
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 March 31, 2017

OR

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

For the transition period from to

Commission file number 001-33365

USA Technologies, Inc.

(Exact name of registrant as specified in its charter)

Pennsylvania

(State or other jurisdiction of incorporation or organization)

23-2679963

(I.R.S. Employer Identification No.)

100 Deerfield Lane, Suite 300, Malvern, Pennsylvania

(Address of principal executive offices)

19355

(Zip Code)

(610) 989-0340

(Registrant's telephone number, including area code)

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, 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 Act). Yes No

As of April 24, 2017, there were 40,331,645 shares of Common Stock, no par value, outstanding.

**USA TECHNOLOGIES, INC.
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Part I. Financial Information
Item 1. Consolidated Financial Statements

USA Technologies, Inc.
Consolidated Balance Sheets

| (\$ in thousands, except shares) | March 31, 2017 (unaudited) | June 30, 2016 (audited) |
|---|---|--|
| Assets | | |
| Current assets: | | |
| Cash and Cash Equivalents | \$ 17,780 | \$ 19,272 |
| Accounts receivable, less allowance for doubtful accounts of \$2,851 and \$2,814, respectively | 6,734 | 4,899 |
| Finance receivables, less allowance for credit losses of \$25 and \$0, respectively | 2,057 | 3,588 |
| Inventory, net | 4,147 | 2,031 |
| Prepaid expenses and other current assets | 1,628 | 987 |
| Deferred income taxes | 2,271 | 2,271 |
| Total current assets | 34,617 | 33,048 |
| Finance receivables, less current portion | 7,548 | 3,718 |
| Other assets | 137 | 348 |
| Property and equipment, net | 9,173 | 9,765 |
| Deferred income taxes | 25,359 | 25,453 |
| Intangibles, net | 666 | 798 |
| Goodwill | 11,492 | 11,703 |
| Total assets | \$ 88,992 | \$ 84,833 |
| Liabilities and shareholders' equity | | |
| Current liabilities: | | |
| Accounts payable | \$ 11,529 | \$ 12,354 |
| Accrued expenses | 3,111 | 3,458 |
| Line of credit, net | 7,021 | 7,119 |
| Current obligations under long-term debt | 786 | 629 |
| Income taxes payable | — | 18 |
| Warrant liabilities | — | 3,739 |
| Deferred gain from sale-leaseback transactions | 255 | 860 |
| Total current liabilities | 22,702 | 28,177 |
| Long-term liabilities: | | |
| Long-term debt, less current portion | 1,239 | 1,576 |
| Accrued expenses, less current portion | 52 | 15 |
| Deferred gain from sale-leaseback transactions, less current portion | — | 40 |
| Total long-term liabilities | 1,291 | 1,631 |
| Total liabilities | 23,993 | 29,808 |
| Commitments and contingencies (Note 10) | | |
| Shareholders' equity: | | |
| Preferred stock, no par value: | | |
| Authorized shares- 1,800,000 Series A convertible preferred- Authorized shares- 900,000 Issued and outstanding shares- 445,063 with liquidation preference of \$18,775 and \$18,108, respectively | 3,138 | 3,138 |
| Common stock, no par value: Authorized shares- 640,000,000 Issued and outstanding shares- 40,327,675 and 37,783,444, respectively | 245,463 | 233,394 |
| Accumulated deficit | (183,602) | (181,507) |
| Total shareholders' equity | 64,999 | 55,025 |
| Total liabilities and shareholders' equity | \$ 88,992 | \$ 84,833 |

See accompanying notes.

USA Technologies, Inc.
Consolidated Statements of Operations
(Unaudited)

| (\$ in thousands, except shares and per share data) | Three months ended March 31, | | Nine months ended March 31, | |
|---|---------------------------------|-------------------|--------------------------------|-------------------|
| | 2017 | 2016 | 2017 | 2016 |
| Revenues: | | | | |
| License and transaction fees | \$ 17,459 | \$ 14,727 | \$ 50,463 | \$ 41,326 |
| Equipment sales | 9,001 | 5,634 | 19,341 | 14,138 |
| Total revenues | 26,460 | 20,361 | 69,804 | 55,464 |
| Costs of sales/revenues: | | | | |
| Cost of services | 11,876 | 9,703 | 34,508 | 27,475 |
| Cost of equipment | 7,959 | 4,986 | 16,170 | 11,787 |
| Total costs of sales/revenues | 19,835 | 14,689 | 50,678 | 39,262 |
| Gross profit | 6,625 | 5,672 | 19,126 | 16,202 |
| Operating expenses: | | | | |
| Selling, general and administrative | 5,947 | 6,094 | 18,649 | 15,652 |
| Depreciation and amortization | 259 | 173 | 774 | 439 |
| Total operating expenses | 6,206 | 6,267 | 19,423 | 16,091 |
| Operating income (loss) | 419 | (595) | (297) | 111 |
| Other income (expense): | | | | |
| Interest income | 114 | 67 | 387 | 138 |
| Interest expense | (188) | (180) | (601) | (403) |
| Change in fair value of warrant liabilities | - | (4,805) | (1,490) | (5,692) |
| Total other expense, net | (74) | (4,918) | (1,704) | (5,957) |
| Income (loss) before income taxes | 345 | (5,513) | (2,001) | (5,846) |
| (Provision) benefit for income taxes | (209) | 93 | (94) | (88) |
| Net income (loss) | 136 | (5,420) | (2,095) | (5,934) |
| Cumulative preferred dividends | (334) | (334) | (668) | (668) |
| Net loss applicable to common shares | \$ (198) | \$ (5,754) | \$ (2,763) | \$ (6,602) |
| Net loss per common share - basic and diluted | \$ (0.00) | \$ (0.16) | \$ (0.07) | \$ (0.18) |
| Basic and diluted weighted average number of common shares outstanding | 40,327,697 | 36,161,626 | 39,703,690 | 35,972,633 |

See accompanying notes.

USA Technologies, Inc.
Consolidated Statement of Shareholders' Equity
(Unaudited)

| (\$ in thousands, except shares) | Series A Convertible Preferred Stock | | Common Stock | | Accumulated | Total |
|--|--|-----------------|-------------------|------------------|---------------------|------------------|
| | Shares | Amount | Shares | Amount | Deficit | |
| Balance, June 30, 2016 | 445,063 | \$ 3,138 | 37,783,444 | \$233,394 | \$ (181,507) | \$ 55,025 |
| Reclass of fair value of warrant liability upon exercise of warrants | | | | 5,229 | | 5,229 |
| Exercise of warrants | | | 2,401,408 | 6,193 | | 6,193 |
| Stock based compensation | | | | | | |
| 2013 Stock Incentive Plan | | | 149,356 | 288 | | 288 |
| 2014 Stock Option Incentive Plan | | | | 155 | | 155 |
| 2015 Equity Incentive Plan | | | | 235 | | 235 |
| Retirement of common stock | | | (6,533) | (31) | | (31) |
| Net loss | | | | | (2,095) | (2,095) |
| Balance, March 31, 2017 | <u>445,063</u> | <u>\$ 3,138</u> | <u>40,327,675</u> | <u>\$245,463</u> | <u>\$ (183,602)</u> | <u>\$ 64,999</u> |

See accompanying notes.

USA Technologies, Inc.
Consolidated Statements of Cash Flows
(Unaudited)

| (\$ in thousands) | Three months ended March 31, | | Nine months ended March 31, | |
|--|---------------------------------|------------|--------------------------------|------------|
| | 2017 | 2016 | 2017 | 2016 |
| OPERATING ACTIVITIES: | | | | |
| Net income (loss) | \$ 136 | \$ (5,420) | \$ (2,095) | \$ (5,934) |
| Adjustments to reconcile net income (loss) to net cash provided/(used) by operating activities: | | | | |
| Charges incurred in connection with the vesting and issuance of common stock and common stock options for employee and director compensation | 233 | 142 | 678 | 651 |
| Gain on disposal of property and equipment | (28) | (15) | (59) | (57) |
| Amortization of deferred financing fees | 72 | - | 98 | - |
| Bad debt expense | 127 | 506 | 577 | 980 |
| Depreciation | 1,165 | 1,190 | 3,642 | 3,863 |
| Amortization of intangible assets | 45 | 44 | 132 | 44 |
| Change in fair value of warrant liabilities | - | 4,805 | 1,490 | 5,692 |
| Deferred income taxes, net | 209 | (93) | 94 | 88 |
| Recognition of deferred gain from sale-leaseback transactions | (216) | (215) | (646) | (645) |
| Changes in operating assets and liabilities: | | | | |
| Accounts receivable | (41) | (1,660) | (2,388) | (2,070) |
| Finance receivables | (4,232) | (366) | (2,113) | (735) |
| Inventory | 647 | 250 | (2,042) | 1,118 |
| Prepaid expenses and other assets | 136 | (160) | (406) | (366) |
| Accounts payable | 2,441 | 4,154 | (825) | 1,487 |
| Accrued expenses | 160 | 1,166 | (414) | 1,151 |
| Income taxes payable | (6) | - | (18) | (70) |
| Net cash provided/(used) by operating activities | 848 | 4,328 | (4,295) | 5,197 |
| INVESTING ACTIVITIES: | | | | |
| Purchase and additions of property and equipment | (183) | (164) | (792) | (331) |
| Purchase of property for rental program | (691) | - | (2,026) | - |
| Proceeds from sale of property and equipment | 44 | 19 | 105 | 124 |
| Cash paid for assets acquired from VendScreen | - | (5,625) | - | (5,625) |
| Net cash used by investing activities | (830) | (5,770) | (2,713) | (5,832) |
| FINANCING ACTIVITIES: | | | | |
| Cash used for the retirement of common stock | - | - | (31) | (40) |
| Payment of deferred financing costs | (90) | - | (90) | - |
| Proceeds from exercise of common stock warrants | - | 1,652 | 6,193 | 1,681 |
| Proceeds (payments) from line of credit, net | - | 33 | - | 3,033 |
| Repayment of long-term debt | (182) | (151) | (556) | (512) |
| Net cash (used)/provided by financing activities | (272) | 1,534 | 5,516 | 4,162 |
| Net (decrease) increase in cash | (254) | 92 | (1,492) | 3,527 |
| Cash at beginning of period | 18,034 | 14,809 | 19,272 | 11,374 |
| Cash at end of period | \$ 17,780 | \$ 14,901 | \$ 17,780 | \$ 14,901 |
| <i>Supplemental disclosures of cash flow information:</i> | | | | |
| Interest paid in cash | \$ 59 | \$ 191 | \$ 528 | \$ 404 |
| Depreciation expense allocated to cost of services | \$ 950 | \$ 1,051 | \$ 3,000 | \$ 3,436 |
| Reclass of rental program property to inventory, net | \$ 8 | \$ 347 | \$ 74 | \$ 845 |
| Prepaid items financed with debt | \$ - | \$ - | \$ 54 | \$ 103 |
| Equipment and property acquired under capital lease | \$ 54 | \$ 409 | \$ 326 | \$ 444 |
| Disposal of property and equipment | \$ 87 | \$ 189 | \$ 748 | \$ 526 |
| Fair value of common stock warrants at issuance recorded as a debt discount | \$ - | \$ 52 | \$ - | \$ 52 |
| Debt financing cost financed with debt | \$ - | \$ 79 | \$ - | \$ 79 |

See accompanying notes.

USA Technologies, Inc.
Notes to Consolidated Financial Statements
(Unaudited)

1. BUSINESS

USA Technologies, Inc. (the “Company”, “We”, “USAT”, or “Our”) was incorporated in the Commonwealth of Pennsylvania in January 1992. We are a provider of technology-enabled solutions and value-added services that facilitate electronic payment transactions primarily within the unattended Point of Sale (“POS”) market. We are a leading provider in the small ticket, beverage and food vending industry and are expanding our solutions and services to other unattended market segments, such as amusement, commercial laundry, kiosk and others. Since our founding, we have designed and marketed systems and solutions that facilitate electronic payment options, as well as telemetry Internet of Things (“IoT”) and machine-to-machine (“M2M”) services, which include the ability to remotely monitor, control, and report on the results of distributed assets containing our electronic payment solutions. Historically, these distributed assets have relied on cash for payment in the form of coins or bills, whereas, our systems allow them to accept cashless payments such as through the use of credit or debit cards or other emerging contactless forms, such as mobile payment.

INTERIM FINANCIAL INFORMATION

The accompanying unaudited consolidated financial statements of USA Technologies, Inc. have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements and therefore should be read in conjunction with the Company’s Annual Report on Form 10-K for the year ended June 30, 2016. In the opinion of management, all adjustments considered necessary for a fair presentation, consisting of normal recurring adjustments, have been included. Operating results for the three and nine months ended March 31, 2017 are not necessarily indicative of the results that may be expected for the year ending June 30, 2017. The balance sheet at June 30, 2016 has been derived from the audited consolidated financial statements at that date, but does not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements.

2. ACCOUNTING POLICIES

CONSOLIDATION

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

USE OF ESTIMATES

The preparation of the consolidated financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

CASH AND CASH EQUIVALENTS

Cash equivalents represent all highly liquid investments with original maturities of three months or less. Cash equivalents are comprised of money market funds. The Company maintains its cash in bank deposit accounts, which may exceed federally insured limits at times.

ACCOUNTS RECEIVABLE AND ALLOWANCE FOR UNCOLLECTIBLE ACCOUNTS

Accounts receivable include amounts due to the Company for sales of equipment, other amounts due from customers, merchant service receivables, and unbilled amounts due from customers, net of the allowance for uncollectible accounts.

The Company maintains an allowance for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments, including from a shortfall in the customer transaction fund flow from which the Company would normally collect amounts due.

The allowance is determined through an analysis of various factors including the aging of the accounts receivable, the strength of the relationship with the customer, the capacity of the customer transaction fund flow to satisfy the amount due from the customer, an assessment of collection costs and other factors. The allowance for doubtful accounts receivable is management's best estimate as of the respective reporting date. The Company writes off accounts receivable against the allowance when management determines the balance is uncollectible and the Company ceases collection efforts. Management believes that the allowance recorded is adequate to provide for its estimated credit losses.

FINANCE RECEIVABLES

The Company offers extended payment terms to certain customers for equipment sales under its Quick Start Program. In accordance with the Financial Accounting Standards Board ("FASB") Accounting Standards Codification® ("ASC") Topic 840, "Leases", agreements under the Quick Start Program qualify for sales-type lease accounting. Accordingly, the future minimum lease payments are classified as finance receivables in the Company's consolidated balance sheets. Finance receivables for Quick Start leases are generally for a sixty month term. Finance receivables are carried at their contractual amount and charged off against the allowance for credit losses when management determines that recovery is unlikely and the Company ceases collection efforts. The Company recognizes a portion of the note or lease payments as interest income in the accompanying consolidated financial statements based on the effective interest rate method.

INVENTORY, Net

Inventory consists of finished goods and packaging materials. The Company's inventory is stated at the lower of cost (average cost basis) or market.

PROPERTY AND EQUIPMENT, Net

Property and equipment are recorded at cost. Property and equipment are depreciated on the straight-line basis over the estimated useful lives of the related assets. Leasehold improvements are amortized on the straight-line basis over the lesser of the estimated useful life of the asset or the respective lease term.

GOODWILL AND INTANGIBLE ASSETS

The Company's intangible assets include goodwill, non-compete agreements, brand, developed technology and customer relationships.

Goodwill represents the excess of cost over fair value of the net assets purchased in acquisitions. The Company accounts for goodwill in accordance with ASC 350, "Intangibles – Goodwill and Other". Under ASC 350, goodwill is not amortized to earnings, but instead is subject to periodic testing for impairment. Testing for impairment is to be done at least annually and at other times if events or circumstances arise that indicate that impairment may have occurred. The Company has selected April 1 as its annual test date.

FAIR VALUE OF FINANCIAL INSTRUMENTS

The FASB issued Accounting Standards Update ("ASU") 2010-06, "Fair Value Measurements and Disclosures ("Topic 820"): Improving Disclosures about Fair Value Measurements." ASU 2010-06 amends certain disclosure requirements of Subtopic 820-10. This ASU provides additional disclosures for transfers in and out of Levels 1 and 2 and for activity in Level 3. This ASU also clarifies certain other existing disclosure requirements including level of desegregation and disclosures around inputs and valuation techniques.

The Company's financial assets and liabilities are accounted for in accordance with ASC 820 "Fair Value Measurement." Under ASC 820 the Company uses inputs from the three levels of the fair value hierarchy to measure its financial assets and liabilities. The three levels are as follows:

Level 1- Inputs are unadjusted quoted prices in active markets for identical assets or liabilities that the Company has the ability to access at the measurement date.

Level 2- Inputs are other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (i.e., interest rates, yield curves, etc.), and inputs that are derived principally from or corroborated by observable market data by correlation or other means (market corroborated inputs).

Level 3- Inputs are unobservable and reflect the Company's assumptions that market participants would use in pricing the asset or liability. The Company develops these inputs based on the best information available.

The Company's financial instruments, principally accounts receivable, short-term finance receivables, prepaid expenses and other assets, accounts payable and accrued expenses, are carried at cost which approximates fair value due to the short-term maturity of these instruments. The fair value of the Company's obligations under its long-term debt agreements and the long-term portion of its finance receivables approximates their carrying value as such instruments are at market rates currently available to the Company.

REVENUE RECOGNITION

Revenue from the sale or QuickStart lease of equipment is recognized on the terms of freight-on-board shipping point. Activation fee revenue, if applicable, is recognized when the Company's cashless payment device is initially activated for use on the Company network. Transaction processing revenue is recognized upon the usage of the Company's cashless payment and control network. License fees for access to the Company's devices and network services are recognized on a monthly basis. In all cases, revenue is only recognized when persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the price is fixed and determinable, and collection of the resulting receivable is reasonably assured. The Company estimates an allowance for product returns at the date of sale and license and transaction fee refunds on a monthly basis. The company makes an adjustment for rebates and product returns.

ePort hardware is available to customers under the QuickStart program pursuant to which the customer would enter into a five-year non-cancelable lease with either the Company or a third-party financing company for the devices. The Company utilizes its best estimate of selling price when calculating the revenue to be recorded under these leases. The leases qualify for sales type lease accounting. Accordingly, the Company recognizes a portion of lease payments as interest income for leases not placed with a third-party financing company. At the end of the lease period, the customer would have the option to purchase the device at its residual value.

PREFERRED STOCK

The Company adopted the provisions of ASU 2014-16 in determining whether the Company's Series A Convertible Preferred Stock ("preferred stock") is more equity-like or debt-like, and whether derivatives embedded in the preferred stock, if any, must be bifurcated and accounted for separately from its host contract. Based upon management's review of the preferred stock features, management has determined that the preferred stock is more equity-like and that the embedded derivatives do not require bifurcation. As such, the adoption of this standard did not have a material impact on the company's financial statements.

ACCOUNTING FOR EQUITY AWARDS

In accordance with the ASC Topic 718, the cost of employee services received in exchange for an award of equity instruments is based on the grant-date fair value of the award and allocated over the vesting period of the award.

INCOME TAXES

The Company follows the ASC Topic 740, "Accounting for Uncertainty in Income Taxes", which provides detailed guidance for the financial statement recognition, measurement and disclosure of uncertain tax positions recognized in the consolidated financial statements. Accordingly, tax positions must meet a "more-likely-than-not" recognition threshold at the effective date to be recognized upon the adoption of ASC Topic 740 and in subsequent periods.

Income taxes are computed using the asset and liability method of accounting. Under the asset and liability method, a deferred tax asset or liability is recognized for estimated future tax effects attributable to temporary differences and carryforwards. The measurement of deferred income tax assets is adjusted by a valuation allowance, if necessary, to recognize future tax benefits only to the extent that, based on available evidence, it is more likely than not such benefits will be realized. The Company recognizes interest and penalties, if any, related to uncertain tax positions in selling, general and administrative expenses. No interest or penalties related to uncertain tax positions were accrued or incurred during the three and nine months ended March 31, 2017 and 2016.

EARNINGS (LOSS) PER COMMON SHARE

Basic earnings (loss) per share are calculated by dividing income (loss) applicable to common shares by the weighted average common shares outstanding for the period. Diluted earnings per share are calculated by dividing income (loss) applicable to common shares by the weighted average common shares outstanding for the period plus the effect of potential common shares unless such effect is anti-dilutive.

SOFTWARE DEVELOPMENT COSTS

The Company follows the ASC Topic 350-40, "Accounting for the Cost of Computer Software Developed or obtained for Internal Use", which provides for guidance for what costs can be capitalized for internal use.

Capitalized costs for internal-use software are included in fixed assets in the consolidated balance sheet and are amortized over three years. Costs incurred during the preliminary project along with post-implementation stages of internal use computer software development and costs incurred to maintain existing product offerings are expensed as incurred. The capitalization and ongoing assessment of recoverability of development costs require considerable judgment by management with respect to certain external factors, including, but not limited to, technological and economic feasibility and estimated economic life.

RECENT ACCOUNTING PRONOUNCEMENTS

The Company is evaluating whether the effects of the following recent accounting will have a material effect on the Company's consolidated financial position, results of operations or cash flows.

In January 2017, the FASB issued ASU 2017-04 – "Intangibles-Goodwill and Other (Topic 350): Simplifying the test for Goodwill Impairment.

RECLASSIFICATION

Commencing with the June 30, 2016 financial statements, the Company changed the manner in which it presents certain unfunded finance receivables in its consolidated balance sheets and the related statements of cash flows. These finance receivables have yet to be and are expected to be funded by a third-party funding source. The previous accounting classification recorded these amounts as accounts receivable in the consolidated balance sheets and the related statements of cash flows. The impact of this change on the Statement of Cash Flows is as follows:

| | Three months ended | | Nine months ended | |
|---|------------------------|------------------------|------------------------|------------------------|
| | March 31, 2016 | | March 31, 2016 | |
| | Accounts Receivable | Finance Receivables | Accounts Receivable | Finance Receivables |
| Per Original Statement of Cash Flows | \$ (1,872) | \$ (154) | \$ (3,352) | \$ 547 |
| Reclass of Unfunded Leases, beginning of period (starting BS) | (2,096) | 2,096 | (1,026) | 1,026 |
| Reclass of Finance Receivables, end of period | 2,308 | (2,308) | 2,308 | (2,308) |
| Impact from the reclassification | 212 | (212) | 1,282 | (1,282) |
| Adjusted Statement of Cash Flows | \$ (1,660) | \$ (366) | \$ (2,070) | \$ (735) |

3. FINANCE RECEIVABLES

Finance receivables consist of the following:

| (\$ in thousands) | March 31, 2017 (unaudited) | June 30, 2016 |
|--|----------------------------------|------------------|
| Total finance receivables | \$ 9,605 | \$ 7,306 |
| Less current portion | 2,057 | 3,588 |
| Non-current portion of finance receivables | \$ 7,548 | \$ 3,718 |

The Company collects monthly payments of its finance receivables from the customers' transaction fund flow. Accordingly, as the fund flow from these customers' transactions is generally sufficient to satisfy the amount due to the Company, the risk of loss is considered low and the Company has provided for an allowance for credit losses for finance receivables of \$25 thousand and zero as of March 31, 2017 and June 30, 2016, respectively. The number of Finance Receivables that are in a loss position is nine and zero as of March 31, 2017 and June 30, 2016 respectively.

Credit Quality Indicators

| Credit risk profile based on payment activity: (\$ in thousands) | March 31, 2017 (unaudited) | June 30, 2016 |
|---|----------------------------------|------------------|
| Performing | \$ 9,527 | \$ 7,174 |
| Nonperforming | 78 | 132 |
| Total | \$ 9,605 | \$ 7,306 |

Age Analysis of Past Due Finance Receivables As of March 31, 2017

| (\$ in thousands) | 31 – 60 Days Past Due | 61 – 90 Days Past Due | Greater than 90 Days Past Due | Total Past Due | Current | Total Finance Receivables |
|-------------------|-----------------------------|-----------------------------|-------------------------------------|-------------------|---------|---------------------------------|
| QuickStart Leases | \$ 31 | \$ 1 | \$ 21 | \$ 53 | \$9,552 | \$ 9,605 |

Age Analysis of Past Due Finance Receivables As of June 30, 2016

| (\$ in thousands) | 31 – 60 Days Past Due | 61 – 90 Days Past Due | Greater than 90 Days Past Due | Total Past Due | Current | Total Finance Receivables |
|-------------------|-----------------------------|-----------------------------|-------------------------------------|-------------------|---------|---------------------------------|
| QuickStart Leases | \$ 98 | \$ 31 | \$ 3 | \$ 132 | \$7,174 | \$ 7,306 |

4. GOODWILL AND INTANGIBLES

On January 15, 2016, the Company executed an Asset Purchase Agreement with VendScreen, Inc (“VendScreen”) a Portland, Oregon based developer of vending industry cashless payment technology, by which it acquired substantially all of VendScreen's assets and assumed specified liabilities, for a cash payment of \$5.62 million and the corresponding goodwill recorded was \$4.0 million. In December 2016, the company finalized the opening balance sheet of VendScreen and recorded a reduction of goodwill for \$211 thousand and increased finance receivables for the same amount. The final goodwill amount related to VendScreen opening balance sheet is \$3.8 million.

The following table summarizes the final purchase price allocation to reflect the fair values of the assets acquired and liabilities assumed at the date of acquisition.

| | |
|--|------------------------|
| Consideration: | |
| Fair value of total consideration paid in cash | <u>\$ 5,625</u> |
| Acquisition related costs: | |
| | <u>\$ 842</u> |
| Recognized amounts of identifiable assets acquired and liabilities assumed: | |
| Financial Assets: | |
| Accounts Receivable | 3 |
| Finance Receivables | 839 |
| Other Current Assets | 20 |
| Deferred Income Taxes | 18 |
| | <u>880</u> |
| Property, Plant & Equipment | 81 |
| Identifiable Intangible Assets: | |
| Developed Technology | 639 |
| Customer Relationships | 149 |
| Brand | 95 |
| Noncompete Agreement | 2 |
| Fair Value of Intangible Assets | <u>885</u> |
| Financial Liabilities | |
| Accrued Liabilities | <u>\$ (50)</u> |
| Total identifiable net assets | <u>\$ 1,796</u> |
| Goodwill | <u>\$ 3,829</u> |
| Total Fair Value | <u>\$ 5,625</u> |

During the three and nine months ending March 31, 2017, there was \$45 thousand and \$132 thousand, respectively, of amortization expense relating to acquired intangible assets. There was \$44 amortization expense relating to acquired intangible assets during the three and nine months ended March 31, 2016. Intangible asset balances consisted of the following:

| (\$ in thousands) | Balance June 30, 2016 | Additions/ Adjustments | Amortization | Balance March 31, 2017 | Amortization Period |
|---------------------------|--------------------------|---------------------------|-----------------|---------------------------|------------------------|
| Intangible Assets: | | | | | |
| Non-compete agreements | \$ 1 | \$ — | \$ (1) | \$ — | 2 years |
| Brand | 79 | — | (24) | 55 | 3 years |
| Developed technology | 576 | — | (96) | 480 | 5 years |
| Customer relationships | 142 | — | (11) | 131 | 10 years |
| Total Intangible Assets | <u>\$ 798</u> | <u>\$ —</u> | <u>\$ (132)</u> | <u>\$ 666</u> | |
| Goodwill | <u>\$ 11,703</u> | <u>\$ (211)</u> | <u>\$ —</u> | <u>\$ 11,492</u> | Indefinite |

5. LINE OF CREDIT

During the fiscal year ended June 30, 2016, the Company entered into a Loan and Security Agreement and other ancillary documents (as amended, the “Heritage Loan Documents”) with Heritage Bank of Commerce (“Heritage Bank”), providing for a secured asset-based revolving line of credit in an amount of up to \$12.0 million (the “Heritage Line of Credit”) at an interest rate calculated based on the Federal Reserves’ Prime, which was 3.75% at March 31, 2017, plus 2.25%. The Heritage Line of Credit and the Company’s obligations under the Heritage Loan Documents are secured by substantially all of the Company’s assets, including its intellectual property.

During March 2017, the Company entered into the third amendment with Heritage Bank that extended the maturity date of the Heritage Line of Credit from March 29, 2017 to September 30, 2018. The Company paid a total of \$90 thousand in deferred financing costs.

At the time of maturity, all outstanding advances under the Heritage Line of Credit as well as any unpaid interest are due and payable. Prior to maturity of the Heritage Line of Credit, the Company may prepay amounts due under the Heritage Line of Credit without penalty, and subject to the terms of the Heritage Loan Documents, may re-borrow any such amounts.

The Heritage Loan Documents contain customary representations and warranties and affirmative and negative covenants applicable to the Company. The Heritage Loan Documents also require the Company to achieve a minimum Adjusted EBITDA, as defined in the Heritage Loan Documents, measured on a quarterly basis; that the number of the Company’s connections as of the end of each fiscal quarter shall not decrease below a specified number or by more than five percent as compared to the number of the Company’s connections as of the end of the immediately prior fiscal quarter; and that the Company shall maintain a minimum balance of unrestricted cash at Heritage Bank.

The balance due on the Heritage Line of Credit was \$7.0 million at March 31, 2017 and \$7.1 million at June 30, 2016. Included in the Heritage Line of Credit balance is \$90 thousand of unamortized debt issuance costs, which is reflected in our net liability of \$7.0 million for the quarter ending March 31, 2017. As of March 31, 2017, \$5.0 million was available under our line of credit. Interest expense on the line of credit was approximately \$100 thousand and \$300 thousand for the three and nine months ended March 31, 2017, respectively.

6. LONG-TERM DEBT

The Company periodically enters into capital lease obligations to finance certain office, network equipment and related support for use in its daily operations. During the nine-month period ended March 31, 2017, the Company commenced capital lease obligations of \$380 thousand. The obligations are due in two to five years in monthly or quarterly installments of \$1 thousand to \$21 thousand. The value of the acquired equipment is included in property and equipment and amortized accordingly.

7. FAIR VALUE OF FINANCIAL INSTRUMENTS

As of June 30, 2016, the fair values of the Company’s Level 3 financial instrument totaled \$3.7 million for 2.2 million warrants. The Level 3 financial instrument consist of common stock warrants issued by the Company in March 2011, which include features requiring liability treatment of the warrants. The fair value of warrants issued in March 2011 to purchase shares of the Company’s common stock is based on valuations performed by an independent third-party valuation firm. The fair value was determined using proprietary valuation models using the quality of the underlying securities of the warrants, restrictions on the warrants and security underlying the warrants, time restrictions and precedent sale transactions completed in the secondary market or in other private transactions. During the nine months ended March 31, 2017 all of the aforementioned warrants were exercised and the then-fair value warrant liability was reclassified as Common Stock.

The following table summarizes the changes in the Company's Level 3 financial instruments for the three and nine months ended March 31, 2017 and 2016.

| (\$ in thousands) | Three months ended March 31, | | Nine months ended March 31, | |
|---|---------------------------------|------------|--------------------------------|------------|
| | 2017 | 2016 | 2017 | 2016 |
| Beginning balance | \$ — | \$ (1,865) | \$ (3,739) | \$ (978) |
| Increase due to change in fair value of warrant liabilities | — | (4,805) | (1,490) | (5,692) |
| Reclass of fair value of warranty liability to common stock upon exercise of warrants | — | 706 | 5,229 | 706 |
| Ending balance | \$ — | \$ (5,964) | \$ — | \$ (5,964) |

There were no transfers of assets or liabilities between level 1, level 2, or level 3 during the three and nine months ended March 31, 2017 and March 31, 2016. As of March 31, 2017 and June 30, 2016, the Company held no Level 1 or Level 2 financial instruments.

8. INCOME TAXES

For the three and nine months ended March 31, 2017, income tax expense of \$209 thousand and \$94 thousand, respectively, (substantially all deferred income taxes) were recorded. The expense are based upon income before income taxes using an estimated annual effective income tax rate of 31% for the fiscal year ending June 30, 2017. The provision for the nine months ended March 31, 2017 consists of a charge for the tax effect of the change in the fair value of warrant liabilities which was treated discretely offset by a tax benefit based upon income before benefit for income taxes using the estimated annual effective income tax rate of 23% for the fiscal year ending June 30, 2017. All of those warrants were exercised as of September 30, 2016.

For the three and nine months ended March 31, 2016, an income tax benefit/(provision) of \$93 thousand and \$(88) thousand respectively, (substantially all deferred income taxes) were recorded. The benefit (provision) consist of a charge for the tax effect of the change in the fair value of warrant liabilities which was treated discretely offset by a tax benefit based upon loss before benefit (provision) for income taxes using an estimated annual effective income tax rate of 33% for the fiscal year ended June 30, 2016.

9. EQUITY

WARRANTS

During the three months ended March 31, 2017 and 2016, there were 0 and 634,100 warrants exercised. During the nine months ended March 31, 2017, 2,376,675 warrants were exercised at \$2.6058 per share yielding proceeds of \$6.2 million, and 24,733 warrants were exercised at \$2.10 per share in a cashless exercise. The following table summarizes warrant activity for the three and nine months ended March 31, 2017 and 2016:

| | Three months ended March 31, | | Nine months ended March 31, | |
|-------------------|---------------------------------|-----------|--------------------------------|-----------|
| | 2017 | 2016 | 2017 | 2016 |
| Beginning balance | 23,978 | 4,298,000 | 2,445,653 | 4,309,000 |
| Issued | — | 23,978 | — | 23,978 |
| Exercised | — | (634,100) | (2,401,408) | (645,100) |
| Expired | — | — | — | — |
| Cancelled | — | — | (20,267) | — |
| Ending balance | 23,978 | 3,687,878 | 23,978 | 3,687,878 |

STOCK OPTIONS

The Company estimates the grant date fair value of the stock options it grants using a Black-Scholes valuation model. The Company's assumption for expected volatility is based on its historical volatility data related to market trading of its own common stock. The Company bases its assumptions for expected life of the new stock option grants on the life of the option granted, and if relevant, its analysis of the historical exercise patterns of its stock options. The dividend yield assumption is based on dividends expected to be paid over the expected life of the stock option. The risk-free interest rate assumption is determined by using the U.S. Treasury rates of the same period as the expected option term of each stock option.

In August 2016 stock options were awarded to purchase up to 20,080 shares of common stock at an exercise price of \$4.98 per share. The options vest on August 31, 2017, and expire if not exercised prior to August 31, 2023. The options are intended to qualify as incentive stock options under Section 422 of the Internal Revenue Code of 1986, as amended. During the quarter ending March 31, 2017, three employees were issued the option to purchase 105,000 shares of common stock, of which 75,000 are classified as non-qualified stock options, exercisable at \$4.00 per share, and the remaining 30,000 are intended to qualify as incentive stock options, exercisable at \$4.05 per share. Of the 105,000 shares of common stock issued for the option to purchase, 95,000 shares expire on March 31, 2024 and 10,000 expire on February 6, 2024. The fair value of options granted during the nine months ended March 31, 2017 and 2016 was estimated using the following weighted average assumptions:

| | Nine months ended March 31, | |
|--|--------------------------------|---------------|
| | 2017 | 2016 |
| Expected volatility | 49 - 50 % | 59 - 66 % |
| Expected life | 3 - 4 years | 4 - 4.5 years |
| Expected dividends | — % | — % |
| Risk-free interest rate | 1.06 - 1.90 % | 1.34 - 1.49 % |
| Number of options granted | 125,080 | 194,586 |
| Weighted average exercise price | \$ 4.17 | \$ 3.21 |
| Weighted average grant date fair value | \$ 1.68 | \$ 1.64 |

Stock based compensation related to stock options for the three months ended March 31, 2017 and 2016 was \$61 thousand and \$67 thousand, respectively and \$155 thousand and \$274 thousand, respectively for the nine months ended March 31, 2017 and 2016.

COMMON STOCK

On July 1, 2016 \$40 thousand of stock grants were awarded to each non-employee Director based on the prior 30-day average closing price of the Company's Common Stock, for a total of 56,784 shares. The shares vest as follows: 18,960 on July 1, 2017, 18,960 on July 1, 2018 and 18,954 on July 1, 2019. The total expense recognized for these grants during the three and nine months ended March 31, 2017 was \$37 thousand and \$110 thousand.

During the nine months ended March 31, 2017, the Company awarded an aggregate of 78,711 shares to its Chief Executive Officer and Chief Services Officer under its fiscal year 2016 long term stock incentive plan and an aggregate of 13,771 shares to three non-employee Directors in satisfaction of board fees. During the nine-month period, the Chief Executive Officer cancelled 6,533 shares of Common Stock awarded to him under the 2016 fiscal year long term stock incentive plan in satisfaction of \$31 thousand of related payroll obligations.

During the nine months ended March 31, 2017, the Company issued an aggregate of 2,401,408 shares upon the exercise of outstanding warrants.

LTI PLANS

The Board approved the Fiscal Year 2017 Long-Term Stock Incentive Plan (the "2017 LTI Stock Plan") which provides that executive officers would be awarded shares of common stock of the Company in the event that certain metrics relating to the Company's 2017 fiscal year would result in specified ranges of year-over-year percentage growth. The metrics are total number of connections as of June 30, 2017 as compared to total number of connections as of June 30, 2016 (50%

weighting) and adjusted EBITDA earned during the 2017 fiscal year as compared to the adjusted EBITDA earned during the 2016 fiscal year (50% weighting).

If none of the minimum threshold year-over-year percentage target goals are achieved, the executive officers would not be awarded any shares. If all of the year-over-year percentage target goals are achieved, the executive officers would be awarded shares having the following value: Chief Executive Officer (“CEO”) - \$675,000 (150% of base salary), Chief Services Officer (“CSO”) - \$250,000 (100% of base salary), and Chief Financial Officer (“CFO”) - \$103,125 (75% of base salary less proration for the current fiscal year). If all of the maximum distinguished year-over-year percentage target goals are achieved, the executive officers would be awarded shares having the following value: CEO - \$1,012,500 (225% of base salary), CSO - \$375,000 (150% of base salary), and CFO - \$154,688 (112.50% of base salary less prorated for the current fiscal year). Assuming the minimum threshold year-over-year percentage target goal would be achieved for a particular metric, the number of shares to be awarded for that metric would be determined on a pro rata basis, provided that the award would not exceed the maximum distinguished award for that metric. The shares awarded under the 2017 LTI Stock Plan would vest as follows: one-third at the time of issuance; one-third on June 30, 2018; and one-third on June 30, 2019.

The Company had long-term stock incentive plans (“LTI”) in prior fiscal years for its then executive officers. Stock based compensation related to the LTI plans was as follows in the three and nine months ended March 31, 2017 and 2016:

| (\$ in thousands, except per share data) | Three months ended March 31, | | Nine months ended March 31, | |
|--|---------------------------------|--------------|--------------------------------|---------------|
| | 2017 | 2016 | 2017 | 2016 |
| FY17 LTI Plan | \$ 81 | \$ — | \$ 236 | \$ — |
| FY16 LTI Plan | 23 | 24 | 73 | 134 |
| FY15 LTI Plan | 3 | 8 | 6 | 48 |
| FY14 LTI Plan | — | 2 | — | 10 |
| Total | <u>\$ 107</u> | <u>\$ 34</u> | <u>\$ 315</u> | <u>\$ 192</u> |

10. COMMITMENTS AND CONTINGENCIES

During the nine months ended March 31, 2017 the Company entered into a lease agreement for its operations in Portland, Oregon, which commenced October 1, 2016. The new location consists of 5,362 square feet and will expire in December 2019. The lease includes monthly rental payments of \$11 thousand. The straight-line rent expense for this lease is \$11 thousand per month.

From time to time, the Company is involved in various legal proceedings arising during the normal course of business which, in the opinion of the management of the Company, will not have a material adverse effect on the Company’s financial position, results of operations or cash flows.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Forward-Looking Statements

This Form 10-Q contains certain forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, regarding, among other things, the anticipated financial and operating results of the Company. For this purpose, forward-looking statements are any statements contained herein that are not statements of historical fact and include, but are not limited to, those preceded by or that include the words, "estimate," "could," "should," "would," "likely," "may," "will," "plan," "intend," "believes," "expects," "anticipates," "projected," or similar expressions. Those statements are subject to known and unknown risks, uncertainties and other factors that could cause the actual results to differ materially from those contemplated by the statements. The forward-looking information is based on various factors and was derived using numerous assumptions. Important factors that could cause the Company's actual results to differ materially from those projected, include, for example:

- general economic, market or business conditions unrelated to our operating performance;
- the ability of the Company to raise funds in the future through sales of securities or debt financing in order to sustain its operations if an unexpected or unusual event would occur;
- the ability of the Company to compete with its competitors to obtain market share;
- whether the Company's current or future customers purchase, lease, rent or utilize ePort devices or our other products in the future at levels currently anticipated by our Company;
- whether the Company's customers continue to utilize the Company's transaction processing and related services, as our customer agreements are generally cancelable by the customer on thirty to sixty days' notice;
- the ability of the Company to satisfy its trade obligations included in accounts payable and accrued expenses;
- the ability of the Company to sell to third party lenders all or a portion of our finance receivables;
- the ability of a sufficient number of our customers to utilize third party financing companies under our QuickStart program in order to improve our net cash used by operating activities;
- the incurrence by us of any unanticipated or unusual non-operating expenses which would require us to divert our cash resources from achieving our business plan;
- the ability of the Company to predict or estimate its future quarterly or annual revenues and expenses given the developing and unpredictable market for its products;
- the ability of the Company to retain key customers from whom a significant portion of its revenues are derived;
- the ability of a key customer to reduce or delay purchasing products from the Company;
- the ability of the Company to obtain widespread commercial acceptance of its products and service offerings such as ePort QuickConnect, mobile payment and loyalty programs;
- whether any patents issued to the Company will provide the Company with any competitive advantages or adequate protection for its products, or would be challenged, invalidated or circumvented by others;
- the ability of the Company to operate without infringing the intellectual property rights of others;
- the ability of our products and services to avoid unauthorized hacking or credit card fraud;

- whether our remediation of the control deficiencies that gave rise to the material weakness that we identified in our internal controls over financial reporting, and which was reflected in our annual report on Form 10-K for the fiscal year ended June 30, 2016, would be effective or successful;
- whether we experience additional material weaknesses in our internal controls over financial reporting in the future, and are not able to accurately or timely report our financial condition or results of operations;
- whether our suppliers would increase their prices, reduce their output or change their terms of sale; and
- our ability to obtain additional financing in the future for working capital, capital expenditures, acquisitions, general corporate purposes or other purposes may be impaired.

Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance, or achievements. Actual results or business conditions may differ materially from those projected or suggested in forward-looking statements as a result of various factors including, but not limited to, those described above. We cannot assure you that we have identified all the factors that create uncertainties. Moreover, new risks emerge from time to time and it is not possible for our management to predict all risks, nor can we assess the impact of all risks on our business or the extent to which any risk, or combination of risks, may cause actual results to differ from those contained in any forward-looking statements. Readers should not place undue reliance on forward-looking statements.

Any forward-looking statement made by us in this Form 10-Q speaks only as of the date of this Form 10-Q. Unless required by law, we undertake no obligation to publicly revise any forward-looking statement to reflect circumstances or events after the date of this Form 10-Q or to reflect the occurrence of unanticipated events.

OVERVIEW OF THE COMPANY

USA Technologies, Inc. (the “Company”, “We”, “USAT”, or “Our”) was incorporated in the Commonwealth of Pennsylvania in January 1992. We are a provider of technology-enabled solutions and value-added services that facilitate electronic payment transactions primarily within the unattended Point of Sale (“POS”) market. We are a leading provider in the small ticket, beverage and food vending industry and are expanding our solutions and services to other unattended market segments, such as amusement, commercial laundry, kiosk and others. Since our founding, we have designed and marketed systems and solutions that facilitate electronic payment options, as well as telemetry Internet of Things (“IoT”) and machine-to-machine (“M2M”) services, which include the ability to remotely monitor, control, and report on the results of distributed assets containing our electronic payment solutions. Historically, these distributed assets have relied on cash for payment in the form of coins or bills, whereas, our systems allow them to accept cashless payments such as through the use of credit or debit cards or other emerging contactless forms, such as mobile payment.

The Company generates revenue in multiple ways. During the quarters ended March 31, 2017 and 2016, we derived 66.0% and 72.3% of our revenues from recurring license and transaction fees related to our ePort Connect service and 34.0% and 27.7% of our revenue from equipment sales, respectively. Connections to our service stem from the sale or lease of our POS electronic payment devices or certified payment software or the servicing of similar third-party installed POS terminals. Connections to the ePort Connect service are the most significant driver of the Company’s revenues, particularly the recurring revenues from license and transaction fees. Customers can obtain POS electronic payment devices from us in the following ways:

- Purchasing devices directly from the Company or one of its authorized resellers;
- Financing devices under the Company’s QuickStart Program, which are non-cancellable sixty month sales-type leases, through an unrelated equipment financing company, if available, or directly from the Company; and
- Renting devices under the Company’s JumpStart Program, which are cancellable month-to-month operating leases.

Highlights of the Company are below:

- Over 88 employees with its headquarters in Malvern, Pennsylvania;

- Over 12,400 customers and 504,000 connections to our service;
- Three direct sales teams at the national, regional, and local customer-level and a growing number of OEMs and national distribution partners;
- 77 United States and foreign patents are in force;
- The Company's fiscal year ends June 30th; and
- The Company has traded on the NASDAQ under the symbol "USAT" since 2007.

The Company has deferred tax assets of approximately \$27.6 million resulting from a series of operating loss carry forwards that may be available to offset future taxable income from federal income taxes over the next five or more years.

CRITICAL ACCOUNTING POLICIES

Our consolidated financial statements are prepared applying certain critical accounting policies. The Securities and Exchange Commission ("SEC") defines "critical accounting policies" as those that require application of management's most difficult, subjective, or complex judgments. Critical accounting policies require numerous estimates and strategic or economic assumptions that may prove inaccurate or subject to variations and may significantly affect our reported results and financial position for the period or in future periods. Changes in underlying factors, assumptions, or estimates in any of these areas could have a material impact on our future financial condition and results of operations. Our financial statements are prepared in accordance with U.S. GAAP, and they conform to general practices in our industry. We apply critical accounting policies consistently from period to period and intend that any change in methodology occur in an appropriate manner. Accounting policies currently deemed critical are listed below:

Revenue Recognition

Revenue from the sale or QuickStart lease of equipment is recognized on the terms of freight-on-board shipping point. Activation fee revenue, if applicable, is recognized when the Company's cashless payment device is initially activated for use on the Company network. Transaction processing revenue is recognized upon the usage of the Company's cashless payment and control network. License fees for access to the Company's devices and network services are recognized on a monthly basis. In all cases, revenue is only recognized when persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the price is fixed and determinable, and collection of the resulting receivable is reasonably assured. The Company estimates an allowance for product returns at the date of sale and license and transaction fee refunds on a monthly basis. The company makes an adjustment for rebates and product returns.

ePort hardware is available to customers under the QuickStart program pursuant to which the customer would enter into a five-year non-cancelable lease with either the Company or a third-party financing company for the devices. The Company utilizes its best estimate of selling price when calculating the revenue to be recorded under these leases. The leases qualify for sales type lease accounting. Accordingly, the Company recognizes a portion of lease payments as interest income for leases not placed with a third-party financing company. At the end of the lease period, the customer would have the option to purchase the device at its residual value.

Long Lived Assets

In accordance with ASC 360, "Impairment or Disposal of Long-Lived Assets", the Company reviews its definite lived long-lived assets whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. If the carrying amount of an asset or group of assets exceeds its net realizable value, the asset will be written down to its fair value. In the period when the plan of sale criteria of ASC 360 are met, definite lived long-lived assets are reported as held for sale, depreciation and amortization cease, and the assets are reported at the lower of carrying value or fair value less costs to sell.

Goodwill and Intangible Assets

Goodwill represents the excess of cost over fair value of the net assets purchased in acquisitions. The Company accounts for goodwill in accordance with ASC 350, “Intangibles – Goodwill and Other”. Under ASC 350, goodwill is not amortized to earnings, but instead is subject to periodic testing for impairment. Testing for impairment is to be done at least annually and at other times if events or circumstances arise that indicate that impairment may have occurred. The Company has selected April 1 as its annual test date.

Non-compete agreements, brand, developed technology, and customer relationships, with an estimated economic life, are carried at cost less accumulated amortization, which is calculated on a straight-line basis over their estimated economic life. The Company reviews intangibles, subject to amortization, for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

Allowance for Doubtful Accounts

The Company maintains an allowance for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments, including from a shortfall in the customer transaction fund flow from which the Company would normally collect amounts due.

The allowance is determined through an analysis of various factors including the aging of the accounts receivable, the strength of the relationship with the customer, the capacity of the customer transaction fund flow to satisfy the amount due from the customer, an assessment of collection costs and other factors. The allowance for doubtful accounts receivable is management’s best estimate as of the respective reporting date. The Company writes off accounts receivable against the allowance when management determines the balance is uncollectible and the Company ceases collection efforts. Management believes that the allowance recorded is adequate to provide for its estimated credit losses.

HIGHLIGHTS FOR THE THREE MONTHS ENDED MARCH 31, 2017 AND MARCH 31, 2016 INCLUDE:

| <i>(Connections and \$'s in thousands, transactions in millions, eps is not rounded)</i> | As of and for the three months ended March 31, | | Change | % Change |
|--|---|------------------|-----------------|--------------|
| | 2017 | 2016 | | |
| Revenues: | | | | |
| License and transaction fees | \$ 17,459 | \$ 14,727 | \$ 2,732 | 18.6% |
| Equipment sales | 9,001 | 5,634 | 3,367 | 59.8% |
| Total revenues | \$ 26,460 | \$ 20,361 | \$ 6,099 | 30.0% |
| License and transaction fee margin | 32.0% | 34.1% | (2.1%) | |
| Equipment sales gross margin | 11.6% | 11.5% | 0.1% | |
| Overall Gross Margin | 25.0% | 27.9% | (2.9%) | |
| Operating income/(loss) | \$ 419 | \$ (595) | \$ 1,014 | 170.4% |
| Net income/(loss) | \$ 136 | \$ (5,420) | \$ 5,556 | 102.5% |
| Net loss per common shares - basic and diluted | \$ (0.00) | \$ (0.16) | \$ 0.16 | 100.0% |
| Net cash provided by (used in) operating activities | \$ 848 | \$ 4,328 | \$ (3,480) | (80.4%) |
| Net New Connections | 35,000 | 32,000 | 3,000 | 9.4% |
| Total Connections (at period end) | 504,000 | 401,000 | 103,000 | 25.7% |
| Total Number of Transactions (millions) | 104.9 | 82.0 | 22.9 | 27.9% |
| Transaction Volume (millions) | \$ 202.5 | \$ 151.0 | \$ 51.5 | 34.1% |
| Adjusted EBITDA | \$ 1,862 | \$ 1,347 | \$ 515 | 38.2% |
| Non-GAAP net income | \$ 345 | \$ (87) | \$ 432 | 496.6% |

HIGHLIGHTS FOR THE NINE MONTHS ENDED MARCH 31, 2017 AND MARCH 31, 2016 INCLUDE:

| <i>(Connections and \$'s in thousands, transactions in millions, eps is not rounded)</i> | As of and for the nine months ended March 31, | | | |
|--|--|------------------|------------------|--------------|
| | 2017 | 2016 | Change | % Change |
| Revenues: | | | | |
| License and transaction fees | \$ 50,463 | \$ 41,326 | \$ 9,137 | 22.1% |
| Equipment sales | 19,341 | 14,138 | 5,203 | 36.8% |
| Total revenues | \$ 69,804 | \$ 55,464 | \$ 14,340 | 25.9% |
| License and transaction fee margin | 31.6% | 33.5% | (1.9%) | |
| Equipment sales gross margin | 16.4% | 16.6% | (0.2%) | |
| Overall Gross Margin | 27.4% | 29.2% | (1.8%) | |
| Operating (loss)/income | \$ (297) | \$ 111 | \$ (408) | (367.6%) |
| Net loss | \$ (2,095) | \$ (5,934) | \$ 3,839 | 64.7% |
| Net loss per common shares - basic and diluted | \$ (0.07) | \$ (0.18) | \$ 0.11 | 61.1% |
| Net cash provided by (used in) operating activities | \$ (4,295) | \$ 5,197 | \$ (9,492) | (182.6%) |
| Net New Connections | 75,000 | 68,000 | 7,000 | 10.3% |
| Total Connections (at period end) | 504,000 | 401,000 | 103,000 | 25.7% |
| Total Number of Transactions (millions) | 300.2 | 227.2 | 73.0 | 32.1% |
| Transaction Volume (millions) | \$ 577.3 | \$ 415.7 | \$ 161.6 | 38.9% |
| Adjusted EBITDA | \$ 4,297 | \$ 5,358 | \$ (1,061) | (19.8%) |
| Non-GAAP net (loss) income | \$ (369) | \$ 660 | \$ (1,029) | (155.9%) |

TRENDING QUARTERLY FINANCIAL DATA

The following tables show certain financial and non-financial data over a five-quarter period that management believes give readers insight into certain trends and relationships about the Company's financial performance.

Table 1: Five Quarters of Select Key Performance Indicators

Five Quarter Connections & Other Data

| | As of and for the three months ended | | | | |
|--|--------------------------------------|----------------------|-----------------------|------------------|-------------------|
| | March 31, 2017 | December 31, 2016 | September 30, 2016 | June 30, 2016 | March 31, 2016 |
| Connections: | | | | | |
| Gross New Connections | 40,000 | 25,000 | 22,000 | 33,000 | 34,000 |
| % from Existing Customer Base | 88% | 80% | 86% | 83% | 91% |
| Net New Connections | 35,000 | 21,000 | 19,000 | 28,000 | 32,000 |
| Total Connections | 504,000 | 469,000 | 448,000 | 429,000 | 401,000 |
| Customers: | | | | | |
| New Customers Added | 500 | 500 | 350 | 300 | 125 |
| Total Customers | 12,400 | 11,900 | 11,400 | 11,050 | 10,750 |
| Volumes: | | | | | |
| Total Number of Transactions (millions) | 104.9 | 100.1 | 95.1 | 89.3 | 82.1 |
| Transaction Volume (millions) | \$ 202.5 | \$ 191.5 | \$ 183.4 | \$ 169.0 | \$ 151.0 |
| Financing Structure of Connections: | | | | | |
| JumpStart | 8.6% | 6.8% | 7.7% | 6.5% | 7.4% |
| QuickStart & All Others * | 91.4% | 93.2% | 92.3% | 93.5% | 92.6% |
| Total | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% |

* Includes credit sales with standard trade receivable terms

Highlights of USAT's connections for the quarter ended March 31, 2017 include:

- 35,000 net new connections to our ePort Connect service in the quarter; and
- 504,000 connections to the ePort Connect service compared to the same quarter last year of approximately 401,000 connections, an increase of 103,000 connections, or 25.7%.

Table 2: Quarter Ended March 31, 2017 compared to Quarter Ended March 31, 2016

| (\$ in thousands, except shares and per share data) | For the three months ended March 31, | | | | Change | % Change |
|--|--------------------------------------|------------|------------|------------|-----------|----------|
| | 2017 | % of Sales | 2016 | % of Sales | | |
| Revenues: | | | | | | |
| License and transaction fees | \$ 17,459 | 66.0% | \$ 14,727 | 72.3% | \$ 2,732 | 18.6% |
| Equipment sales | 9,001 | 34.0% | 5,634 | 27.7% | 3,367 | 59.8% |
| Total revenues | 26,460 | 100.0% | 20,361 | 100.0% | 6,099 | 30.0% |
| Costs of sales/revenues: | | | | | | |
| Cost of services | 11,876 | 68.0% | 9,703 | 65.9% | 2,173 | 22.4% |
| Cost of equipment | 7,959 | 88.4% | 4,986 | 88.5% | 2,973 | 59.6% |
| Total costs of sales/revenues | 19,835 | 75.0% | 14,689 | 72.1% | 5,146 | 35.0% |
| Gross profit | 6,625 | 25.0% | 5,672 | 27.9% | 953 | 16.8% |
| Operating expenses: | | | | | | |
| Selling, general and administrative | 5,947 | 22.5% | 6,094 | 29.9% | (147) | (2.4%) |
| Depreciation and amortization | 259 | 1.0% | 173 | 0.8% | 86 | 49.7% |
| Total operating expenses | 6,206 | 23.5% | 6,267 | 30.8% | (61) | (1.0%) |
| Operating income (loss) | 419 | 1.6% | (595) | (2.9%) | 1,014 | (170.4%) |
| Other income (expense): | | | | | | |
| Interest income | 114 | 0.4% | 67 | 0.3% | 47 | 70.1% |
| Interest expense | (188) | (0.7%) | (180) | (0.9%) | (8) | (4.4%) |
| Change in fair value of warrant liabilities | — | 0.0% | (4,805) | (23.6%) | 4,805 | 100.0% |
| Total other expense, net | (74) | (0.3%) | (4,918) | (24.2%) | 4,844 | (98.5%) |
| Income (loss) before income taxes | 345 | 1.3% | (5,513) | (27.1%) | 5,858 | 106.3% |
| (Provision) benefit for income taxes | (209) | (0.8%) | 93 | 0.5% | (302) | 324.7% |
| Net income (loss) | 136 | 0.5% | (5,420) | (26.6%) | 5,556 | 102.5% |
| Cumulative preferred dividends | (334) | (1.3%) | (334) | (1.6%) | — | 0.0% |
| Net loss applicable to common shares | \$ (198) | (0.7%) | \$ (5,754) | (28.3%) | \$ 5,556 | 96.6% |
| Net loss per common share - basic and diluted | \$ (0.00) | | \$ (0.16) | | \$ 0.16 | 100.0% |
| Basic and diluted weighted average number of common shares outstanding | 40,327,697 | | 36,161,626 | | 4,166,071 | 11.5% |

Revenue. The increase in net new connections of approximately 35,000 for the three months ended March 31, 2017 compared to approximately 32,000 in the same period last year represents an increase of 9.4%. The Company's total connections have grown to 504,000 at March 31, 2017 compared to 401,000 at March 31, 2016, or a 25.7% increase year-over-year. The increase in total connections is driving the growth in license and transaction fees of 18.6% quarter-over-quarter. The increase in equipment revenue is due to more units sold during the three-month period ended March 31, 2017 compared to the same period last year.

Gross Margin. License and transaction fees gross margin for the three-month period ended March 31, 2017 decreased to 32.0% from the gross margin of 34.1% during the three-month period ended March 31, 2016. The decrease in license and transaction gross margin is attributable to, among other things, reduced fees periodically extended to customers who offer strategic and/or large market opportunities.

Equipment gross margins increased from 11.5% for the three-month period ended March 31, 2016 to 11.6% for the three-month period ended March 31, 2017. The increase in equipment gross margin is primarily attributable to cost reductions with respect to our products during the three-month period ended March 31, 2017 as compared to the quarter end March 31, 2016.

Operating Expenses. Operating expenses decreased \$61 thousand or 1.0% for the three-month period ended March 31, 2017 compared to the prior period in 2016, representing 23.5% and 30.8% of sales, respectively. The \$86 thousand increase in depreciation and amortization is primarily due to the assets acquired in the VendScreen acquisition. As reflected in

Table 5 below, our SG&A expense for the March 31, 2017 quarter was approximately \$0.1 million less than our SG&A expense for the March 31, 2016 quarter, representing 22.5% and 29.9% of sales, respectively.

Total Other Income (Expense). Total Other Income (Expense) includes interest expense, other income, and the change in the fair value of warrants. The primary driver for volatility in Other Income / (Expense) has been non-cash changes to the fair value of the warrant liabilities which are based on the Company's stock price. Using the Black-Scholes model, the Company adjusts the warrant liability for fair value through the income statement quarterly. For the three-month period ended March 31, 2017, the Company did not record any expense for the change in the fair value of warrant liabilities compared to recording an expense of \$4.8 million for the three months ended March 31, 2016. As the warrants giving rise to the warrant liability were exercised in September 2016, there was no such liability recorded in the March 31, 2017 quarter.

Net Income (Loss). Net income (loss) is a function of the items described above. Net income for the quarter end March 31, 2017 was \$0.1 million compared to net loss of \$5.4 million for the comparable period a year ago. The primary reason for the difference in net income (loss) was the warrant liability charge taken during the quarter ended March 31, 2016. The Company earned (\$0.00) per share during the quarter as compared to a loss of (\$0.16) per share during the prior corresponding quarter.

Adjusted EBITDA. For the three months ended March 31, 2017, adjusted EBITDA increased to \$1.9 million from \$1.3 million for the quarter ended March 31, 2016. The increase was primarily due to the net income earned during the quarter ended March 31, 2017 as compared to the net loss incurred during the prior corresponding quarter adjusted for the fair value of the warrant liabilities.

Non-GAAP Net Income (Loss). Non-GAAP net income increased to \$0.3 million for the three months ended March 31, 2017 compared to a Non-GAAP net loss of \$0.1 million for the quarter ended March 31, 2016. The increase was primarily due to the net income earned during the quarter ended March 31, 2017 as compared to the net loss incurred during the prior corresponding quarter adjusted for the fair value of the warrant liabilities. an increase in gross profit.

Weighted Average Shares Outstanding. The increase in the weighted average number of common shares was due to exercises of warrants and to stock issued pursuant to the Company's stock compensation programs.

Table 3: Nine Months Ended March 31, 2017 compared to the Nine Months Ended March 31, 2016

| (\$ in thousands, except shares and per share data) | For the nine months ended March 31, | | | | Change | % Change |
|---|-------------------------------------|---------------|-------------------|----------------|------------------|-----------------|
| | 2017 | % of Sales | 2016 | % of Sales | | |
| Revenues: | | | | | | |
| License and transaction fees | \$ 50,463 | 72.3% | \$ 41,326 | 74.5% | \$ 9,137 | 22.1% |
| Equipment sales | 19,341 | 27.7% | 14,138 | 25.5% | 5,203 | 36.8% |
| Total revenues | 69,804 | 100.0% | 55,464 | 100.0% | 14,340 | 25.9% |
| Costs of sales/revenues: | | | | | | |
| Cost of services | \$ 34,508 | 68.4% | \$ 27,475 | 66.5% | 7,033 | 25.6% |
| Cost of equipment | 16,170 | 83.6% | 11,787 | 83.4% | 4,383 | 37.2% |
| Total costs of sales/revenues | 50,678 | 72.6% | 39,262 | 70.8% | 11,416 | 29.1% |
| Gross profit | 19,126 | 27.4% | 16,202 | 29.2% | 2,924 | 18.0% |
| Operating expenses: | | | | | | |
| Selling, general and administrative | 18,649 | 26.7% | 15,652 | 28.2% | 2,997 | 19.1% |
| Depreciation and amortization | 774 | 1.1% | 439 | 0.8% | 335 | 76.3% |
| Total operating expenses | 19,423 | 27.8% | 16,091 | 29.0% | 3,332 | 20.7% |
| Operating (loss) income | (297) | (0.4%) | 111 | 0.2% | (408) | (367.6%) |
| Other income (expense): | | | | | | |
| Interest income | 387 | 0.6% | 138 | 0.2% | 249 | 180.4% |
| Interest expense | (601) | (0.9%) | (403) | (0.7%) | (198) | (49.1%) |
| Change in fair value of warrant liabilities | (1,490) | (2.1%) | (5,692) | (10.3%) | 4,202 | 73.8% |
| Total other expense, net | (1,704) | (2.4%) | (5,957) | (10.7%) | 4,253 | 71.4% |
| (Loss) before income taxes | (2,001) | (2.9%) | (5,846) | (10.5%) | 3,845 | 65.8% |
| Provision for income taxes | (94) | (0.1%) | (88) | (0.2%) | (6) | (6.8%) |
| Net loss | (2,095) | (3.0%) | (5,934) | (10.7%) | 3,839 | 64.7% |
| Cumulative preferred dividends | (668) | (1.0%) | (668) | (1.2%) | — | 0.0% |
| Net loss applicable to common shares | (2,763) | (4.0%) | (6,602) | (11.9%) | \$ 3,839 | 58.1% |
| Net loss per common share - basic and diluted | (0.07) | | (0.18) | | \$ 0.11 | 61.1% |
| Basic and diluted weighted average number of common shares outstanding | 39,703,690 | | 35,972,633 | | 3,731,057 | 10.4% |

Revenue. The Company's total connections have grown to 504,000 at March 31, 2017 compared to 401,000 at March 31, 2016, or a 25.7% increase year-over-year. The increase in total connections is driving the growth in license and transaction fees of 22.1% year over year.

Gross Margin. License and transaction fees gross margin for the nine months ended March 31, 2017 decreased to 31.6% from the gross margin of 33.5% during the nine months ended March 31, 2016. The decrease in license and transaction gross margin is attributable to, among other things, reduced fees periodically extended to customers who offer strategic and/or large market opportunities.

Equipment gross margin decreased slightly from 16.6% for the nine-month period ended March 31, 2016 to 16.4% for the nine-month period ended March 31, 2017. The decrease in gross margin on a year-to-date basis is primarily attributable to reduced pricing periodically extended to customers who offer strategic and/or large market opportunities.

Operating Expenses. Operating expenses increased \$3.3 million or 20.7% for the nine-month period ended March 31, 2017 compared to the prior period in fiscal year 2016. The \$2.4 million increase of professional services is attributable to SOX 404 compliance, internal audit, and audit of our financial statements driven primarily by our status as a first time accelerated filer which required an audit of our annual SOX 404 assessment. The \$0.8 million increase in salaries and benefits increase is due to employee compensation, headcount and employee related medical benefits. The \$0.3 million increase in premises, equipment and insurance costs is due to increasing rent expense for leased properties and employer business insurance. The \$0.4 million increase in marketing related expenses is due to marketing and customer promotions.

Total operating expenses as a percentage of sales decreased for the nine months ended March 31, 2017 to 27.8% compared to 29.0% for the nine months ended March 31, 2016.

Total Other Income (Expense). Total Other Income (Expense) includes interest expense, other income, and the change in the fair value of warrants. The primary driver for volatility in Other Income / (Expense) has been non-cash changes to the fair value of the warrant liabilities which are based on the Company's stock price. Using the Black-Scholes model, the Company adjusts the warrant liability for fair value through the income statement quarterly. For the nine months ended March 31, 2017, the Company recorded a \$1.5 million expense for the change in the fair value of warrant liabilities (all attributable to the quarter ended September 30, 2016) compared to the \$5.7 million expense for the nine months ended March 31, 2016. As the warrants associated with the liability were exercised in September 2016, there will be no fair value expense recorded in subsequent periods.

Net Loss. Net loss is a function of the items described above. Net loss for the nine months ended March 31, 2017 was \$2.1 million compared to a net loss of \$5.9 million for the comparable period a year ago. The Company lost (\$0.07) per share during the nine month period as compared to a loss of (\$0.18) per share during the prior corresponding nine month period.

Adjusted EBITDA. For the nine months ended March 31, 2017, adjusted EBITDA decreased to \$4.3 million from \$5.4 million for the nine months ended March 31, 2016 or 19.8%. The decrease was primarily due to increased adjustments made for VendScreen non-recurring charges and litigation related professional fees during the prior corresponding nine month period as well as favorable comparable operating results for the prior corresponding nine month period after adjustment for the warrant liabilities.

Non-GAAP Net Income (Loss). Non-GAAP net loss decreased to (\$0.4) million for the nine months ended March 31, 2017 compared to non-GAAP net income for the nine months ended March 31, 2016 of \$0.7 million. The decrease was primarily due to increased adjustments made for VendScreen non-recurring charges and litigation related professional fees during the prior corresponding nine month period as well as favorable comparable operating results for the prior corresponding nine month period after adjustment for the warrant liabilities.

Weighted Average Shares Outstanding. The increase in the weighted average number of common shares was due to exercises of warrants and to stock issued pursuant to the Company's stock compensation programs.

Table 4: Reconciliation of Net Income (Loss) to Adjusted EBITDA:

| (\$ in thousands) | Three months ended March 31, | | Nine months ended March 31, | |
|---|---------------------------------|------------|--------------------------------|------------|
| | 2017 | 2016 | 2017 | 2016 |
| Net income (loss) | \$ 136 | \$ (5,420) | \$ (2,095) | \$ (5,934) |
| Less interest income | (114) | (67) | (387) | (138) |
| Plus interest expenses | 188 | 180 | 601 | 403 |
| Plus income tax provision / (Less income tax benefit) | 209 | (93) | 94 | 88 |
| Plus depreciation expense | 1,165 | 1,190 | 3,642 | 3,863 |
| Plus amortization expense | 45 | 44 | 132 | 44 |
| EBITDA | 1,629 | (4,166) | 1,987 | (1,674) |
| Plus loss on fair value of warrant liabilities / (Less gain on fair value of warrant liabilities) | — | 4,805 | 1,490 | 5,692 |
| Plus stock-based compensation | 233 | 142 | 678 | 651 |
| Plus VendScreen non-recurring charges | — | 461 | 109 | 584 |
| Plus Litigation related professional fees | — | 105 | 33 | 105 |
| Adjustments to EBITDA | 233 | 5,513 | 2,310 | 7,032 |
| Adjusted EBITDA | \$ 1,862 | \$ 1,347 | \$ 4,297 | \$ 5,358 |

As used herein, Adjusted EBITDA represents net income (loss) before interest income, interest expense, income taxes, depreciation, amortization, non-recurring fees and charges that were incurred in connection with the integration of the

VendScreen business, change in fair value of warrant liabilities and stock-based compensation expense. We have excluded the non-operating item, change in fair value of warrant liabilities, because it represents a non-cash gain or charge that is not related to the Company's operations. We have excluded the non-cash expense, stock-based compensation, as it does not reflect the cash-based operations of the Company. We have excluded the non-recurring costs and expenses incurred in connection with the VendScreen transaction in order to allow more accurate comparison of the financial results to historical operations. Adjusted EBITDA is a non-GAAP financial measure which is not required by or defined under GAAP (Generally Accepted Accounting Principles). The presentation of this financial measure is not intended to be considered in isolation or as a substitute for the financial measures prepared and presented in accordance with GAAP, including the net income or net loss of the Company or net cash used in operating activities. Management recognizes that non-GAAP financial measures have limitations in that they do not reflect all of the items associated with the Company's net income or net loss as determined in accordance with GAAP, and are not a substitute for or a measure of the Company's profitability or net earnings. Adjusted EBITDA is presented because we believe it is useful to investors as a measure of comparative operating performance. Additionally, the Company utilizes Adjusted EBITDA as a metric in its executive officer and management incentive compensation plans.

Table 5: Selling General & Administrative (SG&A) Expenses

| (\$ in thousands) | March 31, 2017 | | December 31, 2016 | | September 30, 2016 | | June 30, 2016 | | March 31, 2016 | |
|--|----------------|-----------|-------------------|-----------|--------------------|-----------|---------------|-----------|----------------|-------|
| | % of SG&A | % of SG&A | % of SG&A | % of SG&A | % of SG&A | % of SG&A | % of SG&A | % of SG&A | % of SG&A | |
| Salaries and benefit costs | \$ 3,060 | 51.5% | \$ 2,849 | 49.2% | \$ 3,129 | 45.3% | \$ 3,050 | 45.4% | \$ 2,760 | 45.4% |
| Marketing related expenses | 569 | 9.6% | 578 | 10.0% | 329 | 4.8% | 635 | 9.4% | 362 | 5.9% |
| Professional services | 1,472 | 24.8% | 1,213 | 20.9% | 2,520 | 36.5% | 1,533 | 22.8% | 1,152 | 18.9% |
| Bad debt expense | 127 | 2.0% | 352 | 6.1% | 97 | 1.3% | 470 | 7.0% | 505 | 8.3% |
| Premises, equipment and insurance costs | 482 | 8.1% | 498 | 8.6% | 499 | 7.2% | 555 | 8.3% | 460 | 7.5% |
| Research and development expenses | 95 | 1.6% | 173 | 3.0% | 124 | 1.8% | 123 | 1.8% | 131 | 2.1% |
| VendScreen non-recurring charges | — | 0.0% | 8 | 0.1% | 101 | 1.5% | 258 | 3.8% | 461 | 7.6% |
| Litigation related professional fees | — | 0.0% | — | 0.0% | 33 | 0.5% | 51 | 0.8% | 105 | 1.7% |
| Other expenses | 142 | 2.4% | 122 | 2.1% | 77 | 1.1% | 46 | 0.7% | 158 | 2.6% |
| Total SG&A expenses | \$ 5,947 | 100% | \$ 5,793 | 100% | \$ 6,909 | 100% | \$ 6,721 | 100% | \$ 6,094 | 100% |
| Total Revenue | \$ 26,460 | | \$ 21,756 | | \$ 21,588 | | \$ 21,944 | | \$ 20,361 | |
| SG&A expenses as a percentage of revenue | 22.5% | | 26.6% | | 32.0% | | 30.6% | | 29.9% | |

Salaries and Benefit Costs. Includes employee compensation and benefits, directors' fees, cash incentive bonus plans, and stock-based compensation. The increase in cost for the three months ended March 31, 2017 compared to three months ended December 31, 2016, related to an increase in employee headcount as we continue to expand our operations offset by a decrease in the bonus accrual during the three-months ended March 31, 2017 as compared to the December 31, 2016 quarter.

Marketing Related expenses. Marketing related costs include marketing activities and customer promotions.

Professional Services. Includes information technology, legal, public relations, auditing, SOX 404 and other consulting work. Professional service expense during the March 31, 2017 quarter increased by approximately \$0.3 million from the professional service expense during the December 31, 2016 quarter, reflecting increases in SOX 404 compliance costs.

Bad Debt expense. Provision for bad debt reflects the most current assessment of reserves required.

Premises, equipment and insurance costs. Includes facilities, supplies, printing and postage, sales and use taxes, and workers' compensation.

Research and development expenses. Includes product development costs that cannot be capitalized, including materials and contractors. Research and development costs decreased for the three-month period ended March 31, 2017 compared to the three-month period ended December 31, 2016 due to an increase in our capitalized production costs.

VendScreen Non-recurring charges. Reflects professional fees incurred in connection with the VendScreen integration.

Litigation related professional fees. Includes legal and other professional fees incurred in connection with the class action litigation as well as the investigation conducted by the Special Litigation Committee of the Board of Directors described in our Form 10-K for the 2016 fiscal year (the "SLC Investigation").

Other expenses. Includes bank fees, recruiting expenses, non-inventory supplies, subscriptions, and the gain or loss on the disposal of assets.

| (\$ in thousands) | Nine months ended | | | |
|--|-------------------|---------------|-------------------|---------------|
| | March 31, 2017 | % of SG&A | March 31, 2016 | % of SG&A |
| Salaries and benefit costs | \$ 9,038 | 48.5% | \$ 8,231 | 52.6% |
| Marketing related expenses | 1,476 | 7.9% | 1,030 | 6.6% |
| Professional services | 5,205 | 27.9% | 2,773 | 17.7% |
| Bad debt expense | 576 | 3.1% | 980 | 6.3% |
| Premises, equipment and insurance costs | 1,479 | 7.9% | 1,206 | 7.7% |
| Research and development expenses | 392 | 2.1% | 359 | 2.3% |
| VendScreen non-recurring charges | 109 | 0.6% | 584 | 3.7% |
| Litigation related professional fees | 33 | 0.2% | 105 | 0.7% |
| Other expenses | 341 | 1.8% | 384 | 2.4% |
| Total SG&A expenses | <u>\$ 18,649</u> | <u>100.0%</u> | <u>\$ 15,652</u> | <u>100.0%</u> |
| Total Revenue | \$ 69,804 | | \$ 55,464 | |
| SG&A expenses as a percentage of revenue | 26.7% | | 28.2% | |

Salaries and Benefit Costs. Includes employee compensation and benefits, directors' fees, incentives, and stock-based compensation. The increase in cost for the nine months ended March 31, 2017, related to increases in employee compensation, headcount (primarily due to the VendScreen acquisition), and employee health benefits.

Marketing Related expenses. Marketing related costs increased due to marketing activities and customer promotions.

Professional Services. Includes information technology, legal, public relations, auditing, SOX 404 and other consulting work. The increase for the nine months ended March 31, 2017 is related to SOX 404 compliance, internal audit, and audit of our financial statements driven primarily by our status as a first time accelerated filer which required an audit of our annual SOX 404 assessment.

Bad Debt expense. Provision for bad debt reflects the most current assessment of reserves required.

Premises, equipment and insurance costs. Includes facilities, supplies, printing and postage, sales and use taxes, and workers' compensation. The increase for the nine months ended March 31, 2017 compared to the same period in 2016 is primarily attributable to increases in rent expense reflecting the addition of the Portland, Oregon office in January 2016 and the new lease agreement for the Malvern, Pennsylvania office.

Research and development expenses. Includes product development costs that cannot be capitalized, including materials and contractors.

Vendscreen Non-recurring charges. Reflects professional fees incurred in connection with the VendScreen integration.

Litigation related professional fees. Includes legal and other professional fees incurred in connection with the class action litigation as well as the SLC Investigation.

Other expenses. Includes bank fees, recruiting expenses, non-inventory supplies, and subscriptions.

Table 6: Non-GAAP Income (Loss) per Share

| (\$ in thousands) | Three months ended March 31, | | Nine months ended March 31, | |
|--|---------------------------------|------------|--------------------------------|------------|
| | 2017 | 2016 | 2017 | 2016 |
| Net income (loss) | \$ 136 | \$ (5,420) | \$ (2,095) | \$ (5,934) |
| Non-GAAP adjustments: | | | | |
| Non-cash portion of income tax provision | 209 | (38) | 94 | 213 |
| Fair value of warrant adjustment | — | 4,805 | 1,490 | 5,692 |
| VendScreen non-recurring charges | — | 461 | 109 | 584 |
| Litigation related professional fees | — | 105 | 33 | 105 |
| Non-GAAP net income (loss) | \$ 345 | \$ (87) | \$ (369) | \$ 660 |
| Net income (loss) | \$ 136 | \$ (5,420) | \$ (2,095) | \$ (5,934) |
| Cumulative preferred dividends | (334) | (334) | (668) | (668) |
| Net income (loss) applicable to common shares | \$ (198) | \$ (5,754) | \$ (2,763) | \$ (6,602) |
| Non-GAAP net income (loss) | \$ 345 | \$ (87) | \$ (369) | \$ 660 |
| Cumulative preferred dividends | (334) | (334) | (668) | (668) |
| Non-GAAP net income (loss) applicable to common shares | \$ 11 | \$ (421) | \$ (1,037) | \$ (8) |
| Net income (loss) per common share - basic and diluted | \$ (0.00) | \$ (0.16) | \$ (0.07) | \$ (0.18) |
| Non-GAAP net income (loss) per common share - basic and diluted | \$ 0.00 | \$ (0.01) | \$ (0.03) | \$ (0.00) |
| Basic and diluted weighted average number of common shares outstanding | 40,327,697 | 36,161,626 | 39,703,690 | 35,972,633 |

The increase in the weighted average number of common shares was due to exercises of warrants and to stock issued through the Company's stock compensation programs.

As used herein, non-GAAP net income (loss) represents GAAP (Generally Accepted Accounting Principles) net income (loss) excluding costs or benefits relating to any adjustment for fair value of warrant liabilities and non-cash portions of the Company's income tax benefit (provision), non-recurring fees and charges that were incurred in connection with the integration of the VendScreen business, and professional fees incurred in connection with the class action litigation and the SLC Investigation. Non-GAAP net earnings (loss) per common share - diluted is calculated by dividing non-GAAP net income (loss) applicable to common shares by the number of diluted weighted average shares outstanding. Management believes that non-GAAP net income (loss) is an important measure of USAT's business. Non-GAAP net income (loss) is a non-GAAP financial measure which is not required by or defined under GAAP. The presentation of this financial measure is not intended to be considered in isolation or as a substitute for the financial measures prepared and presented in accordance with GAAP, including the net income or net loss of the Company or net cash used in operating activities. Management recognizes that non-GAAP financial measures have limitations in that they do not reflect all of the items associated with the Company's net income or net loss as determined in accordance with GAAP, and are not a substitute for or a measure of the Company's profitability or net earnings. Management believes that non-GAAP net income (loss) and non-GAAP net earnings (loss) per share are important measures of the Company's business. Management uses the aforementioned non-GAAP measures to monitor and evaluate ongoing operating results and trends and to gain an understanding of our comparative operating performance. We believe that this non-GAAP financial measure serves as a useful metric for our management and investors because they enable a better understanding of the long-term performance of our core business and facilitate comparisons of our operating results over multiple periods, and when taken together with the corresponding GAAP financial measures and our reconciliations, enhance investors' overall understanding of our current and future financial performance. Additionally, the Company utilizes non-GAAP net income (loss) as a metric in its executive officer and management incentive compensation plans.

Table 7: Balance Sheet as of March 31, 2017 Compared to June 30, 2016

| (\$ in thousands) | March 31, 2017 | June 30, 2016 | Change | % Change |
|--|-------------------|------------------|-----------------|----------------|
| Assets | | | | |
| Current assets: | | | | |
| Cash and Cash Equivalents | \$ 17,780 | \$ 19,272 | \$ (1,492) | (7.7%) |
| Accounts receivable, less allowance for doubtful accounts of \$2,851 and \$2,814, respectively | 6,734 | 4,899 | 1,835 | 37.5% |
| Finance receivables, less allowance for credit losses of \$25 and \$0, respectively | 2,057 | 3,588 | (1,531) | (42.7%) |
| Inventory, net | 4,147 | 2,031 | 2,116 | 104.2% |
| Prepaid expenses and other current assets | 1,628 | 987 | 641 | 64.9% |
| Deferred income taxes | 2,271 | 2,271 | — | — |
| Total current assets | 34,617 | 33,048 | 1,569 | 4.7% |
| Finance receivables, less current portion | 7,548 | 3,718 | 3,830 | 103.0% |
| Other assets | 137 | 348 | (211) | (60.6%) |
| Property and equipment, net | 9,173 | 9,765 | (592) | (6.1%) |
| Deferred income taxes | 25,359 | 25,453 | (94) | (0.4%) |
| Intangibles, net | 666 | 798 | (132) | (16.5%) |
| Goodwill | 11,492 | 11,703 | (211) | (1.8%) |
| Total assets | \$ 88,992 | \$ 84,833 | \$ 4,159 | 4.9% |
| Liabilities and shareholders' equity | | | | |
| Current liabilities: | | | | |
| Accounts payable | \$ 11,529 | \$ 12,354 | \$ (825) | (6.7%) |
| Accrued expenses | 3,111 | 3,458 | (347) | (10.0%) |
| Line of credit, net | 7,021 | 7,119 | (98) | (1.4%) |
| Current obligations under long-term debt | 786 | 629 | 157 | 25.0% |
| Income taxes payable | — | 18 | (18) | (100.0%) |
| Warrant liabilities | — | 3,739 | (3,739) | (100.0%) |
| Deferred gain from sale-leaseback transactions | 255 | 860 | (605) | (70.3%) |
| Total current liabilities | 22,702 | 28,177 | (5,475) | (19.4%) |
| Long-term liabilities | | | | |
| Long-term debt, less current portion | 1,239 | 1,576 | (337) | (21.4%) |
| Accrued expenses, less current portion | 52 | 15 | 37 | 246.7% |
| Deferred gain from sale-leaseback transactions, less current portion | — | 40 | (40) | (100.0%) |
| Total long-term liabilities | 1,291 | 1,631 | (340) | (20.8%) |
| Total liabilities | 23,993 | 29,808 | (5,815) | (19.5%) |
| Shareholders' equity: | | | | |
| Preferred stock, no par value | 3,138 | 3,138 | — | 0.0% |
| Common stock, no par value | 245,463 | 233,394 | 12,069 | 5.2% |
| Accumulated deficit | (183,602) | (181,507) | (2,095) | (1.2%) |
| Total shareholders' equity | 64,999 | 55,025 | 9,974 | 18.1% |
| Total liabilities and shareholders' equity | \$ 88,992 | \$ 84,833 | \$ 4,159 | 4.9% |
| Net working capital | \$ 11,915 | \$ 4,871 | \$ 7,044 | 144.6% |

Key points from the Balance Sheet as of March 31, 2017 compared to June 30, 2016 include:

- \$10.0 million increase to shareholders' equity primarily due to \$12.1 million increase in common stock offset by our \$2.1 million net loss. The increase in common stock included \$6.2 million of cash proceeds and \$5.2 million of the reclassification of fair value of warrant liability, both attributable to warrants exercised during the September 30, 2016 quarter for 2.4 million shares of common stock; and
- \$7.0 million increase in net working capital primarily attributable to a \$1.8 million increase in accounts receivable, a \$2.1 million increase in inventory, an increase of \$600 thousand of prepaid expenses and other current assets, a decrease in accounts payable of \$0.8 million, and a \$3.7 million decrease due to the elimination of any warrant liabilities as of March 31, 2017.

LIQUIDITY AND CAPITAL RESOURCES
Table 8: Quarterly Cash Flows

| (\$ in thousands) | Three months ended | | | | |
|---|--------------------|----------------------|-----------------------|------------------|-------------------|
| | March 31, 2017 | December 31, 2016 | September 30, 2016 | June 30, 2016 | March 31, 2016 |
| OPERATING ACTIVITIES: | | | | | |
| Net (loss) income | \$ 136 | \$ 233 | \$ (2,464) | \$ (872) | \$ (5,420) |
| Adjustments to reconcile net (loss) income to net cash provided by (used in) operating activities: | | | | | |
| Charges incurred in connection with the vesting and issuance of common stock for employee and director compensation | | | | | |
| | 233 | 233 | 211 | 198 | 142 |
| Gain on disposal of property and equipment | (28) | (31) | — | (110) | (15) |
| Amortization of deferred financing fees | 72 | (79) | 105 | 13 | — |
| Bad debt expense | 127 | 352 | 97 | 470 | 506 |
| Depreciation | 1,165 | 1,220 | 1,257 | 1,272 | 1,190 |
| Amortization of intangible assets | 45 | 43 | 44 | 43 | 44 |
| Impairment of intangible asset | — | — | — | 432 | — |
| Change in fair value of warrant liabilities | — | — | 1,490 | (18) | 4,805 |
| Deferred income taxes, net | 209 | — | (115) | (748) | (93) |
| Recognition of deferred gain from sale-leaseback transactions | (216) | (215) | (215) | (215) | (215) |
| Changes in operating assets and liabilities: | | | | | |
| Accounts receivable | (41) | (1,309) | (1,038) | 2,977 | (1,660) |
| Finance receivables | (4,232) | 2,125 | (5) | (2,587) | (366) |
| Inventory | 647 | (467) | (2,223) | (82) | 250 |
| Prepaid expenses and other assets | 136 | (318) | (224) | (397) | (160) |
| Accounts payable | 2,441 | 397 | (3,661) | 329 | 4,154 |
| Accrued expenses | 160 | (1,061) | 486 | 115 | 1,166 |
| Income taxes payable | (6) | (1) | (10) | 453 | — |
| Net change in operating assets and liabilities | (895) | (634) | (6,675) | 808 | 3,384 |
| Net cash provided (used) by operating activities | 848 | 1,122 | (6,265) | 1,273 | 4,328 |
| INVESTING ACTIVITIES: | | | | | |
| Purchase and additions of property and equipment | (183) | (441) | (168) | (207) | (164) |
| Purchase of property for rental program | (691) | (693) | (642) | — | — |
| Proceeds from sale of property and equipment | 44 | 61 | — | 265 | 19 |
| Cash paid for assets acquired from VendScreen | — | — | — | — | (5,625) |
| Net cash provided by (used in) investing activities | (830) | (1,073) | (810) | 58 | (5,770) |
| FINANCING ACTIVITIES: | | | | | |
| Cash used for the retirement of common stock | — | — | (31) | (173) | — |
| Payment of deferred financing costs | (90) | — | — | — | — |
| Proceeds from exercise of common stock warrants | — | — | 6,193 | 3,237 | 1,652 |
| Proceeds (payments) from line of credit, net | — | — | — | 138 | 33 |
| Repayment of long-term debt | (182) | (213) | (161) | (162) | (151) |
| Net cash (used in) provided by financing activities | (272) | (213) | 6,001 | 3,040 | 1,534 |
| Net (decrease) increase in cash | (254) | (164) | (1,074) | 4,371 | 92 |
| Cash at beginning of period | 18,034 | 18,198 | 19,272 | 14,901 | 14,809 |
| Cash at end of period | \$ 17,780 | \$ 18,034 | \$ 18,198 | \$ 19,272 | \$ 14,901 |
| <i>Supplemental disclosures of cash flow information:</i> | | | | | |
| Interest paid in cash | \$ 59 | \$ 382 | \$ 87 | \$ 147 | \$ 191 |
| Income taxes paid by cash | \$ — | \$ — | \$ — | \$ 501 | \$ — |
| Depreciation expense allocated to cost of services | \$ 950 | \$ 967 | \$ 1,072 | \$ 1,139 | \$ 1,051 |
| Reclass of rental program property to inventory, net | \$ 8 | \$ (55) | \$ (11) | \$ 415 | \$ 347 |
| Prepaid items financed with debt | \$ — | \$ — | \$ 54 | \$ — | \$ — |
| Equipment and property acquired under capital lease | \$ 54 | \$ 18 | \$ 254 | \$ — | \$ 409 |
| Disposal of property and equipment | \$ 87 | \$ 570 | \$ — | \$ 555 | \$ 189 |
| Fair value of common stock warrants at issuance recorded as a debt discount | \$ — | \$ — | \$ — | \$ — | \$ 52 |
| Debt financing cost financed with debt | \$ — | \$ — | \$ — | \$ — | \$ 79 |

Operating cash flow of \$0.8 million for the quarter ended March 31, 2017 decreased \$3.5 million from the quarter ended March 31, 2016. Reasons for this included:

- The Company secured late in the current quarter a large contract which was the primary cause of the finance receivables cash effect of (\$3.9) million;
- Accounts receivable cash effect of \$1.6 million primarily due to a decrease in net amounts due from customers for ePort Connect service; and
- Accounts payable and accrued expenses cash effect of (\$2.7) million primarily due to the timing of payments;

For the same quarter to quarter period, net cash used by investing activities decreased \$4.9 million, primarily due to the \$5.6 million cash outlay for the purchase of Vendscreen in January 2016 offset by a cash outlay of \$0.7 million during the current quarter for property for rental program.

For the same quarter to quarter period, net cash from financing activities decreased \$1.8 million, primarily due to a decrease in proceeds from the exercise of warrants of \$1.7 million.

Operating cash flow for the nine months ended March 31, 2017 decreased \$9.5 million from the nine month period ended March 31, 2016. Primary components which contributed were:

- Finance receivable cash effect of \$(1.4) million primarily due to a current quarter large contract offset by increased fundings;
- Accounts payable and accrued expenses cash effect of (\$3.9) million primarily due to timing of payments;
- Inventory cash effect of \$(3.2) million primarily due to inventory growth to meet expected demand;

For the same nine month periods, net cash used by investing activities decreased \$3.1 million, primarily due to the \$5.6 million cash outlay for the purchase of VendScreen in January 2016, offset by a \$2.0 million increase in purchase of property for the rental program and a \$0.5 million increase in the purchase and additions of property and equipment.

For the same nine month periods, net cash provided by financing activities increased \$1.4 million, primarily due to an increase in proceeds from the exercise of warrants of \$4.5 million offset by a decrease in proceeds from the line of credit of \$3.0 million.

In September 2014, the Company reintroduced QuickStart, a program whereby our customers are able to purchase our ePort hardware via a five-year, non-cancellable finance agreement. Under the QuickStart program, the Company sells the equipment to customers and creates a long-term and current finance receivable for five-year agreements. In the third and fourth quarters of fiscal 2015, the Company signed vendor agreements with two finance companies, whereby our customers would enter into agreements directly with the finance companies as part of our QuickStart program. Under this scenario, the Company invoices the finance company for the equipment financed by our customer, and typically receives full payment within thirty days. Prior to the reintroduction of QuickStart, the Company had financed its customers' acquisition of ePort equipment primarily through the JumpStart rental program. Under Jumpstart, the Company records an investing capital expenditure cash outflow for the equipment provided and fixed assets on the balance sheet, and then receives rental income from a month-to-month lease. Customers who utilize third party finance companies in connection with the QuickStart program improve our cash flow from operations, and our QuickStart program reduces cash flow needed for investing activities otherwise incurred by us for our JumpStart program.

Since entering into vendor agreements with two third-party finance companies, the majority of QuickStart sales consummated have been with customers entering into agreements directly with the finance companies. Our customers have shifted from acquiring our products via JumpStart, which accounted for 65% of our gross connections in fiscal year 2014, to QuickStart and sales under normal trade receivable terms, which accounted for 89% and 91% of our gross connections in fiscal year 2015 and 2016, respectively. JumpStart was approximately 8.6% of gross connections in the three months ending March 31, 2017.

The Company is seeking to expand its outside financing partners in order to accommodate expected growth.

Sources of Cash

The Company's net working capital, which is defined as current assets less current liabilities, was \$11.9 million, \$14.8 million, \$14.0 million, \$4.9 million, and (\$0.2) million over the last five quarter-end reporting dates beginning March 31, 2017 and ending March 31, 2016. As of March 31, 2017, the Company's primary sources of cash include:

- Cash on hand of approximately \$17.8 million;
- \$5.0 million available under the line of credit provided we continue to satisfy the various covenants set forth in the loan agreement, including the requirement to meet minimum quarterly adjusted EBITDA, as defined in the loan agreement.;
- Sales to third party lenders of all or a portion of our finance receivables which may occur in future quarters; and
- Anticipated cash which may be provided by operating activities in future quarters.

The Company believes its existing cash and available cash resources described above, would provide sufficient capital resources to operate its anticipated business over the next twelve months.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

There have been no significant changes to our market risk since June 30, 2016. For a discussion of our exposure to market risk, refer to Part II, Item 7A. "Quantitative and Qualitative Disclosures about Market Risk," contained in our Annual Report on Form 10-K for the year ended June 30, 2016.

Item 4. Controls and Procedures.

(a) Disclosure Controls and Procedures

Our management evaluated, with the participation of our chief executive officer and chief financial officer, the effectiveness as of the end of the period covered by this Form 10-Q of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 (the "Exchange Act")). We maintain disclosure controls and procedures to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules, and that such information is accumulated and communicated to our management, including our chief executive officer and chief financial officer, to allow timely decisions regarding required disclosure. Based on this evaluation, our chief executive officer and chief financial officer have concluded that our disclosure controls and procedures were not effective as of the end of such period because of the material weakness in our internal control over financial reporting identified in our Annual Report on Form 10-K for the fiscal year ended June 30, 2016 (the "2016 Form 10-K"), as described below. Notwithstanding the material weakness identified in the 2016 Form 10-K, our management, including our chief executive officer and chief financial officer, has concluded that the consolidated financial statements included in this Form 10-Q present fairly, in all material respects, our financial position, results of operations and cash flows for the periods presented in conformity with accounting principles generally accepted in the United States.

(b) Changes in Internal Control Over Financial Reporting

There were no changes in our internal controls over financial reporting that occurred during our fiscal quarter ended March 31, 2017 that materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

In our Form 2016 10-K, we stated that management had identified control deficiencies, including three significant deficiencies, in the design or operating effectiveness of the Company's internal control over financial reporting, which when aggregated, represent a material weakness in internal control. The significant deficiencies included that the operation of an existing control did not result in timely resolution of account receivable aging issues; the design of certain of our internal controls allowed for errors or omissions in the accrual process; and one operational control did not identify certain merchant receivables as one of the critical accounts to be audited on a monthly basis. In order to address the significant deficiencies identified in our 2016 Form 10-K, the Company implemented changes in its internal controls over financial reporting during the quarter ended September 30, 2016, and remains committed to remediating the control deficiencies that gave rise to the material weakness.

Part II - Other Information.

Item 1. Legal Proceedings

As previously reported, in our 2016 Form 10-K, on June 1, 2016, a purported shareholder filed a purported derivative action on behalf of the Company in the Chester County, Pennsylvania, Court of Common Pleas (No. 2016-05225-MJ), against certain current and former officers and Directors. On August 17, 2016, the Company filed with the Chester County Court a motion to dismiss the complaint. On March 8, 2017, the Court entered an order granting the Company's motion to dismiss the complaint. On April 6, 2017, the plaintiff appealed the order to the Superior Court of Pennsylvania.

Item 3. Defaults Upon Senior Securities

There were no defaults on any senior securities. On February 1, 2017, an additional \$334 thousand of dividends were accrued on our cumulative Series A Convertible Preferred Stock. The total accrued and unpaid dividends on our Series A Convertible Preferred Stock as of March 31, 2017 was \$14.32 million. The dividend accrual dates for our Preferred Stock are February 1 and August 1. The annual cumulative dividend on our Preferred Stock is \$1.50 per share.

Item 6. Exhibits

| Exhibit Number | Description |
|---------------------------|---|
| 10.1 | Third Amendment to Loan and Security Agreement dated as of March 24, 2017 by and between the Company and Heritage Bank of Commerce (Portions of this exhibit were redacted pursuant to a confidentiality treatment request) |
| 31.1 | Certifications of Chief Executive Officer pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934. |
| 31.2 | Certifications of Chief Financial Officer pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934. |
| 32.1 | Certification of the Chief Executive Officer pursuant to 18 USC Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 32.2 | Certification of the Chief Financial Officer pursuant to 18 USC Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

USA TECHNOLOGIES, INC.

Date: May 9, 2017

/s/ Stephen P. Herbert

Stephen P. Herbert,
Chief Executive Officer

Date: May 9, 2017

/s/ Priyanka Singh

Priyanka Singh
Chief Financial Officer

**THIRD AMENDMENT
TO
LOAN AND SECURITY AGREEMENT**

This Third Amendment to Loan and Security Agreement is entered into as of March 24, 2017 (the “Amendment”), by and between HERITAGE BANK OF COMMERCE (“Bank”), and USA TECHNOLOGIES, INC. (“Borrower”).

RECITALS

Borrower and Bank are parties to that certain Loan and Security Agreement dated as of March 29, 2016 and as amended from time to time, including pursuant to that certain Waiver to Loan and Security Agreement dated as of June 30, 2016 and that certain Second Amendment and Waiver to Loan and Security Agreement dated as of September 30, 2016 (collectively, the “Agreement”). The parties desire to amend the Agreement in accordance with the terms of this Amendment.

NOW, THEREFORE, the parties agree as follows:

1. The following definition in Section 1.1 of the Agreement is amended and restated in its entirety to read as follows:

“Revolving Maturity Date” means September 30, 2018.

2. The following is added to the end of Section 6.8 of the Agreement:

The aggregate balance maintained in Borrower’s deposit account(s) with Avidbank shall not exceed \$*** at any time.

3. Section 6.3(b) of the Agreement is amended and restated in its entirety to read as follows:

(b) as soon as available, but in any event (i) within twenty five (25) days after the end of Borrower’s fiscal quarter, a churn report in form satisfactory to Bank; and (ii) within fifty (50) days after the end of Borrower’s fiscal quarter, a Borrower prepared consolidated balance sheet, income, and cash flow statement covering Borrower’s consolidated operations during such quarter, prepared in accordance with GAAP, consistently applied, in a form acceptable to Bank, and a Compliance Certificate signed by a Responsible Officer in substantially the form of Exhibit D hereto;

4. The following is added as a new subsection (h) to the end of section 6.3:

(h) Within ninety (90) days following the beginning of each fiscal year, Borrower’s annual operating projections (including income statements, balance sheets and cash flow statements presented in a monthly format) for such fiscal year reviewed by Borrower’s board of directors, in form reasonably satisfactory to Bank.

5. Section 6.9(a) of the Agreement is amended and restated in its entirety to read as follows:

(a) Maximum Churn Rate. Borrower’s number of connections as at the end of each fiscal quarter shall not decrease (i) by more than five percent (5%) as compared to Borrower’s number of connections as at the end of the immediately preceding fiscal quarter or (ii) below *** connections.

- 6.
-

7. The following is hereby added to the end of Section 6.9(b) of the Agreement:

Borrower's minimum quarterly Adjusted EBITDA for each of the quarters ending September 30, 2017, December 31, 2017, March 31, 2018, and June 30, 2018, shall be as follows:

| Quarterly Period ending | Minimum Adjusted EBITDA |
|--------------------------------|--------------------------------|
| September 30, 2017 | \$880,000 |
| December 31, 2017 | \$1,000,000 |
| March 31, 2018 | \$1,000,000 |
| June 30, 2018 | \$1,000,000 |

8. Exhibit D to the Agreement is replaced in its entirety with the Exhibit D attached hereto.
9. Borrower represents and warrants that the representations and warranties contained in the Agreement are true and correct as of the date of this Amendment, and that no Event of Default has occurred and is continuing.
10. Unless otherwise defined, all initially capitalized terms in this Amendment shall be as defined in the Agreement. The Agreement, as amended hereby, shall be and remain in full force and effect in accordance with its respective terms and hereby is ratified and confirmed in all respects. Except as expressly set forth herein, the execution, delivery, and performance of this Amendment shall not operate as a waiver of, or as an amendment of, any right, power, or remedy of Bank under the Agreement, as in effect prior to the date hereof. Borrower ratifies and reaffirms the continuing effectiveness of all agreements entered into in connection with the Agreement.
11. This Amendment may be executed in two or more counterparts, each of which shall be deemed an original, but all of which together shall constitute one instrument. In the event that any signature is delivered by facsimile transmission or by e-mail delivery of a ".pdf" format data file, such signature shall create a valid and binding obligation of the party executing (or on whose behalf such signature is executed) with the same force and effect as if such facsimile or ".pdf" signature page were an original hereof.
12. As a condition to the effectiveness of this Amendment, Bank shall have received, in form and substance satisfactory to Bank, the following:
- (a) the original signed Amendment and all other Loan Documents being executed in connection herewith, duly executed by Borrower;
 - (b) an amendment and renewal facility fee equal to \$90,000, plus an amount equal to all Bank Expenses incurred through the date of this Amendment;
 - (c) affirmation of guaranty; and
 - (d) such other documents, and completion of such other matters, as Bank may reasonably deem necessary or appropriate.

[remainder of this page intentionally left blank]

IN WITNESS WHEREOF, the undersigned have executed this Amendment as of the first date above written.

USA TECHNOLOGIES, INC.

By: /s/ Stephen P. Herbert

Name: Stephen P. Herbert

Title: Chairman and CEO

HERITAGE BANK OF COMMERCE

By: /s/ Karla Schrader

Name: Karla Schrader

Title: VP

**Exhibit D
Compliance Certificate**

TO: HERITAGE BANK OF COMMERCE

FROM: USA TECHNOLOGIES, INC.

The undersigned authorized officer of USA TECHNOLOGIES, INC. hereby certifies that in accordance with the terms and conditions of the Loan and Security Agreement between Borrower and Bank (the "Agreement"), (i) Borrower is in complete compliance for the period ending _____ with all required covenants except as noted below and (ii) all representations and warranties of Borrower stated in the Agreement are true and correct as of the date hereof; provided, that those representations and warranties expressly referring to another date shall be true, correct, and complete in all material respects as of such date. Attached herewith are the required documents supporting the above certification. The Officer further certifies that these are prepared in accordance with Generally Accepted Accounting Principles (GAAP) and are consistently applied from one period to the next except as explained in an accompanying letter or footnotes.

Please indicate compliance status by circling Yes/No under "Complies" column.

| <u>Reporting Covenant</u> | <u>Required</u> | | <u>Complies</u> | |
|---|---|---------------|-----------------|----|
| A/R & A/P Agings | Monthly within 25 days | | Yes | No |
| Borrowing Base Certificate | Monthly within 25 days | | Yes | No |
| Copies of non-HBC bank statements | Monthly within 30 days | | Yes | No |
| Churn Report | Quarterly within 25 days | | Yes | No |
| Quarterly financial statements | Quarterly within 50 days | | Yes | No |
| Compliance Certificate | Quarterly within 50 days | | Yes | No |
| Annual financial statements (CPA Audited) | FYE within 120 days | | Yes | No |
| Annual financial projections (board reviewed) | Within 90 days of fiscal year beginning | | Yes | No |
| 10K and 10Q | Within 5 days of filing | | Yes | No |
| A/R Audit | Semi-Annually | | Yes | No |
| IP Notices | As required under Section 6.10 | | Yes | No |
| | | | | |
| <u>Financial Covenant</u> | <u>Required</u> | <u>Actual</u> | <u>Complies</u> | |
| Maximum Churn Rate (quarterly) | 5% | ____% | Yes | No |
| Minimum Connections (quarterly) | *** | _____ | Yes | No |
| Minimum Cash at Bank (at all times) | \$*** | \$_____ | Yes | No |
| Minimum Adjusted EBITDA (quarterly) | See Section 6.9(b) | _____ | Yes | No |

Comments Regarding Exceptions: See Attached.

| |
|----------------------|
| BANK USE ONLY |
|----------------------|

Sincerely,

SIGNATURE

TITLE

DATE

Received by:

AUTHORIZED SIGNER

Date:

Verified:

AUTHORIZED SIGNER

Date:

Compliance Status

Yes

No



**CERTIFICATION PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Stephen P. Herbert, certify that:

1. I have reviewed this quarterly report on Form 10-Q of USA Technologies, 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 issuer as of, and for, the periods presented in this report;
4. The registrant's other certifying officer 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 upon such evaluation; and
 - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the issuer's most recent fiscal quarter (the issuer's fourth fiscal quarter in the case of an annual report) that has materially affected or is reasonably likely to materially affect, the issuer's internal control over financial reporting; and
5. The issuer's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting to the auditors and the audit committee of the issuer's board of directors (or persons performing the equivalent functions):
 - a. all significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the issuer'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 issuer's internal control over financial reporting.

Date: May 9, 2017

/s/ Stephen P. Herbert

Stephen P. Herbert
Chief Executive Officer

**CERTIFICATION PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Priyanka Singh, certify that:

1. I have reviewed this quarterly report on Form 10-Q of USA Technologies, 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 issuer as of, and for, the periods presented in this report;
4. The registrant's other certifying officer 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 upon such evaluation; and
 - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the issuer's most recent fiscal quarter (the issuer's fourth fiscal quarter in the case of an annual report) that has materially affected or is reasonably likely to materially affect, the issuer's internal control over financial reporting; and
5. The issuer's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting to the auditors and the audit committee of the issuer's board of directors (or persons performing the equivalent functions):
 - a. all significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the issuer'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 issuer's internal control over financial reporting.

Date: May 9, 2017

/s/ Priyanka Singh

Priyanka Singh
Chief Financial Officer

**CERTIFICATION PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002
(18 U.S.C. SECTION 1350)**

In connection with the accompanying Quarterly Report of USA Technologies, Inc., (the "Company") on Form 10-Q for the period ended March 31, 2017 (the "Report"), I, Stephen P. Herbert., Chief Executive Officer of the Company, hereby certify that to my knowledge:

- (1) 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 results of operations of the Company.

Date: May 9, 2017

/s/ Stephen P. Herbert

Stephen P. Herbert
Chief Executive Officer

**CERTIFICATION PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002
(18 U.S.C. SECTION 1350)**

In connection with the accompanying Quarterly Report of USA Technologies, Inc., (the "Company") on Form 10-Q for the period ended March 31, 2017 (the "Report"), I, Priyanka Singh, Chief Financial Officer of the Company, hereby certify that to my knowledge:

- (1) 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 results of operations of the Company.

Date: May 9, 2017

/s/ Priyanka Singh

Priyanka Singh
Chief Financial Officer
