Crexendo, Inc.
Form 10-K
March 06, 2019

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

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2018:
Or
TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Crexendo, Inc.
(Exact name of registrant as specified in its charter)

Nevada	001-32277	87-0591719
(State or Other Jurisdiction of Incorporation or Organization)	(Commission File Number)	(I.R.S. Employer Identification No.)

1615 South 52nd Street, Tempe, AZ 85281
(Address of Principal Executive Office) (Zip Code)

(602) 714-8500
(Registrant's telephone number, including area code)
(Former name, former address and former fiscal year, if changed since last report)

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

Title of each class	Name of each exchange on which registered
Common Stock, par value $0.001 per share	OTCQX Marketplace

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes No

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

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company.

Large accelerated filer		Accelerated filer
Non-accelerated filer	(Do not check if a smaller reporting company)	Smaller reporting company
		Emerging growth company

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

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

The aggregate market value of the common stock held by non-affiliates of the registrant as of December 31, 2018 was approximately $7,451,917.

The number of shares of the registrant's common stock outstanding as of February 28, 2019 was 14,394,113.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the Registrant's 2019 Annual Meeting of Stockholders are incorporated by reference in Part III of this Annual Report on Form 10-K.

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PART I

Throughout this Annual Report, we refer to Crexendo, Inc., together with its subsidiaries, as “we,” “us,” “our Company,” “Crexendo®” or “the Company.” As used in this Annual Report, “Ride The Cloud™” is a registered trademark of our Company in the United States and other countries. All other product names are or may be trademarks of, and are used to identify the products and services of, their respective owners.

THIS ANNUAL REPORT ON FORM 10-K CONTAINS FORWARD-LOOKING STATEMENTS. THESE STATEMENTS RELATE TO FUTURE EVENTS OR OUR FUTURE FINANCIAL PERFORMANCE. IN SOME CASES, YOU CAN IDENTIFY FORWARD-LOOKING STATEMENTS BY TERMINOLOGY SUCH AS “MAY,” “WILL,” “SHOULD,” “EXPECT,” “PLAN,” “INTEND,” “ANTICIPATE,” “BELIEVE,” “ESTIMATE,” “PROJECT,” “PREI “POTENTIAL” OR “CONTINUE” (INCLUDING THE NEGATIVE OF SUCH TERMS), OR OTHER SIMILAR TERMINOLOGY. THESE STATEMENTS ARE ONLY ESTIMATIONS, AND ARE BASED UPON VARIOUS ASSUMPTIONS THAT MAY NOT BE REALIZED. ACTUAL EVENTS OR RESULTS MAY DIFFER MATERIALLY. IN EVALUATING THESE STATEMENTS, YOU SHOULD SPECIFICALLY CONSIDER VARIOUS FACTORS, INCLUDING, BUT NOT LIMITED TO, THE RISKS OUTLINED BELOW UNDER ITEM 1A. THESE FACTORS MAY CAUSE OUR ACTUAL RESULTS TO DIFFER MATERIALLY FROM ANY FORWARD-LOOKING STATEMENT.

ALTHOUGH WE BELIEVE THAT THE ESTIMATIONS REFLECTED IN THE FORWARD-LOOKING STATEMENTS ARE REASONABLE, WE CANNOT GUARANTEE FUTURE RESULTS, LEVELS OF ACTIVITY, PERFORMANCE OR ACHIEVEMENTS. MOREOVER, NEITHER WE NOR ANY OTHER PERSON ASSUMES RESPONSIBILITY FOR THE ACCURACY AND COMPLETENESS OF THE FORWARD-LOOKING STATEMENTS. WE DO NOT INTEND TO UPDATE ANY OF THE FORWARD-LOOKING STATEMENTS AFTER THE DATE OF THIS ANNUAL REPORT TO CONFORM SUCH STATEMENTS TO ACTUAL RESULTS OR TO CHANGES IN OUR EXPECTATIONS, UNLESS REQUIRED BY LAW.

ITEM 1. BUSINESS

OVERVIEW

Crexendo, Inc. is a next-generation CLEC and an award-winning leader and provider of unified communications cloud telecom services, broadband Internet services, and other cloud business services that are designed to provide enterprise-class cloud services to any size business at affordable monthly rates. The Company has two operating segments, which consist of Cloud Telecommunications and Web Services.

Cloud Telecommunications - Our cloud telecommunications services transmit calls using IP or cloud technology, which converts voice signals into digital data packets for transmission over the Internet or cloud. Each of our calling plans provides a number of basic features typically offered by traditional telephone service providers, plus a wide range of enhanced features that we believe offer an attractive value proposition to our customers. This platform enables a user, via a single “identity” or telephone number, to access and utilize services and features regardless of how the user is connected to the Internet or cloud, whether it’s from a desktop device or a mobile device.

We generate recurring revenue from our cloud telecommunications and broadband Internet services. Our cloud telecommunications contracts typically have a thirty-six to sixty month term. We generate product revenue and equipment financing revenue from the sale and lease of our cloud telecommunications equipment. Revenues from the sale of equipment, including those from sales-type leases, are recognized at the time of sale or at the inception of the lease, as appropriate.

Web Services - We generate recurring revenue from website hosting and other professional services.

OUR SERVICES AND PRODUCTS

Our goal is to provide a broad range of cloud-based products and services that nearly eliminate the cost of a businesses' technology infrastructure and enable businesses of any size to more efficiently run their business. By providing a variety of comprehensive and scalable solutions, we are able to cater to businesses of all sizes on a monthly subscription basis without the need for expensive capital investments, regardless of where their business is in its lifecycle. Our products and services can be categorized in the following offerings:

Cloud Telecommunications Services - Our cloud telecommunications service offering includes hardware, software, and unified communication solutions for businesses using IP or cloud technology over any high-speed internet connection. These services are rendered through a variety of devices and user interfaces such as a Crexendo branded desktop phones and/or mobile and desktop applications. Some examples of mobile devices are Android cell phones, iPhones, iPads or Android tablets. These services enable our customers to seamlessly communicate with others through phone calls that originate/terminate on our network or PSTN networks. Our cloud telecommunications services are powered by our proprietary implementation of standards based Web and VoIP cloud technologies. Our services use our highly scalable complex infrastructure that we build and manage based on industry standard best practices to achieve greater efficiencies, better quality of service (QoS) and customer satisfaction. Our infrastructure comprises of compute, storage, network technologies, 3rd party products and vendor relationships. We also develop end user portals for account management, license management, billing and customer support and adopt other cloud technologies through our partnerships.

Crexendo's cloud telecommunication service offers a wide variety of essential and advanced features for businesses of all sizes. Many of these features included in the service offering are:

Business Productivity Features such as dial-by extension and name, transfer, conference, call recording, Unlimited calling to anywhere in the US and Canada, International calling, Toll free (Inbound and Outbound)

Individual Productivity Features such as Caller ID, Call Waiting, Last Call Return, Call Recording, Music/Message-On-Hold, Voicemail, Unified Messaging, Hot-Desking

Group Productivity Features such as Call Park, Call Pickup, Interactive Voice Response (IVR), Individual and Universal Paging, Corporate Directory, Multi-Party Conferencing, Group Mailboxes, Web and mobile devices based collaboration applications

Call Center Features such as Automated Call Distribution (ACD), Call Monitor, Whisper and Barge, Automatic Call Recording, One way call recording, Analytics

Advanced Unified Communication Features such as Find-Me-Follow-Me, Sequential Ring and Simultaneous Ring, Voicemail transcription

Mobile Features such as extension dialing, transfer and conference and seamless hand-off from WiFi to/from 3G and 4G, LTE, as well as other data services. These features are also available on CrexMo, an intelligent mobile application for iPhones and Android smartphones, as well as iPads and Android tablets

Traditional PBX Features such as Busy Lamp Fields, System Hold. 16-48 Port density Analog Devices

Expanded Desktop Device Selection such as Entry Level Phone, Executive Desktop, DECT Phone for roaming users

Advanced Faxing solution such as Cloud Fax (cFax) allowing customers to send and receive Faxes from their Email Clients, Mobile Phones and Desktops without having to use a Fax Machine simply by attaching a file

Web based online portal to administer, manage and provision the system.

Asynchronous communication tools like SMS/MMS, chat and document sharing to keep in pace with emerging communication trends.

Many of these services are included in our basic offering to our customers for a monthly recurring fee and do not require a capital expense. Some of the advanced features such as Automatic Call Recording and Call Center Features require additional monthly fees. Crexendo continues to invest and develop its technology and CPaaS offerings to make them more competitive and profitable.

Website Services - Our website services segment allows businesses to host their websites in our data center for a recurring monthly fee.

SEGMENT INFORMATION

The Company has two operating segments, which consist of Cloud Telecommunications and Web Services. Segment revenue and income (loss) before income tax provision was as follows (in thousands):

	Year Ended December 31,	
		2017
	2018	As Adjusted
Revenue:		
Cloud Telecommunications	$11,083	$9,141
Web Services	825	1,046
Consolidated revenue	$11,908	$10,187

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	Year Ended December 31,	
	2018	2017 As Adjusted
Income/(loss) before income tax provision:		
Cloud Telecommunications	$(608)	$(1,422)
Web Services	400	500
Loss before income tax	$(208)	$(922)

TECHNOLOGY

We believe our proprietary implementation of standard Web, IP, Cloud, Mobile and Internet technologies represent a key component of our business model. We believe these technologies and how we deliver them to our customers distinguish our services and products from the services and products offered by our competitors. Our technology infrastructure and virtual network operation center, all of which is built and managed on industry standard computers, storage, network, data and platforms offers us greater efficiencies while maintaining scalability and redundancy. The synergies between Web and Telecommunication protocols such as TCP/IP, HTTP, XML, SIP and innovations in computing, load balancing, redundancy and high availability of Web and Telecommunications technologies offers us a unique advantage in delivering these services to our customers seamlessly from our data center.

Our Cloud Telecommunications technology is continuously being enhanced with additional features and software functionality. Our current functionality includes:

High-end desktop telephony devices such as Gigabit, PoE, 6 Line Color Phone with 10 programmable buttons and lower end Monochrome 2 Line wall mountable device;

Basic Business Telephony Features such as those offered in a traditional private branch exchange (“PBX”) systems like extension dialing, Direct Inward Dialing (DID), Hold/Resume, Music-On-Hold, Call Transfer (Attended and Unattended), Conferencing, Local, Long Distance, Toll-Free and International Dialing, Voicemail, Auto-Attendant and traditional faxing;

Advanced telephony features such as Call Park, Call Pickup, Paging (through the phones), Overhead paging, Call Recording;

Call Center Functionality such as Agent Log In/Log Out, Whisper, Barge and Call center reporting;

Unified Communications features like Simultaneous Ring, Sequential Ring, Status based Routing (Find-Me-Follow-Me), 10-party instant conference, and Mobile application (CrexMo);

Crexendo Mobile Application (CrexMo), which allows users to place and receive extension calls using Crexendo's network, transfer and conference other users right from their mobile device as if they were in the office. It also provided users instant access to visual voicemail and call logs;

End User Portal and Unified Messaging with Voicemail, Call Recording and eFax inbox.

Collaboration products like group chat, SMS/MMS, document sharing, video and web conferencing

Our website software platform is continuously being enhanced and is an innovative website-building environment. We continue to invest and develop on our Web platform to make it more easy-to-use, enable larger mobile and 3rd party integration features thus enabling our web customers to drive more traffic to their web-sites.

RESEARCH AND DEVELOPMENT

We invested $801,000 and $750,000 for the years ended December 31, 2018 and 2017, respectively, in the research and development of our technologies and data center. The majority of these expenditures were for enhancements to our cloud telecommunications products and services and website development software.

COMPETITION

The market for cloud business communications services is large and increasingly competitive. We expect competition to continue to increase in the future. Some of these competitors include:

traditional on-premise, hardware business communications providers such as Alcatel-Lucent Enterprise, Avaya Inc., Cisco Systems, Inc., Mitel, and Siemens Enterprise Networks, LLC, any of which may now or in the future also host their solutions through the cloud;

software providers such as Microsoft Corporation (Microsoft Teams (formerly Skype for Business)) and BroadSoft, Inc. (acquired by Cisco Systems, Inc.) that generally license their software and may now or in the future also host their solutions through the cloud, and their resellers including major carriers and cable companies;

established communications providers that resell on-premise hardware, software, and hosted solutions, such as AT&T, Verizon Communications Inc., and Comcast Corporation in the United States, TELUS and others in Canada, and BT, Vodafone, and others in the U.K., all of whom have significantly greater resources than us and do now or may in the future also develop and/or host their own or other solutions through the cloud;

other cloud companies such as 8x8, Inc., RingCentral, Inc., Amazon.com, Inc., DialPad, Inc., Fusion, Fuze (formerly Thinking Phone Networks), StarBlue (merger of Star2Star and BlueFace), Intermedia.net, Inc., J2 Global, Inc., Jive Communications, Inc. (acquired by LogMeIn, Inc.), Microsoft Corporation (Microsoft Teams (formerly Skype for Business)), Mitel, Nextiva, Inc., Slack Technologies, Inc., Vonage Holdings Corp., and West Corporation;

other large internet companies such as Alphabet Inc., Facebook, Inc., Oracle Corporation, and Salesforce.com, Inc., any of which might launch its own cloud-based business communication services or acquire other cloud-based business communications companies in the future; and

established contact center providers such as Amazon.com, Inc., Aspect Software, Inc., Avaya Inc., Five9, Inc., Genesys Telecommunications Laboratories, Inc., and NewVoiceMedia.

Additionally, should we determine to pursue acquisition opportunities, we may compete with other companies with similar growth strategies. Some of these competitors may be larger and have greater financial resources than we do. Competition for these acquisition targets could also result in increased prices of acquisition targets and a diminished pool of companies available for acquisition.

There are relatively low barriers to entry into our business. Our proprietary technology does not preclude or inhibit competitors from entering our markets. In particular, we anticipate new entrants will attempt to develop competing products and services or new forums for conducting e-commerce and telecommunications services which could be deemed competition. Additionally, if telecommunications service providers with more resources and name recognition were to enter our markets, they may redefine our industry and make it difficult for us to compete.

Expected technology advances associated with the Cloud, increasing use of the Cloud, and new software products are welcome advancements that we believe will broaden the Cloud’s viability. We anticipate that we can compete successfully by relying on our infrastructure, marketing strategies and techniques, systems and procedures, and by adding additional products and services in the future. We believe we can continue the operation of our business by periodic review and revision to our product offerings and marketing approach.

INTELLECTUAL PROPERTY

Our success depends in part on using and protecting our proprietary technology and other intellectual property. Furthermore, we must conduct our operations without infringing on the proprietary rights of third parties. We also rely upon trade secrets and the know-how and expertise of our key employees. To protect our proprietary technology and other intellectual property, we rely on a combination of the protections provided by applicable copyright, trademark and trade secret laws, as well as confidentiality procedures and licensing arrangements. Although we believe we have taken appropriate steps to protect our intellectual property rights, including requiring employees and third parties who are granted access to our intellectual property to enter into confidentiality agreements, these measures may not be sufficient to protect our rights against third parties. Others may independently develop or otherwise acquire unpatented technologies or products similar or superior to ours.

We license from third parties certain software and Internet tools which we include in our services and products. If any of these licenses were terminated, we could be required to seek licenses for similar software and Internet tools from other third parties or develop these tools internally. We may not be able to obtain such licenses or develop such tools in a timely fashion, on acceptable terms, or at all.

Companies participating in the software, Internet technology, and telecommunication industries are frequently involved in disputes relating to intellectual property. We may be required to defend our intellectual property rights against infringement, duplication, discovery and misappropriation by third parties or to defend against third-party claims of infringement. Likewise, disputes may arise in the future with respect to ownership of technology developed by employees who were previously employed by other companies. Any such litigation or disputes could be costly and divert our attention from our business. An adverse determination could subject us to significant liabilities to third parties, require us to seek licenses from, or pay royalties to, third parties, or require us to develop appropriate alternative technology. Some or all of these licenses may not be available to us on acceptable terms, or at all. In addition, we may be unable to develop alternate technology at an acceptable price, or at all. Any of these events could have a material adverse effect on our business prospects, financial position, or results of operations.

EMPLOYEES

As of December 31, 2018, we had 56 employees; 54 full-time and 2 part-time, including 3 executives, 16 sales representatives and sales management, 9 engineers and IT support, 20 in operations and customer support, 8 in accounting, finance, and legal.

CORPORATE INFORMATION

Crexendo, Inc. was incorporated as a Nevada corporation under the name “Netgateway, Inc.” on April 13, 1995. In November 1999, we were reincorporated under the laws of Delaware. In July 2002, we changed our corporate name to “iMergent, Inc.” In May 2011, our stockholders approved an amendment to our Certificate of Incorporation to change our name from "iMergent, Inc." to "Crexendo, Inc." The name change was effective May 18, 2011. Our ticker symbol "IIG" on the New York Stock Exchange was changed to “EXE” on May 18, 2011. We changed the name to better reflect the scope and direction of our business activities of assisting and providing web-based technology solutions to any size business who are seeking to take advantage of the benefits of conducting business on the cloud. On January 13, 2015, the Company moved to the OTCQX Marketplace and our ticker symbol was changed to “CXDO”. In November 2016, we were reincorporated as a Nevada corporation.

We are headquartered at 1615 South 52nd Street, Tempe, AZ, 85281, and our telephone number is (602) 714-8500. Our website is www.crexendo.com. Our website and the information contained therein or connected thereto shall not be deemed to be incorporated into this Annual Report.

We make available free of charge on or through our Internet website our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to those reports as soon as reasonably practicable after such material is electronically filed with or furnished to the Securities Exchange and Commission (“SEC”).

You may read and copy this Annual Report at the SEC’s public reference room at 450 Fifth Street, NW, Washington D.C. 20549. Information on the operation of the public reference room can be obtained by calling the SEC at 1-800-SEC-0330. The SEC maintains an Internet site that contains reports, proxy and information statements and other information regarding our filings at www.sec.gov.

GOVERNMENTAL REGULATION

As a provider of Internet communications services, we are subject to regulation in the U.S. by the FCC. Some of these regulatory obligations include contributing to the Federal Universal Service Fund, Telecommunications Relay Service Fund and federal programs related to number administration; providing access to E-911 services; protecting customer information; and porting phone numbers upon a valid customer request. We are also required to pay state and local

911 fees and contribute to state universal service funds in those states that assess Internet voice communications services. We are a competitive local exchange carrier (CLEC) in forty-seven states. We are subject to the same FCC regulations applicable to telecommunications companies, as well as regulation by the public utility commission in these states. Specific regulations vary on a state-by-state basis, but generally include the requirement to register or seek certification to provide its services, to file and update tariffs setting forth the terms, conditions and prices for our intrastate services and to comply with various reporting, record-keeping, surcharge collection, and consumer protection requirements.

We are subject to regulations generally applicable to all businesses. We are also subject to an increasing number of laws and regulations directly applicable to telecommunication, internet access and commerce. The adoption of any such additional laws or regulations may decrease the rate of growth of the Internet, which could in turn decrease the demand for our products and services. Such laws may also increase our costs of doing business or otherwise have an adverse effect on our business prospects, financial position or results of operations. Moreover, the applicability to the Internet of existing laws governing issues such as property ownership, libel, and personal privacy is uncertain. Future federal or state legislation or regulation could have a material adverse effect on our business prospects, financial condition and results of operations.

ITEM 1A. RISK FACTORS.

Our quarterly and annual results of operations have fluctuated in the past and may continue to do so in the future. As a result, we may fail to meet or to exceed the expectations of research analysts or investors, which could cause our stock price to fluctuate.

Our quarterly and annual results of operations have varied historically from period to period, and we expect that they will continue to fluctuate due to a variety of factors, some of which are outside of our control, including:

our ability to retain existing customers and resellers, expand our existing customers' user base, and attract new customers;

our ability to introduce new solutions;

the actions of our competitors, including pricing changes or the introduction of new solutions;

our ability to effectively manage our growth;

our ability to successfully penetrate the market for larger businesses;

the mix of annual and multi-year subscriptions at any given time;

the timing, cost, and effectiveness of our advertising and marketing efforts;

the timing, operating cost, and capital expenditures related to the operation, maintenance and expansion of our business;

service outages or information security breaches and any related impact on our reputation;

our ability to accurately forecast revenues and appropriately plan our expenses;

our ability to realize our deferred tax assets;

costs associated with defending and resolving intellectual property infringement and other claims;

changes in tax laws, regulations, or accounting rules;

the timing and cost of developing or acquiring technologies, services or businesses, and our ability to successfully manage any such acquisitions;

adverse weather conditions;

the impact of worldwide economic, political, industry, and market conditions; and,

our ability to maintain compliance with all regulatory requirements.

Any one of the factors above, or the cumulative effect of some or all of the factors referred to above, may result in significant fluctuations in our quarterly and annual results of operations. This variability and unpredictability could result in our failure to meet the expectations of securities analysts or investors for any period, which could cause our stock price to decline. In addition, a significant percentage of our operating expenses is fixed in nature and is based on forecasted revenues trends. Accordingly, in the event of revenue shortfalls, we may not be able to mitigate the negative impact on net income (loss) and margins in the short term. If we fail to meet or exceed the expectations of research analysts or investors, the market price of our shares could fall substantially, and we could face costly lawsuits, including securities class-action suits.

We have incurred operating losses in current and prior periods.

We sustained operating losses in the current and prior years. Our ability to obtain positive cash flows from operating activities will depend on many factors including, but not limited to, our ability to (i) improve sales and marketing efficiencies, (ii) reduce costs, (iii) reach more highly qualified prospects, and (iv) achieve operational improvements. We have incurred operating losses in each of the three prior years and may incur operating losses in the foreseeable future. Continued losses could cause a determination that a “going concern option” should be applied to us.

Fluctuations in our operating results may affect our stock price and ability to raise capital.

Our operating results for any given quarter or fiscal year should not be relied upon as an indication of future performance. Our future results will fluctuate, and those results may fall below the expectations of investors and may cause the trading price of our common stock to fall. This may impair our ability to raise capital, should we seek to do so. Our quarterly results may fluctuate based on, including but not limited to our sales results, marketing, management, our ability to compete, pricing, and other risk factors contained in this section.

Our Chief Executive Officer owns a significant amount of our common stock and could exercise substantial corporate control. There may be limited ability to sell the company absent the consent of the CEO.

Steven G. Mihaylo, Chief Executive Officer (“CEO”) of Crexendo, Inc., owns 70% of the outstanding shares of our common stock based on the number of shares outstanding as of December 31, 2018. As a result, Mr. Mihaylo would have the ability to determine the outcome of matters submitted to our stockholders for approval, including the election of directors and any merger, amalgamation, consolidation or sale of all or substantially all of our assets. Mr. Mihaylo may have the ability to control the management and affairs of our Company. As a “control company” it may not be required that the company maintains an independent board. As a director and officer, Mr. Mihaylo owes a fiduciary duty to our stockholders. As a stockholder, Mr. Mihaylo is entitled to vote his shares, in his own interests, which may not always be in the interests of our stockholders generally. Accordingly, even though certain transactions may be in the best interests of other stockholders, this concentration of ownership may harm the market price of our common stock by, among other things, delaying, deferring or preventing a change in control of our Company, impeding a merger, amalgamation, consolidation, takeover or other business combination involving our Company, or discouraging a potential acquirer from making a tender offer or otherwise attempting to obtain control of our Company.

In addition, sales or other dispositions of our shares by Mr. Mihaylo may depress our stock price. Sales of a significant number of shares of our common stock in the public market could harm the market price of our common stock. As additional shares of our common stock become available for resale in the public market, the supply of our common stock will increase, which could result in a decrease in the market price of our common stock.

Some of the provisions of our certificate of incorporation and bylaws could make it more difficult for a third party to acquire us, even if doing so might be beneficial to our stockholders by providing them with the opportunity to sell their shares at a premium to the then market price. Our bylaws contain provisions regulating the introduction of business at annual stockholders' meetings by anyone other than the board of directors. These provisions may have the effect of making it more difficult, delaying, discouraging, preventing or rendering costlier an acquisition or a change in control of our Company.

Our securities have been thinly traded. An active trading market in our equity securities may cease to exist, which would adversely affect the market price and liquidity of our common stock, in addition our stock price has been subject to fluctuating prices.

Our common stock is traded exclusively in the over-the-counter market. We cannot predict the actions of market makers, investors or other market participants, and can offer no assurances that the market for our securities will be stable. If there is no active trading market in our equity securities, the market price and liquidity of the securities will be adversely affected. The market price of our common stock could decline as a result of sales of a large number of shares of our common stock in the market or the perception that these sales could occur. These sales also might make it more difficult for us to sell equity securities in the future at a time and at a price that we deem appropriate. As of February 28, 2019, we had outstanding 14,394,113 shares of common stock.

Additional dilution will result if outstanding options to acquire shares of our common stock are exercised. In addition, in the event future financings are required they could be convertible into or exchangeable for our equity securities, investors may experience additional dilution.

Lack of sufficient stockholder equity or continued losses from operations could subject us to fail to comply with the listing requirements of the OTCQX, if that occurred, the price of our common stock and our ability to access the capital markets could be negatively impacted, and our business will be harmed. We currently do not meet the minimum listing requirement for the NYSE or NASDAQ.

Our common stock is currently listed on OTCQX. We have had annual losses from continuing operations for the last five years with the possibility of continued losses. While at current such losses would not impact our listing with OTCQX requirement may change from time to time and it is possible we may not remain in compliance with the minimum condition of OTCQX listing standards. Delisting from the OTCQX could negatively affect the trading price of our stock and could also have other negative results, including the potential loss of confidence by suppliers and employees, the failure to attract the interest of institutional investors, and fewer business development opportunities. At present we do not meet the minimum listing requirements for the New York Stock Exchange (NYSE) or the NASDAQ Stock Exchange (NASDAQ) which may make raising capital, issuing additional securities or using the securities of the Company to effect acquisitions or merger more difficult or expensive.

We may undertake acquisitions, mergers or change to our capital structure to expand our business, which may pose risks to our business and dilute the ownership of our existing stockholders.

As part of a potential growth strategy, we may attempt to acquire or merge with certain businesses. Whether we realize benefits from any such transactions will depend in part upon the integration of the acquired businesses; the performance of the acquired products, services and capacities of the technologies acquired, as well as the personnel hired in connection therewith. Accordingly, our results of operations could be adversely affected from transaction-related charges, amortization of intangible assets, and charges for impairment of long-term assets. While we believe that we have established appropriate and adequate procedures and processes to mitigate these risks, there can be no assurance that any potential transaction will be successful.

In addition, the financing of any acquisition may require us to raise additional funds through public or private sources. Additional funds may not be available on terms that are favorable to us and, in the case of equity financings, may result in dilution to our stockholders. Future acquisitions by us could also result in large and immediate write-offs or assumptions of debt and contingent liabilities, any of which may have a material adverse effect on our consolidated financial position, results of operations, and cash flows.

Our ability to use our net operating loss carry-forwards may be reduced in the event of an ownership change, and could adversely affect our financial results.

As of December 31, 2018, we had net operating loss (“NOL”) carry-forwards of approximately $22,722,000, of which $5,761,000 is subject to Section 382 limitations. Section 382 of the Internal Revenue Code, as amended (the “Code”) imposes limitations on a corporation’s ability to utilize its NOL carry-forwards. In general terms, an ownership change results from transactions increasing the ownership of certain stockholders in the stock of a corporation by more than 50% over a three-year period. Since our formation, we have issued a significant number of shares, and purchasers of those shares have sold some of them, resulting in two ownership changes, as defined by Code Section 382. As a result of the last ownership change, utilization of our NOL is subject to an annual limitation determined by multiplying the value of our stock at the time of the ownership change by the applicable federal long-term tax-exempt rate. The annual limitation is approximately $461,000. Any limited amounts may be carried over into later years, and the amount of the limitation may, under certain circumstances, be increased by the “recognized built-in gains” that occur during the five-year period after the ownership change (the recognition period). Future changes in ownership of more than 50% may also limit the use of these remaining NOL carry-forwards. Our earnings, if any, and cash resources would be materially and adversely affected if we cannot receive the full benefit of the remaining NOL carry-forwards. An ownership change could occur as a result of circumstances that are not within our control.

The telecommunications industry is highly competitive. We face intense competition from traditional telephone companies, wireless companies, cable companies and alternative voice communication providers and other VoIP companies.

Our Cloud telecommunications services compete with other voice over internet protocol (VoIP) providers. In addition, we also compete with traditional telephone service providers which provide telephone service based on the public switched telephone network (PSTN). Our VoIP offering is not fully compatible with such customers. Some of these traditional providers have also added VoIP services. There is also competition from cable providers, which have added VoIP service offerings in bundled packages to their existing cable customers. The telecommunications industry is highly competitive. We face intense competition from traditional telephone companies, wireless companies, cable companies, and alternative voice communication providers.

Most traditional wire line and wireless telephone service providers, cable companies, and some VoIP providers are substantially larger and better capitalized than we are and have the advantage of a large existing customer base. Because most of our target customers are already purchasing communications services from one or more of these providers, our success is dependent upon our ability to attract target customers away from their existing providers. Our competitors’ financial resources may allow them to offer services at prices below cost or even for free in order to maintain and gain market share or otherwise improve their competitive positions.

The markets for our products and services are continuing to evolve and are increasingly competitive. Demand and market acceptance for recently introduced and proposed new products and services and sales of such products and services are subject to a high level of uncertainty and risk. Our business may suffer if the market develops in an unexpected manner, develops more slowly than in the past or becomes saturated with competitors, if any new products and services do not sustain market acceptance. A number of very large, well-capitalized, high profile companies serve the e-commerce, VoIP and Cloud technology markets. If any of these companies entered our markets in a focused and concentrated fashion, we could lose customers, particularly more sophisticated and financially stable customers.

Our VoIP or cloud telecommunications service competes against established well financed alternative voice communication providers, (such as 8x8 and Ring Central) who may provide comparable services at comparable or lower pricing.

Pricing in the telecommunications industry is very fluid and competitive. Price is often a substantial motivation factor in a customer's decision to switch to our telephony products and services. Our competitors may reduce their rates which may require us to reduce our rates, which would affect our margins and revenues, or otherwise make our pricing non-competitive. We may be at a disadvantage compared with those competitors who have substantially greater resources than us or may otherwise be better positioned to withstand an extended period of downward pricing pressure.

Many of our current and potential competitors have longer operating histories, significantly greater resources and brand awareness, and a larger base of customers than we have. As a result, these competitors may have greater credibility with our existing and potential customers. Our competitors may also offer bundled service arrangements that present a more differentiated or better integrated product to customers. Announcements, or expectations, as to the introduction of new products and technologies by our competitors or us could cause customers to defer purchases of our existing products, which also could have a material adverse effect on our business, financial condition or operating results.

Changes to rates by our suppliers, competitors and increasing regulatory charges may require us to raise prices which could impact results.

Pricing in the telecommunications industry is very fluid and competitive. Price is often a substantial motivating factor in a customer's decision to switch to our cloud telecommunications products and services. Our competitors may reduce their rates which may require us to reduce our rates, which would affect our margins and revenues, or otherwise make our pricing non-competitive. Our upstream carriers, suppliers and vendors may increase their rates thus directly impacting our cost of sales, which would affect our margins. Interconnected VoIP traffic may be subject to increased charges. Should this occur, the rates paid to our underlying carriers may increase which could reduce our profitability. Changes in our underlying costs of sales may increase rates we charge our customers which could make us less competitive and impact our sales and retention of existing customers.

We have targeted sales to mid-market and larger enterprise customers. Not properly managing these customers could negatively affect our business, margins, cash flow and operations.

Selling to larger enterprise customers contains inherent risks and uncertainties. Our sales cycle has become more time-consuming and expensive. The delays associated with closing and installing larger customers may impact results on a quarter to quarter basis. There may be additional pricing pressure in this market which may affect margins and profitability. Revenue recognition may be delayed for some complex transactions, all of which could harm our business and operating results. The loss of a large customer may have a material negative impact on quarterly or annual results.

Multi-location users require additional and expensive customer service which may require additional expense and impact margins on enterprise sales. Enterprise customers may demand more features, integration services and customization which require additional engineering and operational time which could impact margins on an enterprise sale. Multi-location enterprise customer sales may have different requirement in different locations which may be difficult to fulfill or satisfy various interests which could result in cancellations.

Enterprise customers might demand we provide service locations internationally where we may encounter technical, logistical, infrastructure and regulatory limitations on our ability to implement or deliver our services. Our inability to provide service in certain international locations may result in a cancellation of the entire contract. Further with larger enterprise customer sales, the risk of customers transporting desktop devices internationally without our knowledge may increase.

Sales to small and medium-sized businesses face risks as they may have fewer financial resources to weather an economic downturn.

A substantial percentage of our revenues come from small and medium-sized businesses. These customers may be more adversely affected by economic downturns than larger, more established businesses. The majority of our customers pay for our subscriptions with credit and debit cards. Weakness in certain segments of the credit markets and in the U.S. and global economies may result in increased numbers of rejected credit and debit card payments, which could negatively affect our business. If small and medium-sized businesses experience financial hardship as a result of a weak economy, industry consolidation, or any other reason, the overall demand for our subscriptions could be materially and adversely affected.

We must acquire new customers on an ongoing basis to maintain and increase our customers and revenues.

We will have to acquire new customers in order to increase revenues. We incur significant costs to acquire new customers, and those costs are an important factor in determining our profitability. Therefore, if we are unsuccessful in retaining customers or are required to spend significant amounts to acquire new customers beyond those budgeted, our revenue could decrease, which could prevent us from reaching profitability and have our net loss increase. Marketing expenditures are an ongoing requirement and will become a larger ongoing requirement of our business.

If we do not successfully expand our sales including our partner channel program and direct sales, we may be unable to substantially increase our sales.

We sell our products primarily through direct sales and our partner channel, and we must substantially expand the number of partners and producing direct sales personnel to increase organic revenue substantially. If we are unable to expand our partner channel network and hire and retain qualified sales personnel, our ability to increase our organic revenue and grow our business could be compromised. The challenge of attracting, training, and retaining qualified candidates, may make it difficult to grow revenue.

We face risks in our sales to certain market segments including, but not limited to, sales subject to HIPPA Regulations.

We have sold and will continue to attempt to sell to certain customer segments which may have requirements for additional privacy or security. In addition sales may be made to customers that are subject to additional security requirements and or HIPPA requirements. Selling into segments with additional requirements increases potential liability which in some instances may be unlimited. While the Company believes it meets or exceeds all requirements for sales into such segments, there is no assurance that the Company systems fully comply with all requirements. Our customers can use our services to store contact and other personal or identifying information, and to process, transmit, receive, store and retrieve a variety of communications and messages, including information about their own customers and other contacts. In addition, customers may use our services to store protected health information, or PHI, that is protected under the Health Insurance Portability and Accountability Act, or HIPAA, Noncompliance with laws and regulations relating to privacy and HIPAA may lead to significant fines, penalties or civil liability.

Our collection, processing, storage, use, and transmission of personal data could give rise to liabilities as a result of governmental regulation, conflicting legal requirements, differing views on data privacy, or security breaches.

We collect, process, store, use, and transmit personal data on a daily basis. Personal data is increasingly subject to legal and regulatory protections around the world, which vary widely in approach and which possibly conflict with one another. In recent years, for example, U.S. legislators and regulatory agencies, such as the Federal Trade Commission, as well as U.S. states have increased their focus on protecting personal data by law and regulation and have increased enforcement actions for violations of privacy and data protection requirements. The European Commission also recently approved and adopted the GDPR, a new data protection law, which took effect beginning in May 2018. These data protection laws and regulations are intended to protect the privacy and security of personal data, including credit card information that is collected, processed, and transmitted in or from the relevant jurisdiction. Implementation of and compliance with these laws and regulations may be more costly or take longer than we anticipate, or could otherwise adversely affect our business operations, which could negatively impact our financial position or cash flows. Further, we have taken the position that the cost involved in continually protecting data under GDPR was exorbitant compared to the small revenue received from Countries subject to GDPR. As a consequence, we stopped hosting websites in GDPR-complaint Countries or Countries from which the bulk of business came from Countries subject to GDPR. We also took steps to block those Countries from accessing any other sites we host. Additionally, media coverage of data breaches has escalated, in part because of the increased number of enforcement actions, investigations, and lawsuits. As this focus and attention on privacy and data protection increases, we also risk exposure to potential liabilities and costs resulting from compliance with or any failure to comply with applicable legal requirements, conflicts among these legal requirements, or differences in approaches to privacy.

We could be liable for breaches of security on our website, fraudulent activities of our users, or the failure of third-party vendors to deliver credit card transaction processing services.

We engage in electronic billing and processing of our customers using secure transmission of sometimes confidential information over public networks. We have systems and processes in place that we deem more than sufficient and industry standard that are designed to protect consumer information and prevent fraudulent credit card transactions and other security breaches. Our failure to protect against fraud or breaches may subject us to costly breach notification and other mitigation obligations, class action lawsuits, investigations, fines, forfeitures, or penalties from governmental agencies that could adversely affect our operating results. We may be unable to prevent our customers from fraudulently receiving goods and services. Our liability could also increase if a large fraction of transactions using our services involve fraudulent or disputed credit card transactions. We may also experience losses due to subscriber fraud and theft of service. Subscribers have, in the past, obtained access to our service without paying for monthly service and international toll calls by unlawfully using fraudulently obtained codes. If our existing anti-fraud procedures are not adequate or effective, consumer fraud and theft of service could have a material adverse effect on our business, financial condition, and operating results.

We face risks in our strategy of designing and developing our own desktop telephones (”desktop devices”).

We continue to primarily sell Crexendo ® branded desktop devices, although, the Company also supports third party devices manufactured by Yealink, Cisco, and Polycom. Our desktop devices are being manufactured by third party vendors in China. The Crexendo branded desktop devices include firmware specifically designed for our cloud telecommunications services. If the phones are successfully manufactured there is no assurance of the acceptance of the desktop devices. Successful roll out is not guaranteed and is contingent on various factors including but not limited to; meeting certain industry standards, the availability of our vendors to meet agreed terms, supply from vendors being sufficient to meet demand, industry acceptance of the desktop devices, desktop devices meeting the needs of our customers, competitive pricing of the desktop devices, feature set of the desktop devices being up to competitive standards, regulatory approval as required of the desktop devices and competitor claims relating to the desktop devices. Our failure to be able to fully implement the sale of the Crexendo desktop devices or the inability to have desktop devices manufactured to meet our supply needs may cause us damage as well as require us to have to purchase desktop devices from other suppliers at a higher price which could affect sales and margins. Our desktop devices come preloaded with our firmware and are not currently intended to work with other competitors’ or vendors' services.

Our churn rate may increase in future periods due to customer cancellations or other factors, which may adversely impact our revenue or require us to spend more money to grow our customer base.

Our customers generally have initial service periods of between three and five year and may discontinue their subscriptions for our services after the expiration of their initial subscription period. In addition, our customers may renew for lower subscription amounts or for shorter contract lengths. We may not accurately predict cancellation rates for our customers. Our cancellation rates may increase or fluctuate because of a number of factors, including customer usage, pricing changes, number of applications used by our customers, customer satisfaction with our service, the acquisition of our customers by other companies and deteriorating general economic conditions. If our customers do not renew their subscriptions for our service or decrease the amount they spend with us, our revenue will decline, and our business will suffer.

Our rate of customer cancellations may increase in future periods due to many factors, some of which are beyond our control, such as the financial condition of our customers or the state of credit markets. In addition, a single, protracted service outage or a series of service disruptions, whether due to our services or those of our bandwidth carriers, may result in a sharp increase in customer cancellations.

If we do not successfully expand our physical infrastructure and build diverse geo redundant locations, which require large investments, we may be unable to substantially increase our sales and retain customers.

Our ability to provide cloud telecommunications services is dependent upon on our physical and cloud based infrastructure. While most of our physical equipment required for providing these services is redundant in nature and offers high availability, certain types of failures or malfunctioning of critical hardware/software equipment, including but not limited to fire, water or other physical damage may impact our ability to deliver continuous service to our customers. Act of God or terrorism or vandalism or gross negligence of person(s) currently or formerly associated with the company may result in loss of revenue, profitability and retaining and acquiring new customers.

Our ability to recover from disasters, if and when they occur is paramount to offer continued service to our existing customers. In addition to our physical infrastructure, we have a cloud infrastructure deployment with AWS to provide continuous service to our customers in the event of a disaster or failure of our physical infrastructure. If our third-party service providers fail to maintain these facilities properly, or fail to respond quickly to problems, our customers may experience service interruptions. The failure of any of these third party service providers to properly maintain services may be subject to factors including but not limited to the following: (i) cause a loss of customers, (ii) adversely affect our reputation, (iii) cause negative publicity, (iv) negatively impact our ability to acquire customers, (v) negatively impact our revenue and profitability, (vi) potential law suits for not reaching E-911 services, and (vii) potential law suits for loss of business and loss of reputation.

We may not be able to scale our business efficiently or quickly enough to meet our customers' growing needs, in which case our operating results could be harmed.

As usage of our cloud telecommunications services by mid-market and larger distributed enterprises expands and as customers continue to integrate our services across their enterprises, we are required to devote additional resources to improving our application architecture, integrating our products and applications across our technology platform as well as expanding integration and performance. We will need to appropriately scale our internal business systems and our services organization, including customer support and services and regulatory compliance, to serve a growing customer base. Any failure of or delay in these efforts could cause to prevent acquisition of customers, impaired system performance and reduced customer satisfaction. These issues could result in decreased sales to new customers, lower renewal rates by existing customers, which could hurt our revenue growth and our reputation. We cannot be sure that the expansion and improvements to our infrastructure and systems will be fully or effectively implemented on a timely basis, if at all. These efforts may reduce revenue and our margins and adversely impact our financial results.

Our success depends in part upon the capacity, reliability, and performance of our network infrastructure, including the capacity provided by our Internet bandwidth suppliers.

We depend on these companies to provide uninterrupted and error-free service. Some of these providers are also our competitors. We do not have control over these providers. We may be subject to interruptions or delays in network service. If we fail to maintain reliable bandwidth or performance that could significantly reduce customer demand for our services and damage our business.

Our success depends in part upon the capacity, reliability, and performance of our telecom carriers, and their network infrastructure, including the capacity provided by our Tier 1 and non-Tier 1 Telecom suppliers for Telecom Origination and Termination Services

We depend on these companies to provide uninterrupted and error-free service telecom services, sourcing of DIDs, porting of numbers and delivering telephone calls from and to endpoints and devices on our network. Some of these providers are also our competitors. We do not have control over these providers. We may be subject to interruptions or delays in their service. If we fail to maintain reliable connectivity or performance with our upstream carriers it could then significantly reduce customer demand for our services and damage our business.

Our ability to provide telecommunications services is dependent upon third-party facilities and equipment, the failure of which could cause delays or interruptions of our service and impact our revenue and profitability.

Our ability to provide quality and reliable cloud telecommunications service is in part dependent upon the proper functioning of facilities and equipment owned and operated by third parties and is, therefore, beyond our control. Our cloud telecommunications service (and to a lesser extend our e-commerce services) requires our customers to have an operative broadband Internet connection and an electrical power supply, which are provided by the customer’s Internet service provider and electric utility company and not by us. The quality of some broadband Internet connections may be too poor for customers to use our services properly. In addition, if there is any interruption to a customer’s broadband Internet service or electrical power supply, that customer will be unable to make or receive calls, including emergency calls (our E-911 service), using our service. We outsource several of our network functions to third-party providers. If our third-party service providers fail to maintain these facilities properly, or fail to respond quickly to problems, our customers may experience service interruptions. The failure of any of these third party service providers to properly maintain services may be subject to factors including but not limited to the following: (i) cause a loss of customers, (ii) adversely affect our reputation, (iii) cause negative publicity, (iv) negatively impact our ability to acquire customers, (v) negatively impact our revenue and profitability, (vi) potential law suits for not reaching E-911 services, and (vii) potential law suits for loss of business and loss of reputation.

We rely on third parties to provide a portion of our customer service responses, initiate local number portability for our customers, deliver calls to and from PSTN and other public telephone VoIP/Wireless service providers and provide aspects of our E-911 service.

We offer our cloud telecommunications customers support 24 hours a day, seven days a week. We may rely on third parties (sometimes outside of the U.S) to respond to customer inquiries. These third-party providers generally represent us without identifying themselves as independent parties. The ability of third-party providers to provide these representatives may be disrupted due to issues outside our control.

We also maintain an agreement with an E-911 provider to assist us in routing emergency calls directly to an emergency service dispatcher at the PSAP in the area of the customer’s registered location and terminating E-911 calls. We also contract with a provider for the national call center that operates 24 hours a day, seven days a week to receive certain emergency calls and with several companies that maintain PSAP databases for the purpose of deploying and operating E-911 services. The dispatcher will have automatic access to the customer's telephone number and registered location information. If a customer moves their Crexendo service to a new location, the customer's registered location information must be updated and verified by the customer. Until that takes place, the customer will have to verbally advise the emergency dispatcher of his or her actual location at the time of an emergency 9-1-1 call. This can lead to delays in the delivery of emergency services

Interruptions in service from these vendors could also cause failures in our customers’ access to E-911 services and expose us to liability.

We also have agreements with companies that initiate our local number portability, which allow new customers to retain their existing telephone numbers when subscribing to our services. We will need to work with these companies to properly port numbers. The failure to port numbers may subject us to loss of customers or regulatory review.

If any of these third parties do not provide reliable, high-quality service, our reputation and our business will be harmed. In addition, industry consolidation among providers of services to us may impact our ability to obtain these services or increase our expense for these services.

Our dependence on outside contractors and third-party agents for fulfillment of certain items and critical manufacturing services could result in product or delivery delays and/or damage our customer relations.

We outsource the manufacturing of certain products we sell and products we provide. We submit purchase orders to agents or the companies that manufacture the products. We describe, among other things, the type and quantities of products or components to be supplied or manufactured and the delivery date and other terms applicable to the products or components. Our suppliers or manufacturers potentially may not accept any purchase order that we submit. Our reliance on outside parties involves a number of potential risks, including: (i) the absence of adequate capacity, (ii) the unavailability of, or interruptions in access to, production or manufacturing processes, (iii) reduced control over delivery schedules, (iv) errors in the product, and (v) claims of third party intellectual infringement or defective merchandise. If delays, problems or defects were to occur, it could adversely affect our business, cause claims for damages to be filed against us, and negatively impact our consolidated operations and cash flows.

Errors in our technology or technological issues outside our control could cause delays or interruptions to our customers.

Our services (including cloud telecommunications and e-commerce) may be disrupted by problems with our technology and systems such as malfunctions in our software or facilities. In addition there may be service interruptions for reasons outside our control. Our customers and potential customers subscribing to our services have experienced interruptions in the past and may experience interruptions in the future as a result of these types of problems. Interruptions could cause us to lose customers and offer customer credits, which could adversely affect our revenue and profitability. Network and Telecommunication interruptions may also impair our ability to sign-up new customers. In addition since our systems and our customers' ability to use our services are Internet-dependent, our services may be subject to "cyber-attacks" from the Internet, which could have a significant impact on our systems and services. Our customers' ability to use our services is dependent on third-party internet providers which may suffer service disruptions. If service interruptions adversely affect the perceived reliability of our service, we may have difficulty attracting and retaining customers and our growth may suffer.

Our operations could be hurt by a natural disaster, network security breach, or other catastrophic event.

We maintain a fully redundant physical infrastructure in our data center in Tempe, Arizona and a cloud infrastructure deployment with AWS for disaster recovery. This system does not guarantee continued reliability if a catastrophic event occurs. Despite implementation of network security measures, our servers may be vulnerable to computer viruses, break-ins, and similar disruptions from unauthorized tampering with our computer systems including, but not limited to, denial of service attacks. In addition, if there is a breach or alleged breach of security or privacy involving our services including but not limited to data loss, or if any third party undertakes illegal or harmful actions using our communications or e-commerce services, our business and reputation could suffer substantial adverse publicity and impairment. We have experienced interruptions in service in the past. While we do not believe that we have lost customers as a consequence, the harm to our reputation is difficult to assess. We have taken and continue to take steps to improve our infrastructure to prevent service interruptions.

Failure in our data center or services could lead to significant costs and disruptions.

All data centers, including ours, are subject to various points of failure. Problems with cooling equipment, generators, uninterruptible power supply, routers, switches, or other equipment, whether or not within our control, could result in service interruptions for our customers as well as equipment damage. Any failure or downtime could affect a significant percentage of our customers. The total destruction or severe impairment of our data center facilities could result in significant downtime of our services and the loss of customer data.

Internet security issues and growing Cyber threats pose risks to the development of e-commerce and our business.

Security and privacy concerns may inhibit the growth of the Internet and other online services generally, especially as a means of conducting commercial transactions.

We could experience security breaches in the transmission and analysis of confidential and proprietary information of the consumer, the merchant, or both, as well as our own confidential and proprietary information.

Anyone able to circumvent security measures could misappropriate proprietary information or cause interruptions in our operations, as well as the operations of the merchant. We may be required to expend significant capital and other resources to protect against security breaches or to minimize problems caused by security breaches. To the extent that we experience breaches in the security of proprietary information which we store and transmit, our reputation could be damaged and we could be exposed to a risk of loss or litigation.

We collect personal and credit card information from our customers and employees could misuse this information.

The PCI Data Security Standard ("PCI DSS") is a specific set of comprehensive security standards required by credit card brands for enhancing payment account data security, including but not limited to requirements for security management, policies, procedures, network architecture, and software design. We maintain credit card and other personal information in our systems. Due to the sensitive nature of retaining such information we have implemented policies and procedures to preserve and protect our data and our customers' data against loss, misuse, corruption, misappropriation caused by systems failures, unauthorized access, or misuse. Notwithstanding these policies, we could be subject to liability claims by individuals and customers whose data resides in our databases for the misuse of that information. While the Company believes its systems meet or exceed industry standards, the Company does not believe it is required to meet PCI level 1 compliance and has not certified under that level. Failure to meet PCI compliance levels could negatively impact the Company's ability to collect and store credit card information which could cause substantial disruption to our business. Notwithstanding the results of this assessment there can be no assurance that payment card brands will not request further compliance assessments or set forth additional requirements to maintain access to credit card processing services, which could incur substantial additional costs and could have a material adverse effect on our business.

We depend upon industry standard protocols, best practices, solutions, third-party software, technology, tools including but not limited to Open Source software.

We rely on non-proprietary third party licensing and software some of which may be Open Source and protected under various licensing agreements. We may be subject to additional royalties, license or trademark infringement costs or other unknown costs when one or more of these third-party technologies are affected or need to be replaced due to end-of-support or end-of-sale of such third parties.

We may incur substantial expenses in defending against third-party patent and trademark infringement claims regardless of their merit.

From time to time, parties may assert patent infringement claims against us in the form of letters, lawsuits, and other forms of communication. Third parties may also assert claims against us alleging infringement of copyrights, trademark rights, trade secret rights or other proprietary rights or alleging unfair competition. If there is a determination that we have infringed third-party proprietary rights, we could incur substantial monetary liability and be prevented from using the rights in the future.

We depend on our senior management and other key personnel, and a loss of these individuals could adversely impact our ability to execute our business plan and grow our business.

We depend on the continued services of our key personnel, including our Officers and certain engineers. Each of these individuals has acquired specialized knowledge and skills with respect to our operations. The loss of one or more of these key personnel could negatively impact our performance. In addition, we expect to hire additional personnel as we continue to execute our strategic plan, particularly if we are successful in expanding our operations. Competition for the limited number of qualified personnel in our industry is intense. At times, we have experienced difficulties in hiring personnel with the necessary training or experience.

Our public filings are subject to review by the SEC.

Our SEC filings are reviewed by the SEC from time to time and any significant changes required as a result of any such review may result in material liability to us and have a material adverse impact on the trading price of our common stock.

Examinations by relevant tax authorities may result in material changes in related tax reserves for tax positions taken in previously filed tax returns or may impact the valuation of certain deferred income tax assets, such as net operating loss carry-forwards.

Based on the outcome of examinations by relevant tax authorities, or as a result of the expiration of statutes of limitations for specific jurisdictions, it is reasonably possible that the related tax reserves for tax positions taken regarding previously filed tax returns will materially change from those recorded in our financial statements. In addition, the outcome of examinations may impact the valuation of certain deferred income tax assets (such as net operating loss carry-forwards) in future periods. It is not possible to estimate the impact of the amount of such changes, if any, to previously recorded uncertain tax positions.

Changes in our business model and sales strategies may adversely impact revenue.

When the Company shifted away from a seminar sales model, our web services revenue was adversely impacted. Our website hosting revenue has continued to decline since we no longer sell our website development software through a seminar sales model. The Company is not actively marketing its website development software or website hosting services. Our web services segment revenue may continue to decline over time as more competitors enter the website building and hosting industry.

From time to time we had been the subject of governmental inquiries and investigations related to our discontinued seminar sales model and business practices that could require us to pay refunds, damages or fines, which could negatively impact our financial results or ability to conduct business. We have received customer complaints and civil actions.

From time to time, we received inquiries from federal, national, state, city and local government officials in the various jurisdictions in which we operated. These inquiries had historically been related to our discontinued seminar sales practices. There is still the potential of review of past sales and sales of our current web and telecom services. We respond to these inquiries and have generally been successful in addressing the concerns of these persons and entities, without a formal complaint or charge being made, although there is often no formal closing of the inquiry or investigation. The ultimate resolution of these or other inquiries or investigations may have a material adverse effect on our business or operations, or a formal complaint could be initiated. During the ordinary course of business, we also receive a number of complaints and inquiries from customers, governmental and private entities. In some cases, these complaints and inquiries from agencies and customers have ended up in civil court. We may continue to receive customer and agency claims and actions.

Changes in laws and regulations and the interpretation and enforcement of such laws and regulations could adversely impact our financial results or ability to conduct business.

We are subject to a variety of federal and state laws and regulations as well as oversight from a variety of governmental agencies and public service commissions. The laws governing our business may change in ways that harm our business. Federal or state governmental agencies administering and enforcing such laws may also choose to interpret and apply them in ways that harm our business. These interpretations are also subject to change. Regulatory action could materially impair or force us to change our business model and may adversely affect our revenue, increase our compliance costs, and reduce our profitability. In addition, governmental agencies such as the SEC, Internal Revenue Service (IRS), Federal Trade Commission (FTC), Federal Communication Commission (FCC) and state taxing authorities may conclude that we have violated federal laws, state laws or other rules and regulations, and we could be subject to fines, penalties or other actions that could adversely impact our financial results or our ability to conduct business.

The FCC net neutrality rules have changed. We cannot predict the effect of this, nor the impact of this change on our business.

On January 4, 2018, the Federal Communications Commission, or FCC, released an order that largely repeals rules that the FCC had in place which prevented broadband internet access providers from degrading or otherwise disrupting a broad range of services provisioned over consumers' and enterprises' broadband internet access lines. There are efforts in Congress to prevent the Order from becoming effective and a number of state attorneys general have filed an appeal of the FCC's January 4, 2018 order. We cannot predict whether the FCC's January 4, 2018 order will remain effective. Many of the largest providers of broadband services, like cable companies and traditional telephone companies, have publicly stated that they will not degrade or disrupt their customers' use of applications and services, like ours. If such providers were to degrade, impair, or block our services, it would negatively impact our ability to provide services to our customers, likely result in lost revenue and profits, and we would incur legal fees in attempting to restore our customers' access to our services. Broadband internet access providers may also attempt to charge us or our customers additional fees to access services like ours that may result in the loss of customers and revenue, decreased profitability, or increased costs to our offerings that may make our services less competitive. We cannot predict the potential impact of the FCC's January 4, 2018 order on us at this time.

Our Telecommunications services are required to comply with industry standards, FCC regulations, privacy laws as well as certain State and local jurisdiction specific regulations failure to comply with those may subject us to penalties and may also require us to modify existing products and/or service.

The acceptance of telecommunications services is dependent upon our meeting certain industry standards. We are required to comply with certain rules and regulations of the FCC regarding safety standards. Standards are continuously being modified and replaced. As standards evolve, we may be required to modify our existing products or develop and support new versions of our products. We must comply with certain federal, state, and local requirements regarding how we interact with our customers, including marketing practices, consumer protection, privacy, and billing issues, the provision of 9-1-1 emergency service and the quality of service we provide to our customers. The failure of our products and services to comply, or delays in compliance, with various existing and evolving standards could delay future offerings and impact our sales, margins, and profitability. Changes to the Universal Service Funds by the FCC or various States may require us to increase our costs which could negatively affect revenue and margins.

We are subject to Federal laws and FCC regulations that require us to protect customer information. While we have protections in place to protect customer information there is no assurance that our systems will not be subject to failure or intentional fraudulent attack. The failure to protect required information could subject us to penalties and diminish the confidence our customers have in our systems which could negatively affect results. While we try to comply with all applicable data protection laws, regulations, standards, and codes of conduct, as well as our own posted privacy policies and contractual commitments to the extent possible, any failure by us to protect our users' privacy and data, including as a result of our systems being compromised by hacking or other malicious or surreptitious activity, could result in a loss of user confidence in our services and ultimately in a loss of users, which could materially and adversely affect our business as well as subject us to law suits, civil fines and criminal penalties.

Governmental entities, class action lawyers and consumer advocates are reviewing the data collection and use by companies that must maintain such data. Our own requirements as well as regulatory codes of conduct, enforcement actions by regulatory agencies, and lawsuits by other parties could impose additional compliance costs on us as well as subject us to unknown potential liabilities. These evolving laws, rules and practices may also curtail our current business activities which may delay or affect our ability to become profitable as well as affect customers and other business opportunities.

We are also subject to the privacy and data protection-related obligations in our contracts with our customers and other third parties. Any failure, or perceived failure, to comply with federal, state, or international laws, or to comply with our contractual obligations related to privacy, could result in proceedings or actions against us which could result in significant liability to us as well as harm to our reputation. Additionally, third parties with whom we contract may violate or appear to violate laws or regulations which could subject us to the same risks.

There is considerable uncertainty with respect to the state of law governing data transfers between the European Union ("EU"), and other countries with similar data protection laws, and it remains unclear what the final resolution will be for cross-border data transfers of personal information. There may be risks associated with data transfer and customers who use International Locations.

States are adding regulation for VoIP providers which could increase our costs and change certain aspects of our service.

Certain states take the position that offerings by VoIP providers are intrastate and therefore subject to state regulation. We have registered as a CLEC in most states, however our rates are not regulated in the same manner as traditional telephone service providers. Some states are also requiring that we register as a seller of VoIP services even though we have registered as a CLEC. Some states argue that if the beginning and desktop devices of communications are known, and if some of these communications occur entirely within the boundaries of a state, the state can regulate that offering and may therefore add additional taxes or surcharges or regulate rates in a similar matter to traditional telephone service providers. We believe that the FCC has pre-empted states from regulating VoIP providers in the same manner as providers of traditional telecommunications services. We cannot predict how this issue will be resolved or its impact on our business at this time.

Our ability to offer services outside the U.S. is subject to different regulations which may be unknown and uncertain.

Regulatory treatment of VoIP providers outside the United States varies from country to country, and local jurisdictions. Many times, the laws are vague, unclear and regulations are not enforced uniformly. We are licensed as a VoIP seller in Canada, and are considering expanding to other Countries. We also cannot control if our customers take their devices out of the United States and use them abroad. Our resellers may sell to customers who maintain facilities outside the United States. The failure by us or our customers and resellers to comply with laws and regulations could reduce our revenue and profitability. As we expand to additional Countries there may be additional regulations that we are required to comply with, the failure to comply or properly assess regulations may subject us to penalties, fines and other actions which could materially affect our business.

ITEM 2. PROPERTIES

Our corporate office consists of approximately 22,000 square feet of office space in Tempe, Arizona owned by our CEO. Our corporate office is located at 1615 South 52nd Street, Tempe, Arizona 85281. We maintain property insurance on the corporate office building as required by the lease and tenant fire and casualty insurance on our assets located in these buildings in an amount that we deem adequate.

ITEM 3. LEGAL PROCEEDINGS

From time to time we receive inquiries from federal, state, city and local government officials as well as the FCC and taxing authorities in the various jurisdictions in which we operate. These inquiries and investigations related primarily to our discontinued seminar operations and concern compliance with various city, county, state, and/or federal regulations involving sales, representations made, customer service, refund policies, services and marketing practices. We respond to these inquiries and have generally been successful in addressing the concerns of these persons and entities, without a formal complaint or charge being made, although there is often no formal closing of the inquiry or investigation. There can be no assurance that the ultimate resolution of these or other inquiries and investigations will not have a material adverse effect on our business or operations, or that a formal complaint will not be initiated. We also receive complaints and inquiries in the ordinary course of our business from both customers and governmental and non-governmental bodies on behalf of customers, and in some cases these customer complaints have risen to the level of litigation. There can be no assurance that the ultimate resolution of these matters will not have a material adverse effect on our business or results of operations.

ITEM 4. MINE SAFETY DISCLOSURES

The disclosure required by this item is not applicable

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

MARKET INFORMATION

Our common stock began trading on the NYSE - MKT on August 16, 2004 under the symbol "IIG." In May 2011, our stockholders approved an amendment to our Certificate of Incorporation to change our name from "iMergent, Inc." to "Crexendo, Inc." The name change was effective May 18, 2011. Our ticker symbol "IIG" on the New York Stock Exchange was changed to "EXE" on May 18, 2011. On January 13, 2015, the Company moved to the OTCQX Marketplace and our ticker symbol was changed to "CXDO". The following table sets forth the range of high and low sales prices as reported on the OTCQX Marketplace for the periods indicated.

	High	Low
Year Ended December 31, 2018		
October to December 2018	$3.00	$1.54
July to September 2018	2.70	1.50
April to June 2018	2.90	2.31
January to March 2018	3.49	2.00
Year Ended December 31, 2017		
October to December 2017	$2.71	$1.46
July to September 2017	1.95	1.45
April to June 2017	1.84	1.45
January to March 2017	1.60	1.45

SECURITY HOLDERS

There were approximately 1,151 holders of record of our shares of common stock as of December 31, 2018. The number of holders does not include individual participants in security positions listings.

DIVIDENDS

There were no dividends declared for the years ended December 31, 2018 and 2017.

ISSUER PURCHASES OF EQUITY SEQURITIES

None

RECENT SALES OF UNREGISTERED SECURITIES

None

ITEM 6. SELECTED FINANCIAL DATA

Not required.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

SAFE HARBOR

In addition to historical information, this Annual Report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Actual results could differ materially from those projected in the forward-looking statements as a result of a number of factors, risks and uncertainties, including the risk factors set forth in Item 1A. above and the risk factors set forth in this Annual Report. Generally, the words "anticipate", "expect", "intend", "believe" and similar expressions identify forward-looking statements. The forward-looking statements made in this Annual Report are made as of the filing date of this Annual Report with the SEC, and future events or circumstances could cause results that differ significantly from the forward-looking statements included here. Accordingly, we caution readers not to place undue reliance on these statements. We expressly disclaim any obligation to update or alter our forward-looking statements, whether, as a result of new information, future events or otherwise after the date of this document.

OVERVIEW

Crexendo, Inc. is a next-generation CLEC and an award-winning leader and provider of unified communications cloud telecom services, broadband internet services, and other cloud business services that are designed to provide enterprise-class cloud services to any size business at affordable monthly rates. The Company has two operating segments, which consist of Cloud Telecommunications and Web Services.

Cloud Telecommunications - Our cloud telecommunications services transmit calls using IP or cloud technology, which converts voice signals into digital data packets for transmission over the Internet or cloud. Each of our calling plans provides a number of basic features typically offered by traditional telephone service providers, plus a wide range of enhanced features that we believe offer an attractive value proposition to our customers. This platform enables a user, via a single "identity" or telephone number, to access and utilize services and features regardless of how the user is connected to the Internet or cloud, whether it's from a desktop device or an application on a mobile device.

We generate recurring revenue from our cloud telecommunications and broadband Internet services. Our cloud telecommunications contracts typically have a thirty-six to sixty month term. We generate product revenue and equipment financing revenue from the sale and lease of our cloud telecommunications equipment. Revenues from the sale of equipment, including those from sales-type leases, are recognized at the time of sale or at the inception of the lease, as appropriate.

Our Cloud Telecommunications service revenue increased 24% or $1,842,000 to $9,636,000 for the year ended December 31, 2018 as compared to $7,794,000 for the year ended December 31, 2017. Our Cloud Telecommunications product revenue increased 7% or $100,000 to $1,447,000 for the year ended December 31, 2017 as compared to $1,347,000 for the year ended December 31, 2017. As of December 31, 2018 and 2017, our backlog was $23,029,000 and $19,871,000, respectively.

Web Services – We generate recurring revenue from website hosting and other professional services.

Our Web Services revenue decreased 21% or $221,000 to $825,000 for the year ended December 31, 2018 as compared to $1,046,000 for the year ended December 31, 2017.

Results of Consolidated Operations

The following discussion of financial condition and results of operations should be read in conjunction with the Consolidated Financial Statements and Notes thereto and other financial information included herein this Annual Report.

Results of Consolidated Operations (in thousands, except for per share amounts)

	Year Ended December 31,	
		2017
Consolidated	2018	As Adjusted
Service revenue	$10,461	$8,840
Product revenue	1,447	1,347
Total revenue	11,908	10,187
Loss before income taxes	(208)	(922)
Income tax provision	(15)	(7)
Net loss	(223)	(929)
Basic/diluted net loss per share	$(0.02)	$(0.07)

	For the three months ended			
Consolidated	March 31, 2018	June 30, 2018	September 30, 2018	December 31, 2018
Service revenue	$2,442	$2,540	$2,712	$2,767
Product revenue	366	437	314	330
Total revenue	2,808	2,977	3,026	3,097
Income/(loss) before income taxes	(59)	50	(191)	(8)
Income tax provision	(4)	(3)	(8)	-
Net income/(loss)	(63)	47	(199)	(8)
Basic net income/(loss) per common share (1)	$(0.00)	$0.00	$(0.01)	$(0.00)
Diluted net income/(loss) per common share (1)	$(0.00)	$0.00	$(0.01)	$(0.00)

	For the three months ended			
	March 31, 2017	June 30, 2017	September 30, 2017	December 31, 2017
Consolidated	As Adjusted	As Adjusted	As Adjusted	As Adjusted
Service revenue	$2,015	$2,133	$2,259	$2,433
Product revenue	279	303	385	380

Total revenue	2,294	2,436	2,644	2,813
Income/(loss) before income taxes	(511)	(252)	(182)	23
Income tax benefit/(provision)	(4)	(4)	(8)	9
Net income/(loss)	(515)	(256)	(190)	32
Basic net income/(loss) per common share (1)	$(0.04)	$(0.02)	$(0.01)	$0.00
Diluted net income/(loss) per common share (1)	$(0.04)	$(0.02)	$(0.01)	$0.00

(1)
Net income (loss) per common share is computed independently for each of the quarters presented. Therefore, the sums of quarterly net income (loss) per common share amounts do not necessarily equal the total for the twelve month periods presented.

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Year Ended December 31, 2018 Compared to Year Ended December 31, 2017

Service Revenue

Service revenue consists primarily of fees collected for cloud telecommunications services, professional services, interest from sales-type leases, broadband Internet services, website hosting, and web management services. Service revenue increased 18% or $1,621,000, to $10,461,000 for the year ended December 31, 2018 as compared to $8,840,000 for the year ended December 31, 2017. Cloud Telecommunications service revenue increased 24% or $1,842,000, to $9,636,000 for the year ended December 31, 2018 as compared to $7,794,000 for the year ended December 31, 2017. Web service revenue decreased 21% or $221,000, to $825,000 for the year ended December 31, 2018 as compared to $1,046,000 for the year ended December 31, 2017.

Product Revenue

Product revenue consists primarily of fees collected for the sale of desktop phone devices and third party equipment. Product revenue increased by 7% or $100,000, to $1,447,000 for the year ended December 31, 2018 as compared to $1,347,000 for the year ended December 31, 2017. Product revenue fluctuates from one period to the next based on timing of installations. Our typical customer installation is complete within 30 days. However, larger enterprise customers can take multiple months, depending on size and the number of locations. Product revenue is recognized when products have been installed and services commence. We believe growth will initially be seen through increase in our backlog.

Loss Before Income Taxes

Loss before income tax decreased 77% or $714,000 to $208,000 for the year ended December 31, 2018 as compared to $922,000 for the year ended December 31, 2017. The decrease in loss before income tax is primarily due to an increase in revenue of $1,721,000 and a decrease in other expense of $186,000, primarily related to a decrease in interest expense from the related party note payable which was substantially paid off in September 2017. This was offset by an increase in total operating expenses of $1,193,000.

Income Tax Provision

We had an income tax provision of $15,000 for the year ended December 31, 2018 compared to an income tax provision of $7,000 for the year ended December 31, 2017. We had a pre-tax loss for the years ended December 31, 2018 and 2017 of $208,000 and $922,000, respectively, and a full valuation allowance on all of our deferred tax assets for the years ended December 31, 2018 and 2017.

Use of Non-GAAP Financial Measures

To evaluate our business, we consider and use non-generally accepted accounting principles (Non-GAAP) net income (loss) and Adjusted EBITDA as a supplemental measure of operating performance. These measures include the same adjustments that management takes into account when it reviews and assesses operating performance on a period-to-period basis. We consider Non-GAAP net income (loss) to be an important indicator of overall business performance because it allows us to evaluate results without the effects of share-based compensation, rent expense paid with common stock, and amortization of intangibles. We define EBITDA as U.S. GAAP net income (loss) before interest income, interest expense, other income and expense, provision for income taxes, and depreciation and amortization. We believe EBITDA provides a useful metric to investors to compare us with other companies within our industry and across industries. We define Adjusted EBITDA as EBITDA adjusted for share-based compensation, and rent expense paid with stock. We use Adjusted EBITDA as a supplemental measure to review and assess operating performance. We also believe use of Adjusted EBITDA facilitates investors' use of operating performance comparisons from period to period, as well as across companies.

In our March 5, 2019 earnings press release, as furnished on Form 8-K, we included Non-GAAP net loss, EBITDA and Adjusted EBITDA. The terms Non-GAAP net loss, EBITDA, and Adjusted EBITDA are not defined under U.S. GAAP, and are not measures of operating income, operating performance or liquidity presented in analytical tools, and when assessing our operating performance, Non-GAAP net loss, EBITDA, and Adjusted EBITDA should not be considered in isolation, or as a substitute for net loss or other consolidated income statement data prepared in accordance with U.S. GAAP. Some of these limitations include, but are not limited to:

EBITDA and Adjusted EBITDA do not reflect our cash expenditures or future requirements for capital expenditures or contractual commitments;

they do not reflect changes in, or cash requirements for, our working capital needs;

they do not reflect the interest expense, or the cash requirements necessary to service interest or principal payments, on our debt that we may incur;

they do not reflect income taxes or the cash requirements for any tax payments;

although depreciation and amortization are non-cash charges, the assets being depreciated and amortized will be replaced sometime in the future, and EBITDA and Adjusted EBITDA do not reflect any cash requirements for such replacements;

while share-based compensation is a component of operating expense, the impact on our financial statements compared to other companies can vary significantly due to such factors as the assumed life of the options and the assumed volatility of our common stock; and

other companies may calculate EBITDA and Adjusted EBITDA differently than we do, limiting their usefulness as comparative measures.

We compensate for these limitations by relying primarily on our U.S. GAAP results and using Non-GAAP net income (loss), EBITDA, and Adjusted EBITDA only as supplemental support for management's analysis of business performance. Non-GAAP net income (loss), EBITDA and Adjusted EBITDA are calculated as follows for the periods presented.

Reconciliation of Non-GAAP Financial Measures

In accordance with the requirements of Regulation G issued by the SEC, we are presenting the most directly comparable U.S. GAAP financial measures and reconciling the unaudited Non-GAAP financial metrics to the comparable U.S. GAAP measures.

Reconciliation of U.S. GAAP Net Income/(Loss) to Non-GAAP Net Income/(Loss)
(Unaudited)

	Three Months Ended December 31,		Year Ended December 31,	
		2017		2017
	2018	As Adjusted	2018	As Adjusted
	(In thousands)		(In thousands)	

U.S. GAAP net income/(loss)	$(8)	$32	$(223)	$(929)
Share-based compensation	94	92	438	573
Amortization of rent expense paid in stock, net of deferred gain	-	-	-	38
Amortization of intangible assets	18	23	72	96
Non-cash interest expense	-	3	-	201
Non-GAAP net income/(loss)	$104	$150	$287	$(21)
Non-GAAP net income/(loss) per common share:				
Basic	$0.01	$0.01	$0.02	$(0.00)
Diluted	$0.01	$0.01	$0.02	$(0.00)
Weighted-average common shares outstanding:				
Basic	14,394,113	14,276,729	14,332,092	13,938,342
Diluted	14,902,330	14,732,765	15,095,262	13,938,342

Reconciliation of U.S. GAAP Net Income/(Loss) to EBITDA to Adjusted EBITDA
(Unaudited)

	Three Months Ended December 31,		Year Ended December 31,	
		2017		2017
	2018	As Adjusted	2018	As Adjusted
	(In thousands)		(In thousands)	
U.S. GAAP net income/(loss)	$(8)	$32	$(223)	$(929)
Depreciation and amortization	26	25	92	106
Interest expense	4	4	12	209
Interest and other expense/(income)	4	(6)	(10)	(21)
Income tax provision/(benefit)	-	(9)	15	7
EBITDA	26	46	(114)	(628)
Share-based compensation	94	92	438	573
Amortization of rent expense paid in stock, net of deferred gain	-	-	-	38
Adjusted EBITDA	$120	$138	$324	$(17)

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States. The following accounting policies are the most critical in understanding our consolidated financial position, results of operations or cash flows, and that may require management to make subjective or complex judgments about matters that are inherently uncertain.

Goodwill – Goodwill is tested for impairment using a fair-value-based approach on an annual basis (December 31) and between annual tests if indicators of potential impairment exist.

Intangible Assets - Our intangible assets consist primarily of customer relationships and developed technology. The intangible assets are amortized following the patterns in which the economic benefits are consumed. We periodically review the estimated useful lives of our intangible assets and review these assets for impairment whenever events or changes in circumstances indicate that the carrying value of the assets may not be recoverable. The determination of impairment is based on estimates of future undiscounted cash flows. If an intangible asset is considered to be impaired, the amount of the impairment will be equal to the excess of the carrying value over the fair value of the asset.

Contingent liabilities - Contingent liabilities require significant judgment in estimating potential payouts. Contingent considerations arising from business combinations require management to estimate future payouts based on forecasted results, which are highly sensitive to the estimates of discount rates and future revenues. These estimates can change significantly from period to period and reviewed each reporting period to establish the fair value of the contingent liability.

For additional information on use of estimates, see summary of Significant Accounting Policies in the notes to the Consolidated Financial Statements.

Segment Operating Results

The Company has two operating segments, which consist of Cloud Telecommunications and Web Services. The information below is organized in accordance with our two reportable segments. Segment operating income (loss) is equal to segment net revenue less segment cost of service revenue, cost of product revenue, sales and marketing, research and development, and general and administrative expenses.

Operating Results of our Cloud Telecommunications Segment (in thousands)

	Year Ended December 31,	
		2017
Cloud Telecommunications	2018	As Adjusted
Service revenue	$9,636	$7,794
Product revenue	1,447	1,347
Total revenue	11,083	9,141
Operating expenses:		
Cost of service revenue	2,973	2,611
Cost of product revenue	727	549
Research and development	776	724
Selling and marketing	3,403	2,833
General and administrative	3,817	3,663
Total operating expenses	11,696	10,380
Operating loss	(613)	(1,239)
Other income/(expense)	5	(183)
Loss before tax provision	$(608)	$(1,422)

Quarterly Financial Information

	For the three months ended			
Cloud Telecommunications	March 31, 2018	June 30, 2018	September 30, 2018	December 31, 2018
Service revenue	$2,217	$2,332	$2,509	$2,578
Product revenue	366	437	314	330
Total revenue	2,583	2,769	2,823	2,908
Operating expenses:				
Cost of service revenue	708	704	797	764
Cost of product revenue	187	201	161	178
Research and development	175	188	207	206
Selling and marketing	829	767	910	897
General and administrative	872	965	1,032	948
Total operating expenses	2,771	2,825	3,107	2,993
Operating loss	(188)	(56)	(284)	(85)
Other income/(expense)	4	3	-	(2)
Loss before tax provision	$(184)	$(53)	$(284)	$(87)

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	For the three months ended			
	March 31, 2017	June 30, 2017	September 30, 2017	December 31, 2017
Cloud Telecommunications	As Adjusted	As Adjusted	As Adjusted	As Adjusted
Service revenue	$1,735	$1,867	$1,999	$2,193
Product revenue	279	303	385	380
Total revenue	2,014	2,170	2,384	2,573
Operating expenses:				
Cost of service revenue	614	629	641	727
Cost of product revenue	108	124	151	166
Research and development	184	179	187	174
Selling and marketing	662	684	735	752
General and administrative	1,034	902	866	861
Total operating expenses	2,602	2,518	2,580	2,680
Operating loss	(588)	(348)	(196)	(107)
Other income/(expense)	(30)	(32)	(122)	1
Loss before tax provision	$(618)	$(380)	$(318)	$(106)

Year Ended December 31, 2018 Compared to Year Ended December 31, 2017

Service Revenue

Cloud Telecommunications service revenue consists primarily of fees collected for cloud telecommunications services, professional services, interest from sales-type leases, administrative fees, and broadband Internet services. Service revenue increased 24% or $1,842,000, to $9,636,000 for the year ended December 31, 2018 as compared to $7,794,000 for the year ended December 31, 2017. The increase in service revenue is due to an increase in contracted service revenue, usage charges, and professional services revenue of $1,919,000, offset by a decrease in cancellation charges of $77,000. A substantial portion of Cloud Telecommunications segment revenue is generated through thirty-six to sixty month service contracts. As such, we believe growth in Cloud Telecommunications segment will initially be seen through increases in our backlog.

Product Revenue

Product revenue consists primarily of fees collected for the sale of desktop phone devices and third party equipment. Product revenue increased 7% or $100,000, to $1,447,000 for the year ended December 31, 2018 as compared to $1,347,000 for the year ended December 31, 2017. Product revenue fluctuates from one period to the next based on timing of installations, as we recognize revenue when the installation is complete. Our typical customer installation is complete within 30 days. However, larger enterprise customers can take multiple months, depending on size and the number of locations. Product revenue is recognized when products have been installed and services commence. We believe growth will initially be seen through increases in our backlog.

Backlog

Backlog represents the total contract value of all contracts signed, less revenue recognized from those contracts as of December 31, 2018 and 2017. Below is a table which displays the Cloud Telecommunications segment revenue backlog as of December 31, 2018 and 2017, which we expect to recognize as revenue within the next thirty-six to sixty months (in thousands):

Cloud Telecommunications Services backlog as of December 31, 2018	$ 23,029
Cloud Telecommunications Services backlog as of December 31, 2017	$ 19,871

Cost of Service Revenue

Cost of service revenue consists primarily of fees we pay to third-party telecommunications carriers and software providers, broadband Internet fees, and costs related to installations and customer support salaries and benefits. Cost of service revenue increased 14% or $362,000, to $2,973,000 for the year ended December 31, 2018 as compared to $2,611,000 for the year ended December 31, 2017. The increase in cost of service revenue was primarily due to an increase in salaries and benefits of $174,000 as a result of an increase in customer support headcount, an increase in costs related to installations of $54,000, an increase in stock options expense of $43,000, an increase in credit card processing fees of $39,000, an increase in bandwidth costs of $38,000, and a $14,000 increase in freight. These increases are directly related to the growth in monthly recurring revenue.

Cost of Product Revenue

Cost of product revenue consists of the costs associated with desktop phone devices, inventory costs, and the purchase of third party equipment. Cost of product revenue increased 32% or $178,000, to $727,000 for the year ended December 31, 2018 as compared to $549,000 for the year ended December 31, 2017. The increase is primarily due to the increase in product revenue, an increase in shipping costs, an increase in device costs, and an increased volume of replacement phones being sent out to customers.

Research and Development

Research and development expenses primarily consist of payroll and related expenses, related to the development of new cloud telecommunications features and products. Research and development expenses increased 7% or $52,000, to $776,000 for the year ended December 31, 2018 as compared to $724,000 for the year ended December 31, 2017. The increase is primarily due to an $83,000 increase in costs for the development of a new customer user interface and the Android app, offset by a $31,000 decrease in salary and benefits due to a decrease in headcount.

Selling and Marketing

Selling and marketing expenses consist primarily of direct and channel sales representative salaries and benefits, partner channel commissions, amortization of costs to acquire contracts, tradeshows, the production of marketing materials, and sales support software. Selling and marketing expenses increased 20% or $570,000, to $3,403,000 for the year ended December 31, 2018 as compared to $2,833,000 for the year ended December 31, 2017. The increase in selling and marketing expense was due to an increase in commission expenses of $339,000 directly related to an increase in revenue, an increase in salaries and benefits of $185,000, an increase in travel expenses of $38,000, and an increase in bad debt of $14,000, offset by a decrease in stock options expense of $5,000 and a decrease in business development costs of $1,000, which includes trade shows and other marketing materials.

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General and Administrative

General and administrative expenses consist of salaries and benefits for executives, administrative personnel, legal, rent, accounting, other professional services, and other administrative corporate expenses. General and administrative expenses increased 4% or $154,000, to $3,817,000 for the year ended December 31, 2018 as compared to $3,663,000 for the year ended December 31, 2017. Consolidated general and administrative expenses increased less than 1%, or $19,000 to $4,091,000 for the year ended December 31, 2018 compared to $4,072,000 for the year ended December 31, 2017. As Web Services segment revenue continues to decrease and Cloud Telecommunications segment revenue continues to increase, a higher percentage of general and administrative costs are being allocated to the Cloud Telecommunications segment. The increase in consolidated general and administrative expenses is primarily due to an increase in accounting and other professional services of $104,000, an increase in computer supplies and office equipment of $75,000, an increase in administrative salaries and benefits of $42,000, an increase in repairs and maintenance of $29,000, and an increase in other administrative corporate expenses of $11,000, offset by a decrease in stock options expense of $159,000 and a decrease in software expense of $83,000.

Other Income/(Expense)

Other income/(expense) primarily relates to the allocated portions of interest expense, offset by sublease rental income. Net other expense decreased 103% or $188,000 to $5,000 of net other income for the year ended December 31, 2018 as compared to net other expense of $(183,000) for the year ended December 31, 2017. The decrease is due to a decrease in allocated interest expense of $177,000 primarily related to the related party note payable, which was substantially paid off in September 2017 and an increase in other income of $11,000, which is primarily related to sublease rental income.

Operating Results of our Web Services Segment (in thousands)

	Year Ended December 31,	
		2017
Web Services	2018	As Adjusted
Service revenue	$825	$1,046
Operating expenses:		
Cost of service revenue	119	106
Research and development	25	26
General and administrative	274	409
Total operating expenses	418	541
Operating income	407	505
Other expense	(7)	(5)
Income before tax provision	$400	$500

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Quarterly Financial Information

	For the three months ended			
Web Services	March 31, 2018	June 30, 2018	September 30, 2018	December 31, 2018
Service revenue	$225	$208	$203	$189
Operating expenses:				
Cost of service revenue	21	27	36	35
Research and development	6	6	7	6
General and administrative	73	69	69	63
Total operating expenses	100	102	112	104
Operating income	125	106	91	85
Other income/(expense)	-	(3)	2	(6)
Income before tax provision	$125	$103	$93	$79

	For the three months ended			
	March 31, 2017	June 30, 2017	September 30, 2017	December 31, 2017
Web Services	As Adjusted	As Adjusted	As Adjusted	As Adjusted
Service revenue	$280	$266	$260	$240
Operating expenses:				
Cost of service revenue	30	25	23	28
Research and development	6	6	7	7
General and administrative	137	107	88	77
Total operating expenses	173	138	118	112
Operating income	107	128	142	128
Other income/(expense)	-	-	(6)	1
Income before tax provision	$107	$128	$136	$129

Year Ended December 31, 2018 Compared to Year Ended December 31, 2017

Service Revenue

Service revenue is generated primarily through website hosting, professional web management services, and extended payment term agreements (EPTAs). Web services revenue decreased 21% or $221,000, to $825,000 for the year ended December 31, 2018 as compared to $1,046,000 for the year ended December 31, 2017. The decrease in service revenue is primarily due to a decrease in hosting revenue of $181,000 and a $40,000 decrease in EPTA revenue due to decrease in outstanding receivables.

Cost of Service Revenue

Cost of service revenue consists primarily of bandwidth, customer service costs, and credit card processing fees. Cost of service revenue increased 12% or $13,000, to $119,000 for the year ended December 31, 2018 as compared to $106,000 for the year ended December 31, 2017. The increase in cost of revenue is primarily related to an increase in customer service costs of $20,000, offset by a decrease in credit card fees of $5,000 and a decrease in web domain costs of $2,000, both directly related to decrease in revenue.

Research and Development

Research and development expenses primarily consist of salaries and benefits, and related expenses which are attributable to the development of our website development software products. Research and development expenses decreased 4% or $1,000, to $25,000 for the year ended December 31, 2018 as compared to $26,000 for the year ended December 31, 2017. The decrease was primarily related to a reduction in the allocation of salaries and benefits expenses.

General and Administrative

General and administrative expenses consist of salaries and benefits for executives, administrative personnel, legal, rent, accounting, other professional services, and other administrative corporate expenses. General and administrative expenses decreased 33% or $135,000, to $274,000 for the year ended December 31, 2018 as compared to $409,000 for the year ended December 31, 2017. The decrease in general and administrative expenses is primarily due to less of an allocation of corporate general and administrative expenses resulting from the 21% decrease in service revenue for the year ended December 31, 2018. Consolidated general and administrative expenses increased less than 1%, or $19,000 to $4,091,000 for the year ended December 31, 2018 compared to $4,072,000 for the year ended December 31, 2017. As Web Services segment revenue continues to decrease and Cloud Telecommunications segment revenue continues to increase, a higher percentage of general and administrative costs are being allocated to the Cloud Telecommunications segment. The increase in consolidated general and administrative expenses is primarily due to an increase in accounting and other professional services of $104,000, an increase in computer supplies and office equipment of $75,000, an increase in administrative salaries and benefits of $42,000, an increase in repairs and maintenance of $29,000, and an increase in other administrative corporate expenses of $11,000, offset by a decrease in stock options expense of $159,000 and a decrease in software expense of $83,000.

Other Income/(Expense)

Other income/(expense) primarily relates to interest income from the collection of EPTA receivables, foreign exchange gains or losses, and the allocated portions of interest expense and sublease rental income. Other expense increased 40% or $2,000, to $7,000 for the year ended December 31, 2018 as compared to $5,000 for the year ended December 31, 2017. The increase is due to a decrease in net foreign exchange gains of $19,000 and a $3,000 decrease in interest income from the collection of EPTAs, offset by a decrease in allocated interest expense of $20,000 primarily related to the related party note payable, which was substantially paid off in September 2017.

LIQUIDITY AND CAPITAL RESOURCES

As of December 31, 2018 and 2017, we had cash and cash equivalents of $1,849,000 and $1,282,000, respectively. Changes in cash and cash equivalents are dependent upon changes in, among other things, working capital items such as contract liabilities, contract costs, accounts payable, accounts receivable, prepaid expenses, and various accrued expenses, as well as purchases of property and equipment and changes in our capital and financial structure due to debt repayments and issuances, stock option exercises, sales of equity investments and similar events. We believe that our operations along with existing liquidity sources will satisfy our cash requirements for at least the next 12 months. If the assumptions underlying our business plan regarding future revenue and expenses change or if unexpected opportunities or needs arise, we may seek to raise additional cash by selling equity or debt securities.

Working Capital

Working capital increased 44% or $401,000 to $1,322,000 as of December 31, 2018 as compared to $921,000 as of December 31, 2017. The increase in working capital was related to an increase in cash and cash equivalents of

$567,000, an increase in trade receivables, net of allowance for doubtful accounts of $47,000, an increase in contract assets of $9,000, an increase in inventories of $139,000, an increase in income tax receivable of $1,000, and a decrease in notes payable, current portion, of $13,000, offset by a decrease in equipment financing receivables of $49,000, a decrease in contract costs of $8,000, a decrease in prepaid expenses of $7,000, a decrease in other current assets of $10,000, an increase in accounts payable of $76,000, an increase in accrued expenses of $170,000, an increase in capital lease obligations, current portion of $28,000, and an increase in contract liabilities, current portion, of $27,000.

Cash, Cash Equivalents, and Restricted Cash

Cash, cash equivalents, and restricted cash increased 41% or $567,000, to $1,949,000 as of December 31, 2018 as compared to $1,382,000 as of December 31, 2017. During the year ended December 31, 2018, operating activities provided $452,000. Financing activities provided $122,000, primarily related to proceeds from stock option exercises of $155,000 and proceeds from notes payable of $130,000, offset by repayments on notes payable of $153,000, and repayments on the capital lease of $10,000. Cash used for investing activities was $7,000, related to the purchase of equipment in the second quarter of 2018.

Inventories

Inventories increased 106% or $139,000 to $270,000 as of December 31, 2018 as compared to $131,000 as of December 31, 2017. Inventory balances fluctuate based on timing of installations and inventory shipments. A large inventory shipment was received in the fourth quarter of 2018.

Prepaid Expenses

Prepaid expenses decreased 3% or $7,000 to $244,000 as of December 31, 2018 as compared to $251,000 as of December 31, 2017.

Trade Receivables

Current and long-term trade receivables, net of allowance for doubtful accounts, increased 6% or $26,000, to $429,000 as of December 31, 2018 as compared to $403,000 as of December 31, 2017. Current trade receivables, net of allowance for doubtful accounts, increased 13% or $47,000, to $419,000 as of December 31, 2018 as compared to $372,000 as of December 31, 2017. The increase in current trade receivables can be attributed to an unpaid down payment invoice for seven new locations for an existing customer. Long-term trade receivables, net of allowance for doubtful accounts, decreased 68% or $21,000, to $10,000 as of December 31, 2018 as compared to $31,000 as of December 31, 2017. The decrease is primarily due to the write-off of uncollectible accounts.

Accounts Payable and Accrued Expenses

Accounts payable increased 96% or $76,000, to $155,000 as of December 31, 2018 as compared to $79,000 as of December 31, 2017. The aging of accounts payable as of December 31, 2018 and 2017 were generally within our vendors' terms of payment. The increase is primarily related to the timing of the check processing schedule.

Accrued expenses increased 18% or $170,000 to $1,131,000 as of December 31, 2018 as compared to $961,000 as of December 31, 2017. Sales tax accrual increased $137,000, partner commissions accrual increased $63,000, salaries and benefits accrual increased $24,000, accrued audit and tax preparation fees increased $24,000, and warranty reserve increased $16,000, offset by a $61,000 decrease in accrued accounts payable, a $27,000 decrease in accrued sales bonuses, and a decrease in other accrued expenses of $6,000.

Notes Payable

Notes payables decreased 29% or $23,000, to $56,000 as of December 31, 2018 as compared to $79,000 at December 31, 2017. The decrease in notes payable can be attributed to payments made on financing contracts of $153,000, offset by additional financing arrangements entered into during the period of $130,000.

Capital Lease

Capital lease obligations increased $144,000, to $144,000 as of December 31, 2018 as compared to $0 at December 31, 2017. The company entered into a $154,000 capital lease in the second quarter of 2018 for data center hardware, installation and support, offset by repayments of $10,000.

Contract Liabilities

Contract liabilities increased 8% or $75,000 to $1,063,000 as of December 31, 2018 as compared to $988,000 as of December 31, 2017. The increase is primarily due to one customer paying their entire 60 month agreement upfront and for an increase in down payments on jobs that have not installed yet, offset by a reclassification to revenue for installations completed during the period.

Capital

Total stockholders’ equity increased 23% or $370,000, to $2,000,000 as of December 31, 2018 as compared to $1,630,000 as of December 31, 2017. The increase in total stockholders’ equity was attributable to an increase in additional paid-in capital of $438,000 for stock options issued to employees and $155,000 for proceeds from the exercise of stock options, offset by a net loss of $223,000.

OFF BALANCE SHEET ARRANGEMENTS

As of December 31, 2018, we are not involved in any off-balance sheet arrangements, as defined in Item 303(a)(4)(ii) of SEC Regulation S-K.

RELATED PARTY TRANSACTIONS

None

RECENT ACCOUNTING PRONOUNCEMENTS

For a summary of recent accounting pronouncements and the anticipated effects on our consolidated financial statements, see Note 1 to the consolidated financial statements, which is incorporated by reference herein.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISKS

Not required

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

CREXENDO, INC. AND SUBSIDIARIES

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS AND SCHEDULE

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of
Crexendo, Inc.
Tempe, AZ

Opinion on the Consolidated Financial Statements

We have audited the accompanying consolidated balance sheets of Crexendo, Inc. and subsidiaries (the "Company") as of December 31, 2018 and 2017, the related consolidated statements of operations, stockholders' equity, and cash flows for the years then ended, and the related notes and financial statement schedule listed in the accompanying index (collectively referred to as the "consolidated financial statements"). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company and subsidiaries at December 31, 2018 and 2017, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Basis for Opinion

These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's consolidated financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) ("PCAOB") and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion.

Our audits included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ Urish Popeck & Co., LLC

We have served as the Company's auditor since 2016.
Pittsburgh, PA
March 5, 2019

CREXENDO, INC. AND SUBSIDIARIES
Consolidated Balance Sheets
(In thousands, except par value and share data)

	December 31,	
	2018	2017
Assets		
Current assets:		
Cash and cash equivalents	$1,849	$1,282
Restricted cash	100	100
Trade receivables, net of allowance for doubtful accounts of $14 as of December 31, 2018 and $19 as of December 31, 2017	419	372
Contract assets	12	3
Inventories	270	131
Equipment financing receivables	67	116
Contract costs	371	379
Prepaid expenses	244	251
Income tax receivable	1	-
Other current assets	-	10
Total current assets	3,333	2,644
Long-term trade receivables, net of allowance for doubtful accounts of $0 as December 31, 2018 and $10 as of December 31, 2017	10	31
Long-term equipment financing receivables, net	184	58
Property and equipment, net	124	8
Intangible assets, net	167	239
Goodwill	272	272
Contract costs, net of current portion	342	364
Other long-term assets	117	121
Total Assets	$4,549	$3,737
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	$155	$79
Accrued expenses	1,131	961
Capital lease obligations	28	-
Notes payable	56	69
Contract liabilities	641	614
Total current liabilities	2,011	1,723
Contract liabilities, net of current portion	422	374

Capital lease obligations, net of current portion	116	-
Notes payable, net of current portion	-	10
Total liabilities	2,549	2,107
Stockholders' equity:		
Preferred stock, par value $0.001 per share - authorized 5,000,000 shares; none issued	—	—
Common stock, par value $0.001 per share - authorized 25,000,000 shares, 14,394,113 shares issued and outstanding as of December 31, 2018 and 14,287,556 shares issued and outstanding as of December 31, 2017	14	14
Additional paid-in capital	61,153	60,560
Accumulated deficit	(59,167)	(58,944)
Total stockholders' equity	2,000	1,630
Total Liabilities and Stockholders' Equity	$4,549	$3,737

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

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CREXENDO, INC. AND SUBSIDIARIES
Consolidated Statements of Operations
(In thousands, except per share and share data)

	Year Ended December 31,	
	2018	2017
Service revenue	$10,461	$8,840
Product revenue	1,447	1,347
Total revenue	11,908	10,187
Operating expenses:		
Cost of service revenue	3,092	2,717
Cost of product revenue	727	549
Selling and marketing	3,403	2,833
General and administrative	4,091	4,072
Research and development	801	750
Total operating expenses	12,114	10,921
Loss from operations	(206)	(734)
Other income/(expense):		
Interest income	7	10
Interest expense	(12)	(209)
Other income, net	3	11
Total other expense, net	(2)	(188)
Loss before income tax	(208)	(922)
Income tax provision	(15)	(7)
Net loss	$(223)	$(929)
Net loss per common share:		
Basic	$(0.02)	$(0.07)
Diluted	$(0.02)	$(0.07)
Weighted-average common shares outstanding:		
Basic	14,332,092	13,938,342
Diluted	14,332,092	13,938,342

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

CREXENDO, INC. AND SUBSIDIARIES
Consolidated Statements of Stockholders' Equity
(In thousands, except share data)

	Common Stock		Additional Paid-in Capital	Accumulated Deficit	Total Stockholders' Equity
	Shares	Amount			
Balance, January 1, 2017	13,578,556	$14	$58,716	$(58,015)	$715
Share-based compensation	-	-	530	-	530
Vesting of restricted stock units	27,000	-	43	-	43
Issuance of common stock for exercise of stock options	607,000		1,162		1,162
Issuance of common stock for interest on related party note payable	75,000	-	109	-	109
Net loss	-	-	-	(929)	(929)
Balance, December 31, 2017	14,287,556	14	60,560	(58,944)	1,630
Share-based compensation	-	-	438	-	438
Issuance of common stock for exercise of stock options	106,557	-	155	-	155
Net loss	-	-	-	(223)	(223)
Balance, December 31, 2018	14,394,113	$14	$61,153	$(59,167)	$2,000

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

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CREXENDO, INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows
(In thousands)

	Year Ended December 31,	
	2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss	$(223)	$(929)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Amortization of prepaid rent	-	54
Depreciation and amortization	92	106
Non-cash interest expense	-	201
Share-based compensation	438	573
Amortization of deferred gain	-	(16)
Changes in assets and liabilities:		
Trade receivables	(26)	(16)
Contract assets	(9)	(1)
Equipment financing receivables	(77)	123
Inventories	(139)	39
Contract costs	30	(40)
Prepaid expenses	32	129
Income tax receivable	(1)	-
Other assets	14	13
Accounts payable and accrued expenses	246	(73)
Income tax payable	-	(5)
Contract liabilities	75	136
Net cash provided by operating activities	452	294
CASH FLOWS FROM INVESTING ACTIVITIES		
Sale of certificate of deposit	-	252
Purchase of property and equipment	(7)	-
Net cash provided by/(used for) investing activities	(7)	252
CASH FLOWS FROM FINANCING ACTIVITIES		
Repayments made on capital lease	(10)	-
Proceeds from notes payable	130	111
Repayments made on notes payable	(153)	(1,156)
Proceeds from exercise of options	155	1,162
Net cash provided by financing activities	122	117
NET INCREASE IN CASH, CASH EQUIVALENTS, AND RESTRICTED CASH	567	663
	1,382	719

CASH, CASH EQUIVALENTS, AND RESTRICTED CASH AT THE BEGINNING OF THE YEAR		
CASH, CASH EQUIVALENTS, AND RESTRICTED CASH AT THE END OF THE YEAR	$1,949	$1,382
Supplemental disclosure of cash flow information:		
Cash used during the year for:		
Income taxes, net	$(16)	$(12)
Interest expense	$(12)	$(8)
Supplemental disclosure of non-cash investing and financing information:		
Issuance of common stock for payment of interest on related-party note payable	$-	$109
Prepaid assets financed through notes payable	$97	$111
Prepaid assets financed through capital lease obligations	$25	$-
Property and equipment financed through capital lease obligations	$129	$-

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

CREXENDO, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements

1.
Description of Business and Significant Accounting Policies

Description of Business - Crexendo, Inc. is incorporated in the state of Nevada. As used hereafter in the notes to consolidated financial statements, we refer to Crexendo, Inc. and its wholly owned subsidiaries, as “we,” “us,” or “our Company.” Crexendo is a next-generation CLEC and an award-winning leader and provider of unified communications cloud telecom services, broadband Internet services, and other cloud business services that are designed to provide enterprise-class cloud services to any size business at affordable monthly rates. The Company has two operating segments, which consist of Cloud Telecommunications and Web Services.

Basis of Presentation – The consolidated financial statements include the accounts and operations of Crexendo, Inc. and its wholly owned subsidiaries, which include Crexendo Business Solutions, Inc. and Crexendo International, Inc. All intercompany account balances and transactions have been eliminated in consolidation. The consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (“US GAAP”) and pursuant to the rules and regulations of the SEC. These consolidated financial statements reflect the results of operations, financial position, changes in stockholders’ equity, and cash flows of our Company.

Certain prior year amounts have been reclassified for consistency with the current period presentation. These reclassifications had no effect on the reported results of operations.

Cash and Cash Equivalents - We consider all highly liquid, short-term investments with maturities of three months or less at the time of purchase to be cash equivalents. As of December 31, 2018 and 2017, we had cash and cash equivalents in financial institutions in excess of federally insured limits in the amount of $1,645,000 and $1,038,000, respectively.

Restricted Cash – We classified $100,000 and $100,000 as restricted cash as of December 31, 2018 and 2017, respectively. Cash is restricted for compensating balance requirements on purchasing card agreements. As of December 31, 2018 and 2017, we had restricted cash in financial institutions in excess of federally insured limits in the amount of $100,000 and $100,000, respectively.

The following table provides a reconciliation of cash and cash equivalents and restricted cash reported on the balance sheet to the cash, cash equivalents, and restricted cash shown in the consolidated statement of cash flows (in thousands):

	December 31, 2018	December 31, 2017
Cash and cash equivalents	$1,849,000	$1,282,000
Restricted cash	100,000	100,000
Total cash, cash equivalents, and restricted cash shown in the consolidated statement of cash flows	$1,949,000	$1,382,000

Trade Receivables – Trade receivables from our cloud telecommunications and web services segments are recorded at invoiced amounts.

Allowance for Doubtful Accounts – The allowance represents estimated losses resulting from customers' failure to make required payments. The allowance estimate is based on historical collection experience, specific identification of probable bad debts based on collection efforts, aging of trade receivables, customer payment history, and other known factors, including current economic conditions. We believe that the allowance for doubtful accounts is adequate based on our assessment to date, however, actual collection results may differ materially from our expectations.

Contract Assets – Contract assets primarily relate to the Company's rights to consideration for work completed but not billed as of the reporting date. The contract assets are transferred to receivables when the rights become unconditional.

Contract Costs – Contract costs primarily relate to incremental commission costs paid to sales representatives and sales leadership as a result of obtaining telecommunications contracts which are recoverable. The Company capitalized contract costs in the amount of $713,000 and $743,000 at December 31, 2018 and December 31, 2017, respectively. Capitalized commission costs are amortized based on the transfer of goods or services to which the assets relate which typically range from thirty-six to sixty months, and are included in selling and marketing expenses. During the year ended December 31, 2018 and 2017, the Company amortized $476,000 and $410,000, respectively, and there was no impairment loss in relation to the costs capitalized.

Inventory – Finished goods telecommunications equipment inventory is stated at the lower of cost or net realizable value (first-in, first-out method). In accordance with applicable accounting guidance, we regularly evaluate whether inventory is stated at the lower of cost or net realizable value. If net realizable value is less than cost, the write-down is recognized as a loss in earnings in the period in which the excess occurs.

Property and Equipment - Depreciation and amortization expense is computed using the straight-line method in amounts sufficient to allocate the cost of depreciable assets over their estimated useful lives ranging from two to five years. The cost of leasehold improvements is amortized using the straight-line method over the shorter of the estimated useful life of the asset or the term of the related lease. Depreciation expense is included in general and administrative expenses and totaled $20,000 and $10,000 for the years ended December 31, 2018 and 2017, respectively. Depreciable lives by asset group are as follows:

Computer and office equipment	2 to 5 years
Computer software	3 years
Furniture and fixtures	4 years
Leasehold improvements	2 to 5 years

Maintenance and repairs are expensed as incurred. The cost and accumulated depreciation of property and equipment sold or otherwise retired are removed from the accounts and any related gain or loss on disposition is reflected in the statement of operations.

Goodwill – Goodwill is tested for impairment using a fair-value-based approach on an annual basis (December 31) and between annual tests if indicators of potential impairment exist.

Intangible Assets - Our intangible assets consist primarily of customer relationships. The intangible assets are amortized following the patterns in which the economic benefits are consumed. We periodically review the estimated useful lives of our intangible assets and review these assets for impairment whenever events or changes in circumstances indicate that the carrying value of the assets may not be recoverable. The determination of impairment is based on estimates of future undiscounted cash flows. If an intangible asset is considered to be impaired, the amount of the impairment will be equal to the excess of the carrying value over the fair value of the asset.

Contract Liabilities – Our contract liabilities consist primarily of advance consideration received from customers for telecommunications contracts. The product and monthly service revenue is recognized on completion of the implementation and the remaining activation fees are reclassified as deferred revenue.

Use of Estimates - In preparing the consolidated financial statements, management makes assumptions, estimates and judgments that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the consolidated financial statements and the reported amounts of net sales and expenses during the reported periods. Specific estimates and judgments include valuation of goodwill and intangible assets in connection with business acquisitions, allowances for doubtful accounts, uncertainties related to certain income tax benefits, valuation of deferred income tax assets, valuations of share-based payments and recoverability of long-lived assets. Management's estimates are based on historical experience and on our expectations that are believed to be reasonable. The combination of these factors forms 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 our current estimates and those differences may be material.

Product and Service Revenue Recognition - Revenue is recognized upon transfer of control of promised products or services to customers in an amount that reflects the consideration we expect to receive in exchange for those products or services and excludes any amounts collected on behalf of third parties. We enter into contracts that can include various combinations of products and services, which are generally capable of being distinct and accounted for as separate performance obligations. We recognize revenue for delivered elements only when we determine there are no uncertainties regarding customer acceptance. Changes in the allocation of the sales price between delivered and undelivered elements can impact the timing of revenue recognized but does not change the total revenue recognized on any agreement. Revenue is recognized net of any taxes collected from customers, which are subsequently remitted to governmental authorities. For more detailed information about revenue, see Note 3.

Cost of Service Revenue – Cost of service includes Cloud Telecommunications and Web Services cost of service revenue. Cloud Telecommunications cost of service revenue primarily consists of fees we pay to third-party telecommunications and broadband Internet providers, costs of other third party services we resell, personnel and travel expenses related to system implementation, and customer service. Web Services cost of service revenue consists primarily of customer service costs and outsourcing fees related to fulfillment of our professional web management services.

Cost of Product Revenue – Cost of product revenue primarily consists of the costs associated with the purchase of desktop devices and other third party equipment we purchase for resale.

Product Warranty – We provide for the estimated cost of product warranties at the time we recognize revenue. We evaluate our warranty obligations on a product group basis. Our standard product warranty terms generally include post-sales support and repairs or replacement of a product at no additional charge for a specified period of time. We base our estimated warranty obligation upon warranty terms, ongoing product failure rates, and current period product shipments. If actual product failure rates, repair rates or any other post-sales support costs were to differ from our estimates, we would be required to make revisions to the estimated warranty liability. Warranty terms generally last for the duration that the customer has service. For 2018, the annual warranty provision and actual warranty costs were approximately 1.1% of annual net product revenue.

Research and Development - Research and development costs are expensed as incurred. Costs related to internally developed software are expensed as research and development expense until technological feasibility has been achieved, after which the costs are capitalized.

Fair Value Measurements - The fair value of our financial assets and liabilities was determined based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value which are the following:

Level 1 — Unadjusted quoted prices that are available in active markets for the identical assets or liabilities at the measurement date.

Level 2 — Other observable inputs available at the measurement date, other than quoted prices included in Level 1, either directly or indirectly, including:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets in non-active markets;
- Inputs other than quoted prices that are observable for the asset or liability; and
- Inputs that are derived principally from or corroborated by other observable market data.

Level 3 — Unobservable inputs that cannot be corroborated by observable market data and reflect the use of significant management judgment. These values are generally determined using pricing models for which the assumptions utilize management's estimates of market participant assumptions.

Lease Obligations – At the inception of each lease, we evaluate the lease terms to determine whether the lease will be accounted for as an operating or capital lease. A lease that transfers substantially all of the benefits and risks incidental to ownership of property are accounted for as capital leases. At the inception of a capital lease, an asset and payment obligation is recorded at an amount equal to the lesser of the present value of the minimum lease payments and the property's fair market value. Capital lease obligations are classified as either short or long-term based on the due dates of future minimum lease payments, net of interest. All other leases are accounted for as operating leases and the related lease payments are charged to expenses as incurred.

Notes Payable – We record notes payable net of any discounts or premiums. Discounts and premiums are amortized as interest expense or income over the life of the note in such a way as to result in a constant rate of interest when applied to the amount outstanding at the beginning of any given period.

Income Taxes - We recognize a liability or asset for the deferred tax consequences of all temporary differences between the tax basis of assets and liabilities and their reported amounts in the consolidated financial statements that will result in taxable or deductible amounts in future years when the reported amounts of the assets and liabilities are recovered or settled. Accruals for uncertain tax positions are provided for in accordance with accounting guidance. Accordingly, we may recognize the tax benefits from an uncertain tax position only if it is more-likely-than-not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position should be measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. Accounting guidance is also provided on de-recognition of income tax assets and liabilities, classification of current and deferred income tax assets and liabilities, accounting for interest and penalties associated with tax positions, and income tax disclosures. Judgment is required in assessing the future tax consequences of events that have been recognized in the financial statements or tax returns. Variations in the actual outcome of these future tax consequences could materially impact our financial position, results of operations, and cash flows. In assessing the need for a valuation allowance, we evaluate all significant available positive and negative evidence, including historical operating results, estimates of future taxable income and the existence of prudent and feasible tax planning strategies. We have placed a full valuation allowance on net deferred tax assets.

Interest and penalties associated with income taxes are classified as income tax expense in the consolidated statements of operations.

Stock-Based Compensation - For equity-classified awards, compensation expense is recognized over the requisite service period based on the computed fair value on the grant date of the award. Equity classified awards include the issuance of stock options.

Comprehensive Income/(Loss) – There were no other components of comprehensive income/(loss) other than net loss for the years ended December 31, 2018 and 2017.

Operating Segments - Accounting guidance establishes standards for the way public business enterprises are to report information about operating segments in annual financial statements and requires enterprises to report selected information about operating segments in financial reports issued to stockholders. The Company has two operating segments, which consist of Cloud Telecommunications and Web Services. Research and development expenses are allocated to Cloud Telecommunications and Web Services segments based on the level of effort, measured primarily by wages and benefits attributed to our engineering department. Indirect sales and marketing expenses are allocated to the Cloud Telecommunications and Web Services segments based on level of effort, measured by month-to-date contract bookings. General and administrative expenses are allocated to both segments based on revenue recognized for each segment. Accounting guidance also establishes standards for related disclosure about products and services, geographic areas and major customers. We generate over 90% of our total revenue from customers within North America (United States and Canada) and less than 10% of our total revenues from customers in other parts of the world.

Significant Customers – No customer accounted for 10% or more of our total revenue for the years ended December 31, 2018 and 2017. One telecommunications services customer accounted for 22% and 11% of total trade accounts receivable as of December 31, 2018 and 2017, respectively.

Recently Adopted Accounting Pronouncements - In July 2015, the Financial Accounting Standards Board ("FASB) issued ASU 2015-11, Inventory, which will require an entity to measure in scope inventory at the lower of cost and net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. Subsequent measurement is unchanged for inventory measured using LIFO or the retail inventory method. The amendments do not apply to inventory that is measured using last-in, first-out (LIFO) or the retail inventory method. The amendments apply to all other inventory, which includes inventory that is measured using first-in, first-out (FIFO) or average cost. We adopted this guidance effective January 1, 2017. The adoption of this guidance did not have an impact on our consolidated financial statements.

In January 2017, the FASB issued ASU 2017-01, Business Combinations (Topic 805) Clarifying the Definition of a Business, that provides guidance to assist entities with evaluating when a set of transferred assets and activities (set) is a business. Under the new guidance, an entity first determines whether substantially all of the fair value of the gross assets acquired is concentrated in a single identifiable asset or a group of similar identifiable assets. If this threshold is met, the set is not a business. If it's not met, the entity then evaluates whether the set meets the requirement that a business include, at a minimum, an input and a substantive process that together significantly contribute to the ability to create outputs. Under today's guidance, it doesn't matter whether all the value relates primarily to one asset. Under ASU 2017-01, a set is not a business when substantially all of the fair value of the gross assets acquired is concentrated in a single identifiable asset or a group of similar identifiable assets. The ASU includes guidance on which types of assets can and cannot be combined into a single identifiable asset or a group of similar identifiable assets for the purpose of applying the threshold. The ASU is effective for fiscal years beginning after December 15, 2017, and interim periods within those years. We adopted this guidance effective January 1, 2018. The adoption of this guidance did not have an impact on our consolidated financial statements.

In November 2016, the FASB issued ASU 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash, which requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. As a result, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. We adopted the new accounting standards effective January 1, 2018. Amounts generally described as restricted cash are now presented with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. As a result of adoption, there was no impact to cash flows from operating, investing or financing activities for the nine months ended September 30, 2018 and 2017. A reconciliation of cash and cash equivalents and restricted cash presented on the balance sheet to the totals presented in the statement of cash flows as cash, cash equivalents, and restricted cash has been added to the footnote disclosures, see Note 1.

In August 2016, the FASB issued ASU No. 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments, which amends ASC 230, to clarify guidance on the classification of certain cash receipts and payments in the statement of cash flows. The changes to the classification of how certain cash receipts and payments are presented within the statement of cash flows had no impact on our consolidated financial statements.

The adoption of these new ASUs required us to restate the previously reported cash and cash equivalent amounts reported in prior periods to include restricted cash, see Note 2-Changes in Accounting Principles.

In June 2014, the FASB issued ASU 2014-12, Compensation – Stock Compensation, which requires that a performance target that affects vesting and could be achieved after the requisite service period be treated as a performance condition. A reporting entity should apply existing guidance in ASC 718, Compensation-Stock Compensation, as it relates to such awards. ASU 2014-12 is effective for us in our first quarter of fiscal 2017 with early adoption permitted using either of two methods: (i) prospective to all awards granted or modified after the effective date; or (ii) retrospective to all awards with performance targets that are outstanding as of the beginning of the earliest annual period presented in the financial statements and to all new or modified awards thereafter, with the cumulative effect of applying ASU 2014-12 as an adjustment to the opening retained earnings balance as of the beginning of the earliest annual period presented in the financial statements. The Company adopted ASU 2014-12 effective January 1, 2017. The adoption of this ASU did not impact our consolidated financial statements, as there are no performance targets associated with outstanding awards.

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers. The objective of ASU 2014-09 is to establish a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. The Company adopted this guidance on January 1, 2018 utilizing the full retrospective method of adoption allowed by the standard, in order to provide for comparative results in all periods presented. Under the standard, revenue is recognized when a customer obtains control of promised goods or services in an amount that reflects the consideration the entity expects to receive in exchange for those goods or services. In addition, the standard requires disclosure of the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. We elected to adopt the standard effective January 1, 2018, using the full retrospective method, which required us to restate each prior reporting period presented, see Note 2-Changes in Accounting Principles. The most significant impact of the standard relates to our accounting for incremental costs to obtain a contract and principal versus agent considerations. Specifically, incremental sales leadership commissions were expensed immediately rather than ratably over the term of the related contracts. Revenue from the resell of broadband Internet services and professional website management services were recognized on a gross basis as a principal rather than on net basis as an agent. The new standard focuses on control of the specified goods and service as the overarching principle and the Company does not control the delivery of the goods and services. Revenue recognition related to our hardware, telecommunications services and website hosting services remains substantially unchanged. See Note 2 for disclosures related to changes in accounting policies.

In May 2017, the FASB issued ASU 2017-09, Compensation—Stock Compensation (Topic 718): Scope of Modification Accounting, the amendments provide guidance on determining which changes to the terms and conditions of share-based payment awards require an entity to apply modification accounting under Topic 718. Effective for all entities for annual periods, including interim periods within those annual periods, beginning after December 15, 2017. The Company adopted ASU 2017-09 effective January 1, 2018. The adoption of this ASU did not impact our consolidated financial statements.

Recently Issued Accounting Pronouncements - In August 2018, the FASB issued ASU 2018-13, which changes the fair value measurement disclosure requirements of ASC 820. The amendments in this ASU are the result of a broader disclosure project called FASB Concepts Statement, Conceptual Framework for Financial Reporting — Chapter 8: Notes to Financial Statements, which the Board finalized in August 2018. The Board used the guidance in the Concepts Statement to improve the effectiveness of ASC 820’s disclosure requirements. The ASU is effective for all entities for fiscal years beginning after December 15, 2019, including interim periods therein. Early adoption is permitted. The Company is in the process of evaluating the impact of this new ASU on our consolidated financial statements.

In August 2018, the FASB issued Accounting Standards Update (ASU) 2018-07, to simplify the accounting for share-based payments to nonemployees by aligning it with the accounting for share-based payments to employees, with certain exceptions. The new guidance expands the scope of Accounting Standards Codification (ASC) 718 to include share-based payments granted to nonemployees in exchange for goods or services used or consumed in an entity's own operations and supersedes the guidance in ASC 505-50. The guidance also applies to awards granted by an investor to employees and nonemployees of an equity method investee for goods or services used or consumed in the investee's operations. The guidance in ASC 718 does not apply to instruments issued to a lender or an investor in a financing (e.g., in a capital raising) transaction. It also does not apply to equity instruments granted when selling goods or services to customers in the scope of ASC 606. However, the guidance states that share-based payments granted to a customer in exchange for a distinct good or service to be used or consumed in the grantor's own operations are accounted for under ASC 718. The guidance is effective for public business entities (PBEs) in annual periods beginning after December 15 2018, and interim periods within those annual periods. The Company is in the process of evaluating the impact of this new ASU on our consolidated financial statements.

In July 2018, the FASB issued ASU 2018-11 to provide entities with relief from the costs of implementing certain aspects of the new leasing standard, ASU 2016-02 (codified as ASC 842). Specifically, under the amendments in ASU 2018-11:

Entities may elect not to recast the comparative periods presented when transitioning to ASC 842 (Issue 1).

Lessors may elect not to separate lease and non-lease components when certain conditions are met (Issue 2).

These amendments are consistent with the tentative decisions that the Board made at its November 29, 2017, meeting and further refined at its March 7, 2018, and March 28, 2018, meetings. In addition, on July 19, 2018, the FASB issued ASU 2018-10, which made 16 separate amendments to ASC 842. The Company is in the process of evaluating the impact of this new ASU on our consolidated financial statements.

In July 2018, the FASB has issued Accounting Standards Update (ASU) 2018-10, "Codification Improvements to Topic 842, Leases." The clarifications address the rate implicit in the lease, impairment of the net investment in the lease, lessee reassessment of lease classification, lessor reassessment of lease term and purchase options, variable payments that depend on an index or rate and certain transition adjustments. The amendments have the same effective date and transition requirements as the new leases standard. The Company is in the process of evaluating the impact of this new ASU on our consolidated financial statements.

In January 2017, the FASB issued ASU 2017-04, Intangibles - Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment, which eliminates Step 2 from the goodwill impairment test. The annual, or interim, goodwill impairment test is performed by comparing the fair value of a reporting unit with its carrying amount. An impairment charge should be recognized for the amount by which the carrying amount exceeds the reporting unit's fair value; however, the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. In addition, income tax effects from any tax deductible goodwill on the carrying amount of the reporting unit should be considered when measuring the goodwill impairment loss, if applicable. The amendments also eliminate the requirements for any reporting unit with a zero or negative carrying amount to perform a qualitative assessment and, if it fails that qualitative test, to perform Step 2 of the goodwill impairment test. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary. This guidance is effective for annual or any interim goodwill impairment tests in fiscal years beginning after December 15, 2019. Early adoption is permitted. ASU 2017-04 should be adopted on a prospective basis. The Company is in the process of evaluating the potential impact of this new ASU on our consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, Leases, in order to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet for those leases classified as operating leases under previous Generally Accepted Accounting Principles ("GAAP"). The ASU 2016-02 requires that a lessee should recognize a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the underlying asset for the lease term on the balance sheet. In July 2018, the FASB issued ASU 2018-10, Codification Improvements to Topic 842, Leases, to clarify how to apply certain aspects of the new leases standard. In July 2018, the FASB also issued ASU 2018-11, Leases (Topic 842): Targeted Improvements, to give entities another option for transition and to provide lessors with a practical expedient to reduce the cost and complexity of implementing the new standard. The transition option allows entities to not apply the new leases standard in the comparative periods they present in their financial statements in the year of adoption. In December 2018, the FASB's issued ASU 2018-20, Leases (Topic 842): Narrow Scope Improvements for Lessors, which simplifies how lessors implement the new leasing guidance in ASC 842, Leases. ASU 2018-20 amends the guidance in ASC 842 as follows; lessors may elect to account for sales and other similar taxes collected from lessees as lessee costs and to exclude them from the consideration in the contract and from variable payments not included in the consideration in the contract, lessors should exclude from variable payments, and therefore from revenue, all costs paid by lessees directly to third parties, and lessors should allocate certain variable payments to lease and nonlease components when the facts and circumstances that trigger the variable payments occur. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018 (including interim periods within those periods) using a modified retrospective approach and early adoption is permitted. The Company is in the process of evaluating the impact of this new ASU on our consolidated financial statements.

2.
Changes in Accounting Principles

Except for the changes below, the Company has consistently applied the accounting principles to all periods presented in these consolidated financial statements. The Company adopted Topic 606 Revenue from Contracts with Customers with a date of the initial application of January 1, 2018. As a result, the Company has changed its accounting policies for revenue recognition as detailed below.

The Company applied Topic 606 retrospectively using the practical expedient in paragraph 606-10-65-1(f)(3), under which the Company does not disclose the amount of consideration allocated to the remaining performance obligations or an explanation of when the Company expects to recognize that amount as revenue for all reporting periods presented before the date of the initial application – i.e. January 1, 2018. The details of the significant changes and quantitative impact of the changes are disclosed below.

A.
Commission fees payable

The Company previously recognized management level indirect sales commission expense related to contracts as selling expenses when they were incurred. Under Topic 606, the Company capitalizes those commission fees as costs of obtaining a contract, when they are incremental and, if they are expected to be recovered, it amortizes them consistently with the pattern of transfer of the good or service over the specific contract life or the average contract life for the group of contracts that resulted in the achievement of the sales commissions. If the expected amortization period is one year or less, the commission fee is expensed when incurred. The adoption of this new accounting policy resulted in a cumulative adjustment to the accumulated deficit related to the incremental contract acquisition cost that was previously expensed being capitalized. Refer to Impacts to Previously Reported Results below for the impact of adoption of the standard on our consolidated financial statements.

B.
Principal versus agent considerations

For the majority of our contracts, we expect no changes. We have certain contracts where we recognize revenue from reselling third party products and services, such as broadband Internet access and professional website management services as a principal on a gross basis. Under Topic 606, the Company recognizes revenue on a net basis as an agent. The new standard focuses on control of the specified goods and service as the overarching principle and the Company does not control the delivery of the goods and services. The adoption of this new accounting policy required us to restate certain previously reported results, including the reduction of service revenue and related cost of service revenue. There was no impact on the accumulated deficit as a result of any changes to our current policy. Refer to Impacts to Previously Reported Results below for the impact of adoption of the standard on our consolidated financial statements.

The Company adopted ASU 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash, which requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash. As a result, amounts generally described as restricted cash are included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. Refer to Impacts of Previously Reported Results below for the impact of the standard on our consolidated financial statements.

Impacts to Previously Reported Results

Adoption of the standards related to revenue recognition and statement of cash flows impacted our previously reported results as follows:

		(Topic 606)	
Condensed Consolidated Balance Sheet		New Revenue	
December 31, 2017	As Previously	Standard	As
(In thousands)	Reported	Adjustment	Adjusted

Trade receivables, net of allowance for doubtful accounts	$375	$(3)	$372
Contract assets	-	3	3
Contract costs	-	379	379
Prepaid expenses	530	(279)	251
Total current assets	2,544	100	2,644
Long-term prepaid expenses	173	(173)	-
Contract costs, net of current portion	-	364	364
Total assets	3,446	291	3,737
Deferred revenue, current portion	957	(957)	-
Contract liabilities	-	614	614
Total current liabilities	2,066	(343)	1,723
Deferred revenue, net of current portion	31	(31)	-
Contract liabilities, net of current portion	-	374	374
Accumulated deficit	(59,235)	291	(58,944)
Total stockholders' equity	1,339	291	1,630
Total Liabilities and Stockholders' Equity	3,446	291	3,737

Condensed Consolidated Statement of Operations		(Topic 606)	
		New Revenue	
Year Ended December 31, 2017	As Previously	Standard	As
(In thousands, except per share amounts)	Reported	Adjustment	Adjusted
Service revenue	$9,030	$(190)	$8,840
Total revenue	10,377	(190)	10,187
Cost of service revenue	2,908	(191)	2,717
Selling and marketing	2,924	(91)	2,833
Total operating expenses	11,202	(281)	10,921
Loss from operations	(825)	91	(734)
Loss before income tax	(1,013)	91	(922)
Net loss	(1,020)	91	(929)
Diluted loss per share	$(0.07)	$-	$(0.07)

Condensed Consolidated Statements of Stockholders' Equity			Additional		Total
(In thousands)	Common Stock		Paid-in	Accumulated	Stockholders'
	Shares	Amount	Capital	Deficit	Equity
Balance at January 1, 2017, as previously reported	13,578,556	$14	$58,716	$(58,215)	$515
Impact of change in accounting principle	-	-	-	200	200
As adjusted balance at January 1, 2017	13,578,556	14	58,716	(58,015)	715
As adjusted net loss	709,000	-	1,844	(929)	915
As adjusted balance as of December 31, 2017	14,287,556	$14	$60,560	$(58,944)	$1,630

		(Topic 606)	(Topic 230)	
Condensed Consolidated Statement of Cash Flows		New Revenue	Statement of	
Year Ended December 31, 2017	As Previously	Standard	Cash Flows	As
(In thousands)	Reported	Adjustment	Adjustments	Adjusted

Net loss	$(1,020)	$91	$-	$(929)
Trade receivables	(17)	1	-	(16)
Contract assets	-	(1)	-	(1)
Contract costs	-	(40)	-	(40)
Prepaid expenses	180	(51)	-	129
Contract liabilities	-	136	-	136
Deferred revenue	136	(136)	-	-
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE PERIOD	619	-	(619)	-
CASH, CASH EQUIVALENTS, AND RESTRICTED CASH AT THE BEGINNING OF THE PERIOD	-	-	719	719
CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD	1,282	-	(1,282)	-
CASH, CASH EQUIVALENTS, AND RESTRICTED CASH AT THE END OF THE PERIOD	-	-	1,382	1,382

Adoption of the standards related to revenue recognition (Topic 606) and statement of cash flows presentation of restricted cash (Topic 230) had no impact to cash provided by or used for financing, or investing on our consolidated statement of cash flows.

3.
Revenue

Revenue is measured based on a consideration specified in a contract with a customer, and excludes any sales incentives and amounts collected on behalf of third parties. The Company recognizes revenue when it satisfies a performance obligation by transferring control over a product or service to a customer. Taxes assessed by a governmental authority that are both imposed on and concurrent with a specific revenue-producing transaction, that are collected by the Company from a customer, are excluded from revenue. The following is a description of principal activities – separated by reportable segments – from which the Company generates its revenue. For more detailed information about reportable segments, see Note 19.

Cloud Telecommunications Segment

Products and services may be sold separately or in bundled packages. The typical length of a contract for service is thirty-six to sixty months. Customers are billed for these services on a monthly basis. For bundled packages, the Company accounts for individual products and services separately if they are distinct – i.e. if a product or service is separately identifiable from other items in the bundled package and if a customer can benefit from it on its own or with other resources that are readily available to the customer. The consideration (including any discounts) is allocated between separate products and services in a bundle based on their relative stand-alone selling prices. The stand-alone selling prices are determined based on the prices at which the Company separately sells the desktop devices and telecommunication services. For items that are not sold separately (e.g. additional features) the Company estimates stand-alone selling prices using the adjusted market assessment approach. When we provide a free trial period, we do not begin to recognize recurring revenue until the trial period has ended and the customer has been billed for the services.

Desktop Devices - Revenue generated from the sale of telecommunications equipment (desktop devices) is recognized when the customer takes possession of the devices and the cloud telecommunications services begin. The Company typically bills and collects the fees for the equipment upon entering into a contract with a customer. Cash receipts are recorded as a contract liability until implementation is complete and the services begin.

Equipment Financing Revenue - Fees generated from renting our cloud telecommunication equipment (IP or cloud telephone desktop devices) through leasing contracts are recognized as revenue based on whether the lease qualifies as an operating lease or sales-type lease. The two primary accounting provisions which we use to classify transactions as sales-type or operating leases are: 1) lease term to determine if it is equal to or greater than 75% of the economic life of the equipment and 2) the present value of the minimum lease payments to determine if they are equal to or greater than 90% of the fair market value of the equipment at the inception of the lease. The economic life of most of our products is estimated to be three years, since this represents the most frequent contractual lease term for our products, and there is no residual value for used equipment. Residual values, if any, are established at the lease inception using estimates of fair value at the end of the lease term. The vast majority of our leases that qualify as sales-type leases are non-cancelable and include cancellation penalties approximately equal to the full value of the lease receivables. Leases that do not meet the criteria for sales-type lease accounting are accounted for as operating leases. Revenue from sales-type leases is recognized upon installation and the interest portion is deferred and recognized as earned. Revenue from operating leases in recognized ratably over the applicable service period.

Cloud Telecommunications Services - Telecommunication services include voice, data, and collaboration software. The Company recognizes revenue as services are provided in service revenue. Telecommunications services are billed and paid on a monthly basis.

Broadband Internet Access – Fees generated from reselling broadband Internet access are recognized as revenue net of the costs charged by the third party service providers. Broadband Internet access services are billed and paid on a monthly basis.

Professional Services Revenue – Professional services revenue includes activation fees and any professional installation services. Installation services are recognized as revenue when the services are completed. The Company generally allocates a portion of the activation fees to the desktop devices, which is recognized at the time of the installation or customer acceptance, and a portion to the service, which is recognized over the contract term using the straight-line method. Our telecommunications services contracts typically have a term of thirty-six to sixty months.

Commission Revenue - We have affiliate agreements with third-party entities that are resellers of satellite television services and Internet service providers. We receive commissions when the services are bundled with our offerings and we recognize commission revenue when received.

Web Services Segment

Website Hosting Service – Fees generated from hosting customer websites are recognized as revenue as the services are provided in service revenue. Website hosting services are billed and collected on a monthly basis.

Professional Website Management Service and Other– Fees generated from reselling professional website management services are recognized as revenue net of the costs charged by the third party service providers. Professional website management services are billed and paid on a monthly basis.

Disaggregation of Revenue

In the following table, revenue is disaggregated by primary major product line, and timing of revenue recognition. The table also includes a reconciliation of the disaggregated revenue with the reportable segments.

Three Months Ended December 31, 2018	Cloud		Total
(In thousands)	Telecommunications	Web Services	Reportable
	Segment	Segment	Segments
Major products/services lines			
Desktop devices	$330	$-	$330
Equipment financing revenue	22	-	22
Telecommunications services	2,343	-	2,343
Fees, commissions, and other, recognized over time	181	-	181
One time fees, commissions and other	32	-	32
Website hosting services	-	156	156
Website management services and other	-	33	33
	$2,908	$189	$3,097
Timing of revenue recognition			
Products and fees recognized at a point in time	$362	$-	$362
Services and fees transferred over time	2,546	189	2,735
	$2,908	$189	$3,097

Three Months Ended December 31, 2017	Cloud		Total
(In thousands)	Telecommunications	Web Services	Reportable
	Segment	Segment	Segments
	As Adjusted	As Adjusted	As Adjusted
Major products/services lines			
Desktop devices	$380	$-	$380
Equipment financing revenue	38	-	38
Telecommunications services	1,929	-	1,929
Fees, commissions, and other, recognized over time	138	-	138

One time fees, commissions and other	88	-	88
Website hosting services	-	212	212
Website management services and other	-	28	28
	$2,573	$240	$2,813
Timing of revenue recognition			
Products and fees recognized at a point in time	$468	$-	$468
Services and fees transferred over time	2,105	240	2,345
	$2,573	$240	$2,813

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Year Ended December 31, 2018	Cloud		Total
(In thousands)	Telecommunications	Web Services	Reportable
	Segment	Segment	Segments
Major products/services lines			
Desktop devices	$1,447	$-	$1,447
Equipment financing revenue	105	-	105
Telecommunications services	8,817	-	8,817
Fees, commissions, and other, recognized over time	629	-	629
One time fees, commissions and other	85	-	85
Website hosting services	-	708	708
Website management services and other	-	117	117
	$11,083	$825	$11,908
Timing of revenue recognition			
Products and fees recognized at a point in time	$1,532	$-	$1,532
Services and fees transferred over time	9,551	825	10,376
	$11,083	$825	$11,908

Year Ended December 31, 2017	Cloud		Total
(In thousands)	Telecommunications	Web Services	Reportable
	Segment	Segment	Segments
	As Adjusted	As Adjusted	As Adjusted
Major products/services lines			
Desktop devices	$1,347	$-	$1,347
Equipment financing revenue	187	-	187
Telecommunications services	6,992	-	6,992
Fees, commissions, and other, recognized over time	450	-	450
One time fees, commissions and other	165	-	165
Website hosting services	-	940	940
Website management services and other	-	106	106
	$9,141	$1,046	$10,187
Timing of revenue recognition			

Products and fees recognized at a point in time	$1,512	$-	$1,512
Services and fees transferred over time	7,629	1,046	8,675
	$9,141	$1,046	$10,187

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Contract balances

The following table provides information about receivables, contract assets, and contract liabilities from contracts with customers.

(In thousands)	December 31, 2018	December 31, 2017 As Adjusted
Receivables, which are included in Trade receivables, net of allowance for doubtful accounts	$429	$403
Contract assets	12	3
Contract liabilities	1,063	988

Significant changes in the contract assets and the contract liabilities balances during the period are as follows:

(In thousands)	For the Year Ended December 31, 2018		For the Year Ended December 31, 2017 As Adjusted	
	Contract assets	Contract Liabilities	Contract assets	Contract Liabilities
Revenue recognized that was included in the contract liability balance at the beginning of the period	$-	$(837)	$-	$(642)
Increase due to cash received, excluding amounts recognized as revenue during the period	-	912	-	778
Transferred to receivables from contract assets recognized at the beginning of the period	(2)	-	(1)	-
Increase due to additional unamortized discounts	11	-	2	-

Transaction price allocated to the remaining performance obligations

The following table includes estimated revenue expected to be recognized in the future related to performance obligations that are unsatisfied (or partially unsatisfied) at the end of the reporting period (in thousands):

	2019	2020	2021	2022	2023	Total
Desktop devices	$262	-	-	-	-	$262
Telecommunications service	$8,716	6,338	4,512	2,562	639	$22,767
All consideration from contracts with customers is included in the amounts presented above						

The Company applies the transition practical expedient in paragraph 606-10-65-1(f)(3) and does not disclose the amount of the transaction price allocated to the remaining performance obligations and an explanation of when the Company expects to recognize that amount as revenue for the year ended December 31, 2017.

4.
Net Loss Per Common Share

Basic net loss per common share is computed by dividing the net loss for the period by the weighted-average number of common shares outstanding during the period. Diluted net loss per common share is computed giving effect to all dilutive common stock equivalents, consisting of common stock options and warrants. Diluted net loss per common share for the year ended December 31, 2018 and 2017 is the same as basic net loss per common share as the common share equivalents were anti-dilutive due to the net loss. The following table sets forth the computation of basic and diluted net loss per common share:

	Year Ended December 31,	
		2017
	2018	As Adjusted
Net loss (in thousands)	$(223)	$(929)
Weighted-average share reconciliation:		
Weighted-average shares outstanding	14,332,092	13,938,342
Weighted-average basic shares outstanding	14,332,092	13,938,342
Diluted shares outstanding	14,332,092	13,938,342
Net loss per common share:		
Basic	$(0.02)	$(0.07)
Diluted	$(0.02)	$(0.07)

Common stock equivalent shares are not included in the computation of diluted loss per share, as the Company has a net loss and the inclusion of such shares would be anti-dilutive due to the net loss. At December 31, 2018 and 2017, the common stock equivalent shares were, as follows:

	Year Ended December 31,	
	2018	2017
Shares of common stock issuable under equity incentive plans outstanding	3,664,000	3,648,939
Common stock equivalent shares excluded from diluted net loss per share	3,664,000	3,648,939

5.
Trade Receivables, net

Our trade receivables balance consists of traditional trade receivables and residual Extended Payment Term Agreements (EPTAs) sold prior to July 2011. Below is an analysis of our trade receivables as shown on our balance sheet (in thousands):

	December 31,	
	2018	2017
Gross trade receivables	$443	$432
Less: allowance for doubtful accounts	(14)	(29)
Trade receivables, net	$429	$403
Current trade receivables, net	$419	$372
Long-term trade receivables, net	10	31
Trade receivables, net	$429	$403

6.
Equipment Financing Receivables

We rent certain cloud telecommunication equipment (IP desktop devices) through leasing contracts that we classify as either operating leases or sale-type leases. Equipment finance receivables are expected to be collected over the next thirty-six to sixty months. Equipment finance receivables arising from the rental of our cloud telecommunications equipment through sales-type leases, were as follows (in thousands):

	December 31,	
	2018	2017
Gross financing receivables	$392	$264
Less unearned income	(141)	(90)
Financing receivables, net	251	174
Less: Current portion of finance receivables, net	(67)	(116)
Finance receivables due after one year	$184	$58

7.
Prepaid Expenses

Prepaid expenses consisted of the following (in thousands):

	December 31,	
		2017
	2018	As Adjusted
Prepaid corporate insurance	$43	$44
Prepaid software services	28	17
Prepaid tax liability deposit	48	-
Prepaid inventory deposits	61	117
Other prepaid expenses	64	73
Total prepaid assets	$244	$251

8.
Property and Equipment

Property and equipment consisted of the following (in thousands):

December 31,

	2018	2017
Software	$333	$681
Computers and office equipment	1,524	1,685
Leasehold improvements	25	27
Less accumulated depreciation and amortization	(1,758)	(2,385)
Total property and equipment, net	$124	$8

Depreciation and amortization expense is included in general and administrative expenses and totaled $20,000 and $10,000 for the years ended December 31, 2018 and 2017, respectively.

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9.
Intangible Assets

The net carrying amount of intangible assets is as follows (in thousands):

	December 31,	
	2018	2017
Customer relationships	$941	$941
Less: accumulated amortization	(774)	(702)
Total	$167	$239

Amortization expense is included in general and administrative expenses and totaled $72,000 and $96,000 for the years ended December 31, 2018 and 2017, respectively.

The following table outlines the estimated future amortization expense related to intangible assets held at December 31, 2018 (in thousands):

Year ending December 31,	
2019	$(53)
2020	(39)
2021	(29)
2022	(21)
2023	(18)
Thereafter	(7)
Total	$(167)

10.
Goodwill

The Company has recorded goodwill as a result of its business acquisitions. Goodwill is recorded when the purchase price paid for an acquisition exceeds the estimated fair value of the net identified tangible and intangible assets acquired. In each of the Company’s acquisitions, the objective of the acquisition was to expand the Company’s product offerings and customer base and to achieve synergies related to cross selling opportunities, all of which contributed to the recognition of goodwill

The Company tests goodwill for impairment on an annual basis or more frequently if events or changes in circumstances indicate that goodwill might be impaired. The changes in the carrying amount of goodwill for the years ended December 31, 2018 and 2017 were as follows (in thousands):

	Acquisition Related Goodwill

Balance at January 1, 2017	$272
Increase (decrease)	-
Balance at December 31, 2017	272
Increase (decrease)	-
Balance at December 31, 2018	$272

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11.
Accrued Expenses

Accrued expenses consisted of the following (in thousands):

	December 31,	
	2018	2017
Accrued wages and benefits	$301	$303
Accrued accounts payable	243	242
Accrued sales and telecommunications taxes	480	343
Product warranty liability	16	-
Other	91	73
Total accrued expenses	$1,131	$961

The changes in aggregate product warranty liabilities for the years ended December 31, 2018 and 2017 were as follows (in thousands):

	Warranty Liabilities
Balance at January 1, 2017	$-
Accrual for warranties	10
Warranty settlements	(10)
Balance at December 31, 2017	-
Accrual for warranties	31
Warranty settlements	(15)
Balance at December 31, 2018	$16

Product warranty expense is included in cost of product revenue expense and totaled $31,000 and $10,000 for the years ended December 31, 2018 and 2017, respectively.

12.
Notes Payable

Related Party Note Payable

On December 30, 2015, Crexendo, Inc. (the "Company") entered into a Term Loan Agreement (the "Loan Agreement"), with Steven G. Mihaylo, as Trustee of The Steven G. Mihaylo Trust dated August 19, 1999 (the "Lender"). Mr. Mihaylo is the principal shareholder and Chief Executive Officer of the Company. The term of the Loan is five years, with simple interest paid at 9% per annum until a balloon payment is due December 30, 2020. The Loan Agreement provides for interest to be paid in shares of common stock of the Company (the “Common Stock”) at a stock price of $1.20. For the first two years of the Loan term, interest will be paid in advance at the beginning of each year; for the last three years of the Loan term, interest will be paid at the end of each year. After the second year of the Loan term, there is no pre-payment penalty for early repayment of the outstanding principal amount of the Loan. If the Loan is repaid within the first two years of the Loan term, the Company will forfeit prepaid interest as a pre-payment penalty.

In February 2017, the Company entered into a second amendment to our Loan Agreement with Steven G. Mihaylo. The amendment extends the ability of the Board of Directors to request the remaining $1.0 million available under the Loan Agreement if necessary to fund operations through May 30, 2018. All other terms remain the same as initial loan agreement.

In September 2017, Steven G. Mihaylo exercised 444,999 options for a total strike price of $974,000. In December 2017, Steven G. Mihaylo exercised 12,001 options for a total strike price of $22,000. The Company used the proceeds from the stock options exercise to repay $996,000 of the $1.0 million outstanding related party note payable. During the year ended December 31, 2017, the Company accelerated the amortization of the debt discount in the amount of $77,000 as a result of the repayment.

In September 2018, the Company repaid the remaining $4,000 of the $1.0 million related party note payable.

Other notes payable

Other notes payable consists of short and long-term financing arrangements for software licenses, subscriptions, support and corporate insurance.

The Company's outstanding balances under its note payable agreements as of December 31, 2018 and 2017 were as follows (in thousands):

	Year Ended December 31,	
	2018	2017
Related-party note payable	$-	$4
Other notes payable	56	75
Total notes payable	56	79
Less: notes payable, current portion	(56)	(69)
Notes payable, net of current portion	$-	$10

As of December 31, 2018, future principal payments are scheduled as follows (in thousands):

Year ending December 31,	
2019	$56
Total	$56

13.
Fair Value Measurements

We have financial instruments as of December 31, 2018 and 2017 for which the fair value is summarized below (in thousands):

	December 31, 2018		December 31, 2017	
	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
Assets:				
Trade receivables, net	$429	$429	$403	$403
Equipment financing receivables	251	251	174	174
Liabilities:				
Capital lease obligations	$144	$144	$-	$-
Notes payable	56	56	79	79

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14.
Equity

Common Stock

Shares of common stock reserved for future issuance as of December 31, 2018 were as follows:

Stock-based compensation plans:

Outstanding option awards	3,664,000
Available for future grants	1,853,852
	5,517,852

15.
Stock-Based Compensation

We have various incentive stock-based compensation plans that provide for the grant of stock options, restricted stock units (RSUs), and other share-based awards of up to 5,517,852 shares to eligible employees, consultants, and directors. As of December 31, 2018, we had 1,853,852 shares remaining in the plans available to grant.

Stock Options

The weighted-average fair value of stock options on the date of grant and the assumptions used to estimate the fair value of stock options granted during the years ended December 31, 2018 and 2017 using the Black-Scholes option-pricing model were as follows:

	Year Ended December 31,	
	2018	2017
Weighted-average fair value of options granted	$1.86	$0.78
Expected volatility	88%	60%
Expected life (in years)	4.30	4.30
Risk-free interest rate	2.69%	1.98%
Expected dividend yield	0.00%	0.00%

The expected volatility of the options is determined using historical volatilities based on historical stock prices. The expected life of the options granted is based on our historical share option exercise experience. The risk-free interest rate is determined using the yield available for zero-coupon U.S. government issues with a remaining term equal to the expected life of the option. The Company has not declared any dividends, therefore, it is assumed to be zero.

The following table summarizes the stock option activity under the plans for the years ended December 31, 2018 and 2017:

	Number of Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contract Life	Aggregate Intrinsic Value (in thousands)
Outstanding at January 1, 2017	3,932,114	$2.59	5.2 years	$400
Granted	527,500	1.59		
Exercised	(607,000)	1.92		
Cancelled/forfeited	(203,675)	1.61		
Outstanding at December 31, 2017	3,648,939	2.61	4.3 years	1,346
Granted	329,000	2.83		
Exercised	(106,557)	1.46		
Cancelled/forfeited	(207,382)	1.72		
Outstanding at December 31, 2018	3,664,000	2.71	3.5 years	1,007
Shares vested and expected to vest	3,593,178	2.71	3.5 years	997
Exercisable as of December 31, 2018	3,363,569	2.73	3.3 years	968
Exercisable as of December 31, 2017	3,185,420	2.78	4.1 years	1,037

The total intrinsic value of options exercised during the years ended December 31, 2018 and 2017, was $107,000 and $59,000 respectively.

As of December 31, 2018, the total future compensation expense related to non-vested options not yet recognized in the consolidated statements of operations was approximately $452,000 and the weighted-average period over which these awards are expected to be recognized is approximately 2.1 years.

Restricted Stock Units:

The following table summarizes the RSUs activity under the plans for the years ended December 31, 2018 and 2017:

	Number of Units	Weighted-Average Fair Value
Outstanding at January 1, 2017	-	$-
Granted	27,000	1.60
Vested	(27,000)	1.60
Cancelled/forfeited	-	-
Outstanding at December 31, 2017	-	-
Granted	-	-
Vested	-	-

Cancelled/forfeited	-	-
Outstanding at December 31, 2018	-	-

The weighted-average grant-date fair value of RSUs granted during the years ended December 31, 2018 and 2017 was $0 and $1.60, respectively.

The following table summarizes the statement of operations effect of stock-based compensation for the years ended December 31, 2018 and 2017 (in thousands):

	Year Ended December 31,	
	2018	2017
Share-based compensation expense by type:		
Stock options	$438	$530
Restricted stock units	-	43
Total cost related to share-based compensation expense	$438	$573
Share-based compensation expense by financial statement line item:		
Cost of revenue	$136	$93
Research and development	71	85
Selling and marketing	69	74
General and administrative	162	321
Total cost related to share-based compensation expense	$438	$573

There is no tax benefit related to stock compensation expense due to a full valuation allowance on net deferred tax assets at December 31, 2018 and 2017, respectively.

16. Income Taxes

The income tax expense/(benefit) consisted of the following for the years ended December 31, 2018 and 2017 (in thousands):

	Year Ended December 31,	
	2018	2017
Current income tax expense:		
Federal	$-	$-
State and local	15	7
Current income tax expense	$15	$7

There was no deferred income tax expense (benefit) for the years ended December 31, 2018 and 2017.

The income tax provision attributable to loss before income tax benefit for the years ended December 31, 2018 and 2017 differed from the amounts computed by applying the U.S. federal statutory tax rate of 21% and 34.0%, respectively, as a result of the following (in thousands):

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	Year Ended December 31,	
	2018	2017 As Adjusted
U.S. federal statutory income tax benefit	$(43)	$(314)
Increase in income tax benefit resulting from:		
State and local income tax expense, net of federal effect	539	995
Change in the valuation allowance for net deferred income tax assets	(583)	(5,472)
Change in the tax rate for net deferred income tax assets	-	4,527
Other, net	102	271
Income tax expense	$15	$7

As of December 31, 2018 and 2017, significant components of net deferred income tax assets and liabilities were as follows (in thousands):

	December 31,	
	2018	2017 As Adjusted
Deferred income tax assets:		
Accrued expenses	$45	$41
Deferred revenue	278	255
Net operating loss carry-forwards	5,946	6,449
Foreign tax credits	-	-
Stock-based compensation	2,258	2,242
Property and equipment	-	4
Other	505	554
Subtotal	9,032	9,545
Valuation allowance	(8,755)	(9,338)
Total deferred income tax assets	277	207
Deferred income tax liabilities:		
Property and equipment	(28)	-
Prepaid expenses and other	(249)	(207)
Total deferred income tax liabilities	(277)	(207)

Net deferred income tax assets (liabilities)	$-	$-

During the fiscal year ended June 30, 2002 (our fiscal year was subsequently changed to December 31), we experienced a change in ownership, as defined by the Internal Revenue Code, as amended (the "Code") under Section 382. A change of ownership occurs when ownership of a company increases by more than 50 percentage points over a three-year testing period of certain stockholders. As a result of this ownership change we determined that our annual limitation on the utilization of our federal pre-ownership change net operating loss ("NOL") carry-forwards is approximately $461,000 per year. We will only be able to utilize $5,761,000 of our pre-ownership change NOL carry-forwards and will forgo utilizing $14,871,000 of our pre-ownership change NOL carry-forwards as a result of this ownership change. We do not account for forgone NOL carryovers in our deferred tax assets and only account for the NOL carry-forwards that will not expire unutilized as a result of the restrictions of Code Section 382.

As of December 31, 2018, we had NOL and research and development tax credit carry-forwards for U.S. federal income tax reporting purposes of approximately $22,722,000 and $129,000 respectively. $22,485,000 of the NOLs will begin to expire in 2020 through 2037, and the remaining $237,000 of the NOLs will not expire. The research and development credits will begin to expire in 2019 through 2020.

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We also have state NOL and research and development credit carry-forwards of approximately $18,060,000 and $61,000 which expire on specified dates as set forth in the rules of the various states to which the carry-forwards relate.

We also have foreign NOL carry-forwards of approximately $710,000 which expire on specified dates as set forth in the rules of the various countries in which the carry-forwards relate.

In assessing the recovery of the deferred tax assets, we considered whether it is more likely than not that some portion or all of our deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income in the periods in which those temporary differences become deductible. We considered the scheduled reversals of future deferred tax liabilities, projected future taxable income, from telecommunications services segment, the suspension of the sale of product and services through the direct mail seminar sales channel for our web services segment, and tax planning strategies in making this assessment. As a result, we determined it was more likely than not that the deferred tax assets would not be realized as of December 31, 2018 and 2017; accordingly, we recorded a full valuation allowance. The valuation allowance for deferred tax assets as of December 31, 2018 and 2017 was $8,755,000 and $9,338,000 respectively.

On December 22, 2017, the Tax Cuts and Jobs Act of 2017 (“Tax Act”) was signed into law. The new law includes, among other items, a permanent reduction to the U.S. corporate income tax rate from 34% to 21% effective January 1, 2018. As a result of the reduction of the corporate income tax rate to 21.0%, U.S. GAAP requires companies to remeasure their deferred tax assets and liabilities as of the date of enactment, with resulting tax effects accounted for in the reporting period of enactment. The Company remeasured deferred tax assets and liabilities based on the rates at which they are expected to be utilized in the future. As a result, our net deferred tax assets, without regard to the valuation allowance, decreased by $4.5 million. This decrease was offset by a corresponding decrease in our valuation allowance. There was no charge to our income tax expense as a result of the reduction in corporate income tax rate.

The net change in our valuation allowance was a decrease of $583,000 for the year ended December 31, 2018 and an increase of $5,472,000 for the year ended December 31, 2017.

Accounting guidance clarifies the accounting for uncertain tax positions and requires companies to recognize the impact of a tax position in their financial statements, if that position is more likely than not of being sustained on audit, based on the technical merits of the position.

Although we believe our estimates are reasonable, there can be no assurance that the final tax outcome of these matters will not be different from that which we have reflected in our historical income tax provisions and accruals. Such difference could have a material impact on our income tax provision and operating results in the period in which it makes such determination.

The aggregate changes in the balance of unrecognized tax benefits during the years ended December 31, 2018 and 2017 were as follows (in thousands):

Balance as of January 1, 2017	$891
Reductions due to lapsed statute of limitations	(891)
Balance as of December 31, 2017	-
Reductions due to lapsed statute of limitations	-
Balance as of December 31, 2018	$-

Estimated interest and penalties related to the underpayment or late payment of income taxes are classified as a component of income tax provision in the consolidated statements of operations. There were no accrued interest and penalties as of December 31, 2018 and 2017, respectively.

Our U.S. federal income tax returns for fiscal 2015 through 2018 are open tax years. We also file in various states, with few exceptions, we are no longer subject to state income tax examinations by tax authorities for years prior to fiscal 2014.

17.
Commitments and Contingencies

Capital Lease Obligations

The Company leases equipment and support under a capital lease agreement which extends through 2023. The outstanding balance for capital leases was $144,000 and $0 as of December 31, 2018 and December 31, 2017, respectively. The Company recorded assets under capital lease obligations of $129,000 and $0 as of December 31, 2018 and December 31, 2017, respectively. Related accumulated depreciation totaled $15,000 and $0 as of December 31, 2018 and December 31, 2017, respectively. The $25,000 support contract has been classified as a prepaid expense that will be amortized over the service period of 3 years. Amortization expense is included in general and administrative expenses and totaled $8,000 and $0 for the year ended December 31, 2018 and 2017, respectively. The interest rate on the capital lease obligation is 6.7% and interest expense was $4,000 and $0 for the year ended December 31, 2018 and 2017, respectively. Future minimum capital lease payments at December 31, 2018 were as follows (in thousands):

Year ending December 31,	
2019	$36
2020	37
2021	36
2022	37
2023	21
Total minimum lease payments	167
Less: amount representing interest	23
Present value of minimum lease payments	$144

Operating Leases

We lease office space under non-cancelable operating lease agreements. We had one lease agreement in Reno, NV, which expired at the end of the third quarter of 2018. The operating lease for our Reno, NV office contained customary escalation clauses. Rental expense incurred on operating leases for the year ended December 31, 2018 and 2017 was approximately $15,000 and $20,000, respectively.

Sale-Leaseback

On February 28, 2014, the Company sold and leased back the land, building and furniture associated with the corporate headquarters in Tempe, Arizona to a Company that is owned by the major shareholder and CEO of the Company for $2.0 million in cash. The Company recognized a deferred gain of $281,000 on sale-leaseback, which was amortized over the initial lease term of 36 months to offset rent expense. Deferred gain amortization for the years ended December 31, 2018 and 2017 was $0 and $16,000, respectively.

Effective March 1, 2017 the rent agreement was renewed for a three year term with rent payable in cash. Rent expense incurred on the sale-leaseback during the years ended December 31, 2018 and 2017 was $300,000 and $288,000, respectively.

Future aggregate minimum lease obligations under the operating lease and sale-leaseback as of December 31, 2018, exclusive of taxes and insurance, are as follows (in thousands):

Year ending December 31,	
2019	$300
2020	50
Total	$350

Legal Proceedings

From time to time we receive inquiries from federal, state, city and local government officials as well as the FCC and taxing authorities in the various jurisdictions in which we operate. These inquiries and investigations related primarily to our discontinued seminar operations and concern compliance with various city, county, state, and/or federal regulations involving sales, representations made, customer service, refund policies, services and marketing practices. We respond to these inquiries and have generally been successful in addressing the concerns of these persons and entities, without a formal complaint or charge being made, although there is often no formal closing of the inquiry or investigation. There can be no assurance that the ultimate resolution of these or other inquiries and investigations will not have a material adverse effect on our business or operations, or that a formal complaint will not be initiated. We also receive complaints and inquiries in the ordinary course of our business from both customers and governmental and non-governmental bodies on behalf of customers, and in some cases these customer complaints have risen to the level of litigation. There can be no assurance that the ultimate resolution of these matters will not have a material adverse effect on our business or results of operations.

We are also subject to various claims and legal proceedings covering matters that arise in the ordinary course of business. We believe that the resolution of these other cases will not have a material adverse effect on our business, financial position, or results of operations.

We have recorded liabilities of approximately $0 and $0 as of December 31, 2018 and 2017, respectively, for estimated losses resulting from various legal proceedings in which we are engaged. Attorney’s fees associated with the various legal proceedings are expensed as incurred. We are also subject to various claims and legal proceedings covering matters that arise in the ordinary course of business. We believe that the resolution of these other cases will not have a material adverse effect on our business, financial position, or results of operations.

18.
Employee Benefit Plan

We have established a retirement savings plan for eligible employees. The plan allows employees to contribute a portion of their pre-tax compensation in accordance with specified guidelines. For the years ended December 31, 2018 and 2017, we contributed approximately $115,000 and $111,000 to the retirement savings plan, respectively.

19.
Segments

Management has chosen to organize the Company around differences based on its products and services. Cloud Telecommunications segment generates revenue from selling cloud telecommunication products and services and broadband Internet services. Web Services segment generates revenue from website hosting and other professional services. The Company has two operating segments, which consist of Cloud Telecommunications and Web Services.

Segment revenue and income/(loss) before income tax provision was as follows (in thousands):

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	Year Ended December 31,	
	2018	2017 As Adjusted
Revenue:		
Cloud telecommunications	$11,083	$9,141
Web services	825	1,046
Consolidated revenue	11,908	10,187
Income/(loss) from operations:		
Cloud telecommunications	(613)	(1,239)
Web services	407	505
Total operating loss	(206)	(734)
Other income/(expense), net:		
Cloud telecommunications	5	(183)
Web services	(7)	(5)
Total other expense, net	(2)	(188)
Income/(loss) before income tax provision		
Cloud telecommunications	(608)	(1,422)
Web services	400	500
Loss before income tax provision	$(208)	$(922)

Depreciation and amortization was $86,000 and $95,000 for the Cloud Telecommunications segment for the years ended December 31, 2018 and 2017, respectively. Depreciation and amortization was $6,000 and $11,000 for the Web Services segment for the years ended December 31, 2018 and 2017, respectively.

Interest income was $7,000 and $10,000 for the Web Services segment for the years ended December 31, 2018 and 2017, respectively.

Interest expense was $12,000 and $189,000 for the Cloud Telecommunications segment for the years ended December 31, 2018 and 2017 respectively. Interest expense was $0 and $20,000 for the Web Services segment for the years ended December 31, 2018 and 2017, respectively.

20.
Quarterly Financial Information (in thousands, unaudited)

	For the three months ended			
Consolidated	March 31,	June 30,	September 30,	December 31,
	2018	2018	2018	2018
Service revenue	$2,442	$2,540	$2,712	$2,767
Product revenue	366	437	314	330
Total revenue	2,808	2,977	3,026	3,097
Operating expenses:				
Cost of service revenue	729	731	833	799
Cost of product revenue	187	201	161	178
Selling and marketing	829	767	910	897
General and administrative	945	1,034	1,101	1,011
Research and development	181	194	214	212
Total operating expenses	2,871	2,927	3,219	3,097
Income/(loss) from operations	(63)	50	(193)	-
Total other income/(expense), net	4	-	2	(8)
Income/(loss) before income taxes	(59)	50	(191)	(8)
Income tax provision	(4)	(3)	(8)	-
Net income/(loss)	$(63)	$47	$(199)	$(8)
Basic net income/(loss) per common share (1)	$(0.00)	$0.00	$(0.01)	$(0.00)
Diluted net income/(loss) per common share (1)	$(0.00)	$0.00	$(0.01)	$(0.00)

	For the three months ended			
Consolidated	March 31,	June 30,	September 30,	December 31,
	2017	2017	2017	2017
	As Adjusted	As Adjusted	As Adjusted	As Adjusted
Service revenue	$2,015	$2,133	$2,259	$2,433
Product revenue	279	303	385	380
Total revenue	2,294	2,436	2,644	2,813
Operating expenses:				
Cost of service revenue	644	654	664	755
Cost of product revenue	108	124	151	166

Selling and marketing	662	684	735	752
General and administrative	1,171	1,009	954	938
Research and development	190	185	194	181
Total operating expenses	2,775	2,656	2,698	2,792
Income/(loss) from operations	(481)	(220)	(54)	21
Total other income/(expense), net	(30)	(32)	(128)	2
Income/(loss) before income taxes	(511)	(252)	(182)	23
Income tax benefit/(provision)	(4)	(4)	(8)	9
Net income/(loss)	$(515)	$(256)	$(190)	$32
Basic net income/(loss) per common share (1)	$(0.04)	$(0.02)	$(0.01)	$0.00
Diluted net income/(loss) per common share (1)	$(0.04)	$(0.02)	$(0.01)	$0.00

(1)
Net income (loss) per common share is computed independently for each of the quarters presented. Therefore, the sums of quarterly net income (loss) per common share amounts do not necessarily equal the total for the twelve month periods presented.

ITEM 9.
CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None

ITEM 9A.
CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures pursuant to Rule 13(a)-15(b) under the Exchange Act, as the end of the period covered by this annual report on Form 10-K.

Based on this evaluation, our chief executive officer and chief financial officer concluded that, as of December 31, 2018 our disclosure controls and procedures are designed at a reasonable assurance level and are effective to provided reasonable assurance that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time period 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.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting that occurred during the year ended December 31, 2018 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Management's Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in Rule 13a-15(f) of the Exchange Act. Our management conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in Internal Control- Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 Framework). Based on this assessment, management concluded that our internal control over financial reporting was effective as of December 31, 2018.

Limitations of Effectiveness of Control and Procedures

In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. In addition, the design of disclosure controls and procedures must reflect the fact that there are resource constraints and that management is required to apply its judgment in evaluating the benefits of possible controls and procedures relative to their costs.

ITEM 9B.
OTHER INFORMATION

None

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PART III

ITEM 10.
DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Information with respect to this item will be set forth in the definitive proxy statement to be delivered to stockholders in connection with the 2019 Annual Meeting of Stockholders (the “Proxy Statement”). Such information is incorporated herein by reference.

We have adopted a code of ethics that applies to all employees, including employees of our subsidiaries, as well as each member of our Board of Directors. The code of ethics is available at our website at www.crexendo.com.

ITEM 11.
EXECUTIVE COMPENSATION

Information with respect to this item will be set forth in the Proxy Statement under the heading “Executive Compensation and Other Matters,” and is incorporated herein by reference.

ITEM 12.
SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDERS MATTERS

Information with respect to this item will be set forth in the Proxy Statement under the heading “Beneficial Ownership of Shares,” and is incorporated herein by reference.

ITEM 13.
CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

Information with respect to this item will be set forth in the Proxy Statement under the heading “Corporate Governance” and is incorporated herein by reference.

ITEM 14.
PRINCIPAL ACCOUNTANT FEES AND SERVICES

Information with respect to this item will be set forth in the Proxy Statement under the headings “Fees of Independent Registered Public Accounting Firm” and “Pre-Approval Policies and Procedures,” and is incorporated herein by reference.

PART IV

ITEM 15.
EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

Documents filed as part of this Report:

1.
Financial Statements – consolidated financial statements of Crexendo, Inc. and subsidiaries as set forth under Item 8 of this Report.
2.
The Financial Statement Schedule on page 66 of this Annual Report.
3.
Exhibit Index as seen below.

EXHIBIT INDEX

Exhibit No.	Exhibit Description	Incorporated By Reference Form	Date	Number	Filed Herewith
2.1	Agreement and Plan of Merger dated February 28, 2000 by and among Netgateway, Inc., Galaxy Acquisition Corp. and Galaxy Enterprises, Inc.	8-K	3/21/00	10.1	
3.1	Certificate of Incorporation	S-1	6/1/99	3.1	
3.2	Certificate of Amendment to Certificate of Incorporation	S-1	9/7/00	3.1	
3.3	Certificate of Amendment to Certificate of Incorporation	10-K	10/15/02	3.3	
3.4	Amended and Restated Bylaws	10-Q	11/20/01	3.2	
3.5	Certificate of Ownership and Merger (4)	S-1/A	11/12/99	3.3	
3.6	Articles of Merger	S-1/A	11/12/99	3.4	
4.1	Form of Common Stock Certificate	10-K	10/15/02	4.1	
4.2*	Form of Representatives' Warrant	S-1	6/1/99	4.1	
10.1*	1998 Stock Compensation Program	S-1	6/1/99	10.6	
10.2*	Amended and Restated 1998 Stock Option Plan for Senior Executives	10-K	9/29/03	10.2	
10.3*	Amended and Restated 1999 Stock Option Plan for Non-Executives	10-K	9/29/03	10.3	
10.5*	2003 Equity Incentive Plan	10-K	9/10/04	10.11	
10.6*	2013 Long-Term Incentive Plan	14A	4/30/13		
10.7	Deed of Sale, dated February 28, 2014, from Crexendo, Inc. to SGM EXE, LLC.	8-K	3/4/14	10.1	
10.8	Lease Agreement dated as of March 1, 2014 between Crexendo, Inc. and SGM EXE, LLC.	8-K	3/4/14	10.2	
10.9	Stock Purchase Agreement, dated December 24, 2014 between Crexendo, Inc. and CEO Steven G. Mihaylo	8-K	12/24/14	10.1	
10.10	Term Loan Agreement, dated December 31, 2015 between Crexendo, Inc. and CEO Steven G. Mihaylo	8-K	12/31/15	10.1	
10.11	Amendment to a term Loan Agreement, dated June 28, 2016, between Crexendo, Inc. and Steven G. Mihaylo, as Trustee of the Steven G. Mihaylo Trust dated August 19, 1999	8-K	6/30/16	10.1	
10.12		8-K	12/14/16	3.1	

	Reincorporation in state of Nevada for Crexendo, Inc. (Nevada) Articles of Incorporation				
10.13	Reincorporation in state of Nevada for Crexendo, Inc. (Nevada) bylaws	8-K	12/14/16	3.2	
10.14	Amendment to a term Loan Agreement, dated February 27, 2017, between Crexendo, Inc. and Steven G. Mihaylo, as Trustee of the Steven G. Mihaylo Trust dated August 19, 1999	8-K	3/2/17	10.1	
21.1	Subsidiaries of Crexendo, Inc.				X
23.1	Consent of Independent Registered Public Accounting Firm (Urish Popeck & Co., LLC)				X
31.1	Certification Pursuant to Rules 13a-14(a) under the Securities Exchange Act of 1934 as amended				X
31.2	Certification Pursuant to Rules 13a-14(a) under the Securities Exchange Act of 1934 as amended				X
32.1	Certification Pursuant to 18 U.S.C. Section 1350				X
32.2	Certification Pursuant to 18 U.S.C. Section 1350				X
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				

* Indicates a management contract or compensatory plan or arrangement.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

		CREXENDO, INC.
Date: March 5, 2019	By:	/s/ Steven G. Mihaylo Steven G. Mihaylo Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Date: March 5, 2019	By:	/s/ Steven G. Mihaylo Steven G. Mihaylo Chief Executive Officer, Chairman of the Board of Directors
Date: March 5, 2019	By:	/s/ RONALD VINCENT Ronald Vincent Chief Financial Officer
Date: March 5, 2019	By:	/s/ Todd Goergen Todd Goergen Director
Date: March 5, 2019	By:	/s/ Jeff Bash Jeff Bash Director
Date: March 5, 2019	By:	/s/ David Williams David Williams Director
Date: March 5, 2019	By:	/s/ Anil Puri Anil Puri Director

CREXENDO, INC. AND SUBSIDIARIES
Schedule II- Valuation and Qualifying Accounts

	Balance at Beginning of Year	Additions	Deductions	Balance at End of Year
	(in thousands)			
Year ended December 31, 2018				
Allowance for doubtful accounts receivable	$29	-	(15)	$14
Deferred income tax asset valuation allowance	$9,338	-	(583)	$8,755
Year ended December 31, 2017, As Adjusted				
Allowance for doubtful accounts receivable	$47	-	(18)	$29
Deferred income tax asset valuation allowance	$14,810	-	(5,472)	$9,338