

**Regency Affiliates, Inc. and Subsidiaries**  
**Condensed Consolidated Financial Statements**  
**March 31, 2020**

**Regency Affiliates, Inc. and Subsidiaries**  
**Index to the Condensed Consolidated Financial Statements**

	<u>Page</u>
Independent Auditor's Review Report .....	1
Financial Statements	
Condensed Consolidated Balance Sheets.....	2
Condensed Consolidated Statements of Income .....	3
Condensed Consolidated Statements of Changes in Equity.....	4
Condensed Consolidated Statements of Cash Flows .....	5
Notes to Condensed Consolidated Financial Statements .....	6-18



**ROSENBERG RICH BAKER BERMAN & COMPANY**

265 Davidson Avenue, Suite 210 • Somerset, NJ 08873-4120 • PHONE 908-231-1000 • FAX 908-231-6894  
111 Dunnell Road, Suite 100 • Maplewood, NJ 07040 • PHONE 973-763-6363 • FAX 973-769-4430

**INDEPENDENT AUDITOR’S REVIEW REPORT**

Board of Directors and Stockholders of  
Regency Affiliates, Inc. and Subsidiaries

We have reviewed the accompanying interim condensed consolidated financial statements of Regency Affiliates, Inc. and Subsidiaries, which comprise the interim condensed consolidated balance sheet as of March 31, 2020, and the related interim condensed consolidated statements of income, changes in equity, and cash flows for the three months ended March 31, 2020 and 2019, and the related notes to the interim condensed consolidated financial statements.

**Management’s Responsibility for the Financial Information**

Management is responsible for the preparation and fair presentation of the interim condensed consolidated financial information in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal controls sufficient to provide a reasonable basis for the preparation and fair presentation of interim condensed consolidated financial information in accordance with accounting principles generally accepted in the United States of America.

**Auditor’s Responsibility**

Our responsibility is to conduct our reviews in accordance with auditing standards generally accepted in the United States of America applicable to reviews of interim condensed consolidated financial information. A review of interim condensed consolidated financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with auditing standards generally accepted in the United States of America, the objective of which is the expression of an opinion regarding the consolidated financial information as a whole. Accordingly, we do not express such an opinion.

**Conclusion**

Based on our reviews, we are not aware of any material modifications that should be made to the accompanying interim condensed consolidated financial information for it to be in accordance with accounting principles generally accepted in the United States of America.

*Rosenberg Rich Baker Berman & Company*

Somerset, New Jersey  
May 15, 2020

**Regency Affiliates, Inc. and Subsidiaries**  
**Condensed Consolidated Balance Sheets**

	March 31, 2020	December 31, 2019
	(unaudited)	
<b>Assets</b>		
Current Assets:		
Cash and cash equivalents	\$ 860,007	\$ 619,136
Restricted cash	468,674	382,083
Short-term investments	5,807,997	6,317,768
Prepaid expenses	380,832	528,254
Prepaid insurance	123,086	90,600
Prepaid income taxes	2,033,000	2,225,329
Rent receivable	79,646	73,477
Total current assets	9,753,242	10,236,647
Real Estate		
Self-storage properties	35,127,512	35,127,512
Less accumulated depreciation	(3,077,196)	(2,882,734)
Property and equipment, net	15,977	17,333
Investment in partnerships/LLC	53,968,643	53,396,024
Prepaid insurance, net of current portion	173,350	196,000
Other assets	154,028	154,028
Total assets	\$ 96,115,556	\$ 96,244,810
<b>Liabilities and Shareholders' Equity</b>		
Current Liabilities:		
Accounts payable and accrued expenses	\$ 413,713	\$ 367,244
Mortgage note payable, net	343,861	-
Deferred revenue	176,985	168,938
Deferred rent	81,081	81,081
Income tax payable	30,000	81,424
Dividends payable	411,299	411,299
Tenant security deposits	7,261	7,261
Total current liabilities	1,464,200	1,117,247
Non-current Liabilities:		
Mortgage note payable, net	24,829,335	25,170,040
Total liabilities	26,293,535	26,287,287
Commitments and contingencies		
Shareholders' Equity		
Serial preferred stock, par value \$0.10; 2,000,000 shares authorized; no shares issued and outstanding	-	-
Common stock, par value \$0.01; 8,000,000 shares authorized; 4,815,058 and 4,815,058 shares issued and outstanding, as of March 31, 2020 and December 31, 2019, respectively	48,151	48,151
Additional paid-in capital	14,014,556	14,014,556
Retained earnings	55,655,878	55,802,608
Total shareholders' equity	69,718,585	69,865,315
Noncontrolling interest	103,436	92,208
Total equity	69,822,021	69,957,523
Total liabilities and shareholders' equity	\$ 96,115,556	\$ 96,244,810

See independent auditor's review report and notes to the condensed consolidated financial statements.

**Regency Affiliates, Inc. and Subsidiaries**  
**Condensed Consolidated Statements of Income**  
(unaudited)

	For the Three Months Ended March 31,	
	2020	2019
Revenue		
Rental	\$ 906,783	\$ 872,891
Insurance, late fees and other income	73,225	81,189
Retail	4,872	-
Total revenue	984,880	954,080
Operating expenses:		
Self-storage cost of operations	382,368	437,581
Self-storage depreciation expense	194,462	194,459
General and administrative expenses	421,596	511,118
Total operating expenses	998,426	1,143,158
Loss from operations	(13,546)	(189,078)
Other income (expense):		
Management agreement income	38,559	51,412
Income from equity investment in partnerships/LLC	572,619	797,754
License agreement income	28,328	29,113
Interest income	20,995	82,086
Interest expense	(315,941)	(312,475)
Amortization of debt discount	(3,156)	(3,156)
Total other income (expense)	341,404	644,734
Net income before income taxes	327,858	455,656
Income tax expense	141,411	58,039
Net income	186,447	397,617
Net income attributable to noncontrolling interest	17,791	1,282
Net income allocated to shareholders	\$ 168,656	\$ 396,335

See independent auditor's review report and notes to the condensed consolidated financial statements.

**Regency Affiliates, Inc. and Subsidiaries**  
**Condensed Consolidated Statements of Changes in Equity**  
**For the Three Months Ended March 31, 2020 and 2019**  
**(unaudited)**

	Preferred Stock		Common Stock		Additional Paid-In Capital	Retained Earnings	Shareholders' Equity	Noncontrolling Interest	Total Equity
	Shares	Amount	Shares	Amount					
Balance at January 1, 2019	-	\$ -	4,815,058	\$ 48,151	\$ 14,039,310	\$ 55,367,342	\$ 69,454,803	\$ 36,923	\$ 69,491,726
Stock options compensation expense	-	-	-	-	4,515	-	4,515	-	4,515
Dividends declared	-	-	-	-	-	(308,164)	(308,164)	-	(308,164)
Net income	-	-	-	-	-	396,335	396,335	1,282	397,617
Balance at March 31, 2019	-	\$ -	4,815,058	\$ 48,151	\$ 14,043,825	\$ 55,455,513	\$ 69,547,489	\$ 38,205	\$ 69,585,694
Balance at January 1, 2020	-	\$ -	4,815,058	\$ 48,151	\$ 14,014,556	\$ 55,802,608	\$ 69,865,315	\$ 92,208	\$ 69,957,523
Dividend paid to noncontrolling interest	-	-	-	-	-	-	-	(6,563)	(6,563)
Dividends declared	-	-	-	-	-	(315,386)	(315,386)	-	(315,386)
Net income	-	-	-	-	-	168,656	168,656	17,791	186,447
Balance at March 31, 2020	-	\$ -	4,815,058	\$ 48,151	\$ 14,014,556	\$ 55,655,878	\$ 69,718,585	\$ 103,436	\$ 69,822,021

See independent auditor's review report and notes to the condensed consolidated financial statements.

**Regency Affiliates, Inc. and Subsidiaries**  
**Condensed Consolidated Statements of Cash Flows**  
**(unaudited)**

	For the Three Months Ended March 31,	
	2020	2019
<b>Cash Flows From Operating Activities</b>		
Net Income	\$ 186,447	\$ 397,617
Adjustments to reconcile net income to net cash from operating activities:		
Non-cash expenses:		
Depreciation and amortization	195,818	195,756
Income from equity investment in partnerships/LLCs	(572,619)	(1,769,801)
Impairment of equity investment in partnerships/LLCs	-	972,047
Stock based compensation, net of forfeiture	-	4,515
Amortization of debt discount	3,156	3,156
Changes in operating assets and liabilities		
Prepaid expenses	147,422	29,633
Prepaid insurance	(9,836)	(2,464)
Prepaid income taxes	192,329	56,039
Rent receivable	(6,169)	(12,198)
Other assets	-	-
Accounts payable and accrued expense	46,469	74,662
Deferred revenue	8,047	17,488
Income tax payable	(51,424)	-
Tenant security deposits	-	(75)
Total adjustments	(46,807)	(431,242)
Net cash provided by (used in) operating activities	139,640	(33,625)
<b>Cash Flows From Investing Activities</b>		
Distributions of earnings from partnerships	-	1,500,000
Purchase of equipment	-	(1,133)
Purchases of short-term investments	(2,510,229)	-
Proceeds from maturities short-term investments	3,020,000	-
Net cash provided by investing activities	509,771	1,498,867
<b>Cash Flows From Financing Activities</b>		
Dividends paid to common shareholders	(315,386)	(308,314)
Dividends paid to noncontrolling shareholder	(6,563)	-
Net cash used in financing activities	(321,949)	(308,314)
Net increase or decrease in cash and cash equivalent:	327,462	1,156,928
Cash and cash equivalents and restricted cash - beginning	1,001,219	4,438,725
Cash and cash equivalents and restricted cash - ending	\$ 1,328,681	\$ 5,595,653
<b>Supplemental Disclosures of Cash Flow Information</b>		
Cash paid during the period for:		
Interest	\$ 315,941	\$ 312,469
Income taxes	\$ -	\$ -
Non-cash investing and financing activities:		
Common stock dividends declared	\$ 315,386	\$ 308,164

See independent auditor's review report and notes to the condensed consolidated financial statements.

**Regency Affiliates, Inc. and Subsidiaries**  
**Notes to Condensed Consolidated Financial Statements**

**Note 1. Summary of Significant Accounting Policies**

*Basis of Presentation*

The accompanying financial statements are presented on an accrual basis in accordance with U.S. generally accepted accounting principles (“U.S. GAAP”) as defined in the Financial Accounting Standards Board Accounting Standards Codification (the “Codification”) for interim financial information. Accordingly, they do not include all of the information and notes required by accounting principles generally accepted in the United States of America. However, in the opinion of the management of the Company, all adjustments necessary for a fair presentation of the financial position and operating results have been included in these statements. These unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company’s Annual Report for the fiscal year ended December 31, 2019, as posted with OTC Markets on March 30, 2020. Operating results for the three months ended March 31, 2020 are not necessarily indicative of the results that may be expected for any subsequent quarters or for the year ending December 31, 2020.

In November 2016, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2016-18, “Statement of Cash Flows (Topic 230): Restricted Cash,” (“ASU 2016-18”). ASU 2016-18 requires restricted cash be included with cash and cash equivalents when reconciling the total beginning and ending amounts on the statement of cash flows. The standard also requires companies who report cash and restricted cash separately on the balance sheet to reconcile those amounts to the statement of cash flows. The Company adopted ASU 2016-18 in the first quarter of Fiscal 2019. The other provisions of ASU 2016-18 did not have a material effect on the Company.

*Nature of Operations*

Regency Affiliates, Inc. (“Regency” or “the Company”) invests in assets that generate attractive, predictable and sustainable returns on capital. The Company’s objective is to generate long term value for its shareholders. Management seeks sound investment opportunities to meet its business characteristics and valuation criteria.

The Company holds a limited partnership interest in Security Land and Development Company Limited Partnership (“Security Land”), which owns and operates 34.3 acres of land and rental property of approximately 717,000 square feet in Woodlawn, Maryland, which is occupied by the United States Social Security Administration’s Office of Disability and International Operations. In November 2000, the Company acquired a 5% limited partnership interest in 1500 Woodlawn Limited Partnership, the general partner of Security Land. See Note 2, “Investment in Security Land and Development Company Limited Partnership.”

In addition, Regency Power Corporation (“Regency Power”, 100% owned subsidiary of the Company) owned a 50% interest in MESC Capital, LLC, a Delaware limited liability company (“MESC Capital”). MESC Capital owns a 100% interest in Mobile Energy Services Company, LLC, an Alabama limited liability company (“Mobile Energy”), which owns an on-site energy facility that supplies steam and electricity to a Kimberly-Clark tissue mill in Mobile, Alabama. See Note 3.

In April 2016, Regency formed a new, wholly owned subsidiary, RSS Investments LLC (“RSS”). RSS acquired a majority ownership (80%) of SSCP Harrisburg Holdings, LLC, a Delaware limited liability company (“Harrisburg Holdings”). Harrisburg Holdings is the sole member of SSCP Harrisburg Intermediate Holdings, LLC, a Delaware limited liability company (“Intermediate Holdings”). Simultaneously with RSS’s investment in Harrisburg Holdings, Harrisburg Intermediate Holdings acquired a portfolio of five self-storage facilities in Harrisburg, Pennsylvania. Through our controlling interest of SSCP Harrisburg Holdings, LLC, we are focused on the ownership, operation, and acquisition of self-storage properties located within the Harrisburg, Pennsylvania area.



**Regency Affiliates, Inc. and Subsidiaries**  
**Notes to Condensed Consolidated Financial Statements**

**Note 1. Summary of Significant Accounting Policies (continued)**

*Principles of Consolidation*

These condensed consolidated financial statements include the accounts of the Company, and its wholly owned subsidiaries, Regency Power and RSS. All significant intercompany balances and transactions have been eliminated in consolidation.

*Noncontrolling Interest*

The Company consolidates its 80% equity interest in Harrisburg Holdings and reports the remaining 20% interest by the third party, SSCP Management LLC, as a noncontrolling interest on the condensed balance sheet. At March 31, 2020 and December 31, 2019, the noncontrolling equity interest was \$103,436 and \$92,208 respectively. The net income or net loss of Harrisburg Holdings is allocated based on the ownership percentages on the condensed statements of income. For the three months ended March 31, 2020 and 2019, Harrisburg Holdings had net income of \$88,955 and \$6,409, respectively, resulting in net income attributable to the noncontrolling interest for the three months ended March 31, 2020 and 2019 of \$17,791 and \$1,282 respectively.

*Cash and Cash Equivalents*

Cash and cash equivalents represent cash and short-term highly liquid investments with original maturities of three months or less. The Company places its cash and cash equivalents with high credit quality financial institutions that may exceed federally insured amounts at times. Uninsured cash balances were \$54,948 and \$0 as of March 31, 2020 and December 31, 2019, respectively. As of March 31, 2020 and December 31, 2019, the Company's cash equivalents were \$0 and \$0, respectively.

*Short-Term Investments*

Short-term investments consist of treasury bills with original maturity dates greater than three months at the date of purchase. Short-term investments are valued at cost, which approximates fair value. As of March 31, 2020 and December 31, 2019, the Company's short-term investments were \$5,807,997 and \$6,317,768, respectively.

*Investments in Partnerships / LLC*

The Company uses the equity method of accounting for its investments in partnerships in equity securities in which it has more than a 20% interest but does not have a controlling interest and is not the primary beneficiary. Investments owned over 50% with a controlling interest are consolidated within these financial statements.

*Restricted Cash*

The self-storage properties hold escrow funds in money market trust accounts for real estate taxes, insurance, and replacement reserves disbursements to be paid when due, pursuant to the terms of the bank financing agreement.

*Self-Storage Properties*

Self-storage properties are carried at historical cost less accumulated depreciation and any impairment losses. Major replacements and betterments, which improve or extend the life of an asset, are capitalized. Expenditures for ordinary repairs and maintenance are expensed as incurred and are included in self-storage cost of operation. Estimated depreciable lives of self-storage properties are determined by considering the age and other indicators about the condition of the assets at their respective dates of acquisition, resulting in an estimated useful life for assets within each category. All self-storage property assets are depreciated using the straight-line method. Buildings and improvements are depreciated over estimated useful lives of 39 years.

**Regency Affiliates, Inc. and Subsidiaries**  
**Notes to Condensed Consolidated Financial Statements**

**Note. 1. Summary of Significant Accounting Policies (continued)**

*Self-Storage Properties (continued)*

When a self-storage property is acquired in a business combination, the purchase price of the acquired self-storage property is allocated to land, buildings and improvements, furniture and equipment, customer in-place leases, assumed real estate leasehold interests, other assets acquired and liabilities assumed, based on the estimated fair value of each component. When a portfolio of self-storage properties is acquired, the purchase price is allocated to the individual self-storage properties based on the fair value determined using an income approach with appropriate risk-adjusted capitalization rates, which take into account the relative size, age and location of the individual self-storage properties.

These items consist of the following at:

	March 31, 2020	December 31, 2019
Land	\$ 4,870,000	\$ 4,870,000
Building and improvements	30,222,363	30,222,363
Furniture and equipment	35,149	35,149
	35,127,512	35,127,512
Less: Accumulated Depreciation	(3,077,196)	(2,882,734)
Self-Storage Properties, net	\$ 32,050,316	\$ 32,244,778

Depreciation expense on these properties was \$194,462 and \$194,459 for the three months ended March 31, 2020 and 2019, respectively.

*Property and Equipment*

Property and equipment is carried at cost less accumulated depreciation. Depreciation is provided over the estimated useful lives of the assets using the straight-line method as follows: machinery and equipment - 7 years. Repairs and maintenance costs are expensed as incurred.

These items consist of the following at:

	March 31, 2020	December 31, 2019
Machinery and equipment	\$ 46,368	\$ 46,368
Less: Accumulated depreciation	(30,391)	(29,035)
Property and equipment, net	\$ 15,977	\$ 17,333

Depreciation expense was \$1,356 and \$1,297 for the three months ended March 31, 2020 and 2019, respectively.

*Income Taxes*

The Company utilizes FASB ASC 740-10, "Income Taxes", which requires an asset and liability approach to financial accounting and reporting for income taxes. The difference between the financial statement and tax basis of assets and liabilities is determined annually. Deferred income tax assets and liabilities are computed for those temporary differences that have future tax consequences using the current enacted tax laws and rates that apply to the periods in which they are expected to affect taxable income. In some situations, FASB ASC 740-10 permits the recognition of expected benefits of utilizing net operating loss and tax credit carryforwards. Valuation allowances are established based upon management's estimate, if necessary. Income tax expense (benefit) is the current tax payable or refund for the period plus or minus the net change in the deferred tax assets and liabilities.

**Regency Affiliates, Inc. and Subsidiaries**  
**Notes to Condensed Consolidated Financial Statements**

**Note 1. Summary of Significant Accounting Policies (continued)**

*Use of Estimates*

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities as of the date of the financial statements, and also affect the amounts of revenues and expenses reported for each period. Actual results could differ from those which result from using such estimates. Management utilizes various other estimates, including but not limited to, assessing the collectability of rents receivable, determining the estimated lives of long-lived assets, determining the potential impairment of intangibles, the fair value of stock options, the recognition of revenue, and other legal claims and contingencies. The results of any changes in accounting estimates are reflected in the financial statements in the period in which the changes become evident. Estimates and assumptions are reviewed periodically, and the effects of revisions are reflected in the period that they are determined to be necessary.

*Revenue and Expense Recognition*

Effective January 1, 2019, the Company adopted Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 606, Revenue from Contracts with Customers ("ASC 606"). The guidance includes a five-step framework that requires an entity to: (i) identify the contract(s) with a customer, (ii) identify the performance obligations in the contract, (iii) determine the transaction price, (iv) allocate the transaction price to the performance obligations in the contract, and (v) recognize revenue when the entity satisfies a performance obligation.

Management has determined that all of its leases are operating leases. Substantially all leases may be terminated on a month-to-month basis and rental income is recognized ratably over the lease term using the straight-line method. Rents received in advance are deferred and recognized on a straight-line basis over the related lease term associated with the prepayment. Promotional discounts and other incentives are recognized as a reduction to rental income over the applicable lease term. Other property related revenue consists of ancillary revenues such as tenant insurance related access fees and commissions and sales of storage supplies with are recognized in the period earned.

*Revenue and Expense Recognition, continued*

For insurance income, the Company acts as an agent and recognized revenue for only its commission on the arrangement. The Company has a contract with the insurance carrier for acting as an agent, with a set commission amount. The performance obligation is met, and revenue is earned, when the Company sells a policy to a customer, which is evidenced by a signed contract. There is no variable consideration for this revenue stream.

Property tax expense is based on actual amounts billed or estimates of anticipated bills or assessments that have not yet been received from the taxing authorities. Cost of operations, general and administrative expense, interest expense, and advertising expenditures are expensed as incurred.

*Advertising Expenses*

The Company expenses advertising costs when incurred. Advertising and marketing costs totaled \$1,422 and \$1,741 for the three months ended March 31, 2020 and 2019, respectively.

**Regency Affiliates, Inc. and Subsidiaries**  
**Notes to Condensed Consolidated Financial Statements**

**Note 1. Summary of Significant Accounting Policies (continued)**

*Stock-Based Compensation*

The Company follows ASC 718, Compensation - Stock Compensation, which addresses the accounting for stock-based payment transactions, requiring such transactions to be accounted for using the fair value method. Awards of shares for property or services are recorded at the more readily measurable of the fair value of the stock and the fair value of the service. The Company uses the Black-Scholes option-pricing model to determine the grant date fair value of stock-based awards under ASC 718. The fair value is charged to earnings depending on the terms and conditions of the award, and the nature of the relationship of the recipient of the award to the Company. The Company records the grant date fair value in line with the period over which it was earned. For employees and consultants, this is typically considered to be the vesting period of the award. The Company estimates the expected forfeitures and updates the valuation accordingly.

*Fair Value Measurements*

The carrying amounts of cash, restricted cash, prepaid expenses, accounts payable, accrued liabilities, deferred revenue, and other liabilities approximate their fair value due to the short-term nature of these instruments. Cash equivalents, consisting of U.S. Treasury Bills, are adjusted to fair value at each balance sheet date based on quoted prices which are considered level 1 inputs.

ASC 820 "Fair Value Measurements and Disclosures" provides the framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements).

Fair value is defined as an exit price, representing the amount that would be received upon the sale of an asset or payment to transfer a liability in an orderly transaction between market participants. Fair value is a market-based measurement that is determined based on assumptions that market participants would use in pricing an asset or liability. A three-tier fair value hierarchy is used to prioritize the inputs in measuring fair value as follows:

- Level 1 Quoted prices in active markets for identical assets or liabilities.
- Level 2 Quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, or other inputs that are observable, either directly or indirectly.
- Level 3 Significant unobservable inputs that cannot be corroborated by market data.

**Regency Affiliates, Inc. and Subsidiaries**  
**Notes to Condensed Consolidated Financial Statements**

**Note 1. Summary of Significant Accounting Policies (continued)**

*Fair Value Measurements*

The fair value of the Company's financial instruments are as follows:

	Quoted Prices in Active Markets for Identical Assets or Liabilities (Level 1)	Quoted Prices for Similar Assets or Liabilities in Active Markets (Level 2)	Significant Unobservable Inputs (Level 3)	Total
U.S. Treasury Bills as of March 31, 2020	\$ <u>5,807,997</u>	\$ <u>-</u>	\$ <u>-</u>	\$ <u>5,807,997</u>
U.S. Treasury Bills as of December 31, 2019	\$ <u>6,317,768</u>	\$ <u>-</u>	\$ <u>-</u>	\$ <u>6,317,768</u>

*Limitations*

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial statements. These estimates are subjective in nature, involve uncertainties and matters of significant judgment, and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

*Subsequent Events Evaluation*

The Company has evaluated subsequent events through May 15, 2020, which is the date these financial statements were available to be issued.

**Note 2. Investment in Security Land and Development Company Limited Partnership**

The Company owns a limited partnership interest in Security Land, which owns and operates an office complex. The Company has limited voting rights and is entitled to certain allocations of the profit and loss and operating cash flow distributions of Security Land.

For the three months ended March 31, 2020 and 2019, the Company's income from its equity investment in Security Land was \$549,497 and \$477,392 respectively.

The Company also owns a 5% limited partnership interest in 1500 Woodlawn Limited Partnership, the general partner of Security Land. The Company recognized income of \$23,122 and \$20,101 for the three months ended March 31, 2020 and 2019, respectively, from this investment.

On December 6, 2018, the Company entered into a second amended and restated limited partnership agreement (the "Amended Partnership Agreement") with Woodlawn and other limited partners. Among other things, the Amended Partnership Agreement allowed Security Land to enter into a new agreement with the United States General Services Administration and refinance its debt, as described below. As part of the Amended Partnership Agreement, the income allocated to the Company was reduced from 95% to 48.969%.

**Regency Affiliates, Inc. and Subsidiaries**  
**Notes to Condensed Consolidated Financial Statements**

**Note 2. Investment in Security Land and Development Company Limited Partnership (continued)**

On December 6, 2018, Security Land entered into an agreement (“Management Agreement”) with Woodlawn and the Company. Pursuant to the Management Agreement, there is an asset management fee payable to the Company at a rate of 1.3% of monthly rental income in the applicable period, payable monthly through the date of sale of the property. For the three months ended March 31, 2020 and 2019, the Company recognized \$38,559 and \$51,412 from the management fee agreement.

On December 17, 2018, Security Land signed a new ten-year lease with the United States General Services Administration, which became effective as of November 1, 2018 and expires on October 31, 2028. The initial annual rent will be approximately \$11,750,000 per annum. Based on the new lease, Security Land arranged for new debt totaling approximately \$30,000,000. The new debt will be used to pay off existing debt and provide for capital improvements of the facility. In connection with the new lease and debt, on December 19, 2018, Security Land paid to the Company a distribution of \$1,214,963.

Summarized Condensed Balance Sheet information for Security Land is as follows:

	March 31, 2020	December 31, 2019
Balance Sheet Data		
Cash and cash equivalents	\$ 2,131,619	\$ 1,949,022
Restricted cash	18,370,871	18,160,617
Real estate, net	18,810,107	19,144,768
Deferred charges, net	1,752,153	439,525
Receivables and other assets	1,301,907	1,000,076
Leasing cost, net of accumulated amortization	-	1,054,696
Total Assets	\$ 42,366,657	\$ 41,748,704
Accounts payable and accrued expenses	\$ 319,732	\$ 387,391
Project note payable	23,885,006	24,318,473
Accrued interest payable	44,585	46,929
Total Liabilities	\$ 24,249,322	\$ 25,752,793
Partners' capital:		
Total Partners' Capital	18,117,334	16,995,911
Total Liabilities and Partner's Capital	\$ 42,366,657	\$ 41,748,704

Summarized Condensed Statements of Income information for Security Land is as follows:

	For the Three Months Ended March 31,	
	2020	2019
Revenues	\$ 3,111,390	\$ 3,088,300
Expenses	1,989,967	2,113,412
Net income	\$ 1,121,423	\$ 974,888

**Regency Affiliates, Inc. and Subsidiaries**  
**Notes to Condensed Consolidated Financial Statements**

**Note 3. Investment in MESC Capital LLC**

The Company owns a 50% membership interest in MESC Capital, which, through its subsidiary, owns an on-site energy facility that supplies steam and electricity to a Kimberly-Clark tissue mill in Mobile, Alabama pursuant to an Amended and Restated Tissue Mill and Energy Services and Site Coordination Agreement that expired on April 30, 2019.

The Company accounts for the Investment in Partnerships using the equity method, whereby the carrying value of these investments are increased or decreased by the Company's allocable share of book income or loss. The Company recognized income of \$0 and \$1,272,309 for the three months ended March 31, 2020 and 2019, respectively, from this investment.

For the three months ended March 31, 2020 and 2019, the Company recorded impairment of \$0 and \$972,048, respectively. The impairment charge was included in income from equity investment in partnerships/LLC on the Company's condensed consolidated statement of income. On July 23, 2019, the Company received its final distributions from MESC Capital of \$2,050,261 and as such, the investment in MESC Capital is \$0 as of March 31, 2020.

Summarized Condensed Income Statement information for MESC Capital LLC is as follows:

	For the Three Months Ended March 31,	
	2020	2019
Revenues	\$ -	\$ 3,800,365
Expenses	-	1,255,748
Net income	\$ -	\$ 2,544,617

**Note 4. Stock Based Compensation**

*2003 Incentive Stock Plan*

Effective as of March 17, 2003, the Company's Board of Directors and Stockholders approved and adopted the 2003 Stock Incentive Plan (the "2003 Plan"). The 2003 Plan allows the Administrator (as defined in the 2003 Plan), currently the Compensation Committee, to determine the issuance of incentive stock options, non-qualified stock options and restricted stock to eligible employees and outside directors and consultants of the Company. The Company has reserved 500,000 shares of common stock for issuance under the 2003 Plan. The exercise price of any option granted under the 2003 Plan is determined by the Administrator, and no option or award exercise date can exceed ten years from the grant date. On August 13, 2008, the Company's Board of Directors approved an amendment to the 2003 Plan that increased the total number of authorized shares available from 500,000 to 750,000. All other terms of the Plan remain in full force and effect.

Total stock-based compensation expense, net of forfeitures, recorded within General and Administrative Expenses in the Condensed Statements of Income was \$0 and \$4,515 during the three months ended March 31, 2020 and 2019, respectively. These amounts recognize the vested portion of the requisite grant terms. Unamortized stock-based compensation for these option awards as of March 31, 2020 was \$0.

As of March 31, 2020, 85,000 shares remain available for issuance under the 2003 Plan.

**Regency Affiliates, Inc. and Subsidiaries**  
**Notes to Condensed Consolidated Financial Statements**

**Note 4. Stock Based Compensation (continued)**

The following is a summary of the status of the Company's options for the three months ended March 31, 2020:

	Exercise Price Range	Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Intrinsic Value
Outstanding at January 1, 2019	\$ 6.50-9.50	85,000	\$ 7.74	5.35	
Issued	-	-			
Exercised	-	-	-		
Forfeited	-	-	-		
Outstanding at March 31, 2019	<u>\$ 6.50-9.50</u>	<u>85,000</u>	<u>\$ 7.74</u>	<u>5.11</u>	<u>\$ -</u>
Exercisable at March 31, 2019	<u>\$ 6.50</u>	<u>64,000</u>	<u>\$ 7.16</u>	<u>4.44</u>	<u>\$ -</u>
Outstanding at January 1, 2020	\$ 6.50	50,000	\$ 6.50	2.94	\$ -
Issued	-	-			
Exercised	-	-	-		
Forfeited	-	-	-		
Outstanding at March 31, 2020	<u>\$ 6.50</u>	<u>50,000</u>	<u>\$ 6.50</u>	<u>2.69</u>	<u>\$ -</u>
Exercisable at March 31, 2020	<u>\$ 6.50</u>	<u>50,000</u>	<u>\$ 6.50</u>	<u>2.69</u>	<u>\$ -</u>

**Note 5. Income Taxes**

As referred to in Note 1, the Company accounts for income taxes under FASB ASC 740-10, "Income Taxes". The deferred taxes are the result of temporary differences between financial reporting and tax reporting for depreciation, earnings from the Company's partnership investment in Security Land and the recognition of income tax carry-forward items.

The Company files consolidated income tax returns with its wholly owned subsidiaries. As of December 31, 2014, for regular federal and state income tax purposes, the Company has utilized all of its net operating loss carryforwards (NOLs). The Company believes it is no longer subject to income tax examinations for years prior to 2014 by the respective taxing authorities.

The Company and the general partner of Security Land are in disagreement as to the manner in which taxable income of Security Land is to be allocated pursuant to the partnership agreement and applicable law, for years 2004 through 2017, the Company has reported taxable income and loss from Security Land in a manner it believes is proper, but which was different than the manner reported by Security Land. An investigation or other action by the applicable tax authorities to resolve this difference could have an adverse impact on the Company's operations and financial results.

The Company's 2014 and 2015 tax returns are under examination by the Internal Revenue Service ("IRS").

To safeguard itself from any possible negative impact, in February 2016, the Company purchased an insurance policy and binder to insure against the negative tax consequences should any arise from the disagreement with Security Land regarding reported taxable income allocations. The Company paid \$633,900 for the policy and binder which provide coverage of up to \$10 million over the next seven years in the event the IRS or a state taxing authority were to investigate and reject the Company's tax positions taken. The policy is subject to certain limitations, exclusions and retentions.



**Regency Affiliates, Inc. and Subsidiaries**  
**Notes to Condensed Consolidated Financial Statements**

**Note 5. Income Taxes (continued)**

For the three months ended March 31, 2020 and 2019, the Company has recorded tax expense of \$141,411 and \$58,039, respectively, including expense of \$24,000 and \$34,000, respectively, for state income taxes. The Company's applicable statutory tax rates are 21% and 7.5% for federal and state tax purposes, respectively, for the three months ended March 31, 2020. The reconciliation of the Company's income tax expense for the three months ended March 31, 2020 and 2019 is as follows:

	For the Three Months Ended March 31,	
	2020	2019
Income tax at federal statutory rate	\$ 69,000	\$ 94,000
State taxes, net of federal benefit	24,000	34,000
Permanent differences	-	-
Other	48,411	(69,961)
Total income tax expense	\$ 141,411	\$ 58,039

**Note 6. Related Party Transactions**

In May 2016, the Company entered into a consulting agreement with a non-independent member of its Board of Directors, to provide consulting, financial analyses, and due diligence services for any new potential investment available to the Company, and ongoing financial monitoring of existing investments. Terms of the agreement include an initial fee of \$7,500 and a fee of \$7,200 each month thereafter. In addition, the agreement called for a 25,000 non-qualified common stock option award, exercisable at \$9.50 per share with a term of 10 years and vesting of 5,000 options per year over a 5-year period. The Company may terminate the agreement at any time for cause; the consultant may terminate the agreement at will. The fair value of the options granted was \$83,400. On May 31, 2019, the consulting agreement was terminated. During the three months ended March 31, 2020 and 2019, the Company recorded stock-based compensation expense, net of forfeitures, of \$0 and \$3,225, respectively, related to this stock option. In addition, under the terms of the agreement, the Company paid \$0 and \$21,600 to the consultant during the three months ended March 31, 2020 and 2019, respectively.

**Note 7. Contingencies, Risks, and Uncertainties**

The Company is subject to numerous contingencies, risks and uncertainties including, but not limited to, the following that could have a severe impact on the Company:

A default in the Lease or sudden catastrophe to the Security West Building from uninsured acts of God or war could have a materially adverse impact upon the Company's investment in Security Land and Development Company Limited Partnership and, therefore, its financial position and results of operations.

Royalty, an affiliate of the Company's management, beneficially owns approximately 49% of the Company's common stock. As a result, Royalty has the ability to control the outcome of all matters requiring shareholder approval, including the election and removal of directors and any merger, consolidation or sale of all or substantially all of the Company's assets.

There are many public and private companies that are also searching for operating businesses and other business opportunities as potential acquisition or merger candidates. The Company will be in direct competition with these other companies in its search for business opportunities. Many of these entities have significantly greater financial and personnel resources than the Company.

**Regency Affiliates, Inc. and Subsidiaries**  
**Notes to Condensed Consolidated Financial Statements**

**Note 7. Contingencies, Risks, and Uncertainties (continued)**

The Company and the general partner of Security Land are in disagreement as to the manner in which taxable income of Security Land is to be allocated pursuant to the partnership agreement and applicable law, for years 2004 through 2017, the Company reported taxable income (loss) from Security Land in a manner the Company believes is proper, but which was different than the manner reported by Security Land (See Note 5). This may result in an investigation or other action by the applicable tax authorities and any action taken by tax authorities to resolve this difference could have an adverse impact on the Company's operations and financial results. In February 2016, the Company obtained an insurance policy to protect against such losses, however, it may not be sufficient under all circumstances to cover all potential losses to the Company in the event of any such adverse determinations.

In September 2016, the Company received an Internal Revenue Service letter indicating its 2014 Federal Form 1120 was selected for examination. In September 2017, the Company received an Internal Revenue Service letter indicating its 2015 Federal Form 1120 was selected for examination. Management has submitted the initial documentation requested.

The Company's operations may be affected by the recent and ongoing outbreak of the coronavirus disease 2019 (COVID-19) which in March 2020, was declared a pandemic by the World Health Organization. Governmental authorities in the States where we operate have taken and may continue to take measures in order to combat the spread of disease including forced closures of business establishments. The full impact of the COVID-19 outbreak is unknown, resulting in a high degree of uncertainty for potentially extended periods of time. At this time, neither the duration nor scope of the disruption can be predicted, therefore, the negative impact on our financial position and operating results cannot be reasonably estimated. The results of this pandemic may have material adverse impact on the Company's financial position, operations and cash flows. Possible areas that may be affected include, but are not limited to, disruption to the Company's customers and revenue, labor workforce, unavailability of products and supplies used in operations, and the decline in value of assets held by the Company which includes our investments in partnerships. The Company is closely monitoring the impact of the coronavirus (COVID-19) pandemic on all aspects of its business.

**Note 8. Lease Commitments**

In January 2016, Regency paid a \$201,329 security deposit and entered into a new, seven-year office lease agreement, for a 4,081 square foot space for its New York City location. Base rental payments under this agreement are \$74 per square foot per year, with a 1.75% fixed annual escalation. In addition, the Company is responsible to pay the tenant's share of real estate tax increases above the 2016/2017 base year and electricity usage. A rent concession has been granted to waive the first three months' rent. On the third anniversary of rent commencement, and provided the Company is not in default of any rental obligations, the landlord agrees to reduce the security deposit to six months' base rent, or approximately \$151,000. The lease also contains an early termination clause which is effective after five years, with proper notice and payment of an early termination fee. The office relocated in May 2016, the first month of the lease term. Rent expense for the three months ended March 31, 2020 and 2019 was \$79,889 and \$78,179, respectively.

**Regency Affiliates, Inc. and Subsidiaries**  
**Notes to Condensed Consolidated Financial Statements**

**Note 8. Lease Commitments (continued)**

As of March 31, 2020, future minimum payments under this operating lease are as follows:

For the Years Ended December 31,	
2020 (remainder of the year)	\$ 241,379
2021	327,471
2022	333,202
2023	111,709
2024	-
Total	\$ <u>1,013,761</u>

**Note 9. License Agreement**

In May 2016, a new License Agreement commenced with an unrelated entity which provides the use of leased space within the Company's New York City office, for \$8,833 per month, plus monthly office service fees, through June 2018. Annual one-year renewal periods are available, with license and service fee increases of 2.25% and 2.5%, respectively, until the expiration of the office lease.

License fee income and related service fees for the three months ended March 31, 2020 and 2019 was \$28,328 and \$29,113, respectively.

**Note 10. Simplified Employee Pension- Individual Retirement Account (SEP-IRA)**

The Company adopted a SEP-IRA Plan in 2004. During the three months ended March 31, 2020 and 2019, the Company expensed contributions of \$81,216 and \$96,107, respectively, to the SEP-IRA Plan. The SEP-IRA Plan covers all employees who receive compensation from the Company during the year. Employer contributions are discretionary and determined annually. In addition, the SEP-IRA Plan allows participants to make elective deferral contributions through payroll deductions.

**Note 11. Dividends**

The Board of Directors has a dividend policy whereby the Board expects to declare a total annual dividend to common shareholders of \$0.262 per share, to be paid in equal, quarterly installments of \$0.0655 per share, provided that the determination to pay any cash dividends for any quarterly period will be made at the applicable time by the Board, in the Board's sole discretion, in compliance with the requirements of applicable law, and with consideration of the Company's future earnings and financial condition and other factors as may be deemed appropriate for consideration by the Board. The dividend policy will remain in effect until the Board determines, in its sole discretion, that it is in the best interests of the Company and its common shareholders to terminate the dividend policy.

**Regency Affiliates, Inc. and Subsidiaries**  
**Notes to Condensed Consolidated Financial Statements**

**Note 12. Mortgage Note Payable**

On April 18, 2016, SSCP, through its five self-storage properties, obtained a \$25,250,000 bank note to fund the acquisition. The note is a non-recourse debt financing with a ten year term, 4.95% fixed interest rate, and has a maturity date of May 6, 2026. The note is guaranteed by the owners of SSCP and is secured by all assets of SSCP. The only amount due during the first four years of the note is interest. The Company paid \$126,250 in fees for underwriting of the note. These were recorded as a debt discount and are amortized over the life of the note. Amortization expense of debt discount was \$3,156 and \$3,156 for the three months ended March 31, 2020 and 2019, respectively.

Under the terms of this agreement, the Company is required to meet and maintain certain financial covenants. The covenant at March 31, 2020 is:

Minimum Debt Service Coverage Ratio	1.45 to 1.00
Actual Debt Service Coverage Ratio	1.96 to 1.00

As of March 31, 2020, future minimum principal payments due under the note are as follows:

For the Years Ended December 31:	Amount
2020 (remainder of the year)	248,531
2021	388,486
2022	408,158
2023	428,826
2024	450,542
Thereafter	23,325,457
Total	<u>\$ 25,250,000</u>