

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2023

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission File Number 001-41092



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

Delaware
(State or other jurisdiction of incorporation or organization)
12015 Lee Jackson Memorial Highway, Suite 210
Fairfax, Virginia
(Address of principal executive offices)

54-1167364
(I.R.S. Employer Identification No.)

22033
(Zip Code)

Registrant's telephone number, including area code: (703) 383-3000

<u>Title of each class</u>	<u>Securities registered pursuant to Section 12(b) of the Act:</u> <u>Trading Symbol</u>	<u>Name of each exchange on which registered</u>
Common Stock, par value \$0.001 per share	WAVD	The NASDAQ Stock Market LLC

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 every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files).

Yes No

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

Non-accelerated filer
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

Number of shares outstanding by each class of common stock, as of November 7, 2023:

Common Stock, \$0.001 par value – 2,013,180 shares outstanding

This document is also available through our website at <http://ir.wavedancer.com/>.

**WAVEDANCER, INC.
FORM 10-Q****Table of Contents**

	Page Number
PART I.	FINANCIAL INFORMATION
Item 1.	Unaudited Condensed Consolidated Financial Statements
	Condensed Consolidated Balance Sheets as of September 30, 2023 and December 31, 2022 4
	Condensed Consolidated Statements of Operations for the three months ended September 30, 2023 and 2022 5
	Condensed Consolidated Statements of Operations for the nine months ended September 30, 2023 and 2022 6
	Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2023 and 2022 7
	Condensed Consolidated Statements of Changes in Stockholders' Equity for the three and nine months ended September 30, 2023 and 2022 8
	Notes to Condensed Consolidated Financial Statements 9
Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations 20
Item 4.	Controls and Procedures 26
PART II.	OTHER INFORMATION 27
Item 1.	Legal Proceedings 27
Item 1A.	Risk Factors 27
Item 2	Unregistered Sales of Equity Securities and Use of Proceeds 27
Item 3.	Defaults Upon Senior Securities 27
Item 4.	Mine Safety Disclosures 27
Item 5.	Other Information 27
Item 6.	Exhibits 28
	SIGNATURES 29

PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

WAVEDANCER, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

	September 30, 2023	December 31, 2022
ASSETS		
Current assets		
Cash and cash equivalents	\$ 877,198	\$ 731,081
Accounts receivable	1,479,780	1,629,559
Prepaid expenses and other current assets	363,668	442,445
Total current assets	<u>2,720,646</u>	<u>2,803,085</u>
Intangible assets, net of accumulated amortization of \$440,400 and \$308,217, respectively	1,049,600	1,181,783
Goodwill	1,125,101	1,125,101
Right-of-use operating lease asset	279,132	376,104
Property and equipment, net of accumulated depreciation and amortization of \$423,916 and \$391,628, respectively	66,703	98,991
Other assets	20,623	79,305
Assets held for sale	-	2,316,845
Total assets	<u>\$ 5,261,805</u>	<u>\$ 7,981,214</u>
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable	\$ 495,895	\$ 573,789
Revolving line of credit	500,000	425,000
Premium financing note payable	94,071	-
Accrued payroll and related liabilities	604,079	676,796
Commissions payable	24,296	125,033
Income taxes payable	3,101	3,101
Other accrued liabilities	217,108	283,497
Contract liabilities	26,026	182,756
Operating lease liabilities - current	218,695	203,342
Deferred acquisition consideration	-	1,415,098
Total current liabilities	<u>2,183,271</u>	<u>3,888,412</u>
Operating lease liabilities - non-current	134,790	303,778
Deferred tax liabilities, net	59,121	59,121
Total liabilities	<u>2,377,182</u>	<u>4,251,311</u>
Stockholders' equity		
Common stock, \$0.001 par value 100,000,000 shares authorized; 2,148,291 and 2,083,860 shares issued, 1,980,986 and 1,916,555 shares outstanding as of September 30, 2023 and December 31, 2022, respectively	2,148	2,084
Additional paid-in capital	36,303,586	35,883,831
Accumulated deficit	(32,455,900)	(31,190,801)
Treasury stock, 167,305 shares at cost, as of September 30, 2023 and December 31, 2022	(965,211)	(965,211)
Total stockholders' equity	<u>2,884,623</u>	<u>3,729,903</u>
Total liabilities and stockholders' equity	<u>\$ 5,261,805</u>	<u>\$ 7,981,214</u>

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

WAVEDANCER, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
 (Unaudited)

	Three Months Ended September 30,	
	2023	2022
Revenues		
Professional fees	\$ 1,921,300	\$ 2,114,012
Software sales	45,977	192,367
Total revenues	<u>1,967,277</u>	<u>2,306,379</u>
Cost of revenues		
Cost of professional fees	1,268,820	1,467,065
Cost of software sales	48,645	100,718
Total cost of revenues excluding depreciation and amortization	<u>1,317,465</u>	<u>1,567,783</u>
Gross profit	649,812	738,596
Selling, general and administrative expenses	<u>1,166,657</u>	<u>1,868,714</u>
Operating income (loss) from continuing operations	(516,845)	(1,130,118)
Gain on sale of equity investment and settlement of contingent consideration receivable	382,525	-
Other income (expense), net	3,113	3,188
Interest expense	<u>(18,725)</u>	<u>(20,437)</u>
Income (loss) from continuing operations before income taxes	(149,932)	(1,147,367)
Provision for income taxes	<u>-</u>	<u>23,000</u>
Net income (loss) from continuing operations	(149,932)	(1,170,367)
Loss from discontinued operations	-	(3,530,152)
Net income (loss)	<u>\$ (149,932)</u>	<u>\$ (4,700,519)</u>
Basic and diluted loss per share from continuing operations	\$ (0.08)	\$ (0.64)
Basic and diluted loss per share from discontinued operations	-	(1.92)
Basic and diluted net loss per share	<u>\$ (0.08)</u>	<u>\$ (2.56)</u>
Weighted average common shares outstanding		
Basic and diluted	<u>1,939,790</u>	<u>1,838,213</u>

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

WAVEDANCER, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Nine Months Ended September 30,	
	2023	2022
Revenues		
Professional fees	\$ 5,992,715	\$ 6,458,534
Software sales	159,307	2,593,877
Total revenues	<u>6,152,022</u>	<u>9,052,411</u>
Cost of revenues		
Cost of professional fees	3,979,059	4,283,365
Cost of software sales	161,340	2,430,139
Total cost of revenues excluding depreciation and amortization	<u>4,140,399</u>	<u>6,713,504</u>
Gross profit	2,011,623	2,338,907
Selling, general and administrative expenses	4,432,550	6,745,357
Gain on litigation settlement	(1,442,468)	-
Operating loss from continuing operations	(978,459)	(4,406,450)
Gain on sale of equity investment and settlement of contingent consideration receivable	382,525	-
Other income, net	3,335	3,977
Interest expense	(90,982)	(59,574)
Loss from continuing operations before income taxes and equity in net loss of affiliate	(683,581)	(4,462,047)
Provision for income taxes	-	789,573
Net loss from continuing operations before equity in net loss of affiliate	(683,581)	(5,251,620)
Equity in net loss of affiliate	(245,525)	-
Net loss from continuing operations	(929,106)	(5,251,620)
Income (loss) from discontinued operations	(335,993)	(3,052,648)
Net loss	<u>\$ (1,265,099)</u>	<u>\$ (8,304,268)</u>
Basic and diluted loss per share from continuing operations	\$ (0.48)	\$ (2.97)
Basic and diluted loss per share from discontinued operations	\$ (0.17)	\$ (1.73)
Basic and diluted net loss per share	<u>\$ (0.65)</u>	<u>\$ (4.70)</u>
Weighted average common shares outstanding		
Basic and diluted	<u>1,929,067</u>	<u>1,768,853</u>

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

WAVEDANCER, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Nine Months Ended September 30,	
	2023	2022
Cash flows from operating activities		
Net loss	\$ (1,265,099)	\$ (8,304,268)
Adjustments to reconcile net loss to net cash used in operating activities:		
Loss from discontinued operations	335,993	3,052,648
Depreciation and amortization	164,471	165,770
Stock-based compensation	557,147	1,187,552
Deferred income tax expense	-	775,257
Amortization of right-of-use assets	96,972	136,441
Accretion of deferred acquisition consideration	27,370	59,467
Gain on litigation settlement	(1,442,468)	-
Gain on sale of equity investment and settlement of contingent consideration receivable	(382,525)	-
Equity in loss of affiliate	245,525	-
Changes in operating assets and liabilities:		
Accounts receivable	149,779	132,688
Prepaid expenses and other current assets	61,925	84,842
Other assets	58,682	-
Accounts payable	(77,894)	(422,939)
Contract liabilities	(156,730)	(149,149)
Accrued payroll and related liabilities and other accrued liabilities	(139,106)	653,786
Operating lease liability	(153,635)	(142,420)
Commissions payable	(100,737)	846
Cash used in operating activities of continuing operations	(2,020,330)	(2,769,479)
Cash used in operating activities of discontinued operations	(693,106)	(2,330,754)
Net cash used in operating activities	(2,713,436)	(5,100,233)
Cash flows from investing activities		
Acquisition of property and equipment	-	(234,060)
Proceeds from sale of equity investment and settlement of contingent consideration receivable	1,400,000	-
Proceeds from disposal of business	935,974	-
Net cash provided by (used in) investing activities	2,335,974	(234,060)
Cash flows from financing activities		
Borrowings under revolving line of credit	575,000	-
Repayments under revolving line of credit	(500,000)	-
Premium financing borrowings	305,759	-
Premium financing repayments	(211,688)	-
Proceeds from issuance of stock	347,108	1,887,000
Proceeds from exercise of stock options	7,400	37,642
Net cash provided by financing activities	523,579	1,924,642
Net increase (decrease) in cash and cash equivalents	146,117	(3,409,651)
Cash and cash equivalents, beginning of period	731,081	4,931,302
Cash and cash equivalents, end of period	\$ 877,198	\$ 1,521,651
Supplemental cash flow information		
Interest paid	\$ 18,356	\$ 1,002
Non-cash investing and financing activities:		
Non-cash proceeds on disposal of business	\$ 1,263,000	\$ -
Value of common stock issued in connection with common stock purchase agreement	\$ -	\$ 112,500

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

WAVEDANCER, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
(Unaudited)

	Shares of Common Stock Issued	Common Stock	Additional Paid-In Capital	Accumulated Deficit	Treasury Stock	Total
Balances at December 31, 2022	2,083,860	\$ 2,084	\$ 35,883,831	\$ (31,190,801)	\$ (965,211)	\$ 3,729,903
Net loss	-	-	-	(1,349,952)	-	(1,349,952)
Stock option compensation	-	-	353,658	-	-	353,658
Forfeiture of stock options on disposal of business (Note 2)	-	-	(407,322)	-	-	(407,322)
Stock issued	7,431	7	56,259	-	-	56,266
Amortization of stock issue costs	-	-	(18,635)	-	-	(18,635)
Issuance of stock from exercise of options	2,000	2	7,398	-	-	7,400
Balances at March 31, 2023	2,093,291	2,093	35,875,189	(32,540,753)	(965,211)	2,371,318
Net income	-	-	-	234,785	-	234,785
Stock option compensation	-	-	88,159	-	-	88,159
Amortization of stock issue costs	-	-	(76,673)	-	-	(76,673)
Balances at June 30, 2023	2,093,291	2,093	35,886,675	(32,305,968)	(965,211)	2,617,589
Net loss	-	-	-	(149,932)	-	(149,932)
Stock option compensation	-	-	180,816	-	-	180,816
Stock issued	55,000	55	290,787	-	-	290,842
Amortization of stock issue costs	-	-	(54,692)	-	-	(54,692)
Balances at September 30, 2023	2,148,291	\$ 2,148	\$ 36,303,586	\$ (32,455,900)	\$ (965,211)	\$ 2,884,623

	Shares of Common Stock Issued	Common Stock	Additional Paid-In Capital	Accumulated Deficit	Treasury Stock	Total
Balances at December 31, 2021	1,888,231	\$ 1,888	\$ 31,806,458	\$ (13,436,963)	\$ (930,211)	\$ 17,441,172
Net loss	-	-	-	(2,078,307)	-	(2,078,307)
Stock option compensation	-	-	312,176	-	-	312,176
Issuance of stock from exercise of options	10,500	11	26,788	-	-	26,799
Balances at March 31, 2022	1,898,731	1,899	32,145,422	(15,515,270)	(930,211)	15,701,840
Net loss	-	-	-	(1,525,442)	-	(1,525,442)
Stock option compensation	-	-	529,565	-	-	529,565
Issuance of stock from exercise of options	5,200	5	8,387	-	-	8,392
Balances at June 30, 2022	1,903,931	1,904	32,683,374	(17,040,712)	(930,211)	14,714,355
Net loss	-	-	-	(4,700,519)	-	(4,700,519)
Stock option compensation	-	-	614,094	-	-	614,094
Stock issued	166,300	166	1,999,334	-	-	1,999,500
Issuance of stock from exercise of options	10,700	11	37,440	-	(35,000)	2,451
Balances at September 30, 2022	2,080,931	\$ 2,081	\$ 35,334,242	\$ (21,741,231)	\$ (965,211)	\$ 12,629,881

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

WAVEDANCER, INC.
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Summary of Significant Accounting Policies

Organization and Business

Founded in 1979 as Information Analysis Incorporated (“IAI”), IAI changed its name to WaveDancer, Inc. (“WaveDancer” or the “Company”) and converted from a Virginia corporation to a Delaware corporation in December 2021. The Company is in the business of developing and maintaining information technology (“IT”) systems, modernizing client information systems, and performing other IT-related professional services to government and commercial organizations.

On March 17, 2023, the Company sold effectively 75.1% of the equity of its Gray Matters, Inc. subsidiary (“GMI”) to Gray Matters Data Corporation (“GMDC”). Subsequent to the sale, the Company discontinued consolidating GMI and the Company has reflected GMI as a discontinued operation in its consolidated statements of operations for all periods presented. Unless otherwise noted, all amounts and disclosures throughout these Notes to Condensed Consolidated Financial Statements relate to the Company’s continuing operations. See Note 2 for further information about the sale transaction, the deconsolidation of GMI, and treatment of GMI as a discontinued operation.

Prior to March 17, 2023, we had two operating segments: Tellenger and Blockchain SCM. Given the classification of GMI, which comprised all of the material operations of the Blockchain SCM segment, as a discontinued operation (see Note 2). After March 17, 2023, the Company manages its business as one reportable operating segment.

Liquidity and Going Concern

During the nine months ended September 30, 2023, the Company generated an operating loss from continuing operations of \$978,459. As of September 30, 2023, the Company had working capital of \$537,375 including cash and cash equivalents of \$877,198. We estimate that over the twelve months from the date of these financial statements our operating activities may use as much as \$1.0 million to \$1.5 million of cash. On August 2, 2023, the Company realized \$118,655 of cash proceeds from the sale of 20,000 shares of common stock, and on August 9, 2023, the Company received \$1,400,000 of cash from the sale of its remaining equity interest in GMDC and its contingent consideration receivable from GMDC. On August 9, 2023, the Company repaid \$500,000 on the Summit line of credit and has no further borrowing capacity thereunder. On September 29, 2023, the Company issued 35,000 shares of its common stock to its chairman and CEO for \$175,000 of cash. The transaction was approved by the board of directors and was at a premium to the trading price on the date of the transaction. We estimate that within twelve months from the issuance of these financial statements, the Company will need to raise additional capital to meet its ongoing operating cash flow requirements as well as to grow its business either organically or through acquisitions. The Company is evaluating strategic alternatives which include the potential merger or sale of the Company. There is no assurance that such activities will result in any transactions or provide additional capital. Accordingly, there is substantial doubt about the Company’s ability to continue as a going concern for at least one year from the date that the accompanying unaudited condensed consolidated financial statements are issued.

The accompanying unaudited condensed consolidated financial statements have been prepared assuming that the Company will continue as a going concern, which contemplates continuity of operations, realization of assets, and satisfaction of liabilities in the ordinary course of business. The propriety of using the going-concern basis is dependent upon, among other things, the achievement of future profitable operations, the ability to generate sufficient cash from operations and potential other funding sources, in addition to cash on-hand, to meet its obligations as they become due. The Company’s unaudited condensed consolidated financial statements do not include any adjustment that might result from the outcome of this uncertainty.

Reverse Stock Split

On October 18, 2023, the Company effected a reverse stock split of its common stock, par value \$0.001 per share, (the “Common Stock”) at a ratio of one-for-ten (the “Reverse Stock Split”). The Reverse Stock split affected all issued common stock and options and warrants to acquire common stock. No fractional shares were issued as a result of the reverse split and any fractional share otherwise issuable were rounded up to the nearest whole number. All shares and per share amounts in the condensed consolidated financial statements and accompanying notes have been retroactively adjusted to give effect to the Reverse Stock Split. Following the Reverse Stock Split, the Company’s issued and outstanding shares of Common Stock decreased from 19,809,834 pre-split shares to approximately 1,980,983 post-split shares, before finalizing the rounding of fractional shares. As a result of the Reverse Stock Split, the exercise prices of the outstanding options and warrants were increased by a factor of ten.

Unaudited Interim Condensed Consolidated Financial Statements

The accompanying unaudited condensed consolidated financial statements (“financial statements”) have been prepared in conformity with U.S. generally accepted accounting principles (“GAAP”) for interim financial information and with the instructions for Form 10-Q and Article 8-03 of Regulation S-X. Accordingly, certain information and footnote disclosures normally included in annual financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”) for interim financial statements. In the opinion of management, the financial statements include all adjustments necessary (which are of a normal and recurring nature) for the fair and not misleading presentation of the results of the interim periods presented. These unaudited interim condensed consolidated financial statements should be read in conjunction with the Company’s audited financial statements for the year ended December 31, 2022 included in the Annual Report on Form 10-K filed by the Company with the SEC on April 17, 2023 (the “Annual Report”), as amended. The accompanying December 31, 2022 condensed consolidated balance sheet was derived from the audited financial statements included in the Annual Report but does not include all disclosures required by accounting principles generally accepted in the United States of America. The results of operations for any interim periods are not necessarily indicative of the results of operations for any other interim period or for a full fiscal year.

The unaudited condensed consolidated financial statements as of and for the three and nine months ended September 30, 2023 include the accounts of WaveDancer and its condensed consolidated subsidiaries (collectively, the "Company", "we" or "our"). All significant intercompany transactions and balances have been eliminated in consolidation.

Other than as discussed in "Equity Method Investments" below, there have been no changes in the Company's significant accounting policies as of September 30, 2023, as compared to the significant accounting policies disclosed in Note 1, "Summary of Significant Accounting Policies" in the Company's Annual Report.

Equity Method Investments

The Company accounts for investments in which it owns between 20% to 50% of the common stock or has the ability to exercise significant influence, but not control, over the investee using the equity method of accounting in accordance with ASC 323 - *Equity Method Investments and Joint Ventures* ("ASC 323"). Under the equity method, an investor initially records an investment in the stock of an investee at cost and adjusts the carrying amount of the investment to recognize the investor's share of the earnings or losses of the investee after the date of acquisition. The Company reflects its share of gains and losses from the investment in equity in net loss of affiliate in the unaudited condensed consolidated statements of operations using the most recently available earnings data at the end of the period.

In connection with the sale of GMI to GMDC on March 17, 2023, (the "Sale Date"), the Company received common stock in GMDC representing approximately 24.9% of the equity of GMDC. See Note 2 for further information about the sale transaction, the deconsolidation of GMI, and the treatment of GMI as a discontinued operation. The Company accounted for its investment in GMDC in accordance with the equity method from March 17, 2023 through August 9, 2023. On August 9, 2023, the Company sold its remaining equity interest in GMDC in exchange for \$400,000 in cash, and recognized a gain on sale of \$64,525. As of September 30, 2023 the Company has no equity investment in GMDC and any other equity exposure to the GMI business.

Use of Estimates

Preparation of condensed consolidated financial statements in conformity with GAAP requires us to make estimates and assumptions that affect the amounts reported and disclosed in the financial statements and the accompanying notes. Actual results could differ materially from these estimates due to uncertainties. On an ongoing basis, we evaluate our estimates, including those related to the allowance for credit losses; fair values of financial instruments, intangible assets, and goodwill, including the underlying estimates of cash flows of our products and reporting unit; useful lives of intangible assets and property and equipment; the valuation of stock-based compensation, and the valuation of deferred tax assets and liabilities, among others. We base our estimates on assumptions, both historical and forward looking, that are believed to be reasonable, and the results of which form the basis for making judgments about the carrying values of assets and liabilities.

Concentration of Credit Risk

During the three months ended September 30, 2023, the Company's prime contracts with U.S. government agencies represented 8.3% of revenue and subcontracts under federal procurements represented 90.6% of revenue. The terms of these contracts and subcontracts vary from single transactions to five years. Three subcontracts under federal procurements represented 29.3%, 19.9%, and 18.6% of revenue, respectively. Revenue from one prime contractor under which the Company has multiple subcontracts represented 56.6% of the Company's revenue in aggregate.

During the three months ended September 30, 2022, the Company's prime contracts with U.S. government agencies represented 11.4% of revenue and subcontracts under federal procurements represented 82.8% of revenue. The terms of these contracts and subcontracts vary from single transactions to five years. Three subcontracts under federal procurements represented 30.9%, 21.3%, and 13.0% of revenue, respectively. Revenue from one prime contractor under which the Company has multiple subcontracts represented 49.9% of the Company's revenue in aggregate.

During the nine months ended September 30, 2023, the Company's prime contracts with U.S. government agencies represented 9.1% of revenue and subcontracts under federal procurements represented 89.3% of revenue. The terms of these subcontracts vary from one to five years. Three subcontracts under federal procurements represented 30.3%, 21.1%, and 16.6% of revenue, respectively. Revenue from one prime contractor under which the Company has multiple subcontracts represented 54.5% of the Company's revenue in aggregate.

During the nine months ended September 30, 2022, the Company's prime contracts with U.S. government agencies represented 28.6% of revenue and subcontracts under federal procurements represented 67.8% of revenue. The terms of these contracts and subcontracts vary from single transactions to five years. Three subcontracts under federal procurements represented 27.4%, 16.5%, and 10.5% of revenue, respectively. Revenue from one prime contractor under which the Company has multiple subcontracts represented 41.4% of the Company's revenue in aggregate.

The Company sold third-party software and maintenance contracts under agreements with one major supplier, accounting for 9.7% and 11.8% of total revenue during the three- and nine-months ended September 30, 2022, respectively.

As of September 30, 2023, the Company's accounts receivable included receivables from two subcontracts under federal procurements that represented 42.2% and 17.2% of the Company's outstanding accounts receivable, respectively. Receivables from one prime contractor under which the Company has multiple subcontracts represented 69.8% of the Company's outstanding accounts receivable in aggregate.

As of September 30, 2022, the Company's accounts receivable included receivables from two subcontracts under federal procurements that represented 46.5% and 13.6% of the Company's outstanding accounts receivable, respectively. Receivables from one prime contractor under which the Company has multiple subcontracts represented 66.8% of the Company's outstanding accounts receivable in aggregate.

Note 2. Sale and Deconsolidation of GMI and Discontinued Operations

On March 17, 2023, the Company entered in and closed a Stock Purchase Agreement with GMDC, a company newly formed by StealthPoint LLC, a San Francisco based venture fund, under which the Company sold all of the shares of its subsidiary, Gray Matters, Inc. In exchange for this sale, the Company received common shares of GMDC representing on a primary share basis, assuming the conversion of the Series A preferred stock referenced below, 24.9% interest in the purchaser, cash consideration of \$935,974 and contingent annual payments equal to five percent (5%) of the purchaser's GAAP based revenue through December 31, 2029 attributable to the purchaser's blockchain-enabled digital supply chain management platform and associated technologies. Payments will be calculated for each calendar year and are due by March 31 of the following year. GMDC also paid the Company \$133,148 for certain of GMI's operating expenses for the period beginning March 1, 2023 through March 17, 2023.

The equity interest StealthPoint and other GMDC investors received is in the form of Series A non-participating convertible preferred stock having a one-times (1x) liquidation preference and no cumulative dividends. In addition, the Company and GMDC entered into a transition services agreement whereby the Company continues to provide certain administrative services for GMI. The value of these services is estimated to be \$65,000 which was paid by GMDC at closing and is not subject to adjustment. The \$65,000 prepayment is included in other accrued liabilities on the unaudited condensed consolidated balance sheet as of March 31, 2023 and has been amortized as a reduction to selling, general and administrative expenses ratably over the three-month period ending June 30, 2023 after which time no further transition services were provided. The total cash received at closing was \$1,000,974. The Company also has the right to appoint a representative to GMDC's board of directors and a right to co-invest in the anticipated Series B preferred stock financing round which GMDC intends to consummate in the future. The Company recognized a gain on the sale of GMI of \$100,615 in the first quarter of 2023, which was included in net loss on discontinued operations in the unaudited condensed consolidated statement of operations, and immediately deconsolidated GMI upon its sale. GMDC was not a related party of the Company at the time of its purchase of GMI. Subsequent to our deconsolidation of GMI, GMI and GMDC are related parties of the Company due to our equity interest in GMDC.

The components of the consideration received and the methods for determining their fair values as of March 17, 2023 were as follows:

Consideration	Amount	Description and Valuation Methodology
Cash at closing	\$ 935,974	Cash received at closing less estimated value of transition services to be provided.
Cash after closing	133,148	Actual cash operating expenses of GMI from March 1 through March 17, 2023 (prior to the transfer of GMI to GMDC).
GMDC common stock	581,000	Based on Series A preferred stock issuance to other GMDC investors for \$3,000,000 in cash and application of an option pricing model backsolve method and a minority interest discount to estimate the fair value of the common shares of GMDC.
Contingent payments	682,000	Estimated by applying a discount rate of 40.8% to the projected cash receipts expected over the 7-year horizon. (See Note 5).
Total consideration	<u>\$ 2,332,122</u>	

The GMDC common stock was accounted for as an equity method investment from March 17, 2023 and through its sale on August 9, 2023. During this period, a net loss of \$245,525 in the equity investment was recorded. On August 9, 2023, the Company sold its remaining equity interest in GMDC in exchange for \$400,000 in cash, and recognized a gain on sale of \$64,525. The contingent consideration receivable of \$682,000 was settled in cash for \$1,000,000 and a gain of \$318,000 was recognized during the three months ended September 30, 2023 (see Note 5).

The following table sets forth details of net earnings from discontinued operations for the nine months ended September 30, 2023 and 2022, which reflects the results of the Blockchain SCM operating segment through the date our controlling financial interest in it was sold – March 17, 2023 (See Note 1).

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2023	2022	2023	2022
Revenue	\$ -	\$ -	\$ -	\$ 566,862
Cost of revenue	-	256,974	74,223	1,118,301
Excess of contract costs over revenue	-	(256,974)	(74,223)	(551,439)
Operating expenses -				
Salaries and benefits	-	463,502	484,249	1,076,781
Intangibles amortization	-	303,791	85,338	917,496
Stock based compensation, before forfeitures	-	215,775	65,487	268,283
Forfeiture of stock options	-	-	(407,322)	-
Other operating expenses	-	113,078	134,633	702,534
Change in fair value of contingent consideration	-	-	-	(930,000)
Goodwill impairment	-	2,254,624	-	2,254,624
Gain on disposal of business	-	-	(100,615)	-
Loss before income tax benefit	-	(3,607,744)	(335,993)	(4,841,157)
Income tax benefit	-	77,592	-	1,788,509
Net loss on discontinued operations	\$ -	\$ (3,530,152)	\$ (335,993)	\$ (3,052,648)

During the nine months ended September 30, 2023, there was a total of 715,000 unvested stock options forfeited by GMI employees, including 527,500 forfeited by employees who resigned from WaveDancer, on the Sale Date, and were offered employment by GMDC. Stock-based compensation expense of \$407,322, previously recognized for these forfeited options, was taken back into income in March 2023.

The following table presents the components of the assets of our discontinued operations that were classified as held for sale as of December 31, 2022. As of March 31, 2023, GMI had been sold and its accounts deconsolidated from the condensed consolidated balance sheet.

	December 31, 2022
Customer relationship intangible asset, net of amortization	\$ 1,057,722
Technology intangible asset, net of amortization	760,698
Capitalized software development costs	498,425
Total assets of discontinued operations	\$ 2,316,845

Note 3. Revenue from Contracts with Customers

Nature of Products and Services

We generate revenue from the sales of information technology professional services, sales of third-party software licenses and implementation and training services, sales of third-party support and maintenance contracts based on those software products, and incentive payments received from third-party software suppliers for facilitating sales directly between that supplier and a customer introduced by the Company. We sell through our direct relationships with end customers and under subcontractor arrangements.

Professional services are offered through several arrangements – through time and materials arrangements, fixed-price-per-unit arrangements, fixed-price arrangements, or combinations of these arrangements within individual contracts. Revenue under time and materials arrangements is recognized over time in the period the hours are worked or the expenses are incurred, as control of the benefits of the work is deemed to have passed to the customer as the work is performed. Revenue under fixed-price-per-unit arrangements is recognized at a point in time when delivery of units has occurred, and units are accepted by the customer or are reasonably expected to be accepted. Generally, revenue under fixed-price arrangements and mixed arrangements is recognized either over time or at a point in time based on the allocation of transaction pricing to each identified performance obligation as control of each is transferred to the customer. For fixed-price arrangements under which documentary evidence of acceptance or receipt of deliverables is not present or withheld by the customer, the Company recognizes revenue when it has the right to invoice the customer. For fixed-price arrangements for which the Company is paid a fixed fee to make itself available to support a customer, with no predetermined deliverables to which transaction prices can be estimated or allocated, revenue is recognized ratably over time.

Third-party software licenses are classified as enterprise server-based software licenses or desktop software licenses, and desktop licenses are further classified by the type of customer and whether the licenses are bulk licenses or individual licenses. The Company’s obligations as the seller for each class differ based on its reseller agreements and whether its customers are government or non-government customers. Revenue from enterprise server-based sales to either government or non-government customers is usually recognized in full at a point in time based on when the customer gains use of the full benefit of the licenses, after the licenses are implemented. If the transaction prices of the performance obligations related to implementation and customer support for the individual contract is material, these obligations are recognized separately over time, as performed. Revenue for desktop software licenses for government customers is usually recognized on a gross basis at a point in time, based on when the customer’s administrative contact gains training in and beneficial use of the administrative portal. Revenue for bulk desktop software licenses for non-government customers is usually recognized on a gross basis at a point in time, based on when the customer’s administrative contact gains training in and beneficial use of the administrative portal. For desktop software licenses sold on an individual license basis to non-government customers, where the Company has no obligation to the customer after the third-party makes delivery of the licenses, the Company has determined it is acting as an agent, and the Company recognizes revenue upon delivery of the licenses only for the net of the selling price and its contract costs.

Third-party support and maintenance contracts for enterprise server-based software include a performance obligation under the Company’s reseller agreements for it to be the first line of support (direct support) and second line of support (intermediary between customer and manufacturer) to the customer. Because of the support performance obligations, and because the amount of support is not estimable, the Company recognizes revenue ratably over time as it makes itself available to provide the support.

Incentive payments are received under reseller agreements with software manufacturers and suppliers where the Company introduces and courts a customer, but the sale occurs directly between the customer and the supplier or between the customer and the manufacturer. Since the transfer of control of the licenses cannot be measured from outside of these transactions, revenue is recognized when payment from the manufacturer or supplier is received.

Disaggregation of Revenue from Contracts with Customers

Contract Type	Three Months Ended September 30,			
	2023		2022	
	Amount	Percentage	Amount	Percentage
Services time & materials	\$ 1,714,509	87.2%	\$ 1,896,829	82.2%
Services fixed price over time	102,402	5.2%	58,965	2.6%
Services combination	33,090	1.7%	50,440	2.2%
Services fixed price per unit	71,299	3.6%	107,778	4.7%
Third-party software	45,977	2.3%	59,076	2.6%
Software support & maintenance	-	0.0%	44,804	1.9%
Incentive payments	-	0.0%	88,487	3.8%
Total revenue	<u>\$ 1,967,277</u>	<u>100.0%</u>	<u>\$ 2,306,379</u>	<u>100.0%</u>

Contract Type	Nine Months Ended September 30,			
	2023		2022	
	Amount	Percentage	Amount	Percentage
Services time & materials	\$ 5,314,845	86.4%	\$ 5,963,361	65.9%
Services fixed price over time	307,206	5.0%	161,273	1.8%
Services combination	99,270	1.6%	80,520	0.9%
Services fixed price per unit	271,394	4.4%	253,379	2.8%
Third-party software	159,307	2.6%	2,345,884	25.9%
Software support & maintenance	-	0.0%	142,891	1.6%
Incentive payments	-	0.0%	105,103	1.1%
Total revenue	\$ 6,152,022	100.0%	\$ 9,052,411	100.0%

Contract Balances*Accounts Receivable*

Trade accounts receivable are recorded at the billable amount where the Company has the unconditional right to bill, net of allowances for doubtful accounts. The allowance for doubtful accounts is based on the Company's assessment of the collectability of accounts. Management regularly reviews the adequacy of the allowance for doubtful accounts by considering the age of each outstanding invoice, each customer's expected ability to pay and collection history, when applicable, to determine whether a specific allowance is appropriate. Accounts receivable deemed uncollectible are charged against the allowance for doubtful accounts when identified. There were no such allowances recognized as of September 30, 2023 and December 31, 2022.

Accounts receivable as of September 30, 2023 and December 31, 2022, consist of the following:

	September 30, 2023	December 31, 2022
Billed federal government	\$ 1,456,519	\$ 1,573,407
Billed commercial and local government	22,000	56,152
Unbilled receivables	1,261	-
Accounts receivable	\$ 1,479,780	\$ 1,629,559

Billed receivables from the federal government include amounts due from both prime contracts and subcontracts where the federal government is the end customer.

Contract Liabilities

Contract liabilities consist of amounts that have been invoiced and for which the Company has the right to bill, but that have not been recognized as revenue because the related goods or services have not been transferred. Changes in contracts liabilities balances are as follows:

Balance at December 31, 2022	\$ 182,756
Contract liabilities added	-
Revenue recognized	(55,665)
Balance at March 31, 2023	127,091
Contract liabilities added	-
Revenue recognized	(55,088)
Balance at June 30, 2023	72,003
Contract liabilities added	-
Revenue recognized	(45,977)
Balance at September 30, 2023	\$ 26,026
Balance at December 31, 2021	\$ 186,835
Contract liabilities added	19,280
Revenue recognized	(56,423)
Balance at March 31, 2022	149,692
Contract liabilities added	87,612
Revenue recognized	(71,461)
Balance as of June 30, 2022	165,843
Contract liabilities added	2,491
Revenue recognized	(130,648)
Balance at September 30, 2022	\$ 37,686

Revenues recognized during the three months ended September 30, 2023 and 2022, from the balances as of December 31, 2022 and 2021, were \$45,977 and \$48,708, respectively. Revenues recognized during the nine months ended September 30, 2023 and 2022, from the balances as of December 31, 2022 and 2021, were \$156,730 and \$160,809, respectively.

Deferred Costs of Revenue

Deferred costs of revenue consist of the costs of third-party support and maintenance contracts for enterprise server-based software. These costs are reported under the prepaid expenses and other current assets caption on the Company's condensed consolidated balance sheets. The Company recognizes these direct costs ratably over time as it makes itself available to provide its performance obligation for software support, commensurate with its recognition of revenue. As of September 30, 2023, and December 31, 2022 the Company had \$0 of deferred costs of revenue. Changes in deferred costs of revenue balances for the nine months ended September 30, 2022, are as follows:

Balance at December 31, 2021	\$ 154,218
Deferred costs added	2,800
Deferred costs expensed	(55,362)
Balance at March 31, 2022	101,656
Deferred costs expensed	(53,434)
Balance as of June 30, 2022	48,222
Deferred costs expensed	(48,222)
Balance as of September 30, 2022	\$ -

Note 4. Leases

The Company has two significant operating leases, one for its headquarters offices in Fairfax, Virginia and one for additional office space in Annapolis, Maryland. The leases both commenced in 2021 and have original lease terms ranging from 37 to 67 months and rental rates escalate by approximately 2.5% annually under both leases. The Company determines if an arrangement is a lease at inception.

As of September 30, 2023 and December 31, 2022, the Company does not have any sales-type or direct financing leases.

Each of the Company's operating lease assets represent its right to use an underlying asset for the lease term and the related lease liability represent its obligation to make lease payments arising from the lease. Operating lease assets and liabilities are recognized at the commencement date based on the present value of lease payments over the lease term. Since the leases do not provide an implicit rate, the Company uses its incremental borrowing rate based on the information available at the lease commencement dates in determining the present value of lease payments. The operating lease assets also include any lease payments made and exclude lease incentives. Lease expense for lease payments is recognized on a straight-line basis over the lease term. The Company's lease agreements include rental payments escalating annually for inflation at a fixed rate. These payments are included in the initial measurement of the operating lease liabilities and operating lease assets. The Company does not have any rental payments which are based on a change in an index or a rate that can be considered variable lease payments, which would be expensed as incurred.

The Company's lease agreements do not contain any material residual value guarantees or material restrictions or covenants.

The Company does not sublease any real estate to third parties.

As of September 30, 2023, our two operating leases had a weighted average remaining lease term of 28 months and a weighted average discount rate of 5.1%. Future lease payments under operating leases as of September 30, 2023, were as follows:

2023	58,041
2024	174,721
2025	74,804
2026	70,220
Total lease payments	377,786
Less: discount	(24,301)
Present value of lease liabilities	\$ 353,485

The total expense incurred related to its operating leases was \$38,053 and \$53,560 for the three months ended September 30, 2023 and 2022, respectively, and \$118,567 and \$164,281 for the nine months ended September 30, 2023 and 2022, respectively, and is included in selling, general and administrative expenses on the condensed consolidated statements of operations.

Note 5. Fair Value Measurements

The Company 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. Valuation techniques used to measure fair value must maximize the use of observable inputs and minimize the use of unobservable inputs. The standard describes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value which are the following:

- Level 1—Quoted prices in active markets for identical assets or liabilities;
- Level 2—Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; and
- Level 3—Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

The following table presents the fair value hierarchy for the Company's financial instruments measured at fair value on a recurring basis as of September 30, 2023 and December 31, 2022:

	September 30, 2023			
	Level 1	Level 2	Level 3	Total
Cash equivalents:				
Money market funds	\$ 809,997	\$ -	\$ -	\$ 809,997
	December 31, 2022			
	Level 1	Level 2	Level 3	Total
Cash equivalents:				
Money market funds	\$ 58,242	\$ -	\$ -	\$ 58,242

As discussed in Note 2 above, in connection with its sale of GMI, the Company received contingent consideration that requires to GMDC to make annual payments equal to five percent (5%) of the purchaser's GAAP based revenue through December 31, 2029, up to a cumulative maximum of \$4,000,000, attributable to the purchaser's blockchain-enabled digital supply chain management platform and associated technologies. The fair value of the contingent consideration was estimated based on GMDC's forecast of revenue, the estimated after-tax payments to the Company, and the present value of the after-tax payments based on discount rate that reflects the risk of achieving the timing and amounts of forecasted payments. The significant inputs utilized in estimating the fair value of contingent consideration include the forecast of revenues, the income tax rate of 27.0 percent, and the discount rate of 40.75 percent. On August 9, 2023, the Company and GMDC agreed to terminate all rights and obligations with respect to the calculation and payment of future contingent payments from GMDC to the Company in exchange for the payment of \$1,000,000 cash by GMDC to the Company, resulting in a gain of \$318,000.

The following table is a roll-forward of the Level 3 fair value measurements, which are not considered financial instruments.

Fair value of contingent consideration:	
December 31, 2022	\$ -
Additions	682,000
March 31, 2023	682,000
Additions	-
June 30, 2023	682,000
Settlements	(682,000)
September 30, 2023	\$ -

There were no unrealized gains or losses recognized in income for the three- or nine-month periods ended September 30, 2023.

Note 6. Intangible Assets and Goodwill

Information regarding our intangible assets is as follows:

	Weighted Average Useful Life (Years)	Balance December 31, 2022	Additions	Balance September 30, 2023
Intangible assets with estimated useful lives				
Customer relationships	8.0	\$ 1,090,000	\$ -	\$ 1,090,000
Non-compete agreements	3.0	120,000	-	120,000
Accumulated amortization		(308,217)	(132,183)	(440,400)
Sub-total		901,783	(132,183)	769,600
Intangible assets with indefinite lives				
Trade names	Indefinite	280,000	-	280,000
Net identifiable intangible assets		\$ 1,181,783	\$ (132,183)	\$ 1,049,600
<hr/>				
	Weighted Average Useful Life (Years)	Balance December 31, 2021	Additions	Balance September 30, 2022
Intangible assets with estimated useful lives				
Customer relationships	8.0	\$ 1,090,000	\$ -	\$ 1,090,000
Non-compete agreements	3.0	120,000	-	120,000
Accumulated amortization		(131,973)	(132,183)	(264,156)
Sub-total		1,078,027	(132,183)	945,844
Intangible assets with indefinite lives				
Trade names	Indefinite	280,000	-	280,000
Net identifiable intangible assets		\$ 1,358,027	\$ (132,183)	\$ 1,225,844

As of September 30, 2023, expected amortization expense relating to purchased intangible assets for each of the next five years and thereafter is as follows:

2023	\$ 44,061
2024	146,307
2025	136,248
2026	136,248
2027	136,248
Thereafter	170,488
Total	\$ 769,600

Note 7. Stock-Based Compensation

We have three stock-based compensation plans. The 2006 Stock Incentive Plan was adopted in 2006 ("2006 Plan") and had options granted under it through April 12, 2016. The 2016 Stock Incentive Plan was adopted in 2016 ("2016 Plan") and had options granted under it through November 15, 2021. On October 11, 2021, the Board of Directors approved the 2021 Stock Incentive Plan ("2021 Plan") and on December 2, 2021, our shareholders approved the 2021 Plan.

The Company recognizes compensation costs on a straight-line basis over the service period of the awards. There were no option awards granted in the three and nine months ended September 30, 2023. Fair values of option awards granted in the three and nine months ended September 30, 2022, were estimated using the Black-Scholes option pricing model under the following assumptions:

	Three Months	Nine Months
Risk-free interest rate	2.85% - 2.90%	1.91% - 2.90%
Dividend yield	0 %	0 %
Expected term (years)	3.25 - 6.00	3.25 - 6.00
Expected volatility	45.9% - 48.1%	45.8% - 48.5%

Determining the assumptions for the expected term and volatility requires management to exercise significant judgment. The expected term represents the weighted-average period that options granted are expected to be outstanding giving consideration to vesting schedules. Since the Company does not have an extended history of actual exercises, the Company has estimated the expected term using a simplified method which calculates the expected term as the average of the time-to-vesting and the contractual life of the awards. Given the limited public market for the Company's stock, the Company has elected to estimate its expected volatility by benchmarking its volatility to that of several public company issuers that operate within its market segment. The guideline companies' volatility was increased by a size adjustment premium of 30% to compensate for the difference in size between the guideline companies and the Company in its calculation.

There were 53,500 options with grant date fair values totaling \$168,900, and 131,200 options with grant date fair values totaling \$1,639,870, granted during the three and nine months ended September 30, 2022, respectively. There were zero and 10,700 options exercised during the three months ended September 30, 2023 and 2022, respectively. There were 2,000 and 26,400 options exercised during the nine months ended September 30, 2023 and 2022, respectively. As of September 30, 2023, there was \$431,067 of total unrecognized compensation cost related to nonvested share-based compensation arrangements granted under the stock incentive plans; that cost is expected to be recognized over a weighted-average period of 11 months.

Total compensation expense related to these plans was \$180,816 and \$398,319 for the three months ended September 30, 2023 and 2022, respectively, and \$557,146 and \$971,777 for the nine months ended September 30, 2023 and 2022, respectively, and is included in selling, general and administrative expenses on the condensed consolidated statements of operations.

Note 8. Settlement of Litigation

On April 28, 2023, the Company and Jeffrey Gerald, the individual from whom the WaveDancer purchased all the outstanding shares of GMI, executed an agreement to settle pending litigation between them (the "Settlement Agreement"). On January 25, 2023, Gerald, as the result of the termination of his employment, filed a lawsuit against the Company for one year's severance of \$150,000 and benefits to which he claimed he was entitled under his employment agreement with the Company. He had also claimed an anticipatory breach of the payment of \$1,500,000 of deferred consideration otherwise due him on December 10, 2023, under the Stock Purchase Agreement between him and the Company and an anticipatory breach to release from escrow 43,648 shares of the Company's common stock which are held in escrow for application against potential indemnity claims under the Stock Purchase Agreement.

The Company filed an answer denying Gerald's claims. In addition, the Company filed a counterclaim seeking damages from Gerald associated with the acquisition transaction and arising under the Stock Purchase Agreement.

The principal terms of the Settlement Agreement were:

- (a) All amounts due to Gerald related to the GMI acquisition, including the \$1,500,000 of deferred consideration, were deemed satisfied and such obligations were extinguished;
- (b) The Company removed restrictions from 43,648 shares of the Company's common stock;
- (c) The Company paid Gerald \$25,000 as reimbursement for legal costs; and,
- (d) Gerald and the Company agreed to mutual general releases of one another.

As a result of the settlement, the Company recognized a gain, net of expenses, of \$1,442,468 in the second quarter of 2023.

Note 9. Revolving Line of Credit and Notes Payable

On September 30, 2022, the Company entered a revolving line of credit with Summit Community Bank ("Summit") that provided for on-demand or short-term borrowings of up to \$1,000,000 at a variable interest rate equal to the prime rate as published in *The Wall Street Journal*, with a minimum rate of 3.99% and a maximum rate of 20.00%, and subject to a borrowing base calculated using outstanding accounts receivable. Borrowings under the line of credit are secured by the assets of the Company. There were no borrowings and \$500,000 of repayments during the three months ended September 30, 2023, and there were \$575,000 of borrowings and \$500,000 of repayments during the nine months ended September 30, 2023. This line of credit expired on August 16, 2023.

On September 11, 2023, the Company and Summit entered a new line of credit agreement with the same terms as the preceding agreement, except that the maximum availability under the new line was reduced from \$1,000,000 to \$500,000. As of September 30, 2023, there was \$500,000 outstanding and no borrowing availability under this line of credit. The line of credit expires on January 16, 2024.

Premium Financing Note Payable

The Company entered into a Premium Finance Agreement (“Premium Agreement”) on March 7, 2023, to purchase a one-year term directors and officers insurance policy. The Premium Agreement is for \$305,759 at a fixed rate of 8.75% per annum, amortized over ten months. The Premium Agreement requires ten fixed monthly principal and interest payments of \$31,815 from March 24, 2023 to December 24, 2023.

Note 10. Sales of Shares Under Common Stock Purchase Agreement

On July 8, 2022, we entered into a Common Stock Purchase Agreement (the “Purchase Agreement” or “ELOC”) and a Registration Rights Agreement (the “Registration Rights Agreement”) with B. Riley Principal Capital II, LLC (“B. Riley”). Pursuant to the Purchase Agreement, subject to certain limitations and conditions, the Company has the right, but not the obligation, to sell to B. Riley up to \$15,000,000 of shares of the Company’s common stock, par value \$0.001 per share (“Common Stock”), from time to time. Sales of Common Stock to B. Riley under the Purchase Agreement, and the timing of any such sales, are solely at the Company’s option, and the Company is under no obligation to sell any securities to B. Riley under the Purchase Agreement. Pursuant to the Registration Rights Agreement, the Company agreed to file a registration statement with the Securities Exchange Commission (the “SEC”) to register under the Securities Act of 1933, as amended (the “Securities Act”) the resale by B. Riley of up to 450,000 shares of Common Stock that the Company may issue or elect, in the Company’s sole discretion, to issue and sell to B. Riley, from time to time under the Purchase Agreement.

On August 11, 2022 and November 10, 2022, the Company issued to B. Riley 8,984 and 2,995 shares, respectively, as a commitment fee in accordance with the Purchase Agreement. The total value of the commitment fee shares was \$150,000 and is included in prepaid expenses and other current assets on the unaudited consolidated condensed balance sheet as of December 31, 2022. The commitment fee represents prepaid stock issuance cost and is being amortized to additional paid in capital as shares are sold under the Purchase Agreement. For the three and nine months ended September 30, 2023, the Company amortized \$54,692 and \$150,000 of the commitment fee, respectively.

During the three months ended September 30, 2023, the Company sold 20,000 shares of common stock under the ELOC at an average price of \$5.90 per share, net of fees of \$0.30 per share. The net proceeds from this sale were \$118,655. During the nine months ended September 30, 2023, the Company sold 27,429 shares of common stock under the ELOC at an average price of \$6.30 per share, net of fees of approximately \$0.30 per share. The net proceeds from these sales were \$172,108. There were no sales under the Purchase Agreement during the three and nine months ended September 30, 2022.

Note 11. Income Taxes

For the three and nine months ended September 30, 2022, the Company’s effective tax rate was 0%. The difference between the statutory tax rate and the effective tax rate is primarily driven by the presence of a full valuation allowance against all deferred tax assets.

Note 12. Earnings Per Share

Basic earnings (loss) per share excludes dilution and is computed by dividing the loss available to common shareholders by the weighted-average number of shares outstanding for the period. Diluted earnings (loss) per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock, except for periods when the Company reports a net loss because the inclusion of such items would be antidilutive. The antidilutive effects of 23,104 shares from stock options and zero shares from warrants, and 29,456 shares from stock options and zero shares from warrants, were excluded from diluted shares for the three and nine months ended September 30, 2022, respectively. The antidilutive effects of 43,735 shares from stock options and zero shares from warrants, and 57,009 shares from stock options and 15,000 shares from warrants, were excluded from diluted shares for the three and nine months ended September 30, 2022, respectively.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**Cautionary Statement Regarding Forward-Looking Statements**

This Form 10-Q contains forward-looking statements regarding our business, customer prospects, or other factors that may affect future earnings or financial results that are subject to the safe harbor created by the Private Securities Litigation Reform Act of 1995. Such statements involve risks and uncertainties which could cause actual results to vary materially from those expressed in the forward-looking statements. Investors should read and understand the risk factors detailed in our Annual Report on Form 10-K for the fiscal year ended December 31, 2022 ("Annual Report") and in other filings with the Securities and Exchange Commission.

We operate in a rapidly changing environment that involves a number of risks, some of which are beyond our control. This list highlights some of the risks which may affect future operating results. These are the risks and uncertainties we believe are most important for you to consider. Additional risks and uncertainties, not presently known to us, which we currently deem immaterial, or which are similar to those faced by other companies in our industry or business in general, may also impair our business operations. If any of the following risks or uncertainties actually occur, our business, financial condition and operating results would likely suffer. These risks include, among others, the following:

- We have had operating losses in three of each of the last four years and may not achieve or maintain profitability in the future.
- A portion of our revenue is expected to be generated by sales to government entities, which are subject to a number of challenges and risks.
- We face intense competition and could lose market share to our competitors, which could adversely affect our business, financial condition, and results of operations.
- We rely on our management team and other key employees and will need additional personnel to grow our business, and the loss of one or more key employees or our inability to hire, integrate, train and retain qualified personnel, including members for our board of directors, could harm our business.
- We are dependent on a few key customer contracts for a significant portion of our future revenue, and a significant reduction in services to one or more of these contracts would reduce our future revenue and harm our anticipated operating results.
- We are dependent on information technology, and disruptions, failures or security breaches of our information technology infrastructure could have a material adverse effect on our operations.
- We depend on computing infrastructure operated by Microsoft and other third parties to support some of our solutions and customers, and any errors, disruption, performance problems, or failure in their or our operational infrastructure could adversely affect our business, financial condition, and results of operations.
- Failure to comply with governmental laws and regulations could harm our business.
- We are subject to risks associated with our strategic investments, and impairments in the value of our investments could negatively impact our financial results.
- Our failure to raise additional capital or generate the significant capital necessary to expand our operations and invest in new products and subscriptions could reduce our ability to compete and could harm our business.
- The requirements of being a public company may strain our resources, divert management's attention, and affect our ability to attract and retain qualified board members.
- If we are not able to maintain and enhance our brand and our reputation as a provider of high-quality security solutions and services, our business and results of operations may be adversely affected.

In some cases, you can identify forward-looking statements by terms such as "may," "will," "should," "could," "would," "expect," "plans," "anticipates," "believes," "estimates," "projects," "predicts," "intends," "potential" and similar expressions intended to identify forward-looking statements. These statements reflect our current views with respect to future events and are based on assumptions and subject to risks and uncertainties. Given these uncertainties, you should not place undue reliance on these forward-looking statements. We discuss many of these risks in greater detail under the heading "Risk Factors" in Item 1A of our 2022 10-K. Also, these forward-looking statements represent our estimates and assumptions only as of the date of this report. Except as required by law, we assume no obligation to update any forward-looking statements after the date of this report.

Our Business

Founded in 1979 as Information Analysis Incorporated, the Company changed its name to WaveDancer, Inc. and converted from a Virginia corporation to a Delaware corporation in December 2021. The Company is in the business of developing and maintaining information technology (“IT”) systems, modernizing client information systems, and performing other IT-related professional services to government and commercial organizations.

On March 17, 2023, the Company sold effectively 75.1% of the equity of its Gray Matters, Inc. subsidiary (“GMI”) to Gray Matters Data Corporation (“GMDC”). The Company’s retained interest in GMI of 24.9% was initially accounted for as an equity method investment. Subsequent to the sale the Company discontinued consolidating GMI and the Company has reflected GMI as a discontinued operation in its consolidated statements of operations for all periods presented. Unless otherwise noted, all amounts and disclosures throughout this Item 2 relate to the Company’s continuing operations. See Note 2 to the unaudited condensed consolidated financial statements for further information about the sale transaction, the deconsolidation of GMI, and treatment of GMI as a discontinued operation. On August 9, 2023, the Company sold its remaining 24.9% interest in GMI to GMDC. On August 9, 2023, the Company sold its remaining equity interest in GMDC in exchange for \$400,000 in cash, and recognized a gain on sale of \$64,525. As of September 30, 2023 the Company has no equity method investment in GMDC and any other equity exposure to the GMI business.

The Company is an IT provider primarily for the benefit of federal government agencies. At present, we primarily apply our technology, services and experience to legacy software migration and modernization, developing web-based and mobile device solutions, including dynamic electronic forms development and conversion, data analytics, and we are in the process of acquiring talent and expertise in developing cybersecurity and cloud services practices. Our focus is on enterprise IT solutions primarily relating to system modernization, cloud-based solutions and cybersecurity protection.

Since the Company’s inception, we have performed software development and conversion projects for over 100 commercial and government customers including, but not limited to, the Department of Agriculture, Department of Defense, Department of Education, Department of Homeland Security, Department of the Treasury, U.S. Small Business Administration, U.S. Army, U.S. Air Force, Department of Veterans Affairs, and General Dynamics Information Technology (formerly Computer Sciences Corporation, CSRA).

Modernization has been a core competency of the Company for over 20 years. We have modernized over 100 million lines of COBOL code for over 35 governmental and commercial customers. We maintain a pool of skilled COBOL programmers. This provides us with a competitive advantage as the labor pool of such programmers is shrinking as aging software professionals retire. Our business has also historically relied upon the reselling of applications, primarily for forms development.

Through our acquisition in April 2021 of Tellenger, Inc. (“Tellenger”), which is now a wholly owned subsidiary of the Company, we acquired competencies in web-based solutions and cybersecurity. Tellenger is a boutique IT consulting and software development firm specializing in modernization, software development, cybersecurity, cloud solutions, and data analytics. We believe combining web-based solutions with system modernization will provide us with the skill sets that are needed to migrate legacy systems to the cloud. We foresee this as a key component of our modernization growth since there are billions of lines of code, in both the governmental and commercial sectors, that eventually must be modernized. It is also our intention to better leverage our resources, largely gained through the acquisition of Tellenger, to take advantage of the growth in the cybersecurity market.

In December 2021, we announced the reorganization of our entire professional services practice into Tellenger, and as a result, our professional services are contained in a single entity. Through Tellenger, we perform services such as business process re-engineering, cloud migrations, and Software-as-a-Service (“SaaS”) implementations on behalf of clients in the private and public sector with an aim to increase productivity, gain efficiencies, and achieve key performance indicators.

Our Strategy

Our strategy is to grow our business organically as well as through acquisitions. Through the acquisition of Tellenger, Inc. in 2021, we began to reposition our legacy professional services business by allocating resources away from third-party product reselling and toward professional services, which management viewed as higher margin. To grow organically, we are focused on bidding as a prime contractor on government proposals and in expanding our outreach to larger prime contractors for subcontract and teaming opportunities.

As discussed below under ‘Liquidity and Capital Resources’, the Company will need to raise additional capital to grow its business either organically or through acquisition. We are actively pursuing strategic alternatives which include the potential merger or sale of the Company. Any such transaction, if consummated, could fundamentally alter the Company’s business.

Results of Continuing Operations – Three Months Ended September 30, 2023 and 2022

Revenue

Total revenue was \$1,967,277 for the three months ended September 30, 2023, compared with \$2,306,379 in the prior year quarter, a decrease of \$339,102, or 14.7%. The decrease in revenue was driven by our de-emphasis of third-party software sales which accounted for just 2.3% of our sales in the third quarter of 2023 as compared to 8.3% in the prior year quarter. Professional services revenue decreased by \$192,712, or 9.1%, to \$1,921,300 in the third quarter of 2023 from \$2,114,012 in the third quarter of 2022. The decline in professional services revenue is driven primarily by one software modernization project where we had fewer resources deployed in the third quarter of 2023 as compared to the comparable prior year quarter based on current project deliverables.

Gross Profit

Gross profit decreased by \$88,784 or 12.0%, to \$649,812 for the three months ended September 30, 2023 as compared to \$738,596 in the prior year quarter. The decrease in gross profit includes an increase from professional services of \$5,533 and a decrease from third-party software sales of \$94,317. Professional services gross profit as a percent of revenue declined from 37.5% to 35.8% due to a change in the mix of contracts generating revenue and the related billing rates resulting as well as increases in our costs of labor that outpaced billing rate increases.

Selling, General and Administrative Expenses

The following table shows the major elements of SG&A expenses for the three months ended September 30, 2023 and 2022 and the changes between periods:

	2023	2022	Increase/ (Decrease)
Salaries and benefits	\$ 500,301	\$ 611,053	\$ (110,752)
Stock based compensation	180,816	398,319	(217,503)
Legal and professional fees	84,671	444,547	(359,876)
Depreciation & Amortization	56,644	53,597	3,047
Acquisition costs	68,457	38,617	29,840
Software, IT and office expenses	88,349	78,812	9,537
Governance and investor relations	38,901	97,800	(58,899)
Insurance	89,338	81,979	7,359
Marketing and promotions	460	29,629	(29,169)
All other	58,720	34,361	24,359
Total SG&A	\$ 1,166,657	\$ 1,868,714	\$ (702,057)

Operating Income from Continuing Operations

Our operating loss from continuing operations was \$516,845 in the third quarter of 2023 as compared to a loss of \$1,130,118 in the corresponding quarter in 2022, an improvement of \$613,273, or 54.3%. The decrease in the operating loss from continuing operations is primarily the result of the decrease in SG&A expenses of \$702,057, as shown above, partially offset by the decrease in gross profit of \$88,784.

Results of Discontinued Operations – Three Months Ended September 30, 2023 and 2022

The sale of GMI to GMDC occurred on March 17, 2023, and as a result, there was no activity for GMI in the third quarter of 2023. Following is the detail of discontinued operations for the third quarter of 2022:

	2022
Revenue	\$ -
Cost of revenue	256,974
Gross profit	(256,974)
Operating expenses -	
Salaries and benefits	463,502
Depreciation and amortization	303,791
Stock based compensation	215,775
Other operating expenses	113,078
Goodwill impairment	2,254,624
Loss before income tax benefit	(3,607,744)
Income tax benefit	77,592
Net income on discontinued operations	\$ (3,530,152)

Results of Continuing Operations – Nine Months Ended September 30, 2023 and 2022

Revenue

Total revenue was \$6,152,022 for the nine months ended September 30, 2023, compared with \$9,052,411 in the corresponding prior year period, a decrease of \$2,900,389, or 32.0%. The decrease in revenue was driven primarily by our de-emphasis of third-party software sales which accounted for just 2.6% of our sales in the nine months ended September 30, 2023, as compared to 28.7% in the nine months ended September 30, 2022. Professional services revenue decreased by \$465,819 to \$5,992,715 for the nine months ended September 30, 2023, from \$6,458,534 in the corresponding nine months of 2022. The decline in professional services revenue arose after the first quarter and is driven primarily by one software modernization project where we had fewer resources deployed in the second and third quarters of 2023 as compared to the comparable prior year quarters based on current project deliverables.

Gross Profit

Gross profit decreased by \$327,284 or 14.0%, to \$2,011,623 for the nine months ended September 30, 2023, as compared to \$2,338,907 in the prior year. The decrease in gross profit includes a decrease from professional services of \$161,513 and from third-party software sales of \$165,771. Professional services gross profit as a percent of revenue declined slightly from 33.7% to 33.6% due primary to changes in the mix of contracts generating revenue and the related billing rates.

Selling, General and Administrative Expenses

The following table shows the major elements of SG&A expenses for the nine months ended September 30, 2023 and 2022 and the changes between periods:

	2023	2022	Increase/ (Decrease)
Salaries and benefits	\$ 1,595,216	\$ 2,022,252	\$ (427,036)
Stock based compensation	557,146	971,777	(414,631)
Legal and professional fees	672,582	1,467,736	(795,154)
Depreciation & Amortization	164,472	165,977	(1,505)
Acquisition costs	512,975	829,478	(316,503)
Software, IT and office expenses	267,693	327,210	(59,517)
Governance and investor relations	246,439	376,904	(130,465)
Insurance	253,384	188,931	64,453
Marketing and promotions	1,328	102,996	(101,668)
All other	161,315	292,096	(130,781)
Total SG&A	\$ 4,432,550	\$ 6,745,357	\$ (2,312,807)

Operating Loss from Continuing Operations

Our operating loss from continuing operations was \$978,459 for nine months ended September 30, 2023 as compared to \$4,406,450 for the comparable prior year period, a decrease in the loss of \$3,427,991 or 77.8%. The decrease in the operating loss from continuing operations is primarily the result of the gain on litigation settlement of \$1,442,468 along with the decrease in SG&A expenses of \$2,312,807, as shown above, partially offset by the decrease in gross profit of \$327,284.

Results of Discontinued Operations – Nine Months Ended September 30, 2023 and 2022

The sale of GMI to GMDC occurred on March 17, 2023, and as a result we had approximately two fewer weeks of costs and expenses for GMI for the first quarter of 2023 as compared to the first quarter of 2022, and no activity for the second and third quarters of 2023 as compared to full activity during the second and third quarters of 2022, as follows:

	2023	2022	Increase/ (Decrease)
Revenue	\$ -	\$ 566,862	\$ (566,862)
Cost revenue	74,223	1,118,301	(1,044,078)
Gross profit	(74,223)	(551,439)	477,216
Operating expenses -			
Salaries and benefits	484,249	1,076,781	(592,532)
Depreciation and amortization	85,338	917,496	(832,158)
Stock based compensation, before forfeitures	65,487	268,283	(202,796)
Forfeiture of stock options	(407,322)	-	(407,322)
Other operating expenses	134,633	702,534	(567,901)
Change in fair value of contingent consideration	-	(930,000)	930,000
Goodwill impairment	-	2,254,624	(2,254,624)
Gain on disposal of business	(100,615)	-	(100,615)
Loss before income tax benefit	(335,993)	(4,841,157)	4,505,164
Income tax benefit	-	1,788,509	(1,788,509)
Net income (loss) on discontinued operations	\$ (335,993)	\$ (3,052,648)	\$ 2,716,655

Critical Accounting Estimates

Our accounting policies are described in Note 1 of our consolidated financial statements – *Organization and Summary of Significant Accounting Policies*. Our condensed consolidated financial statements and the accompanying notes thereto included elsewhere in this Quarterly Report on Form 10-Q are prepared in accordance with U.S. GAAP. The preparation of condensed consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, costs and expenses, and related disclosures. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. Actual results could differ significantly from our estimates. To the extent that there are differences between our estimates and actual results, our future financial statement presentation, financial condition, results of operations, and cash flows will be affected.

There have been no material changes to our critical accounting estimates as compared to the critical accounting estimates discussed in our Annual Report on Form 10-K for the year ended December 31, 2022 except for two new fair value measures for the first quarter of 2023:

- 1) the determination of the fair value of the contingent consideration receivable from GMDC, as discussed in Notes 2 and 5 to the accompanying consolidated financial statements, and
- 2) the determination of the initial fair value of our equity method investment in GMDC as of March 17, 2023.

The determination of the fair value of the contingent consideration is a recurring fair value measure at the end of each reporting period and includes significant judgmental inputs not observable in the market. Significant judgment was employed in determining the assumptions used in the determination of fair value as of March 31, 2023 and, accordingly, changes in assumptions could have a material impact on the increase or decrease in the fair value of contingent consideration recorded in any given period.

Equity Method Investment in GMDC

The Company received 993,768 common shares of GMDC representing 19.0 percent of the fully diluted capitalization. Prior to closing the acquisition on March 17 and through March 31, 2023, GMDC raised \$3,000,000 by issuing Series A preferred shares at \$1.00 per share representing 57.2 percent of the fully diluted capitalization. The Series A transaction was considered by the Company to be the most reliable indication of the fair value of total equity of GMDC. We utilized an option pricing model backsolve method (“OPM Backsolve”) to solve for the total equity value that results in a value of Series A equal to its issuance price, and to estimate the fair value of common shares. The significant inputs utilized in the OPM Backsolve include an estimated time to exit of four years, an estimated volatility of 75.0 percent, and a risk-free rate of 4.29 percent. A minority interest discount of 23.5% was also applied.

Liquidity and Capital Resources

On September 30, 2023, the Company had a net working capital of \$537,375, including cash and cash equivalents of \$877,198 and \$500,000 outstanding under its line of credit with Summit bank. For the nine months ended September 30, 2023, we generated a net loss from continuing operations of \$929,106. As discussed below, our ability to generate sufficient cash flows to meet our obligations for the twelve months following the issuance of these financial statements is dependent upon factors which are sufficiently outside of management’s control. Accordingly, there is substantial doubt about our ability to continue as a going concern.

The Company will need to raise additional capital to grow its business either organically or through acquisition. The Company is also pursuing strategic alternatives which include the potential merger or sale of the Company. There is no assurance that our efforts will result in any transactions or provide additional capital, which creates substantial doubt about the Company’s ability to continue as a going concern for at least one year from the date that the accompanying financial statements are issued. We estimate that within twelve months from the date of issuing these financial statements, the Company will need to raise additional capital to meet its ongoing operating cash flow requirements.

We used cash from continuing operations of \$2,020,330 during the nine months ended September 30, 2023 and anticipate that over the twelve months from the date of these financial statements our operating activities may use as much as \$1.0 million to \$1.5 million.

On August 9, 2023, the Company received \$1,400,000 of cash from GMDC from: 1) the sale of the common stock of GMDC held by the Company; and, 2) in satisfaction of the contingent consideration receivable due from GMDC to the Company. On August 9, 2023, the Company repaid \$500,000 on the Summit line of credit and has no further borrowing capacity thereunder. The line of credit expires on January 16, 2024. The Company has no commitments for capital spending nor any plans for material capital expenditures.

Item 4. Controls and Procedures

Disclosure Controls and Procedures

Our management, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, and people performing similar functions, has evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act), as of September 30, 2023 (the "Evaluation Date"). Based upon this evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of the Evaluation Date, our disclosure controls and procedures are effective to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act (i) is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and (ii) is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure.

Changes in Internal Controls over Financial Reporting

There were no changes in the Company's internal control over financial reporting during the quarter ended September 30, 2023, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Inherent Limitations on Effectiveness of Controls

Because of the inherent limitations in all control systems, no control system can provide absolute assurance that all control issues and instances of fraud, if any, within a company have been detected. These inherent limitations include the realities that judgments in decision making can be faulty and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of a person, by collusion of two or more people or by management override of the control. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and may not be detected. Notwithstanding these limitations, we believe that our disclosure controls and procedures are designed to provide reasonable assurance of achieving their objectives.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

There are no pending legal proceedings to which we are a party or to which any of our property is subject and, to the best of our knowledge, no such actions against us are contemplated or threatened.

Item 1A. Risk Factors

“Item 1A. Risk Factors” of our annual report on Form 10-K for the year ended December 31, 2022, as amended, includes a discussion of our risk factors. There have been no material changes from the risk factors described in our annual report on Form 10-K for the year ended December 31, 2022.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

On September 27, 2023, the Company sold 35,000 shares of common stock at a price of \$5.00 per share in a private placement offering from which it raised aggregate gross proceeds of \$175,000. The Company relied upon Rule 506(b) of Regulation D in issuing these shares. No placement fees or commissions were paid in connection with the offering. The proceeds are for use for general corporate purposes.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not applicable

Item 5. Other Information

None.

Item 6. Exhibits

31.1	Certification of Chief Executive Officer Pursuant to Rules 13a-14(a) and 15d-14(a) of the Securities Exchange Act of 1934	Filed with this Form 10-Q
31.2	Certification of Chief Financial Officer Pursuant to Rules 13a-14(a) and 15d-14(a) of the Securities Exchange Act of 1934	Filed with this Form 10-Q
32.1	Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	Filed with this Form 10-Q
32.2	Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	Filed with this Form 10-Q
101.INS	Inline XBRL Instance Document	Filed with this Form 10-Q
101.SCH	Inline XBRL Taxonomy Extension Schema	
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase	
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase	
101.LAB	Inline XBRL Taxonomy Extension Label Linkbase	
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase	
104	Cover Page Interactive Data File (embedded within the Inline XBRL document and contained in Exhibit 101)	

SIGNATURES

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

WaveDancer, Inc.
(Registrant)

Date: November 13, 2023

By: /s/ G. James Benoit, Jr.
G. James Benoit,
Chief Executive Officer

Date: November 13, 2023

By: /s/ Timothy G. Hannon
Timothy G. Hannon,
Chief Financial Officer

**CERTIFICATION of Chief Executive Officer Pursuant to Rules 13a-14(a)
and 15d-14(a) of the Securities Exchange Act of 1934**

I, G. James Benoit, Jr., certify that:

1. I have reviewed this quarterly report on Form 10-Q of WaveDancer, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 13, 2023

By: /s/ G. James Benoit, Jr.
G. James Benoit,
Chief Executive Officer

A signed original of this written statement required by Section 302 has been provided to WaveDancer, Inc. and will be retained by WaveDancer, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.

**CERTIFICATION of Chief Financial Officer Pursuant to Rules 13a-14(a)
and 15d-14(a) of the Securities Exchange Act of 1934**

I, Timothy G. Hannon, certify that:

1. I have reviewed this quarterly report on Form 10-Q of WaveDancer, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 13, 2023

By: /s/ Timothy G. Hannon
Timothy G. Hannon,
Chief Financial Officer

A signed original of this written statement required by Section 302 has been provided to WaveDancer, Inc. and will be retained by WaveDancer, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906
OF THE SARBANES-OXLEY ACT OF 2002**

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code), I, G. James Benoit, Jr., Chief Executive Officer of WaveDancer, Inc., a Delaware corporation (the "Company"), do hereby certify, to the best of my knowledge, that:

- 1 the Company's Quarterly Report on Form 10-Q for the period ended September 30, 2023, as filed with the Securities and Exchange Commission on the date hereof, (the "Report") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- 2 the information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company for the periods presented therein.

Date: November 13, 2023

By: /s/ G. James Benoit, Jr.
G. James Benoit,
Chief Executive Officer

A signed original of this written statement required by Section 906 has been provided to WaveDancer, Inc. and will be retained by WaveDancer, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906
OF THE SARBANES-OXLEY ACT OF 2002**

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code), I, Timothy G. Hannon, Chief Financial Officer of WaveDancer, Inc., a Delaware corporation (the "Company"), do hereby certify, to the best of my knowledge, that:

- 1 the Company's Quarterly Report on Form 10-Q for the period ended September 30, 2023, as filed with the Securities and Exchange Commission on the date hereof, (the "Report") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- 2 the information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company for the periods presented therein.

Date: November 13, 2023

By: /s/ Timothy G. Hannon
Timothy G. Hannon,
Chief Financial Officer

A signed original of this written statement required by Section 906 has been provided to WaveDancer, Inc. and will be retained by WaveDancer, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.