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Richard Mills, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

Dated: August 4, 2023

By: /s/ Richard Mills
Richard Mills
Chief Executive Officer

EXHIBIT 32.2

CHIEF FINANCIAL OFFICER CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350

In connection with the Quarterly Report of Creative Realities, Inc. (the "Company") on Form 10-Q for the three and six months ended June 30, 2023, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Will Logan, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

Dated: August 4, 2023

By: /s/ Will Logan
Will Logan
Chief Financial Officer

Exhibit 99.1

FOR IMMEDIATE RELEASE

Creative Realities Reports 2nd Quarter 2023 Results

- ***Announces 2Q 2023 Revenue of $9.2 million***
- ***Announces Record Annual Recurring Revenue run-rate now ~$15.2 million***
- ***Announces 2Q Gross Profit of $4.3 million (46.7%)***
- ***Announces 1H 2023 Record Gross Profit of $9.4 million (49.0%)***
- ***Reiterates Projected Backlog Revenue exceeds $110 million***

LOUISVILLE, KY – **August 4, 2023** – Creative Realities, Inc. ("Creative Realities," "CRI," or the "Company") (NASDAQ: CREX, CREXW), a leading provider of digital signage and media solutions, announced its financial results for the three and six months ended June 30, 2023.

Rick Mills, Chief Executive Officer, commented "I am pleased to report second quarter 2023 revenue of $9.2 million, with $4.3 million in gross profit, which equates to a second quarter gross profit margin of 46.7% – a 406 basis-point improvement over the second quarter of last year – continuing the improved year-over-year trend in our margins that was evident in the first quarter. This brings the Company's gross profit to a record $9.4 million for the first six months of the year at a record gross profit margin for the first half of any year of 49.0%, the latter of which is an approximately 960 basis-point improvement over 2022."

Mr. Mills continued, "We continue to focus on critical path actions to grow both our customer base and, importantly, our annual SaaS subscription revenue contracts, or ARR, the latter of which now exceeds a $15.2 million run-rate. CRI continues to win in the marketplace, having now successfully converted approximately 69% of our RFP opportunities over the past 12 months. Our new customer acquisition momentum, combined with continued growth in our ARR, has strengthened our expectations for the near and long-term prospects of this business. We are actively competing in a significant number of new customer engagements for which an award of business is currently pending.

"The current quarter has met our expectations. We have had a shift in the revenue ramp associated with the Bowling deployment due to unexpected supply chain delays for certain route/switch equipment, which was being procured and delivered by a third-party, that have since been alleviated in full. We expect that these delays could ultimately impact our full year revenue results, however we believe the revenues from this project have not vanished but have instead experienced a shift in timing. The associated revenues will be realized, and we continue to project a step-function change in run-rate revenue on a go-forward basis beginning in the third quarter, with an increasing effect in subsequent quarters thereafter for the foreseeable future. The Company expects to generate between $60 million and $80 million in revenue for the next twelve-month period beginning in third quarter 2023, but expects that generating an $80 million run-rate may take an additional quarter or two as we catch up on the third-party supply chain delays that were recently resolved," Mr. Mills added.

"Importantly, we also project ongoing improvements in profitability associated with both scale and new deployments, the latter of which drive SaaS and other downstream recurring and services revenue at significantly more favorable margins. We are demonstrating the improvements in profitability already and, as we realize our backlog of $110 million, EBITDA and free cash flow will follow. These effects are running in parallel with accelerated debt service as we simultaneously reduce debt and grow profit into an optimal leverage ratio."

Mr. Mills encouraged investors to attend the Company's earnings release call, "In addition to providing additional context to our second quarter earnings, we will convey several important announcements and updates relating to new customer acquisitions and the scaling of our CMS platforms."

Revenue backlog is primarily related to projected network deployments and project work, which upon execution will result in additional ARR. The Company's backlog calculation is comprised of the full rollout of projects that have been communicated to us by our current customers under contract, and includes all revenues to be received by the Company by deploying all of our products and services necessary to service such stated projects, including projected revenues that are not currently subject to binding purchase orders or firm commitments.

2Q 2023 Financial Overview

All references to current year and prior year represent references to the three months ended June 30, 2023 and 2022, respectively.

Key Highlights:

- Revenue in-line with previously communicated expectations for second quarter 2023, between $9 - $10 million.
- Expansion of gross margin percentage to 46.7% in the current year from 42.7% in the prior year.
- Expansion of Annualized Recurring Revenue to forward run-rate of ~$15.2 million.

Revenue, gross profit, and gross margin:

- Revenue in the current year were $9,196, representing a decrease of $1,727, or 16%, as compared to prior year. Hardware revenues were $3,437 in the current year, a decrease of $2,230, or 39%, as compared to the prior year. Hardware revenues generated in the prior year were driven by two customers which refreshed their digital hardware throughout their entire geographic footprint. These refresh activities are cyclical in nature and no current customer executed a similar large-scale refresh during the current year. Those refresh activities represented $2,418 in incremental hardware revenue during the prior year.

- Services and other revenues in the current year were $5,759, an increase of $503, or 10%, as compared to prior year driven primarily by increases in installation services revenue and growth in managed services revenue. Managed services revenue, which includes both software-as-a-service ("SaaS"), help desk technical subscription services, and other services revenues. While those managed services revenues were effectively flat at $3,835, the prior year figure included the last remaining software license contracts associated with Safe Space Solutions, which were discontinued earlier in 2023.

- Gross profit decreased by $364, or 8% in the current year as compared to prior year driven by an increase in installation services revenue.

- Gross profit margin increased to 47% during the current year, from 43% in the prior year driven by (1) favorable revenue mix during the three months ended June 30, 2023 as managed services, which includes higher margin SaaS and other services revenues, increased to 42% of total revenue in the current year as compared to 35% of total revenues in the prior year, and (2) margin expansion in hardware, partially offset by reduced revenue in the current year.

Operating expenses:

- Sales and marketing expenses generally include the salaries, taxes, and benefits of our sales and marketing personnel, as well as trade show activities, travel, and other related sales and marketing costs. Sales and marketing expenses increased by $82, or 7%, in the current year as compared to the prior year driven primarily by the Company's enhanced investments into sales and marketing activities. Following the Company's merger with Reflect Systems, Inc. (the "Merger"), the Company adopted certain tools, technology, and processes – particularly with respect to lead generation and brand marketing – that were historically undercapitalized by the Company and have since accelerated new customer acquisition. Through completion of the Merger, the Company also acquired a media sales business unit that serves to monetize customer networks via the direct sale of advertising to be displayed on digital advertising networks owned by those customers. This business utilizes internal and third-party sales agents - the salaries and commissions of which are included within Sales and Marketing Expense within the Condensed Consolidated Statement of Operations. We expect the sales and marketing expenses of the Company for the three months ended June 30, 2023 to adequately reflect normal spend in these areas in future reporting periods.

- Research and development expenses generally include personnel and development tools costs associated with the continued development of the Company's content management systems and other related application development. The Company capitalizes certain of these expenses and amortizes those costs through the Condensed Consolidated Statement of Operations on a straight-line basis over the economic useful life of the software feature or functionality. Research and development expenses decreased by $41, or 10%, in the current year as compared to prior year driven primarily by an elevated level of capitalized activity during the current quarter associated with a customer-facing opportunity.

- General and administrative expenses were effectively flat, increasing $33, or 1%, in the current year as compared to prior year driven by reductions (1) of $203 in stock compensation expense as outstanding performance awards were fully expensed as of December 31, 2022, and (2) in certain expenses following completion of integration activities/projects completed during 2022 following the Reflect Merger (including but not limited to consolidation of CMS tools, cloud hosting environments, IT tools) that materialized through the balance of 2022. These decreases were offset by increases of $278 in personnel costs in the current year as a result of higher headcount following the Merger and scaled up operations in response to an increase in customer acquisitions.

Operating loss, net loss, and EBITDA:

- Operating loss was $0.7 million for the current year ended as compared to breakeven in the prior year, inclusive of approximately $0.8 and $0.5 million in non-cash amortization of fixed and intangible assets in the current and prior year, respectively.

- Net loss was $1.4 million for the current period as compared to net income of $1.3 million for the same period in 2022, which was driven in the prior year by a non-cash gain of $2.5 million on mark-to-market liabilities no longer included in the Company's condensed consolidated balance sheet.

- Adjusted EBITDA was approximately $0.3 million in the current period as compared to $0.9 million in the prior period, with Adjusted EBITDA margin percentage of 3.2% in the current period as compared to 8.3% in the prior period. See the appendix for a description of these non-GAAP financial measures and reconciliation to our net income.

A reconciliation of the GAAP-basis net income/(loss) to Adjusted EBITDA is provided in a table at the end of this press release.

Other notes:

- **Cash**: The Company's cash on hand as of June 30, 2023 increased to $3.3 million from $1.6 million as of December 31, 2022 as a result of collections on accounts receivable, annual billings associated with our SaaS-based contracts, and increases in customer deposits on future deployments, partially offset by investments in software development projects and repayment of debt.

- **Debt**: Through June 30, 2023, the Company has repaid in excess of $2.5 million in principal on debt, reducing the Company's leverage ratio. The Company anticipates that starting on September 1, 2023, it will begin making principal debt payments of approximately $399. In response to these conditions, management plans to either refinance or recapitalize its debt should the Company not produce sufficient cash flows to continue to make repayments of principal.

Conference Call Details

The Company will host a conference call to review the results of the Company's second quarter 2023, and provide additional commentary about the Company's recent performance, on Friday, August 4, 2023 at 9:00 am Eastern Time.

Prior to the call, participants should register at http://bit.ly/CRIearnings2023Q2. Once registered, participants can use the dial-in information provided in the registration email to listen to the Company's prepared remarks and participate in the live question and answer session. An archived edition of the conference call will also be posted on our website at www.cri.com later that same day and will remain available to interested parties via the same link for one year.

About Creative Realities, Inc.

Creative Realities helps clients use place-based digital media to achieve business objectives such as increased revenue, enhanced customer experiences, and improved productivity. The Company designs, develops and deploys digital signage experiences for enterprise-level networks, and is actively providing recurring SaaS and support services across diverse vertical markets, including but not limited to retail, automotive, digital-out-of-home (DOOH) advertising networks, convenience stores, foodservice/QSR, gaming, theater, and stadium venues.

With its recent acquisition of Reflect Systems, Inc. (“Reflect”), a leading provider of digital signage software platforms, the Company is poised to extend its product and service offering and accelerate growth in SaaS revenue. While Reflect provided a broad range of digital signage solutions, Reflect’s flagship products are the market-leading ReflectView digital signage platform and Reflect AdLogic ad management platform. ReflectView is the industry’s most comprehensive, scalable, enterprise-grade digital signage platform, powering enterprise customer networks. Meanwhile, Reflect AdLogic has become the benchmark for digital signage powered ad networks, delivering nearly 50 million ads daily. The acquisition of Reflect also brought to the Company a media sales division with the expertise and relationships to help any digital signage venue owner develop and execute a monetization plan for their network.

Use of Non-GAAP Measures

Creative Realities, Inc. prepares its consolidated financial statements in accordance with United States generally accepted accounting principles (“GAAP”). In addition to disclosing financial results prepared in accordance with GAAP, the Company discloses information regarding “EBITDA” and “Adjusted EBITDA.” CRI defines “EBITDA” as earnings before interest, income taxes, depreciation and amortization of intangibles. CRI defines “Adjusted EBITDA” as EBITDA excluding stock-based compensation, fair value adjustments and both cash and non-cash non-recurring gains and charges. EBITDA and Adjusted EBITDA are not measures of performance defined in accordance with GAAP. However, EBITDA and Adjusted EBITDA are used internally in planning and evaluating the Company’s operating performance. Accordingly, management believes that disclosure of these metrics offers investors, bankers and other stakeholders an additional view of the Company’s operations that, when coupled with the GAAP results, provides a more complete understanding of the Company’s financial results.

EBITDA and Adjusted EBITDA should not be considered as an alternative to net income/(loss) or to net cash used in operating activities as measures of operating results or liquidity. Our calculation of EBITDA and Adjusted EBITDA may not be comparable to similarly titled measures used by other companies, and the measures exclude financial information that some may consider important in evaluating the Company’s performance. A reconciliation of GAAP net income/(loss) to EBITDA and Adjusted EBITDA is included in the accompanying financial schedules.

For further information, please refer to Creative Realities, Inc.’s filings available online at www.sec.gov, including its Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 30, 2023.

Cautionary Note on Forward-Looking Statements

This press release contains "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, Section 21E of the Securities Exchange Act of 1934, as amended, and the Private Securities Litigation Reform Act of 1995, and includes, among other things, discussions of our business strategies, product releases, future operations and capital resources. Words such as "estimates," "projected," "expects," "anticipates," "forecasts," "plans," "intends," "believes," "seeks," "may," "will," "should," "future," "propose" and variations of these words or similar expressions (or the negative versions of such words or expressions) are intended to identify forward-looking statements. Forward-looking statements are not guarantees of future performance, conditions or results. They are based on the opinions, estimates and beliefs of management as of the date such statements are made, and they are subject to known and unknown risks, uncertainties, assumptions and other factors, many of which are outside of our control, that may cause the actual results, level of activity, performance or achievements to be materially different from those expressed or implied by such forward-looking statements. Some of these risks are discussed in the “Risk Factors” section contained in Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2022 and in our Quarterly Report on Form 10-Q for the period ended June 30, 2023, and the Company’s subsequent filings with the U.S. Securities and Exchange Commission. Important factors, among others, that may affect actual results or outcomes include: our ability to effectively integrate Reflect’s business operations, our strategy for customer retention, growth, product development, market position, financial results and reserves, our ability to execute on our business plan, our ability to retain key personnel, our ability to remain listed on the Nasdaq Capital Market, our ability to realize the revenues included in our future guidance and backlog reports, our ability to satisfy our upcoming debt obligations and other liabilities, the ability of the Company to continue as a going concern, potential litigation, supply chain shortages, and general economic and market conditions impacting demand for our products and services, including those as a result of the COVID-19 pandemic. Readers should not place undue reliance upon any forward-looking statements. We assume no obligation to update or revise the forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law.

Contact

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CREATIVE REALITIES, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except per share amounts)

	June 30, 2023	December 31, 2022
	(unaudited)	
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 3,264	$ 1,633
Accounts receivable, net	6,496	8,263
Work-in-process and inventories, net	1,148	2,267
Prepaid expenses and other current assets	784	1,819
Total current assets	$ 11,692	$ 13,982
Property and equipment, net	453	201
Operating lease right-of-use assets	1,356	1,584
Intangibles, net	23,936	23,752
Goodwill	26,453	26,453
Other assets	44	43
TOTAL ASSETS	$ 63,934	$ 66,015
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable	$ 2,892	$ 3,757
Accrued expenses	3,217	3,828
Deferred revenues	2,827	1,223
Customer deposits	3,985	2,478
Current maturities of operating leases	645	711
Short-term portion of Secured Promissory Note	833	1,248
Short-term portion of related party Consolidation Term Loan, net of $747 and $745 discount, respectively	3,245	1,251
Short-term related party Term Loan (2022)	119	2,000
Total current liabilities	17,763	16,496
Long-term Secured Promissory Note	-	208
Long-term related party Acquisition Term Loan, net of $1,139 and $1,484 discount, respectively	8,861	8,516
Long-term related party Consolidation Term Loan, net of $469 and $840 discount, respectively	2,724	4,349
Long-term obligations under operating leases	711	873
Contingent acquisition consideration, at fair value	9,881	9,789
Other liabilities	136	205
TOTAL LIABILITIES	40,076	40,436
SHAREHOLDERS' EQUITY		
Common stock, $0.01 par value, 66,666 shares authorized; 7,409 and 7,266 shares issued and outstanding, respectively	74	72
Additional paid-in capital	76,618	75,916
Accumulated deficit	(52,834)	(50,409)
Total shareholders' equity	23,858	25,579
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 63,934	$ 66,015

CREATIVE REALITIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share amounts)
(Unaudited)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2023	2022	2023	2022
Sales				
Hardware	$ 3,437	$ 5,667	$ 7,759	$ 12,126
Services and other	5,759	5,256	11,381	9,554
Total sales	9,196	10,923	19,140	21,680
Cost of sales				
Hardware	2,724	4,610	5,930	9,992
Services and other	2,174	1,651	3,823	3,134
Total cost of sales	4,898	6,261	9,753	13,126
Gross profit	4,298	4,662	9,387	8,554
Operating expenses:				
Sales and marketing expenses	1,229	1,147	2,365	1,854
Research and development expenses	377	418	743	659
General and administrative expenses	2,595	2,562	5,493	5,422
Depreciation and amortization expense	797	468	1,576	1,175
Deal and transaction expenses	-	37	-	428
Total operating expenses	4,998	4,632	10,177	9,538
Operating income/(loss)	(700)	30	(790)	(984)
Other income (expenses):				
Interest expense, including amortization of debt discount	(787)	(750)	(1,590)	(1,199)
Change in fair value of warrant liability	-	2,433	-	7,902
Change in fair value of equity guarantee	(16)	(73)	(92)	(73)
Loss on debt waiver consent	-	-	-	(1,212)
Loss on warrant amendment	-	(345)	-	(345)
Gain/(loss) on settlement of obligations	-	21	-	(274)
Other income (expense)	123	(1)	135	5
Total other income (expense)	(680)	1,285	(1,547)	4,804
Net (loss) income before income taxes	(1,380)	1,315	(2,337)	3,820
Provision for income taxes	(45)	(53)	(88)	(56)
Net (loss) income	$ (1,425)	$ 1,262	$ (2,425)	$ 3,764
Basic (loss) earnings per common share	$ (0.19)	$ 0.17	$ (0.33)	$ 0.62
Diluted (loss) earnings per common share	$ (0.19)	$ 0.17	$ (0.33)	$ 0.62
Weighted average shares outstanding - basic	7,406	7,234	7,379	6,060
Weighted average shares outstanding - diluted	7,406	7,234	7,379	6,060

CREATIVE REALITIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Six Months Ended June 30,	
	2023	**2022**
Operating Activities:		
Net (loss) income	$ (2,425)	$ 3,764
Adjustments to reconcile net (loss) income to net cash provided by operating activities		
Depreciation and amortization	1,576	1,175
Amortization of debt discount	714	541
Amortization of stock-based compensation	493	1,014
Loss on debt waiver consent	-	1,212
Loss on warrant amendment	-	345
Change on change in fair value of warrants	-	274
Bad debt expense	309	106
Gain on change in fair value of warrants	-	(7,902)
Loss on change in fair value of contingent consideration	92	73
Deferred income taxes	46	-
Changes to operating assets and liabilities:		
Accounts receivable	1,458	(4,035)
Work-in-process and inventories	1,119	(562)
Prepaid expenses and other current assets	1,035	(811)
Accounts payable	(585)	2,487
Accrued expenses	(559)	229
Deferred revenues	1,604	1,178
Customer deposits	1,507	809
Other	(40)	40
Net cash provided by (used in) operating activities	6,344	(63)
Investing activities		
Acquisition of business, net of cash acquired	-	(17,186)
Purchases of property and equipment	(219)	(32)
Capitalization of labor for software development	(1,984)	(2,328)
Net cash used in investing activities	(2,203)	(19,546)
Financing activities		
Principal payments on finance leases	(6)	-
Proceeds from sale of common stock in PIPE, net of offering expenses	-	1,814
Proceeds from sale & exercise of pre-funded warrants in PIPE, net of offering expenses	-	8,295
Proceeds from Acquisition Loan, net of offering expenses	-	9,868
Repayment of Term Loan (2022)	(1,881)	-
Repayment of Secured Promissory Note	(623)	(411)
Net cash (used in) provided by financing activities	(2,510)	19,566
Increase (decrease) in Cash and Cash Equivalents	1,631	(43)
Cash and Cash Equivalents, beginning of period	1,633	2,883
Cash and Cash Equivalents, end of period	$ 3,264	$ 2,840

RECONCILIATION OF GAAP NET LOSS TO ADJUSTED EBITDA
(in thousands, unaudited)

Creative Realities, Inc. prepares its consolidated financial statements in accordance with United States generally accepted accounting principles ("GAAP"). In addition to disclosing financial results prepared in accordance with GAAP, the Company discloses information regarding "EBITDA" and "Adjusted EBITDA." CRI defines "EBITDA" as earnings before interest, income taxes, depreciation and amortization of intangibles. CRI defines "Adjusted EBITDA" as EBITDA excluding stock-based compensation, fair value adjustments and both cash and non-cash non-recurring gains and charges.

EBITDA and Adjusted EBITDA are non-GAAP financial measures and should not be considered as a substitute for net income (loss), operating income (loss) or any other performance measure derived in accordance with United States generally accepted accounting principles ("GAAP") or as an alternative to net cash provided by operating activities as a measure of CRI's profitability or liquidity. CRI's management believes EBITDA and Adjusted EBITDA are useful financial metrics because they allow external users of CRI's financial statements, such as industry analysts, investors, lenders and rating agencies, to more effectively evaluate CRI's operating performance, compare the results of its operations from period to period and against CRI's peers without regard to CRI's financing methods, hedging positions or capital structure and because it highlights trends in CRI's business that may not otherwise be apparent when relying solely on GAAP measures. CRI also presents EBITDA and Adjusted EBITDA because it believes EBITDA and Adjusted EBITDA are important supplemental measures of its performance that are frequently used by others in evaluating companies in its industry. Because EBITDA and Adjusted EBITDA exclude some, but not all, items that affect net income (loss) and may vary among companies, the EBITDA and Adjusted EBITDA CRI presents may not be comparable to similarly titled measures of other companies.

The following table presents a reconciliation of EBITDA and Adjusted EBITDA from net loss, CRI's most directly comparable financial measure calculated and presented in accordance with GAAP.

	Quarters Ended				
Quarters ended	**June 30 2023**	**March 31 2023**	**December 31 2022**	**September 30 2022**	**June 30 2022**
GAAP net income (loss)	$ (1,425)	$ (1,000)	$ (1,334)	$ (554)	$ 1,262
Interest expense:					
Amortization of debt discount	358	356	364	363	360
Other interest, net	429	447	423	394	390
Depreciation/amortization:					
Amortization of intangible assets	754	754	743	848	431
Amortization of employee share-based awards	151	225	448	456	316
Depreciation of property & equipment	43	25	30	37	37
Income tax expense/(benefit)	45	43	33	(10)	53
EBITDA	$ 355	$ 850	$ 707	$ 1,534	$ 2,849
Adjustments					
Gain on fair value of warrant liability	-	-	-	-	(2,433)
Gain on settlement of obligations	-	-	-	(37)	(21)
Loss on warrant amendment	-	-	-	-	345
(Gain)/loss on fair value of equity guarantee	16	76	(705)	(442)	73
Disposal of Safe Space Solutions inventory	-	-	909	-	-
Deal and transaction expenses	-	-	54	110	37
Other (income)/expense	(123)	(12)	7	2	1
Stock-based compensation – Director grants	43	43	56	82	82
Adjusted EBITDA	$ 291	957	1,028	1,249	933