

Data Storage Corp
Form 10-Q
November 15, 2016

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, 2016

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

For the transition period from _____ to _____

Commission File No. 001-35384

DATA STORAGE CORPORATION

(Exact name of registrant as specified in its charter)

NEVADA

98-0530147

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(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)

68 South Service Road
Melville, N.Y. **11747**
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: **(212) 564-4922**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

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

Large Accelerated Filer Accelerated Filer
Non-Accelerated Filer Smaller Reporting Company
(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

The number of shares of the registrant's common stock outstanding as of September 30, 2016 was 36,588,240.

DATA STORAGE CORPORATION

FORM 10-Q

September 30, 2016

INDEX

| | Page |
|--|-------------|
| <u>PART I— FINANCIAL INFORMATION</u> | |
| Item 1. <u>Financial Statements</u> | 3 |
| <u>Consolidated Balance Sheets as of September 30, 2016 (unaudited) and December 31, 2015</u> | 3 |
| <u>Consolidated Statements of Operations for the three and nine months ended September 30, 2016 and 2015 (unaudited)</u> | 4 |
| <u>Consolidated Statements of Cash Flows for the Nine months ended September 30, 2016 and 2015 (unaudited)</u> | 5 |
| <u>Notes to Consolidated Financial Statements</u> | 6 - 16 |
| Item 2. <u>Management’s Discussion and Analysis of Financial Condition and Results of Operations</u> | 17 -18 |
| Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u> | 19 |
| Item 4. <u>Control and Procedures</u> | 19 |
| <u>PART II— OTHER INFORMATION</u> | |
| Item 1. <u>Legal Proceedings</u> | 20 |
| Item 1A. <u>Risk Factors</u> | 20 |
| Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u> | 20 |
| Item 3. <u>Defaults Upon Senior Securities</u> | 20 |
| Item 4. <u>Mine Safety Disclosures</u> | 20 |
| Item 5. <u>Other Information</u> | 20 |

PART I

ITEM 1. Financial Statements

DATA STORAGE CORPORATION AND SUBSIDIARY

CONDENSED CONSOLIDATED BALANCE SHEETS

| | September 30, 2016 (UNAUDITED) | December 31, 2015 |
|---|--------------------------------------|----------------------|
| ASSETS | | |
| Current Assets: | | |
| Cash and cash equivalents | \$ 105,471 | \$ 67,045 |
| Accounts receivable (less allowance for doubtful accounts of \$15,000 in 2016 and \$15,000 in 2015) | 103,633 | 118,619 |
| Prepaid expenses and other current assets | 275,408 | 231,443 |
| Total Current Assets | 484,512 | 417,107 |
| Property and Equipment: | | |
| Property and equipment | 3,375,958 | 3,375,958 |
| Less—Accumulated depreciation | (3,198,587) | (3,064,492) |
| Net Property and Equipment | 177,371 | 311,466 |
| Other Assets: | | |
| Goodwill | 2,201,828 | 2,201,828 |
| Employee loans | - | 85,800 |
| Other assets | 15,156 | 6,060 |
| Intangible assets, net | 327,457 | 350,433 |
| Investment in joint venture – at equity | 17,545 | 20,117 |
| Total Other Assets | 2,561,986 | 2,664,238 |
| Total Assets | 3,223,869 | 3,392,811 |
| LIABILITIES AND STOCKHOLDERS' DEFICIT | | |
| Current Liabilities: | | |
| Accounts payable and accrued expenses | 1,619,019 | 1,051,349 |
| Revolving credit facility | 99,292 | 99,292 |
| Dividend payable | 591,623 | 513,073 |
| Deferred revenue | 342,506 | 436,563 |
| Leases payable | 252,841 | 241,983 |

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| | | |
|---|---------------|---------------|
| Note payable – bank | 350,000 | 350,000 |
| Convertible debt – related parties net of discount | 901,924 | 901,924 |
| Total Current Liabilities | 4,157,205 | 3,594,184 |
| Deferred rental obligation | 1,741 | 1,251 |
| Note Payable – related party | 12,000 | 12,000 |
| Leases payable long-term | 155,571 | 346,583 |
| Convertible debt – related parties | 1,199,439 | 1,189,439 |
| Total Long Term Liabilities | 1,368,751 | 1,549,273 |
| Total Liabilities | 5,525,956 | 5,143,457 |
| Stockholders' Deficit: | | |
| Preferred Stock, \$.001 par value; 10,000,000 shares authorized; 1,401,786 shares issued and outstanding in each period | 1,402 | 1,402 |
| Common stock, par value \$.001; 250,000,000 shares authorized; 36,588,240 shares issued and outstanding in each period | 36,588 | 36,588 |
| Additional paid in capital | 12,841,752 | 12,805,332 |
| Accumulated deficit | (15,181,829) | (14,593,968) |
| Total Stockholders' (Deficit) Equity | (2,302,087) | (1,750,646) |
| Total Liabilities and Stockholders' (Deficit) | \$ 3,223,869 | \$3,392,811 |

The accompanying notes are an integral part of these consolidated financial statements.

DATA STORAGE CORPORATION AND SUBSIDIARY

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

| | Three months Ended September 30, | | Nine months Ended September 30, | |
|---|-------------------------------------|--------------|------------------------------------|--------------|
| | 2016 | 2015 | 2016 | 2015 |
| Sales | \$922,919 | \$930,686 | \$2,912,152 | \$2,988,503 |
| Cost of sales | 622,836 | 612,916 | 1,861,148 | 1,865,380 |
| Gross Profit | 300,083 | 317,770 | 1,051,004 | 1,123,123 |
| Operating Expenses | | | | |
| Selling, general and administrative | 389,684 | 400,984 | 1,285,145 | 1,395,856 |
| Research and development | 23,527 | 15,000 | 69,640 | 51,000 |
| Total Operating Expenses | 413,211 | 415,984 | 1,354,785 | 1,446,856 |
| Loss from Operations | (113,128) | (98,214) | (303,781) | (323,733) |
| Other Income (Expense) | | | | |
| Interest income | - | 1 | - | 2 |
| Interest expense | (70,231) | (71,893) | (204,466) | (218,828) |
| Bad Debt Recovery | - | - | 1,508 | - |
| Net gain (loss) on equity method investment | (2,362) | 31,625 | (2,572) | 26,972 |
| Total Other Income (Expense) | (72,593) | (40,267) | (205,530) | (191,854) |
| Loss before provision for income taxes | (185,721) | (138,481) | (509,311) | (515,587) |
| Provision for income taxes | — | — | — | — |
| Net Loss | (185,721) | (138,481) | (509,311) | (515,587) |
| Preferred Stock Dividends | (26,178) | (24,294) | (78,550) | (71,106) |
| Net Loss Attributable to Common Stockholders | \$(211,899) | \$(162,775) | \$(587,861) | \$(586,693) |
| Loss per Share – Basic and Diluted | \$(0.01) | \$(0.00) | \$(0.01) | \$(0.02) |
| Weighted Average Number of Shares - Basic and Diluted | 36,588,240 | 36,588,240 | 36,588,240 | 36,588,240 |

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

DATA STORAGE CORPORATION AND SUBSIDIARY**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(UNAUDITED)**

| | Nine months ended September 30, | |
|---|------------------------------------|--------------|
| | 2016 | 2015 |
| Cash Flows from Operating Activities: | | |
| Net loss | \$(509,311) | \$(515,587) |
| Adjustments to reconcile net loss to net cash provided by operating activities: | | |
| Depreciation and amortization | 157,071 | 412,462 |
| Net (gain) loss on equity method investment | 2,572 | (26,972) |
| Write off employee loan | 85,800 | - |
| Non cash interest expense | 174,851 | 158,673 |
| Loan Impairment | - | 18,300 |
| Stock based compensation | 36,420 | 73,883 |
| Changes in Assets and Liabilities: | | |
| Accounts receivable | 14,986 | (23,714) |
| Other assets | (9,096) | (450) |
| Prepaid expenses and other current assets | (43,965) | (147,307) |
| Employee loan | - | (28,000) |
| Accounts payable and accrued expenses | 392,816 | 128,084 |
| Deferred revenue | (94,057) | (26,905) |
| Deferred rent | 490 | 490 |
| Net Cash Provided by Operating Activities | 208,577 | 22,957 |
| Cash Flows from Financing Activities: | | |
| Issuance of convertible debt | 10,000 | 80,000 |
| Repayments of revolving credit facility | - | (10,000) |
| Repayments of capital lease obligations | (180,151) | (165,320) |
| Net Cash (Used in) Financing Activities | (170,151) | (95,320) |
| Increase (Decrease) in Cash and Cash Equivalents | 38,426 | (72,363) |
| Cash and Cash Equivalents, Beginning of Period | 67,045 | 110,448 |
| Cash and Cash Equivalents, End of Period | \$105,471 | \$38,085 |
| Cash paid for interest | \$29,615 | \$44,334 |
| Cash paid for income taxes | \$- | \$- |
| Non cash investing and financing activities: | | |

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| | | |
|--|----------|-------------|
| Accrual of preferred stock dividend | \$78,550 | \$71,106 |
| Conversion of due to related party to convertible debt | \$- | \$245,601 |
| Conversion of due to officer to convertible debt | \$- | \$1,065,762 |
| Acquisition of equipment under capital lease | | \$14,443 |

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

DATA STORAGE CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
NINE MONTHS ENDED SEPTEMBER 30, 2016 AND 2015

Note 1 - Basis of presentation, organization and other matters

Headquartered in Melville, N.Y., Data Storage Corporation (“DSC” or the “Company”) offers its cloud based disaster recovery and business continuity solutions and services to businesses within the healthcare, banking and finance, distribution services, manufacturing, construction, education and government sectors.

DSC derives revenues from long term subscription services and professional services related to the implementation of subscription services that provide organizations in the education, government and healthcare industries protection of critical computerized data. In 2009, the Company’s revenues consisted primarily of offsite data backup, de-duplication, continuous data protection and Cloud Disaster Recovery solutions and protecting information for our clients. In 2010, DSC expanded its solutions based on the asset acquisition of SafeData to provide business continuity solution to the IBM user marketplace. In 2012, DSC continued to assimilate and acquire organizations, expanded its technology as well as its technical group and positioned the new organization for growth. In October 2012, DSC purchased the software and assets of Message Logic. The Message Logic acquisition provides DSC with ownership of the pending patent and intellectual property to insure email compliance to organizations within its client base and target audience. In 2012 DSC entered into a joint venture agreement with ABC Services LLC to provide an IBM Power i cloud with 50% ownership in the entity Secure Infrastructure and Services, LLC.

DSC maintains equipment for cloud storage and cloud computing in our data centers in Massachusetts, and New York. DSC delivers its solutions over highly reliable, redundant and secure fiber optic networks with separate and diverse routes to the Internet. DSC’s network and geographical diversity is important to clients seeking storage hosting and disaster recovery solutions, ensuring protection of data and continuity of business in the case of a network interruption.

Liquidity

The financial statements have been prepared using accounting principles generally accepted in the United States of America applicable for a going concern, which assumes that the Company will realize its assets and discharge its liabilities in the ordinary course of business. For the nine months ended September 30, 2016, the Company has

generated revenues of \$2,912,152 but has incurred a net loss attributable to common shareholders of \$587,861. Its ability to continue as a going concern is dependent upon achieving sales growth, reduction of operation expenses and ability of the Company to obtain the necessary financing to meet its obligations and pay its liabilities arising from normal business operations when they come due, and upon profitable operations. The Company has been funded by the Mr. Charles M. Piluso, the Company's Chief Executive Officer ("CEO") and largest shareholder since inception as well as several Directors. It is the intention of Mr. Piluso to continue to fund the Company on an as-needed basis.

The condensed balance sheet at December 31, 2015 was derived from audited financial statements but does not include all disclosures required by accounting principles generally accepted in the United States of America. The other information in these condensed financial statements is unaudited but, in the opinion of management, reflects all adjustments necessary for a fair presentation of the results for the periods covered. All such adjustments are of a normal recurring nature unless disclosed otherwise. These condensed financial statements, including notes, have been prepared in accordance with the applicable rules of the Securities and Exchange Commission and do not include all of the information and disclosures required by accounting principles generally accepted in the United States of America for complete financial statements. These condensed financial statements should be read in conjunction with the financial statements and additional information as contained in our Annual Report on Form 10-K for the year ended December 31, 2015.

Note 2 - Summary of Significant Accounting Policies

Stock Based Compensation

The Company follows the requirements of FASB ASC 718-10-10, *Share-Based Payments* with regard to stock-based compensation issued to employees. The Company has stock-based incentives for consultants and employees that over achieve. This plan is discretionary. The expense for this stock-based compensation is equal to the fair value of the stock that was determined by using closing price on the day the stock was awarded multiplied by the number of shares awarded. The Company records its options at fair value using the Black-Scholes valuation model.

Recently Issued and Newly Adopted Accounting Pronouncements

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers" ("ASU 2014-09"), which requires entities to recognize revenue in a way that depicts the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods or services. The new guidance also requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. In July 2015, the FASB voted to delay the effective date of ASU 2014-09 by one year to the first quarter of 2018 to provide companies sufficient time to implement the standards. Early adoption will be permitted, but not before the first quarter of 2017. Adoption can occur using one of two prescribed transition methods. In March and April 2016, the FASB issued ASU 2016-08, "Revenue

from Contracts with Customers: Principal versus Agent Considerations (Reporting Revenue Gross versus Net)” and ASU 2016-10, “Revenue from Contracts with Customers: Identifying Performance Obligations and Licensing” which provide supplemental adoption guidance and clarification to ASC 2014-09. ASU 2016-08 and ASU 2016-10 must be adopted concurrently with the adoption of ASU 2014-09. The Company is currently evaluating the impact of these new standards.

On August 2014, FASB issued Accounting Standards Update No. 2014-15, Presentation of Financial Statements - Going Concerns (Subtopic 205-40): Disclosures of Uncertainties about an Entity's Ability to Continue as a Going Concern. The amendments require management to assess an entity's ability to continue as a going concern by incorporating and expanding upon certain principles that are currently in U.S. auditing standards. Specifically, the amendments (1) provide a definition of the term substantial doubt, (2) require an evaluation every reporting period including interim periods, (3) provide principles for considering the mitigating effect of management's plans, (4) require certain disclosures when substantial doubt is alleviated as a result of consideration of management's plans, (5) require an express statement and other disclosures when substantial doubt is not alleviated, and (6) require an assessment for a period of one year after the date that the financial statements are issued (or available to be issued). The amendments in this Update are effective for the annual period ending after December 15, 2016, and for annual periods and interim periods thereafter. Early application is permitted. The adoption of ASU 2014-15 is not expected to have a material impact on our financial position or results of operations.

In April 2015, the Financial Accounting Standards Board (FASB) issued ASU 2015-05, "Customer's Accounting for Fees Paid in a Cloud Computing Arrangement." This ASU provides clarification on whether a cloud computing arrangement includes a software license. If a software license is included, the customer should account for the license consistent with its accounting of other software licenses. If a software license is not included, the arrangement should be accounted for as a service contract. This ASU is effective for annual reporting periods beginning after December 15, 2015, and interim periods within those years. Adoption of ASU 2015-05 did not have a material impact on our financial position or results of operations.

During February 2016, the FASB issued ASU No. 2016-02, "Leases" ("ASU 2016-02"). The standard requires lessees to recognize a lease liability and a lease asset for all leases, including operating leases, with a term greater than 12 months on its balance sheet. The update also expands the required quantitative and qualitative disclosures surrounding leases. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. The Company is currently evaluating the impact of the new standard.

In March 2016, FASB issued ASU No. 2016-09, "Improvements to Employee Share-based Payment Accounting" ("ASU 2016-09"). ASU 2016-09 simplifies several aspects of the accounting for employee share-based payment transactions for both public and nonpublic entities, including the accounting for income taxes, forfeitures, and statutory tax withholding requirements, as well as classification in the statement of cash flows. ASU 2016-09 is effective for annual periods beginning after December 15, 2017, and interim periods within annual periods beginning after December 15, 2018. Early adoption is permitted. The Company is currently evaluating the standard and the impact on its consolidated financial statements and footnote disclosures.

In August 2016, the FASB issued ASU No. 2016-15, "Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments" ("ASU 2016-15"). ASU 2016-15 addresses eight specific cash flow issues with the objective of reducing diversity in practice regarding how certain cash receipts and cash payments are presented in the statement of cash flows. The standard provides guidance on the classification of the following items: (1) debt

prepayment or debt extinguishment costs, (2) settlement of zero-coupon debt instruments, (3) contingent consideration payments made after a business combination, (4) proceeds from the settlement of insurance claims, (5) proceeds from the settlement of corporate-owned life insurance policies, (6) distributions received from equity method investments, (7) beneficial interests in securitization transactions, and (8) separately identifiable cash flows. The Company is required to adopt ASU 2016-15 for fiscal years, and for interim periods within those fiscal years, beginning after December 15, 2017 on a retrospective basis. Early adoption is permitted, including adoption in an interim period. The Company is currently evaluating the impact of adoption of ASU 2016-15.

We have reviewed all FASB issued Accounting Standards Update (“ASU”) accounting pronouncements and interpretations thereof that have effectiveness dates during the periods reported and in future periods. The Company has carefully considered the new pronouncements that alter previous generally accepted accounting principles and does not believe that any new or modified principles will have a material impact on the corporation’s reported financial position or operations in the near term. The applicability of any standard is subject to the formal review of our financial management and certain standards are under consideration.

Management does not believe there would have been a material effect on the accompanying consolidated financial statements had any other recently issued, but not yet effective, accounting standards been adopted in the current period.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its subsidiary, Data Storage Corporation, a Delaware Corporation. All significant inter-company transactions and balances have been eliminated in consolidation.

Equity Investments

Equity investments in which the Company exercises significant influence but does not control and is not the primary beneficiary are accounted for using the equity method. The Company’s share of its equity method investee’s earnings or losses is included in other income in the accompanying Consolidated Statements of Operations.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and

disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from these estimates.

Estimated Fair Value of Financial Instruments

The Company's financial instruments include cash, accounts receivable, accounts payable, line of credit and due to related parties. Management believes the estimated fair value of these accounts at September 30, 2016 approximate their carrying value as reflected in the balance sheets due to the short-term nature of these instruments or the use of market interest rates for debt instruments. The carrying values of certain of the Company's notes payable and capital lease obligations approximate their fair values based upon a comparison of the interest rate and terms of such debt given the level of risk to the rates and terms of similar debt currently available to the Company in the marketplace.

Cash, Cash Equivalents and Short-Term Investments

The Company considers all highly liquid investments with an original maturity or remaining maturity at the time of purchase, of six months or less to be cash equivalents.

Concentration of Credit Risk and Other Risks and Uncertainties

Financial instruments and assets subjecting the Company to concentration of credit risk consist primarily of cash and cash equivalents, short-term investments and trade accounts receivable. The Company's cash and cash equivalents are maintained at major U.S. financial institutions. Deposits in these institutions may exceed the amount of insurance provided on such deposits.

The Company's customers are primarily concentrated in the United States.

The Company provides credit in the normal course of business. The Company performs ongoing credit evaluations of its customers and maintains allowances for doubtful accounts on factors surrounding the credit risk of specific customers, historical trends, and other information.

For the nine months ended September 30, 2016 DSC had one customer representing 19% of sales. For the nine months ended September 30, 2015, DSC had no customer concentrations.

Accounts Receivable/Allowance for Doubtful Accounts

The Company sells its services to customers on an open credit basis. Accounts receivable are uncollateralized, non-interest-bearing customer obligations. Accounts receivables are due within 30 days. The allowance for doubtful accounts reflects the estimated accounts receivable that will not be collected due to credit losses and allowances. Provisions for estimated uncollectible accounts receivable are made for individual accounts based upon specific facts and circumstances including criteria such as their age, amount, and customer standing. Provisions are also made for other accounts receivable not specifically reviewed based upon historical experience. Clients are invoiced in advance for services as reflected in deferred revenue on the Company's balance sheet.

Property and Equipment

Property and equipment is recorded at cost and depreciated over their estimated useful lives or the term of the lease using the straight-line method for financial statement purposes. Estimated useful lives in years for depreciation are five to seven years for property and equipment. Additions, betterments and replacements are capitalized, while

expenditures for repairs and maintenance are charged to operations when incurred. As units of property are sold or retired, the related cost and accumulated depreciation are removed from the accounts, and any resulting gain or loss is recognized in income.

Income Taxes

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. At September 30, 2016, the Company had a full valuation allowance against its deferred tax assets.

Goodwill and Other Intangibles

In accordance with GAAP, the Company tests goodwill and other intangible assets for impairment on at least an annual basis. Goodwill impairment exists if the net book value of a reporting unit exceeds its estimated fair value. The impairment testing is performed in two steps:

(i) the Company determines impairment by comparing the fair value of a reporting unit with its carrying value, and (ii) if there is an impairment, the Company measures the amount of impairment loss by comparing the implied fair value of goodwill with the carrying amount of that goodwill. To determine the fair value of these intangible assets, the Company uses many assumptions and estimates using a market participant approach that directly impact the results of the testing. In making these assumptions and estimates, the Company uses industry accepted valuation models and set criteria that are reviewed and approved by various levels of management.

In September 2011, the Financial Accounting Standards Board (the "FASB") issued Accounting Standards Update ("ASU") 2011-08, "Intangibles-Goodwill and Other (Topic 350): Testing Goodwill for Impairment", to allow entities to use a qualitative approach to test goodwill for impairment. ASU 2011-08 permits an entity to first perform a qualitative assessment to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying value. If it is concluded that this is the case, it is necessary to perform the currently prescribed two-step goodwill impairment test. Otherwise, the two-step goodwill impairment test is not required. The Company adopted ASU 2011-08 in fiscal 2013 and thus performed a qualitative assessment. This adoption did not have a material impact on the Company's condensed consolidated financial statements.

Revenue Recognition

The Company's revenues consist principally of cloud storage and cloud computing revenues, SaaS and IaaS. Storage revenues consist of monthly charges related to the storage of materials or data (generally on a per unit basis). Sales are generally recorded in the month the service is provided. For customers who are billed on an annual basis, deferred revenue is recorded and amortized over the life of the contract. Set up fees charged in connection with storage contracts are deferred and recognized on a straight-line basis over the life of the contract.

Impairment of Long-Lived Assets

In accordance with FASB ASC 360-10-35, we review our long-lived assets for impairment whenever events and circumstances indicate that the carrying value of an asset might not be recoverable. An impairment loss, measured as the amount by which the carrying value exceeds the fair value, is recognized if the carrying amount exceeds estimated undiscounted future cash flows.

Advertising Costs

The Company expenses the costs associated with advertising as they are incurred. The Company incurred \$106,865 and \$27,325 for advertising costs for the nine months ended September 30, 2016 and 2015, respectively.

Net Income (Loss) Per Common Share

In accordance with FASB ASC 260, Earnings Per Share, basic income (loss) per share is computed by dividing net income (loss) by the weighted average number of shares of common stock outstanding during the period. Diluted earnings per share is computed by dividing net income (loss) adjusted for income or loss that would result from the assumed conversion of potential common shares from contracts that may be settled in stock or cash by the weighted average number of shares of common stock, common stock equivalents and potentially dilutive securities outstanding during each period. The inclusion of the potential common shares to be issued would have an anti-dilutive effect on diluted loss per share and therefore they are not included in the calculation. Potentially dilutive securities at September 30, 2016 include 7,045,463 options and 133,334 warrants.

Note 3 - Property and Equipment

Property and equipment, at cost, consist of the following:

| | September 30, 2016 | December 31, 2015 |
|--------------------------------|-----------------------|----------------------|
| Storage equipment | \$ 2,075,639 | \$ 2,075,639 |
| Website and software | 533,418 | 533,418 |
| Furniture and fixtures | 14,037 | 14,037 |
| Computer hardware and software | 86,184 | 86,184 |
| Data Center Equipment | 666,680 | 666,680 |
| | 3,375,958 | 3,375,958 |
| Less: Accumulated depreciation | 3,198,587 | 3,064,492 |
| Net property and equipment | \$ 177,371 | \$ 311,466 |

Depreciation expense for the nine months ended September 30, 2016 and 2015 was \$134,095 and \$321,278, respectively.

Note 4 - Goodwill and Intangible Assets

Goodwill and intangible assets consisted of the following:

| | | September 30, 2016 | |
|---|-------------------------------|--------------------|-----------------------------|
| | Estimated life in years | Gross amount | Accumulated Amortization |
| Goodwill | Indefinite | \$2,201,828 | N/A |
| Intangible Assets | | | |
| Intangible assets not subject to amortization | | | |
| Trademarks | Indefinite | 294,268 | N/A |
| Intangible assets subject to amortization | | | |
| Customer list | 5 - 15 | 897,274 | 864,086 |
| Non-compete agreements | 4 | 262,147 | 262,147 |
| Total Intangible Assets | | 1,453,689 | 1,126,233 |

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| | | |
|--------------------------------------|-------------|--------------|
| Total Goodwill and Intangible Assets | \$3,655,517 | \$ 1,126,233 |
|--------------------------------------|-------------|--------------|

Scheduled amortization over the next two years as follows:

| | |
|--|----------|
| For The Twelve Months ending September 30, | |
| 2017 | 25,529 |
| Total | \$25,529 |

Amortization expense for the nine months ended September 30, 2016 and 2015 was \$22,976 and \$91,185 respectively.

Note 5 – Investment in At Equity

The Company has a 50% non-controlling ownership interest in Secure Infrastructure & Services, LLC who provides infrastructure-as-a-Service (IaaS) for IBM iSeries and AIX v7 systems, Power HA services and network infrastructure hardware and services as needed to support the IaaS and PowerHA implementation and ongoing needs for customers and services sold under the Company. ASC 810 requires the Company to evaluate non-consolidated entities periodically and as circumstances change to determine if an implied controlling interest exists. During Fiscal 2013, the Company evaluated this equity investment and concluded that this is a variable interest entity and the Company is not the primary beneficiary. Secure Infrastructure & Services, LLC's fiscal year end is December 31.

The following presents unaudited summary financial information for Secure Infrastructure & Services, LLC. Such summary financial information has been provided herein based upon the individual significance of this unconsolidated equity investment to the consolidated financial information of the Company.

| | September 30, 2016 |
|---------------------------|-----------------------|
| Current assets | \$ 276,101 |
| Non-current assets | \$ 42,678 |
| Current liabilities | \$ 348,770 |
| Members' equity (deficit) | \$ (29,991) |

The equity balance carried on the Company's balance sheet amounts to \$17,545 as of September 30, 2016.

| | Nine months Ended September 30, 2016 |
|--------------------|--|
| Net sales | \$ 1,328,753 |
| Gross profit | \$ 336,469 |
| Operating expenses | \$ 341,614 |
| Net income(loss) | \$ (5,145) |

The Company's share of the net loss from Secure Infrastructure & Services, LLC for the nine months ended September 30, 2016 was \$2,572.

Note 6 – Capital Lease Obligations

The Company entered into a new lease agreement with Systems Trading, Inc. on May 1, 2014 to refinance all outstanding leases into one capital lease. This lease obligation is payable to Systems Trading, Inc. with monthly installments of \$21,826 from June 1, 2014 through May 1, 2018. This lease is secured with the computer equipment and has been capitalized. Pursuant to Accounting Standards Codification (“ASC”) 470-50-40, Debt Modifications and Extinguishments-Derecognition, the Company determined that modification accounting applied to the refinancing. The new capital lease obligation has an effective interest rate of 7.22%.

On July 10, 2015, the Company entered into a lease with Systems Trading, Inc. The lease is for \$14,443, calls for monthly payments of \$420 and expires on August 1, 2018. It carries an interest rate of 3%. On November 1, 2015, the Company added to the existing lease with Systems Trading. The lease addendum totaled \$7,998, calls for monthly payments of \$258 and expires on August 1, 2018. It carries no interest.

Future minimum lease payments under the capital leases are as follows:

| | |
|--|------------|
| As of September 30, 2016 | \$428,679 |
| Less amount representing interest | (20,267) |
| Total obligations under capital leases | 408,412 |
| Less current portion of obligations under capital leases | (252,841) |
| Long-term obligations under capital leases | \$ 155,571 |

Long-term obligations under capital leases at September 30, 2016 mature as follows:

| | |
|--|-----------|
| For the twelve months ending September 30, | |
| 2017 | \$270,051 |
| 2018 | 158,628 |
| | \$428,679 |

The assets held under the capital leases are included in property and equipment as follows:

| | |
|--------------------------------|-------------|
| Equipment | \$1,361,995 |
| Less: accumulated depreciation | (1,138,509) |
| | \$223,486 |

Note 7 - Commitments and Contingencies

Revolving Credit Facility

On January 31, 2008, the Company entered into a revolving credit line with a bank. The credit facility provides for \$100,000 at prime plus .5%, or 3.75% at September 30, 2016, and is secured by all assets of the Company and personally guaranteed by the Company's principal shareholder. As of September 30, 2016, the Company owed \$99,292 under this agreement.

Operating Leases

The Company currently leases office space in Melville, NY, and Warwick, RI.

The lease for office space in Melville, NY, calls for monthly payments of \$3,498 beginning July 1, 2016. This lease commenced on June 1, 2016 and continues through September 30, 2017.

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The lease for office space in Warwick, RI calls for monthly payments of \$2,324 beginning February 1, 2014 which escalates to \$2,460 on February 1, 2017. This lease commenced on February 1, 2014 and continues through January 31, 2019.

Minimum obligations under these lease agreements are as follows:

| | |
|--|-----------|
| For the twelve months ending September 30, | |
| 2017 | \$74,450 |
| 2018 | 29,520 |
| 2019 | 9,840 |
| | \$113,810 |

Rent expense for the nine months ended September 30, 2016 and September 30, 2015 was \$101,865 and \$98,078 respectively.

Note 8 –Related Party Debt

Convertible Debt - Related Party

On January 31, 2012, the Company issued a \$500,000 convertible promissory note to a director of the company in consideration of a loan in the amount of \$500,000. The note is convertible into shares of the Company's common stock at \$0.85 per share and carries interest at 10% per annum. Interest is payable quarterly through the maturity date of January 31, 2015. DSC has accrued interest on this note totaling \$236,781 and is in arrears on its interest payments. On May 13, 2015, the maturity date of the note was extended to May 6, 2016. On October 10, 2016, this note has been approved by the board for the conversion of debt to equity with interest payable through October 25, 2016.

On February 28, 2013, the Company issued a \$100,000 convertible promissory note to a director of the company in consideration of a loan in the amount of \$100,000. The note is convertible into shares of the Company's common stock at \$0.15 per share and carries interest at 10% per annum. Interest is payable quarterly through the note's maturity date of February 28, 2014. The Company issued 66,667 warrants valued at of \$17,851 which was recorded as a discount to the convertible promissory note. In 2014, the Company defaulted on this note and is subject to additional interest of 5% per annum as well as additional 10% warrants for each year that it remains in default. DSC has accrued interest on this note totaling \$38,822. On May 13, 2015, the maturity date of the note was extended to May 6, 2016. On October 10, 2016, this note has been approved by the board for the conversion of debt to equity with interest payable through October 25, 2016.

On August 9, 2013, the Company issued a \$100,000 convertible promissory note to the CEO of the Company in consideration of a loan in the amount of \$100,000. The convertible promissory note is convertible into shares of common stock of the Company at \$0.15 and carries interest at 10% per annum. Interest is payable quarterly through the note's maturity date of April 30, 2014. The Company issued 66,667 warrants valued at \$17,851 in connection with this note, which was recorded as a discount to the convertible promissory notes based on its relative fair value with an offset to additional paid in capital. In 2014, the Company defaulted on this note and is subject to additional interest of 5% per annum as well as the additional 10% warrants for each year in default. DSC has accrued interest on this note totaling \$34,411. On May 13, 2015, the maturity date was extended to May 6, 2016. On October 10, 2016, this note has been approved by the board for the conversion of debt to equity with interest payable through October 25, 2016.

Effective January 1, 2015, the Company issued a \$1,189,439 convertible promissory note to the Company's CEO. This note was issued to convert debt that is owed to the CEO and to 875 Merrick LLC. The note carries interest at 10% per annum. Interest shall accrue and be payable in arrears on December 31, 2017. The note and all accrued and unpaid interest is convertible into shares of the Company's common stock at \$0.85 per share. DSC has accrued interest on this note totaling \$216,218. On October 10, 2016, this note has been approved by the board for the conversion of debt to equity with interest payable through October 25, 2016.

Effective January 1, 2015, the Company issued a \$121,924 convertible promissory note to the Company's CEO. This note was issued to convert debt that is owed to the CEO and to 875 Merrick LLC. The note carries interest of 10% per annum. Interest shall accrue and be payable in arrears on December 31, 2016. The note and all accrued and unpaid interest is convertible into shares the Company's common stock at \$0.15 per share. DSC has accrued interest on this note totaling \$22,163. On October 10, 2016, this note has been approved by the board for the conversion of debt to equity with interest payable through October 25, 2016.

On February 19, 2015, the Company issued an \$80,000 convertible promissory note to the Company's CEO in consideration of an \$80,000 loan. The note carries interest at 10% per annum. Interest shall accrue and be payable in arrears on February 18, 2016. The note and all accrued and unpaid interest is convertible into shares of the Company's common stock at \$0.15 per share. DSC has accrued interest on this note totaling \$14,960. On October 10, 2016, this note has been approved by the board for the conversion of debt to equity with interest payable through October 25, 2016.

Note Payable – Related Party

On October 7, 2015, the Company issued a \$12,000 promissory note to the Company's CEO in consideration of a \$12,000 loan. The note carries interest at 10% per annum. Interest shall accrue and be payable in arrears on October 6, 2017. DSC has accrued interest on this note totaling \$1,261. This note has been approved by the board for the conversion of debt to equity On October 10, 2016, this note has been approved by the board for the conversion of debt to equity with interest payable through October 25, 2016.

On September 7, 2016, the Company issued a \$10,000 promissory note to the Company's CEO in consideration of a \$10,000 loan. The note carries interest at 10% per annum. Interest shall accrue and be payable in arrears on September 8, 2018. DSC has accrued interest on this note totaling \$134. On October 10, 2016, this note has been approved by the board for the conversion of debt to equity with interest payable through October 25, 2016.

Note 9 – Note Payable – bank

In connection with the 2012 acquisition of Message Logic, LLC, the Company acquired software subject to a UCC filing in the amount of \$350,000 plus accrued interest. On September 5, 2014, the Company entered into an agreement whereby the Company will pay all arrears interest over 7 months at \$3,910 per month. In addition, the Company has agreed to make monthly interest payments at \$1,553 per month with the principal balance of \$350,000 payable on April 30, 2016. This note is currently in default. The company is currently in negotiations with the bank to attempt to negotiate a self amortizing loan. The company has accrued interest on this loan of \$7,765.

Note 10 - Stockholders' (Deficit)

Capital Stock

The Company has 260,000,000 shares of capital stock authorized, consisting of 250,000,000 shares of Common Stock, par value \$0.001, 10,000,000 shares of Preferred Stock, par value \$0.001 per share.

Common Stock Options

2008 Equity Incentive Plan

In October 2008, the Company's board of directors (the "Board") adopted, the 2008 Equity Incentive Plan (the "2008 Plan"). Under the 2008 Plan, we may grant options (including incentive stock options) to purchase our common stock or restricted stock awards to our employees, consultants or non-employee directors. The 2008 Plan is administered by the Board. Awards may be granted pursuant to the 2008 Plan for 10 years from the date the Board approved the 2008 Plan. Any grant under the 2008 Plan may be repriced, replaced or regranted at the discretion of the Board. From time to time, we may issue awards pursuant to the 2008 Plan.

The material terms of options granted under the 2008 Plan (all of which have been nonqualified stock options) are consistent with the terms described in the footnotes to the "Outstanding Equity Awards at Fiscal Year-End December 31, 2011", including five-year graded vesting schedules and exercise prices equal to the fair market value of our common stock on the date of grant. Stock grants made under the 2008 Plan have not been subject to vesting

requirements. The 2008 Plan was terminated with respect to the issuance of new awards as of February 3, 2012. There are 2,081,090 options outstanding under this plan as of September 30, 2016.

2010 Incentive Award Plan

The Company has reserved 2,000,000 shares of common stock for issuance under the terms of the Data Storage Corporation 2010 Incentive Award Plan (the "2010 Plan"). The 2010 Plan is intended to promote the interests of the Company by attracting and retaining exceptional employees, consultants, directors, officers and independent contractors (collectively referred to as the "Participants"), and enabling such Participants to participate in the long-term growth and financial success of the Company. Under the 2010 Plan, the Company may grant stock options, which are intended to qualify as "incentive stock options" under Section 422 of the Internal Revenue Code of 1986, as amended, non-qualified stock options, stock appreciation rights and restricted stock awards, which are restricted shares of common stock (collectively referred to as "Incentive Awards"). Incentive Awards may be granted pursuant to the 2010 Plan for 10 years from the Effective Date. From time to time, we may issue Incentive Awards pursuant to the 2010 Plan. Each of the awards will be evidenced by and issued under a written agreement.

On April 23, 2012, the Board of Directors of the Company amended and restated the Data Storage Corporation 2010 Plan. The 2010 Plan, as amended and restated, has been renamed the "Amended and Restated Data Storage Corporation Incentive Award Plan". The new plan provides for flexibility in vesting periods and includes a limit of \$100,000 per employee per year for incentive stock options

There are 4,714,373 options outstanding under this plan as of September 30, 2016. There were 36,627 shares available for future grants under the plans.

A summary of the Company's option activity and related information follows:

| | Number of Shares Under Options | Range of Option Price Per Share | Weighted Average Exercise Price |
|---|--------------------------------------|---------------------------------------|---------------------------------------|
| Options Outstanding at January 1, 2015 | 6,854,802 | \$0.02 - 0.85 | \$ 0.26 |
| Options Granted | 250,000 | 0.35 | 0.35 |
| Options Exercised | - | - | - |
| Options Expired | (59,339) | 0.02 | 0.02 |
| Options Outstanding at September 30, 2016 | 7,045,463 | \$0.15 - 0.85 | \$ 0.28 |
| Options Exercisable at September 30, 2016 | 5,683,447 | 0.15 - 0.85 | \$ 0.27 |

Share-based compensation expense for options totaling \$36,420 and \$73,833 was recognized in our results for the nine months ended September 30, 2016 and 2015, respectively and is based on awards vested.

During the nine months ended September 30, 2016, the Company granted 250,000 options to an employee (valued on the grant date at \$0.04 using the Black Scholes pricing model).

The following weighted-average assumptions were used for grants made under the stock option plans for the nine months ended September 30, 2016:

| | |
|------------------------|----------|
| Expected volatility | 229.13 % |
| Expected term (years) | 10 |
| Risk free rate | 2.22 % |
| Dividend yield | 0 % |
| Annual forfeiture rate | 0 % |

The valuation methodology used to determine the fair value of the options issued during the year was the Black-Scholes option-pricing model. The Black-Scholes model requires the use of a number of assumptions including volatility of the stock price, the average risk-free interest rate, and the weighted average expected life of the options.

The risk-free interest rate assumption is based upon observed interest rates on zero coupon U.S. Treasury bonds whose maturity period is appropriate for the term of the Warrants and is calculated by using the average daily historical stock prices through the day preceding the grant date.

Estimated volatility is a measure of the amount by which the Company's stock price is expected to fluctuate each year during the expected life of the award. The Company's estimated volatility is an average of the historical volatility of peer entities whose stock prices were publicly available. The Company's calculation of estimated volatility is based on historical stock prices of these peer entities over a period equal to the expected life of the awards. The Company uses the historical volatility of peer entities due to the lack of sufficient historical data of its stock price.

As of September 30, 2016, there was \$24,550 of total unrecognized compensation expense related to unvested employee options granted under the Company's share based compensation plans that is expected to be recognized over a weighted average period of approximately 1.25 years.

Common Stock Warrants

A summary of the Company's warrant activity and related information follows:

| | Number of Shares <u>Under Warrants</u> | Range of Warrants Price <u>Per Share</u> | Weighted Average <u>Exercise Price</u> |
|--|---|---|---|
| Warrants Outstanding at January 1, 2016 | 133,334 | \$ 0.01 | \$ 0.01 |
| Warrants Granted | - | - | - |
| Warrants Exercised | - | - | - |
| Warrants Cancelled | - | - | - |
| Warrants Outstanding at September 30, 2016 | 133,334 | 0.01 | 0.01 |
| Warrants Exercisable at September 30, 2016 | 133,334 | 0.01 | 0.01 |

Note 11 - Litigation

We are currently not involved in any litigation that we believe could have a materially adverse effect on our financial condition or results of operations. There is no action, suit, proceeding, inquiry or investigation before or by any court, public board, government agency, self-regulatory organization or body pending or, to the knowledge of the executive officers of our company or any of our subsidiaries, threatened against or affecting DSC, its common stock, any of its subsidiaries or of DSC's or DSC's subsidiaries' officers or directors in their capacities as such, in which an adverse decision could have a material adverse effect.

Note 12 – Subsequent Events

On October 25, 2016, the Company, through its wholly-owned subsidiary (the "Subsidiary"), entered into and closed two Asset Purchase Agreements (collectively, the "Purchase Agreements") with ABC Services Inc. ("ABC I"), a New York corporation, and ABC Services II Inc. ("ABC II" and collectively with ABC I, "ABC"), a New York Corporation, pursuant to which the Subsidiary purchased certain assets from ABC, including tangible assets and service agreements, in consideration of an aggregate 64,669,936 shares of common stock of the Company (the "Shares"). The closing occurred on October 25, 2016. In the event that the audits of ABC I or ABC II for the fiscal year ended December 31, 2015 provide that either ABC I or ABC II have generated less than \$2,000,000 in revenue, then such entity's respective Shares will be reduced by the proportionate amount of such shortfall.

In addition, on October 25, 2016 (the "Effective Date"), the Company entered into three Conversion Agreements with three affiliates (collectively, the "Affiliates") of the Company pursuant to which the Company and the Affiliates agreed to convert an aggregate of \$2,678,124.28 in debt owed by the Company to the Affiliates into shares of common stock of the Company at a conversion price of \$0.10 per share (the "Conversion Price") resulting in the issuance of an aggregate of 26,781,242 shares of common stock of the Company to the Affiliates. Specifically, the Company and Charles Piluso converted \$1,802,521.08 into 18,025,210, the Company, John Coghlan converted \$138,822 into 1,388,220 shares of common stock of the Company and the Company and Clifford Stein converted \$736,781.20 into 7,367,812 shares of common stock of the Company. At the end of the 90 day period following the Effective Date, if the average closing price during any ten (10) day period during the 90 day period is greater than \$0.10 per share (the "Adjusted Conversion Price"), then the Conversion Price will be adjusted to equal the Adjusted Conversion Price; provided, however, that the Adjusted Conversion Price will have a ceiling of \$0.20 per share, whereby if the 10 day average closing price is greater than \$0.20 per share during the 90 day period, then the Conversion Price will be adjusted to equal \$0.20 per share. There will only be one adjustment.

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

This Quarterly Report on Form 10-Q contains forward looking statements, including without limitation, statements related to our plans, strategies, objectives, expectations, intentions and adequacy of resources. Investors are cautioned that such forward-looking statements involve risks and uncertainties including without limitation the following: (i) our plans, strategies, objectives, expectations and intentions are subject to change at any time at our discretion; (ii) our plans and results of operations will be affected by our ability to manage growth; and (iii) other risks and uncertainties indicated from time to time in our filings with the Securities and Exchange Commission.

In some cases, you can identify forward-looking statements by terminology such as “may,” “will,” “should,” “could,” “expect,” “plans,” “intends,” “anticipates,” “believes,” “estimates,” “predicts,” “potential,” or “continue” or the negative of such comparable terminology. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance, or achievements. Moreover, neither we nor any other person assumes responsibility for the accuracy and completeness of such statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. We are under no duty to update any of the forward-looking statements after the date of this report.

Company Overview

Data Storage Corporation (“DSC” or “the Company”) is focused on our infrastructure, disaster recovery and email archival and compliance solutions. Our mission: Protecting our client’s data, ensuring business continuity, assisting in their compliance requirements and giving our clients better control over their digital information. We continue to stay on top of this dynamic industry with new solutions and services. The Company owns intellectual property with our proprietary email archival and data analysis software, Message Logic. We provide Recovery Clouds for Managed Service Providers, so that these companies can enter the industry of providing Disaster Recovery and Business Continuity solutions at a lower entry point. Our IBM solutions continue to grow with our joint venture, Secure Infrastructure and Services LLC, leading the way for Infrastructure as a Service on IBM’s Power i systems for the past two years.

DSC is a 16-year veteran in cloud storage and cloud computing providing data protection, disaster recovery, business continuity and compliance solutions that assist organizations in protecting their data, minimizing downtime and ensuring regulatory compliance. Serving the business continuity market, DSC’s clients save time and money, gain more control and better access to data and enable a high level of security for their data. Solutions include: Infrastructure-as-a-Service, data backup, recovery and restore, high availability data replication services; email archive and compliance for compliance officer alerts and e-discovery; continuous data protection; data de-duplication; and virtualized system recovery. DSC has forged relationships with leading organizations.

Headquartered in Melville, NY, with offices in New York City and Providence, Rhode Island, DSC offers its solutions and services to businesses within the healthcare, banking and finance, distribution services, manufacturing, construction, education and government industries.

DSC derives its revenues from the sale and subscription of services and solutions through several technical centers: New York Metro, Boston, Chicago and New Jersey.

DSC services clients from its staffed technical offices in New York and Rhode Island, which consist of modern offices and a technology suite adapted to meet the needs of a technology based business. DSC's mission is to provide a high level of service to organizations that need to ensure that their data is intact and available upon demand.

DSC varies its use of resource, technology and work processes to meet the changing opportunities and challenges presented by the market and the internal customer requirements.

RESULTS OF OPERATIONS

For the three months ended September 30, 2016 as compared to the three months ended September 30, 2015

Net Sales Net sales for the three months ended September 30, 2016 were \$922,919, a decrease of \$7,767, or 1%, compared to \$930,686 for the three months ended September 30, 2015. The decrease is attributable to a decrease in subscription revenue.

Cost of Sales. For the three months ended September 30, 2016, cost of sales were \$622,836, an increase of 9,920, or 1.6%, compared to \$612,916 for the three months ended September 30, 2015. The increase in cost of sales is the result of an increase in infrastructure services. DSC's gross margin is 32.5% for the three months ended September 30, 2016 as compared to 34.1% for the three months ended September 30, 2015.

Operating Expenses. For the three months ended September 30, 2016, operating expenses were \$413,211, a decrease of \$2,773, or 1%, as compared to \$415,984 for the three months ended September 30, 2015. The small increase is due to the Company's continued efforts to keep costs at a minimum.

Other Income (Expense). Interest expense (including amortization of debt discount) for the three months ended September 30, 2016 decreased \$1,662 to \$70,231 from \$71,893 for the three months ended September 30, 2016. Income on the investment in joint venture at equity, decreased \$33,987 to a loss of \$2,362 from a gain of \$31,625 in 2016, which was attributable to an increase in expenses in 2016.

Net Loss. Net loss for the three months ended September 30, 2016 was \$185,721 an increase of \$47,240, or 34%, as compared to a net loss of \$138,481 for the three months ended September 30, 2015.

For the nine months ended September 30, 2016 as compared to the nine months ended September 30, 2015

Net Sales Net sales for the nine months ended September 30, 2016 were \$2,912,152, a decrease of \$76,351, or 2.6%, compared to \$2,988,503 for the nine months ended September 30, 2015. The decrease is attributable to the decrease in subscription revenue.

Cost of Sales. For the nine months ended September 30, 2016, cost of sales were \$1,861,148 a decrease of \$4,232, or 0.02%, compared to \$1,865,380 for the nine months ended September 30, 2015. The decrease in cost of sales is the result lower infrastructure services for subscription revenue. DSC's gross margin is 36.1% for the nine months ended September 30, 2016 as compared to 37.6% for the nine months ended September 30, 2015.

Operating Expenses. For the nine months ended September 30, 2016, operating expenses were \$1,354,785, a decrease of \$92,071, or 6.4%, as compared to \$1,446,856 for the nine months ended September 30, 2015. The majority of the decrease in operating expenses for the nine months ended September 30, 2016 is a result of decrease in salaries and an increase in marketing. Salaries expense decreased \$167,134 to \$597,751 for the nine months ended September 30, 2016 as compared to \$764,885 for the nine months ended September 30, 2015. Marketing expense increased \$79,540 to \$106,865 for the nine months ended September 30, 2016 as compared to \$27,325 for the nine months ended September 30, 2015.

Other Income (expense). Interest income for the nine months ended September 30, 2016 decreased \$2 to \$0 from \$2 for the nine months ended September 30, 2015. Interest expense for the nine months ended September 30, 2016 decreased \$14,362 to \$204,466 from \$218,828 for the nine months ended September 30, 2015.

Net Loss. Net loss for the nine months ended September 30, 2016 was \$509,311 a decrease of \$6,276, or 1.2%, as compared to net loss of \$515,587 for the nine months ended September 30, 2015.

LIQUIDITY AND CAPITAL RESOURCES

The financial statements have been prepared using accounting principles generally accepted in the United States of America applicable for a going concern, which assumes that the Company will realize its assets and discharge its liabilities in the ordinary course of business. The Company has been funded by the CEO and largest shareholder combined with private placements of the Company's stock. The Company has been successful in raising money as needed. Further it is the intention of management to continue to raise money through stock issuances and to fund the Company on an as needed basis. During 2016, we intend to continue to work to increase our presence in the IBM marketplace utilizing our increased technical expertise, capacity for data storage and managed services and expand our presence in the email archiving marketplace through our acquisition of Message Logic.

To the extent we are successful in growing our business, identifying potential acquisition targets and negotiating the terms of such acquisition, and the purchase price includes a cash component, we plan to use our working capital and the proceeds of any financing to finance such acquisition costs. Our opinion concerning our liquidity is based on current information. If this information proves to be inaccurate, or if circumstances change, we may not be able to meet our liquidity needs.

During the nine months ended September 30, 2016 the Company's cash increased \$38,426 to \$105,471, from \$67,045 at December 31, 2015. Net cash of \$208,577 was provided by the Company's operating activities. No cash was used in investing activities. Net cash of (\$170,151) was used in the Company's financing activities, primarily due to capital lease payments.

The Company's working capital deficiency was \$3,672,690 at September 30, 2016, increasing \$495,613 or 15.6% from \$3,177,077 at December 31, 2015.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Interest Rate Sensitivity

Interest due on the Company's loans is based upon the applicable stated fixed contractual rate with the lender. Interest earned on DSC bank accounts is linked to the applicable base interest rate. For the nine months ended September 30, 2016 and 2015, DSC had interest expense, net of interest income, of \$204,466 and \$218,828, respectively. DSC believes that its results of operations are not materially affected by changes in interest rates.

DSC's exposure to market risk is confined to its cash and cash equivalents, all of which have maturities of less than three months and bear and pay interest in U.S. dollars. Since DSC invests in highly liquid, relatively low yield investments, we do not believe interest rate changes would have a material impact on us.

DSC does not hold any derivative instruments and does not engage in any hedging activities.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures.

As of the end of the period covered by this Report, under the supervision and with the participation of DSC's management, including its principal executive officer and principal financial officer, DSC conducted an evaluation of its disclosure controls and procedures, as such term is defined under Rule 13a-15(e) and Rule 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Based on this evaluation, DSC's principal executive officer and principal financial officers have concluded that DSC's disclosure controls and procedures are not effective to ensure that information required to be disclosed by DSC in the reports it files or submits under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the Securities and Exchange Commission's (the "SEC") rules based on the material weakness described below.

The material weaknesses identified during management's assessment were (i) a lack of sufficient internal accounting expertise to provide reasonable assurance that our financial statements and notes thereto are prepared in accordance with GAAP and (ii) a lack of segregation of duties to ensure adequate review of financial statement preparation. In

light of these material weaknesses, management has concluded that, as of September 30, 2016, DSC did not maintain effective internal control over financial reporting. As defined by the Public Company Accounting Oversight Board Auditing Standard No. 5, a material weakness is a deficiency or a combination of deficiencies, such that there is a reasonable possibility that a material misstatement of the annual or interim financial statements will not be prevented or detected. In order to ensure the effectiveness of DSC's disclosure controls in the future DSC intends on adding financial staff resources to our accounting and finance department.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation.

Changes in Internal Control Over Financial Reporting.

There have been no changes in our internal control over financial reporting that occurred during the last fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings.

We are currently not involved in any litigation that we believe could have a materially adverse effect on our financial condition or results of operations. There is no action, suit, proceeding, inquiry or investigation before or by any court, public board, government agency, self-regulatory organization or body pending or, to the knowledge of the executive officers of our company or any of our subsidiaries, threatened against or affecting DSC, its common stock, any of its subsidiaries or of DSC's or DSC's subsidiaries' officers or directors in their capacities as such, in which an adverse decision could have a material adverse effect.

Item 1A. Risk Factors.

As a smaller reporting company, we are not required to provide disclosure pursuant to this item

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

None.

Item 3. Defaults Upon Senior Securities.

There were no defaults upon senior securities during the period ended September 30, 2016.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information.

Not applicable.

20

Item 6. Exhibits

(a) Exhibits

(b) Exhibits

| # | Description |
|------|--|
| 3.1 | Articles of Incorporation (incorporated by reference to Exhibit 3.1 to the Registrant's Registration Statement on Form SB-2 filed on December 17, 2007 (the "SB-2")). |
| 3.2 | Certificate of Amendment to Articles of Incorporation (incorporated by reference to Exhibit 3.1 to Form 8-K filed on October 24, 2008). |
| 3.3 | Certificate of Amendment to Articles of Incorporation (incorporated by reference to Exhibit 3.1.1 on Form 8-K filed on January 6, 2009). |
| 3.4 | Bylaws (incorporated by reference to Exhibit 3.2 to the SB-2). |
| 3.5 | Amended Bylaws (incorporated by reference to Exhibit 3.2 to Form 8-K filed on October 24, 2008). |
| 4.1 | Share Exchange Agreement, dated October 20, 2008, by and among Euro Trend Inc., Data Storage Corporation and the shareholders of Data Storage Corporation named on the signature page thereto (incorporated by reference to Exhibit 10.1 to Form 8-K filed on October 24, 2008). |
| 4.2 | Share Exchange Agreement, dated October 20, 2008, by and among, Euro Trend Inc., Data Storage Corporation and the shareholders of Data Storage Corporation named on the signature page thereto (incorporated by reference to Exhibit 10.1 to Form 8-K/A filed on June 29, 2009). |
| 4.3 | Registration Rights Agreement, dated November 29, 2011, by and between Data Storage Corporation and Southridge Partners II, LP (incorporated herein by reference to Exhibit 10.2 to Form 8-K filed on December 2, 2011). |
| 4.4 | Equity Purchase Agreement, dated November 29, 2011, by and between Data Storage Corporation and Southridge Partners II, LP (incorporated herein by reference to Exhibit 10.2 to Form 8-K filed on December 2, 2011). |
| 4.5 | Convertible Promissory Note, dated February 28, 2013, by and between the Company and John F. Coghlan. (incorporated herein by reference to Exhibit 4.1 to Form 10-Q filed on May 20, 2013) |
| 4.6 | Warrant to Purchase Common Stock, dated February 28, 2013, by and between the Company and John F. Coghlan (incorporated herein by reference to Exhibit 4.2 to Form 10-Q filed on May 20, 2013) |
| 4.7 | Securities Purchase Agreement, dated February 28, 2013, by and between the Company and John F. Coghlan. (incorporated herein by reference to Exhibit 10.1 to Form 10-Q filed on May 20, 2013) |
| 4.8 | Securities Purchase Agreement between Charles M. Piluso and the Company dated as of August 9, 2013 (incorporated by reference to Exhibit 2.3 of Schedule 13D/A No. 1 filed by Charles M. Piluso on August 14, 2013 (File No. 005-84248)). |
| 4.9 | 10% Convertible Promissory Note due April 30, 2015 (incorporated by reference to Exhibit 2.4 of Schedule 13D/A No. 1 filed by Charles M. Piluso on August 14, 2013 (File No. 005-84248)). |
| 4.10 | Warrant to Purchase Common Stock dated as of August 9, 2013 (incorporated by reference to Exhibit 2.5 of Schedule 13D/A No. 1 filed by Charles M. Piluso on August 14, 2013 (File No. 005-84248)). |
| 10.1 | Asset Purchase Agreement dated November 10, 2008, by and between Novastor Corporation as Seller and Data Storage Corporation as Purchaser (incorporated by reference to Exhibit 10.1 to Form 8-K filed on November 12, 2008). |

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- 10.2 Joint Venture – Strategic Alliance Agreement, dated March 2, 2010, by and between Data Storage Corporation and United Telecomp, LLC (incorporated by reference to Exhibit 10.1 to Form 8-K filed on March 3, 2010).
Term Sheet for Acquisition by Data Storage Corporation of 80% of the Equity of e-ternity Business Continuity
- 10.3 Consultants, Inc., dated May 16, 2012 (incorporated by reference to Exhibit 99.1 to Form 8-K, filed on May 30, 2012).
Term Sheet for Acquisition by Data Storage Corporation of Message Logic, Inc., dated August 31, 2012 (incorporated by reference to Exhibit 99.1 to Form 8-K filed on September 4, 2012).
- 10.4 Asset Purchase Agreement, dated June 17, 2010, between SafeData, LLC and Data Storage Corporation (incorporated by reference to Exhibit 10.1 to Form 8-K filed on June 23, 2010).
- 10.5 Asset Purchase Agreement, dated October 31, 2012, by and between Data Storage Corporation and Message Logic, Inc. (incorporated by reference to Exhibit 2.1 to Form 8-K filed on January 30, 2013).
- 10.6 Stock Purchase Agreement, dated October 31, 2012, by and between Data Storage Corporation and Zojax Group, LLC (incorporated by reference to Exhibit 10. 1 to Form 8-K filed on November 7, 2012).
- 10.7 Form of Employment Agreement between Peter Briggs and Data Storage Corporation (incorporated by reference to Exhibit 10.2 to Form 8-K filed on June 23, 2010).
- 10.8 Data Storage Corporation 2010 Incentive Award Plan (incorporated by reference to Exhibit 10.1 on Form S-8/A filed on October 25, 2010).
- 10.9

- 10.10 Amended and Restated Data Storage Corporation 2010 Incentive Award Plan (incorporated by reference to Exhibit 10.1 to Form 8-K filed on April 26, 2012).
- 10.11 Stock Purchase Agreement, dated as of March 1, 2011, by and between Data Storage Corporation and John F. Coghlan (incorporated by reference to Exhibit 10.1 to Form 8-K filed on March 7, 2011).
- 10.12 Stock Purchase Agreement, dated September 7, 2012, by and between Data Storage Corporation and John F. Coghlan (incorporated by reference to Exhibit 2.1 to Form 8-K filed on September 13, 2012).
- 10.13 Stock Purchase Agreement, dated September 7, 2012, by and between Data Storage Corporation and Clifford Stein (incorporated by reference to Exhibit 2.2 to Form 8-K filed on September 13, 2012).
- 10.14 Stock Purchase Agreement, dated September 18, 2012, by and between Data Storage Corporation and Jan Burman (incorporated by reference to Exhibit 2.1 to Form 8-K filed on September 21, 2012).
- 10.15 Stock Purchase Agreement, dated September 18, 2012, by and between Data Storage Corporation and Charles M. Piluso (incorporated by reference to Exhibit 2.2 to Form 8-K filed on September 21, 2012).
- 10.16 Stock Purchase Agreement, dated September 18, 2012, by and between Data Storage Corporation and Piluso Family Associates (incorporated by reference to Exhibit 2.3 to Form 8-K filed on September 21, 2012).
- 10.17 Asset Purchase Agreement by and between ABC Services Inc., and Data Storage Corporation Inc. and Data Storage Corporation as of October 25, 2016 (incorporated by reference to Exhibit 10.1 to Form 8-K filed on October 31, 2016)
- 10.18 Asset Purchase Agreement by and between ABC Services II Inc., and Data Storage Corporation Inc. and Data Storage Corporation as of October 25, 2016 (incorporated by reference to Exhibit 10.2 to Form 8-K filed on October 31, 2016)
- 10.19 Conversion Agreement by and between Data Storage Corporation and Charles M. Piluso dated October 25, 2016 (incorporated by reference to Exhibit 10.3 to Form 8-K filed on October 31, 2016)
- 10.20 Conversion Agreement by and between Data Storage Corporation and John F. Coghlan dated October 25, 2016 (incorporated by reference to Exhibit 10.4 to Form 8-K filed on October 31, 2016)
- 10.21 Conversion Agreement by and between Data Storage Corporation and Clifford Stein dated October 25, 2016 (incorporated by reference to Exhibit 10.5 to Form 8-K filed on October 31, 2016)
- 14 Code of Ethics (incorporated by reference to Exhibit 14.1 to Form 10-K filed on March 31, 2009).
- 21 List of Subsidiaries of Data Storage Corporation (incorporated by reference to Exhibit 21 to the Registration Statement on Form S-1 filed on February 6, 2012).
- 31.1 Certification of President, Chief Executive Officer, Chief Financial Officer, Chairman of the Board of Directors Pursuant to Rule 13a-14(a) and Rule 15d-14(a) under the Exchange Act.
- 32.1 Certification of President, Chief Executive Officer, Chief Financial Officer, Chairman of the Board of Directors Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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.

DATA STORAGE CORPORATION

Date: November 14, 2016 By: */s/ Charles M. Piluso*

Charles M. Piluso

President, Chief Executive Officer

Chief Financial Officer

(Principal Executive, Financial and Accounting Officer)