CLEARSTAR®

Annual Report and Accounts 2016

CLEARSTAR®

CLEARSTAR®

Your Background Screening Company

Innovative, Flexible Background Screening Technology and Services Backed by Years of Industry Experience and Solution-Focused Client Service

Your Drug Screening Company

Streamlined, Paperless Drug Test Ordering and CCF Available for Mobile Wallets with Results Professionally Reviewed by a Full-Time Medical Review Officer

WebCCF

Your Health Screening Company

Online Ordering of Clinical Blood Tests, Doctor-Ordered in All 50 States, Including MMR, Varicella, Hepatitis, QuantiFERON, and Hundreds More

Your Mobile Screening Company

Industry-First Mobile Facial Recognition and ID Validation Paired with a Qualified Labor Address Book for Hiring Labor On-The-Spot and Managing it On-The-Go

CLEARID

SPHERE

Your Global Screening Company

Globally-Native Platform, Global Records Sourced From a World-Class Supplier Network, and Clear Compliance Guidance From Experts You Trust

Your Custom Branding Company

Custom Branding Available for Most ClearStar Solutions, Making it Easy to Harness the Power of ClearStar as Your Own to Grow Your Business Quickly

Your Logo Here

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Directors, Secretary & Advisers

Directors

Bernard "Barney" Quinn
Non-executive Chairman

Robert James Vale Jr.
Chief Executive Officer

David Alexander Pattillo
Chief Financial Officer

Kenneth Wayne Dawson Jr.
Chief Information & Security Officer

Samuel "André" Schnabl
Non-executive Director

Company Secretary

Nicolas Simon Dufour

Registered Office

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Cayman Islands

Principal place of business

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USA

Nominated Adviser & Broker

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United Kingdom

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Legal Advisers – under English Law

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United Kingdom

– under US Law

Eversheds Sutherland (US) LLP
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48 Gracechurch Street
London
EC3V 0EJ
United Kingdom

Financial Summary

- Revenue increased by 3% to $16.0 million (2015: $15.5 million)
- Gross margin maintained at 61.3% (2015: 61.2%)
- General and administrative expenses reduced by 7.8% to $7.5 million (2015: $8.2 million)
- EBITDA improved by $290,000 to a $666,000 loss (2015: $956,000 loss)
- As of 31 December 2016, the Company had net cash of $2.4 million (30 June 2016: $3.1 million; 31 December 2015: $3.9 million)

Operational Summary

Direct Services

- Significant progress in direct services resulting in organic revenue growth of approximately 77% to $1.9 million (2015: $1.1 million)
- Successful in targeting larger, higher-volume direct clients, with particular demand in the transportation industry
- Benefitted from strengthening the direct services sales team and introduction of the new ClearID and ClearContact solutions
- Strong organic growth mitigated the contraction in revenue due to the attrition of clients gained through the SingleSource acquisition, with total Direct Services Division revenues slightly above the previous year at $3.80 million (2015: $3.77 million)

Channel Partner and Consumer Reporting Agencies

- Channel Partner and Consumer Reporting Agency revenue grew by 4% to $12.2 million (2015: $11.7 million) with increased demand for ClearStar's technologically-differentiated suite of products and solutions
- Largest service offering by revenue was medical information services, which accounted for 39% of division sales
- Ongoing improvement to offering, including adding new integration points, product development in areas of data distribution and improvements to user interface

Technology and Product Advancement

- Gained initial traction from the development of its global platform to satisfy interface, compliance and architectural demands outside the US
- The Company's clinical testing service was made available via ClearStar's proprietary WebCCF technology and number of collection sites increased to over 15,000

Post period

- ClearStar was awarded a contract by IntelliCentrics, a global leader in vendor credentialing in the healthcare industry, to provide its medical information services to streamline the drug and titer testing process

Chairman's Statement

Barney Quinn, *Chairman*

21 April 2017

This has been a crucial year for ClearStar: coming on the back of a transformational period last year, we had to demonstrate that we had built upon those foundations. The crucial element was that, in addition to the cost control measures and operational efficiencies introduced in 2015, we entered this year with the right people focused on the right markets. This laid the foundations for a successful 2016.

With the right people in place, our focus this year was on growing direct sales and services – and we had a very successful year with direct revenues increasing organically year-on-year by 77%. This was important because we had planned for attrition of some clients we had inherited from our SingleSource acquisition the year before.

Our Channel Partner and Consumer Reporting Agency revenue also grew with increased demand for ClearStar's technologically-differentiated suite of products and solutions.

Therefore, we were pleased that the strong organic growth mitigated the contraction in revenue due to the attrition of some non-compliant clients and that we could report another year of revenue growth. Importantly, the quality of our revenue also improved as we increased the proportion contributed by larger, higher-volume direct clients.

The story of the year was the growth of the "gig economy". The fluidity of the labour market continued to expand thereby increasing the demand for our direct services and providing new opportunities for revenue generation. We anticipate this being a key growth driver in the coming years. We are also better-placed to target this opportunity thanks to our increased brand recognition – and we plan to continue to expand our sales & marketing efforts to strengthen this recognition.

During the year, we also launched our global platform, Sphere. ClearStar now provides a suite of advanced services, directly and indirectly through our Channel Partner and CRA customers, on a global basis. We believe that we are one of only a limited number of providers of an integrated global solution – and the only company with cross-border data centres that are compliant with US and EU regulations. We plan to leverage this position to grow our global business – both through forming new relationships with channel partners and employers outside of the US as well as through up-selling to our existing client base. Sphere has received good initial client response, strengthening our belief that we can generate meaningful international revenue in 2017.

Finally, I would like to thank all of our staff and shareholders for their ongoing support. With the strengthening of ClearStar's foundations, we are well-positioned to benefit as the markets continue to improve and expand. Consequently, we are confident of delivering continued growth and shareholder value. I look forward to continuing to report our progress.

Chief Executive's Review

Robert J. Vale, *Chief Executive Officer*

21 April 2017

Our results for 2016 demonstrate that ClearStar's underlying businesses are robust and continue to deliver revenue growth – with annual turnover of $16.0 million (2015: $15.5 million). This year we streamlined our business, strengthened our direct sales team and launched our global platform. ClearStar now provides a suite of advanced services, directly and indirectly through our Channel Partner and Consumer Reporting Agency ("CRA") customers, on a global basis.

Divisional Progress

In Direct Services, as mentioned, we strengthened and expanded our direct sales and services team – in particular, by recruiting employees with significant experience and expertise in engaging with large companies, which is our primary target market. As a result, organic direct revenues increased by 77% to $1.9 million, and we were successful in 'upscaling' the client base by targeting larger, higher-volume direct clients, especially in the transportation industry. This growth included an increase in sales of direct medical information services by 56% to $745,000, which we now provide to around 600 clients.

As previously announced, we experienced attrition among our acquired SingleSource client base, but this was largely mitigated by the growth in organic sales resulting in total Direct Services Division revenues of $3.80 million (2015: $3.77 million).

During the year we commenced the on-boarding process for the three-year contract, signed at the end of 2015, with a leading global relocation and specialised logistics solutions provider, which includes an initial deployment of our global Sphere platform and maiden deployment of ClearID and ClearContact biometric recognition and electronic addressbook products. We're receiving increasing interest in these solutions, which were launched this year, and have commenced several trials with potential clients.

The strengthening of our direct sales and services team, as well as our global offer, was demonstrated with the award, post period, of a contract by IntelliCentrics for our titer and drug screening solution. IntelliCentrics is a healthcare industry leader with over 10,000 distinct installations of vendor credentialing across the US, Canada and the UK.

Turning to our Channel Partners and CRAs Division, sales grew by 4% to $12.2 million in 2016, primarily as a result of increased business from some of our largest clients. The primary services contributor to revenues was medical information services, which consisted mostly of drug testing but also clinical testing and occupational testing, which accounted for $4.9 million. The total number of employers to which we provide our medical testing and results review services is now over 14,500.

Technology and Product Advancement

A significant milestone was achieved this year with the launch of our global platform, Sphere – developed to satisfy interface, compliance and architectural demands outside the US – and we began processing international records. We're receiving increasing interest in our global solutions from US-based organisations that have global operations or that require access to the global records of prospective employees as well as businesses based outside of the US. As such, we're confident of more widespread usage of Sphere in 2017 and expect meaningful revenue contribution from global customers.

Other key developments in 2016 include achieving certification from the U.S. Department of Commerce under the EU-U.S. Privacy Shield for the transfer of personally identifiable information (PII) from the European Union to the United States, representing a further testament to the strength of our privacy and compliance standards.

We also continued to grow our network of collection sites for medical information services to over 15,000 and made our clinical testing service available via our proprietary WebCCF technology. The ease-of-use of this solution is a market differentiator for ClearStar and we believe sales in clinical testing will increase as result of availability via WebCCF.

Outlook

As a result of the progress made in 2016, we entered 2017 well positioned with a stronger client base and a more comprehensive service offering.

The fluidity of the labour market continues to expand thereby increasing the demand for our direct services and providing new opportunities for revenue generation. Our global platform, Sphere, is gaining traction, with the strong initial client response strengthening our belief that we can generate meaningful global revenue in 2017. Consequently, we are confident of delivering continued growth and shareholder value, and we look forward to updating the market as the year progresses.

CFO's Statement

David Pattillo, *Chief Financial Officer*

21 April 2017

We continued to achieve revenue growth with total revenues increasing by 3% for the year ended 31 December 2016 to $16.0 million compared with $15.5 million for the year ended 31 December 2015.

Gross profit increased by 4% to $9.8 million (2015: $9.5 million) and gross profit margin was maintained at 61.3% (2015: 61.2%). This increase was primarily due to achieving greater purchase economies.

Total operating expenses, including depreciation and amortisation, increased by approximately $194,000, or 1.7%, to $11.9 million for 2016 compared with $11.7 million for 2015.

General and administrative expenses decreased by approximately $636,000, or 7.8%, to $7.5 million for 2016 compared with $8.2 million for the prior year, primarily due to better operating efficiencies that we achieved from the integration of the SingleSource acquisition.

Selling and marketing expenses were reduced by approximately $175,000, or 11.9%, to $1.3 million (2015: $1.5 million), largely as a result of the consolidation of the SingleSource sales and marketing team.

Research and development increased by approximately $863,000, or 107%, to $1.7 million for 2016 compared with $808,000 for 2015. This was primarily due to more products going into production, including the Sphere global platform, which changes the accounting treatment of much of the software development costs from being capitalised to being expensed.

Depreciation and amortisation increased by approximately $142,000, or 11%, to $1.4 million (2015: $1.3 million), primarily due to more products going into production, including Sphere, and thereby commencing amortising on the capitalised asset.

EBITDA for 2016 improved by $290,000 to a $666,000 loss, compared with $956,000 loss for the prior year. We reported a loss before tax of approximately $2.1 million in 2016 compared with a loss before tax of approximately $2.3 million for 2015.

As of 31 December 2016, total assets were $9.7 million with the largest assets being goodwill and other intangible assets of $5.0 million, net cash of $2.4 million, and accounts receivable of $1.4 million. For 2016, we utilised $1.5 million in cash compared with $2.6 million in the prior year, representing a 43% improvement in cash utilisation.

Our total liabilities as of 31 December 2016 were $1.6 million, and stockholders' equity was $8.1 million, resulting in a debt-to-equity ratio of 20%.

We utilised $460,000 in cash in operating activities compared with $1.0 million for the previous year, mainly due to improvement in working capital accounts. Cash used in investment activities was reduced to $0.9 million from $1.5 million in the previous year. This reduction is primarily the result of lower capitalised software development costs as more products were brought into production during the course of the year. We also paid $96,000 in financing activities related to capital lease obligations.

The ClearStar Solution

Key growth engine – **Direct Services**

ClearStar's direct services offering was enhanced during the year with the launch of its leading-edge biometric recognition software and electronic address book solutions – ClearID and ClearContact – enabling ClearStar to mobilise background screening. This has contributed to ClearStar gaining larger, higher-volume customers – with particular demand from employers that rely on remote hiring or where large numbers of temporary workers are employed on a sustained basis.

How it works

ClearID and ClearContact are provided via a mobile device (phone, tablet) to enable employers to bring screening to where the workers are – providing rapid, remote authentication – as well as a workforce recruitment and management solution.

1 The applicant provides their signature on the electronic consent form

2 A photo is taken, with the phone camera, of the applicant's government-issued photo ID

3 A photo of the applicant is taken with the phone camera

4 ClearStar's facial recognition and background screening technology processes the information against the criteria set by the employer and provides the results – on the mobile phone – within five minutes

5 Once the applicant is screened with ClearID, the ClearContact electronic addressbook stores their details, including background screen expiration date. ClearContact can locate and secure qualified casual labourers within a certain radius within minutes – enabling workers to be quickly employed when and where needed

The ClearStar Solution

Key growth engine – **Direct Services** (cont)

UniGroup®

UNITED VAN LINES
MAYFLOWER
UNIGROUP LOGISTICS
UNIGROUP WORLDWIDE MOVING

Transportation and logistics case study

UniGroup has a highly decentralized global network of independent agents and van operators who utilize a large number of workers. Accuracy of screening and speed to hire are critical.

ClearStar provided a customised Applicant Portal for conducting background screens on drivers, sales associates, estimators, packers and casual workers, deployed via ClearID to enable remote authentication of applicants in the field using facial recognition technology and mobile validation of government IDs.

ClearContact is used to communicate with eligible causal workers about future work assignments to meet future work demand.

As a result, the speed and efficiency of the recruitment process has been increased, while enhancing the applicant screening experience.

Demand drivers

- **Expanding** 'gig economy' and increasingly casual and transitory nature of the workforce
- **Government** emphasis on employment and job creation, particularly in underprivileged or 'forgotten' areas of the US where casual work is more prevalent
- **Regulatory** focus on curbing employment of illegal immigrants
- **Security** concerns

The ClearStar Solution

Key growth engine – **Global Platform**

ClearStar's global platform, Sphere, provides services for US businesses seeking to operate overseas or hire overseas employees as well as for international customers.

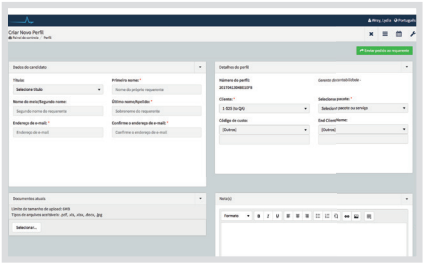
ClearStar offers more than 2000 services in more than 230 countries.

Sphere value proposition

Dispersed platform to meet data residency requirements

Seamless user interface

Sphere interfaces with Aurora (US-focused platform) on the front end to provide a complete screening solution with seamless user experience

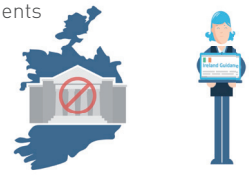


Privacy Shield Framework

US government has certified ClearStar for personal data transfer between the EU and the US

Experienced team

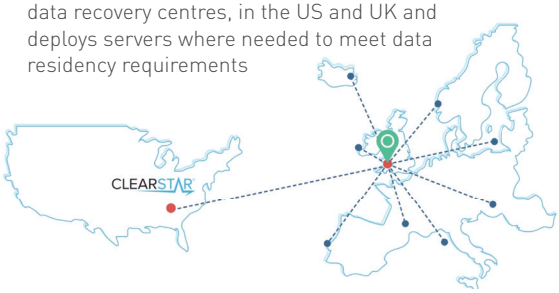
ClearStar's experienced team can explain global screening with clear ordering requirements and compliance guides to reduce turnaround time

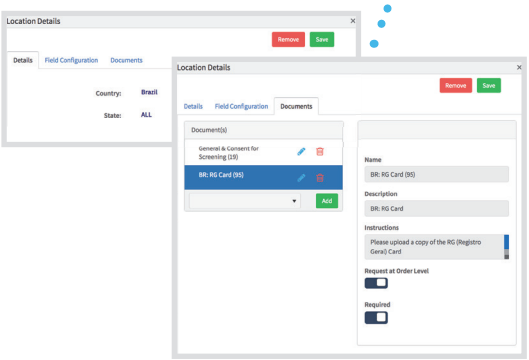


Language capabilities

Currently configured for three languages with capacity for up to 30

ClearStar has two data centres, and two data recovery centres, in the US and UK and deploys servers where needed to meet data residency requirements





Technological compatibility and flexibility

Compatible with existing privacy laws in nearly all major countries with flexibility to adapt to changes in laws

Security and compliance

ClearStar has trusted relationships with local providers who must pass ClearStar's ongoing reputational and sanction screening and credentialing requirements

Directors' Report

For the year ended 31 December 2016

Principal Activities

ClearStar is a technology and service provider to the background check industry, supporting background screening companies, employers and employees with their recruitment and employment application decisions. ClearStar provides employment intelligence to its clients through a suite of IT applications for day-to-day use in their business. Employment intelligence aims to improve business insight to support better recruitment and other decisions affecting employees generally, by increasing the quality, reliability and visibility of information available to management.

Business Review

The information that fulfils the requirements of the business review, including details of the 2016 results, principal risks and uncertainties and the outlook for future years, are set out in the Chairman's and Chief Executive Officer's Statement and the Business and Financial Review, on pages 3 to 9.

Admission to AIM

ClearStar was admitted to trading on the AIM market of the London Stock Exchange on 11 July 2014, at which time 15,500,000 new Ordinary Shares were placed to raise gross proceeds of approximately US $15 million.

Further information relating to movements on share capital is set out in Note 6 to the consolidated financial statements on page 34.

Dividends

The Company is primarily seeking to achieve capital growth for its shareholders, and it is the Board's intention during the current phase of the Company's development to retain future distributable profits and only recommend dividends when appropriate and practicable. In the long term, the Directors intend to follow a progressive dividend policy in respect of excess equity over and above that required to fund the Group.

Directors

The following Directors held office as indicated below for the year ended 31 December 2016 and up to the date of signing the consolidated financial statements except where otherwise shown.

Barney Quinn – *Non-executive Chairman*

Robert J. Vale, Jr. – *Founding Member, Director and Chief Executive Officer*

Kenneth W. Dawson, Jr. – *Founding Member, Director and Chief Information and Security Officer*

David A. Pattillo – *Director and Chief Financial Officer*

André Schnabl – *Non-executive Director*

Election of Directors

Although not required under the Company's Articles of Association and The Companies Law of the Cayman Islands, the Company is seeking at its annual Stockholders meeting confirmation that the shareholders are satisfied with the current Board and approve for the current Board to continue in office until the next Board election. The 2017 Annual Meeting will be held at 10 a.m. EDT on 23 May 2017 at the offices of Eversheds Sutherland (US) LLP, 999 Peachtree St, NE, Suite 2300, Atlanta, GA 30309, USA.

Directors' Remuneration and Interests

The Directors' Remuneration Report is set out on pages 16 to 17. It includes details of Directors' remuneration, interests in the Ordinary Shares of the Company and share options.

Corporate Governance

The Board's Corporate Governance Statement is set out on pages 14 to 15.

Share Capital and Substantial Shareholdings

Details of the share capital of the Company as of and at 31 December 2016 are set out in Note 6 to the consolidated financial statements. At 31 March 2017, a total of 36,302,900 Ordinary Shares were outstanding; the following Shareholders own 3 per cent. or more of the Ordinary Shares:

Robert J. Vale, Jr. [1]	31.14%
Kenneth W. Dawson, Jr.	11.81%
William T. White [2]	10.49%
River & Mercantile Group	9.88%
Hargreave Hale Limited	7.28%
Standard Life Investments Limited	6.46%
Artemis Investment Management LLP	4.83%
Ennismore Fund Management Limited	4.62%
David Pattillo	3.59%

(1) The aggregate number of shares shown for Mr. Vale includes (a) 26.47% held by and controlled by Mr. Vale; and (b) 4.67% held by or on behalf of Mr. Vale's children.

(2) The aggregate number of shares shown for Mr. White includes (a) 6.85% held by and controlled by Mr. White; and (b) 3.64% held by or on behalf of Mr. White's children.

Directors' Responsibilities Statement

For the year ended 31 December 2016

Under the Company's Articles of Association and The Companies Law of the Cayman Islands, all corporate powers are exercised by or under the authority of, and the business and affairs of the corporation managed under the direction of, its Board of Directors, subject to any limitations set forth in the Company's Articles of Association. The Company has prepared financial statements in accordance with Generally Accepted Accounting Principles in the United States ("U.S. GAAP"). The Directors

(1) Discharge their duties as a Director, including duties as member of a committee, in a manner he or she believes in good faith to be in the best interests of the corporation, and with the care an ordinarily prudent person in a like position would exercise under similar circumstances.

(2) In discharging their duties of Directors, Directors rely on information, opinions, reports or statements, including financial statements and other financial data, if prepared or presented by:

(a) One or more officers or employees of the corporation whom the Directors reasonably believe to be reliable and competent in the matters presented; or

(b) Legal counsel, public accountants or other persons as to matters the Directors reasonably believe are within the person's professional or expert competence; or

(c) A committee of the Board of Directors of which a Director is not a member if the Director reasonably believes the committee merits confidence.

(3) Are not entitled to rely if the Directors have knowledge concerning the matter in question that makes reliance otherwise permitted by subsection (2) above unwarranted.

Independent Auditors

The Audit Committee of the Board of Directors reviews annually the quality and cost effectiveness of the external audit and the independence and objectivity of the external auditors. Aprio, LLP ("Aprio"), formerly Habif, Arogeti & Wynne, LLP, was engaged to perform the 2016 audit for fees of approximately $72,000, the 2016 corporate income tax compliance returns for fees of approximately $29,000 and various income tax consulting work for fees of approximately $21,000.

Directors' Biographies

For the year ended 31 December 2016

Barney Quinn
Non-executive Chairman

Barney has significant experience in the global application software and cloud markets. He was the CEO of then AIM-traded Workplace Systems International plc and then latterly a non-executive director at the company. For many years Barney was an executive board director of the publicly-quoted Sherwood International plc and has also been a non-director with two other listed software companies, SSP Holdings plc and Raft International plc. At Becrypt, the privately-held encryption software specialist, he was non-executive chairman for seven years. Barney is currently a non-executive director of Rosslyn Data Technologies plc and non-executive Chairman of Arkivum Limited. He also advises a number of cloud-based technology companies.

Robert Vale
Chief Executive Officer

Robert is Chief Executive Officer of ClearStar, which he founded in partnership with Ken Dawson and William White in 1995. Prior to forming ClearStar, he was the Manager of Loss Prevention Technical Support for United Parcel Service (UPS). This group was responsible for all loss prevention, risk mitigation and security-related system designs, development, implementation and 24/7 management of systems for UPS worldwide. During his tenure, he worked with the Aerospace Testing Alliance to assist in developing security guidelines for UPS' airline.

A founding member of the National Association of Professional Background Screeners (NAPBS), Robert is often called upon to deliver keynote presentations on the subject of large-scale systems management, technology trends and personal information security. Robert has been a guest instructor at the Federal Law Enforcement Training Centre and has published numerous articles for security trade journals. He has been a member of ASIS International, the pre-eminent organisation for security professionals, since 1987.

Robert holds a Bachelor of Science degree from the State University of New York, Plattsburgh, and served six years in the United States Air Force as Security Police – Security Specialist.

Ken Dawson
Chief Information & Security Officer

Ken is a founding member of ClearStar, who has diversified experience in data management, architecture and security or realtime, analytical technology solutions. Ken currently serves as its Chief Information & Security Officer. In this role, Ken is responsible for evaluating, designing and implementing background check technology solutions that combine information from disparate information sources in varied data formats into cohesive, consistent and richly formatted reports.

Prior to forming ClearStar in 1995, Ken developed enterprise systems for United Parcel Service (UPS) and Kaiser Permanente. Ken began his career in software development and content delivery in 1990 while working as an intern for Conatec, Inc., an aerospace engineering firm.

Ken is a certified information systems professional and studied Aerospace Engineering at the University of Maryland.

David Pattillo
Chief Financial Officer

David is Chief Financial Officer of ClearStar. In this role he provides leadership and direction in all areas of finance and accounting, including financial planning and forecasting, and accessing capital to fund growth. Additionally, he is responsible for establishing and maintaining the accounting controls and processes to mitigate financial risk and ensure timely financial reporting.

David has an accomplished career in leading companies through high growth expansion, both domestically and internationally. Prior to ClearStar, David was the CFO of MyCelx Technologies Corporation which he led through an IPO on AIM in 2011. Prior to that, David was CFO of Harry's Farmers Market, a company which he helped guide from start-up through an IPO on NASDAQ. David has public company reporting experience as CFO of both MyCelx Technologies Corporation and Harry's Farmers Market.

David has valuable board experience as he has been an executive board member of both private and public companies. David holds a Bachelor of Science degree from Clemson University and an MBA from the University of Georgia.

André Schnabl
Non-executive Director

André retired in 2012 as Managing Partner of the Atlanta office of Grant Thornton, LLP. Prior to assuming the Managing Partner role, André led the Technology Industry Practice, which focused on serving the needs of software, medical device and telecommunications clients. Throughout his career, André has excelled at linking people, vision, strategies and diligent execution to drive sustainable revenue growth and a highly productive corporate culture. During his tenure as the leader of the Atlanta office, André drove the formulation and execution of a strategy that achieved three-fold revenue growth.

Seeking ways to influence excellence among audit committee chairs and members, in 2012 André launched the "Grant Thornton Peer 2 Peer Audit Committee Forum". In partnership with Kennesaw State University's "Center of Corporate Governance", the Forum is designed specifically to give audit committee members an effective way to stay current on the many regulatory, risk, and business issues affecting their roles as audit committee members and the companies on whose boards they serve.

André has served on numerous corporate and not-for-profit boards.

Corporate Governance Report

For the year ended 31 December 2016

The Company is incorporated and registered in the Cayman Islands (registration number 287331). The Directors recognize the importance of sound corporate governance and, whilst the UK Corporate Governance Code published by the Financial Reporting Council does not apply to AIM companies, the Directors' objectives are (i) to observe the requirements of the UK Corporate Governance Code to the extent they consider appropriate in light of the Group's size, stage of development and resources, and (ii) to follow, so far as practicable, the recommendations set out in the corporate governance code for small and mid-size quoted companies published by the QCA. The Board has established an Audit Committee, a Remuneration Committee, a Nominations Committee and an AIM Compliance and Corporate Governance Committee, with formally delegated duties and responsibilities as described below.

Audit Committee

The Audit Committee is responsible for monitoring the integrity of the Company's consolidated financial statements, reviewing significant financial reporting issues, reviewing the effectiveness of the Company's internal control and risk management systems and overseeing the relationship with the external auditors (including advising on their appointment, agreeing to the scope of the audit and reviewing the audit findings). The Audit Committee continues to monitor the need for an internal audit department following Admission.

The Audit Committee is comprised of André Schnabl, who acts as Chairman, and Barney Quinn. The Audit Committee met three times during 2016. The Audit Committee also meets regularly with the Company's external auditors.

Remuneration Committee

The Remuneration Committee is responsible for determining and agreeing with the Board regarding the framework for the remuneration of the Chairman, the Board Members and other designated senior executives and, within the terms of the agreed framework, determining the total individual remuneration packages of such persons including, where appropriate, bonuses, incentive payments and share options or other share awards. The remuneration of non-executive Directors is a matter for the Chairman and the executive members of the Board. No Director is involved in any decision as to his or her own remuneration. The Remuneration Committee is also responsible for issuing awards of relevant shares and options to purchase Ordinary Shares of the Company under the Company's 2014 Share Option and Incentive Plan.

The Remuneration Committee is comprised of André Schnabl, who acts as Chairman, and Barney Quinn. The Remuneration Committee met three times during 2016.

Nominations Committee

The Nominations Committee is responsible for identifying and nominating members of the Board, recommending Directors to be appointed to each committee of the Board and the chair of each such committee. The Nominations Committee also arranges for evaluation of the Board.

The Nominations Committee is comprised of Barney Quinn, who acts as Chairman, and André Schnabl. The Nominations Committee met twice during 2016.

AIM Compliance and Corporate Governance Committee

The AIM Compliance and Corporate Governance Committee is responsible for ensuring that the Company is complying with the AIM Rules. It also assesses the Company's corporate governance obligations every year. The AIM Compliance and Corporate Governance Committee is chaired by Robert J. Vale, Jr. and its other members are David A. Pattillo and Kenneth W. Dawson, Jr. It meets as often as is required.

Board of Directors

The Board consists of two Non-executive Directors with relevant experience to complement the three Executive Directors and to provide an independent view to the Executive Directors. The Non-executive Directors are Barney Quinn (Chairman) and André Schnabl. The three Executive Directors are Robert J. Vale, Jr. (Chief Executive Officer), Kenneth W. Dawson, Jr. (Chief Information and Security Officer) and David A. Pattillo (Chief Financial Officer).

The Board is responsible for formulating, reviewing and approving the Company's strategy, budgets and corporate actions.

Relations with Shareholders

Copies of the Annual Report and Consolidated Financial Statements are issued to all shareholders and copies are available on the Company's website (www.clearstar.net/investors/financial-reports/). The Company also uses its website to provide information to shareholders and other interested parties, subject to applicable restrictions of the United States securities laws. The Chief Financial Officer and Secretary also deal with shareholder correspondence as and when it arises. At the Company's Annual Meeting, the Chairman along with the Chief Executive Officer and other Directors are available before and after the meeting for further discussions with shareholders.

Internal Control

The Board is ultimately responsible for the Company's system of internal control and reviewing its effectiveness on an ongoing basis. The system is designed to manage rather than eliminate the risk of failure to achieve the Company's strategic objectives and cannot provide absolute assurance against material misstatement or loss. The key risk management processes and internal control procedures include the following:

- The involvement of the Executive Directors in day-to-day business operations.
- Clearly defined responsibilities and limits of authority.
- A system of financial reporting, forecasting and budgeting. Budgets are prepared annually for the business based upon a multi-year strategic plan narrowed to a current year tactical plan to take advantage of current opportunities and address near term risks. Reviews occur through the management structure culminating in a Company budget which is considered and approved by the Board. Company management accounts are prepared monthly and submitted to the Board for review. Variances from budget and prior year are monitored, and the reasons for significant variances are reviewed.
- An ongoing process for identifying, evaluating and seeking to manage significant risks across the Company.

Corporate Secretary

The Company's corporate secretary is ClearStar's Executive Vice President and General Counsel, Nicolas S. Dufour.

Directors' Remuneration Report

For the year ended 31 December 2016

As an AIM-listed company, ClearStar is not required to comply with Schedule 8 of The Large and Medium- sized Companies and Groups (Accounts and Reports) Regulations 2008. The following disclosures are therefore made on a voluntary basis. The information is unaudited.

Remuneration Policy

The Company's remuneration policy is based on the following broad principles:

- to provide competitive remuneration packages to attract and retain quality individuals;
- to align the interests of management with the interests of shareholders; and
- to set the pay of the Executive and Non-executive Directors with due account taken of (i) pay and conditions throughout the Company and (ii) corporate governance best practice.

Remuneration consists of the following elements:

Base Pay

Executive Directors' base pay is designed to reflect the role and responsibility of the individual within the Company. Salary levels are reviewed annually.

Annual Bonus

All Executive Directors and members of senior management participate in the Company's annual bonus scheme, which is based on the achievement of individual and Company performance targets at the discretion of the Compensation Committee. Annual bonuses are designed to incentivise performance and reward achievement in line with the agreed corporate strategy.

Long-term Incentives

The Compensation Committee considers that equity based long-term incentive schemes are the most effective way to align the interests of participants and shareholders.

Service Contracts

Barney Quinn

Mr. Quinn entered into an agreement with the Company on 30 May 2014 to serve as its Chairman. The service contract provides for, among other things:

(i) annual board fees of $55,000 and participation in the Executive Bonus Plan to be directed by the Compensation Committee;

(ii) grant of $35,000 of stock options based on the IPO price to purchase Ordinary Shares of the Company, vested ratably over a one-year period; and

(iii) a three-year term (automatically renewing for successive one-year periods). The agreement provides for customary non-solicitation, non-compete and nondisclosure restrictions.

Robert J. Vale, Jr.

Mr. Vale entered into an employment agreement with the Company on 7 July 2014 to serve as its Chief Executive Officer and to serve on the Board at the request of the Company. The employment agreement provides for, among other things:

(i) annual salary of $480,000 and participation in the Executive Bonus Plan to be directed by the Compensation Committee;

(ii) a two-year term (automatically renewing for successive one-year periods). The agreement may only be terminated by Mr. Vale upon six-month prior written notice or by the Company upon providing for one-year base salary, payable in 24 semi-monthly instalments in arrears, as severance if he is terminated without cause or resigns for good reason. The agreement provides for customary non-solicitation, non-compete and non-disclosure restrictions.

Kenneth W. Dawson, Jr.

Mr. Dawson entered into an employment agreement with the Company on 7 July 2014 to serve as its Chief Information and Security Officer and to serve on the Board of Directors. The employment agreement provides for, among other things:

(i) annual salary of $250,000 and participation in the Executive Bonus Plan to be directed by the Compensation Committee;

(ii) a two-year term (automatically renewing for successive one-year periods). The agreement may only be terminated by Mr. Dawson upon six-month prior written notice or by the Company upon providing for one-year base salary, payable in 24 semi-monthly instalments in arrears, as severance if he is terminated without cause or resigns for good reason. The agreement provides for customary non-solicitation, non-compete and non-disclosure restrictions.

David A. Pattillo

Mr. Pattillo entered into an employment agreement with the Company on 7 July 2014 to serve as its Chief Financial Officer and to serve on the Board of Directors. The employment agreement provides for, among other things:

(i) annual salary of $250,000 and participation in the Executive Bonus Plan to be directed by the Compensation Committee; and

(ii) a two-year term (automatically renewing for successive one-year periods). The agreement may only be terminated by Mr. Pattillo upon six-month prior written notice or by the Company upon providing for one-year base salary, payable in 24 semi-monthly instalments in arrears, as severance if he is terminated without cause or resigns for good reason. The agreement provides for customary non-solicitation, non-compete and non-disclosure restrictions.

André Schnabl

Mr. Schnabl entered into an agreement with the Company on 30 May 2014 to serve on the Board of Directors. The service contract provides for, among other things:

(i) annual board fees of $45,000 and participation in the Executive Bonus Plan to be directed by the Compensation Committee;

(ii) grant of $35,000 of stock options based on the IPO price to purchase Ordinary Shares of the Company, vested ratably over a one-year period; and

(iii) a three-year term (automatically renewing for successive one-year periods). The agreement provides for customary non-solicitation, non-compete and nondisclosure restrictions.

All Directors are elected by the shareholders at an annual or special meeting, to serve until the next election and until their successors are elected and qualified, or until their earlier death, resignation or removal.

The Director's remuneration for 2016 was as follows (Benefits in kind include medical and life insurance and 401(k) matching contributions):

	Salary and Director's fees US$	Benefits in kind US$	Performance related bonus US$	2016 Total US$
Non-executive Chairman				
Barney Quinn	$55,000	–	–	$55,000
Executive				
Robert J. Vale, Jr.	$480,000	$9,380	–	$489,380
Kenneth W. Dawson, Jr.	$250,000	$14,180	–	$264,180
David A. Pattillo	$250,000	$13,763	–	$263,763
Non-executive				
André Schnabl	$45,000	–	–	$45,000

The interests of the Directors at 31 December 2016 in the shares of the Company, not including interests of investment funds in respect of which the Director may have a managerial interest, and with respect to which such Director disclaims beneficial ownership, were:

	Number of Ordinary Shares	Percentage of issued share capital
Barney Quinn [1]	150,000	0.41%
Robert J. Vale, Jr. [2]	11,306,000	31.14%
Kenneth W. Dawson, Jr.	4,288,000	11.81%
David A. Pattillo	1,228,900	3.39%
André Schnabl	45,000	0.12%

(1) The interests of Mr. Quinn include 25,000 shares held by his wife, Jennifer Quinn

(2) The aggregate number of shares shown for Mr. Vale includes (a) 9,610,000 shares held by and controlled by Mr. Vale; and (b) 1,696,000 shares held by or on behalf of Mr. Vale's children.

Share Options

Options for Ordinary Shares awarded to Directors under the 2014 Share Option and Incentive Plan in place on 31 December 2016 were:

Option holder	Type of award	Earliest exercise date and date of vesting	Exercise price ($US)	Number of shares
Barney Quinn	Non-executive Chairman Stock Option	11 July 2014	$0.97	36,082
David A. Pattillo	Employee Stock Option	11 July 2014*	$0.97	105,000
	Employee Stock Option	4 January 2016*	$0.51	60,000
André Schnabl	Non-executive Director Stock Option	11 July 2014	$0.97	36,802

* Vesting ratably over a three-year period

Consolidated Financial Statements

For the years ended 31 December 2016 and 2015

Independent Auditors' Report

HA+W | Aprio
The new name for HA+W

Advisory Assurance Tax Private Client

To the Stockholders of
ClearStar, Inc. and subsidiaries

We have audited the accompanying consolidated financial statements of ClearStar, Inc. and subsidiaries, which comprise the consolidated balance sheets as of December 31, 2016 and 2015, and the related consolidated statements of operations, changes in stockholders' equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of ClearStar, Inc. and subsidiaries as of December 31, 2016 and 2015 and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Aprio, LLP

Atlanta, Georgia
April 14, 2017

Aprio, LLP Five Concourse Parkway, Suite 1000, Atlanta, Georgia 30328 404.892.9651 Aprio.com

Consolidated Statements of Operations

(US$, in thousands)

for the years ended 31 December 2016 and 2015

	Year Ended 31 December 2016 $	Year Ended 31 December 2015 $
Net revenue	**16,032**	15,516
Cost of revenue	**6,197**	6,023
Gross profit	**9,835**	9,493
Operating expenses		
Selling and marketing	**1,299**	1,474
Research and development	**1,671**	808
Depreciation and amortisation	**1,429**	1,287
General and administrative	**7,531**	8,167
Total operating expenses	**11,930**	11,736
Loss from operations	**(2,095)**	(2,243)
Other expense		
Interest expense	**(16)**	(22)
Total other expense	**(16)**	(22)
Net loss before taxes	**(2,111)**	(2,265)
Provision for income taxes	**61**	53
Net loss	**(2,172)**	(2,318)

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

Consolidated Balance Sheets

(US$, in thousands)

for the years ended 31 December 2016 and 2015

	As of 31 December 2016 $	As of 31 December 2015 $
ASSETS		
Current assets		
Cash	**2,420**	3,893
Accounts receivable – trade, net	**1,442**	1,609
Research and development tax credits	**138**	82
Prepaid expenses	**257**	291
Total current assets	**4,257**	5,875
Property and equipment, at cost		
Computer equipment	**687**	749
Furniture and fixtures	**277**	279
Leasehold improvements	**62**	72
Less accumulated depreciation	**(560)**	(412)
Total property and equipment, net	**466**	688
Other assets		
Goodwill and other intangible assets	**4,976**	5,268
Deposits	**11**	11
Total other assets	**4,987**	5,279
Total assets	**9,710**	11,842
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable	**1,130**	1,203
Accrued liabilities	**119**	82
Deferred revenue	**54**	54
State income taxes	**5**	7
Current portion of obligations under capital lease	**99**	92
Total current liabilities	**1,407**	1,438

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

Consolidated Balance Sheets *(continued)*

(US$, in thousands)

for the years ended 31 December 2016 and 2015

	As of 31 December 2016 $	As of 31 December 2015 $
LIABILITIES AND STOCKHOLDERS' EQUITY (contd.)		
Long-term liabilities		
Accrued liabilities	**46**	50
Deferred income taxes	**99**	45
Obligations under capital lease, net of current portion	**68**	171
Total long-term liabilities	**213**	266
Stockholders' equity		
Common stock, $0.0001 par value; 100,000,000 shares authorised; 36,302,900 shares issued and outstanding	**4**	4
Additional paid-in capital	**13,602**	13,478
Accumulated deficit	**(5,516)**	(3,344)
Stockholders' equity	**8,090**	10,138
Total liabilities and stockholders' equity	**9,710**	11,842

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

Consolidated Statements of Changes in Stockholders' Equity

(US$, in thousands, except no. of shares)

for the years ended 31 December 2016 and 2015

	Common Stock		Additonal Paid-in Capital	Accumulated Deficit	Total
	Shares No.	Amount $	$	$	$
Balances at 1 January 2015	**36,302,900**	**4**	**13,346**	**(1,026)**	**12,324**
Non-cash stock compensation	–	–	132	–	132
Net loss	–	–	–	(2,318)	(2,318)
Balances at 31 December 2015	**36,302,900**	**4**	**13,478**	**(3,344)**	**10,138**
Non-cash stock compensation	–	–	124	–	124
Net loss	–	–	–	(2,172)	(2,172)
Balances at 31 December 2016	**36,302,900**	**4**	**13,602**	**(5,516)**	**8,090**

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

Consolidated Statements of Cash Flows

(US$, in thousands)

for the years ended 31 December 2016 and 2015

	Year Ended 31 December 2016 $	Year Ended 31 December 2015 $
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss	**(2,172)**	(2,318)
Adjustments to reconcile net loss to net cash used for operating activities:		
Change in allowance for doubtful accounts	**13**	5
Depreciation and amortisation	**1,429**	1,287
Deferred income taxes	**54**	45
Non-cash stock compensation	**124**	132
Loss on disposal of property and equipment	**2**	–
Change in operating assets and liabilities:		
Accounts receivable	**154**	(518)
Research and development tax credits	**(56)**	(55)
Prepaid expenses	**34**	(79)
Deposits	–	2
Accounts payable	**(73)**	629
Accrued liabilities	**33**	(87)
Deferred revenue	–	(48)
State income taxes	**(2)**	3
Total adjustments	**1,712**	1,316
Net cash used for operating activities	**(460)**	(1,002)
CASH FLOWS FROM INVESTING ACTIVITIES		
Acquisition of property and equipment	**(32)**	(96)
Proceeds from disposition of property and equipment	**1**	–
Capitalised software development costs	**(886)**	(1,396)
Net cash used for investing activities	**(917)**	(1,492)
CASH FLOWS FROM FINANCING ACTIVITIES		
Principal payments on capital lease obligations	**(96)**	(90)
Net cash used for financing activities	**(96)**	(90)
Net cash decrease for year	**(1,473)**	(2,584)
Cash at beginning of year	**3,893**	6,477
Cash at end of year	**2,420**	3,893

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

Consolidated Statements of Cash Flows *(continued)*

(US$, in thousands)

for the years ended 31 December 2016 and 2015

SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION	**Year Ended 31 December 2016 $**	Year Ended 31 December 2015 $
Cash paid:		
Interest	**16**	22
Income taxes	**7**	4
	23	26

SUPPLEMENTAL SCHEDULE OF NONCASH INVESTING AND FINANCING ACTIVITIES

During the year ended 31 December 2016, the Company retired obsolete and fully-depreciated property and equipment of approximately $94,000.

During the year ended 31 December 2016, the Company retired fully-amortised intangible assets of approximately $871,000.

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

Notes to the Consolidated Financial Statements

for the years ended 31 December 2016 and 2015

1. Summary of Significant Accounting Policies

a) Nature of Operations

ClearStar, Inc. ("ClearStar"), an exempt company incorporated in the Cayman Islands on 23 April 2014, is a holding company that owns a 100% interest in ClearStar, Inc. ("ClearStar US"), an entity formed on 23 March 1995, and incorporated in the state of Delaware, and ClearStar Limited ("ClearStar UK"), a dormant entity formed in the United Kingdom on 17 January 2014. The interest in ClearStar US was transferred to ClearStar on 1 July 2014. The interest in ClearStar UK was transferred to ClearStar on 22 July 2014. The Company is a technology and service provider to the background check industry, supporting background screening companies, employers and employees with their recruitment and employment application decisions. The Company provides employment intelligence to its clients through a suite of IT applications for day-to-day use in their business. Employment intelligence aims to improve business insight to support better recruitment and other decisions affecting employees generally, by increasing the quality, reliability and visibility of information available to management.

Effective 14 July 2015, ClearStar introduced a Depository Interest programme to enable its ordinary shares to be traded in CREST by qualifying shareholders. As a result, there are two lines of capital stock – restricted under the existing ticker CLST and unrestricted under the ticker CLSU.

b) Principles of Consolidation

The consolidated financial statements include the accounts of ClearStar and its 100% owned subsidiaries, ClearStar US and ClearStar UK (collectively the "Company").

All significant intercompany transactions and balances have been eliminated in consolidation.

c) Basis of Accounting

The historical financial information has been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America ("US GAAP").

d) Use of Estimates

The preparation of consolidated financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Estimates are used for, but not limited to, the allowance for doubtful accounts, depreciable lives of property and equipment, certain accrued liabilities, amortisation of other intangible assets, stock-based compensation and income taxes. Actual results could differ from these estimates.

e) Concentration of Credit Risk Arising From Cash Deposits in Excess of Insured Limits

The Company maintains cash balances at certain financial institutions that at times may exceed federally insured limits. From time to time, the Company's cash balances exceed such limits. The Company has not experienced any losses in such accounts. The Company believes it is not exposed to any significant risks on cash.

f) Accounts Receivable

The Company extends credit to customers in a broad range of industries located throughout the United States and abroad based on the size of the customer, its payment history, and other factors. The Company generally does not require collateral to support customer receivables. The Company provides an allowance for doubtful accounts based upon a review of the outstanding accounts receivable, historical collection information and existing economic conditions. The Company determines if receivables are past due based on days outstanding, and amounts are written off when determined to be uncollectable by management. The maximum accounting loss from the credit risk associated with accounts receivable is the amount of the receivable recorded, which is the face amount of the receivable, net of the allowance for doubtful accounts.

Notes to the Consolidated Financial Statements *(continued)*

for the years ended 31 December 2016 and 2015

g) Property and Equipment

Property and equipment are stated at cost. Expenditures for maintenance and repairs are expensed currently, while renewals and betterments that materially extend the life of an asset are capitalised. The cost of assets sold, retired, or otherwise disposed of, and the related allowance for depreciation are eliminated from the accounts, and any resulting gain or loss is recognised.

Depreciation of property and equipment is provided using the straight-line method over the estimated useful lives of the assets, which are as follows:

Computer equipment	3 – 4 years
Furniture and fixtures	5 – 7 years
Leasehold improvements	Lesser of estimated useful life or life of the lease

Depreciation expense for the years ended 31 December 2016 and 2015 was approximately $251,000 and $258,000, respectively.

h) Goodwill

Goodwill recorded in the consolidated financial statements represents the excess of the purchase price of an acquisition over the fair value of acquired net assets on the date of acquisition. Goodwill is not amortised since it has an indefinite life. Accordingly, the carrying value of goodwill is reviewed for impairment by the Company annually, or more often if events or circumstances indicate that there may be impairment. The Company has not recorded any goodwill impairment charges.

In our evaluation of goodwill impairment, we perform a qualitative assessment to determine if it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If the qualitative assessment is not conclusive, we proceed to a two-step process to test goodwill for impairment including comparing the fair value of the reporting unit to its carrying value (including attributable goodwill). Fair value for our reporting unit is determined using an income or market approach, incorporating market participant considerations and management's assumptions on revenue growth rates, operating margins, discount rates and expected capital expenditures. Fair value determinations may include both internal and third-party valuations. Unless circumstances otherwise dictate, we perform our annual impairment testing in the fourth quarter. If the carrying amount of the goodwill exceeds the implied fair value of that goodwill, the Company will recognise an impairment loss as an expense.

i) Intangible Assets

Intangible assets, other than capitalised software development costs, arose from the purchase of certain assets in an acquisition and are reported net of amortisation. These costs are amortised using the straight-line method over their estimated useful life. The estimated useful life for customer relationships and trade name are 7 and 1 year(s), respectively.

The Company has capitalised external direct costs of services consumed in developing and obtaining internal-use computer software and the payroll and payroll-related costs for employees who are directly associated with and who devote time to developing the internal-use computer software.

Management's judgment is required in determining the point at which various projects enter the application development stage at which costs may be capitalised, in assessing the ongoing value of the capitalised costs, and in determining the estimated useful lives over which the costs are amortised. Costs in relation to the preliminary stages of projects are expensed in the period in which they are incurred. The Company expects to continue to invest in internally developed software and to capitalise costs in accordance with US GAAP.

j) Impairment of Long-Lived Assets

Long-lived assets, such as property and equipment, and purchased intangible assets subject to amortisation, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If circumstances require a long-lived asset or asset group be tested for possible impairment, the Company first compares undiscounted cash flows expected to be generated by that asset or asset group to its carrying amount. If the carrying amount of the long-lived asset or asset group is not recoverable on an undiscounted cash flow basis, an impairment is recognised to the extent that the carrying amount exceeds its fair value. Fair value is determined through various valuation techniques including discounted cash flow models, quoted market values and third party independent appraisals, as considered necessary. Management determined that there were no impairments during the years ended 31 December 2016 and 2015.

Notes to the Consolidated Financial Statements *(continued)*

for the years ended 31 December 2016 and 2015

k) Revenue Recognition

The Company requires that four basic criteria be met before revenue can be recognised for all transactions: (i) persuasive evidence of an arrangement exists; (ii) the price is fixed or determinable; (iii) collectability is reasonably assured; and (iv) delivery has occurred. Fixed monthly fees are derived primarily from customers' use of services that are provided for an agreed number of transactions. Arrangements for these services generally have terms of one year or less, and the fixed monthly fees are recognised as services are provided. One-time setup fees are recognised based on the Company's configuring and activating customers on internal and third party systems. The Company recognises one-time setup fees revenue rateably over 12 months or the period beyond which the initial contract term is expected to extend and the customer continues to benefit, whichever is longer. Annual certification fees are billed annually and are recognised rateably over the contract period. The Company recognises revenue from the per-transaction search results and/or search result review services and drug testing services at the time of delivery as the Company has no significant ongoing obligation after delivery.

Deferred revenue consists of payments received in advance of revenue recognition and contractual billings in excess of recognised revenue.

l) Advertising

The Company expenses advertising costs as incurred. Advertising expenses for the years ended 31 December 2016 and 2015 were approximately $292,000 and $473,000, respectively.

m) Income Taxes

ClearStar is incorporated as an exempted company in the Cayman Islands which currently does not levy income taxes on individuals or companies. ClearStar and its operating subsidiary, ClearStar US, are both taxed as corporations for US federal income tax purposes.

Income taxes are provided for the tax effects of transactions reported in the consolidated financial statements and consist of taxes currently due plus deferred income taxes. Deferred income taxes are recognised for differences between the basis of assets and liabilities for financial statement and income tax purposes. Deferred income tax assets and liabilities represent the future tax return consequences of those differences, which will either be taxable or deductible when the assets or liabilities are recovered or settled. Deferred income taxes are also recognised for operating losses that are available to offset future taxable income. The tax provision differs from the expense that would result from applying federal statutory rates to income before income taxes primarily because of the marginal tax rates used to compute deferred income taxes, the effect of state taxes and permanent differences between determining income for financial statement purposes and taxable income.

The Company is subject to tax audits in numerous jurisdictions, including the United States, individual states and localities, and abroad. Tax audits by their nature are often complex and can require several years to complete. In the normal course of business, the Company is subject to challenges from the Internal Revenue Service ("IRS") and other tax authorities regarding amounts of taxes due. These challenges may alter the timing or amount of taxable income or deductions, or the allocation of income among tax jurisdictions. The Company accounts for the uncertain tax provisions using a minimum probability threshold that a tax position must meet before a financial statement benefit is recognised. The minimum threshold is defined as a tax position that is more likely than not to be sustained upon examination by the applicable taxing authority, including resolution of any related appeals or litigation processes, based on the technical merits of the position. The tax benefit to be recognised is measured as the largest amount of benefit that is greater than fifty per cent. likely of being realised upon ultimate settlement. The Company recognises interest and penalties related to unrecognised tax benefits as part of income tax expense. The cumulative effect of considering uncertain tax positions resulted in no uncertain tax liability in the consolidated balance sheets. At 31 December 2016 and 2015, the Company does not have any unrecognised tax benefits.

The Company is not subject to income tax examinations for the years ending prior to 31 December 2013.

n) Research and Development

Expenditures related to the development of new products and processes are expensed as incurred. Research and development expenses were approximately $1,671,000 and $808,000, net of approximately $46,000 and $18,000 of tax credits, for the years ended 31 December 2016 and 2015, respectively.

Notes to the Consolidated Financial Statements *(continued)*

for the years ended 31 December 2016 and 2015

o) Stock-Based Compensation

The Company values stock options at the time of grant using a Black-Scholes model approach and records that fair market value as compensation expense, less an estimate for forfeitures, over the requisite service period, using the straight-line method. Stock-based compensation expense for the years ended 31 December 2016 and 2015 was approximately $124,000 and $132,000, respectively.

p) Fair Value of Financial Instruments

Due to the short-term nature of cash, accounts receivable, prepaid expenses, accounts payable, and accrued liabilities, their fair value approximates carrying value.

In specific circumstances, certain assets and liabilities are reported or disclosed at fair value. Fair value is the exit price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the Company's principal market for such transactions. If there is not an established principal market, fair value is derived from the most advantageous market.

Valuation inputs are classified in the following hierarchy:

(i) Level 1 inputs are unadjusted quoted prices in active markets for identical assets or liabilities.

(ii) Level 2 inputs are directly or indirectly observable valuation inputs for the asset or liability, excluding Level 1 inputs.

(iii) Level 3 inputs are unobservable inputs for the asset or liability.

Highest priority is given to Level 1 inputs and the lowest priority to Level 3 inputs. Acceptable valuation techniques include the market approach, income approach and cost approach. In some cases, more than one valuation technique is used.

q) Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update No. 2014-09 ("ASU 2014-09") "Revenue from Contracts with Customers." ASU 2014-09 supersedes the revenue recognition requirements in "Revenue Recognition (Topic 605)" and requires entities to recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods or services. As currently issued and amended, ASU 2014-09 is effective for annual reporting periods beginning after 15 December 2017, including interim periods within that reporting period, though early adoption is permitted for annual reporting periods beginning after 15 December 2016. We are currently in the process of evaluating the impact of the adoption of ASU 2014-09 on our consolidated financial statements, implementing accounting system changes related to the adoption and considering additional disclosure requirements.

In February 2015, the FASB issued Accounting Standards Update No. 2015-02 ("ASU 2015-02") "Consolidation (Topic 810): Amendments to the Consolidation Analysis." ASU 2015-02 changes the analysis that a reporting entity must perform to determine whether it should consolidate certain types of legal entities. We adopted this standard in the first quarter of 2016 on a retrospective basis. The adoption of this standard did not have a material impact on our consolidated financial statements.

In November 2015, the FASB issued Accounting Standards Update No. 2015-17 ("ASU 2015-17") "Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes." ASU 2015-17 simplifies the presentation of deferred income taxes by eliminating the separate classification of deferred income tax liabilities and assets into current and noncurrent amounts in the consolidated balance sheet. The amendments in the update require that all deferred tax liabilities and assets be classified as noncurrent in the consolidated balance sheets. The amendments in this update are effective for annual periods beginning after 15 December 2016, and interim periods therein and may be applied either prospectively or retrospectively to all periods presented. Early adoption is permitted. We have early adopted this standard in the fourth quarter of 2015 on a retrospective basis. Prior periods have been retrospectively adjusted.

As a result of the adoption of ASU 2015-17, the Company made no adjustments to the consolidated balance sheet as of 31 December 2016.

In February 2016, the FASB issued Accounting Standards Update No. 2016-02, "Leases", which requires that lease arrangements longer than 12 months' result in an entity recognizing an asset and liability. The pronouncement is effective for periods beginning after 15 December 2018, with early adoption permitted. The Company is currently evaluating the impact this guidance is expected to have on its consolidated financial statements.

Notes to the Consolidated Financial Statements *(continued)*

for the years ended 31 December 2016 and 2015

In March 2016, the FASB issued Accounting Standards Update No. 2016-09, "Improvements to Employee Share Based Payment Accounting" which simplifies several aspects of the accounting for share-based payment transactions, including income tax consequences, classification of awards, forfeitures and classification on the statement of cash flows. The provisions of this ASU are effective for fiscal years beginning after 15 December 2016, and interim periods within those fiscal years. The Company will adopt the new standard in the first quarter of 2017 and does not expect this will not have a material effect on its consolidated financial statements. The Company has elected to account for forfeitures as they occur, rather than estimate expected forfeitures.

In August 2016, the FASB issued Accounting Standards Update 2016-15 ("ASU 2016-15") "Statement of Cash Flows (Topic 230): Clarification of Certain Cash Receipts and Cash Payments" which would eliminate the diversity in practice related to the classification of certain receipts and payments in the statement of cash flows, by adding or clarifying guidance on eight specific cash flow issues. ASU 2016-15 is effective for annual and interim reporting periods beginning after 15 December 2017 for public entities with early adoption permitted. The amendments in this update should be applied retrospectively to all periods presented, unless deemed impracticable, in which case, prospective application is permitted. The Company does not expect the implementation of this standard to have a material effect on its consolidated financial statements.

In January 2017, the FASB issued Accounting Standards Update No. 2017-04 ("ASU 2017-04") "Intangibles - Goodwill and Other (Topic 350): Simplifying the Accounting for Goodwill Impairment." ASU 2017-04 removes the requirement to perform a hypothetical purchase price allocation to measure goodwill impairment. A goodwill impairment will now be the amount by which a reporting unit's carrying value exceeds its fair value, not to exceed the carrying amount of goodwill. ASU 2017-04 is effective for annual periods and interim periods within those annual periods beginning after 15 December 2019, and early adoption is permitted. The Company is in the process of evaluating the impact of this standard on its consolidated financial statements.

r) Reclassifications

Certain reclassifications have been made to the 2015 consolidated financial statement presentation to correspond to the current year's format. These reclassifications have no effect on previously reported net income.

2. Accounts Receivable

Accounts receivable consisted of the following:

	As of 31 December 2016 $000	As of 31 December 2015 $000
Trade accounts receivable	**1,472**	1,626
Allowance for doubtful accounts	**(30)**	(17)
	1,442	1,609

Notes to the Consolidated Financial Statements *(continued)*

for the years ended 31 December 2016 and 2015

3. Goodwill and Other Intangible Assets

Goodwill and other intangible assets were comprised of the following at 31 December 2016:

		Gross Cost				Accumulated Amortisation				
	Life (years)	Beginning $000	Additions $000	Disposal $000	Ending $000	Beginning $000	Additions $000	Disposal $000	Ending $000	Net $000
Goodwill	Indefinite	2,283	–	–	2,283	–	–	–	–	2,283
Software Development	3	2,919	886	(842)	2,963	1,368	939	(842)	1,465	1,498
Customer Relationships	7	1,673	–		1,673	239	239		478	1,195
Trade name	1	29	–	(29)	–	29	–	(29)	–	–
		6,904	886	(871)	6,919	1,636	1,178	(871)	1,943	4,976

Goodwill and other intangible assets were comprised of the following at 31 December 2015:

		Gross Cost			Accumulated Amortisation			
	Life (years)	Beginning $000	Additions $000	Ending $000	Beginning $000	Additions $000	Ending $000	Net $000
Goodwill	Indefinite	2,283	–	2,283	–	–	–	2,283
Software Development	3	1,523	1,396	2,919	607	761	1,368	1,551
Customer Relationships	7	1,673	–	1,673	–	239	239	1,434
Trade name	1	29	–	29	–	29	29	–
		5,508	1,396	6,904	607	1,029	1,636	5,268

Approximate aggregate future amortisation expense is as follows:

Year Ending 31 December:

	Amount $000
2017	1,118
2018	735
2019	367
2020	239
2021	234
	2,693

Notes to the Consolidated Financial Statements *(continued)*

for the years ended 31 December 2016 and 2015

4. Commitments and Contingencies

● Operating Leases

The Company leases office space and equipment. The lease agreements expire on various dates through February 2022.

Minimum lease payments under operating leases are recognised on a straight-line basis over the term of the lease including any periods of free rent for payment terms subject to escalation. Aggregate rent, common area maintenance charges and property tax expense for the years ended 31 December 2016 and 2015 was approximately $286,000 and $290,000, respectively.

At 31 December 2016, future minimum lease payments under non-cancellable operating leases were as follows:

Year Ending 31 December::

	Amount $000
2017	181
2018	178
2019	134
2020	133
2021	136
2022	23
	785

● Capital Leases

The Company leased computer equipment under two agreements classified as capital leases that expire through November 2018. The lease obligations bear an interest rate of up to 8.7 per cent. per annum and are payable in monthly instalments totalling $9,334.

Assets and liabilities under capital leases are recorded at the lower of the present value of the minimum lease payments or the fair value of the assets. The assets are depreciated over the shorter of the estimated useful lives or the lease term if ownership does not transfer to the Company at the end of the lease. Depreciation of assets under capital leases is included in depreciation expense.

Computer equipment held under capital leases consisted of the following:

	As of 31 December 2016 $000	As of 31 December 2015 $000
Cost of equipment and installation	**390**	390
Less: accumulated depreciation	**(238)**	(141)
	152	249

Notes to the Consolidated Financial Statements *(continued)*

for the years ended 31 December 2016 and 2015

At 31 December 2016, future minimum lease payments under capital lease agreements consist of the following:

Year Ending 31 December:

	Amount $000
2017	107
2018	70
	177
Less: interest	(10)
	167
Less: current portion	(99)
	68

- **Board of Directors Fees**

Effective 30 May 2014, the Company contracts with two non-executive directors ("NEDs") for 3-year terms subjective to renewal for successive one-year periods. The Company pays approximately $100,000 per annum to the NEDs. For the years ended 31 December 2016 and 2015, director fees were approximately $100,000 and $100,000, respectively. Options granted to the NEDs were approximately 72,000 shares, vesting over a one-year term (Note 7).

- **Long-Term Vendor Commitment**

In November 2014, the Company executed a three-year vendor contract for data centre and related services, requiring an annual fee of approximately $157,000, payable in equal monthly instalments in advance through January 2018.

Notes to the Consolidated Financial Statements *(continued)*

for the years ended 31 December 2016 and 2015

5. Income Taxes

- **Tax effects of temporary differences are as follows:**

	As of 31 December 2016 $000	As of 31 December 2015 $000
Non-current deferred tax assets (liabilities):		
Allowance for doubtful accounts	**10**	6
Prepaid expenses	**(14)**	(29)
Amortisation of software development	**(536)**	(556)
Amortisation of other intangible assets	**122**	79
Amortisation of goodwill	**(99)**	(45)
Accrued liabilities	**18**	18
Deferred revenue	–	10
Basis differences in property and equipment	**(42)**	(28)
Net operating losses	**2,305**	1,623
Stock-based compensation	**113**	69
Tax credits	**154**	101
Other adjustments	**(2)**	(16)
Total non-current	**2,029**	1,232
Less: valuation allowance	**(2,128)**	(1,277)
Net deferred tax assets (liabilities)	**(99)**	(45)

Deferred tax assets and liabilities are recognised for the expected tax consequences of temporary differences between the book and tax bases of the Company's assets and liabilities. Valuation allowances are recorded to reduce deferred tax assets when it is more likely than not that a tax benefit will not be realised. Management does not expect deferred tax assets to be fully realised in future years. Therefore, a valuation allowance has been recorded.

- **The components of the provision for income taxes are as follows:**

	Year Ended 31 December 2016 $000	Year Ended 31 December 2015 $000
Current tax expense:		
Federal	–	–
State	7	8
	7	8
Deferred tax expense:		
Federal	51	43
State	3	2
	54	45
Total provision for income taxes	61	53

Notes to the Consolidated Financial Statements *(continued)*

for the years ended 31 December 2016 and 2015

The effective income tax rate differs from the federal statutory income tax rate due to state income taxes, certain non-deductible expenses and an increase of approximately $851,000 in the valuation allowance for the period.

At 31 December 2016, the Company had approximately $6,481,000 in net operating loss carryforwards ("NOL") available to use against taxable income. The NOL's expire through 2036.

At 31 December 2016, the Company had approximately $154,000 in federal research and development ("R&D") credits available to use against taxable income. The R&D credits will begin to expire starting in 2034.

6. Stockholders' Equity

The Board has authorised 100,000,000 shares of Ordinary Shares, $0.0001 par value. As of 31 December 2016 and 2015, there were 36,302,900 shares issued and outstanding.

7. Stock-Based Compensation

In June 2014, the Board adopted the 2014 Share Option and Incentive Plan (the "Plan") that authorised the Board to grant options and restricted stock to employees and directors to acquire up to 3,000,000 shares of the Company's Ordinary Shares. The option price generally may not be less than the underlying stock's fair market value on the date of the grant. The options generally vest rateably up to a three-year period beginning the date of grant and expire as determined by the Board, but not more than 10 years from the date of grant. The amounts granted each calendar year is limited depending on certain terms of the Plan. As of 31 December 2016, approximately 1,134,000 shares remain available for grant under the Plan. The Plan terminates in June 2024.

The following table summarises activity of the Company's stock options during the years ended 31 December 2016 and 2015:

	Shares	Weighted-Average Exercise Price
Outstanding at 1 January 2015	1,290,165	$0.97
Granted	525,000	$0.94
Forfeited or cancelled	(279,000)	$0.96
Outstanding at 31 December 2015	1,536,165	$0.96
Granted	405,000	$0.51
Forfeited or cancelled	(75,000)	$0.95
Outstanding at 31 December 2016	1,866,165	$0.86
Exercisable at 31 December 2016	863,165	$0.96
Exercisable at 31 December 2015	415,165	$0.97

As of 31 December 2016, there was approximately $123,000 of total unrecognised compensation costs related to unvested stock options, which is expected to be recognised over a weighted-average period of 0.98 years. To the extent the actual forfeiture rate is different from what we have estimated, stock-based compensation expense related to these awards will be different from our expectations.

Notes to the Consolidated Financial Statements *(continued)*

for the years ended 31 December 2016 and 2015

The following assumptions were used for the Black-Scholes option pricing model:

	4 Jan 2016	1 July 2015	2 Jan 2015
Weighted-average fair value on day of grant	$0.14	$0.26	$0.25
Risk-free interest rate	1.00%	1.00%	1.00%
Expected dividend yield	0.00%	0.00%	0.00%
Expected volatility	32.90%	32.90%	33.18%
Weighted-average expected life of option	4.00 years	4.00 years	4.00 years

8. Earnings Per Share

Basic earnings per share is computed by dividing net income by the weighted average number of shares of common stock outstanding during the period. Diluted earnings per share is computed by dividing net income by the weighted average number of shares of common stock and common stock equivalents outstanding during the period. Dilutive common stock equivalents represent shares issuable upon assumed exercise of stock options.

	Year Ended 31 December 2016	Year Ended 31 December 2015
Basic income per share	**($0.06)**	($0.06)
Diluted income per share	**($0.06)**	($0.06)
Weighted-average common shares outstanding:		
Basic and diluted	**36,302,900**	36,302,900

9. Employee Retirement Plan

The Company sponsors an employee retirement plan known as the ClearStar, Inc. 401(k) Profit Sharing Plan Trust (the "401k Plan"). Under the 401k Plan, employees may contribute up to the maximum contributions as set periodically by the Internal Revenue Service. Additionally, the Company may make a discretionary contribution to the 401k Plan. The employer contributions vest over six years. Participant contributions are always 100 per cent. vested.

For the years ended 31 December 2016 and 2015, matching contributions were approximately $148,000 and $143,000, respectively.

10. Concentrations

- **Significant Vendor**

A significant vendor is defined as one from which the Company receives at least 10 per cent. of its total purchases. For the years ended 31 December 2016 and 2015, the Company had purchases from two suppliers totalling approximately $3,331,000 and $3,168,000 which comprised approximately 54 and 53 per cent. of the Company's purchases, respectively. Accounts payable and accrued liabilities included approximately $539,000 and $510,000 to these vendors at 31 December 2016 and 2015, respectively.

- **Significant Customer**

A significant customer is defined as one from whom at least 10 per cent. of annual revenue is derived. For the year ended 31 December 2016, the Company had sales to one customer totalling approximately $1,748,000, which comprised approximately 11 per cent. At 31 December 2016, the accounts receivable balance included approximately $148,000 from this customer. There were no significant customers for the year ended 31 December 2015.

Notes to the Consolidated Financial Statements *(continued)*

for the years ended 31 December 2016 and 2015

11. Related Party Transactions

The Company contracted with a certain shareholder of the Company to provide consulting services. During the years ended 31 December 2016 and 2015, the Company incurred approximately $41,000 and $26,000, respectively, in consulting fees to this related party.

The Company leased one of its office spaces from Flying Diamond, LLC, a company owned by two shareholders (see Note 4). Rental expense paid to the related party for the years ended 31 December 2016 and 2015 was approximately $83,000 and $87,000, respectively. This lease was terminated in November 2016.

12. Subsequent Events

The Company evaluated subsequent events through 14 April 2017, when these consolidated financial statements were available to be issued. Management is not aware of any significant events that occurred subsequent to the consolidated balance sheet date but prior to the filing of this report that would have a material impact on the consolidated financial statements.

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