

Since 1983

mancon

Management Consulting, Inc. and Subsidiaries

Consolidating Financial Statements

Year Ended December 31, 2019

DHG
DIXON HUGHES GOODMAN LLP

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Independent Accountants' Review Report

Board of Directors
Management Consulting, Inc. and Subsidiaries
Virginia Beach, Virginia

We have reviewed the accompanying consolidating financial statements of Management Consulting, Inc. and subsidiaries which comprise the consolidating balance sheets as of December 31, 2019, and the related consolidating statements of operations, changes in equity, and cash flows for the year then ended, and the related notes to the consolidating financial statements. A review includes primarily applying analytical procedures to management's financial data and making inquiries of company management. A review is substantially less in scope than an audit, the objective of which is the expression of an opinion regarding the consolidating financial statements as a whole. Accordingly, we do not express such an opinion.

Management's Responsibility for the Consolidating Financial Statements

Management is responsible for the preparation and fair presentation of the consolidating financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of the consolidating financial statements that are free from material misstatement whether due to fraud or error.

Accountants' Responsibility

Our responsibility is to conduct the review engagement in accordance with *Statements on Standards for Accounting and Review Services* promulgated by the Accounting and Review Services Committee of the American Institute of Certified Public Accountants. Those standards require us to perform procedures to obtain limited assurance that there are no material modifications that should be made to the consolidating financial statements for them to be in accordance with accounting principles generally accepted in the United States of America. We believe that the results of our procedures provide a reasonable basis for our conclusion.

Accountants' Conclusion

Based on our review, we are not aware of any material modifications that should be made to the accompanying consolidating financial statements in order for them to be in conformity with accounting principles generally accepted in the United States of America.

Change in Accounting Principle

As discussed in Note 2 to the consolidating financial statements, the Company has changed its method of accounting for investments in equity securities (excluding equity method investments) in 2019 due to the adoption of Accounting Standards Update (ASU) 2016-01, *Financial Instruments - Recognition and Measurement of Financial Assets and Financial Liabilities*, using the modified retrospective approach. Our conclusion is not modified with respect to this matter.

Dixon Hughes Goodman LLP

Norfolk, Virginia
June 19, 2020

Management Consulting, Inc. and Subsidiaries
Consolidating Balance Sheets
December 31, 2019

	Management Consulting, Inc. & Subsidiary	MANCON LLC	Eliminations	Consolidated
ASSETS				
Current assets:				
Cash and cash equivalents	\$ 6,301,831	\$ 6,764	\$ -	\$ 6,308,595
Investments	38,663,272	-	(37,832,935)	830,337
Accounts receivable	-	21,582,450	-	21,582,450
Inventories	-	32,395,799	-	32,395,799
Prepaid expenses	-	547,530	-	547,530
Income tax refunds receivable	992,705	251,421	-	1,244,126
Due from health and welfare trust	-	66,820	-	66,820
	<u>45,957,808</u>	<u>54,850,784</u>	<u>(37,832,935)</u>	<u>62,975,657</u>
Property and equipment, net	-	4,485,682	-	4,485,682
Other assets:				
Deferred income tax asset	493,745	-	-	493,745
Other receivables	-	83,646	(14,853)	68,793
Related party notes receivable	7,757,835	-	-	7,757,835
Security deposits	-	36,500	-	36,500
	<u>8,251,580</u>	<u>120,146</u>	<u>(14,853)</u>	<u>8,356,873</u>
	<u><u>\$ 54,209,388</u></u>	<u><u>\$ 59,456,612</u></u>	<u><u>\$ (37,847,788)</u></u>	<u><u>\$ 75,818,212</u></u>
LIABILITIES AND EQUITY				
Current liabilities:				
Accounts payable	\$ 114,933	\$ 7,700,619	\$ (85,350)	\$ 7,730,202
Line of credit	-	3,006,982	-	3,006,982
Accrued payroll and related expenses	-	1,391,108	-	1,391,108
Accrued vacation	-	794,447	-	794,447
Accrued health and welfare	-	160,541	-	160,541
Accrued profit sharing expense	-	721,511	-	721,511
	<u>114,933</u>	<u>13,775,208</u>	<u>(85,350)</u>	<u>13,804,791</u>
Other liabilities:				
Related party loan payable	-	2,233,170	-	2,233,170
	<u>114,933</u>	<u>16,008,378</u>	<u>(85,350)</u>	<u>16,037,961</u>
Controlling interest	54,094,455	43,448,234	(43,448,234)	54,094,455
Noncontrolling interest	-	-	5,685,796	5,685,796
	<u>54,094,455</u>	<u>43,448,234</u>	<u>(37,762,438)</u>	<u>59,780,251</u>
	<u><u>\$ 54,209,388</u></u>	<u><u>\$ 59,456,612</u></u>	<u><u>\$ (37,847,788)</u></u>	<u><u>\$ 75,818,212</u></u>

See accompanying notes and independent accountants' review report.

Management Consulting, Inc. and Subsidiaries
Consolidating Statements of Operations
Year Ended December 31, 2019

	Management Consulting, Inc. & Subsidiary	MANCON LLC	Eliminations	Consolidated
Contract revenue	\$ 1,364,219	\$ 178,953,581	\$ (1,364,219)	\$ 178,953,581
Direct costs of contract revenue	3,985	143,262,495	-	143,266,480
Gross profit	1,360,234	35,691,086	(1,364,219)	35,687,101
Indirect costs of contract revenue	2,566,531	33,279,961	-	35,846,492
Costs not allocable to contracts	248,775	115,857	-	364,632
Income (loss) from operations	(1,455,072)	2,295,268	(1,364,219)	(524,023)
Other income (expense):				
Interest income	139,471	20,530	-	160,001
Dividend income	10,707	-	-	10,707
Interest expense	-	(157,504)	-	(157,504)
Realized and unrealized gain on investments	132,406	-	-	132,406
Gain on sale of property and equipment	-	34,113	-	34,113
Miscellaneous income	-	152,324	-	152,324
Total other income	282,584	49,463	-	332,047
Income (loss) before income taxes	(1,172,488)	2,344,731	(1,364,219)	(191,976)
Income tax benefit	(29,696)	-	-	(29,696)
Net income attributable to the noncontrolling interest	-	-	980,512	980,512
Net income (loss) attributable to the controlling interest	(1,142,792)	2,344,731	(2,344,731)	(1,142,792)
Net income (loss)	<u>\$ (1,142,792)</u>	<u>\$ 2,344,731</u>	<u>\$ (1,364,219)</u>	<u>\$ (162,280)</u>

See accompanying notes and independent accountants' review report.

Management Consulting, Inc. and Subsidiaries
Consolidating Statements of Changes in Equity
Year Ended December 31, 2019

	<u>Management Consulting, Inc. & Subsidiary</u>				<u>MANCON LLC</u>		<u>Consolidated Total</u>
	<u>Common Stock</u>	<u>Additional Paid-in Capital</u>	<u>Retained Earnings</u>	<u>Accumulated Other Comprehensive Income</u>	<u>Members' Equity</u>	<u>Eliminations</u>	
Balance, January 1, 2019	\$ 25,000	\$ 11,498,859	\$ 43,000,591	\$ 712,797	\$ 42,489,859	\$ (37,781,315)	\$ 59,945,791
Net income (loss)	-	-	(1,142,792)	-	2,344,731	(1,364,219)	(162,280)
Change resulting from adoption of new accounting standard (Note 2)	-	-	712,797	(712,797)	-	-	-
Distributions	-	-	-	-	(1,386,356)	1,383,096	(3,260)
Equity attributable to noncontrolling interest	-	-	-	-	-	5,685,796	5,685,796
Equity attributable to controlling interest	<u>25,000</u>	<u>11,498,859</u>	<u>42,570,596</u>	<u>-</u>	<u>43,448,234</u>	<u>(43,448,234)</u>	<u>54,094,455</u>
Balance, December 31, 2019	<u>\$ 25,000</u>	<u>\$ 11,498,859</u>	<u>\$ 42,570,596</u>	<u>\$ -</u>	<u>\$ 43,448,234</u>	<u>\$ (37,762,438)</u>	<u>\$ 59,780,251</u>

See accompanying notes and independent accountants' review report.

Management Consulting, Inc. and Subsidiaries
Consolidating Statements of Cash Flows
Year Ended December 31, 2019

	Management Consulting, Inc. & Subsidiary	MANCON LLC	Eliminations	Consolidated
Cash flows from operating activities:				
Net income (loss)	\$ (1,142,792)	\$ 2,344,731	\$ (1,364,219)	\$ (162,280)
Adjustments to reconcile net income (loss) to net cash used by operating activities:				
Depreciation	-	1,381,574	-	1,381,574
Deferred income taxes	(713,976)	-	-	(713,976)
Gain on sale of property and equipment	-	(34,113)	-	(34,113)
Non-cash contribution expense for donated stock	248,709	-	-	248,709
Realized and unrealized gain on investments	(132,406)	-	-	(132,406)
Allocated income from subsidiary	(1,364,219)	-	1,364,219	-
Change in assets and liabilities:				
Accounts receivable	-	(3,020,617)	-	(3,020,617)
Inventories	-	(920,209)	-	(920,209)
Income taxes, net	(395,850)	(84,333)	-	(480,183)
Prepaid expenses	-	99,308	-	99,308
Other receivables	-	1,208,110	(1,268,069)	(59,959)
Due from health and welfare trust	-	9,228	-	9,228
Accounts payable	(1,329,831)	(3,126,192)	1,268,069	(3,187,954)
Accrued expenses	-	(440,002)	-	(440,002)
Net cash used by operating activities	(4,830,365)	(2,582,515)	-	(7,412,880)
Cash flows from investing activities:				
Property and equipment acquisitions	-	(1,193,003)	-	(1,193,003)
Principal payments received from note receivable, net	3,738,330	-	-	3,738,330
Proceeds from sales of property and equipment	-	198,268	-	198,268
Proceeds from sales of investments	118,762	-	-	118,762
Purchase of investments	(10,707)	-	-	(10,707)
Net cash provided (used) by investing activities	3,846,385	(994,735)	-	2,851,650
Cash flows from financing activities:				
Advances on line of credit, net	-	3,006,982	-	3,006,982
Distributions from investment in subsidiary	1,383,096	-	(1,383,096)	-
Distributions paid	-	(1,386,356)	1,383,096	(3,260)
Net cash provided by financing activities	1,383,096	1,620,626	-	3,003,722
Net change in cash and cash equivalents	399,116	(1,956,624)	-	(1,557,508)
Cash and cash equivalents, beginning of year	5,902,715	1,963,388	-	7,866,103
Cash and cash equivalents, end of year	<u>\$ 6,301,831</u>	<u>\$ 6,764</u>	<u>\$ -</u>	<u>\$ 6,308,595</u>
Supplemental disclosure of cash flow information:				
Cash paid for interest	<u>\$ -</u>	<u>\$ 157,504</u>	<u>\$ -</u>	<u>\$ 157,504</u>
Cash paid for income taxes	<u>\$ 1,084,406</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1,084,406</u>

See accompanying notes and independent accountants' review report.

Notes to Consolidating Financial Statements

1. Organization and Nature of Business

Management Consulting, Inc. (“INC”) was incorporated in Virginia in 1983. It is a closely held corporation engaged in the sale of commercial industrial, packing, and office supplies, project management, inventory management, and warehouse services for United States government agencies, state agencies and commercial entities. INC is headquartered in Virginia Beach, Virginia and operates primarily in Virginia, California, Florida, Ohio and Texas; however, since a major portion of INC’s work is through federal government contracts, it also operates in other areas throughout the United States and overseas. MANCON Investments, LLC (“MANCON Investments”) a Virginia limited liability company, was organized on January 1, 2017, and is owned 100% by INC and was formed to hold the non-operating investment assets and report the investment income activity of the consolidated group. Collectively, these entities are presented as “Management Consulting, Inc. & Subsidiary or INC.” On January 1, 2017, INC transferred its non-operating investments assets into MANCON Investments.

MANCON LLC (“MANCON LLC”), a Virginia limited liability company, was organized on January 1, 2017, and was formed by INC to hold the operating assets and report the operational results of the consolidated group. INC owns 90% of MANCON LLC’s membership interest with the remaining 10% being owned by INC’s shareholders. On January 1, 2017, INC transferred its operating assets into MANCON LLC.

2. Summary of Significant Accounting Policies

Principles of consolidation

The consolidating financial statements include the accounts of Management Consulting, Inc. and its wholly and majority-owned subsidiaries, MANCON Investments and MANCON LLC, respectively (collectively, the “Company”). All significant intercompany transactions have been eliminated in consolidation. Management Consulting, Inc. has 90% ownership interest in MANCON LLC; therefore, noncontrolling ownership interest exists within consolidated equity and within consolidated net income (loss). For 2019, net income attributable to the noncontrolling interest was approximately \$981,000. At December 31, 2019, noncontrolling interest within consolidated equity was approximately \$5,686,000.

Adoption of new accounting standard

Accounting Standards Update No. 2016-01

In 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-01, *Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*, which requires entities to measure substantially all equity securities at fair value and recognize changes in fair value in net income. Prior to issuance of this ASU, the Company held unrealized gains and losses related to equity investments in accumulated other comprehensive income and equity investments without readily determinable fair values were measured at amortized cost. The Company adopted the new standard effective January 1, 2019 using the modified retrospective method with a cumulative-effect adjustment to retained earnings. The adoption of the ASU did not have a significant impact on the Company’s financial statements. As of January 1, 2019, the Company reclassified net after-tax unrealized gains on equity securities from accumulated other comprehensive income to retained earnings. A summary of the effects of the initial adoption of ASU 2016-01:

Increase (decrease):

Accumulated other comprehensive income	\$ (712,797)
Retained earnings	\$ 712,797

Management Consulting, Inc. and Subsidiaries

Notes to Consolidating Financial Statements

Revenue and cost recognition

For financial reporting purposes, MANCON LLC's revenues and earnings on fixed-price, government contracts are generally recognized on the percentage-of-completion method of accounting as costs are incurred (cost-to-cost basis). Revenues include costs incurred plus a portion of estimated fees or profits based on the relationship of costs incurred to total estimated costs. Revenues on time-and-material contracts are recognized based on hours incurred, extended at contract rates plus material expenses incurred.

Contract revenues are derived substantially from the U.S. government under various contracts types. Although these revenues are subject to adjustment upon audit by the respective government agencies, management does not expect such adjustments to have a material effect on MANCON LLC's financial position or results of operations.

The Company has negotiated final settlement of indirect cost rates for all years through 2010.

The entire balance of INC's revenue is generated from its investment in MANCON LLC which is eliminated in consolidation.

On June 3, 2020, the FASB issued ASU 2020-05, *Revenue from Contracts with Customers (Topic 606) and Leases (Topic 842): Effective Dates for Certain Entities*, extending one-year delays to certain companies to provide immediate, near-term relief for whom these standards are either currently effective or imminently effective.

The ASU permits private companies and not-for-profit organizations that have not yet issued (or made available) financial statements with Accounting Standards Codification (ASC) 606, *Revenue from Contracts with Customers* implemented to defer one year to annual reporting periods beginning after December 15, 2019. Therefore, the Company has chosen to delay implementation of ASC 606 and will adopt this standard on its December 31, 2020 yearend consolidating financial statements.

Credit risk

Financial instruments which potentially subject the Company to concentration of credit risk consist primarily of temporary cash investments and accounts receivable. The Company places its temporary cash investments with high credit quality financial institutions. In evaluating this credit risk, the Company periodically evaluates the stability of these financial institutions. At December 31, 2019, INC and MANCON LLC had on deposit approximately \$7,388,941 and \$-0-, respectively, in excess of the amount insured by the Federal Deposit Insurance Corporation.

A concentration of credit risk with MANCON LLC's major customers, as described in Note 11, exists with respect to trade accounts receivable. However, because these customers are comprised of various agencies of the United States government and the Virginia Department of Transportation (VDOT), management considers credit risk to be minimal.

Cash and cash equivalents

The Company considers all highly liquid investments with a remaining maturity of three months or less at the time of purchase to be cash equivalents. The carrying value of cash and cash equivalents approximates fair value because of the short-term maturities of those financial instruments.

Investments

The Company carries substantially all investments in equity securities at fair value and record the subsequent changes in fair values in the consolidating statements of operations as a component of investment gains (losses). Prior to January 1, 2019, substantially all equity security investments were classified as available-for-sale and were also carried at fair value. However, the periodic changes in fair value of these securities were recorded as components of other comprehensive income. Any gains and losses realized upon the ultimate disposition of the securities would be reported in the consolidating statements of operations when equity securities were sold (on a specific identification basis) or were other-than-temporarily impaired.

Management Consulting, Inc. and Subsidiaries

Notes to Consolidating Financial Statements

Equity method investments

INC records its investment in MANCON LLC using the equity method of accounting. The gains (losses) are shown as revenue on INC's statement of operations and 100% is eliminated in consolidation.

Accounts receivable and allowance for doubtful accounts

MANCON LLC grants uncollateralized credit in the form of accounts receivable to its customers, which are primarily agencies of the United States Government and state and local governments and provides an allowance for doubtful accounts based upon management's assessment of the collectability of existing specific accounts. MANCON LLC evaluates each of its accounts receivable individually and provides a charge to income when appropriate, in the opinion of management, to absorb probable credit losses.

Inventories

Inventories consist of finished goods and are stated at the lower of cost or net realizable value determined on a last-in, first-out (LIFO) basis. At December 31, 2019, the reserve required under the LIFO method was \$940,275.

Property and equipment

Property and equipment are recorded at cost and depreciated by straight-line or accelerated methods over estimated useful lives which range as follows:

Vehicles	5 years
Software	3 years
Machinery and equipment	5 - 7 years
Office equipment	5 years
Furniture and fixtures	5 - 7 years
Leasehold improvements	5 - 39 years

Maintenance and repairs of property and equipment are charged to operations and major improvements are capitalized. Upon retirement, sale, or other disposition of property and equipment, the cost and accumulated depreciation are eliminated from the accounts and the related gain or loss is recognized as other income.

Income taxes

INC follows the asset and liability method of accounting for income taxes. Income taxes are provided for the tax effects of transactions reported in the consolidating financial statements and consist of taxes currently due plus deferred taxes related primarily to differences between the basis for financial and income tax reporting on equity securities and investment in consolidated subsidiaries that are taxed as partnerships. The deferred tax asset represents the future tax return consequences of those differences, which will be taxable/deductible when the differences are settled. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized.

MANCON LLC and MANCON Investments are limited liability companies whereby the earnings of the companies are includable in the tax returns of the members based on their proportionate share of total earnings. Consequently, no provision for income taxes is included in the consolidating financial statements for MANCON LLC and MANCON Investments.

Tax positions must meet a recognition threshold of more likely than not in order for the benefit of those tax positions to be recognized in the consolidating financial statements. The Company has determined that it does not have any material unrecognized tax benefits or obligations as of December 31, 2019. Interest and penalties related to income tax assessments, if any, are reflected in costs not allocable to contracts in the accompanying consolidating statements of operations. As of the date of these consolidating financial statements, INC remains under audit by the Internal Revenue Service for the year ended December 31, 2017, but no material changes to previous tax positions on that return are expected by management.

Management Consulting, Inc. and Subsidiaries

Notes to Consolidating Financial Statements

Presentation of sales taxes

MANCON LLC's sales are subject to sales tax imposed by various jurisdictions. MANCON LLC collects sales tax from customers and remits it to the applicable jurisdiction. MANCON LLC's accounting policy is to exclude the tax collected and remitted from contract revenues and cost of contract revenues.

Use of estimates

The preparation of consolidating financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidating financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates and assumptions.

Subsequent events

In preparing these consolidating financial statements, the Company has evaluated events and transactions for potential recognition or disclosure through June 19 2020, the date which the consolidating financial statements were available to be issued.

Subsequent to the consolidating balance sheet date, the World Health Organization declared the outbreak of COVID-19, a novel strain of coronavirus, a pandemic. The coronavirus outbreak is disrupting supply chains and affecting production and sales across a range of industries. The extent of the impact of the outbreak on the Company's operational and financial performance will depend on certain developments, including the duration and spread of the outbreak, impact on the Company's customers, employees and vendors, and governmental, regulatory and private sector responses. The consolidating financial statements do not reflect any adjustments as a result of the subsequent increase in economic uncertainty. As of the consolidating balance sheet date, the Company has significant receivable and inventory balances outstanding. The full economic impact of this pandemic has not been determined, including the impact on the creditworthiness of the Company's customers and the future sale of inventory.

3. Investments

Cost and fair value of healthcare equity securities at December 31, 2019, are as follows:

At cost	\$ 82,755
Unrealized gain	<u>747,582</u>
	<u>\$ 830,337</u>

For the year ending December 31, 2019, net unrealized investment gains recognized in the statement of operations for securities still held at December 31, 2019 was \$132,406. There were no recognized gains on sales of equity securities during 2019.

4. Fair Value Measurements

The Company measures fair value in accordance with the provisions of ASC Topic 820-10, which provides a framework for measuring fair value under generally accepted accounting principles. It defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. It requires that valuation techniques maximize the use of observable inputs and minimize the use

Management Consulting, Inc. and Subsidiaries

Notes to Consolidating Financial Statements

of unobservable inputs. It also establishes a fair value hierarchy, which prioritizes the valuation inputs into three broad levels.

There are three general valuation techniques that may be used to measure fair value, as described below:

- Level 1: Observable inputs such as quoted prices in active markets for identical assets and liabilities.
- Level 2: Inputs other than quoted prices in active markets that are either directly or indirectly observable.
- Level 3: Unobservable inputs about which little or no market data exists, therefore requiring a fund to develop its own assumptions.

INC's asset and liabilities itemized below were measured at fair value at December 31, 2019, as follows:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Investments:				
Stocks	\$ 830,337	\$ -	\$ -	\$ 830,337

The following is a description of valuation methodologies for assets and liabilities measured at fair value. Fair value for Level 1 is based upon quoted market prices.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Company believes the valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

5. Property and Equipment

All major classes of property and equipment were held by MANCON LLC and consisted of the following at December 31, 2019:

Vehicles	\$ 6,204,353
Software	1,312,853
Machinery and equipment	1,471,530
Office equipment	1,256,974
Furniture and fixtures	1,470,192
Leasehold improvements	<u>1,128,290</u>
	12,844,192
Accumulated depreciation	<u>(8,358,510)</u>
	<u>\$ 4,485,682</u>

6. Line of Credit

At December 31, 2019, MANCON LLC had a \$10,000,000 line of credit available with a financial institution through July 31, 2020. At December 31, 2019, MANCON LLC had outstanding draws of \$3,006,982 on the line of credit. The line of credit is subject to certain covenants, which the Company was in compliance with at December 31, 2019, and is collateralized by MANCON LLC's accounts receivable, inventory and all cash proceeds related to these assets. The line of credit is also guaranteed by MANCON Investments. Interest on outstanding draws is payable at the thirty-day LIBOR plus 1.75% (3.51% at December 31, 2019).

Management Consulting, Inc. and Subsidiaries

Notes to Consolidating Financial Statements

7. Income Taxes

Income tax expense (benefit) for the year ended December 31, 2019 for INC consists of the following:

Provision for deferred income tax expense (benefit)	\$ (713,976)
Provision for current federal and state income tax	<u>684,280</u>
	<u>\$ (29,696)</u>

At December 31, 2019, the Company's income tax expense does not materially differ from the amount which would be obtained by applying statutory income tax rates of 26% to consolidated net loss before income taxes.

The tax effects of temporary differences that give rise to significant portions of the net deferred tax asset at December 31, 2019 are:

Deferred tax asset:	
Net operating loss carryforward (federal and state)	<u>\$ 786,028</u>
Deferred tax liability:	
Unrealized gain on investment	(201,800)
Outside basis of INC's investment in LLC	<u>(90,483)</u>
	<u>(292,283)</u>
Total net deferred tax asset	<u>\$ 493,745</u>

The net operating loss carryforward, which is generating the deferred tax asset noted above, is approximately \$2,800,000 and can be carried forward indefinitely by INC.

8. Profit Sharing Plan

The Company has a qualified 401(k) profit sharing plan in which employees with over six months of service are eligible to participate. Contributions to the plan are determined by the Board of Directors on an annual basis. There were discretionary and matching contributions of \$694,201 (MANCON LLC - \$593,206 and INC - \$100,995) during the year ended December 31, 2019.

9. Lease Commitments

During 2019, MANCON LLC paid \$1,124,356 in rent expense to a company under common ownership. The lease agreement is on a month to month basis.

MANCON LLC also leases other facilities from nonrelated parties. These leases expire at various times through 2023 and some of these leases contain lease escalation clauses. During the year ended December 31, 2019, total rental expenses (including amounts shown in the first paragraph paid to related parties) included in the consolidating statements of operations approximated \$1,749,000.

Management Consulting, Inc. and Subsidiaries

Notes to Consolidating Financial Statements

Future minimum rental payments required under the non-cancellable operating leases at December 31, 2019, are as follows:

<u>Year Ending</u> <u>December 31,</u>	
2020	\$ 576,786
2021	570,319
2022	210,708
2023	<u>9,616</u>
	<u>\$ 1,367,429</u>

10. Health and Welfare Trust

The Company has two health and welfare trusts for the benefit of its employees. During 2019, INC and MANCON LLC recorded health and welfare expense of \$56,401 and \$4,567,353 during the year ended December 31, 2019, respectively. The Company records an estimated amount due to/from the trusts based on claim activity and the trust's assets and these amounts are shown on the consolidating balance sheets.

11. Concentrations of Credit Risk

MANCON LLC's revenues earned from contracts with United States Government agencies were \$48,980,911 during the year ended December 31, 2019. Of this amount, \$2,975,269 remained outstanding at December 31, 2019. Revenues earned from contracts with state and local government agencies were \$125,521,086 during the year ended December 31, 2019. Of this amount, \$16,346,133 remained outstanding at December 31, 2019.

12. Related Party Transactions

MANCON LLC held loans totaling \$2,233,170 due to a member at December 31, 2019. Interest is paid annually at prime plus 1% (5.75% at December 31, 2019). The loans are unsecured and have no stated maturity date. The member has unconditionally waived the right to demand payment until January 1, 2021. During the year ended December 31, 2019, interest expense to the member was \$140,323.

In April 2012, INC issued a note receivable of \$6,300,000 to its majority stockholder, bearing interest at the applicable federal rate of 1.15%, payable in full June 2020. During the year ended December 31, 2019, the stockholder made principal payments totaling \$1,500,000. At December 31, 2019, the principal balance on this note was \$3,500,000 and total interest income earned during 2019 was \$46,128.

In November 2011, INC loaned \$3,600,000 to a partnership owned by a stockholder, bearing interest at the applicable federal rate of 1.19%, payable in full in June 2020. Total principal payments on this note were \$185,000, during the year ended December 31, 2019. At December 31, 2019, the principal and accrued interest balance on this note was \$2,212,000. Total interest income earned on this note was \$27,531 during the year ended December 31, 2019.

In December 2015, INC made advances to its majority stockholder in exchange for a note receivable of \$1,500,000, bearing interest at the applicable federal rate of 0.56% payable in full no later than December 1, 2018. On January 11, 2019, the unpaid principal and interest on the loan was paid in full.

Management Consulting, Inc. and Subsidiaries

Notes to Consolidating Financial Statements

In March 2013, INC loaned \$2,750,000 to a partnership owned by a minority stockholder and his spouse, bearing interest at the applicable federal rate of 1.09%, payable in full June 30, 2021. During the year ended December 31, 2019, this related party repaid \$305,000 on the note. Total interest earned on this note was \$6,321 during the year ended December 31, 2019. The balance of principal and accrued interest outstanding at December 31, 2019 was \$386,000.

Two members of the Company are the beneficiaries of a trust which owns an entity that provided property and casualty insurance services to the Company in prior years. During 2018, the entity refunded prior paid premiums to the Company through issuance of a note receivable from the related party insurance company, totaling \$1,684,000, bearing interest at the applicable federal rate of 2.87%, payable in full no later than July 1, 2027. During the year ended December 31, 2019, the Company earned interest on the note totaling \$48,331. The balance of principal and accrued interest outstanding at December 31, 2019 was \$1,659,835.

In May 2017, INC issued a note receivable to its majority stockholder, totaling \$1,126,000, bearing interest at the applicable federal rate of 1.15% payable in full no later than December 31, 2019. In January 2019, the remaining principal and interest on the loan was paid in full.

13. Common Stock

INC has authorized 2,500 shares of \$10 par value Class A common stock and 97,500 shares of no par value Class B common stock. At December 31, 2019, common stock consisted of the following:

	<u>Shares Authorized</u>	<u>Shares Outstanding</u>
Class A - Voting Common Stock	2,500	2,500
Class B - Non-Voting Common Stock	<u>97,500</u>	<u>78,720</u>
	<u>100,000</u>	<u>81,220</u>

Holders of the class A stock are entitled to one vote per share in the affairs of INC, while the holders of the class B stock are not entitled to vote. In all other matters, including, but not limited to, dividend and distribution rights and the liquidation rights of the stockholders upon dissolution of INC, the rights of class A and class B stockholders are equal.

DHG