Staffing 360 Solutions, Inc.
Form 10-Q
August 14, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2018

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from ________ to _________

Commission File Number: 001-37575

STAFFING 360 SOLUTIONS, INC.

(Exact name of registrant as specified in its charter)

DELAWARE	68-0680859
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

641 Lexington Avenue, Suite 2701

New York, New York 10022

(Address of principal executive offices) (Zip Code)

(646) 507-5710

(Registrant's telephone number, including area code)

N/A

(Former name, former address and former fiscal year, if changed since last report)

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

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

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

Large Accelerated Filer		Accelerated Filer
Non-Accelerated Filer	(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 Exchange Act). Yes No

As of August 14, 2018, there were 4,720,377 outstanding common stock shares, par value $0.00001 per share, of the issuer.

Form 10-Q Quarterly Report

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PART I-FINANCIAL INFORMATION

Item 1. Financial Statements

STAFFING 360 SOLUTIONS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(All amounts in thousands, except share, par values and stated values)

	June 30, 2018 (Unaudited)	December 30, 2017
ASSETS		
Current Assets:		
Cash	$ 2,886	$ 3,100
Accounts receivable, net	28,985	33,392
Prepaid expenses and other current assets	1,421	1,443
Total Current Assets	33,292	37,935
Property and equipment, net	1,469	1,618
Identifiable intangible assets, net	16,572	17,145
Goodwill	28,714	27,169
Other assets	2,923	2,881
Total Assets	$ 82,970	$ 86,748
LIABILITIES AND STOCKHOLDERS' DEFICIT		
Current Liabilities:		
Accounts payable and accrued expenses	$ 22,221	$ 16,709
Current portion of debt, net	683	245
Accounts receivable financing	15,988	25,983
Other current liabilities	7,524	6,372
Total Current Liabilities	46,416	49,309
Term loan - related party, net	40,342	38,749
Warrant Liability	—	1,426
Other long-term liabilities	4,034	4,049
Total Liabilities	90,792	93,533
Commitments and contingencies	—	—
Stockholders' Deficit:		
Staffing 360 Solutions, Inc. Equity:		
Preferred stock, $0.00001 par value, 20,000,000 shares authorized;		
Series A Preferred Stock - Related Party, 1,663,008 shares designated, $1.00 stated value, 1,663,008 shares issued and outstanding, as of June 30, 2018 and December 30, 2017	—	—

Series B Preferred Stock, 200,000 shares designated, $10.00 stated value, 0 shares issued and outstanding, as of June 30, 2018 and December 30, 2017	—	—
Series C Preferred Stock, 2,000,000 shares designated, $1.00 stated value, 0 shares issued and outstanding, as of June 30, 2018 and December 30, 2017	—	—
Common stock, $0.00001 par value, 40,000,000 and 20,000,000 shares authorized as of June 30, 2018 and December 30, 2017, respectively; 4,272,094 and 3,909,114 shares issued and outstanding, as of June 30, 2018 and December 30, 2017, respectively	—	—
Additional paid in capital	59,314	57,574
Accumulated other comprehensive income	1,121	783
Accumulated deficit	(68,257)	(65,142)
Total Stockholders' Deficit	(7,822)	(6,785)
Total Liabilities and Stockholders' Deficit	$ 82,970	$ 86,748

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

STAFFING 360 SOLUTIONS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(All amounts in thousands, except share and per share values)

(UNAUDITED)

	Q2 2018	Q2 2017	Q2 2018 YTD	Q2 2017 YTD
Revenue	$59,727	$42,117	$115,518	$82,829
Cost of Revenue, excluding depreciation and amortization stated below	47,845	34,193	92,055	67,579
Gross Profit	11,882	7,924	23,463	15,250
Operating Expenses:				
Selling, general and administrative expenses	11,030	6,439	22,218	13,562
Depreciation and amortization	712	760	1,510	1,520
Total Operating Expenses	11,742	7,199	23,728	15,082
Income (Loss) From Operations	140	725	(265)	168
Other (Expenses) Income:				
Interest expense	(1,951)	(580)	(3,906)	(1,082)
Amortization of debt discount and deferred financing costs	(115)	(839)	(237)	(1,398)
Loss on extinguishment of debt, net	—	—	—	(1,368)
Change in fair value of warrant liability	341	287	879	195
Gain from sale of business	238	—	238	—
Re-measurement loss on intercompany note	(721)	—	(146)	—
Other, net	(9)	(23)	241	(19)
Total Other Expenses, net	(2,217)	(1,155)	(2,931)	(3,672)
Loss Before Provision for Income Tax	(2,077)	(430)	(3,196)	(3,504)
Benefit from (Provision for) income taxes	233	(2)	81	(7)
Net Loss	(1,844)	(432)	(3,115)	(3,511)
Dividends - Series A preferred stock - related party	50	50	100	100
Deemed Dividends - Series D preferred stock	—	1,129	—	2,009
Net Loss Attributable to Common Stock Holders	$(1,894)	$(1,611)	$(3,215)	$(5,620)
Basic and Diluted Net Loss per Share:				

Net Loss	$(0.45)	$(0.16)	$(0.77)	$(1.41)
Net Loss Attributable to Common Stock Holders	$(0.46)	$(0.59)	$(0.79)	$(2.26)
Weighted Average Shares Outstanding – Basic and Diluted	4,142,309	2,715,189	4,063,316	2,487,523

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

STAFFING 360 SOLUTIONS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(All amounts in thousands)

(UNAUDITED)

	Q2 2018	Q2 2017	Q2 2018 YTD	Q2 2017 YTD
Net Loss	$(1,844)	$(432)	$(3,115)	$(3,511)
Other Comprehensive loss				
Foreign exchange translation adjustment	1,254	(281)	338	(303)
Comprehensive Loss Attributable to the Company	$(590)	$(713)	$(2,777)	$(3,814)

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

STAFFING 360 SOLUTIONS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(All amounts in thousands)

(UNAUDITED)

	Q2 2018 YTD	Q2 2017 YTD
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$(3,115)	$(3,511)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	1,510	1,520
Amortization of debt discount and deferred financing costs	237	1,398
Loss on extinguishment of debt, net	—	1,368
Gain in fair value of warrants	(879)	(195)
Stock based compensation	663	618
Re-measurement loss on intercompany note	146	—
Gain from sale of business	(238)	—
Other	—	(87)
Changes in operating assets and liabilities:		
Accounts receivable	12,919	2,281
Prepaid expenses and other current assets	(57)	(269)
Other assets	(58)	295
Accounts payable and accrued expenses	1,960	(1,201)
Interest payable - related party	(160)	—
Other current liabilities	(88)	138
Other long-term liabilities	(11)	53
Other	167	(304)
NET CASH PROVIDED BY OPERATING ACTIVITIES	12,996	2,104
CASH FLOWS FROM INVESTING ACTIVITIES:		
Acquisition of business, net of cash acquired	(1,910)	—
Disposal of business, net of cash	1,968	—
Purchase of property and equipment	(140)	(126)
Collection of UK factoring facility deferred purchase price	3,550	—
NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES	3,468	(126)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Repayments of term loan	(254)	—
Repayment of promissory notes	—	(5,486)
Proceeds from term loan - related party	—	9,050
Proceeds from term loan	2,047	—
Proceeds from convertible notes	—	400
Repayment of bonds	—	(50)

Repayments on accounts receivable financing, net	(18,813)	(2,709)
Dividends paid to related parties	(100)	—
Proceeds from At-The-Market Facility	629	208
Repayment of Series D Preferred Stock	—	(1,500)
Payments made for earn-outs	(165)	(1,075)
Third party financing costs	(20)	(938)
NET CASH USED IN FINANCING ACTIVITIES	(16,676)	(2,100)
NET DECREASE IN CASH	(212)	(122)
Effect of exchange rates on cash	(2)	(2)
Cash - Beginning of period	3,100	650
Cash - End of period	$2,886	$526

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

STAFFING 360 SOLUTIONS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(All amounts in thousands, except share, per share and stated value per share)

(UNAUDITED)

NOTE 1 – ORGANIZATION AND DESCRIPTION OF BUSINESS

Staffing 360 Solutions, Inc. (“we,” “us,” “our,” “Staffing 360,” or the “Company”) was incorporated in the State of Nevada on December 22, 2009, as Golden Fork Corporation, which changed its name to Staffing 360 Solutions, Inc., ticker symbol “STAF”, on March 16, 2012. On June 15, 2017, the Company changed its state of domicile to Delaware.

The Company effected a one-for-ten reverse stock split on September 17, 2015 and a one-for-five reverse stock split on January 3, 2018. All share and per share information in these consolidated financial statements has been retroactively adjusted to reflect these reverse stock splits.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation and Principles of Consolidation

These condensed consolidated financial statements and related notes are presented in accordance with generally accepted accounting principles in the United States (“GAAP”), expressed in U.S. dollars.

The unaudited condensed consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

These unaudited condensed consolidated financial statements reflect all adjustments including normal recurring adjustments, which, in the opinion of management, are necessary to present fairly the financial position, results of operations and cash flows for the periods presented in accordance with the GAAP.

These unaudited condensed consolidated financial statements should be read in conjunction with the Company’s consolidated financial statements and notes thereto for the fiscal year ended December 30, 2017, the transition period ended December 31, 2016 and fiscal year ended May 31, 2016, which are included in the Company’s December 30, 2017 Form 10-K, filed with the United States Securities and Exchange Commission on March 29, 2018. The Company assumes that the users of the interim financial information herein have read, or have access to, the audited consolidated financial statements for the preceding period, and that the adequacy of additional disclosure needed for a fair presentation may be determined in that context. The results of operations for the period ended June 30, 2018 are not necessarily indicative of results for the entire year ending December 29, 2018. This report is for the periods April 1, 2018 to June 30, 2018 (“Q2 2018”), April 2, 2017 to July 1, 2017 (“Q2 2017”), December 31, 2017 to June 30, 2018 (“Q2 2018 YTD”) and January 1, 2017 to July 1, 2017 (“Q2 2017 YTD”).

Clement May Acquisition

On June 28, 2018, the Company and Longbridge Recruitment 360 Limited (“Longbridge”), a wholly-owned subsidiary of the Company, entered into share purchase agreements (“Share Purchase Agreements”) to acquire all of the share capital of Clement May Limited (“CML”). Consideration for the acquisition of all the shares was (i) an aggregate cash payment of £1,550 ($2,047), (ii) 15,000 shares of the Company’s common stock, (iii) the assignment of certain outstanding debt owed to the CML Majority Holder to the Principal as set forth in that Share Purchase Agreement, (iv) an earn-out payment of up to £500, the amount to be calculated pursuant to that Share Purchase Agreement and to be paid on or around December 28, 2018, and (v) deferred consideration of £350, to be paid on or around June 28, 2019, depending on the satisfaction of certain conditions set forth in that Share Purchase Agreement. To finance the above transaction, the Company entered into a term loan with HSBC Bank plc. Refer to Note 5 for further details.

PeopleServe Disposition

On June 6, 2018, the Company divested the stock of PeopleServe Inc., and PeopleServe PRS, Inc. for a total consideration of $1,502, net of $567 that was remitted back to the buyer on July 31, 2018 in connection with a net working capital true up. The Company recorded a gain of $238 from sale of the business.

Revenue Recognition

On January 1, 2018, the Company adopted the new accounting standard ASC 606, Revenue from Contracts with Customers for all open contracts and related amendments as of January 1, 2018 using the modified retrospective method. The adoption had no impact to the reported results. Results for reporting periods beginning after January 1, 2018 will be presented under ASC 606, while the comparative information will not be restated and will continue to be reported under the accounting standards in effect for those periods.

The Company accounts for revenues when both parties to the contract have approved the contract, the rights and obligations of the parties are identified, payment terms are identified, and collectability of consideration is probable. Payment terms vary by client and the services offered.

The Company has primarily two main forms of revenue – temporary contractor revenue and permanent placement revenue. Temporary contractor revenue is accounted for as a single performance obligation satisfied over time because the customer simultaneously receives and consumes the benefits of the Company's performance on an hourly basis. The contracts stipulate weekly billing and the Company has elected the "as invoiced" practical expedient to recognize revenue based on the hours incurred at the contractual rate as we have the right to payment in an amount that corresponds directly with the value of performance completed to date. Permanent placement revenue is recognized on the date the candidate's full-time employment with the customer has commenced. The customer is invoiced on the start date, and the contract stipulates payment due under varying terms, typically 30 days. The contract with the customer stipulates a guarantee period whereby the customer may be refunded if the employee is terminated within a short period time, however this has historically been infrequent, and immaterial upon occurrence. As such, the Company's performance obligations are satisfied upon commencement of the employment, at which point control has transferred to the customer. Revenue in Q2 2018 was comprised of $56,838 of temporary contractor revenue and $2,889 of permanent placement revenue, compared with $41,323 and $794 for Q2 2017, respectively. Revenue in Q2 2018 YTD was comprised of $109,835 of temporary contractor revenue and $5,683 of permanent placement revenue, compared with $81,250 and $1,579 for Q2 2017 YTD, respectively. Refer to Note 8 for further details on breakdown by segments.

Reclassifications

We may make certain reclassifications to prior period amounts to conform with the current year's presentation. These reclassifications did not have a material effect on our condensed consolidated statement of financial position, results of operations or cash flows.

Income Taxes

The Company's provision for income taxes is based upon an estimated annual tax rate for the year applied to federal, state and foreign income. On a quarterly basis, the annual effective tax rate is adjusted, as appropriate, based upon changed facts and circumstances, if any, as compared to those forecasted at the beginning of the fiscal year and each interim period thereafter. The Company's effective tax rate may change from period to period based on recurring and non-recurring factors including the geographical mix of earnings, enacted tax legislation, state and local income taxes, and tax audit settlements. The effective income tax rate was 2.52%, 12.8%, 11.1% and 8% for the period ending Q2 2018, Q2 2017, Q2 2018 YTD and Q2 2017 YTD, respectively.

On December 22, 2017, the Tax Cuts and Jobs Act of 2017 (the "Tax Act") was signed into law making significant changes to the Internal Revenue Code. The changes include, but are not limited to, a U.S. corporate tax rate decrease from 35% to 21%, the transition of U.S. international taxation from a worldwide tax system to a territorial system, allowing for immediate expensing of certain qualified property, modifications to many business deductions and credits, and providing various tax incentives. Shortly after the Tax Act was enacted, Staff Accounting Bulletin No. 118 ("SAB 118") was issued to address the application of U.S. GAAP in situations when a registrant does not have the necessary information available, prepared, or analyzed (including computations) in reasonable detail to complete the accounting for certain income tax effects of the Tax Act. SAB 118 provides that in these cases a registrant should continue to apply Financial Accounting Standards Board ("FASB") Accounting Standards Update No. 2009-06, Income Taxes ("Topic 740") based on the provisions of the tax laws that were in effect immediately prior to the Tax Act. SAB 118 provides a measurement period that should not extend beyond one year from the Tax Act enactment date for registrants to complete the accounting under Topic 740.

The Company remeasured domestic deferred tax assets and liabilities based on the rates at which they are expected to reverse in the future, which is generally the 21% rate imposed by the Tax Act. The Company recorded an expense of $3.7 million to reduce the net deferred tax assets, along with a corresponding benefit for the reduction of the valuation allowance recorded against these balances in our financial statements for the year ended December 30, 2017.

At June 30, 2018, in accordance with SAB 118, the Company has not completed its accounting for the tax effects of the one-time transition tax imposed by the Tax Act. In order to determine the amount of the liability with respect to the one-time transition tax, the Company must determine, in addition to other factors, the amount of post-1986 Earnings & Profits of the relevant subsidiaries, as well as the amount of non-U.S. income taxes paid on such earnings. In order to quantify the liability, we are awaiting further interpretative guidance, continuing to assess available tax methods and elections, and continuing to gather additional information to more precisely compute the amount of the transition tax. Therefore, we have not recorded an estimate of the transition tax in our financial statements.

STAFFING 360 SOLUTIONS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(All amounts in thousands, except share, per share and stated value per share)

(UNAUDITED)

In addition, the Company is continuing to evaluate whether Global Intangible Low Tax Income taxes (“GILTI”) are recorded as a current period expense when incurred or whether such amounts should be factored into the Company's measurement of its deferred taxes. As a result, the Company has not included an estimate of the tax impacts related to GILTI in the second quarter of 2018. The Company has not elected a method and will only do so after completing their analysis of the GILTI provisions.

Foreign Currency

Staffing 360 Solutions, Inc. has an intercompany note due from Longbridge Recruitment 360 (U.K.) Limited (“Longbridge”), denominated in U.S. dollars. Longbridge’s functional currency is Pound Sterling. The note matures in September 15, 2022, bears interest at a rate of interest equal to the mid-term monthly Applicable Federal Rate (AFR), as published each month by the U.S. Internal Revenue Service pursuant to Section 1274(d) of the Internal Revenue Code, compounded semiannually. Interest is payable in cash quarterly on the first business day of each calendar quarter. Longbridge may prepay all or any portion of the principal amount of this Note at any time, in whole or in part, without premium or penalty. As the note is denominated in U.S. dollars and due to weakening of the Pound Sterling, the Company recorded a non cash foreign currency remeasurement loss of $721 and $146 in Q2 2018 and Q2 2018 YTD, respectively.

Recent Accounting Pronouncements

In February 2016, the FASB issued ASU 2016-02, “Leases” (Topic 842). This guidance will be effective for public entities for fiscal years beginning after December 15, 2018 including the interim periods within those fiscal years. Early application is permitted. Under the new provisions, all lessees will report a right-of-use asset and a liability for the obligation to make payments for all leases with the exception of those leases with a term of 12 months or less. All other leases will fall into one of two categories: (i) Financing leases, similar to capital leases, which will require the recognition of an asset and liability, measured at the present value of the lease payments and (ii) Operating leases which will require the recognition of an asset and liability measured at the present value of the lease payments. Lessor accounting remains substantially unchanged with the exception that no leases entered into after the effective date will be classified as leveraged leases. For sale leaseback transactions, the sale will only be recognized if the criteria in the new revenue recognition standard are met. The Company is currently evaluating the impact of adopting this guidance.

NOTE 3 – LOSS PER COMMON SHARE

The Company utilizes the guidance per ASC 260, “Earnings per Share”. Basic earnings per share are calculated by dividing income available to stockholders by the weighted average number of common stock shares outstanding during each period. Our Series A preferred stock holders (related parties) receive certain dividends or dividend equivalents that are considered participating securities and our loss per share is computed using the two-class method. For Q2 2018 YTD and Q2 2017 YTD, pursuant to the two-class method, as a result of the net loss, losses were not allocated to the participating securities.

Diluted earnings per share are computed using the weighted average number of common stock shares and dilutive common share equivalents outstanding during the period. Dilutive common stock equivalents consist of common shares issuable upon the conversion of preferred stock, convertible notes and the exercise of stock options and warrants (calculated using the modified treasury stock method). Such securities, shown below, presented on a common share equivalent basis and outstanding as of June 30, 2018 and July 1, 2017 have been excluded from the per share computations, since their inclusion would be anti-dilutive:

	June 30, 2018	July 1, 2017
Convertible promissory notes	—	253,885
Convertible preferred shares	43,239	43,239
Warrants	925,935	912,234
Restricted shares - unvested	565,932	271,852
Long term incentive plan (LTIP)	178,728	178,728
Options	125,400	125,460
Total	1,839,234	1,785,398

STAFFING 360 SOLUTIONS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(All amounts in thousands, except share, per share and stated value per share)

(UNAUDITED)

NOTE 4 – ACCOUNTS RECEIVABLE BASED FINANCING FACILITIES

HSBC Invoice Finance (UK) Ltd – New Facility

On February 8, 2018, CBS Butler, Longbridge and The JM Group, entered into a new arrangement with HSBC Invoice Finance (UK) Ltd ("HSBC") which provides for HSBC to purchase the subsidiaries' accounts receivable up to an aggregate amount of £11,500 across all three subsidiaries. The terms of the arrangement provide for HSBC to fund 90% of the purchased accounts receivable upfront and, a secured borrowing line of 70% of unbilled receivables capped at £1,000 (within the overall aggregate total facility of £11,500). The arrangement has an initial term of 12 months, with an automatic rolling three-month extension and carries a service charge of 1.80%.

On June 28, 2018, the Company's new subsidiary Clement May Limited ("CML") entered into a new agreement with a minimum term of twelve months for purchase of debt ("APD") with HSBC, joining CBS Butler, Longbridge and The JM Group (collectively, with CML, the "Borrowers") as "Connected Clients" as defined in the APD. The new Connected Client APDs carry an aggregate Facility Limit of £20,000 across all Borrowers. The obligations of the Borrowers are secured by a fixed charge and a floating charge on the Borrowers' respective accounts receivable and are subject to cross-company guarantees among the Borrowers. In addition, the secured borrowing line against unbilled receivables was increased to £1,500 for a period of 90 days.

Under ASU 2016-16, "Statement of Cash Flows (Topic 230, Classification of Certain Cash Receipts and Cash Payments, a consensus of the FASB Emerging Issues Task Force), the upfront portion of the sale of accounts receivable is classified within operating activities, while the deferred purchase price portion (or beneficial interest), once collected, is classified within investing activities.

ABN AMRO Commercial Finance

In conjunction with the HSBC Invoice Finance (UK) Ltd – New Facility, on February 8, 2018, Longbridge and The JM Group terminated this facility and the remaining balance was paid in full.

CBS Butler

In conjunction with the HSBC Invoice Finance (UK) Ltd – New Facility, on February 8, 2018, CBS Butler terminated this facility and the remaining balance was paid in full.

NOTE 5 – DEBT

	June 30, 2018	December 30, 2017
Jackson Investment Group - related party	$40,000	$ 40,000
HSBC Term Loan	2,047	—
ABN AMRO	—	254
Total Debt, Gross	42,047	40,254
Less: Debt Discount and Deferred Financing Costs	(1,022)	(1,260)
Total Debt, Net	41,025	38,994
Less: Current Portion, Net	(683)	(245)
Total Long-Term Debt, Net	$40,342	$ 38,749

HSBC Term Loan

On June 26, 2018, the Company's UK subsidiary, Staffing 360 Solutions Limited (the "S360 Ltd"), entered into a term loan agreement (the "Term Loan") with HSBC Bank plc ("HSBC plc"). The Term Loan was drawn down on June 28, 2018 in an original principal amount of £1,550 ($2,047) to fund the upfront cash consideration of the Clement May acquisition. The Term Loan matures on June 28, 2021, unless otherwise accelerated or terminated earlier. The interest rate on the Term Loan is 2.35% over the base rate of 0.5%, which is subject to periodic adjustment, and is payable in monthly installments of principal and interest. The obligations of S360 Ltd under the term Loan are secured by fixed and floating charges in favor of HSBC plc on all of S360 Ltd and its UK subsidiaries' assets, undertakings, accounts receivable and certain other assets pursuant to the terms of the Term Loan agreement.

Non-interest bearing convertible note - April 11, 2017

On April 11, 2017, the Company entered into a non-interest bearing convertible note for $477, whereby the Company received cash of $400, maturing in October 2017. The Company paid this in full on September 18, 2017.

STAFFING 360 SOLUTIONS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(All amounts in thousands, except share, per share and stated value per share)

(UNAUDITED)

Jackson Investment Group Term Loan Note #2 – Related Party

On April 5, 2017, the Company amended the note and warrant purchase agreement and entered into a second subordinated secured note for $1,650. Under the terms of this amended agreement, the Company issued to Jackson 59,397 shares of common stock, with an additional 74,184 shares of common stock that was issued after obtaining shareholder approval for issuance of shares to Jackson in excess of the 19.99% limit in June 2017. Also on April 5, 2017, the Company amended the Warrant to allow Jackson to purchase up to an additional 275,508 shares of common stock, modified the initial exercise price of the Warrant to $5.00 per share and modified the conversion price of accrued interest on the note issued to Jackson in January 2017 to $7.50. The Warrant was also amended to increase the amount of common stock issuable to Jackson pursuant to the anti-dilution clause contained therein. The second note accrues interest on the principal amount at a rate of 6% per annum and has a maturity date of June 8, 2019; however, in the event the Company satisfied all of its outstanding obligations with Midcap Financial Trust, the maturity date would have been adjusted to July 25, 2018. No interest or principal is payable on the second note until maturity. At any time during the term of the second note, upon notice to Jackson, the Company may also, at its option, redeem all or some of the then outstanding principal amount of the note by paying to Jackson an amount not less than $100 of the outstanding principal (and in multiples of $100), plus any accrued but unpaid interest and liquidated damages and other amounts due under the note. The second note’s principal is not convertible into shares of common stock; however, 50% of the accrued interest on the second note can be converted into shares of common stock, at the sole election of Jackson at maturity or in the event of a prepayment by the Company, at a conversion price equal to $7.50 per share. The proceeds of this transaction were used to redeem the remaining shares and conversion rights of the Series D Preferred Stock. The Company has accounted for these warrants as a liability under ASC 815-40 due to certain anti-dilution protection provisions. The Company has recorded a liability of $1,426 at December 30, 2017. One April 25, 2018, the Company and Jackson amended the Warrant to remove the anti-dilution clauses. Refer to Note 6 for further details.

8% Convertible Note (July 8, 2015) and 8% Convertible Note (February 8, 2016)

On January 3, 2017, the Company entered into an amendment agreement pursuant to which, the parties refinanced an aggregate amount of $2,688 of indebtedness and extended all amortization payments for the two 8% convertible notes dated July 8, 2015 and February 8, 2016 (collectively, the “Amendment”) to October 1, 2018, which was approximately 21 months from the date of the refinancing.

The Amendment had a new face value of $3,126, and an 8% interest rate per annum, with no interest payments due until October 1, 2017, payable quarterly thereafter, and an overall term of 21 months with principal due at maturity. The Amendment was convertible into shares of common stock at a price of $3.00 per share ($15 per shares after stock split in Q1 2018) at holder's election, and the holder agreed to eliminate the 20% pre-payment penalty for an early redemption. In connection with the refinancing, the Company issued the holder 120,000 shares of common stock, valued at $498. The Amendment resulted in the extinguishment of the old notes of $2,688 and recording of the new debt and debt issue costs. The Company recorded a $870 loss upon extinguishment. On January 26, 2017, the Amendment was paid in full resulting a loss of $498.

Series B Bonds

The balance of $50 was paid in full in April 2017.

NOTE 6 – EQUITY

Common Stock

The Company issued the following shares of common stock during the six month period ended June 30, 2018:

Shares issued to/for:	Number of common shares issued	Fair Value of shares issued	Fair Value at Issuance (minimum and maximum per share)	
At-the-Market Facility	237,232	$ 629	$ 1.61	$ 3.59
Employees	85,000	137	1.61	1.61
Consultants	15,522	48	1.50	3.42
Acquisition	15,000	21	1.38	1.38
Board and Committee members	9,800	24	1.74	3.25
Reverse stock split (rounding up shares)	426	-	-	-
	362,980	$ 859		

Subsequent to June 30, 2018, the Company sold 400,000 shares of common stock through its at-the-market facility at a value of $1,449, and granted 5,600 shares of common stock valued $8 to the board of directors.

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Restricted Shares

The Company has issued shares to employees and board and committee members under its 2015 Omnibus Incentive Plan and 2016 Omnibus Incentive Plan. Under these plans, the shares are restricted for a period of three years from issuance. As of June 30, 2018, the Company has a total of 565,932 shares unvested issued to employees and Board and committee members. In accordance with ASC 718, Compensation – Stock Compensation, the Company recognizes stock based compensation from restricted stock based upon the fair value of the award at issuance over the vesting term on a straight-line basis. The fair value of the award is calculated by multiplying the number of restricted shares by the Company's stock price on the date of issuance. The impact of forfeitures has historically been immaterial to the financial statements. The Company recorded compensation expense associated with these restricted shares of $235, $196, $480 and $369, for the periods ended Q2 2018, Q2 2017, Q2 2018 YTD and Q2 2017 YTD, respectively.

Stock Options

The Company recorded share based payment expense of $53, $105, $135 and $198 for the periods ended Q2 2018, Q2 2017, Q2 2018 YTD and Q2 2017 YTD, respectively.

Convertible Preferred Shares

Series A Preferred Stock – Related Party

In the period ended Q2 2018 YTD and Q2 2017 YTD, the Company paid $100 and $0, respectively, in dividends to its Series A preferred stock holders. At July 1, 2017, the Company has accrued $100 with respect to Series A dividends payable to preferred stock holders.

Series D Preferred Stock

The Series D Preferred Stock contained beneficial conversion features; a portion was quantifiable at the date of issuance in the amount of $615, which was recognized immediately due to the immediate convertibility of the Series D Preferred Stock and that it had no true redemption date. The additional contingent beneficial conversion feature was quantifiable only at the date of each subsequent conversion. Both beneficial conversion features represent additional value to the holders. As such, they represent a dividend on the Series D Preferred Stock and recorded as a Deemed Dividend. These Deemed Dividends are presented on the Statement of Operations for purposes of calculation Earnings Per Share only and have no net impact on Shareholders' Deficit. Deemed Dividends recorded were $0 and $2,009 for Q2 2018 YTD and Q2 2017 YTD, respectively.

On April 5, 2017, the Company entered into an agreement with holders of the Series D Preferred shares to redeem the remaining 62 shares of Series D Preferred Stock and terminate all future conversion rights, in return for $1,500 in cash and 60,000 shares of common stock.

Warrants

The Company had accounted for the warrants issued to Jackson as a liability under ASC 815-40 due to certain anti-dilution protection provisions. The warrants issued to Jackson are considered to be Level 3 liabilities under ASC 820. On April 25, 2018, the Company and Jackson amended the Warrant to remove the anti-dilution clauses. No economic terms were adjusted. These clauses were the basis for recording the warrants as a liability. Therefore, upon execution of this amendment, the Company recorded a mark-to-market gain and reclass the remaining liability to Additional paid-in capital. The Company recorded a change in fair value of the warrant liability of $341, $287, $879 and $195 in Q2 2018, Q2 2017, Q2 2018 YTD and Q2 2017 YTD, respectively, using Black-Scholes valuation model.

NOTE 7 – COMMITMENTS AND CONTINGENCIES

Earn-out Liabilities and Stock Value Guarantees

Pursuant to the acquisition of Control Solutions International, Inc. (“CSI”) on November 4, 2013, the purchase price included monthly cash payments to the former owner and shareholder of CSI for performance-based compensation equal to 20% of CSI’s consolidated gross profit from the date of closing through the end of the sixteenth quarter following the date of closing not to exceed a total of $2,100. During Q2 2018 and Q2 2017, the Company paid $0 and $24, respectively, towards the earn-out liability. During Q2 2018 YTD and Q2 2017 YTD, the Company paid $15 and $48, respectively, towards the earn-out liability No further payments are due.

Pursuant to the acquisition of The JM Group on November 5, 2015, the purchase price includes a cash payment to the shareholders for performance-based compensation of (a) £850 if the gross profit for the 12 month period ending on the anniversary date of the date of

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completion (the "Anniversary TTM Gross Profit") is equal to 90% or more of the gross profit for the twelve months ending October 31, 2015 (the "Completion TTM Gross Profit"); or (b) if the Anniversary TTM Gross Profit is less than 90% of the Completion TTM Gross Profit, a sum equal to £850 multiplied by the Anniversary TTM Gross Profit/Completion TTM Gross Profit. The Company recorded the maximum contingent liability amount of £850 ($1,180). At December 31, 2016, the remaining balance was $1,026 and was recorded in other current liabilities. While unpaid, the balance accrued interest at 10.25% per annum. The balance was paid in full in January 2017.

Pursuant to the acquisition of Clement May on June 28, 2018, the purchase price includes an earnout payment of up to £500 to be paid on or around December 28, 2018; and deferred consideration of £350, the amount to be calculated and paid pursuant to the Share Purchase Agreement, to be paid on or around June 28, 2019.

Legal Proceedings

NewCSI, Inc. vs. Staffing 360 Solutions, Inc.

On May 22, 2014, NewCSI, Inc. ("NewCSI"), the former owners of Control Solutions International, filed a complaint in the United States District Court for the Western District of Texas, Austin Division, against the Company arising from the terms of the Stock Purchase Agreement dated August 14, 2013 between the Company and NewCSI. NewCSI claims that the Company breached a provision of the Stock Purchase Agreement ("SPA § 2.7") that required the Company to calculate and pay to NewCSI 50% of certain "Deferred Tax Assets" within 90 days after December 31, 2013, subject to certain criteria. The Complaint sought payment of the amount allegedly owed under SPA § 2.7 and acceleration of earn-out payments provided for in the Stock Purchase Agreement of $1,400, less amounts paid to date, and attorneys' fees.

On December 31, 2014, NewCSI filed an amended complaint to which NewCSI added an additional count asserting an "Adjustment Event" had occurred requiring an acceleration of earn-out payments provided for in the CSI Stock Purchase Agreement of $2,100, less amounts paid as of December 31, 2014 totaling $429 (balance of $1,671 at December 31, 2014), should the Company or CSI "be unable, or admit in writing its inability, to pay its debts as they mature." The Company responded denying the material allegations and interposing numerous affirmative defenses, including that the earn-out liability was fully expensed at the time of the acquisition and fully accrued for on the Company's balance sheet as part of the purchase accounting at the time of the acquisition. A the trial was held May 18-20, 2015. On May 20, 2015, the jury rendered a verdict, finding that the Company had not complied with SPA § 2.7 and owed $154, but that NewCSI had not proven that the Company or CSI had become unable to pay debts as they came due.

On June 3, 2015, NewCSI filed a Motion for Entry of Judgment as Matter of Law seeking entry of a judgment in the amount of $154, plus accelerated earn-out payments in the amount of $1,152, plus statutory interest. NewCSI did not challenge the jury verdict on the ability to pay issue. Also on June 3, 2015, the Company filed a Motion for Entry of Judgment as a Matter of Law seeking entry of judgment against NewCSI on the jury's finding that the Company had not complied with SPA § 2.7, or, in the alternative, for a reduction of damages to $154 and to hold that NewCSI may not be awarded accelerated earn-out payments as that would result in an illegal penalty.

On October 21, 2015, judgment was entered in this action in favor of NewCSI and against the Company in the amount of $1,307, plus pre-judgment interest, post-judgment interest, and costs.

On January 26, 2016, the District Court set the bond in respect of the NewCSI litigation at $1,384. The Company has filed a notice of appeal to the United States Court of Appeals for the Fifth Circuit ("Appellate Court") seeking reversal of the judgment and posted a supersedeas bond to stay the execution of the judgment pending appeal. On April 18, 2016, the Court granted the NewCSI shareholders' request for payment of attorneys' fees, but reserved judgment on the amount of fees to award pending the outcome of the Company's appeal. On November 3, 2016, oral arguments for the appeal were heard and on July 26, 2017, the Appellate Court affirmed the trial Court's decision but left the legal fee award open for determination by further proceedings in the trial court. On August 29, 2017 the surety company released the supersedeas bond to the New CSI shareholders' counsel, which was amount was approximately $5 less than the judgment amount with accumulated interest. Payment of this remaining balance has been made by the Company.

On September 29, 2017 NewCSI filed a Supplemental Motion in the United States District Court for the Western District of Texas, Austin Division, seeking $629 in attorneys' fees. The Company opposed this motion but the magistrate judge issued a report and recommendation on November 17, 2017 recommending an award of fees in the amount of $606. The Company filed an objection with the trial judge to the magistrate's report and recommendation. On May 30, 2018 the trial judge issued an order adopting the report and recommendation of the magistrate judge and awarding NewCSI the amount of $606 in legal fees, plus interest at the statutory rate of 2.27% per annum. The Company paid $606 in full settlement of this matter in June 2018.

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Staffing 360 Solutions, Inc. v. Former Officers of Staffing 360 Solutions, Inc.

On November 13, 2015, in a separate proceeding, Staffing 360 initiated an arbitration before JAMS entitled Staffing 360 Solutions, Inc. v. Former Officers of Staffing 360 Solutions, Inc., against three officers of Staffing 360, each a former Staffing 360 officer and employee. In its demand for arbitration and statement of claim, Staffing 360 alleged that these individuals breached their employment agreements with Staffing 360 and the fiduciary duties each owed to the Company. The three respondents responded with a counterclaim alleging wrongful termination and have moved to dismiss the arbitration, as well as moved for severance in relation to the remainder of their contracts. On July 20, 2016, the arbitrator decided in favor of both of the respondents' motions. Further on September 21, 2016 the arbitrator rendered the final award, which was set at $1,433. The former officers brought an action in US District Court in New York City under the caption Dealy et al., v. Staffing 360 Solutions, Inc., requesting that the Court convert this arbitration award into a judgment. On July 11, 2017, the Court entered an order confirming the arbitrator's award and granting judgement against the Company. In August 2017, the Company paid $1,582 in full satisfaction of this matter.

NOTE 8 – SEGMENTS

The Company generated revenue and gross profit by segment as follows:

	Q2 2018	Q2 2017	Q2 2018 YTD	Q2 2017 YTD
Commercial Staffing - US	$23,549	$23,308	$44,945	$45,719
Professional Staffing - US	14,066	12,232	28,733	23,928
Professional Staffing - UK	22,112	6,577	41,840	13,182
Total Revenue	$59,727	$42,117	$115,518	$82,829
Commercial Staffing - US	$3,917	$4,288	$7,815	$8,305
Professional Staffing - US	4,214	2,245	8,199	4,117
Professional Staffing - UK	3,751	1,391	7,449	2,828
Total Gross Profit	$11,882	$7,924	$23,463	$15,250
Selling, general and administrative expenses	$(11,030)	$(6,439)	$(22,218)	$(13,562)
Depreciation and amortization	(712)	(760)	(1,510)	(1,520)
Interest expense	(1,951)	(580)	(3,906)	(1,082)
Amortization of debt discount and deferred financing costs	(115)	(839)	(237)	(1,398)
Loss on extinguishment of debt, net	—	—	—	(1,368)
Change in fair value of warrant liability	341	287	879	195
Gain from sale of business	238	—	238	—

Re-measurement loss on intercompany note	(721)	—	(146)	—
Other (expense) income, net	(9)	(23)	241	(19)
Loss Before Provision for Income Tax	$(2,077)	$(430)	$(3,196)	$(3,504)

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The following table disaggregates revenues by segments:

Q2 2018	Commercial Staffing - US	Professional Staffing - US	Professional Staffing - UK	Total
Permanent Revenue	$43	$ 1,666	$ 1,180	$2,889
Temporary Revenue	23,506	12,400	20,932	56,838
Total	$23,549	$ 14,066	$ 22,112	$59,727

Q2 2017	Commercial Staffing - US	Professional Staffing - US	Professional Staffing - UK	Total
Permanent Revenue	$12	$ 153	$ 629	$794
Temporary Revenue	23,296	12,079	5,948	41,323
Total	$23,308	$ 12,232	$ 6,577	$42,117

Q2 2018 YTD	Commercial Staffing - US	Professional Staffing - US	Professional Staffing - UK	Total
Permanent Revenue	$115	$ 3,173	$ 2,395	$5,683
Temporary Revenue	44,830	25,560	39,445	109,835
Total	$44,945	$ 28,733	$ 41,840	$115,518

Q2 2017 YTD	Commercial Staffing - US	Professional Staffing - US	Professional Staffing - UK	Total
Permanent Revenue	$44	$ 279	$ 1,256	$1,579
Temporary Revenue	45,675	23,649	11,926	81,250
Total	$45,719	$ 23,928	$ 13,182	$82,829

As of June 30, 2018 and December 30, 2017, the Company has assets in the U.S., the U.K. and Canada as follows:

	June 30, 2018	December 30, 2017
United States	$42,971	$ 53,814
United Kingdom	39,948	32,861
Canada	51	73
Total Assets	$82,970	$ 86,748

NOTE 9 – ACQUISITIONS

In accordance with ASC 805, the Company accounts for acquisitions using the purchase method under which the acquisition purchase price is allocated to the assets acquired and liabilities assumed based upon their respective fair values. The Company utilizes management estimates and, in some instances, may retain the services of an independent third-party valuation firm to assist in determining the fair values of assets acquired, liabilities assumed and contingent consideration granted. Such estimates and valuations require the Company to make significant assumptions, including projections of future events and operating performance.

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In connection with the acquisition of Clement May, the Company recorded the following identifiable intangible assets, based on preliminary valuation.

	Clement May
Goodwill	$ 1,545
Intangible assets	
Tradenames	$ 470
Non-compete	273
Customer Relationships	451
	$ 1,194

Goodwill of Clement May is included in the Company's Professional-UK reportable segment.

These identified intangible assets are being amortized on a straight-line basis over their weighted average estimated useful life of 8.4 years. The Company acquired a total of $14,305 in receivables and fair value of these receivables equals the contract value; and recorded contingent consideration associated with Clement May of £850 ($1,122).

The following table summarizes the final allocation of the purchase price to the estimated fair values of net assets acquired at the date of the acquisition:

	Clement May
Purchase price	$ 3,543
Less:	
Net assets acquired	$ (804)
Intangible assets	(1,194)

Goodwill	$1,545

The Company recorded a total of $105 in third party expenses associated with consummating this acquisition, which are included in Selling, general and administrative expenses, excluding depreciation and amortization stated on the Consolidated Statement of Operations.

The following unaudited pro forma consolidated results of operation have been prepared, as if the acquisition of FirstPro and CBS Butler had occurred as of June 1, 2016, and acquisition of Clement May acquired on January 1, 2017.

	Q2 2018	Q2 2017	Q2 2018 YTD	Q2 2017 YTD
Revenues	$71,089	$70,280	$139,545	$140,668
Net loss from continuing operations	(1,779)	(780)	(2,911)	(4,296)

NOTE 10 – OTHER RELATED PARTY TRANSACTIONS

In addition to the Series A Preferred Shares and Notes issued to Jackson, the following are other related party transactions:

Board and Committee Members

The Company had the following activity with its Board and Committee Members:

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	Q2 2018				Q2 2017			
	Cash Compensation	Shares Issued	Value of Shares Issued	Compensation Expense Recognized	Cash Compensation	Shares Issued	Value of Shares Issued	Compensation Expense Recognized
Dimitri Villard	$ 19	1,400	$ 2	$ 20	$ 19	5,200	$ 24	$ 17
Jeff Grout	19	1,400	2	20	19	5,200	24	17
Nick Florio	19	1,400						