

# CYNERGISTEK, INC

## FORM 10-Q (Quarterly Report)

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

Washington, DC 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 September 30, 2021

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: 000-27507

**CYNERGISTEK, INC.**

(Exact Name of Registrant as Specified in Its Charter)

**Delaware**

(State or Other Jurisdiction of  
Incorporation or Organization)

**37-1867101**

(IRS Employer  
Identification Number)

**11940 Jollyville Road, Suite 300-N**

**Austin, Texas**

(Address of Principal Executive Offices)

**78759**

(Zip Code)

**(949) 614-0700**

(Registrant's telephone number, including area code)

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, \$.001 par value per share	CTEK	NYSE American

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 .

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

Emerging growth company

Indicate by check mark whether the registrant is a shell company (as defined by Section 12b-2 of the Exchange Act).

Yes  No .

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 standard provided pursuant to Section 13(a) of the Exchange Act.

The number of shares of the issuer’s common stock, \$0.001 par value, outstanding as of November 11, 2021, was 13,186,048.

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FORM 10-Q  
TABLE OF CONTENTS

	Page
<u>PART I – FINANCIAL INFORMATION</u>	4
<u>ITEM 1. FINANCIAL STATEMENTS.</u>	4
<u>ITEM 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.</u>	21
<u>ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.</u>	31
<u>ITEM 4. CONTROLS AND PROCEDURES.</u>	31
<u>PART II - OTHER INFORMATION</u>	31
<u>ITEM 1A. RISK FACTORS.</u>	31
<u>ITEM 5. OTHER INFORMATION.</u>	32
<u>ITEM 6. EXHIBITS.</u>	33

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**PART I – FINANCIAL INFORMATION**  
**ITEM 1. FINANCIAL STATEMENTS.**

**CYNERGISTEK, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**

	September 30, 2021 (unaudited)	December 31, 2020
<b>ASSETS</b>		
<b>Current assets:</b>		
Cash and cash equivalents	\$ 5,088,141	\$ 5,613,654
Accounts receivable, net of allowance for doubtful accounts	1,773,227	2,063,136
Unbilled services	648,968	566,713
Prepaid and other current assets	1,392,791	2,032,420
Income taxes receivable	1,845,502	1,680,866
<b>Total current assets</b>	<b>10,748,629</b>	<b>11,956,789</b>
<b>Property and equipment, net</b>	<b>283,966</b>	<b>541,525</b>
<b>Deposits</b>	<b>34,310</b>	<b>64,586</b>
<b>Deferred income taxes</b>	<b>6,003,866</b>	<b>4,959,125</b>
<b>Intangible assets, net</b>	<b>5,042,021</b>	<b>6,063,617</b>
<b>Goodwill</b>	<b>8,394,483</b>	<b>8,394,483</b>
<b>Total assets</b>	<b>\$ 30,507,275</b>	<b>\$ 31,980,125</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>Current liabilities:</b>		
Accounts payable and accrued expenses	\$ 766,006	\$ 1,326,919
Accrued compensation and benefits	1,153,093	814,830
Deferred revenue	1,671,922	1,265,864
Current portion of earnout liability	200,000	-
Current portion of promissory note to related party	281,250	562,500
Current portion of operating lease liability	84,009	252,398
<b>Total current liabilities</b>	<b>4,156,280</b>	<b>4,222,511</b>
<b>Long-term liabilities:</b>		
Earnout liability, less current portion	50,000	1,300,000
Promissory note to related party, less current portion	-	140,625
Paycheck Protection Program loan	-	2,825,500
Operating lease liability, less current portion	-	40,031
<b>Total long-term liabilities</b>	<b>50,000</b>	<b>4,306,156</b>
<b>Commitments and contingencies</b>		
<b>Stockholders' equity:</b>		
Common stock, par value at \$0.001, 33,333,333 shares authorized, 12,882,997 shares issued and outstanding at September 30, 2021, and 12,024,967 shares issued and outstanding at December 31, 2020	12,883	12,024
Additional paid-in capital	41,154,149	38,564,520
Accumulated deficit	(14,866,037)	(15,125,086)
<b>Total stockholders' equity</b>	<b>26,300,995</b>	<b>23,451,458</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$ 30,507,275</b>	<b>\$ 31,980,125</b>

The accompanying notes are an integral part of these condensed consolidated financial statements.

**CYNERGISTEK, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
**(UNAUDITED)**

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2021	2020	2021	2020
<b>Net revenues</b>	\$ 3,825,679	\$ 4,502,909	\$ 11,874,343	\$ 14,176,307
<b>Cost of revenues</b>	1,972,545	2,909,788	6,146,436	9,679,816
Gross profit	1,853,134	1,593,121	5,727,907	4,496,491
<b>Operating expenses:</b>				
Sales and marketing	1,092,906	1,325,965	3,547,525	4,490,797
General and administrative	2,646,064	1,480,597	5,793,316	5,381,929
Change in valuation of contingent earn-out	250,000	-	(1,050,000)	-
Depreciation	48,383	48,296	144,265	141,668
Amortization of acquisition-related intangibles	340,539	416,191	1,021,596	1,248,574
Finance cost for equity commitment	-	-	-	390,000
Total operating expenses	4,377,892	3,271,049	9,456,702	11,652,968
<b>Loss from operations</b>	(2,524,758)	(1,677,928)	(3,728,795)	(7,156,477)
<b>Other income (expense):</b>				
Gain on forgiveness of PPP loan and other income and expense	2,843,254	-	2,843,266	-
Interest income	-	1,867	-	9,545
Interest expense	(9,982)	(26,046)	(47,322)	(77,654)
Total other income (expense)	2,833,272	(24,179)	2,795,944	(68,109)
<b>Income (loss) before provision for income taxes</b>	308,514	(1,702,107)	(932,851)	(7,224,586)
<b>Income tax benefit</b>	911,900	425,708	1,191,900	1,642,902
<b>Net income (loss)</b>	1,220,414	(1,276,399)	259,049	(5,581,684)
<b>Deemed dividends from warrant anti-dilution provisions</b>	(8,343)	-	(14,177)	-
<b>Net income (loss) attributable to common shareholders</b>	\$ 1,212,071	\$ (1,276,399)	\$ 244,872	\$ (5,581,684)
<b>Net income (loss) per share:</b>				
Basic	\$ 0.10	\$ (0.12)	\$ 0.02	\$ (0.53)
Diluted	\$ 0.10	\$ (0.12)	\$ 0.02	\$ (0.53)
<b>Number of weighted average shares outstanding:</b>				
Basic	12,141,088	10,597,024	12,101,466	10,486,334
Diluted	12,610,443	10,597,024	12,573,978	10,486,334

The accompanying notes are an integral part of these condensed consolidated financial statements.

**CYNERGISTEK, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY**  
**THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2021**  
**(UNAUDITED)**

	Common Stock		Additional	Accumulated	Total
	Shares	Amount	Paid-in Capital	Deficit	Stockholders' Equity
Balance at December 31, 2020	12,024,967	\$ 12,024	\$ 38,564,520	\$ (15,125,086)	\$ 23,451,458
Stock compensation expense	-	-	228,437	-	228,437
Restricted stock units exercised	95,731	96	(96)	-	-
Deemed dividend	-	-	-	-	-
Net loss	-	-	-	(914,477)	(914,477)
Balance at March 31, 2021	12,120,698	12,120	38,792,861	(16,039,563)	22,765,418
Stock compensation expense	-	-	338,272	-	338,272
Net loss	-	-	-	(46,888)	(46,888)
Balance at June 30, 2021	12,120,698	12,120	39,131,133	(16,086,451)	23,056,802
Net common stock sold	762,299	763	1,351,064	-	1,351,827
Stock compensation expense	-	-	671,952	-	671,952
Deemed dividend	-	-	-	-	-
Net income	-	-	-	1,220,414	1,220,414
Balance at September 30, 2021	<u>12,882,997</u>	<u>\$ 12,883</u>	<u>\$ 41,154,149</u>	<u>\$ (14,866,037)</u>	<u>\$ 26,300,995</u>

The accompanying notes are an integral part of these condensed consolidated financial statements.

**CYNERGISTEK, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY**  
**THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2020**  
**(UNAUDITED)**

	Common Stock		Additional	Accumulated	Total
	Shares	Amount	Paid-in Capital	Earnings (Deficit)	Stockholders' Equity
Balance at December 31, 2019	10,359,164	\$ 10,359	\$ 34,821,863	\$ 3,343,402	\$ 38,175,624
Stock compensation expense	-	-	411,007	-	411,007
Shares issued from restricted stock units	20,000	20	(20)	-	-
Net loss	-	-	-	(1,850,623)	(1,850,623)
Balance at March 31, 2020	10,379,164	10,379	35,232,850	1,492,779	36,736,008
Stock compensation expense	-	-	606,265	-	606,265
Finance cost for equity commitment	-	-	390,000	-	390,000
Shares issued from restricted stock units	217,860	217	(217)	-	-
Net loss	-	-	-	(2,454,661)	(2,454,661)
Balance at June 30, 2020	10,597,024	10,596	36,228,898	(961,882)	35,277,612
Stock compensation expense	-	-	378,077	-	378,077
Net loss	-	-	-	(1,276,399)	(1,276,399)
Balance at September 30, 2020	<u>10,597,024</u>	<u>\$ 10,596</u>	<u>\$ 36,606,975</u>	<u>\$ (2,238,281)</u>	<u>\$ 34,379,290</u>

The accompanying notes are an integral part of these condensed consolidated financial statements.

**CYNERGISTEK, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(UNAUDITED)**

	<b>Nine Months Ended September 30,</b>	
	<b>2021</b>	<b>2020</b>
<b>Cash flows from operating activities:</b>		
Net income (loss)	\$ 259,049	\$ (5,581,684)
<b>Adjustments to reconcile net income (loss) to net cash used for operating activities:</b>		
Depreciation	144,265	141,668
Amortization of intangible assets	1,021,596	1,248,574
Change in net deferred tax assets	(1,044,741)	(113,458)
Bad debt expense	-	56,489
Stock compensation for equity awards granted to employees and directors	1,238,661	1,395,349
Change in valuation of contingent earn-out	(1,050,000)	-
Finance cost for equity commitment	-	390,000
Paycheck Protection Program loan forgiveness	(2,825,500)	-
Other	(17,912)	(36,445)
<b>Changes in operating assets and liabilities:</b>		
Accounts receivable	289,909	1,255,803
Unbilled services	(82,255)	(157,787)
Prepaid and other current assets	639,629	(171,859)
Income taxes receivable	(164,636)	(1,478,933)
Deposits	30,276	7,900
Accounts payable and accrued expenses	(560,913)	163,138
Accrued compensation and benefits	338,263	(522,358)
Deferred revenue	406,058	117,418
Income taxes payable	-	(31,976)
<b>Net cash used for operating activities</b>	<b>(1,378,251)</b>	<b>(3,318,161)</b>
<b>Cash flows from investing activities:</b>		
Purchases of property and equipment	(77,214)	(127,028)
<b>Net cash used for investing activities</b>	<b>(77,214)</b>	<b>(127,028)</b>
<b>Cash flows from financing activities:</b>		
Proceeds from Paycheck Protection Program loan	-	2,825,500
Payments on promissory note to related party	(421,875)	(421,875)
Net proceeds from sale of common stock	1,351,827	-
<b>Net cash provided by financing activities</b>	<b>929,952</b>	<b>2,403,625</b>
<b>Net change in cash and cash equivalents</b>	<b>(525,513)</b>	<b>(1,041,564)</b>
<b>Cash and cash equivalents, beginning of period</b>	<b>5,613,654</b>	<b>5,328,726</b>
<b>Cash and cash equivalents, end of period</b>	<b>\$ 5,088,141</b>	<b>\$ 4,287,162</b>

The accompanying notes are an integral part of these condensed consolidated financial statements.

**CYNERGISTEK, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)**  
**(UNAUDITED)**

	Nine Months Ended September 30,	
	2021	2020
<b>Supplemental disclosure of cash flow information:</b>		
Interest paid	\$ 30,791	\$ 67,777
Income taxes paid (refunded)	\$ 17,228	\$ (18,535)
<b>Non-cash investing and financing activities:</b>		
Capitalized right-to-use asset resulting from an extension of an operating lease commitment	\$ 29,480	\$ 185,454
Capitalized operating lease liability resulting from an extension of an operating lease commitment	\$ 28,992	\$ 185,454

The accompanying notes are an integral part of these condensed consolidated financial statements.

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**NINE MONTHS ENDED SEPTEMBER 30, 2021 AND 2020**  
**(UNAUDITED)**

**1. BASIS OF PRESENTATION**

The accompanying unaudited condensed consolidated financial statements of CynergisTek, Inc. and its subsidiaries (the “Company,” “we,” “us,” or “CynergisTek”) have been prepared in accordance with generally accepted accounting principles of the United States of America (“GAAP”) for interim financial statements pursuant to the rules and regulations of the Securities and Exchange Commission. Accordingly, these financial statements do not include all of the information and notes required by GAAP for complete financial statements. These unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2020, as filed with the Securities and Exchange Commission (“SEC”) on March 25, 2021, as amended by Amendment No. 1 on Form 10-K/A filed with the SEC on April 29, 2021.

The unaudited condensed consolidated financial statements included herein reflect all adjustments (which include only normal, recurring adjustments) that are, in the opinion of management, necessary to state fairly our financial position and results of operations as of and for the periods presented. The results for such periods are not necessarily indicative of the results to be expected for the full year.

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, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. As a result, actual results could differ from those estimates.

The accompanying unaudited condensed consolidated financial statements include the accounts of CynergisTek and its wholly owned subsidiaries. All intercompany balances and transactions have been eliminated.

Based on our integration strategies, and an analysis of how our Chief Operating Decision Makers review, manage and are compensated, we have determined that the Company operates as one segment. For the periods presented, all revenues were derived from domestic operations.

We have performed an evaluation of subsequent events through the date of filing these unaudited condensed consolidated financial statements with the SEC.

**Liquidity and Capital Resources**

As of September 30, 2021, our cash balance was \$5.1 million, current assets minus current liabilities was positive \$6.6 million. The level of additional cash needed to fund operations and our ability to conduct business for the next twelve months will be influenced primarily by the following factors:

- our ability to manage our operating expenses and maintain gross margins while attracting, recruiting and retaining cybersecurity privacy professionals;
- demand for our services from healthcare providers; the near-term impact of the COVID-19 pandemic on our customers’ allocation of time and resources to security and privacy, and their ability to pay for existing services as well as enter into new contractual arrangements during a period of crisis;
- general economic conditions and changes in healthcare reimbursement and regulatory environment, including effects of the COVID-19 pandemic; and
- our ability to collect accounts receivable from health care customers whose operations and cash flow have been significantly impacted by the COVID-19 pandemic.

[Table of Contents](#)

We have historically funded our operating costs, acquisition activities, working capital requirements and capital expenditures with cash from operations, proceeds from the issuances of our common stock and other financing arrangements. We are currently operating in a cash flow negative position while we seek to maintain and grow our cybersecurity business and cover our public company expenses during this uncertain time. In connection with our most recent results for the nine months ended September 30, 2021, we reported a loss from operations of \$1.2 million after excluding non-cash items for depreciation, amortization of intangibles, stock-based compensation, the change in valuation of the contingent earnout and non-recurring severance related costs. Cash used in operating activities was \$1.4 million for the nine months ended September 30, 2021.

In late 2019, a novel strain of coronavirus (COVID-19) was first detected in Wuhan, China. Following the outbreak of this virus, governments throughout the world, including in the United States of America, have quarantined certain affected regions, restricted travel and imposed significant limitations on other economic activities. Our customer base is heavily concentrated in the healthcare provider space. The healthcare industry has experienced significant financial losses due to the pandemic and are still contending with strained budgets but are showing signs of re-engagement.

Sales cycles are longer and pricing pressure is constant. The resurgence of the virus with the Delta Variant has caused some to return to operating with caution. Our operations team is closely monitoring the impact to the Company's business, including its cash flows, customers and employees. We are working with a number of our active customers since the outbreak began providing relief in the form of extended payment terms and other contractual restructurings. If the situation continues to impact our customers' cash flow or resources available for cybersecurity and privacy projects, our cash flows, financial position and operating results for fiscal year 2021 and beyond will be negatively impacted.

We did experience a negative financial impact from March 2020 through September 2021 that management anticipates will continue to impact revenue and earnings for the foreseeable future due to the pandemic related to COVID-19 and variants thereof, primarily because many of the economic effects of the early stages of the COVID-19 pandemic resulting from the various shelter-in-place and other social distancing orders. The severity and duration of the COVID-19 pandemic is uncertain, and such uncertainty will likely continue in the near term. We will continue to actively monitor the situation taking into account the impact to our employees, customers and partners.

At the end of 2019 and through the second quarter of 2021, we reduced staffing levels to reduce expenses that included permanent and temporary cost reductions, the precise extent of which will depend on the duration of the COVID-19 disruptions to our customers and our short-term financial performance. In addition, we received the PPP Loan (as defined in Note 9 to the unaudited condensed consolidated financial statements below) pursuant to the CARES Act (as defined in Note 9 to the unaudited condensed consolidated financial statements below), which was fully forgiven in August 2021 as described in Note 9 to the unaudited condensed consolidated financial statements. We also received approximately \$0.7 million per quarter in employee retention tax credits in the first, second and third quarters of 2021.

With the proceeds from the PPP Loan and the employee retention tax credits, we have tried to minimize staff reductions in the areas of Sales and Delivery, our primary customer facing roles, to lessen the impact to our customers during this time of heightened security risks for the healthcare industry. If necessary, we could further reduce personnel and other variable and semi-variable costs to conserve cash and operate as a going concern. However, those actions if required, could negatively impact the long-term outlook of the business.

As described in Note 12 to the unaudited condensed consolidated financial statements, on November 12, 2020, we entered into an Equity Distribution Agreement (the "Equity Distribution Agreement") with Craig-Hallum Capital Group LLC (as "Agent") thereunder, under which we may offer and sell, from time to time at our sole discretion, shares of our common stock having an aggregate offering price of up to \$5.0 million in an "at-the-market" or ATM offering, to or through the Agent. The Company agreed to pay the Agent a commission of three percent (3.0%) of the gross sales price per share of any common stock sold through the Agent under the Equity Distribution Agreement.

During September of 2021, the Company received gross proceeds under the Equity Distribution Agreement of \$1,434,000 from the issuance of 762,000 shares of our common stock and paid an aggregate of \$81,000 to the Agent in commissions and other offering-related expenses, yielding net proceeds of \$1,352,000.

We believe that our existing sources of liquidity, including cash and cash equivalents, the proceeds from the PPP Loan, employee retention tax credits and tax refunds from NOL carrybacks, the ability to raise equity under our

effective Registration Statement on Form S-3 (File No. 333-249615), filed with the Securities and Exchange Commission on October 22, 2020 (including via the Equity Distribution Agreement) and future operating cash flows will be sufficient to meet our projected capital needs for at least the next twelve months. As we execute our plans over the next twelve months, we intend to carefully monitor the impact on our operating expenses, working capital needs and cash balances relative to the availability of cost-effective debt and equity financing. In the event that capital is not available, we may then have to scale back operations, reduce expenses, and/or curtail future plans to manage our liquidity and capital resources. However, we cannot provide assurance that we will be able to raise additional capital. The COVID-19 pandemic will likely continue to create uncertainty and volatility in the financial markets which may impact our operations and our ability to access capital and/or the terms under which we can do so.

The impact of the COVID-19 pandemic on the economy and our operations is fluid and constantly evolving; we will continue to assess a variety of measures to improve our financial performance and liquidity.

The accompanying unaudited condensed consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts and classification of liabilities that might be necessary should the Company be unable to continue as a going concern.

## 2. RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

### Recently Issued Accounting Pronouncements Adopted

None.

### Recently Issued Accounting Pronouncements Not Yet Adopted

In June 2016, the FASB issued an amendment to the guidance on the measurement of credit losses on financial instruments. The amendment updates the guidance for measuring and recording credit losses on financial assets measured and amortized cost by replacing the “incurred loss” model with an “expected loss” model. Accordingly, these financial assets will be presented at the net amount expected to be collected. The amendment also requires that credit losses related to available-for-sale debt securities be recorded as an allowance through net income rather than reducing the carrying amount under the current, other-than-temporary-impairment model. The guidance is effective for smaller reporting companies for fiscal years beginning after December 15, 2022, including interim periods within those fiscal years. Early adoption is permitted for annual periods after December 15, 2018. Management does not expect the impact from this guidance will have a material impact on our consolidated financial statements.

## 3. ACCOUNTS RECEIVABLE

A summary of accounts receivable is as follows:

	September 30, 2021	December 31, 2020
Trade receivables	\$ 1,773,227	\$ 2,083,761
Allowance for doubtful accounts	-	(20,625)
Total accounts receivable, net	<u>\$ 1,773,227</u>	<u>\$ 2,063,136</u>

## 4. DEFERRED COMMISSIONS

Our incremental costs of obtaining a contract, which consist of sales commissions, are deferred and amortized over the period of contract performance. Deferred commissions are included in prepaid and other current assets in our consolidated balance sheets. We had \$659,000 and \$730,000 of unamortized deferred commissions as of September 30, 2021, and December 31, 2020, respectively. We had \$199,000 and \$567,000 of commissions expense for the three and nine months ended September 30, 2021, respectively. Commissions expense for the three and nine months ended September 30, 2020, was \$169,000 and \$493,000, respectively.

**5. PROPERTY AND EQUIPMENT**

A summary of property and equipment follows:

	<b>September 30, 2021</b>	<b>December 31, 2020</b>
Furniture and fixtures	\$ 235,245	\$ 235,245
Computers and office equipment	855,438	792,181
Right of use assets	214,935	1,843,818
Property and equipment at cost	1,305,618	2,871,244
Less accumulated depreciation and amortization	(1,021,652)	(2,329,719)
	<u>\$ 283,966</u>	<u>\$ 541,525</u>

**6. LEASES**

We previously leased approximately 9,600 square feet of office space in Austin, Texas. In March 2020, we amended this lease reducing the office space to 5,000 square feet and extended the lease term to May 31, 2022. We lease approximately 3,700 square feet of office space in Minneapolis, Minnesota. In July 2021, we amended this lease extending the term to January 31, 2022. We leased approximately 18,000 square feet of office space in Mission Viejo, California. This lease terminated in April 2021. During the first quarter of 2019, we subleased this space to two subtenants. The terms of these subleases ended concurrently with the end of our lease obligation in April 2021.

We used a discount rate of 5.5% in determining our operating lease liabilities which represented our incremental borrowing rate. Short-term leases with initial terms of twelve months or less are not capitalized.

Right-of-use assets and liabilities are recognized based on the present value of future minimum lease payments over the expected lease term at commencement date. Certain lease agreements contain extension options; however, we have not included such options as part of right-of-use assets and lease liabilities because we originally did not expect to extend the leases. We measure and record a right-of-use asset and lease liability based on the discount rate implicit in the lease, if known. In cases where the discount rate implicit in the lease is not known, we measure the right-of-use assets and lease liabilities using a discount rate equal to our estimated incremental borrowing rate for loans with similar collateral and duration.

Operating lease expense was comprised of the following:

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2021</b>	<b>2020</b>	<b>2021</b>	<b>2020</b>
Operating lease cost	\$ 72,196	\$ 171,220	\$ 338,731	\$ 550,467
Sublet income	-	(116,299)	(148,491)	(348,546)
Net operating lease cost	<u>\$ 72,196</u>	<u>\$ 54,921</u>	<u>\$ 190,240</u>	<u>\$ 201,921</u>

Maturities of lease liabilities are as follows:

	<b>Operating Leases</b>
2021 (remaining fiscal year)	\$ 39,754
2022	46,603
Total lease payments	86,357
Less imputed interest	(2,348)
Total lease liabilities	84,009
Less current portion of lease liabilities	(84,009)
Long-term lease liabilities	<u>\$ -</u>

**7. INTANGIBLE ASSETS**

Intangible assets are amortized over expected useful lives ranging from 1.5 to 10 years and consist of the following:

	September 30, 2021			December 31, 2020		
	Carrying Amount	Accumulated Amortization and Impairment	Net Book Value	Carrying Amount	Accumulated Amortization and Impairment	Net Book Value
Acquired technology	\$ 10,100,000	\$ (5,594,544)	\$ 4,505,456	\$ 10,100,000	\$ (4,934,720)	\$ 5,165,280
Customer relationships	4,650,000	(4,499,265)	150,735	4,650,000	(4,445,000)	205,000
Trademarks	2,300,000	(1,914,170)	385,830	2,300,000	(1,606,663)	693,337
Total	\$ 17,050,000	\$ (12,007,979)	\$ 5,042,021	\$ 17,050,000	\$ (10,986,383)	\$ 6,063,617

**8. DEFERRED REVENUE**

We record deferred revenues when amounts are billed to customers, or cash is received from customers, in advance of our performance. During the nine months ended September 30, 2021 and 2020, \$821,000 and \$1,115,000, respectively, of managed services revenues were recognized, that were included in deferred revenue at the beginning of the respective periods. During the nine months ended September 30, 2021 and 2020, \$269,000 and \$165,000, respectively, of consulting and professional services revenues were recognized, that were included in deferred revenue at the beginning of the respective periods.

**9. PAYCHECK PROTECTION PROGRAM LOAN**

On April 20, 2020, we received \$2,825,500 in loan funding from the Small Business Administration (“SBA”) Paycheck Protection Program (“PPP”), established pursuant to the Coronavirus Aid, Relief and Economic Security Act (the “CARES Act”). The unsecured loan (the “PPP Loan”) is evidenced by a promissory note issued by the Company (the “Note”) in favor of BMO Harris Bank N.A.

The Company used the PPP Loan proceeds to cover payroll costs, rent and utilities in accordance with the relevant terms and conditions of the CARES Act.

Under the terms of the Note and the PPP Loan, interest accrued on the outstanding principal at the rate of 1.0% per annum. The term of the Note was two years, unless sooner provided in connection with an event of default under the Note. To the extent the PPP Loan amount was not forgiven, the Company would have been obligated to make equal monthly payments of principal and interest, beginning seven months from the date of the Note, until the maturity date. The Company had not started making interest payments prior to its notice of forgiveness decision received from the SBA in August 2021. Details regarding the Note can be found in our Current Report on Form 8-K filed with the SEC on April 20, 2020.

The Company recognized interest charges associated with the PPP Loan of approximately \$2,000 and \$16,000, respectively, for the three and nine months ended September 30, 2021. The Company recognized interest charges of approximately \$7,000 and \$13,000, respectively, for the three and nine months ended September 30, 2020. The Company received notice in August 2021 from the SBA that the full principal balance and related interest was forgiven and the Company recognized “Other income” of \$2,862,000 in the accompanying unaudited condensed statement of operations for the quarterly period ended September 30, 2021.

**10. PROMISSORY NOTES**

In connection with the acquisition of CTEK Security, Inc. (formerly CynergisTek, Inc.), we issued a promissory note totaling \$4,500,000 to Michael McMillan (the “Seller Note”). In March 2018, the Company repaid \$2,250,000 plus accrued interest on the Seller Note and agreed to amend and restate the Seller Note in the remaining principal amount of \$2,250,000. The Seller Note bears interest at a rate of 8% per annum, provides for quarterly payments of principal and interest and matures on March 31, 2022. As of September 30, 2021, and December 31, 2020, the outstanding principal balance due under the Seller Note was \$281,000 and \$703,000, respectively.

Interest charges associated with the Seller Note totaled approximately \$8,000 and \$31,000, respectively for the three and nine months ended September 30, 2021, and \$19,000 and \$65,000, respectively for the three and nine months ended September 30, 2020.

**11. REVENUES**

Below is a summary of our revenues disaggregated by revenue source.

	<u>Three Months Ended</u>		<u>Nine Months Ended</u>	
	<u>September 30,</u>		<u>September 30,</u>	
	<u>2021</u>	<u>2020</u>	<u>2021</u>	<u>2020</u>
Managed services	\$ 2,210,910	\$ 2,732,612	\$ 6,819,570	\$ 8,672,377
Consulting and professional services	1,614,769	1,770,297	5,054,773	5,503,930
Net revenues	\$ 3,825,679	\$ 4,502,909	\$ 11,874,343	\$ 14,176,307

**12. COMMON STOCK**

On November 12, 2020 we entered into an Equity Distribution Agreement with Craig-Hallum Capital Group LLC (“Agent”) under which the Company may offer and sell, from time to time at its sole discretion, shares of its common stock to or through the Agent as its sales agent, having an aggregate offering price of up to \$5,000,000.

Pursuant to the Equity Distribution Agreement, sales of our common stock, can be made under the Company’s effective Registration Statement on Form S-3 (File No. 333-249615), filed with the Securities and Exchange Commission on October 22, 2020, and the prospectus supplement relating to this offering, filed on November 12, 2020, by any method that is deemed to be an “at the market offering” as defined in Rule 415(a)(4) under the Securities Act of 1933, as amended, including block transactions. The Agent agreed to use commercially reasonable efforts to sell the common stock from time to time, based upon instructions from the Company (including any price, time or size limits or other customary parameters or conditions the Company may impose). The Company will pay the Agent a commission of three percent (3.0%) of the gross sales price per share of our common stock sold through the Agent under the Agreement, and also has provided the Agent with customary indemnification rights. The Company will also reimburse the Agent for its reasonable out-of-pocket accountable fees and disbursements in an amount not to exceed \$50,000 through the fourth business day following execution of the Agreement, and in an amount not to exceed \$5,000 for each quarterly period thereafter.

During September 2021, the Company received gross proceeds under the Agreement of \$1,434,000 from the issuance of 762,000 shares of our common stock and paid an aggregate of \$81,000 in commissions and other offering-related expenses, yielding net proceeds of \$1,352,000. To date the total gross proceeds received from November 17, 2020 through September 30, 2021 by the Company under the Agreement is \$3,461,000 from the issuance of 2,077,000 shares of our common stock and the Company has paid an aggregate of \$265,000 in commissions and other offering-related expenses, yielding net proceeds of \$3,196,000.

**13. WARRANTS, OPTIONS AND RESTRICTED STOCK UNITS****Warrant Issued for Securities Purchase Agreement**

On April 3, 2020, we entered into a Securities Purchase Agreement (“Securities Purchase Agreement”) with Horton Capital Management, LLC (“Horton”) which provided that Horton was committed to purchase up to an aggregate of \$2,500,000 of shares of the Company’s common stock over the term of the agreement, at the election of the Company, which terminated on March 31, 2021. Additionally, if and when the Company sold shares to Horton under the Securities Purchase Agreement, the Company agreed to grant to Horton a warrant, with the same number of shares of common stock purchased by Horton in the particular funding, with an exercise price equal to 125% of the purchase price of the shares of common stock sold in such funding, with a 10-year term. No purchases were made under the Securities Purchase Agreement.

Upon signing the Securities Purchase Agreement, the Company issued Horton a warrant (the “Horton Warrant”) to purchase up to 500,000 shares of common stock in consideration of Horton’s obligation to purchase the shares, at an exercise price of \$2.50 per share, subject to certain anti-dilution adjustments as set forth in the warrant. The fair value of this warrant of \$390,000 was determined at the issuance date using the Black-Scholes option-pricing model and was expensed during the second quarter of 2020.

At the end of 2020, the Company issued common stock under the Equity Distribution Agreement receiving net proceeds of \$1,843,000 from the issuance of 1,315,000 shares of our common stock that resulted in a Q1 2021 anti-dilution adjustment increasing the number of shares under the Horton Warrant to 518,915 and reducing the exercise price to \$2.41. The resulting difference in fair value of the Horton Warrant with the new exercise price was \$6,000 and determined using the Black-Scholes option-pricing model and recorded as a deemed dividend in our consolidated statements of stockholders’ equity. As the Company has an accumulated deficit, the deemed dividend was recorded within additional paid-in capital.

In September 2021, the Company issued additional common stock under the Equity Distribution Agreement receiving net proceeds of \$1,352,000 from the issuance of 762,000 shares of our common stock that resulted in a Q3 2021 anti-dilution adjustment increasing the number of shares under the Horton Warrant to 524,170 and reducing the exercise price to \$2.38. The resulting difference in fair value of the Horton Warrant with the new exercise price was \$8,000 and determined using the Black-Scholes option-pricing model and recorded as a deemed dividend in our consolidated statements of stockholders’ equity. As the Company has an accumulated deficit, the deemed dividend was recorded within additional paid-in capital.

The detailed terms and conditions of the Securities Purchase Agreement and the Horton Warrant can be found in the documents, which were included as Exhibits 10.1 and 10.3, respectively, to our Current Report on Form 8-K, filed with the SEC on April 7, 2020.

Below is a summary of warrant activities during the nine-month period ended September 30, 2021:

<b>Warrants</b>	<b>Shares</b>	<b>Weighted Average Exercise Price</b>	<b>Weighted Average Remaining Term in Years</b>	<b>Aggregate Intrinsic Value</b>
Outstanding at December 31, 2020	577,779	\$ 2.57	8.29	\$ -
Granted	24,170	\$ 2.38	8.51	\$ -
Exercised	-	-		
Cancelled	-	-		
Outstanding at September 30, 2021	601,949	\$ 2.39	7.58	\$ -
Exercisable at September 30, 2021	601,949	\$ 2.39	7.58	\$ -

## 2020 Equity Incentive Plan

The 2020 Equity Incentive Plan provides for a total number of shares available for issuance of 3,745,621 shares of our common stock, and it provides for the granting of stock options, stock appreciation rights, restricted stock units and restricted stock to our employees, members of the Board of Directors and service providers.

Below is a summary of stock option activities during the three-month period ended September 30, 2021:

Options	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Term in Years	Aggregate Intrinsic Value
Outstanding at December 31, 2020	1,040,839	\$ 3.27	9.66	\$ 46,750
Granted	100,000	\$ 2.75		
Exercised	-	-		
Cancelled	(47,334)	1.94		
Outstanding at September 30, 2021	1,093,505	\$ 3.29	7.77	\$ -
Exercisable at September 30, 2021	510,172	\$ 4.66	6.72	\$ -

During the nine months ended September 30, 2021, we granted 100,000 options to an employee to purchase shares of our common stock at an exercise price of \$2.75 per share. The exercise price equals the fair value of our stock on the grant date. The options have graded vesting annually over three years. The fair value of the options of approximately \$135,000 was determined using the Black-Scholes option-pricing model.

Below is a summary of restricted stock unit activity during the nine-month period ended September 30, 2021:

Restricted Stock Units	Shares	Weighted Average Grant Date Fair Value per Share	Weighted Average Vesting Period in Years
Non-vested at December 31, 2020	555,350	\$ 3.38	1.24
Granted	300,000	2.39	
Vested	(255,000)	2.45	
Cancelled and forfeited	(116,000)	3.41	
Non-vested at September 30, 2021	484,350	\$ 3.23	0.62

There are 325,000 shares of restricted stock units which have vested but had not yet been issued as of September 30, 2021.

For the three and nine months ended September 30, 2021 and 2020, stock-based compensation and other equity instrument related expenses, net of forfeitures, recognized in the consolidated statements of operations were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2021	2020	2021	2020
Cost of revenues	\$ 2,546	\$ 96,283	\$ (644)	\$ 382,739
Sales and marketing	(139,111)	34,758	(75,281)	192,649
General and administrative	808,517	247,036	1,314,586	819,961
Finance cost for equity commitment	-	-	-	390,000
Total stock-based compensation and other equity instrument related expenses	\$ 671,952	\$ 378,077	\$ 1,238,661	\$ 1,785,349

**14. BASIC AND DILUTED NET INCOME (LOSS) PER SHARE**

Basic net income (loss) per share is calculated using the weighted average number of shares of our common stock issued and outstanding during a certain period and is calculated by dividing net income (loss) by the weighted average number of shares of our common stock issued and outstanding during such period. Diluted net income (loss) per share is calculated using the weighted average number of common and potentially dilutive common shares outstanding during the period, using the as-if-converted method for secured convertible notes, and the treasury stock method for options and warrants. Diluted net loss per share does not include potentially dilutive securities because such inclusion in the computation would be anti-dilutive.

For the three and nine months ended September 30, 2021, potentially dilutive securities consisted of options and warrants to purchase 1,695,000 shares of common stock at prices ranging from \$1.08 to \$4.86 per share. Of these potentially dilutive securities, 144,000 and 148,000 shares to purchase common stock from the options and warrants for the three and nine months ended September 30, 2021, respectively, are included in the computation of diluted earnings per share. Also excluded from potentially dilutive securities are 484,350 shares of non-vested restricted stock units.

For the three and nine months ended September 30, 2020, potentially dilutive securities consisted of options and warrants to purchase 1,514,000 shares of common stock at prices ranging from \$1.08 to \$4.05 per share. Of these potentially dilutive securities, none of the shares to purchase common stock from the options and warrants are included in the computation of diluted earnings per share, because the effect of including the remaining instruments would be anti-dilutive. Also excluded from potentially dilutive securities are 55,000 shares of restricted stock units which have vested but had not been issued by period end and 845,500 shares of non-vested restricted stock units.

	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2021</b>	<b>2020</b>	<b>2021</b>	<b>2020</b>
<b>Numerators:</b>				
Net income (loss) attributable to common shareholders	\$ 1,212,071	\$ (1,276,399)	\$244,872	\$(5,581,684)
<b>Denominator:</b>				
Denominator for basic calculation weighted average shares	12,141,088	10,597,024	12,101,466	10,486,334
<b>Dilutive common stock equivalents:</b>				
Options and warrants	144,355	-	147,512	-
Restricted stock units vested but not issued	325,000	-	325,000	-
Denominator for diluted calculation weighted average shares	12,610,443	10,597,024	12,573,978	10,486,334
<b>Net income (loss) per share:</b>				
Basic	\$ 0.10	\$ (0.12)	\$ 0.02	\$ (0.53)
Diluted	\$ 0.10	\$ (0.12)	\$ 0.02	\$ (0.53)

## **15. REMAINING PERFORMANCE OBLIGATIONS**

We had remaining performance obligations of approximately \$18.4 million as of September 30, 2021. Our remaining performance obligations represent the amount of transaction price for which work has not been performed and revenue has not been recognized. When applying Accounting Standards Codification (“ASC”) Topic 606, with only the non-cancelable portion of these contracts included in our performance obligations we had approximately \$16.0 million as of September 30, 2021. We expect to recognize revenue on approximately 87% of the remaining non-cancelable portion of these performance obligations over the next 24 months, with the balance thereafter.

## **16. CONCENTRATIONS**

### **Cash Concentrations**

At times, cash balances held in financial institutions are in excess of federally insured limits. Management performs periodic evaluations of the relative credit standing of financial institutions and limits the amount of risk by selecting financial institutions with a strong credit standing.

### **Major Customers**

Our largest customer accounted for approximately 13% and 9% of our revenues for the nine months ended September 30, 2021 and 2020, respectively. Our largest customer had accounts receivable totaling approximately \$59,000 and \$74,000 as of September 30, 2021, and December 31, 2020, respectively.

## **17. EARNOUT LIABILITY – BACKBONE ENTERPRISES**

In 2019, we entered into a Stock Purchase Agreement (the “Backbone Purchase Agreement”) with Backbone Enterprises Inc., a Minnesota corporation (“Backbone”), and its stockholders (the “Stockholders”), pursuant to which we acquired 100% of the issued and outstanding shares of common stock (the “Shares”) of Backbone from the Stockholders. Pursuant to the Backbone Purchase Agreement, the aggregate purchase price for the Shares included an earn-out, pursuant to which the Stockholders may be entitled to an additional \$4,000,000 based upon the post-closing financial performance of Backbone, to be calculated based upon revenue generated by the Backbone business during the three-year earn-out period. There was no earn-out earned for the first year of the agreement. We performed an updated valuation of the contingent earn-out as of June 30, 2021, which resulted in a full write-off of the previous estimate of \$1,300,000. The Company renegotiated the terms of the earnout and as a result performed an updated valuation of the contingent earn-out as of September 30, 2021, which resulted in a recovery from the previous estimate of \$250,000.

## **18. EMPLOYMENT AGREEMENTS**

### **Caleb Barlow**

On July 26, 2021, Caleb Barlow, notified the Board of Directors (the “Board”) of his resignation as the President and Chief Executive Officer of the Company, effective immediately. Mr. Barlow also informed the Board of his resignation as a member of the Board, to be effective August 26, 2021. The Board accepted Mr. Barlow’s resignation and, on July 26, 2021, appointed Michael “Mac” McMillan as President and Chief Executive Officer of the Company, effective immediately. Mr. Barlow’s resignation included a severance payment of approximately \$578,000 and issuance of 200,000 shares of common stock as a result of the accelerated vesting and settlement of 200,000 restricted stock units that was paid and settled in October 2021.

**Michael H. McMillan**

In connection with Mr. McMillan’s appointment as President and Chief Executive Officer, the Company and Mr. McMillan entered into an employment agreement (the “Employment Agreement”) to be effective as of July 26, 2021 (the “Effective Date”). Pursuant to the Employment Agreement, Mr. McMillan has the duties and responsibilities as are commensurate with the positions of President and Chief Executive Officer, as reasonably and lawfully directed by the Board. The initial term of the Employment Agreement is 12 months from the Effective Date.

Pursuant to the Employment Agreement, Mr. McMillan’s base salary will be \$300,000. Except in the event that Mr. McMillan’s employment is terminated for Cause (as defined below), the base salary is guaranteed and shall, in any event, be paid through the end of the 12-month term of the Employment Agreement. The Company has the right to terminate Mr. McMillan’s employment for “Cause,” which is defined in the Employment Agreement to mean: (a) acts or omissions constituting gross negligence, recklessness or willful misconduct on the part of Mr. McMillan with respect to his obligations or otherwise relating to the business of Company; (b) Mr. McMillan’s material breach of the Employment Agreement; and (c) Mr. McMillan’s conviction or entry of a plea of nolo contendere for fraud, misappropriation or embezzlement, or any felony or crime of moral turpitude.

The preceding description of the Employment Agreement is a summary of its material terms, does not purport to be complete. The Employment Agreement was filed as Exhibit 10.1 to our Current Report on Form 8-K filed with the SEC on July 26, 2021.

## ITEM 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

The following discussion of the financial condition and results of operations of the Company should be read in conjunction with the condensed consolidated financial statements and the related notes thereto included elsewhere in this Quarterly Report on Form 10-Q. This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), and Section 27A of the Securities Act, and is subject to the safe harbors created by those sections. Words such as “anticipates,” “expects,” “intends,” “plans,” “believes,” “seeks,” “estimates,” “may,” “will” and variations of these words or similar expressions are intended to identify forward-looking statements.

In addition, any statements that refer to expectations, projections or other characterizations of future events or circumstances, including any underlying assumptions, are forward-looking statements. These statements are not guarantees of future performance and are subject to risks, uncertainties and assumptions that are difficult to predict.

Therefore, our actual results could differ materially and adversely from those expressed in any forward-looking statements as a result of various factors. We undertake no obligation to revise or publicly release the results of any revisions to these forward-looking statements.

Due to possible uncertainties and risks, readers are cautioned not to place undue reliance on the forward-looking statements contained in this Quarterly Report, which speak only as of the date of this Quarterly Report, or to make predictions about future performance based solely on historical financial performance. We disclaim any obligation to update forward-looking statements contained in this Quarterly Report.

Readers should carefully review the risk factors described in other documents we file from time to time with the SEC, including our Form 10-K for the fiscal year ended December 31, 2020, as amended. You should interpret many of the risks identified in these reports as being heightened as a result of the ongoing and numerous adverse impacts of the COVID-19 pandemic. Our filings with the SEC, including our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those filings, pursuant to Sections 13(a) and 15(d) of the Exchange Act, are available free of charge at [www.CynergisTek.com](http://www.CynergisTek.com), when such reports are available via the EDGAR system maintained by the SEC at [www.sec.gov](http://www.sec.gov).

### OVERVIEW

We are engaged in the business of helping U.S. based companies in highly regulated industries, including healthcare, be prepared to handle unforeseen cyber threats, comply with regulations, and gain the confidence that their efforts are strengthening their security posture and building resilience. This is achieved through our cybersecurity, privacy and compliance services.

CynergisTek was born in healthcare and is one of the few consulting and advisory companies focused on converging security and privacy with a methodology to validate the rigor and effectiveness of their programs. We believe that our years of experience of understanding our clients’ unique challenges allows us to provide our customers with services designed around industry best practices to improve security controls, policies and procedures and to protect sensitive information. Our team of subject matter experts and consultants are comprised of knowledgeable professionals who have learned their craft both in the classroom and through years of practical on-the-job experience, including as policy makers, attorneys and leaders in cybersecurity, privacy and compliance.

Our services are categorized into four service groups, which are: assess, build, manage, and validate. These services are designed to meet the client where they are in their security journey as recurring managed services under long-term contracts structured to provide a sustainable and growing program, or under shorter duration consulting or professional services engagements.

- **Assess** – identify, measure, and test security and privacy risk of an organization’s readiness and verify and validate their programs meet compliance and business objectives through IT audits, technical testing, and risk and program assessments.
- **Build** – develop policies and procedures and playbooks to help build out a fully comprehensive risk management program and provide resources to help organizations prioritize, implement and execute initiatives to strengthen their security and privacy programs.

- **Manage** - provide on-going management and oversight of specific components of an organization's security and privacy programs to address or give alerts when an issue arises and to offer our expertise that they need to accelerate the effectiveness of their programs.
- **Validate** – verify the processes, people, and technology are working effectively and provide insight to the ROI of an organization's security investment through advanced services requiring highly experienced resources and/or technology to deliver.

For sophisticated organizations our Resilience Partner Program encompasses a bundle of services from the assess, build, manage, and validate categories to deliver clarity and guidance as a consistent partner helping maintain and grow their security infrastructure. This highly customizable managed service allows CynergisTek to meet the unique needs of client wanting to work with a partner over a multiyear engagement.

#### *Impact of COVID-19 Pandemic*

In December 2019, a novel strain of the coronavirus (COVID-19) surfaced, which spread globally and was declared a pandemic by the World Health Organization in March 2020. The challenges posed by the COVID-19 pandemic on the global economy increased significantly in the first several months of 2020. In response to the COVID-19 pandemic, national and local governments around the world instituted certain measures, including travel bans, prohibitions on group events and gatherings, shutdowns of certain businesses, curfews, shelter-in-place orders and recommendations to practice social distancing. Variants of the COVID-19 virus pose similar and other unknown risks to the economy and our business.

In planning for the possible disruption of our business, we took steps to reduce expenses throughout the Company. This included substantially reducing Company travel for a period of time, as well as our participation in trade shows and other business meetings and decreasing expenditures. We also implemented workforce reductions during 2020 and the beginning of 2021, decreasing employment and related expenses. Continued progression of the pandemic could result in a decline in customer orders, as our customers could shift purchases to lower-priced or other perceived value offerings or reduce their purchases of our services due to decreased budgets, reduced access to credit or various other factors, which could have a material adverse impact on our results of operations and cash flow. While the current impacts of COVID-19, including from variants thereof, are reflected in our results of operations, we cannot at this time separate the direct COVID-19 impacts from other factors that cause our performance to vary from year to year. The ultimate duration and impact of the ongoing pandemic related to COVID-19 and its variants on our business, results of operations, financial condition and cash flows is dependent on future developments, including the duration and severity of the pandemic, and the related length of its impact on the global economy, which are uncertain and, given the daily evolution of the COVID-19 pandemic and the global responses to curb its spread, cannot be predicted at this time. Even after the pandemic related to COVID-19 and its variants has subsided, we may continue to experience an adverse impact to our business as a result of its national and, to some extent, global economic impact, including any recession that has occurred or may occur in the future. Furthermore, the extent to which our mitigation efforts are successful, if at all, is not presently ascertainable. However, we anticipate that our results of operations in future periods may continue to be adversely impacted by the pandemic related to COVID-19 and its variants, and its negative effects on global economic conditions.

Our common stock currently trades on the NYSE American exchange under the stock symbol "CTEK".

Where appropriate, references to "CynergisTek," the "Company," "Redspin," "we," "us," or "our" include CynergisTek, Inc., a Delaware corporation and its wholly-owned subsidiaries, CTEK Solutions, Inc., a California corporation, CTEK Security, Inc., a Texas corporation, Delphiis, Inc., a California corporation and Backbone Enterprises, Inc., a Minnesota corporation.

## RESULTS OF OPERATIONS

### For the Three Months Ended September 30, 2021, Compared to the Three Months Ended September 30, 2020

#### Revenue

Revenue decreased \$0.7 million to \$3.8 million for the three months ended September 30, 2021, as compared to the same period in 2020. Managed Services revenue decreased \$0.5 million due to the impact of some customers canceling contracts, delaying renewals, a slowdown in net new customers due to the COVID-19 pandemic, customers holding off on purchasing or trying to reduce budgets and a number of customers delaying the start of services due to technical issues related to one of our 3<sup>rd</sup> party applications that we expect to be resolved in the next few months. Consulting and professional services decreased \$0.2 million due to underperformance in our Backbone business unit. We have seen an increase in sales bookings recently along with an increase in our backlog or remaining performance obligations that we expect will result in higher revenues starting in Q4.

#### Cost of Revenue

Cost of revenue consists primarily of salaries and related expenses of direct labor and indirect support staff. Cost of revenue was \$2.0 million for the three months ended September 30, 2021, as compared to \$2.9 million for the same period in 2020. Salary and related costs were lower by \$0.7 million due to the reduced headcount in response to the lower revenue and the benefit from the employee retention credit provided under the CARES Act, technology related costs were lower by \$0.1 million as a result of expense reduction efforts prompted by the lower revenue and stock compensation expense was down \$0.1 million as a result of the reduction in headcount.

Gross margin was 48% of revenue for the three months ended September 30, 2021. Excluding the employee retention tax credit, gross margin would have been 35% for the three months ended September 30, 2021, compared to 35% for the same period in 2020. Margins remained flat with the benefit from lower salary and related costs and the employee retention credit offsetting the impact from the decline in revenue.

#### Sales and Marketing

Sales and marketing expenses include salaries, commissions and expenses for sales and marketing personnel, travel and entertainment, and other selling and marketing costs. Sales and marketing expenses decreased to \$1.1 million for the three months ended September 30, 2021, as compared to \$1.3 million for the same period in 2020. This decrease was due to \$0.1 million of payroll-related expense reduction efforts taken in reaction to the lower revenue resulting from the COVID-19 pandemic, \$0.1 million of employee retention tax credits provided under the CARES Act and \$0.2 million in lower stock compensation expense as a result of the reduction in headcount. Those reductions were partially offset by an increase of \$0.2 million in marketing and travel spend to support our Redspin business line and we are beginning to ramp back up our sales and marketing efforts to grow sales.

#### General and Administrative

General and administrative expenses include personnel costs for finance, administration, information systems, general management, facilities expenses, professional fees, legal expenses and other administrative costs including those required to be a publicly traded company. General and administrative expenses increased \$1.1 million to \$2.6 million for the three months ended September 30, 2021, compared to \$1.5 million for the three months ended September 30, 2020. The increase is due to \$0.7 million in non-recurring severance costs and \$0.5 million in accelerated stock-based compensation as a result of the departure of our former CEO. This increase was partially offset by \$0.1 million of employee retention tax credits provided under the CARES Act.

### **Change in Valuation of Contingent Earn-out**

The Company renegotiated the contingent earn-out with the sellers of Backbone Enterprises, Inc. during the quarter and performed an updated valuation as of September 30, 2021, which resulted in an increase from the previous estimate of \$250,000 related to the potential for payout for meeting earn-out criteria in the final two years of the annual earn-out measurement periods.

### **Depreciation**

Depreciation expense was consistent at \$48,000 for the three months ended September 30, 2021, compared to \$48,000 for the same period in 2020.

### **Amortization of Acquisition-Related Intangibles**

Amortization of acquisition-related intangibles was \$0.3 million for the three months ended September 30, 2021, compared to \$0.4 million for the three months ended September 30, 2020. Amortization expense decreased over the comparable periods as the remaining balance of amortizable intangible assets decreased.

### **Net Interest Expense**

Net interest expense for the three months ended September 30, 2021, was \$10,000, compared to net interest expense of \$24,000 for the same period in 2020.

### **Other Income and Expense**

The Company received notice in August 2021 from the SBA that the full principal balance and related interest of the PPP Loan was forgiven and the Company recognized income of \$2,862,000

### **Income Tax**

Income tax benefit for the three months ended September 30, 2021, was \$0.9 million, compared to income tax benefit of \$0.4 million for the same period in 2020. These amounts were based on estimated annual income tax rates we anticipate for the year.

## **For the Nine Months Ended September 30, 2021, Compared to the Nine Months Ended September 30, 2020**

### **Revenue**

Revenue decreased \$2.3 million to \$11.9 million for the nine months ended September 30, 2021, as compared to the same period in 2020. Managed Services revenue decreased \$1.9 million due to the impact of some customers canceling contracts, delaying renewals, a slowdown in net new customers due to the COVID-19 pandemic, customers holding off on purchasing or trying to reduce budgets and a number of customers delaying the start of services due to technical issues related to one of our 3<sup>rd</sup> party applications that we expect to be resolved in the next few months. Consulting and professional services decreased \$0.4 million primarily due to lower revenue from two customers who completed contract work in the first half of 2020, lower revenues from our Backbone business unit as a result of the COVID-19 pandemic, and customers holding off on delivery of previously sold professional services as they attempt to minimize spend with third-party contractors or prospects limiting their purchasing of new services as they look to reduce budgets.

### **Cost of Revenue**

Cost of revenue was \$6.1 million for the nine months ended September 30, 2021, as compared to \$9.7 million for the same period in 2020. We reduced salary and related costs and stock-based compensation associated with our reduction in force by approximately \$1.8 million due to the lower revenue from the COVID-19 pandemic and received a \$1.6 million benefit from the employee retention credit provided under the CARES Act and \$0.2 million lower technology related costs as a result of the lower revenue.

Gross margin was 48% of revenue for the nine months ended September 30, 2021, and 32% for the same period in 2020. After adjusting for the benefit from the employee retention tax credit in 2021, gross margin was 35%. Margins improved as a result of targeted expense reductions we made over the last few quarters in reaction to the lower revenue due to COVID-19.

### **Sales and Marketing**

Sales and marketing expenses decreased to \$3.5 million for the nine months ended September 30, 2021, as compared to \$4.5 million for the same period in 2020. This decrease was due to \$0.6 million in lower marketing and sales support payroll and benefit costs from the headcount reductions due to the COVID-19 pandemic, \$0.3 million in lower stock compensation expense as a result of the reduction in headcount and \$0.3 million of employee retention tax credits provided under the CARES Act. This decrease was partially offset by \$0.1 million in recruiting costs to bring on a new sales leader and additional direct sales leads and an increase of \$0.1 million in marketing spend to support our Redspin business line and slowly ramping back up our sales and marketing efforts to grow sales.

### **General and Administrative**

General and administrative expenses increased \$0.4 million to \$5.8 million for the nine months ended September 30, 2021, compared to \$5.4 million for the same period in 2020. The increase is due to \$0.6 million in severance related costs and \$0.5 million in higher stock-based compensation from the acceleration of vesting of restricted stock units as a result of the departure of our former CEO, which were partially offset by \$0.3 million in lower payroll and benefit related costs due to the expense reduction efforts taken in reaction to the lower revenue from the COVID-19 pandemic, \$0.2 million less in recruiting costs due to 2020 being higher, and \$0.2 million of employee retention tax credits provided under the CARES Act.

### **Change in Valuation of Contingent Earn-out**

As of June 30, 2021 we performed a valuation of the contingent earn-out to the sellers of Backbone Enterprises, Inc., which resulted in a reduction of the previous estimate of \$1,300,000 related to the potential for payout for not meeting earn-out criteria in the final two years of the annual earn-out measurement periods. In September of 2021 the Company renegotiated the earnout with the sellers and performed an updated valuation as of September 30, 2021, which resulted in a reduction of the previous estimate to \$1,050,000.

### **Depreciation**

Depreciation remained relatively consistent at \$144,000 for the nine months ended September 30, 2021, as compared to \$142,000 for the same period in 2020.

### **Amortization of Acquisition-Related Intangibles**

Amortization of acquisition-related intangibles was \$1.0 million for the nine months ended September 30, 2021, compared to \$1.2 million for the nine months ended September 30, 2020. Amortization expense decreased over the comparable periods as a portion of the intangible assets are now fully amortized.

### **Finance Cost for Equity Commitment**

In April 2020 we issued a warrant to an investor in return for an obligation by them to purchase our common stock as a stated price as described in Note 13 to the unaudited condensed consolidated financial statements. The fair value of this warrant of \$390,000 was recorded as an expense at the time of issuance.

### **Net Interest Expense**

Net interest expense for the nine months ended September 30, 2021, was \$47,000, compared to \$68,000 for the same period in 2020.

## **Other Income and Expense**

The Company received notice in August 2021 from the SBA that the full principal balance and related interest on the PPP Loan was forgiven and the Company recognized income of \$2,862,000

## **Income Tax**

Income tax benefit for the nine months ended September 30, 2021, was \$1.2 million, compared to income tax benefit of \$1.6 million for the same period in 2020. These amounts were based on estimated annual income tax rates we anticipate for the year.

## **Liquidity and Capital Resources**

As of September 30, 2021, our cash balance was \$5.1 million, current assets minus current liabilities was positive \$6.6 million. The level of additional cash needed to fund operations and our ability to conduct business for the next twelve months will be influenced primarily by the following factors:

- our ability to manage our operating expenses and maintain gross margins while attracting, recruiting and retaining cybersecurity privacy professionals;
- demand for our services from healthcare providers; the near-term impact of the COVID-19 pandemic on our customers' allocation of time and resources to security and privacy, and their ability to pay for existing services as well as enter into new contractual arrangements during a period of crisis;
- general economic conditions and changes in healthcare reimbursement and regulatory environment, including effects of the COVID-19 pandemic; and
- our ability to collect accounts receivable from health care customers whose operations and cash flow have been significantly impacted by the COVID-19 pandemic.

We have historically funded our operating costs, acquisition activities, working capital requirements and capital expenditures with cash from operations, proceeds from the issuances of our common stock and other financing arrangements. We are currently operating in a cash flow negative position while we seek to maintain and grow our cybersecurity business and cover our public company expenses during this uncertain time. In connection with our most recent results for the nine months ended September 30, 2021, we reported a loss from operations of \$1.2 million after excluding non-cash items for depreciation, amortization of intangibles, stock-based compensation, the change in valuation of the contingent earnout and non-recurring severance related costs. Cash used in operating activities was \$1.4 million for the nine months ended September 30, 2021.

In late 2019, a novel strain of coronavirus (COVID-19) was first detected in Wuhan, China. Following the outbreak of this virus, governments throughout the world, including in the United States of America, have quarantined certain affected regions, restricted travel and imposed significant limitations on other economic activities. Our customer base is heavily concentrated in the healthcare provider space. The healthcare industry has experienced significant financial losses due to the pandemic and are still contending with strained budgets but are showing signs of re-engagement.

Sales cycles are longer and pricing pressure is constant. The resurgence of the virus with the Delta Variant has caused some to return to operating with caution. Our operations team is closely monitoring the impact to the Company's business, including its cash flows, customers and employees. We are working with a number of our active customers since the outbreak began providing relief in the form of extended payment terms and other contractual restructurings.

If the situation continues to impact our customers' cash flow or resources available for cybersecurity and privacy projects, our cash flows, financial position and operating results for fiscal year 2021 and beyond will be negatively impacted.

We did experience a negative financial impact from March 2020 through September 2021 that management anticipates will continue to impact revenue and earnings for the foreseeable future due to the pandemic related to COVID-19 and variants thereof, primarily because many of the economic effects of the early stages of the COVID-19 pandemic resulting from the various shelter-in-place and other social distancing orders. The severity and duration of the COVID-19 pandemic is uncertain, and such uncertainty will likely continue in the near term. We will continue to actively monitor the situation taking into account the impact to our employees, customers and partners.

At the end of 2019 and through the second quarter of 2021, we reduced staffing levels to reduce expenses that included permanent and temporary cost reductions, the precise extent of which will depend on the duration of the COVID-19 disruptions to our customers and our short-term financial performance. In addition, we received the PPP Loan (as defined in Note 9 to the unaudited condensed consolidated financial statements below) pursuant to the CARES Act (as defined in Note 9 to the unaudited condensed consolidated financial statements below), which was fully forgiven in August 2021 as described in Note 9 to the unaudited condensed consolidated financial statements. We also received approximately \$0.7 million per quarter in employee retention tax credits in the first, second and third quarters of 2021. With the proceeds from the PPP Loan and the employee retention tax credits, we have tried to minimize staff reductions in the areas of Sales and Delivery, our primary customer facing roles, to lessen the impact to our customers during this time of heightened security risks for the healthcare industry. If necessary, we could further reduce personnel and other variable and semi-variable costs to conserve cash and operate as a going concern. However, those actions if required, could negatively impact the long-term outlook of the business.

As described in Note 12 to the unaudited condensed consolidated financial statements, on November 12, 2020, we entered into an Equity Distribution Agreement (the “Equity Distribution Agreement”) with Craig-Hallum Capital Group LLC (as “Agent”) thereunder, under which we may offer and sell, from time to time at our sole discretion, shares of our common stock having an aggregate offering price of up to \$5.0 million in an “at-the-market” or ATM offering, to or through the Agent. The Company agreed to pay the Agent a commission of three percent (3.0%) of the gross sales price per share of any common stock sold through the Agent under the Equity Distribution Agreement.

During September of 2021, the Company received gross proceeds under the Equity Distribution Agreement of \$1,434,000 from the issuance of 762,000 shares of our common stock and paid an aggregate of \$81,000 to the Agent in commissions and other offering-related expenses, yielding net proceeds of \$1,352,000.

We believe that our existing sources of liquidity, including cash and cash equivalents, the proceeds from the PPP Loan, employee retention tax credits and tax refunds from NOL carrybacks, the ability to raise equity under our effective Registration Statement on Form S-3 (File No. 333-249615), filed with the Securities and Exchange Commission on October 22, 2020 (including via the Equity Distribution Agreement) and future operating cash flows will be sufficient to meet our projected capital needs for at least the next twelve months. As we execute our plans over the next twelve months, we intend to carefully monitor the impact on our operating expenses, working capital needs and cash balances relative to the availability of cost-effective debt and equity financing. In the event that capital is not available, we may then have to scale back operations, reduce expenses, and/or curtail future plans to manage our liquidity and capital resources. However, we cannot provide assurance that we will be able to raise additional capital. The COVID-19 pandemic will likely continue to create uncertainty and volatility in the financial markets which may impact our operations and our ability to access capital and/or the terms under which we can do so.

The impact of the COVID-19 pandemic on the economy and our operations is fluid and constantly evolving; we will continue to assess a variety of measures to improve our financial performance and liquidity.

#### **Application of Critical Accounting Policies**

The SEC defines critical accounting policies as those that are, in management’s view, most important to the portrayal of our financial condition and results of operations and most demanding of our judgment. The discussion and analysis of our financial condition and results of operations are based upon our financial statements, which were prepared in accordance with accounting principles generally accepted in the U.S., which is referred to as “GAAP.” The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosures of contingent assets and liabilities. On

an on-going basis, we evaluate these estimates, including those related to stock-based compensation, customer programs and incentives, bad debts, intangible assets, income taxes, contingencies and litigation. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

We consider the following accounting policies to be those most important to the portrayal of our financial condition and those that require the most subjective judgment:

### **Revenue Recognition and Deferred Revenue**

We operate under a consolidated strategy and management structure, deriving revenue from the following sources:

- Managed services
- Consulting and professional services

Revenue is recognized pursuant to ASC Topic 606, “Revenue from Contracts with Customers”. Accordingly, revenue is recognized at an amount that reflects the consideration to which we expect to be entitled in exchange for transferring goods or services to a customer. This principle is applied using the following 5-step process:

1. **Identify the contract with the customer** - A contract with a customer exists when (i) we enter into an enforceable contract with a customer that defines each party’s rights regarding the services to be transferred and identifies the payment terms related to these services, (ii) the contract has commercial substance and the parties are committed to perform, and (iii) we determine that collection of substantially all consideration to which it will be entitled in exchange for services that will be transferred is probable based on the customer’s intent and ability to pay the promised consideration.
2. **Identify the performance obligations in the contract** - Performance obligations promised in a contract are identified based on the services that will be transferred to the customer that are both capable of being distinct, whereby the customer can benefit from the service either on its own or together with other resources that are readily available from third parties or from us, and are distinct in the context of the contract, whereby the transfer of the services is separately identifiable from other promises in the contract. To the extent a contract includes multiple promised services, we apply judgment to determine whether promised services are capable of being distinct and distinct in the context of the contract. If these criteria are not met the promised services are accounted for as a combined performance obligation.
3. **Determine the transaction price** - The transaction price is determined based on the consideration to which we will be entitled in exchange for transferring services to the customer.
4. **Allocate the transaction price to the performance obligations in the contract** - If the contract contains a single performance obligation, the entire transaction price is allocated to the single performance obligation. Contracts that contain multiple performance obligations require an allocation of the transaction price to each performance obligation based on a relative standalone selling price (“SSP”) basis. Determination of SSP requires judgment. We determine standalone selling price taking into account available information such as historical selling prices of the performance obligation, overall strategic pricing objective, market conditions and internally approved pricing guidelines related to the performance obligations.
5. **Recognize revenue when (or as) each performance obligation is satisfied** - We satisfy performance obligations over time. Revenue is recognized over the time the related performance obligation is satisfied by transferring a promised service to a customer.

### Managed Services

Managed services contracts are typically long-term contracts lasting three years. Revenue is earned monthly during the term of the contract, as services are provided at a fixed fee and is recognized ratably over the contract term beginning on the commencement date of the contract. Revenue related to managed services provided is recognized based on the customer utilization of such resources, which management estimates to occur ratably over the customer contract term.

### Consulting and Professional Services

Consulting and professional services contracts are typically short-term, project-based services rendered on either a fixed fee or a time and materials basis. These contracts are normally for a duration of less than one year. For fixed fee arrangements, revenue is normally recognized ratably over the term of the project. For time and materials arrangements, revenues are recognized as the services are rendered.

### Deferred and Unbilled Revenue

We receive payments from customers based on billing schedules established in our contracts. Deferred revenue primarily consists of billings or payments received in advance of the amount of revenue recognized and such amounts are recognized as the revenue recognition criteria are met. Unbilled revenue reflects our conditional right to receive payment from customers for our completed performance under contracts.

### **Accounts Receivable Valuation and Related Reserves**

We estimate the losses that may result from that portion of our accounts receivable that may not be collectible as a result of the inability of our customers to make required payments. Management specifically analyzes customer concentration, customer creditworthiness, current economic trends, COVID-19 developments and changes in customer payment terms when evaluating the adequacy of the allowance for doubtful accounts. We review past due accounts on a monthly basis and record an allowance for doubtful accounts where we deem appropriate.

### **Impairment Review of Goodwill and Intangible Assets**

We periodically evaluate our intangible assets and goodwill relating to acquisitions for impairment. Goodwill is not amortized but is evaluated at least annually at year end for any impairment in the carrying value. We review our intangible assets for impairment whenever events or changes in circumstances indicate that the carrying value of such assets may not be recoverable. Factors we consider important which could trigger an impairment review include, but are not limited to, the following: significant underperformance relative to expected historical or projected future operating results; significant changes in the manner of our use of the acquired assets or the strategy for our overall business; and a significant negative industry or economic trend for a sustained period. Goodwill and intangible asset impairment assessments are generally determined based on fair value techniques, including determining the estimated future discounted and undiscounted cash flows over the remaining useful life of the asset. Those models require estimates of future revenue, profits, capital expenditures and working capital for each reporting unit. We estimate these amounts by evaluating historical trends, the current state of the Company's industries and the economy, current budgets, and operating plans. Determining the fair value of reporting units and goodwill includes significant judgment by management and different judgments could yield different results. Any resulting impairment loss could have a material impact on our financial condition and results of operations.

### **Stock-Based Compensation**

Under the fair value recognition provisions of the authoritative guidance, stock-based compensation cost granted to employees is measured at the grant date based on the fair value of the award and is recognized as expense over the requisite service or performance period, which is the vesting period. Stock options and warrants issued to consultants and other non-employees as compensation for services to be provided to us are accounted for based upon the fair value of the services provided or the estimated fair value of the option or warrant, whichever can be more clearly determined. We currently use the Black-Scholes option pricing model to determine the fair value of stock options and warrants. The determination of the fair value of stock-based payment awards on the date of grant using

an option-pricing model is affected by our stock price as well as assumptions regarding a number of complex and subjective variables. These variables include our expected stock price volatility over the term of the awards, the expected term of the award, the risk-free interest rate and any expected dividends. Compensation cost associated with grants of restricted stock units are also measured at fair value on the date of the grant. We evaluate the assumptions used to value restricted stock units on a quarterly basis. When factors change, including the market price of the stock, stock-based compensation expense may differ significantly from what has been recorded in the past. If there are any modifications or cancellations of the underlying unvested securities, we may be required to accelerate, increase or cancel any remaining unearned stock-based compensation expense.

### Income Taxes

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial reporting requirements and those imposed under federal and state tax laws. Deferred taxes are provided for timing differences in the recognition of revenue and expenses for income tax and financial reporting purposes and are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Deferred income tax expense represents the change during the period in the deferred tax assets and liabilities. Realization of the deferred tax asset is largely dependent on generating sufficient taxable income in future years. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all the deferred tax assets will not be realized. Use of our net operating loss deferred assets may be limited by changes in our ownership.

Reference is made to our Annual Report on Form 10-K for the fiscal year ended December 31, 2020, filed with the SEC on March 25, 2021, for additional discussion of our critical accounting policies.

### OFF-BALANCE SHEET ARRANGEMENTS

As of September 30, 2021, we did not have any other relationships with unconsolidated entities or financial partners, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

### CONTRACTUAL OBLIGATIONS AND CONTINGENT LIABILITIES AND COMMITMENTS

As of September 30, 2021, expected future cash payments related to contractual obligations and commercial commitments were as follows:

	Payments Due by Period				
	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Promissory note	\$ 290,000	\$ 290,000	\$ -	\$ -	\$ -
Operating leases	86,000	86,000	-	-	-
Total	\$ 376,000	\$ 376,000	\$ -	\$ -	\$ -

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.**

As a “smaller reporting company” as defined by Rule 229.10(f)(1), we are not required to provide the information required by this Item 3.

### **ITEM 4. CONTROLS AND PROCEDURES.**

We maintain disclosure controls and procedures (as defined in Rules 13a-15(c) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”)) that are designed to ensure that information required to be disclosed in our reports under the Exchange Act, is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms, 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.

We carried out an evaluation, 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 Exchange Act), as of the end of the period covered by this Quarterly Report. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this Quarterly Report to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities Exchange Commission’s rules and forms, and that such information is accumulated and communicated to our management, including each of such officers as appropriate to allow timely decisions regarding required disclosure.

No change in our internal control over financial reporting occurred during our last fiscal quarter that has materially affected or is reasonably likely to materially affect our internal control over financial reporting. The Company is continually monitoring and assessing the impact of COVID-19 on its internal controls in an effort to ensure that its internal controls respond to any changes in its operating environment.

## **PART II - OTHER INFORMATION**

### **ITEM 1A. RISK FACTORS.**

As of the date of this filing, except as set forth herein, there have been no material changes to the Risk Factors included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2020, filed with the SEC on March 25, 2021, as amended by Amendment No. 1 on Form 10-K/A filed with the SEC on April 29, 2021 (the “2020 Form 10-K”). The Risk Factors set forth in the 2020 Form 10-K should be read carefully in connection with evaluating our business and in connection with the forward-looking statements contained in this Quarterly Report on Form 10-Q. Any of the risks described in the 2020 Form 10-K, could materially adversely affect our business, financial condition or future results and the actual outcome of matters as to which forward-looking statements are made. These are not the only risks we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results.

## **ITEM 5. OTHER INFORMATION**

On October 12, 2021, Timothy McMullen joined the Company as its Chief Operating Officer. In connection with Mr. McMullen's appointment as Chief Operating Officer, the Company and Mr. McMullen entered into an employment agreement (the "McMullen Agreement") to be effective as of October 12, 2021. Pursuant to the McMullen Agreement, Mr. McMullen will have the duties and responsibilities as are commensurate with the positions of Chief Operating Officer, as reasonably and lawfully directed by the CEO. The McMullen Agreement provides for an initial employment term of 12 months, with automatic renewal for an additional 12 months, unless either party provides notice of intention not to renew. As compensation for his role as Chief Operating Officer, the Company will pay Mr. McMullen an annual base salary of \$300,000, provide Mr. McMullen access to the Company's incentive-based bonus plan with the potential to receive a discretionary bonus of up to 55% of his base annual salary, and, from time to time, grant Mr. McMullen certain equity incentive awards, including an initial grant of 150,000 stock options, issued at fair market value with 1/3 of the options eligible to vest annually and all options eligible to vest after three years. In the event Mr. McMullen's employment is terminated by the Company for cause or he resigns without good reason, Mr. McMullen will be entitled to receive his base annual salary prorated to the date of such termination but will not be entitled to any additional compensation or payments by the Company. In the event Mr. McMullen's employment is terminated by the Company without cause or he resigns for good reason, he will be entitled to receive his base annual salary prorated to the date of such termination, the acceleration of all unvested stock options and certain other incentive units, and payment based on an additional six months of the base annual salary.

The foregoing description of the McMullen Agreement does not purport to be complete and is subject to, and qualified in its entirety by, the full text of the McMullen Agreement which was filed as Exhibit 10.1 to the Company's Current Report on Form 8-K filed with the SEC on October 14, 2021.

**ITEM 6. EXHIBITS.**

<b>No.</b>	<b>Item</b>
31.1	<a href="#">Certification of the Chief Executive Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act of 1934, as amended.</a> †
31.2	<a href="#">Certification of the Chief Financial Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act of 1934, as amended.</a> †
32.1	<a href="#">Certification of the CEO and CFO pursuant to Rule 13a-14(b) and Rule 15d-14(b) of the Securities Exchange Act of 1934 and 18 U.S.C. Section 1350.</a> †
101.INS	XBRL Instance Document*
101.SCH	XBRL Taxonomy Extension Schema Document*
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document*
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document*
101.LAB	XBRL Taxonomy Extension Label Linkbase Document*
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document*
104	Cover Page Interactive Data File (embedded within the Inline XBRL document). †

† Filed herewith.

+ Furnished herewith. In accordance with Item 601(b)(32)(ii) of Regulation S-K, this exhibit shall not be deemed “filed” for the purposes of Section 18 of the Securities and Exchange Act of 1934 or otherwise subject to the liability of that section, nor shall it be deemed incorporated by reference in any filing under the Securities Act of 1933 or the Securities Exchange Act of 1934.

\* Pursuant to Rule 406T of Regulation S-T, this XBRL information will not be deemed “filed” for the purpose of Section 18 of the Securities Exchange Act of 1934 or otherwise subject to the liability of that section, nor will it be deemed filed or made a part of a registration statement or prospectus for purposes of Sections 11 and 12 of the Securities Act of 1933, or otherwise subject to liability under those sections.

SIGNATURES

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

CYNERGISTEK, INC.

Date: November 11, 2021

By: /s/ Michael McMillan  
Michael McMillan  
President and Chief Executive Officer  
(Principal Executive Officer)

Date: November 11, 2021

By: /s/ Paul T. Anthony  
Paul T. Anthony  
Chief Financial Officer  
(Principal Accounting Officer)

## CERTIFICATION OF THE CHIEF EXECUTIVE OFFICER PURSUANT TO RULE 13A-14(A) AND RULE 15D-14(A) OF THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED

I, Mac McMillan, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of CynergisTek, Inc. (the “Registrant”);
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: November 11, 2021

/s/ Mac McMillan  
Mac McMillan,  
Chief Executive Officer  
(Principal Executive Officer)

## CERTIFICATION OF THE CHIEF FINANCIAL OFFICER PURSUANT TO RULE 13A-14(A) AND RULE 15D-14(A) OF THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED

I, Paul T. Anthony, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of CynergisTek, Inc. (the “Registrant”);
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: November 11, 2021

/s/ Paul T. Anthony  
Paul Anthony,  
Chief Financial Officer  
(Principal Financial Officer)

CERTIFICATION OF THE CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER PURSUANT TO  
RULE 13A-14(B) AND RULE 15D-14(B) OF THE SECURITIES EXCHANGE ACT OF 1934 AND 18 U.S.C.  
SECTION 1350

In connection with the Quarterly Report of CynergisTek, Inc. (the "Company") on Form 10-Q for the quarter ended September 30, 2021, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), we, Caleb Barlow, Chief Executive Officer and Paul T. Anthony, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to the best of our knowledge:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition of the Company as of the dates presented and the results of operations of the Company for the periods presented.

Date: November 11, 2021

By: /s/ Mac McMillan  
Mac McMillan,  
Chief Executive Officer

By: /s/ Paul T. Anthony  
Paul Anthony,  
Chief Financial Officer

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.

This certification accompanies the Quarterly Report pursuant to Rule 13a-14(b) or Rule 15d-14(b) under the Securities Exchange Act of 1934 and 18 U.S.C. Section 1350 and shall not be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934.