FalconStor Software, Inc. and Subsidiaries CONDENSED CONSOLIDATED BALANCE SHEETS

	December 31, 2016	December 31, 2015
	(unaudited)	
Assets		
Current assets:		
Cash and cash equivalents	\$ 3,391,528	\$ 6,013,382
Marketable securities	—	7,420,042
Accounts receivable, net	5,003,972	6,635,262
Prepaid expenses and other current assets	1,245,085	1,742,668
Inventory	6,181	70,534
Deferred tax assets, net		205,816
Total current assets	9,646,766	22,087,704
Property and equipment, net	1,174,942	1,565,932
Deferred tax assets, net	577,735	110,060
Software development costs, net	547,558	1,116,816
Other assets, net	973,949	1,139,377
Goodwill	4,150,339	4,150,339
Other intangible assets, net	209,456	256,137
Total assets	\$ 17,280,745	\$ 30,426,365
Liabilities and Stockholders' Deficit		
Current liabilities:		
Accounts payable	\$ 419,877	\$ 1,005,944
Accrued expenses	4,471,010	6,783,514
Deferred tax liabilities, net	_	89,343
Deferred revenue, net	15,236,123	16,553,519
Total current liabilities	20,127,010	24,432,320
Other long-term liabilities	1,170,844	735,089
Deferred tax liabilities, net	254,776	27,069
Deferred revenue, net	8,430,692	9,122,289
Total liabilities	29,983,322	34,316,767
Commitments and contingencies		
Series A redeemable convertible preferred stock	9,000,000	7,818,554
Total stockholders' deficit	(21,702,577)) (11,708,956)
Total liabilities and stockholders' deficit	\$ 17,280,745	\$ 30,426,365

FalconStor Software, Inc. and Subsidiaries CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)

2016 2015 2016 2015 Revenue: Product revenue \$ 2,650,901 \$ 3,470,274 \$ 10,116,897 \$ 24,847,724 Support and services revenue 4,785,353 5,925,026 20,146,449 23,723,267 Total revenue 7,436,254 9,395,300 30,263,346 48,570,901 Cost of revenue: 222,213 323,843 932,446 1,942,985 Support and service 1,676,129 1,863,312 7,351,857 7,739,149 Total cost of revenue 1,898,342 2,187,155 8,284,303 9,682,134 Gross profit \$ 5,537,912 \$ 7,02,9145 \$ 2,1979,043 \$ 38,888,870 Operating expenses:		Three Months Ended December 31,			Twelve Months Ended December 31,			
Product revenue \$ 2,650,901 \$ 3,470,274 \$ 10,116,897 \$ 24,847,724 Support and services revenue 4,785,353 5,925,026 20,146,449 23,723,267 Total revenue 7,436,254 9,395,300 30,263,346 48,570,991 Cost of revenue: 222,213 323,843 932,446 1,942,985 Support and service 1,667,129 1,863,312 7,531,857 7,73,149 Total cost of revenue 5,537,912 \$ 7,20,145 \$ 21,97,043 \$ 38,88,857 Operating expenses: Research and development costs 2,227,278 3,059,879 11,702,956 12,787,606 Selling and marketing 2,533,442 4,216,300 13,918,493 18,021,989 General and administrative 1,369,840 1,971,790 6,470,579 9,181,289 Investigation, nitigation, and settlement related costs - - - 8,842 Operating expenses 6,130,560 9,247,969 32,269,417 40,172,721 Total operating expenses 6,130,560 9,247,969 32,269,417 40,172,721		2016	_	2015		2016		2015
Support and services revenue $4,785,353$ $5,925,026$ $20,146,449$ $23,723,267$ Total revenue $7,436,254$ $9,395,300$ $30,263,346$ $48,570,991$ Cost of revenue: $222,213$ $323,843$ $932,446$ $1,942,985$ Support and service $1,676,129$ $1,863,312$ $7,351,857$ $7,739,149$ Total cost of revenue $1,898,342$ $2,187,155$ $8,284,303$ $9,682,134$ Gross profit\$ 5,537,912\$ 7,08,145\$ 21,979,043\$ 38,888,857Operating expenses: $2,227,278$ $3,059,879$ $11,702,956$ $12,787,606$ Selling and marketing $2,533,442$ $4,216,300$ $13,918,493$ $18,021,989$ General and administrative $1,369,840$ $1,971,790$ $6,470,579$ $9,181,289$ Investigation, litigation, and settlement related costs $ 8,842$ Restructuring costs $ 7,73,89$ $172,995$ Total operating expenses $6,130,560$ $9,247,969$ $32,269,417$ $40,172,721$ Operating loss $(52,2648)$ $(2,039,824)$ $(10,290,374)$ $(1,283,864)$ Interest and other (loss) income, net $(386,610)$ $70,014$ $(212,123)$ $(269,954)$ Loss before income taxes $(979,258)$ $(1,998,794)$ $$(1,929,361)$ $(15,23,818)$ Provision (benefit) for income taxes $211,869$ $(28,193)$ $587,207$ $375,543$ Net loss $$(1,191,127)$ $$(1,941,617)$ $$(1,998,794)$ $$(1,929,361)$ <td>Revenue:</td> <td></td> <td></td> <td></td> <td></td> <td></td> <td></td> <td></td>	Revenue:							
Total revenue $7,436,254$ $9,395,300$ $30,263,346$ $48,570,991$ Cost of revenue:Product $222,213$ $323,843$ $932,446$ $1,942,985$ Support and service $1,676,129$ $1,863,312$ $7,351,857$ $7,739,149$ Total cost of revenue $1,898,342$ $2,187,155$ $8,284,303$ $9,682,134$ Gross profit\$ 5,537,912\$ 7,208,145\$ 21,979,043\$ 38,888,857Operating expenses: $2,227,278$ $3,059,879$ $11,702,956$ $12,787,606$ Selling and marketing $2,533,442$ $4,216,300$ $13,918,493$ $18,021,989$ General and administrative $1,369,840$ $1,971,790$ $6,470,579$ $9,181,289$ Investigation, litigation, and settlement related costs $ -$ Restructuring costs $ 8,842$ Restructuring costs $ 8,842$ Interest and other (loss) income, net $(386,610)$ $70,014$ $(121,213)$ $(269,954)$ Loss before income taxes $(21,1869)$ $(2,919,81,28)$ $587,207$ $375,543$ Net loss\$ $(1,191,127)$ \$ $(1,941,157)$ $(1,553,818)$ Provision (benefit) for income taxes $211,869$ $(22,95,014)$ \$ $(1,929,374)$ Less: Accretion to redemption value of Series A redeemable $668,177$ $156,670$ $1,181,446$ $587,613$ Net loss attributable to common stockholders\$ $(2,055,2208)$ \$ $(2,295,014)$ \$ $(1,298,81,30)$ \$ $(3,282,1$	Product revenue	\$ 2,650,901	\$	3,470,274	\$	10,116,897	\$	24,847,724
Cost of revenue: 222,213 323,843 932,446 1,942,985 Support and service 1,676,129 1,863,312 7,351,857 7,739,149 Total cost of revenue 1,898,342 2,187,155 8,284,303 9,682,134 Gross profit \$ 5,537,912 \$ 7,208,145 \$ 21,979,043 \$ 38,888,857 Operating expenses: $=$ $=$ $=$ $=$ Research and development costs 2,227,278 $3,059,879$ $11,702,956$ $12,787,606$ Selling and marketing 2,533,442 4,216,300 $13,918,493$ $18,021,989$ General and administrative $1,369,840$ $1,971,790$ $6,70579$ $9,181,289$ Investigation, litigation, and settlement related costs $ -$	Support and services revenue	4,785,353	_	5,925,026	_	20,146,449	_	23,723,267
Product 222,213 323,843 932,446 1,942,985 Support and service 1,676,129 1,863,312 7,351,857 7,739,149 Total cost of revenue 1,898,342 2,187,155 8,284,303 9,682,134 Gross profit \$ 5,537,912 \$ 7,208,145 \$ 21,979,043 \$ 38,888,857 Operating expenses: 11,702,956 12,787,606 Selling and marketing 2,533,442 4,216,300 13,918,493 18,021,989 General and administrative 1,369,840 1,971,790 6,470,579 9,181,289 Investigation, litigation, and settlement related costs - - - 8,842 Restructuring costs - - - 8,842 Restructuring expenses 6,130,560 9,247,969 32,269,417 40,172,721 Operating loss icomen, net (386,610) 70,014 (122,123) (269,954) Interest and other (loss) income, net (386,610) 70,014 (121,213) (269,954) Less: Accrual of Series A redeemab	Total revenue	 7,436,254		9,395,300	_	30,263,346		48,570,991
Support and service $1,676,129$ $1,863,312$ $7,351,857$ $7,739,149$ Total cost of revenue $1,898,342$ $2,187,155$ $8,284,303$ $9,682,134$ Gross profit\$ 5,537,912\$ 7,208,145\$ 21,979,043\$ 38,888,857Operating expenses: $2,227,278$ $3,059,879$ $11,702,956$ $12,787,606$ Selling and marketing $2,533,442$ $4,216,300$ $13,918,493$ $18,021,989$ General and administrative $1,369,840$ $1,971,790$ $6,470,579$ $9,181,289$ Investigation, litigation, and settlement related costs $ 8,842$ Restructuring costs $ 8,842$ Restructuring costs $ 8,842$ Interest and other (loss) income, net $(592,648)$ $(2,039,824)$ $(10,29,374)$ $(1,283,864)$ Interest and other (loss) income, net $(386,610)$ $70,014$ $(122,123)$ $(269,954)$ Loss before income taxes $211,869$ $(28,193)$ $587,207$ $375,543$ Net loss 5 $(1,191,127)$ 5 $(1,0998,794)$ 5 $(1,929,361)$ Less: Accrual of Series A redeemable convertible preferred stock $668,177$ $156,670$ $1,181,446$ $587,613$ Net loss attributable to common stockholders 8 $(2,055,208)$ 8 $(2,295,14)$ 8 $(2,295,14)$ 8 $(2,295,14)$ 8 $(2,295,14)$ 8 $(2,295,14)$ 8 $(2,28,130)$ 8 $(3,282,177)$ Basic net los	Cost of revenue:							
Total cost of revenue1.898,3422,187,1558,284,3039,682,134Gross profit\$ 5,537,912\$ 7,208,145\$ 21,979,043\$ 38,888,857Operating expenses:Research and development costs $2,227,278$ $3,059,879$ $11,702,956$ $12,787,606$ Selling and marketing $2,533,442$ $4,216,300$ $13,918,493$ $18,021,989$ General and administrative $1,369,840$ $1,971,790$ $6,470,579$ $9,181,289$ Investigation, litigation, and settlement related costs $ 8,842$ Restructuring costs $ 177,389$ $172,995$ Total operating expenses $6,130,560$ $9,247,969$ $32,269,417$ $40,172,721$ Operating loss $(592,648)$ $(2,039,824)$ $(10,290,374)$ $(1,283,864)$ Interest and other (loss) income, net $(386,610)$ $70,014$ $(121,213)$ $(269,954)$ Loss before income taxes $(979,258)$ $(1,969,810)$ $(10,411,587)$ $(1,553,818)$ Provision (benefit) for income taxes $211,869$ $(28,193)$ $587,207$ $375,543$ Net loss\$ $(1,191,127)$ \$ $(1,941,617)$ \$ $(10,998,794)$ \$ $(1,929,361)$ Less: Accrutal of Series A redeemable convertible preferred stock $195,904$ $196,727$ $777,890$ $765,203$ Less: Accrutal of Series A redeemable convertible preferred stock 5 $(0,05)$ \$ $(0,06)$ \$ $(3,282,177)$ Basic net loss per share attributable to common stockholders\$ $(2,055,208)$ \$ $(2,295,014)$	Product	222,213		323,843		932,446		1,942,985
Gross profit \$ 5,537,912 \$ 7,208,145 \$ 21,979,043 \$ 38,888,857 Operating expenses: Research and development costs 2,227,278 3,059,879 11,702,956 12,787,606 Selling and marketing 2,533,442 4,216,300 13,918,493 18,021,989 General and administrative 1,369,840 1,971,790 6,470,579 9,181,289 Investigation, litigation, and settlement related costs — — — 8,842 Restructuring costs — — — 8,842 Restructuring costs — — 177,389 172,995 Total operating expenses 6,130,560 9,247,969 32,269,417 40,172,721 Operating loss (592,648) (2,039,824) (10,290,374) (1,283,864) Interest and other (loss) income, net (386,610) 70,014 (121,213) (269,954) Loss before income taxes (979,258) (1,969,810) (10,411,587) (1,553,818) Provision (benefit) for income taxes 211,869 (28,193) 587,207 375,543 Net loss \$ (1,191,127) \$ (1,941,617) \$ (1,999,361) <td>Support and service</td> <td> 1,676,129</td> <td></td> <td>1,863,312</td> <td></td> <td>7,351,857</td> <td></td> <td>7,739,149</td>	Support and service	 1,676,129		1,863,312		7,351,857		7,739,149
Operating expenses: Research and development costs $2,227,278$ $3,059,879$ $11,702,956$ $12,787,606$ Selling and marketing $2,533,442$ $4,216,300$ $13,918,493$ $18,021,989$ General and administrative $1,369,840$ $1,971,790$ $6,470,579$ $9,181,289$ Investigation, litigation, and settlement related costs $ 8,842$ Restructuring costs $ 8,842$ Restructuring costs $ 8,842$ Interest and other (loss) income, net $(592,648)$ $(2,039,824)$ $(10,290,374)$ $(1,283,864)$ Interest and other (loss) income taxes $(979,258)$ $(1,969,810)$ $(10,411,587)$ $(1,553,818)$ Provision (benefit) for income taxes $211,869$ $(28,193)$ $587,207$ $375,543$ Net loss \$ (1,191,127) \$ $(1,941,617)$ \$ $(1,999,874)$ \$ $(1,929,374)$ $(1,292,361)$ Less: Accretion to redemption value of Series A redeemable convertible preferred stock $95,904$ $196,727$ $777,890$ $765,203$ Less: Accretion to redemption value of	Total cost of revenue	1,898,342		2,187,155	_	8,284,303		9,682,134
Research and development costs $2,227,278$ $3,059,879$ $11,702,956$ $12,787,606$ Selling and marketing $2,533,442$ $4,216,300$ $13,918,493$ $18,021,989$ General and administrative $1,369,840$ $1,971,790$ $6,470,579$ $9,181,289$ Investigation, litigation, and settlement related costs $ 8,842$ Restructuring costs $ 8,842$ Restructuring costs $ 8,842$ Operating expenses $6,130,560$ $9,247,969$ $32,269,417$ $40,172,721$ Operating loss $(592,648)$ $(2,039,824)$ $(10,290,374)$ $(1,283,864)$ Interest and other (loss) income, net $(386,610)$ $70,014$ $(121,213)$ $(269,954)$ Loss before income taxes $(979,258)$ $(1,969,810)$ $(10,411,587)$ $(1,553,818)$ Provision (benefit) for income taxes $211,869$ $(28,193)$ $587,207$ $375,543$ Net loss\$ $(1,91,127)$ \$ $(1,941,617)$ \$ $(1,998,794)$ \$ $(1,929,361)$ Less: Accrual of Series A redeemable convertible preferred stock $195,904$ $196,727$ $777,890$ $765,203$ Less: Accruation to redemption value of Series A redeemable convertible preferred stock $668,177$ $156,670$ $1,181,446$ $587,613$ Net loss attributable to common stockholders\$ $(2,055,208)$ \$ $(2,295,014)$ \$ $(12,958,130)$ \$ $(3,282,177)$ Basic net loss per share attributable to common stockholders\$ $(0,05)$ \$ $(0,06)$ \$	Gross profit	\$ 5,537,912	\$	7,208,145	\$	21,979,043	\$	38,888,857
Selling and marketing $2,533,442$ $4,216,300$ $13,918,493$ $18,021,989$ General and administrative $1,369,840$ $1,971,790$ $6,470,579$ $9,181,289$ Investigation, litigation, and settlement related costs $ 8,842$ Restructuring costs $ 8,842$ Restructuring costs $ 8,842$ Operating expenses $6,130,560$ $9,247,969$ $32,269,417$ $40,172,721$ Operating loss $(592,648)$ $(2,039,824)$ $(10,290,374)$ $(1,283,864)$ Interest and other (loss) income, net $(386,610)$ $70,014$ $(121,213)$ $(269,954)$ Loss before income taxes $(979,258)$ $(1,969,810)$ $(10,411,587)$ $(1,553,818)$ Provision (benefit) for income taxes $211,869$ $(28,193)$ $587,207$ $375,543$ Net loss\$ (1,191,127)\$ $(1,998,794)$ \$ $(1,929,361)$ Less: Accrual of Series A redeemable convertible preferred stock $195,904$ $196,727$ $777,890$ $765,203$ Less: Accrution to redemption value of Series A redeemable $668,177$ $156,670$ $1,181,446$ $587,613$ Net loss attributable to common stockholders\$ $(2,055,208)$ \$ $(12,958,130)$ \$ $(3,282,177)$ Basic net loss per share attributable to common stockholders\$ (0.05) \$ (0.06) \$ (0.30) \$ (0.08) Diluted net loss per share attributable to common stockholders\$ (0.05) \$ (0.06) \$ (0.30) \$ (0.08) Weighted a	Operating expenses:							
General and administrative1,369,8401,971,7906,470,5799,181,289Investigation, litigation, and settlement related costs———8,842Restructuring costs———177,389172,995Total operating expenses6,130,5609,247,96932,269,41740,172,721Operating loss(592,648)(2,039,824)(10,290,374)(1,283,864)Interest and other (loss) income, net(386,610)70,014(121,213)(269,954)Loss before income taxes(979,258)(1,969,810)(10,411,587)(1,553,818)Provision (benefit) for income taxes211,869(28,193)587,207375,543Net loss\$(1,191,127)\$(1,941,617)\$(1,999,794)\$Less: Accrual of Series A redeemable convertible prefered stock195,904196,727777,890765,203Less: Accruat of Series A redeemable convertible prefered stock668,177156,6701,181,446587,613Net loss attributable to common stockholders\$(0.05)\$(0.30)\$(0.08)Basic net loss per share attributable to common stockholders\$(0.05)\$(0.30)\$(0.08)Weighted average basic shares outstanding $43,818,413$ $41,356,757$ $43,091,878$ $41,093,644$	Research and development costs	2,227,278		3,059,879		11,702,956		12,787,606
Investigation, litigation, and settlement related costs $ -$ <	Selling and marketing	2,533,442		4,216,300		13,918,493		18,021,989
Restructuring costs $ 177,389$ $172,995$ Total operating expenses $6,130,560$ $9,247,969$ $32,269,417$ $40,172,721$ Operating loss $(592,648)$ $(2,039,824)$ $(10,290,374)$ $(1,283,864)$ Interest and other (loss) income, net $(386,610)$ $70,014$ $(121,213)$ $(269,954)$ Loss before income taxes $(979,258)$ $(1,969,810)$ $(10,411,587)$ $(1,553,818)$ Provision (benefit) for income taxes $211,869$ $(28,193)$ $587,207$ $375,543$ Net loss $$$ $$(1,191,127)$ $$(1,941,617)$ $$(10,998,794)$ $$(1,929,361)$ Less: Accrual of Series A redeemable convertible preferred stock $195,904$ $196,727$ $777,890$ $765,203$ Less: Accretion to redemption value of Series A redeemable convertible preferred stock $$(2,055,208)$ $$(2,295,014)$ $$(12,958,130)$ $$(3,282,177)$ Basic net loss per share attributable to common stockholders $$(0.05)$ $$(0.06)$ $$(0.30)$ $$(0.08)$ Diluted net loss per share attributable to common stockholders $$(0.05)$ $$(0.06)$ $$(0.30)$ $$(0.08)$ Weighted average basic shares outstanding $43,818,413$ $41,356,757$ $43,091,878$ $41,093,644$	General and administrative	1,369,840		1,971,790		6,470,579		9,181,289
Total operating expenses $6,130,560$ $9,247,969$ $32,269,417$ $40,172,721$ Operating loss $(592,648)$ $(2,039,824)$ $(10,290,374)$ $(1,283,864)$ Interest and other (loss) income, net $(386,610)$ $70,014$ $(121,213)$ $(269,954)$ Loss before income taxes $(979,258)$ $(1,969,810)$ $(10,411,587)$ $(1,553,818)$ Provision (benefit) for income taxes $211,869$ $(28,193)$ $587,207$ $375,543$ Net loss $\$$ $(1,191,127)$ $\$$ $(1,941,617)$ $\$$ $(19,998,794)$ $\$$ $(1,929,361)$ Less: Accrual of Series A redeemable convertible preferred stock $195,904$ $196,727$ $777,890$ $765,203$ Less: Accretion to redemption value of Series A redeemable $668,177$ $156,670$ $1,181,446$ $587,613$ Net loss attributable to common stockholders $\$$ (0.05) $\$$ (0.06) $\$$ (0.30) $\$$ (0.08) Diluted net loss per share attributable to common stockholders $\$$ (0.05) $\$$ (0.06) $\$$ (0.08) Weighted average basic shares outstanding $43,818,413$ $41,356,757$ $43,091,878$ $41,093,644$	Investigation, litigation, and settlement related costs	—		—		_		8,842
Operating loss $(592,648)$ $(2,039,824)$ $(10,290,374)$ $(1,283,864)$ Interest and other (loss) income, net $(386,610)$ $70,014$ $(121,213)$ $(269,954)$ Loss before income taxes $(979,258)$ $(1,969,810)$ $(10,411,587)$ $(1,553,818)$ Provision (benefit) for income taxes $211,869$ $(28,193)$ $587,207$ $375,543$ Net loss $$(1,191,127)$ $$(1,941,617)$ $$(10,998,794)$ $$(1,929,361)$ Less: Accrual of Series A redeemable convertible preferred stock $195,904$ $196,727$ $777,890$ $765,203$ Less: Accretion to redemption value of Series A redeemable convertible preferred stock $668,177$ $156,670$ $1,181,446$ $587,613$ Net loss attributable to common stockholders $$(2,055,208)$ $$(2,295,014)$ $$(12,958,130)$ $$(3,282,177)$ Basic net loss per share attributable to common stockholders $$(0.05)$ $$(0.06)$ $$(0.30)$ $$(0.08)$ Diluted net loss per share attributable to common stockholders $$(0.05)$ $$(0.06)$ $$(0.30)$ $$(0.08)$ Weighted average basic shares outstanding $43,818,413$ $41,356,757$ $43,091,878$ $41,093,644$	Restructuring costs	 _		_		177,389		172,995
Interest and other (loss) income, net(386,610)70,014(121,213)(269,954)Loss before income taxes(979,258)(1,969,810)(10,411,587)(1,553,818)Provision (benefit) for income taxes211,869(28,193) $587,207$ $375,543$ Net loss\$ (1,191,127)\$ (1941,617)\$ (10,998,794)\$ (1,929,361)Less: Accrual of Series A redeemable convertible preferred stock195,904196,727 $777,890$ $765,203$ Less: Accretion to redemption value of Series A redeemable $668,177$ 156,670 $1,181,446$ $587,613$ Net loss attributable to common stockholders\$ (2,055,208)\$ (2,295,014)\$ (12,958,130)\$ (3,282,177)Basic net loss per share attributable to common stockholders\$ (0.05)\$ (0.06)\$ (0.30)\$ (0.08)Diluted net loss per share attributable to common stockholders\$ (0.05)\$ (0.06)\$ (0.30)\$ (0.08)Weighted average basic shares outstanding $43,818,413$ $41,356,757$ $43,091,878$ $41,093,644$	Total operating expenses	6,130,560		9,247,969	_	32,269,417		40,172,721
Loss before income taxes $(979,258)$ $(1,969,810)$ $(10,411,587)$ $(1,553,818)$ Provision (benefit) for income taxes $211,869$ $(28,193)$ $587,207$ $375,543$ Net loss\$ $(1,191,127)$ \$ $(1,941,617)$ \$ $(10,998,794)$ \$ $(1,929,361)$ Less: Accrual of Series A redeemable convertible preferred stock $195,904$ $196,727$ $777,890$ $765,203$ Less: Accretion to redemption value of Series A redeemable convertible preferred stock $668,177$ $156,670$ $1,181,446$ $587,613$ Net loss attributable to common stockholders\$ $(2,055,208)$ \$ $(2,295,014)$ \$ $(12,958,130)$ \$ $(3,282,177)$ Basic net loss per share attributable to common stockholders\$ (0.05) \$ (0.06) \$ (0.30) \$ (0.08) Diluted net loss per share attributable to common stockholders\$ (0.05) \$ (0.06) \$ (0.30) \$ (0.08) Weighted average basic shares outstanding $43,818,413$ $41,356,757$ $43,091,878$ $41,093,644$	Operating loss	(592,648)		(2,039,824)		(10,290,374)		(1,283,864)
Provision (benefit) for income taxes $211,869$ $(28,193)$ $587,207$ $375,543$ Net loss\$ (1,191,127)\$ (1,941,617)\$ (10,998,794)\$ (1,929,361)Less: Accrual of Series A redeemable convertible preferred stock $195,904$ $196,727$ $777,890$ $765,203$ Less: Accretion to redemption value of Series A redeemable convertible preferred stock $668,177$ $156,670$ $1,181,446$ $587,613$ Net loss attributable to common stockholders\$ (2,055,208)\$ (2,295,014)\$ (12,958,130)\$ (3,282,177)Basic net loss per share attributable to common stockholders\$ (0.05)\$ (0.06)\$ (0.30)\$ (0.08)Diluted net loss per share attributable to common stockholders\$ (0.05)\$ (0.06)\$ (0.30)\$ (0.08)Weighted average basic shares outstanding $43,818,413$ $41,356,757$ $43,091,878$ $41,093,644$	Interest and other (loss) income, net	(386,610)		70,014	_	(121,213)		(269,954)
Net loss \$ (1,191,127) \$ (1,941,617) \$ (10,998,794) \$ (1,929,361) Less: Accrual of Series A redeemable convertible preferred stock 195,904 196,727 777,890 765,203 Less: Accretion to redemption value of Series A redeemable convertible preferred stock 668,177 156,670 1,181,446 587,613 Net loss attributable to common stockholders \$ (2,055,208) \$ (2,295,014) \$ (12,958,130) \$ (3,282,177) Basic net loss per share attributable to common stockholders \$ (0.05) \$ (0.06) \$ (0.30) \$ (0.08) Diluted net loss per share attributable to common stockholders \$ (0.05) \$ (0.06) \$ (0.30) \$ (0.08) Weighted average basic shares outstanding 43,818,413 41,356,757 43,091,878 41,093,644	Loss before income taxes	(979,258)		(1,969,810)		(10,411,587)		(1,553,818)
Less: Accrual of Series A redeemable convertible preferred stock $195,904$ $196,727$ $777,890$ $765,203$ Less: Accretion to redemption value of Series A redeemable convertible preferred stock $668,177$ $156,670$ $1,181,446$ $587,613$ Net loss attributable to common stockholders\$ (2,055,208)\$ (2,295,014)\$ (12,958,130)\$ (3,282,177)Basic net loss per share attributable to common stockholders\$ (0.05)\$ (0.06)\$ (0.30)\$ (0.08)Diluted net loss per share attributable to common stockholders\$ (0.05)\$ (0.06)\$ (0.30)\$ (0.08)Weighted average basic shares outstanding $43,818,413$ $41,356,757$ $43,091,878$ $41,093,644$	Provision (benefit) for income taxes	211,869		(28,193)		587,207		375,543
dividends195,904196,727777,890765,203Less: Accretion to redemption value of Series A redeemable convertible preferred stock $668,177$ $156,670$ $1,181,446$ $587,613$ Net loss attributable to common stockholders\$ (2,055,208)\$ (2,295,014)\$ (12,958,130)\$ (3,282,177)Basic net loss per share attributable to common stockholders\$ (0.05)\$ (0.06)\$ (0.30)\$ (0.08)Diluted net loss per share attributable to common stockholders\$ (0.05)\$ (0.06)\$ (0.30)\$ (0.08)Weighted average basic shares outstanding $43,818,413$ $41,356,757$ $43,091,878$ $41,093,644$	Net loss	\$ (1,191,127)	\$	(1,941,617)	\$	(10,998,794)	\$	(1,929,361)
convertible preferred stock $668,177$ $156,670$ $1,181,446$ $587,613$ Net loss attributable to common stockholders\$ (2,055,208)\$ (2,295,014)\$ (12,958,130)\$ (3,282,177)Basic net loss per share attributable to common stockholders\$ (0.05)\$ (0.06)\$ (0.30)\$ (0.08)Diluted net loss per share attributable to common stockholders\$ (0.05)\$ (0.06)\$ (0.30)\$ (0.08)Weighted average basic shares outstanding $43,818,413$ $41,356,757$ $43,091,878$ $41,093,644$		 195,904		196,727		777,890		765,203
Basic net loss per share attributable to common stockholders\$ (0.05)\$ (0.06)\$ (0.30)\$ (0.08)Diluted net loss per share attributable to common stockholders\$ (0.05)\$ (0.06)\$ (0.30)\$ (0.08)Weighted average basic shares outstanding43,818,41341,356,75743,091,87841,093,644		668,177		156,670	_	1,181,446		587,613
Diluted net loss per share attributable to common stockholders\$ (0.05)\$ (0.06)\$ (0.30)\$ (0.08)Weighted average basic shares outstanding43,818,41341,356,75743,091,87841,093,644	Net loss attributable to common stockholders	\$ (2,055,208)	\$	(2,295,014)	\$	(12,958,130)	\$	(3,282,177)
Weighted average basic shares outstanding 43,818,413 41,356,757 43,091,878 41,093,644	Basic net loss per share attributable to common stockholders	\$ (0.05)	\$	(0.06)	\$	(0.30)	\$	(0.08)
	Diluted net loss per share attributable to common stockholders	\$ (0.05)	\$	(0.06)	\$	(0.30)	\$	(0.08)
Weighted average diluted shares outstanding 43,818,413 41,356,757 43,091,878 41,093,644	Weighted average basic shares outstanding	 43,818,413		41,356,757	_	43,091,878		41,093,644
	Weighted average diluted shares outstanding	43,818,413		41,356,757		43,091,878		41,093,644

FalconStor Software, Inc. and Subsidiaries Reconciliation of GAAP to Non-GAAP Financial Measures (Unaudited)

		Three Months Ended December 31,			welve Mo Decem	nths Ended ber 31,	
		2016	2015	2	016		2015
GAAP loss from operations	\$	(592,648)	\$ (2,039,824)	\$(10,2	90,374)	\$ (1,283,864)
Non-cash stock option expense (1)		(63,944)	756,430	2,3	28,218		1,929,377
Legal related costs (3)			_		_		8,842
Restructuring costs (4)			_	1	77,389		172,995
Non-GAAP (loss) income from operations	\$	(656,592)	\$ (1,283,394)	\$ (7,7	84,767)	\$	827,350
GAAP net loss attributable to common stockholders	\$ (2	2,055,208)	\$ (2,295,014)	\$(12,9	58,130)	\$ (3,282,177)
Non-cash stock option expense, net of income taxes (2)		(63,944)	756,430	2,3	28,218		1,929,377
Legal related costs (3)		—	_		—		8,842
Restructuring costs (4)			_	1	77,389		172,995
Effects of Series A redeemable convertible preferred stock (5)		864,081	353,397	1,9	59,336		1,352,816
Non-GAAP net (loss) income	\$ (1	,255,071)	\$ (1,185,187)	\$ (8,4	93,187)	\$	181,853
GAAP gross margin		74 %	77 %		73 %		80 %
Non-cash stock option expense (1)		0 %	0 %		0 %		0 %
Non-GAAP gross margin	_	74 %	77 %		73 %	_	80 %
GAAP gross margin - Product		92 %	91 %		91 %		92 %
Non-cash stock option expense (1)		0 %	0 %		0 %		0 %
Non-GAAP gross margin - Product	_	92 %	91 %	_	91 %	_	92 %
GAAP gross margin - Support and Service		65 %	69 %		64 %		67 %
Non-cash stock option expense (1)		0 %	0 %		0 %		0 %
Non-GAAP gross margin - Support and Service	_	65 %	69 %		64 %	_	68 %
GAAP operating margin		(8%)	(22%)		(34%)		(3%)
Non-cash stock option expense (1)		(1%)	8%		8%		4%
Legal related (benefits) costs (3)		0%	0%		0%		0%
Restructuring costs (4)		0%	0%		1%		0%
Non-GAAP operating margin	_	(9%)	(14%)		(26%)	_	2%
GAAP Basic EPS	\$	(0.05)	\$ (0.06)	\$	(0.30)	\$	(0.08)
Non-cash stock option expense, net of income taxes (2)		0.00	0.02		0.05		0.05
Legal related (benefits) costs (3)		0.00	0.00		0.00		0.00
Restructuring costs (4)		0.00	0.00		0.00		0.00
Effects of Series A redeemable convertible preferred stock (5)		0.02	0.01		0.05		0.03
Non-GAAP Basic EPS	\$	(0.03)	\$ (0.03)	\$	(0.20)	\$	0.00
						-	

GAAP Diluted EPS	\$	(0.05)	\$	(0.06)	\$	(0.30)	\$	(0.08)
Non-cash stock option expense, net of income taxes (2)		0.00		0.02		0.05		0.04
Legal related (benefits) costs (3)		0.00		0.00		0.00		0.00
Restructuring costs (4)		0.00		0.00		0.00		0.00
Effects of Series A redeemable convertible preferred stock (5)		0.02		0.01		0.05		0.03
Non-GAAP Diluted EPS	\$	(0.03)	\$	(0.03)	\$	(0.20)	\$	0.00
Weighted average basic shares outstanding (GAAP and as adjusted)	43,818,413		41,356,757		43,091,878		41,093,644	
Weighted average diluted shares outstanding (GAAP)	43,818,413		41,356,757		43,091,878		41,093,644	
Weighted average diluted shares outstanding (as adjusted)	43,818,413		41,356,757		43,091,878		42,906,072	

Footnotes:

(1) Represents non-cash, stock-based compensation charges as follows:

	Three Months Ended December 31,					Ended 31,		
		2016 2015		2016			2015	
Cost of revenues - Product	\$		\$		\$		\$	
Cost of revenues - Support and Service		(4,618)		18,419		80,903		98,776
Research and development costs		1,229		577,355		1,653,336		806,348
Selling and marketing		9,502		60,632		241,481		285,787
General and administrative		(70,057)		100,024		352,498		738,466
Total non-cash stock based compensation expense	\$	(63,944)	\$	756,430	\$	2,328,218	\$	1,929,377

- (2) Represents the effects of non-cash stock-based compensation expense recognized in accordance with the FASB Accounting Standards Codification, Topic 718, net of related income tax effects. For the three and twelve months ended December 31, 2016 and 2015, the tax expense for both GAAP and Non-GAAP basis approximate the same amount. Included in sharebased compensation expense for the twelve months ended December 31, 2016 and 2015 was \$1.5 million and \$0.5 million, respectively, related to costs associated with our exclusive source code license and development agreement which were paid through the issuance of our common stock.
- (3) Legal related costs represent expenses/gains in connection with the Company's investigations, litigation and settlement related costs for each respective period presented.
- (4) Represents restructuring costs which were incurred during each respective period presented.
- (5) Represents the effects of the accretion to redemption value of the Series A redeemable convertible preferred stock and accrual of Series A redeemable convertible preferred stock dividends.