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

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2023

OR

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

For transition period from __________ to __________

Commission file number 001-39331

System1, Inc.
(Exact name of registrant as specified in its charter)

Delaware	**92-3978051**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
4235 Redwood Avenue **Marina Del Rey, CA**	**90066**
(Address of Principal Executive Offices)	(Zip Code)

(310) 924-6037
(Registrant's telephone number including area code)

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

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Class A common stock, par value $0.0001 per share	SST	The New York Stock Exchange
Redeemable warrants, each whole warrant exercisable for one Class A common stock at an exercise price of $11.50 per share	SST.WS	The New York Stock Exchange

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☒ No ☐

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

Large accelerated filer	☐	Accelerated filer	☒
Non-accelerated filer	☐	Smaller reporting company	☒
Emerging growth company	☒		

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.☐

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

As of August 3, 2023, there were 93,606,858 shares of Class A common stock, $0.0001 par value per share, outstanding and 21,512,757 shares issued and outstanding of Class C common stock, $0.0001 par value per share.

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PART I—FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements (Unaudited)

System1, Inc. and Subsidiaries

Condensed Consolidated Balance Sheets (Unaudited)

(In thousands, except for par values)

	Successor	
	June 30, 2023	December 31, 2022
ASSETS		
Current assets:		
Cash and cash equivalents	$ 8,603	$ 24,606
Restricted cash, current	11,762	9,074
Accounts receivable, net of allowance for credit losses	62,789	80,927
Prepaid expenses and other current assets	11,976	11,901
Total current assets	95,130	126,508
Restricted cash, non-current	5,825	5,395
Property and equipment, net	5,047	4,022
Internal-use software development costs, net	10,162	6,948
Intangible assets, net	437,323	492,686
Goodwill	515,591	515,591
Operating lease right-of-use assets	5,637	6,484
Other non-current assets	3,498	2,822
Total assets	$ 1,078,213	$ 1,160,456
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 19,942	$ 12,068
Accrued expenses and other current liabilities	77,466	95,447
Protected incentive plan liability, current	12,272	15,436
Deferred revenue	80,461	70,164
Operating lease liabilities, current	2,243	2,149
Debt, net	15,138	15,021
Related-party loan fee payable	2,400	—
Total current liabilities	209,922	210,285
Long-term debt, net	391,888	399,504
Related-party loan	5,000	—
Warrant liability	8,406	7,798
Deferred tax liability	29,851	43,355
Protected incentive plan liability, non-current	24,298	15,824
Operating lease liabilities, non-current	4,778	5,875
Other liabilities	7,125	5,027
Total liabilities	681,268	687,668
Commitments and contingencies (Note 9)		
STOCKHOLDERS' EQUITY		
Class A common stock - $0.0001 par value; 500,000 shares authorized, 93,602 and 91,674 Class A shares issued and outstanding as of June 30, 2023 and December 31, 2022, respectively	9	9
Class C common stock - $0.0001 par value; 25,000 shares authorized, 21,513 and 21,747 Class C shares issued and outstanding as of June 30, 2023 and December 31, 2022, respectively	2	2
Additional paid-in capital	842,350	829,687
Accumulated deficit	(514,809)	(445,301)
Accumulated other comprehensive loss	(270)	(417)
Total stockholders' equity attributable to System1, Inc.	327,282	383,980
Non-controlling interest	69,663	88,808
Total stockholders' equity	396,945	472,788
Total liabilities and stockholders' equity	$ 1,078,213	$ 1,160,456

See notes to unaudited condensed consolidated financial statements.

System1, Inc. and Subsidiaries
Condensed Consolidated Statements of Operations (Unaudited)
(In thousands, except for per share and per unit data)

	Successor				Predecessor
	Three Months Ended June 30, 2023	Three Months Ended June 30, 2022	Six Months Ended June 30, 2023	Period from January 27, 2022 through June 30, 2022	Period from January 1, 2022 through January 26, 2022
Revenue	$ 147,238	$ 219,797	$ 315,092	$ 385,905	$ 52,712
Operating expenses:					
Cost of revenue (excluding depreciation and amortization)	93,882	152,558	214,284	$ 272,942	41,507
Salaries and benefits	43,991	49,511	82,389	97,709	31,181
Selling, general, and administrative	17,735	16,747	34,907	31,835	15,665
Depreciation and amortization	28,052	32,094	57,426	54,022	1,000
Total operating expenses	183,660	250,910	389,006	456,508	89,353
Operating loss	(36,422)	(31,113)	(73,914)	(70,603)	(36,641)
Other (income) expense:					
Interest expense, net	12,342	7,324	23,793	12,100	1,049
Change in fair value of warrant liabilities	2,018	(4,139)	609	9,622	—
Total other expense	14,360	3,185	24,402	21,722	1,049
Loss before income tax	(50,782)	(34,298)	(98,316)	(92,325)	(37,690)
Income tax benefit	(6,605)	(454)	(11,013)	(15,103)	(629)
Net loss	(44,177)	$ (33,844)	$ (87,303)	$ (77,222)	$ (37,061)
Net loss attributable to non-controlling interest	(8,947)	(8,107)	(18,121)	(15,416)	—
Net loss attributable to System1, Inc.	$ (35,230)	$ (25,737)	$ (69,182)	$ (61,806)	$ (37,061)
Net loss per share:					
Basic	$ (0.38)	$ (0.29)	$ (0.74)	$ (0.71)	n/a
Diluted	$ (0.38)	$ (0.33)	$ (0.74)	$ (0.71)	n/a
Shares used in net loss per share calculations:					
Weighted average shares outstanding - basic	93,425	89,701	92,945	86,840	n/a
Weighted average shares outstanding - diluted	93,425	91,182	92,945	86,840	n/a
Basic and diluted net loss per unit	n/a	n/a	n/a	n/a	$ (1.81)
Weighted average units outstanding - basic and diluted	n/a	n/a	n/a	n/a	20,488

See notes to unaudited condensed consolidated financial statements.

System1, Inc. and Subsidiaries
Condensed Consolidated Statements of Comprehensive Loss (Unaudited)
(In thousands)

	Successor				Predecessor
	Three Months Ended June 30, 2023	Three Months Ended June 30, 2022	Six Months Ended June 30, 2023	Period from January 27, 2022 through June 30, 2022	Period from January 1, 2022 through January 26, 2022
Net loss	$ (44,177)	$ (33,844)	$ (87,303)	$ (77,222)	$ (37,061)
Other comprehensive income (loss):					
Foreign currency translation income (loss)	187	(524)	79	(421)	87
Comprehensive loss	$ (43,990)	$ (34,368)	$ (87,224)	$ (77,643)	$ (36,974)
Comprehensive loss attributable to non-controlling interest	(8,897)	(8,046)	(18,087)	(15,355)	—
Comprehensive loss attributable to System1, Inc.	$ (35,093)	$ (26,322)	$ (69,137)	$ (62,288)	$ (36,974)

See notes to unaudited condensed consolidated financial statements.

System1, Inc. and Subsidiaries
Condensed Consolidated Statements of Changes in Stockholders' Equity (Unaudited)
(In thousands)

	Class A Common Stock		Class C Common Stock						
	Shares	Amount	Shares	Amount	Additional Paid-In-Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	Non-Controlling Interest	Total Stockholders' Equity
Successor:									
For the period from January 1, 2023 to March 31, 2023									
BALANCE—December 31, 2022	91,674	$ 9	21,747	$ 2	$ 829,687	$ (445,301)	$ (417)	$ 88,808	$ 472,788
Net loss	—	—	—	—	—	(33,952)	—	(9,174)	(43,126)
Cumulative-effect of adoption of ASU 2016-13	—	—	—	—	—	(326)	—	—	(326)
Issuance of restricted stock, net of forfeitures and shares withheld for taxes	832	—	—	—	(1,730)	—	—	—	(1,730)
Issuance of common stock in connection with settlement of incentive plan	407	—	—	—	1,658	—	—	—	1,658
Conversion of Class C shares to Class A shares	234	—	(234)	—	956	—	—	(956)	—
Increase in tax receivable agreement liability	—	—	—	—	(441)	—	—	—	(441)
Other comprehensive loss	—	—	—	—	—	—	(62)	(46)	(108)
Stock-based compensation	—	—	—	—	6,963	—	—	—	6,963
BALANCE—March 31, 2023	93,147	$ 9	21,513	$ 2	$ 837,093	$ (479,579)	$ (479)	$ 78,632	$ 435,678
Net loss	—	—	—	—	—	(35,230)	—	(8,947)	(44,177)
Issuance of restricted stock, net of forfeitures and shares withheld for taxes	455	—	—	—	(314)	—	—	—	(314)
Other comprehensive income	—	—	—	—	—	—	209	(22)	187
Stock-based compensation	—	—	—	—	5,571	—	—	—	5,571
BALANCE—June 30, 2023	93,602	9	21,513	2	842,350	(514,809)	(270)	69,663	396,945

See notes to unaudited condensed consolidated financial statements.

System1, Inc. and Subsidiaries
Condensed Consolidated Statements of Changes in Stockholders' Equity (Unaudited)
(In thousands)

	Class A Common Stock		Class C Common Stock		Class D Common Stock						
	Shares	Amount	Shares	Amount	Shares	Amount	Additional Paid-In-Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	Non-Controlling Interest	Total Stockholders' Equity
Successor:											
For the period from January 27, 2022 to March 31, 2022											
BALANCE—January 26, 2022	51,750	$ 5	—	$ —	—	$ —	$ 574,003	$ (107,797)	$ —	$ —	$ 466,211
Effect of the Merger	29,017	3	22,077	2	1,450	—	148,359	—	—	198,691	347,055
BALANCE—January 27, 2022	80,767	$ 8	22,077	$ 2	1,450	$ —	$ 722,362	$ (107,797)	$ —	$ 198,691	$ 813,266
Net loss	—	—	—	—	—	—	—	(36,069)	—	(7,309)	(43,378)
Issuance of common stock in connection with the Merger, net of offering costs, underwriting discounts and commissions	930	—	—	—	—	—	661	—	—	—	661
Issuance of common stock in connection with the acquisition of business	2,000	—	—	—	—	—	25,500	—	—	—	25,500
Issuance of market-based restricted stock units upon vesting	—	—	—	—	1,450	—	—	—	—	—	—
Conversion of Class D shares to Class A shares	2,900	1	—	—	(2,900)	—	—	—	—	—	1
Net deferred tax liability resulting from changes in outside basis difference on investment in S1 Holdco, LLC	—	—	—	—	—	—	(2,596)	—	—	—	(2,596)
Other comprehensive income / (loss)	—	—	—	—	—	—	—	—	103	(184)	(81)
Stock-based compensation	—	—	—	—	—	—	31,398	—	—	—	31,398
Distribution to members	—	—	—	—	—	—	—	—	—	(247)	(247)
BALANCE—March 31, 2022	86,597	$ 9	22,077	$ 2	—	$ —	$ 777,325	$ (143,866)	$ 103	$ 190,951	$ 824,524
Net loss	—	—	—	—	—	—	—	(25,737)	—	(8,107)	(33,844)
Exercise of warrants	3,969	—	—	—	—	—	27,989	—	—	—	27,989
Issuance of restricted stock, net of forfeitures and shares withheld for taxes	21	—	—	—	—	—	—	—	—	—	—
Other comprehensive income	—	—	—	—	—	—	—	—	(524)	(14)	(538)
Stock-based compensation	—	—	—	—	—	—	6,995	—	—	—	6,995
Distribution to members	—	—	—	—	—	—	—	—	—	(1,254)	(1,254)
BALANCE—June 30, 2022	90,587	$ 9	22,077	$ 2	—	$ —	$ 812,309	$ (169,603)	$ (421)	$ 181,576	$ 823,872

See notes to unaudited condensed consolidated financial statements.

System1, Inc. and Subsidiaries
Condensed Consolidated Statements of Changes in Members' Deficit (Unaudited)
(In thousands)

	Members' Deficit	Accumulated Other Comprehensive Income (Loss)	Total Members' Deficit
Predecessor:			
For the period January 1, 2022 to January 26, 2022			
BALANCE—January 1, 2022	$ (28,829)	$ 428	$ (28,401)
Net loss	(37,061)	—	(37,061)
Accumulated other comprehensive income	—	87	87
Stock-based compensation expense	23,705	—	23,705
BALANCE—January 26, 2022	$ (42,185)	$ 515	$ (41,670)

See notes to unaudited condensed consolidated financial statements.

System1, Inc. and Subsidiaries

Condensed Consolidated Statements of Cash Flows (Unaudited)

(In thousands)

	Successor		Predecessor
	Six Months Ended June 30, 2023	Period from January 27, 2022 through June 30, 2022	Period from January 1, 2022 through January 26, 2022
Cash flows from Operating Activities:			
Net loss	$ (87,303)	$ (77,222)	$ (37,061)
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation and amortization	57,426	54,022	1,000
Stock-based compensation	31,656	57,470	23,705
Noncash lease expense	878	694	115
Change in fair value of warrants	608	9,622	—
Deferred tax benefits	(13,493)	(22,746)	(816)
Other	3,588	2,860	(9)
Changes in operating assets and liabilities:			
Accounts receivable	16,158	(8,136)	11,118
Prepaids and other assets	(834)	(2,002)	1,069
Accounts payable	7,818	6,535	(67,600)
Accrued expenses and other liabilities	(10,963)	(11,225)	57,488
Long-term earnout liabilities	(15,000)	5,694	—
Deferred revenue	10,297	7,211	311
Other long-term liabilities	516	(31,080)	77
Net cash provided by (used in) operating activities	1,352	(8,303)	(10,603)
Cash flows from Investing Activities:			
Purchases of property and equipment	(1,581)	(2,310)	—
Capitalized software development costs	(3,487)	(3,497)	(441)
Acquisition of businesses, net of cash acquired	—	(444,074)	—
Net cash used in investing activities	(5,068)	(449,881)	(441)
Cash flows from Financing Activities:			
Proceeds from related-party loan	39,000	—	—
Repayment of related-party loan	(34,000)	—	—
Proceeds from term loan and line of credit	—	449,000	—
Repayment of term loan	(10,000)	(177,488)	—
Payments for financing costs	—	(24,845)	—
Payment of acquisition holdback	(1,250)	(1,715)	—
Taxes paid related to net settlement of stock awards	(3,052)	—	—
Redemptions of Class A common stock	—	(510,469)	—
Proceeds from warrant exercises	—	5,027	—
Cash received from the Backstop	—	246,484	—
Taxes paid on behalf of S1 Holdco partnership members	(66)	(1,501)	—
Net cash used in financing activities	(9,368)	(15,507)	—
Effect of exchange rate changes in cash, cash equivalent and restricted cash	199	604	(19)
Net decrease in cash, cash equivalents and restricted cash	(12,885)	(473,087)	(11,063)
Cash and cash equivalents and restricted cash, beginning of the period	39,075	517,553	48,639
Cash and cash equivalents and restricted cash, end of the period	$ 26,190	$ 44,466	$ 37,576
Reconciliation of cash, cash equivalents and restricted cash to the Condensed Consolidated Balance Sheets:			
Cash and cash equivalents	$ 8,603	$ 37,442	$ 36,833
Restricted cash	17,587	7,024	743
Total cash, cash equivalents and restricted cash	$ 26,190	$ 44,466	$ 37,576
Supplemental cash flow information:			
Cash paid for operating lease liabilities	$ —	$ 563	$ 175
ROU assets obtained in exchange for operating lease liabilities	$ —	$ 2,064	$ 7,987
Capitalized assets financed by accounts payable	$ 53	$ —	$ —
Stock-based compensation included in capitalized software development costs	$ 1,124	$ —	$ —
Settlement of incentive plan through issuance of common stock	$ 1,658	$ —	$ —
Equity issuance to settle intercompany loan	$ —	$ —	$ 941
Deferred consideration for acquisition	$ —	$ 7,059	$ —

See notes to unaudited condensed consolidated financial statements.

1. ORGANIZATION AND DESCRIPTION OF BUSINESS

System1, Inc. and subsidiaries (“System1” or the “Company”) operates an omnichannel customer acquisition platform, delivering high-intent customers to advertisers and selling antivirus software packages to end user customers.

The Company provides its omnichannel customer acquisition platform services through its proprietary responsive acquisition marketing platform (“RAMP”). Operating seamlessly across major advertising networks and advertising category verticals to acquire users, RAMP allows the Company to monetize such users through its relationships with third party advertisers and advertising networks (“Advertising Partners”). Through RAMP, third party advertising platforms and publishers (“Network Partners”) send user traffic to, and monetize user traffic on, the Company’s owned and operated websites. RAMP operates across the Company’s network of owned and operated websites and related products, allowing it to monetize user traffic that it sources from various acquisition marketing channels, including Google, Facebook, Taboola and Zemanta.

The Company, through Total Security Limited ("Protected"; formerly Protected.net Group Limited) , also provides antivirus software solutions, offering customers a single packaged solution that provides protection and reporting to the end user. The Company delivers its antivirus software solutions directly to end-user customers around the world. The antivirus software solutions product offering comprises a core security package with varying levels of extra protection based on a customer's specific needs. The software is sold in either a monthly or annual subscription predominantly through its flagship products TotalAV and TotalAdBlock.

Going Concern

Starting in the third quarter of 2022 and continuing into 2023, the Company experienced declining cash flows and financial performance as a result of deteriorating macroeconomic conditions, resulting in reductions in both advertiser and overall consumer demand for the Company's marketing services. In response to these conditions, the Company obtained additional financing in the second quarter of 2023 as previously disclosed which was expected to provide the Company sufficient liquidity to manage through the current business environment. However, subsequent to the quarter ended June 30, 2023, the Company has experienced increased customer acquisition costs in addition to the loss of a Network Partner, both of which have further negatively impacted the Company’s future cash forecasts, and may negatively impact the Company’s forecasted compliance with the maximum leverage ratio covenant of the Term Loan (defined in Note 10) in the latter half of 2023. As of June 30, 2023, the Company had cash on hand of $8,603, an accumulated deficit of $514,809, and generated cash flows from operations of $ 1,352 for the six months ended June 30, 2023. The Company has principal and interest payments due of approximately $15,000 per quarter, and as of the date of this filing, the remaining available capacity under the 2023 Revolving Note (defined in Note 14) was $10,000.

The declining cash flows and financial performance raise substantial doubt regarding the Company's ability to continue as a going concern for a period of one year following the date that these condensed consolidated financial statements are issued. The Company has developed plans for cost reduction measures, including some already implemented, to address the Company’s forecasted reduction to future cash flows and reduce the Company’s leverage ratio. The Company is also evaluating strategic alternatives, including but not limited to raising additional capital by selling equity or debt securities, seeking incremental financing from related parties or financial institutions, or by other means. However, the Company does not have definitive plans or agreements in place, and as a result, the Company cannot provide assurances that additional measures will be available on acceptable terms or at all. To the extent the Company's financial performance does not improve or the Company's plans are not successful or finalized, the Company may have insufficient available cash balances to fund their operations by the end of the calendar year.

While the Company will seek to expeditiously implement such plans, there can be no assurance that the plans will be sufficient to maintain appropriate liquidity to support the Company’s on-going operations or maintain compliance with debt covenants. Accordingly, the Company believes that there is substantial doubt about its ability to continue as a going concern for the twelve-month period following the date of this filing.

The condensed consolidated financial statements do not include any adjustments that might result from the outcome of these uncertainties. Accordingly, the condensed consolidated financial statements have been prepared on a basis that assumes the Company will continue as a going concern and which contemplates the realization of assets and satisfaction of liabilities and commitments in the ordinary course of business.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation, Principles of Consolidation and Summary of Significant Accounting Policies

The Company was a special purpose acquisition company originally incorporated as a Cayman Islands exempted company on February 11, 2020 under the name Trebia Acquisition Corp. (“Trebia”). The Company was formed for the purpose of effecting a merger, share exchange, asset acquisition, share purchase, reorganization or similar business combination with one or more businesses. On January 27, 2022, the Company consummated a business combination (the "Merger"), which resulted in the acquisition of S1 Holdco and System1 SS Protect Holdings, Inc. As a result of the Merger, the results of operations, financial position and cash flows of the Predecessor and Successor may not be directly comparable.

The Company was deemed the accounting acquirer in the Merger based on an analysis of the criteria outlined in Accounting Standards Codification (“ASC”) 805, *Business Combinations* and S1 Holdco was deemed to be the predecessor entity. Accordingly, the historical financial statements of S1 Holdco became the historical financial statements of the Company, upon the consummation of the Merger. As a result, the financial statements included in this report reflect (i) the historical operating results of S1 Holdco prior to the Merger ("Predecessor") and (ii) the combined results of the Company, including S1 Holdco and Protected following the closing of the Merger ("Successor"). The accompanying financial statements include a Predecessor period, which was the period January 1, 2022 through January 26, 2022, concurrent with the Merger and Successor periods from January 27, 2022 through June 30, 2022, and thereafter. A black-line between the Successor and Predecessor periods has been placed in the condensed consolidated financial statements and in the tables to the notes to the condensed consolidated financial statements to highlight the lack of comparability between these two periods as the Merger resulted in a new basis of accounting for the Company.

The accompanying condensed consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (“U.S. GAAP”). The accompanying condensed consolidated financial statements include the accounts of System1, Inc. and its subsidiaries for the Successor periods, and S1 Holdco for the Predecessor period. All intercompany accounts and transactions have been eliminated in the consolidation of the financial statements. The condensed consolidated financial statements have been prepared by the Company and are unaudited, pursuant to the rules and regulations of the United States Securities and Exchange Commission (“SEC”). Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. GAAP have been condensed or omitted pursuant to such SEC rules and regulations. The interim condensed consolidated financial statements included herein reflect all adjustments (consisting of normal recurring adjustments) which are, in the opinion of management, necessary for a fair statement of the financial position, results of operations and cash flows for the interim periods presented. The condensed consolidated statements of operations for the three and six months ended June 30, 2023 (Successor), the three months ended June 30, 2022 (Successor), the period from January 1, 2022 through January 26, 2022 (Predecessor) and for the period from January 27, 2022 through June 30, 2022 (Successor) are not necessarily indicative of the results to be anticipated for the entire year ending December 31, 2023 or thereafter.

Certain prior period amounts in the condensed consolidated financial statements have been reclassified to conform with the current period presentation. These reclassifications had no effect on the results of operations or financial position for any period presented.

(Dollars, number of shares and number of units in thousands, except for per share or per unit amounts)

Adoption of Recent Accounting Pronouncements

On January 1, 2023, the Company adopted ASU No. 2016-13, "Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Loss on Financial Instruments". Accordingly, upon adoption of this new standard, the Company recorded an allowance for credit losses of $327, with a corresponding cumulative adjustment to the beginning balance of accumulated deficit in the first quarter of fiscal 2023.

Risks and Concentrations

The Company is subject to certain business and operational risks, including competition from alternative technologies, as well as dependence on key Advertising Partners, key employees, key contracts, and growth to achieve its business and operational objectives.

The following table illustrates the level of concentration as a percentage of total revenue for the Company's key Advertising Partners:

	Successor				Predecessor
	Three Months Ended June 30, 2023	Three Months Ended June 30, 2022	Six Months Ended June 30, 2023	Period from January 27, 2022 through June 30, 2022	Period from January 1, 2022 through January 26, 2022
Google	55 %	69 %	60 %	71 %	88 %
Microsoft	2 %	3 %	2 %	3 %	4 %

Accounts receivable are primarily derived from Advertising Partners located within the United States. As of June 30, 2023, two of the Company’s largest Advertising Partners, Google and Yahoo, represented 65% and 13%, respectively, of the Company’s accounts receivables balance. As of December 31, 2022, these two Advertising Partners represented 68% and 11%, respectively, of the Company’s accounts receivable balance.

Use of Estimates

The preparation of these condensed consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements, and the reported amounts of revenue and expenses during the reporting period.

Significant estimates and assumptions reflected in these condensed consolidated financial statements include, but are not limited to: (1) valuation of goodwill, acquired intangible assets and long-lived assets, (2) valuation and recognition of the Company's stock-based compensation awards, and (3) income taxes. Significant estimates affecting the condensed consolidated financial statements have been prepared on the basis of the most current and best available information, including historical experience, known trends and other market-specific or other relevant factors that the Company believes to be reasonable. Management evaluates its estimates, as there are changes in circumstances, facts and experience. Changes in estimates are recorded in periods which they become known. However, actual results from the resolution of such estimates and assumptions may vary from those used in the preparation of the condensed consolidated financial statements.

Concentration of Credit Risk

Cash is deposited with high-credit-quality financial institutions and, at times, such balances with any one financial institution may exceed the insurance limits of the prevailing regulatory body. Historically, the Company has not experienced any losses related to these cash balances and believes that there is minimal risk of expected future losses. However, there can be no assurance that there will not be losses on these deposits.

3. MERGER

On June 28, 2021, the Company entered into a Business Combination Agreement (as amended on November 30, 2021, January 10, 2022 and January 25, 2022) (the “Business Combination Agreement” or "BCA"), by and among S1 Holdco, Trebia, and Protected (collectively, the “Companies”). On January 26, 2022 (the “Closing Date”), the Company consummated the business combination (the "Merger") pursuant to the Business Combination Agreement. Following the consummation of the Merger, the combined company is organized via an “Up-C” structure, in which substantially all of the assets and business operations of System1 are held by S1 Holdco. The combined Companies’ business continues to operate through the subsidiaries of S1 Holdco and Protected. Additionally, Trebia’s ordinary shares and public warrants ceased trading on the New York Stock Exchange ("NYSE"), and System1 Inc.'s Class A common stock and the Public Warrants began trading on the NYSE on January 28, 2022 under the symbols “SST” and “SST.WS,” respectively.

The consideration paid to the existing equity holders of S1 Holdco and Protected in connection with the Merger consisted of the following:

- Cash;
- Class A common stock;
- Class C common stock;
- Replacement Awards.

The aggregate cash consideration was $440,155.

The aggregate equity consideration paid and/or retained for S1 Holdco Class B Units was $ 610,144, consisting of (a) the aggregate equity consideration payable under the Business Combination Agreement, consisting of shares of Class A common stock and Replacement Awards, and (b) the aggregate Class B Units in S1 Holdco retained by S1 Holdco equity holders at the Closing.

The fair value of the Class A common stock was determined by utilizing the transaction closing price per share per the BCA of $ 10.00 and a discount of 10%, as the shares were not immediately available for sale upon issuance and this restriction is viewed to be a function of the security characteristics.

Additionally, the aggregate Class B units in S1 Holdco retained by S1 Holdco equity holders at the Closing Date resulted in a non-controlling interest. The 22,077 Class B units in S1 Holdco and the corresponding Class C common stock in the Company were determined to have an estimated value of $198,691. As the Class B units in S1 Holdco together with the corresponding shares of the Company's Class C common stock are exchangeable for shares of Class A common stock on a one-for-one basis, the fair value was determined using the same method as for the shares of Class A common stock, utilizing the transaction closing price of $10.00 and a discount of 10% (as the units and the corresponding shares of Class C common stock were not immediately available for sale upon issuance and this restriction is viewed to be a function of the security characteristics). The fair value of $198,691 was included in non-controlling interest on the accompanying condensed consolidated balance sheet and condensed consolidated statements of changes in stockholders' equity.

In connection with the Merger, System1 and Cannae Holdings, Inc. (“Cannae”), an investor in the Sponsor of Trebia, entered into a backstop agreement (the “Backstop Agreement”) on June 28, 2021, as amended on January 10, 2022, whereby Cannae agreed, to subscribe for up to 25,000 shares of Trebia Class A common stock in order to fund up to $250,000 of redemptions by shareholders of Trebia. See discussion below regarding the Amended and Restated Sponsor Agreement, which was amended in conjunction with the Backstop Agreement. As a result of shareholder redemptions, Cannae provided $246,484 of the cash used to fund the Closing Cash Consideration pursuant to its obligations under the Backstop Agreement and in exchange received 24,648 shares of Class A common stock ("Backstop shares").

Additionally, pursuant to the Backstop Agreement, the Selling Shareholders (i.e., certain shareholders of S1 Holdco and Protected prior to the Merger) agreed that, in the event shareholders of Trebia requested redemption of Trebia outstanding equity immediately prior to the Merger in excess of a certain dollar value threshold, certain equity holders of S1 Holdco and Protected would reduce their cash consideration and proportionally increase their equity consideration for the Merger, which is referred to as the “Seller Backstop Election”. In the event that the Seller Backstop Election was made, the Sponsors would forfeit their shares to allow the Company to then issue shares to the Selling Shareholders. The Seller Backstop Election was triggered and, as a result, the Sponsors forfeited 930 shares of Trebia Class B ordinary shares which were converted at time of Merger, at a one-to-one ratio, into shares of Class A common stock of System1 and delivered to the various selling shareholders of S1 Holdco, collectively referred to as the “Sponsor Promote Shares”. The total consideration amount, in a combination of cash and equity consideration, did not change from the amount agreed in the Business Combination Agreement due to this Seller Backstop Election. The Company recorded $7,706 in Salaries and benefits expense and $ 661 in Selling, general and administrative expense for Sponsor Promote Shares during the period January 27, 2022 through March 31, 2022 (Successor).

In connection with the execution of the Business Combination Agreement and the Backstop Agreement, on June 28, 2021, as amended on January 10, 2022, the sponsors of Trebia entered into the Amended and Restated Sponsor Agreement whereby the sponsors agreed to forfeit up to 2,600 shares of Trebia Class B common stock in order for the Company to then issue the shares to Cannae (“Backstop forfeiture shares”), in exchange for Cannae entering into the Backstop Agreement. On January 27, 2022, based upon the final backstop funding provided by Cannae, the sponsors forfeited 2,533 shares of Trebia Class B shares, after which the Company then issued 2,533 shares of Class A common stock to Cannae. Trebia recorded a forward purchase liability of $25,336 immediately prior to the Merger, representing the fair value of the Backstop shares and the Backstop forfeiture shares.

In accordance with the Amended and Restated Sponsor Agreement entered into concurrently with the Business Combination Agreement, the Company issued 1,450 Class D shares to the Trebia sponsors in exchange for 1,450 Trebia Class B shares ("Sponsor RSA's"). The difference in the fair value of the two was treated as a capital contribution. The founders of S1 Holdco and Protected were also issued 1,450 Class D shares ("Seller RSUs"). Further, in connection with the Merger, the Company also effected an incentive plan for Protected business.

Concurrently with the consummation of the Merger, System1 entered into a tax receivable agreement with the minority holders of S1 Holdco, (the “Tax Receivable Agreement” or "TRA"), pursuant to which, among other things, the parties to the Tax Receivable Agreement have agreed to the allocation and payment of 85% of the actual savings, if any, in U.S. federal, state and local income tax that System1 may realize as a result of certain tax benefits (if any) related to the transactions contemplated by the Business Combination Agreement and future exchanges of Class B Units in S1 Holdco (together with the corresponding shares of the Company’s shares of Class C common stock) in exchange for shares of the Company’s Class A common stock. As of the Closing Date, the fair value of obligations under the TRA were determined to be zero as any tax savings were uncertain. The TRA is contingent consideration and subsequent changes in fair value of the contingent liability are recognized in earnings.

The Company adopted ASU No. 2021-08, *Business Combinations: Contract Assets & Liabilities* on January 1, 2022 and accordingly, has recorded contract assets and contract liabilities acquired as part of the Merger based on what the Company would have recorded under ASC 606, *Revenue from Contracts with Customers,* as of the acquisition date, as if the Company had entered into the original contract at the same date and on the same terms as S1 Holdco and Protected.

The Merger has been accounted for as a business combination using the acquisition method of accounting. The total purchase price was allocated to the tangible and identifiable intangible assets acquired and liabilities assumed based on their respective fair values on the acquisition date.

(Dollars, number of shares and number of units in thousands, except for per share or per unit amounts)

The purchase consideration was allocated to the following assets and liabilities:

	Amount
Tangible assets acquired and liabilities assumed:	
Cash and marketable securities	$ 68,748
Accounts receivable	79,086
Prepaid expenses	7,807
Income tax receivable	4,566
Property, plant & equipment, net	1,551
Other assets	6,950
Accounts payable	(9,798)
Deferred revenue	(60,768)
Accrued expenses and other current liabilities	(110,004)
Income tax payable	(2,091)
Notes payable	(172,038)
Deferred tax liabilities	(138,613)
Other liabilities	(8,474)
Total tangible assets acquired and liabilities assumed	(333,078)
Intangible assets	562,100
Goodwill	821,277
Net assets acquired	$ 1,050,299
Consideration:	
Cash	$ 440,155
Equity	411,453
Total consideration attributable to System1	851,608
Total consideration attributable to non-controlling interest	198,691
Total consideration	$ 1,050,299

The intangible assets as of the closing date of the acquisition included:

	Amount	Weighted Average Useful Life (in Years)
Trademarks	$ 246,400	10
Customer relationships	119,700	4
Technology	196,000	4
Total	$ 562,100	

The fair value of the intangible assets acquired was determined using income-based approach methodologies. Intangible assets are amortized over their estimated economic useful lives using a straight-line method, which approximates the pattern in which the economic benefits are consumed. Customer relationships are amortized on an accelerated basis. To determine the amortization period for each of the customer relationships assets and to evaluate the pattern of usage of economic benefits, the Company performed a customer attrition analysis of the Company's customer relationships to estimate the attrition rate and consequently the life expectancy for the existing customer relationships.

Key assumptions used in the valuation of intangible assets are below:

(Dollars, number of shares and number of units in thousands, except for per share or per unit amounts)

Trademarks – The Company valued trademarks using the relief-from-royalty method under the income-based approach. Key assumptions include forecasted revenue, an estimated royalty rate applicable to the trademarks, and a discount rate.

Customer relationships – The Company valued customer relationships using an excess-earnings method utilizing distributor inputs. Key assumptions include customer attrition rate, revenue growth rate, existing customer revenue, deferred revenue, and a discount rate.

Technology – The Company valued technology using the excess-earnings method utilizing company-specific inputs. Key assumptions include forecasted revenue, technology migration rate and a discount rate.

The goodwill arising from the acquisition consists largely of the expected synergies from combining operations as well as the value of the workforce. Goodwill is not deductible for tax purposes.

Unaudited Pro Forma Information

The following table provides unaudited pro forma information as if the Merger and other 2022 acquisitions (r efer to Note 4—*ACQUISITIONS*) occurred as of January 1, 2021. The unaudited pro forma information reflects adjustments for additional amortization resulting from the fair value adjustments to assets acquired and liabilities assumed, adjustments for alignment of accounting policies, adjustments for transaction expenses, adjustments for certain stock-based compensation and equity related expenses incurred as a result of the transaction and the resulting tax effects, as if the Merger and acquisitions of Answers, CouponFollow and RoadWarrior occurred January 1, 2021. The pro forma results do not include any anticipated cost synergies or other effects of the merged companies. Accordingly, pro forma amounts are not necessarily indicative of the results that actually would have occurred had the acquisitions been completed on the dates indicated, nor is it indicative of the future operating results of the combined company.

	Three months ended June 30, 2022	Six months ended June 30, 2022
Pro forma revenue	$ 219,912	$ 455,836
Pro forma net (loss)	$ (20,474)	$ (25,436)

4. ACQUISITIONS

Answers Holdings, Inc.

On May 4, 2022, the Company acquired the assets of Answers Holdings, Inc. and its subsidiaries, collectively ("Answers") for total cash consideration of $4,632. The acquisition of Answers constitutes a business combination under ASC 805, *Business Combinations*.

This acquisition expands the Company's portfolio of Owned & Operated Advertising publishing sites and search destinations to include a destination for higher education and lifelong learning content. The results of Answers' operations as of and after the date of acquisition have been included in the Company's condensed consolidated financial statements. The operating results of Answers are reported within the Owned and Operated Advertising segment.

The purchase consideration was allocated to the following assets and liabilities:

(Dollars, number of shares and number of units in thousands, except for per share or per unit amounts)

		Amount
Assets acquired and liabilities assumed:		
Working capital	$	32
Trademark - 10 years weighted average useful life		1,100
Goodwill		3,500
Net assets acquired	$	4,632
Total consideration:		
Cash	$	4,632

The goodwill arising from the acquisition consists largely of the expected synergies from combining operations, and is deductible for tax purposes over 15 years. The Company incurred $93 in transaction costs related to the acquisition.

Trademark – The Company valued the trademark using the relief-from-royalty method under the income approach. Key assumptions include forecasted revenue, an estimated royalty rate applicable to the trademark and a discount rate.

NextGen Shopping, Inc.

On March 4, 2022, the Company acquired NextGen Shopping, Inc. (d/b/a “CouponFollow”) for total cash consideration of $ 75,087, of which $16,446 was deferred, $5,600 was held-back, and $25,500 related to the fair value of 2,000 shares of Class A common stock issued. The fair value of the shares of Class A common stock was determined by utilizing the closing price per share of the Company's Class A common stock listed on the NYSE as of March 3, 2022, and a discount rate of 7.5%, as the shares were not immediately available for sale upon issuance, and this restriction was deemed to be a function of the security characteristics. The deferred consideration of $16,446 was paid during the three months ended June 30, 2022. The held-back consideration amount will become payable eighteen months subsequent to the acquisition date, subject to the Company's satisfaction of any potential post-closing purchase price adjustments and indemnification claims. The cash payment included the transaction costs of $3,129 that the Company paid on behalf of CouponFollow in connection with the closing of the transaction. The acquisition of CouponFollow constitutes a business combination under ASC 805.

In conjunction with this acquisition, the Company also committed to pay postcombination compensation of $ 8,500, which is payable in cash and subject to continued services from certain individuals of CouponFollow. Separately, in conjunction with the acquisition, the Company entered into the CouponFollow Incentive Plan, providing up to $10,000 of postcombination compensation which is payable in stock or cash at the option of the Company, and subject to continued service from certain individuals, and up to $25,000 which is payable in stock or cash at the option of the Company contingent upon achieving certain financial thresholds and the continued employment of certain key individuals of CouponFollow.

This acquisition leverages CouponFollow’s reputation, software and large organic traffic to vertically integrate with the Company’s RAMP platform and generate paid traffic for shopping-related products. The results of CouponFollow’s operations from the date of acquisition have been included in the Company’s condensed consolidated financial statements. The operating results of CouponFollow are reported within the Owned and Operated Advertising segment.

The total purchase price was allocated to the assets acquired and liabilities assumed based on their respective fair values on the acquisition date.

The purchase consideration was allocated to the following assets and liabilities:

(Dollars, number of shares and number of units in thousands, except for per share or per unit amounts)

		Amount
Cash and cash equivalents	$	21,232
Accounts receivable		5,860
Other current assets		446
Accounts payable		(116)
Accrued expenses and other current liabilities		(118)
Income tax payable		(197)
Deferred tax liabilities		(10,895)
Trademark - 10 years weighted average useful life		38,100
Software - 4 years weighted average useful life		4,100
Goodwill		42,175
Net assets acquired	$	100,587
Consideration:		
Cash	$	75,087
Equity		25,500
Total consideration	$	100,587

The goodwill arising from the acquisition consists largely of the expected synergies from combining operations as well as the value of the workforce. The goodwill is not deductible for tax purposes. The Company incurred $813 in transaction costs related to the acquisition.

Trademark – The Company valued the trademark using the relief-from-royalty method under the income approach. Key assumptions include forecasted revenue, an estimated royalty rate applicable to the trademarks and a discount rate.

Software – Acquired software technology was valued using the excess-earnings method utilizing company-specific inputs. Key assumptions include forecasted revenue, an estimated royalty rate applicable to the software and a discount rate.

RoadWarrior, LLC

On February 9, 2022, the Company acquired the assets of RoadWarrior, LLC (“RoadWarrior”) for total cash consideration of $ 19,636. The acquisition of RoadWarrior constitutes a business combination under ASC 805. The acquisition expands the Company’s Mapquest.com website technology, and provides additional functionality for customers centered around route planning for delivery drivers and teams. The results of RoadWarrior’s operations as of and after the date of acquisition have been included in the Company’s condensed consolidated financial statements. The operating results of RoadWarrior are reported within the Owned and Operated Advertising segment prospectively from the date of acquisition.

The total purchase price was allocated to the assets acquired and liabilities assumed based on their respective fair values on the acquisition date.

The purchase consideration was allocated to the following assets and liabilities:

(Dollars, number of shares and number of units in thousands, except for per share or per unit amounts)

	Amount
Working capital	$ 155
Trademark - 10 years weighted average useful life	2,200
Software - 4 years weighted average useful life	1,000
Customer relationships - 3 years weighted average useful life	1,300
Goodwill	14,981
Net assets acquired	$ 19,636
Total consideration	
Cash	$ 19,636

The goodwill arising from the acquisition consists largely of the expected synergies from combining operations as well as the value of the workforce. The goodwill is deductible for tax purposes over 15 years. The Company incurred $308 in transaction costs related to the acquisition.

Trademark – The Company valued the trademark using the relief-from-royalty method under the income approach. Key assumptions include forecasted revenue, an estimated royalty rate applicable to the trademarks and a discount rate.

Software – Acquired software technology was valued using the excess-earnings method utilizing company-specific inputs. Key assumptions include forecasted revenue, an estimated royalty rate applicable to the software and a discount rate.

Customer relationships – The Company valued customer relationships using an excess-earnings method utilizing distributor inputs. Key assumptions include customer attrition rate, revenue growth rate, existing customer revenue, deferred revenue, and a discount rate.

5. GOODWILL, INTERNAL-USE SOFTWARE DEVELOPMENT COSTS, NET, AND INTANGIBLE ASSETS, NET

Goodwill

Goodwill by reportable segments was as follows:

	Partner Network	Subscription	Total
Goodwill at December 31, 2022 and June 30, 2023	$ 82,407	$ 433,184	$ 515,591

During the six months ended June 30, 2023, the Company determined there were no triggering events. As such, no quantitative assessment for impairment was required, and accordingly, the Company did not record any goodwill impairment charges during the six months ended June 30, 2023.

Internal-use software development costs and other intangible assets

Internal-use software development costs and intangible assets, net consisted of the following:

(Dollars, number of shares and number of units in thousands, except for per share or per unit amounts)

	June 30, 2023 (Successor)		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Total internal-use software development costs	$ 11,187	$ (1,025)	$ 10,162
Intangible assets, net:			
Trademarks and trade names	$ 287,853	$ (40,631)	$ 247,222
Developed technology	196,224	(69,839)	126,385
Customer relationships	121,000	(60,682)	60,318
Software	5,100	(1,702)	3,398
Total intangible assets, net	$ 610,177	$ (172,854)	$ 437,323

	December 31, 2022 (Successor)		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Total internal-use software development costs	$ 7,206	$ (258)	$ 6,948
Intangible assets, net:			
Trademarks and trade names	$ 287,857	$ (26,241)	$ 261,616
Developed technology	196,128	(45,322)	150,806
Customer relationships	121,000	(44,770)	76,230
Software	5,100	(1,066)	4,034
Total intangible assets, net	$ 610,085	$ (117,399)	$ 492,686

The internal-use software development costs include capitalized costs not ready for its internal use of $ 5,032 and $4,955 as of June 30, 2023 (Successor) and December 31, 2022 (Successor), respectively.

Amortization expense associated with the Company’s intangible assets and internal-use software development costs was as follows:

	Successor				Predecessor
	Three Months Ended June 30, 2023	Three Months Ended June 30, 2022	Six Months Ended June 30, 2023	Period from January 27, 2022 through June 30, 2022	Period from January 1, 2022 through January 26, 2022
Amortization expense for internal-use software development	$ 839	$ 78	$ 1,396	$ 143	$ 355
Amortization expense for intangible assets	$ 26,898	$ 31,867	$ 55,456	$ 53,611	$ 629

No impairment of internal-use software development cost or intangible assets was identified for any of the periods presented.

6. ACCRUED EXPENSES AND OTHER CURRENT LIABILITIES

(Dollars, number of shares and number of units in thousands, except for per share or per unit amounts)

	Successor	
	June 30, 2023	December 31, 2022
Accrued payroll and related benefits	$ 11,245	$ 12,890
Accrued marketing expenses	23,152	38,911
Accrued professional fees	1,131	2,706
VAT tax liability	3,386	4,343
Accrued tax liability	1,278	1,176
Holdback liability	5,775	6,885
Accrued revenue share	20,587	16,921
Other liabilities	10,912	11,615
Accrued expenses and other current liabilities	$ 77,466	$ 95,447

7. DEFERRED REVENUE

Deferred revenue activities were as follows:

	Deferred Revenue
January 1, 2022 (Predecessor)	$ 1,971
Additions	620
Revenue recognized	(309)
January 26, 2022 (Predecessor)	$ 2,282

	Deferred Revenue
January 27, 2022 (Successor)	$ —
Additions*	141,941
Revenue recognized	(73,573)
June 30, 2022 (Successor)	$ 68,368

	Deferred Revenue
January 1, 2023 (Successor)	$ 70,164
Additions	113,392
Revenue recognized	(103,095)
June 30, 2023 (Successor)	$ 80,461

* Includes $61,156 from the 2022 acquisitions.

During the periods January 1, 2022 through January 26, 2022 (Predecessor) and January 27, 2022 through June 30, 2022 (Successor), and the six months ended June 30, 2023 (Successor), $309, $0, and $52,659, respectively, of the deferred revenue recognized existed at the beginning of each respective period.

We expect to recognize revenue related to the remaining performance obligations within the next twelve months.

8. INCOME TAXES

(Dollars, number of shares and number of units in thousands, except for per share or per unit amounts)

The Company is the sole managing member of S1 Holdco and, as a result, consolidates the financial results of S1 Holdco. S1 Holdco is treated as a partnership for U.S. federal and most applicable state and local income tax purposes. As a partnership, S1 Holdco is not subject to U.S. federal and certain state and local income taxes. Any taxable income or loss generated by S1 Holdco is passed through to and included in the taxable income or loss of its members, including the Company, on a pro rata basis. The Company is subject to U.S. federal income taxes, in addition to state and local income taxes with respect to its allocable share of any taxable income or loss of S1 Holdco, as well as any stand-alone income or loss generated by the Company.

The following table presents the Company's Income tax benefit and the effective income tax rate:

	Successor				Predecessor
	Three Months Ended June 30, 2023	**Three Months Ended June 30, 2022**	**Six Months Ended June 30, 2023**	**Period from January 27, 2022 through June 30, 2022**	**Period from January 1, 2022 through January 26, 2022**
Income tax benefit	$ (6,605)	$ (454)	$ (11,013)	$ (15,103)	$ (629)
Effective tax rate	13 %	1 %	11 %	16 %	2 %

The provision for income taxes differs from the amount of income tax computed by applying the U.S. statutory federal tax rate of 21% to the loss before income taxes due to the exclusion of non-controlling loss, effects of predecessor flow through income allocations, state taxes, foreign rate differential, non-deductible expenses, increase to the valuation allowance related to unrealizable deferred tax assets, outside basis adjustments, and Global Intangible Low-taxed Income. As of June 30, 2023, the Company had a full valuation allowance on its U.S. federal and state net deferred tax assets as it was more likely than not that those deferred tax assets would not be realized.

During the six months ended June 30, 2023, and the periods from January 1, 2022 through January 26, 2022, and from January 27, 2022 through June 30, 2022, inclusive of interest, no payments were made to the parties to the Tax Receivable Agreement. The total amount of Tax Receivable Agreement Payments due under the Tax Receivable Agreement was $1,477 and $1,036 as of June 30, 2023 and December 31, 2022, respectively.

9. COMMITMENTS AND CONTINGENCIES

In June 2023, S1 Holdco entered into a multi-year agreement with a web services provider whereby the Company is contractually obligated to spend $15,000 between July 2023 and June 2026. As of June 30, 2023 (Successor), the Company remains contrac tually obligated to spend $14,070 towards this commitment.

As of June 30, 2023, the Company had various non-cancelable operating lease commitments for office space which have been recorded as Operating lease liabilities.

Litigation

The Company is subject to various legal proceedings and claims that arise in the ordinary course of business. The Company believes the ultimate liability, if any, with respect to these actions will not materially affect the consolidated financial position, results of operations, or cash flows reflected in the condensed consolidated financial statements. There can be no assurance, however, that the ultimate resolution of such actions will not materially or adversely affect the Company's condensed consolidated financial position, results of operations, or cash flows. The Company accrues for losses when the loss is deemed probable and the liability can reasonably be estimated.

In July 2021, System1 OpCo (f/k/a System1, LLC) received initial correspondence from counsel for a United Kingdom-based marketing research company and its United States subsidiary (collectively, the "Demanding Group") alleging trademark infringement (i) based on its use of the "SYSTEM1" trade name and mark in the United States, and (ii) subsequently based on its use of the "SYSTEM1" trade name and mark in the United Kingdom. The correspondence demanded that System1 OpCo cease and desist from using the "SYSTEM1" name and mark, and even though the Company received similar correspondence from the Demanding Group regarding its alleged infringing use of the SYSTEM1 trade name and mark in the United Kingdom, no lawsuit was ever filed in the United Kingdom. In September 2021, the Demanding Group filed a lawsuit in the United States District Court for the Southern District of New York (the “Infringement Suit”), alleging (i) trademark infringement, (ii) false designation of origin, (iii) unfair competition and (iv) certain violations of New York business laws, seeking, among other things, an injunction, disgorgement of profits, actual damages and attorneys’ fees and costs. The Company believes that the Demanding Group’s infringement and other allegations and claims set forth in the Infringement Suit would have been subject to a laches defense, among other defenses. The parties entered into a Co-Existence and Settlement Agreement in June 2023 in which the parties have agreed to co-exist with their current usage of the “System1” mark in their respective business operations with certain requirements and other conditions, and includes the payment of a fixed amount to the Demanding Party over the course of seventeen (17) months (the “Settlement Agreement”). Pursuant to the Settlement Agreement, the Infringement Suit has been dismissed with prejudice. The amount accrued as of June 30, 2023 for the loss is consistent with the terms of the Settlement Agreement and is considered immaterial.

In March 2023, the Company received a demand letter from counsel for Alta Partners, LLC (“Alta”), which purports to be a holder of certain Public Warrants of the Company (“Demand Letter”). The Demand Letter alleges, among other claims, that the Company breached the terms of the Warrant Agreement, and that Alta is entitled to approximately $5,700 in damages, plus prejudgment interest, as a result. On April 20, 2023, counsel for the Company responded to the Demand Letter, denying that any breach occurred or that Alta is entitled to any damages. In June 2023, counsel for Alta sent the Company a draft complaint (the “Complaint”) alleging substantially the same claims as those set forth in Alta’s Demand Letter. The Complaint has not been filed as of June 30, 2023. The Company continues to deny liability with respect to the claims set forth in the Demand Letter and the Complaint, and intends to defend itself vigorously against any such claims. The Company has not accrued a loss for this matter as a loss, or range of losses, is not reasonably estimable as of June 30, 2023.

10. DEBT, NET

In connection with the Merger, Orchid Merger Sub II LLC (a subsidiary of S1 Holdco) entered into a new loan (“Term Loan”) and revolving facility (“2022 Revolving Facility”) with Bank of America, N.A., on January 27, 2022, providing for a 5.5 year term loan with a principal balance of $400,000 and with the net proceeds of $376,000, of which a portion of the proceeds were used by S1 Holdco, to settle the outstanding debt of $ 172,038 with Cerberus Business Finance, LLC. The 2022 Revolving Facility provided for borrowing availability of up to$50,000. As of June 30, 2023, $50,000 was outstanding on the 2022 Revolving Facility and principal of $375,000 was outstanding on the Term Loan. Through December 31, 2025, $5,000 of the Term Loan is payable quarterly. From March 31, 2026, $7,500 of the Term Loan is payable quarterly. The Term Loan matures in 2027.

For every interest period, the interest rate on the Term Loan is the adjusted Term Secured Overnight Financing Rate (“Term SOFR”) plus 4.75%. The Term Loan is amortized in quarterly installments on each scheduled payment date. The Term Loan comes with a leverage covenant, which goes into effect only if the utilization on the 2022 Revolving Facility exceeds 35% of the $50,000 2022 Revolving Facility at each quarter-end starting from the first full quarter after the effective date of the Merger, such that the first lien leverage ratio (as defined in the credit agreement) should not exceed 5.40. The facility has certain financial and nonfinancial covenants, including a leverage ratio. The facility also requires that the Company delivers its audited consolidated financial statements to its lender within 120 days of its fiscal year end, December 31. Should the Company fail to distribute the financial statements to its lender within 120 days, it is allowed an additional 30 to cure.

The 2022 Revolving Facility matures in January 2027, and accordingly, it is classified within long-term debt, net on the consolidated balance sheet as of June 30, 2023. The interest rate on the 2022 Revolving Facility is the adjusted Term SOFR plus 2.5% with an adjusted Term SOFR floor of 0%. In March 2022, the Company borrowed $49,000 under its 2022 Revolving Facility, to fund a portion of the purchase price related to its CouponFollow acquisition. In October 2022, the Company borrowed the remaining $1,000 available.

(Dollars, number of shares and number of units in thousands, except for per share or per unit amounts)

The carrying values of the Company's debt, net of discounts, deferred financing and debt issuance costs were as follows:

	Successor	
	June 30, 2023	December 31, 2022
Term Loan[1,2]	$ 357,026	$ 364,525
2022 Revolving Facility	50,000	50,000
Total Debt, net	$ 407,026	$ 414,525

[1] Includes loan fees of $ 932 and $1,061, respectively, recorded as a reduction of the carrying amount of the debt and amortized to interest expense using the effective interest method.

[2] Estimated fair value of the Term Loan was $ 313,125 as of June 30, 2023.

As of the date of this filing, the Company was in compliance with all debt covenants.

Refer to Note 14—*RELATED-PARTY TRANSACTIONS* for additional information regarding the Company's indebtedness.

11. FAIR VALUE MEASUREMENT

The following tables present the Company’s fair value hierarchy for liabilities measured at fair value on a recurring basis:

	Successor	
	June 30, 2023	December 31, 2022
	Level 1	Level 1
Public warrants	$ 8,406	$ 7,798

The fair value of the Public Warrants was estimated using the Public Warrants’ quoted market price.

Changes in estimated fair value of Levels 1, 2 and 3 financial liabilities were as follows:

	Former CEO equity profits interest	Contingent consideration
	Level 3	Level 3
Fair value of liabilities at December 31, 2021 (Predecessor) and January 26, 2022 (Predecessor)	$ 11,132	$ 1,682

	Public Warrant liability	Private Warrant liability	Contingent consideration
	Level 1	Level 2	Level 3
Fair value of liabilities at January 27, 2022 (Successor)	$ 18,285	$ 8,727	$ 1,682
Additions	—	—	573
Settlements	(1,147)	(21,818)	(1,715)
Change in fair value	(3,469)	13,091	28
Fair value of liabilities at June 30, 2022 (Successor)	$ 13,669	$ —	$ 568

(Dollars, number of shares and number of units in thousands, except for per share or per unit amounts)

	Public Warrant liability
	Level 1
Fair value of liabilities at December 31, 2022 (Successor)	$ 7,798
Change in fair value	608
Fair value of liabilities at June 30, 2023 (Successor)	$ 8,406

There were no transfers in or out of levels during the six months ended June 30, 2023 (Successor), the period January 1, 2022 through January 26, 2022 (Predecessor), and the period January 27, 2022 through June 30, 2022 (Successor).

12. NET LOSS PER SHARE OR UNIT

For the three and six months ended June 30, 2023 (Successor), the three months ended June 30, 2022 (Successor), and the period from January 27, 2022 through June 30, 2022 (Successor), the basic net loss per share was calculated by dividing net loss attributable to common stockholders by the weighted average number of shares of common stock outstanding. For the period from January 1, 2022 through January 26, 2022 (Predecessor), the basic net loss per unit attributable to members was calculated by dividing the net loss attributable to common equity holders by the weighted-average number of membership units outstanding. Basic and diluted net loss per share was calculated as follows:

	Successor				Predecessor
	Three Months Ended June 30, 2023	Three Months Ended June 30, 2022	Six Months Ended June 30, 2023	Period from January 27, 2022 through June 30, 2022	Period from January 1, 2022 through January 26, 2022
Net loss per share:					
Basic	$ (0.38)	$ (0.29)	$ (0.74)	$ (0.71)	n/a
Diluted	$ (0.38)	$ (0.33)	$ (0.74)	$ (0.71)	n/a
Numerator:					
Net loss attributable to System1, Inc.	$ (35,230)	$ (25,737)	$ (69,182)	$ (61,806)	n/a
Change in fair value or warrant liabilities	n/a	(4,139)	n/a	n/a	n/a
Net loss used in diluted computation	$ (35,230)	$ (29,876)	$ (69,182)	$ (61,806)	n/a
Denominator:					
Weighted-average common shares outstanding used in computing basic net loss per share	93,425	89,701	92,945	86,840	n/a
Adjustment for incremental shares from applying treasury stock method	n/a	1,481	n/a	n/a	n/a
Weighted-average common shares outstanding used in computing diluted net loss per share	93,425	91,182	92,945	86,840	n/a
Basic and diluted net loss per unit	n/a	n/a	n/a	n/a	$ (1.81)
Numerator:					
Net loss	n/a	n/a	n/a	n/a	$ (37,061)
Denominator:					
Weighted-average membership units outstanding - basic and diluted	n/a	n/a	n/a	n/a	20,488

Shares of Class C common stock outstanding for the three and six months ended June 30, 2023 (Successor), the three months ended June 30, 2022 (Successor), and the period from January 27, 2022 through June 30, 2022 (Successor) are considered potentially dilutive of the shares of Class A common stock under the application of the if-converted method, and are included in the computation of diluted loss per share, except when the effect would be anti-dilutive. For the three and six months ended June 30, 2023 (Successor) and the three months ended June 30, 2022 and the period from January 27, 2022 through June 30, 2022 (Successor), 21,513 and 22,077 shares of Class C common stock were excluded from the computation of net loss per share, respectively. For the three and six months ended June 30, 2023 (Successor), and the period from January 27, 2022 through June 30, 2022 (Successor), Loss per share excludes Public Warrants as their effect was anti-dilutive.

(Dollars, number of shares and number of units in thousands, except for per share or per unit amounts)

13. SEGMENT REPORTING

We have three reportable segments:

- Owned and Operated Advertising — revenue earned by directly acquiring traffic to the Company's owned and operated websites and utilizing the RAMP platform and related services to connect Advertising Partners to the Company's owned and operated websites;
- Partner Network — revenue earned from revenue-sharing arrangements with Network Partners for the use of the RAMP platform, and related services provided to them to direct advertising by the Advertising Partners to their advertising space; and
- Subscription — revenue primarily derived from the (i) delivery of the antivirus software and (ii) delivery of the additional add-on service(s).

The following table summarizes revenue by the Company's three reportable segments:

	Successor				Predecessor
	Three Months Ended June 30, 2023	Three Months Ended June 30, 2022	Six Months Ended June 30, 2023	Period from January 27, 2022 through June 30, 2022	Period from January 1, 2022 through January 26, 2022
Owned and Operated Advertising	$ 77,300	$ 157,952	$ 183,325	$ 284,836	$ 49,249
Partner Network	19,614	19,077	34,707	30,427	3,463
Subscription	50,324	42,768	97,060	70,642	—
Total revenue	$ 147,238	$ 219,797	$ 315,092	$ 385,905	$ 52,712

The following table summarizes adjusted gross profit by the Company's three reportable segments:

	Successor				Predecessor
	Three Months Ended June 30, 2023	Three Months Ended June 30, 2022	Six Months Ended June 30, 2023	Period from January 27, 2022 through June 30, 2022	Period from January 1, 2022 through January 26, 2022
Owned and Operated Advertising	$ 27,589	$ 36,799	$ 57,428	$ 66,217	$ 8,768
Partner Network	14,808	13,908	25,025	22,321	3,012
Subscription	17,920	22,890	32,075	35,537	—
Adjusted gross profit	$ 60,317	73,597	114,528	$ 124,075	$ 11,780
Other cost of revenue	6,961	6,358	13,720	11,112	575
Salaries and benefits	43,991	49,511	82,389	97,709	31,181
Selling, general and administrative	17,735	16,747	34,907	31,835	15,665
Depreciation and amortization	28,052	32,094	57,426	54,022	1,000
Interest expense, net	12,342	7,324	23,793	12,100	1,049
Change in fair value of warrant liabilities	2,018	(4,139)	609	9,622	—
Net loss before income tax	$ (50,782)	$ (34,298)	$ (98,316)	$ (92,325)	$ (37,690)

The following table summarizes revenue by geographic region:

(Dollars, number of shares and number of units in thousands, except for per share or per unit amounts)

	Successor				Predecessor
Geographic Region	Three Months Ended June 30, 2023	Three Months Ended June 30, 2022	Six Months Ended June 30, 2023	Period from January 27, 2022 through June 30, 2022	Period from January 1, 2022 through January 26, 2022
United States	$ 93,410	$ 167,872	$ 210,609	$ 302,480	$ 51,701
United Kingdom	50,324	42,924	97,177	70,643	—
Other countries	3,504	9,001	7,306	12,782	1,011
Total revenue	$ 147,238	$ 219,797	$ 315,092	$ 385,905	$ 52,712

The following table summarizes property and equipment, net and operating leases by reportable segments:

	Successor	
	June 30, 2023	December 31, 2022
Owned and Operated Advertising	$ 9,080	$ 9,646
Subscription	1,604	860
Total	$ 10,684	$ 10,506

14. RELATED-PARTY TRANSACTIONS

Payment Processing Agreement

Protected utilizes multiple payment processors in order to process credit card payments from its subscription customers, including Paysafe Financial Services Limited (“Paysafe”). In March 2021 Paysafe completed a merger with Foley Trasimene Acquisition Corp. II (“Foley Trasimene”), a special purpose acquisition company sponsored by entities affiliated with William Foley, who was also a sponsor of Trebia Acquisition Corp. and was a member of the Company’s Board of Directors. Protected's payment processing agreement with Paysafe was negotiated before the announcements of both (i) the Merger as well as (ii) the business combination between Paysafe and Foley Trasimene. The Company incurred credit card processing fees related to Paysafe for the three months ended June 30, 2023 and 2022 (Successor), of $1,012 and $484, respectively. The Company incurred credit card processing fees related to Paysafe for the six months ended June 30, 2023, the period from January 27, 2022 through June 30, 2022 (Successor) and the period January 1, 2022 through January 26, 2022 (Predecessor) of $2,135, $1,022 and $0, respectively. The amount receivable from Paysafe was $334 and $2,447 as of June 30, 2023 (Successor) and December 31, 2022 (Successor), respectively.

Office Facilities

The Company has agreements with JDI Property Holdings Limited (“JDI”), an entity controlled by a director of the Company, which allows for the Company to occupy desks at JDI’s property in such a place as JDI specifies from time to time in exchange for GBP 52 per month. The agreements with JDI expire on October 31, 2026. Additionally, the Company utilizes a JDI credit card and the Company reimburses JDI monthly. The amount owed to JDI was immaterial as of June 30, 2023 (Successor) and December 31, 2022 (Successor).

Protected Incentive Plan Installment Payments

On August 30, 2022, the Company, Protected and Just Develop It Limited (“JDIL”), an entity controlled by a director of the Company, entered into a Conditional Consent, Waiver and Acknowledgement (the “Waiver”) pursuant to which JDIL agreed to waive its right to the Year 3 Stock Bonus Pool (as such term is defined in the BCA), consisting of $50,000 of Class A common stock payable in January 2024 and as set forth in Section 12.11(a) of the BCA dated June 28, 2021 (as amended), by and among S1 Holdco, Protected and the other parties signatory thereto in exchange for $ 40,000 in cash payable in four (4) quarterly installments of $10,000 each, commencing on August 30, 2022 and on each three (3) month anniversary thereafter. On June 1, 2023, the Company further modified the 2023 Award, deferring the last quarterly cash installment of $10,000 such that $5,000 was due on May 30, 2023, $5,000 is due on July 1, 2023, and providing additional cash bonus payments of up to $ 10,000, $6,000 due on October 1, 2023 (the "October Payment") and $1,000 due on the first of each month of November 2023 through February 2024 (together the "Remaining Payments"), based on the achievement of certain performance thresholds around marketing spend and operating contribution of Protected. As of the date these condensed consolidated financial statements were filed, based on its current forecast, the Company assesses it is probable the October Payment will be due in the first quarter of 2024, and the Remaining Payments will be paid according to the schedule mentioned above. Refer to Note 15—*STOCK-BASED COMPENSATION* for additional information.

Related-Party Loan

On April 10, 2023, Orchid Merger Sub II, LLC ("Orchid Sub"), a wholly-owned subsidiary of the Company, entered into a $20,000 Revolving Note (the “2023 Revolving Note”) with Lone Star Friends Trust (acting by and through its trustee, Stanley Blend, “Lone Star”) and CEE Holding Trust (acting by and through its trustee, Jackson Hole Trust Company, “CEE”, and together with Lone Star, collectively, the “Lenders” and each, a “Lender”), which are trusts established for the benefit of Michael Blend (Chief Executive Officer, co-founder and stockholder) and Charles Ursini (co-founder and stockholder), respectively, in a private transaction approved by the independent and noninterested members of the Company’s Board of Directors (the “Board”). Each Lender provided a $10,000 commitment for an aggregate principal of $20,000 under the 2023 Revolving Note to Orchid Sub on a several but not joint basis (each, a “Commitment” and, collectively, the “Commitments”).

Any borrowed loan amounts outstanding under the 2023 Revolving Note accrue interest at the rate per annum equal to the Secured Overnight Financing Rate as administered by the Federal Reserve Bank of New York plus 3.15%. Orchid Sub may borrow amounts under the 2023 Revolving Note in increments of $100, and may prepay any amounts borrowed at any time without penalty or interest (other than applicable breakage costs, if any). The Company may borrow up to its commitment amount, and may reuse the loan again after the balance has been paid down. The maturity date under the 2023 Revolving Note is July 10, 2024 (the "Maturity Date") with automatic three-month extensions, unless we or any Lender provides written notice . The lenders are also entitled to (i) an unused commitment fee equal to 1.0% per annum of the actual daily amount of total unfunded commitments under the 2023 Revolving Note during the period from the closing date to the maturity date, payable quarterly in arrears and (ii) a loan fee equal to 12.0% of each lender's commitment under the 2023 Revolving Note, or $2,400 in total, payable within 180 days of April 10, 2023. Further, this loan fee was capitalized in Prepaid and other current assets and will be amortized on a straight-line basis through the Maturity Date. The available balance on the 2023 Revolving Note was $10,000 as of the date these condensed consolidated financial statements were issued.

Cannae Services Agreement

On June 20, 2023, the Company engaged Cannae Holdings, LLC (a wholly owned subsidiary of Cannae Holdings, Inc.), a greater than 5% holder of the Company's Class A Common Stock, to provide certain observations and recommendations relating to the accounting and finance functions of the Company. Fees for the services include an initial retainer of $100 and $25 monthly during the term of the engagement. The initial retainer of $ 100 was accrued in Accounts payable as of June 30, 2023. Either party may terminate the agreement with or without cause provided adequate written notice. On August 2, 2023, the agreement was terminated, with an effective termination date of August 11, 2023.

15. STOCK-BASED COMPENSATION

The Company recorded the following stock-based compensation expense for the periods presented:

(Dollars, number of shares and number of units in thousands, except for per share or per unit amounts)

	Successor				Predecessor
	Three Months Ended June 30, 2023	Three Months Ended June 30, 2022	Six Months Ended June 30, 2023	Period from January 27, 2022 through June 30, 2022	Period from January 1, 2022 through January 26, 2022
Stock-based compensation expense	$ 17,730	$ 25,168	$ 31,656	$ 57,470	$ 23,705

Protected Incentive Plan

During the three and six months ended June 30, 2023, the Company recognized $12,778 and $20,310, respectively, for both the 2023 Award and 2024 Award of the Protected Incentive Plan within Salaries and benefits on the condensed consolidated statements of operations. Although the last twelve months cash EBITDA target for the 2024 Award of the Protected Incentive Plan has not yet been met, the Company determined that it was probable of achievement. Refer to Note 14—*RELATED-PARTY TRANSACTIONS* for additional information regarding installment payments.

CouponFollow Incentive Plan

As of June 30, 2023, the Company has determined that it was not probable that the CouponFollow business would achieve any of the contingent earnout targets during the Performance Periods, and accordingly, it did not record a liability for any of the tier amounts set forth in the CouponFollow Incentive Plan. During the three and six months ended June 30, 2023, the Company recognized $833 and $1,101, respectively, for the Fixed Amount of the CouponFollow Incentive Plan within Salaries and benefits expenses on the accompanying condensed consolidated statements of operations. The amount for the six months ended June 30, 2023 is net of a $566 difference between the fair value of the Class A common stock issued to settle the earnout liability for the First Performance Period for fiscal 2022 and the carrying value of the earnout liability.

On March 1, 2023, the Company settled the first Fixed Amount of $ 3,333 for the performance period ending December 31, 2022, in shares. The Company issued 407 shares of Class A Common stock, with an aggregate fair value of $ 1,658, net of shares withheld for taxes, on the date of settlement.

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

SYSTEM1 MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Unless otherwise indicated or the context otherwise requires, references in this section to “the Company,” “System1,” “we,” “us,” “our” and other similar terms refer to System1 Inc. and its subsidiaries.

The following discussion and analysis of the financial condition and results of operations of System1 should be read together with our unaudited condensed consolidated financial statements and related notes included elsewhere in this Quarterly Report on Form 10-Q (this "Quarterly Report"). The following discussion and analysis should also be read together with the section entitled “Organization and description of business” as of June 30, 2023 (Successor) and for the period from January 1, 2022 through January 26, 2022 (Predecessor), and the period from January 27, 2022 through June 30, 2022 (Successor), as well as information contained in our Annual Report on Form 10-K for the year ended December 31, 2022 (Successor) (our "Form 10-K"). In addition to historical information, the following discussion and analysis contains forward-looking statements. Our actual results may differ significantly from those projected in such forward-looking statements. Factors that might cause future results to differ materially from those projected in such forward-looking statements include, but are not limited to, those discussed in the sections entitled “Risk Factors” in this Quarterly Report and our Form 10-K. Dollars, number of shares and number of units are presented in thousands, except percentages, per share and per unit information, unless otherwise noted.

References to "Note" or “Notes” are to the notes included in our unaudited condensed consolidated financial statements appearing elsewhere in this Quarterly Report.

Company Overview

We operate an omnichannel customer acquisition platform, delivering high-intent customers to advertisers and selling antivirus software packages to end user customers.

We provide our omnichannel customer acquisition platform services through our proprietary responsive acquisition marketing platform (“RAMP”). Operating seamlessly across major advertising networks and advertising category verticals to acquire users on our behalf, RAMP allows us to monetize these acquired users through our relationships with third party advertisers and advertising networks (“Advertising Partners”). RAMP also allows third party advertising platforms and publishers (“Network Partners”), to send user traffic to, and monetize user traffic on, our owned and operated websites. RAMP operates across our network of owned and operated websites and related products, allowing us to monetize user traffic that we source from various acquisition marketing channels, including Google, Facebook, Taboola and Zemanta.

Through RAMP, we process approximately 95 million daily advertising campaign optimizations and ingest over 7 billion rows of data daily across nearly 40 advertising verticals as of June 30, 2023. We are able to efficiently monetize user intent by linking data on consumer engagement, such as first party search data, with data on monetization and advertising spend. This context-enriched data, combined with our proprietary and data science driven algorithms, creates a closed-loop system that is not reliant on personally identifiable information or information obtained through third-party cookies, but which allows RAMP to efficiently match consumer demand with the appropriate advertiser or advertising experience across advertising verticals.

The business of S1 Holdco, LLC (“S1 Holdco”), one of the entities acquired in the Merger described below, was founded in 2013 with a focus on monetizing user traffic acquired by its network. Since launching, it has expanded to support additional advertising formats across numerous advertising platforms, and has acquired several leading websites, enabling it to control user acquisition and experience, and monetize user traffic. Today S1 Holdco owns and operates over 40 websites, including leading search engines like info.com and Startpage.com, and publishing digital media sites and utilities, such as HowStuffWorks, Mapquest and ActiveBeat.

We, through Total Security Limited ("Protected"; formerly Protected.net Group Limited), also provide antivirus software solutions directly to customers, offering a single packaged solution that provides protection and reporting to the end user. We deliver our antivirus software solutions directly to customers around the world. The antivirus software solutions product offering comprises a core security package with varying levels of extra protection based on a customer's specific needs, and is available on an unlimited number of devices. Other product offerings of Protected include adblocking software and online identity protection. Our products are sold either as a monthly or annual subscription predominantly through the flagship brand TotalAV, and also through the TotalAdBlock and ID Protect brands. As of June 30, 2023, Protected had approximately 2.8 million active subscribers for its products.

Our primary operations are in the United States; and we also have operations in Canada, the United Kingdom and the Netherlands. Operations outside the United States are subject to risks inherent in operating under different legal systems and various political and economic environments. Among the risks are changes in existing tax laws, possible limitations on foreign investment and income repatriation, government foreign exchange controls, and exposure to currency exchange fluctuations. We do not engage in hedging activities to mitigate our exposure to fluctuations in foreign currency exchange rates.

As a result of the current uncertainty in economic activity, including geopolitical developments and other macroeconomic factors such as rising interest rates, inflation and supply chain disruptions, we are unable to predict the size and duration of the impact on our revenue and our results of operations.

The Merger

On June 28, 2021, we entered into a Business Combination Agreement (as amended on November 30, 2021, January 10, 2022 and January 25, 2022), (the "Business Combination Agreement") by and among us, S1 Holdco and Protected. On January 26, 2022 (the "Closing Date"), the Company consummated the business combination (the "Merger") pursuant to the Business Combination Agreement. Following the consummation of the Merger, the combined company was organized via an "Up-C" structure, in which substantially all of the assets and business operations of System1 are held by S1 Holdco. Our combined business continues to operate through the subsidiaries of S1 Holdco and Protected. Additionally, Trebia's ordinary shares and public warrants ceased trading on the New York Stock Exchange ("NYSE"), and System1 Inc.'s Class A common stock and the Public Warrants began trading on the NYSE on January 28, 2022 under the symbols "SST" and "SST.WS," respectively.

The Company was deemed the accounting acquirer in the Merger, and S1 Holdco was deemed to be the predecessor entity. Accordingly, the historical financial statements of S1 Holdco became the historical financial statements of the Company, upon the consummation of the Merger. As a result, the financial statements included in this report reflect (i) the historical operating results of S1 Holdco prior to the Merger; and (ii) the consolidated results of the Company, including S1 Holdco and Protected following the closing of the Merger. The accompanying financial information include a Predecessor period, which include the periods through January 26, 2022 concurrent with the Merger, and a Successor period from January 27, 2022 through June 30, 2022. A black-line between the Successor and Predecessor periods has been placed in the consolidated financial statements and in the tables within the notes to the consolidated financial statements to highlight the lack of comparability between these two periods as the Merger resulted in a new basis of accounting for S1 Holdco.

Refer to *Note 3—MERGER* and *Note 5 — GOODWILL , INTERNAL-USE SOFTWARE DEVELOPMENT COSTS, NET, AND INTANGIBLE ASSETS, NET* — for additional information.

Results of Operations

The following tables set forth our consolidated results of operations and our consolidated results of operations as a percentage of revenue for the periods presented.

	Successor				Predecessor
	Three Months Ended June 30, 2023	Three Months Ended June 30, 2022	Six Months Ended June 30, 2023	Period from January 27, 2022 through June 30, 2022	Period from January 1, 2022 through January 26, 2022
(in thousands)					
Revenue	$ 147,238	$ 219,797	$ 315,092	$ 385,905	$ 52,712
Operating expenses:					
Cost of revenue (excluding depreciation and amortization)	93,882	152,558	214,284	272,942	41,507
Salaries and benefits	43,991	49,511	82,389	97,709	31,181
Selling, general, and administrative	17,735	16,747	34,907	31,835	15,665
Depreciation and amortization	28,052	32,094	57,426	54,022	1,000
Total operating expenses	183,660	250,910	389,006	456,508	89,353
Operating loss	(36,422)	(31,113)	(73,914)	(70,603)	(36,641)
Other expense:					
Interest expense, net	12,342	7,324	23,793	12,100	1,049
Change in fair value of warrant liabilities	2,018	(4,139)	609	9,622	—
Total other expense	14,360	3,185	24,402	21,722	1,049
Loss before income tax	(50,782)	(34,298)	(98,316)	(92,325)	(37,690)
Income tax benefit	(6,605)	(454)	(11,013)	(15,103)	(629)
Net loss	$ (44,177)	$ (33,844)	$ (87,303)	$ (77,222)	$ (37,061)
Net loss attributable to non-controlling interest	(8,947)	(8,107)	(18,121)	(15,416)	—
Net loss attributable to System1, Inc.	$ (35,230)	$ (25,737)	$ (69,182)	$ (61,806)	$ (37,061)

	Successor				Predecessor
	Three Months Ended June 30, 2023	Three Months Ended June 30, 2022	Six Months Ended June 30, 2023	Period from January 27, 2022 through June 30, 2022	Period from January 1, 2022 through January 26, 2022
Revenue	100 %	100 %	100 %	100 %	100 %
Operating expenses:					
Cost of revenue (excluding depreciation and amortization)	64 %	69 %	68 %	71 %	79 %
Salaries and benefits	30 %	23 %	26 %	25 %	59 %
Selling, general, and administrative	12 %	8 %	11 %	8 %	30 %
Depreciation and amortization	19 %	15 %	18 %	14 %	2 %
Total operating expenses	125 %	114 %	123 %	118 %	170 %
Operating loss	(25) %	(14) %	(23) %	(18) %	(70) %
Other expense:					
Interest expense, net	8 %	3 %	8 %	3 %	2 %
Change in fair value of warrant liabilities	1 %	(2) %	— %	2 %	— %
Total other expense	10 %	1 %	8 %	6 %	2 %
Loss before income tax	(34) %	(16) %	(31) %	(24) %	(72) %
Income tax benefit	(4) %	— %	(3) %	(4) %	(1) %
Net loss	(30) %	(15) %	(28) %	(20) %	(70) %
Net loss attributable to non-controlling interest	(6) %	(4) %	(6) %	(4) %	— %
Net loss attributable to System1, Inc.	(24) %	(12) %	(22) %	(16) %	(70) %

* Percentages may not sum due to rounding

The comparability of our operating results for the six months ended June 30, 2023 (Successor) compared to the period from January 1, 2022 through January 26, 2022 (Predecessor) and the period from January 27, 2022 through June 30, 2022 (Successor) was impacted by the Merger, as discussed above, and other acquisitions.

Comparisons of Results of Operations for the three and six months ended June 30, 2023 (Successor), against the three months ended June 30, 2022 and the combined period from January 1, 2022 through January 26, 2022 (Predecessor) and the period from January 27, 2022 through June 30, 2022 (Successor).

Revenue

The following tables set forth our revenue by reportable segment.

	Three Months Ended June 30, 2023	Three Months Ended June 30, 2022	2023 vs. 2022 change (%)
Revenue:			
Owned and Operated	$ 77,300	$ 157,952	(51)%
Partner Network	19,614	19,077	3%
Subscription	50,324	42,768	18%
Total revenue	$ 147,238	$ 219,797	(33)%

	Successor		Predecessor	
	Six Months Ended June 30, 2023	Period from January 27, 2022 through June 30, 2022	Period from January 1, 2022 through January 26, 2022	2023 vs. 2022 change (%)
Revenue:				
Owned and Operated Advertising	$ 183,325	$ 284,836	$ 49,249	(45)%
Partner Network	34,707	30,427	3,463	2%
Subscription	97,060	70,642	—	37%
Total revenue	$ 315,092	$ 385,905	$ 52,712	(28)%

Refer to the Revenue discussions below.

Owned and Operated Advertising ("O&O")

The decrease in O&O revenue for the three months ended June 30, 2023, and six months ended June 30, 2023, compared to the same prior year periods, respectively, was primarily due to deteriorating macroeconomic conditions, such as reductions in both advertiser and overall consumer demand, which led to a decreased supply of consumer sessions available to be acquired. For the three months ended June 30, 2023, compared to the same prior year period, sessions decreased 193 million to 820 million from 1,013 million, with a corresponding decrease in Revenue per Session ("RPS") of approximately $0.07 to $0.09 from $0.16. For the six months ended June 30, 2023, compared to the same prior year period, sessions decreased 142 million to 1,846 million from 1,988 million, with a corresponding decrease in RPS of approximately $0.07 to $0.10 from $0.17.

Partner Network

The increase in Partner Network revenue for the three months ended June 30, 2023, and six months ended June 30, 2023, compared to the same prior year periods, respectively, was due to our continued investment in this business and growth from newer partners that continue to generate more traffic to our platform. This was partially offset by deteriorating macroeconomic conditions, such as reductions to both advertiser and overall consumer demand, leading to a reduction in RPS. For the three months ended June 30, 2023, compared to the same prior year period, sessions increased 316 million to 677 million from 361 million, and RPS decreased by approximately $0.02 to $0.03 from $0.05. For the six months ended June 30, 2023, compared to the same prior year period, sessions increased 455 million to 1,125 million from 670 million, and RPS decreased by approximately $0.02 to $0.03 from $0.05.

Subscription

The increase in Subscription revenue for the three months ended June 30, 2023, and six months ended June 30, 2023, compared to the same prior year periods, respectively, was primarily due to increases in our subscriber base, the number of subscription renewals and subscription prices, which resulted in a higher revenue per subscription. Additionally, the six months ended June 30, 2023 included two full quarters of revenue, as compared to the prior year period, which included approximately five months of revenue.

Cost of revenue

	Successor		
	Three Months Ended June 30, 2023	**Three Months Ended June 30, 2022**	**2023 vs. 2022 change (%)**
Cost of revenue	$ 93,882	$ 152,558	(38) %
Percent of revenue	64 %	69 %	

	Successor		Predecessor	
	Six Months Ended June 30, 2023	**Period from January 27, 2022 through June 30, 2022**	**Period from January 1, 2022 through January 26, 2022**	**2023 vs. 2022 change (%)**
Cost of revenue	$ 214,284	$ 272,942	$ 41,507	(32)%
Percent of revenue	68 %	71 %	79 %	

The dollar decrease in cost of revenue for the three months ended June 30, 2023, and six months ended June 30, 2023, compared to the same prior year periods, was primarily due to a $71 and $133 million decrease, respectively, in our O&O reportable segment, which was directionally consistent with the decrease in revenue. For the three months ended June 30, 2023, compared to the same prior year period, our Cost per Session ("CPS") decreased $0.06 to $0.06 from $0.12. For the six months ended June 30, 2023, compared to the same prior year period, our CPS decreased $0.06 to $0.07 from $0.13. These decreases were partially offset by a $13 million and $30 million increase in our Subscription reportable segment for the three months ended June 30, 2023, and the six months ended June 30, 2023, respectively. The increases in Subscription cost of revenue as a percent of revenue for the three and six months ended June 30, 2023, as compared to the same prior year periods, was primarily due to the increased upfront advertising costs incurred to acquire new customers.

The following supplemental tables set forth our adjusted gross profit by reportable segment.

	Successor		
	Three Months Ended June 30, 2023	**Three Months Ended June 30, 2022**	**2023 vs. 2022 change (%)**
Segment Adjusted Gross Profit:			
Owned and Operated Advertising	$ 27,589	$ 36,799	(25) %
Partner Network	14,808	13,908	6 %
Subscription	17,920	22,890	(22) %
Total Adjusted Gross Profit	$ 60,317	$ 73,597	(18) %

	Successor		Predecessor	
	Six Months Ended June 30, 2023	Period from January 27, 2022 through June 30, 2022	Period from January 1, 2022 through January 26, 2022	2023 vs. 2022 change (%)
Segment Adjusted Gross Profit:				
Owned and Operated Advertising	$ 57,428	$ 66,217	$ 8,768	(23)%
Partner Network	25,025	22,321	3,012	(1)%
Subscription	32,075	35,537	—	(10)%
Total Adjusted Gross Profit	$ 114,528	$ 124,075	$ 11,780	(16)%

Refer to the Revenue and Cost of revenue discussions above.

Salaries and benefits

	Successor		
	Three Months Ended June 30, 2023	Three Months Ended June 30, 2022	2023 vs. 2022 change (%)
Salaries and benefits	43,991	49,511	(11) %
Percent of revenue	30 %	23 %	

	Successor		Predecessor	
	Six Months Ended June 30, 2023	Period from January 27, 2022 through June 30, 2022	Period from January 1, 2022 through January 26, 2022	2023 vs. 2022 change (%)
Salaries and benefits	$ 82,389	$ 97,709	$ 31,181	(36) %
Percent of revenue	26 %	25 %	59 %	

The decrease in salaries and benefits for the three months ended June 30, 2023 compared to the same prior year period, was primarily due to a $7 million decrease in stock-based compensation, of which $5 million of the decrease was related to the Protected Incentive Plan, partially offset by a $2 million increase in wages and severance. For additional information on our stock-based compensation, refer to Note 15—*STOCK-BASED COMPENSATION*.

The decrease in salaries and benefits for the six months ended June 30, 2023 compared to the same prior year period, was primarily due to a $49 million decrease in stock-based compensation related to the first quarter 2022 Merger, partially offset by a $5 million increase in wages and severance.

Selling, general, and administrative

	Successor		
	Three Months Ended June 30, 2023	Three Months Ended June 30, 2022	2023 vs. 2022 change (%)
Selling, general, and administrative	17,735	16,747	6 %
Percent of revenue	12 %	8 %	

	Successor		Predecessor	
	Six Months Ended June 30, 2023	Period from January 27, 2022 through June 30, 2022	Period from January 1, 2022 through January 26, 2022	2023 vs. 2022 change (%)
Selling, general, and administrative	$ 34,907	$ 31,835	$ 15,665	(27)%
Percent of revenue	11 %	8 %	30 %	

Selling, general, and administrative expense for the three months ended June 30, 2023 remained relatively consistent as compared to the same prior year period.

The decrease in selling, general, and administrative expense for the six months ended June 30, 2023 compared to the same prior year period, was primarily due to additional costs associated with the Merger and acquisitions in the prior year, partially offset by the current year costs associated with the 2022 Form 10-Q restatements.

Depreciation and amortization

	Successor		
	Three Months Ended June 30, 2023	Three Months Ended June 30, 2022	2023 vs. 2022 change (%)
Depreciation and amortization	28,052	32,094	(13) %

	Successor		Predecessor	
	Six Months Ended June 30, 2023	Period from January 27, 2022 through June 30, 2022	Period from January 1, 2022 through January 26, 2022	2023 vs. 2022 change (%)
Depreciation and amortization	$ 57,426	$ 54,022	$ 1,000	4%

The decrease in depreciation and amortization expense for the three months ended June 30, 2023, compared to the same prior year period, was primarily due to the Customer relationships being amortized on an accelerated basis and were acquired in a previous period .

The increase in depreciation and amortization expense for the six months ended June 30, 2023, compared to the same prior year period, was primarily due to additions of intangible assets as a result of the first quarter 2022 Merger.

Interest expense, net

	Successor		
	Three Months Ended June 30, 2023	Three Months Ended June 30, 2022	2023 vs. 2022 change (%)
Interest expense, net	12,342	7,324	69 %

	Successor		Predecessor	
	Six Months Ended June 30, 2023	Period from January 27, 2022 through June 30, 2022	Period from January 1, 2022 through January 26, 2022	2023 vs. 2022 change (%)
Interest expense, net	$ 23,793	$ 12,100	$ 1,049	81%

The increase in interest expense for the three months ended June 30, 2023, and the six months ended June 30, 2023, compared to the same prior year periods, was primarily due to higher interest rates experienced during the current periods presented, as compared to the same prior year periods, respectively.

Change in fair value of warrant liabilities

The change in fair value of warrant liabilities for the three months ended June 30, 2023, and the six months ended June 30, 2023, compared to the same prior year periods, respectively, was driven by the fluctuations in the market value of our Class A common stock.

Income tax (benefit)

	Successor		
	Three Months Ended June 30, 2023	Three Months Ended June 30, 2022	2023 vs. 2022 change (%)
Income tax benefit	$ (6,605)	$ (454)	>100%
Effective tax rate	13%	1%	

	Successor		Predecessor	
	Six Months Ended June 30, 2023	Period from January 27, 2022 through June 30, 2022	Period from January 1, 2022 through January 26, 2022	2023 vs. 2022 change (%)
Income tax benefit	$ (11,013)	$ (15,103)	$ (629)	(30)%
Effective tax rate	11%	16%	2%	

The difference between the effective tax rates for the periods presented above and the federal statutory tax rate of 21% was primarily due to the exclusion of non-controlling income (loss), effects of predecessor flow through income allocations, state taxes, foreign rate differential, non-deductible expenses, increase to the valuation allowance related to unrealizable deferred tax assets, outside basis adjustments, and Global Intangible Low-taxed Income.

Liquidity and Capital Resources

As of June 30, 2023 (Successor), we had available cash and cash equivalents of $8,603.

To date, our available liquidity and operations have been financed through the initial public offering of Trebia, the Merger, credit facilities, and cash flows from operations. We are subject to certain business risks, including dependence on key employees, dependence on key contracts, competition from alternative technologies, and dependence on growth to achieve our business and operational objectives.

Our revenue is dependent on two key Advertising Partners, which are Google and Microsoft.

Going Concern

Starting in the third quarter of 2022 and continuing into 2023, we experienced declining cash flows and financial performance as a result of deteriorating macroeconomic conditions, resulting in reductions in both advertiser and overall consumer demand for our marketing services. In response to these conditions, we obtained additional financing in the second quarter of 2023 as previously disclosed which was expected to provide us sufficient liquidity to manage through the current business environment. However, subsequent to the quarter ended June 30, 2023, we have experienced increased customer acquisition costs in addition to the loss of a Network Partner, both of which have further negatively impacted our future cash forecasts, and may negatively impact our forecasted compliance with the maximum leverage ratio covenant of the Term Loan in the latter half of 2023. As of June 30, 2023, we had cash on hand of $8,603, an accumulated deficit of $514,809, and generated cash flows from operations of $1,352 for the six months ended June 30, 2023. We have principal and interest payments due of approximately $15,000 per quarter, and as of the date of this filing, the remaining available capacity under the 2023 Revolving Note was $10,000.

The declining cash flows and financial performance raise substantial doubt regarding our ability to continue as a going concern for a period of one year following the date that these condensed consolidated financial statements are issued. We have developed plans for cost reduction measures, including some already implemented, to address our forecasted reduction to future cash flows and reduce our leverage ratio. We are also evaluating strategic alternatives, including but not limited to raising additional capital by selling equity or debt securities, seeking incremental financing from related parties or financial institutions, or by other means. However, we do not have definitive plans or agreements in place, and as a result, we cannot provide assurances that additional measures will be available on acceptable terms or at all. To the extent our financial performance does not improve or our plans are not successful or finalized, we may have insufficient available cash balances to fund our operations by the end of the calendar year.

While we will seek to expeditiously implement such plans, there can be no assurance that the plans will be sufficient to maintain appropriate liquidity to support our on-going operations or maintain compliance with debt covenants. Accordingly, we believe that there is substantial doubt about our ability to continue as a going concern for the twelve-month period following the date of this filing.

The condensed consolidated financial statements do not include any adjustments that might result from the outcome of these uncertainties. Accordingly, the condensed consolidated financial statements have been prepared on a basis that assumes we will continue as a going concern and which contemplates the realization of assets and satisfaction of liabilities and commitments in the ordinary course of business.

Credit Facilities

In connection with the Merger discussed above, Orchid Merger Sub II LLC (a subsidiary of S1 Holdco) entered into a term loan (“Term Loan”) and revolving facility (“2022 Revolving Facility”) on January 27, 2022, providing for a 5.5 year facility with a principal balance of $400,000 and with the net proceeds of $376,000.

We have been able, and expect to continue to be able, to make timely payments on the principal and interest . We are currently in compliance with our borrowing covenants.

On April 10, 2023, Orchid Sub, our wholly-owned subsidiary, entered into a $20,000 Revolving Note (the “2023 Revolving Note”) with Lone Star Friends Trust (acting by and through its trustee, Stanley Blend, “Lone Star”) and CEE Holding Trust (acting by and through its trustee, Jackson Hole Trust Company, “CEE”, and together with Lone Star, collectively, the “Lenders” and each, a “Lender”), which are trusts established for the benefit of Michael Blend (Chief Executive Officer, co-founder and stockholder) and Charles Ursini (co-founder and stockholder), respectively, in a private transaction approved by the independent and noninterested members of our Board of Directors (the “Board”). Each Lender provided a $10,000 commitment for an aggregate principal of $20,000 under the 2023 Revolving Note to Orchid Sub on a several but not joint basis (each, a “Commitment” and, collectively, the “Commitments”). The 2023 Revolving Note is available through July 2024, with automatic three-month extensions, unless we or any Lender provides written notice. The available balance under the 2023 Revolving Note was $10,000 as of the date these condensed consolidated financial statements were issued.

For additional information regarding our credit facilities, refer to Note 10—*DEBT, NET* and Note 14—*RELATED-PARTY TRANSACTIONS*.

Cash Flows

The following table summarizes our cash flows for the periods presented:

	Successor		Predecessor
(in thousands)	Six Months Ended June 30, 2023	Period from January 27, 2022 through June 30, 2022	Period from January 1, 2022 through January 26, 2022
Net cash provided by operating activities	$ 1,352	$ (8,303)	$ (10,603)
Net cash used in investing activities	$ (5,068)	$ (449,881)	$ (441)
Net cash used in financing activities	$ (9,368)	$ (15,507)	$ —

Operating Activities

Our cash flows used in operating activities are primarily influenced by growth in our operations, timing of collections from our clients and related payments to our suppliers for advertising inventory and data. We typically pay suppliers in advance of collections from our clients, and our collection and payment cycles can vary from period to period. In addition, seasonality may impact cash flows from operating activities on a sequential quarterly basis during the year.

During the six months ended June 30, 2023 (Successor), cash provided by operating activities of $1,352 resulted primarily from depreciation and amortization expense of $57,426, stock-based compensation of $31,656, and a decrease in accounts receivable of $16,158. This was partially offset by a net loss of $87,303 and a payment for the Protected incentive plan of $15,000.

During the period from January 1, 2022 through January 26, 2022 (Predecessor), cash used in operating activities of $10,603 resulted primarily from a net loss of $37,061, and a decrease in accounts payable of $67,600 due to the Merger. This was partially offset by an increase in accrued expenses of $57,488, stock-based compensation of $23,705 and a decrease in accounts receivable of $11,118 due to the Merger.

During the period from January 27, 2022 to June 30, 2022 (Successor), cash used in operating activities of $8,303 resulted primarily from a net loss of $77,222, non-cash tax benefit of $22,746, a decrease in accrued expenses of $11,225, a decrease in other long-term liabilities of $31,080, an increase in accounts receivable of $8,136 due to the Merger. This was partially offset by an increase in the non-cash depreciation and amortization expense of $54,022, non-cash stock-based compensation of $57,470, non-cash change in fair value of warrants of $9,622, a decrease in deferred revenue of $7,211 due to the Merger, and an increase in accounts payable of $6,535.

Investing Activities

Our primary investing activities consist of acquisitions of businesses, which included the first quarter 2022 acquisitions of S1 Holdco, Protected, CouponFollow and RoadWarrior, and the second quarter 2022 acquisition of Answers, as well as costs capitalized for internally developed software.

During the six months ended June 30, 2023 (Successor), cash used in investing activities of $5,068 resulted from purchases of property and equipment of $1,581, and capitalized expenditures related to internal-use software development costs of $3,487.

During the period from January 1, 2022 through January 26, 2022 (Predecessor), cash used in investing activities of $441 resulted from capitalized expenditures related to internal-use software development costs.

During the period from January 27, 2022 to June 30, 2022 (Successor), cash used in investing activities of $449,881 resulted primarily from the acquisitions of S1 Holdco, Protected, CouponFollow, RoadWarrior, and Answers, capitalized expenditures for internally developed software of $3,497 and purchases of property and equipment of $2,310.

Financing Activities

In the six months ended June 30, 2023 (Successor), cash used in financing activities of $9,368 resulted primarily from repayment of related-party loan of $34,000, repayment of term loan of $10,000, taxes paid related to net settlement of stock awards of $3,052, and payment of acquisition holdback of $1,250. This was partially offset by proceeds from related-party loan of $39,000.

During the period from January 1, 2022 to January 26, 2022 (Predecessor), there was no cash provided or used in financing activities.

During the period from January 27, 2022 to June 30, 2022 (Successor), cash used in financing activities of $15,507 resulted primarily from redemptions of Trebia Class A ordinary shares of $510,469, repayment of existing term loan of $177,488, and payment of debt financing costs related to the Term Loan of $24,845, partially offset by proceeds from the Term Loan and 2022 Revolving Facility of $449,000 and the Backstop Agreement of $246,484.

Share Repurchases

In August 2022, our Board of Directors authorized up to $25,000 for the repurchase of our Class A common stock and Public Warrants ("2022 Repurchase Program"). During the six months ended June 30, 2023, no repurchases of our equity securities were made by us or by any of our affiliated purchasers. As of June 30, 2023, we had $23,878 available under this authorization remaining.

Off-Balance Sheet Arrangements

We do not have any relationships with entities often referred to as structured finance or special purpose entities that have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. We did not have any other off-balance sheet arrangements during the periods presented other than the indemnification agreements.

Contractual Obligations and Known Future Cash Requirements

Service Agreement

In June 2023, we entered into a multi-year agreement with a web services provider whereby we are contractually obligated to spend $15,000 between July 2023 and June 2026. As of June 30, 2023 (Successor), we remain contractually obligated to spend $14,070 towards this commitment.

Debt Obligations

In connection with the Merger, Orchid Merger Sub II LLC (a subsidiary of S1 Holdco) entered into a new loan (“Term Loan”) and revolving facility (“2022 Revolving Facility”) with Bank of America, N.A., on January 27, 2022, providing for a 5.5 year term loan with a principal balance of $400,000 and with the net proceeds of $376,000, of which a portion of the proceeds were used by S1 Holdco, to settle the outstanding debt of $172,038 with Cerberus Business Finance, LLC. The 2022 Revolving Facility provided for borrowing availability of up to $50,000. As of June 30, 2023, $50,000 was outstanding on the 2022 Revolving Facility and principal of $375,000 was outstanding on the Term Loan. Through December 31, 2025, $5,000 of the Term Loan is payable quarterly. From March 31, 2026, $7,500 of the Term Loan is payable quarterly. The Term Loan matures in 2027.

For every interest period, the interest rate on the Term Loan is the adjusted Term Secured Overnight Financing Rate (“Term SOFR”) plus 4.75%. The Term Loan is amortized in quarterly installments on each scheduled payment date. The Term Loan comes with a leverage covenant, which goes into effect only if the utilization on the 2022 Revolving Facility exceeds 35% of the $50,000 2022 Revolving Facility at each quarter-end starting from the first full quarter after the effective date of the Merger, such that the first lien leverage ratio (as defined in the credit agreement) should not exceed 5.40. The facility has certain financial and nonfinancial covenants, including a leverage ratio. The facility also requires that the Company delivers its audited consolidated financial statements to its lender within 120 days of its fiscal year end, December 31. Should the Company fail to distribute the financial statements to its lender within 120 days, it is allowed an additional 30 days to cure.

The 2022 Revolving Facility matures in January 2027, and accordingly, it is classified within long-term debt, net on the consolidated balance sheet as of June 30, 2023. The interest rate on the 2022 Revolving Facility is the adjusted Term SOFR plus 2.5% with an adjusted Term SOFR floor of 0%. In March 2022, the Company borrowed $49,000 under its 2022 Revolving Facility, to fund a portion of the purchase price related to its CouponFollow acquisition. In October 2022, the Company borrowed the remaining $1,000 available.

The carrying values of our debt, net of discounts, deferred financing and debt issuance costs were as follows:

	Successor	
	June 30, 2023	December 31, 2022
Term Loan[1,2]	$ 357,026	$ 364,525
2022 Revolving Facility	50,000	50,000
Total Debt, net	$ 407,026	$ 414,525

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[1] Includes loan fees of $932 and $1,061, respectively, recorded as a reduction of the carrying amount of the debt and amortized to interest expense using the effective interest method.

[2] Estimated fair value of the Term Loan was $313,125 as of June 30, 2023.

We have principal and interest payments due of approximately $15,000 per quarter.

Related-Party Loan

On April 10, 2023, Orchid Merger Sub II, LLC ("Orchid Sub") , our wholly-owned subsidiary, entered into a $20,000 Revolving Note (the “2023 Revolving Note”) with Lone Star Friends Trust (acting by and through its trustee, Stanley Blend, “Lone Star”) and CEE Holding Trust (acting by and through its trustee, Jackson Hole Trust Company, “CEE”, and together with Lone Star, collectively, the “Lenders” and each, a “Lender”), which are trusts established for the benefit of Michael Blend (Chief Executive Officer, co-founder and stockholder) and Charles Ursini (co-founder and stockholder), respectively, in a private transaction approved by the independent and noninterested members of our Board of Directors (the “Board”). Each Lender provided a $10,000 commitment for an aggregate principal of $20,000 under the 2023 Revolving Note to Orchid Sub on a several but not joint basis (each, a “Commitment” and, collectively, the “Commitments”).

Any borrowed loan amounts outstanding under the 2023 Revolving Note accrue interest at the rate per annum equal to the Secured Overnight Financing Rate as administered by the Federal Reserve Bank of New York plus 3.15%. Orchid Sub may borrow amounts under the 2023 Revolving Note in increments of $100, and may prepay any amounts borrowed at any time without penalty or interest (other than applicable breakage costs, if any). We may borrow up to our commitment amount, and may reuse the loan again after the balance has been paid down. The maturity date under the 2023 Revolving Note is July 10, 2024 (the "Maturity Date") with automatic three-month extensions, unless we or any Lender provides written notice . The lenders are also entitled to (i) an unused commitment fee equal to 1.0% per annum of the actual daily amount of total unfunded commitments under the 2023 Revolving Note during the period from the closing date to the maturity date, payable quarterly in arrears and (ii) a loan fee equal to 12.0% of each lender's commitment under the 2023 Revolving Note, or $2,400 in total, payable within 180 days of April 10, 2023. Further, this loan fee was capitalized in Prepaid and other current assets and will be amortized on a straight-line basis through the Maturity Date. The available balance on the 2023 Revolving Note was $10,000 as of the date these condensed consolidated financial statements were issued.

Incentive Plans

Refer to Note 15—*STOCK-BASED COMPENSATION*.

Contingencies

From time to time, we are subject to contingencies that arise in the ordinary course of business. We record an accrual for a contingency when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. We do not currently believe the resolution of any such contingencies will have a material adverse effect upon our condensed consolidated financial statements.

Critical Accounting Policies and Estimates

Our condensed consolidated financial statements are prepared in accordance with GAAP. The preparation of these condensed consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, expenses and related disclosures. We evaluate our estimates and assumptions on an ongoing basis. Our estimates are based on historical experience and various other assumptions that we believe to be reasonable under the circumstances. Our actual results could differ from these estimates.

There have been no changes to our critical accounting policies and estimates since the filing of our Annual Report on Form 10-K for the year ended December 31, 2022.

Goodwill

Goodwill represents the excess of the purchase price over the fair value of net assets acquired and identifiable intangibles in a business combination. We account for goodwill in accordance with Accounting Standards Codification ("ASC") 350, *Intangibles—Goodwill and Other*, which requires us to test goodwill at the reporting unit level for impairment at least annually, or if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. We perform our annual goodwill impairment test on December 31.

We have the option (i) to assess goodwill for possible impairment by performing a qualitative analysis to determine if it is more likely than not that the fair value of a reporting unit is less than its carrying amount or (ii) to perform the quantitative impairment test. The quantitative impairment test involves comparing the estimated fair value of a reporting unit with its respective carrying amount, including goodwill. If the estimated fair value exceeds the carrying amount, goodwill is considered not to be impaired. If, however, the fair value of the reporting unit is less than carrying amount, an impairment loss is recognized in an amount equal to the excess.

The fair values of our reporting units were computed by weighting a discounted cash flow model and a reference transaction model which included inputs developed using both internal and market-based data. The key assumptions in the discounted cash flow model included, but were not limited to, the weighted average cost of capital, revenue growth rates (including long-term growth rates), and operating margins. The weighted average cost of capital reflected the increases in market interest rates. The reference transaction model derives indications of value based on mergers and acquisition transactions in the digital advertising industry. Key assumptions in this model included, but were not limited to, the selection of comparable transactions, revenue and EBITDA multiples and EBITDA margins from those transactions. Unanticipated events or circumstances may occur that could affect the accuracy or validity of such assumptions, estimates or actual results.

As a result of adverse macroeconomic impacts as a result of changes in market conditions, increases in interest rates, and weakening of consumer demand during the third quarter of 2022, which contributed to reduced forecasted revenue and reduced expectations for future cash flows, we performed quantitative goodwill impairments tests of our four reporting units as of September 30, 2022. As a result, we fully impaired goodwill of $329,133 in our Publishing and Lead Generation reporting unit and partially impaired goodwill of $10,976 in our Partner Network reporting unit. The fair value of our Subscription reporting unit and our Search and Applications reporting unit exceeded their carrying amounts by 13% and 2%, respectively.

During the quarter ended December 31, 2022, we realigned our reporting structure due to changes in management such that our Search and Applications reporting unit became part of the Publishing and Lead Generation reporting unit and the new reporting unit was renamed Owned and Operating Advertising. Based on our annual impairment assessment as of December 31, 2022, we determined that the goodwill attributable to Owned and Operating Advertising of $26,200 was fully impaired. The fair value of our Partner Network reporting unit and our Subscription reporting unit exceeded their carrying amounts by 9% and 18%, respectively, as of December 31, 2022.

As of December 31, 2022, all our goodwill relates to our Partner Network and Subscription reporting units. Goodwill associated with the Partner Network and Subscription reporting units were $82,407 and $433,184 respectively, as of December 31, 2022. Any further deterioration in key assumptions or changes in the macroeconomic environment, including further interest rate increases, could adversely impact the fair value of these reporting units and could result in an impairment charge in the future. The Company applied a hypothetical sensitivity analysis by increasing the discount rate used in the valuation of the Partner Network and Subscription reporting units by 100 basis points as of December 31, 2022. An increase in the discount rate would result in the estimated fair values of the Partner Network and Subscription reporting units decreasing by approximately 7% and 13%, respectively. The fair values of each of these reporting units would continue to exceed their carrying amounts, though the excess of the fair value over the carrying amount would be reduced to approximately 1% and 5% for the Partner Networks and Subscription reporting units, respectively.

During the six months ended June 30, 2023, management determined there was no triggering event, and accordingly, no quantitative assessment for impairment was required. No goodwill impairment charges were recorded during the six months ended June 30, 2023. Refer to Note 5 — *GOODWILL, INTERNAL-USE SOFTWARE DEVELOPMENT COSTS, NET, AND INTANGIBLE ASSETS, NET* for additional information.

Recently Issued Accounting Pronouncements

See Note 2—*SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES-Adoption of Recent Accounting Pronouncements* for a discussion of recently issued accounting pronouncements not yet adopted.

Item 3. Quantitative and Qualitative Disclosure about Market Risk

As a “smaller reporting company”, as defined by Rule 10(f)(1) of Regulation S-K, we are not required to provide this information.

Item 4. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures

Pursuant to Rules 13a-15(b) and 15d-15(b) under the Securities Exchange Act, we have evaluated, under the supervision and with the participation of our management, including our Chief Executive Officer (“CEO”) and Chief Financial Officer (“CFO”), the effectiveness of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act as of the end of the period covered by this report. Based on that evaluation, our CEO and CFO concluded that, as of June 30, 2023, due to the material weaknesses in our internal control over financial reporting described below, our disclosure controls and procedures were not effective to ensure that the information required to be disclosed in the reports required to be filed or submitted under the Securities Exchange Act is (i) recorded, processed, summarized, and reported within the time periods specified in the SEC’s rules and forms, and (ii) accumulated and communicated to our management, including our CEO and CFO, as appropriate, to allow timely decisions regarding required disclosure.

(b) Material weaknesses in internal control over financial reporting

We have identified material weaknesses in our internal control over financial reporting as of June 30, 2023. A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis.

The material weaknesses identified were as follows:

- We did not design and maintain an effective control environment commensurate with our financial reporting requirements. Specifically, we lacked a sufficient number of professionals with an appropriate level of accounting knowledge, training and experience to appropriately analyze, record and disclose accounting matters timely and accurately. Additionally, the limited personnel resulted in an inability to consistently establish appropriate authorities and responsibilities in pursuit of financial reporting objectives, as demonstrated by, among other things, insufficient segregation of duties in our finance and accounting functions.
- We did not design and maintain effective controls in response to the risks of material misstatement. Specifically, changes to existing controls or the implementation of new controls have not been sufficient to respond to changes to the risks of material misstatement to financial reporting.

These material weaknesses contributed to the following additional material weaknesses:

- We did not design and maintain effective controls to timely analyze and record the financial statement effects from acquisitions. Specifically, we did not design and maintain effective controls over the (i) application of U.S. GAAP to such transactions, including accounting for post-combination compensation arrangements, (ii) review of the inputs and assumptions used in the measurement of assets acquired and liabilities assumed, including discounted cash flow analysis to value acquired intangible assets at an appropriate level of precision, (iii) the tax impacts of acquisitions to the financial statements, and (iv) conforming of U.S. GAAP and accounting policies of acquired entities to that of the Company. In addition, we did not design and maintain effective controls relating to the oversight and ongoing recording of the financial statement results of the acquired businesses.
- We did not design and maintain formal accounting policies, procedures and controls to achieve complete, accurate and timely financial accounting, reporting and disclosures, including controls over the preparation and review of business performance reviews, account reconciliations and journal entries, and (ii) maintaining appropriate segregation of duties. Additionally, we did not design and maintain controls over the classification and presentation of accounts and disclosures in the consolidated financial statements, including the statement of cash flows.
- We did not design and maintain effective controls over the completeness and accuracy of accrued liabilities, stock-based compensation and equity transactions.
- We did not design and maintain effective controls over the accuracy and valuation of goodwill, including the allocation of goodwill to reporting units and the identification and measurement of goodwill impairment.

These material weaknesses resulted in the restatement of the Company's condensed consolidated financial statements as of March 31, 2022 and for the predecessor period from January 1, 2022 to January 26, 2022 and the successor period from January 27, 2022 to March 31, 2022; as of June 30, 2022 and for the predecessor period from January 1, 2022 to January 26, 2022 and the successor periods for the three months ended June 30, 2022 and from January 27, 2022 to June 30, 2022; and as of September 30, 2022 and for the predecessor period from January 1, 2022 to January 26, 2022 and the successor periods for the three months ended September 30, 2022 and from January 27, 2022 to September 30, 2022. These material weaknesses also resulted in immaterial misstatements to substantially all of the S1 Holdco, LLC accounts, which were recorded prior to the issuance of the consolidated financial statements as of December 31, 2021, 2020, 2019 and 2018 and for the years then ended; as of March 31, 2021 and 2020 and for the three-month periods then ended; as of June 30, 2021 and 2020 and for the six-month periods then ended; and as of September 30, 2021 and 2020 and for the nine-month periods then ended.

These material weaknesses resulted in immaterial adjustments to stock-based compensation expense and accrued expenses and other current liabilities accounts of the financial statements of System1, Inc. as of March 31, 2022 and for the successor period from January 27, 2022 to March 31, 2022; as of June 30, 2022 and for the successor periods for the three months ended June 30, 2022 and from January 27, 2022 to June 30, 2022; and as of September 30, 2022 and for the successor periods for the three months ended September 30, 2022 and from January 27, 2022 to September 30, 2022; as of December 31, 2022 and for the successor periods for the three months ended December 31, 2022 and from January 27, 2022 to December 31, 2022; as of and for the three months ended March 31, 2023; and as of and for the three months ended June 30, 2023, all of which were recorded prior to the issuance of these condensed consolidated financial statements.

Further, these material weaknesses resulted in immaterial adjustments to related party loan fee payable and related party loan as of June 30, 2023 as well as cash flows from operating and financing activities of System1, Inc. as of March 31, 2023 and for the three months ended March 31, 2023, and as of June 30, 2023 and for the six months ended June 30, 2023, all of which were recorded prior to the issuance of these condensed consolidated financial statements.

- We did not design and maintain effective controls over the accounting for complex financial instruments, including the impact of these instruments on earnings per share.

This material weakness also resulted in a material misstatement of the Trebia warrant liabilities, change in the fair value of the Trebia warrant liabilities, forward purchase agreement liabilities, change in the fair value of the forward purchase agreement liabilities, classification of redeemable shares of Class A common stock issued in connection with Trebia's initial public offering, additional paid-in-capital, accumulated deficit, Earnings Per Share, and related financial disclosures of Trebia Acquisition Corp. as of December 31, 2020 and for the period from February 11, 2020 (inception) through December 31, 2020, as of September 30, 2020 and for three month period ended September 30, 2020 and for the period from February 11, 2020 (inception) through September 30, 2020, as of June 30, 2020 and for three month period ended June 30, 2020 and for the period from February 11, 2020 (inception) through June 30, 2020, as of March 31, 2021 and for three month period ended March 31, 2021. This material weakness also resulted in material adjustments relating to the Trebia forward purchase agreement liabilities and repurchases of common stock impacting the accumulated deficit and additional paid-in capital in the opening balance sheet as of January 27, 2022 and the earnings per share computations for the quarter ended June 30, 2022 of the Company.

Additionally, these material weaknesses could result in a misstatement of substantially all of our accounts or disclosures that would result in a material misstatement to the annual or interim consolidated financial statements that would not be prevented or detected.

- We did not design and maintain effective controls over information technology ("IT") general controls for information systems that are relevant to the preparation of our financial statements. Specifically, we did not design and maintain: (i) program change management controls to ensure that IT program and data changes affecting financial IT applications and underlying accounting records are identified, tested, authorized, and implemented appropriately; (ii) user access controls to ensure appropriate segregation of duties and that adequately restrict user and privileged access to financial applications, programs, and data to appropriate Company personnel; (iii) computer operations controls to ensure that critical batch jobs are monitored and data backups are authorized and monitored; and (iv) testing and approval controls for program development to ensure that new software development is aligned with business and IT requirements.

These IT deficiencies did not result in a material misstatement to the financial statements; however, the deficiencies, when aggregated, could impact the effectiveness of IT-dependent controls (such as automated controls that address the risk of material misstatement to one or more assertions, along with the IT controls and underlying data that support the effectiveness of system-generated data and reports) that could result in misstatements potentially impacting all financial statement accounts and disclosures that would not be prevented or detected. Accordingly, we have determined these IT deficiencies in the aggregate constitute a material weakness.

(c) Remediation plan for the material weaknesses

Our remediation plan consists of the following:

- Hiring additional senior level accounting personnel with applicable technical accounting knowledge, training and experience in accounting matters, supplemented by third party resources;
- Designing and implementing controls to formalize roles and review responsibilities to align with our team's skills and experience and designing and implementing controls over segregation of duties;
- Engaging an accounting advisory firm to assist with the documentation, evaluation, remediation and testing of our internal control over financial reporting based on the criteria established in *Internal Control - Integrated Framework* (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission;
- Engaging third-party experts to assist with the preparation of technical accounting analyses and valuations associated with business combinations;
- Designing and implementing controls related to accounting for acquisitions and other technical accounting and financial reporting matters, including controls over the preparation and review of accounting memoranda addressing these matters, valuations and key assumptions utilized in the valuations, tax impacts, and ongoing recording of the financial statement results of the acquired businesses;
- Designing and implementing formal accounting policies, procedures and controls supporting our period-end financial reporting process, including controls over the preparation and review of account reconciliations and journal entries, business performance reviews, foreign exchange gains/losses for intercompany transactions, and classification and presentation of accounts and disclosures, including the statement of cash flows;
- Designing and implementing controls over the completeness and accuracy of accrued liabilities, stock-based compensation and equity transactions;
- Designing and implementing controls related to accounting for complex financial instruments, including the earnings per share impacts;
- Designing and implementing controls over the accuracy and valuation of goodwill, including the allocation of goodwill to reporting units and the identification and measurement of goodwill impairment;
- Implementing an enhanced enterprise resource planning software for automation and enforcing segregation of duties across the organization; and
- Designing and implementing IT general controls, including controls over change management, the review and update of user access rights and privileges, controls over batch jobs and data backups, and program development approvals and testing.

While we believe that these efforts will improve our internal control over financial reporting, remediation of the material weaknesses will require validation and testing of the design and operating effectiveness of internal controls over a sustained period of financial reporting cycles. Therefore, these material weaknesses have not been remediated as of June 30, 2023.

(d) Changes in Internal Control over Financial Reporting.

There have been no changes in our internal control over financial reporting during the three months ended June 30, 2023, as defined under Rule 13a-15(f) under the Exchange Act, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Part II

Item 1. Legal Proceedings

Information in response to this Item is included in "Part I — Item 1. — Note 9—*COMMITMENTS AND CONTINGENCIES*" and is incorporated by reference into Part II of this Quarterly Report on Form 10-Q.

Item 1A. Risk Factors.

Other than as set forth below and with respect to the material weaknesses described herein, which could further amplify our previously disclosed risks, particularly with respect to the consequences of a material weakness in internal control over financial reporting, there have been no material changes from the risk factors previously disclosed in response to "Part I—Item 1A. Risk Factors" of our Annual Report on Form 10-K for the year ended December 31, 2022.

We have identified conditions and events that raise substantial doubt about our ability to continue as a going concern.

As previously reported, starting in the third quarter of 2022 we have experienced declining cash flows and financial performance as a result of deteriorating macroeconomic conditions, resulting in reductions in both advertiser and overall consumer demand for our marketing services. In response to these conditions, in April 2023 we entered into into an incremental revolver note (the “2023 Revolving Note”) with related parties for $20,000, which was expected to provide us with sufficient liquidity to manage through the current business environment. However, subsequent to the quarter ended June 30, 2023, we experienced increased customer acquisition costs in addition to the loss of a Network Partner, both of which have further negatively impacted our future cash forecasts, and could negatively impact our compliance with certain covenants in our Credit and Guaranty Agreement, dated as of January 27, 2022 (the "Credit Agreement"), among S1 Holdco, Orchid Merger Sub II, LLC ("Orchid Sub"), the other guarantors and each lender from time to time party thereto and Bank of America, N.A. ("BofA"), as the administrative agent, under which Orchid Sub, our wholly owned subsidiary, providing for an aggregate principal $400,000 term loan (the "Term Loan") and $50,000 revolving facility (the "2022 Revolving Facility"). As of June 30, 2023, we had cash on hand of $8,603, an accumulated deficit of $514,809 and generated cash flows from operations of $1,352 for the six months ended June 30, 2023. We have principal and interest payments due of approximately $15,000 per quarter. As of the date of this filing, the remaining available capacity under the 2023 Revolving Note was $10,000.

The declining cash flows and financial performance raise substantial doubt regarding our ability to continue as a going concern for a period of one year following the issuance of the condensed consolidated financial statements appearing within this Quarterly Report on Form 10-Q. Nevertheless, our financial statements do not include any adjustments that might result from the outcome of this uncertainty. Although we have developed plans for cost reduction measures to address our forecasted reduction to future cash flows and reduce our leverage ratio, as well as evaluating strategic alternatives including but not limited to raising additional capital by selling equity or debt securities, seeking incremental financing from related parties or financial institutions, or by other means, there can be no assurance that we will be able to obtain additional funding on acceptable terms, if at all. To the extent that we raise additional capital through future equity offerings, the ownership interest of our common stockholders will be diluted, which may be significant. In the event that we are unable to obtain any or sufficient additional funding, we may not be able to satisfy certain covenants under the Credit Agreement, which could constitute an event of default and provide BofA the ability to immediately call the outstanding principal balances of the Term Loan and 2022 Revolving Facility, and there can be no assurance that we will be able to continue as a going concern, which will force us to delay, reduce or discontinue certain aspects of our business strategy.

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

Share Repurchases

In August 2022, our Board of Directors authorized up to $25,000 for the repurchase of our Class A common stock and Public Warrants. During the quarter ended June 30, 2023, no repurchases of our equity securities were made by us or by any of our affiliated purchasers. As of June 30, 2023, we had $23,878 available under this authorization remaining.

Item 3. Defaults Upon Senior Securities

On May 1, 2023, the Company did not deliver audited financial statements as required under the terms of its credit agreement. On May 1, 2023, the Company received a notice of default, which started a 30 day cure period, ending on May 31, 2023, within which the Company could remedy the default. On June 1, 2023, as a result of not delivering audited financial statements for the fiscal year ended December 31, 2022, the default constitutes an event of default. As a result, the outstanding principal balances of $430,000 for the Term Loan and 2022 Revolving Facility were callable by Bank of America at the request of, or with the consent of, the required majority of lenders thereunder. The Company delivered audited financial statements on June 5, 2023, which cured the continuing event of default, thus Bank of America no longer has the ability to exercise remedies with respect thereto.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Item 6. Exhibits

		Incorporated by Reference				Filed or Furnished Herewith
Exhibit No.	Description	Form	File No.	Exhibit	Filing Date	
2.1(a)	Business Combination Agreement, dated as of June 28, 2021, by and among Trebia Acquisition Corp., S1 Holdco, LLC, System1 SS Protect Holdings, Inc., and the other parties that are signatory thereto.	8-K	001-39331	2.1	6/29/2021	
	0					
2.1(b)	Amendment No. 1 to the Business Combination Agreement, dated as of November 30, 2021, by and among Trebia Acquisition Corp., S1 Holdco, LLC, System1 SS Protect Holdings, Inc., and the other parties that are signatory thereto.	S-4	333-260714	2.2	12/1/2021	
2.1(c)	Amendment No. 2 to the Business Combination Agreement, dated January 10, 2022, by and among S1 Holdco, LLC, a Delaware limited liability company, System1 SS Protect Holdings, Inc., a Delaware corporation and the other parties signatory thereto.	8-K	001-39331	10.1	1/20/2022	
2.1(d)	Amendment No. 3 to the Business Combination Agreement, dated January 25, 2022, by and among S1 Holdco, LLC, a Delaware limited liability company, System1 SS Protect Holdings, Inc., a Delaware corporation and the other parties signatory thereto.	8-K	001-39331	10.1	1/26/2022	
3.1	Certificate of Incorporation of System1, Inc.	8-K	001-39331	3.1	2/2/2022	
3.2	Second Amended and Restated Bylaws of System1, Inc.	8-K	001-39331	3.1	3/1/2023	
4.1	Warrant Agreement, dated June 19, 2020, by and between Trebia Acquisition Corp. and Continental Stock Transfer & Trust Company, as warrant agent.	8-K	001-39331	4.1	6/2/2020	
10.1^	System1, Inc. 2022 Incentive Award Plan.	8-K	001-39331	10.2	2/20/2022	
10.2	Amended and Restated Backstop Facility Agreement, dated January 10, 2022, by and between Trebia Acquisition Corp. and Cannae Holdings, Inc.	8-K	001-39331	10.3	1/10/2022	
10.3	Conditional Consent, Waiver and Acknowledgement, dated as of August 30, 2022, by and among System1, Inc., Protected.net Group Limited and Just Develop It Limited.	8-K	001-39331	10.1	8/30/2022	
10.4	Lock-Up Agreement, dated as of August 30, 2022, by and between System1, Inc. and Christopher Phillips.	8-K	001-39331	10.2	8/30/2022	
10.5	Lock-Up Agreement, dated as of August 30, 2022, by and between System1, Inc. and Nicholas Baker.	8-K	001-39331	10.3	8/30/2022	
10.6	Transition and Advisory Services Agreement, dated as of November 2, 2022, by and among System1, Inc. and Paul Filsinger.	8-K	001-39331	10.4	11/2/2022	
10.7#	Credit and Guaranty Agreement, dated as of January 27, 2022, among Orchid Finco LLC, System1 Midco, LLC, Orchid Merger Sub II, LLC and the subsidiaries from time to time party thereto, S1 Holdco, LLC, Bank of America, N.A. and the lenders from time to time party thereto.	10-K	001-39331	10.7	6/6/2023	
10.8	Amended and Restated Revolving Note, dated May 16, 2023, by and among Orchid Merger Sub II, LLC, Lone Star Friends Trust and CEE Holding Trust.	10-K	001-39331	10.8	6/6/2023	
10.9	Registration Rights Agreement, dated January 27, 2022, by and among System1, Inc. and the other parties that are signatory thereto.	S-1	333-262608	10.3	2/9/2022	

		Incorporated by Reference				Filed or Furnished Herewith
Exhibit No.	Description	Form	File No.	Exhibit	Filing Date	
10.10	Registration Rights Agreement, dated June 19, 2020, among the Company, the Sponsors and certain other security holders named therein.	8-K	001-39331	10.2	06/22/2020	
10.11	Form of Indemnification Agreement	8-K	001-39331	10.4	3/2/2022	
10.12^	Employment Agreement, dated as of June 15, 2023, by and between Mr. Kidambi and the Company.	8-K	001-39331	10.1	6/22/2023	
10.13^	Employment Agreement, dated as of August 28, 2016, between Elizabeth Sestanovich and OpenMail LLC.	10-K	001-39331	10.13	6/6/2023	
10.14^	Employment Agreement, dated as of September 15, 2015, between Brian Coppola and OpenMail LLC.	10-K	001-39331	10.14	6/6/2023	
10.15^	Employment Agreement, dated as of February 8, 2018, between Daniel Weinrot and OpenMail LLC.	10-K	001-39331	10.15	6/6/2023	
10.16^	Employment Agreement, dated as of May 2, 2021, between Jennifer Robinson and System1, LLC.	10-K	001-39331	10.16	6/6/2023	
10.17	Form of Stockholders Agreement	S-4/A	333-260714	10.3	12/16/2021	
10.18	First Amendment to Conditional Consent, Waiver and Acknowledgement, dated as of June 1, 2023, by and among System1, Inc., Protected.net Group Limited and Just Develop It Limited., dated as of June 1, 2023, by and among System1, Inc., Protected.net Group Limited and Just Develop It Limited.	10-K	001-39331	10.18	6/6/2023	
31.1	Certification of principal executive officer pursuant to Rules 13a-15(e) and 15d-15(e), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002					X
31.2	Certification of principal financial and accounting officer pursuant to Rules 13a-15(e) and 15d-15(e), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002					X
32.1*	Certification of principal executive officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002					X
32.2*	Certification of principal financial and accounting officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002					X
101.INS	XBRL Instance Document – The instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document.					X
101.SCH	XBRL Taxonomy Extension Schema Document.					X
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.					X
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.					X
101.LAB	XBRL Taxonomy Extension Labels Linkbase Document.					X
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.					X
104	Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101)					X

Schedules and exhibits have been omitted pursuant to Item 601(a)(5) of Regulation S-K. The Registrant will furnish copies of any such schedules and exhibits to the SEC upon request.

*   This certification shall not be deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934, or otherwise subject to the liability of that section, nor shall it be deemed to be incorporated by reference into any filing under the Securities Act of 1933 or the Securities Exchange Act of 1934.

^   Indicates management contract or compensatory plan.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

		System1 Inc.
Date: August 9, 2023	By:	/s/ Michael Blend
		Michael Blend
		Chief Executive Officer
Date: August 9, 2023	By:	/s/ Tridivesh Kidambi
		Tridivesh Kidambi
		Chief Financial Officer

Exhibit 31.1

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO SECTION 302 OF
THE SARBANES-OXLEY ACT OF 2002

I, Michael Blend, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of System1, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

    a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

    b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

    c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

    d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

    a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

    b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ Michael Blend
Michael Blend
Chief Executive Officer
(Principal Executive Officer)
Date: August 9, 2023

Exhibit 31.2

CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER
PURSUANT TO SECTION 302 OF
THE SARBANES-OXLEY ACT OF 2002

I, Tridivesh Kidambi, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of System1, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ Tridivesh Kidambi
Tridivesh Kidambi
Chief Financial Officer
(Principal Financial Officer)
Date: August 9, 2023

Exhibit 32.1

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2023 of System1, Inc. (the “Company”) as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Michael Blend, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge:

1. The Report fully complies with the requirements of Section 13(a) or Section 15(d) of the Securities Exchange Act of 1934, as amended; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Michael Blend
Michael Blend
Chief Executive Officer
(Principal Executive Officer)

Date: August 9, 2023

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission (the “SEC”) or its staff upon request.

This certification accompanies the Form 10-Q to which it relates, is not deemed filed with the SEC and is not to be incorporated by reference into any filing of the Company under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended (whether made before or after the date of the Form 10-Q), irrespective of any general incorporation language contained in such filing.

Exhibit 32.2

CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER
PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2023 of System1, Inc. (the “Company”) as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Tridivesh Kidambi, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge:

1. The Report fully complies with the requirements of Section 13(a) or Section 15(d) of the Securities Exchange Act of 1934, as amended; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Tridivesh Kidambi
Tridivesh Kidambi
Chief Financial Officer
(Principal Financial Officer)

Date: August 9, 2023

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission (the “SEC”) or its staff upon request.

This certification accompanies the Form 10-Q to which it relates, is not deemed filed with the SEC and is not to be incorporated by reference into any filing of the Company under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended (whether made before or after the date of the Form 10-Q), irrespective of any general incorporation language contained in such filing.