

# **FINANCIAL CONTROLS AND REPORTING POLICY**

**EFFECTIVE DATE: January 15, 2024**

**DOCUMENT NO.: FIN-2024-001**

WHEREAS, Nexus Industrial Intelligence, Inc., a Delaware corporation (the "Company"), develops and provides proprietary artificial intelligence and machine learning software solutions for industrial applications;

WHEREAS, the Company requires comprehensive financial controls and reporting standards that address its technology-driven business model and complex revenue streams; and

WHEREAS, the Board of Directors has determined it to be in the Company's best interests to adopt this Financial Controls and Reporting Policy (this "Policy").

NOW, THEREFORE, the Company hereby adopts the following Policy:

## **1.0 FINANCIAL CONTROLS AND REPORTING POLICY**

### **1.1 Revenue Recognition Standards for SaaS Licensing**

(a) The Company shall recognize revenue from its NexusCore™ Industrial AI Platform and related software-as-a-service offerings in accordance with ASC 606 and the following criteria:

(i) Identification of customer contracts with specific performance obligations; (ii) Determination of transaction price including variable consideration; (iii) Allocation of transaction price to performance obligations; and (iv) Recognition of revenue upon satisfaction of performance obligations.

(b) Multi-year enterprise contracts shall be recognized ratably over the subscription term, with any implementation services recognized as performed.

(c) Contract modifications and amendments shall be evaluated to determine whether they constitute:

(i) Separate contracts requiring independent revenue recognition; (ii) Termination of existing contract and creation of new contract; or (iii) Modification of existing contract requiring prospective or cumulative adjustment.

(d) Usage-based pricing components shall be recognized based on:

(i) Actual usage measured at defined intervals; (ii) Minimum commitment levels specified in contracts; and (iii) Variable consideration constraints for usage estimates.

## **1.2 AI Technology Asset Valuation**

(a) The Company's proprietary artificial intelligence and machine learning assets shall be valued according to:

(i) Direct development costs; (ii) Allocated overhead costs; (iii) Capitalized research and development expenses; and (iv) Fair market value assessments by qualified third parties.

(b) Impairment testing shall be conducted quarterly for AI/ML assets considering:

(i) Technical obsolescence indicators; (ii) Market competition and technological advances; (iii) Customer adoption metrics and usage patterns; and (iv) Revenue generation capability.

(c) Amortization of capitalized AI/ML assets shall follow:

(i) Straight-line methodology over estimated useful life; (ii) Regular reassessment of useful life assumptions; (iii) Adjustment for significant technological changes; and (iv) Documentation of amortization policy changes.

## **1.3 Internal Controls for Cloud-Based Services**

(a) The Company shall maintain SOC 2 Type II compliance for all cloud-based services, including:

(i) Security controls; (ii) Availability monitoring; (iii) Processing integrity verification; and (iv) Confidentiality safeguards.

(b) Continuous monitoring procedures shall include:

(i) Real-time system performance metrics; (ii) Automated alert mechanisms; (iii) Incident response protocols; and (iv) Service level agreement compliance tracking.

(c) Third-party service provider oversight shall encompass:

(i) Annual vendor security assessments; (ii) Contractual compliance monitoring; (iii) Service quality metrics review; and (iv) Contingency planning for vendor disruptions.

## **1.4 Financial Data Security and Privacy Controls**

(a) All financial data shall be protected through:

(i) Encryption at rest and in transit; (ii) Role-based access controls; (iii) Audit logging and monitoring; and (iv) Regular security assessments.

(b) Data retention and disposal procedures shall include:

(i) Classification-based retention schedules; (ii) Secure destruction protocols; (iii) Compliance with regulatory requirements; and (iv) Documentation of disposal activities.

(c) Access control management shall require:

(i) Quarterly access reviews; (ii) Segregation of duties enforcement; (iii) Privileged account monitoring; and (iv) Immediate termination of access upon employee departure.

## **1.5 Reporting Requirements**

(a) Financial reporting shall include:

(i) Monthly closing procedures with reconciliations; (ii) Quarterly financial statements with AI segment reporting; (iii) Annual audited financial statements; and (iv) Board of Directors financial package.

(b) Key performance indicators shall be reported monthly:

(i) Customer acquisition and retention metrics; (ii) Revenue per customer analytics; (iii) AI platform usage statistics; and (iv) Operating efficiency measures.

(c) Compliance reporting shall encompass:

(i) SOC 2 audit results; (ii) Privacy regulation compliance status; (iii) Security incident reports; and (iv) Internal control effectiveness assessments.

## **2.0 ACCOUNTING PROCEDURES AND STANDARDS**

### **2.1 Subscription Revenue Recognition**

(a) The Company shall recognize subscription revenue according to the following criteria:

(i) Contract existence with commercial substance; (ii) Identifiable rights regarding goods/services; (iii) Identifiable payment terms; (iv) Probable collection of consideration; and (v) Transfer of control to customer.

(b) Multi-year Enterprise Contracts shall be subject to the following provisions:

(i) Revenue allocation across performance periods must reflect the standalone selling price of each component; (ii) Material rights granted to customers shall be treated as separate performance obligations; (iii) Contract modifications shall be evaluated to determine whether they constitute separate contracts; and (iv) Volume discounts shall be accounted for as variable consideration.

(c) Performance Obligation Identification Requirements:

(i) Distinct goods or services shall be identified separately; (ii) Series of substantially similar services shall be treated as a single performance obligation; (iii) Customer options for additional goods/services shall be evaluated for materiality; and (iv) Non-refundable upfront fees shall be assessed for distinct benefit delivery.

## **2.2 R&D Expense Capitalization**

(a) Research and development costs shall be capitalized when:

(i) Technical feasibility is established; (ii) Management intends to complete the project; (iii) Resources are available for completion; and (iv) Future economic benefits are probable.

(b) Specific Capitalization Criteria:

(i) Development phase costs must be clearly distinguishable from research phase expenses; (ii) Internal labor costs shall be capitalized only when directly attributable to development; (iii) Overhead allocation must follow documented methodology; and (iv) Impairment assessments shall be conducted quarterly.

(c) Documentation Requirements:

(i) Technical feasibility studies must be formally documented; (ii) Resource allocation plans shall be maintained; (iii) Economic benefit projections must be updated semi-annually; and (iv) Capitalization decisions shall be reviewed by the audit committee.

## **2.3 Contract Asset Recognition**

(a) Contract assets shall be recognized when:

(i) Performance obligations are satisfied; (ii) Payment is not yet due; and (iii) Right to consideration is conditional.

(b) Measurement and Valuation Guidelines:

(i) Initial recognition at transaction price less any amounts invoiced; (ii) Regular assessment for impairment using expected credit loss model; (iii) Separate presentation from contract receivables; and (iv) Disclosure of significant financing components.

(c) Contract Modification Treatment:

(i) Prospective treatment for distinct additional services; (ii) Cumulative catch-up adjustment for modifications within same performance obligation; (iii) Combination of both approaches for hybrid modifications; and (iv) Documentation of modification impact assessment.

## **2.4 Deferred Revenue Treatment**

(a) Deferred revenue shall be recorded for:

(i) Advance payments received; (ii) Undelivered performance obligations; and (iii) Implementation services in progress.

(b) Recognition and Measurement Requirements:

(i) Systematic recognition based on performance obligation satisfaction; (ii) Regular review of estimated service delivery timelines; (iii) Adjustment of recognition patterns for changed circumstances; and (iv) Documentation of significant judgments and estimates.

## **2.5 ASC 606 Compliance Requirements**

### **(a) Revenue Recognition Documentation:**

(i) Maintenance of detailed contract reviews; (ii) Performance obligation identification worksheets; (iii) Transaction price allocation calculations; and (iv) Timing of transfer of control assessment.

### **(b) Disclosure Requirements:**

(i) Disaggregation of revenue into appropriate categories; (ii) Contract balances and significant changes therein; (iii) Performance obligations descriptions and timing; and (iv) Significant judgments in application of the standard.

## **2.6 Special Considerations**

### **(a) Implementation Services:**

(i) Assessment of distinct performance obligation status; (ii) Recognition pattern determination; (iii) Integration with software deliverables; and (iv) Customer acceptance criteria.

### **(b) Contract Combinations:**

(i) Evaluation of contracts entered simultaneously; (ii) Assessment of commercial objective and pricing dependencies; (iii) Documentation of combination decisions; and (iv) Impact on revenue recognition timing.

## **2.7 Internal Controls and Review Procedures**

### **(a) Regular Review Requirements:**

(i) Quarterly review of significant contracts; (ii) Annual assessment of capitalization policies; (iii) Semi-annual review of recognition patterns; and (iv) Documentation of review conclusions.

### **(b) Approval Requirements:**

(i) Senior management approval for non-standard terms; (ii) Audit committee review of significant judgments; (iii) Legal department review of contract modifications; and (iv) Finance committee approval of policy changes.

## **3.0 TECHNOLOGY ASSET MANAGEMENT**

### **3.1 IP Valuation Standards**

#### **(a) Intellectual property shall be valued considering:**

(i) Development costs, including all direct and indirect expenses associated with the creation, testing, and deployment of proprietary technology assets; (ii) Market comparables, with reference to similar technologies, licensing arrangements, and recent market transactions; (iii) Revenue potential, including projected income streams, licensing opportunities, and commercial applications; and (iv) Technological obsolescence risk, assessed through industry analysis and technological advancement forecasts.

(b) Valuation methodology shall incorporate:

(i) Income-based approaches, utilizing discounted cash flow analysis; (ii) Cost-based methodologies, accounting for replacement and reproduction costs; (iii) Market-based comparisons, referencing similar technology transactions; and (iv) Risk-adjusted valuation metrics specific to AI/ML technologies.

(c) Regular revaluation shall occur:

(i) Annually for material technology assets; (ii) Upon significant market changes; (iii) Following substantial technological improvements; and (iv) Prior to any transfer or licensing arrangement.

### **3.2 Software Development Cost Allocation**

(a) Development costs shall be allocated to:

(i) Direct labor, including software engineers, data scientists, and technical architects; (ii) Infrastructure costs, encompassing computing resources and development platforms; (iii) Third-party services, including consultants, contractors, and specialized service providers; and (iv) Overhead allocation, based on established cost accounting principles.

(b) Capitalization criteria shall include:

(i) Technical feasibility of completion; (ii) Intent and ability to complete development; (iii) Probability of generating future economic benefits; (iv) Availability of adequate resources; and (v) Ability to measure attributable costs reliably.

(c) Cost tracking requirements shall specify:

(i) Detailed time recording systems; (ii) Project-specific cost codes; (iii) Regular cost review procedures; and (iv) Documentation of development milestones.

### **3.3 Technology Asset Depreciation**

(a) AI/ML assets shall be depreciated over:

(i) Expected useful life, determined through technical analysis and market forecasts; (ii) Technical obsolescence period, considering industry innovation rates; and (iii) Contract term limitations, where applicable.

(b) Depreciation methodology shall consider:

(i) Straight-line depreciation for standard technology assets; (ii) Accelerated depreciation for rapidly evolving technologies; (iii) Performance-based depreciation for usage-dependent assets; and (iv) Component-based depreciation for complex systems.

(c) Depreciation review requirements include:

(i) Annual reassessment of useful life estimates; (ii) Regular impairment testing; (iii) Documentation of technological changes affecting asset value; and (iv) Adjustment procedures for revised estimates.

### **3.4 Cloud Infrastructure Cost Attribution**

(a) Cloud costs shall be attributed based on:

(i) Direct usage metrics, including compute hours, storage volume, and API calls; (ii) Shared resource allocation, utilizing approved cost distribution methodologies; (iii) Customer-specific instances, with dedicated resource tracking; and (iv) Development environments, separated from production costs.

(b) Cost allocation methodology shall include:

(i) Resource tagging requirements; (ii) Usage monitoring protocols; (iii) Cost center assignment procedures; and (iv) Regular reconciliation processes.

(c) Reporting requirements shall specify:

(i) Monthly cost allocation reports; (ii) Usage trend analysis; (iii) Variance explanations; and (iv) Cost optimization recommendations.

### **3.5 Asset Management Controls**

(a) Technology asset controls shall include:

(i) Regular inventory audits; (ii) Access control procedures; (iii) Change management protocols; and (iv) Security compliance requirements.

(b) Documentation requirements shall specify:

(i) Asset registration procedures; (ii) Maintenance records; (iii) Version control protocols; and (iv) Disposal procedures.

(c) Compliance monitoring shall include:

(i) Regular control assessments; (ii) Audit trail maintenance; (iii) Policy adherence verification; and (iv) Remediation tracking.

### **3.6 Reporting and Review**

(a) Regular reporting shall include:

(i) Quarterly asset valuations; (ii) Development cost analyses; (iii) Depreciation schedules; and (iv) Cloud cost allocation summaries.

(b) Annual review requirements shall specify:

(i) Comprehensive asset portfolio assessment; (ii) Valuation methodology evaluation; (iii) Cost allocation effectiveness review; and (iv) Control framework assessment.

## **4.0 COMPLIANCE AND AUDIT PROCEDURES**

### **4.1 AI Algorithm Audit Requirements**

(a) The Company shall maintain:

(i) Algorithm version control, including: - Documented version history with timestamps - Change logs detailing modifications - Authorized approver signatures - Impact assessments for each iteration - Rollback procedures and contingencies

(ii) Training data documentation, encompassing: - Data source identification and verification - Data quality metrics and validation reports - Bias detection methodologies - Sample retention protocols - Data lineage tracking

(iii) Performance metrics, including: - Accuracy measurements - Precision and recall statistics - False positive/negative rates - Model drift indicators - Response time benchmarks

(iv) Validation procedures, comprising: - Cross-validation protocols - Test case documentation - Independent verification methods - Acceptance criteria - Performance thresholds

### **4.2 Data Privacy Compliance**

(a) The Company shall ensure:

(i) GDPR compliance, including: - Data Protection Impact Assessments (DPIAs) - Subject access request procedures - Right to erasure protocols - Cross-border transfer mechanisms - Breach notification procedures

(ii) CCPA compliance, encompassing: - Consumer rights fulfillment processes - Opt-out mechanisms - Service provider agreements - Data inventory maintenance - Annual disclosure requirements

(iii) Industry-specific regulations, addressing: - HIPAA requirements where applicable - FERPA compliance for educational data - GLBA standards for financial information - PCI DSS for payment data - Sector-specific privacy frameworks

(iv) Contractual privacy obligations, including: - Data processing agreements - Confidentiality provisions - Data handling specifications - Retention requirements - Destruction protocols



### **4.3 Financial Control Testing**

(a) Controls shall be tested for:

- (i) Design effectiveness, including: - Control objective alignment - Risk mitigation adequacy - Process integration assessment - Documentation completeness - Control environment evaluation
- (ii) Operating effectiveness, comprising: - Transaction testing protocols - Sample selection criteria - Evidence collection standards - Exception documentation - Remediation tracking
- (iii) Change management, addressing: - Control modification procedures - Impact analysis requirements - Approval workflows - Implementation verification - Post-change monitoring
- (iv) Exception handling, including: - Deviation documentation - Root cause analysis - Corrective action plans - Management reporting - Follow-up procedures

### **4.4 Third-Party Audit Protocols**

(a) External audits shall address:

- (i) Financial statements, including: - Balance sheet verification - Income statement review - Cash flow analysis - Notes to financial statements - Management representations
- (ii) SOC 2 compliance, encompassing: - Security controls assessment - Availability monitoring - Processing integrity - Confidentiality measures - Privacy safeguards
- (iii) Security controls, comprising: - Access management systems - Encryption protocols - Network security measures - Incident response procedures - Business continuity plans
- (iv) Privacy compliance, addressing: - Data collection practices - Storage security measures - Transfer protocols - Retention policies - Disposal procedures

### **4.5 Continuous Monitoring Requirements**

(a) The Company shall implement:

- (i) Real-time monitoring systems for: - Algorithm performance - Data privacy compliance - Financial control effectiveness - Security measure adherence
- (ii) Periodic assessments of: - Risk management frameworks - Control environment effectiveness - Compliance program adequacy - Audit finding remediation

### **4.6 Reporting and Documentation**

(a) The Company shall maintain:

- (i) Audit documentation including: - Engagement letters - Work papers - Testing evidence - Findings reports - Management responses

(ii) Compliance reports addressing: - Regulatory requirements - Internal control effectiveness - Risk assessment results - Remediation status - Outstanding issues

#### **4.7 Remediation Procedures**

(a) The Company shall establish:

(i) Issue tracking systems for: - Audit findings - Compliance violations - Control deficiencies - Security incidents

(ii) Resolution protocols including: - Root cause analysis - Corrective action plans - Implementation timelines - Effectiveness testing - Close-out procedures

### **EXHIBITS**

**Exhibit A: Control Framework Matrix**

**Exhibit B: Revenue Recognition Decision Tree**

**Exhibit C: Technology Asset Valuation Methodology**

### **APPENDICES**

**Appendix 1: Defined Terms**

**Appendix 2: Compliance Checklist**

**Appendix 3: Audit Program**

IN WITNESS WHEREOF, this Policy has been executed as of the date first written above.

NEXUS INDUSTRIAL INTELLIGENCE, INC.

By: \_\_\_\_\_ Name: Dr. Sarah Chen Title: Chief Executive Officer

By: \_\_\_\_\_ Name: David Kumar Title: Chief Financial Officer

ATTEST:

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Corporate Secretary