

Financial statements and report of independent certified
public accountants

PD-Rx Pharmaceuticals, Inc.

June 30, 2019 and 2018

Contents

	Page
REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS	3
FINANCIAL STATEMENTS	
BALANCE SHEETS	5
STATEMENTS OF EARNINGS	6
STATEMENT OF STOCKHOLDERS' EQUITY	7
STATEMENTS OF CASH FLOWS	8
NOTES TO FINANCIAL STATEMENTS	9

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REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Board of Directors
PD-Rx Pharmaceuticals, Inc.

We have audited the accompanying financial statements of PD-Rx Pharmaceuticals, Inc. (an Oklahoma corporation), which comprise the balance sheets as of June 30, 2019 and 2018, and the related statements of earnings, stockholders' equity, and cash flows for the years then ended, and the related notes to the financial statements.

Management's responsibility for the financial statements

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

Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of PD-Rx Pharmaceuticals, Inc. as of June 30, 2019 and 2018, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note A to the financial statements, the Company adopted new accounting guidance in 2019 related to the presentation of deferred income taxes. Our opinion is not modified with respect to this matter.



Oklahoma City, OK
October 29, 2019

PD-Rx Pharmaceuticals, Inc.

BALANCE SHEETS

June 30,

ASSETS	<u>2019</u>	<u>2018</u>
CURRENT ASSETS		
Cash and cash equivalents	\$ 2,409,182	\$ 3,860,455
Certificates of deposit	750,000	3,500,048
Accounts receivable (net of allowance for doubtful accounts of \$105,026 and \$17,911 in 2019 and 2018)	2,533,749	2,638,110
Inventories	1,465,579	1,185,438
Deferred income taxes, current	-	125,799
Prepaid income taxes	266,213	258,929
Other	131,915	151,194
Total current assets	7,556,638	11,719,973
PROPERTY AND EQUIPMENT, net	960,130	992,292
DEFERRED INCOME TAXES	141,789	-
	<u>\$ 8,658,557</u>	<u>\$ 12,712,265</u>
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable	\$ 589,514	\$ 883,100
Accrued and other current liabilities	1,058,204	989,476
Total current liabilities	1,647,718	1,872,576
DEFERRED INCOME TAXES	-	42,742
Total liabilities	1,647,718	1,915,318
COMMITMENTS AND CONTINGENCIES (Note E)		
STOCKHOLDERS' EQUITY		
Preferred stock - \$.10 par value; authorized, 10,000,000 shares; issued and outstanding, none	-	-
Common stock - \$.01 par value; 3,000,000 authorized; 2,094,804 shares issued in 2018 and 2019, respectively	20,948	20,948
Additional paid-in capital	1,344,461	1,344,461
Retained earnings	5,886,531	9,672,639
	7,251,940	11,038,048
Less common stock in treasury - at cost; 379,718 shares in 2019 and 2018	(241,101)	(241,101)
	<u>7,010,839</u>	<u>10,796,947</u>
	<u>\$ 8,658,557</u>	<u>\$ 12,712,265</u>

The accompanying notes are an integral part of these statements.

PD-Rx Pharmaceuticals, Inc.

STATEMENTS OF EARNINGS

Year ended June 30,

	<u>2019</u>	<u>2018</u>
Net sales	\$ 20,870,974	\$ 24,967,418
Cost of sales	<u>13,286,202</u>	<u>16,432,161</u>
Gross profit	7,584,772	8,535,257
Selling, general and administrative expenses	<u>7,650,506</u>	<u>7,644,541</u>
Operating (loss) income	(65,734)	890,716
Other income (expense)		
Interest income and other	50,392	72,203
Interest expense	-	(220)
Gain on disposition of assets	<u>907</u>	<u>18,102</u>
Other income, net	<u>51,299</u>	<u>90,085</u>
(Loss) Earnings before income taxes	(14,435)	980,801
Income tax benefit (expense)	<u>1,516</u>	<u>(359,638)</u>
NET (LOSS) EARNINGS	\$ <u>(12,919)</u>	\$ <u>621,163</u>
(LOSS) EARNINGS PER COMMON SHARE – BASIC AND DILUTED	\$ <u>(.01)</u>	\$ <u>0.36</u>

The accompanying notes are an integral part of these statements.

PD-Rx Pharmaceuticals, Inc.

STATEMENT OF STOCKHOLDERS' EQUITY

Years ended June 30, 2019 and 2018

	<u>Common stock</u>					
	<u>Shares</u>	<u>Amount</u>	<u>Additional paid-in capital</u>	<u>Retained earnings</u>	<u>Common stock in treasury</u>	<u>Total stockholders' equity</u>
Balance at July 1, 2017	2,094,804	\$ 20,948	\$ 1,344,461	\$ 10,183,433	\$ (212,060)	\$ 11,336,782
Dividends	-	-	-	(1,131,957)	-	(1,131,957)
Repurchased - Treasury Stock	-	-	-	-	(29,041)	(29,041)
Net earnings	-	-	-	621,163	-	621,163
Balance at June 30, 2018	2,094,804	20,948	1,344,461	9,672,639	(241,101)	10,796,947
Dividends	-	-	-	(3,773,189)	-	(3,773,189)
Net loss	-	-	-	(12,919)	-	(12,919)
Balance at June 30, 2019	<u>2,094,804</u>	<u>\$ 20,948</u>	<u>\$ 1,344,461</u>	<u>\$ 5,886,531</u>	<u>\$ (241,101)</u>	<u>\$ 7,010,839</u>

The accompanying notes are an integral part of this statement.

PD-Rx Pharmaceuticals, Inc.

STATEMENTS OF CASH FLOWS

Year ended June 30,

	<u>2019</u>	<u>2018</u>
Cash flows from operating activities		
Net (loss) earnings	\$ (12,919)	\$ 621,163
Adjustments to reconcile net (loss) earnings to net cash (used in) provided by operating activities		
Provision for deferred income taxes	(58,732)	37,448
Depreciation and amortization	177,326	176,543
Bad debt expense	93,446	20,524
Loss on disposition of property and equipment and donation	(907)	(18,102)
Changes in assets and liabilities		
Accounts receivable	10,915	(991,181)
Inventories	(280,141)	25,872
Prepaid income taxes	(7,284)	(28,310)
Other assets	19,279	(40,982)
Accounts payable	(293,586)	470,034
Accrued and other current liabilities	68,728	148,853
Net cash (used in) provided by operating activities	(283,875)	421,898
Cash flows from investing activities		
Purchases of property and equipment	(145,727)	(274,388)
Proceeds from sale of property and equipment	1,470	39,751
Maturities of certificates of deposit	3,750,048	4,000,000
Purchases of certificates of deposits	(1,000,000)	(4,250,048)
Net cash provided (used in) investing activities	2,605,791	(484,685)
Cash flows from financing activities		
Dividend paid	(3,773,189)	(1,131,957)
Treasury stock repurchased	-	(29,041)
Net cash used in financing activities	(3,773,189)	(1,160,998)
NET DECREASE IN CASH AND CASH EQUIVALENTS	(1,451,273)	(1,223,785)
Cash and cash equivalents at beginning of year	3,860,455	5,084,240
Cash and cash equivalents at end of year	\$ 2,409,182	\$ 3,860,455
<u>Supplemental cash flow information:</u>		
Cash paid during the year for income taxes, net	\$ 64,500	\$ 350,500

The accompanying notes are an integral part of these statements.

PD-Rx Pharmaceuticals, Inc.

NOTES TO FINANCIAL STATEMENTS

June 30, 2019 and 2018

NOTE A - NATURE OF OPERATIONS AND SUMMARY OF ACCOUNTING POLICIES

PD-Rx Pharmaceuticals, Inc. (the Company) is involved principally in the repackaging and distribution of prepackaged pharmaceutical products. The Company's customers consist primarily of physicians, pharmacies and medical clinics located in the south-central, southeastern, and western United States.

A summary of the significant accounting policies consistently applied in the preparation of the accompanying financial statements follows.

1. Cash and Cash Equivalents

The Company considers highly liquid debt instruments with maturities of three months or less when acquired to be cash equivalents.

At June 30, 2019 and 2018, the Company had all of its cash and cash equivalents with one financial institution. The Company maintains its cash in bank deposit accounts and certificates of deposit which, at times may exceed the Federal Deposit Insurance Corporation (FDIC) insurance limit. Additionally, the Company invests in short-term, collateralized repurchase agreements through its bank. The Company has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk in such accounts.

2. Certificates of Deposit

Certificates of deposit are carried at cost, which approximates fair value. All certificates of deposit have a maturity date of less than one year.

3. Accounts Receivable

Accounts receivable result primarily from product sales to customers, are due within 30 days, and are stated at amounts due, net of an allowance for doubtful accounts. Accounts outstanding longer than the contractual payment terms are considered past due.

The Company determines its allowance for doubtful accounts by considering a number of factors, including the length of time accounts receivable are past due, the Company's previous loss history, the customer's current ability to pay its obligation to the Company, and the condition of the general economy and the industry as a whole. The Company writes off accounts receivable when they become uncollectible. Late charges accrue on past due balances and are discontinued on accounts considered uncollectible.

4. Inventories

Inventories are stated at the lower of cost or market. Cost is determined by the average cost method.

PD-Rx Pharmaceuticals, Inc.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2019 and 2018

NOTE A - NATURE OF OPERATIONS AND SUMMARY OF ACCOUNTING POLICIES - CONTINUED

5. Property and Equipment

Property and equipment are recorded at cost and depreciated using the straight-line method over the estimated useful lives of the assets. The estimated useful lives used in computing depreciation are:

Building and components	7 to 39 years
Equipment	3 to 8 years
Computer software costs	5 years
Furniture and fixtures	7 years
Automobiles	5 years

Long-lived assets to be held and used are reviewed for impairment whenever events or changes in circumstances indicate that the related carrying amount may not be recoverable. When required, impairment losses are recognized based upon the estimated fair value of the asset. There were no events or changes in circumstances indicating that the carrying value of such assets may not be recoverable as of June 30, 2019 or 2018.

6. Earnings Per Share

Basic earnings per share is computed by the weighted average number of common shares outstanding, which is the number of common shares issued less common stock in treasury. Diluted earnings per share is computed by the weighted average number of common shares outstanding less the effect of any dilutive securities. There were no dilutive securities for the years ended June 30, 2019 and 2018, respectively.

7. Revenue Recognition

Revenue is recognized on sales of products at the time of shipment. Sales are recorded net of sales returns. The Company's policy on returned products is to accept returns without charge within 15 days of shipment. Products returned between 15 and 30 days are assessed a 25% restocking charge. Returned products are not accepted after 30 days.

8. Shipping and Handling Costs

Shipping and handling costs are reported as a component of selling, general, and administrative expenses and totaled approximately \$158,000 and \$162,000 for 2019 and 2018, respectively.

9. Advertising Expense

The Company expenses advertising the first time advertising takes place. Advertising expense for the years ended June 30, 2019 and 2018 was approximately \$165,000 and \$178,000, respectively.

PD-Rx Pharmaceuticals, Inc.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2019 and 2018

NOTE A - NATURE OF OPERATIONS AND SUMMARY OF ACCOUNTING POLICIES - CONTINUED

10. Income Taxes

The Company utilizes the asset and liability approach for accounting for deferred income taxes. Deferred income taxes are recognized for the tax consequences of temporary differences and carry-forwards by applying enacted tax rates applicable to future years to differences between the financial statement amounts and the tax bases of existing assets and liabilities. A valuation allowance is established if it is more likely than not that some portion of the deferred tax asset will not be realized.

The Company recognizes the financial statement benefit of a tax position only after determining that the relevant tax authority would more likely than not sustain the position following an audit. For tax positions meeting the more-likely-than-not threshold, the amount recognized in the financial statements is the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement with the relevant tax authority. The Company recognizes interest accrued related to unrecognized tax benefits in interest expense and recognizes penalties in income tax expense.

The Company is subject to income taxes in the U.S. federal jurisdiction and various state jurisdictions. Tax regulations within each jurisdiction are subject to the interpretation of the related tax laws and regulations and require significant judgment to apply. Generally, the Company is no longer subject to U.S. federal, state and local income tax examinations by tax authorities for the years before 2016.

11. Fair Value of Financial Instruments

The carrying amount of cash and cash equivalents, accounts receivable, accounts payable and accrued and other liabilities, approximates fair value because of the highly liquid nature of these instruments.

12. Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Actual results could differ from those estimates.

13. Reclassification

Certain reclassifications have been made to prior period financial statements and related disclosures to conform to current period presentation.

PD-Rx Pharmaceuticals, Inc.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2019 and 2018

NOTE A - NATURE OF OPERATIONS AND SUMMARY OF ACCOUNTING POLICIES - CONTINUED

13. Recently Issued Accounting Standards

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers*, which supersedes the revenue recognition requirements in Topic 605, *Revenue Recognition*, and most industry-specific guidance. The core principle of the new standard is for the recognition of revenue to depict the transfer of goods or services to customers in amounts that reflect the payment to which the company expects to be entitled in exchange for those goods or services. The new standard will also result in enhanced revenue disclosures, provide guidance for transactions that were not previously addressed comprehensively and improve guidelines for multiple-element arrangements. The ASU will be effective for annual periods beginning after December 15, 2017, using either a full or a modified retrospective application approach; however, in July 2015 the FASB decided to defer the effective date by one year (now effective July 1, 2019 for the Company) by issuing ASU No. 2015-14, *Revenue from Contracts with Customers: Deferral of the Effective Date*. The Company is in the process of evaluating the impact of adopting this standard on its financial statements.

In November 2015, the FASB issued ASU No. 2015-17, *Balance Sheet Classification of Deferred Taxes* (Topic 705). Current guidance requires an entity to separate deferred income tax liabilities and assets into current and noncurrent amounts in a classified statement of financial position. Deferred tax liabilities and assets are classified as current or noncurrent based on the classification of the related asset or liability for financial reporting. Deferred tax liabilities and assets that are not related to an asset or liability for financial reporting are classified according to the expected reversal date of the temporary difference. To simplify the presentation of deferred income taxes, the amendments in this update require that deferred income tax liabilities and assets be classified as noncurrent in a classified statement of financial position. This guidance is effective for annual periods beginning after December 15, 2017, with early adoption permitted. The company adopted this guidance on a prospective basis; therefore, prior periods were not retrospectively adjusted.

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)* (ASU 2016-02). Under ASU 2016-2, an entity will be required to recognize right-of-use assets and lease liabilities on its balance sheet and disclose key information about leasing arrangements. ASU 2016-02 offers specific accounting guidance for a lease, a lessor and sale and leaseback transactions. Lessees and lessors are required to disclose qualitative and quantitative information about leasing arrangements to enable a user of the financial statements to assess the amount, timing and uncertainty of cash flows arising from the leases. ASU 2016-02 is effective for annual periods beginning after December 15, 2019; however, the FASB decided to defer the effective date by one year (now effective July 1, 2021 for the Company). The Company is in the process of evaluating the impact of adopting this standard on its financial statements.

In June 2016, the FASB issued ASU 2016-13, *"Measurement of Credit Losses on Financial Instruments"* that will change how companies measure credit losses for most financial assets and certain other instruments that aren't measured at fair value through net income. The standard will replace today's "incurred loss" approach with an "expected loss" model for instruments measured at amortized cost. The amendments in this update will be effective for annual periods beginning after December 15, 2020; however, the FASB decided to defer the effective date by one year (now effective July 1, 2022 for the Company). The Company is in the process of evaluating the impact of adopting this standard on its financial statements.

PD-Rx Pharmaceuticals, Inc.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2019 and 2018

NOTE B – PROPERTY AND EQUIPMENT

Property and equipment consist of the following at June 30:

	2019	2018
Building and components	\$ 922,503	\$ 837,084
Equipment	1,272,441	1,227,612
Computer software costs	721,351	716,351
Furniture and fixtures	101,883	97,033
Automobiles	200,913	200,913
	<u>3,219,091</u>	<u>3,078,993</u>
Less accumulated depreciation and amortization	<u>(2,414,721)</u>	<u>(2,242,461)</u>
	804,370	836,532
Land	<u>155,760</u>	<u>155,760</u>
	<u>\$ 960,130</u>	<u>\$ 992,292</u>

Depreciation and amortization expense totaled \$177,326 and \$176,543 for the years ended June 30, 2019 and 2018, respectively.

NOTE C – NOTES PAYABLE

The Company has a \$500,000 revolving line of credit with a bank that matures February 2020. At June 30, 2019 and 2018, there were no amounts outstanding on the line of credit. The line of credit is payable in monthly installments of interest only at BOK Financial Corporation National prime (effective rate of 6.25% at June 30, 2019), and is collateralized by inventories, property and equipment, accounts receivable, and general intangibles. Borrowings under the line are limited to established ratios of accounts receivable and inventories as specified by the terms of the agreement. The revolving line of credit with the bank is subject to related loan agreements that require the Company, among other things, to maintain a minimum current ratio of 1.4 to 1 and a maximum debt to worth ratio of 2.0 to 1. At June 30, 2019, the Company was in compliance with these covenants.

NOTE D – INCOME TAXES

The provision for income taxes consists of the following for the years ended June 30:

	2019	2018
Current	\$ 57,216	\$ 322,190
Deferred	<u>(58,732)</u>	<u>37,448</u>
	<u>\$ (1,516)</u>	<u>\$ 359,638</u>

PD-Rx Pharmaceuticals, Inc.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2019 and 2018

NOTE D – INCOME TAXES – CONTINUED

On December 22, 2017, the President of the United States of America signed into law Public Law No. 115-97, a comprehensive tax reform bill commonly referred to as the Tax Cuts and Jobs Act (the “Tax Act”), that significantly reforms the Internal Revenue Code of 1986, as amended, (the “Code”). Among other changes, the Tax Act reduces the maximum U.S. corporate income tax rate from 35% to 21% and allows for immediate expensing of capital expenditures for tangible personal property for a period of time. The change in the U.S. corporate income tax rate is effective for calendar year 2019 and forward. Due to the Company’s June 30 fiscal year, the fiscal year 2018 U.S. income tax rate is computed partially under the pre-tax reform rates and partially under the post-tax reform rates. The deferred tax positions are all computed under the post-tax reform rates as they are all in future periods.

The income tax expense reflected in the accompanying statements of earnings differs from the expected federal income tax rates for the following reasons for the years ended June 30:

	2019	2018
Computed at 21% and 27.5% in 2019 and 2018	\$ (3,000)	\$ 270,200
Increase (decrease) in income taxes		
Nondeductible expenses	1,800	3,500
Adjustment of prior year estimates	-	5,500
State income tax expense	(300)	41,000
Tax reform	-	40,000
Other	(16)	(562)
	<u>\$ (1,516)</u>	<u>\$ 359,638</u>

The temporary differences that give rise to deferred tax assets (liabilities) include the following at June 30:

	2019	2018
Deferred tax assets		
Allowance for doubtful accounts	\$ 26,751	\$ 4,562
Vacation accrual	132,425	114,116
Tax basis capitalized inventory costs	10,779	7,121
	<u>169,955</u>	<u>125,799</u>
Total deferred tax assets	169,955	125,799
Deferred tax liabilities		
Book basis/tax basis differences on property and equipment	(28,166)	(42,742)
	<u>(28,166)</u>	<u>(42,742)</u>
Total deferred tax liabilities	(28,166)	(42,742)
Net deferred tax asset	<u>\$ 141,789</u>	<u>\$ 83,057</u>

PD-Rx Pharmaceuticals, Inc.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2019 and 2018

NOTE E – COMMITMENTS AND CONTINGENCIES

The Company is subject to various federal, state, and local government regulations. Matters subject to regulation include the distribution and recordkeeping of certain pharmaceutical products. Additionally, some states have passed or proposed laws and regulations that are intended to protect the integrity of the supply channel. For example, Florida and other states have implemented pedigree requirements that require drugs to be accompanied by paperwork tracing drugs back to the manufacturers. Also, from time to time, the Company is subject to review by regulating entities to ensure compliance with laws and regulations. Management has developed policies and procedures designed to ensure that the Company complies with laws and regulations. Management is not aware of any noncompliance with such laws and regulations.

From time to time, the Company is involved in legal actions arising in the normal course of business. Management of the Company, based in part on advice of legal counsel, is of the opinion that the ultimate outcome of such actions will not have a material adverse effect on the Company's financial position or results of operations.

The Company has employment agreements with its chief executive officer (CEO) and chief operating officer (COO). Provisions of these employment agreements include, among other things, the following:

- Three-year terms with automatic one-year extensions after each full year of employment.
- Base salaries with minimum 5% annual increases.
- Annual bonuses based on a percentage of gross sales.
- Contingent compensation upon the occurrence of a specified event, including:
 - Compensation through end of employment agreement upon change in control, as defined,
 - Compensation for three months following the month of death upon death of the officer, or
 - Compensation through end of employment agreement upon termination of the officer for reasons other than cause or resignation due to significant change in duties, as defined.

At June 30, 2019, the maximum contingent compensation as described above is approximately \$750,000 for each the CEO and COO. Such contingent compensation is payable in annual installments under certain circumstances. The Company does not recognize an expense or a liability relating to contingent compensation until an obligating event occurs.

The Company has keyman life insurance of \$1,000,000 per officer to partially fund the obligations in the event of death. Management believes that voluntary resignation of the officers terminates all obligations under the agreements.

The PD-Rx Pharmaceuticals, Inc. 401(k) Plan (the "Plan") is a defined contribution plan for all eligible employees of the Company. Participants may contribute any amount to the Plan subject to applicable Internal Revenue Code limitations. The Company also has the option to make discretionary profit sharing contributions to participant accounts. The Company's contributions to the Plan vest to the participants based on years of service. These contributions are fully vested upon completion of three years of service, as defined by the Plan. The total Company contributions related to the Plan were approximately \$282,000 and \$274,000 for the years ended June 30, 2019 and 2018, respectively.

PD-Rx Pharmaceuticals, Inc.

NOTES TO FINANCIAL STATEMENTS – CONTINUED

June 30, 2019 and 2018

NOTE F – SUBSEQUENT EVENTS

The Company has evaluated events and transactions that occurred subsequent to June 30, 2019 through October 29, 2019, the date these financial statements were available to be issued. The Company is not aware of any subsequent events which would require recognition or disclosure in the financial statements.