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# Independent Auditors' Review Report

The Board of Directors
Monitronics International, Inc.:

## Report on the Financial Statements

We have reviewed the accompanying condensed consolidated balance sheet of Monitronics International, Inc. and subsidiaries (the Company) as of June 30, 2021, the related condensed consolidated statements of operations and comprehensive income (loss), stockholders' equity, and cash flows for the six-month periods ended June 30, 2021 and 2020.

*Management's Responsibility*

The Company's management is responsible for the preparation and fair presentation of the interim financial information in accordance with U.S. generally accepted accounting principles; this responsibility includes the design, implementation, and maintenance of internal control sufficient to provide a reasonable basis for the preparation and fair presentation of interim financial information in accordance with U.S. generally accepted accounting principles.

*Auditors' Responsibility*

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

*Conclusion*

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

KPMG LLP

Dallas, Texas
September 17, 2021

**MONITRONICS INTERNATIONAL, INC. AND SUBSIDIARIES**
**Condensed Consolidated Balance Sheets**
**Amounts in thousands, except share amounts**
**(unaudited)**

| | June 30, 2021 | December 31, 2020 |
|---|---|---|
| **Assets** | | |
| Current assets: | | |
| Cash and cash equivalents | $ 7,294 | $ 6,123 |
| Restricted cash | 133 | 171 |
| Trade receivables, net of allowance for doubtful accounts of $2,675 in 2021 and $3,096 in 2020 | 10,795 | 13,360 |
| Inventories, net | 13,414 | 7,612 |
| Prepaid and other current assets | 25,739 | 22,612 |
| Total current assets | 57,375 | 49,878 |
| Property and equipment, net of accumulated depreciation of $25,669 in 2021 and $17,621 in 2020 | 44,547 | 41,943 |
| Subscriber accounts and deferred contract acquisition costs, net of accumulated amortization of $352,307 in 2021 and $254,928 in 2020 | 1,034,596 | 1,102,977 |
| Dealer network and other intangible assets, net of accumulated amortization of $44,658 in 2021 and $32,118 in 2020 | 108,833 | 113,010 |
| Deferred income tax asset, net | 584 | 584 |
| Operating lease right-of-use asset | 19,802 | 17,962 |
| Other assets | 25,072 | 20,309 |
| Total assets | $ 1,290,809 | $ 1,346,663 |
| **Liabilities and Stockholders' Equity** | | |
| Current liabilities: | | |
| Accounts payable | $ 16,040 | $ 20,728 |
| Other accrued liabilities | 59,182 | 58,721 |
| Deferred revenue | 13,564 | 13,300 |
| Holdback liability | 6,170 | 8,536 |
| Current portion of long-term debt | 8,225 | 8,225 |
| Total current liabilities | 103,181 | 109,510 |
| Non-current liabilities: | | |
| Long-term debt | 1,003,137 | 970,994 |
| Long-term holdback liability | 1,124 | 1,223 |
| Operating lease liabilities | 16,163 | 15,305 |
| Other liabilities | 71,783 | 89,038 |
| Total liabilities | 1,195,388 | 1,186,070 |
| Commitments and contingencies | | |
| Stockholders' equity: | | |
| Preferred stock, $0.01 par value. Authorized 5,000,000 shares; no shares issued | — | — |
| Common stock, $0.01 par value. Authorized 45,000,000 shares; issued and outstanding 22,500,000 shares at both June 30, 2021 and December 31, 2020 | 225 | 225 |
| Additional paid-in capital | 379,175 | 379,175 |
| Accumulated deficit | (282,726) | (216,714) |
| Accumulated other comprehensive (loss) income, net | (1,253) | (2,093) |
| Total stockholders' equity | 95,421 | 160,593 |
| Total liabilities and stockholders' equity | $ 1,290,809 | $ 1,346,663 |

**MONITRONICS INTERNATIONAL, INC. AND SUBSIDIARIES**
**Condensed Consolidated Statements of Operations and Comprehensive Income (Loss)**
**Amounts in thousands**
**(unaudited)**

| | Six Months Ended June 30, | |
|---|---|---|
| | 2021 | 2020 |
| Net revenue | $ 266,515 | $ 243,383 |
| Operating expenses: | | |
| Cost of services | 73,163 | 55,634 |
| Selling, general and administrative, including long-term incentive compensation | 80,258 | 76,994 |
| Radio conversion costs | 18,629 | 8,491 |
| Amortization of subscriber accounts, deferred contract acquisition costs and other intangible assets | 109,896 | 107,649 |
| Depreciation | 8,076 | 6,560 |
| Goodwill Impairment | — | 81,943 |
| | 290,022 | 337,271 |
| Operating loss | (23,507) | (93,888) |
| Other expense: | | |
| Interest expense | 40,500 | 40,549 |
| Refinancing expense | 710 | — |
| | 41,210 | 40,549 |
| Loss before income taxes | (64,717) | (134,437) |
| Income tax expense | 1,295 | 1,220 |
| Net loss | (66,012) | (135,657) |
| Other comprehensive loss: | | |
| Unrealized gain (loss) on derivative contracts, net of tax | 840 | (1,794) |
| Total other comprehensive income (loss), net of tax | 840 | (1,794) |
| Comprehensive loss | $ (65,172) | $ (137,451) |

**MONITRONICS INTERNATIONAL, INC. AND SUBSIDIARIES**
**Condensed Consolidated Statements of Cash Flows**
**Amounts in thousands**
**(unaudited)**

| | Six Months Ended June 30, 2021 | Six Months Ended June 30, 2020 |
|---|---|---|
| Cash flows from operating activities: | | |
| Net loss | $ (66,012) | $ (135,657) |
| Adjustments to reconcile net loss to net cash provided by operating activities: | | |
| Amortization of subscriber accounts, deferred contract acquisition costs and other intangible assets | 109,896 | 107,649 |
| Depreciation | 8,076 | 6,560 |
| Long-term incentive compensation | 129 | 536 |
| Trade bad debt expense | 3,620 | 4,720 |
| Goodwill impairment | — | 81,943 |
| Other non-cash activity, net | 3,134 | 2,091 |
| Changes in assets and liabilities: | | |
| Trade receivables | (1,055) | (3,047) |
| Inventories | (5,860) | (764) |
| Prepaid expenses and other assets | (7,110) | (4,058) |
| Subscriber accounts - deferred contract acquisition costs | (2,529) | (1,223) |
| Payables and other liabilities | (8,179) | (3,139) |
| Net cash provided by operating activities | 34,110 | 55,611 |
| Cash flows from investing activities: | | |
| Capital expenditures | (10,317) | (7,781) |
| Cost of subscriber accounts acquired, net of holdback payments | (33,354) | (58,072) |
| Cost of intangible assets acquired | (8,363) | (428) |
| Net cash used in investing activities | (52,034) | (66,281) |
| Cash flows from financing activities: | | |
| Proceeds from long-term debt | 56,500 | 65,000 |
| Payments on long-term debt | (19,113) | (21,613) |
| Payment of refinancing costs | (5,380) | — |
| Contingent bonus payments on dealer acquired accounts | (1,975) | (2,086) |
| Earnout Payments | (10,975) | — |
| Net cash provided by financing activities | 19,057 | 41,301 |
| Net increase in cash, cash equivalents and restricted cash | 1,133 | 30,631 |
| Cash, cash equivalents and restricted cash at beginning of period | 6,294 | 15,001 |
| Cash, cash equivalents and restricted cash at end of period | $ 7,427 | $ 45,632 |
| Supplemental cash flow information: | | |
| State taxes paid, net | $ 2,150 | $ 2,532 |
| Interest paid | 38,047 | 39,973 |
| Accrued capital expenditures | 994 | 806 |
| Earnout Payments liability | 102,123 | 85,852 |

**MONITRONICS INTERNATIONAL, INC. AND SUBSIDIARIES**
**Condensed Consolidated Statement of Stockholders' Equity**
**Amounts in thousands, except share amounts**
**(unaudited)**

| | Common Stock | | Additional Paid-in Capital | Accumulated Deficit | Accumulated Other Comprehensive Income (Loss) | Total Stockholders' Equity |
|---|---|---|---|---|---|---|
| | Shares | Amount | | | | |
| Balance as of December 31, 2020 | 22,500,000 | $ 225 | $ 379,175 | $ (216,714) | $ (2,093) | $ 160,593 |
| Net loss ................................................ | — | — | — | (66,012) | — | (66,012) |
| Other comprehensive income ................ | — | — | — | — | 840 | 840 |
| Balance at June 30, 2021 | 22,500,000 | $ 225 | $ 379,175 | $ (282,726) | $ (1,253) | $ 95,421 |

| | Common Stock | | Additional Paid-in Capital | Accumulated Deficit | Accumulated Other Comprehensive Income (Loss) | Total Stockholders' Equity |
|---|---|---|---|---|---|---|
| | Shares | Amount | | | | |
| Balance at December 31, 2019 | 22,500,000 | $ 225 | $ 379,175 | $ (33,331) | $ 9 | $ 346,078 |
| Adoption of ASU 2016-13 | — | — | — | (1,627) | — | (1,627) |
| Adjusted balance at January 1, 2020 | 22,500,000 | $ 225 | $ 379,175 | $ (34,958) | $ 9 | $ 344,451 |
| Net loss ................................................ | — | — | — | (135,657) | — | (135,657) |
| Other comprehensive loss .................... | — | — | — | — | (1,794) | (1,794) |
| Balance at June 30, 2020 | 22,500,000 | $ 225 | $ 379,175 | $ (170,615) | $ (1,785) | $ 207,000 |

**MONITRONICS INTERNATIONAL, INC. AND SUBSIDIARIES**
**Notes to Condensed Consolidated Financial Statements**
**For the Period Ended June 30, 2021**
**(unaudited)**

## (1) Basis of Presentation

Monitronics International, Inc. and its subsidiaries (collectively, "Monitronics" or the "Company", doing business as Brinks Home™) provide residential customers and commercial client accounts with monitored home and business security systems, as well as interactive and home automation services, in the United States, Canada and Puerto Rico. Monitronics customers are obtained through our direct-to-consumer sales channel (the "Direct to Consumer Channel"), which offers professional installation security solutions, as well as Do-It-Yourself options, and our exclusive authorized dealer network (the "Network Sales Channel"), which provides product and installation services, as well as support to customers.

The Company's unaudited condensed consolidated balance sheet as of June 30, 2021, and the unaudited condensed statements of operations and cash for the six months ended June 30, 2021 and 2020, include the results of Monitronics and all of its direct and indirect subsidiaries. The accompanying interim condensed consolidated financial statements are unaudited but, in the opinion of management, reflect all adjustments (consisting of normal recurring accruals) necessary for a fair presentation of the results for such periods in accordance with generally accepted accounting principles in the United States ("GAAP"). The results of operations for any interim period are not necessarily indicative of results for the full year. These unaudited condensed consolidated financial statements should be read in conjunction with the Monitronics Annual Report on Form 10-K for the year ended December 31, 2020, filed with the SEC on March 18, 2021.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of revenue and expenses for each reporting period. The significant estimates made in preparation of the Company's condensed consolidated financial statements primarily relate to valuation of subscriber accounts, deferred tax assets and other indefinite-lived intangible assets. These estimates are based on management's best estimates and judgment. Management evaluates its estimates and assumptions on an ongoing basis using historical experience and other factors, including consideration of the potential impacts of the COVID-19 pandemic, and adjusts them when facts and circumstances change. As the effects of any future events cannot be determined with any certainty, actual results could differ from the estimates upon which the carrying values were based.

The Company has reclassified certain prior period amounts on the condensed consolidated statement of cash flows to conform to current period presentation.

*AT&T Digital Life Asset Purchase*

On April 9, 2021, the Company, as buyer, entered into a Master Sales and Marketing Agreement and Technology Transfer Agreement (the "Agreements") with AT&T Digital Life ("Digital Life"), as seller. Pursuant to the Agreements, the Company purchased a list of approximately 190,000 active customers with the exclusive right to sign these customers to monitoring contracts with the Company until August 2025 (the "customer-related intangible asset"), as well as a perpetual license to certain technology to support the radio conversion process for customers that elect to convert to the Company's services (the "technology license asset", together with the customer-related intangible asset, the "agreement assets").

The Agreements provide for an upfront cash payment for the agreement assets of $7,500,000 to Digital Life at the closing date, and a second $7,500,000 cash payment in the future period contingent on a certain number of customers having converted to the Company's services.

The transaction was accounted for as an asset acquisition by allocating the total cost to the acquired assets on a relative fair value basis. The company recognized $3,916,000 for the customer-related intangible asset and $4,434,000 for the technology license asset at the closing date of April 9, 2021. Included in the amounts recognized for the customer-related intangible asset and technology license asset is $850,000 of direct acquisition costs. These assets are presented in Dealer network and other intangible assets, net of accumulated amortization, in our condensed consolidated balance sheets. Future contingent payments for the agreement assets are not deemed "probable" as defined by ASC 450-20 ("Contingencies – Loss Contingences") for the period ending June 30, 2021 and are therefore not reflected in our condensed consolidated balance sheets. The company will continue to assess the probability each period going forward and will recognize the contingent payments as intangible assets in the subsequent period when payment becomes probable as defined by ASC 450-20.

Additionally, the Agreements establish that the Company will pay a commission to Digital Life for a certain limited number of months of each converted customer's life measured from the conversion date, subject to adjustments for customer accounts that are no longer active. The commission obligation is accounted for as per ASC 450-20 and ASC 340-40 ("Other Assets and Deferred Costs – Contracts with Customers") according to actual customer conversion activity each period. Capitalized and accrued commissions payable to Digital Life for the period ending June 30, 2021 were not material to our condensed consolidated financial statements.

**(2) Recent Accounting Pronouncements**

In December 2019, the FASB issued ASU 2019-12, *Simplifying the Accounting for Income Taxes* ("ASU 2019-12"). ASU 2019-12 simplifies the accounting for income taxes by removing certain exceptions to the general principles in ASC 740, *Income Taxes*. We adopted ASU 2019-12 effective January 1, 2021. The adoption of this ASU did not have a material impact on our condensed consolidated financial statements.

In March 2020, the FASB issued ASU 2020-04, *Reference Rate Reform (Topic 848)* ("ASU 2020-04"). ASU 2020-04 provides optional guidance for a limited period of time to ease potential accounting impact associated with transitioning away from reference rates that are expected to be discontinued, such as the London Interbank Offered Rate ("LIBOR"). The amendments in this ASU apply only to contracts, hedging relationships, and other transactions that reference LIBOR or another reference rate expected to be discontinued. The amendments in ASU 2020-04 can be adopted as of March 12, 2020 and are effective through December 31, 2022. The guidance is optional and may be elected over time as reference rate reform activities occur. During the second quarter of 2020, the Company elected to apply the hedge accounting expedients related to probability and the assessments of effectiveness for future LIBOR-indexed cash flows to assume that the index upon which future hedged transactions will be based matches the index on the corresponding derivatives. Application of these expedients preserves the presentation of derivatives consistent with past presentation. The Company continues to evaluate the impact of the guidance and may apply other elections as applicable as additional changes in the market occur.

**(3) Other Accrued Liabilities**

Other accrued liabilities consisted of the following (amounts in thousands):

| | June 30, 2021 | December 31, 2020 |
|---|---|---|
| Accrued payroll and related liabilities | $ 8,215 | $ 11,563 |
| Interest payable | 345 | 278 |
| Income taxes payable | 1,311 | 2,301 |
| Operating lease liabilities | 4,250 | 3,418 |
| Contingent dealer liabilities | 2,061 | 2,756 |
| Earnout Payments liability | 35,646 | 31,633 |
| Other | 7,354 | 6,772 |
| Total Other accrued liabilities | $ 59,182 | $ 58,721 |

**(4) Debt**

Debt consisted of the following (amounts in thousands):

| | June 30, 2021 | December 31, 2020 |
|---|---|---|
| Takeback Loan Facility, matures March 29, 2024, LIBOR plus 6.5%, subject to a LIBOR floor of 1.25%, with an effective rate of 7.8% | $ 804,302 | $ 812,219 |
| Term Loan Facility, matures July 3, 2024, LIBOR plus 5.0%, subject to a LIBOR floor of 1.5%, with an effective rate of 6.6% | 149,268 | 150,000 |
| Revolving Credit Facility, matures July 3, 2024, LIBOR plus 5.0%, subject to a LIBOR floor of 1.5%, or base rate (with a floor of 4.5%) plus 4.0%, with an effective rate of 10.2% | 57,792 | 17,000 |
| | $ 1,011,362 | $ 979,219 |
| Less: Current portion of long-term debt | (8,225) | (8,225) |
| Long-term debt | $ 1,003,137 | $ 970,994 |

*Takeback Loan Facility*

On August 30, 2019 (the “Effective Date”), pursuant to the terms of the chapter 11 reorganization plan (the “Plan”), the Company entered into an $822,500,000 takeback term loan facility (the "Takeback Loan Facility") with the lenders party thereto, and Alter Domus, formerly known as Cortland Capital Market Services, LLC., as administrative agent.

On March 18, 2021, the Company entered into Amendment No. 2 to the Takeback Loan Facility which was accounted for as a modification of the existing debt agreement. This amendment provides additional capacity under financial covenants to facilitate the Company’s growth strategies and includes a 1% interest rate increase beginning in January 2022. The Company capitalized deferred financing costs associated with Amendment No. 2 in the amount of $3,905,000.

On May 28, 2021, the Company entered into Amendment No. 3 to the Takeback Loan Facility. This amendment adds LIBOR replacement provisions and aligns certain covenants with those of the Credit Facilities.

The Takeback Loan Facility requires periodic interest payments based on the selected LIBOR term, or monthly if on a base rate, and quarterly principal payments of $2,056,250, and matures on March 29, 2024. Interest on loans made under the Takeback Loan Facility accrues at an interest rate per year equal to the LIBOR rate (with a floor of 1.25%) plus 6.5% or base rate plus 5.5%; increasing to 7.5% and 6.5% respectively beginning in January 2022. The Takeback Loan Facility, subject to certain exceptions, is guaranteed by each of the Company's existing and future domestic subsidiaries and is secured by substantially all the assets of the Company and such subsidiary guarantors. See note 12, Consolidating Guarantor Financial Information for further information. The Takeback Loan Facility contains customary representations, warranties, covenants and events of default and related remedies.

As of June 30, 2021, the Company has deferred financing costs, net of accumulated amortization, of $3,804,000 related to the Takeback Loan Facility. The deferred financing costs are presented within Long-term debt in our condensed consolidated balance sheets.

*Credit Facilities*

On the Effective Date, pursuant to the terms of the Plan, the Company entered into a $145,000,000 senior secured revolving credit facility, as amended on June 17, 2020 (the "Revolving Credit Facility"), including a $10,000,000 swingline loan, and $150,000,000 in senior secured term loans (the "Term Loan Facility" and together with the Revolving Credit Facility, the "Credit Facilities") with the lenders party thereto, KKR Capital Markets LLC as lead arranger and bookrunner, KKR Credit Advisors (US) LLC as Structuring Advisor and Encina Private Credit SPV, LLC as administrative agent, swingline lender and L/C issuer. On May 5, 2021, the Company entered into Amendment No. 2 to the Credit Facilities which was accounted for as a modification of the existing debt agreement. This amendment provides additional capacity under financial covenants to facilitate the Company’s growth strategies and includes a 1% interest rate increase beginning in January 2022. The Company capitalized deferred financing costs associated with Amendment No. 2 in the amount of $1,475,000.

As of June 30, 2021, the Company had approximately $600,000 available under a standby letter of credit issued. As of June 30, 2021, $85,900,000 is available for borrowing under the Revolving Credit Facility, subject to certain financial covenants.

The maturity date of loans made under the Credit Facilities is July 3, 2024, subject to a springing maturity of March 29, 2024, or earlier, depending on any repayment, refinancing or changes in the maturity date of the Takeback Loan Facility. Interest on loans made under the Credit Facilities accrues at an interest rate per year equal to the LIBOR rate (with a floor of 1.5%) plus 5.0% or base rate (with a floor of 4.5%) plus 4.0%, dependent upon the type of borrowing requested by the Company. In January 2022, the applicable rate increases by 1% as per Amendment No. 2. There is a commitment fee of 0.75% on unused portions of the Revolving Credit Facility.

The Credit Facilities, subject to certain exceptions, are guaranteed by each of the Company's existing and future domestic subsidiaries and are secured by substantially all the assets of the Company and such subsidiary guarantors. See note 12, Consolidating Guarantor Financial Information for further information. The Credit Facilities contain customary representations, warranties, covenants and events of default and related remedies.

As of June 30, 2021, the Company has deferred financing costs, net of accumulated amortization, of $1,440,00 related to the Credit Facilities. The deferred financing costs are presented within Long-term debt in our condensed consolidated balance sheets.

The terms of the Takeback Loan Facility and the Credit Facilities provide for certain financial and nonfinancial covenants. As of June 30, 2021, the Company was in compliance with all required covenants under these financing arrangements.

As of June 30, 2021, principal payments scheduled to be made on the Company's debt obligations are as follows (amounts in thousands):

| | | |
|---|---|---|
| Remainder of 2021 | $ | 4,112 |
| 2022 | | 8,225 |
| 2023 | | 8,225 |
| 2024 | | 996,044 |
| 2025 | | — |
| 2026 | | — |
| Thereafter | | — |
| Total principal payments | | 1,016,606 |
| *Less:* | | |
| Unamortized deferred debt costs and discounts | | 5,244 |
| Total debt on condensed consolidated balance sheet | $ | 1,011,362 |

## (5) Derivatives

*Interest Rate Cap*

In November of 2019, the Company entered into an interest rate cap agreement to reduce the interest rate risk inherent in the Company's variable rate Takeback Loan Facility. The interest rate cap agreement provides the right to receive cash if the reference interest rate rises above a contractual rate. The premium paid for the interest rate cap agreement was $3,020,000, which was the initial fair value of the interest rate cap recorded on the condensed consolidated balance sheets.

The critical terms of the interest rate cap were designed to mirror the terms of the Company's variable rate Takeback Loan Facility and are highly effective at offsetting the cash flows being hedged. The Company designated the interest rate cap as a cash flow hedge of the variability of the LIBOR-based interest payments on $750,000,000 of principal of the Takeback Loan Facility. The interest rate cap agreement will expire on December 31, 2023. The effective portion of the interest rate cap's change in fair value is recorded in Accumulated other comprehensive income (loss). Any ineffective portions of the interest rate cap's change in fair value are recognized in current earnings in Interest expense.

On April 19, 2021, the interest rate cap agreement was simultaneously dedesignated and redesignated to update the assessment of effectiveness methodology to support the ability to change from 1-month LIBOR to 3-month LIBOR for interest payments on the Takeback Loan. Upon redesignation, the hedge relationship continues to be highly effective at offsetting the cash flows being hedged. The amounts previously recognized in Accumulated other comprehensive income (loss) relating to the dedesignation ("frozen AOCI") are amortized on a straight-line basis to Interest expense over the remaining life of the interest rate cap agreement.

During the six months ended June 30, 2021, interest expense of $366,000 was reclassified from Accumulated other comprehensive income (loss) to Interest expense on the condensed consolidated statements of operations and comprehensive income (loss). Of these amounts, $95,000 represents amortization of frozen AOCI from amounts relating to the dedesignation. The Company expects to reclassify approximately $738,000 from Accumulated other comprehensive income (loss) to Interest expense on the condensed consolidated statements of operations and comprehensive income (loss) in the next twelve months.

The fair value of the interest rate cap was $592,000 at June 30, 2021, and constituted an asset of the Company. The fair value of the interest rate cap is included in non-current Other assets, net on the condensed consolidated balance sheets based on the maturity date of the derivative instrument. See note 6, Fair Value Measurements for related fair value disclosures.

The impact of the derivatives on the condensed consolidated financial statements is depicted below (amounts in thousands):

| | Six Months Ended June 30, 2021 | | Six Months Ended June 30, 2020 | |
|---|---|---|---|---|
| Effective portion of gain (loss) recognized in Accumulated other comprehensive income (loss) due to change in fair value of asset | $ | 474 | $ | (2,162) |
| Effective portion of loss reclassified from Accumulated other comprehensive income (loss) into Net income (loss) (b) | $ | 271 | $ | 368 |
| Reclassification of loss from Accumulated other comprehensive income (loss) into Net income (loss) related to dedesignation (b) | $ | 95 | $ | — |

(b) Amounts are included in Interest expense in the condensed consolidated statements of operations and comprehensive income (loss).

On July 1, 2021, the Company elected to dedesignate the interest rate cap agreement and will discontinue hedge accounting treatment. The remaining amount of unrealized losses in Accumulated other comprehensive income (loss) will be amortized to Interest expense in our condensed consolidated statements of operations and comprehensive income (loss) over the remaining term of the agreement. Subsequent to the dedesignation date, changes in the fair value of the of the interest rate cap will be recorded in Unrealized gain (loss) on derivative financial instruments, net in our condensed consolidated statements of operations and comprehensive income (loss).

## (6) Fair Value Measurements

According to the FASB ASC Topic 820, *Fair Value Measurement*, fair value is defined as the amount that would be received for selling an asset or paid to transfer a liability in an orderly transaction between market participants and requires that assets and liabilities carried at fair value are classified and disclosed in the following three categories:

- Level 1 - Quoted prices for identical instruments in active markets.
- Level 2 - Quoted prices for similar instruments in active or inactive markets and valuations derived from models where all significant inputs are observable in active markets.
- Level 3 - Valuations derived from valuation techniques in which one or more significant inputs are unobservable in any market.

The following summarizes the fair value level of assets that are measured on a recurring basis at June 30, 2021 and December 31, 2020 (amounts in thousands):

| | Level 1 | | Level 2 | | Level 3 | | Total | |
|---|---|---|---|---|---|---|---|---|
| **June 30, 2021** | | | | | | | | |
| Interest rate cap agreement - assets (a) | $ | — | $ | 592 | $ | — | $ | 592 |
| Total | $ | — | $ | 592 | $ | — | $ | 592 |
| **December 31, 2020** | | | | | | | | |
| Interest rate cap agreement - assets (a) | $ | — | $ | 117 | $ | — | $ | 117 |
| Total | $ | — | $ | 117 | $ | — | $ | 117 |

(a) Interest rate cap asset value is included in non-current Other assets on the condensed consolidated balance sheets.

The Company has determined that the significant inputs used to value the interest rate cap fall within Level 2 of the fair value hierarchy. As a result, the Company has determined that its interest rate cap valuation is classified in Level 2 of the fair value hierarchy.

Carrying values and fair values of financial instruments that are not carried at fair value are as follows (amounts in thousands):

| | June 30, 2021 | | December 31, 2020 | |
|---|---|---|---|---|
| Long term debt, including current portion: | | | | |
| Carrying value | $ | 1,003,137 | $ | 979,219 |
| Fair value (a) | $ | 991,644 | $ | 883,377 |

(a) The fair value is based on market quotations from third party financial institutions and is classified as Level 2 in the hierarchy.

The Company’s other financial instruments', including cash and cash equivalents, restricted cash, accounts receivable, accounts payable and contingent dealer liabilities, carrying values approximate their fair values because of their nature.

## (7) Stock-Based Compensation

On August 3, 2020, the Board of Directors (the "Board") adopted the Monitronics International, Inc. 2020 Incentive Award Plan (the "Plan"), pursuant to which the company may grant cash, equity and equity-based incentive awards to eligible service providers. The Plan provides for the grant of non-qualified stock options, stock appreciation rights, restricted stock, restricted stock units, dividend equivalents and other stock or cash-based awards (collectively, "awards"). Non-employee directors of the Company, as well as employees and consultants of the Company or its subsidiaries (collectively, "participants") are eligible to receive awards under the Plan. The Plan authorizes the issuance of 2,500,000 shares of common stock.

As of June 30, 2021, and pursuant to the Plan, a total of 1,471,750 Performance-Based Restricted Stock Unit awards ("PRSUs") and a total of 455,205 Time-Based Restricted Stock Unit awards ("TRSUs") are outstanding. These awards cover shares of common stock and were granted to certain of the company's directors, executives and senior leadership employees. Each RSU represents a contractual right to receive one share of the company’s common stock upon becoming fully vested and payable subject to the terms and conditions of the respective award agreement. Both the PRSUs and the TRSUs are subject to performance condition such that the awards are not payable unless there is a change in control of the company. Because a change in control is not probable of occurring as of the reporting date, no compensation expense has been recognized for either the PRSUs or the TRSUs for the period ended June 30, 2021.

## (8) Stockholders' Equity

*Common Stock*

The Company had 22,500,000 issued and outstanding shares of Common Stock, par value $0.01 per share ("Common Stock") as of both June 30, 2021 and December 31, 2020.

*Accumulated Other Comprehensive Income (Loss)*

The following table provides a summary of the changes in Accumulated other comprehensive income (loss) for the six months ended June 30, 2021 (amounts in thousands):

| | | Accumulated Other Comprehensive Income (Loss) |
|---|---|---|
| Balance at December 31, 2020 | $ | (2,093) |
| Unrealized gain on interest rate cap recognized through Accumulated other comprehensive income (loss), net of income tax of $0 | | 499 |
| Interest cost of interest rate cap reclassified into Net loss, net of income tax of $0 (a) | | 182 |
| Balance at March 31, 2021 | $ | (1,412) |
| Unrealized loss on interest rate cap recognized through Accumulated other comprehensive income (loss), net of income tax of $0 | | (25) |
| Interest cost of interest rate cap reclassified into Net loss, net of income tax of $0 (a) | | 184 |
| Balance at June 30, 2021 | $ | (1,253) |

(a) Amounts reclassified into Net loss are included in Interest expense on the condensed consolidated statements of operations. See note 5, Derivatives for further information.

The following table provides a summary of the changes in Accumulated other comprehensive income (loss) for the six months ended June 30, 2020 (amounts in thousands):

| | | Accumulated Other Comprehensive Income (Loss) |
|---|---|---|
| Balance at December 31, 2019 | $ | 9 |
| Unrealized loss on interest rate cap recognized through Accumulated other comprehensive income (loss), net of income tax of $0 | | (1,997) |
| Interest cost of interest rate cap reclassified into Net loss, net of income tax of $0 (a) | | 184 |
| Balance at March 31, 2020 | $ | (1,804) |
| Unrealized loss on interest rate cap recognized through Accumulated other comprehensive income (loss), net of income tax of $0 | | (165) |
| Interest cost of interest rate cap reclassified into Net loss, net of income tax of $0 (a) | | 184 |
| Balance at June 30, 2020 | $ | (1,785) |

(a) Amounts reclassified into Net loss are included in Interest expense on the condensed consolidated statements of operations. See note 5, Derivatives for further information

## (9) Commitments, Contingencies and Other Liabilities

The Company is involved in litigation and similar claims incidental to the conduct of its business. Matters that are probable of unfavorable outcome to the Company and which can be reasonably estimated are accrued. Such accruals are based on information known about the matters, management's estimate of the outcomes of such matters and experience in contesting, litigating and settling similar matters. In management's opinion, none of the pending actions are likely to have a material adverse impact on the Company's financial position or results of operations. The Company accrues and expenses legal fees related to loss contingency matters as incurred.

*Asset Purchase Agreements Subject to Earnout Payments*

On June 17, 2020, the Company acquired certain contracts for the provision of alarm monitoring and related services (the "Accounts") as well as the related accounts receivable, intellectual property and equipment inventory of Protect America, Inc. The Company paid approximately $16,600,000 at closing and will make 50 subsequent monthly payments ("Earnout Payments" will here to be defined as contingent payments to acquire subscriber accounts) consisting of a portion of the revenue attributable to the Accounts, subject to adjustment for Accounts that are no longer active, which began in August 2020. The transaction was accounted for as an asset acquisition with the cost of the assets acquired recorded as of June 17, 2020 and an estimated undiscounted liability for the Earnout Payments of approximately $86,000,000. The Earnout Payments liability for Protect America was estimated based on the terms of the payout and the forecasted attrition of the Protect America subscriber base. The estimated Earnout Payments liability for Protect America as of June 30, 2021 is approximately $70,300,000. Of this amount, $42,300,000 is presented within non-current Other Liabilities, and the remainder is presented within current Other accrued liabilities on the consolidated balance sheets.

On December 23, 2020, the Company completed a transaction (the "Select Security Transaction") to acquire approximately 40,000 alarm monitoring contracts (“Accounts”) from Kourt Security Partners, LLC, doing business as Select Security (the "Seller"). The Company will take ownership of the Accounts through an earnout structure that includes a $10,914,000 upfront payment and 50 subsequent monthly payments ("Earnout Payments") consisting of a portion of the revenue attributable to the Accounts, subject to adjustment for Accounts that are no longer active. The Seller transferred title of the Accounts and other certain business assets to GS Security Alarm LLC ("GSSA"), a bankruptcy-remote special purpose vehicle designed only to transact the sale of Accounts and related assets to the Company. The Company was significantly involved in the design of GSSA; however, the Company does not own any equity interest in GSSA. Accordingly, GSSA was identified as a consolidated variable interest entity (“VIE”) of the Company. On the closing date, the Company recorded a discounted liability of $31,300,000 representing the estimated Earnout Payments owed to GSSA’s equity holder. The Earnout Payments liability was estimated based on the terms of the payout and the forecasted attrition of the subscriber base, discounted at an effective interest rate of 10.9%. At June 30, 2021, the total Earnout Payments liability to GSSA’s equity holder is $31,800,000. Of this amount, $24,200,000 is presented within non-current Other liabilities and the remainder is presented within current Other accrued liabilities on the consolidated balance sheets.

We monitor actual versus forecasted attrition to identify the need for potential adjustments to the Earnout Payments liabilities each period. The monthly Earnout Payments are classified as Cash flows from financing activities on the consolidated statements of cash flows.

## (10) Revenue Recognition

*Disaggregation of Revenue*

Revenue is disaggregated by source of revenue as follows (in thousands):

| | Six Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | 2021 | | 2020 | |
| Alarm monitoring revenue | $ | 235,416 | $ | 221,071 |
| Product, installation and service revenue | | 29,026 | | 20,007 |
| Other revenue | | 2,073 | | 2,305 |
| Total Net revenue | $ | 266,515 | $ | 243,383 |

*Contract Balances*

The following table provides information about receivables, contract assets and contract liabilities from contracts with customers (in thousands):

| | June 30, 2021 | | December 31, 2020 | |
|---|---|---|---|---|
| Trade receivables, net | $ | 10,795 | $ | 13,360 |
| Contract assets, net - current portion (a) | $ | 17,473 | $ | 13,982 |
| Contract assets, net - long-term portion (b) | $ | 19,001 | $ | 16,319 |
| Deferred revenue | $ | 13,564 | $ | 13,300 |

(a) Amount is included in Prepaid and other current assets in the unaudited condensed consolidated balance sheets.
(b) Amount is included in Other assets in the unaudited condensed consolidated balance sheets.

## (11) Leases

The Company primarily leases buildings and equipment. The Company determines if a contract is a lease at the inception of the arrangement. The Company reviews all options to extend, terminate, or purchase its right of use assets at the inception of the lease and accounts for these options when they are reasonably certain of being exercised. Certain real estate leases contain lease and non-lease components, which are accounted for separately.

Leases with an initial term of 12 months or less are not recorded on the condensed consolidated balance sheet. Lease expense for these leases is recognized on a straight-line basis over the lease term.

All of the Company's leases are currently determined to be operating leases.

*Components of Lease Expense*

The components of lease expense were as follows (in thousands):

| | Six Months Ended June 30, 2021 | Six Months Ended June 30, 2020 |
|---|---|---|
| Operating lease cost (c) | $ 753 | $ 391 |
| Operating lease cost (d) | 1,856 | 2,137 |
| Total operating lease cost | $ 2,609 | $ 2,528 |

(c) Amount is included in Cost of services in the unaudited condensed consolidated statements of operations and comprehensive income (loss).
(d) Amount is included in Selling, general and administrative, including stock-based and long-term incentive compensation in the unaudited condensed consolidated statements of operations and comprehensive income (loss).

*Remaining Lease Term and Discount Rate*

The following table presents the weighted-average remaining lease term and the weighted-average discount rate:

| | As of June 30, 2021 |
|---|---|
| Weighted-average remaining lease term for operating leases (in years) | 7.9 |
| Weighted-average discount rate for operating leases | 11.2 % |

All of the Company's lease contracts do not provide a readily determinable implicit rate. For these contracts, the Company's estimated incremental borrowing rate is based on information available either upon adoption of ASU 2016-02, Leases (Topic 842) or at the inception of the lease.

*Supplemental Cash Flow Information*

The following is the supplemental cash flow information associated with the Company's leases (in thousands):

| | Six Months Ended June 30, 2021 | Six Months Ended June 30, 2020 |
|---|---|---|
| Cash paid for amounts included in the measurement of lease liabilities: | | |
| Lease payments included in cash flows from operating activities (a) | $ 2,294 | $ 1,963 |
| Right-of-use assets obtained in exchange for new: | | |
| Operating lease liabilities | $ 2,959 | $ 663 |

(a) Cash flow impacts from Operating lease right-of-use assets and Operating lease liabilities are presented net on the cash flow statement in changes in Payables and other liabilities.

*Maturities of Lease Liabilities*

As of June 30, 2021, maturities of lease liabilities were as follows:

| | | |
|---|---|---|
| Remainder of 2021 | $ | 2,302 |
| 2022 | | 4,391 |
| 2023 | | 3,937 |
| 2024 | | 3,694 |
| 2025 | | 3,344 |
| Thereafter | | 14,167 |
| Total lease payments | $ | 31,835 |
| Less: Interest | | (11,422) |
| Total lease obligations | $ | 20,413 |

**(12) Consolidating Guarantor Financial Information**

Monitronics (the "Parent Issuer") entered into the Takeback Loan Facility and the Credit Facilities in August 2019 and both are guaranteed by all of the Company's existing domestic subsidiaries. Consolidating guarantor financial information has not been presented in these notes as substantially all of the Company's operations are now conducted by the Parent Issuer entity. Due to the Select Security Transaction, $32,316,000 of subscriber accounts and $211,900 of net accounts receivable are held in trust by GSSA for the period ending June 30, 2021. GSSA is a consolidated VIE and a non-guarantor that will hold the subscriber accounts and related accounts receivable in trust until title of the assets transfers to the Company in accordance with the agreement. The Company believes that disclosing any additional information would not be material in evaluating the sufficiency of the guarantees.