

UNITED COMMUNITY BANKS INC

Form S-4

May 17, 2017

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As filed with the Securities and Exchange Commission on May 17, 2017

File No. 333-

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM S-4

REGISTRATION STATEMENT

UNDER

THE SECURITIES ACT OF 1933

UNITED COMMUNITY BANKS, INC.

(Exact name of issuer as specified in its charter)

Georgia

6022

58-1807304

(State or other jurisdiction of
incorporation or organization)

(Primary Standard Industrial
Classification Code Number)

(I.R.S. Employer
Identification Number)

United Community Banks, Inc.

125 Highway 515 East

Blairsville, Georgia 30512

(706) 745-2151

Jimmy C. Tallent

125 Highway 515 East

Blairsville, Georgia 30512

(706) 745-2151

(Address, including zip code, and telephone number,
including area code, of registrant's principal executive
offices)

(Name, address, including zip code, and telephone
number,
including area code, of agent for service)

Copies to:

James W. Stevens

Troutman Sanders LLP

600 Peachtree Street, Suite 5200

Atlanta, Georgia 30308

(404) 885-3721

Neil E. Grayson

Nelson Mullins Riley & Scarborough, LLP

104 S. Main Street, Suite 900

Greenville, South Carolina 29601

(864) 250-2235

Approximate date of commencement of proposed sale of the securities to the public: The exchange of the Registrant's shares for shares of common stock of HCSB Financial Corporation will take place upon consummation of the merger of HCSB Financial Corporation into the Registrant.

If the securities being registered on this form are being offered in connection with the formation of a holding company and there is compliance with General Instruction G, check the following box.

If this form is filed to register additional securities of an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. _____

If this form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. _____

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

Large accelerated filer

Accelerated filer

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Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company
Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 7(a)(2)(B) of the Securities Act.

If applicable, place an X in the box to designate the appropriate rule provision relied upon in conducting this transaction:

Exchange Act Rule 13e-4(i) (Cross-Border Issuer Tender Offer)

Exchange Act Rule 14d-1(d) (Cross-Border Third-Party Tender Offer)

CALCULATION OF REGISTRATION FEE

Title of Each Class of Securities to be Registered	Amount to be Registered	Proposed Maximum Offering Price per Share	Proposed Maximum Aggregate Offering Price	Amount of Registration Fee
Common Stock, par value \$1.00 per share	2,478,820(1)	Not Applicable	\$ 64,449,313(2)	\$ 7,470.00(3)

(1)

The number of shares of the Registrant's common stock being registered hereunder is based upon the anticipated maximum number of such shares required to consummate the proposed merger of HCSB Financial Corporation, a South Carolina corporation, into the Registrant. The Registrant will remove from registration by means of a post-effective amendment any shares being registered that are not issued in connection with such merger.

(2)

Estimated solely for the purpose of calculating the registration fee required by Section 6(b) of the Securities Act of 1933 pursuant to Rules 457(c) and 457(f)(1) of the Securities Act. The proposed maximum aggregate offering price of the registrant's common stock was calculated based upon the market value of shares of common stock, par value \$0.01 per share, of HCSB Financial Corporation ("HCSB common stock") in accordance with Rule 457(c) under the Securities Act as the product of (i) \$0.13, the average of the high and low prices of HCSB common stock as reported on OTCQB on May 16, 2017, and (ii) 495,763,940, the estimated maximum possible number of shares of HCSB common stock which may be canceled and exchanged in the merger, including shares of HCSB common stock issuable pursuant to equity awards.

(3)

Computed pursuant to Rules 457(f)(1) and 457(c) of the Securities Act, based on a rate of \$115.90 per \$1,000,000 of the proposed maximum aggregate offering price.

The Registrant hereby amends this registration statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this registration statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until this registration statement shall become effective on such date as the Commission acting pursuant to said Section 8(a) may determine.

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The information in this document is not complete and may be changed. We may not sell the securities offered by this document until the registration statement filed with the Securities and Exchange Commission is effective. This document is not an offer to sell these securities, and we are not soliciting an offer to buy these securities, in any state where the offer or sale is not permitted.

SUBJECT TO COMPLETION, DATED MAY 17, 2017

PROXY STATEMENT/PROSPECTUS

MERGER PROPOSED — YOUR VOTE IS VERY IMPORTANT

These materials are a proxy statement of HCSB Financial Corporation (“HCSB”) and a prospectus of United Community Banks, Inc. (“United”). They are furnished to you in connection with the notice of the special meeting of shareholders of HCSB to be held on [•], 2017. At the special meeting of HCSB shareholders, you will be asked to vote on the merger of HCSB with and into United described in more detail herein and holders of HCSB voting common stock will be asked to approve, on a non-binding advisory basis, the compensation that certain executive officers of HCSB will receive in connection with the merger pursuant to existing agreements or arrangements with HCSB.

As of [•], 2017, the record date for the HCSB special meeting of shareholders, there were [•] shares of voting common stock and [•] shares of non-voting common stock issued and outstanding and entitled to vote at that meeting. Holders of HCSB voting common stock will vote on all three proposals. Holders of HCSB non-voting common stock will vote only on the merger proposal. Approval of the merger agreement requires the affirmative vote of (i) two-thirds of the issued and outstanding shares of HCSB voting common stock and (ii) a majority of the issued and outstanding shares of HCSB non-voting common stock. Approval of the merger-related compensation proposal requires that the number of votes cast at the special meeting, in person or by proxy, in favor of the proposal exceeds the number of votes cast against the proposal. The proposal to adjourn or postpone the special meeting, if necessary or appropriate, including to solicit additional proxies to approve the merger agreement, will be approved if the number of votes cast at the special meeting, in person or by proxy, in favor of the proposal exceeds the number of votes cast against the proposal.

In connection with the merger, if approved and consummated, holders of HCSB voting common stock and non-voting common stock (which we refer to as the “HCSB common stock”) will be entitled to receive, in exchange for each share of HCSB common stock, consideration equal to 0.0050 shares of United common stock.

As a result, a maximum of 2,478,820 shares of United common stock will be issued to HCSB shareholders if the merger is approved and consummated. This document is a United prospectus with respect to the offering and issuance of such 2,478,820 shares of United common stock.

Based on United’s closing price of \$26.70 per share on April 19, 2017, the last trading day before the execution of the merger agreement, the merger consideration represented approximately \$0.1335 for each share of HCSB common stock and approximately \$66,184,486 million on an aggregate basis. Based on United’s closing price of \$[•] per share on [•], 2017, the last practicable trading day before the date of the enclosed document, the merger consideration represented approximately \$[•] for each share of HCSB common stock and approximately \$[•] million on an aggregate basis. We encourage you to obtain current market quotations for United common stock and HCSB common stock before you vote. United’s common stock is traded on the NASDAQ Global Select Market under the symbol “UCBI,” and HCSB’s voting common stock is traded on the OTCQB tier of the OTC Markets Group Inc. under the symbol “HCFB.” The accompanying materials contain information regarding the proposed merger and the companies participating in the merger, and the Agreement and Plan of Merger pursuant to which the merger will be consummated if approved. We encourage you to read the entire document carefully, including the “Risk Factors” section beginning on page 19, for a discussion of the risks related to the proposed merger.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or passed upon the adequacy or accuracy of these materials. Any representation to the contrary is a criminal offense. Shares of common stock of United are not savings accounts, deposits or other obligations of any

bank and are not insured or guaranteed by the Federal Deposit Insurance Corporation or any other governmental agency.

The date of these materials is [•], 2017, and they are expected to be first mailed to shareholders on or about [•], 2017.

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WHERE YOU CAN FIND MORE INFORMATION

Both United and HCSB are subject to the information requirements of the Securities Exchange Act of 1934, which means that they are both required to file certain reports, proxy statements, and other business and financial information with the Securities and Exchange Commission (“SEC”). You may read and copy any materials that either United or HCSB files with the SEC at the Public Reference Room of the SEC at 100 F. Street N.E., Washington, D.C. 20549. You may also obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains a website at <http://www.sec.gov> where you can access reports, proxy, information and registration statements, and other information regarding registrants that file electronically with the SEC. Such filings are also available free of charge at United’s website at <http://www.ucbi.com> under the “Investor Relations” heading or from HCSB’s website at <http://www.hcsbaccess.com> under the “Investor Information” link under the “About Us” heading. Except as specifically incorporated by reference into this document, information on those websites or filed with the SEC is not part of this document.

United has filed a registration statement on Form S-4 of which this document forms a part. As permitted by SEC rules, this document does not contain all of the information included in the registration statement or in the exhibits or schedules to the registration statement. You may read and copy the registration statement, including any amendments, schedules and exhibits, at the addresses set forth below. Statements contained in this document as to the contents of any contract or other documents referred to in this document are not necessarily complete. In each case, you should refer to the copy of the applicable contract or other document filed as an exhibit to the registration statement. This document incorporates by reference documents that United and HCSB have previously filed, and that they may file through the date of the special meeting of HCSB shareholders, with the SEC. They contain important information about the companies and their financial condition. For further information, please see the section entitled “Incorporation of Certain Documents by Reference.” These documents are available without charge to you upon written or oral request to the applicable company’s principal executive offices. The respective addresses and telephone numbers of such principal executive offices are listed below.

United Community Banks, Inc.	HCSB Financial Corporation
125 Highway 515 East	3640 Ralph Ellis Boulevard
Blairsville, Georgia 30512	Loris, South Carolina 29569
Attention: Investor Relations	Attention: Jennifer W. Harris
(706) 781-2265	(843) 716-4272

To obtain timely delivery of these documents, you must request the information no later than [•], 2017 in order to receive them before HCSB’s special meeting of shareholders.

United’s common stock is traded on the NASDAQ Global Select Market under the symbol “UCBI,” and HCSB’s voting common stock is traded on the OTCQB tier of the OTC Markets Group Inc. under the symbol “HCFB.”

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HCSB FINANCIAL CORPORATION

3640 Ralph Ellis Boulevard

Loris, South Carolina 29569

Notice Of Special Meeting Of Shareholders

To Be Held On [•], 2017

A special meeting of shareholders of HCSB Financial Corporation will be held on [•], 2017, at [•] a.m., at [•] for the following purposes:

1.

To consider and vote on the Agreement and Plan of Merger, under which HCSB Financial Corporation (“HCSB”) will merge with and into United Community Banks, Inc. (“United”), as more particularly described in the accompanying materials;

2.

To cast a non-binding advisory vote to approve the compensation that certain executive officers of HCSB will receive under existing agreements or arrangements with HCSB in connection with the merger;

3.

To consider and vote upon a proposal to approve the adjournment or postponement of the special meeting, if necessary or appropriate, including to solicit additional proxies to approve the merger agreement; and

4.

To transact such other business as may properly come before the special meeting or any adjournments of the special meeting.

If HCSB shareholders approve the merger agreement, HCSB will be merged with and into United. HCSB shareholders will receive 0.0050 shares of United common stock in exchange for each of their shares of HCSB common stock in the merger.

Holders of HCSB voting common stock will vote on all three proposals. Holders of HCSB non-voting common stock will vote only on the merger proposal. Approval of the merger agreement requires the affirmative vote of (i) two-thirds of the issued and outstanding shares of HCSB voting common stock and (ii) a majority of the issued and outstanding shares of HCSB non-voting common stock. Approval of the merger-related compensation proposal requires that the number of votes cast at the special meeting, in person or by proxy, in favor of the proposal exceeds the number of votes cast against the proposal. Approval of the adjournment proposal requires that the number of votes cast at the special meeting, in person or by proxy, in favor of the proposal exceeds the number of votes cast against the proposal. Only shareholders of record of HCSB common stock at the close of business on [•], 2017 will be entitled to vote at the special meeting or any adjournments thereof. HCSB’s Board of Directors has adopted a resolution approving the merger and the merger agreement and unanimously recommends that you vote “FOR” the proposal to approve the merger agreement, “FOR” the merger-related compensation proposal, and “FOR” the adjournment proposal. Business and financial information about HCSB is available without charge to you upon written or oral request made to HCSB Financial Corporation, 3640 Ralph Ellis Boulevard, Loris, South Carolina 29569, Attention: Jennifer W. Harris, telephone number (843) 716-4272. To obtain delivery of such business and financial information before the special meeting, your request must be received no later than [•], 2017.

YOUR VOTE IS VERY IMPORTANT. You can vote your shares over the internet or by telephone. If you requested or received a paper proxy card or voting instruction form by mail, you may also vote by signing, dating and returning your proxy card or voting instruction form. If you are the record holder of the shares, you may change your vote by: (1) if you voted over the internet or by telephone, voting again over the internet or by telephone by the applicable deadline described herein; (2) if you previously completed and returned a proxy card, submitting a new proxy card with a later date and returning it to HCSB prior to the vote at the special meeting; (3) submitting timely written notice

of revocation to HCSB's Corporate Secretary, D. Singleton Bailey, at HCSB Financial Corporation, 3640 Ralph Ellis Boulevard, Loris, South Carolina 29569, at any time prior to the vote at the special meeting; or (4) attending the special meeting in person and voting your shares at the special meeting. If your shares are held in street name, you

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may change your vote by submitting new voting instructions to your brokerage firm, bank or other similar entity or, if you have obtained a legal proxy from your brokerage firm, bank, or other similar entity giving you the right to vote your shares, you may change your vote by attending the special meeting and voting in person.

By Order of the Board of Directors,

[•], 2017

Loris, South Carolina

Jan H. Hollar, Chief Executive Officer

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QUESTIONS AND ANSWERS ABOUT THE MERGER

Q:

What am I being asked to approve?

A:

HCSB shareholders are being asked to (1) approve the Agreement and Plan of Merger between HCSB and United, pursuant to which HCSB will be merged with and into United, (2) approve, on a non-binding advisory basis, the compensation that certain executive officers of HCSB will receive in connection with the merger pursuant to existing agreements or arrangements with HCSB, and (3) approve a proposal to adjourn or postpone the special meeting, if necessary or appropriate, including to solicit additional proxies to approve the merger agreement. Holders of HCSB voting common stock will vote on all three proposals. Holders of HCSB non-voting common stock will vote only on the merger proposal. Approval of the merger agreement requires the affirmative vote of (i) two-thirds of the issued and outstanding shares of HCSB voting common stock and (ii) a majority of the issued and outstanding shares of HCSB non-voting common stock. Approval of the merger-related compensation proposal requires that the number of votes cast at the special meeting, in person or by proxy, in favor of the proposal exceeds the number of votes cast against the proposal. Approval of the adjournment proposal requires that the number of votes cast at the special meeting, in person or by proxy, in favor of the proposal exceeds the number of votes cast against the proposal. The HCSB Board of Directors has unanimously approved and adopted the merger and the merger agreement and recommends voting “FOR” approval of the merger agreement, “FOR” approval of the merger-related compensation proposal, and “FOR” approval of the adjournment proposal.

Q:

When is the merger expected to be completed?

A:

We plan to complete the merger during the third quarter of 2017.

Q:

What will I receive in the merger?

A:

Holders of HCSB voting common stock and non-voting common stock (which we refer to as the “HCSB common stock”) will receive 0.0050 shares (which we refer to as the “exchange ratio”) of United common stock for each share of HCSB common stock. United will not issue fractional shares in the merger. Instead, you will receive a cash payment, without interest, for the value of any fraction of a share of United common stock that you would otherwise be entitled to receive in an amount equal to such fractional part of a share of United common stock multiplied by the purchase price per share of HCSB common stock as determined by multiplying (i) the exchange ratio by (ii) the closing price for United common stock on the NASDAQ Global Select Market trading day immediately preceding the effective time of the merger.

To review what you will receive in the merger in greater detail, see “Proposal No. 1 — The Merger — The Merger Consideration” beginning on page 35.

Q:

What should I do now?

A:

After you have carefully read this document, please vote by proxy over the internet, by telephone or through the mail. If you hold shares of HCSB common stock in more than one account, you must vote all shares over the internet, by telephone or through the mail. If you vote over the internet or by telephone, you do not need to return any documents through the mail.

If you vote using one of the methods described below, you will be designating Michael S. Addy and Jan H. Hollar as your proxies to vote your shares as you instruct. If you vote over the internet or by telephone or by signing and returning your proxy card without giving specific voting instructions, these individuals will vote your shares by following the recommendations of the HCSB Board of Directors. If any other business properly comes before the special meeting, these individuals will vote on those matters in a manner they consider appropriate.

Registered Holder: You do not have to attend the special meeting to vote. The HCSB Board of Directors is soliciting proxies so that you can vote before the special meeting. Even if you currently plan to attend the special meeting, we recommend that you vote by proxy before the special meeting so

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that your vote will be counted if you later decide not to attend. However, if you attend the special meeting and vote your shares by ballot, your vote at the special meeting will revoke any vote you submitted previously by proxy. If you are the record holder of your shares, there are three ways you can vote by proxy:

-
- By Internet: You may vote over the internet by going to [•] and following the instructions when prompted;
-
- By Telephone: You may vote by telephone by calling toll free [•]; or
-
- By Mail: You may vote by completing, signing, dating and returning the enclosed proxy card.

Street Holder: If your shares are held in street name, you may vote your shares before the special meeting by mail, by completing, signing, and returning the voting instruction form you received from your brokerage firm, bank or other similar entity. You should check your voting instruction form to see if any alternative method, such as internet or telephone voting, is available to you.

Q:

What constitutes a quorum for the special meeting?

A:

The presence at the special meeting, in person or by proxy, of holders of a majority of the outstanding shares of HCSB voting common stock and HCSB non-voting common stock entitled to vote at the special meeting will constitute a quorum for the transaction of business. Abstentions and broker non-votes, if any, will be included in determining the number of shares present at the meeting for the purpose of determining the presence of a quorum.

Q:

What vote is required to approve each proposal?

A:

Approval of the merger agreement requires the affirmative vote of (i) two-thirds of the issued and outstanding shares of HCSB voting common stock and (ii) a majority of the issued and outstanding shares of HCSB non-voting common stock. If you fail to vote, mark "ABSTAIN" on your proxy, or fail to instruct your brokerage firm, bank, or other similar entity giving you the right to vote your shares with respect to the merger proposal, it will have the same effect as a vote "AGAINST" the proposal. Approval of the merger-related compensation proposal requires that the number of votes cast at the special meeting, in person or by proxy, in favor of the proposal exceeds the number of votes cast against the proposal. Approval of the adjournment proposal requires that the number of votes cast at the special meeting, in person or by proxy, in favor of the proposal exceeds the number of votes cast against the proposal.

Q:

What impact will my vote have on the amounts that certain executive officers of HCSB may receive in connection with the merger?

A:

Certain of HCSB's executive officers are entitled, pursuant to the terms of their existing employment agreements with HCSB, to receive certain payments in connection with the merger. If the merger is completed, HCSB is contractually obligated to make these payments to these executives under certain circumstances. Accordingly, even if the HCSB shareholders vote not to approve these payments, the compensation will be payable, subject to the terms and conditions of the agreements. HCSB is seeking your approval of these payments on a non-binding advisory basis in order to comply with Section 951 of the Dodd-Frank Act and Rule 14a-21(c) under the Securities Exchange Act of 1934.

Q:

Why is my vote important?

A:

If you do not return your proxy, it will be more difficult for HCSB to obtain the necessary quorum to hold the special meeting. In addition, your failure to submit a proxy or vote in person, or failure to instruct your brokerage firm, bank, or other similar entity how to vote, or abstention will have the same effect as a vote “AGAINST” approval of the merger agreement, as applicable. The merger agreement must be approved by the affirmative vote of (i) two-thirds of the issued and outstanding shares of HCSB voting common stock and (ii) a majority of the issued and outstanding shares of HCSB non-voting common stock. The HCSB Board of Directors unanimously recommends that you vote “FOR” the merger proposal.

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Q:

What information should I consider?

A:

We encourage you to read carefully this entire document and the documents incorporated by reference herein. Among other disclosures, you should review the factors considered by each company's Board of Directors discussed in "Proposal No. 1 — The Merger — Background of the Merger" beginning on page 21 and "Proposal No. 1 — The Merger — Reasons for the Merger and Recommendation of the HCSB Board of Directors" beginning on page 24.

Q:

Will my ownership percentage and voting interest be reduced after the merger?

A:

Yes. HCSB shareholders currently have the right to vote in the election of the HCSB Board of Directors and on other matters affecting HCSB. Upon the completion of the merger, each HCSB shareholder receiving shares of United common stock in accordance with the merger agreement will be a shareholder of United with a percentage ownership of United that is smaller than such shareholder's current percentage ownership of HCSB. It is currently expected that the former shareholders of HCSB as a group will receive shares in the merger constituting approximately [•]% of the outstanding shares of United's common stock immediately after the merger. Because of this, HCSB shareholders will have less influence on the management and policies of United than they now have on the management and policies of HCSB.

Q:

What are the tax consequences of the merger to me?

A:

The merger will qualify as a "reorganization" within the meaning of Section 368(a) of the Internal Revenue Code of 1986, as amended (the "Code"). Accordingly, HCSB's shareholders generally will not recognize gain or loss for federal income tax purposes on the exchange of shares of HCSB common stock for United common stock, except with respect to cash received in lieu of fractional shares of United common stock or upon the exercise of dissenters' rights. The tax consequences to HCSB shareholders are described in greater detail in "Proposal No. 1 — The Merger — Material Federal Income Tax Consequences and Opinion of Tax Counsel" beginning on page 50. Your tax consequences will depend on your personal situation. You should consult your tax adviser for a full understanding of the tax consequences of the merger to you.

Q:

Are HCSB shareholders entitled to dissenters' rights?

A:

Yes. HCSB shareholders are entitled to dissenters' rights under Chapter 13 of the South Carolina Business Corporation Act of 1988 (the "SCBCA"), provided they satisfy the special criteria and conditions set forth in Chapter 13 of the SCBCA. More information regarding these dissenters' rights is provided in this document, and the provisions of the SCBCA that grant dissenters' rights and govern such procedures are attached as Appendix B to this document. You should read these provisions carefully and in their entirety. See "Dissenters' Rights" beginning on page 49.

Q:

Should I send in my stock certificates now?

A:

No. After the merger is completed, you will receive written instructions from United or its exchange agent, Continental Stock Transfer & Trust Company, for exchanging your HCSB common stock certificates for United common stock.

Q:

Who should I call with questions?

A:

You should call Jennifer W. Harris, HCSB Financial Corporation, at (843) 716-4272.

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SUMMARY

This summary highlights material information from these materials regarding the proposed merger. For a more complete description of the terms of the proposed merger, you should carefully read this entire document and the documents incorporated by reference into this document. The Agreement and Plan of Merger, which is the legal document that governs the proposed merger, is in Appendix A to these materials. In addition, the sections entitled “Where You Can Find More Information”, in the forepart of this document, and “Incorporation of Certain Documents By Reference”, on page 59, contain references to additional sources of information about United and HCSB.

•

The Companies (see pages 54 and 57)

United Community Banks, Inc.

125 Highway 515 East

Blairsville, Georgia 30512

(706) 745-2151

United is the third largest bank holding company headquartered in Georgia. At March 31, 2017, United had total consolidated assets of \$10.7 billion, total loans of \$6.96 billion, total deposits of \$8.75 billion and shareholders' equity of \$1.10 billion. United conducts substantially all of its operations through its wholly-owned Georgia bank subsidiary, United Community Bank (the “Bank”), which as of March 31, 2017, operated at 134 offices in Georgia, North Carolina, South Carolina and Tennessee.

United's community banks offer a full range of retail and corporate banking services, including checking, savings and time deposit accounts, secured and unsecured loans, wire transfers, brokerage services and other financial services, and are led by local bank presidents and management with significant experience in, and ties to, their communities.

Each of the local bank presidents has authority, alone or with other local officers, to make most credit decisions.

United also operates United Community Mortgage Services, a full-service retail mortgage lending operation approved as a seller/servicer for Fannie Mae and the Federal Home Mortgage Corporation, as a division of the Bank. The Bank owns an insurance agency, United Community Insurance Services, Inc., known as United Community Advisory Services. United also owns a captive insurance subsidiary, United Community Risk Management Services, Inc., that provides risk management services for United's subsidiaries. Another subsidiary of the Bank, United Community Payment Systems, LLC, provides payment processing services for the Bank's commercial and small business customers. Additionally, United provides retail brokerage services through a third party broker/dealer.

United was incorporated in 1987, as a Georgia corporation. Its principal executive offices are located at 125 Highway 515 East, Blairsville, Georgia 30512, and its telephone number is (706) 781-2265. Its website is <http://www.ucbi.com>.

Information on United's website is not incorporated into this document by reference and is not a part hereof.

For a complete description of United's business, financial condition, results of operations and other important information, please refer to United's filings with the SEC that are incorporated by reference in this document, including its Annual Report on Form 10-K for the year ended December 31, 2016 and its quarterly report on Form 10-Q for the quarter ended March 31, 2017. For instructions on how to find copies of these documents, see “Where You Can Find More Information.”

HCSB Financial Corporation

3640 Ralph Ellis Boulevard

Loris, South Carolina 29569

(843) 716-4272

HCSB was incorporated on June 10, 1999 to become a holding company for Horry County State Bank. Horry County State Bank is a state chartered bank which commenced operations on January 4, 1988. Horry County State Bank's primary market includes Horry and Georgetown Counties in South Carolina and Columbus and Brunswick Counties in North Carolina. From Horry County State Bank's eight branch locations, Horry County State Bank offers a full range of deposit services, including checking

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accounts, savings accounts, certificates of deposit, money market accounts, and IRAs. In addition, Horry County State Bank offers a variety of loan products designed for consumers, businesses and farmers. As of March 31, 2017, HCSB had total consolidated assets of \$384.0 million, net loans of \$225.3 million, deposits of \$322.3 million and shareholders' equity of \$36.1 million.

For a complete description of HCSB's business, financial condition, results of operations and other important information, please refer to HCSB's filings with the SEC that are incorporated by reference in this document, including its Annual Report on Form 10-K, as amended on Form 10-K/A, for the year ended December 31, 2016 and its quarterly report on Form 10-Q for the quarter ended March 31, 2017. For instructions on how to find copies of these documents, see "Where You Can Find More Information."

•
The Merger Agreement (see page 35)

If HCSB shareholders approve the merger agreement, subject to receipt of the required regulatory approvals and satisfaction of the other closing conditions, HCSB will be merged with and into United. Holders of HCSB common stock will receive 0.0050 shares of United common stock for each share of HCSB common stock.

You will also receive a cash payment, without interest, for the value of any fraction of a share of United common stock that you would otherwise be entitled to receive in an amount equal to such fractional part of a share of United common stock multiplied by the purchase price per share of HCSB common stock as determined by multiplying (i) the exchange ratio by (ii) the closing price for United common stock on the NASDAQ Global Select Market trading day immediately preceding the effective time of the merger.

Following the merger, HCSB's wholly-owned South Carolina bank subsidiary, Horry County State Bank, will be merged with and into the Bank, United's wholly-owned Georgia bank subsidiary, and the Bank will be the surviving bank.

HCSB's Reasons for the Merger and Recommendation of the HCSB Board of Directors (see page 24)

The HCSB Board of Directors supports the merger and believes that it is in the best interests of HCSB and its shareholders. The HCSB Board of Directors believes that the merger will allow HCSB to better serve its customers and markets and that the merger will permit HCSB shareholders to have an equity interest in a resulting financial institution with greater financial resources, more significant economies of scale, and a larger shareholder base, which will increase the liquidity of the HCSB shareholders' common stock. The HCSB Board of Directors believes that the terms of the merger are fair to and in the best interest of HCSB and its shareholders.

Accounting Treatment (see page 49)

The merger will be accounted for as a purchase of a business for financial reporting and accounting purposes under generally accepted accounting principles in the United States.

Conditions, Termination, and Effective Date (see pages 35 and 36)

The merger will not occur unless certain conditions are met, and United or HCSB can terminate the merger agreement if specified events occur or fail to occur. Following the merger, HCSB's South Carolina bank subsidiary, Horry County State Bank, will be merged into United's Georgia bank subsidiary, the Bank.

The merger and the bank merger must be approved by the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Department of Banking and Finance of the State of Georgia and the South Carolina State Board of Financial Institutions. As of the date of this document, we have not yet received any of the required regulatory approvals.

The closing of the merger will not occur until after the merger is approved by the foregoing regulators and by the HCSB shareholders, the other conditions to closing have been satisfied and the certificate of merger is filed as required under Georgia law and South Carolina law.

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Federal Income Tax Consequences (see page 50)

The merger will qualify as a “reorganization” within the meaning of Section 368(a) of the Code. Accordingly, HCSB’s shareholders generally will not recognize gain or loss for federal income tax purposes on the exchange of shares of HCSB common stock for United common stock, except with respect to cash received in lieu of fractional shares of United common stock or upon the exercise of dissenters’ rights. The tax consequences to HCSB shareholders are described in greater detail in “Proposal No. 1 — The Merger — Material Federal Income Tax Consequences and Opinion of Tax Counsel” beginning on page 50. Tax matters are complicated, and the tax consequences of the merger may vary among HCSB shareholders. We urge each HCSB shareholder to contact his or her own tax advisor to fully understand the tax implications of the merger.

Opinion of HCSB’s Financial Advisor (see page 27)

Hovde Group, LLC (“Hovde”) has rendered an opinion to HCSB that based on and subject to the procedures, matters, and limitations described in its opinion and other matters it considered relevant, as of the date of its opinion, the merger consideration is fair from a financial point of view to the shareholders of HCSB. A summary of Hovde’s opinion begins on page 27 and the full opinion is attached as Appendix C to these materials.

Markets for Common Stock

United’s common stock trades on the NASDAQ Global Select Market under the ticker symbol “UCBI.” HCSB’s voting common stock trades on the OTCQB tier of the OTC Markets Group Inc. under the ticker symbol “HCFB.” The following table sets forth, for the periods indicated, the high, low and closing sales prices per share of United’s common stock and HCSB’s voting common stock as quoted on NASDAQ and the OTCQB, respectively.

	United Common Stock			HCSB Voting Common Stock		
	High	Low	Close	High	Low	Close
2017						
Second Quarter (through [•], 2017)	\$ [•]	\$ [•]	\$ [•]	\$ [•]	\$ [•]	\$ [•]
First Quarter	30.47	25.29	27.69	0.59	0.15	0.38
2016						
Fourth Quarter	30.22	20.26	29.62	0.19	0.11	0.15
Third Quarter	21.13	17.42	21.02	0.50	0.14	0.18
Second Quarter	20.60	17.07	18.29	0.50	0.16	0.32
First Quarter	19.27	15.74	18.47	0.35	0.16	0.16
2015						
Fourth Quarter	22.23	18.61	19.49	0.18	0.16	0.16
Third Quarter	22.23	18.58	20.44	0.18	0.11	0.18
Second Quarter	21.23	17.91	20.87	0.30	0.04	0.15
First Quarter	19.53	16.48	18.88	0.15	0.10	0.10

The closing sales price of United common stock as of April 19, 2017, the last trading day before the merger agreement was announced, was \$26.70. The closing sales price of United common stock as of [•], 2017, the most recent date feasible for inclusion in these materials, was \$[•]. Trading in HCSB voting common stock is very limited and sporadic, with an average daily trading volume since January 1, 2017 of less than .005% of the outstanding shares. The closing sales price of HCSB voting common stock as of April 19, 2017, the last trading day before the merger agreement was announced, was \$0.35. The closing sales price of HCSB voting common stock as of [•], 2017, the most recent date feasible for inclusion in these materials, was \$[•].

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Assuming there is no adjustment in the merger consideration, if the merger had been completed on April 19, 2017, the implied value of one share of HCSB voting common stock exchanged for 0.0050 of a share of United common stock, would have been \$0.1335 based on United's closing sales price on that date. If the merger had been completed on [•], 2017, the most recent date feasible for inclusion in these materials, the implied value of one share of HCSB voting common stock exchanged for 0.0050 of a share of United common stock, would have been \$[•].

There were [•] shareholders of record of HCSB voting common stock as of [•], 2017. There were [•] shareholders of record of HCSB non-voting common stock as of [•], 2017.

Dividends (see page 48)

United declared cash dividends of \$0.09 per share of common stock in the first quarter of 2017, \$0.30 per share in 2016, \$0.22 per share in 2015 and \$0.11 per share in 2014. United intends to continue paying cash dividends, but the amount and frequency of cash dividends, if any, will be determined by United's Board of Directors after consideration of certain non-financial and financial factors including earnings, capital requirements, and the financial condition of United, and will depend on cash dividends paid to it by the Bank. The ability of the Bank to pay dividends to it is restricted by certain regulatory requirements.

No cash dividends were declared on HCSB's common stock in the first quarter of 2017 or in 2016, 2015 or 2014.

Differences in Legal Rights between Shareholders of HCSB and United (see page 44)

Following the merger you will no longer be a HCSB shareholder and your rights as a shareholder will no longer be governed by HCSB's articles of incorporation and bylaws and the SCBCA. You will be a United shareholder, and your rights as a United shareholder will be governed by United's articles of incorporation and bylaws and the Georgia Business Corporation Code. Your former rights as a HCSB shareholder and your new rights as a United shareholder are different in certain ways, including the following:

-

The articles of incorporation of HCSB authorize more shares of voting common stock and non-voting common stock than the articles of incorporation of United.

-

The articles of incorporation of United authorize more shares of preferred stock than the articles of incorporation of HCSB.

-

Holders of HCSB non-voting common stock, who currently have no voting rights except as required by the SCBCA, will have voting rights as holders of United common stock.

-

The bylaws of HCSB set forth different requirements for calling special meetings of shareholders than do the bylaws of United.

-

The bylaws of HCSB set forth different advance notice requirements for shareholders proposals than do the bylaws of United.

-

The bylaws of United provide that the number of directors may range between eight to fourteen directors while the bylaws of HCSB provide that the number of directors may range between five to twenty-five.

-

The bylaws of HCSB set forth different requirements for removal of directors than do the articles of incorporation of United.

-

The SCBCA, applicable to HCSB, requires supermajority shareholder approval of certain business transactions while the articles of incorporation and bylaws of United do not provide any supermajority requirement.

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The SCBCA, applicable to HCSB, provides for unanimous shareholder action by written consent in lieu of meeting while the bylaws of United require only the minimum number of votes necessary to authorize such action for shareholder action by written consent.

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The bylaws of HCSB do not provide for an exclusive forum for legal proceedings while the bylaws of United provide that the exclusive forum for certain legal proceedings is Georgia.

•

The articles of incorporation of HCSB generally may be amended upon approval by two-thirds of the votes entitled to be cast on the amendment, while the articles of incorporation of United may be amended upon approval by a majority of the votes entitled to be cast on the amendment.

Interests of Directors and Officers of HCSB and Horry County State Bank in the Merger (see page 42)

Some of the directors and officers of HCSB have interests in the merger in addition to their interests as shareholders generally, including the following:

•

Each outstanding share of HCSB restricted stock issued to Jan H. Hollar, J. Rick Patterson, and W. Jack McElveen will vest at the effective time of the merger and be converted into the merger consideration.

•

Employment agreements between HCSB and each of Ms. Hollar and Messrs. Patterson and McElveen provide for change in control compensation upon the completion of the merger.

•

United will indemnify and provide liability insurance to the present directors and officers of HCSB and Horry County State Bank for a period of six years following the closing of the merger with respect to acts or omissions occurring prior to merger.

Dissenters' Rights (see page 49)

Under South Carolina law, holders of HCSB common stock will be entitled to dissent from the merger and to obtain payment in cash of the fair value of his or her shares of HCSB common stock. Set forth below is a summary of the procedures that must be followed by the holders of HCSB common stock in order to exercise their dissenters' rights. This summary is qualified in its entirety by reference to the text of the applicable South Carolina statutes, a copy of which is attached to this proxy statement/prospectus as Appendix B to this document.

A record holder of HCSB common stock who wishes to assert dissenters' rights (i) must deliver to HCSB before the vote is taken on the merger agreement written notice of his or her intent to demand payment for his or her shares if the merger is effectuated, and (ii) must not vote his or her shares in favor of the merger agreement. If a shareholder notifies HCSB that he or she intends to dissent, a vote in favor of the merger agreement cast by the holder of a proxy solicited by HCSB shall not disqualify a shareholder from demanding payment for his shares. A shareholder who does not satisfy these requirements is not entitled to payment for his or her shares under the applicable South Carolina statutes.

If the merger is authorized at the HCSB special meeting, HCSB will deliver, no later than 10 days after the special meeting, a written dissenters' notice to all HCSB shareholders who satisfied the two requirements set forth above. The written dissenters' notice will state where the payment demand must be sent and where stock certificates must be deposited, will inform holders of uncertificated shares to what extent transfer of the shares is to be restricted after the payment demand is received, will supply a form for demanding payment that includes the date of the first announcement to news media or to shareholders of the terms of the proposed merger and requires that the person asserting dissenters' rights certify whether or not he or she or, if he or she is a nominee asserting dissenters' rights on behalf of a beneficial shareholder, the beneficial shareholder acquired beneficial ownership of the shares before that date, will set a date by which HCSB must receive the payment demand, which date will not be less than 30 or more than 60 days after the written dissenters' notice is delivered, will set a date by which certificates for certificated shares must be deposited, which date will not be earlier than 20 days after the demand date, and will be accompanied by a copy of the applicable South Carolina statutes. A shareholder that sent a dissenters' notice must demand payment,

certify whether he or she (or the beneficial shareholder on whose behalf he or she is asserting dissenters' rights) acquired the beneficial ownership of the shares before the date set forth in the dissenters' notice, and deposit his or her certificates in accordance with the terms of the notice. A dissenting shareholder who does not comply substantially with the requirements that he or she demand payment and deposit his or her share certificates where required, each by the date set in the dissenters' notice, is not entitled to payment for his or her shares under the applicable South Carolina statutes.

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As soon as the merger is consummated, or upon receipt of a payment demand, HCSB will pay to each dissenting shareholder who substantially complied with the requirements set forth above the amount HCSB estimates to be the fair value of his or her shares, plus accrued interest. The payment will be accompanied by HCSB's balance sheet as of the end of a fiscal year ending not more than 16 months before the date of payment, an income statement for that year, a statement of changes in shareholders' equity for that year, and the latest available interim financial statements, if any; a statement of HCSB's estimate of the fair value of the shares and an explanation of how the fair value was calculated; an explanation of how the interest was calculated; a statement of the dissenter's right to demand additional payment; and a copy of the applicable South Carolina statutes. If HCSB does not consummate the proposed merger within 60 days after the date set for demanding payment and depositing share certificates, HCSB, within the same 60 day period, shall return the deposited certificates and release the transfer restrictions imposed on the uncertificated shares. If the shareholder believes the amount paid or offered is less than fair value of his or her shares or that the interest due is calculated incorrectly, or HCSB fails to make payment or offer payment within 60 days after the date set for demanding payment, or if the merger is not consummated, HCSB fails to return the deposited certificates or release transfer restrictions imposed on uncertificated shares within 60 days after the date set for demanding payment, he or she may notify HCSB in writing of his or her own estimate of fair value of his shares and amount of interest due and demand payment of his or her estimate (less the payment already received) or reject HCSB's offer and demand payment of the fair value of his or her shares and interest due. However, a dissenting shareholder waives his or her right to demand additional payment if he or she fails to notify HCSB of his or her demand in writing within 30 days after HCSB made or offered payment for his or her shares. If a demand for additional payment remains unsettled, HCSB will commence a court proceeding within 60 days after receiving the demand for additional payment and petition the court to determine the fair value of the shares and the accrued interest. If HCSB does not commence the proceeding within the 60 day period, HCSB shall pay each dissenter whose demand remains unsettled the amount demanded.

Exercise of dissenters' rights by holders of HCSB common stock will result in the recognition of gain or loss, as the case may be, for federal income tax purposes.

- Special Shareholders' Meeting

Date, Time, and Place

The special meeting of shareholders of HCSB will be held on [•], 2017 at [•] a.m., at [•]. At the special meeting, HCSB shareholders will be asked to:

- approve the Agreement and Plan of Merger between HCSB and United, pursuant to which HCSB will be merged with and into United;
- approve, on a non-binding advisory basis, the compensation that certain executive officers of HCSB will receive under existing agreements or arrangements with HCSB in connection with the merger; and
- approve the adjournment or postponement of the special meeting, if necessary or appropriate, including to solicit additional proxies to approve the merger agreement.

Holders of HCSB voting common stock will vote on all three proposals. Holders of HCSB non-voting common stock will vote only on the merger proposal.

Record Date and Shares Entitled to Vote

You are entitled to vote at the shareholders' meeting if you owned shares of HCSB common stock on [•], 2017. As of this date, [•] shares of HCSB voting common stock were issued and outstanding and entitled to vote at the special meeting, and [•] shares of HCSB non-voting common stock were issued and outstanding and entitled to vote at the special meeting.

Support Agreements

All of the directors of HCSB have agreed to vote their shares in favor of the merger agreement; provided that such voting support agreements terminate in the event that the HCSB Board of Directors withdraws its recommendation in favor of the merger or approves or recommends an acquisition proposal

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from another party. As of the record date, HCSB's directors own [•] shares, or [•]%, of outstanding HCSB voting common stock, and no shares of outstanding HCSB non-voting common stock.

Vote Required (see page 39)

As of the record date, [•] shares of HCSB voting common stock were issued and outstanding and [•] shares of HCSB non-voting common stock were issued and outstanding, each of which is entitled to one vote per share.

Approval of the merger agreement requires the affirmative vote of (i) two-thirds of the issued and outstanding shares of HCSB voting common stock and (ii) a majority of the issued and outstanding shares of HCSB non-voting common stock. Your failure to vote your shares (including your failure to instruct your broker to vote your shares) or your abstaining from voting will have the same effect as a vote "AGAINST" the merger agreement. The HCSB Board of Directors has unanimously adopted and approved the merger agreement and unanimously recommends that HCSB shareholders vote "FOR" the approval of the merger agreement.

As referenced above, all of the directors of HCSB have agreed to vote their shares in favor of the merger agreement; provided that such voting support agreements terminate in the event that the HCSB Board of Directors withdraws its recommendation in favor of the merger or approves or recommends an acquisition proposal from another party. As of the record date, HCSB's directors own [•] shares, or [•]%, of outstanding HCSB voting common stock, and no shares of outstanding HCSB non-voting common stock.

The approval, on a non-binding advisory basis, of the proposal regarding compensation that certain executive officers of HCSB will receive under existing agreements or arrangements with HCSB in connection with the merger requires that the number of votes cast at the special meeting, in person or by proxy, in favor of the proposal exceeds the number of votes cast against the proposal. The HCSB Board of Directors unanimously recommends that HCSB shareholders vote "FOR" the approval of the compensation payable under existing agreements that certain of its officers will receive from HCSB in connection with the merger.

Approval of the merger agreement and approval of the compensation payable under existing agreements that certain HCSB officers will receive in connection with the merger are subject to separate votes of the HCSB shareholders, and approval of the compensation is not a condition to completion of the merger.

The approval of the proposal to adjourn or postpone the special meeting, if necessary or appropriate, including to solicit additional proxies to approve the merger agreement requires that the number of votes cast at the special meeting, in person or by proxy, in favor of the proposal exceeds the number of votes cast against the proposal. The HCSB Board of Directors unanimously recommends that shareholders vote "FOR" this proposal.

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We are providing the following information to help you analyze the financial aspects of the merger. The following tables set forth summary historical operations and financial condition data and summary performance, asset quality and other information of United at and for the periods indicated, which is derived from United's historical consolidated financial statements. You should read this data in conjunction with United's Consolidated Financial Statements and notes thereto incorporated herein by reference from United's Annual Report on Form 10-K for the year ended December 31, 2016 and United's quarterly report on Form 10-Q for the quarter ended March 31, 2017. Financial amounts as of and for the three months ended March 31, 2017 and 2016 are unaudited and are not necessarily indicative of the results of operations for the full year or any other interim period, and management of United believes that such amounts reflect all adjustments (consisting only of normal recurring adjustments) necessary for a fair statement of its results of operations and financial position as of the dates and for the periods indicated. You should not assume the results of operations for past years and for the three months ended March 31, 2017 and 2016 indicate results for any future period. United's "net operating income" is determined by methods other than in accordance with generally accepted accounting principles ("GAAP"). Please see the following "Non-GAAP Performance Measures Reconciliation" below for a reconciliation of the difference between United's non-GAAP net operating income and its GAAP net income.

	At or for the Three Months Ended March 31,		For the Years Ended December 31,				
	2017	2016	2016	2015	2014	2013	2012
	(in thousands, except per share data)						
INCOME SUMMARY							
Interest revenue	\$ 90,958	\$ 80,721	\$ 335,020	\$ 278,532	\$ 248,432	\$ 245,840	\$ 265,977
Interest expense	7,404	5,769	25,236	21,109	25,551	27,682	37,909
Net interest revenue	83,554	74,592	309,784	257,423	222,881	218,158	228,068
Provision for credit losses	800	(200)	(800)	3,700	8,500	65,500	62,500
Fee revenue	22,074	18,606	93,967	72,529	55,554	56,598	56,112
Total revenue	104,828	93,758	404,281	326,252	269,935	209,256	221,680
Expenses	62,826	57,885	241,289	211,238	162,865	174,304	186,774
Income before income tax expense	42,002	35,873	162,992	115,014	107,070	34,952	34,906
Income tax expense (benefit)	18,478	13,578	62,336	43,436	39,450	(238,188)	1,050
Net income	23,524	22,295	100,656	71,578	67,620	273,140	33,856
Preferred dividends	—	21	21	67	439	12,078	12,148
Net income available to common shareholders – GAAP	\$ 23,524	\$ 22,274	\$ 100,635	\$ 71,511	\$ 67,181	\$ 261,062	\$ 21,708

Merger-related and other charges	2,054	2,653	8,122	17,995	—	—	—
Income tax benefit of merger-related and other charges	(758)	(1,004)	(3,074)	(6,388)	—	—	—
Impairment of deferred tax asset on cancelled non-qualified stock options	—	—	976	—	—	—	—
Release of disproportionate tax effect lodged in OCI	3,400	—	—	—	—	—	—
Net income available to common shareholders – operating(1)	\$ 28,220	\$ 23,923	\$ 106,659	\$ 83,118	\$ 67,181	\$ 261,062	\$ 21,708

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	At or for the Three Months Ended March 31,		For the Years Ended December 31,				
	2017	2016	2016	2015	2014	2013	2012
	(in thousands, except per share data)						
PERFORMANCE MEASURES							
Per common share:							
Diluted net income – GAAP	\$.33	\$.31	\$ 1.40	\$ 1.09	\$ 1.11	\$ 4.44	\$.38
Diluted net income – operating(1)	.39	.33	1.48	1.27	1.11	4.44	.38
Cash dividends declared	.09	.07	.30	.22	.11	—	—
Book value	15.40	14.35	15.06	14.02	12.20	11.30	6.67
Tangible book value(3)	13.30	12.40	12.95	12.06	12.15	11.26	6.57
Key performance ratios:							
Return on common equity – GAAP(2)	8.54%	8.57%	9.41%	8.15%	9.17%	46.72%	5.43%
Return on common equity – operating(1)(2)	10.25	9.20	9.98	9.48	9.17	46.72	5.43
Return on tangible common equity – operating(1)(2)(3)	12.10	10.91	11.86	10.24	9.32	47.35	6.27
Return on assets – GAAP	.89	.93	1.00	.85	.91	3.86	.49
Return on assets – operating(1)	1.07	1.00	1.06	.98	.91	3.86	.49
Dividend payout ratio – GAAP	27.27	22.58	21.43	20.18	9.91	—	—
Dividend payout ratio – operating(1)	23.08	21.21	20.27	17.32	9.91	—	—
Net interest margin (fully taxable equivalent)	3.45	3.41	3.36	3.30	3.26	3.30	3.51
Efficiency ratio – GAAP	59.29	61.94	59.80	63.96	58.26	63.14	65.43
Efficiency ratio – operating(1)	57.35	59.10	57.78	58.51	58.26	63.14	65.43
	10.24	10.72	10.54	10.27	9.69	10.35	8.47

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Average equity to average assets							
Average tangible equity to average assets(3)	8.96	9.41	9.21	9.74	9.67	10.31	8.38
Average tangible common equity to average assets(3)	8.96	9.32	9.19	9.66	9.60	7.55	5.54
Tangible common equity to risk-weighted assets(3)	12.07	12.77	11.84	12.82	13.82	13.17	8.26
ASSET QUALITY							
Non-performing loans	\$ 19,812	\$ 22,419	\$ 21,539	\$ 22,653	\$ 17,881	\$ 26,819	\$ 109,894
Foreclosed properties	5,060	5,163	7,949	4,883	1,726	4,221	18,264
Total non-performing assets (NPAs)	24,872	27,582	29,448	27,536	19,607	31,040	128,158
Allowance for loan losses	60,543	66,310	61,442	68,448	71,619	76,762	107,137
Net charge-offs	1,679	2,138	6,766	6,259	13,879	93,710	69,831
Allowance for loan losses to loans	.87%	1.09%	.89%	1.14%	1.53%	1.77%	2.57%
Net charge-offs to average loans	.10	.14	.11	.12	.31	2.22	1.69
NPAs to loans and foreclosed properties	.36	.45	.43	.46	.42	.72	3.06
NPAs to total assets	.23	.28	.28	.29	.26	.42	1.88
AVERAGE BALANCES (\$ in millions)							
Loans	\$ 6,904	\$ 6,004	\$ 6,413	\$ 5,298	\$ 4,450	\$ 4,254	\$ 4,166
Investment securities	2,822	2,718	2,691	2,368	2,274	2,190	2,089
Earning assets	9,872	8,876	9,257	7,834	6,880	6,649	6,547
Total assets	10,677	9,634	10,054	8,462	7,436	7,074	6,865
Deposits	8,592	7,947	8,177	7,055	6,228	6,027	5,885
Shareholders' equity	1,093	1,033	1,059	869	720	732	582
	71,700	72,162	71,910	65,488	60,588	58,787	57,857

Common shares –
basic (thousands)

Common shares –
diluted (thousands)

71,708	72,166	71,915	65,492	60,590	58,845	57,857
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	At or for the Three Months Ended March 31,		For the Years Ended December 31,				
	2017	2016	2016	2015	2014	2013	2012
	(in thousands, except per share data)						
AT PERIOD END							
(\$ in millions)							
Loans	\$ 6,965	\$ 6,106	\$ 6,921	\$ 5,995	\$ 4,672	\$ 4,329	\$ 4,175
Investment securities	2,767	2,757	2,762	2,656	2,198	2,312	2,079
Total assets	10,732	9,781	10,709	9,616	7,558	7,424	6,801
Deposits	8,752	7,960	8,638	7,873	6,335	6,202	5,952
Shareholders' equity	1,102	1,034	1,076	1,018	740	796	581
Common shares outstanding (thousands)	70,973	71,544	70,899	71,484	60,259	59,432	57,741

(1)

Excludes merger-related charges, a first quarter 2017 release of disproportionate tax effects lodged in OCI and first quarter 2017 branch closure charges, a 2016 deferred tax asset impairment charge related to cancelled non-qualified stock options and 2015 impairment losses on surplus bank property.

(2)

Net income available to common shareholders, which is net of preferred stock dividends, divided by average realized common equity, which excludes accumulated other comprehensive income (loss).

(3)

Excludes effect of acquisition related intangibles and associated amortization.

TABLE OF CONTENTS**Non-GAAP Performance Measures Reconciliation**

This document and the documents incorporated by reference into this document include non-GAAP financial measures, which are performance measures determined by methods other than in accordance with GAAP. Such non-GAAP financial measures include, among others the following: taxable equivalent interest revenue, taxable equivalent net interest revenue, total operating revenue, operating expense, tangible book value per share, tangible common equity to assets and tangible common equity to risk-weighted assets. Management uses these non-GAAP financial measures because it believes they are useful for evaluating our operations and performance over periods of time, as well as in managing and evaluating our business and in discussions about our operations and performance. Management believes these non-GAAP financial measures provide users of our financial information with a meaningful measure for assessing our financial results and credit trends, as well as comparison to financial results for prior periods. These non-GAAP financial measures should not be considered as a substitute for operating results determined in accordance with GAAP and may not be comparable to other similarly titled financial measures used by other companies.

The following is a reconciliation of these operating performance measures to GAAP performance measures.

	At or for the Three Months Ended March 31,		For the Years Ended December 31,				
	2017	2016	2016	2015	2014	2013	2012
	(in thousands, except per share data)						
Expense reconciliation							
Expenses (GAAP)	\$ 62,826	\$ 57,885	\$ 241,289	\$ 211,238	\$ 162,865	\$ 174,304	\$ 186,774
Merger-related and other charges	(2,054)	(2,653)	(8,122)	(17,995)	—	—	—
Expenses – operating	\$ 60,772	\$ 55,232	\$ 233,167	\$ 193,243	\$ 162,865	\$ 174,304	\$ 186,774
Net income reconciliation							
Net income (GAAP)	\$ 23,524	\$ 22,295	\$ 100,656	\$ 71,578	\$ 67,620	\$ 273,140	\$ 33,856
Merger-related and other charges	2,054	2,653	8,122	17,995	—	—	—
Income tax benefit of merger-related and other charges	(758)	(1,004)	(3,074)	(6,388)	—	—	—
Impairment of deferred tax asset on cancelled non-qualified stock options	—	—	976	—	—	—	—
	3,400	—	—	—	—	—	—

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Release of disproportionate tax effects lodged in OCI							
Net income – operating	\$ 28,220	\$ 23,944	\$ 106,680	\$ 83,185	\$ 67,620	\$ 273,140	\$ 33,856
Net income available to common shareholders reconciliation							
Net income available to common shareholders (GAAP)	\$ 23,524	\$ 22,274	\$ 100,635	\$ 71,511	\$ 67,181	\$ 261,062	\$ 21,708
Merger-related and other charges	2,054	2,653	8,122	17,995	—	—	—
Income tax benefit of merger-related and other charges	(758)	(1,004)	(3,074)	(6,388)	—	—	—
Impairment of deferred tax asset on cancelled non-qualified stockoptions	—	—	976	—	—	—	—
Release of disproportionate tax effects lodged in OCI	3,400	—	—	—	—	—	—
Net income available to common shareholders – operating	\$ 28,220	\$ 23,923	\$ 106,659	\$ 83,118	\$ 67,181	\$ 261,062	\$ 21,708
Diluted income per common share reconciliation							
Diluted income per common share (GAAP)	\$.33	\$.31	\$ 1.40	\$ 1.09	\$ 1.11	\$ 4.44	\$.38

Merger-related and other charges	.01	.02	.07	.18	—	—	—
Impairment of deferred tax asset on cancelled non-qualified stock options	—	—	.01	—	—	—	—
Release of disproportionate tax effects lodged in OCI	.05	—	—	—	—	—	—
Diluted income per common share – operating	\$.39	\$.33	\$ 1.48	\$ 1.27	\$ 1.11	\$ 4.44	\$.38

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	At or for the Three Months Ended March 31,		For the Years Ended December 31,				
	2017	2016	2016	2015	2014	2013	2012
	(in thousands, except per share data)						
Book value per common share reconciliation							
Book value per common share (GAAP)	\$ 15.40	\$ 14.35	\$ 15.06	\$ 14.02	\$ 12.20	\$ 11.30	\$ 6.67
Effect on goodwill and other intangibles	(2.10)	(1.95)	(2.11)	(1.96)	(.05)	(.04)	(.10)
Tangible book value per common share	\$ 13.30	\$ 12.40	\$ 12.95	\$ 12.06	\$ 12.15	\$ 11.26	\$ 6.57
Return on tangible common equity reconciliation							
Return on common equity (GAAP)	8.54%	8.57%	9.41%	8.15%	9.17%	46.72%	5.43%
Merger-related and other charges	.47	.63	.48	1.33	—	—	—
Impairment of deferred tax asset on cancelled non-qualified stock options	—	—	.09	—	—	—	—
Release of disproportionate tax effects lodged in OCI	1.24	—	—	—	—	—	—
Return on common equity – operating	10.25	9.20	9.98	9.48	9.17	46.72	5.43
Effect on goodwill and other intangibles	1.85	1.71	1.88	.76	.15	.63	.84
Return on tangible	12.10%	10.91%	11.86%	10.24%	9.32%	47.35%	6.27%

common equity – operating							
Return on assets reconciliation							
Return on assets (GAAP)	.89%	.93%	1.00%	.85%	.91%	3.86%	.49%
Merger-related and other charges	.05	.07	.05	.13	—	—	—
Impairment of deferred tax asset on cancelled non-qualified stock options	—	—	.01	—	—	—	—
Release of disproportionate tax effects lodged in OCI	.13	—	—	—	—	—	—
Return on assets – operating	1.07%	1.00%	1.06%	.98%	.91%	3.86%	.49%
Dividend payout ratio reconciliation							
Dividend payout ratio (GAAP)	27.27%	22.58%	21.43%	20.18%	9.91%	—%	—%
Merger-related and other charges	(.98)	(1.37)	(1.02)	(2.86)	—	—	—
Impairment of deferred tax asset on cancelled non-qualified stock options	—	—	(.14)	—	—	—	—
Release of disproportionate tax effects lodged in OCI	(3.21)	—	—	—	—	—	—
Dividend payout ratio – operating	23.08%	21.21%	20.27%	17.32%	9.91%	—%	—%
Efficiency ratio reconciliation							
Efficiency ratio (GAAP)	59.29%	61.94%	59.80%	63.96%	58.26%	63.14%	65.43%

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Merger-related and other charges	(1.94)	(2.84)	(2.02)	(5.45)	—	—	—
Efficiency ratio – operating	57.35%	59.10%	57.78%	58.51%	58.26%	63.14%	65.43%
Average equity to assets reconciliation							
Equity to assets (GAAP)	10.24%	10.72%	10.54%	10.27%	9.69%	10.35%	8.47%
Effect of goodwill and other intangibles	(1.28)	(1.31)	(1.33)	(.53)	(.02)	(.04)	(.09)
Tangible equity to assets	8.96	9.41	9.21	9.74	9.67	10.31	8.38
Effect of preferred equity	—	(.09)	(.02)	(.08)	(.07)	(2.76)	(2.84)
Tangible common equity to assets	8.96%	9.32%	9.19%	9.66%	9.60%	7.55%	5.54%
Tangible common equity to risk-weighted assets reconciliation							
Tier 1 capital ratio (Regulatory)	11.46%	11.32%	11.23%	11.45%	12.06%	12.74%	14.16%
Effect of other comprehensive income	(.24)	(.25)	(.34)	(.38)	(.35)	(.39)	(.51)
Effect of deferred tax limitation	1.13	1.85	1.26	2.05	3.11	4.26	—
Effect of trust preferred	(.25)	(.08)	(.25)	(.08)	(1.00)	(1.04)	(1.15)
Effect of preferred equity	—	—	—	(.15)	—	(2.39)	(4.24)
Basel III intangibles transition adjustment	(.03)	(.07)	(.06)	(.10)	—	—	—
Basel III disallowed investments	—	—	—	.03	—	—	—
Tangible common equity	12.07%	12.77%	11.84%	12.82%	13.82%	13.18%	8.26%

to risk-weighted
assets

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TABLE OF CONTENTS**SUMMARY CONSOLIDATED FINANCIAL INFORMATION OF HCSB**

We are providing the following information to help you analyze the financial aspects of the merger. The following tables set forth summary historical operations and financial condition data and summary performance, asset quality and other information of HCSB at and for the periods indicated, which is derived from HCSB's historical consolidated financial statements. You should read this data in conjunction with HCSB's Consolidated Financial Statements and notes thereto incorporated herein by reference from HCSB's Annual Report on Form 10-K, as amended on Form 10-K/A, for the year ended December 31, 2016 and HCSB's quarterly report on Form 10-Q for the quarter ended March 31, 2017. Financial amounts as of and for the three months ended March 31, 2017 and 2016 are unaudited and are not necessarily indicative of the results of operations for the full year or any other interim period, and management of HCSB believes that such amounts reflect all adjustments (consisting only of normal recurring adjustments) necessary for a fair statement of its results of operations and financial position as of the dates and for the periods indicated. You should not assume the results of operations for past years and for the three months ended March 31, 2017 and 2016 indicate results for any future period.

	At and for the Three Months Ended March 31,		At and for the Years Ended December 31,				
	2017	2016	2016	2015	2014	2013	2012
	(in thousands, except share and per share data)						
STATEMENTS OF INCOME							
Interest income	\$ 3,259	\$ 2,989	\$ 12,368	\$ 13,726	\$ 16,095	\$ 17,071	\$ 17,071
Interest expense	637	1,046	2,972	4,454	5,054	5,301	5,301
Net interest income	2,622	1,943	9,396	9,272	11,041	11,770	11,770
Provision for loan losses	—	1,424	3,923	—	1,061	(1,497)	(1,497)
Net interest income after provision for loan losses	2,622	519	5,473	9,272	9,980	13,267	13,267
Noninterest income	413	416	20,614	3,135	3,556	3,956	3,956
Noninterest expense	2,742	4,218	19,231	12,626	13,749	15,460	15,460
Net income (loss) before provision for income taxes	293	(3,283)	6,856	(219)	(213)	1,763	1,763
Provision for income taxes	—	—	610	27	78	—	—
Net income (loss) before provision (benefit) for income taxes	293	(3,283)	6,246	(246)	(291)	1,763	1,763
	—	(398)	—	(1,512)	(1,112)	(852)	(852)

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Preferred
dividends and
accretion of
preferred shares

Gain on
redemption of
preferred shares

Net income
(loss) available
to common
shareholders

COMMON
AND PER
SHARE DATA

Net income
(loss) per
common share:

Basic

Diluted

Cash dividends
declared per
common
share

Book value per
common share

Outstanding
common shares

Weighted
average basic
common shares

Weighted
average diluted
common shares

Dividend
payout ratio

PERIOD-END
BALANCES

Total assets

Investment
securities
available for
sale, at fair
value

Total loans,
including loans
held for sale

Deposits

—	—	13,778	—	—	—	
\$ 293	\$ (3,681)	\$ 20,024	\$ (1,758)	\$ (1,403)	\$ 911	\$
\$ 0.00	\$ (0.96)	\$ 0.07	\$ (0.46)	\$ (0.37)	\$ 0.24	\$
0.00	(0.96)	0.07	(0.46)	(0.37)	0.24	
—	—	—	—	—	—	
0.07	(7.16)	0.07	(6.54)	(6.33)	(7.83)	
495,763,940	3,846,340	495,763,940	3,846,340	3,816,340	3,738,337	
468,013,940	3,846,340	301,460,946	3,823,244	3,770,355	3,738,337	
469,054,565	3,846,340	307,252,250	3,823,244	3,770,355	3,738,337	
n/a%	n/a%	n/a%	n/a%	n/a%	n/a%	
\$ 384,014	\$ 363,363	\$ 375,934	\$ 361,423	\$ 421,447	\$ 434,586	\$
104,341	83,205	106,529	89,701	106,674	94,602	
229,033	199,635	215,112	209,367	235,543	256,424	
322,339	335,461	313,269	330,831	391,337	406,044	

Federal Home Loan Bank advances	24,000	17,000	24,000	17,000	17,000	22,000
Shareholders' equity	36,112	(14,648)	35,327	(12,250)	(11,247)	(16,442)
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	At and for the Three Months Ended March 31,		At and for the Years Ended December 31,				
	2017	2016	2016	2015	2014	2013	2012
	(in thousands, except share and per share data)						
AVERAGE BALANCES							
Total assets	\$ 376,161	\$ 360,123	\$ 377,660	\$ 400,538	\$ 444,720	\$ 459,000	\$ 521,205
Interest-earning assets	346,097	319,395	342,258	352,035	392,985	401,946	477,476
Investment securities available for sale, at fair value	105,773	86,902	92,970	95,602	112,679	81,560	94,901
Total loans, including loans held for sale	218,316	205,314	205,048	226,365	249,358	280,208	337,445
Deposits	313,697	329,345	324,256	369,744	411,911	425,760	475,998
Federal Home Loan Bank advances	24,000	17,000	18,186	17,000	21,685	22,000	22,000
Other borrowings	—	17,248	6,247	18,338	18,360	19,375	24,475
Shareholders’ equity	35,756	(11,856)	24,577	(11,234)	(12,850)	(12,435)	(5,093)
SELECT PERFORMANCE RATIOS							
Return on average assets	0.32%	(3.57)%	1.65%	(0.06)%	(0.07)%	0.38%	(1.83)%
Return on average shareholders’ equity	3.33	n/a	25.41	n/a	n/a	n/a	n/a
Net interest margin	3.08	2.45	2.75	2.63	2.81	2.93	2.96
CAPITAL RATIOS							
Average shareholders’ equity as a percentage of average assets	9.51%	(3.29)%	6.51%	(2.80)%	(2.89)%	(2.71)%	(0.98)%
Shareholders’ equity as a percentage of assets	9.40	(4.03)	9.40	(3.39)	(2.67)	(3.78)	(2.51)
	15.02	(5.97)	15.54	(4.15)	(3.61)	(3.19)	(3.44)

Tier 1 risk-based
capital

Total risk-based capital	16.27	(5.97)	16.80	(4.15)	(3.61)	(3.19)	(3.44)
Tier 1 leverage	10.29	(3.86)	10.15	(2.87)	(2.36)	(2.23)	(2.34)

ASSET QUALITY INFORMATION

Allowance for loan losses	\$ 3,717	\$ 3,719	\$ 3,750	\$ 4,601	\$ 5,787	\$ 9,443	\$ 14,150
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Nonaccrual loans	1,915	6,115	2,025	8,742	11,661	10,631	22,567
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Nonperforming assets	4,532	17,385	4,912	22,366	31,332	35,603	42,188
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Loans 90 days past due and still accruing interest	—	—	—	—	170	—	157
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Net loans charged-off	33	2,306	4,774	1,186	4,717	3,210	17,558
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Allowance for loan losses as a percentage of gross loans	1.62%	1.86%	1.74%	2.20%	2.46%	3.68%	4.68%
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Nonaccrual loans and loans 90 days past due and still accruing interest as a percentage of gross loans	0.84	3.06	0.94	4.18	5.02	4.15	7.52
---	------	------	------	------	------	------	------

Nonperforming assets and loans 90 days past due and still accruing interest as a percentage of total assets	1.18	4.78	1.31	6.19	7.43	8.19	9.00
---	------	------	------	------	------	------	------

Net loans charged-off as a percentage of average gross loans	0.06	4.32	2.33	0.52	1.89	1.15	5.20
--	------	------	------	------	------	------	------

OTHER DATA

Number of full-service branches	8	8	8	8	11	11	11
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Number of full-time equivalent	80	89	81	90	105	104	111
--------------------------------------	----	----	----	----	-----	-----	-----

teammates

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The following table shows per common share data regarding basic and diluted earnings, cash dividends and book value for (i) United and HCSB on a historical basis, (ii) United and HCSB on a pro forma combined basis, and (iii) HCSB on a pro forma equivalent basis. The pro forma information has been derived from and should be read in conjunction with United's and HCSB's audited consolidated financial statements for the year ended December 31, 2016 and United's and HCSB's unaudited consolidated financial statements for the quarter ended March 31, 2017 incorporated herein by reference. This information is presented for illustrative purposes only. You should not rely on the pro forma combined or pro forma equivalent amounts as they are not necessarily indicative of the operating results or financial position that would have occurred if the merger had been completed as of the dates indicated, nor are they necessarily indicative of the future operating results or financial position of the combined company. The pro forma information, although helpful in illustrating the financial characteristics of the combined company under one set of assumptions, does not reflect the benefits of expected cost savings, opportunities to earn additional revenue, the impact of restructuring and merger-related costs, or other factors that may result as a consequence of the merger and, accordingly, does not attempt to predict or suggest future results.

Unaudited Comparative Per Common Share Data

	United	HCSB	United Pro Forma Combined	HCSB Pro Forma Equivalent Per Share(1)
Basic Earnings				
Year ended December 31, 2016	\$ 1.40	\$.07	\$ 1.64	\$.01
Three months ended March 31, 2017	\$.33	\$.00	\$.32	\$.00
Diluted Earnings				
Year ended December 31, 2016	\$ 1.40	\$.07	\$ 1.64	\$.01
Three months ended March 31, 2017	\$.33	\$.00	\$.32	\$.00
Cash Dividends Declared(2)				
Year ended December 31, 2016	\$.30	\$.00	\$.30	\$.00
Three months ended March 31, 2017	\$.09	\$.00	\$.09	\$.00
Book Value				
December 31, 2016	\$ 15.06	\$.07	\$ 15.04	\$.08
March 31, 2017	\$ 15.40	\$.07	\$ 15.37	\$.08

(1)

Computed by multiplying the United pro forma combined amounts by the exchange ratio of 0.0050.

(2)

United pro forma combined cash dividends paid are based only upon United's historical amounts.

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RISK FACTORS

In addition to the other information, including risk factors, incorporated by reference herein from United's Annual Report on Form 10-K for the year ended December 31, 2016, you should carefully read and consider the following factors in evaluating the merger.

Because the market price of United common stock will fluctuate, HCSB shareholders cannot be sure of the value of the merger consideration they will receive.

Upon completion of the merger, each share of HCSB common stock will be converted into the merger consideration consisting of shares of United common stock. The market value of the merger consideration received by HCSB shareholders will vary with the price of United's common stock, and there will be no adjustment to the merger consideration for changes in the market price of either shares of United common stock or shares of HCSB common stock. United's stock price changes daily as a result of a variety of other factors in addition to the business and relative prospects of United, including general market and economic conditions, industry trends, and the regulatory environment. These factors are beyond United's control. Therefore, at the time of the special meeting, holders of HCSB common stock will not know the precise market value of the consideration they will receive at the effective time of the merger. Shareholders should obtain current market quotations for shares of United common stock and for shares of HCSB common stock.

HCSB's officers and directors have interests in the merger in addition to or different from the interests that they share with you as a HCSB shareholder.

Some of HCSB's executive officers participated in negotiations of the merger agreement with United, and the HCSB Board of Directors approved the merger agreement and is recommending that HCSB shareholders vote for the merger agreement. In considering these facts and the other information contained in these materials, you should be aware that certain of HCSB's executive officers and directors have economic interests in the merger that are different from or in addition to the interests that they share with you as a HCSB shareholder. These interests include, upon the completion of the merger, the payment of certain amounts to Jan H. Hollar, J. Rick Patterson, and W. Jack McElveen under existing employment agreements and the acceleration of vesting of outstanding HCSB restricted common stock held by these executive officers and other HCSB employees. See "Proposal No.1 — The Merger — Interests of the Directors and Officers of HCSB in the Merger" on page 42.

United may be unable to successfully integrate Horry County State Bank's operations and retain its key employees. The merger involves the integration of two companies that previously operated independently. The difficulties of combining the companies' operations include integrating personnel, departments, systems, operating procedures and information technologies and retaining key employees. Failures in integrating operations or the loss of key personnel could have a material adverse effect on the business and results of operations of the combined company.

Regulatory approvals may not be received, may take longer than expected or may impose conditions that are not presently anticipated or cannot be met.

Before the transactions contemplated by the merger agreement, including the merger and the bank merger, may be completed, various approvals must be obtained from bank regulatory authorities. These governmental entities may impose conditions on the granting of such approvals. Such conditions or changes and the process of obtaining regulatory approvals could have the effect of delaying completion of the merger or of imposing additional costs or limitations on United following the merger. The regulatory approvals may not be received at all, may not be received in a timely fashion, and may contain conditions on the completion of the merger that are not anticipated or cannot be met. If the consummation of the merger is delayed, including by a delay in receipt of necessary governmental approvals, the business, financial condition and results of operations of each company may also be materially adversely affected.

If the merger is not completed, United common stock and HCSB common stock could be materially adversely affected.

The merger is subject to customary conditions to closing, including the approval of the HCSB shareholders. In addition, United and HCSB may terminate the merger agreement under certain

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circumstances. If United and HCSB do not complete the merger, the market price of United common stock or HCSB common stock may fluctuate to the extent that the current market prices of those shares reflect a market assumption that the merger will be completed. Further, whether or not the merger is completed, United and HCSB will also be obligated to pay certain investment banking, legal and accounting fees and related expenses in connection with the merger, which could negatively impact results of operations when incurred. In addition, neither company would realize any of the expected benefits of having completed the merger. If the merger is not completed, United and HCSB cannot assure their respective shareholders that additional risks will not materialize or not materially adversely affect the business, results of operations and stock prices of United and HCSB.

The termination fee contained in the merger agreement may discourage other companies from trying to acquire HCSB.

HCSB has agreed to pay a termination fee of \$2.0 million to United if, under certain circumstances, the merger agreement is terminated and, at the time of termination, a competing offer is outstanding or such offer has been accepted by HCSB. This fee could discourage other companies from trying to acquire HCSB.

HCSB shareholders will have a reduced ownership and voting interest after the merger and will exercise less influence over management.

HCSB shareholders currently have the right to vote in the election of the HCSB Board of Directors and on other matters affecting HCSB. Upon the completion of the merger, each HCSB shareholder receiving shares of United common stock in accordance with the merger agreement will be a shareholder of United with a percentage ownership of United that is smaller than such shareholder's current percentage ownership of HCSB. It is currently expected that the former shareholders of HCSB as a group will receive shares in the merger constituting approximately [•]% of the outstanding shares of United's common stock immediately after the merger. Because of this, HCSB shareholders will have less influence on the management and policies of United than they now have on the management and policies of HCSB.

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PROPOSAL NO. 1 — THE MERGER

Background of the Merger

Following the recapitalization of HCSB in April 2016, as part of its ongoing consideration and evaluation of its long-term prospects and strategies, the HCSB Board of Directors and senior management have regularly reviewed and assessed its business strategies and objectives, all with the goal of enhancing long-term value for its shareholders. The HCSB Board of Directors' reviews and assessments have included discussions regarding strategic alternatives, including capital planning, efforts to improve earnings (such as revenue increases and expense reductions), and growth strategies (such as organic growth and mergers and acquisitions). The HCSB Board of Directors conducted strategic planning meetings that have included the use of outside advisors who have provided reviews of factors influencing the financial institutions industry generally and HCSB in particular (including the economic, interest rate and regulatory environment); the competitive landscape of community banking participants in South Carolina, the Southeast region and nationally; public trading prices of financial institution stocks; and financial institution merger and acquisition activity and valuations. These strategic planning meetings have included discussions regarding potential business considerations, economies of scale, increased client service, and shareholder value benefits that might be achieved if HCSB were to become a larger institution through acquisitions or a merger with a larger financial institution.

The HCSB Board of Directors and HCSB's executive officers have also been contacted from time to time by various investment bankers and financial institutions, including United, who expressed a general interest in exploring strategic alternatives in the event that HCSB were to seek a merger partner. These contacts occurred through impromptu meetings at investor conferences and financial institutions industry conferences and other informal meetings and telephone calls. These meetings and the other inquiries that had been received from various institutions involved general discussions regarding a potential merger but did not involve specific proposed transaction terms.

On July 12, 2016, Jan Hollar, the Chief Executive Officer of HCSB, and Lynn Harton, the President and Chief Operating Officer of United, met to discuss, among other things, their prior experiences with financial institutions business combinations and, in particular, Mr. Harton's past experience with acquiring distressed financial institutions. Ms. Hollar and Mr. Harton were familiar with one another as a result of previous business relationships and, specifically, United's investment in HCSB as part of HCSB's private placement transaction that was consummated in April 2016.

On October 21, 2016, an executive officer of a financial institution (referred to herein as "Institution A") contacted Ms. Hollar to express Institution A's interest in pursuing strategic alternatives with HCSB. Ms. Hollar agreed to meet with the Institution A executive, and the parties met on November 18, 2016 in Myrtle Beach, South Carolina to discuss HCSB, Institution A and the financial institutions industry in general. At the conclusion of the meeting, the Institution A executive informed Ms. Hollar that Institution A's investment banker would contact her.

On November 28, 2016, Institution A's investment banker contacted Ms. Hollar and stated that Institution A had an interest in exploring a business combination with HCSB.

On November 29, 2016, the HCSB Board of Directors met by telephone, and HCSB's outside legal counsel, Nelson Mullins Riley & Scarborough, LLP ("Nelson Mullins"), also participated in the meeting. At this meeting, Ms. Hollar informed the HCSB Board of Directors that she had been contacted by Institution A and its investment banker about Institution A's interest in exploring a business combination with HCSB. Ms. Hollar also informed the HCSB Board of Directors that she had previously held conversations with executives from two other institutions, one of which was United, who had expressed interest in discussing a business combination when HCSB concluded the time was right. She further indicated that, should the HCSB Board of Directors decide to explore strategic alternatives, HCSB's investment banker, Hovde Group, LLC ("Hovde"), recommended expanding the pool of potential strategic partners to obtain a better indication of HCSB's value. During this meeting, Nelson Mullins discussed the fiduciary duties of the HCSB Board of Directors in connection with business combination transactions. Finally, Ms. Hollar sought guidance from the HCSB Board of Directors on whether to proceed with further discussions with any potential business combination partners. After discussion, the HCSB Board of

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Directors unanimously authorized management and Hovde to explore business combination opportunities with suitable candidates.

On December 9, 2016, Ms. Hollar met with Mr. Harton in Greenville, South Carolina, and Mr. Harton expressed United's interest in exploring a potential business combination with HCSB. On December 13, 2016, Mr. Harton and Ms. Hollar spoke again by phone to discuss United's interest in conducting due diligence on HCSB for purposes of pursuing a potential business combination with HCSB.

At its regularly scheduled meeting on December 15, 2016, the HCSB Board of Directors discussed the status of the search for potential business combination partners. Ms. Hollar reported that, with Hovde's assistance, management had identified eight institutions, including United and Institution A, that management believed would be attractive potential business combination partners, taking into account the institution's likely interest in HCSB, ability and willingness to offer an attractive share price, current regulatory standing, current merger and acquisition activity, and likely timing for a transaction.

This list of potential business combination partners included United, Institution A, and six other financial institutions, all of which Ms. Hollar or Hovde had had general conversations with since the last meeting of the HCSB Board of Directors. Six of these eight financial institutions, including United and Institution A, expressed interest in being included if HCSB were to commence a formal process of searching for a business combination partner. Following Ms. Hollar's report, the HCSB Board of Directors discussed the process and timing of a potential business combination and the pros and cons of proceeding at this time or waiting until a later date. After a thorough discussion, due to the existence of multiple interested financial institutions that the HCSB Board of Directors believed to be viable candidates to successfully execute a business combination, the HCSB Board of Directors unanimously authorized management to proceed with discussions with the six interested financial institutions.

At the regularly scheduled meeting of the HCSB Board of Directors on January 19, 2017, Ms. Hollar provided the HCSB Board of Directors with an update on the status of the search for a potential business combination partner, and the HCSB Board of Directors agreed formally to engage Hovde as its financial advisor for a potential business combination.

Over the next several weeks, HCSB or Hovde held discussions with each of the interested parties, and HCSB executed non-disclosure agreements with Institution A and United and began to provide each of them with due diligence materials. During February 2017, Hovde created an electronic data room containing the due diligence materials provided by HCSB, and United and Institution A were each granted access to the data room.

At its regularly scheduled board meeting on February 16, 2017, Ms. Hollar updated the HCSB Board of Directors on the status of the search for a potential business combination partner, including the on-going discussions with United and Institution A. Ms. Hollar informed the HCSB Board of Directors that the other four institutions were not in a position to continue discussions at this time due to their involvement in other matters. After discussion, the HCSB Board of Directors directed management to proceed with formal due diligence and negotiations with United and Institution A.

On February 21, 2017, Ms. Hollar and Rick Patterson, the Chief Operating Officer of HCSB, met in Greenville, South Carolina with Mr. Harton and Chris Zych, the Director of Mergers and Acquisitions and Management Reporting of United, to discuss due diligence and general matters associated with a potential business combination between the parties. Ms. Hollar and Mr. Patterson held a similar meeting on March 2, 2017 with executive officers of Institution A. Prior to these meetings, HCSB did not discuss specific proposed transaction terms with either United or Institution A. On March 7, 2017, the HCSB Board of Directors met, together with Hovde and Nelson Mullins, to discuss the preliminary non-binding letters of intent that had been received from United and Institution A. United's letter of intent proposed a fixed exchange ratio of 0.0050 shares of United common stock for each share of HCSB common stock. Based on the closing price of United common stock on March 6, 2017, this exchange ratio implied a price of \$0.1442 per share of HCSB common stock. Institution A's letter of intent proposed a floating exchange ratio, leading to a fixed merger consideration of \$0.125 per share, consisting of 100% Institution A common stock.

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Hovde discussed the letters of intent with the HCSB Board of Directors, providing a comparison of the terms and the financial metrics of the two offers and a summary of the negotiations that had led to these offers. Hovde also advised the HCSB Board of Directors regarding selected precedent merger transactions and discussed HCSB's prospects as an independent institution. This discussion included a review of HCSB's earnings projections as an independent financial institution prepared by certain members of senior management of HCSB for the years ending December 31, 2017 through 2022 based on execution of HCSB's current business strategy and Hovde's net present value sensitivity analysis of HCSB's estimated valuation based on such earnings projections. Hovde also reviewed each potential merger partner's branch map, comparative loan and deposit composition, historical financial information, historical stock price performance, analyst estimates and recommendations, shareholder base, current peer trading multiples, management and board of directors, historical merger activity, market capitalization and stock trading volume and liquidity, potential merger financial impact, and transaction pricing or form of consideration mix sensitivity analysis. Hovde further discussed with the HCSB Board of Directors selected proposed nonfinancial terms (including the retention of HCSB officers, board representation, severance for HCSB employees and proposed timing of due diligence and signing of a definitive agreement), strategic fit, and integration factors (including each partner's business model and strategy, primary operating market and senior management). Nelson Mullins also participated in the discussion and reviewed the fiduciary duties of the HCSB Board of Directors in connection with business combination transactions.

The HCSB Board of Directors then discussed the opportunities and risks associated with each of the two letters of intent, including the potential value of the merger consideration and the likelihood that a merger would ultimately be consummated on the terms reflected in the letters of intent. The HCSB Board of Directors discussed the opportunities and risks associated with HCSB remaining an independent institution, particularly in light of the potential continuing low interest rate environment, bank regulatory pressures and increasing compliance and other costs, the high level of competition from larger institutions and community banks in HCSB's market, regulatory considerations, and variable economic conditions. The HCSB Board of Directors also discussed recent increases in financial institution merger and acquisition activity levels and valuations and the current trading prices of some of HCSB's possible merger partners, which might enable such parties to execute a merger with HCSB on reasonably attractive financial terms.

Following this discussion, the HCSB Board of Directors unanimously determined to continue negotiations with United but asked Hovde to seek an increase in the merger consideration.

On March 9, 2017, the HCSB Board of Directors met again with representatives of Nelson Mullins to discuss the United offer. During this meeting, Ms. Hollar informed the HCSB Board of Directors that United was unwilling to increase its proposed merger consideration as it believed that its current offer represented the full value of HCSB. The HCSB Board of Directors reviewed the United proposal again and compared it against other alternatives, including remaining independent. The HCSB Board of Directors noted that there had been some recent trading in HCSB stock at prices materially higher than the implied value of United's per share offer, including recent trades at \$.38 per share. The HCSB Board of Directors noted, however, that the trading volume in HCSB's stock was extremely light and sporadic, with an average daily trading volume since January 1, 2017 of less than .005% of the outstanding shares, and that the recent trading prices were not indicative of the actual value of HCSB common stock. Following this discussion, the HCSB Board of Directors unanimously approved the United letter of intent and authorized management to negotiate a definitive agreement with United.

Over the next several weeks, HCSB and United and their respective advisers engaged in additional due diligence (including HCSB performing "reverse" due diligence on United which included, among other actions, meetings of the HCSB management team with members of United's management team and reviews of analyst reports) and negotiated the terms of the merger agreement and the related ancillary agreements.

On April 10 2017, the HCSB Board of Directors held a meeting, with Hovde and Nelson Mullins participating, to review a near-final draft of the merger agreement and to discuss the reverse due diligence findings. Hovde rendered its oral opinion, subsequently confirmed in writing, that, as of April 10, 2017 and based upon and subject to the assumptions made, procedures followed, matters considered and limitations on the review undertaken as set forth in its opinion, the proposed merger consideration was fair, from a financial point of view, to the HCSB shareholders. Ms. Hollar reported that United was still completing its

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diligence on HCSB, which she anticipated would be finalized within the next seven to ten days but which she did not believe would result in any proposed changes to the merger terms. After further discussion, the HCSB Board of Directors unanimously approved the merger agreement and authorized Ms. Hollar to execute the agreement on behalf of HCSB upon completion of United's diligence review. On April 18, 2017, United completed its final diligence review, with no changes proposed to the merger terms.

The merger agreement was entered into on April 19, 2017. On the morning of April 20, 2017, HCSB and United issued a joint news release publicly announcing the merger agreement.

United's Reasons for the Merger

United's board of directors believes that the completion of the merger presents a unique opportunity for United to further its growth strategy in coastal South Carolina. The terms of the merger, including the merger consideration, are the result of arm's-length negotiations between representatives of United and HCSB. In reaching its decision to approve the merger, United's board of directors consulted with its legal advisors regarding the terms of the transaction and with management of United. In approving the entry into the merger agreement, United's board of directors considered the following material factors:

- HCSB's strategic presence around the attractive Myrtle Beach market will further United's strategic focused coastal South Carolina growth plan;
- HCSB's and United's respective management teams share a common business vision and commitment to their respective clients, shareholders, employees and other constituencies;
- The two companies have complementary service-focused business models;
- United's management believes that the merger will be accretive to United's earnings per share in the first full year (excluding one-time charges) due to a combination of revenue synergies, cost efficiencies and other cost savings opportunities for the combined company; and
- The merger is likely to provide an increase in shareholder value, including the benefits of a stronger strategic position.

United's board of directors also considered potential risks associated with the merger in connection with its deliberations of the proposed transaction, including the challenges of integrating HCSB's business, operations and workforce with those of United, the potential negative impact on United's stock price and the need to obtain shareholder and regulatory approvals in order to complete the transaction.

United's board of directors considered all of these factors as a whole and, on balance, United's board of directors believes that the opportunities created by the merger to increase the value of United's franchise more than offset any integration or other risks inherent in the merger.

The foregoing discussion of the information and factors considered by United's board of directors is not exhaustive, but includes the material factors considered by United's board of directors. In view of the wide variety of factors considered by United's board of directors in connection with its evaluation of the merger and the complexity of these matters, United's board of directors did not consider it practical to, nor did it attempt to, quantify, rank or otherwise assign relative weights to the specific factors that it considered in reaching its decision. In considering the factors described above, individual members of United's board of directors may have given different weights to different factors.

On the basis of these considerations, United's entry into the merger agreement was unanimously approved by United's board of directors on April 13, 2017.

HCSB's Reasons for the Merger and Recommendation of the HCSB Board of Directors

It should be noted that the explanation of the reasoning of the HCSB Board of Directors and certain information presented in this section is forward-looking in nature and should be read in light of the factors set forth in the section entitled “Special Note Regarding Forward-Looking Statements.”

In reaching its decision to approve the merger agreement and recommend that HCSB’s shareholders approve the merger agreement, in addition to relying on personal knowledge of HCSB, United and the banking industry, the HCSB Board of Directors consulted with outside financial and legal advisors,

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reviewed various financial data and due diligence information, and considered the views of HCSB's Chief Executive Officer, who is also a director. After such consultation and review, and after considering HCSB's future prospects as an independent company and its strategic alternatives, the HCSB Board of Directors concluded that the proposed merger with United was in the best interests of HCSB and its shareholders.

In evaluating the merger agreement and reaching its decision to approve the merger agreement and recommend that HCSB shareholders approve the merger agreement, the HCSB Board of Directors considered a number of factors, which it reviewed with its outside financial and legal advisors, including the following, which are not intended to be exhaustive and are not presented in any relative order of importance:

- the length of time to sufficiently improve HCSB's financial condition to enable the company to remove the valuation allowance on its deferred tax asset;
- the fact that 100% of the HCSB shares of common stock will be converted into the right to receive United common stock in the merger, which will allow HCSB shareholders who desire to do so to participate substantially in the future performance of the combined HCSB and United business and the potential synergies resulting from the merger;
- the greater liquidity in the trading market for United common stock relative to the trading market for HCSB common stock;
- the current and prospective business and economic environment of the markets served by HCSB, including the competitive environment in HCSB's markets, the pressure on net interest margins resulting from a low interest rate environment, the continuing consolidation of the financial services industry, the increased regulatory burdens on financial institutions and the uncertainties in the regulatory climate going forward, and the escalating need for investment in technology;
- the regular quarterly cash dividend declared and historically paid by United on outstanding shares of its common stock;
- the views of the HCSB Board of Directors with respect to other potential HCSB strategic alternatives, including remaining independent, competing for organic growth, pursuing other merger partners, making acquisitions or engaging in share repurchases;
- the overall greater scale that will be achieved by the merger, which should better position the combined company for growth and profitability;
- the business, earnings, operations, financial condition, management, prospects, capital levels, technology and asset quality of both HCSB and United, taking into account the results of HCSB's due diligence of United;
- the financial analysis prepared by Hovde, HCSB's financial advisor, and the opinion delivered to the HCSB Board of Directors by Hovde, to the effect that, as of April 10, 2017 and based upon and subject to the assumptions, limitations, qualifications and conditions described in such opinion, the merger consideration was fair, from a financial point of view, to the HCSB shareholders;

- the financial terms of recent business combinations in the financial services industry reviewed by the HCSB Board of Directors and a comparison of the multiples paid in such selected business combinations with the terms of the merger, including information that was included in the Hovde fairness opinion analysis that indicated that the merger consideration, as a percentage of adjusted tangible book value and as a multiple of earnings, was higher than the comparable nationwide transactions group median and the comparable Southeast transactions group median and the merger consideration represented a core deposit premium that was also higher than the comparable nationwide transactions group median and the comparable Southeast transactions group median;

- the results of HCSB's exploration of possible merger partners other than United, and the views of the HCSB Board of Directors with respect to the likelihood of any such other merger occurring and providing greater value to HCSB shareholders;

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- the views of the HCSB Board of Directors with respect to the complementary aspects of the HCSB and United businesses, including customer focus, geographic coverage, business orientation and compatibility of the companies' management and operating styles, which the HCSB Board of Directors believes should facilitate integration and enhance the likelihood of successful post-merger operations;
- the belief of the HCSB Board of Directors that combining the two companies presents potential opportunities to realize operational, technological, marketing and other synergies resulting from the merger;
- the HCSB Board of Directors' understanding of United's commitment to enhancing its strategic position in South Carolina and in the Southeast region;
- the views of the HCSB Board of Directors as to the likelihood that the regulatory approvals necessary to complete the merger would be obtained;
- the views of the HCSB Board of Directors as to the ability of United's management team to successfully integrate and operate the business of the combined company after the merger;
- the effect of the merger on HCSB's officers and employees, including the prospects for continued employment and the severance and other benefits agreed to be provided by United to employees of HCSB; and
- the fact that HCSB shareholders would be entitled to dissenters' rights in connection with the merger.

The HCSB Board of Directors also considered a variety of risks and other potentially negative factors concerning the merger, including the following, which are not intended to be exhaustive and are not presented in any relative order of importance:

- the fact that the estimated value of the merger consideration represents a discount to sporadic and limited recent trading prices of HCSB common stock;
- if the market price of United's common stock decreases prior to completion of the merger, the aggregate value of consideration to be received by HCSB's shareholders receiving stock in the merger will decrease as well;
- the fact that HCSB would be prohibited from affirmatively soliciting acquisition proposals after execution of the merger agreement, and the possibility that, while it was not viewed as precluding other proposals, the \$2 million termination fee payable by HCSB upon the termination of the merger agreement under certain circumstances could potentially discourage certain other potential acquirers from making a competing offer to acquire HCSB;
- HCSB will lose the autonomy and local strategic decision-making capability associated with being an independent financial institution;

- the possibility that the merger and the related integration process could result in the loss of key employees, in the disruption of HCSB's ongoing business and in the loss of customers for the combined company;
- the fact that, while HCSB expects that the merger will be consummated, there can be no assurance that all conditions to the parties' obligations to complete the merger agreement will be satisfied, including the risk that certain regulatory approvals, the receipt of which are conditions to the consummation of the merger, might not be obtained, and, as a result, the merger may not be consummated;
- the fact that HCSB's officers and employees will have to focus on actions required to complete the merger, which will divert their attention from HCSB's day-to-day business, and that HCSB will incur substantial transaction costs even if the merger is not consummated;

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- the risk that potential benefits and synergies sought in the merger may not be realized or may not be realized within the expected time period, and the risks associated with the integration of the two companies;
- the restrictions on the conduct of HCSB's business prior to the completion of the merger, which are customary for public company merger agreements involving financial institutions, but which, subject to specific exceptions, could delay or prevent HCSB from undertaking business opportunities that may arise or any other action it would otherwise take with respect to the operations of HCSB absent the pending completion of the merger;
- the significant risks and costs involved in connection with entering into and completing the merger, or failing to complete the merger in a timely manner, or at all, including as a result of any failure to obtain required regulatory approvals, such as the risks and costs relating to diversion of management and employee attention from other strategic opportunities and operational matters, potential employee attrition, and the potential effect on business and customer relationships; and
- the possibility of litigation in connection with the merger.

In addition, the HCSB Board of Directors was aware of and considered the fact that some of HCSB's directors and executive officers may have other interests in the merger that may be different from, or in addition to, their interests as HCSB shareholders, as more fully described under "Proposal No. 1 — The Merger — Interests of HCSB's Directors and Executive Officers in the Merger." The HCSB Board of Directors also realized that there can be no assurance about future results, including results expected or considered in the factors listed above. However, the HCSB Board of Directors concluded that the potential positive factors outweighed the risks and other potentially negative factors associated with the merger.

In reaching its conclusion, the HCSB Board of Directors did not find it practical to assign, and did not assign, any relative or specific weight to the different factors that were considered, and individual members of the HCSB Board of Directors may have given different weight to different factors.

The HCSB Board of Directors unanimously adopted the merger agreement and recommends that you vote "FOR" approval of the merger agreement.

Each of the HCSB directors have entered into voting support agreements with United, pursuant to which they have agreed to vote in favor of the merger agreement at the special meeting. For more information regarding the support agreements, please see the section entitled "Special Shareholders' Meeting — Support Agreements" beginning on page 9.

Opinion of HCSB's Financial Advisor

The fairness opinion of HCSB's financial advisor in connection with the merger, Hovde, is described below. The description contains projections, estimates and other forward looking statements about the future earnings or other measures of the future performance of HCSB, United and the combined companies after the merger. You should not rely on any of these statements as having been made or adopted by Hovde, HCSB or United. You should review the copy of the fairness opinion, which is attached as Appendix C.

Hovde has acted as HCSB's financial advisor in connection with the proposed merger. Hovde is a nationally recognized investment banking firm with substantial experience in transactions similar to the merger and is familiar with HCSB and its operations. As part of its investment banking business, Hovde is continually engaged in the valuation of businesses and their securities in connection with, among other things, mergers and acquisitions. Hovde reviewed the financial aspects of the proposed merger with the HCSB Board of Directors and, on April 10, 2017, delivered a written opinion to the HCSB Board of Directors that the merger consideration to be received by the shareholders of HCSB in connection with the merger is fair to the shareholders of HCSB.

The full text of Hovde's written opinion is included in this document as Appendix C and is incorporated herein by reference. You are urged to read the opinion in its entirety for a description of the procedures followed, assumptions

made, matters considered and qualifications and limitations on the review undertaken by Hovde. The summary of the Hovde's opinion included in this document is qualified in

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its entirety by reference to the full text of such opinion. Hovde's opinion was directed to the HCSB Board of Directors and addresses only the fairness of the merger consideration to be paid to HCSB shareholders in connection with the merger. Hovde did not opine on any individual stock, cash, or other components of consideration payable in connection with the merger. Hovde's opinion does not address the underlying business decision to proceed with the merger and does not constitute a recommendation to any of the shareholders as to how such shareholder should vote at the special meeting of HCSB shareholders on the merger or any related matter.

During the course of its engagement and for the purpose of rendering its opinion, Hovde:

- reviewed a draft of the merger agreement dated April 7, 2017, as provided to Hovde by HCSB;
- reviewed unaudited consolidated financial statements for HCSB and United for the year ended December 31, 2016;
- reviewed certain historical annual reports of each of HCSB and United, including audited annual reports for the year ending December 31, 2016;
- reviewed certain historical publicly available business and financial information concerning each of HCSB and United;
- reviewed certain internal financial statements and other financial and operating data concerning of HCSB and United;
- reviewed financial projections prepared by certain members of senior management of HCSB;
- reviewed the terms of recent merger, acquisition and control investment transactions, to the extent publicly available, involving financial institutions and financial institution holding companies that Hovde considered relevant;
- assessed general economic, market and financial conditions;
- reviewed the pro forma impact of the merger on the combined company's earnings per share, consolidated capitalization and financial ratios;
- evaluated the pro forma ownership of United's common stock by the holders of HCSB's common stock relative to the pro forma contribution of HCSB's assets, liabilities, equity and earnings to the combined company;
- reviewed historical market prices and trading volumes of HCSB's and United's common stock; and
- reviewed certain publicly available financial and stock market data relating to selected public companies that Hovde deemed relevant to its analysis.

Hovde also conducted meetings and had discussions with members of senior management of HCSB and United for purposes of reviewing the business, financial condition, results of operations and future prospects of HCSB and United; the history and past and current operations of HCSB and United; and HCSB's and United's historical financial performance. Hovde discussed with management of HCSB and United their assessment of the rationale for the merger. Hovde also performed such other analyses and considered such other factors as Hovde deemed appropriate, and took into account its experience in other similar transaction and securities valuations, as well as its knowledge of the banking and financial services industry.

Hovde assumed, without independent verification, that the representations as well as the financial and other information provided to Hovde by HCSB or included in the merger agreement, which has formed a substantial basis for this opinion, are true and complete. Hovde relied upon the management of HCSB as to the reasonableness and achievability of the financial forecasts and projections (and the assumptions and bases therein) provided to Hovde by HCSB, and Hovde assumed such forecasts and projections have been reasonably prepared by HCSB on a basis reflecting the best currently available information and HCSB's judgments and estimates. Hovde assumed that such forecasts and projections would be realized in the amounts and at the times contemplated thereby, and Hovde does not in any respect assume any

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responsibility for the accuracy or reasonableness thereof. Hovde has been authorized by HCSB to rely upon such forecasts and projections and other information and data, including without limitation the projections, and Hovde expresses no view as to any such forecasts, projections or other information or data, or the bases or assumptions on which they were prepared.

In performing its review, Hovde relied upon the accuracy and completeness of all of the financial and other information that was available to Hovde from public sources, that was provided to Hovde by HCSB and United or their respective representatives or that was otherwise reviewed by Hovde and assumed such accuracy and completeness for purposes of rendering its opinion. Hovde has further relied on the assurances of the respective managements of HCSB and United that they are not aware of any facts or circumstances that would make any of such information inaccurate or misleading. Hovde has not been asked to and has not undertaken an independent verification of any of such information and Hovde does not assume any responsibility or liability for the accuracy or completeness thereof. Hovde assumed that each party to the merger agreement would advise them promptly if any information previously provided to them became inaccurate or was required to be updated during the period of Hovde's review. Hovde is not an expert in the evaluation of loan and lease portfolios for purposes of assessing the adequacy of the allowances for losses with respect thereto. Hovde assumed that such allowances for HCSB and United are, in the aggregate, adequate to cover such losses, and will be adequate on a pro forma basis for the combined entity. Hovde was not requested to make, and did not make, an independent evaluation, physical inspection or appraisal of the assets, properties, facilities, or liabilities (contingent or otherwise) of HCSB and United, the collateral securing any such assets or liabilities, or the collectability of any such assets and, Hovde was not furnished with any such evaluations or appraisals, nor did Hovde review any loan or credit files of HCSB and United.

Hovde has assumed that the merger will be consummated substantially in accordance with the terms set forth in the merger agreement, without any waiver of material terms or conditions by HCSB or any other party to the merger agreement and that the final merger agreement will not differ materially from the draft Hovde reviewed. Hovde has assumed that the merger will be consummated in compliance with all applicable laws and regulations. HCSB has advised Hovde that HCSB is not aware of any factors that would impede any necessary regulatory or governmental approval of the merger. Hovde has assumed that the necessary regulatory and governmental approvals as granted will not be subject to any conditions that would be unduly burdensome on HCSB and United or would have a material adverse effect on the contemplated benefits of the merger.

HCSB engaged Hovde on January 25, 2017 to serve as a financial advisor to HCSB in connection with the proposed merger and to issue a fairness opinion to the HCSB Board of Directors in connection with such proposed transaction. Pursuant to the terms of the engagement, at the time the merger is completed, HCSB will pay Hovde a completion fee, which is contingent upon the completion of the merger. Pursuant to the engagement agreement, in addition to its fees and regardless of whether the merger is consummated, HCSB has agreed to reimburse Hovde for certain reasonable out-of-pocket expenses incurred in performing its services and to indemnify Hovde against certain claims, losses and expenses arising out of the merger or Hovde's engagement.

In performing its analyses, Hovde made numerous assumptions with respect to industry performance, general business, economic, market and financial conditions and other matters, many of which are beyond the control of Hovde, HCSB and United. Hovde's opinion was necessarily based on financial, economic, market and other conditions and circumstances as they existed on, and on the information made available to Hovde as of, the dates used in its opinion. Any estimates contained in the analyses performed by Hovde are not necessarily indicative of actual values or future results, which may be significantly more or less favorable than suggested by these analyses. Additionally, estimates of the value of businesses or securities do not purport to be appraisals or to reflect the prices at which such businesses or securities may be sold or the prices at which any securities may trade at any time in the future.

Accordingly, these analyses and estimates are inherently subject to substantial uncertainty. Hovde's opinion does not address the relative merits of the merger as compared to any other business combination in which HCSB might engage. In addition, Hovde's fairness opinion was among several factors taken into consideration by the HCSB Board of Directors in making its determination to approve the merger agreement and the merger. Consequently, the analyses described below should not be viewed as solely determinative of the decision of the HCSB Board of

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Directors or HCSB's management with respect to the fairness of the merger consideration to be received by HCSB's shareholders in connection with the merger.

The following is a summary of the material analyses prepared by Hovde and delivered to the HCSB Board of Directors on April 10, 2017, in connection with the delivery of its fairness opinion. This summary is not a complete description of the analyses underlying the fairness opinion or the presentation prepared by Hovde, but it summarizes the material analyses performed and presented in connection with such opinion. The preparation of a fairness opinion is a complex analytical process involving various determinations as to the most appropriate and relevant methods of financial analysis and the application of those methods to the particular circumstances. Therefore, a fairness opinion is not readily susceptible to partial analysis or summary description. In arriving at its opinion, Hovde did not attribute any particular weight to any analysis or factor that it considered, but rather made qualitative judgments as to the significance and relevance of each analysis and factor. The financial analyses summarized below include information presented in tabular format. The analyses and the summary of the analyses must be considered as a whole and selecting portions of the analyses and factors or focusing on the information presented below in tabular format, without considering all analyses and factors or the full narrative description of the financial analyses, including the methodologies and assumptions underlying the analyses, could create a misleading or incomplete view of the process underlying the analyses and opinion of Hovde. The tables alone are not a complete description of the financial analyses.

Market Approach — Comparable Transactions. As part of its analysis, Hovde reviewed publicly available information related to two comparable groups (a "Regional Group" and a "Nationwide Group") of select acquisition transactions of banks. The Regional Group consisted of acquisition transactions of banks in the Southeast Region of the United States (consisting of the states of Alabama, Arkansas, Florida, Georgia, Mississippi, North Carolina, South Carolina, Tennessee, Virginia, and West Virginia) announced since January 1, 2015, in which the sellers' total assets were between \$200 million and \$1.0 billion, last-twelve-months ("LTM") return on average assets ("ROAA") were between 0.00% and 1.00%, and tangible equity to tangible assets greater than 10.0%. The Nationwide Group consisted of acquisition transactions of banks in the United States announced since January 1, 2015, in which the sellers' total assets were between \$250 million and \$500 million, last-twelve-months return on average assets were between 0.40% and 1.00%, and tangible equity to tangible assets were between 10.0% and 15.0%. In each case, for which financial information was available, no transaction that fit the selection criteria was excluded. Information for the target institutions was based on balance sheet data as of, and income statement data for the twelve months preceding the most recent quarter prior to announcement of the transactions. The resulting two groups consisted of the following transactions (14 transactions for the Regional Group and 13 transactions for the Nationwide Group):

Regional Group:

Buyer (State)	Target (State)
Little Bank, Inc. (NC)	Union Banc Corp. (NC)
Seacoast Banking Corporation of Florida (FL)	GulfShore Bancshares, Inc. (FL)
Bay Banks of Virginia, Inc. (VA)	Virginia BanCorp, Inc. (VA)
Home BancShares, Inc. (AR)	Giant Holdings, Inc. (FL)
BNC Bancorp (NC)	High Point Bank Corporation (NC)
Seacoast Banking Corporation of Florida (FL)	Floridian Financial Group, Inc. (FL)
Southern BancShares (N.C.), Inc. (NC)	Heritage Bankshares, Inc. (VA)
Renasant Corporation (MS)	KeyWorth Bank (GA)
Home BancShares, Inc. (AR)	Florida Business BancGroup, Inc. (FL)
Bank of the Ozarks, Inc. (AR)	Bank of the Carolinas Corporation (NC)
Pinnacle Financial Partners, Inc. (TN)	Magna Bank (TN)
Pinnacle Financial Partners, Inc. (TN)	CapitalMark Bank & Trust (TN)
Sunshine Bancorp, Inc. (FL)	Community Southern Holdings, Inc. (FL)

United Community Banks, Inc. (GA)

MoneyTree Corporation. (TN)

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Nationwide Group:

Buyer (State)	Target (State)
Citizens Community Bancorp, Inc. (WI)	Wells Financial Corp. (MN)
Little Bank, Inc. (NC)	Union Banc Corp. (NC)
Seacoast Banking Corporation of Florida (FL)	GulfShore Bancshares, Inc. (FL)
Bay Banks of Virginia, Inc. (VA)	Virginia BanCorp, Inc. (VA)
United Community Bancorp, Inc. (IL)	Liberty Bancshares, Inc. (IL)
Home BancShares, Inc. (AR)	Giant Holdings, Inc. (FL)
Standard Financial Corp. (PA)	Allegheny Valley Bancorp, Inc. (PA)
Seacoast Banking Corporation of Florida (FL)	Floridian Financial Group, Inc. (FL)
Southern BancShares (N.C.), Inc. (NC)	Heritage Bankshares, Inc. (VA)
Renasant Corporation (MS)	KeyWorth Bank (GA)
Glacier Bancorp, Inc. (MT)	Cañon Bank Corporation (CO)
Southwest Bancorp, Inc. (OK)	First Commercial Bancshares, Inc. (OK)
United Community Banks, Inc. (GA)	MoneyTree Corporation. (TN)

For each precedent transaction, Hovde compared the implied ratio of deal value to certain financial characteristics of HCSB as follows:

- the multiple of the purchase consideration to the acquired company's tangible common book value (the "Price-to-Tangible Common Book Value Multiple");
- the multiple of the purchase consideration to the acquired company's LTM net earnings per share (the "Price-to-LTM Earnings Multiple"); and
- the multiple of the difference between the purchase consideration and the acquired company's tangible book value to the acquired company's core deposits (the "Premium-to-Core Deposits Multiple").

The results of the analysis are set forth in the table below. Transaction multiples for the merger were derived from the estimated per share purchase price of \$0.1335 (based on the closing price of United's common stock on April 19, 2017 of \$26.70 and an exchange ratio of 0.0050), which implied a merger consideration of \$66,159,698 for HCSB and were based on December 31, 2016 financial results of HCSB.

Implied Value for HCSB Based On:	Price-to-Tangible Common Book Value Multiple	Price-to-"Adjusted" Tangible Common Book Value Multiple(1)	Price-to-"Economic" Tangible Common Book Value Multiple(2)	Price-to-LTM Earnings Multiple(3)(4)	Premium-to-Core Deposits Multiple(5)
Total Deal Value	187.3%	117.8%	142.8%	31.7x	4.9%
Precedent Transactions					
Regional Group:					
Median	144.3%	144.3%	144.3%	22.6x	7.2%
Minimum	84.2%	84.2%	84.2%	12.5x	(2.8)%
Maximum	242.1%	242.1%	242.1%	34.7x	18.3%

Precedent Transactions

Nationwide Group:

Median	137.0%	137.0%	137.0%	20.6x	5.4%
Minimum	84.2%	84.2%	84.2%	12.5x	(2.8)%
Maximum	164.1%	164.1%	164.1%	34.7x	12.0%

(1)

HCSB's tangible common equity has been adjusted to reflect the reversal of HCSB's approximate \$20.8 million valuation allowance on its deferred tax asset.

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(2)

Based on HCSB's tangible common equity after adjusting for the estimated deferred tax asset valuation allowance reversal and the impairment associated with 382(g) for this specific transaction.

(3)

HCSB's LTM earnings reflect 2017 earnings estimates from management and excludes the non-core impact associated with the reversal of HCSB's approximate \$20.8 million valuation allowance on its deferred tax asset.

(4)

Price to LTM EPS multiples are considered non-meaningful for value greater than 40.0x or less than 5.0x.

(5)

HCSB's tangible common equity has been adjusted to reflect the full valuation allowance reversal of approximately \$20.8 million.

Using publicly available information, Hovde compared the financial performance of HCSB with that of the median of the precedent transactions from both the Regional and Nationwide Groups. The performance highlights are based on December 31, 2016 financial results of HCSB.

	Tangible Equity/ Tangible Assets(1)	Core Deposits	LTM ROAA(2)	LTM ROAE(2)	Efficiency Ratio	NPA's/ Assets(3)	ALLL/ NPLs(4)
HCSB	14.16%	66.93%	1.65%	25.41%	126.13%	6.20%	18.35%
Precedent Transactions Regional Group:							
Median	11.60%	77.75%	0.65%	5.60%	73.35%	1.81%	85.19%
Precedent Transactions Nationwide Group:							
Median	10.99%	81.88%	0.66%	6.13%	71.87%	1.34%	101.22%

(1)

HCSB's financial data as of December 31, 2016; Assets and Tangible Equity / Tangible Assets have been adjusted to reflect the reversal of HCSB's approximate \$20.8 million valuation allowance on its deferred tax asset.

(2)

Returns include non-core gains associated with the recapitalization in FY2016; net income includes the extinguishment of HCSB's subordinated debt, trust preferred securities, and preferred stock issued to the United States Treasury as a part of TARP at significant discounts, in addition to write-downs in its loan portfolio.

(3)

Non-performing assets (including accruing, restructured loans) as a percent of total assets.

(4)

Allowance for loan and lease losses as a percentage of non-performing loans (including accruing, restructured loans).

No company or transaction used as a comparison in the above transaction analyses is identical to HCSB, and no transaction was consummated on terms identical to the terms of the merger agreement. Accordingly, an analysis of these results is not strictly mathematical. Rather, it involves complex considerations and judgments concerning differences in financial and operating characteristics of the companies. The resulting values of the Regional Group precedent transactions indicated an implied aggregate valuation ranging between \$47.2 million and \$81.1 million compared to the proposed merger consideration of \$66.2 million. The resulting values of the Nationwide Group precedent transactions indicated an implied aggregate valuation ranging between \$42.9 million and \$76.9 million compared to the proposed merger consideration of \$66.2 million.

Income Approach — Discounted Cash Flow Analysis. Taking into account various factors including, but not limited to, HCSB's recent performance, the current banking environment and the local economy in which HCSB operates, Hovde determined, in consultation with and based on information provided by management of HCSB, earnings estimates for HCSB over a forward looking six year period, and HCSB

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management developed the forward-looking projections and key assumptions, which formed the basis for the discounted cash flow analyses. The resulting projected net income numbers used for the analysis were \$2.1 million for 2017, \$3.1 million for 2018, \$3.4 million for 2019, \$3.9 million for 2020, \$4.8 million for 2021, and \$5.7 million for 2022.

To determine present values of HCSB based on these projections, Hovde utilized two discounted cash flow models, each of which capitalized terminal values using a different methodology: (1) terminal price/ earnings multiple (“DCF Terminal P/E Multiple”); and (2) terminal price/tangible book value multiple (“DCF Terminal P/TBV Multiple”).

In the DCF Terminal P/E Multiple analysis, an estimated value of HCSB’s common stock was calculated based on the present value of HCSB’s after-tax net income based on HCSB management’s forward-looking projections. Hovde utilized a terminal value at the end of 2022 by applying a range of price-to-earnings multiples of 18.6x to 22.6x, with a midpoint of 20.6x, which is based around the median price-to-earnings multiple derived from transactions in the Nationwide Group. The present value of HCSB’s projected dividends, if any, plus the terminal value was then calculated assuming a range of discount rates between 11.5% and 14.5%, with a midpoint of 13.0%. This range of discount rates was chosen to reflect different assumptions regarding the required rates of return of holders or prospective buyers of HCSB’s common stock. The resulting aggregate values of HCSB’s common stock of the DCF Terminal P/E Multiple ranged between \$48.8 million and \$69.0 million, with a midpoint of \$58.2 million.

In the DCF Terminal P/TBV Multiple model, the same earnings estimates and projected net income were used; however, in arriving at the terminal value at the end of 2022, Hovde applied a range of price-to-tangible book value multiples of 1.27x to 1.47x with the midpoint being 1.37x, which is based around the median price-to-tangible book value multiple derived from transactions in the Nationwide Group. The present value of projected dividends, if any, plus the terminal value, was then calculated assuming a range of discount rates between 11.5% and 14.5%, with a midpoint of 13.0%. The resulting aggregate values of HCSB’s common stock of the DCF Terminal P/TBV Multiple ranged between \$46.3 million and \$62.3 million, with a midpoint of \$53.8 million.

These analyses and their underlying assumptions yielded a range of values for HCSB, which are outlined in the table below:

Implied Value for HCSB Based On:	Price-to-Tangible Book Value Multiple	Price-to-LTM Earnings Multiple(1)	Premium-to-Core Deposits Multiple(2)
Total Deal Value	187.3%	31.7	4.9%
DCF Analysis – Terminal P/E Multiple			
Midpoint	164.9%	27.9	1.0%
DCF Analysis – Terminal P/TBV Multiple			
Midpoint	152.3%	25.8	(1.2)%

(1)

HCSB’s LTM earnings reflect 2017 earnings estimates from management and excludes the non-core impact associated with the reversal of HCSB’s approximate \$20.8 million valuation allowance on its deferred tax asset.

(2)

HCSB’s tangible common equity has been adjusted to reflect the reversal of HCSB’s approximate \$20.8 million valuation allowance on its deferred tax asset.

Hovde noted that while the discounted cash flow present value analysis is a widely used valuation methodology, it relies on numerous assumptions, including asset and earnings growth rates, projected dividend payouts, terminal values and discount rates. Hovde’s analysis does not purport to be indicative of the actual values or expected values of HCSB’s common stock.

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United Comparable Companies Analysis: Hovde used publicly available information to compare selected financial and trading information for United and a group of 10 publicly-traded financial institutions selected by Hovde which was based on publicly-traded banks in the Southeast United States with total assets between \$7.5 billion and \$20.0 billion, LTM ROAA greater than 0.90%, LTM ROATCE greater than 10.0% and TCE/TA greater than 8.0%:

Bank of the Ozarks, Inc.	United Bankshares, Inc.
Pinnacle Financial Partners, Inc.	Home Bancshares, Inc.
WesBanco, Inc.	FCB Financial Holdings, Inc.
South State Corporation	Renasant Corporation
Union Bankshares Corporation	TowneBank

The analysis compared publicly available financial and market trading information for United and the data for the 10 financial institutions identified above as of and for the most recent twelve-month period which was publicly available. The table below compares the data for United and the median data for the 10 financial institutions identified above, with pricing data as of April 7, 2017.

	Market Cap (\$M)	Price/ Tangible Book Value	Price/ LTM EPS	Price/ 2017E EPS	Dividend Yield	YTD/Price Change	Two Year Total Return
United	\$ 1,894.1	205.8%	19.1x	16.7x	1.35%	(9.9)%	44.5%
Comparable Companies:							
Median	\$ 2,300.1	250.6%	20.5x	18.4x	1.64%	(5.3)%	42.0%

United fell within the range of pricing metrics of comparable companies. No company used as a comparison in the above analyses is identical to United. Accordingly, an analysis of these results is not strictly mathematical. Rather, it involves complex considerations and judgments concerning differences in financial and operating characteristics of the companies.

Accretion / Dilution Analysis: Hovde performed pro forma merger analyses that combined projected income statement and balance sheet information of HCSB and United. Assumptions regarding the accounting treatment, acquisition adjustments and cost savings were used to calculate the financial impact that the merger would have on certain projected financial results of United. In the course of this analysis, Hovde used the median FactSet consensus estimates for earnings estimates for United for the years ending December 31, 2017 and December 31, 2018 and used earnings estimates provided by HCSB's management for HCSB for the years ending December 31, 2017 and December 31, 2018. This analysis indicated that the merger is expected to be accretive by one cent per share to United's consensus estimated earnings per share of \$1.80 in 2018 and accretive by one cent per share to United's consensus estimated earnings per share of \$1.89 in 2019. The analysis also indicated that the merger is expected to be dilutive to tangible book value per share for United by two cents per share in 2018 and by one cent per share in 2019 and that United would maintain capital ratios in excess of those required for United to be considered well-capitalized under existing regulations. For all of the above analyses, the actual results achieved by HCSB and United prior to and following the merger will vary from the projected results, and the variations may be material.

Other Factors and Analyses. Hovde took into consideration various other factors and analyses, including but not limited to: current market environment; merger and acquisition environment; movements in the common stock valuations of selected publicly-traded banking companies; and movements in the S&P 500 Index.

Conclusion. Based upon the foregoing analyses and other investigations and assumptions set forth in its opinion, without giving specific weightings to any one factor or comparison, Hovde determined that the merger consideration to be paid in connection with the merger is fair from a financial point of view to HCSB's shareholders. Each shareholder is encouraged to read Hovde's fairness opinion in its entirety. The full text of this fairness opinion is included as Appendix C to this document.

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The Merger Consideration

Holders of HCSB common stock will receive 0.0050 shares of United common stock in exchange for each of their shares of HCSB common stock in the merger.

United will not issue fractional shares in the merger. Instead, you will receive a cash payment, without interest, for the value of any fraction of a share of United common stock that you would otherwise be entitled to receive in an amount equal to such fractional part of a share of United common stock multiplied by the purchase price per share of HCSB common stock as determined by multiplying (i) the exchange ratio by (ii) the closing price for United common stock on the NASDAQ Global Select Market trading day immediately preceding the effective time of the merger.

The Merger Agreement

The material features of the merger agreement are summarized below:

Effective Date

The merger agreement provides that the merger will be effective upon the date and time specified in the Certificate of Merger reflecting the merger filed with the Secretary of State of the State of Georgia and the Articles of Merger reflecting the merger filed with the Secretary of State of the State of South Carolina.

The merger and the bank merger must be approved by the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Department of Banking and Finance of the State of Georgia and the South Carolina State Board of Financial Institutions. Management of United and HCSB anticipate that the merger will become effective during the third quarter of 2017.

Terms of the Merger

If HCSB shareholders approve the merger agreement, and subject to the receipt of required regulatory approvals and the satisfaction of the other closing conditions set forth in the merger agreement, HCSB will be merged with and into United. In connection with the merger, HCSB shareholders (other than shareholders holding dissenting shares or cancelled shares) will receive 0.0050 shares of United common stock in exchange for each share of HCSB common stock. United shareholders will continue to hold their existing United common stock.

If, prior to the effective time, either party should change the number of its outstanding shares as a result of a stock split, reverse stock split, stock dividend, recapitalization, reclassification, or similar transaction, then a proportionate and appropriate adjustment will be made to the number of shares of United common stock to be delivered pursuant to the merger in exchange for a share of HCSB common stock.

If the merger is completed, HCSB will be merged with and into United. Following the merger, the articles of incorporation, bylaws, corporate identity, and existence of United will not be changed, and HCSB will cease to exist as a separate entity. Following the merger, HCSB's wholly-owned South Carolina bank subsidiary, Horry County State Bank, will be merged with and into the Bank, a wholly-owned Georgia bank subsidiary of United. The Bank will be the surviving bank.

Registration of United Common Stock

As a condition to the merger, United agreed to register with the SEC the shares of United common stock to be exchanged for shares of HCSB common stock and to maintain the effectiveness of such registration through the issuance of such shares in connection with the closing of the merger. However, such registration will not cover resales of United common stock by any former holders of HCSB common stock, and United is under no obligation to maintain the effectiveness of such registration, or to prepare and file any post-effective amendments to such registration, after the issuance of such shares in connection with the closing of the merger.

Treatment of HCSB Restricted Stock

All awards of shares of HCSB common stock subject to vesting, repurchase or other lapse restriction granted pursuant to the HCSB Financial Corporation 2016 Equity Incentive Plan, whether vested or

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unvested, that are outstanding as of immediately prior to the effective time of the merger, shall become fully vested and shall be cancelled and converted automatically into the right to receive the merger consideration in respect of each share of HCSB common stock underlying such restricted share award.

Representations and Warranties Made by United and HCSB in the Merger Agreement

United and HCSB have made certain customary representations and warranties to each other in the merger agreement. For information on these representations and warranties, please refer to the merger agreement attached as Appendix A. The representations and warranties in the merger agreement do not survive the effective time of the merger.

The representations and warranties included in the merger agreement were made only for purposes of the merger agreement and as of specific dates, are solely for the benefit of United and HCSB, may be subject to limitations, qualifications or exceptions agreed upon by the parties, including those included in confidential disclosures made for the purposes of, among other things, allocating contractual risk between United and HCSB rather than establishing matters as facts, and may be subject to standards of materiality that differ from those standards relevant to investors.

The representations and warranties and other provisions of the merger agreement should not be read alone, but instead should be read only in conjunction with the information provided elsewhere in this document and in the documents incorporated by reference into this document. United and HCSB will provide additional disclosures in their public reports to the extent they are aware of the existence of any material facts that are required to be disclosed under federal securities laws and that might otherwise contradict the terms and information contained in the merger agreement and will update such disclosure as required by federal securities laws.

Certain representations and warranties of United and HCSB are qualified as to “materiality” or “material adverse effect.” For purposes of the merger agreement, a “material adverse effect,” when used in reference to either United or HCSB, shall mean any change, event, development, violation, effect or circumstance which, individually or in the aggregate, (i) has, or is reasonably likely to have, a material adverse effect on the business, operations, properties, assets, financial condition or prospects of United or HCSB, respectively, on a consolidated basis, or (ii) prevents or materially impairs, or would be reasonably likely to prevent or materially impair, the ability of United or HCSB, respectively, to timely consummate the transactions contemplated by the merger agreement or to perform its agreements or covenants under the merger agreement; provided, that a “material adverse effect” shall specifically exclude any adverse effect attributable to or resulting from:

- any change in banking laws, rules or regulations of general applicability;
- any change in U.S. generally accepted accounting principles or regulatory accounting principles applicable to banks or their holding companies generally;
- any action or omission expressly required by the merger agreement or taken with the express prior written consent of the other party to the merger agreement;
- general changes in national economic, monetary, market or financial conditions affecting financial institutions, including changes in prevailing interest rates, inflation, credit markets, or capital market conditions, except, in all cases, to the extent such changes disproportionately affect HCSB;
- changes in national political conditions, including the outbreak or escalation of acts of terrorism; or
- the public disclosure of the merger agreement or the transactions contemplated by the merger agreement.

Termination and Conditions of Closing

The merger agreement may be terminated at any time either before or after approval of the merger agreement by the shareholders of HCSB, but not later than the effective date of the merger:

(1)

by mutual written agreement of United and HCSB;

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(2)

by either party, if after the date of the merger agreement, any events or occurrences have occurred and are continuing that, individually or in the aggregate have had or would reasonably be expected to have a material adverse effect on the other party;

(3)

by either party, if the terms, covenants or conditions of the merger agreement to be complied with or performed by the other party before the closing have not been substantially complied with or substantially performed at or before the closing date and such noncompliance or nonperformance has not been waived by such party, or in the event of a material breach by the other party of any covenant, agreement, or obligation contained in the merger agreement which breach has not been cured within twenty days after the giving of written notice to the other party of such breach or, if such breach is not capable of being cured within twenty days, the other party has not begun to cure such breach within twenty days after such written notice;

(4)

by United, if it learns of any fact or condition not disclosed in the merger agreement, the disclosure memorandum delivered in connection with the merger agreement, or HCSB's financial statements, which fact or condition was required to be disclosed by HCSB pursuant to the provisions of the merger agreement and which fact or condition would reasonably be expected to have, either individually or in the aggregate, a material adverse effect on HCSB or United;

(5)

by either party, if any regulatory approval required to be obtained has been denied by the relevant governmental entity or any governmental entity of competent jurisdiction has issued a final, nonappealable injunction permanently enjoining or otherwise prohibiting the consummation of the transactions contemplated by the merger agreement;

(6)

by United, if the holders of more than 10% of the outstanding shares of HCSB common stock elect to exercise their statutory right to dissent from the merger and demand payment in cash for the "fair value" of their shares of HCSB common stock;

(7)

by either party, if the closing date shall not have occurred on or before January 2, 2018, unless the failure of the closing to occur by such date is due to the failure of the party seeking to terminate the merger agreement to perform or observe the covenants and agreements of such party under the merger agreement;

(8)

by either party, if the merger agreement is not approved by any required vote of the HCSB shareholders as required by applicable law; or

(9)

by HCSB if, prior to obtaining the required vote of the HCSB shareholders, the board of directors has effected an adverse recommendation change.

HCSB may only terminate the merger agreement pursuant to (9) listed above so long as HCSB complies with its obligations discussed under "Limitation on Discussion with Others" below and:

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HCSB's board of directors determines in good faith, after consultation with HCSB's financial advisor and outside counsel, that it has received an acquisition proposal (that did not result from a breach of the merger agreement) that is a superior proposal;

- HCSB's board of directors determines in good faith, after consultation with HCSB's outside counsel, that a failure to accept such superior proposal would be reasonably likely to constitute a breach of the fiduciary duties of the members of the board of directors of HCSB;
- HCSB's board of directors provides written notice to United of its receipt of the superior proposal and its intent to announce an adverse recommendation change on the third business day following delivery of such notice, which notice shall specify the material terms and conditions of the superior proposal (it being understood that any amendment to any material term of such superior proposal shall require a new written notice);
- after providing such written notice, HCSB negotiates in good faith with United (if requested by United) and provides United reasonable opportunity during the three business day period following the written notice to make such adjustments in the terms and conditions of the merger agreement as would enable HCSB's board of directors to proceed without an adverse recommendation change (provided, however, that United shall not be required to propose any such adjustments); and

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- HCSB's board of directors, following such three business day period, determines in good faith, after consultation with HCSB's financial advisor and outside counsel, that such acquisition proposal nonetheless continues to constitute a superior proposal and that failure to take such action would be reasonably likely to constitute a breach of the fiduciary duties of the members of the board of directors of HCSB.

The term "adverse recommendation change" means (i) the withdrawal, qualification or modification, or public proposal to withdraw, qualify or modify, in a manner adverse to United, the recommendation of the board of directors of HCSB that the HCSB shareholders adopt and approve the merger agreement and the transactions contemplated by the merger agreement, including the merger, or (ii) the approval or recommendation, or public proposal to approve or recommend, any acquisition proposal.

The term "acquisition proposal" means (i) any proposal or offer with respect to a merger, joint venture, partnership, consolidation, dissolution, liquidation, tender offer, recapitalization, reorganization, rights offering, share exchange, business combination or similar transaction, involving HCSB or any of its subsidiaries; and (ii) any acquisition by any person resulting in, or proposal or offer, which, if consummated, would result in, any person becoming the beneficial owner, directly or indirectly, of 10% or more of the total voting power of any class of equity securities of HCSB or any of its subsidiaries, or 10% or more of the consolidated total assets of HCSB, in each case, other than the transactions contemplated by the merger agreement.

The term "superior proposal" means any acquisition proposal with respect to which the board of directors of HCSB (i) determines in good faith that such acquisition proposal, if accepted, is reasonably likely to be consummated on a timely basis, taking into account all legal, financial, regulatory and other aspects of the acquisition proposal and the third party making the acquisition proposal, and (ii) determines in good faith judgment (based on, among other things, the advice of HCSB's financial advisor) to be more favorable to HCSB's shareholders than the merger taking into account all relevant factors (including whether, in the good faith judgment of the board of directors of HCSB, after obtaining advice of HCSB's financial advisor, the third party making such acquisition proposal is reasonably able to finance the transaction and close it timely, and any proposed changes to the merger agreement that may be proposed by United in response to such acquisition proposal).

HCSB must pay to United a termination fee of approximately \$2.0 million if, while an acquisition proposal is outstanding or after such an offer has been accepted, (i) either party terminates the merger agreement pursuant to (7) listed above, (ii) HCSB terminates the merger agreement other than pursuant to (2) or (3) listed above, or (iii) United terminates the merger agreement after an adverse recommendation change.

The following summarizes the required conditions of closing:

- approval of the merger agreement by at least two-thirds of the issued and outstanding shares of HCSB common stock designated as voting common stock and at least a majority of the issued and outstanding HCSB common stock designated as non-voting common stock;
- approval of the merger and the bank merger by all government authorities, bodies or agencies having jurisdiction over such transactions, including the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Department of Banking and Finance of the State of Georgia and the South Carolina State Board of Financial Institutions, and the expiration of all applicable waiting or similar periods required by law;
- no order, injunction, decree or judgment preventing the consummation of the merger or the other transactions contemplated by the merger agreement issued by any court or governmental body or agency of competent jurisdiction or other legal restraint or prohibition preventing the consummation of the merger or the other transactions contemplated by the merger agreement shall be in effect;
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no statute, rule, regulation, order, injunction or decree shall have been enacted, entered, promulgated or enforced by any governmental entity which prohibits or makes illegal consummation of the merger;

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- effectiveness of the registration statement of United relating to the shares of United common stock to be issued to HCSB shareholders in the merger, of which this document forms a part, and no stop order shall have been entered with respect thereto;
- the accuracy of the representations and warranties of each party in the merger agreement as of the date of the merger agreement and the day on which the merger is completed, subject to the materiality standards provided in the merger agreement, except, at each such time, as a result of changes or events expressly permitted or contemplated by the merger agreement or where the failure to be true and correct, either individually or in the aggregate, is not reasonably likely to have a material adverse effect on United;
- the performance and compliance by each party in all material respects of all agreements and covenants required to be performed by it at or prior to the effective time of the merger under the merger agreement;
- the delivery of officers' certificates, secretary's certificates and certificates of valid existence to United and HCSB by the other;
- receipt by each of United and HCSB of an opinion of its respective legal counsel as to certain tax matters; and
- payment of the merger consideration by United.

Surrender of Certificates

A letter of transmittal and instructions for effecting the surrender of certificates representing such holder's shares of HCSB common stock to United's exchange agent, Continental Stock Transfer & Trust Company, in order to receive payment of the consideration from United in connection with the merger will be mailed no later than five business days after the closing date of the merger to each holder of HCSB common stock of record at the effective time of the merger.

Upon the surrender of certificates representing such holder's shares of HCSB common stock (or affidavits of loss in lieu thereof) for cancellation to United's exchange agent and delivery of the letter of transmittal, duly executed and properly completed, with respect to such certificates, the record holder of such certificates will be entitled to receive in exchange therefore the merger consideration to be paid therefor pursuant to the terms of the merger agreement. No interest will be paid or accrue on any cash payable upon surrender of any certificate representing shares of HCSB common stock.

Until a holder delivers HCSB common stock to United, the holder may not receive payment of any dividends or other distributions on shares of United common stock into which his, her, or its shares of HCSB common stock have been converted, if any.

Required Shareholder Approval and Consent

The holders of at least two-thirds of the outstanding shares of HCSB common stock designated as voting common stock and at least a majority of the outstanding shares of HCSB common stock designated as non-voting common stock must approve the merger agreement for the merger to be completed. Abstentions from voting and broker non-votes will be included in determining whether a quorum is present and will have the effect of a vote against the merger agreement.

As of [•], 2017, the record date for determining the HCSB shareholders entitled to notice of and to vote at the special meeting, the outstanding voting securities of HCSB consisted of [•] shares of voting common stock and [•] shares of non-voting common stock, with each registered holder of HCSB common stock being entitled to one vote per share.

All of the directors of HCSB have agreed to vote their shares in favor of the merger. As of the record date, HCSB's directors owned [•] shares, or [•]%, of the outstanding HCSB voting common stock.

Expenses

All expenses incurred by United in connection with the merger, including all fees and expenses of its agents, representatives, counsel and accountants and the fees and expenses related to filing these materials and all regulatory applications with state and federal authorities will be paid by United. All expenses

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incurred by HCSB in connection with the merger agreement, including all fees and expenses of its agents, representatives, counsel and accountants will be paid by HCSB.

Conduct of Business of HCSB Pending Closing

The merger agreement provides that, pending consummation of the merger, HCSB will, except as required by applicable law, as expressly required or contemplated by the merger agreement, or with the prior written consent of United:

- conduct its business only in the ordinary course, without the creation of any indebtedness for borrowed money (other than deposit and similar accounts and customary credit arrangements between banks in the ordinary course of business);
- not enter into any new line of business or change in any material respect its lending, investment, underwriting, risk and asset liability management and other banking and operating, securitization and servicing policies (including any change in the maximum ratio or similar limits as a percentage of its capital exposure applicable with respect to its loan portfolio or any segment thereof);
- maintain its properties and assets in good operating condition, ordinary wear and tear excepted;
- maintain and keep in full force and effect all material insurance;
- make no change in the authorized or issued capital stock or other securities of HCSB, or issue or grant any right or option to purchase or otherwise acquire any of the capital stock or other securities of HCSB;
- not declare or make any dividend, distribution or payment in respect to the HCSB common stock,
- make no amendment to its articles of incorporation or bylaws, and maintain its corporate existence and powers;
- not acquire by merging or consolidating with, or by purchasing a substantial portion of the assets of, or by any other manner, any business or any corporation, partnership, association or other entity or division thereof or otherwise acquire or agree to acquire any assets which are material, individually or in the aggregate, to HCSB;
- not sell, mortgage, lease, buy or otherwise acquire, transfer or dispose of any real property or interest therein (except for sales in the ordinary course of business, including sales of other real estate owned and properties under contract at or above HCSB's carrying value as of the date of the merger agreement) or, except in the ordinary course of business, sell or transfer, mortgage, pledge or subject to any lien any other tangible or intangible asset;
- provide United with five business days' prior notice before execution of an agreement to make any loan or extension of credit in an amount in excess of \$500,000 (excluding any loan or extension of credit of a smaller amount on an outstanding loan or line of credit in excess of \$500,000);
-

not renew or amend any existing loan or extension of credit that is characterized as “Special Mention”, “Substandard”, “Doubtful”, or “Loss” in the books and records of HCSB; provided, however, that HCSB may amend or renew any existing loan that is characterized as “Special Mention”, “Substandard”, “Doubtful”, or “Loss”, in the event United shall not have disapproved of such request in writing within five (5) business days upon receipt of such request from HCSB;

- make no material change to its methodology for determining its allowance for loan and lease losses;
- make no change in the banking and safe deposit arrangements of HCSB, other than in the ordinary course of business, consistent with past practice;
- not make application for the opening, relocation or closing of any, or open, relocate or close any, branch office, loan production office or other significant office or operations facility of HCSB;

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- except in the ordinary course of business, not terminate, materially amend or waive any material right under any material contract or enter into any contract that would constitute a material contract if it were in effect on the date of the merger agreement;
- maintain the books and records of HCSB in the usual, regular and ordinary course;
- not, and will not permit Horry County State Bank to, prepare or file any tax return inconsistent with past practice or, on any tax return, take any position, make any election, or adopt any method inconsistent with positions taken, elections made or methods used in preparing or filing similar tax returns in prior periods, make or change any express or deemed election related to taxes, change an annual accounting period, adopt or change any method of accounting, file an amended tax return, surrender any right to claim a refund of taxes, enter into any closing agreements with respect to tax, or consent to any extension or waiver of the limitation period applicable to any tax proceedings related to HCSB or Horry County State Bank;
- promptly advise United orally and in writing of any change or event having, or which would reasonably be expected to have, a material adverse effect;
- file all reports required to be filed with any regulatory or governmental agencies between the date of the merger agreement and the closing date of the merger and deliver to United copies of all such reports promptly after the same are filed;
- not adopt any new benefit plans or programs or amend any existing benefit plans or programs, the effect of which is to increase benefits to any current or former employees, directors, officers or independent contractors or their descendants or beneficiaries or the liabilities of HCSB or its successors; and
- not grant or enter into any new employment agreement, retention agreement, severance pay, termination pay, retention pay, change in control or transaction or deal bonus or arrangement or other benefit plan.

Limitation on Discussions with Others

The merger agreement provides that HCSB may not, and may not authorize or permit any of its affiliates, officers, directors, employees, agents or advisors to, directly or indirectly, solicit or entertain offers from, negotiate with or in any manner encourage, discuss, accept or consider an acquisition proposal (as defined above) of any other third party. In addition, the merger agreement requires HCSB to immediately cease and cause to be terminated any previously undertaken or ongoing activities, discussions or negotiations with any other third party with respect to any acquisition proposal. Furthermore, if HCSB or any of its affiliates, officers, directors, employees, agents, or advisors receives any communication regarding an acquisition proposal between the date of the merger agreement and the closing date of the merger, then HCSB shall immediately notify United of the receipt of such acquisition proposal. Notwithstanding the foregoing, prior to obtaining the approval of the shareholders of HCSB, the merger agreement does not prohibit HCSB from furnishing nonpublic information regarding HCSB to, or entering into a confidentiality agreement or discussions or negotiations with, any third party in response to a bona fide, unsolicited written acquisition proposal submitted by such third party if: (i) the acquisition proposal did not result from a breach of the merger agreement, (ii) HCSB's board of directors has determined in good faith, after consultation with its financial advisors and outside counsel, that such acquisition proposal constitutes or is reasonably likely to result in a superior

proposal, (iii) HCSB's board of directors determines in good faith, after consultation with its outside counsel, that a failure to take such action would be reasonably likely to result in a breach of the fiduciary duties of the members of the HCSB board of directors, (iv) (A) HCSB gives United prompt (but in no event later than 24 hours) notice (which notice may be oral, and, if oral, shall be subsequently confirmed in writing) (1) of HCSB's or any of its directors, officers, employees, representatives, agents or advisors receipt of any acquisition proposal (which notice shall include the identity of such person or group and the material terms and conditions of any proposals or offers, including, if applicable, copies of any written requests, proposals or offers, including proposed agreements) and (2) of HCSB's furnishing nonpublic information to, or entering into discussions or negotiations with, such person or group, and (B) HCSB receives from such person or group an executed

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confidentiality agreement containing terms no less favorable to HCSB than the terms of the confidentiality agreement entered into between HCSB and United, and (v) contemporaneously with, or promptly after, furnishing any such nonpublic information to such person or group, HCSB furnishes such nonpublic information to United (to the extent such nonpublic information has not been previously furnished by HCSB to United). In addition to the foregoing, HCSB shall keep United reasonably informed on a prompt basis of the status and material terms of any such acquisition proposal, including any material amendments or proposed amendments as to price and other material terms thereof and any change in HCSB's intentions with respect to the transactions contemplated by the merger agreement.

Interests of the Directors and Officers of HCSB in the Merger

In considering the recommendation of the HCSB Board of Directors with respect to the merger agreement, HCSB shareholders should be aware that the executive officers and directors of HCSB have certain interests in the merger that may be different from, or in addition to, the interests of HCSB shareholders generally. The HCSB Board of Directors was aware of these interests and considered them, among other matters, in approving the merger agreement and the transactions contemplated thereby and making its recommendation that HCSB shareholders vote to approve the merger agreement. These interests are described in further detail below. For purposes of all HCSB agreements and plans described below, the completion of the merger contemplated by the merger agreement will constitute a change of control, change in control or term of similar meaning.

Indemnification and Insurance

To the fullest extent permitted by applicable law, United has agreed that for six years after the completion of the merger, it will (subject to certain limitations) indemnify, and provide advance of expenses to, present and former HCSB directors and officers with respect to liabilities arising from acts or omissions occurring prior to the merger. Prior to the effective time of the merger, United will purchase, or direct HCSB to purchase, an extended reporting period endorsement under HCSB's existing directors' and officers' liability insurance coverage for acts or omissions occurring prior to the merger effective time by such directors and officers, which shall maintain such HCSB directors' and officers' liability insurance policy in effect for a period of six years after the merger effective time; provided that United shall not be obligated to make aggregate annual premium payments for such six-year period an amount in excess of 250% of the annual premium payments on such HCSB directors' and officers' liability insurance policy in effect as of the date of the merger agreement. If the amount of the premiums necessary to maintain or procure such insurance coverage exceeds such 250% maximum premium amount, then United shall use its reasonable best efforts to maintain the most advantageous policies of directors' and officers' liability insurance obtainable for a premium equal to such 250% maximum premium amount.

Existing HCSB Employment Agreements

HCSB is currently a party to amended and restated employment agreements, which we refer to as the employment agreements, with each of Jan H. Hollar, J. Rick Patterson, and W. Jack McElveen. These agreements provide that if HCSB terminates Ms. Hollar, Mr. Patterson, or Mr. McElveen without cause or any of them terminates for good reason within 12 months following a change in control, the executive will be entitled to (i) severance compensation in an amount equal to 299% of his or her then current annual base salary plus any bonus earned through the date of termination (including any amounts awarded for previous years but which were not yet paid) and (ii) continued participation, in accordance with the terms of the applicable benefit plans, in HCSB's group health plan pursuant to plan continuation rules under COBRA. In addition, these agreements provide that any restrictions on any outstanding equity incentive awards (including restricted stock) granted to the executives will lapse and such incentive awards will immediately become 100% vested.

Under these agreements, if any severance payments are deemed to constitute "excess parachute payments" within the meaning of Section 280G of the Internal Revenue Code of 1986, as amended, then the agreements include a "best net after tax" compliance provision. Under these employment agreements, the best net after tax provision will cause the executive's severance payment to either be (i) reduced to an

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amount which does not trigger the Section 280G-related excise tax or (ii) paid in full, depending on which payment would result in the executive receiving the greatest after tax payment. If paid in full thus triggering the excise tax, the executive would be liable for any such tax owed on the parachute payments.

Each employment agreement also provides that during the term of employment and for a period of 24 months for Ms. Hollar and Mr. Patterson and for a period of 12 months for Mr. McElveen following termination, the executive may not (a) compete with HCSB or any of its affiliates by, directly or indirectly, forming, serving as an organizer, director or officer of, or consultant to, or acquiring or maintaining more than a 1% passive investment in, a depository financial institution or holding company therefor if such depository institution or holding company has one or more offices within 30 miles from the main office of Horry County State Bank or any branch or loan production office of Horry County State Bank, subject to certain exclusions contained in the employment agreement, (b) solicit Horry County State Bank's customers with which the executive had material contact in connection with products or services provided by Horry County State Bank for the purpose of providing financial services, or (c) solicit Horry County State Bank's employees or consultants.

Severance and Release Agreements

Each of Ms. Hollar and Messrs. Patterson and McElveen are expected to enter into a severance and release agreement, which we refer to as the severance agreements, with United. The purpose of these agreements is to provide severance pay to Ms. Hollar and Messrs. Patterson and McElveen in full and complete satisfaction of the obligations to Ms. Hollar and Messrs. Patterson and McElveen under their existing employment agreements with HCSB, which are summarized above. For an estimate of the amounts that would be payable in connection with the merger to each of Ms. Hollar and Messrs. Patterson and McElveen pursuant to the severance agreements, see "Quantification of Potential Payments to HCSB's Named Executive Officers in Connection with the Merger" below. In exchange for the payments under the severance agreements, Ms. Hollar and Messrs. Patterson and McElveen will release and discharge United from any and all claims, demands, and liabilities that Ms. Hollar and Messrs. Patterson and McElveen have ever had or may have against United or United's officers, directors, or employees, both known and unknown, including, but not limited to, any and all claims, demands, and liabilities based on employment or the termination of the employment relationship. Ms. Hollar and Messrs. Patterson and McElveen will also agree not to file or consent to the filing of any lawsuit, complaint, or action against United, or United's officers, directors, or employees arising out of or in any way related to her or his employment or the termination of her or his employment.

Treatment of Outstanding HCSB Restricted Stock

Each share of HCSB common stock subject to restrictions on transfer and/or forfeiture granted under the HCSB 2016 Equity Incentive Plan that is issued and outstanding immediately prior to the effective time will become fully vested and will be converted automatically into and represent the right to receive the merger consideration, subject to any income or employment tax withholding required under the Internal Revenue Code of 1986, as amended, or any provision of applicable law.

As of the date of this document, Ms. Hollar, Mr. Patterson, and Mr. McElveen held 12,000,000 shares, 7,500,000 shares, and 5,000,000 shares, respectively, of unvested HCSB restricted stock. For an estimate of the amounts that would be payable in connection with the merger to each of Ms. Hollar and Messrs. Patterson and McElveen on settlement of their unvested equity-based awards, see "Quantification of Potential Payments to HCSB's Named Executive Officers in Connection with the Merger" below.

Other than the named executive officers, no HCSB directors hold unvested HCSB equity awards and two HCSB executive officers hold 3,250,000 shares of unvested HCSB restricted stock.

Employment with United

As of the date of this document, no named executive officer of HCSB has been offered employment with United.

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Quantification of Potential Payments to HCSB's Named Executive Officers in Connection with the Merger

The following table and related footnotes are intended to comply with Item 402(t) of Regulation S-K under the Securities Exchange Act of 1934, which requires disclosure of information about the payments and benefits that each of HCSB's "named executive officers," which consists of its principal executive officer, principal financial officer and the other most highly compensated executive officer, will or may receive that are based on or otherwise relate to the merger ("merger-based compensation"). This merger-based compensation is referred to as "golden parachute" compensation by the applicable SEC disclosure rules. This compensation is subject to a non-binding advisory vote of HCSB's holders of voting common stock, as described in "PROPOSAL NO. 2 — ADVISORY VOTE ON MERGER-RELATED COMPENSATION."

The amounts indicated below are estimates based on multiple assumptions that may or may not actually occur or be accurate on the relevant date, including an assumption that the employment of each of the three named executive officers is terminated immediately following the completion of the merger, and do not reflect certain compensation actions that may occur before the completion of the merger. For purposes of calculating such amounts, we have assumed July 3, 2017 as the closing date of the merger.

Name	Cash \$(1)	Equity \$(2)	Pension/ NQDC (\$)	Perquisites/Tax Benefits (\$)	Reimbursements (\$)	Other \$(3)	Total (\$)
Jan H. Hollar	\$ 771,217	\$ 511,461	—	—	—	\$ 20,000	\$ 1,302,678
J. Rick Patterson	\$ 685,526	\$ 319,663	—	—	—	—	\$ 1,005,189
William J. McElveen, Jr.	\$ 685,526	\$ 213,109	—	—	—	\$ 20,000	\$ 918,635

(1)

The amounts set forth represent double trigger payments (i.e., amounts triggered by a change in control for which payment is conditioned upon the executive officer's termination without cause or resignation for good reason within a twelve month time period following the change in control) due to the named executive officer pursuant to their employment agreements. These amounts also include minimum pro-rata annual bonuses due to Ms. Hollar, Mr. Patterson and Mr. McElveen, respectively, for the year in which the change in control occurs pursuant to their employment agreements.

(2)

The amounts set forth represent the value attributable to the vesting of the registered stock previously granted to Ms. Hollar, Mr. Patterson, and Mr. McElveen that will vest immediately upon completion of the merger. These values were determined based on the acceleration of vesting upon a change in control of all unvested restricted stock assuming the following: (i) a fair market value as of July 3, 2017 (the intended date of the change in control) of \$0.145 and (ii) both performance measures had already been met but none of the annual time vesting milestones had been achieved.

(3)

The amounts set forth represent the value attributable to the right of each of the named executive officers to continued participation, in accordance with the terms of the applicable benefit plans, in HCSB's group health plan pursuant to plan continuation rules under COBRA for the legally required periods, pursuant to their employment agreements. These values are estimated to be \$20,000 for each executive, except for Patterson who does not participate in the HCSB health plan and would decline any COBRA benefits.

Differences in Legal Rights between Shareholders of HCSB and United

Following the merger you will no longer be a HCSB shareholder and, if you receive shares of United following the merger, your rights as a shareholder will no longer be governed by HCSB's articles of incorporation and bylaws and the SCBCA. You will be a United shareholder and your rights as a United shareholder will be governed by United's

articles of incorporation and bylaws and the Georgia Business Corporation Code. Your former rights as a HCSB shareholder and your new rights as a United shareholder are different in certain ways, including the following:

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	HCSB Shareholder Rights	United Shareholder Rights
Authorized, Issued and Outstanding Capital Stock	The authorized capital stock of HCSB currently consists of 500,000,000 shares of voting common stock, \$0.01 par value per share, 150,000,000 shares of non-voting common stock, \$0.01 par value per share, and 5,000,000 shares of preferred stock, \$0.01 par value per share. As of [•], 2017, [•] shares of common stock were issued and outstanding, [•] shares of non-voting common stock were issued and outstanding and no shares of preferred stock were issued and outstanding.	The authorized capital stock of United currently consists of 150,000,000 shares of common stock, \$1.00 par value per share, 26,000,000 shares of non-voting common stock, \$1.00 par value per share, and 10,000,000 shares of preferred stock, \$1.00 par value per share. As of [•], 2017, [•] shares of common stock were issued and outstanding, no shares of non-voting common stock were issued and outstanding and no shares of preferred stock were issued and outstanding.
Shareholder Ability to Call Special Meetings	The bylaws of HCSB provide that special meetings may be called by the Chief Executive Officer, the President, the Chairman of the Board of Directors or a majority of the Board of Directors, and by the holders of at least 10% of all the votes entitled to be cast on any issue proposed to be considered at such special meeting.	The bylaws of United provide that special meetings may be called by the Board of Directors, the Chairman of the Board of Directors, the Chief Executive Officer, the President or the Chief Financial Officer, and by the holders of at least 25% of the shares of shares entitled to vote on the matter considered at the special meeting.
Advance Notice Requirements for Shareholder Proposals	The bylaws of HCSB provide that for business to be brought properly before an annual meeting by a shareholder, the shareholder must have given timely notice in writing to the Secretary. To be timely, the notice must be given, either by personal delivery or by United States mail, postage prepaid, return receipt requested, to the Secretary not less than 30 nor more than 60 days in advance of the annual meeting. A shareholder's notice shall set forth for each matter the shareholder proposes to bring before the annual meeting (i) a description of the business desired to be brought before the annual meeting (including the specific proposal(s) to be presented) and the reasons for conducting such business at the annual meeting; (ii) the name and record address of the shareholder proposing such business; (iii) the class and number of shares that are owned of record, and the class and number of shares that are held beneficially, but not held of record, by the shareholder as of the record date of the meeting; and (iv) any interest of the shareholder in such business. HCSB shareholders do not have the ability to submit a	The bylaws of United provide that for business to be brought properly before an annual meeting by a shareholder, the stockholder must have given timely notice of the business in writing to the Secretary. To be timely, the notice must be delivered or mailed to and received at the principal offices of United on or before the later to occur of (i) 14 days prior to the annual meeting or (ii) five days after notice of the meeting is provided to the shareholders. A shareholder's notice must set forth (i) a brief description of each matter of business the shareholder proposes to bring before the meeting and the reasons for conducting that business at the meeting; (ii) the name, as it appears on United's books, and address of the shareholder proposing the business; (iii) the series or class and number of shares of United's capital stock that are beneficially owned by the shareholder; and (iv) any material interest of the shareholder in the proposed business. United shareholders do not have the ability to submit a proposal for a special meeting of shareholders.

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	HCSB Shareholder Rights	United Shareholder Rights
Number of Directors	<p>proposal for a special meeting of shareholders.</p> <p>The bylaws of HCSB provide that the number of directors may be increased or decreased by action of the HCSB Board of Directors at any time, but in no event shall the number be less than five or greater than 25. If, in any case after proxy materials for an annual meeting have been mailed, any person nominated becomes unable or unwilling to serve, the number of authorized directors shall automatically be reduced by a number equal to the number of such persons. HCSB's Board of Directors currently has seven directors.</p>	<p>The bylaws of United provide that the number of directors on United's Board of Directors may range from eight to fourteen. The number of directors may be increased or decreased from time to time by the Board of Directors by resolution, but no decrease shall have the effect of shortening the term of an incumbent director. United's Board of Directors currently has nine directors.</p>
Removal of Directors	<p>The bylaws of HCSB provide that directors may be removed with or without cause by the affirmative vote of the holders of at least a majority of the shares entitled to vote at an election of directors.</p>	<p>The articles of incorporation of United provide that directors may be removed only for cause and only upon the affirmative vote of the holders of two-thirds of the issued and outstanding shares entitled to vote on the removal.</p>
Approval of Business Transactions	<p>The SCBCA provides that, unless the articles of incorporation require a different vote, a plan of merger or share exchange may only be approved by (i) two-thirds of the votes entitled to be cast on the plan, regardless of the class or voting group to which the shares belong and (ii) two-thirds of the votes entitled to be cast on the plan within each voting group entitled to vote as a separate voting group on the plan. The articles of incorporation of HCSB do not alter this default voting standard with respect to HCSB voting common stock. However, the articles of incorporation of HCSB alter this default voting standard with respect to HCSB non-voting common stock by requiring the holders of a majority of the issued and outstanding shares of non-voting common stock to approve any agreement, merger or business consolidation, or any other transaction or action by HCSB that would have the effect of changing any preference or any relative or other right provided for the benefit of the holders of the HCSB non-voting common stock.</p>	<p>Neither the articles of incorporation nor bylaws of United require any supermajority approval of business transactions generally. The articles of incorporation of United provide that in order to engage in a merger, consolidation, sale or transfer or disposition of all or substantially all of the assets of United, sale of \$1 million or more in securities, a plan of liquidation, or any other transaction with any holder of 10% or more of the issued and outstanding shares of United that would increase the percentage ownership of such shareholder, such transaction must be approved by either a resolution adopted by at least three-fourths of the directors then in office, or the affirmative vote of the holders of at least 75% of the outstanding shares of common stock of United and the separate affirmative vote of at least 75% of the outstanding shares of common stock, excluding those shares held by such shareholder.</p>

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HCSB Shareholder Rights

The South Carolina Business Combinations Statute provides that a 10% or greater shareholder of a resident domestic corporation cannot engage in a “business combination” (as defined in the statute) with such corporation for a period of two years following the date on which the 10% shareholder became such, unless the business combination or the acquisition of shares is approved by a majority of the disinterested members of such corporation’s board of directors before the 10% shareholder’s share acquisition date. This statute further provides that at no time (even after the two-year period subsequent to such share acquisition date) may the 10% shareholder engage in a business combination with the relevant corporation unless certain approvals of the board of directors or disinterested shareholders are obtained or unless the consideration given in the combination meets certain minimum standards set forth in the statute. The law is very broad in its scope and is designed to inhibit unfriendly acquisitions but it does not apply to corporations whose articles of incorporation contain a provision electing not to be covered by the law. The articles of incorporation of HCSB do not contain such a provision.

United Shareholder Rights

The bylaws of United provide that any action required or permitted to be taken at a meeting of shareholders may be taken without a meeting if a written consent (or consents) has been signed by the holders of outstanding United stock having not less than the minimum number of votes that would be necessary to authorize or take such action at a meeting at which all shares entitled to vote thereon were present and voted. Prompt notice of the taking of the corporate action without a meeting by less than unanimous written consent must be given to those shareholders who have not consented in writing.

Shareholder Action Without Meeting	The SCBCA provides that shareholder action by written consent in lieu of a meeting is permitted only if such consent is unanimous. Neither the articles of incorporation nor bylaws of HCSB alter this default standard.
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	HCSB Shareholder Rights	United Shareholder Rights
Exclusive Forum	The bylaws of HCSB do not set forth an exclusive forum for legal proceedings.	The bylaws of United provide that the United States District Court for the Northern District of Georgia or, if such court lacks jurisdiction, any Georgia state court that has jurisdiction, shall, to the fullest extent permitted by law, be the sole and exclusive forum for certain legal proceedings.
Amendments to Articles of Incorporation and Bylaws	The SCBCA provides that, unless the articles of incorporation require a different vote, a South Carolina corporation's articles of incorporation generally may be amended only upon approval by (i) two-thirds of the votes entitled to be cast on the amendment, regardless of the class or voting group to which the shares belong and (ii) two-thirds of the votes entitled to be cast on the amendment within each voting group entitled to vote as a separate voting group on the amendment. The articles of incorporation of HCSB do not alter this default voting standard. HCSB's bylaws provide that HCSB's Board of Directors may alter, amend or repeal any provision of the bylaws, or new bylaws may be adopted at any meeting at which a quorum is present, by the affirmative vote of a majority of the directors. HCSB's bylaws also provide that HCSB's shareholders may alter, amend or repeal any provision of the bylaws, or new bylaws may be adopted at any meeting of the shareholders at which a quorum is present or represented by proxy, by the affirmative vote of the holders of a majority of each class of shares entitled to vote thereon. Upon adoption of any new bylaw by the shareholders, the shareholders may expressly provide that the Board of Directors may not adopt, amend or repeal that bylaw or any bylaw on that subject.	United's articles of incorporation specifically provide that any amendment or repeal of any provision of the articles of incorporation or Article II (Stockholders' Meetings) or Article III (Board of Directors) of the bylaws requires the affirmative vote of holders of a majority of the shares of United's capital stock then issued and outstanding and entitled to vote on such matters. United's bylaws provide that United's Board of Directors may alter, amend or repeal United's bylaws or adopt new bylaws, subject to the voting requirement included in United's articles of incorporation. Any bylaws adopted by United's Board of Directors may be altered, amended or repealed, and new bylaws adopted, by the shareholders of United.
Dividends	United declared cash dividends of \$0.09 per share of common stock in the first quarter of 2017, \$0.30 per share in 2016, \$0.22 per share in 2015 and \$0.11 per share in 2014. United intends to continue paying cash dividends, but the amount and frequency of cash dividends, if any, will be determined by United's	

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Board of Directors after consideration of certain non-financial and financial factors including earnings, capital requirements, and the financial condition of United, and will depend on cash dividends paid to it by its subsidiary bank. The ability of United's subsidiary bank to pay dividends to it is restricted by certain regulatory requirements. No cash dividends were declared on HCSB's common stock in the first quarter of 2017 or in 2016, 2015 or 2014.

Accounting Treatment

The merger will be accounted for as a purchase for financial reporting and accounting purposes under generally accepted accounting principles in the United States. After the merger, the results of operations of HCSB will be included in the consolidated financial statements of United. The merger consideration will be allocated based on the fair values of the assets acquired and the liabilities assumed. Any excess of cost over fair value of the net tangible and identified intangible assets of HCSB acquired will be recorded as goodwill. Any identified intangible asset may be amortized by charges to operations under generally accepted accounting principles in the United States.

Regulatory Approvals

The Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Department of Banking and Finance of the State of Georgia and the South Carolina State Board of Financial Institutions must approve the merger. In determining whether to grant that approval, the Federal Reserve will consider the effect of the merger on the financial and managerial resources and future prospects of the companies and banks concerned and the convenience and needs of the communities to be served.

The review of the merger application by the Federal Reserve, the Federal Deposit Insurance Corporation, the Georgia Department of Banking and Finance or the South Carolina State Board of Financial Institutions will not include an evaluation of the proposed transaction from the financial perspective of the individual shareholders of HCSB. Further, no shareholder should construe an approval of the merger application by the Federal Reserve, the Federal Deposit Insurance Corporation, the Georgia Department of Banking and Finance or the South Carolina State Board of Financial Institutions to be a recommendation that the shareholders vote to approve the proposal. Each shareholder entitled to vote should evaluate the proposal to determine the personal financial impact of the completion of the proposed transaction. Shareholders not fully knowledgeable in such matters are advised to obtain the assistance of competent professionals in evaluating all aspects of the proposal including any determination that the completion of the proposed transaction is in the best financial interest of the shareholder.

Dissenters' Rights

Under South Carolina law, holders of HCSB common stock will be entitled to dissent from the merger and to obtain payment in cash of the fair value of his or her shares of HCSB common stock. Set forth below is a summary of the procedures that must be followed by the holders of HCSB common stock in order to exercise their dissenters' rights of appraisal. This summary is qualified in its entirety by reference to the text of the applicable South Carolina statutes, a copy of which is attached as Appendix B to this document.

A record holder of HCSB common stock who wishes to assert dissenters' rights (i) must deliver to HCSB before the vote is taken on the merger agreement written notice of his or her intent to demand payment for his or her shares if the merger is effectuated, and (ii) must not vote his or her shares in favor of the merger agreement.

If the merger is approved at the HCSB special meeting, HCSB will deliver, no later than 10 days after the special meeting, a written dissenters' notice to all HCSB shareholders who satisfied the two requirements set forth above. The written dissenters' notice will state where the payment demand must be sent and where stock certificates must be deposited, will include a form for demanding payment that includes the date of the first announcement to news media or to shareholders of the terms of the merger and requires that the person asserting dissenters' rights certify whether or not he or she or, if he or she is a

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nominee asserting dissenters' rights on behalf of a beneficial shareholder, the beneficial shareholder acquired beneficial ownership of the shares before that date, and will set a date by which HCSB must receive the payment demand, which date will not be less than 30 or more than 60 days after the written dissenters' notice is delivered. A dissenting shareholder who does not demand payment or deposit his or her share certificate as required by the dissenters' notice will not be entitled to payment for his or her shares, and such shareholder's shares of HCSB common stock will be converted into the right to receive the merger consideration in connection with the merger.

As soon as the merger is consummated, or upon receipt of a payment demand, HCSB will pay to each dissenting shareholder who properly demanded payment the amount HCSB estimates to be the fair value of his or her shares, plus accrued interest. If the shareholder believes the amount of the payment is less than fair value or that the interest is calculated incorrectly or HCSB fails to make payment within 60 days after the date set for demanding payment, or if the merger is not consummated, HCSB fails to return the deposited certificates within 60 days after the date set for demanding payment, he or she may notify HCSB in writing of his or her own estimate of fair value and amount of interest due and demand payment of his estimate (less the payment already received). However, a dissenting shareholder waives his or her right to demand additional payment if he or she fails to notify HCSB of his or her demand in writing within 30 days after HCSB made payment for his or her shares. If a demand for payment remains unsettled, HCSB will commence a court proceeding to determine the fair value of the shares and the accrued interest. Exercise of dissenters' rights by holders of HCSB common stock will result in the recognition of gain or loss, as the case may be, for federal income tax purposes.

Material U.S. Federal Income Tax Consequences and Opinion of Tax Counsel

Subject to the limitations, assumptions and qualifications described herein, in the opinion of each of Troutman Sanders LLP and Nelson Mullins Riley & Scarborough, LLP, the following discussion summarizes the anticipated material U.S. federal income tax consequences of the merger generally applicable to "U.S. holders" (as defined below) of HCSB common stock that exchange their shares in the merger. This summary is based upon the Internal Revenue Code of 1986, as amended (the "Code"), Treasury regulations promulgated thereunder, judicial authorities, published positions of the Internal Revenue Service ("IRS") and other applicable authorities, all as in effect on the date of this discussion and all of which are subject to change (possibly with retroactive effect) and differing interpretations. The opinions of tax counsel for each of United and HCSB are filed as Exhibit 8.1 and Exhibit 8.2, respectively, to the registration statement on Form S-4 of which this document is a part. These opinions will be based on representations, covenants and undertakings provided by United and HCSB and on customary factual assumptions. If any of the representations or assumptions upon which the opinions are based are inconsistent with the actual facts, the U.S. federal income tax consequences of the mergers could be adversely affected. Neither of the opinions described above will be binding on the IRS or any court. United and HCSB have not sought and will not seek any ruling from the IRS regarding any matters relating to the mergers, and as a result, there can be no assurance that the IRS will not assert, or that a court would not sustain, a position contrary to any of the conclusions set forth below.

This summary is limited to U.S. holders (as defined below) that hold their shares of HCSB common stock as a capital asset within the meaning of Section 1221 of the Code (generally, property held for investment). Furthermore, this discussion does not address all of the tax consequences that may be relevant to a particular HCSB shareholder or to HCSB shareholders that are subject to special rules under U.S. federal income tax laws, such as: shareholders that are not U.S. holders; banks, thrifts, or other financial institutions; insurance companies; mutual funds; tax-exempt organizations; S corporations, partnerships or other pass-through entities (or investors in such entities); regulated investment companies; real estate investment trusts; retirement plans, individual retirement accounts or other tax-deferred accounts; dealers in stocks and securities or currencies; persons subject to the alternative minimum tax provisions of the Code; former citizens or residents of the U.S.; persons whose functional currency is not the U.S. dollar; traders in securities that elect to use a mark-to-market method of accounting; persons who own more than 5% of the outstanding common stock of HCSB; persons who hold HCSB common stock as part of a straddle, hedge, constructive sale, wash sale, conversion or other integrated transaction; and U.S. holders who acquired their shares of HCSB common stock through the exercise of an employee stock option, through a qualified retirement plan or otherwise as compensation.

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In addition, this discussion does not address any alternative minimum tax or any state, local or foreign tax consequences of the merger, nor does it address any other U.S. federal tax consequences (such as gift or estate taxes) including any tax consequences arising under the unearned income Medicare contribution tax pursuant to Section 1411 of the Code. Determining the actual tax consequences of the merger to each HCSB shareholder may be complex. They will depend on each HCSB shareholder's specific situation and on factors that are not within the control of United or HCSB. Accordingly, each HCSB shareholder should consult its tax advisor with respect to the particular tax consequences of the merger to such holder.

For purposes of this section, the term "U.S. holder" means a beneficial owner of HCSB common stock that for United States federal income tax purposes is: a citizen or resident of the United States; a corporation, or other entity treated as a corporation for U.S. federal income tax purposes, created or organized in or under the laws of the United States, any state thereof or the District of Columbia; an estate that is subject to U.S. federal income tax on its income regardless of its source; or a trust, the substantial decisions of which are controlled by one or more U.S. persons and which is subject to the primary supervision of a U.S. court, or a trust that validly has elected under applicable Treasury regulations to be treated as a U.S. person for U.S. federal income tax purposes.

If a partnership (including any entity or arrangement that is treated as a partnership for U.S. federal income tax purposes) holds HCSB common stock, the tax treatment of a partner generally will depend on the status of the partners and the activities of the partnership. Partnerships and partners in such a partnership should consult their tax advisers about the tax consequences of the merger to them.

Holders of HCSB common stock are urged to consult with their own tax advisors as to the tax consequences of the merger given their particular circumstances.

Tax Consequences of the Merger

The merger will be treated as a "reorganization" within the meaning of Section 368(a) of the Code. Consummation of the merger is conditioned upon each of United and HCSB receiving a written tax opinion, dated the closing date of the merger, from their respective outside legal counsels to the effect that, based upon facts, representations and assumptions set forth in such opinions, (i) the merger will be treated for federal income tax purposes as a reorganization within the meaning of Section 368(a) of the Code, and (ii) United and HCSB will each be a party to that reorganization within the meaning of Section 368(b) of the Code. An opinion of counsel represents the counsel's best legal judgment and is not binding on the IRS or any court, and as a result, there can be no assurance that the IRS will not assert, or that a court would not sustain, a position contrary to any such opinion. In addition, if any of the representations or assumptions upon which these opinions are based are inconsistent with the actual facts, the U.S. federal income tax consequences of the merger could be adversely affected. Accordingly, each HCSB shareholder should consult its tax advisor with respect to the particular tax consequences of the merger to such holder.

Tax Consequences to United and HCSB

Each of United and HCSB will be a party to the merger within the meaning of Section 368(b) of the Code, and neither United nor HCSB will recognize any gain or loss as a result of the merger.

Tax Consequences to Shareholders

Exchange Solely for United Common Stock. A U.S. holder will not recognize any gain or loss in connection with such U.S. holder's exchange of all of its shares of HCSB common stock for shares of United common stock, except in respect of cash received in lieu of any fractional share of United common stock.

Cash Received in Lieu of a Fractional Share. If a U.S. holder receives cash in the merger instead of a fractional share interest in United common stock, the U.S. holder will be treated as having received such fractional share in the merger, and then as having received cash in exchange for such fractional share. Gain or loss will be recognized in an amount equal to the difference between the amount of cash received and the HCSB's shareholder's adjusted tax basis allocable to such fractional share. This gain or loss will be a capital gain or loss, and will be long-term capital gain or loss if, as of the effective date of the merger, the U.S. holder held its shares of HCSB common stock for more than one year.

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Exchange Solely for Cash upon Exercise of Dissenters' Rights. Upon the proper exercise of dissenters' rights, the exchange of HCSB shares solely for cash generally will result in recognition of gain or loss by the U.S. holder in an amount equal to the difference between the amount of cash received by the U.S. holder and the U.S. holder's tax basis in its HCSB common stock (generally the purchase price paid by the U.S. holder to acquire such stock). The gain or loss generally will be a capital gain or loss, and will be long-term capital gain or loss if, as of the effective date of the merger, the U.S. holder held its shares of HCSB common stock for more than one year.

Tax Basis in, and Holding Period for, United Common Stock. The aggregate tax basis of the United common stock received by a U.S. holder as a result of the merger will be the same as such shareholder's aggregate tax basis in its HCSB common stock surrendered in the merger, decreased by the amount of basis allocable to a fractional share of United common stock deemed received and exchanged for cash in the merger) (as discussed above). The holding period of the United common stock (including any fractional share deemed received and redeemed as discussed above) a U.S. holder receives as a result of the exchange will include the holding period of HCSB common stock surrendered in the merger. If a U.S. holder has differing bases or holding periods in respect of its shares of HCSB common stock, it should consult its tax advisor with regard to identifying the bases or holding periods of the particular shares of United common stock received in the exchange.

Backup Withholding and Information Reporting. A non-corporate U.S. holder may be subject under certain circumstances to information reporting and backup withholding (currently at a rate of 28%) on any cash payments received. A U.S. holder generally will not be subject to backup withholding, however, if such U.S. holder (1) furnishes a correct taxpayer identification number, certifies that it is not subject to backup withholding and otherwise comply with all the applicable requirements of the backup withholding rules; or (2) provide proof that it is otherwise exempt from backup withholding. Any amounts withheld under the backup withholding rules are not an additional tax and generally will be allowed as a refund or credit against the U.S. holder's U.S. federal income tax liability, provided such U.S. holder timely furnishes the required information to the IRS. U.S. holders should consult their own tax advisors regarding the application of backup withholding based on their particular circumstances and the availability and procedure for obtaining an exemption from backup withholding.

A HCSB shareholder who receives United common stock as a result of the merger will be required to retain records pertaining to the merger. Each HCSB shareholder who is required to file a U.S. federal income tax return and who is a "significant holder" that receives United common stock in the merger will be required to file a statement with such U.S. federal income tax return in accordance with Treasury Regulations Section 1.368-3 setting forth information regarding the parties to the merger, the date of the merger, such HCSB shareholder's basis in the HCSB common stock surrendered and the fair market value of the United common stock and cash received in the merger. A "significant holder" is a holder of HCSB common stock who, immediately before the merger, owned at least 5% of the outstanding stock of HCSB or securities of HCSB with a basis for federal income tax purposes of at least \$1 million.

THE PRECEDING DISCUSSION IS INTENDED ONLY AS A SUMMARY OF THE MATERIAL UNITED STATES FEDERAL INCOME TAX CONSEQUENCES OF THE MERGER AND DOES NOT PURPORT TO BE A COMPLETE ANALYSIS OR DISCUSSION OF ALL POTENTIAL TAX EFFECTS RELEVANT THERETO. HCSB SHAREHOLDERS ARE URGED TO CONSULT THEIR OWN TAX ADVISORS AS TO THE SPECIFIC TAX CONSEQUENCES TO THEM OF THE MERGER, INCLUDING TAX RETURN REPORTING REQUIREMENTS, THE APPLICABILITY AND EFFECT OF NON-U.S., FEDERAL, STATE, LOCAL, AND OTHER APPLICABLE TAX LAWS, AND THE EFFECT OF ANY PROPOSED CHANGES IN THE TAX LAWS.

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PROPOSAL NO. 2 — ADVISORY VOTE ON MERGER-RELATED COMPENSATION

Section 951 of the Dodd-Frank Act and Rule 14a-21(c) under the Securities Exchange Act of 1934 require that HCSB seek a non-binding advisory vote from its shareholders to approve certain compensation that its named executive officers will receive from HCSB and Horry County State Bank in connection with the merger.

HCSB is presenting this proposal, which gives HCSB shareholders the opportunity to express their views on such merger-related compensation by voting for or against the following resolution:

“RESOLVED, that the compensation that may become payable to HCSB’s named executive officers in connection with the completion of the merger, as disclosed in the section captioned “Proposal 1 — Description of the Merger — Interests of Directors and Officers of HCSB in the Merger” and the related tables and narrative, is hereby approved.”

The HCSB Board of Directors unanimously recommends that shareholders approve the merger-related compensation arrangements described in this document by voting “FOR” the above proposal.

Approval of this proposal is not a condition to completion of the merger, and the vote with respect to this proposal is advisory only and will not be binding on HCSB or United. Therefore, if the merger is approved by the HCSB shareholders and completed, the merger-related compensation will still be paid to the HCSB named executive officers.

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INFORMATION ABOUT UNITED COMMUNITY BANKS, INC.

General

Financial and other information about United is set forth on United's Form 10-K for the year ended December 31, 2016 (which includes certain provisions of United's Proxy Statement for its 2017 Annual Meeting) and the quarterly report on Form 10-Q for the quarter ended March 31, 2017 which is incorporated herein by reference.

Securities

The authorized capital stock of United currently consists of 150,000,000 shares of common stock, \$1.00 par value per share, 26,000,000 shares of non-voting common stock, \$1.00 par value per share, and 10,000,000 shares of preferred stock, \$1.00 par value per share.

Common Stock

All voting rights are vested in the holders of the common stock. Each holder of common stock is entitled to one vote per share on any issue requiring a vote at any meeting. The shares do not have cumulative voting rights. Upon liquidation, holders of United's common stock, together with holders of United's non-voting common stock, junior preferred stock, junior participating preferred stock and Series E preferred stock, will be entitled to receive on a pro rata basis, after payment or provision for payment of all our debts and liabilities, and after all distributions payments are made to holders of United's Series A preferred stock, Series B preferred stock, Series C preferred stock, Series D preferred stock and Series H preferred stock, all of United's assets available for distribution, in cash or in kind. Subject to the rights of holders of United's Series A preferred stock, Series B preferred stock, Series C preferred stock, Series D preferred stock and Series H preferred stock to receive dividends, all shares of United's common stock, together with all shares of United's non-voting common stock, junior preferred stock and Series E preferred stock, are entitled to share equally in any dividends that United's Board of Directors may declare on its common stock, non-voting common stock, junior preferred stock and Series E preferred stock from sources legally available for distribution.

The outstanding shares of United common stock are, and the shares of United common stock to be issued by United in connection with the merger will be, duly authorized, validly issued, fully paid, and nonassessable.

As of [•], 2017, [•] shares of common stock were issued and outstanding, exclusive of [•] shares issuable to participants in United's Deferred Compensation Plan and [•] shares reserved for issuance upon the exercise of outstanding options and vesting of restricted stock.

Non-Voting Common Stock

United's authorized non-voting common stock consists of 26,000,000 shares. Except with respect to voting rights and as specifically set forth below, the non-voting common stock has the same designations, powers, preferences, limitations, restrictions, and relative rights as, and is identical in all respects to, United's common stock.

Except as required by Georgia law or United's articles of incorporation, holders of the non-voting common stock have no right to vote on any matter submitted to a vote at a meeting of United's shareholders. United's articles of incorporation provide that, in addition to any other vote required by law, the affirmative vote of the holders of a majority of the outstanding shares of the non-voting common stock, voting separately as a class, will be required to amend, alter or repeal any provision of the articles of incorporation that significantly and adversely affects the rights, preferences or privileges of the non-voting common stock.

Subject to any preferential dividend rights of any preferred stock of United, the holders of non-voting common stock will be entitled to receive, to the extent permitted by law, such dividends as may be declared from time to time by United's Board of Directors on the common stock. If a dividend is declared and paid

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with respect to United's common stock, then the Board of Directors will declare and pay an equivalent dividend, on a per share basis, to the non-voting common stock. Likewise, if the Board of Directors declares and pays a dividend on the non-voting common stock, it will declare and pay an equivalent dividend, on a per share basis, on the common stock.

After distribution in full of any preferential amount to be distributed to the holders of any preferred stock of United, holders of non-voting common stock and common stock will be entitled to receive, in the event of the voluntary or involuntary liquidation, dissolution, distribution of assets or winding-up of United, all of United's remaining assets of whatever kind available for distribution to the shareholders ratably in proportion to the number of shares of common stock and non-voting common stock held by them.

The non-voting common stock may be converted into common stock by any holder of non-voting common stock, other than the initial holder of such non-voting common stock or an affiliate thereof, who acquires one or more shares of non-voting common stock in an "Approved Transfer". An "Approved Transfer" means a sale or other transfer (i) to an affiliate of the holder of the non-voting common stock to be transferred under common control with such holder's ultimate parent, general partner or investment advisor but only if the transferee agrees in writing for the benefit of United to be bound by the terms of an applicable Investor Agreement; (ii) in a widely distributed public offering registered pursuant to the Securities Act of 1933; (iii) to a person that is acquiring at least a majority of United's outstanding "voting securities" (as defined in the Bank Holding Company Act and any rules or regulations promulgated thereunder) not including any voting securities such person is acquiring from the holder of the non-voting common stock to be transferred or its affiliates; or (iv) upon certification by the holder of the non-voting common stock to be transferred in writing to United that such holder believes that the transferee shall not, after giving effect to such transfer, own for purposes of the Bank Holding Company Act, or the Change of Bank Control Act, and any rules and regulations promulgated thereunder, more than 2% of any class of voting securities of United outstanding at such time.

As of [•], 2017, no shares of non-voting common stock were issued and outstanding.

Preferred Stock

United is authorized to issue 10,000,000 shares of preferred stock, issuable in specified series and having specified voting, dividend, conversion, liquidation, and other rights and preferences as United's Board of Directors may determine. The preferred stock may be issued for any lawful corporate purpose without further action by United shareholders. The issuance of any preferred stock that has conversion rights might have the effect of diluting the interests of United's other shareholders. In addition, shares of preferred stock could be issued with certain rights, privileges, and preferences, which would deter a tender or exchange offer or discourage the acquisition of control of United.

Of such authorized number of shares of preferred stock, (i) 1,000,000 shares of junior preferred stock are authorized, with no shares issued and outstanding; (ii) 287,411 shares of Series A preferred stock are authorized, with no shares issued and outstanding; (iii) 180,000 shares of Series B preferred stock are authorized, with no shares issued and outstanding; (iv) 65,000 shares of Series C preferred stock are authorized, with no shares issued and outstanding; (v) 25,000 shares of Series D preferred stock are authorized, with no shares issued and outstanding; (vi) 1,000,000 shares of Series E preferred stock are authorized, with no shares issued and outstanding; (vii) 195,872 shares of Series F preferred stock are authorized, with no shares issued and outstanding; (viii) 151,185 shares of Series G preferred stock are authorized, with no shares issued and outstanding, and (ix) 9,992 shares of Series H preferred stock are a;

text-align: left" ROWSPAN=1> * Brian J. Rosin⁽⁷⁾ 33,000 * Birame Sock⁽⁸⁾ 13,735 * All directors and named executive officers as a group (7 people) 2,142,675 48.6% 100%

*

Represents less than 1%.

(1) Except as otherwise set forth below, the business address and telephone number of each of the persons listed above is c/o Function(x) Inc., 902 Broadway, New York, New York 10010, telephone (212) 231-0092.

(2) Mr. Sillerman beneficially owns 2,073,079 shares of common stock, including: (i) directly 8,113 shares of common stock owned by Mr. Sillerman (consisting of (A) 1,863 shares of common stock owned by Mr. Sillerman; and (B) 6,250 shares of common stock issuable upon the exercise of warrants held by Mr. Sillerman which are exercisable at \$1,600.00 per share); and (ii) indirectly 2,064,966 shares of common stock (consisting of (A) 3,125 shares of

common stock issuable upon the exercise of warrants held by Sillerman Investment Company II LLC (SIC II) that are exercisable at \$1,104.00 per share, (B) 8,778 shares of common stock issuable upon the exercise of warrants held by SIC II which are exercisable at \$1,600.00 per share; (C) 17,500 shares of common stock issuable upon the exercise of warrants held by Sillerman Investment Company III LLC (SIC III) that are exercisable at \$35.60 per share, (D) 11,250 shares of common stock issuable upon the exercise of warrants held by SIC III that are

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exercisable at \$70.20 per share, (E) 7,500 shares of common stock that are issuable upon the exercise of warrants held by SIC III that are exercisable at \$59.60 per share, (F) 38,750 shares of common stock that are issuable upon the exercise of warrants held by SIC III that are exercisable at \$72.60 per share, (G) 1,540,563 shares of common stock held by SIC III and (H) 437,500 shares of common stock held by Sillerman Investment Company IV LLC.

SIC III, SIC IV and SIC VI collectively hold 33,175 shares of Series C Preferred Stock, which are not convertible into common stock by their terms. However, the Company, SIC III, SIC IV and SIC VI are party to an Exchange (3) Agreement pursuant to which these shares may be exchanged for common stock upon the occurrence of certain conditions, which have not yet been satisfied. If these conditions are satisfied and the exchange occurs, these shares of Series C Preferred Stock would be exchanged for 6,379,808 shares of common stock.

Mr. Horan beneficially owns (i) 78 shares of common stock exercisable upon the exercise of stock options that are exercisable or will be exercisable within 60 days of February 17, 2017 at \$8,000.00 per share; (ii) 31 shares of common stock exercisable upon the exercise of stock options that are exercisable or will be exercisable within 60 days of February 17, 2017 at \$2,000.00 per share; (iii) 19 shares of common stock exercisable upon the exercise of stock options that are exercisable or will be exercisable within 60 days of February 17, 2017 at \$1,200.00 per share; (iv) 14 shares of common stock exercisable upon the exercise of stock options that are exercisable or will be exercisable within 60 days of February 17, 2017 at \$3,088.00 per share; (v) 31 shares of common stock exercisable upon the exercise of stock options that are exercisable or will be exercisable within 60 days of February 17, 2017 at (4) \$1,968.00 per share, (vi) 21 shares of common stock exercisable upon the exercise of stock options that are exercisable or will be exercisable within 60 days of February 17, 2017 at \$976.00 per share, (vii) 20 shares of common stock exercisable upon the exercise of stock options that are exercisable or will be exercisable within 60 days of February 17, 2017 at \$1,040.00 per share, (viii) 1,939 shares of common stock exercisable upon the exercise of stock options that are exercisable or will be exercisable within 60 days of February 17, 2017 at \$89.46 per share, (ix) 5,000 shares of common stock issuable upon the exercise of options that are exercisable or will be exercisable within 60 days of February 17, 2017 at \$46.60 per share, (x) 280 shares of common stock issuable upon the exercise of options that are exercisable or will be exercisable within 60 days of February 17, 2017 at \$9.20 per share and (xi) 2,952 shares of common stock.

Mr. Meyer beneficially owns (i) 20 shares of common stock exercisable upon the exercise of stock options that are exercisable or will be exercisable within 60 days of February 17, 2017 at \$976.00 per share, (ii) 22 shares of common stock exercisable upon the exercise of stock options that are exercisable or will be exercisable within 60 days of February 17, 2017 at \$1,040.00 per share, (iii) 2,194 shares of common stock exercisable upon the exercise (5) of stock options that are exercisable or will be exercisable within 60 days of February 17, 2017 at \$89.20 per share, (iv) 2,500 shares of common stock exercisable upon the exercise of stock options that are exercisable or will be exercisable within 60 days of February 17, 2017 at \$46.60 per share, (v) 3,166 shares of common stock exercisable upon the exercise of stock options that are exercisable or will be exercisable within 60 days of February 17, 2017 at \$46.60 per share and (vi) 2,952 shares of common stock.

(6) Mr. Nelson beneficially owns 1,622 shares of common stock.

(7) Mr. Rosin was granted 33,000 common shares under the Company's equity incentive plan, which may vest at any time prior to January 25, 2018, at Mr. Rosin's option.

(8) Ms. Sock beneficially owns (i) 18 shares of common stock exercisable upon the exercise of stock options that are exercisable or will be exercisable within 60 days of February 17, 2017 at \$1,200.00 per share; (ii) 31 shares of common stock exercisable upon the exercise of stock options that are exercisable or will be exercisable within 60 days of February 17, 2017 at \$1,968.00 per share, (iii) 20 shares of common stock exercisable upon the exercise of stock options that are exercisable or will be exercisable within 60 days of February 17, 2017 at \$976.00 per share, (iv) 19 shares of common stock exercisable upon the exercise of stock options that are exercisable or will be exercisable within 60 days of February 17, 2017 at \$1,040.00 per share, (v) 1,847 shares of common stock exercisable upon the exercise of stock options that are exercisable or will be exercisable within 60 days of February 17, 2017 at \$89.20 per share, (vi) 750 shares of common stock issuable upon the exercise of stock options that are exercisable or that are exercisable within 60 days of February 17, 2017 at \$46.60 per share, (vii) 2,700 shares of common stock issuable upon the exercise of stock options that are exercisable or that are exercisable within 60

days of February 17, 2017 at \$9.20 per share, (viii) 8,334 shares of restricted stock issued pursuant to the 2011 Executive Equity Incentive Plan, which will vest within 60 days of February 17, 2017; and (ix) 16 shares of common stock.

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Aegis Capital Corp. and Laidlaw & Company (UK) Ltd. are the joint book-running managers of the offering. We have entered into an underwriting agreement dated _____, 2017 with the underwriters. Subject to the terms and conditions of the underwriting agreement, we have agreed to sell to the underwriters and the underwriters have agreed to purchase, at the public offering price less the underwriting discounts and commissions set forth on the cover page of this prospectus, the following respective number of shares of our common stock:

Underwriter	Number of Shares
Aegis Capital Corp.	
Laidlaw & Company (UK) Ltd.	
Total	

The underwriters have committed to purchase all the shares of common stock offered by us other than those covered by the option to purchase additional shares described below, if it purchases any shares. The obligations of the underwriters may be terminated upon the occurrence of certain events specified in the underwriting agreement. Furthermore, pursuant to the underwriting agreement, the underwriters' obligations are subject to customary conditions, representations and warranties contained in the underwriting agreement, such as receipt by the underwriters of officers' certificates and legal opinions.

We have agreed to indemnify the underwriters against specified liabilities, including liabilities under the Securities Act of 1933, and to contribute to payments the underwriters may be required to make in respect thereof.

The underwriters are offering the common stock, subject to prior sale, when, as and if issued to and accepted by it, subject to approval of legal matters by its counsel and other conditions specified in the underwriting agreement. The underwriters reserve the right to withdraw, cancel or modify offers to the public and to reject orders in whole or in part.

The underwriters propose to offer the common stock offered by us to the public at the public offering price set forth on the cover of this prospectus. In addition, the underwriters may offer some of the common stock to other securities dealers at such price less a concession of \$ _____ per share. After the initial offering, the public offering price and concession to dealers may be changed.

We have granted the underwriters an over-allotment option. This option, which is exercisable for up to 45 days after the date of this prospectus, permits the underwriters to purchase a maximum of _____ additional shares of common stock from us to cover over-allotments. If the underwriters exercise all or part of this option, it will purchase shares of common stock covered by the option at the public offering price that appears on the cover page of this prospectus supplement, less the underwriting discount. If this option is exercised in full, the total price to the public will be approximately \$ _____,000 and the total proceeds to us will be \$ _____,000.

Discounts and Commissions. The following table shows the public offering price, underwriting discount and proceeds, before expenses, to us. The information assumes either no exercise or full exercise by the underwriter of its over-allotment option.

Total

	Per Share	Without Over-Allotment	With Over-Allotment
Public offering price	\$	\$	\$
Underwriting discount (7%)	\$	\$	\$
Proceeds, before expenses, to us	\$	\$	\$

We have paid an expense deposit of \$25,000 to the underwriters, which will be applied against the accountable expenses that will be paid by us to the underwriters in connection with this offering. The underwriting agreement, however, provides that in the event the offering is terminated, the \$25,000 expense deposit paid to the underwriters will be returned to the extent offering expenses are not actually incurred.

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We have agreed to pay the underwriters a non-accountable expense allowance equal to 1% of the public offering price of the shares (excluding shares that we may sell to the underwriters to cover over-allotments). We have also agreed to pay all expenses relating to the offering, including (a) all filing fees and communication expenses relating to the registration of the shares to be sold in the offering (including the over-allotment shares) with the Commission; (b) all actual Public Filing System filing fees associated with the review of the offering by FINRA; (c) all fees, expenses and disbursements relating to background checks of our officers and directors in an amount not to exceed \$5,000 per individual with a \$15,000 cap; (d) all fees, expenses and disbursements relating to the registration or qualification of the Public Securities under the blue sky securities laws of such states and other jurisdictions as the underwriter may reasonably designate (including, without limitation, all filing and registration fees, and the reasonable fees and disbursements of blue sky counsel, it being agreed that such fees and expenses will be limited to: if the offering is commenced on either the NASDAQ Capital Market, NASDAQ Global Market or NASDAQ Global Select Market, we will make a payment of \$5,000 to such counsel at closing); (e) all fees, expenses and disbursements relating to the registration, qualification or exemption of the shares under the securities laws of such foreign jurisdictions as the underwriters may reasonably designate; (f) the costs of all mailing and printing of the underwriting documents (including, without limitation, the Underwriting Agreement, and, if appropriate, any Agreement Among Underwriters, Selected Dealers Agreement, Underwriters Questionnaire and Power of Attorney), Registration Statements, Prospectuses and all amendments, supplements and exhibits thereto and as many preliminary and final Prospectuses as the underwriters may reasonably deem necessary; (g) the costs and expenses of a public relations firm; (h) the costs of preparing, printing and delivering certificates representing the shares; (i) fees and expenses of the transfer agent for the shares of common stock; (j) stock transfer and/or stamp taxes, if any, payable upon the transfer of securities from us to the underwriters; (k) the costs associated with post-closing advertisement of the offering in the national editions of the Wall Street Journal and the New York Times; (l) the costs, up to a maximum of \$2,500, associated with bound volumes of the public offering materials as well as commemorative mementos and Lucite tombstones, each of which we will provide within a reasonable time after the closing in such quantities as the underwriters may reasonably request; (m) the fees and expenses of our accountants; (n) the fees and expenses of our legal counsel and other agents and representatives; (o) the fees and expenses of the underwriters' legal counsel not to exceed \$75,000, (p) the \$29,500 cost associated with the underwriters' use of Ipreo's book-building, prospectus tracking and compliance software for the offering; and (q) up to \$20,000 of the underwriters' actual accountable road show expenses for the offering.

We estimate that the total expenses of the offering including all expenses to be reimbursed to the underwriters, excluding the underwriting discount, will be approximately \$.

Discretionary Accounts. The underwriters do not intend to confirm sales of the securities offered hereby to any accounts over which it has discretionary authority.

Lock-Up Agreements. Pursuant to certain lock-up agreements, (a) our executive officers and directors owning 1% or more of our outstanding common stock as of the pricing date of the offering, have agreed, subject to certain exceptions, not to offer, issue, sell, contract to sell, encumber, grant any option for the sale of or otherwise dispose of any securities of the company subject to certain limited exceptions without the prior written consent of the underwriters, for a period of 90 days from the date of the pricing of the offering, and (b) we, and any successor, have agreed, subject to certain exceptions, not to for a period of 90 days from the date of the pricing of the offering (1) offer, pledge, sell, contract to sell, sell any option or contract to purchase, purchase any option or contract to sell, grant any option, right or warrant to purchase, lend, or otherwise transfer or dispose of, directly or indirectly, any shares of our capital stock; (2) enter into any swap or other arrangement that transfers to another, in whole or in part, any of the economic consequences of ownership of our capital stock, whether any such transaction described in (1) or (2) above is to be settled by delivery of shares of our capital stock or such other securities, in cash or otherwise.

This lock-up provision applies to common stock and to securities convertible into or exchangeable or exercisable for common stock. It also applies to common stock owned now or acquired later by the person executing the agreement or for which the person executing the agreement later acquires the power of

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disposition. The exceptions permit, among other things, (1) the issuance by us of stock options pursuant to our existing stock incentive plans, or (2) the issuance of common stock upon the exercise of outstanding stock options and warrants.]

Underwriters' Warrants. We have agreed to issue to the underwriters warrants to purchase up to a total of [] shares of common stock (2.5% of the shares of common stock sold). The warrants are exercisable at \$ per share (125% of the price of the shares sold in the offering), commencing one year from the effective date of the offering, and expiring five years after the effective date of the offering. The warrants have been deemed to be underwriters' compensation by FINRA and are therefore subject to a 180-day lock-up pursuant to Rule 5110(g)(1) of FINRA. The underwriters (or permitted assignees under the Rule) will not sell, transfer, assign, pledge, or hypothecate these warrants or the securities underlying these warrants, nor will it engage in any hedging, short sale, derivative, put, or call transaction that would result in the effective economic disposition of the warrants or the underlying securities for a period of 180 days from the effective date of the offering. In addition, the warrants provide for registration rights upon request, in certain cases. We will bear all fees and expenses attendant to registering the securities issuable on exercise of the warrants other than underwriting commissions incurred and payable by the holders. The exercise price and number of shares issuable upon exercise of the warrants may be adjusted in certain circumstances including in the event of a stock dividend, extraordinary cash dividend or our recapitalization, reorganization, merger or consolidation. However, the warrant exercise price or underlying shares will not be adjusted for issuances of shares of common stock at a price below the warrant exercise price. The 53,200 warrants we issued to Aegis Capital Corp. in connection with our private placement that closed on July 12, 2016 (see "Other Relationships") are also deemed underwriters' compensation by FINRA and are also subject to these lock-up terms.

Electronic Offer, Sale and Distribution of Shares. A prospectus supplement in electronic format may be made available on the websites maintained by the underwriters or selling group members, if any, participating in this offering and the underwriters participating in this offering may distribute prospectus supplements electronically. The underwriters may agree to allocate a number of shares to selling group members for sale to their online brokerage account holders. Internet distributions will be allocated by the underwriters and selling group members that will make internet distributions on the same basis as other allocations. Other than the prospectus supplement in electronic format, the information on these websites is not part of this prospectus supplement or the registration statement of which this prospectus supplement forms a part, has not been approved or endorsed by us or any underwriters in its capacity as underwriter, and should not be relied upon by investors.

Stabilization. In connection with this offering, the underwriters may engage in stabilizing transactions, overallotment transactions, syndicate covering transactions, penalty bids and purchases to cover positions created by short sales.

Stabilizing transactions permit bids to purchase shares so long as the stabilizing bids do not exceed a specified maximum, and are engaged in for the purpose of preventing or retarding a decline in the market price of the shares while the offering is in progress.

Overallotment transactions involve sales by the underwriters of shares in excess of the number of shares the underwriters are obligated to purchase. This creates a syndicate short position which may be either a covered short position or a naked short position. In a covered short position, the number of shares over-allotted by the underwriter is not greater than the number of shares that it may purchase in the overallotment option. In a naked short position, the number of shares involved is greater than the number of shares in the overallotment option. The underwriters may close out any short position by exercising its overallotment option and/or purchasing shares in the open market. Syndicate covering transactions involve purchases of shares in the open market after the distribution has been completed in order to cover syndicate short positions. In determining the source of shares to close out the short position, the underwriters will consider, among other things, the price of shares available for purchase in the open market as compared with the price at which it may purchase shares through exercise of the overallotment option. If

the underwriters sell more shares than could be covered by exercise of the overallotment option and, therefore, has a naked short position, the

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position can be closed out only by buying shares in the open market. A naked short position is more likely to be created if the underwriters are concerned that after pricing there could be downward pressure on the price of the shares in the open market that could adversely affect investors who purchase in the offering.

Penalty bids permit the underwriters to reclaim a selling concession from a syndicate member when the shares originally sold by that syndicate member are purchased in stabilizing or syndicate covering transactions to cover syndicate short positions.

These stabilizing transactions, syndicate covering transactions and penalty bids may have the effect of raising or maintaining the market price of our shares or common stock or preventing or retarding a decline in the market price of our shares or common stock. As a result, the price of our common stock in the open market may be higher than it would otherwise be in the absence of these transactions. Neither we nor the underwriters make any representation or prediction as to the effect that the transactions described above may have on the price of our common stock. These transactions may be effected on The Nasdaq Capital Market.

Passive market making. In connection with this offering, the underwriters and selling group members may engage in passive market making transactions in our common stock on The Nasdaq Capital Market in accordance with Rule 103 of Regulation M under the Exchange Act, during a period before the commencement of offers or sales of the shares and extending through the completion of the distribution. A passive market maker must display its bid at a price not in excess of the highest independent bid of that security. However, if all independent bids are lowered below the passive market maker's bid, that bid must then be lowered when specified purchase limits are exceeded.

Other Relationships

Aegis Capital Corp. served as our exclusive placement agent for our private placement of convertible debentures and common stock purchase warrants that closed on July 12, 2016. As compensation for serving as placement agent, Aegis Capital Corp. received \$320,000 and five-year warrants to purchase 53,200 shares of our common stock at an initial exercise price of \$6.528 per share, subject to adjustment.

Offer restrictions outside the United States

Other than in the United States, no action has been taken by us or the underwriter that would permit a public offering of the securities offered by this prospectus supplement in any jurisdiction where action for that purpose is required. The securities offered by this prospectus supplement may not be offered or sold, directly or indirectly, nor may this prospectus supplement or any other offering material or advertisements in connection with the offer and sale of any such securities be distributed or published in any jurisdiction, except under circumstances that will result in compliance with the applicable rules and regulations of that jurisdiction. Persons into whose possession this prospectus supplement comes are advised to inform themselves about and to observe any restrictions relating to the offering and the distribution of this prospectus supplement. This prospectus supplement does not constitute an offer to sell or a solicitation of an offer to buy any securities offered by this prospectus supplement in any jurisdiction in which such an offer or a solicitation is unlawful.

Australia

This prospectus is not a disclosure document under Chapter 6D of the Australian Corporations Act, has not been lodged with the Australian Securities and Investments Commission and does not purport to include the information required of a disclosure document under Chapter 6D of the Australian Corporations Act. Accordingly, (i) the offer of the securities under this prospectus is only made to persons to whom it is lawful to offer the securities without

disclosure under Chapter 6D of the Australian Corporations Act under one or more exemptions set out in section 708 of the Australian Corporations Act, (ii) this prospectus is made available in Australia only to those persons as set forth in clause (i) above, and (iii) the offeree must be sent a notice stating in substance that by accepting this offer, the offeree represents that the offeree is such a person as set forth in clause (i) above, and, unless permitted under the Australian Corporations Act, agrees not to sell or offer for sale within Australia any of the securities sold to the offeree within 12 months after its transfer to the offeree under this prospectus.

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China

The information in this document does not constitute a public offer of the securities, whether by way of sale or subscription, in the People's Republic of China (excluding, for purposes of this paragraph, Hong Kong Special Administrative Region, Macau Special Administrative Region and Taiwan). The securities may not be offered or sold directly or indirectly in the PRC to legal or natural persons other than directly to qualified domestic institutional investors.

European Economic Area Belgium, Germany, Luxembourg and Netherlands

The information in this document has been prepared on the basis that all offers of securities will be made pursuant to an exemption under the Directive 2003/71/EC (Prospectus Directive), as implemented in Member States of the European Economic Area (each, a Relevant Member State), from the requirement to produce a prospectus for offers of securities.

An offer to the public of securities has not been made, and may not be made, in a Relevant Member State except pursuant to one of the following exemptions under the Prospectus Directive as implemented in that Relevant Member State:

- a. to legal entities that are authorized or regulated to operate in the financial markets or, if not so authorized or regulated, whose corporate purpose is solely to invest in securities;
- b. to any legal entity that has two or more of (i) an average of at least 250 employees during its last fiscal year; (ii) a total balance sheet of more than €43,000,000 (as shown on its last annual unconsolidated or consolidated financial statements) and (iii) an annual net turnover of more than €50,000,000 (as shown on its last annual unconsolidated or consolidated financial statements);
- c. to fewer than 100 natural or legal persons (other than qualified investors within the meaning of Article 2(1)(e) of the Prospectus Directive) subject to obtaining our prior consent or the prior consent of any underwriter for any such offer; or
- d. in any other circumstances falling within Article 3(2) of the Prospectus Directive, provided that no such offer of securities shall result in a requirement for the publication by us of a prospectus pursuant to Article 3 of the Prospectus Directive.

France

This document is not being distributed in the context of a public offering of financial securities (offre au public de titres financiers) in France within the meaning of Article L.411-1 of the French Monetary and Financial Code (Code monétaire et financier) and Articles 211-1 et seq. of the General Regulation of the French Autorité des marchés financiers (AMF). The securities have not been offered or sold and will not be offered or sold, directly or indirectly, to the public in France.

This document and any other offering material relating to the securities have not been, and will not be, submitted to the AMF for approval in France and, accordingly, may not be distributed or caused to be distributed, directly or indirectly, to the public in France.

Such offers, sales and distributions have been and shall only be made in France to (i) qualified investors (investisseurs qualifiés) acting for their own account, as defined in and in accordance with Articles L.411-2-II-2° and D.411-1 to D.411-3, D. 744-1, D.754-1 and D.764-1 of the French Monetary and Financial Code and any implementing regulation and/or (ii) a restricted number of non-qualified investors (cercle restreint d'investisseurs) acting for their

own account, as defined in and in accordance with Articles L.411-2-II-2° and D.411-4, D.744-1, D.754-1 and D.764-1 of the French Monetary and Financial Code and any implementing regulation.

Pursuant to Article 211-3 of the General Regulation of the AMF, investors in France are informed that the securities cannot be distributed (directly or indirectly) to the public by the investors otherwise than in accordance with Articles L.411-1, L.411-2, L.412-1 and L.621-8 to L.621-8-3 of the French Monetary and Financial Code.

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Ireland

The information in this document does not constitute a prospectus under any Irish laws or regulations and this document has not been filed with or approved by any Irish regulatory authority as the information has not been prepared in the context of a public offering of securities in Ireland within the meaning of the Irish Prospectus (Directive 2003/71/EC) Regulations 2005 (the Prospectus Regulations). The securities have not been offered or sold, and will not be offered, sold or delivered directly or indirectly in Ireland by way of a public offering, except to (i) qualified investors as defined in Regulation 2(1) of the Prospectus Regulations and (ii) fewer than 100 natural or legal persons who are not qualified investors.

Israel

The securities offered by this prospectus have not been approved or disapproved by the Israeli Securities Authority (the ISA), or ISA, nor have such securities been registered for sale in Israel. The shares may not be offered or sold, directly or indirectly, to the public in Israel, absent the publication of a prospectus. The ISA has not issued permits, approvals or licenses in connection with the offering or publishing the prospectus; nor has it authenticated the details included herein, confirmed their reliability or completeness, or rendered an opinion as to the quality of the securities being offered. Any resale in Israel, directly or indirectly, to the public of the securities offered by this prospectus is subject to restrictions on transferability and must be effected only in compliance with the Israeli securities laws and regulations.

Italy

The offering of the securities in the Republic of Italy has not been authorized by the Italian Securities and Exchange Commission (Commissione Nazionale per le Società e la Borsa, CONSOB pursuant to the Italian securities legislation and, accordingly, no offering material relating to the securities may be distributed in Italy and such securities may not be offered or sold in Italy in a public offer within the meaning of Article 1.1(t) of Legislative Decree No. 58 of 24 February 1998 (Decree No. 58), other than:

to Italian qualified investors, as defined in Article 100 of Decree no. 58 by reference to Article 34-ter of CONSOB Regulation no. 11971 of 14 May 1999 (Regulation no. 11971) as amended (Qualified Investors); and in other circumstances that are exempt from the rules on public offer pursuant to Article 100 of Decree No. 58 and Article 34-ter of Regulation No. 11971 as amended.

Any offer, sale or delivery of the securities or distribution of any offer document relating to the securities in Italy (excluding placements where a Qualified Investor solicits an offer from the issuer) under the paragraphs above must be:

made by investment firms, banks or financial intermediaries permitted to conduct such activities in Italy in accordance with Legislative Decree No. 385 of 1 September 1993 (as amended), Decree No. 58, CONSOB Regulation No. 16190 of 29 October 2007 and any other applicable laws; and

in compliance with all relevant Italian securities, tax and exchange controls and any other applicable laws. Any subsequent distribution of the securities in Italy must be made in compliance with the public offer and prospectus requirement rules provided under Decree No. 58 and the Regulation No. 11971 as amended, unless an exception from those rules applies. Failure to comply with such rules may result in the sale of such securities being declared null and void and in the liability of the entity transferring the securities for any damages suffered by the investors.

Japan

The securities have not been and will not be registered under Article 4, paragraph 1 of the Financial Instruments and Exchange Law of Japan (Law No. 25 of 1948), as amended (the FIEL) pursuant to an exemption from the registration requirements applicable to a private placement of securities to Qualified Institutional Investors (as defined in and in accordance with Article 2, paragraph 3 of the FIEL and the regulations promulgated thereunder). Accordingly, the securities may not be offered or sold, directly or indirectly, in Japan or to, or for the benefit of, any resident of Japan other than Qualified Institutional

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Investors. Any Qualified Institutional Investor who acquires securities may not resell them to any person in Japan that is not a Qualified Institutional Investor, and acquisition by any such person of securities is conditional upon the execution of an agreement to that effect.

Portugal

This document is not being distributed in the context of a public offer of financial securities (oferta pública de valores mobiliários) in Portugal, within the meaning of Article 109 of the Portuguese Securities Code (Código dos Valores Mobiliários). The securities have not been offered or sold and will not be offered or sold, directly or indirectly, to the public in Portugal. This document and any other offering material relating to the securities have not been, and will not be, submitted to the Portuguese Securities Market Commission (Comissão do Mercado de Valores Mobiliários) for approval in Portugal and, accordingly, may not be distributed or caused to be distributed, directly or indirectly, to the public in Portugal, other than under circumstances that are deemed not to qualify as a public offer under the Portuguese Securities Code. Such offers, sales and distributions of securities in Portugal are limited to persons who are qualified investors (as defined in the Portuguese Securities Code). Only such investors may receive this document and they may not distribute it or the information contained in it to any other person.

Sweden

This document has not been, and will not be, registered with or approved by Finansinspektionen (the Swedish Financial Supervisory Authority). Accordingly, this document may not be made available, nor may the securities be offered for sale in Sweden, other than under circumstances that are deemed not to require a prospectus under the Swedish Financial Instruments Trading Act (1991:980) (Sw. lag (1991:980) om handel med finansiella instrument). Any offering of securities in Sweden is limited to persons who are qualified investors (as defined in the Financial Instruments Trading Act). Only such investors may receive this document and they may not distribute it or the information contained in it to any other person.

Switzerland

The securities may not be publicly offered in Switzerland and will not be listed on the SIX Swiss Exchange (SIX) or on any other stock exchange or regulated trading facility in Switzerland. This document has been prepared without regard to the disclosure standards for issuance prospectuses under art. 652a or art. 1156 of the Swiss Code of Obligations or the disclosure standards for listing prospectuses under art. 27 ff. of the SIX Listing Rules or the listing rules of any other stock exchange or regulated trading facility in Switzerland. Neither this document nor any other offering material relating to the securities may be publicly distributed or otherwise made publicly available in Switzerland.

Neither this document nor any other offering material relating to the securities have been or will be filed with or approved by any Swiss regulatory authority. In particular, this document will not be filed with, and the offer of securities will not be supervised by, the Swiss Financial Market Supervisory Authority (FINMA).

This document is personal to the recipient only and not for general circulation in Switzerland.

United Arab Emirates

Neither this document nor the securities have been approved, disapproved or passed on in any way by the Central Bank of the United Arab Emirates or any other governmental authority in the United Arab Emirates, nor have we received authorization or licensing from the Central Bank of the United Arab Emirates or any other governmental authority in the United Arab Emirates to market or sell the securities within the United Arab Emirates. This document does not constitute and may not be used for the purpose of an offer or invitation. No services relating to the securities, including the receipt of applications and/or the allotment or redemption of such shares, may be rendered within the United Arab Emirates by us.

No offer or invitation to subscribe for securities is valid or permitted in the Dubai International Financial Centre.

United Kingdom

Neither the information in this document nor any other document relating to the offer has been delivered for approval to the Financial Services Authority in the United Kingdom and no prospectus (within the meaning of

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section 85 of the Financial Services and Markets Act 2000, as amended (FSMA)) has been published or is intended to be published in respect of the securities. This document is issued on a confidential basis to qualified investors (within the meaning of section 86(7) of FSMA) in the United Kingdom, and the securities may not be offered or sold in the United Kingdom by means of this document, any accompanying letter or any other document, except in circumstances which do not require the publication of a prospectus pursuant to section 86(1) FSMA. This document should not be distributed, published or reproduced, in whole or in part, nor may its contents be disclosed by recipients to any other person in the United Kingdom.

Any invitation or inducement to engage in investment activity (within the meaning of section 21 of FSMA) received in connection with the issue or sale of the securities has only been communicated or caused to be communicated and will only be communicated or caused to be communicated in the United Kingdom in circumstances in which section 21(1) of FSMA does not apply to us.

In the United Kingdom, this document is being distributed only to, and is directed at, persons (i) who have professional experience in matters relating to investments falling within Article 19(5) (investment professionals) of the Financial Services and Markets Act 2000 (Financial Promotions) Order 2005 (FPO), (ii) who fall within the categories of persons referred to in Article 49(2)(a) to (d) (high net worth companies, unincorporated associations, etc.) of the FPO or (iii) to whom it may otherwise be lawfully communicated (together relevant persons). The investments to which this document relates are available only to, and any invitation, offer or agreement to purchase will be engaged in only with, relevant persons. Any person who is not a relevant person should not act or rely on this document or any of its contents.

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INDEMNIFICATION FOR SECURITIES ACT LIABILITIES

Section 145 of the Delaware General Corporation Law, as amended, authorizes us to indemnify any director or officer under certain prescribed circumstances and subject to certain limitations against certain costs and expenses, including attorney's fees actually and reasonably incurred in connection with any action, suit or proceeding, whether civil, criminal, administrative or investigative, to which a person is a party by reason of being one of our directors or officers if it is determined that such person acted in accordance with the applicable standard of conduct set forth in such statutory provisions. Our certificate of incorporation contains provisions relating to the indemnification of director and officers and our by-laws extend such indemnities to the full extent permitted by Delaware law. We may also purchase and maintain insurance for the benefit of any director or officer, which may cover claims for which we could not indemnify such persons.

Insofar as indemnification for liabilities arising under the Securities Act may be permitted to directors, officers or persons controlling us pursuant to the foregoing provisions, or otherwise, we have been advised that in the opinion of the SEC, such indemnification is against public policy as expressed in the Act and is, therefore, unenforceable.

LEGAL MATTERS

The validity of the common stock being offered hereby will be passed upon for us by Reed Smith LLP, New York, New York.

Certain legal matters in connection with this offering will be passed on for the underwriters by Sichenzia Ross Ference Kesner LLP, New York, New York.

EXPERTS

The consolidated financial statements as of June 30, 2016 and 2015 and for each of the years then ended included in this Registration Statement, of which this Prospectus forms a part, have been so included in reliance on the report of BDO USA, LLP, an independent registered public accounting firm (the report on the consolidated financial statements contains an explanatory paragraph regarding the Company's ability to continue as a going concern) appearing elsewhere herein, given on the authority of said firm as experts in auditing and accounting.

WHERE YOU CAN FIND ADDITIONAL INFORMATION

We have filed with the Securities and Exchange Commission, Washington, D.C. 20549, under the Securities Act, a registration statement on Form S-1 relating to the shares of common stock offered hereby. This prospectus does not contain all of the information set forth in the registration statement and the exhibits and schedules thereto. For further information with respect to our Company and the shares we are offering by this prospectus you should refer to the registration statement, including the exhibits and schedules thereto. You may inspect a copy of the registration statement without charge at the Public Reference Section of the Securities and Exchange Commission at Room 1024, 450 Fifth Street, N.W., Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the Securities and Exchange Commission. The Securities and Exchange Commission also maintains an Internet site that contains reports, proxy and information statements and other information regarding registrants that file electronically with the Securities and Exchange Commission. The Securities and Exchange

Commission's World Wide Web address is <http://www.sec.gov>.

We file periodic reports, proxy statements and other information with the Securities and Exchange Commission in accordance with requirements of the Exchange Act. These periodic reports, proxy statements and other information are available for inspection and copying at the regional offices, public reference facilities and Internet site of the Securities and Exchange Commission referred to above.

Information contained on our website is not a prospectus and does not constitute a part of this prospectus.

You should rely only on the information contained in or provided in this prospectus. We have not authorized anyone else to provide you with different information. We are not making an offer of these securities in any state where the offer is not permitted. You should not assume the information in this prospectus is accurate as of any date other than the date on the front of this prospectus.

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INFORMATION INCORPORATED BY REFERENCE

All documents that we subsequently file with the SEC pursuant to Section 13(a), 13(c), 14 or 15(d) of the Exchange Act after the effective date of the registration statement of which this prospectus forms a part and prior to the termination of this offering (unless we specifically provide otherwise in each case, and excluding any information furnished and not filed with the SEC) will be deemed to be incorporated by reference into this prospectus. Information that we file with the SEC will automatically update and may replace information previously filed with the SEC.

We will provide without charge to each person, including any beneficial owner, to whom this prospectus is delivered, upon his or her written or oral request, a copy of any or all reports or documents referred to above which have been or may be incorporated by reference into this prospectus but not delivered with this prospectus excluding exhibits to those documents unless they are specifically incorporated by reference into those documents. You can request those documents from us, at no cost, by writing or telephoning us at: Function(x) Inc., 902 Broadway, 11th Floor, New York, New York 10010 or by calling (212) 231-0092.

You also may access the incorporated reports and other documents referenced above on our website at www.functionxinc.com. The information contained on, or that can be accessed through, our website is not part of this prospectus.

Information furnished under Items 2.02 or 7.01 (or corresponding information furnished under Item 9.01 or included as an exhibit) in any past or future Current Report on Form 8-K that we file with the SEC, unless otherwise specified in such report, is not incorporated by reference in this prospectus.

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As used in this report:	

Function(x) refers to Function(x) Inc., a Delaware corporation formerly known as DraftDay Fantasy Sports Inc. and Viggie Inc. (also herein referred to as the Company)

App refers to the free Viggie application (also herein referred to as the Viggie App)

We, us and our refer to Function(x) and its subsidiaries, individually, or in any combination

SFX refers to SFX Entertainment Inc., a company affiliated with Robert F.X. Sillerman, the Company's Executive Chairman, Chief Executive Officer, and a Director (hereinafter, Mr. Sillerman)

SIC refers to Sillerman Investment Company, LLC, a company affiliated with Mr. Sillerman

SIC II refers to Sillerman Investment Company II, LLC, a company affiliated with Mr. Sillerman

SIC III refers to Sillerman Investment Company III, LLC, a company affiliated with Mr. Sillerman

SIC IV refers to Sillerman Investment Company IV, LLC, a company affiliated with Mr. Sillerman

SIC VI refers to Sillerman Investment Company VI, LLC, a company affiliated with Mr. Sillerman

Reverse Stock Split refers to the reverse stock split effected on September 16, 2016, whereby shareholders are entitled to receive one share for each 20 shares of the Company's common stock.

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(amounts in thousands, except share data)

	December 31, 2016 (Unaudited)	June 30, 2016
Assets		
Current assets:		
Cash and cash equivalents	\$ 122	\$ 537
Marketable securities		2,495
Accounts receivable (net of allowance for doubtful accounts of \$20 at December 31, 2016 and June 30, 2016)	742	307
Prepaid expenses	72	226
Other receivables	50	114
Other current assets	179	110
Current assets of discontinued operations	20	39
Total current assets	1,185	3,828
Restricted cash	498	440
Property & equipment, net	1,260	1,414
Intangible assets, net	9,573	5,339
Goodwill	18,859	11,270
Other assets	432	748
Total assets	\$ 31,807	\$ 23,039
Liabilities, convertible redeemable preferred stock and stockholders equity/(deficit)		
Current liabilities:		
Accounts payable and accrued expenses	\$ 8,901	\$ 11,625
Deferred revenue	682	637
Current portion of loans payable and conversion feature, net	10,794	8,996
Current liabilities of discontinued operations	2,703	2,851
Total current liabilities	23,080	24,109
Loans payable, less current portion		19,716
Deferred revenue	3,446	3,429
Deferred tax liability	102	
Common stock warrant liability	420	10
Other long-term liabilities	901	951
Total liabilities	27,949	48,215
Series A Convertible Redeemable Preferred Stock, \$1,000 stated value, authorized 100,000 shares, issued and outstanding -0- shares as of December 31, 2016 and June 30, 2016		

Commitments and contingencies

Stockholders' equity/(deficit):

Series B Convertible Preferred Stock, \$1,000 stated value, authorized 50,000
shares, issued and outstanding -0- shares as of December 31, 2016 and June 30,
2016

See accompanying Notes to Consolidated Financial Statements

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TABLE OF CONTENTS**Function(x) Inc.****CONSOLIDATED BALANCE SHEETS (continued)**
(amounts in thousands, except share data)

	December 31, 2016 (Unaudited)	June 30, 2016
Series C Convertible Redeemable Preferred Stock, \$1,000 stated value, authorized 100,000 shares, issued and outstanding of 33,175 and 3,000 shares as of December 31, 2016 and June 30, 2016, respectively	34,907	4,940
Series D Preferred Stock, \$1,000 stated value, authorized 150 shares, issued and outstanding -0- shares as of December 31, 2016 and June 30, 2016		
Series E Convertible Preferred Stock, \$1,000 stated value, authorized 10,000 shares, issued and outstanding 4,435 and -0- shares as of December 31, 2016 and June 30, 2016, respectively	7,600	
Common stock, \$0.001 par value: authorized 300,000,000 shares, issued and outstanding 3,244,275 and 3,023,753 shares as of December 31, 2016 and June 30, 2016, respectively	3	3
Additional paid-in-capital	411,075	409,765
Treasury stock, 10,758 shares at December 31, 2016 and June 30, 2016	(11,916)	(11,916)
Accumulated deficit	(438,280)	(428,380)
Accumulated other comprehensive income		(361)
Non-controlling interest	469	773
Total stockholders' equity/(deficit)	3,858	(25,176)
Total liabilities and stockholders' equity/(deficit)	\$31,807	\$23,039
See accompanying Notes to Consolidated Financial Statements		

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TABLE OF CONTENTS**Function(x) Inc.**

CONSOLIDATED STATEMENTS OF OPERATIONS
(amounts in thousands, except share and per share data)
(Unaudited)

	Three Months Ended December 31,		Six Months Ended December 31,	
	2016	2015	2016	2015
Revenues	\$1,215	\$1,782	\$1,875	\$3,255
Selling, general and administrative expenses	(3,574)	(10,025)	(7,614)	(19,409)
Impairment loss (see Note 3)		(30,402)		(30,402)
Operating loss	(2,359)	(38,645)	(5,739)	(46,556)
Other expense:				
Other (expense)/income, net	2,161	1	(326)	3
Interest expense, net	(2,471)	(926)	(4,121)	(1,783)
Total other expense	(310)	(925)	(4,447)	(1,780)
Net loss before provision for income taxes	(2,669)	(39,570)	(10,186)	(48,336)
Income tax expense	(102)		(102)	
Net loss from continuing operations	\$(2,771)	\$(39,570)	\$(10,288)	\$(48,336)
Net loss from discontinued operations		(5,124)	(36)	(9,773)
Net loss	(2,771)	(44,694)	(10,324)	(58,109)
Accretion of Convertible Redeemable Preferred Stock	22	74	44	148
Undeclared Series C Convertible Redeemable Preferred Stock Dividend	(1,017)	(306)	(1,511)	(613)
Add: Net loss attributable to non-controlling interest	141	522	424	689
Net loss attributable to Function(x) Inc. common stockholders	\$(3,625)	\$(44,404)	\$(11,367)	\$(57,885)
Net loss per common share basic and diluted:				
Continuing operations	\$(1.13)	\$(28.25)	\$(3.64)	\$(37.21)
Discontinued operations	\$	\$(3.69)	\$(0.01)	\$(7.56)
Net loss per share attributable to Function(x) Inc. common stockholders basic and diluted	\$(1.13)	\$(31.94)	\$(3.65)	\$(44.77)
Weighted average common shares outstanding basic and diluted	3,196,136	1,390,204	3,113,010	1,292,838
See accompanying Notes to Consolidated Financial Statements				

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Function(x) Inc.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(amounts in thousands)

(Unaudited)

	Three Months Ended December 31,		Six Months Ended December 31,	
	2016	2015	2016	2015
Net loss	\$(2,771)	\$(44,694)	\$(10,324)	\$(58,109)
Other comprehensive income, net of tax:				
Unrealized loss on available for sale securities			(289)	
Reclass of available for sale securities to Consolidated Statements of Operations			650	
Other comprehensive income			361	
Comprehensive loss	\$(2,771)	\$(44,694)	\$(9,963)	\$(58,109)
See accompanying Notes to Consolidated Financial Statements				

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Function(x) Inc.

**CONSOLIDATED STATEMENT OF STOCKHOLDERS
EQUITY/(DEFICIT)
(amounts in thousands)
(Unaudited)**

See accompanying Notes to Consolidated Financial Statements

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TABLE OF CONTENTS**Function(x) Inc.**

CONSOLIDATED STATEMENTS OF CASH FLOWS

(amounts in thousands)

(Unaudited)

	Six months ended December 31,	
	2016	2015
Operating activities:		
Net loss	\$ (10,324)	\$ (58,109)
Adjustments to reconcile net loss to net cash used in operating activities:		
Restricted stock share based compensation	133	9,981
Employee stock options share based compensation	28	346
Accretion of debt issuance costs and discount	1,866	100
Loss on sale of Perk shares and warrants	2,195	
Impairment loss		30,402
Depreciation and amortization	1,420	2,435
Deferred income taxes	102	
Change in fair value of conversion features and warrants	(1,790)	
Gain on settlement of debt	(315)	
Changes in operating assets and liabilities:		
Accounts receivable, net	(435)	2,036
Other receivables	64	621
Restricted cash	(58)	255
Prepaid expenses	154	596
Other assets	246	(5)
Deferred revenue	62	(283)
Accounts payable and accrued expenses	72	6,406
Reward points liability		140
Other liabilities	(50)	(59)
Other		94
Net cash used in operating activities	(6,630)	(5,044)
Investing activities:		
Acquisitions, net of cash acquired		535
Sale of Perk shares and warrants	1,300	
Net cash provided by investing activities	1,300	535
Financing activities:		
Proceeds from loans	6,880	7,100
Repayments on loans	(1,545)	(3,000)
Debt issuance costs	(420)	
Payments related to contingent consideration		(3,076)
Net cash provided by financing activities	4,915	1,024

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Net decrease in cash	(415)	(3,485)
Cash at beginning of period	537	4,217
Cash at end of period	\$ 122	\$ 732
Supplemental cash flow information:		
Cash paid during the period for interest	\$ 30	\$
Non-Cash investing and financing activities:		
Series C conversion with SIC III, SIC IV, and SIC VI notes	\$ 30,175	\$
Series E issuance in connection with the Rant acquisition (Note 6)	7,600	
Rant Note issuance in connection with the Rant acquisition (Note 6)	3,500	
Rant assumed liabilities	1,990	
Warrants issued in connection with Debentures	1,500	
Common stock and warrants issued for DraftDay acquisition		1,757
Common stock and warrants issued for management service contracts		3,475
Loans converted to common stock	885	4,112
See accompanying Notes to Consolidated Financial Statements		

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Function(x) Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

1. Basis of Presentation and Consolidation

Overview

On January 27, 2016, Function(x) Inc. (Company , Function(x) and we) changed its name from Viggie Inc. to DraftDay Fantasy Sports, Inc. (DraftDay), and changed its ticker symbol from VGGL to DDAY. On June 10, 2016, the Company changed its name from DraftDay Fantasy Sports, Inc. to Function(x) Inc., and changed its ticker symbol from DDAY to FNCX. It now conducts business under the name Function(x) Inc.

The Consolidated Financial Statements include the accounts of the Company, its wholly-owned subsidiaries, and DraftDay Gaming Group, Inc. (DDGG). The Company has nine wholly-owned subsidiaries, Function(x) Inc., Project Oda, Inc., Sports Hero Inc., Loyalize Inc., Viggie Media Inc., VX Acquisition Corp., Nextguide Inc., Wetpaint.com, Inc. (Wetpaint), and Choose Digital, Inc. (Choose Digital), each a Delaware corporation. DraftDay owns approximately 60% of the issued and outstanding common stock of DDGG, and also appoints a majority of the members of its Board of Directors.

On September 8, 2015, the Company and its newly created subsidiary DraftDay Gaming Group, Inc. (DDGG) entered into an Asset Purchase Agreement (the Asset Purchase Agreement) with MGT Capital Investments, Inc. (MGT Capital) and MGT Sports, Inc. (MGT Sports), pursuant to which the Company acquired all of the assets of the DraftDay.com business (the DraftDay Business or DraftDay.com) from MGT Capital and MGT Sports.

In December 2015, as a result of the sale of certain assets to Perk and acquisition of the DraftDay Business, we reorganized the organizational management and oversight of the Company into three segments (see Note 4, Segments). Accordingly, prior period financial information has been recast to confirm to the current period presentation. These changes impacted Note 4: Segments and Note 3: Summary of Significant Accounting Policies, with no impact on consolidated net loss or cash flows in any period.

On February 8, 2016, the Company completed the sale of assets related to the Company's rewards business, including the Viggie App, in accordance with the Asset Purchase Agreement (the Perk Agreement) with Perk.com, Inc. (Perk) entered into on December 13, 2015. Management entered into this binding sales agreement following a strategic decision to divest the operations related to the Viggie App and place greater focus on its remaining businesses. The assets, liabilities and operations related to Loyalize Inc., and Nextguide Inc. (as well as the portion of the assets relating to our discontinued rewards business within the Company) have been classified as discontinued operations on the accompanying consolidated financial statements for all periods presented. In accordance with Accounting Standards Codification (ASC) No. 205, *Presentation of Financial Statements*, the inter-segment revenues and expenses related to services provided by Choose Digital to the Viggie rewards business (discontinued operations) are presented at cost in the Consolidated Statements of Operations.

On July 12, 2016, the Company and RACX Inc., a Delaware corporation and wholly-owned subsidiary of the Company (RACX), completed an acquisition pursuant to an Asset Purchase Agreement (the Asset Purchase Agreement) with Rant, Inc., a Delaware corporation, pursuant to which RACX has acquired the assets of Rant (the Asset Purchase) used in the operation of Rant s Rant.com independent media network and related businesses (the Rant Assets). The Company acquired assets of Rant for approximately \$1,990,000 in assumed liabilities, a \$3,000,000 note, and 4,435 shares of Series E Convertible Preferred stock which, upon satisfaction of certain conditions including shareholder approval, will be convertible into shares of our common stock equal to 22% of the fully diluted shares outstanding, in a move to become a market leader in social publishing.

On September 16, 2016, the Company amended its Certificate of Incorporation to effect a reverse stock split of all issued and outstanding shares of common stock at a ratio of 1 for 20 (the Reverse Stock Split). Owners of fractional shares outstanding after the Reverse Stock Split will be paid cash for such fractional

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Function(x) Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

1. Basis of Presentation and Consolidation - (continued)

interests. The effective date of the Reverse Stock Split is September 16, 2016. All common stock share amounts disclosed in these financial statements have been adjusted to reflect the Reverse Stock Split.

Going Concern

These financial statements have been prepared on a going concern basis which assumes the Company's ability to continue to realize its assets and discharge its liabilities in the normal course of business. The Company is unlikely to generate significant revenue or earnings in the immediate or foreseeable future. The continuation of the Company as a going concern is dependent upon the continued financial support from its stockholders, the ability of the Company to obtain necessary equity or debt financing to continue development of its business and to generate revenue. Management intends to raise additional funds through equity and/or debt offerings until sustainable revenues are developed. There is no assurance such equity and/or debt offerings will be successful and therefore there is substantial doubt about the Company's ability to continue as a going concern within one year after the financial statements are issued. The accompanying financial statements do not include any adjustments that might result from the outcome of these uncertainties.

2. Lines of Business

The Company conducts business through three operating segments: Wetpaint, Choose Digital, and DDGG. These operating segments are described below.

Through Wetpaint, the Company reports original news stories and publishes information content covering top television shows, music, celebrities, entertainment news and fashion. Wetpaint publishes more than 55 new articles, videos and galleries each day. The Company generates revenues through wetpaint.com by displaying advertisements to wetpaint.com users as they view its content.

To enhance our digital publishing business, the Company recently acquired assets of Rant Inc. ("Rant"), a leading digital publisher that publishes original content in 13 different verticals, most notably in sports, entertainment, pets, cars, and food. The combined Wetpaint and Rant properties currently have approximately 13.1 million fans on their Facebook pages and generate an average of 16.2 million visits per month.

Over the six months ended December 31, 2016, the Company focused its efforts on growing Wetpaint user engagement and monetization. The Company anticipates applying the same focus and methodology in the near future to the Rant sites to continue to grow and strengthen its publishing business.

Choose Digital is a white-label digital marketplace featuring a recent and wide range of digital content, including music, movies, TV shows, eBooks and audiobooks. The content is sourced from the world's leading record companies and book publishers and an aggregator of movie and TV content. Choose Digital generates revenues when participants in Choose Digital's clients' loyalty programs redeem loyalty credits for digital content provided by Choose Digital. For example, if a participant in a loyalty program redeems credits for a song download provided by Choose Digital, the client loyalty program pays Choose Digital for the download.

The Company's wholly owned subsidiary, DDGG, made a recent investment in the DraftDay.com platform. Through DraftDay.com, users can draft a fantasy sports team within a salary cap, follow game action and reap rewards. DraftDay.com will continue to offer high-quality entertainment to consumers as well as to businesses desiring turnkey solutions to new revenue streams. See Note 6, Acquisitions, for further details on this acquisition.

3. Summary of Significant Accounting Policies

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and notes required by generally accepted accounting principles for complete financial statements. In the opinion of management,

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Function(x) Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

3. Summary of Significant Accounting Policies - (continued)

all adjustments (consisting of normal, recurring adjustments) considered necessary for a fair presentation have been included. Operating results for the six months ended December 31, 2016 are not necessarily indicative of the results that may be expected for the year ending June 30, 2017.

Cash and Cash Equivalents and Restricted Cash

The Company considers all highly liquid securities purchased with original maturities of 90 days or less to be cash equivalents. Cash equivalents are stated at cost which approximates market value and primarily consists of money market funds that are readily convertible into cash. Restricted cash comprises amounts held in deposit that were required as collateral under leases of office space.

Marketable Securities

In February 2016, the Company received 1,370,000 shares of Perk's stock, which is publicly traded on the Toronto Stock Exchange, as part of the consideration in the sale of assets described in the Perk Agreement. These securities are short-term marketable securities, and have been classified as available-for-sale securities. Pursuant to Accounting Standards Codification (ASC) 320-10, *Investments - Debt and Equity Securities*, the Company's marketable securities are marked to market on a quarterly basis, with unrealized gains and losses recorded in equity as Other Comprehensive Income/Loss. On September 30, 2016, the Company sold to Perk the remaining shares (1,013,068) of Perk common stock, the warrants for additional shares, and the right to the Earn-Out Shares received from Perk on the sale of the Viggie rewards business on February 8, 2016. The Company received \$1,300,000 from Perk as consideration therefor. The execution of the Securities Purchase Agreement and closing were simultaneous. In connection with the sale of the Perk shares, the warrants for additional shares and the right to the Earn-Out Shares, the Company recorded a loss of \$2,195,000 in the Other Expense line item of the Consolidated Statements of Operations for the six months ended December 31, 2016.

Accounts Receivable

Accounts receivable are recorded net of an allowance for doubtful accounts. The Company's allowance for doubtful accounts is based upon historical loss patterns, the number of days that the billings are past due and an evaluation of the potential risk associated with delinquent accounts. The Company also considers any changes to the financial condition of its customers and any other external market factors that could impact the collectability of its receivables in the determination of its allowance for doubtful accounts. The Company's allowance for doubtful accounts as of December 31, 2016 and June 30, 2016 was approximately \$20,000.

Concentration of Credit Risk

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of cash and cash equivalents and trade accounts receivable. The Company maintains cash and cash equivalents with domestic financial institutions of high credit quality. The Company performs periodic evaluations of the relative credit standing of all of such institutions.

The Company performs ongoing credit evaluations of customers to assess the probability of accounts receivable collection based on a number of factors, including past transaction experience with the customer, evaluation of their credit history, and review of the invoicing terms of the contract. The Company generally does not require collateral. The Company maintains reserves for potential credit losses on customer accounts when deemed necessary. Actual credit losses during the three months ended December 31, 2016 and December 31, 2015 were \$0.

Fair Value of Financial Instruments

The carrying amounts reported in the consolidated balance sheets for cash and cash equivalents, accounts and other receivables, accounts payable and accrued liabilities approximate fair value because of the immediate or

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Function(x) Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

3. Summary of Significant Accounting Policies - (continued)

short-term maturity of these financial instruments. The carrying amount of Perk marketable securities held is marked-to-market on a quarterly basis using the closing day share price of the last business day of the quarter. The changes to fair value are recorded in Other Comprehensive Income/Loss. The carrying amount of Perk warrants held is marked-to-market on a quarterly basis using the Monte Carlo valuation model. The changes to fair value are recorded in the Consolidated Statement of Operations. The carrying amount of loans payable approximates fair value as current borrowing rates for the same, or similar issues, are the same as those that were given to the Company at the issuance of these loans.

The carrying amounts of the Debenture Conversion feature, Rant Note Conversion feature and warrants is marked-to-market on a quarterly basis using a Monte Carlo simulation. The changes to fair value are recorded as other (expense)/income in the Consolidated Statement of Operations

Property and Equipment

Property and equipment (consisting primarily of computers, software, furniture and fixtures, and leasehold improvements) is recorded at historical cost and is depreciated using the straight-line method over their estimated useful lives. The useful life and depreciation method are reviewed periodically to ensure that they are consistent with the anticipated pattern of future economic benefits. Expenditures for maintenance and repairs are charged to operations as incurred, while betterments are capitalized. Gains and losses on disposals are included in the results of operations. The estimated useful lives of the Company's property and equipment is as follows: computer equipment and software: 3 years; furniture and fixtures: 4 years; and leasehold improvements: the lesser of the lease term or life of the asset.

Business Combinations and Goodwill

Business combinations are accounted for using the acquisition method of accounting. The Company allocates the purchase price of acquired companies to the identifiable assets acquired, liabilities assumed and any non-controlling interest based on their acquisition date estimated fair values. Goodwill as of the acquisition date is measured as the excess of consideration transferred and the net of the acquisition date fair values of the identifiable assets acquired and liabilities assumed. Any contingent consideration to be transferred to the acquiree is recognized at fair value at the acquisition date.

Determining the fair value of assets acquired and liabilities assumed requires the Company to make significant estimates and assumptions, including assumptions related to future cash flows, discount rates, asset lives and the probability of future cash pay-outs related to contingent consideration. The estimates of fair value are based upon assumptions believed to be reasonable by management, but are inherently uncertain and unpredictable and, therefore,

actual results may differ from estimates. As a result, during the measurement period, which may be up to one year from the acquisition date, the Company may record adjustments to the fair value of assets acquired and liabilities assumed, with the corresponding offset to goodwill. Upon the conclusion of the measurement period or final determination of the fair value of assets acquired or liabilities assumed, whichever comes first, any subsequent adjustments are recorded to the Consolidated Statements of Operations.

For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Company's reporting units that are expected to benefit from the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units. Where goodwill has been allocated to a reporting unit and part of the operation within that unit is disposed of, the goodwill associated with the disposed operation is included in the carrying amount of the operation when determining the gain or loss on disposal. Goodwill disposed in these circumstances is measured based on the relative fair values of the disposed operation and the portion of the reporting units retained.

As required by ASC 350, *Goodwill and Other Intangible Assets*, the Company tests goodwill for impairment during the fourth quarter of its fiscal year. Goodwill is not amortized, but instead tested for

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Function(x) Inc.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)**

3. Summary of Significant Accounting Policies - (continued)

impairment at the reporting unit level at least annually and more frequently upon occurrence of certain events. As noted above, the Company has three reporting units. The annual goodwill impairment test is a two step process. First, the Company determines if the carrying value of its reporting unit exceeds fair value, which would indicate that goodwill may be impaired. If the Company then determines that goodwill may be impaired, it compares the implied fair value of the goodwill to its carry amount to determine if there is an impairment loss.

Historically, the Company had one reporting unit. However, in connection with the sale of a significant portion of the Company's assets (see Note 1, Basis of Presentation and Consolidation), the remaining operations were divided into three reporting units (see Note 4, Segments). The Company engaged a third-party valuation firm to test the Choose Digital and Wetpaint reporting units for goodwill impairment. The DDGG reporting unit was not tested for impairment at December 31, 2015 as the acquisition of this entity occurred in September 2015. The Company determined that the fair value of both of the Wetpaint and Choose Digital reporting units were significantly below their respective carrying values, indicating that goodwill related to these reporting units may be impaired. The Company determined the fair value of all long-lived assets other than goodwill related to each reporting unit and calculated the residual goodwill value for each. Upon comparing the residual goodwill values to the respective carrying values, the Company determined that there was an impairment loss on both the Choose Digital and Wetpaint reporting units.

The Company recorded an impairment loss of \$4,335,000 related to the Choose Digital reporting unit and \$10,708,000 related to the Wetpaint reporting unit during the three months ended December 31, 2015. Upon the finalization of the December 31, 2015 Choose Digital and Wetpaint goodwill impairment analysis, the consolidated goodwill ending balances as of March 31, 2016 were adjusted by \$3,350,000 at June 30, 2016. The Company also recorded an additional goodwill impairment loss of \$1,672,000 in the Selling, general and administrative expense line and reduced the gain on the sale of the Viggie Business by \$1,672,000 in the Consolidated Statements of Operations during the nine months ended March 31, 2016 as a result of the finalization of the December 2015 Choose Digital and Wetpaint impairment analysis. There were no impairments recorded during the three and six months ended December 31, 2016.

At June 30, 2016, the Company determined that the fair value of the DDGG reporting unit was significantly below its carrying value, indicating that goodwill may be impaired. The Company determined the fair value of all long-lived assets other than goodwill and calculated the residual goodwill for the reporting unit. The residual goodwill was higher than the carrying value of goodwill related to the DDGG reporting unit, therefore the Company did not record an impairment loss for DDGG goodwill during the the year ended June 30, 2016. There were no impairments recorded during the three and six months ended December 31, 2016.

Other Long-Lived Assets

The Company accounts for the impairment of long-lived assets other than goodwill in accordance with ASC 360, *Property, Plant, and Equipment* (ASC 360), which addresses financial accounting and reporting for the impairment or disposal of long-lived assets. ASC 360 requires impairment losses to be recorded on long-lived assets used in operations when indicators of impairment are present and the undiscounted cash flows estimated to be generated by those assets (fair value) are less than the assets' carrying amounts. In that event, a loss is recognized based on the amount by which the carrying amount exceeds the fair value of the long-lived assets. Loss on long-lived assets to be disposed of is determined in a similar manner, except that fair values are reduced for the cost of disposal.

At December 31, 2015, as described above, the Company determined that the fair value of the Choose Digital and Wetpaint reporting units tested was significantly below the respective carrying values and assessed the fair values of the long-lived assets other than goodwill for each reporting unit. Upon comparing the fair values of the long-lived assets to their respective carrying values, the Company recorded a loss of \$1,331,000 on

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Function(x) Inc.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)**

3. Summary of Significant Accounting Policies - (continued)

intangible assets related to Choose Digital's software and licenses, and a loss of \$11,418,000 on intangible assets related to Wetpaint's technology, trademark, customer relationships and non-competition agreements, during the three months ended December 31, 2015. No impairments were recorded during the three and six months ended December 31, 2016.

At June 30, 2016, the Company determined that certain intangible assets related to the acquisition of Draftday.com were impaired. At June 30, 2016, DDGG's Management Services Agreement By and Between DraftDay Gaming Group, Inc. and Sportech Racing, LLC (Sportech MSA) terminated, which led to a significantly lower revenues forecast for the reporting unit. As a result, the Company determined that the intangible assets related to internally developed software, trade name and non-compete agreements were impaired. The Company recorded a loss of \$749,000 on intangible assets related to DDGG during the year ended June 30, 2016.

No impairments were recorded during the three and six months ended December 31, 2016.

Capitalized Software

The Company records amortization of acquired software on a straight-line basis over the estimated useful life of the software.

In addition, the Company records and capitalizes internally generated computer software and, appropriately, certain internal costs have been capitalized in the amount of \$1,498,000 as of December 31, 2016 and June 30, 2016, in accordance with ASC 350-40 *Internal-use Software* . At the time software is placed into service, the Company records amortization on a straight-line basis over the estimated useful life of the software. The change in capitalized software is due to impairment of long-term assets related to the Choose Digital and Wetpaint businesses described earlier, as well as the abandonment of certain technology as of January 1, 2016, and internal development costs.

DDGG Player Deposits

The Company maintains a separate bank account to hold player deposits in accordance with current industry regulations. The player deposits bank account represents money reserved for player withdrawals and winnings. Accordingly, the Company records an offsetting liability at the time of receipt of player deposits.

Deferred Rent

The Company leases its corporate office, and as part of the lease agreement the landlord provided a rent abatement for the first 10 months of the lease. In 2014, the Company entered into two lease agreements for its satellite offices which

provided for tenant improvement work sponsored by the landlords. The abatement and landlord sponsored improvements have been accounted for as a reduction of rental expense over the life of the lease. The Company accounts for rental expense on a straight-line basis over the entire term of the lease. Deferred rent is equal to the cumulative timing difference between actual rent payments and recognized rental expense. The satellite office leases were terminated in Fiscal 2016. The Company wrote-off residual leasehold improvement and deferred rent balances related to landlord sponsored tenant improvement work, and recorded a write-off of approximately \$83,000 in the Consolidated Statements of Operations for the year ended June 30, 2016.

Revenue Recognition

The Company recognizes revenue when: (1) persuasive evidence exists of an arrangement with the customer reflecting the terms and conditions under which products or services will be provided; (2) delivery has occurred or services have been provided; (3) the fee is fixed or determinable; and (4) collection is reasonably assured. For all revenue transactions, the Company considers a signed agreement, a binding insertion order or other similar documentation to be persuasive evidence of an arrangement.

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Function(x) Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

3. Summary of Significant Accounting Policies - (continued)

Advertising Revenue: the Company generates advertising revenue primarily from third-party advertising via real-time bidding, which is typically sold on a per impression basis.

Deferred Revenue: deferred revenue consists principally of prepaid but unrecognized revenue. Deferred revenue is recognized as revenue when the services are provided and all other revenue recognition criteria have been met.

Barter Revenue: barter transactions represent the exchange of advertising or programming for advertising, merchandise or services. Barter transactions which exchange advertising for advertising are accounted for in accordance with Emerging Issues Task Force Issue No. 99-17 *Accounting for Advertising Barter Transactions* (ASC Topic 605-20-25). Such transactions are recorded at the fair value of the advertising provided based on the Company's own historical practice of receiving cash for similar advertising from buyers unrelated to the counter party in the barter transactions. Barter transactions which exchange advertising or programming for merchandise or services are recorded at the monetary value of the revenue expected to be realized from the ultimate disposition of merchandise or services.

The Company recognized barter revenue and barter expense in the amount of \$0 and \$217,000 for the three months ended December 31, 2016 and December 31, 2015, respectively. The Company recognized barter revenue and barter expense in the amount of \$0 and \$424,000 for the six months ended December 31, 2016 and December 31, 2015, respectively.

Stock-Based Compensation

The Company accounts for stock-based compensation in accordance with ASC 718, *Compensation - Stock Compensation* (ASC 718). Under the fair value recognition provisions of ASC 718, stock-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as expense ratably over the requisite service period. The Company uses the Black-Scholes option pricing model to determine the fair value of stock options and warrants issued. Stock-based awards issued to date are comprised of both restricted stock awards (RSUs) and employee stock options.

Marketing

Marketing costs are expensed as incurred. Marketing expense for the Company for the three months ended December 31, 2016 and December 31, 2015 was approximately \$82,000 and \$239,000 respectively. Marketing expense for the six months ended December 31, 2016 and December 31, 2015 was approximately \$113,000 and \$480,000, respectively.

Income Taxes

The Company uses the liability method of accounting for income taxes as set forth in ASC 740, *Income Taxes* (ASC 740). Under the liability method, deferred taxes are determined based on the temporary differences between the financial statement and tax basis of assets and liabilities using tax rates expected to be in effect during the years in which the basis differences reverse. A valuation allowance is recorded when it is unlikely that the deferred tax assets will not be realized. The Company assesses its income tax positions and record tax benefits for all years subject to examination based upon the Company's evaluation of the facts, circumstances and information available at the reporting date. In accordance with ASC 740-10, for those tax positions where there is a greater than 50% likelihood that a tax benefit will be sustained, the Company's policy will be to record the largest amount of tax benefit that is more likely than not to be realized upon ultimate settlement with a taxing authority that has full knowledge of all relevant information. For those income tax positions where there is less than 50% likelihood that a tax benefit will be sustained, no tax benefit will be recognized in the financial statements.

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Function(x) Inc.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)**

3. Summary of Significant Accounting Policies - (continued)

Comprehensive Loss

In accordance with ASC 220, *Comprehensive Income*, the Company reports by major components and as a single total, the change in its net assets during the period from non-owner sources. Comprehensive income consists of net income (loss), accumulated other comprehensive income (loss), which includes certain changes in equity that are excluded from net income (loss). The Company's comprehensive loss for all periods presented is related to the effect of unrealized gain on available for sale marketable securities.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States 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 expenses during the reporting period. These estimates include, among others, fair value of financial assets and liabilities, net realizable values on long-lived assets, certain accrued expense accounts, and estimates related to stock-based compensation. Actual results could differ from those estimates.

During the three months ended September 30, 2016, there have been no significant changes related to the Company's critical accounting policies and estimates as disclosed in Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations set forth in the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2016.

Recently Issued Accounting Pronouncements

In January 2017, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update 2017-04, *Simplifying the Test for Goodwill Impairment* (ASU 2017-04). The update requires an entity to perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An entity should recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit's fair value but the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. This guidance is effective for annual periods beginning after December 15, 2019, including interim periods within those periods. The Company does not expect the update to have a material impact on its consolidated financial statements.

In January 2017, the FASB issued Accounting Standards Update 2017-01, *Business Combinations* (Topic 805): *Clarifying the Definition of a Business* (ASU 2017-01). The update provides a criteria for determining when an integrated set of assets and activities is not a business. The criteria requires that when substantially all of the fair value of gross assets are acquired in concentrated into a single identifiable asset or a group of similar identifiable assets, the

integrated sets of assets and activities is not a business. Even if this criteria is not met, this update requires that the set of assets and activities must include an input and substantive processes that together significantly contribute to creating an output, at a minimum, and removes the evaluation of whether a market participant could replace the missing elements. This guidance is effective for annual periods beginning after December 15, 2017, including interim periods within those periods. The Company does not expect the update to have a material impact on its consolidated financial statements.

In November 2016, the FASB issued Accounting Standards Update 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash (a consensus of the FASB Emerging Issues Task Force) (ASU 2016-18). This update requires entities to show the changes in the total of cash, cash equivalents, restricted cash and restricted cash equivalents in the statement of cash flows. As a result, entities will no longer present transfers between cash and cash equivalents and restricted cash and restricted cash equivalents in the statement of cash flows. This guidance is effective for fiscal years beginning after December 15, 2017, and interim periods for those years. The Company does not expect the standard to have a material impact on its consolidated financial statements.

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Function(x) Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

3. Summary of Significant Accounting Policies - (continued)

In October 2016, the FASB issued Accounting Standards Update 2016-16, Accounting for Income Taxes: Intra-Entity Asset Transfers of Assets Other than Inventory (ASU 2016-16). This update eliminates the exception for all intra-entity sales of assets other than inventory. As a result, a reporting entity would recognize the tax expense from the sale of the asset in the seller's tax jurisdiction when the transfer occurs, even though the pre-tax effects of that transaction are eliminated in consolidation. Any deferred tax asset that arises in the buyer's jurisdiction would also be recognized at the time of the transfer. ASU 2016-16 is effective for financial statements issued for annual periods beginning after December 15, 2017. The Company does not expect the standard to have a material impact on its consolidated financial statements.

In May 2016, FASB issued Accounting Standards Update 2016-12, Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients (ASU 2016-12). The amendments in this update affect the guidance in Accounting Standards Update 2014-09, Revenue from Contracts with Customers (Topic 606) (ASU 2014-09), which is not yet effective. This update focuses on improving several aspects of ASU 2014-09, such as assessing the collectability criterion in paragraph 606-10-25-1(e) and accounting for contracts that do not meet the criteria for step 1; presentation of sales taxes and other similar taxes collected from customers; non-cash consideration; contract modifications at transition; and completed contracts at transition. ASU 2016-12 is effective for financial statements issued for annual periods beginning after December 15, 2017. The Company does not expect the standard to have a material impact on its consolidated financial statements.

In April 2016, the FASB issued Accounting Standards Update 2016-10, Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing (ASU 2016-10). The amendments in this update affect the guidance in ASU 2014-09, which is not yet effective. This update focuses on clarifying the following two aspects of ASU 2014-09: identifying performance obligations and the licensing implementation guidance, while retaining the related principles for those areas. ASU 2016-10 is effective for financial statements issued for annual periods beginning after December 15, 2017. The Company does not expect the standard to have a material impact on its consolidated financial statements.

In March 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. 2016-09, Compensation—Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting (ASU 2016-09). This update is intended to improve the accounting for employee share-based payments and affects all organizations that issue share-based payment awards to their employees. Several aspects of the accounting for share-based payment award transactions are simplified, including: (a) income tax consequences; (b) classification of awards as either equity or liabilities; and (c) classification on the statement of cash flows. ASU 2016-09 is effective for financial statements issued for annual periods beginning after December 15, 2016. The Company is currently in the process of evaluating the impact of adoption of ASU 2016-09 on its consolidated financial statements.

In February 2016, FASB issued Accounting Standards Update No. 2016-02, Leases (ASU 2016-02). ASU 2016-02 requires lessees to recognize the following for all leases (with the exception of short-term leases) at the commencement date: a lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis; and a right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. Under the new guidance, lessor accounting is largely unchanged. Certain targeted improvements were made to align, where necessary, lessor accounting with the lessee accounting model and Topic 606, Revenue from Contracts with Customers. The new lease guidance also simplified the accounting for sale and leaseback transactions primarily because lessees must recognize lease assets and lease liabilities. Lessees will no longer be provided with a source of off-balance sheet financing. Lessees (for capital and operating leases) and lessors (for sales-type, direct financing, and operating leases) must apply a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. The modified retrospective approach would not require any transition accounting for leases that expired before

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Function(x) Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

3. Summary of Significant Accounting Policies - (continued)

the earliest comparative period presented. Lessees and lessors may not apply a full retrospective transition approach. ASU 2016-02 is effective for financial statements issued for annual periods beginning after December 15, 2018. The Company is currently in the process of evaluating the impact of adoption of ASU 2016-02 on its consolidated financial statements.

In January 2016, FASB issued Accounting Standards Update No. 2016-01, *Financial Instruments- Overall: Recognition and Measurement of Financial Assets and Financial Liabilities* (ASU 2016-01). ASU 2016-01 requires all equity investments to be measured at fair value with changes in the fair value recognized through net income (other than those accounted for under equity method of accounting or those that result in consolidation of the investee). Additionally, it requires an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments. Lastly, the standard eliminates the requirement to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet. ASU 2016-01 is effective for financial statements issued for annual periods beginning after December 15, 2017, and interim periods within those annual periods. The Company does not expect the standard to have a material impact on its consolidated financial statements.

In November 2015, FASB issued Accounting Standards Update No. 2015-17, *Income taxes: Balance Sheet Classification of Deferred Taxes* Business (ASU 2015-17). Topic 740, *Income Taxes*, requires an entity to separate deferred income tax liabilities and assets into current and noncurrent amounts in a classified statement of financial position. Deferred tax liabilities and assets are classified as current or noncurrent based on the classification of the related asset or liability for financial reporting. Deferred tax liabilities and assets that are not related to an asset or liability for financial reporting are classified according to the expected reversal date of the temporary difference. To simplify the presentation of deferred income taxes, ASU 2015-17 requires that deferred income tax liabilities and assets be classified as noncurrent in a classified statement of financial position. ASU 2015-17 is effective for financial statements issued for annual periods beginning after December 15, 2016, and interim periods within those annual periods. The Company does not expect the standard to have a material impact on its consolidated financial statements.

In September 2015, the FASB issued Accounting Standard Update No. 2015-16, *Business Combinations Simplifying the Accounting for Measurement-Period Adjustments* (ASU 2015-16). This standard requires that an acquirer retrospectively adjust provisional amounts recognized in a business combination, during the measurement period. To simplify the accounting for adjustments made to provisional amounts, the amendments in the ASU 2015-16 require that the acquirer recognize adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amount is determined. The acquirer is required to also record, in the same period's financial statements, the effect on earnings of changes in depreciation, amortization, or other income effects, if any, as a result of the change to the provisional amounts, calculated as if the accounting had been completed at the

acquisition date. In addition an entity is required to present separately on the face of the income statement or disclose in the notes to the financial statements the portion of the amount recorded in current-period earnings by line item that would have been recorded in previous reporting periods if the adjustment to the provisional amounts had been recognized as of the acquisition date. ASU 2015-16 is effective for fiscal years beginning after December 15, 2016, and interim periods within fiscal years beginning after December 15, 2017 (July 1, 2017 for the Company). The Company does not believe that the adoption of ASU 2015-16 will have a material impact on its consolidated financial statements.

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TABLE OF CONTENTS**Function(x) Inc.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)****4. Segments**

Historically, the Company had one operating segment. However, in connection with the sale of the Viggie rewards business (discontinued operations) to Perk in February 2016, which represented a significant portion of the Company's assets and revenues, the Company's remaining operations were divided into three operating segments. These segments offer different products and services and are currently presented separately in internal management reports, and managed separately.

Wetpaint: a media channel reporting original news stories and publishing information content covering top television shows, music, celebrities, entertainment news and fashion.

Choose Digital: a business-to-business platform for delivering digital content.

DDGG: a business-to-business operator of daily fantasy sports.

The accounting policies followed by the segments are described in Note 3, Summary of Significant Accounting Policies. The operating segments of the Company include the assets, liabilities, revenues and expenses that management has determined are specifically or primarily identifiable to each segment, as well as direct and indirect costs that are attributable to the operations of each segment. Direct costs are the operational costs that are administered by the Company following the shared services concept. Indirect costs are the costs of support functions that are provided on a centralized or geographic basis by the Company, which include, but are not limited to, finance, human resources, benefits administration, procurement support, information technology, legal, corporate strategy, corporate governance and other professional services and general commercial support functions.

Central support costs have been allocated to each operating segment based on a specific identification basis or, when specific identification is not practicable, a proportional cost allocation method (primarily based on net sales or direct payroll costs), depending on the nature of the services received. Management considers that such allocations have been made on a reasonable basis, but may not necessarily be indicative of the costs that would have been incurred if the operating segments had been operated on a stand-alone basis for the periods presented.

Information regarding the results of each reportable segment is included below. Performance is measured based on unit profit after tax, as included in the internal management reports that are reviewed by the chief operating decision maker, who is the Company's Chief Executive Officer. Business unit profit is used to measure performance as management believes that such information is the most relevant in evaluating the success of each business and determining the going forward strategy for the Company as a whole.

Information about reportable segments (amounts in thousands):

Three Months Ended December 31,							
Wetpaint		Choose Digital		DDGG		Total	
2016	2015	2016	2015	2016	2015	2016	2015

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External revenues	\$834	\$530	\$	\$217	\$256	\$243	\$1,090	\$990
Inter-segment revenues ⁽¹⁾				668				668
Net loss, net of income taxes ⁽²⁾	(1,585)	(28,478)	(47)	(3,645)	(715)	(1,533)	(2,347)	(33,656)

Notes:

- (1) The Choose Digital business provides digital content to the Viggie business. These inter-segment revenues are presented at Choose Digital's cost in this schedule and in the consolidated statements of operations.
- (2) The net loss figures presented exclude certain corporate expenses detailed in the reconciliation to the consolidated net loss below.

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TABLE OF CONTENTS**Function(x) Inc.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)****4. Segments - (continued)**

	Six Months Ended December 31,							
	Wetpaint		Choose Digital		DDGG		Total	
	2016	2015	2016	2015	2016	2015	2016	2015
External revenues	\$1,206	\$1,046	\$58	\$415	\$361	\$326	\$1,625	\$1,787
Inter-segment revenues ⁽¹⁾				1,219				1,219
Net loss, net of income taxes ⁽²⁾	(3,662)	(30,338)	(448)	(4,120)	(1,467)	(1,507)	(5,577)	(35,965)

Notes:

(1) The Choose Digital business provides digital content to the Viggie business. These inter-segment revenues are presented at Choose Digital's cost in this schedule and in the consolidated statements of operations.

(2) The net loss figures presented exclude certain corporate expenses detailed in the reconciliation to the consolidated net loss below.

Reconciliation of revenues attributable to reportable segments to consolidated revenues from continuing operations (amounts in thousands):

	Three Months Ended December 31,		Six Months Ended December 31,	
	2016	2015	2016	2015
Revenues attributable to reportable segments	\$ 1,090	\$ 990	\$ 1,625	\$ 1,787
Licensing revenues related to SFX licensing agreement	125	125	250	250
Other revenues		667		1,218
Revenues per Consolidated Statements of Operations	\$ 1,215	\$ 1,782	\$ 1,875	\$ 3,255
Reconciliation of net loss for reportable segments, net of income taxes to consolidated net loss from continuing operations, net of income taxes (amounts in thousands):				

	Three Months Ended December 31,		Six Months Ended December 31,	
	2016	2015	2016	2015
Net loss for reportable segments, net of income taxes	\$(2,347)	\$(33,656)	\$(5,577)	\$(35,965)
Other net gain (loss)	2,184	(88)	(429)	(297)
	(163)	(33,744)	(6,006)	(36,262)
	(137)	(4,250)	(161)	(8,500)

Stock compensation related to corporate financing activities⁽¹⁾

Corporate expenses allocated to discontinued operations ⁽²⁾	(650)	(1,791)
Interest expense ⁽³⁾	(2,471) (926)	(4,121) (1,783)
Consolidated net loss from continuing operations, net of income taxes	\$(2,771) \$(39,570)	\$(10,288) \$(48,336)

Notes:

Stock compensation expense related to RSUs, options and warrants issues in connection with financing activities.

(1) Expenses related to financing activities are considered to be corporate expenses and are not allocated to reportable segments.

(2) Certain corporate expenses were allocated to the Viggie segment, however such expenses are not classified as discontinued operations because they are fixed and are not affected by the sales transaction.

(3) Interest expense related to corporate debt instruments is not allocated to reportable segments.

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(Unaudited)****4. Segments - (continued)**

Total assets for reportable segments (amounts in thousands):

	December 31, 2016	June 30, 2016
Wetpaint	\$ 21,234	\$ 8,495
Choose Digital	5,226	5,416
DDGG	3,713	3,740
Total assets for reportable segments	\$ 30,173	\$ 17,651
Reconciliation of assets attributable to reportable segments to consolidated assets of continuing operations (amounts in thousands):		

	December 31, 2016	June 30, 2016
Total assets for reportable segments	\$ 30,173	\$ 17,104
Other assets ⁽¹⁾	1,614	5,896
Total consolidated assets, net of current and non-current assets of discontinued operations	\$ 31,787	\$ 23,000

Notes:

(1) Corporate assets that are not specifically related to any of the reporting units.

The Company continues to support the cash needs and operations of DDGG. As of December 31, 2016 the Company has transferred \$1,096,000 to the DDGG subsidiary. A portion of these transfers, or \$500,000, was funded as part of the purchase price commitment. The remaining transfers are part of the subscription agreement entered into with DDGG on May 12, 2016.

On July 12, 2016, to enhance the Company's digital publishing business, the Company acquired assets of Rant. Rant is a leading digital publisher that publishes original content in 13 different verticals, most notably in sports, entertainment, pets, cars, and food. Rant results of operations are included in the Company's digital publishing segment, Wetpaint.

5. Discontinued Operations

On February 8, 2016, the Company completed the sale of assets related to the Company's rewards business, including the Viggle App, in accordance with the Perk Agreement entered into on December 13, 2015. Management entered into this binding sales agreement following a strategic decision to divest the operations related to the Viggle App and place greater focus on its remaining businesses. The Company has classified the Viggle assets, liabilities and operations as discontinued operations in the accompanying Consolidated Financial Statements for all periods presented. In accordance with ASC No. 205, *Presentation of Financial Statements*, the inter-segment revenues and expenses related to services provided by Choose Digital to the Viggle rewards business (discontinued operations) are presented at cost in the Consolidated Statements of Operations.

On December 13, 2015, the Parent entered into the Perk Agreement. Perk's shares are currently traded on the Toronto Stock Exchange. On February 8, 2016, pursuant to the Perk Agreement, the Company completed the sale of the assets related to the Company's rewards business, including Viggle's application, to Perk. The total consideration received net of transaction fees was approximately \$5,110,000, and consisted of the following:

- 1,370,000 shares of Perk common stock, a portion of which was placed in escrow to satisfy any potential indemnification claims;
- 2,000,000 shares of Perk common stock if Perk's total revenues exceed USD \$130,000,000 for the year ended December 31, 2016 or December 31, 2017;

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TABLE OF CONTENTS**Function(x) Inc.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)****5. Discontinued Operations - (continued)**

a warrant entitling the Company to purchase 1,000,000 shares of Perk common stock at a strike price of CDN \$6.25 per share in the event the volume weighted average price (VWAP) of shares of Perk common stock is greater than or equal to CDN \$12.50 for 20 consecutive trading days in the two year period following the closing of the transaction;

a warrant entitling the Company to purchase 1,000,000 shares of Perk common stock at a strike price of CDN \$6.25 per share in the event that the VWAP of Perk common stock is greater than or equal to CDN \$18.75 for 20 consecutive trading days in the two year period following the closing of the transaction, and

Perk assumed certain liabilities of the Company, consisting of the Viggle points liability.

At the time the Company entered into the Perk Agreement, Perk provided the Company with a \$1,000,000 secured line of credit, which the Company fully drew down. The Company had the option of repaying amounts outstanding under that line of credit by reducing the number of Initial Perk Shares by 130,000. The Company exercised this option and received 1,370,000 shares of Perk common stock at closing, and the amounts outstanding under the Line of Credit were deemed paid in full.

At the closing, 37.5% (562,600) of the Initial Perk Shares were issued and delivered to an escrow agent to be used exclusively for the purpose of securing the Company's indemnification obligations under the Perk Agreement.

Additionally, after the closing, the Company delivered 357,032 of the Initial Perk Shares to Gracenote, Inc. and Tribune Media Services, Inc., former providers of technology services of the Company, as per the Settlement and Transfer Agreement dated February 5, 2016, to satisfy an obligation. The Company recognized a gain of \$593,000 in the Consolidated Statements of Operations for the year ended June 30, 2016.

On September 30, 2016, the Company sold to Perk the remaining shares (1,013,068) of Perk common stock, the warrants for additional shares, and the right to the Earn-Out Shares received from Perk on the sale of the Viggle rewards business on February 8, 2016. The Company received \$1,300,000 from Perk as consideration therefor. The execution of the Securities Purchase Agreement and closing were simultaneous. The escrowed shares were released as part of this transaction.

The Company recognized a gain of approximately \$1,060,000 on this transaction, net of transaction fees associated with the sale of the Viggle rewards business.

Results of operations classified as discontinued operations (amounts in thousands):

Three Months Ended December 31,		Six Months Ended December 31,	
2016	2015	2016	2015

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Revenues	\$	\$ 2,330	\$	\$ 5,909
Cost of watchpoints and engagement points		(1,209)		(3,231)
Selling, general and administrative expenses		(6,224)	(36)	(12,408)
Loss before income taxes		(5,103)	(36)	(9,730)
Income taxes (see Note 13, Income Taxes)		(21)		(43)
Net loss	\$	\$ (5,124)	\$ (36)	\$ (9,773)

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TABLE OF CONTENTS**Function(x) Inc.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)****5. Discontinued Operations - (continued)**

Current assets and non-current assets used in discontinued operations (amounts in thousands):

	December 31, 2016	June 30, 2016
Current assets:		
Accounts receivable, net	\$ 20	\$ 39
Prepaid expenses		
Current assets of discontinued operations	\$ 20	\$ 39
Non-current assets:		
Property and equipment, net	\$	\$
Intangible assets, net		
Goodwill		
Other assets		
Non-current assets of discontinued operations	\$	\$

Current liabilities and non-current liabilities used in discontinued operations (amounts in thousands):

	December 31, 2016	June 30, 2016
Current liabilities:		
Accounts payable and accrued expenses	\$ 2,703	\$ 2,634
Reward points payable		
Current portion of loan payable		217
Current liabilities of discontinued operations	\$ 2,703	\$ 2,851
Non-current liabilities:		
Other long-term liabilities	\$	\$
Non-current liabilities of discontinued operations	\$	\$

6. Acquisitions**Acquisition of Choose Digital**

On June 24, 2014, the Company acquired Choose Digital, a Miami, Florida based, digital marketplace platform that allows companies to incorporate digital content into existing rewards and loyalty programs in support of marketing

and sales initiatives.

In connection with our acquisition of Choose Digital, the Company was required to make a contingent payment, which was due within five business days after June 24, 2015, of \$4,800,000, which the Company failed to make timely. As a result, the Company entered into a Forbearance Agreement with AmossyKlein Family Holdings, LLLP (AmossyKlein), as representative of the former shareholders of Choose Digital Inc. (the Stockholders). The Forbearance Agreement provided that the Company would make monthly installment payments to the Stockholders and the Company agreed to deliver an affidavit of confession of judgment to be held in escrow by AmossyKlein s counsel in the event that the Company does not make such installment payments. The Company made the installment payments through December 2015, but failed to make the payment due on January 29, 2016. On May 12, 2016, the Company and AmossyKlein entered into an amendment to the Forbearance Agreement to provide for the payment of the remaining \$1,800,000. The Forbearance Agreement provides that the Company would make a payment of approximately \$300,000 by May 18, 2016, and thereafter, the Company would make monthly payments of \$100,000, plus interest, until the remaining amount is paid in full. In addition, the Company pledged 100,000 shares of common stock held

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Function(x) Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

6. Acquisitions - (continued)

in Perk.com, Inc. as collateral for these obligations. As of the date of this filing, \$354,000 is owed and the 100,000 shares have been released. Finally, the Company agreed if we consummate a sale of a substantial part of its assets or a public equity offering, the Company will first apply the proceeds to remaining amounts due to AmossyKlein, except for payments to advisors or expenses necessary to close such transactions. The Company also agreed to amend the confession of judgment. These payments under the amended forbearance agreement will create additional strain on the Company's limited cash resources. In addition, the requirement to accelerate payments on a sale of a substantial part of the Company's assets or from a public equity offering may hinder its access to additional cash. During the three months ended December 31, 2016, the Company paid approximately \$318,000 under the Forbearance Agreement.

Acquisition of DraftDay.com

On September 8, 2015, the Company and its newly created subsidiary DDGG entered into an Asset Purchase Agreement (the "Asset Purchase Agreement") with MGT Capital Investments, Inc. ("MGT Capital") and MGT Sports, Inc. ("MGT Sports"), pursuant to which the Company acquired all of the assets of the DraftDay.com business (the "DraftDay Business") from MGT Capital and MGT Sports. In exchange for the acquisition of the DraftDay Business, the Company paid MGT Sports the following: (a) 63,647 shares of the Company's Common Stock, par value \$0.001 per share ("Common Stock"), (b) a promissory note in the amount of \$234,000 due September 29, 2015, (c) a promissory note in the amount of \$1,875,000 due March 8, 2016 (the "MGT Note"), and (d) 2,550 shares of common stock of DDGG. In addition, in exchange for providing certain transitional services, DDGG will issue to MGT Sports a warrant to purchase 1,500 shares of DDGG common stock at an exercise price of \$400 per share.

In addition, in exchange for the release of various liens and encumbrances, the Company also agreed to issue to third parties: (a) 4,232 shares of its Common Stock, (b) a promissory note in the amount of \$16,000 due September 29, 2015 and (c) a promissory note in the amount of \$125,000 due March 8, 2016, and DDGG issued: (i) 150 shares of its common stock and (ii) a warrant to purchase 150 shares of DDGG common stock at \$400 per share.

Accordingly, the Company issued a total of 67,879 shares of Common Stock in connection with the acquisition of the DraftDay Business.

The Company contributed the assets of the DraftDay Business to DDGG and received 11,250 shares of DDGG common stock.

The Asset Purchase Agreement contains customary representations, warranties and covenants of MGT Capital and MGT Sports. In addition, on September 8, 2015, DDGG entered into an agreement with Sportech Racing, LLC ("Sportech") pursuant to which Sportech agreed to provide certain management services to DDGG in exchange for 9,000 shares of DDGG common stock.

As a result of the transactions described above, the Company owns a total of 11,250 shares of DDGG common stock, Sportech Inc., an affiliate of Sportech, owns 9,000 shares of DDGG common stock, MGT Sports owns 2,550 shares of DDGG common stock and an additional third party owns 150 shares of DDGG common stock. In addition, MGT Sports holds a warrant to purchase 1,500 shares of DDGG common stock at an exercise price of \$400 and an additional third party holds a warrant to purchase 350 shares of DDGG common stock at \$400 per share. On September 8, 2015, the various stockholders of DDGG entered into a Stockholders Agreement (the "Stockholders Agreement"). The Stockholders Agreement provides that all stockholders will vote their shares of DDGG common stock for a Board comprised of three members, two of which will be designated by the Company and one of which will be designated by Sportech. Mr. Sillerman will serve as the Chairman of DDGG. The Stockholders Agreement also provides customary rights of first refusal for the various stockholders, as well as customary co-sale, drag along and preemptive rights.

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(Unaudited)****6. Acquisitions - (continued)**

As a result of the transactions described herein, the Company issued promissory notes in the aggregate principal amount of \$250,000 due and paid on September 29, 2015 and in the aggregate principal amount of \$2,000,000 due March 8, 2016. All such notes bear interest at a rate of 5% per annum. The Company was not able to make the \$2,000,000 in payments at the due date and on March 24, 2016 converted \$825,000 of the promissory notes to common stock and \$110,000 of the promissory notes to a Series D Preferred Stock (see Note 11, Stockholders (Deficit) Equity). On April 13, 2016, MGT converted all 110 shares of the Company's Series D Preferred Stock into shares of common stock of the Company. Accordingly, the Company issued 18,332 shares of common stock to MGT. Thereafter, there are no shares of the Company's Series D Preferred Stock outstanding. On June 14, 2016, the Company entered into a second exchange agreement with MGT (the "Second MGT Exchange Agreement") relating to the \$940,000 remaining due under the MGT Note. Under the Second MGT Exchange Agreement, the MGT Note shall be exchanged in full for (a) \$11,000 in cash representing accrued interest and (b) 132,092 shares of our common stock, subject to certain adjustments. Issuance of the shares was conditioned upon approval of the Company's shareholders and approval of its listing of additional shares application with NASDAQ. On October 10, 2016, the Company satisfied the MGT Note through the issuance of 136,304 shares of its common stock and payment of interest of \$16,000.

On December 28, 2015, DDGG's Board of Directors effectuated a 1-for-1,000 reverse stock split (the "1-for-1,000 Reverse Split"). Under the terms of the 1-for-1,000 Reverse Split, each share of DDGG's common stock, issued and outstanding as of such effective date, was automatically reclassified and changed into one-thousandth of one share of common stock, without any action by the stockholders. Fractional shares were cashed out.

On May 12, 2016, the Company entered into a subscription agreement with DDGG pursuant to which the Company agreed to purchase up to 550 shares of Series A Preferred Stock of DDGG for \$1 per share. DDGG also entered into a subscription agreement with Sportech pursuant to which Sportech agreed to purchase up to 450 shares of Series A Preferred Stock of DDGG for \$1 per share. In accordance with this agreement, the Company transferred a total of \$550,000 to the DDGG subsidiary since the date of acquisition and through November 20, 2016.

Kuusamo Warrants

In exchange for releasing certain liens and encumbrances with respect to DDGG, the Company issued promissory notes to Kuusamo Capital Ltd. ("Kuusamo Promissory Notes") in the principal amount of \$16,000 due and paid on September 29, 2015 and in the aggregate principal amount of \$125,000 due March 8, 2016. All such notes bear interest at a rate of 5% per annum. The Company was not able to make the \$125,000 payment at the due date. On April 25, 2016, the Company also entered into an exchange agreement with Kuusamo Capital Ltd. ("Kuusamo"), pursuant to which the Company issued 10,394 shares of its common stock to Kuusamo in exchange for a reduction of \$71,000 in principal amount of a promissory note the Company owed to Kuusamo.

The outstanding balance of the Kuusamo Promissory Notes was \$0 and \$54,000 at December 31, 2016 and June 30, 2016, respectively. The Company recorded \$5,000 in interest expense for the year ended June 30, 2016. On September 21, 2016, the Company satisfied the Kuusamo Promissory Note through the issuance of 8,410 shares of its common stock.

Sportech MSA Termination

On April 12, 2016, DDGG entered into an amendment to the transitional management services agreement pursuant to which the DDGG's Management Services Agreement By and Between DraftDay Gaming Group, Inc. and Sportech Racing, LLC (Sportech MSA) terminated effective June 30, 2016. Sportech paid a \$75,000 termination fee, to provide transitional services for 45 days, and has agreed to revert 4,200 shares of DDGG stock back to the Company on August 15, 2016. The Company had previously recorded the value of

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TABLE OF CONTENTS**Function(x) Inc.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)****6. Acquisitions - (continued)**

the services provided by Sportech under the Sportech MSA to prepaid assets, to be recognized as a professional services expense in the Consolidated Statements of Operations over the term of the agreement. Due to the termination of the agreement, the Company reduced prepaid assets and non-controlling interest accounts for the value of the returned 4,200 shares of DDGG stock, and expensed the remaining value of the Sportech services, except for 45 days of transitional services. The value of returned DDGG shares was determined by a third-party valuation firm as of June 30, 2016 using Level 3 inputs. The termination of the Sportech MSA required DDGG to begin performing certain functions on its own.

DDGG Intangibles and Goodwill Impairment

As noted above, at June 30, 2016, the Sportech MSA terminated, which led to a significantly lower revenues forecast for the reporting unit. As a result, the Company determined that intangible assets related to internally developed software, trade name and non-compete agreements were impaired as of June 30, 2016. The Company recorded a loss of approximately \$749,000 on intangible assets related to DDGG during the year ended June 30, 2016. There was no impairment of goodwill (see Note 3, Summary of Significant Accounting Policies).

This acquisition has been accounted for under the acquisition method of accounting in accordance with ASC 805, *Business Combinations*. Under the acquisition method, the consideration transferred is measured at the acquisition closing date. The assets of the DraftDay Business have been measured based on various preliminary estimates using assumptions that the Company's management believes are reasonable utilizing information currently available. Use of different estimates and judgments could yield different results. The Company has performed a preliminary allocation of the purchase price to the underlying net assets acquired and liabilities assumed based on their estimated fair values as of the acquisition date, with any excess of the purchase price allocated to goodwill. The Company has not completed the analysis of certain acquired assets and assumed liabilities, including, but not limited to, other identifiable intangible assets such as customer lists and technology. However, the Company is continuing its review of these items during the measurement period, and further changes to the preliminary allocation will be recognized as the valuations are finalized. Such valuations are being conducted using Level 3 inputs as described in ASC 820, *Fair Value Measurements and Disclosures*, that are generally unobservable and typically reflect management's estimates of assumptions that market participants would use in pricing the asset or liability.

A summary of the fair value of consideration transferred for this acquisition and the fair value of the assets and liabilities at the date of acquisition is as follows (amounts in thousands):

Consideration transferred:

Shares of the Company's common stock on closing market price at issuance	\$ 1,760
Notes issued to sellers	2,250

Total consideration transferred	\$ 4,010
Purchase allocation:	
Goodwill	\$ 1,591
Intangible assets	3,012
Other Assets	799
Total liabilities	(1,392)
	\$ 4,010

The operations of this acquisition are not material, and thus, pro forma disclosures are not presented.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

6. Acquisitions - (continued)

Rant

On July 12, 2016, the Company, and RACX Inc., a Delaware corporation and wholly-owned subsidiary of the Company (RACX), completed an acquisition pursuant to an Asset Purchase Agreement (the Asset Purchase Agreement) with Rant, Inc., a Delaware corporation, pursuant to which RACX has acquired the assets of Rant (the Asset Purchase) used in the operation of Rant's Rant.com independent media network and related businesses, including but not limited to the *www.rantsports.com*, *www.rantlifestyle.com*, *www.rantchic.com*, *www.rantgirls.com*, *www.rant-inc.com*, *www.rantstore.com*, *www.rantcities.com*, *www.rantcars.com*, *www.rantfinance.com*, *www.ranthollywood.com*, *www.rantfood.com*, *www.rantgamer.com*, *www.rantgizmo.com*, *www.rantpets.com*, *www.rantplaces.com*, *www.rantpolitical.com*, *www.rantmn.com*, *www.rantbeats.com*, *www.rantgirls.com*, *www.rantstore.com*, *www.rantcities.com*, *www.rantranet.com*, and *www.rantmovies.com* websites (the Rant Assets).

In consideration for the purchase of the Rant Assets, the Company delivered a Secured Convertible Promissory Note (the Secured Convertible Note) to Rant with a fair value determined to be \$3,500,000 and delivered the stock consideration of \$7,600,000 described below.

The \$3,000,000 Secured Convertible Note matures on July 8, 2017 barring any events of default or a change of control of the Company. The Secured Convertible Note bears interest at 12% per annum, payable at maturity. At the election of Rant, the Secured Convertible Note is convertible into shares of the Company's common stock at a price equal to the lower of (i) \$5.20 per share, or (ii) such lower price as may have been set for conversion of any debt or securities into Common Stock held on or after the date hereof by Sillerman until the first to occur of March 31, 2017 or the date the Note has been satisfied or converted (for the purposes hereof Robert F.X. Sillerman is the Company's Executive Chairman and Chief Executive Officer and/or any affiliate of Robert F.X. Sillerman is herein collectively,

Sillerman). In connection with the Secured Convertible Note, the Company has entered into a Note Purchase Agreement (the NPA) and a Security Agreement (the Rant Security Agreement) with Rant, under which the Company has granted Rant a continuing security interest in substantially all assets of the Company. In connection with the issuance of the Secured Convertible Note, Sillerman and Rant entered into a subordination agreement subordinating repayment of the notes to the Debentures (as described in (b) hereof) and entered into an Intercreditor Agreement providing for the parties' respective rights and remedies with respect to payments against the collateral held as security for both of them.

In connection with the Asset Purchase Agreement, and in addition to the consideration represented by the Secured Convertible Note and the Assumed Liabilities, the Company issued to Rant 4,435 shares of Company Series E Convertible Preferred Stock which, upon satisfaction of certain conditions including shareholder approval, will be convertible into shares of Company common stock equal to 22% of the outstanding common stock of the Company. The number of shares will be adjusted for dilution between the date of closing and the date of any public offering by

the Company of its common stock and to reflect additional capital structure changes through the first of (i) the date Sillerman converts debt and preferred shares to common shares pursuant to the Exchange Agreement just before an offering of the Company's common stock closes or (ii) March 31, 2017.

This acquisition has been accounted for under the acquisition method of accounting in accordance with ASC 805, *Business Combinations*. Under the acquisition method, the consideration transferred is measured at the acquisition closing date. The assets of Rant have been measured based on various preliminary estimates using assumptions that the Company's management believes are reasonable utilizing information currently available. Use of different estimates and judgments could yield different results. The Company has performed a preliminary allocation of the purchase price to the underlying net assets acquired and liabilities assumed based on their estimated fair values as of the acquisition date, with any excess of the purchase price allocated to goodwill. The Company has not completed the analysis of certain acquired assets and assumed liabilities,

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TABLE OF CONTENTS**Function(x) Inc.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)****6. Acquisitions - (continued)**

including, but not limited to, other identifiable intangible assets such as customer lists and technology. However, the Company is continuing its review of these items during the measurement period, and further changes to the preliminary allocation will be recognized as the valuations are finalized. Such valuations are being conducted by a third party valuation expert using Level 3 inputs as described in ASC 820, *Fair Value Measurements and Disclosures*, that are generally unobservable and typically reflect management's estimates of assumptions that market participants would use in pricing the asset or liability.

The preliminary allocation of the purchase price to the underlying net assets acquired and liabilities assumed based on their estimated fair values as of the acquisition date is as follows (amounts in thousands):

Goodwill	\$ 7,589
Intangible assets	5,500
Total liabilities	(1,990)
	\$ 11,099

The goodwill allocated to the Rant acquisition is tax deductible.

7. Property and Equipment

Property and Equipment consists of the following (amounts in thousands):

	December 31, 2016	June 30, 2016
Leasehold Improvements	\$2,261	\$2,261
Furniture and Fixtures	588	588
Computer Equipment	456	456
Software	164	164
Total	3,469	3,469
Accumulated Depreciation and Amortization	(2,209)	(2,055)
Property and Equipment, net	\$1,260	\$1,414

Depreciation and amortization charged to selling, general and administrative expenses for the three months ended December 31, 2016 and 2015 amounted to approximately \$77,000 and \$139,000, respectively.

Depreciation and amortization charged to selling, general and administrative expenses for the six months ended December 31, 2016 and 2015 amounted to \$154,000 and \$279,000, respectively.

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TABLE OF CONTENTS**Function(x) Inc.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)****8. Intangible Assets and Goodwill**

The summary of intangible assets and goodwill is as follows (amounts in thousands):

Description	Amortization Period	December 31, 2016			June 30, 2016		
		Amount	Accumulated Amortization	Carrying Value	Amount	Accumulated Amortization	Carrying Value
Wetpaint technology	60 months	\$4,952	\$ (3,458)	\$ 1,494	\$4,952	\$ (3,276)	\$ 1,676
Wetpaint trademarks	276 months	1,453	(438)	1,015	1,453	(415)	1,038
Wetpaint customer relationships	60 months	917	(837)	80	917	(827)	90
Choose Digital licenses	60 months	829	(589)	240	829	(559)	270
Choose Digital software	60 months	627	(257)	370	627	(212)	415
DraftDay tradename	84 months	180	(61)	119	180	(38)	142
Draftday non-compete agreements	6 months	30	(30)		30	(30)	
DraftDay internally generated capitalized software	60 months	1,498	(485)	1,013	1,498	(303)	1,195
DraftDay customer relationships	24 months	556	(556)		556	(351)	205
Rant trademarks	120 months	2,700	(124)	2,576			
Rant content	24 months	650	(149)	501			
Rant technology	60 months	1,500	(138)	1,362			
Rant advertising relationships	24 months	650	(149)	501			
Other	various	326	(24)	302	326	(18)	308
Total		\$16,868	\$ (7,295)	\$ 9,573	\$11,368	\$ (6,029)	\$ 5,339

See Note 3, Summary of Significant Accounting Policies, for a discussion of the write-downs recorded with respect to intangible assets related to the Wetpaint and Choose Digital businesses in the quarter ended December 31, 2015 and to

the DraftDay business in the quarter ended June 30, 2016. The changes in the gross amounts and useful lives of intangibles related to the Wetpaint, Choose Digital and DraftDay businesses, and to internally generated capitalized software, are a result of these write-downs during the three months ended December 31, 2015 and June, 30, 2016, as well as the abandonment of certain technology as of January 1, 2016, and internal development costs. See Note 6, Acquisitions, for a detailed description of DraftDay and Rant assets and liabilities purchased and their fair values on the date of the acquisition.

Amortization of intangible assets included in selling, general and administrative expenses for the six months ended December 31, 2016 and 2015 amounted to approximately \$1,266,000 and \$2,123,000, respectively.

Future annual amortization expense expected is as follows (amounts in thousands):

Years ending June 30,	
2017	\$ 2,370
2018	\$ 3,026
2019	\$ 1,730
2020	\$ 1,367
2021	\$ 1,036

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(Unaudited)****8. Intangible Assets and Goodwill - (continued)**

Goodwill consists of the following:

Description	Amount
Balance at July 1, 2016	\$ 11,270
Rant preliminary purchase price allocation	7,589
Balance at December 31, 2016	\$ 18,859

9. Loans Payable

The summary of loans payable is as follows (amounts in thousands):

	Maturity Date	Total Facility Amount	December 31, 2016	June 30, 2016
Convertible Debentures (the Debentures), net of discount	7/11/2017	\$ 4,444	\$ 3,629	\$
Secured Convertible Promissory Note (the Secured Convertible Note)	7/8/2017	3,000	3,400	
Line of Credit Promissory Note (the Note)	10/24/2017	20,000		19,716
Line of Credit Grid Note (the Grid Note)*	12/31/2016	5,900	3,465	4,563
Secured Line of Credit (the Secured Revolving Loan I)	12/31/2016	1,500		1,500
Secured Line of Credit (the Secured Revolving Line of Credit)	12/31/2016	500		500
Secured Revolving Loan (the Secured Revolving Loan)	12/31/2016	500		500
Secured Revolving Loan II (the Secured Revolving Loan II)	12/31/2016	500		500
Secured Revolving Loan III (the Secured Revolving Revolving Loan III)	12/31/2016	1,200		135
Convertible Promissory Note (the RI Convertible Note)	12/31/2016	300	300	300
MGT Promissory Notes (the MGT Promissory Notes)	7/31/2016	2,109		943
Kuusamo Promissory Notes (the Kuusamo Promissory Notes)	3/8/2016	141		55
Total Loans Payable, net			\$ 10,794	\$ 28,712

* As of June 30, 2016 the total facility amount on on the Grid Note was \$10,000,000; however, in conjunction with the

Exchange Agreement, this amount was reduced to \$5,900,000.

Convertible Debentures

On July 12, 2016, the Company closed a private placement (the **Private Placement**) of \$4,444,000 principal amount of convertible debentures (the **Debentures**) and common stock warrants (the **Warrants**). The Debentures and Warrants were issued pursuant to a Securities Purchase Agreement, dated July 12, 2016 (the **Purchase Agreement**), by and among the Company and certain accredited investors within the meaning of the Securities Act of 1933, as amended (the **Purchasers**). Upon the closing of the Private Placement, the Company received gross proceeds of \$4,000,000 before placement agent fees, original issue discount, and other expenses associated with the transaction. \$1,162,000 of the proceeds was used to repay the Grid Note.

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Function(x) Inc.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)**

9. Loans Payable - (continued)

The placement agent fees of \$420,000 and original issue discount of \$444,000 were recorded as a reduction to the debenture balance and will be accreted to interest expense over the term of the Debentures.

The Debentures mature on the one-year anniversary of the issuance date thereof. The Debentures are convertible at any time at the option of the holder into shares of the the Company's common stock at an initial conversion price of \$6.2660 per share (the Conversion Price). Based on such initial Conversion Price, the Debentures will be convertible into up to 780,230 shares of common stock. If we issue or sell shares of our common stock, rights to purchase shares of our common stock, or securities convertible into shares of our common stock for a price per share that is less than the Conversion Price then in effect, the Conversion Price then in effect will be decreased to equal such lower price. The adjustments to the Conversion Price will not apply to certain exempt issuances, including issuances pursuant to certain employee benefit plans or for certain acquisitions. In addition, the Conversion Price is subject to adjustment upon stock splits, reverse stock splits, and similar capital changes. However, in no event will the Conversion Price be less than \$0.10 per share. The Debentures are secured by a first priority lien on substantially all of the Company's assets in accordance with a security agreement.

The Debentures bear interest at 10% per annum with interest payable upon maturity or on any earlier redemption date. At any time after the issuance date, we will have the right to redeem all or any portion of the outstanding principal balance of the Debentures, plus all accrued but unpaid interest at a price equal to 120% of such amount. The holders of Debentures shall have the right to convert any or all of the amount to be redeemed into common stock prior to redemption. Subject to certain exceptions, the Debentures contain customary covenants against incurring additional indebtedness and granting additional liens and contain customary events of default. Upon the occurrence of an event of default under the Debentures, a holder of Debentures may require the Company to pay the greater of (i) the outstanding principal amount, plus all accrued and unpaid interest, divided by the Conversion Price multiplied by the daily volume weighted average price or (ii) 115% of the outstanding principal amount plus 100% of accrued and unpaid interest. Pursuant to the Debentures, the Company is required to make amortizing payments of the aggregate principal amount, interest, and other amounts outstanding under the Debentures. Such payments must be made beginning three months from the issuance of the Debentures and on the monthly anniversary through and including the maturity date. The Amortization Amount is payable in cash or in shares of our common stock pursuant to the conversion mechanism contained in the Debentures.

On July 20, 2016, the Company and the Purchasers entered into an Amendment to Securities Purchase Agreement and Consent to Modify Debentures (the Amendment and Consent). The Amendment and Consent provides that, while the Debentures are outstanding, Mr. Sillerman will guarantee that the Company shall have \$1,000,000 available in its commercial bank account or otherwise available in liquid funds. At any time when the Company's available funds fall below \$1,000,000, Mr. Sillerman will provide (the Sillerman Guaranty) the amounts necessary to make-up the shortfall in an aggregate amount not to exceed \$6,000,000; however, the first \$5,000,000 of the guaranty shall be provided by drawing down on our Line of Credit with SIC IV. Any remaining amounts, up to a maximum aggregate

of \$1,000,000 million shall be provided by Sillerman.

As a part of the Private Placement, the Company issued Warrants to the Purchasers providing them with the right to purchase up to an aggregate of 354,650 shares of the Company's common stock at an initial exercise price of \$6.5280 per share. Subject to certain limitations, the Warrants are exercisable on any date after the date of issuance and the exercise price for the Warrant is subject to adjustment for certain events, such as stock splits and stock dividends. If the Company issues or sells shares of its common stock, rights to purchase shares of its common stock, or securities convertible into shares of its common stock for a price per share that is less than the conversion price of the Debentures, the exercise price of the Warrants will be decreased to a lower price based on the amount by which the conversion price of the Debentures was reduced due to such transaction. The foregoing adjustments to the exercise price for future stock issues will not apply to certain

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Function(x) Inc.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)**

9. Loans Payable - (continued)

exempt issuances, including issuances pursuant to certain employee benefit plans or for certain acquisitions. In addition, the exercise price is subject to adjustment upon stock splits, reverse stock splits, and similar capital changes. The Warrants will expire 5 years from the initial issuance date. The fair value of the Warrants as of July 12, 2016 was determined to be \$1,500,000 and the offset was recorded as a debt discount on the Convertible Debentures. The Warrants are recorded as a liability on the Consolidated Balance Sheets due to the adjustment of the exercise price due to subsequent common stock issuances and is being marked to market each reporting period. As of December 31, 2016, the balance of the debt discount related to the Warrants was \$812,500. The fair value of the Warrants as of December 31, 2016 was determined to be \$410,000. The change in fair value of \$1,090,000 was recorded as other income in the Consolidated Statements of Operations for the three months ended December 31, 2016.

The Purchasers shall not have the right to convert the Debentures or exercise the Warrants to the extent that such conversion or exercise would result in such Purchaser being the beneficial owner in excess of 4.99% of our common stock. In addition, the Purchasers have no right to convert the Debentures or exercise the Warrants if the issuance of the shares of common stock upon such conversion or exercise would exceed the aggregate number of shares of our common stock which we may issue upon conversion of the Note and exercise of the Warrants without breaching our obligations under NASDAQ listing rules. Such limitation does not apply if our shareholders approve such issuances. We intend to promptly seek shareholder approval for issuances of shares of common stock issuable upon conversion of the Debentures and exercise of the Warrants.

In connection with the Private Placement, the Company and the Purchasers entered into a Registration Rights Agreement under which the Company was required, on or before 30 days after the closing of the Private Placement, to file a registration statement with the Securities and Exchange Commission (the SEC) covering the resale of the shares of its common stock issuable pursuant to the Debentures and Warrants and to use commercially reasonable efforts to have the registration declared effective as soon as practicable, but in no event later than 90 days after the filing date. The Company will be subject to certain monetary penalties, as set forth in the Registration Rights Agreement, if the registration statement is not filed, does not become effective on a timely basis, or does not remain available for the resale (subject to certain allowable grace periods) of the Registrable Securities, as such term is defined in the Registration Rights Agreement.

Also in connection with the Private Placement, certain stockholders of the Company have executed Lock-Up Agreements, pursuant to which they have agreed not to sell any shares of the Company's common stock until the later of (i) six months following the issuance of the Debentures or (ii) 90 days following the effectiveness of a resale registration statement filed pursuant to the requirements of the Registration Rights Agreement.

The Company valued the Debentures as of July 12, 2016, the issuance date, using the methods of fair value as described ASC 820, *Fair Value Measurements and Disclosures* (ASC 820). The fair value of the conversion feature in the Debentures was determined to be \$1,856,000 as of July 12, 2016 and the offset was recorded as a debt discount.

As of December 31, 2016, the balance of the debt discount on the Debentures related to the Conversion feature was \$1,005,000. The fair value of the Conversion feature as of December 31, 2016 was determined to be \$1,256,000. The change in fair value of \$600,000 was recorded as other income in the Consolidated Statements of Operations for the three months ended December 31, 2016.

On October 12, 2016, the first amortization payment in the amount of \$444,000, plus accrued interest of approximately \$114,000 pursuant to the terms of the Debentures became due and payable to the Purchasers. The Company did not make such payment at the time it was due. As a result of the event of default, the Company accrued \$739,000 to interest expense in the Consolidated Statements of Operations and the Current portion of loans payable on the Consolidated Balance Sheets for the three and six months ended December 31, 2016, which represents all interest that would have been earned through the one year anniversary of the original issue date. Additionally, \$667,000 was accrued to interest expense in the Consolidated Statements of

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

9. Loans Payable - (continued)

Operations and the Current portion of loans payable on the Consolidated Balance Sheets representing the 15% premium on the outstanding principal for the three and six months ending December 31, 2016. In December 2016, the Company made a payment of \$397,000, which included \$383,000 of principal and \$14,000 of interest.

The Company has also not maintained the Minimum Cash Reserve as required by the Purchase Agreement. Pursuant to the terms of the Debentures, the failure to cure the failure to maintain the Minimum Cash Reserve within three trading days constitutes an Event of Default. Among other things: (1) at the Purchaser's election, the outstanding principal amount of the Debentures, plus accrued but unpaid interest, plus all interest that would have been earned through the one year anniversary of the original issue date if such interest has not yet accrued, liquidated damages and other amounts owed through the date of acceleration, shall become, immediately due and payable in either cash or stock pursuant to the terms of the Debentures; and (2) the interest rate on the Debentures will increase to the lesser of 18% or the maximum allowed by law. In addition to other remedies available to the Purchasers, our obligation to repay amounts due under the Debentures is secured by a first priority security interest in and lien on all of our assets and property, including our intellectual property, and such remedies can be exercised by the Purchasers without additional notice to the Company.

The Company entered into waiver agreements with respect to the initial amortization payments due under the Debentures with Purchasers holding approximately 87% of the Debentures. The Waivers entered into with some of the Purchasers related to the failure to pay the amortization amounts do not address the failure to maintain the Minimum Cash Reserve. In addition, the Company is currently in default with respect to the amortization payment due in January 2017.

Pursuant to the terms of the Debentures, the failure to cure the non-payment of the amortization amount within three trading days after the date such payment was due constitutes an Event of Default. Following the occurrence of an event of default, among other things: (1) at the Purchaser's election, the outstanding principal amount of the Debentures, plus accrued but unpaid interest, plus all interest that would have been earned through the one year anniversary of the original issue date if such interest has not yet accrued, liquidated damages and other amounts owed through the date of acceleration, shall become, immediately due and payable in either cash or stock pursuant to the terms of the Debentures; and (2) the interest rate on the Debentures will increase to the lesser of 18% or the maximum allowed by law. In addition to other remedies available to the Purchasers, our obligation to repay amounts due under the Debentures is secured by a first priority security interest in and lien on all of our assets and property, including our intellectual property, and such remedies can be exercised by the Purchasers without additional notice to the Company.

The Company did not receive a waiver from one of its debenture holders, holding approximately 13% of the principal amount of the Debentures with respect to the event of default arising out of the Company's failure to make the first amortization payment when due. Pursuant to the terms of the Debentures, such holder has sent a notice of acceleration, stating that the Company owes \$696,000, reflecting the principal amount of the Debenture plus interest

through November 1, 2016. Interest will accrue at 18% until this amount is satisfied.

Secured Convertible Promissory Note

On July 8, 2016 the Company issued a Secured Convertible Promissory Note (the "Secured Convertible Note") to Rant in the amount of \$3,000,000 as part of the consideration for the purchase of the Rant Assets.

The \$3,000,000 Secured Convertible Note matures on July 8, 2017 barring any events of default or a change of control of the Company. The Secured Convertible Note bears interest at 12% per annum, payable at maturity. At the election of Rant, the Secured Convertible Note is convertible into shares of the Company's common stock at a price equal to the lower of (i) \$5.20 per share, or (ii) such lower price as may have been set for conversion of any debt or securities into common stock held on or after the date hereof by Sillerman

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(Unaudited)****9. Loans Payable - (continued)**

until the first to occur of March 31, 2017 or the date the Note has been satisfied or converted (for the purposes hereof Robert F.X. Sillerman is the Company's Executive Chairman and Chief Executive Officer and/or any affiliate of Robert F.X. Sillerman is herein collectively, "Sillerman"). In connection with the Secured Convertible Note, the Company has entered into a Note Purchase Agreement (the "NPA") and a Security Agreement (the "Rant Security Agreement") with Rant, under which the Company has granted Rant a continuing security interest in substantially all assets of the Company. In connection with the issuance of the Secured Convertible Note, Sillerman and Rant entered into a subordination agreement subordinating repayment of the notes to the Debentures (as described in (b) hereof) and entered into an Intercreditor Agreement providing for the parties' respective rights and remedies with respect to payments against the collateral held as security for both of them.

The events of default under the Debentures noted above also constituted a default under the Secured Convertible Note issued in connection with the acquisition of Rant. The holder of the Secured Convertible Note has executed a waiver that provides that, until May 15, 2017, the events of default arising out of the failure to pay the amounts due under the Debentures as of the date of the waiver and the failure by the Company to maintain the Minimum Cash Reserve shall not constitute events of default for purposes of the Secured Convertible Note. In addition, the Company is currently in default with respect to the Rant Note as a result of the failure to make the Debentures amortization payment due in January 2017.

The Company valued the Secured Convertible Note as of the acquisition date using the methods of fair value as described ASC 820. The fair value of the conversion feature in the Secured Convertible Note was determined to be \$500,000 at the acquisition date. As of December 31, 2016, the fair value of the conversion feature was determined to be \$400,000. The \$100,000 change in fair value from September 30, 2016 to December 31, 2016 was recorded as other income in the Consolidated Statements of Operations for the three months ended December 31, 2016.

Line of Credit Promissory Note

On October 24, 2014, the Company and SIC III, a company affiliated with Mr. Sillerman, entered into a Securities Purchase Agreement (the "Securities Purchase Agreement") pursuant to which SIC III agreed to purchase certain securities issued by the Company for a total of \$30,000,000. Pursuant to the Securities Purchase Agreement, the Company issued a Line of Credit Promissory Note (the "Note"), which provides for a \$20,000,000 line of credit to the Company (see Note 11, Stockholders' Equity, for a discussion of the remaining \$10,000,000 of the Securities Purchase Agreement). The Company also agreed to issue to SIC III warrants to purchase 1,000,000 shares of the Company's common stock. The Company issued warrants to purchase 50,000 shares of the Company's common stock for every \$1,000,000 advanced under the Note. The warrants will be issued in proportion to the amounts the Company draws under the Note. The exercise price of the warrants will be 10% above the closing price of the Company's shares on the date prior to the issuance of the warrants. Exercise of the Warrants was subject to approval of the Company's stockholders, which occurred on January 13, 2015.

The Note provides a right for the Company to request advances under the Note from time to time. The Note bears interest at a rate of 12% per annum, payable in cash on a quarterly basis. The Note matures on October 24, 2017. On October 24, 2014, SIC III made an initial advance under the Note in the principal amount of \$4,500,000. On December 15, 2014, SIC III made an additional advance in the principal amount of \$15,500,000 pursuant to the terms of the Note (the proceeds of which were used to repay amounts outstanding under the DB Line, as discussed above). As of September 30, 2016, the total outstanding principal amount of the Note was \$20,000,000. The Note provides for a 3% discount, such that the amount advanced by SIC III was 3% less than the associated principal amount of the advances. Therefore, the net amount actually outstanding under the Note at September 30, 2016, was \$19,666,000, which includes accretion of the discount of \$266,000 (the 3% discount of \$600,000 is being accreted to the principal balance over the life of the Note).

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9. Loans Payable - (continued)

From and after the occurrence and during the continuance of any event of default under the Note, the interest rate is automatically increased to 17% per annum.

In connection with the first drawdown of \$4,500,000 under the Note, the Company issued SIC III warrants to purchase 11,250 shares of the Company's common stock. These warrants have an exercise price of \$70.20, representing a price equal to 10% above the closing price of the Company's common stock on the day prior to issuance. In connection with the additional drawdown of \$15,500,000 under the Note, the Company issued SIC III warrants to purchase 38,750 shares of the Company's common stock. These warrants have an exercise price of \$72.60, representing a price equal to 10% above the closing price of the Company's common stock on the day prior to issuance. The warrants are exercisable for a period of five years from issuance. Stock compensation expense related to the issuances of warrants to SIC III was \$2,049,000 during the year ended June 30, 2015.

The Note is not convertible into equity securities of the Company.

The Note also contains certain covenants and restrictions, including, among others, that, for so long as the Note is outstanding, the Company will not, without the consent of the holder of the Note, (i) make any loan or advance in excess of \$500,000 to any officer, director, employee or affiliate of the Company (except advances and similar expenditures: (a) under the terms of employee stock or option plans approved by the Board of Directors, (b) in the ordinary course of business, consistent with past practice or (c) to its subsidiaries), (ii) incur any indebtedness that exceeds \$1,000,000 in the aggregate other than indebtedness outstanding under the Note, (iii) guaranty any indebtedness of any unaffiliated third party, (iv) change the principal business of the Company or exit the Company's current business, provided that the foregoing is subject to the Board's compliance with its fiduciary duties, (v) sell, assign, or license material technology or intellectual property of the Company except (a) in the ordinary course of business, consistent with past practice, (b) sales and assignments thereof in any 12 month period that do not have a fair market value in excess of \$500,000 or (c) in connection with a change of control transaction, (vi) enter into any corporate strategic relationship involving the payment, contribution or assignment by the Company of its assets that have a fair market value in excess of \$1,000,000 or (vii) liquidate or dissolve the Company or wind up the business of the Company, except in connection with changes of control or merger, acquisition or similar transactions or as approved by the Company's Board in compliance with their fiduciary duties.

On August 22, 2016, the Company and SIC III, entered into a Note Exchange Agreement pursuant to which \$23,264,000, which represents all of the outstanding principal and accrued interest outstanding under the Notes, was exchanged for 23,264 shares of the Company's Series C Preferred Stock at an exchange price of \$1,000 per share. The Note Exchange Agreement provides for the newly issued shares to be held subject to the obligations to convert the shares into common stock on the terms and on the conditions set forth in the Exchange Agreement. After the exchange, the Notes were retired.

Interest expense on the Note was \$0 and \$613,000 for the three months ended December 31, 2016 and 2015, respectively.

Line of Credit Grid Note

On June 11, 2015, the Company and Sillerman Investment Company IV, LLC (SIC IV) entered into a Line of Credit Grid Note (the Grid Note). The Grid Note provides a right for the Company to request advances under the Grid Note from time to time in an aggregate amount of up to \$10,000,000. The Grid Note bears interest at a rate of 12% per annum, payable in cash on the maturity of the Grid Note. From and after the occurrence and during the continuance of any event of default under the Grid Note, the interest rate is automatically increased to 14% per annum.

The Grid Note is not convertible into equity securities of the Company.

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9. Loans Payable - (continued)

In order for the Company to make requests for advances under the Grid Note, the Company must have an interest coverage ratio equal to or greater than 1, unless SIC IV waives this requirement. The interest coverage ratio is calculated by dividing: (a) the Company's net income for the measurement period, plus the Company's interest expense for the measurement period, plus the Company's tax expense for the measurement period, by (b) the Company's interest expense for the measurement period, plus the amount of interest expense that would be payable on the amount of the requested draw for the twelve months following the request for the advance. The measurement period is the twelve months ended as of the last day of the last completed fiscal quarter prior to the request for the advance. The Company currently does not have an interest coverage ratio equal to or greater than 1, so advances would require the SIC IV to waive this requirement. In addition, in order to make requests for advances under the Grid Note, there can be no event of default under the Note at the time of the request for an advance, including that there has been no material adverse change in the business plan or prospects of the Company in the reasonable opinion of SIC IV.

The Grid Note matures on the first to occur of: (a) December 31, 2016 or (b) upon a Change of Control Transaction. A Change of Control Transaction includes (i) a sale of all or substantially all of the assets of the Company or (ii) the issuance by the Company of common stock that results in any person or group becoming the beneficial owner of a majority of the aggregate ordinary voting power represented by the Company's issued and outstanding common stock (other than as a result of, or in connection with, any merger, acquisition, consolidation or other business combination in which the Company is the surviving entity following the consummation thereof), excluding transactions with affiliates of the Company.

If an event of default occurs under the Grid Note, SIC IV has the right to require the Company to repay all or any portion of the Grid Note. An event of default is deemed to have occurred on: (i) the non-payment of any of the amounts due under the Grid Note within five (5) Business Days after the date such payment is due and payable; (ii) dissolution or liquidation, as applicable, of the Company; (iii) various bankruptcy or insolvency events shall have occurred, (iv) the inaccuracy in any material respect of any warranty, representation, statement, report or certificate the Company makes to Lender under the Note hereto; (v) the Company contests, disputes or challenges in any manner, whether in a judicial proceeding or otherwise, the validity or enforceability of any material provision in the Grid Note; or (vi) a material adverse change in the business plan or prospects of the Company in the reasonable opinion of SIC IV.

As of December 31, 2016 and June 30, 2016 the principal amount outstanding under the Grid Note was \$3,465,000 and \$4,563,000, respectively.

On July 8, 2016, the Company and SIC III, SIC IV and SIC VI entered into an Exchange Agreement pursuant to which, subject to adjustment, (i) 3,000 shares of the Company's Series C Preferred Stock owned by SIC III are to be exchanged for 890,898 shares of the Company's common stock and (ii) all of the debt held by Mr. Sillerman and such affiliates is to be exchanged for 5,066,654 shares of the Company's common stock. Issuance of the shares is

conditioned upon approval of the Company's shareholders, the closing of an offering of the Company's common stock in the amount of at least \$10,000,000 approval of its Listing of Additional Shares application with NASDAQ, the Company shall not be subject to any bankruptcy proceeding, and various other conditions. The exchange price shall be equal to the lesser of \$5.20 and the price at which the Debentures can be exchanged for shares of the Company's common stock. The Company received an independent valuation with respect to the original exchange that the exchange price of \$5.20 reflects fair value. Any additional change is subject to the receipt by the Company of an updated fair value determination. The agreement provides for termination in the event the conditions are not satisfied by March 31, 2017. At the date of this filing, this transaction has not yet closed.

Amended Exchange Agreement/Amended Grid Note

On July 18, 2016, SIC III, SIC IV and SIC VI, LLC entered into an amendment to the Exchange Agreement relating to the exchange of debt and shares of the Series C Preferred Stock of the Company for shares of the

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)**

9. Loans Payable - (continued)

Company's common stock. The Exchange Agreement modified the Grid Note to provide that SIC IV shall be entitled to repayment of up to \$2,000,000 of the outstanding principal balance of the Grid Note and the Company shall be entitled to draw up to an additional \$5,000,000.

On August 22, 2016, the Company and SIC IV, entered into a Note Exchange Agreement pursuant to which \$3,150,000, which represents all of the outstanding principal and accrued interest outstanding under the Grid Note other than \$900,000, was exchanged for 3,150 shares of the Company's Series C Preferred Stock at an exchange price of \$1,000 per share. The Note Exchange Agreement provides for the newly issued shares to be held subject to the obligations to convert the shares into common stock on the terms and on the conditions set forth in the Exchange Agreement. Therefore, the outstanding balance of the Grid Note at December 31, 2016 was \$3,465,000.

Interest expense on the Grid Note for the six months ended December 31, 2016 and 2015 was \$148,000 and \$201,000 respectively.

In connection with the Company's entering into the Perk Credit Agreement (as defined below), SIC IV agreed to subordinate payment of the Grid Note to amounts owed to Perk under the Perk Credit Agreement. SIC IV also consented to the consummation of the Asset Purchase Agreement with Perk. In exchange for such consent and such agreement to subordinate, the Company agreed to provide SIC IV a security interest in the assets of the Company in connection with amounts outstanding under the Grid Note.

The Company entered into a Security Agreement with SIC IV, pursuant to which the Company pledged its assets in connection with such security interest. The foregoing descriptions of the Security Agreement is qualified in its entirety by reference to the full text of the form of Security Agreement.

Secured Revolving Loans and Lines of Credit

On January 27, 2016, Sillerman Investment Company VI LLC (SIC VI), an affiliate of Robert F.X. Sillerman, the Executive Chairman and Chief Executive Officer of the Company, entered into a Secured Revolving Loan agreement (the Secured Revolving Loan I) with the Company and its subsidiaries, wetpaint.com, Inc. and Choose Digital Inc. (collectively, the Subsidiaries), pursuant to which the Company can borrow up to \$1,500,000. The Secured Revolving Loan bears interest at the rate of 12% per annum. In connection with the Secured Revolving Loan, the Company and the Subsidiaries have entered into a Security Agreement (the Security Agreement) with SIC VI, under which the Company and the Subsidiaries have granted SIC VI a continuing security interest in all assets of the Company and the Subsidiaries, with the exception of the Company's interest in DraftDay Gaming Group, Inc. The Company intends to use the proceeds from the Secured Revolving Loan to fund working capital requirements and for general corporate purposes in accordance with a budget to be agreed upon by SIC VI and the Company. As of June 30, 2016, \$1,500,000 had been advanced thereunder. Interest expense on the Secured Revolving Loan I was approximately

\$27,000 for the six months ended December 31, 2016.

The Company and its subsidiaries wetpaint.com, inc., and Choose Digital, Inc. (the Subsidiaries) entered into a secured, revolving Line of Credit on March 29, 2016 with SIC VI (the Secured Revolving Line of Credit), pursuant to which the Company can borrow up to \$500,000. The Secured Revolving Line of Credit bears interest at the rate of 12% per annum. In connection with the Secured Revolving Line of Credit, the Company and the Subsidiaries have entered into a Security Agreement (the Security Agreement) with SIC VI, under which the Company and the Subsidiaries have granted SIC VI a continuing security interest in all assets of the Company and the Subsidiaries, with the exception of the Company's interest in DraftDay Gaming Group, Inc. The Company intends to use the proceeds from the Secured Revolving Line of Credit to fund working capital requirements and for general corporate purposes in accordance with a budget to be

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9. Loans Payable - (continued)

agreed upon by SIC VI and the Company. At June 30, 2016, \$500,000 had been advanced thereunder. Interest expense on the Secured Revolving Line of Credit was approximately \$9,000 for the six months ended December 31, 2016.

On April 29, 2016, SIC VI entered into an additional secured revolving loan agreement with the Company and the Subsidiaries (Secured Revolving Loan), pursuant to which the Company can borrow up to \$500,000. Loans under this loan agreement bear interest at the rate of 12% per annum and mature on December 31, 2016, barring any events of default or a change of control of the Company. As of June 30, 2016, \$500,000 had been advanced thereunder. Interest expense on the Secured Revolving Loan was \$9,000 for the six months ended December 31, 2016.

On May 16, 2016, SIC VI entered into an additional secured revolving loan agreement with the Company and the Subsidiaries (Secured Revolving Loan II), pursuant to which the Company can borrow up to \$500,000. Loans under this loan agreement bear interest at the rate of 12% per annum and mature on December 31, 2016, barring any events of default or a change of control of the Company. As of June 30, 2016, \$500,000 had been advanced thereunder. Interest expense on the Secured Revolving Loan II was approximately \$9,000 for the six months ended December 31, 2016.

On June 27, 2016, SIC VI entered into a secured revolving loan agreement (the Secured Revolving Loan III) with the Company and its subsidiaries, pursuant to which the Company can borrow up to \$1,200,000. The Secured Revolving Loan III bears interest at the rate of 12% per annum and matures on December 31, 2016, barring any events of default or a change of control of the Company. At June 30, 2016, approximately \$135,000 had been advanced thereunder. Interest expense on the Secured Revolving Loan III was approximately \$8,000 for the six months ended December 31, 2016.

On August 22, 2016, the Company and SIC VI entered into a Note Exchange Agreement pursuant to which \$3,608,000, which represented all of the outstanding principal and accrued interest of certain notes held by SIC VI, was exchanged for 3,608 shares of the Company's Series C Preferred Stock at an exchange price of \$1,000 per share. The Note Exchange Agreement provides for the newly issued shares to be held subject to the obligations to convert the shares into common stock on the terms and on the conditions set forth in the Exchange Agreement. The Secured Revolving Loans and Lines of Credit were retired with the exchange transaction.

Related Approvals

Because each of the transactions referred to in the foregoing sections involved Mr. Sillerman, or an affiliate of his, the transactions were subject to certain rules regarding affiliate transactions. As such, each was approved by a Special Committee of the Board of Directors and a majority of the independent members of the Board of Directors of the Company.

Convertible Promissory Note

On June 27, 2016, the Company entered into a Convertible Promissory Note with Reaz Islam (RI), the Company's Chief of Staff, pursuant to which RI loaned the Company \$300,000 (the RI Convertible Note). The RI Convertible Note bears interest at a rate of 12% and matures on December 31, 2016. RI shall have the right to convert the RI Convertible Note into shares of the common stock of the Company at such time, on such terms, and in accordance with such procedures as Mr. Sillerman shall have the right to convert debt held by Mr. Sillerman or his affiliates into shares of the Company's common stock. The RI Convertible Note is subordinate to any note held by Mr. Sillerman or his affiliates and RI has agreed to execute any agreement reasonably required in connection therewith. As of December 31, 2016, \$300,000 of principal was outstanding under the RI Convertible Note. Interest expense for the six months ended December 31, 2016 was approximately \$18,000.

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9. Loans Payable - (continued)

Promissory Notes

In accordance with the Assets Purchase Agreement to purchase the DraftDay Business (see Note 6, Acquisitions), the Company issued promissory notes to MGT Capital (MGT Promissory Notes) in the principal amount of \$234,000 due and paid on September 29, 2015 and in the aggregate principal amount of \$1,875,000 due March 8, 2016. The Company was not able to make the payment at the due date and on March 24, 2016 converted \$824,000 of the promissory notes to common stock and \$110,000 of the promissory notes to a Series D Preferred Stock (see Note 11, Stockholders Equity (Deficit)). All such notes bear interest at a rate of 5% per annum. On April 13, 2016, MGT converted all 110 shares of the Company's Series D Preferred Stock into shares of common stock of the Company. Accordingly, the Company issued 18,332 shares of common stock to MGT. Thereafter, there are no shares of the Company's Series D Preferred Stock outstanding.

On June 14, 2016, the Company entered into a second exchange agreement with MGT (the Second MGT Exchange Agreement) relating to the \$940,000 remaining due under the MGT Note (see Note 6, Acquisitions). Under the Second MGT Exchange Agreement, the MGT Note shall be exchanged in full for (a) \$11,000 in cash representing accrued interest and (b) 132,092 shares of Company common stock, subject to certain adjustments. Issuance of the shares is conditioned upon approval of the Company's shareholders and approval of its Listing of Additional Shares application with NASDAQ. Therefore, the outstanding balance of the MGT Promissory Notes was \$0 at December 31, 2016. The Company recorded interest expense of approximately \$12,000 for the six months ended December 31, 2016. On October 10, 2016, the Company satisfied the MGT Note through the issuance of 136,304 shares of its common stock and payment of interest of approximately \$16,000.

In exchange for releasing certain liens and encumbrances with respect to the DraftDay Business (see Note 6, Acquisitions), the Company issued promissory notes to Kuusamo Capital Ltd. (Kuusamo Promissory Notes) in the principal amount of \$16,000 due and paid on September 29, 2015 and in the aggregate principal amount of \$125,000 due March 8, 2016. The Company was not able to make the payment at the due date. All such notes bear interest at a rate of 5% per annum. On September 21, 2016, the Company satisfied the Kuusamo Promissory Note through the issuance of 8,410 shares of its common stock. The outstanding balance of the Kuusamo Promissory Notes was \$0 at December 31, 2016. The Company recorded interest expense of approximately \$1,000 for the six months ended December 31, 2016.

Accounts Payable Settlements

North America Photon Infotech Ltd. (Photon), a company based in Mauritius that had provided development services to the Company, filed suit in California on March 28, 2016 to collect approximately \$218,000 owed by the Company to Photon. The Company settled this matter on May 12, 2016 in part by issuing a Note in the amount of \$110,000,

payable in six months. Such note was settled on November 15, 2016 with the issuance of 31,510 shares of the Company's common stock.

Interest expense on these notes issued in connection with vendor settlements was approximately \$7,000 and \$22,000 for the three and six months ended December 31, 2016, respectively.

10. Commitments and Contingencies

Litigation

A Complaint (Index #654984/2016) was filed by Andy Mule, on behalf of himself and others similarly situated, in the Supreme Court of the State of New York. The Complaint, which names the Company, each of its current directors, and President, as a former director, as defendants, claims a breach of fiduciary duty relating to the terms of a proposed conversion of debt and preferred shares into common equity by Mr. Sillerman and/or his affiliates. The Complaint seeks unspecified damages and such relief as the Court may

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

10. Commitments and Contingencies - (continued)

deem appropriate. The Company accepted service on October 4, 2016, and filed a motion to dismiss on November 14, 2016. The Plaintiff has until April 7, 2017 to respond. The Company believes that this claim is without merit.

A complaint (Case #8:16-cv-02101-DOC-JCG) was filed in the United States District Court, Central District of California, Southern Division by Stephan Wurth Photography, Inc. The Complaint, which names Wetpaint.com, Inc. and two former employees of Rant, Inc., claims copyright infringement relating to photographs of Anna Kournikova that first appeared on a Rant website some time ago and continued to appear after the Company's purchase of Rant on July 8, 2016. The Company is in settlement discussions.

On January 20, 2017, a Complaint (Case #3D-2017-00898658-CU-CO-CJC) was filed in the Superior Court of California, County of Orange, by Jamboree Center 4 LLC, the former landlord of Rant, Inc., relating to rent Jamboree Center claims is owed for the period after the Company purchased Rant. The Company believes this claim is without merit, as the Company did not assume this liability. The Company intends to vigorously defend this action and seek indemnification from the sellers of the Rant assets.

On January 31, 2017, a complaint (Case #650513/2017) was filed in New York County Supreme Court, New York by Outbrain, Inc. (Outbrain) against the Company and others, alleging failure to pay \$739,190 owed to Outbrain by Rant between July 2015 and January 2016. The Company believes this claim is without merit, as the Company did not assume the liability to Outbrain. The Company intends to vigorously defend this action and seek indemnification from the sellers of the Rant assets.

The Company is subject to litigation and other claims that arise in the ordinary course of business. While the ultimate result of our outstanding legal matters cannot presently be determined, the Company does not expect that the ultimate disposition will have a material adverse effect on its results of operations or financial condition. However, legal matters are inherently unpredictable and subject to significant uncertainties, some of which are beyond our control. As such, there can be no assurance that the final outcome will not have a material adverse effect on the Company's financial condition and results of operations.

11. Stockholders Equity

Common Stock

As of December 31, 2016 there were 300,000,000 shares of authorized common stock and 3,244,275 shares of common stock issued and outstanding, respectively. As of June 30, 2016 there were 300,000,000 shares of authorized common stock and 3,023,753 shares of common stock issued and outstanding, respectively. Except as otherwise provided by Delaware law, the holders of the Company's common stock are entitled to one vote per share on all

matters to be voted upon by the stockholders.

Preferred Stock

The Company has authorized four series of preferred stock, including classes of Series A Preferred Stock, Series B Preferred Stock, Series C Preferred Stock, Series D Preferred Stock and Series E Preferred Stock. At this time, there is no Series A, Series B or Series D preferred stock outstanding. Only Series C and Series E Preferred Stock are outstanding, as described below.

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11. Stockholders Equity - (continued)

Series A Convertible Redeemable Preferred Stock

Prior to September 16, 2013, the Company had authorized a class of series A preferred shares, but none of those shares were issued or outstanding. On September 16, 2013, the Company eliminated the prior class of series A preferred shares and created a new class of Series A Convertible Redeemable Preferred Stock (the "Series A Convertible Redeemable Preferred Stock"). The Company authorized the issuance of up to 100,000 shares of the Series A Convertible Redeemable Preferred Stock. The designation, powers, preferences and rights of the shares of Series A Convertible Redeemable Preferred Stock and the qualifications, limitations and restrictions thereof are summarized as follows:

The shares of Series A Convertible Redeemable Preferred Stock have an initial stated value of \$1,000 per share (the "Stated Value").

The shares of Series A Convertible Redeemable Preferred Stock are entitled to receive quarterly cumulative dividends at a rate equal to 7% per annum of the Stated Value whenever funds are legally available and when and as declared by the Company's board of directors. If the Company declares a dividend or the distribution of its assets, the holders of Series A Convertible Redeemable Preferred Stock shall be entitled to participate in the distribution to the same extent as if they had converted each share of Series A Convertible Redeemable Preferred Stock held into Company common stock.

Each share of Series A Convertible Redeemable Preferred Stock is convertible, at the option of the holders, into shares of Company common stock at a conversion price of \$23.00.

The Company may redeem any or all of the outstanding Series A Convertible Redeemable Preferred Stock at any time at the then current Stated Value, subject to a redemption premium of (i) 8% if redeemed prior to the one year anniversary of the initial issuance date; (ii) 6% if redeemed on or after the one year anniversary of the initial issuance date and prior to the two year anniversary of the initial issuance date; (iii) 4% if redeemed on or after the two year anniversary of the initial issuance date and prior to the three year anniversary of the initial issuance date; (iv) 2% if redeemed on or after the three year anniversary of the initial issuance date and prior to the 42 months anniversary of the initial issuance date; and (v) 0% if redeemed on or after the 42 months anniversary of the initial issuance date.

However, no premium shall be due on the use of up to 33% of proceeds of a public offering of common shares at a price of \$1.00 or more per share.

The Company is required to redeem the Series A Convertible Redeemable Preferred Stock on the fifth anniversary of its issuance.

Upon a change of control of the Company, the holders of Series A Convertible Redeemable Preferred Stock shall be entitled to a change of control premium of (i) 8% if redeemed prior to the one year anniversary of the initial issuance date; (ii) 6% if redeemed on or after the one year anniversary of the initial issuance date and prior to the two year anniversary of the initial issuance date; (iii) 4% if redeemed on or after the two year anniversary of the initial issuance date and prior to the three year anniversary of the initial issuance date; (iv) 2% if redeemed on or after the three year anniversary of the initial issuance date and prior to the 42 months anniversary of the initial issuance date; and (v) 0%

if redeemed on or after the 42 months anniversary of the initial issuance date.

The shares of Series A Convertible Redeemable Preferred Stock are senior in liquidation preference to the shares of Company common stock.

The shares of Series A Convertible Redeemable Preferred Stock shall have no voting rights except as required by law.

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11. Stockholders Equity - (continued)

The consent of the holders of 51% of the outstanding shares of Series A Convertible Redeemable Preferred Stock shall be necessary for the Company to: (i) create or issue any Company capital stock (or any securities convertible into any Company capital stock) having rights, preferences or privileges senior to or on parity with the Series A Convertible Redeemable Preferred Stock; or (ii) amend the Series A Convertible Redeemable Preferred Stock. At December 31, 2016 and June 30, 2016 there were no shares of Series A Convertible Redeemable Preferred Stock outstanding.

Series B Convertible Preferred Stock

On September 16, 2013, the Company created 50,000 shares of Series B Convertible Preferred Stock (the Series B Convertible Preferred Stock). The designation, powers, preferences and rights of the shares of Series B Convertible Preferred Stock and the qualifications, limitations and restrictions thereof are summarized as follows:

The shares of Series B Convertible Preferred Stock have an initial stated value of \$1,000 per share. The shares of Series B Convertible Preferred Stock are convertible, at the option of the holders, into shares of Company common stock at a conversion price of \$23.00. The shares of Series B Convertible Preferred Stock may only be converted from and after the earlier of either of: (x) the first trading day immediately following (i) the closing sale price of the Company's common stock being equal to or greater than \$33.40 per share (as adjusted for stock dividends, stock splits, stock combinations and other similar transactions occurring with respect to the Company's common stock from and after the initial issuance date) for a period of five consecutive trading days following the initial issuance date and (ii) the average daily trading volume of the Company's common stock (as reported on Bloomberg) on the principal securities exchange or trading market where the Company's common stock is listed or traded during the measuring period equaling or exceeding 1,250 shares of Company's common stock per trading day (the conditions set forth in the immediately preceding clauses (i) and (ii) are referred to herein as the Trading Price Conditions) or (y) immediately prior to the consummation of a fundamental transaction, regardless of whether the Trading Price Conditions have been satisfied prior to such time. A fundamental transaction is defined as (i) a sale of all or substantially all of the assets of the Company, (ii) a sale of at least 90% of the shares of capital stock of the Company or (iii) a merger, consolidation or other business combination as a result of which the holders of capital stock of the Company prior to such merger, consolidation or other business combination (as the case may be) hold in the aggregate less than 50% of the Voting Stock of the surviving entity immediately following the consummation of such merger, consolidation or other business combination (as the case may be), in each case of clauses (i), (ii) and (iii), the Board has determined that the aggregate implied value of the Company's capital stock in such transaction is equal to or greater than \$125,000,000.

The shares of Series B Convertible Preferred Stock are not redeemable by either the Company or the holders thereof. The shares of Series B Convertible Preferred Stock are on parity in dividends and liquidation preference with the shares of Company common stock, which shall be payable only if then convertible into common stock.

The shares of Series B Convertible Preferred Stock shall have no voting rights except as required by law.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

11. Stockholders Equity - (continued)

The consent of the holders of 51% of the outstanding shares of Series B Convertible Preferred Stock shall be necessary for the Company to alter, amend or change any of the terms of the Series B Convertible Preferred Stock. At December 31, 2016 and June 30, 2016, there were no shares of Series B Convertible Preferred Stock outstanding.

Series C Convertible Preferred Stock

We amended the Certificate of Designation of our Series C Convertible Preferred Stock as of August 22, 2016. As amended, the designation, powers, preferences, and rights of the shares of Series C Preferred Stock and the qualifications, limitations and restrictions thereof are summarized as follows:

The shares of Series C Convertible Redeemable Preferred Stock have a stated value of \$1,000 per share. Each holder of a share of Series C Convertible Redeemable Preferred Stock shall be entitled to receive dividends (Dividends) on such share equal to twelve percent (12%) per annum (the Dividend Rate) of the Stated Value before any Dividends shall be declared, set apart for or paid upon any junior stock or parity stock. Dividends on a share of Series C Preferred Stock shall accrue daily at the Dividend Rate, commence accruing on the issuance date thereof, compound annually, be computed on the basis of a 360-day year consisting of twelve 30-day months. The Company may redeem any or all of the outstanding Series C Preferred Stock at any time at the then current Stated Value plus accrued Dividends thereon plus a redemption premium equal to the Stated Value multiplied by 6%. However, no premium shall be due on the use of up to 33% of proceeds of a public offering of common stock at a price of \$5.00 or more per share.

The Series C Preferred Stock is not redeemable or convertible into common stock by the holder (except the Series C Preferred Stock held by Mr. Sillerman and affiliates remains subject to the Exchange Agreement and is convertible in accordance therewith).

The consent of the holders of a majority of the shares of Series C Preferred Stock is necessary for the Company to amend the Series C certificate of designation.

Until the August 22, 2016 amendment, the Series C Convertible Preferred Stock was classified as a component of mezzanine equity in the accompanying Consolidated Balance Sheets. As a result of the amendment, the Series C Preferred Stock is now classified as a component of stockholders (deficit) equity.

Preferred Stock Conversion

Sillerman Investment Company III, LLC (SIC III), an affiliate of Robert F.X. Sillerman, the Company's Executive Chairman and Chief Executive Officer of the Company, owned 10,000 shares of Series C Convertible Redeemable Preferred Stock. On May 9, 2016 (the Exchange Date), the Company and SIC III entered into a Subscription Agreement pursuant to which SIC III subscribed for 1,129,032 shares of the Company's common stock at a price of \$6.20 per share. Accordingly, the aggregate purchase price for such shares was \$7,000,000. The Company and SIC III agreed that SIC III would pay the purchase price for such shares by exchanging 7,000 shares of the Company's Series

C Convertible Redeemable Preferred Stock owned by SIC III for the common stock (the Exchange). All conditions of the Subscription Agreement have been satisfied, and therefore 1,129,032 shares of the Company's common stock were issued to SIC III. Mr. Sillerman and his affiliates now own more than 50% of the outstanding shares of the Company's common stock. The Company determined that this was a fair transaction and did not recognize any stock compensation expense in relation with the conversion.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

11. Stockholders Equity - (continued)

On August 22, 2016, the Company and SIC III, SIC IV, SIC VI entered into an Note Exchange Agreement pursuant to which \$30,175,000, which represents all of the outstanding principal and accrued interest of certain notes held by SIC III, SIC IV, and SIC VI other than \$900,000 of debt held by SIC IV pursuant to that certain Line of Credit Grid Note dated as of June 11, 2015, was exchanged for 30,175 shares of the Company's Series C Convertible Preferred Stock at an exchange price of \$1,000 per share. The Note Exchange Agreement provides for the newly issued shares to be held subject to the obligations to convert the shares into common stock on the terms and on the conditions set forth in the Exchange Agreement.

At December 31, 2016 and June 30, 2016, there were 33,175 and 3,000 shares of Series C Convertible Preferred Stock outstanding, respectively.

Series D Convertible Preferred Stock

On March 24, 2016, the Company created a new class of Series D Convertible Redeemable Preferred Stock (the Series D Convertible Preferred Stock). The Company authorized the issuance of up to 110 shares of the Series D Convertible Preferred Stock. The rights, preferences, privileges and restrictions of the shares of Series D Convertible Preferred Stock and the qualifications, limitations and restrictions thereof are summarized as follows:

The shares of Series D Convertible Preferred Stock have a stated value of \$1,000 per share. Each share of Series D Convertible Preferred Stock is convertible, at the option of the holders, at a rate of 167 shares of common stock for one share of converted Series D Convertible Preferred Stock.

Shares of Series D Convertible Preferred Stock are not entitled to a liquidation preference. Conversions of the Series D Convertible Preferred Stock shall be limited such that any given conversion shall not cause the holder's aggregate beneficial ownership of the shares of common stock to exceed 9.99% of the Company's outstanding common stock.

The shares of Series D Convertible Preferred Stock shall have no voting rights except as required by law. The consent of the holders of a majority of the shares of Series D Convertible Preferred Stock is necessary for the Company to amend the Series D certificate of designation. The Series D Convertible Preferred Stock is classified as a component of stockholders' equity in the accompanying consolidated balance sheets. There were no shares of Series D Convertible Preferred Stock outstanding at December 31, 2016 and June 30, 2016.

Series E Convertible Preferred Stock

On July 7, 2016, the Company created a new class of Series E Convertible Preferred Stock (the Series E Convertible Preferred Stock) by filing a Certificate of Designation of the Series E Convertible Preferred Stock of the Company

(the Series E Certificate of Designation) with the Secretary of State of the State of Delaware. The Company authorized the issuance of up to 10,000 shares of the Series E Convertible Preferred Stock. The rights, preferences, privileges and restrictions of the shares of Series E Convertible Preferred Stock and the qualifications, limitations and restrictions thereof are contained in the Series E Certificate of Designation and are summarized as follows:

The shares of Series E Convertible Preferred Stock have a stated value of \$1,000 per share (the Stated Value).

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11. Stockholders Equity - (continued)

Subject to the satisfaction of certain conditions as set forth therein, each share of Series E Convertible Preferred Stock is convertible, at the option of the holders, on the basis of its Stated Value and accrued, but unpaid Dividends, into shares of the Company's common stock at a conversion price equal to the lesser of \$5.20 or the Exchange Price.

The shares of Series E Convertible Preferred Stock shall have no voting rights except as required by law. The consent of the holders of a majority of the shares of Series E Convertible Preferred Stock is necessary for the Company to amend its Series C Certificate of Designation.

As of December 31, 2016, there were 4,435 shares of Series E Convertible Preferred Stock outstanding. There were no shares of Series E Convertible Preferred Stock outstanding as of June 30, 2016.

Subscription Agreement

On December 3, 2015, the Company and SIC IV entered into a Subscription Agreement pursuant to which SIC IV subscribed for 437,500 shares of the Company's common stock at a price of \$9.40 per share. Accordingly, the aggregate purchase price for such shares was \$4,112,000.

Non-controlling Interest

As discussed in Note 6, Acquisitions, on September 8, 2015, the Company acquired the assets of the DraftDay Business and its operations have been consolidated with the Company's operations as of that date. The Company has recorded non-controlling interest in its Consolidated Balance Sheets and Consolidated Statements of Operations for the portion of the DraftDay Business that the Company does not own. In the three months ended September 30, 2016, Sportech invested an additional \$121 into the DraftDay Business in exchange for shares of Series A Preferred Stock of DDGG for \$1 per share. In connection with termination of the Sportech MSA at June 30, 2016 (see Note 6, Acquisitions), Sportech returned 4,200 shares of DDGG stock. The Company reduced non-controlling interest by approximately \$378,000, which represents the fair value of these shares.

12. Share-Based Payments

Equity Incentive Plan

The 2011 Executive Incentive Plan (the Plan) of the Company was approved on February 21, 2011 by the written consent of the holder of a majority of the Company's outstanding common stock. The Plan provides the Company the ability to grant to any officer, director, employee, consultant or other person who provides services to the Company or any related entity, options, stock appreciation rights, restricted stock awards, dividend equivalents and other stock-based awards and performance awards, provided that only employees are entitled to receive incentive stock options in accordance with IRS guidelines. The Plan provides for the issuance of a maximum of 6,250,000 shares of

common stock. Pursuant to the Executive Incentive Plan and the employment agreements, between February 15, 2011 and December 31, 2016, the Compensation Committee of the Company's Board of Directors authorized the grants of restricted stock and stock options described below.

Restricted Stock

Compensation expense related to restricted stock was approximately \$133,000 and \$9,981,000 for the six months ended December 31, 2016 and 2015, respectively. As of December 31, 2016, there was approximately \$239,000 in total unrecognized share-based compensation costs related to restricted stock. There were 65,318 shares of restricted stock granted during the six months ended December 31, 2016.

Stock Options

The Company accounts for these options at fair market value of the options on the date of grant, with the value being recognized over the requisite service period. The fair value of each option award is estimated

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12. Share-Based Payments - (continued)

using a Black-Scholes option valuation model. Expected volatility is based on the historical volatility of the price of comparable companies' stock. The risk-free interest rate is based on U.S. Treasury issues with a term equal to the expected life of the option. The Company uses historical data to estimate expected dividend yield, expected life and forfeiture rates. Options generally have an expiration of 10 years and vest over a period of 3 or 4 years. There were no options granted during the six months ended December 31, 2016 and 2015.

Compensation expense related to stock options of approximately \$13,000 and \$173,000 is included in the accompanying Consolidated Statements of Operations in selling, general and administrative expenses for the three months ended December 31, 2016 and 2015, respectively. Compensation expense related to stock options of approximately \$28,000 and \$346,000 is included in the accompanying Consolidated Statements of Operations in selling, general and administrative expenses for the six months ended December 31, 2016 and 2015, respectively. As of December 31, 2016, there was approximately \$107,000 of total unrecognized stock-based compensation cost which will generally be recognized over a two year period.

13. Income Taxes

For the three and six months ended December 31, 2016 and 2015, the Company did not record an income tax benefit because it has incurred taxable losses and has no history of generating taxable income and therefore the Company cannot presently anticipate the realization of a tax benefit on its Net Operating Loss carryforward. At December 31, 2016 the Company has a Net Operating Loss carryforward of approximately \$165,112,000, which will begin to expire in 2030.

As a result of the Rant Asset Purchase in July 2016, the Company has goodwill of approximately \$7,589,000 that is not amortized for financial reporting purposes. However, these assets are tax deductible, and therefore amortized over 15 years for tax purposes. As such, deferred income tax expense and a deferred tax liability arise as a result of the tax-deductibility of these assets. The resulting deferred tax liability, which is expected to continue to increase over time, will have an indefinite life, resulting in what is referred to as a "naked tax credit." This deferred tax liability could remain on the Company's balance sheet permanently unless there is an impairment of the related assets (for financial reporting purposes), or the business to which those assets relate were to be disposed of. The Company recorded income tax expense of \$102,000 in the three and six months ended December 31, 2016 related to the "naked tax credit."

The Company has evaluated its income tax positions and has determined that it does not have any uncertain tax positions. The Company will recognize interest and penalties related to any uncertain tax positions through its income tax expense.

The Company may in the future become subject to federal, state and local income taxation though it has not been

since its inception. The Company is not presently subject to any income tax audit in any taxing jurisdiction.

14. Related Party Transactions

Shared Services Agreements

The Company also entered into a shared services agreement (SFX Shared Services Agreement) with SFX, pursuant to which it shares costs for services provided by several of the Company s and/or SFX s employees. Such employees will continue to be paid by their current employers, and SFX will reimburse the Company directly for its portion of such salary and benefits and Company will reimburse SFX directly for its portion of such salary and benefits (but not for any bonus, option or restricted share grant made by either company, which will be the responsibility of the company making such bonus, option or restricted share grant). The Audit Committee of each company s Board of Directors reviews and, if appropriate, approves the allocations made and whether payments need to be adjusted or reimbursed, depending on the circumstances. The Company entered into an amendment (the Amendment) to the shared services agreement on January 22,

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Function(x) Inc.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)**

14. Related Party Transactions - (continued)

2015, pursuant to which the Company may provide additional services to SFX, and SFX may provide certain services to the Company. In particular, the shared services agreement provides that, in addition to services already provided, certain employees of the Company may provide human resources, content and programming, and facilities services to SFX, subject to reimbursement based on salary and benefits for the employees providing the services, plus 20% for miscellaneous overhead, based on a reasonable estimate of time spent. In addition, the Amendment provides that SFX may provide certain tax services to the Company, subject to reimbursement based on salary and benefits for the employees providing the services, plus 20% for miscellaneous overhead, based on a reasonable estimate of time spent.

The parties terminated the SFX Shared Services Agreement effective as of January 1, 2016. SFX was reorganized in bankruptcy on December 2, 2016.

The net balance due (to)/from SFX, including amounts related to the Sales Agency Agreement, discussed below, as of December 31, 2016 and June 30, 2016 was approximately \$0 and \$142,000 respectively.

License Agreement

On March 10, 2014, the Company entered into an audio recognition and related loyalty program software license and services agreement with SFX. Pursuant to the terms of the license agreement, SFX paid the Company \$5,000,000 to license its audio recognition software and related loyalty platform for a term of 10 years. The amount was deferred and is being amortized over the ten years period. For the three months ended December 31, 2016 and 2015, the Company recognized \$125,000 and \$125,000, respectively of revenue related to this agreement. For the six months ended December 31, 2016 and 2015, the Company recognized \$250,000 and \$250,000, respectively, of revenue related to this agreement.

Secured Line of Credit

On January 27, 2016, Sillerman Investment Company VI LLC ("SIC VI"), an affiliate of Robert F.X. Sillerman, the Executive Chairman and Chief Executive Officer of the Company, entered into a secured revolving loan agreement (the "Secured Revolving Loan") with the Company and its subsidiaries, Wetpaint and Choose Digital (collectively, the "Subsidiaries"), pursuant to which the Company can borrow up to \$1,500,000. The Secured Revolving Loan bears interest at the rate of 12% per annum. In connection with the Secured Revolving Loan, the Company and the Subsidiaries have entered into a Security Agreement (the "Security Agreement") with SIC VI, under which the Company and the Subsidiaries have granted SIC VI a continuing security interest in all assets of the Company and the Subsidiaries, with the exception of the Company's interest in DraftDay Gaming Group, Inc. The Company intends to use the proceeds from the Secured Revolving Loan to fund working capital requirements and for general corporate purposes in accordance with a budget to be agreed upon by SIC VI and the Company. As of June 30, 2016,

\$1,500,000 had been advanced thereunder. Because Mr. Sillerman is a director, executive officer and greater than 10% stockholder of the Company, a majority of the Company's independent directors approved the transaction. On August 22, 2016, the Company and SIC IV entered into an Note Exchange Agreement pursuant to which \$1,500,000, which represents all of the outstanding principal and accrued interest of certain notes held by SIC IV was exchanged for 1,500 shares of the Company's Series C Convertible Preferred Stock at an exchange price of \$1,000 per share. See Note Exchange Agreement paragraph below for additional information on the August 22, 2016 exchange.

\$500,000 Line of Credit

The Company and its subsidiaries entered into a secured, revolving Line of Credit on March 29, 2016 with SIC VI (the "Secured Revolving Line of Credit"), pursuant to which the Company can borrow up to \$500,000. The Secured Revolving Line of Credit bears interest at the rate of 12% per annum. In connection with the Secured Revolving Line of Credit, the Company and the Subsidiaries have entered into a Security Agreement (the "Security Agreement") with SIC VI, under which the Company and the Subsidiaries have

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14. Related Party Transactions - (continued)

granted SIC VI a continuing security interest in all assets of the Company and the Subsidiaries, with the exception of the Company's interest in DraftDay Gaming Group, Inc. The Company intends to use the proceeds from the Secured Revolving Line of Credit to fund working capital requirements and for general corporate purposes in accordance with a budget to be agreed upon by SIC VI and the Company. At June 30, 2016, \$500,000 had been advanced thereunder. On August 22, 2016, the Company and SIC VI entered into an Note Exchange Agreement pursuant to which \$500,000, which represents all of the outstanding principal and accrued interest of certain notes held by SIC VI was exchanged for 500 shares of the Company's Series C Convertible Preferred Stock at an exchange price of \$1,000 per share. See Note Exchange Agreement paragraph below for additional information on the August 22, 2016 exchange.

Preferred Stock Conversion

Sillerman Investment Company III, LLC (SIC III), an affiliate of Robert F.X. Sillerman, the Company's Executive Chairman and Chief Executive Officer of the Company, owned 10,000 shares of Series C Convertible Redeemable Preferred Stock. On May 9, 2016 (the Exchange Date), the Company and SIC III entered into a Subscription Agreement pursuant to which SIC III subscribed for 1,129,032 shares of the Company's common stock at a price of \$6.20 per share. Accordingly, the aggregate purchase price for such shares was \$7,000,000. The Company and SIC III agreed that SIC III would pay the purchase price for such shares by exchanging 7,000 shares of the Company's Series C Convertible Redeemable Preferred Stock owned by SIC III for the common stock (the Exchange). All conditions of the Subscription Agreement have been satisfied, and therefore 1,129,032 shares of the Company's common stock were issued to SIC III. Mr. Sillerman and his affiliates now own more than 50% of the outstanding shares of the Company's common stock. The Company determined that this was a fair transaction and did not recognize any stock compensation expense in relation with the conversion.

Exchange Agreement

On July 8, 2016, the Company and SIC III, SIC IV and SIC VI, each an affiliate of Mr. Sillerman, entered into an Exchange Agreement pursuant to which, subject to adjustment, (i) 3,000 shares of the Company's Series C Preferred Stock owned by SIC III are to be exchanged for 890,898 shares of the Company's common stock and (ii) all of the debt held by Mr. Sillerman and such affiliates is to be exchanged for 5,066,654 shares of the Company's common stock. Issuance of the shares is conditioned upon approval of the Company's shareholders (see Shareholder Approval in this section), the closing of an offering of the Company's common stock in the amount of at least \$10,000,000, approval of its Listing of Additional Shares application with NASDAQ, the Company shall not be subject to any bankruptcy proceeding, and various other conditions. The exchange price shall be equal to the lesser of \$5.20 and the price at which the Debentures can be exchanged for shares of the Company's common stock. The Company received an independent valuation with respect to the original exchange that the exchange price of \$5.20 reflects fair value. Any additional change is subject to the receipt by the Company of an updated fair value determination. The agreement

provides for termination in the event the conditions are not satisfied by March 31, 2017. At the date of this filing, this transaction has not yet closed.

Amended Exchange Agreement/Amended Grid Note

On July 18, 2016, SIC III, SIC IV and SIC VI, LLC entered into an amendment to the Exchange Agreement relating to the exchange of debt and shares of the Series C Preferred Stock of the Company for shares of the Company's common stock. The Exchange Agreement modified the Grid Note to provide that SIC IV shall be entitled to repayment of up to \$2,000,000 of the outstanding principal balance of the Grid Note and the Company shall be entitled to draw up to an additional \$5,000,000. \$3,605,000 remains available to draw under the Grid Note and at the date of this filing, the current balance is \$2,950,000.

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14. Related Party Transactions - (continued)

Note Exchange Agreement

On August 22, 2016, the Company and SIC III, SIC IV, and SIC VI, each an affiliate of Mr. Sillerman, entered into a Note Exchange Agreement pursuant to which \$30,175,000, which represents all of the outstanding principal and accrued interest of the Note, the Loans, the Secured Revolving Loan, the Secured Revolving Promissory Note, the Secured Revolving Promissory Note II, and the Secured Revolving Promissory Note III (all described and defined in Note 9, Loans Payable) other than \$900,000 of debt held by SIC IV pursuant to that certain Line of Credit Grid Promissory Note dated as of June 11, 2015 (see Grid Note), was exchanged for 30,175 shares of the Company's Series C Preferred Stock (see Amendment to Certificate of Designation of Series C Preferred Stock in this section.) The exchange price is \$1,000 per share. The Note Exchange Agreement provides for the newly issued shares to be held subject to the obligations to convert the shares into common stock on the terms and on the conditions set forth in the Exchange Agreement, and subject to the additional obligations set forth in the Subordination Agreement and the Lockup Agreements. The Grid Note remains subject to the Exchange Agreement.

Related Approvals

Because the above transactions were subject to certain rules regarding affiliate transactions, the Company's Audit Committee and a majority of the independent members of the Company's Board of Directors approved each of these transactions.

15. Fair Value Measurement

The Company values its assets and liabilities using the methods of fair value as described in ASC 820. ASC 820 establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. The three levels of fair value hierarchy are described below:

Level 1 Quoted prices in active markets for identical assets or liabilities.

Level 2 Quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 Inputs that are generally unobservable and typically reflect management's estimates of assumptions that market participants would use in pricing the asset or liability.

In determining fair value, the Company utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible, and considers counter-party credit risk in its assessment of fair value. Observable or market inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's assumptions based on the best information available. The Company has certain liabilities that are required to be recorded at fair value on a recurring basis in accordance with accounting principles generally accepted in the United States, as described below.

The Company issued 1,068 warrants in connection with the May 10, 2012 PIPE. Each warrant has a sale price of \$8,800 and is exercisable into 1 share of common stock at a price of \$12,800 over a term of three years. Further, the exercise price of the warrants is subject to "down round" protection, whereby any issuance of shares at a price below the current price resets the exercise price equal to the price of newly issued shares (the "Warrants"). In connection with the PIPE Exchanges on September 16, 2013, the exercise price of the Warrants was reset to \$2. The fair value of such warrants has been determined utilizing the Binomial Lattice Model in accordance with ASC 820-10, *Fair Value Measurements*. The fair value of the warrants when issued was approximately \$5,281,000. On September 16, 2013, 341 warrants were exchanged in connection with the PIPE Exchanges. The remaining 14,545 warrants were marked to market as of December 31, 2016 and 2015.

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(Unaudited)****15. Fair Value Measurement - (continued)**

to a fair value of \$10,000 and \$10,000, respectively. The Company recorded gains/(losses) of \$0 and \$0 to other income, net in the Consolidated Statements of Operations for the six months ended December 31, 2016 and 2015, respectively. The fair value of the warrant is classified as a current liability on the Consolidated Balance Sheets as of December 31, 2016, due to the Company's intention to retire a significant portion of these warrants in its next round of financing. The Company's warrants were classified as a Level 3 input within the fair value hierarchy because they were valued using unobservable inputs and management's judgment due to the absence of quoted market prices and inherent lack of liquidity.

On February 8, 2016, the Company received Perk warrants as part of the consideration in the sale of the Viggie business. The carrying amount of Perk warrants held is marked-to-market on a quarterly basis using the Monte Carlo valuation model, in accordance with ASC 820-10, *Fair Value Measurements*. The changes to fair value are recorded in the Consolidated Statements of Operations. The fair value of the warrants when issued was approximately \$1,023,000. The warrants were marked to market as of December 31, 2016 to a fair value of \$1,091,000. The Company recorded a loss of approximately \$503,000 to other expense, net in the Consolidated Statements of Operations for the three months ended September 30, 2016. The fair value of the warrant was classified as an other asset on the Consolidated Balance Sheets as of June 30, 2016. The Perk warrants were classified as a Level 3 input within the fair value hierarchy because they were valued using unobservable inputs and management's judgment due to the absence of quoted market prices and inherent lack of liquidity.

In February 2016, the Company received 1,370,000 shares of Perk stock, which is publicly traded on the Toronto Stock Exchange, as part of the consideration in the sale of assets described in the Perk Agreement. These securities are short-term marketable securities, and have been classified as available-for-sale securities. Pursuant to ASC 320-10, *Investments - Debt and Equity Securities* the Company's marketable securities are marked to market on a quarterly basis, with unrealized gains and losses recorded in equity as Other Comprehensive Income/Loss.

On September 30, 2016, the Company sold to Perk the remaining shares (1,013,068) of Perk common stock, the warrants for additional shares, and the right to the Earn-Out Shares received from Perk on the sale of the Viggie rewards business on February 8, 2016. The Company received \$1,300,000 from Perk as consideration therefor. The execution of the Securities Purchase Agreement and closing were simultaneous. In connection with the sale of the Perk shares, the warrants for additional shares and the right to the Earn-Out Shares, the Company recorded a loss of approximately \$2,195,000 in the Other Expense line item of the Consolidated Statements of Operations for the three months ended September 30, 2016.

As discussed in Note 6, Acquisitions, the Company purchased Rant on July 12, 2016. In conjunction with the Rant acquisition, the Company delivered a Secured Convertible Note to Rant in the amount of \$3,000,000 and issued 4,435 of Series E Convertible Preferred Stock. In accordance with ASC 820, the Company had the Secured Convertible Note and Series E Preferred Stock fair valued at the acquisition date. The fair value of the conversion feature of the

Secured Convertible Note was approximately \$500,000 and the fair value of the Series E Preferred Stock was approximately \$7,600,000. The Secured Convertible Note, the fair value of the conversion feature and Series E Preferred Stock were recorded at their acquisition date fair values with a corresponding charges to goodwill in the Consolidated Balance Sheets at September 30, 2016. As of December 31, 2016, the fair value of the conversion feature was determined to be approximately \$400,000. The \$100,000 change in fair value from September 30, 2016 to December 31, 2016 was recorded as other income in the Consolidated Statements of Operations for the three months ended December 31, 2016.

On July 12, 2016, the Company closed the Private Placement of \$4,444,000 principal amount of the Debentures and Warrants. The Debentures and Warrants were fair valued at the Private Placement closing date. The fair value of the Conversion feature was approximately \$1,856,000 and the fair value of the Warrants was \$1,500,000. The Conversion feature and Warrants were recorded at the Private Placement

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15. Fair Value Measurement - (continued)

closing date fair values with corresponding charges to debt discount of approximately \$1,856,000 for the Debentures and approximately \$1,500,000 for the Warrants in the Consolidated Balance Sheets at September 30, 2016. As of December 31, 2016, the fair value of the Conversion feature was determined to be approximately \$1,256,000 and the fair value of the Warrants was determined to be \$410,000. The changes in fair value were recorded as other income in the Consolidated Statements of Operations for the three months ended December 31, 2016.

On August 22, 2016, the Company and SIC III, SIC IV, SIC VI entered into an Note Exchange Agreement pursuant to which \$30,175,000, which represents all of the outstanding principal and accrued interest of certain notes held by SIC III, SIC IV, and SIC VI other than \$900,000 of debt held by SIC IV pursuant to that certain Line of Credit Grid Note dated as of June 11, 2015, was exchanged for 30,175 shares of the Company's Series C Convertible Preferred Stock at an exchange price of \$1,000 per share. The Series C Convertible Preferred Stock was fair valued at the exchange date, August 22, 2016, and determined to be \$28,500,000. The Series C Convertible Preferred Stock was recorded at the exchange date fair value with a corresponding charge to additional paid-in capital of \$1,675,000 in the Consolidated Balance Sheets at September 30, 2016.

Non-financial Assets and Liabilities that are Measured at Fair Value on a Nonrecurring Basis

On a nonrecurring basis, the Company uses fair value measures when analyzing asset impairment. Long-lived assets and certain identifiable intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If it is determined such indicators are present and the review indicates that the assets will not be fully recoverable, based on undiscounted estimated cash flows over the remaining amortization periods, their carrying values are reduced to estimated fair value. Measurements based on undiscounted cash flows are considered to be Level 3 inputs. During the fourth quarter of each year, the Company evaluates goodwill and indefinite-lived intangibles for impairment at the reporting unit level. For each acquisition, the Company performed a detailed review to identify intangible assets and a valuation is performed for all such identified assets. The Company used several market participant measurements to determine estimated value. This approach includes consideration of similar and recent transactions, as well as utilizing discounted expected cash flow methodologies, and/or revenue or EBITDA multiples, among other methods. The amounts allocated to assets acquired and liabilities assumed in the acquisitions were determined using Level 3 inputs. Fair value for property and equipment was based on other observable transactions for similar property and equipment. Accounts receivable represents the best estimate of balances that will ultimately be collected, which is based in part on allowance for doubtful accounts reserve criteria and an evaluation of the specific receivable balances.

Where goodwill has been allocated to a reporting unit and part of the operation within that unit is disposed of, the goodwill associated with the disposed operation is included in the carrying amount of the operation when determining

the gain or loss on disposal. Goodwill disposed in these circumstances is measured based on the relative values of the disposed operation and the portion of the reporting units retained. The relative fair value of each reporting unit is established using discounted expected cash flow methodologies, and/or revenue or EBITDA multiples, or other applicable valuation methods, which are considered to be Level 3 inputs.

The following table presents a reconciliation of assets measured at fair value on a recurring basis using unobservable inputs (level 3):

	(in thousands)
Balance at July 1, 2016	\$ 648
Unrealized losses for the period included in other income (expense), net	(503)
Sale of Perk warrants	(145)
Balance at December 31, 2016	\$

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TABLE OF CONTENTS**Function(x) Inc.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)****15. Fair Value Measurement - (continued)**

As noted above, on September 30, 2016, the Company sold to Perk the remaining shares of Perk common stock, the warrants for additional shares, and the right to the Earn-Out Shares received from Perk on the sale of the Viggie rewards business on February 8, 2016. The Company received \$1,300,000 from Perk as consideration therefor. In connection with the sale of the Perk shares, the warrants for additional shares and the right to the Earn-Out Shares, the Company recorded a loss of approximately \$2,195,000 in the Other Expense line item of the Consolidated Statements of Operations during the three months ended September 30, 2016.

The following table presents a reconciliation of liabilities measured at fair value on a recurring basis using unobservable inputs (level 3):

	(in thousands)
Balance at July 1, 2016	\$ 10
Additions to Level 3	3,856
Changes to fair value	(1,790)
Balance at December 31, 2016	\$ 2,076

16. Subsequent Events**Events of Default**

The Company is currently in events of default under the Debentures issued in the Private Placement for failure to make amortization payments and for failure to maintain the Minimum Cash Reserve.

On October 12, 2016, the first amortization payment in the amount of \$444,000, plus accrued interest of approximately \$114,000 pursuant to the terms of the Debentures became due and payable to the Purchasers. The Company did not make such payment at the time it was due. The Company entered into waiver agreements with Purchasers holding approximately 87% of the principal amount of the Debentures. Such waivers are not binding on the remaining Purchasers of the Debentures. Pursuant to the terms of the Waiver, the Purchasers have agreed to waive the payment of the amortization payments and accrued interest due for October 2016 and November 2016. In consideration for waiving the payment terms of the Debentures, the Company paid, upon execution of the Waiver, 10% of the Amortization Amount that became due on October 12, 2016 and paid on November 12, 2016 10% of the Amortization Amount due in November 2016. All other amounts will be due and payable in accordance with the terms of the Debentures, with the deferred payments due at maturity. The Company did not receive a waiver from one of its debenture holders, holding approximately 13% of the principal amount of the Debentures with respect to the event of default arising out of the Company's failure to make the first amortization payment when due. Pursuant to the terms of

the Debentures, such holder has sent a notice of acceleration, stating that the Company owes approximately \$696,000, reflecting the principal amount of the Debenture plus interest through November 1, 2016. Interest will accrue at 18% until this amount is satisfied. The Company is seeking to settle the matter with the holder; however, there can be no assurance that an agreement will be reached.

The waivers entered into with some of the Purchasers related to the failure to pay the amortization amount do not address the failure to maintain the Minimum Cash Reserve. In addition, the Company is currently in default with respect to the amortization payment due in January 2017.

Pursuant to the terms of the Debentures, the failure to cure the non-payment of amortization or failure to maintain the Minimum Cash Reserve within three trading days after the due date constitutes an Event of Default. Following the occurrence of an event of default, among other things: (1) at the Purchaser's election, the outstanding principal amount of the Debentures, plus accrued but unpaid interest, plus all interest that would have been earned through the one year anniversary of the original issue date if such interest has not yet accrued, liquidated damages and other amounts owed through the date of acceleration, shall become,

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Function(x) Inc.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)**

16. Subsequent Events - (continued)

immediately due and payable in either cash or stock pursuant to the terms of the Debentures; and (2) the interest rate on the Debentures will increase to the lesser of 18% or the maximum allowed by law. In addition to other remedies available to the Purchasers, the Company's obligation to repay amounts due under the Debentures is secured by a first priority security interest in and lien on all of the Company's assets and property, including the Company's intellectual property, and such remedies can be exercised by the Purchasers without additional notice to the Company.

Under terms of the \$3,000,000 Secured Convertible Note issued in connection with the acquisition of Rant, a default under other indebtedness owed by the Company constitutes a default under the Rant Note. As a result of such Event of Default, the holder of the Rant Note has executed a waiver that provides that, until May 15, 2017, the events of default arising out of the failure to pay the amounts due under the Debentures as of the date of the waiver and the failure by the Company to maintain the Minimum Cash Reserve shall not constitute events of default for purposes of the Rant Note. In addition, the Company is currently in default with respect to the Rant Note as a result of the failure to make the Debentures amortization payment due in January 2017.

Secured Lines of Credit

Since the three months ended December 31, 2016, the Company has borrowed an additional \$900,000 under the SIC IV Line of Credit as of the date of this filing. The principal amount now outstanding under the Line of Credit is \$4,115,000 and the Company is entitled to draw up to an additional \$885,000 under the Line of Credit.

Appointment of Chief Operating Officer

On January 19, 2017, the Company named Brian Rosin as its Chief Operating Officer. On January 26, 2017, the Company and Mr. Rosin agreed to the terms of a new employment agreement reflecting his new role.

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Function(x) Inc. (formerly known as Viggle Inc.)

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders
Function(x) Inc. (formerly known as Viggle Inc.)

New York, New York

We have audited the accompanying consolidated balance sheets of Function(x) Inc. (the Company) (formerly known as Viggle Inc.) as of June 30, 2016 and 2015, and the related consolidated statements of operations, stockholders equity (deficit) and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. The Company is not required to, nor were we engaged to perform an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Function(x) Inc. (formerly known as Viggle Inc.) at June 30, 2016 and 2015, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 1 to the consolidated financial statements, the Company has suffered recurring losses from operations and at June 30, 2016 has a deficiency in working capital that raise substantial doubt about its ability to continue as a going concern. Management's plans in regard to these matters are also described in Note 1. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

/s/ BDO USA, LLP

New York, NY
October 11, 2016

TABLE OF CONTENTS**Function(x) Inc.****CONSOLIDATED BALANCE SHEETS**
(amounts in thousands, except share data)

	June 30, 2016	June 30, 2015
Assets		
Current assets:		
Cash and cash equivalents	\$537	\$4,217
Marketable securities	2,495	
Accounts receivable (net of allowance for doubtful accounts of \$20 at June 30, 2016 and 2015)	307	838
Prepaid expenses	226	483
Other receivables	114	661
Other current assets	110	
Current assets of discontinued operations	39	3,431
Total current assets	3,828	9,630
Restricted cash	440	695
Property & equipment, net	1,414	2,334
Intangible assets, net	5,339	18,683
Goodwill	11,270	24,722
Other assets	748	270
Non-current assets of discontinued operations		13,895
Total assets	\$23,039	\$70,229
Liabilities, convertible redeemable preferred stock and stockholders (deficit) equity		
Current liabilities:		
Accounts payable and accrued expenses	\$11,625	\$10,040
Deferred revenue	637	593
Current portion of loans payable	8,996	1,575
Current liabilities of discontinued operations	2,851	13,278
Total current liabilities	24,109	25,486
Loans payable, less current portion	19,716	22,516
Deferred revenue	3,429	3,854
Common stock warrant liability	10	10
Other long-term liabilities	951	1,678
Non-current liabilities of discontinued operations		538
Total liabilities	48,215	54,082
Series A Convertible Redeemable Preferred Stock, \$1,000 stated value, authorized 100,000 shares, issued and outstanding -0- shares as of June 30, 2016 and 2015		
Series C Convertible Redeemable Preferred Stock, \$1,000 stated value,	4,940	11,815

authorized 100,000 shares, issued and outstanding of 3,000 and 10,000 shares
as of June 30, 2016 and 2015, respectively

Commitments and contingencies

Stockholders' (deficit) equity:

Series B Convertible Preferred Stock, \$1,000 stated value, authorized 50,000
shares, issued and outstanding -0- shares as of June 30, 2016 and 2015

Series D Convertible Preferred Stock, \$1,000 stated value, authorized 150
shares, issued and outstanding -0- shares as of June 30, 2016 and 2015

Common stock, \$0.001 par value: authorized 15,000,000 shares, issued and
outstanding 3,023,753 and 1,169,156 shares as of June 30, 2016 and 2015,
respectively

	3	1
Additional paid-in-capital	409,765	383,607
Treasury stock, 10,758 shares at June 30, 2016 and 2015	(11,916)	(11,916)
Accumulated deficit	(428,380)	(367,360)
Accumulated other comprehensive loss	(361)	
Non-controlling interest	773	
Total stockholders' (deficit) equity	(30,116)	4,332
Total liabilities, convertible redeemable preferred stock and stockholders (deficit)	\$23,039	\$70,229

equity

See accompanying Notes to Consolidated Financial Statements

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TABLE OF CONTENTS**Function(x) Inc.****CONSOLIDATED STATEMENTS OF OPERATIONS**
(amounts in thousands, except share and per share data)

	Year Ended June 30,	
	2016	2015
Revenues	\$4,509	\$5,674
Selling, general and administrative expenses	(29,324)	(47,072)
Impairment loss (see Note 8)	(28,541)	(2,085)
Operating loss	(53,356)	(43,483)
Other income (expense):		
Other income, net	(23)	6
Interest expense, net	(3,788)	(2,050)
Total other expense, net	(3,811)	(2,044)
Net loss before provision for income taxes	(57,167)	(45,527)
Income tax expense		
Net loss from continuing operations	(57,167)	(45,527)
Net loss from discontinued operations, net of tax	(6,522)	(33,012)
Net loss	(63,689)	(78,539)
Accretion of Convertible Redeemable Preferred Stock	280	135
Undeclared Series C Convertible Redeemable Preferred Stock Dividend	(1,156)	(468)
Add: Net loss attributable to non-controlling interest	\$1,826	\$
Net loss attributable to common stockholders	\$(62,739)	\$(78,872)
Net loss per common stock basic and diluted:		
Continuing operations	\$(33.03)	\$(54.78)
Discontinued operations	\$(3.83)	\$(39.44)
Net loss per common stock attributable to common stockholders basic and diluted	\$(36.86)	\$(94.22)
Weighted average common stock outstanding basic and diluted	1,702,080	837,093
See accompanying Notes to Consolidated Financial Statements		

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Function(x) Inc.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(amounts in thousands)

	Year Ended June 30,	
	2016	2015
Net loss	\$ (63,689)	\$ (78,539)
Other comprehensive income, net of tax		
Unrealized loss on available for sale securities	(361)	
Other comprehensive loss	(361)	
Comprehensive loss	\$ (64,050)	\$ (78,539)
See accompanying Notes to Consolidated Financial Statements		

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TABLE OF CONTENTS**Function(x) Inc.**

CONSOLIDATED STATEMENTS OF STOCKHOLDERS (DEFICIT) EQUITY (amounts in thousands)

	Common Stock	Class D Preferred Stock	Additional Paid-In Capital	Treasury Stock	Accumulated Other Comprehensive Loss	Accumulated Deficit	Non- Controlling Interest	Total
Balance June 30, 2014	\$1	\$	\$340,178	\$(11,556)	\$	\$(288,821)	\$	\$39,802
Net loss						(78,539)		(78,539)
Purchase of common stock from former officer				(360)				(360)
Accretion of Series C Convertible Redeemable Preferred Stock			135					135
Undeclared Series C Preferred Stock Dividend			(468)					(468)
Common stock offerings			12,459					12,459
Common stock issued for services			208					208
Common stock issued in settlement of Blue Spike litigation			139					139
Share based compensation in connection with Securities Purchase Agreement			2,657					2,657
Restricted stock share based compensation			24,649					24,649
Employee stock options share based compensation			3,650					3,650
Balance June 30, 2015	\$1	\$	\$383,607	\$(11,916)	\$	\$(367,360)	\$	\$4,332
Net loss						(61,863)	\$(1,826)	(63,689)
Unrealized loss on marketable securities					(361)			(361)
Common stock issued for DraftDay acquisition			1,755				610	2,365
Common stock and warrants of Draftday issued for management service							1,733	1,733

contracts								
Series A investment into DDGG						256		256
Series D issuance	110							110
Series D conversion to common stock	(110)	110						
Common stock issued for MGT debt conversion		797						797
Conversion of Sillerman debt to common stock	1	4,111						4,112
Common stock issued for Kuusamo debt conversion		71						71
Common stock issued to Coda search debt conversion		5						5
Common stock purchased PP Reaz Islam		200						200
Accretion of Series C Convertible Redeemable Preferred Stock		280						280
Undeclared Series C Preferred Stock Dividend		(1,156)						(1,156)
Series C conversion to common	1	7,750						7,751
Interest income on note receivable from shareholders		2						2
Other matter related to Choose Digital RSUs (Note 12)					843			843
Restricted stock share based compensation		11,998						11,998
Employee stock options share based compensation		235						235
Balance June 30, 2016	\$3	\$	\$409,765	\$(11,916)	\$(361)	\$(428,380)	\$773	\$(30,116)
See accompanying Notes to Consolidated Financial Statements								

TABLE OF CONTENTS**Function(x) Inc.****CONSOLIDATED STATEMENTS OF CASH FLOWS
(amounts in thousands)**

	Year Ended June 30,	
	2016	2015
Operating activities:		
Net loss	\$ (63,689)	\$ (78,539)
Adjustments to reconcile net loss to net cash used in operating activities:		
Restricted stock based compensation	11,998	24,649
Employee stock options share based compensation	235	3,650
Share based compensation in connection with securities purchase agreement		4,140
Write-off of certain intangible assets related to Choose Digital		2,086
Stock issued for services		208
Stock issued in settlement of litigation		139
Gain on sale of a business	(1,262)	
Gain on settlement of accounts payable	(2,132)	
Fair value loss in financial assets	376	
Loss on abandonment of assets	173	
Loss on settlement of receivables	549	
Impairment loss	28,541	
Decrease in fair value of common stock warrants		(5)
Increase in fair value of contingent consideration related to acquisitions		2,222
Accretion of note discount	200	115
Depreciation and amortization	3,748	6,040
Interest income on notes receivable from shareholders and officer	(2)	
Changes in operating assets and liabilities:		
Marketable securities	(148)	
Accounts receivable	3,299	(157)
Other receivables	547	(581)
Prepaid expenses	2,065	316
Other assets	319	41
Deferred revenue	(381)	(818)
Points liability	(64)	4,102
Accounts payable and accrued expenses	6,213	1,737
Other liabilities	(180)	(40)
Net cash used in operating activities	(9,595)	(30,695)
Investing activities:		
Purchase of property and equipment		(113)
Capitalized software costs		(1,051)
Net cash used in investing activities		(1,164)
See accompanying Notes to Consolidated Financial Statements		

TABLE OF CONTENTS**Function(x) Inc.**

CONSOLIDATED STATEMENTS OF CASH FLOWS (continued) **(amounts in thousands)**

	Year Ended June 30,	
	2016	2015
Financing activities:		
Issuance of common stock and warrants for cash	\$ 200	\$ 12,459
Proceeds from loans	11,535	35,975
Repayments on loans	(3,000)	(27,000)
Sale of Class C Convertible Redeemable Preferred Stock		10,000
Purchase of common stock from former officer		(360)
Restricted cash		4,995
Payments related to contingent consideration	(2,570)	
Repayment on notes payable	(250)	
Net cash provided by financing activities	5,915	36,069
Net change in cash	(3,680)	4,210
Cash at beginning of period	4,217	7
Cash at end of period	\$ 537	\$ 4,217
Supplemental cash flow information:		
Cash paid during the year for interest	\$ 110	\$ 999
Landlord lease incentive build-out allowance	\$	\$ 449
Common stock and warrants issued for DraftDay acquisition	\$ 1,755	\$
DDGG common stock and warrants issued for DraftDay acquisition	\$ 610	\$
Notes issued for DraftDay acquisition	\$ 2,250	\$
Common stock and warrants issued for management service contracts	\$ 2,111	\$
Common stock issued for partially settled notes related to DraftDay acquisition	\$ 868	\$
Preferred Series D shares issued to partially settle notes related to DraftDay acquisition	\$ 110	\$
Settlement of Perk Loan in common stock	\$ 1,000	\$
Loans converted to common stock	\$ 4,117	\$
Preferred Series C shares converted to common stock	\$ 7,751	\$
Reversal of Choose Digital RSU liability (Note 12)	\$ 843	\$
See accompanying Notes to Consolidated Financial Statements		

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Function(x) Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (amounts in thousands, except share and per share data)

1. Basis of Presentation and Consolidation

On January 27, 2016, Function(x) Inc. (Function(x) and/or the Company) changed its name from Viggie Inc. to DraftDay Fantasy Sports, Inc. (DraftDay), and changed its ticker symbol from VGGL to DDAY. On June 10, 2016, the Company changed its name from DraftDay Fantasy Sports, Inc. to Function(x) Inc., and changed its ticker symbol from DDAY to FNCX. It now conducts business under the name Function(x) Inc. The Consolidated Financial Statements include the accounts of the Company and its wholly-owned subsidiaries. The Company has nine wholly-owned subsidiaries, Function(x) Inc., Project Oda, Inc., Sports Hero Inc., Loyalize Inc., Viggie Media Inc., VX Acquisition Corp., Nextguide Inc., Wetpaint.com, Inc. (Wetpaint), and Choose Digital Inc. (Choose Digital), each a Delaware corporation. The Company also owns approximately 49% of the issued and outstanding common stock of DDGG, and also appoints a majority of the members of its Board of Directors. All significant intercompany accounts and transactions have been eliminated in consolidation.

On September 8, 2015, the Company and its newly created subsidiary DraftDay Gaming Group, Inc. (DDGG) entered into an Asset Purchase Agreement (the Asset Purchase Agreement) with MGT Capital Investments, Inc. (MGT Capital) and MGT Sports, Inc. (MGT Sports), pursuant to which the Company acquired all of the assets of the DraftDay.com business (the DraftDay Business or DraftDay.com) from MGT Capital and MGT Sports.

On February 8, 2016, the Company completed the sale of assets related to the Company's rewards business, including the Viggie App, in accordance with the Asset Purchase Agreement (the Perk Agreement) with Perk.com, Inc. (Perk) entered into on December 13, 2015. Management entered into this binding sales agreement following a strategic decision to divest the operations related to the Viggie App and place greater focus on its remaining businesses. The assets, liabilities and operations related to Loyalize Inc., and Nextguide Inc. (as well as the portion of the assets relating to the Company's discontinued rewards business within the Company) have been classified as discontinued operations in the accompanying consolidated financial statements for all periods presented. In accordance with Accounting Standards Codification (ASC) No. 205, *Presentation of Financial Statements*, the inter-segment revenues and expenses related to services provided by Choose Digital to the Viggie rewards business (discontinued operations) are presented at cost in the Consolidated Statements of Operations.

In December 2015, as a result of the sale of certain assets to Perk and acquisition of the DraftDay Business, we reorganized the organizational management and oversight of the Company into three segments (see Note 4, Segments). Accordingly, prior period financial information has been recast to confirm to the current period presentation. These changes impacted Note 4: Segments and Note 3: Summary of Significant Accounting Policies, with no impact on consolidated net loss or cash flows in any period.

On July 12, 2016, the Company and RACX Inc., a Delaware corporation and wholly-owned subsidiary of the Company (RACX), completed an acquisition pursuant to an Asset Purchase Agreement (the Asset Purchase

Agreement) with Rant, Inc., a Delaware corporation, pursuant to which RACX has acquired the assets of Rant (the Asset Purchase) used in the operation of Rant's Rant.com independent media network and related businesses (the Rant Assets). We acquired assets of Rant for \$2,000 in assumed liabilities, a \$3,000 note, and 4,435 shares of Function(x) Inc. Series E Convertible Preferred Stock which, upon satisfaction of certain conditions including shareholder approval, will be convertible into shares of our common stock equal to 22% of the fully diluted shares outstanding, in a move to become a market leader in social publishing.

On September 16, 2016, the Company amended its Certificate of Incorporation to effect a reverse stock split of all issued and outstanding shares of common stock at a ratio of 1 for 20 (the Reverse Stock Split). Owners of fractional shares outstanding after the Reverse Stock Split will be paid cash for such fractional interests. The effective date of the Reverse Stock Split is September 16, 2016. All common stock share amounts disclosed in these financial statements have been adjusted to reflect the Reverse Stock Split.

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Function(x) Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (amounts in thousands, except share and per share data)

1. Basis of Presentation and Consolidation - (continued)

Going Concern

These consolidated financial statements have been prepared on a going concern basis which assumes the Company's ability to continue to realize its assets and discharge its liabilities in the normal course of business. The Company is unlikely to generate significant revenue or earnings in the immediate or foreseeable future. The continuation of the Company as a going concern is dependent upon the continued financial support from its stockholders, the ability of the Company to obtain necessary equity or debt financing to continue development of its business and to generate revenue. Management intends to raise additional funds through equity and/or debt offerings until sustainable revenues are developed. There is no assurance such equity and/or debt offerings will be successful and therefore there is substantial doubt about the Company's ability to continue as a going concern within one year after the financial statements are issued. The accompanying consolidated financial statements do not include any adjustments that might result from the outcome of these uncertainties.

2. Line of Business

The Company conducts business through three operating segments: Wetpaint, Choose Digital and DDGG. These operating segments are described below.

Through Wetpaint, the Company reports original news stories and publishes information content covering top television shows, music, celebrities, entertainment news and fashion. Wetpaint publishes more than 55 new articles, videos and galleries each day. The Company generates revenues through wetpaint.com by displaying advertisements to wetpaint.com users as they view its content.

Choose Digital is a white-label digital marketplace featuring a recent and wide range of digital content, including music, movies, TV shows, eBooks and audiobooks. The content is sourced from the world's leading record companies and book publishers and an aggregator of movie and TV content. Choose Digital generates revenues when participants in Choose Digital's clients' loyalty programs redeem loyalty credits for digital content provided by Choose Digital. For example, if a participant in a loyalty program redeems credits for a song download provided by Choose Digital, the client loyalty program pays Choose Digital for the download.

The Company's wholly owned subsidiary, DDGG, made a recent investment in the DraftDay.com platform. Through DraftDay.com, users can draft a fantasy sports team within a salary cap, follow game action and reap rewards. DraftDay.com will continue to offer high-quality entertainment to consumers as well as to businesses desiring turnkey solutions to new revenue streams. See Note 6, Acquisitions, for further details on this acquisition.

3. Summary of Significant Accounting Policies

Cash and Cash Equivalents and Restricted Cash

The Company considers all highly liquid securities purchased with original maturities of 90 days or less to be cash equivalents. Cash equivalents are stated at cost which approximates market value and primarily consists of money market funds that are readily convertible into cash. Restricted cash comprises amounts held in deposit that were required as collateral under the lease of office space and security interest held by Deutsche Bank Trust Company Americas in connection with the Company's debt agreement more fully described in Note 9, Loans Payable.

Marketable Securities

In February 2016, the Company received 1,370,000 shares of Perk's stock, which is publicly traded on the Toronto Stock Exchange, as part of the consideration in the sale of assets described in the Perk Agreement. These securities are short-term marketable securities, and have been classified as available-for-sale

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Function(x) Inc.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(amounts in thousands, except share and per share
data)**

3. Summary of Significant Accounting Policies - (continued)

securities. Pursuant to ASC 320-10, *Investments - Debt and Equity Securities* the Company's marketable securities are marked to market on a quarterly basis, with unrealized gains and losses recorded in equity as Other Comprehensive Income/Loss.

Accounts Receivable

Accounts receivable are recorded net of an allowance for doubtful accounts. The Company's allowance for doubtful accounts is based upon historical loss patterns, the number of days that the billings are past due and an evaluation of the potential risk associated with delinquent accounts. The Company also considers any changes to the financial condition of its customers and any other external market factors that could impact the collectability of its receivables in the determination of its allowance for doubtful accounts.

Concentration of Credit Risk

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of cash and cash equivalents and trade accounts receivable. The Company maintains cash and cash equivalents with domestic financial institutions of high credit quality. The Company performs periodic evaluations of the relative credit standing of all of such institutions.

The Company performs ongoing credit evaluations of customers to assess the probability of accounts receivable collection based on a number of factors, including past transaction experience with the customer, evaluation of their credit history, and review of the invoicing terms of the contract. The Company generally does not require collateral. The Company maintains reserves for potential credit losses on customer accounts when deemed necessary. Actual credit losses during the years ended June 30, 2016 and June 30, 2015 were \$549 and \$0, respectively.

Fair Value of Financial Instruments

The carrying amounts reported in the Consolidated Balance Sheets for cash and cash equivalents, accounts and other receivables, accounts payable and accrued liabilities approximate fair value because of the immediate or short-term maturity of these financial instruments. The carrying amount of Perk marketable securities held is marked-to-market on a quarterly basis using the closing day share price of the last business day of the quarter. The changes to fair value are recorded in Other Comprehensive Income/Loss. The carrying amount of Perk warrants held is marked-to-market on a quarterly basis using the Monte Carlo valuation model. The changes to fair value are recorded in the Consolidated Statement of Operations. The carrying amount of loans payable approximates fair value as current

borrowing rates for the same, or similar issues, are the same as those that were given to the Company at the issuance of these loans.

Property and Equipment

Property and equipment (consisting primarily of computers, software, furniture and fixtures, and leasehold improvements) is recorded at historical cost and is depreciated using the straight-line method over their estimated useful lives. The useful life and depreciation method are reviewed periodically to ensure they are consistent with the anticipated pattern of future economic benefits. Expenditures for maintenance and repairs are charged to operations as incurred, while betterments are capitalized. Gains and losses on disposals are included in the results of operations. The estimated useful lives of the Company's property and equipment is as follows: computer equipment and software: 3 years; furniture and fixtures: 4 years; and leasehold improvements: the lesser of the lease term or life of the asset.

Business Combinations and Goodwill

Business combinations are accounted for using the acquisition method of accounting. The Company allocates the purchase price of acquired companies to the identifiable assets acquired, liabilities assumed and any non-controlling interest based on their acquisition date estimated fair values. Goodwill as of the acquisition

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3. Summary of Significant Accounting Policies - (continued)

date is measured as the excess of consideration transferred and the net of the acquisition date fair values of the identifiable assets acquired and liabilities assumed. Any contingent consideration to be transferred to the acquiree is recognized at fair value at the acquisition date.

Determining the fair value of assets acquired and liabilities assumed requires the Company to make significant estimates and assumptions, including assumptions related to future cash flows, discount rates, asset lives and the probability of future cash pay-outs related to contingent consideration. The estimates of fair value are based upon assumptions believed to be reasonable by management, but are inherently uncertain and unpredictable and, therefore, actual results may differ from estimates. As a result, during the measurement period, which may be up to one year from the acquisition date, the Company may record adjustments to the fair value of assets acquired and liabilities assumed, with the corresponding offset to goodwill. Upon the conclusion of the measurement period or final determination of the fair value of assets acquired or liabilities assumed, whichever comes first, any subsequent adjustments are recorded to the Consolidated Statements of Operations.

For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Company's reporting units that are expected to benefit from the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units. Where goodwill has been allocated to a reporting unit and part of the operation within that unit is disposed of, the goodwill associated with the disposed operation is included in the carrying amount of the operation when determining the gain or loss on disposal. Goodwill disposed in these circumstances is measured based on the relative values of the disposed operation and the portion of the reporting units retained.

As required by Accounting Standards Codification (ASC) 350, *Goodwill and Other Intangible Assets*, the Company tests goodwill for impairment during the fourth quarter of its fiscal year. Goodwill is not amortized, but instead tested for impairment at the reporting unit level at least annually and more frequently upon occurrence of certain events. As noted above, the Company has three reporting units. The annual goodwill impairment test is a two step process. First, the Company determines if the carrying value of its reporting unit exceeds fair value, which would indicate that goodwill may be impaired. If the Company then determines that goodwill may be impaired, it compares the implied fair value of the goodwill to its carrying amount to determine if there is an impairment loss.

Historically, the Company had one reporting unit. However, in connection with the sale of a significant portion of the Company's assets (see Note 1, Basis of Presentation and Consolidation), the remaining operations were divided into 3 reporting units (see Note 4, Segments). The Company engaged a third-party valuation firm to test the Choose Digital and Wetpaint reporting units for goodwill impairment. The DDGG reporting unit was not tested for impairment at December 31, 2015 as the acquisition of this entity occurred in September 2015. The Company determined that the

fair value of both of the Wetpaint and Choose Digital reporting units were significantly below their respective carrying values, indicating that goodwill related to these reporting units may be impaired. The Company determined the fair value of all long-lived assets other than goodwill related to each reporting unit and calculated the residual goodwill value for each. Upon comparing the residual goodwill values to the respective carrying values, the Company determined that there was an impairment loss on both the Choose Digital and Wetpaint reporting units. As a result, the Company recorded an impairment loss of \$4,335 related to the Choose Digital reporting unit and \$10,708 related to the Wetpaint reporting unit in the Selling, general and administrative expense line of the Consolidated Statements of Operations during the six months ended December 31, 2015. Upon the finalization of the December 31, 2015 Choose Digital and Wetpaint goodwill impairment analysis, the consolidated goodwill ending balances as of March 31, 2016 were adjusted by \$3,350 at June 30, 2016. The Company also recorded an additional goodwill impairment loss of \$1,672 in the Selling, general and administrative expense line and reduced the gain on the sale of the Viggie Business by \$1,672 in the Consolidated Statement of Operations during the nine months ended March 31, 2016 as a result of the finalization of the December 2015 Choose Digital and

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3. Summary of Significant Accounting Policies - (continued)

Wetpaint impairment analysis. There were no other impairments of goodwill related to the Choose Digital or Wetpaint reporting units recorded during the year ended June 30, 2016.

At June 30, 2016, the Company determined that the fair value of the DDGG reporting unit was significantly below its carrying value, indicating that goodwill may be impaired. The Company determined the fair value of all long-lived assets other than goodwill and calculated the residual goodwill for the reporting unit. The residual goodwill was higher than the carrying value of goodwill related to the DDGG reporting unit, therefore the Company did not record an impairment loss for DDGG goodwill during the year ended June 30, 2016.

There were no impairments to goodwill recorded during the year ended June 30, 2015.

Other Long-Lived Assets

The Company accounts for the impairment of long-lived assets other than goodwill in accordance with ASC 360, *Property, Plant, and Equipment* (ASC 360), which addresses financial accounting and reporting for the impairment or disposal of long-lived assets. ASC 360 requires impairment losses to be recorded on long-lived assets used in operations when indicators of impairment are present and the undiscounted cash flows estimated to be generated by those assets are less than the assets' carrying amounts. In that event, a loss is recognized based on the amount by which the carrying amount exceeds the fair value of the long-lived assets. Loss on long-lived assets to be disposed of is determined in a similar manner, except that fair values are reduced for the cost of disposal.

At June 30, 2015, the Company determined that certain intangible assets related to the acquisition of Choose Digital were impaired. Due to a shift in the Company's business operations and utilization of its resources, during the fourth quarter of fiscal 2015, the Company determined that intangible assets related to customer relationships and trade name no longer had value. Therefore, such assets were written off as of June 30, 2015. The total amount of the write off was \$2,085 and is included in selling, general and administrative costs in the accompanying Consolidated Statements of Operations. There were no other impairments of long-lived assets during the year ended June 30, 2015.

At December 31, 2015, as described above, the Company determined that the fair value of the Choose Digital and Wetpaint reporting units tested was significantly below the respective carrying values and assessed the fair values of the long-lived assets other than goodwill for each reporting unit. Upon comparing the fair values of the long-lived assets to their respective carrying values, the Company recorded a loss of \$1,331 on intangible assets related to Choose Digital's software and licenses, and a loss of \$11,418 on intangible assets related to Wetpaint's technology, trademark, customer relationships and non-competition agreements, during the three months ended December 31, 2015. There were no other impairments of long-lived assets related to the Choose Digital or Wetpaint reporting units

during the year ended June 30, 2016.

At June 30, 2016, the Company determined that certain intangible assets related to the acquisition of Draftday.com were impaired. At June 30, 2016, DDGG's Management Services Agreement By and Between DraftDay Gaming Group, Inc. and Sportech Racing, LLC (Sportech MSA) terminated, which led to a significantly lower revenues forecast for the reporting unit. As a result, the Company determined that the intangible assets related to internally developed software, trade name and non-compete agreements were impaired. The Company recorded a loss of \$749 on intangible assets related to DDGG during the year ended June 30, 2016.

Capitalized Software

The Company records amortization of acquired software on a straight-line basis over the estimated useful life of the software.

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3. Summary of Significant Accounting Policies - (continued)

In addition, the Company records and capitalizes internally generated computer software and, appropriately, certain internal costs have been capitalized in the amounts of \$1,498 and \$1,610 as of June 30, 2016 and June 30, 2015, respectively, in accordance with ASC 350-40, *Internal-use Software*. Once software is placed into service, the Company records amortization on a straight-line basis over the estimated useful life of the software. The change in capitalized software is due to impairment of long-term assets related to Choose Digital and Wetpaint businesses described earlier, as well as the abandonment of certain technology as of January 1, 2016, and internal development costs.

DDGG Player Deposits

The Company maintains a separate bank account to hold player deposits in accordance with current industry regulations. The player deposits bank account represents money reserved for player withdrawals and winnings. Accordingly, the Company records an offsetting liability at the time of receipt of player deposits.

Deferred Rent

The Company currently leases office space for its corporate office, and as part of the lease agreement the landlord provided a rent abatement for the first 10 months of the lease. In 2014, the Company entered into two lease agreements for its satellite offices which provided for tenant improvement work sponsored by the landlords. The abatement and landlord sponsored improvements have been accounted for as a reduction of rental expense over the life of the lease. The Company accounts for rental expense on a straight line basis over the entire term of the lease. Deferred rent is equal to the cumulative timing difference between actual rent payments and recognized rental expense. The satellite office leases were terminated in Fiscal 2016. The Company wrote-off residual leasehold improvement and deferred rent balances related to landlord sponsored tenant improvement work, and recorded a write-off of \$83 in the Consolidated Statements of Operations for the year ended June 30, 2016.

Revenue Recognition

The Company recognizes revenue when: (1) persuasive evidence exists of an arrangement with the customer reflecting the terms and conditions under which products or services will be provided; (2) delivery has occurred or services have been provided; (3) the fee is fixed or determinable; and (4) collection is reasonably assured. For all revenue transactions, the Company considers a signed agreement, a binding insertion order or other similar documentation to be persuasive evidence of an arrangement.

Advertising Revenue: the Company generates advertising revenue primarily from third-party advertising via real-time bidding, which is typically sold on a per impression basis.

Deferred Revenue: deferred revenue consists principally of prepaid but unrecognized revenue. Deferred revenue is recognized as revenue when the services are provided and all other revenue recognition criteria have been met.

Barter Revenue: barter transactions represent the exchange of advertising or programming for advertising, merchandise or services. Barter transactions which exchange advertising for advertising are accounted for in accordance with Emerging Issues Task Force Issue No. 99-17 *Accounting for Advertising Barter Transactions* (ASC Topic 605-20-25). Such transactions are recorded at the fair value of the advertising provided based on the Company's own historical practice of receiving cash for similar advertising from buyers unrelated to the counter party in the barter transactions. Barter transactions which exchange advertising or programming for merchandise or services are recorded at the monetary value of the revenue expected to be realized from the ultimate disposition of merchandise or services.

The Company recognized barter revenue and barter expense for the year ended June 30, 2016 of \$428 and \$428, respectively.

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3. Summary of Significant Accounting Policies - (continued)

The Company recognized barter revenue and barter expense for the year ended June 30, 2015 of \$437 and \$437, respectively.

Stock-Based Compensation

The Company accounts for stock-based compensation in accordance with ASC 718, *Compensation - Stock Compensation* (ASC 718). Under the fair value recognition provisions of ASC 718, stock-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as expense ratably over the requisite service period. The Company uses the Black-Scholes option pricing model to determine the fair value of stock options and warrants issued. Stock-based awards issued to date are comprised of both restricted stock awards (RSUs) and employee stock options.

Marketing

Marketing costs are expensed as incurred. Marketing expense for the years ended June 30, 2016 and June 30, 2015 was \$603 and \$528, respectively, including barter expense.

Income Taxes

The Company uses the liability method of accounting for income taxes as set forth in ASC 740, *Income Taxes* (ASC 740). Under the liability method, deferred taxes are determined based on the temporary differences between the financial statement and tax basis of assets and liabilities using tax rates expected to be in effect during the years in which the basis differences reverse. A valuation allowance is recorded when it is unlikely that the deferred tax assets will not be realized. The Company assesses its income tax positions and record tax benefits for all years subject to examination based upon the Company's evaluation of the facts, circumstances and information available at the reporting date. In accordance with ASC 740-10, for those tax positions where there is a greater than 50% likelihood that a tax benefit will be sustained, the Company's policy will be to record the largest amount of tax benefit that is more likely than not to be realized upon ultimate settlement with a taxing authority that has full knowledge of all relevant information. For those income tax positions where there is less than 50% likelihood that a tax benefit will be sustained, no tax benefit will be recognized in the financial statements.

Comprehensive Loss

In accordance with ASC 220, *Comprehensive Income*, the Company reports by major components and as a single total, the change in its net assets during the period from non-owner sources. Comprehensive income consists of net income (loss), accumulated other comprehensive income (loss), which includes certain changes in equity that are excluded from net income (loss). The Company's comprehensive loss for all periods presented is related to the effect of an unrealized loss on available for sale marketable securities.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States 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 expenses during the reporting period. These estimates include, among others, fair value of financial assets and liabilities, net realizable values on long-lived assets, certain accrued expense accounts, and estimates related to stock-based compensation. Actual results could differ from those estimates.

Recently Issued Accounting Pronouncements

In May 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update 2016-12, Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients (ASU 2016-12). The amendments in this update affect the guidance in Accounting Standards

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3. Summary of Significant Accounting Policies - (continued)

Update 2014-09, Revenue from Contracts with Customers (Topic 606) (ASU 2014-09), which is not yet effective. This update focuses on improving several aspects of ASU 2014-09, such as assessing the collectability criterion in paragraph 606-10-25-1(e) and accounting for contracts that do not meet the criteria for step 1; presentation of sales taxes and other similar taxes collected from customers; noncash consideration; contract modifications at transition; and completed contracts at transition. The Company does not expect the standard to have a material impact on its consolidated financial statements.

In April 2016, the FASB issued Accounting Standards Update 2016-10, Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing (ASU 2016-10). The amendments in this update affect the guidance in ASU 2014-09, which is not yet effective. This update focuses on clarifying the following two aspects of ASU 2014-09: identifying performance obligations and the licensing implementation guidance, while retaining the related principles for those areas. The Company does not expect the standard to have a material impact on its consolidated financial statements.

In March 2016, FASB issued Accounting Standards Update No. 2016-09, Compensation – Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting (ASU 2016-09). This update is intended to improve the accounting for employee share-based payments and affects all organizations that issue share-based payment awards to their employees. Several aspects of the accounting for share-based payment award transactions are simplified, including: (a) income tax consequences; (b) classification of awards as either equity or liabilities; and (c) classification on the statement of cash flows. ASU 2016-09 is effective for financial statements issued for annual periods beginning after December 15, 2016. The Company is currently in the process of evaluating the impact of adoption of ASU 2016-09 on its financial statements.

In February 2016, FASB issued Accounting Standards Update No. 2016-02, Leases (ASU 2016-02). ASU 2016-02 requires lessees to recognize the following for all leases (with the exception of short-term leases) at the commencement date: a lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis; and a right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. Under the new guidance, lessor accounting is largely unchanged. Certain targeted improvements were made to align, where necessary, lessor accounting with the lessee accounting model and Topic 606, Revenue from Contracts with Customers. The new lease guidance also simplified the accounting for sale and leaseback transactions primarily because lessees must recognize lease assets and lease liabilities. Lessees will no longer be provided with a source of off-balance sheet financing. Lessees (for capital and operating leases) and lessors (for sales-type, direct financing, and operating leases) must apply a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. The modified retrospective approach would not require any transition

accounting for leases that expired before the earliest comparative period presented. Lessees and lessors may not apply a full retrospective transition approach. ASU 2016-02 is effective for financial statements issued for annual periods beginning after December 15, 2018. The Company is currently in the process of evaluating the impact of adoption of ASU 2016-02 on its financial statements.

In January 2016, FASB issued Accounting Standards Update No. 2016-01, Financial Instruments- Overall: Recognition and Measurement of Financial Assets and Financial Liabilities (ASU 2016-01). ASU 2016-01 requires all equity investments to be measured at fair value with changes in the fair value recognized through net income (other than those accounted for under equity method of accounting or those that result in consolidation of the investee). Additionally, it requires an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments. Lastly, the standard eliminates the requirement to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for

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3. Summary of Significant Accounting Policies - (continued)

financial instruments measured at amortized cost on the balance sheet. ASU 2016-01 is effective for financial statements issued for annual periods beginning after December 15, 2017, and interim periods within those annual periods. The Company does not expect the standard to have a material impact on its consolidated financial statements.

In November 2015, FASB issued Accounting Standards Update No. 2015-17, *Income taxes: Balance Sheet Classification of Deferred Taxes* Business (ASU 2015-17). Topic 740, *Income Taxes*, requires an entity to separate deferred income tax liabilities and assets into current and noncurrent amounts in a classified statement of financial position. Deferred tax liabilities and assets are classified as current or noncurrent based on the classification of the related asset or liability for financial reporting. Deferred tax liabilities and assets that are not related to an asset or liability for financial reporting are classified according to the expected reversal date of the temporary difference. To simplify the presentation of deferred income taxes, ASU 2015-17 requires that deferred income tax liabilities and assets be classified as noncurrent in a classified statement of financial position. ASU 2015-17 is effective for financial statements issued for annual periods beginning after December 15, 2016, and interim periods within those annual periods. The Company does not expect the standard to have a material impact on its consolidated financial statements.

In September 2015, the FASB issued Accounting Standard Update No. 2015-16, *Business Combinations - Simplifying the Accounting for Measurement-Period Adjustments* (ASU 2015-16). This standard requires that an acquirer retrospectively adjust provisional amounts recognized in a business combination, during the measurement period. To simplify the accounting for adjustments made to provisional amounts, the amendments in the ASU 2015-16 require that the acquirer recognize adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amount is determined. The acquirer is required to also record, in the same period's financial statements, the effect on earnings of changes in depreciation, amortization, or other income effects, if any, as a result of the change to the provisional amounts, calculated as if the accounting had been completed at the acquisition date. In addition an entity is required to present separately on the face of the income statement or disclose in the notes to the financial statements the portion of the amount recorded in current-period earnings by line item that would have been recorded in previous reporting periods if the adjustment to the provisional amounts had been recognized as of the acquisition date. ASU 2015-16 is effective for fiscal years beginning after December 15, 2016, and interim periods within fiscal years beginning after December 15, 2017 (July 1, 2017 for the Company). The Company does not believe that the adoption of ASU 2015-16 will have a material impact on its consolidated financial statements.

4. Segments

Historically, the Company had one operating segment. However, in connection with the sale of the Viggie rewards business (discontinued operations) to Perk in February 2016, which represents a significant portion of the Company's

assets and revenues, the Company's remaining operations were divided into three operating segments. These segments offer different products and services are separately reviewed in internal management reports, and managed separately.

Wetpaint: a media channel reporting original news stories and publishing information content covering top television shows, music, celebrities, entertainment news and fashion.

Choose Digital: a business-to-business platform for delivering digital content.

DDGG: a business-to-business operator of daily fantasy sports.

The accounting policies followed by the segments are described in Note 3, Summary of Significant Accounting Policies. The operating segments of the Company include the assets, liabilities, revenues and expenses that management has determined are specifically or primarily identifiable to each segment, as well as

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direct and indirect costs that are attributable to the operations of each segment. Direct costs are the operational costs that are administered by the Company following the shared services concept. Indirect costs are the costs of support functions that are provided on a centralized or geographic basis by the Company, which include, but are not limited to, finance, human resources, benefits administration, procurement support, information technology, legal, corporate strategy, corporate governance and other professional services and general commercial support functions.

Central support costs have been allocated to each operating segment based on a specific identification basis or, when specific identification is not practicable, a proportional cost allocation method (primarily based on net sales or direct payroll costs), depending on the nature of the services received. Management considers that such allocations have been made on a reasonable basis, but may not necessarily be indicative of the costs that would have been incurred if the operating segments had been operated on a stand-alone basis for the periods presented.

Information regarding the results of each reportable segment is included below. Performance is measured based on unit profit after tax, as included in the internal management reports that are reviewed by the Chief Operating Decision Maker, who is the Company's Chief Executive Officer. Business unit profit is used to measure performance as management believes that such information is the most relevant in evaluating the success of each business and determining the going forward strategy for the Company as a whole.

Information about reportable segments:

<i>In thousands of U.S. dollars</i>	For The Year Ended June 30,						
	Wetpaint		Choose Digital		DDGG	Total	
	2016	2015	2016	2015	2016	2016	2015
External revenues	\$1,533	\$3,454	\$664	\$848	\$528	\$2,725	\$4,302
Inter-segment revenues ⁽¹⁾			1,285	855		1,285	855
Net loss, net of income taxes ⁽²⁾	(27,560)	(8,747)	(7,621)	(6,744)	(5,194)	(40,375)	(15,491)

Notes: