

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended: September 30, 2019

or

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

For the transition period from _____ to _____

Commission File Number: 000-55925

AERKOMM INC.

(Exact name of registrant as specified in its charter)

Nevada

(State or other jurisdiction of
incorporation or organization)

46-3424568

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

923 Incline Way, #39, Incline Village, NV 89451

(Address of principal executive offices, Zip Code)

(877) 742-3094

(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Non-accelerated filer

Accelerated filer

Smaller reporting company

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 comply with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

Securities registered pursuant to Section 12(b) of the Act:

Title of each class

Trading Symbol(s)

Name of each exchange on which registered

Not applicable.

As of November 13, 2019, there were 9,540,891 shares of the registrant's common stock issued and outstanding. This number reflects a reverse split in the ratio of 1 for 5 effective January 16, 2019.

AERKOMM INC.

Quarterly Report on Form 10-Q
Period Ended September 30, 2019

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PART I
FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

AERKOMM INC.
CONSOLIDATED FINANCIAL STATEMENTS

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AERKOMM INC. AND SUBSIDIARIES
Consolidated Balance Sheets
September 30, 2019 (Unaudited) and December 31, 2018

| | September 30, | December 31, |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------|-----------------------------|
| | 2019 | 2018 |
| <u>Assets</u> | | |
| Current Assets | | |
| Cash | \$ 2,808,023 | \$ 88,309 |
| Accounts receivable | 649,939 | 1,745,000 |
| Inventories | 2,380,364 | 895,014 |
| Prepaid expenses | 2,507,069 | 1,533,748 |
| Other receivable – related party | 111,111 | - |
| Other receivable – others | 1,461 | 2,616 |
| Temporary deposit – related party | - | 100,067 |
| Other current assets | 13,975 | 11,336 |
| Total Current Assets | <u>8,471,942</u> | <u>4,376,090</u> |
| Property and Equipment | | |
| Cost | 2,715,998 | 2,710,543 |
| Accumulated depreciation | (731,806) | (322,049) |
| | <u>1,984,192</u> | <u>2,388,494</u> |
| Prepayment for land | 35,861,589 | 35,237,127 |
| Construction in progress | - | 416,231 |
| Net Property and Equipment | <u>37,845,781</u> | <u>38,041,852</u> |
| Other Assets | | |
| Intangible asset, net | 3,011,250 | 3,382,500 |
| Goodwill | 1,475,334 | 1,475,334 |
| Operating lease right-of-use assets, net | 364,832 | - |
| Deposits | 108,161 | 107,909 |
| Total Other Assets | <u>4,959,577</u> | <u>4,965,743</u> |
| Total Assets | <u>\$ 51,277,300</u> | <u>\$ 47,383,685</u> |
| <u>Liabilities and Stockholders' Equity</u> | | |
| Current Liabilities | | |
| Accounts payable | \$ 809,908 | \$ 1,650,000 |
| Accrued expenses | 345,864 | 412,165 |
| Other payable – related parties | 112,192 | 173,854 |
| Other payable – others | 2,203,028 | 3,726,932 |
| Long-term loan – current | 8,150 | - |
| Operating lease liability – current – related party | 33,478 | - |
| Operating lease liability – current - others | 352,523 | - |
| Total Current Liabilities | <u>3,865,143</u> | <u>5,962,951</u> |
| Long-term Liabilities | | |
| Long-term loan – non-current | 37,615 | - |
| Operating lease liability – non-current | 19,900 | - |
| Restricted stock deposit liability | 1,000 | 1,000 |
| Total Liabilities | <u>3,923,658</u> | <u>5,963,951</u> |
| Commitments | | |
| Stockholders' Equity | | |
| Preferred stock, \$0.001 par value, 50,000,000 shares authorized, none issued and outstanding as of September 30, 2019 and December 31, 2018 | - | - |
| Common stock, \$0.001 par value, 90,000,000 shares authorized, 9,391,709 shares (excluding 149,162 unvested restricted shares) issued and outstanding as of September 30, 2019; 9,098,090 shares (excluding 149,162 unvested restricted shares) issued and outstanding as of December 31, 2018 | 9,392 | 9,098 |
| Additional paid in capital | 68,872,096 | 56,582,800 |
| Accumulated deficits | (22,172,341) | (15,292,128) |
| Accumulated other comprehensive income | 644,495 | 119,964 |
| Total Stockholders' Equity | <u>47,353,642</u> | <u>41,419,734</u> |
| Total Liabilities and Stockholders' Equity | <u>\$ 51,277,300</u> | <u>\$ 47,383,685</u> |

See accompanying notes to the consolidated financial statements.

AERKOMM INC. AND SUBSIDIARIES
Consolidated Statements of Operations and Comprehensive Loss
For the Three-Month and Nine-Month Periods Ended September 30, 2019 and 2018
(Unaudited)

| | Three Month Period Ended September 30, | | Nine Month Period Ended September 30, | |
|------------------------------------------------------|-------------------------------------------------------|----------------------|------------------------------------------------------|----------------------|
| | 2019 | 2018 | 2019 | 2018 |
| Net sales | \$ - | \$ 1,730,000 | \$ 1,599,864 | \$ 1,730,000 |
| Service income | - | 15,000 | - | 15,000 |
| Total revenue | - | 1,745,000 | 1,599,864 | 1,745,000 |
| Cost of sales | - | 1,650,000 | 1,587,222 | 1,650,000 |
| Operating expenses | 2,733,350 | 2,594,500 | 6,356,161 | 6,180,984 |
| Total Cost and Expenses | 2,733,350 | 4,244,500 | 7,943,383 | 7,830,984 |
| Loss from Operations | (2,733,350) | (2,499,500) | (6,343,519) | (6,085,984) |
| Non-Operating Income (Loss) | | | | |
| Foreign currency exchange gain (loss) | (77,047) | 1,425 | (528,748) | 5,847 |
| Other income (loss), net | (1,386) | 2 | (4,711) | (3,188) |
| Net Non-Operating Income (Loss) | (78,433) | 1,427 | (533,459) | 2,659 |
| Loss before Income Taxes | (2,811,783) | (2,498,073) | (6,876,978) | (6,083,325) |
| Income Tax Expense | - | - | 3,235 | 4,062 |
| Net Loss | (2,811,783) | (2,498,073) | (6,880,213) | (6,087,387) |
| Other Comprehensive Income (Loss) | | | | |
| Change in foreign currency translation adjustments | 59,237 | 2,474 | 524,531 | (1,208) |
| Total Comprehensive Loss | \$(2,752,546) | \$(2,495,599) | \$(6,355,682) | \$(6,088,595) |
| Net Loss Per Common Share: | | | | |
| Basic | <u>\$ (0.2967)</u> | <u>\$ (0.2691)</u> | <u>\$ (0.7377)</u> | <u>\$ (0.7007)</u> |
| Diluted | <u>\$ (0.2967)</u> | <u>\$ (0.2691)</u> | <u>\$ (0.7377)</u> | <u>\$ (0.7007)</u> |
| Weighted Average Shares Outstanding - Basic | <u>9,475,413</u> | <u>9,284,047</u> | <u>9,326,382</u> | <u>8,687,947</u> |
| Weighted Average Shares Outstanding - Diluted | <u>9,475,413</u> | <u>9,284,047</u> | <u>9,326,382</u> | <u>8,687,947</u> |

See accompanying notes to the consolidated financial statements.

AERKOMM INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows
For the Nine-Month Periods Ended September 30, 2019 and 2018
(Unaudited)

| | Nine Months Ended September 30, | |
|------------------------------------------------------------------------------|--------------------------------------------|---------------------|
| | 2019 | 2018 |
| Cash Flows from Operating Activities | | |
| Net loss | \$ (6,880,213) | \$ (6,087,387) |
| Adjustments to reconcile net loss to net cash used for operating activities: | | |
| Depreciation and amortization | 1,126,090 | 458,316 |
| Stock-based compensation expense | 1,394,669 | 1,062,140 |
| R&D expenses transferred from inventory and construction in progress | 416,231 | 439,296 |
| Consulting expense adjustment from change in fair value of warrants | 255,900 | - |
| Reversal of consulting expense and interest expense on warrants | (121,733) | - |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | 1,095,061 | (1,745,000) |
| Inventories | (1,485,350) | - |
| Prepaid expenses | (973,321) | (1,205,910) |
| Other receivable – related party | (111,111) | 46,743 |
| Other receivable – others | 1,155 | (6,804) |
| Temporary deposit – related party | 100,067 | - |
| Other current assets | (2,639) | (3,145) |
| Deposits – related party | 2,462 | (7,403) |
| Deposits – others | (2,714) | 101,610 |
| Accounts payable | (840,092) | 1,650,000 |
| Accrued expenses | (66,301) | (481,763) |
| Other payable - related parties | (61,662) | (214,316) |
| Other payable - others | (1,577,838) | (1,253,797) |
| Operating lease liability | (304,014) | - |
| Net Cash Used for Operating Activities | <u>(8,035,353)</u> | <u>(7,247,420)</u> |
| Cash Flows from Investing Activities | | |
| Prepayment on land and satellite equipment | (624,462) | (33,850,000) |
| Purchase of property and equipment | (6,455) | (241,169) |
| Net Cash Used for Investing Activities | <u>(630,917)</u> | <u>(34,091,169)</u> |
| Cash Flows from Financing Activities | | |
| Repayment of short-term bank loan | - | (10,000) |
| Proceeds from long-term loan | 45,765 | - |
| Proceeds from issuance of common stock | 10,810,688 | 41,262,899 |
| Proceeds from subscribed capital | - | 56,000 |
| Issuance of stock warrants | 5,000 | 906,167 |
| Net Cash Provided by Financing Activities | <u>10,861,453</u> | <u>42,215,066</u> |
| Net Increase in Cash | 2,195,183 | 876,477 |
| Cash, Beginning of Period | 88,309 | 21,504 |
| Foreign Currency Translation Effect on Cash | 524,531 | (1,208) |
| Cash, End of Period | <u>\$ 2,808,023</u> | <u>\$ 896,773</u> |
| Supplemental disclosures of cash flow information: | | |
| Cash paid during the period for income taxes | <u>\$ -</u> | <u>\$ 4,000</u> |
| Cash paid during the period for interest | <u>\$ 338</u> | <u>\$ 2,121</u> |
| Non-cash Operating and Financing Activities: | | |
| Restricted stock deposit liability transferred to common stock | <u>\$ -</u> | <u>\$ (1,644)</u> |

See accompanying notes to the consolidated financial statements.

NOTE 1 - Organization

Aerkomm Inc. (formerly Maple Tree Kids Inc.) (“Aerkomm”) was incorporated on August 14, 2013 in the State of Nevada. Aerkomm was a retail distribution company selling all of its products over the internet in the United States, operating in the infant and toddler products business market. Aerkomm’s common stock is quoted for trading on the OTC Markets Group Inc. OTCQX Best Market under the symbol “AKOM.” On July 17, 2019, the French *Autorité des Marchés Financiers* (the “AMF”) granted visa number 19-372 on the prospectus relating to the admission of Aerkomm’s common stock to list and trade on the Professional Segment of the regulated market of Euronext Paris (“Euronext Paris”). Aerkomm’s common stock began trading on Euronext Paris on July 23, 2019 under the symbol “AKOM” and is denominated in Euros on Euronext Paris. This listing did not alter Aerkomm’s share count, capital structure, or current common stock listing on the OTCQX, where it is also traded (in US dollars) under the symbol “AKOM.”

On December 28, 2016, Aircom Pacific Inc. (“Aircom”) purchased 140,000 shares of Aerkomm’s common stock, representing approximately 86.3% of Aerkomm’s issued and outstanding common stock as of the closing date of purchase. As a result of the transaction, Aircom became the controlling shareholder of Aerkomm. Aircom was incorporated on September 29, 2014 under the laws of the State of California.

On February 13, 2017, Aerkomm entered into a share exchange agreement (“Exchange Agreement”) with Aircom and its shareholders, pursuant to which Aerkomm acquired 100% of the issued and outstanding capital stock of Aircom in exchange for approximately 99.7% of the issued and outstanding capital stock of Aerkomm (or 87.81% on a fully-diluted basis). As a result of the share exchange, Aircom became a wholly-owned subsidiary of Aerkomm, and the former shareholders of Aircom became the holders of approximately 99.7% of Aerkomm’s issued and outstanding capital stock.

On December 31, 2014, Aircom acquired a newly incorporated subsidiary, Aircom Pacific Ltd. (“Aircom Seychelles”), a corporation formed under the laws of the Republic of Seychelles. Aircom Seychelles was formed to facilitate Aircom’s global corporate structure for both business operations and tax planning. Presently, Aircom Seychelles has no operations. Aircom is working with corporate and tax advisers in finalizing its global corporate structure and has not yet concluded its final plan.

On October 17, 2016, Aircom acquired a wholly owned subsidiary, Aircom Pacific Inc. Limited (“Aircom HK”), a corporation formed under the laws of Hong Kong. The purpose of Aircom HK is to conduct Aircom’s business and operations in Hong Kong. Presently, its primary function is business development, both with respect to airlines as well as content providers and advertisement partners based in Hong Kong. Aircom HK is also actively seeking strategic partnerships whom Aircom may leverage in order to provide more and better services to its customers. Aircom also plans to provide local supports to Hong Kong-based airlines via Aircom HK and teleports located in Hong Kong.

On December 15, 2016, Aircom acquired a wholly owned subsidiary, Aircom Japan, Inc. (“Aircom Japan”), a corporation formed under the laws of Japan. The purpose of Aircom Japan is to conduct business development and operations located within Japan. Aircom Japan is in the process of applying for, and will be the holder of, Satellite Communication Blanket License in Japan, which is necessary for Aircom to provide services within Japan. Aircom Japan will also provide local supports to airlines operating within the territory of Japan.

Aircom Telecom LLC (“Aircom Taiwan”), which became a wholly owned subsidiary of Aircom in December 2017, was organized under the laws of Taiwan on June 29, 2016. Aircom Taiwan is responsible for Aircom’s business development efforts and general operations within Taiwan.

On June 13, 2018, Aerkomm established a new wholly owned subsidiary, Aerkomm Taiwan Inc. (“Aerkomm Taiwan”), a corporation formed under the laws of Taiwan. The purpose of Aerkomm Taiwan is to purchase a parcel of land and raise sufficient fund for ground station building and operate the ground station for data processing (although that cannot be guaranteed).

On November 15, 2018, Aircom Taiwan acquired a wholly owned subsidiary, Beijing Yatai Communication Co., Ltd. (“Aircom Beijing”), a corporation formed under the laws of China. The purpose of Aircom Beijing is to conduct Aircom’s business and operations in China. Presently, its primary function is business development, both with respect to airlines as well as content providers and advertisement partners based in China as most business conducted in China requires a local registered company. Aircom Beijing is also actively seeking strategic partnerships whom Aircom may leverage in order to provide more and better services to its customers. Aircom also plans to provide local supports to China-based airlines via Aircom Beijing and teleports located in China.

On October 31, 2019, Aircom Seychelles established a new a wholly owned subsidiary, Aerkomm Pacific Limited (“Aerkomm Malta”), a corporation formed under the laws of Malta. The purpose of Aerkomm Malta is to conduct Aircom’s business and operations to engage with suppliers and potential airlines customers in the European Union.

Aircom and its subsidiaries are full-service, development stage providers of in-flight entertainment and connectivity (“IFEC”) solutions with their initial market in the Asia Pacific region.

NOTE 1 - Organization - Continued

Aerkomm and its subsidiaries (the “Company”) have not generated significant revenues, excluding non-recurring revenues from affiliates in the second quarter of fiscal 2018, and will incur additional expenses as a result of being a public reporting company. Currently, the Company has taken measures that management believes will improve its financial position by financing activities, including through ongoing public offerings, short-term borrowings and equity contributions. On April 23, 2019, the Company filed a post-effective amendment No. 2 (“POS AM No.2”) with the Securities and Exchange Commission (the “SEC”), to extend the public offering to attempt to raise the then remaining \$16.44 million of the originally registered public offering amount, as well as the \$9 million over-subscription option amount (see Note 11). On May 17, 2019, the Company filed a post-effective amendment No. 3 with the SEC to further amend POS AM No. 2 and which was declared effective by the SEC on May 23, 2019. Furthermore, two of the Company’s current shareholders (the “Lenders”) each committed to provide to the Company a \$10 million bridge loan (together, the “Loans”) for an aggregate principal amount of \$20 million, to bridge the Company’s cash flow needs prior to its obtaining a mortgage loan to be secured by a parcel of land (the “Land”) the Company intends to purchase in Taiwan. The Lenders also agreed to an earlier closing of up to 25% of the principal amounts of the Loans upon the Company’s request prior to the time that title to the Land is vested in the Company’s subsidiary, Aerkomm Taiwan, to pay the outstanding payable to the Company’s vendors. As of September 30, 2019, the Company completed two closings in the aggregate gross amount of \$11,459,998, or net amount of \$10,715,758, and issued 269,647 shares of common stock. With the \$4.98 million to be raised in the remainder of the Company’s ongoing public offering, the \$20 million in Loans committed by the Lenders and future capital raising, the Company believes its working capital will be adequate to sustain its operations for the next twelve months.

On January 16, 2019, the Company completed a 1-for-5 reverse split of the Company’s authorized, issued and outstanding shares of common stock, which was completed by the filing of a Certificate of Change Pursuant to NRS 78.209 with the Nevada Secretary of State on December 26, 2018 (see Note 11). All of the references in these financial statements to authorized common stock and issued and outstanding common stock have been adjusted to reflect this reverse split.

NOTE 2 - Summary of Significant Accounting Policies

Changes in Fiscal Year

On March 18, 2018, the Company’s Board of Directors approved a change in the Company’s fiscal year end from December 31 to March 31. On February 12, 2019, the Company’s Board of Directors approved a change in the Company’s fiscal year end from March 31 to December 31. Year-over-year quarterly financial data continue to be comparative to prior periods as the three months that comprise each fiscal quarter in the new fiscal year are the same as those in the Company’s historical financial statements.

Unaudited Interim Financial Information

The accompanying consolidated balance sheet as of September 30, 2019, and the consolidated statements of operations and comprehensive loss and cash flows for the three and nine months ended September 30, 2019 and 2018 are unaudited. The unaudited interim consolidated financial statements have been prepared on the same basis as the annual consolidated financial statements and, in the opinion of management, reflect all adjustments, which include only normal recurring adjustments, necessary to present fairly the Company’s financial position as of September 30, 2019 and the results of operations and cash flows for the three and nine months ended September 30, 2019 and 2018. The financial data and other information disclosed in these notes to the consolidated financial statements related to these three- and nine-month periods are unaudited. The results of operations for the nine months ended September 30, 2019 are not necessarily indicative of the results to be expected for the year ending December 31, 2019 or for any other interim period or other future year.

Principle of Consolidation

Aerkomm consolidates the accounts of its subsidiaries, Aircom, Aircom Seychelles, Aircom HK, Aircom Japan, Aircom Taiwan, Aerkomm Taiwan and Aircom Beijing. All significant intercompany accounts and transactions have been eliminated in consolidation.

Reclassifications of Prior Period Presentation

Certain prior period balance sheet and income statement amounts have been reclassified for consistency with the current period presentation. These reclassifications had no effect on the reported results of operations.

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results may differ from these estimates.

NOTE 2 - Summary of Significant Accounting Policies - Continued

Concentrations of Credit Risk

Financial instruments that potentially subject the Company to significant concentrations of credit risk consist primarily of cash in banks. As of September 30, 2019 and December 31, 2018, the total balance of cash in bank exceeding the amount insured by Federal Deposit Insurance Corporation (“FDIC”) for the Company was approximately \$2,060,000 and \$0, respectively. The balance of cash deposited in foreign financial institutions exceeding the amount insured by local deposit insurance is approximately \$75,000.

The Company performs ongoing credit evaluation of its customers and requires no collateral. An allowance for doubtful accounts is provided based on a review of the collectability of accounts receivable. The Company determines the amount of allowance for doubtful accounts by examining its historical collection experience and current trends in the credit quality of its customers as well as its internal credit policies. Actual credit losses may differ from management’s estimates.

Inventories

Inventories are recorded at the lower of weighted-average cost or net realizable value. The Company assesses the impact of changing technology on its inventory on hand and writes off inventories that are considered obsolete. Estimated losses on scrap and slow-moving items are recognized in the allowance for losses.

Property and Equipment

Property and equipment are stated at cost less accumulated depreciation. When value impairment is determined, the related assets are stated at the lower of fair value or book value. Significant additions, renewals and betterments are capitalized. Maintenance and repairs are expensed as incurred.

Depreciation is computed by using the straight-line and double declining methods over the following estimated service lives: ground station equipment – 5 years, computer equipment - 3 to 5 years, furniture and fixtures - 5 years, satellite equipment – 5 years, vehicles – 5 years and lease improvement – 5 years.

Upon sale or disposal of property and equipment, the related cost and accumulated depreciation are removed from the corresponding accounts, with any gain or loss credited or charged to income in the period of sale or disposal.

The Company reviews the carrying amount of property and equipment for impairment when events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. It determined that there was no impairment loss for the three-month and nine-month periods ended September 30, 2019.

Right-of-Use Asset and Lease Liability

In February 2016, the FASB issued ASU No. 2016-02, “Leases” (Topic 842) (“ASU 2016-02”), which modifies lease accounting for both lessees and lessors to increase transparency and comparability by recognizing lease assets and lease liabilities by lessees for those leases classified as operating leases under previous accounting standards and disclosing key information about leasing arrangements.

A lessee should recognize the lease liability to make lease payments and the right-of-use asset representing its right to use the underlying asset for the lease term. For operating leases, a right-of-use asset and a lease liability are initially measured at the present value of the lease payments. The amortization of the right-of-use asset is allocated over the lease term generally on a straight-line basis.

For the lease within a term of twelve months or less, a lessee is permitted to make an accounting policy election by class of underlying asset not to recognize lease assets and lease liabilities. If a lessee makes this election, it should recognize lease expense for such leases generally on a straight-line basis over the lease term. The Company adopted ASU 2016-02 effective January 1, 2019.

Goodwill and Purchased Intangible Assets

The Company’s goodwill represents the amount by which the total purchase price paid exceeded the estimated fair value of net assets acquired from acquisition of subsidiaries. The Company tests goodwill for impairment on an annual basis, or more often if events or circumstances indicate that there may be impairment.

Purchased intangible assets with finite life are amortized on the straight-line basis over the estimated useful lives of respective assets. Purchased intangible assets with indefinite life are evaluated for impairment when events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Purchased intangible asset consists of satellite system software and is amortized over 10 years.

NOTE 2 - Summary of Significant Accounting Policies - Continued

Fair Value of Financial Instruments

The Company utilizes the three-level valuation hierarchy for the recognition and disclosure of fair value measurements. The categorization of assets and liabilities within this hierarchy is based upon the lowest level of input that is significant to the measurement of fair value. The three levels of the hierarchy consist of the following:

Level 1 - Inputs to the valuation methodology 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 to the valuation methodology are quoted prices for similar assets and liabilities in active markets, quoted prices in markets that are not active or inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the instrument.

Level 3 - Inputs to the valuation methodology are unobservable inputs based upon management's best estimate of inputs market participants could use in pricing the asset or liability at the measurement date, including assumptions.

The carrying amounts of the Company's cash, accounts receivable, other receivable, short-term loan and other payable approximated their fair value due to the short-term nature of these financial instruments. The Company's long-term loan approximated the carrying amount as its interest rate is considered as approximate to the current rate for comparable loans. There were no outstanding derivative financial instruments as of September 30, 2019.

Revenue Recognition

The Company recognizes revenue when performance obligations identified under the terms of contracts with its customers are satisfied, which generally occurs upon the transfer of control in accordance with the contractual terms and conditions of the sale. The Company's major revenue for the nine-month period ended September 30, 2019 was the sales of compact adaptor for smartphone that allows users to turn their smartphone into a satellite smartphone to provide reliable connectivity beyond the coverage of traditional networks. The majority of the Company's revenue is recognized at a point in time when product is shipped or service is provided to the customer. Revenue is measured as the amount of consideration the Company expects to receive in exchange for transferring goods, which includes estimates for variable consideration.

Research and Development Costs

Research and development costs are charged to operating expenses as incurred. For the nine-month periods ended September 30, 2019 and 2018, the Company incurred \$416,231 (unaudited) and \$765,750 (unaudited) of research and development costs, respectively.

Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are computed for differences between the financial statement and tax bases of assets and liabilities that will result in taxable or deductible amounts in the future based on enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized. Income tax expense is the tax payable or refundable for the period plus or minus the change during the period in deferred tax assets and liabilities. Adjustments to prior period's income tax liabilities are added to or deducted from the current period's tax provision.

The Company follows FASB guidance on uncertain tax positions and has analyzed its filing positions in all the federal, state and foreign jurisdictions where it is required to file income tax returns, as well as all open tax years in those jurisdictions. The Company files income tax returns in the US federal, state and foreign jurisdictions where it conducts business. The Company believes that its income tax filing positions and deductions will be sustained on audit and does not anticipate any adjustments that will result in a material adverse effect on its consolidated financial position, results of operations, or cash flows. Therefore, no reserves for uncertain tax positions have been recorded. The Company does not expect its unrecognized tax benefits to change significantly over the next twelve months.

The Company's policy for recording interest and penalties associated with any uncertain tax positions is to record such items as a component of income before taxes. Penalties and interest paid or received, if any, are recorded as part of other operating expenses in the consolidated statement of operations.

NOTE 2 - Summary of Significant Accounting Policies - Continued

Foreign Currency Transactions

Foreign currency transactions are recorded in U.S. dollars at the exchange rates in effect when the transactions occur. Exchange gains or losses derived from foreign currency transactions or monetary assets and liabilities denominated in foreign currencies are recognized in current income. At the end of each period, assets and liabilities denominated in foreign currencies are revalued at the prevailing exchange rates with the resulting gains or losses recognized in income for the period.

Translation Adjustments

If a foreign subsidiary's functional currency is the local currency, translation adjustments will result from the process of translating the subsidiary's financial statements into the reporting currency of the Company. Such adjustments are accumulated and reported under other comprehensive income (loss) as a separate component of stockholders' equity.

Earnings (Loss) Per Share

Basic earnings (loss) per share is computed by dividing income available to common shareholders by the weighted average number of shares of common stock outstanding during the period. Diluted earnings per share is computed by dividing income available to common shareholders by the weighted-average number of shares of common outstanding during the period increased to include the number of additional shares of common stock that would have been outstanding if the potentially dilutive securities had been issued. Potentially dilutive securities include stock warrants and outstanding stock options, shares to be purchased by employees under the Company's employee stock purchase plan.

Subsequent Events

The Company has evaluated events and transactions after the reported period up to November 11, 2019, the date on which these consolidated financial statements were available to be issued. All subsequent events requiring recognition as of September 30, 2019 have been included in these consolidated financial statements.

NOTE 3 - Recent Accounting Pronouncements

Financial Instruments

In June 2016, the FASB issued ASU No. 2016-13, "Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments" ("ASU 2016-13"), which modifies the measurement of expected credit losses of certain financial instruments. ASU 2016-13 will be effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. The Company is currently evaluating the impact of adopting ASU 2016-13 on its consolidated financial statements.

Intangibles

In January 2017, the FASB issued ASU No. 2017-04, "Intangibles - Goodwill and Other" (Topic 350): Simplifying the Test for Goodwill Impairment, which goodwill shall be tested at least annually for impairment at a level of reporting referred to as a reporting unit. ASU 2017-04 will be effective for annual periods beginning after December 15, 2019. The Company is currently evaluating the impact of adopting ASU 2017-04 on its consolidated financial statements.

NOTE 4 - Inventories

As of September 30, 2019 and December 31, 2018, inventories consisted of the following:

| | September 30, 2019 | December 31, 2018 |
|-------------------------------------------------|-------------------------------|------------------------------|
| | (Unaudited) | |
| Satellite equipment for sale under construction | \$ 2,380,364 | \$ 895,014 |
| Supplies | 5,215 | 5,273 |
| | <u>2,385,579</u> | <u>900,287</u> |
| Allowance for inventory loss | (5,215) | (5,273) |
| Net | <u>\$ 2,380,364</u> | <u>\$ 895,014</u> |

As of December 31, 2018, the Company transferred inventories in the amount of \$11,029 to R&D expenses.

AERKOMM INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements

NOTE 5 - Property and Equipment

As of September 30, 2019 and December 31, 2018, the balances of property and equipment were as follows:

| | September 30, 2019 | December 31, 2018 |
|---------------------------------|-------------------------------|------------------------------|
| | (Unaudited) | |
| Ground station equipment | \$ 1,854,027 | \$ 1,854,027 |
| Computer software and equipment | 324,487 | 321,070 |
| Satellite equipment | 275,410 | 275,410 |
| Vehicle | 141,971 | 141,971 |
| Leasehold improvement | 83,721 | 84,721 |
| Furniture and fixture | 36,382 | 33,344 |
| | <u>2,715,998</u> | <u>2,710,543</u> |
| Accumulated depreciation | (731,806) | (322,049) |
| Net | 1,984,192 | 2,388,494 |
| Prepayments - land | 35,861,589 | 35,237,127 |
| Construction in progress | - | 416,231 |
| Net | <u>\$ 37,845,781</u> | <u>\$ 38,041,852</u> |

As of September 30, 2019, the balance of construction in progress was \$0 after the Company transferred \$416,231 (unaudited) to R&D expenses.

On May 1, 2018, the Company and Aer Komm Taiwan entered into a binding memorandum of understanding with Tsai Ming-Yin (the "Seller") with respect to the acquisition by Aer Komm Taiwan of a parcel of land located in Taiwan. The land is expected to be used to build a satellite ground station and data center. On July 10, 2018, the Company, Aer Komm Taiwan and the Seller entered into a certain real estate sales contract regarding this acquisition. Pursuant to the terms of the contract, and subsequent amendments on July 30, 2018, September 4, 2018, November 2, 2018 and January 3, 2019, the Company paid to the seller in installments refundable prepayment of \$33.85 million as of December 31, 2018. On July 2, 2019, the Company paid the remaining purchase price of \$624,462. As of September 30, 2019, the estimated commission payable for the land purchase in the amount of \$1,360,770 (unaudited) was recorded to the cost of land and the payment to be paid after the full payment of the Land acquisition price until no later than December 31, 2020.

Depreciation expense was \$136,449 (unaudited) and \$42,895 (unaudited) for the three-month periods ended September 30, 2019 and 2018 and \$409,757 (unaudited) and \$87,030 (unaudited) for the nine-month periods ended September 30, 2019 and 2018, respectively.

NOTE 6 - Intangible Asset, Net

As of September 30, 2019 and December 31, 2018, the cost and accumulated amortization for intangible asset were as follows:

| | September 30, 2019 | December 31, 2018 |
|---------------------------|-------------------------------|------------------------------|
| | (Unaudited) | |
| Satellite system software | \$ 4,950,000 | \$ 4,950,000 |
| Accumulated amortization | (1,938,750) | (1,567,500) |
| Net | <u>\$ 3,011,250</u> | <u>\$ 3,382,500</u> |

Amortization expense was \$123,750 (unaudited) and \$123,750 (unaudited) for the three-month periods ended September 30, 2019 and 2018 and \$371,250 (unaudited) and \$371,250 (unaudited) for the nine-month periods ended September 30, 2019 and 2018, respectively.

NOTE 7 - Operating Lease Right-of-Use Asset

As of September 30, 2019, the cost and accumulated amortization for operating lease right-of-use asset were as follows:

| | September 30, 2019 |
|--------------------------|-------------------------------|
| | (Unaudited) |
| Right-of-use asset | \$ 669,602 |
| Accumulated amortization | (304,770) |
| Net | <u>\$ 364,832</u> |

Amortization expense of right-of-use asset was \$101,088 (unaudited) and \$345,083 (unaudited) for the three months and nine months ended September 30, 2019.

On June 15, 2019, the lease agreement in Aircom Taiwan was terminated, so the Company disposed the fully amortized right-of-use asset \$40,313 (unaudited).

NOTE 8 - Long-term Loan

The Company has a car loan credit line of NT\$1,500,000 (approximately US\$48,371), which matures on May 21, 2024, from a Taiwan financing company with annual interest rate of 9.7%. The installment payment plan is 60 months to pay off the balance on the 21st of each month. Future installment payments as of September 30, 2019 are as follows:

| | |
|------------------------------------|------------------|
| Twelve months ending September 30, | (Unaudited) |
| 2020 | \$ 12,232 |
| 2021 | 12,232 |
| 2022 | 12,232 |
| 2023 | 12,232 |
| 2024 | <u>8,154</u> |
| Total installment payments | 57,082 |
| Less: Imputed interest | <u>(11,317)</u> |
| Present value of long-term loan | 45,765 |
| Current portion | <u>8,150</u> |
| Non-current portion | <u>\$ 37,615</u> |

NOTE 9 - Lease Liability

A. Lease term and discount rate

The weighted-average remaining lease term (in years) and discount rate related to the operating leases were as follows:

| | |
|---------------------------------------|---------------------------------------------------------|
| | Nine Months Ended September 30, 2019 |
| | (Unaudited) |
| Weighted-average remaining lease term | 0.58 year |
| Weighted-average discount rate | 6.00% |

As most of our leases do not provide an implicit rate, we use the prime rate based on the information available at the lease commencement date to determine the present value of lease payments.

B. Maturity of lease liabilities

| | Related Party | Others | Total |
|------------------------------------|--------------------------|------------------|------------------|
| | (Unaudited) | (Unaudited) | (Unaudited) |
| 10/1/2019-9/30/2020 | \$ 34,321 | \$ 363,265 | \$ 397,586 |
| 10/1/2020-9/30/2021 | - | 20,000 | 20,000 |
| Total lease payments | <u>34,321</u> | <u>383,265</u> | <u>417,586</u> |
| Less: Imputed interest | (843) | (10,842) | (11,685) |
| Present value of lease liabilities | <u>33,478</u> | <u>372,423</u> | <u>405,901</u> |
| Current portion | <u>33,478</u> | <u>352,523</u> | <u>386,001</u> |
| Non-current portion | <u>\$ -</u> | <u>\$ 19,900</u> | <u>\$ 19,900</u> |

NOTE 10 - Income Taxes

Income tax expense for the three-month and nine-month periods ended September 30, 2019 and 2018 consisted of the following:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|----------|---------------------------------------------|-------------|--------------------------------------------|-----------------|
| | 2019 | 2018 | 2019 | 2018 |
| | (Unaudited) | (Unaudited) | (Unaudited) | (Unaudited) |
| Current: | | | | |
| Federal | \$ - | \$ - | \$ - | \$ - |
| State | - | - | 1,600 | 2,400 |
| Foreign | - | - | 1,635 | 1,662 |
| Total | <u>\$ -</u> | <u>\$ -</u> | <u>\$ 3,235</u> | <u>\$ 4,062</u> |

The following table presents a reconciliation of the Company's income tax at statutory tax rate and income tax at effective tax rate for the three-month and nine-month periods ended September 30, 2019 and 2018.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|-----------------------------------------|---------------------------------------------|--------------|--------------------------------------------|-----------------|
| | 2019 | 2018 | 2019 | 2018 |
| | (Unaudited) | (Unaudited) | (Unaudited) | (Unaudited) |
| Tax benefit at statutory rate | \$ (688,749) | \$ (524,572) | \$ (1,703,699) | \$ (1,266,726) |
| Net operating loss carryforwards (NOLs) | 543,562 | 574,508 | 1,235,409 | 1,287,325 |
| Foreign investment losses | 107,200 | 34,551 | 290,900 | 49,200 |
| Stock-based compensation expense | 154,400 | 84,574 | 292,900 | 223,019 |
| Amortization expense | 58,700 | (62,700) | 33,100 | (66,100) |
| Accrued R&D expense | - | - | - | (168,000) |
| Accrued payroll | 900 | - | (40,900) | - |
| Accrued professional expense | - | (47,900) | - | (47,900) |
| Accrued consulting expense | (122,300) | - | (122,300) | - |
| Others | (53,713) | (58,461) | 17,825 | (6,756) |
| Tax expense at effective tax rate | <u>\$ -</u> | <u>\$ -</u> | <u>\$ 3,235</u> | <u>\$ 4,062</u> |

Deferred tax assets (liability) as of September 30, 2019 and December 31, 2018 consist approximately of:

| | September 30, 2019 | December 31, 2018 |
|---------------------------------------------------|-------------------------------|------------------------------|
| | (Unaudited) | |
| Net operating loss carryforwards (NOLs) | \$ 6,234,000 | \$ 5,632,000 |
| Stock-based compensation expense | 1,283,000 | 893,000 |
| Accrued expenses and unpaid expense payable | 52,000 | 184,000 |
| Tax credit carryforwards | 68,000 | 68,000 |
| Excess of tax amortization over book amortization | (629,000) | (818,000) |
| Others | 357,000 | 131,000 |
| Gross | <u>7,365,000</u> | <u>6,090,000</u> |
| Valuation allowance | (7,365,000) | (6,090,000) |
| Net | <u>\$ -</u> | <u>\$ -</u> |

Management does not believe the deferred tax assets will be utilized in the near future; therefore, a full valuation allowance is provided. The net change in deferred tax assets valuation allowance was an increase of approximately \$1,275,000 (unaudited) for the nine months ended September 30, 2019.

As of September 30, 2019 and December 31, 2018, the Company had federal NOLs of approximately \$8,243,000 available to reduce future federal taxable income, expiring in 2037, and additional federal NOLs of approximately \$10,443,000 (unaudited) and \$5,743,000, respectively, were generated and will be carried forward indefinitely to reduce future federal taxable income. As of September 30, 2019 and December 31, 2018, the Company had State NOLs of approximately \$24,328,000 (unaudited) and \$21,049,000 respectively, available to reduce future state taxable income, expiring in 2039.

As of September 30, 2019 and December 31, 2018, the Company has Japan NOLs of approximately \$337,000 (unaudited) and \$319,000, respectively, available to reduce future Japan taxable income, expiring in 2029.

NOTE 10 - Income Taxes - Continued

As of September 30, 2019 and December 31, 2018, the Company has Taiwan NOLs of approximately \$2,189,000 (unaudited) and \$879,000, respectively, available to reduce future Taiwan taxable income, expiring in 2029.

As of September 30, 2019 and December 31, 2018, the Company had approximately \$37,000 (unaudited) and \$37,000 of federal research and development tax credit, available to offset future federal income tax. The credit begins to expire in 2034 if not utilized. As of September 30, 2019 and December 31, 2018, the Company had approximately \$39,000 (unaudited) and \$39,000 of California state research and development tax credit available to offset future California state income tax. The credit can be carried forward indefinitely.

The Company's ability to utilize its federal and state NOLs to offset future income taxes is subject to restrictions resulting from its prior change in ownership as defined by Internal Revenue Code Section 382. The Company does not expect to incur the limitation on NOLs utilization in future annual usage.

NOTE 11 - Capital Stock

1) Preferred Stock:

The Company is authorized to issue 50,000,000 shares of preferred stock, with par value of \$0.001. As of September 30, 2019, there were no preferred stock shares outstanding. The Board of Directors has the authority to issue preferred stock in one or more series, and in connection with the creation of any such series, by resolutions providing for the issuance of the shares thereof, to determine dividends, voting rights, conversion rights, redemption privileges and liquidation preferences.

2) Common Stock:

The Company is authorized to issue 90,000,000 shares of common stock, reflecting a reverse split in the ratio of 1 for 5 effective January 16, 2019, with par value of \$0.001.

On February 13, 2017, all of Aircom's 5,513,334 restricted shares were converted to 2,055,947 shares of Aerkomm's restricted stock at the ratio of 2.681651 to 1, pursuant to the Exchange Agreement (see Note 1). As of September 30, 2019 and December 31, 2018, the restricted shares consisted of the following:

| | September 30, 2019 | December 31, 2018 |
|-------------------------------|-------------------------------|------------------------------|
| | (Unaudited) | |
| Restricted stock - vested | 1,802,373 | 1,802,373 |
| Restricted stock - unvested | 149,162 | 149,162 |
| Total restricted stock | 1,951,535 | 1,951,535 |

The unvested shares of restricted stock were recorded under a deposit liability account awaiting future conversion to common stock when they become vested. On December 21, 2018, the Company repurchased and cancelled an aggregate of 104,413 unvested shares of restricted common stock for a purchase price of \$0.0067 per share.

On May 14, 2018, the Company entered into an underwriting agreement (the "Underwriting Agreement") with Boustead Securities, LLC ("Boustead") in connection with the public offering (the "Offering"), issuance and sale of up to 1,411,782 shares of the Company's common stock on a best efforts basis, with a minimum requirement of 117,647 shares, at the public offering price of \$42.50 per share (originally \$8.5 per share before the 1-to-5 reverse split), less underwriting discounts, for minimum gross proceeds of \$5,000,000 and up to a maximum of \$60,000,000. As of December 31, 2018, pursuant to the Underwriting Agreement, the Company had issued an aggregate of 1,024,980 shares of common stock (including 19 shares that were added as a result of rounding in connection with the one-for-five reverse split concluded on January 16, 2019) for gross proceeds of \$43,560,894, or net proceeds of \$39,810,204. On April 23, 2019, the Company filed a post-effective amendment No. 2 with the Securities and Exchange Commission (the "SEC") to extend the Offering to attempt to raise the then remaining \$16.44 million of the amount that was originally registered in the Offering, as well as a \$9 million over-subscription option amount. On May 17, 2019, the Company filed a post-effective amendment No. 3 with the Securities and Exchange Commission (the "SEC") to extend the Offering subsequently and which was declared effective by the SEC on May 23, 2019. As of September 30, 2019, the Company completed two closings in the aggregate gross amount of \$11,459,998, or net amount of \$10,715,758, and issued 269,647 shares of common stock.

On July 2, 2019, the board of directors approved a supplement to the engagement agreement with one of the Company's service providers pursuant to which the Company agreed to issue to the service provider 23,972 restricted shares of the Company's common stock in consideration of that service provider's agreement to defer the receipt of payment of certain accrued fees due to the service provider.

NOTE 11 - Capital Stock - Continued

3) Stock Warrant:

The Company has entered into a service agreement which provides for the issuance of warrants to purchase shares of its common stock to a service provider as payment for services. The warrants allow the service provider to purchase a number of shares of Aerkomm common stock equal to the service fee value divided by 85% of the share price paid by investors for Aerkomm's common stock in the first subsequent qualifying equity financing event, at an exercise price of \$0.05 per share. For the nine-month periods ended September 30, 2019 and 2018, Aerkomm has issued additional stock warrants exercisable for \$0 and \$26,667, respectively, in value of Aerkomm common stock to the service provider as payment for additional services. As of June 28, 2019, these warrants are equivalent to 4,891 shares of the Company's common stock. On June 29, 2019, the Company settled with the service provider to cancel all these warrants with \$75,000 in three installments payable on July 3, August 1, and September 1, 2019 and all three installments were paid on schedule.

In connection with the Underwriting Agreement with Boustead, the Company agreed to issue to Boustead warrants to purchase a number of the Company's shares equal to 6% of the gross proceeds of the public offering, which shall be exercisable, in whole or in part, commencing on April 13, 2018 and expiring on the five-year anniversary at an initial exercise price of \$53.125 per share, which is equal to 125% of the offering price paid by investors. As of September 30, 2019 and 2018, the Company has issued warrants to Boustead to purchase 77,680 and 61,498 shares, respectively, of the Company's stock and the total warrant value is \$454,600 (unaudited) and \$849,500, respectively. For the nine-month period ended September 30, 2019 and 2018, the Company recorded \$260,900 (unaudited) and \$171,300 (unaudited), respectively, of consulting fee with the corresponding account of additional paid-in capital as the adjustment for the issuance costs of these stock warrants.

NOTE 12 - Major Customer

The Company has one major customer, which represents 10% or more of the total sales of the Company for the period. Sales to and account receivable from the customer for the nine months ended and as of September 30, 2019 were \$1,599,864 (unaudited) and \$649,939 (unaudited), respectively.

NOTE 13 - Major Vendor

The Company has one major vendor, which represents 10% or more of the total purchases of the Company for the period. Purchases from and account payable to the vendor for the nine months ended and as of September 30, 2019 were \$1,587,222 (unaudited) and \$506,308 (unaudited), respectively.

NOTE 14 - Related Party Transactions

A. Name of related parties and relationships with the Company:

| Related Party | Relationship |
|--------------------------------------------------|-----------------------------------------------------------------------------------------------------------------|
| Dmedia Holding LP ("Dmedia") | Major stockholder |
| Bummy Wu | Shareholder |
| Jeffrey Wun | Shareholder and CEO of Aerkomm and Aircom |
| Yih Lieh (Giretsu) Shih | President of Aircom Japan |
| Chien Ming Tseng | President of Aircom Taiwan |
| Hao Wei Peng | Employee of Aircom Taiwan and founding owner of Aircom Taiwan prior to 12/19/2017 |
| Louis Giordimaina | COO - Aviation of Aircom |
| Wealth Wide Int'l Ltd. ("WWI") | Bummy Wu, a shareholder, is the Chairman |
| WISD Intellectual Property Agency, Ltd. ("WISD") | Patrick Li, Director of Aircom, is the Chairman; Chih-Ming (Albert) Hsu, Director of the Company, is a Director |

NOTE 14 - Related Party Transactions - Continued

B. Significant related party transactions:

The Company has extensive transactions with its related parties. It is possible that the terms of these transactions are not the same as those which would result from transactions among wholly unrelated parties.

a. As of September 30, 2019 and December 31, 2018:

| | September 30, 2019 | December 31, 2018 |
|-----------------------------------------------------|-------------------------------|------------------------------|
| | (Unaudited) | |
| Other receivable from Chien Ming Tseng ¹ | \$ 111,111 | \$ - |
| Temporary deposit to Bummy Wu ² | \$ - | \$ 100,067 |
| Operating lease liability to WWI ³ | \$ 33,478 | \$ - |
| Other payable to: | | |
| Hao Wei Peng ⁴ | \$ 47,201 | \$ - |
| WWI ³ | 39,179 | 39,224 |
| Jeffrey Wun ⁴ | 12,807 | 46,236 |
| Louis Giordimaina ⁴ | 3,019 | 6,071 |
| Yih Lieh (Giretsu) Shih ⁴ | - | 15,497 |
| Others ⁴ | 9,986 | 66,826 |
| Total | <u>\$ 112,192</u> | <u>\$ 173,854</u> |

1. Represents temporary advances to employees for payments of previously accrued expenses for regular operating activities, to be offset with the Company's accrued expenses pending official receipts.
 2. In November 2018, Aircom HK's bank account was temporarily frozen by its local bank in Hong Kong (the "HK bank") due to Aircom HK's failure to timely submit to the HK bank corporate documentation relating to the corporate organization and goodstanding of Aircom HK's parent company, Aircom, and Aircom's parent company, Aerkomm. To avoid a potential cash flow issue resulting from this temporary account freeze, Aircom HK withdrew \$100,067 in cash from the HK bank and temporarily deposited it in an existing related party's bank account at a different bank for safe keeping. The Aircom HK's bank account with the HK bank was reactivated by the HK bank subsequently and the cash that was transferred to the related party's account was redeposited into Aircom HK's bank account at the HK bank in February 2019.
 3. Represents rent for a warehouse in Hong Kong to store the Company's hardware, which ended in May 2018, and rent for another Hong Kong office starting June 28, 2018.
 4. Represents payable to employees as a result of regular operating activities.
- b. For the three-month and nine-month periods ended September 30, 2019 and 2018:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|-----------------------------------------------------------|---------------------------------------------|-------------|--------------------------------------------|-------------|
| | 2019 | 2018 | 2019 | 2018 |
| | (Unaudited) | | (Unaudited) | |
| Consulting expense paid to Louis Giordimaina | \$ - | \$ - | \$ - | \$ 222,246 |
| Legal expense paid to WISD | - | 9,387 | - | 10,779 |
| Amortization expense of right-of-use asset charged by WWI | 11,456 | - | 34,328 | - |
| Rental expense charged by WWI | - | 14,706 | - | 17,840 |
| Interest expense charged by Dmedia | - | - | 1,744 | 3,116 |

On May 25, 2018, Mr. Louis Giordimaina was converted from a consultant to a full-time employee and was appointed as Chief Operating Officer – Aviation. The consulting expense paid for the nine-month period ended September 30, 2018 in the amount of \$222,246 represents the consulting services provided prior to the conversion.

NOTE 14 - Related Party Transactions - Continued

Aircom engaged WISD to handle its filing of patent and trademark applications.

The Company had a lease agreement with WWI with a monthly rental cost of \$450 that expired on May 31, 2018 and was not renewed. The Company has another lease agreement with WWI for its office space in Hong Kong with a monthly rental cost of HKD 30,000. The lease term is from June 28, 2018 to June 27, 2020. Effective January 1, 2019, the Company adopted ASU2016-02, "Leases" (Topic 842) ("ASU 2016-02"), and accounted for these leases under amortization of the lease payment under Note 9, Lease Liabilities.

NOTE 15 - Stock Based Compensation

In March 2014, Aircom's Board of Directors adopted the 2014 Stock Option Plan (the "Aircom 2014 Plan"). The Aircom 2014 Plan provided for the granting of incentive stock options and non-statutory stock options to employees, consultants and outside directors of Aircom. On February 13, 2017, pursuant to the Exchange Agreement, Aerkomm assumed the options of Aircom 2014 Plan and agreed to grant options to purchase an aggregate of 1,088,882 shares of the Company's common stock to Aircom's stock option holders.

One-third of stock option shares vested on the first anniversary of the grant date or the employee's acceptance to serve the Company, and the remainder of the grant vested and will vest in 36 equal monthly installments thereafter, subject to the grantee's continuous service through the applicable vesting date. Option prices for such options were determined by Aircom's Board of Directors. The Aircom 2014 Plan became effective upon its adoption by the Board and shall continue in effect for a term of 10 years unless sooner terminated under the terms of Aircom 2014 Plan.

On May 5, 2017, the Board of Directors of Aerkomm adopted the Aerkomm Inc. 2017 Equity Incentive Plan (the "Aerkomm 2017 Plan" and together with the Aircom 2015 Plan, the "Plans") and the reservation of 1,000,000 shares of the Company's common stock for future grant or issuance under the Aerkomm 2017 Plan. On June 23, 2017, the Board of Directors voted to increase the number of shares of common stock reserved for future grant or issuance under the Aerkomm 2017 Plan to 2,000,000 shares. The Aerkomm 2017 Plan provides for the granting of incentive stock options and non-statutory stock options to employees, consultants and outside directors of the Company, as determined by the Compensation Committee of the Board of Directors (or, prior to the establishment of the Compensation Committee on January 23, 2018, the Board of Directors).

On June 23, 2017, the Board of Directors approved the grant of options to purchase an aggregate of 291,000 shares under the Aerkomm 2017 Plan to certain officers and directors of the Company. The option agreements are classified into three types of vesting schedules, which include, 1) 1/6 of the shares subject to the option shall vest commencing on the vesting start date and the remaining shares shall vest at the rate of 1/60 for the next 60 months on the same day of the month as the vesting start date; 2) 1/4 of the shares subject to the option shall vest commencing on the vesting start date and the remaining shares shall vest at the rate of 1/36 for the next 36 months on the same day of the month as the vesting start date; 3) 1/3 of the shares subject to the option shall vest commencing on the first anniversary of vesting start date and the remaining shares shall vest at the rate of 50% each year for the next two years on the same day of the month as the vesting start date.

On July 31, 2017, the Board of Directors approved the grant of options to purchase an aggregate of 109,000 shares under the Aerkomm 2017 Plan to 11 of its employees. One-third of these shares subject to the options vested on the first anniversary of the grant date, one-third of the shares vested on the second anniversary of the grant date, and the remaining shares shall vest on the third anniversary of the grant date.

On December 29, 2017, the Board of Directors approved the grant of options to purchase 4,000 shares under the Aerkomm 2017 Plan to each of three of the Company's independent directors for an aggregate of 12,000 shares. All of these options vested immediately upon grant.

On June 19, 2018, the Compensation Committee approved the grant of options to purchase 32,000 and 30,000 shares under the Aerkomm 2017 Plan to two of the Company executives. One-fourth of the 32,000 shares subject to the option vested on May 1, 2019, and the remaining shares shall vest in three equal yearly installments thereafter. One-third of the 30,000 shares subject to the option vested on May 29, 2019, and the remaining shares shall vest in two equal yearly installments thereafter.

On September 16, 2018 and December 29, 2018, the Compensation Committee approved the grant of options to purchase 4,000 shares under the Aerkomm 2017 Plan to each of four of the Company's independent directors for an aggregate of 16,000 shares. All of these options vested immediately upon grant.

On July 2, 2019, the Board of Directors approved the grant of options to purchase an aggregate of 339,000 shares under the Aerkomm 2017 Plan to 22 of its directors, officers and employees. 25% of the shares vested on the grant date, 25% of the shares vested on July 17, 2019, 25% of the shares will vest on the first anniversary of the grant date, and 25% of the shares will vest upon the second anniversary of the grant date.

NOTE 15 - Stock Based Compensation - Continued

On October 4, 2019, the Board of Directors approved the grant of options to purchase an aggregate of 85,400 shares under the Aerkomm 2017 Plan to three (3) of its employees. 25% of the shares vested on the grant date, and 25% of the shares will vest on each of October 4, 2020, October 4, 2021 and October 4, 2022, respectively.

Option price is determined by the Compensation Committee. The Aerkomm 2017 Plan has been adopted by the Board and shall continue in effect for a term of 10 years unless sooner terminated under the terms of Aerkomm 2017 Plan. The Aerkomm 2017 Plan was approved by the Company's stockholders on March 28, 2018.

Valuation and Expense Information

Measurement and recognition of compensation expense based on estimated fair values is required for all share-based payment awards made to its employees and directors including employee stock options. The Company recognized compensation expense of \$1,394,670 and \$1,062,140 for the nine-month periods ended September 30, 2019 and 2018, respectively, related to such employee stock options.

Determining Fair Value

Valuation and amortization method

The Company uses the Black-Scholes option-pricing-model to estimate the fair value of stock options granted on the date of grant or modification and amortizes the fair value of stock-based compensation at the date of grant on a straight-line basis for recognizing stock compensation expense over the vesting period of the option.

Expected term

The expected term is the period of time that granted options are expected to be outstanding. The Company uses the SEC's simplified method for determining the option expected term based on the Company's historical data to estimate employee termination and options exercised.

Expected dividends

The Company does not plan to pay cash dividends before the options are expired. Therefore, the expected dividend yield used in the Black-Scholes option valuation model is zero.

Expected volatility

Since the Company has no historical volatility, it used the calculated value method which substitutes the historical volatility of a public company in the same industry to estimate the expected volatility of the Company's share price to measure the fair value of options granted under the Plans.

Risk-free interest rate

The Company based the risk-free interest rate used in the Black-Scholes option valuation model on the market yield in effect at the time of option grant provided in the Federal Reserve Board's Statistical Releases and historical publications on the Treasury constant maturities rates for the equivalent remaining terms for the Plans.

Forfeitures

The Company is required to estimate forfeitures at the time of grant and revises those estimates in subsequent periods if actual forfeitures differ from those estimates. The Company uses historical data to estimate option forfeitures and records share-based compensation expense only for those awards that are expected to vest.

NOTE 15 - Stock Based Compensation - Continued

The Company used the following assumptions to estimate the fair value of options granted in 2018 and 2019 under the Plans as follows:

Assumptions

| | |
|-------------------------|-----------------|
| Expected term | 10 years |
| Expected volatility | 59.83% - 61.91% |
| Expected dividends | 0% |
| Risk-free interest rate | 1.98% - 2.99% |
| Forfeiture rate | 0% - 10% |

Aircom 2014 Plan

A summary of the number of shares, weighted average exercise price and estimated fair value of options for Aircom 2014 Plan as of December 31, 2018 and September 30, 2019 is as follows:

| | Number of Shares | Weighted Average Exercise Price Per Share | Weighted Average Fair Value Per Share |
|-------------------------------------------|---------------------|-------------------------------------------------------|------------------------------------------------|
| Options outstanding at January 1, 2018 | 932,262 | \$ 0.4081 | \$ 0.1282 |
| Granted | - | - | - |
| Exercised | - | - | - |
| Forfeited/Cancelled | - | - | - |
| Options outstanding at December 31, 2018 | 932,262 | 0.4081 | 0.1282 |
| Granted | - | - | - |
| Exercised | - | - | - |
| Forfeited/Cancelled | - | - | - |
| Options outstanding at September 30, 2019 | <u>932,262</u> | 0.4081 | 0.1282 |
| Options exercisable at December 31, 2018 | <u>846,287</u> | 0.2892 | 0.0908 |
| Options exercisable at September 30, 2019 | <u>932,262</u> | 0.4081 | 0.1282 |

A summary of the status of nonvested shares under Aircom 2014 Plan as of December 31, 2018 and September 30, 2019 is as follows:

| | Number of Shares | Weighted Average Exercise Price Per Share |
|-----------------------------------------|---------------------|-------------------------------------------------------|
| Options nonvested at January 1, 2018 | 302,467 | \$ 0.8315 |
| Granted | - | - |
| Vested | (216,492) | 0.5349 |
| Forfeited/Cancelled | - | - |
| Options nonvested at December 31, 2018 | 85,975 | 1.5786 |
| Granted | - | - |
| Vested | (85,975) | 1.5715 |
| Forfeited/Cancelled | - | - |
| Options nonvested at September 30, 2019 | <u>-</u> | - |

NOTE 15 - Stock Based Compensation - Continued

Aerkomm 2017 Plan

A summary of the number of shares, weighted average exercise price and estimated fair value of options under Aerkomm 2017 Plan as of December 31, 2018 and September 30, 2019 is as follows:

| | Number of Shares | Weighted Average Exercise Price Per Share | Weighted Average Fair Value Per Share |
|-------------------------------------------------------|-----------------------------|------------------------------------------------------------------|----------------------------------------------------------|
| Options outstanding at January 1, 2018 | 253,000 | \$ 30.8824 | \$ 18.4796 |
| Granted | 78,000 | 19.7462 | 9.2500 |
| Exercised | - | - | - |
| Forfeited/Cancelled | (48,000) | 27.5000 | 16.4610 |
| Options outstanding at December 31, 2018 | <u>283,000</u> | <u>28.3867</u> | <u>16.2781</u> |
| Granted | 339,000 | 3.9600 | 2.0301 |
| Exercised | - | - | - |
| Forfeited/Cancelled | - | - | - |
| Options outstanding at September 30, 2019 (unaudited) | <u><u>622,000</u></u> | <u>15.0738</u> | <u>8.5127</u> |
| Options exercisable at December 31, 2018 | <u>111,589</u> | 28.7052 | 16.5968 |
| Options exercisable at September 30, 2019 (unaudited) | <u><u>353,797</u></u> | 17.0242 | 9.6884 |

A summary of the status of nonvested shares under Aerkomm 2017 Plan as of September 30, 2019 and December 31, 2018 is as follows:

| | Number of Shares | Weighted Average Exercise Price Per Share |
|-----------------------------------------------------|-----------------------------|------------------------------------------------------------------|
| Options nonvested at January 1, 2018 | 168,250 | \$ 32.4079 |
| Granted | 78,000 | 19.7462 |
| Vested | (74,839) | 28.8962 |
| Forfeited/Cancelled | - | - |
| Options nonvested at December 31, 2018 | <u>171,411</u> | <u>28.1794</u> |
| Granted | 339,000 | 3.9600 |
| Vested | (242,208) | 11.6426 |
| Forfeited/Cancelled | - | - |
| Options nonvested at September 30, 2019 (unaudited) | <u><u>268,203</u></u> | <u>12.5008</u> |

As of September 30, 2019 and December 31, 2018, there were approximately \$1,519,000 (unaudited) and \$2,174,000, respectively, of total unrecognized compensation cost related to nonvested share-based compensation arrangements granted under the Plans. Total unrecognized compensation cost will be adjusted for future changes in estimated forfeitures. The Company expects to recognize that cost over a weighted average period of 1 - 5 years.

NOTE 16 - Commitments

As of September 30, 2019, the Company's significant commitment is summarized as follows:

Yihe Culture Media Agreement: On June 20, 2018, the Company entered into a Cooperation Framework Agreement with Shenzhen Yihe Culture Media Co., Ltd. ("Yihe"), the authorized agent of Guangdong Tengen Internet, pursuant to which Yihe will promote the development of strategic cooperation between the Company and Guangdong Tengen Internet. Specifically, Yihe agreed to assist the Company with public relations and advertising, such as market and brand promotion, as well as brand recognition in China (excluding Hong Kong, Macao and Taiwan), including but not limited to news dissemination, creative planning and support of campaigns, financial public relations and internet advertising. More specifically, Yihe will help the Company develop a working application of the WeChat Pay payment solution as well as WeChat applets applicable for Chinese users and relating to cell phone and WiFi connectivity on airplanes, and Yihe will assist the Company in integrating other Tencent internet-based original product offerings. As compensation, the Company agreed to pay Yihe RMB 8 million (approximately US\$1.2 million), RMB 2,000,000 (approximately US\$309,000) of which the Company paid on June 29, 2018 and the remaining RMB 6,000,000 (approximately US\$927,000) of which was to be paid by August 15, 2018. On July 19, 2019, Yihe and the Company agreed to extend the expiration date of the agreement to June 20, 2022. The Company had paid the remaining RMB 6,000,000 on August 12, 2019.

Airbus SAS Agreement: On November 30, 2018, in furtherance of a memorandum of understanding signed in March 2018, the Company entered into an agreement with Airbus SAS ("Airbus"), pursuant to which Airbus will develop and certify a complete solution allowing the installation of our "AERKOMM K++" system on Airbus' single aisle aircraft family including the Airbus A319/320/321, for both Current Engine Option (CEO) and New Engine Option (NEO) models. Airbus will also apply for and obtain on our behalf a Supplemental Type Certificate (STC) from the European Aviation Safety Agency, or EASA, as well as from the U.S. Federal Aviation Administration or FAA, for the retrofit system. It is anticipated that the Bilateral Aviation Safety Agreement between EASA and the Civil Aviation Administration of China, or CAAC, will be finalized and go into effect in 2019. Pursuant to the terms of our Airbus agreement, The Company agreed to pay the service fees that Airbus provides the Company with the retrofit solution which will include the Service Bulletin and the material kits including the update of technical and operating manuals pertaining to the aircraft and provision of aircraft configuration control. The timeframe for the completion and testing of this retrofit solution, including the certification, is approximately 16 months from the purchase order issued in August 2018, although there is no guarantee that the project will be successfully completed in the projected timeframe.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

Use of Terms

Except as otherwise indicated by the context and for the purposes of this report only, references in this report to "we," "us," "our," or "our company" are to the combined business of Aerkomm Inc., a Nevada corporation, and its consolidated subsidiaries, including Aircom Pacific, Inc., a California corporation and wholly-owned subsidiary, or Aircom; Aerkomm Taiwan Inc., a Taiwanese company and wholly-owned subsidiary, or Aerkomm Taiwan; Aircom Pacific Ltd., a Republic of Seychelles company and wholly-owned subsidiary of Aircom, or Aircom Seychelles; Aircom Pacific Inc. Limited, a Hong Kong company and wholly-owned subsidiary of Aircom; Aircom Japan, Inc., a Japanese company and wholly-owned subsidiary of Aircom; Aircom Telecom LLC, a Taiwanese company and wholly-owned subsidiary of Aircom, or Aircom Taiwan; Beijing Yatai Communication Co., Ltd., a corporation formed under the laws of China and wholly-owned subsidiary of Aircom Taiwan, or Aircom Beijing; and Aerkomm Pacific Limited, a corporation formed under the laws of Malta and wholly-owned subsidiary of Aircom Seychelles.

Special Note Regarding Forward Looking Statements

Certain information contained in this report includes forward-looking statements. The statements herein which are not historical reflect our current expectations and projections about our future results, performance, liquidity, financial condition, prospects and opportunities and are based upon information currently available to us and our interpretation of what is believed to be significant factors affecting the businesses, including many assumptions regarding future events. The following factors, among others, may affect our forward-looking statements:

- our future financial and operating results;
- our intentions, expectations and beliefs regarding anticipated growth, market penetration and trends in our business;
- our ability to attract and retain customers;
- our dependence on growth in our customers' businesses;
- the effects of changing customer needs in our market;
- the effects of market conditions on our stock price and operating results;
- our ability to successfully complete the development, testing and initial implementation of our product offerings;
- our ability to maintain our competitive advantages against competitors in our industry;
- our ability to timely and effectively adapt our existing technology and have our technology solutions gain market acceptance;
- our ability to introduce new offerings and bring them to market in a timely manner;
- our ability to maintain, protect and enhance our intellectual property;
- the effects of increased competition in our market and our ability to compete effectively;
- our expectations concerning relationship with customers and other third parties;
- the attraction and retention of qualified employees and key personnel;
- future acquisitions of our investments in complementary companies or technologies; and
- our ability to comply with evolving legal standards and regulations.

Forward-looking statements, which involve assumptions and describe our future plans, strategies, and expectations, are generally identifiable by use of the words "may," "should," "expect," "anticipate," "estimate," "believe," "intend," or "project" or the negative of these words or other variations on these words or comparable terminology. Actual results, performance, liquidity, financial condition, prospects and opportunities could differ materially from those expressed in, or implied by, these forward-looking statements as a result of various risks, uncertainties and other factors, including the ability to raise sufficient capital to continue our operations. Actual events or results may differ materially from those discussed in forward-looking statements as a result of various factors, including, without limitation, the risks outlined under "Risk Factors" included in the prospectus contained in our Post-Effective Amendment No. 3 to Form S-1 as filed with the Securities and Exchange Commission, or the SEC, on May 17, 2019, and matters described in this report generally. In light of these risks and uncertainties, there can be no assurance that the forward-looking statements contained in this report will in fact occur.

Potential investors should not place undue reliance on any forward-looking statements. Except as expressly required by the federal securities laws, there is no undertaking to publicly update or revise any forward-looking statements, whether as a result of new information, future events, changed circumstances or any other reason.

The specific discussions herein about our company include financial projections and future estimates and expectations about our business. The projections, estimates and expectations are presented in this report only as a guide about future possibilities and do not represent actual amounts or assured events. All the projections and estimates are based exclusively on our management's own assessment of our business, the industry in which we work and the economy at large and other operational factors, including capital resources and liquidity, financial condition, fulfillment of contracts and opportunities. The actual results may differ significantly from the projections.

Potential investors should not make an investment decision based solely on our company's projections, estimates or expectations.

Recent Developments

On July 3, 2019, we paid Tsai Ming-Yin (the "**Seller**") a final installment in the amount of US\$624,462 of the purchase price for the acquisition by our wholly owned subsidiary, Aerkomm Taiwan, of a 6.36 acre parcel of land (the "**Land**") located at the Taishui Grottoes in the Xinyi District of Keelung City, Taiwan, which is expected to be used by Aerkomm Taiwan and us to build Aerkomm's first satellite ground station and data center. On July 16, 2019, the Seller provided us with a letter of undertaking (i) not to exercise his right to cancel and terminate our definitive agreement to purchase the Land and (ii) to proceed with the transfer of ownership of the Land to Aerkomm Taiwan. A copy of this letter of undertaking is referenced in the description of exhibits herein as Exhibit 10.2. As of the date of this report, the transfer of the ownership is still in progress.

On July 17, 2019, the French *Autorité des Marchés Financiers* (the "**AMF**") granted visa number 19-372 on the prospectus relating to the admission of our common stock to list and trade on the Professional Segment of the regulated market of Euronext Paris ("**Euronext Paris**"). Our common stock began trading on Euronext Paris in November 2019 under the symbol "AKOM" and is denominated in Euros on Euronext Paris. This listing did not alter our outstanding share count, capital structure, or current common stock listing on the OTCQX, where our common stock also trades (in US dollars) under the symbol "AKOM."

On October 31, 2019, Aircom Seychelles established a new wholly owned subsidiary, Aerkomm Pacific Limited ("Aerkomm Malta"), a corporation formed under the laws of Malta. The purpose of Aerkomm Malta is to conduct Aircom's business and operations to engage with suppliers and potential airlines customers in the European Union.

Overview

With advanced technologies and a unique business model, we, as a development stage service provider of IFEC solutions, intend to provide airline passengers with a broadband in-flight experience that encompasses a wide range of service options. Such options include Wi-Fi, cellular, movies, gaming, live TV, and music. We plan to offer these core services, which we are currently still developing, through both built-in in-flight entertainment systems, such as a seat-back display, as well as on passengers' own personal devices. We also expect to provide content management services and e-commerce solutions related to our IFEC solutions.

We plan to partner with airlines and offer airline passengers free IFEC services. We expect to generate revenue through advertising and in-flight transactions. We believe that this is an innovative approach that differentiates us from existing market players.

To complement and facilitate our planned IFEC service offerings, we intend to build satellite ground stations and related data centers within the geographic regions where we expect to be providing IFEC airline services.

Additionally, we have developed and begun to market two internet connectivity systems, one for hotels primarily located in remote regions and the other for maritime use. Both systems operate through a Ku/Ku high throughput satellite, or HTS. We also expect to develop a remote connectivity system that will be applicable to the highspeed rail industry.

MJet GMBH General Terms Agreement

On March 6, 2019, we signed a General Terms Agreement (GTA) with MJet GMBH, or MJet, an Airbus Corporate Jets ("ACJ") customer and an ACJ A319 corporate jet owner and operator based in Vienna, Austria. The GTA provided for the provision, installation, testing and certification of our Aerkomm K++ system equipment, including the Airbus Service Bulletin and associated material kit and related connectivity services, on an MJet ACJ A319 aircraft under the supervision of Airbus. On June 11, 2019 the GTA was converted into a definitive agreement with MJet (the "**MJet Definitive Agreement**"), and on June 12, 2019 MJet placed a Purchase Order with Aircom. MJet will be our launch customer for the first planned installation of our AERKOMM K++ system equipment by the end of 2019 or first quarter of 2020. Assuming the installation, testing and certification of our AERKOMM K++ system on the MJet A319 is successful, something we cannot guarantee at this time, MJet will pay us a one-time fee for our equipment and a monthly fee for our connectivity services, at which point we would also begin charging MJet for the bandwidth required to use the AERKOMM K++ system services. Assuming the success of this installation, MJet would become the first recurring payment customer of our IFEC AERKOMM K++ system as well as being the launch customer of our Aerkomm K++ solution.

Cooperation Framework Agreement with Shenzhen Yihe Culture Media Co., Ltd. (“Yihe”)

On June 20, 2018, the Company entered into a Cooperation Framework Agreement with Yihe, the authorized agent of Guangdong Tengen Internet, pursuant to which Yihe will promote the development of strategic cooperation between the Company and Guangdong Tengen Internet. Specifically, Yihe agreed to assist the Company with public relations and advertising, such as market and brand promotion, as well as brand recognition in China (excluding Hong Kong, Macao and Taiwan), including but not limited to news dissemination, creative planning and support of campaigns, financial public relations and internet advertising. More specifically, Yihe will help the Company develop a working application of the WeChat Pay payment solution as well as WeChat applets applicable for Chinese users and relating to cell phone and WiFi connectivity on airplanes, and Yihe will assist the Company in integrating other Tencent internet-based original product offerings. As compensation, the Company agreed to pay Yihe RMB 8 million (approximately US\$1.2 million), RMB 2,000,000 (approximately US\$309,000) of which the Company paid on June 29, 2018 and the remaining RMB 6,000,000 (approximately US\$927,000) of which was to be paid by August 15, 2018. On July 19, 2019, Yihe and the Company agreed to extend the agreement to expire June 20, 2022 and to extend the date by which the Company must pay the remaining RMB 6,000,000 to August 12, 2019. As of September 30, 2019, the remaining balance was fully paid.

Business Development

We are actively working with prospective airline customers to provide services to their passengers utilizing the Airbus to-be certified AERKOMM K++ system. We have entered into non-binding memoranda of understanding with a number of airlines, including Air Malta Airlines of Malta, PanAfriqiyah of Malta, and Onur Air of Turkey. There can be no assurances, however, that these will lead to actual purchase agreements.

In view of the increasing demand by the airlines for a bigger data throughput, during the course of discussions between us and Airbus, we have revised our strategy to focus primarily on Ka-band IFEC solutions for airlines and have suspended work on our dual band satellite inflight connectivity solution. The Ku-band system will, however, still be retained for other product applications such as remote locations and maritime use.

In connection with the Airbus project, we also identified owners of ACJ aircraft, as potential customers of our AERKOMM K++ system. ACJ customers, however, would not generate enough internet traffic to make our free-service business model viable. To capitalize on this additional market, we plan to sell our AERKOMM K++ system hardware for installation on ACJ corporate jets and provide connectivity through subscription-based plans. This new corporate jet market would generate additional revenue and income for our company. We are currently in advanced discussions with a number of ACJ customers, some of whom have more than one aircraft in their fleets.

Our AERKOMM K++ System

Following the course of discussions between us and Airbus and in view of the increasing demand by the airlines for a bigger data throughput, we have revised our strategy to focus primarily on Ka-band satellite connectivity solutions for aviation customers and have suspended work on our dual band satellite connectivity solution. Our AERKOMM K++ system will operate through Ka/Ka High Throughput Satellites. The Ku-band system will, however, still be retained for the other applications such as remote locations and maritime use.

Our AERKOMM K++ system will contain a low profile radome (that is, a dome or similar structure protecting our radio equipment) containing two Ka-band antennas, one for transmitting and the other for receiving, and will comply with the ARINC 791 standard of Aeronautical Radio, Incorporated. Our AERKOMM K++ system also meets Airbus Design Organization Approval.

GEO (Geostationary Earth Orbiting) and LEO (Low Earth Orbiting) Ka-band Satellites

Our initial AERKOMM K++ system will work only with geostationary earth orbiting, or GEO, Ka-band satellites. Performance of GEO satellites diminishes greatly in the areas near the Earth’s poles. Only low earth orbiting, or LEO, satellites can collect high quality data over the North and South poles. We are developing technologies to work with LEO satellites and plans to partner with Airbus to develop aircraft installation solutions. As new GEO and LEO Ka-band satellites are regularly launched over the next few years, which, we expect, will enable the provision of worldwide aircraft coverage, we plan to have the necessary technology ready to take advantage of this new trend in Ka-band aviation connectivity, although we cannot assure you that we will be successful in this new area of endeavor.

Ground-based Satellite System Sales

Since our acquisition of Aircom Taiwan in December 2017, this wholly owned subsidiary has been developing ground-based satellite connectivity components which have an application in remote regions that lack regular affordable ground-based communications. In September, 2018, Aircom Taiwan consummated its first sale of such a component, a small cell server terminal, in the amount of \$1,730,000. This server terminal will be utilized by the purchaser in the construction of a satellite-based ground communication system which will act as a multicast service extension of existing networks. The system is designed to extend local existing networks, such as ISPs and mobile operators, into rural areas and create better coverage and affordable connectivity in these areas. Aircom Taiwan expects to sell additional satellite connectivity components, systems and services to be used in ground mobile units in the future, although there can be no assurances that it will be successful in these endeavors.

In addition, in September 2018, Aircom Taiwan provided installation and testing services of a satellite-based ground connectivity system to a remote island resort and received service income related to this project in the amount of \$15,000. Upon the completion of this system’s testing phase, and assuming that the system operates satisfactorily, Aircom Taiwan expects to begin to sell this system to multiple, remotely located resorts. We can make no assurances at this time, however, that this system will operate satisfactorily and we will be successful in introducing this system as a viable product offering, or that we will be able to generate any additional revenue from the sale and deployment of this system.

Principal Factors Affecting Financial Performance

We believe that our operating and business performance is driven by various factors that affect the commercial airline industry, including trends affecting the travel industry and trends affecting the customer bases that we target, as well as factors that affect wireless Internet service providers and general macroeconomic factors. Key factors that may affect our future performance include:

- our ability to enter into and maintain long-term business arrangements with airline partners, which depends on numerous factors including the real or perceived availability, quality and price of our services and product offerings as compared to those offered by our competitors;
- the extent of the adoption of our products and services by airline partners and customers;
- costs associated with implementing, and our ability to implement on a timely basis, our technology, upgrades and installation technologies;
- costs associated with and our ability to execute our expansion, including modification to our network to accommodate satellite technology, development and implementation of new satellite-based technologies, the availability of satellite capacity, costs of satellite capacity to which we may have to commit well in advance, and compliance with regulations;
- costs associated with managing a rapidly growing company;
- the number of aircraft in service in our markets, including consolidation of the airline industry or changes in fleet size by one or more of our commercial airline partners;
- the economic environment and other trends that affect both business and leisure travel;
- continued demand for connectivity and proliferation of Wi-Fi enabled devices, including smartphones, tablets and laptops;
- our ability to obtain required telecommunications, aviation and other licenses and approvals necessary for our operations; and
- changes in laws, regulations and interpretations affecting telecommunications services and aviation, including, in particular, changes that impact the design of our equipment and our ability to obtain required certifications for our equipment.

Emerging Growth Company

We qualify as an “emerging growth company” under the Jumpstart Our Business Startups Act of 2012, or the JOBS Act. As a result, we are permitted to, and intend to, rely on exemptions from certain disclosure requirements. For so long as we are an emerging growth company, we will not be required to:

- have an auditor report on our internal controls over financial reporting pursuant to Section 404(b) of the Sarbanes-Oxley Act;
- comply with any requirement that may be adopted by the Public Company Accounting Oversight Board regarding mandatory audit firm rotation or a supplement to the auditor’s report providing additional information about the audit and the financial statements (i.e., an auditor discussion and analysis);
- submit certain executive compensation matters to shareholder advisory votes, such as “say-on-pay” and “say-on-frequency;” and
- disclose certain executive compensation related items such as the correlation between executive compensation and performance and comparisons of the CEO’s compensation to median employee compensation.

In addition, Section 107 of the JOBS Act also provides that an emerging growth company can take advantage of the extended transition period provided in Section 7(a)(2)(B) of the Securities Act of 1933, as amended, or the Securities Act, for complying with new or revised accounting standards.

In other words, an emerging growth company can delay the adoption of certain accounting standards until those standards would otherwise apply to private companies. We have elected to take advantage of the benefits of this extended transition period. Our financial statements may therefore not be comparable to those of companies that comply with such new or revised accounting standards.

We will remain an “emerging growth company” for up to five years, or until the earliest of (i) the last day of the first fiscal year in which our total annual gross revenues exceed \$1 billion, (ii) the date that we become a “large accelerated filer” as defined in Rule 12b-2 under the Exchange Act of 1934, as amended, or the Exchange Act, which would occur if the market value of our shares of common stock that are held by non-affiliates exceeds \$700 million as of the last business day of our most recently completed second fiscal quarter or (iii) the date on which we have issued more than \$1 billion in non-convertible debt during the preceding three year period.

Results of Operations

Comparison of Three Months Ended September 30, 2019 and 2018

The following table sets forth key components of our results of operations during the three-month periods ended September 30, 2019 and 2018.

| | Three Months Ended September 30, | | Change | |
|------------------------------------|-------------------------------------|----------------|----------------|------------|
| | 2019 | 2018 | \$ | % |
| Sales | \$ - | \$ 1,745,000 | \$ (1,745,000) | (100.0)% |
| Cost of sales | - | 1,650,000 | (1,650,000) | (100.0)% |
| Operating expenses | 2,733,350 | 2,594,500 | 138,850 | 5.4% |
| Loss from operations | (2,733,350) | (2,499,500) | (233,850) | 9.4% |
| Net non-operating income (expense) | (78,433) | 1,427 | (79,860) | (5,596.4)% |
| Loss before income taxes | (2,811,783) | (2,498,073) | (313,710) | 12.6% |
| Net Loss | (2,811,783) | (2,498,073) | (313,710) | 12.6% |
| Other comprehensive income (loss) | 59,237 | 2,474 | 56,763 | 2,294.4% |
| Total comprehensive loss | \$ (2,752,546) | \$ (2,495,599) | \$ (256,947) | 10.3% |

Revenue. Our total revenue was \$0 and \$1,745,000 for the three-month periods ended September 30, 2019 and 2018, respectively. Our total revenue of \$1,745,000 for the three-month period ended September 30, 2018 represents sales of computer server module in the amount of \$1,730,000 and remote island resort ground antenna connectivity service income in the amount of \$15,000.

Cost of sales. Our cost of sales was \$0 and \$1,650,000 for the three-month periods ended September 30, 2019 and 2018, respectively. The cost of sales of \$1,650,000 for the three-month period ended September 30, 2018 represents the cost of computer server module sold by our subsidiary Aircom Taiwan.

Operating expenses. Our operating expenses consist primarily of compensation and benefits, professional advisor fees, research and development expenses, cost of promotion, business development, business travel, transportation costs, and other expenses incurred in connection with general operations. Our operating expenses increased by \$138,850 to \$2,733,350 for the three-month period ended September 30, 2019, from \$2,594,500 for the three-month period ended September 30, 2018. Such increase was mainly due to the increase in stock-based compensation expenses, legal fee, amortization expense and depreciation expense of \$332,201, \$158,097, \$101,088 and \$93,519, respectively, which was offset by the decrease in research and development, marketing and rent expenses of \$469,770, \$83,428 and \$69,878, respectively. The increase in legal fee was mainly related to our dual listing in the Compartment C of Euronext-Paris.

Net non-operating expense. We had \$78,433 in net non-operating expense for the three-month period ended September 30, 2019, as compared to net non-operating income of \$1,427 for the three-month period ended September 30, 2018. Net non-operating expense in the three-month period ended September 30, 2019 mainly due to the loss on foreign exchange translation of \$77,033 and interest expense of \$1,412, while net non-operating income in the three-month period ended September 30, 2018 is due to a foreign exchange translation gain of \$1,425.

Loss before income taxes. Our loss before income taxes increased by \$313,710 to \$2,811,783 for the three-month period ended September 30, 2019, from a loss of \$2,498,073 for the three-month period ended September 30, 2018, as a result of the factors described above.

Total comprehensive loss. As a result of the cumulative effect of the factors described above, our total comprehensive loss increased by \$256,947 to \$2,752,546 for the three-month period ended September 30, 2019, from \$2,495,599 for the three-month period ended September 30, 2018.

Comparison of Nine Months Ended September 30, 2019 and 2018

The following table sets forth key components of our results of operations during the nine-month periods ended September 30, 2019 and 2018.

| | Nine Months Ended September 30, | | Change | |
|------------------------------------|------------------------------------|----------------|--------------|-------------|
| | 2019 | 2018 | \$ | % |
| Sales | \$ 1,599,864 | \$ 1,745,000 | \$ (145,136) | (8.3)% |
| Cost of sales | 1,587,222 | 1,650,000 | (62,778) | (3.8)% |
| Operating expenses | 6,365,161 | 6,180,984 | 175,177 | 2.8% |
| Loss from operations | (6,343,519) | (6,085,984) | (257,535) | 4.2% |
| Net non-operating income (expense) | (533,459) | 2,659 | (536,118) | (20,162.4)% |
| Loss before income taxes | (6,876,978) | (6,083,325) | (793,653) | 13.0% |
| Income tax expense | 3,235 | 4,062 | (827) | (20.4)% |
| Net Loss | (6,880,213) | (6,087,387) | (792,826) | 13.0% |
| Other comprehensive income (loss) | 524,531 | (1,208) | 525,739 | (43,516.4)% |
| Total comprehensive loss | \$ (6,355,682) | \$ (6,088,595) | \$ (267,087) | 4.4% |

Revenue. Our total revenue was \$1,599,864 and \$1,745,000 for the nine-month periods ended September 30, 2019 and 2018, respectively. Our total revenue of \$1,599,864 for the nine-month period ended September 30, 2019 was a non-recurring sale of compact adaptors for smartphone that allows users to turn their smartphone into a satellite smartphone to provide reliable connectivity beyond the coverage of traditional networks as we are still developing our core business in in-flight entertainment and connectivity. Our total revenue of \$1,745,000 for the nine-month period ended September 30, 2018 represents sales of computer server module in the amount of \$1,730,000 and remote island resort ground antenna connectivity service income in the amount of \$15,000.

Cost of sales. Our cost of sales was \$1,587,222 and \$1,650,000 for the nine-month periods ended September 30, 2019 and 2018, respectively. The cost of sales of \$1,587,222 for the nine-month period ended September 30, 2019 was the cost of non-recurring sales of satellite-based mobile communication units, while the cost of sales of \$1,650,000 for the nine-month period ended September 30, 2018 represents the cost of computer server module sold by our subsidiary Aircom Taiwan.

Operating expenses. Our operating expenses consist primarily of compensation and benefits, professional advisor fees, research and development expenses, cost of promotion, business development, business travel, transportation costs, and other expenses incurred in connection with general operations. Our operating expenses increased by \$175,177 to \$6,365,161 for the nine-month period ended September 30, 2019, from \$6,180,984 for the nine-month period ended September 30, 2018. Such increase was mainly due to the increase in payroll and related expense, amortization expense, depreciation expense, stock-based compensation expense, legal fee and accounting fee of \$346,539, \$345,083, \$322,727, \$332,530, \$254,021 and \$214,849, respectively, which was offset by the decrease in consulting fee, research and development expense, investor relation and public listing related expense and rent expense of \$926,218, \$291,190, \$277,916 and \$182,272, respectively. The decrease in consulting fee was mainly related to the decrease in fair value of warrants issued to our underwriter for the public offering and termination of one consulting agreement.

Net non-operating expense. We had \$533,459 in net non-operating expense for the nine-month period ended September 30, 2019, as compared to net non-operating income of \$2,659 for the nine-month period ended September 30, 2018. Net non-operating expense in the nine-month period ended September 30, 2019 mainly due to the loss on foreign exchange translation of \$528,734 and net interest expense of \$4,741, while net non-operating income in the nine-month period ended September 30, 2018 includes a foreign exchange translation gain of \$5,846 and net interest expense of \$3,286.

Loss before income taxes. Our loss before income taxes increased by \$793,653 to \$6,876,978 for the nine-month period ended September 30, 2019, from a loss of \$6,083,325 for the nine-month period ended September 30, 2018, as a result of the factors described above.

Income tax expense. Income tax expense was \$3,235 and \$4,062 for the nine-month period ended September 30, 2019 and 2018, respectively, mainly due to California franchise tax and foreign subsidiary's income tax expenses.

Total comprehensive loss. As a result of the cumulative effect of the factors described above, our total comprehensive loss increased by \$267,087 to \$6,355,682 for the nine-month period ended September 30, 2019, from \$6,088,595 for the nine-month period ended September 30, 2018.

Liquidity and Capital Resources

As of September 30, 2019, we had cash and cash equivalents of \$2,808,023. To date, we have financed our operations primarily through cash proceeds from financing activities, including through our ongoing public offering, short-term borrowings and equity contributions by our stockholders.

The following table provides detailed information about our net cash flow:

Cash Flow

| | Nine Months Ended September 30, | |
|------------------------------------------------------|--------------------------------------------|-------------------|
| | 2019 | 2018 |
| Net cash used for operating activities | \$ (8,035,353) | \$ (7,247,420) |
| Net cash used for investing activity | (630,917) | (34,091,169) |
| Net cash provided by financing activity | 10,861,453 | 42,215,066 |
| Net increase (decrease) in cash and cash equivalents | 2,195,183 | 876,477 |
| Cash at beginning of year | 88,309 | 21,504 |
| Foreign currency translation effect on cash | 524,531 | (1,208) |
| Cash at end of year | <u>\$ 2,808,023</u> | <u>\$ 896,773</u> |

Operating Activities

Net cash used for operating activities was \$8,035,353 for the nine months ended September 30, 2019, as compared to \$7,247,420 for the nine months ended September 30, 2018. In addition to the net loss of \$6,880,213, the increase in net cash used for operating activities during the nine-month period ended September 30, 2019 was mainly due to increase in inventory and prepaid expenses of \$1,485,350 and \$973,321, respectively, and decrease in accounts payable, other payable – others and operating lease liability of \$840,092, \$1,577,838 and \$304,014, respectively, offset by the decrease in accounts receivable of \$1,095,061. In addition to the net loss of \$6,087,387, the decrease in net cash used for operating activities during the nine-month period ended September 30, 2018 was mainly due to increase in accounts receivable and prepaid expenses of \$1,745,000 and \$1,205,910, respectively, and decrease in other payable - others of \$1,253,797, offset by the increase in accounts payable of \$1,650,000.

Investing Activities

Net cash used for investing activities for the nine months ended September 30, 2019 was \$630,917 as compared to \$34,091,169 for the nine months ended September 30, 2018. The net cash used for investing activities for the nine months ended September 30, 2019 was mainly for the purchase of property and equipment and the final payment toward the purchase of the Land to build our first satellite ground station and data center. The net cash used for investing activities for the nine months ended September 30, 2018 was mainly due to the \$35.2 million deposits paid toward the Land.

Financing Activities

Net cash provided by financing activities for the nine months ended September 30, 2019 and 2018 was \$10,861,453 and \$42,215,066, respectively. Net cash provided by financing activities for the nine months ended September 30, 2019 were mainly attributable to net proceeds from the issuance of common stock from ongoing public offering and the borrowing of a long-term loan in the amounts of \$10,810,688 and \$45,765, respectively. Net cash provided by financing activities for the nine months ended September 30, 2018 were mainly attributable to proceeds from the issuance of common stock from public offering, issuance of stock warrants related to the public offering and increase in subscribed capital in the amounts of \$41,262,899, \$906,167 and \$56,000, respectively, offset by the repayment of short-term bank loan of \$10,000.

On May 14, 2018, we entered into an underwriting agreement with Boustead Securities, LLC in connection with the public offering, issuance and sale of up to 1,411,765 shares of our common stock on a best efforts basis, with a minimum requirement of 117,647 shares, at the public offering price of \$42.50 per share, less underwriting discounts, for minimum gross proceeds \$5,000,000 and up to a maximum of \$60,000,000. We also granted Boustead Securities, LLC an over-subscription option, exercisable on or prior to the offering termination date to extend the offering for an additional 45 days, pursuant to which we may sell up to 211,764 additional shares of the common stock at the public offering price, less underwriting discounts. The material terms of this offering are described in the prospectus, dated May 14, 2018, filed by us with the SEC, on May 14, 2018 pursuant to Rule 424(b) under the Securities Act. This offering is registered with the SEC pursuant to a Registration Statement on Form S-1, as amended and supplemented to date (File No. 333-222208), initially filed by us on December 20, 2017.

As of September 30, 2019, we held 13 closings of this offering, pursuant to which we issued and sold an aggregate of 1,294,627 shares of common stock for gross proceeds of approximately \$55.02 million, or net proceeds of approximately \$50.83 million after underwriting discounts, commissions and offering expenses payable by us. The offering period for this public offering expired on January 4, 2019 and we filed a post-effective amendment No. 2 with the SEC on April 23, 2019 to extend the public offering to attempt to raise the remaining \$16.44 million that had not yet been sold. On May 17, 2019, the Company filed a post-effective amendment No. 3 with the SEC to extend the Offering to expire on November 23, 2019, and which was declared effective by the SEC on May 23, 2019.

On May 9, 2019, two of our current shareholders (the “Lenders”) each committed to provide us a \$10 million bridge loan (the “Loans”) for an aggregate principal amount of \$20 million, to bridge our cash flow needs prior to our obtaining a mortgage loan to be secured by a parcel of land (the “Land”) we intend to purchase. The Land consists of approximately 6.36 acres of undeveloped land located at the Taishui Grottoes in the Xinyi District of Keelung City, Taiwan. Aerkomm Taiwan has contracted to purchase the Land for NT\$1,056,297,507, or US\$34,474,462, and as of July 3, 2019 we have paid the purchase price for the Land in full. The Loans will be secured by the Land with the initial closing date of the Loans to be a date, designated by us, within 30 days following the date that the title for the Land is fully transferred to and vested in our subsidiary, Aerkomm Taiwan. The Loans shall bear interest, non-compounding, at the Bank of America Prime Rate plus 1%, annually, calculated on the actual number of days the Loans are outstanding and based on a 365-day year and shall be due and payable upon the earlier of (1) the date of our (or our subsidiary, Aerkomm Taiwan) obtaining a mortgage loan secured by the Land with a principal amount of not less than \$20 million and (2) one year following the initial closing date of the Loans. The Lenders also agreed to an earlier closing of up to 25% of the principal amounts of the Loans upon our request prior to the time that title to the Land is vested in our subsidiary, Aerkomm Taiwan, provided that we provide adequate evidence to the Lenders that the proceeds of such an earlier closing would be applied to pay our vendors. We, of course, cannot provide any assurances that we will be able to raise sufficient additional funds in our public offering to complete our acquisition of the Land or to obtain a mortgage on the Land if and when it is acquired.

On July 10, 2018, in conjunction with the Land acquisition, we entered into a binding letter of commitment with Metro Investment Group Limited, or MIGL, pursuant to which we agreed to pay MIGL an agent commission of four percent (4%) of the full purchase price of the Land, equivalent to approximately US\$1,387,127, for MIGL's services provided with respect to the acquisition. The commission must be paid to MIGL no later than 90 days following payment in full of the purchase price. If there is a delay in payment, we shall be responsible for punitive liquidated damages at the rate of one tenth of one percent (0.1%) of the commission per day of delay with a maximum cap to these damages of five percent (5%). Under applicable Taiwanese law, the commission is due and payable upon signing of the letter of commitment even if the contract is cancelled for any reason and the acquisition is not completed. We have recorded the estimated commission to the cost of land and will be paying the amount no later than 90 days following full payment of the purchase price. On May 9, 2019, we amended the binding letter of commitment with MIGL to extend the payment to be paid after the full payment of the Land acquisition price until no later than December 31, 2020.

With the \$9.98 million to be raised in the remainder of our ongoing public offering (assuming we are successfully able to complete the public offering) and the \$20 million in Loans committed to us by the Lenders, we believe our available working capital will be sufficient to sustain our current financial obligations for the next twelve months. However, even if we successfully raise sufficient capital to satisfy our needs over the next twelve months, following that period we will require additional cash resources for the implementation of our strategy to expand our business or for other investments or acquisitions we may decide to pursue. If our internal financial resources are insufficient to satisfy our capital requirements, we will need seek to sell additional equity or debt securities or obtain additional credit facilities, although there can be no assurances that we will be successful in these efforts. The sale of additional equity securities could result in dilution to our stockholders. The incurrence of indebtedness would result in increased debt service obligations and could require us to agree to operating and financial covenants that would restrict our operations. Financing may not be available in amounts or on terms acceptable to us, if at all. Any failure by us to raise additional funds on terms favorable to us, or at all, could limit our ability to expand our business operations and could harm our overall business prospects.

The Company has not generated significant revenues, excluding non-recurring revenues from affiliates in the second quarter of fiscal 2018, and will incur additional expenses as a result of being a public reporting company. For the nine-month period ended September 30, 2019, the Company incurred a comprehensive loss of \$6,355,682 and had working capital of \$4,606,799 as of September 30, 2019. Currently, the Company has taken measures, as discussed above, that management believes will improve its financial position by financing activities, including through our ongoing public offering, short-term borrowings and equity contributions.

Capital Expenditures

Our operations continue to require significant capital expenditures primarily for technology development, equipment and capacity expansion. Capital expenditures are associated with the supply of airborne equipment to our prospective airline partners, which correlates directly to the roll out and/or upgrade of service to our prospective airline partners' fleets. Capital spending is also associated with the expansion of our network, ground stations and data centers and includes design, permitting, network equipment and installation costs.

Capital expenditures for the nine months ended September 30, 2019 and 2018 were \$630,917 and \$34,091,169, respectively.

We anticipate an increase in capital spending in our fiscal year ended December 31, 2019 and estimate that capital expenditures will range from \$6 million to \$60 million as we begin airborne equipment installations and continue to execute our expansion strategy.

Inflation

Inflation and changing prices have not had a material effect on our business, and we do not expect that inflation or changing prices will materially affect our business in the foreseeable future. However, our management will closely monitor price changes in our industry and continually maintain effective cost control in operations.

Off Balance Sheet Arrangements

We do not have any off balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity or capital expenditures or capital resources that is material to an investor in our securities.

Seasonality

Our operating results and operating cash flows historically have not been subject to significant seasonal variations. This pattern may change, however, as a result of new market opportunities or new product introductions.

Critical Accounting Policies

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires our management to make assumptions, estimates and judgments that affect the amounts reported, including the notes thereto, and related disclosures of commitments and contingencies, if any. We have identified certain accounting policies that are significant to the preparation of our financial statements. These accounting policies are important for an understanding of our financial condition and results of operation. Critical accounting policies are those that are most important to the portrayal of our financial condition and results of operations and require management's difficult, subjective, or complex judgment, often as a result of the need to make estimates about the effect of matters that are inherently uncertain and may change in subsequent periods. Certain accounting estimates are particularly sensitive because of their significance to financial statements and because of the possibility that future events affecting the estimate may differ significantly from management's current judgments. We believe the following critical accounting policies involve the most significant estimates and judgments used in the preparation of our financial statements:

Right-of-Use Asset and Lease Liability. In February 2016, the FASB issued ASU No. 2016-02, "Leases" (Topic 842) ("ASU 2016-02"), which modifies lease accounting for both lessees and lessors to increase transparency and comparability by recognizing lease assets and lease liabilities by lessees for those leases classified as operating leases under previous accounting standards and disclosing key information about leasing arrangements.

A lessee should recognize the lease liability to make lease payments and the right-of-use asset representing its right to use the underlying asset for the lease term. For operating leases, a right-of-use asset and a lease liability are initially measured at the present value of the lease payments. The amortization of the right-of-use asset is allocated over the lease term generally on a straight-line basis.

For the lease within a term of twelve months or less, a lessee is permitted to make an accounting policy election by class of underlying asset not to recognize lease assets and lease liabilities. If a lessee makes this election, it should recognize lease expense for such leases generally on a straight-line basis over the lease term. The Company adopted ASU 2016-02 effective January 1, 2019.

Income Taxes. Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are computed for differences between the financial statement and tax bases of assets and liabilities that will result in taxable or deductible amounts in the future based on enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized. Income tax expense is the tax payable or refundable for the period plus or minus the change during the period in deferred tax assets and liabilities. Adjustments to prior period's income tax liabilities are added to or deducted from the current period's tax provision.

The Company follows FASB guidance on uncertain tax positions and has analyzed its filing positions in all the federal, state and foreign jurisdictions where it is required to file income tax returns, as well as all open tax years in those jurisdictions. The Company files income tax returns in the US federal, state and foreign jurisdictions where it conducts business. The Company believes that its income tax filing positions and deductions will be sustained on audit and does not anticipate any adjustments that will result in a material adverse effect on its consolidated financial position, results of operations, or cash flows. Therefore, no reserves for uncertain tax positions have been recorded. The Company does not expect its unrecognized tax benefits to change significantly over the next twelve months.

The Company's policy for recording interest and penalties associated with any uncertain tax positions is to record such items as a component of income before taxes. Penalties and interest paid or received, if any, are recorded as part of other operating expenses in the consolidated statement of operations.

Foreign Currency Transactions. Foreign currency transactions are recorded in U.S. dollars at the exchange rates in effect when the transactions occur. Exchange gains or losses derived from foreign currency transactions or monetary assets and liabilities denominated in foreign currencies are recognized in current income. At the end of each period, assets and liabilities denominated in foreign currencies are revalued at the prevailing exchange rates with the resulting gains or losses recognized in income for the period.

Earnings (Loss) Per Share. Basic earnings (loss) per share is computed by dividing income available to common shareholders by the weighted average number of shares of common stock outstanding during the period. Diluted earnings per share is computed by dividing income available to common shareholders by the weighted-average number of shares of common outstanding during the period increased to include the number of additional shares of common stock that would have been outstanding if the potentially dilutive securities had been issued. Potentially dilutive securities include stock warrants and outstanding stock options, shares to be purchased by employees under the Company's employee stock purchase plan.

Revenue Recognition. We recognize revenue when performance obligations identified under the terms of contracts with our customers are satisfied, which generally occurs upon the transfer of control in accordance with the contractual terms and conditions of the sale. Our major revenue for the three-month and nine-month periods ended September 30, 2019 was the sales of compact adaptor for smartphone that allows users to turn their smartphone into a satellite smartphone to provide reliable connectivity beyond the coverage of traditional networks. The majority of our revenue is recognized at a point in time when product is shipped or service is provided to the customer. Revenue is measured as the amount of consideration we expect to receive in exchange for transferring goods, which includes estimates for variable consideration.

Inventories. Inventories are recorded at the lower of weighted-average cost or net realizable value. We assess the impact of changing technology on our inventory on hand and writes off inventories that are considered obsolete. Estimated losses on scrap and slow-moving items are recognized in the allowance for losses.

Research and Development Costs. Research and development costs are charged to operating expenses as incurred. For the nine-month periods ended September 30, 2019 and 2018, we incurred approximately \$416,230 and \$707,420 of research and development costs, respectively.

Property and Equipment. Property and equipment are stated at cost less accumulated depreciation. When value impairment is determined, the related assets are stated at the lower of fair value or book value. Significant additions, renewals and betterments are capitalized. Maintenance and repairs are expensed as incurred. Depreciation is computed by using the straight-line and double declining method over the following estimated service lives: computer equipment - 3 to 5 years, furniture and fixtures - 5 years, satellite equipment – 5 years, vehicles – 5 years and lease improvement – 5 years. Construction costs for on-flight entertainment equipment not yet in service are recorded under construction in progress. Upon sale or disposal of property and equipment, the related cost and accumulated depreciation are removed from the corresponding accounts, with any gain or loss credited or charged to income in the period of sale or disposal. We review the carrying amount of property and equipment for impairment when events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. We determined that there was no impairment loss for the nine-month periods ended September 30, 2019 and 2018.

Goodwill and Purchased Intangible Assets. Goodwill represents the amount by which the total purchase price paid exceeded the estimated fair value of net assets acquired from acquisition of subsidiaries. We test goodwill for impairment on an annual basis, or more often if events or circumstances indicate that there may be impairment. Purchased intangible assets with finite life are amortized on the straight-line basis over the estimated useful lives of respective assets. Purchased intangible assets with indefinite life are evaluated for impairment when events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Purchased intangible asset consists of satellite system software and is amortized over 10 years.

Fair Value of Financial Instruments. We utilize the three-level valuation hierarchy for the recognition and disclosure of fair value measurements. The categorization of assets and liabilities within this hierarchy is based upon the lowest level of input that is significant to the measurement of fair value. The three levels of the hierarchy consist of the following:

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

Level 2 - Inputs to the valuation methodology are quoted prices for similar assets and liabilities in active markets, quoted prices in markets that are not active or inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the instrument.

Level 3 - Inputs to the valuation methodology are unobservable inputs based upon management’s best estimate of inputs market participants could use in pricing the asset or liability at the measurement date, including assumptions.

The carrying amounts of our cash, accounts receivable, other receivable, short-term loans, accounts payable, and other payable approximated their fair value due to the short-term nature of these financial instruments.

Translation Adjustments. If a foreign subsidiary’s functional currency is the local currency, translation adjustments will result from the process of translating the subsidiary’s financial statements into the reporting currency of our company. Such adjustments are accumulated and reported under other comprehensive income (loss) as a separate component of stockholder’s equity.

Recent Accounting Pronouncements

Financial Instruments. In June 2016, the FASB issued ASU No. 2016-13, “Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments”, which modifies the measurement of expected credit losses of certain financial instruments. ASU 2016-13 will be effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. We are currently evaluating the impact of adopting ASU 2016-13 on our consolidated financial statements.

Intangibles. In January 2017, the FASB issued ASU No. 2017-04, “Intangibles - Goodwill and Other” (Topic 350): Simplifying the Test for Goodwill Impairment, which goodwill shall be tested at least annually for impairment at a level of reporting referred to as a reporting unit. ASU 2017-04 will be effective for annual periods beginning after December 15, 2019. We are currently evaluating the impact of adopting ASU 2017-04 on our consolidated financial statements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Not applicable.

ITEM 4. CONTROLS AND PROCEDURES.

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures (as defined in Rule 13a-15(e) under the Exchange Act). Disclosure controls and procedures refer to controls and other procedures designed to ensure that information required to be disclosed in the reports we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC and that such information is accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate, to allow timely decisions regarding required disclosure.

As required by Rule 13a-15(e) of the Exchange Act, our management has carried out an evaluation, with the participation and under the supervision of our chief executive officer and chief financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures, as of September 30, 2019.

Based upon, and as of the date of this evaluation, our chief executive officer and chief financial officer determined that, because of the material weaknesses described in Item 9A “Controls and Procedures” of our Transition Report on Form 10-KT filed on April 1, 2019 for the transition period from March 1, 2018 through December 31, 2018 and further referenced below, which we are still in the process of remediating as of September 30, 2019, our disclosure controls and procedures were not effective.

Changes in Internal Control Over Financial Reporting

We regularly review our system of internal control over financial reporting and make changes to our processes and systems to improve controls and increase efficiency, while ensuring that we maintain an effective internal control environment. Changes may include such activities as implementing new, more efficient systems, consolidating activities, and migrating processes.

During its evaluation of the effectiveness of our internal control over financial reporting as of September 30, 2019, our management identified the following material weaknesses:

- We do not have sufficient and skilled accounting personnel with an appropriate level of technical accounting knowledge and experience in the application of accounting principles generally accepted in the United States commensurate with our financial reporting requirements. To mitigate the current limited resources and limited employees, we rely heavily on the use of external legal and accounting professionals.

In order to cure the foregoing material weakness, we have taken or plan to take the following remediation measures:

- On November 5, 2018, we added a staff accountant with a CPA and technical accounting expertise to further support our current accounting personnel. As necessary, we will continue to engage consultants or outside accounting firms in order to ensure proper accounting for our consolidated financial statements.

We intend to complete the remediation of the material weakness discussed above as soon as practicable but we can give no assurance that we will be able to do so. Designing and implementing an effective disclosure controls and procedures is a continuous effort that requires us to anticipate and react to changes in our business and the economic and regulatory environments and to devote significant resources to maintain a financial reporting system that adequately satisfies our reporting obligations. The remedial measures that we have taken and intend to take may not fully address the material weakness that we have identified, and material weaknesses in our disclosure controls and procedures may be identified in the future. Should we discover such conditions, we intend to remediate them as soon as practicable. We are committed to taking appropriate steps for remediation, as needed.

All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Other than in connection with the implementation of the remedial measures described above, there were no changes in our internal controls over financial reporting during quarter ended September 30, 2019 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II
OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

There were no material developments during the quarter ended September 30, 2019 to the legal proceedings previously disclosed in Item 3 “Legal Proceedings” of our Transition Report on Form 10-KT filed on April 1, 2019.

ITEM 1A. RISK FACTORS.

For information regarding risk factors, please refer to our prospectus contained in our Post-Effective Amendment No. 3 to Form S-1 as filed with the SEC on May 17, 2019.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.

We have not sold any equity securities during the quarter ended September 30, 2019 that were not previously disclosed in a current report on Form 8-K that was filed during the quarter.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES.

None.

ITEM 4. MINE SAFETY DISCLOSURES.

Not applicable.

ITEM 5. OTHER INFORMATION.

Subsequent Events

On July 2, 2019, our board of directors approved a supplement to our engagement agreement with one of our service providers pursuant to which we agreed to issue to the service provider 23,972 restricted shares of our common stock in consideration of that service provider’s agreement to defer the receipt of payment of certain accrued fees due to the service provider.

We have no information to disclose that was required to be in a report on Form 8-K during the quarter ended September 30, 2019 but was not reported. There have been no material changes to the procedures by which security holders may recommend nominees to our board of directors.

ITEM 6. EXHIBITS.

| Exhibit No. | Description |
|--------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 2.1 | Agreement and Plan of Merger, dated September 26, 2013, between Aerkomm Inc. and Maple Tree Kids LLC (incorporated by reference to Exhibit 2.1 to the Registration Statement on Form S-1 filed on November 5, 2013) |
| 2.2 | Form of Share Exchange Agreement, dated February 13, 2017, among Aerkomm Inc., Aircom Pacific, Inc. and the shareholders of Aircom Pacific, Inc. (incorporated by reference to Exhibit 2.2 to the Current Report on Form 8-K filed on February 14, 2017) |
| 3.1 | Restated Articles of Incorporation of the registrant (incorporated by reference to Exhibit 2.2 to the Current Report on Form 8-K filed on May 4, 2017) |
| 3.2 | Certificate of Change Pursuant to NRS 78.209 (incorporated by reference to Exhibit 3.1 to the Current Report on Form 8-K filed on January 16, 2019) |
| 3.3 | Restated Bylaws of the registrant (incorporated by reference to Exhibit 3.2 to the Form 8A-12G filed on April 19, 2018) |
| 4.1 | Form of Underwriter Warrant (incorporated by reference to Exhibit 4.1 to Amendment No. 1 to Registration Statement on Form S-1/A filed on February 2, 2018) |
| 10.1 | Amendment No. 3 to Underwriting Agreement between Aerkomm Inc. and Boustead Securities, LLC dated June 27, 2019 (incorporated by reference to Exhibit 1.1 to Amendment No. 1 to the Current Report on Form 8-K filed on June 28, 2019) |
| 10.2 | Letter of Undertaking dated July 6, 2019 (incorporated by reference to Exhibit 99.1 to Amendment No. 1 to the Current Report on Form 8-K filed on July 18, 2019) |
| 10.3 | Definitive Agreement between the Registrant and MJet GMBH dated June 11, 2019 (incorporated by reference to Exhibit 10.3 to the Quarterly Report on Form 10-Q filed on August 14, 2019) |
| 31.1* | Certifications of Principal Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 31.2* | Certifications of Principal Financial and Accounting Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 32.1* | Certification of Principal Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |
| 32.2* | Certification of Principal Financial and Accounting Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |
| 101.INS | XBRL Instance Document |
| 101.SCH | XBRL Taxonomy Extension Schema Document |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document |

* Filed herewith

SIGNATURES

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.

Date: November 14, 2019

AERKOMM INC.

/s/ Jeffrey Wun

Name: Jeffrey Wun

Title: Chief Executive Officer
(Principal Executive Officer)

/s/ Y. Tristan Kuo

Name: Y. Tristan Kuo

Title: Chief Financial Officer
(Principal Financial and Accounting Officer)