

NETSOL TECHNOLOGIES INC
Form 10-Q
November 08, 2013
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION
Washington, DC 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 September 30, 2013

For the transition period from _____ to _____

Commission file number: 0-22773

NETSOL TECHNOLOGIES, INC.
(Exact name of small business issuer as specified in its charter)

NEVADA
(State or other Jurisdiction of
Incorporation or Organization)

95-4627685
(I.R.S. Employer NO.)

24025 Park Sorrento, Suite 410, Calabasas, CA 91302
(Address of principal executive offices) (Zip Code)

(818) 222-9195 / (818) 222-9197
(Issuer's telephone/facsimile numbers, including area code)

Indicate by check mark whether the issuer: (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 issuer was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

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

Large Accelerated Filer
Non-Accelerated Filer

Accelerated Filer
Small Reporting Company

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

The issuer had 9,061,075 shares of its \$.01 par value Common Stock and no shares of Series A 7% Cumulative Convertible Preferred Stock issued and outstanding as of November 6, 2013.

NETSOL TECHNOLOGIES, INC.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited)

NETSOL TECHNOLOGIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(UNAUDITED)

| | As of September 30, 2013 | As of June 30, 2013 |
|--|-----------------------------|------------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 6,755,950 | \$ 7,874,318 |
| Restricted cash | 2,301,822 | 1,875,237 |
| Accounts receivable, net | 18,535,948 | 14,684,212 |
| Revenues in excess of billings | 11,435,167 | 15,367,198 |
| Other current assets | 2,841,126 | 2,273,314 |
| Total current assets | 41,870,013 | 42,074,279 |
| Long term investment | | - |
| Investment under equity method | 554,674 | 545,483 |
| Property and equipment, net | 21,493,298 | 20,978,369 |
| Intangible assets, net | 28,775,799 | 29,452,654 |
| Goodwill | 9,653,330 | 9,653,330 |
| Total assets | \$ 102,347,114 | \$ 102,704,115 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable and accrued expenses | \$ 4,498,965 | \$ 3,923,921 |
| Current portion of loans and obligations under capitalized leases | 3,660,388 | 3,326,465 |
| Other payables - acquisitions | 103,226 | 103,226 |
| Unearned revenues | 3,987,150 | 2,446,018 |
| Loans payable, bank | 1,874,941 | 1,982,161 |
| Common stock to be issued | 320,338 | 88,325 |
| Total current liabilities | 14,445,008 | 11,870,116 |
| Long term loans and obligations under capitalized leases; less current maturities | 1,416,791 | 1,412,212 |
| Total liabilities | 15,861,799 | 13,282,328 |
| Commitments and contingencies | | |
| Stockholders' equity: | | |
| Common stock, \$.01 par value; 15,000,000 shares authorized; 8,990,923 and 8,929,523 issued and outstanding as of September 30, 2013 and June 30, 2013 | 89,909 | 89,295 |
| Additional paid-in-capital | 114,914,808 | 114,292,510 |
| Treasury stock | (415,425) | (415,425) |
| Accumulated deficit | (24,918,371) | (23,821,256) |
| Stock subscription receivable | (2,130,488) | (2,280,488) |
| Other comprehensive loss | (17,916,294) | (15,714,112) |
| Total NetSol stockholders' equity | 69,624,139 | 72,150,524 |
| Non-controlling interest | 16,861,176 | 17,271,263 |
| Total stockholders' equity | 86,485,315 | 89,421,787 |
| Total liabilities and stockholders' equity | \$ 102,347,114 | \$ 102,704,115 |

See accompanying notes to these unaudited consolidated financial statements.

NETSOL TECHNOLOGIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

| | For the Three Months Ended September 30, | |
|---|---|------------|
| | 2013 | 2012 |
| Net Revenues: | | |
| License fees | 2,252,567 | 3,241,501 |
| Maintenance fees | 2,380,409 | 2,045,706 |
| Services | 4,424,340 | 5,784,693 |
| Total net revenues | 9,057,316 | 11,071,900 |
| Cost of revenues: | | |
| Salaries and consultants | 3,456,604 | 3,385,668 |
| Travel | 396,784 | 325,294 |
| Repairs and maintenance | 175,821 | 127,997 |
| Insurance | 39,554 | 37,719 |
| Depreciation and amortization | 1,046,669 | 958,151 |
| Other | 544,337 | 921,858 |
| Total cost of revenues | 5,659,769 | 5,756,687 |
| Gross profit | 3,397,547 | 5,315,213 |
| Operating expenses: | | |
| Selling and marketing | 1,071,412 | 762,963 |
| Depreciation and amortization | 426,617 | 342,001 |
| Bad debt expense | 251,673 | - |
| Salaries and wages | 1,441,132 | 1,153,873 |
| Professional services, including non-cash compensation | 306,663 | 206,502 |
| General and administrative | 1,423,002 | 1,347,928 |
| Total operating expenses | 4,920,499 | 3,813,267 |
| (Loss) income from operations | (1,522,952) | 1,501,946 |
| Other income and (expenses) | | |
| (Loss) gain on sale of assets | (13,795) | 14,296 |
| Interest expense | (69,217) | (292,389) |
| Interest income | 32,854 | 24,167 |
| Gain on foreign currency exchange transactions | 1,111,423 | 395,156 |
| Share of net income from equity investment | 9,192 | - |
| Amortization of financing costs | - | (367,744) |
| Other income | 678 | (32) |
| Total other income (expenses) | 1,071,135 | (226,546) |
| Net (loss) income before income taxes | (451,817) | 1,275,400 |
| Income taxes | (11,131) | (13,996) |
| Net (loss) income after tax | (462,948) | 1,261,404 |
| Non-controlling interest | (634,167) | (332,279) |
| Net (loss) income attributable to NetSol | (1,097,115) | 929,125 |
| Other comprehensive loss: | | |
| Translation adjustment | (3,422,716) | (768,795) |
| Comprehensive income (loss) | (4,519,831) | 160,330 |
| Comprehensive loss attributable to non-controlling interest | (1,220,534) | (232,556) |
| Comprehensive (loss) income attributable to NetSol | (3,299,297) | 392,886 |

Net (loss) income per share:

| | | |
|---|------------|-----------|
| Basic | \$ (0.12) | \$ 0.12 |
| Diluted | \$ (0.12) | \$ 0.12 |
| Weighted average number of shares outstanding | | |
| Basic | 8,956,007 | 7,591,891 |
| Diluted | 8,956,007 | 7,599,136 |

See accompanying notes to these unaudited consolidated financial statements.

NETSOL TECHNOLOGIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

| | For the Three Months Ended September 30, | |
|--|---|--------------|
| | 2013 | 2012 |
| Cash flows from operating activities: | | |
| Net (loss) income | \$ (462,948) | \$ 1,261,404 |
| Adjustments to reconcile net (loss) income to net cash provided by operating activities: | | |
| Depreciation and amortization | 1,473,286 | 1,300,152 |
| Provision for bad debts | 251,673 | - |
| Share of net (income) loss from investment under equity method | (9,192) | - |
| (Gain) loss on sale of assets | 13,795 | (14,296) |
| Stock issued for interest on notes payable | - | 211,111 |
| Stock issued for services | 318,857 | 29,670 |
| Fair market value of warrants and stock options granted | 125,568 | 227,926 |
| Amortization of financing costs | - | 367,744 |
| Changes in operating assets and liabilities: | | |
| Increase in accounts receivable | (3,928,230) | (4,320,159) |
| Decrease in revenue in excess of billing | 3,565,290 | 1,601,584 |
| (Increase) decrease in other current assets | (438,780) | 291,041 |
| Increase in accounts payable and accrued expenses | 2,014,051 | 1,942,654 |
| Net cash provided by operating activities | 2,923,370 | 2,898,831 |
| Cash flows from investing activities: | | |
| Purchases of property and equipment | (2,691,066) | (1,457,134) |
| Sales of property and equipment | 80,287 | 60,501 |
| Increase in intangible assets | (1,362,026) | (1,091,966) |
| Net cash used in investing activities | (3,972,805) | (2,488,599) |
| Cash flows from financing activities: | | |
| Proceeds from the exercise of stock options and warrants | 560,500 | 252,900 |
| Payment to common shareholders against fractional shares | - | (194) |
| Proceeds from exercise of subsidiary options | 176,280 | - |
| Restricted cash | (426,585) | (1,571,442) |
| Proceeds from bank loans | 519,040 | 2,651,048 |
| Payments on capital lease obligations and loans - net | (198,853) | (1,160,684) |
| Net cash provided by financing activities | 630,382 | 171,628 |
| Effect of exchange rate changes in cash | (699,315) | (161,679) |
| Net (decrease) increase in cash and cash equivalents | (1,118,368) | 420,181 |
| Cash and cash equivalents, beginning of period | 7,874,318 | 7,599,607 |
| Cash and cash equivalents, end of period | \$ 6,755,950 | \$ 8,019,788 |

See accompanying notes to the unaudited consolidated financial statements.

NETSOL TECHNOLOGIES, INC. AND SUBSIDIARIES
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)
 (UNAUDITED)

| | For the Three Months Ended September 30, | |
|--|---|--------------|
| | 2013 | 2012 |
| SUPPLEMENTAL DISCLOSURES: | | |
| Cash paid during the period for: | | |
| Interest | \$ 61,466 | \$ 102,198 |
| Taxes | \$ - | \$ 24,253 |
| NON-CASH INVESTING AND FINANCING ACTIVITIES: | | |
| Stock issued for the conversion of convertible notes payable | \$ - | \$ 1,050,000 |
| Stock issued for the conversion of interest payable | \$ - | \$ 391,111 |

See accompanying notes to the unaudited consolidated financial statements.

NETSOL TECHNOLOGIES, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

NOTE 1 - BASIS OF PRESENTATION AND PRINCIPLES OF CONSOLIDATION

The Company designs, develops, markets, and exports proprietary software products to customers in the automobile finance and leasing, banking, healthcare, and financial services industries worldwide. The Company also provides system integration, consulting, IT products and services in exchange for fees from customers.

The consolidated condensed interim financial statements included herein have been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations, although the Company believes that the disclosures are adequate to make the information presented not misleading.

These statements reflect all adjustments, consisting of normal recurring adjustments, which, in the opinion of management, are necessary for fair presentation of the information contained therein. It is suggested that these condensed consolidated financial statements be read in conjunction with the financial statements and notes thereto included in the Company's annual report on Form 10-K for the year ended June 30, 2013. The Company follows the same accounting policies in preparation of interim reports. Results of operations for the interim periods are not indicative of annual results.

The accompanying consolidated financial statements include the accounts of NetSol Technologies, Inc. and subsidiaries (collectively, the "Company") as follows:

Wholly-owned Subsidiaries

NetSol Technologies Americas, Inc. ("NTA") formerly NetSol Technologies North America, Inc. ("NTNA")
NetSol Connect (Private), Ltd. ("Connect")
NetSol-Abraxas Australia Pty Ltd. ("Abraxas")
NetSol Technologies Europe Limited ("NTE")
NetSol Technologies Limited ("NetSol UK")
NTPK (Thailand) Co. Limited ("NTPK Thailand")
NetSol Technologies (Beijing) Co. Ltd. (NetSol Beijing)
Netsol Omni (Private) Limited ("Omni")

Majority-owned Subsidiaries

NetSol Technologies, Ltd. ("NetSol PK")
NetSol Innovation (Private) Limited ("NetSol Innovation")
Vroozi, Inc. ("Vroozi")
Virtual Lease Services Holdings Limited ("VLSH")
Virtual Lease Services Limited ("VLS")
Virtual Lease Services (Ireland) Limited (VLSIL)

For comparative purposes, prior year's consolidated financial statements have been reclassified to conform to report classifications of the current year.

NOTE 2 – ACCOUNTING POLICIES

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

New Accounting Pronouncements

Accounting Standards Update No. 2013-11, Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists: An unrecognized tax benefit, or a portion of an unrecognized tax benefit, should be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward, except as follows. To the extent a net operating loss carryforward, a similar tax loss, or a tax credit carryforward is not available at the reporting date under the tax law of the applicable jurisdiction to settle any additional income taxes that would result from the disallowance of a tax position or the tax law of the applicable jurisdiction does not require the entity to use, and the entity does not intend to use, the deferred tax asset for such purpose, the unrecognized tax benefit should be presented in the financial statements as a liability and should not be combined with deferred tax assets. The assessment of whether a deferred tax asset is available is based on the unrecognized tax benefit and deferred tax asset that exist at the reporting date and should be made presuming disallowance of the tax position at the reporting date. For example, an entity should not evaluate whether the deferred tax asset expires before the statute of limitations on the tax position or whether the deferred tax asset may be used prior to the unrecognized tax benefit being settled. The amendments in this Update do not require new recurring disclosures. ASU Topic No. 2013 is effective for fiscal years, and interim periods within those years, beginning after December 15, 2013. The adoption of this guidance is not expected to have a material impact on the Company's consolidated financial statements.

NETSOL TECHNOLOGIES, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

In March 2013, the FASB issued guidance on a parent's accounting for the cumulative translation adjustment upon derecognition of a subsidiary or group of assets within a foreign entity. This new guidance requires that the parent release any related cumulative translation adjustment into net income only if the sale or transfer results in the complete or substantially complete liquidation of the foreign entity in which the subsidiary or group of assets had resided. The new guidance will be effective for us beginning July 1, 2014. We do not anticipate material impacts on the Company's financial statements upon adoption.

NETSOL TECHNOLOGIES, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

NOTE 3 – EARNINGS PER SHARE

Basic earnings per share are computed based on the weighted average number of shares of common stock outstanding during the period. Diluted earnings per share is computed based on the weighted average number of shares of common stock plus the effect of dilutive potential common shares outstanding during the period using the treasury stock method. Dilutive potential common shares include outstanding stock options, warrants, convertible note payable and stock awards.

The components of basic and diluted earnings per share were as follows:

| For the three months ended September 30, 2013 | Net Loss | Shares | Per Share |
|---|---------------|-----------|-----------|
| Basic loss per share: | | | |
| Net loss available to common shareholders | \$(1,097,115) | 8,956,007 | \$(0.12) |
| Effect of dilutive securities | | | |
| Stock options | - | - | - |
| Warrants | - | - | - |
| Diluted loss per share | \$(1,097,115) | 8,956,007 | \$(0.12) |
| | | | |
| For the three months ended September 30, 2012 | Net Income | Shares | Per Share |
| Basic income per share: | | | |
| Net income available to common shareholders | \$ 929,125 | 7,591,891 | \$ 0.12 |
| Effect of dilutive securities | | | |
| Stock options | - | - | - |
| Warrants | - | 7,245 | - |
| Diluted income per share | \$ 929,125 | 7,599,136 | \$ 0.12 |

As of September 30, 2013 and 2012, the following potential dilutive shares were excluded from the shares used to calculate diluted earnings per share as their inclusion would be anti-dilutive.

| | As of September 30, 2013 | 2012 |
|------------------|-----------------------------|--------|
| Stock Options | 57,914 | - |
| Warrants | 50,202 | - |
| Convertible Note | - | 59,644 |
| | 108,116 | 59,644 |

NOTE 4 – OTHER COMPREHENSIVE INCOME AND FOREIGN CURRENCY:

The accounts of NTE, VLSH and VLS use the British Pound; VLSIL uses the Euro; NetSol PK, Connect, and NetSol Innovation use Pakistan Rupees; NTPK Thailand uses Thai Baht; Abraxas uses the Australian dollar; and NetSol Beijing uses Chinese Yuan as the functional currencies. NetSol Technologies, Inc., and its subsidiaries, NTA and Vroozi, use the U.S. dollar as the functional currency. Assets and liabilities are translated at the exchange rate on the balance sheet date, and operating results are translated at the average exchange rate throughout the period. Accumulated translation losses classified as an item of accumulated other comprehensive loss in the stockholders' equity section of the consolidated balance sheet were \$17,916,294 and \$15,714,112 as of September 30, 2013 and June 30, 2013 respectively. During the three months ended September 30, 2013 and 2012, comprehensive

loss in the consolidated statements of operations included translation loss of \$2,202,182 and \$536,239, respectively.

NOTE 5 – ACCOUNTS RECEIVABLE

Accounts receivable include \$154,050 due from a related party.

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NETSOL TECHNOLOGIES, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

NOTE 6 - OTHER CURRENT ASSETS

Other current assets consisted of the following:

| | As of September 30, 2013 | As of June 30, 2013 |
|-------------------------|-----------------------------|------------------------|
| Prepaid Expenses | \$ 512,517 | \$ 559,217 |
| Advance Income Tax | 881,596 | 887,893 |
| Employee Advances | 40,319 | 43,794 |
| Security Deposits | 183,801 | 189,382 |
| Tender Money Receivable | 91,734 | 106,398 |
| Other Receivables | 298,624 | 222,609 |
| Other Assets | 765,396 | 197,915 |
| Due From Related Party | 67,139 | 66,106 |
| Total | \$ 2,841,126 | \$ 2,273,314 |

Due from related party as of September 30, 2013 is a receivable from Atheeb NetSol Saudi Company Limited.

NOTE 7 - PROPERTY AND EQUIPMENT

Property and equipment, net, consisted of the following:

| | As of September 30, 2013 | As of June 30, 2013 |
|--------------------------------|-----------------------------|------------------------|
| Office furniture and equipment | \$ 2,357,632 | \$ 2,508,975 |
| Computer equipment | 20,635,789 | 19,987,480 |
| Assets under capital leases | 1,210,529 | 1,126,860 |
| Building | 2,262,187 | 2,391,550 |
| Land | 2,327,070 | 2,460,144 |
| Capital work in progress | 5,756,021 | 5,104,283 |
| Autos | 714,474 | 689,440 |
| Improvements | 510,942 | 513,044 |
| Subtotal | 35,774,644 | 34,781,776 |
| Accumulated depreciation | (14,281,346) | (13,803,407) |
| Property and equipment, net | \$ 21,493,298 | \$ 20,978,369 |

For the three months ended September 30, 2013 and 2012, depreciation expense totaled \$997,560 and \$754,108, respectively. Of these amounts, \$613,110 and \$454,745, respectively, are reflected in cost of revenues.

The Company's capital work in progress consists of ongoing enhancements to its facilities and infrastructure necessary to meet the Company's expected long term growth needs. The Company recorded capitalized interest of \$68,280 and \$292,390 as of September 30, 2013 and June 30, 2013, respectively.

Assets acquired under capital leases were \$1,210,529 and \$1,126,860 as of September 30, 2013 and June 30, 2013, respectively. Accumulated amortization related to these leases was \$380,738 and \$350,048 as of September 30, 2013 and June 30, 2013, respectively.

NETSOL TECHNOLOGIES, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

NOTE 8 - INTANGIBLE ASSETS

Intangible assets consisted of the following:

| | Product Licenses | Customer Lists | Technology | Total |
|--|---------------------|-------------------|------------|---------------|
| Intangible assets - June 30, 2013 - cost | \$ 44,837,558 | \$ 6,052,377 | \$ 242,702 | \$51,132,637 |
| Additions | 1,362,026 | - | - | 1,322,150 |
| Effect of translation adjustment | (1,595,186) | - | - | (1,555,310) |
| Accumulated amortization | (16,129,094) | (5,897,502) | (97,082) | (22,123,678) |
| Net balance - September 30, 2013 | \$ 28,475,304 | \$ 154,875 | \$ 145,620 | \$28,775,799 |

(A) Product Licenses

Product licenses include internally-developed original license issues, renewals, enhancements, copyrights, trademarks, and trade names. Product licenses include unamortized software development and enhancement costs of \$22,235,935. Product licenses are being amortized on a straight-line basis over their respective lives, which is currently a weighted average of approximately 8 years. Amortization expense for the three months ended September 30, 2013 and 2012 was \$433,559 and \$503,406, respectively.

(B) Customer Lists

Customer lists are being amortized based on a straight-line basis, which approximates the anticipated rate of attrition, which is currently a weighted average of approximately 5 years. Amortization expense for the three months ended September 30, 2013 and 2012 was \$30,048 and \$30,286, respectively.

(C) Technology

Technology assets are being amortized on a straight-line basis over their respective lives, which is currently a weighted average of approximately 5 years. Amortization expense for the three months ended September 30, 2013 and 2012 was \$12,119 and \$12,353.

(D) Future Amortization

Estimated amortization expense of intangible assets over the next five years is as follows:

| | |
|--------------------|------------|
| Year ended: | |
| September 30, 2014 | 1,746,484 |
| September 30, 2015 | 1,306,724 |
| September 30, 2016 | 872,360 |
| September 30, 2017 | 711,323 |
| September 30, 2018 | 688,878 |
| Thereafter | 23,450,029 |

NETSOL TECHNOLOGIES, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

NOTE 9 – GOODWILL

Goodwill represents the excess of the aggregate purchase price over the fair value of the net assets acquired in businesses combinations. Goodwill was comprised of the following amounts:

| | As of September 30, 2013 | As of June 30, 2013 |
|--------------|-----------------------------|------------------------|
| Asia Pacific | \$ 1,303,372 | \$ 1,303,372 |
| Europe | 3,685,858 | 3,685,858 |
| USA | 4,664,100 | 4,664,100 |
| Total | \$ 9,653,330 | \$ 9,653,330 |

The Company has determined that there was no impairment of the goodwill for either period presented.

NOTE 10 – INVESTMENT UNDER EQUITY METHOD

On April 10, 2009, the Company entered into an agreement to form a joint venture with the Atheeb Trading Company, a member of the Atheeb Group (“Atheeb”). The joint venture entity Atheeb NetSol Saudi Company Ltd. is a company organized under the laws of the Kingdom of Saudi Arabia. The venture was formed with an initial capital contribution of \$268,000 by the Company and \$266,930 by Atheeb with a profit sharing ratio of 50.1:49.9, respectively. The final formation of the company was completed on March 7, 2010. Since currently the Company does not have control over the operational and financial matters of Atheeb Netsol, therefore, it is considered as an associated company and accounted for under equity method.

| | |
|--|-----------|
| Net book value at June 30, 2013 | \$545,482 |
| Net income for the three months ended September 30, 2013 | 18,346 |
| NetSol's share (50.1%) | 9,192 |
| Total income | 9,192 |
| Income adjusted against investment | 9,192 |
| Net book value at September 30, 2013 | \$554,674 |

NOTE 11 - ACCOUNTS PAYABLE AND ACCRUED EXPENSES

Accounts payable and accrued expenses consisted of the following:

| | As of September 30, 2013 | As of June 30, 2013 |
|-----------------------|-----------------------------|------------------------|
| Accounts Payable | \$ 1,235,754 | \$ 825,025 |
| Accrued Liabilities | 2,117,431 | 2,055,066 |
| Accrued Payroll | 63,942 | 25,529 |
| Accrued Payroll Taxes | 284,883 | 218,084 |
| Interest Payable | 76,370 | 71,872 |
| Deferred Revenues | 798 | 937 |
| Taxes Payable | 719,787 | 727,408 |
| Total | \$ 4,498,965 | \$ 3,923,921 |

NETSOL TECHNOLOGIES, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

NOTE 12 – DEBTS

(A) LOANS AND LEASES PAYABLE

Notes payable consisted of the following:

| Name | | As of September 30 2013 | Current Maturities | Long-Term Maturities |
|---------------------------|------|----------------------------|-----------------------|-------------------------|
| D&O Insurance | (1) | \$ 44,411 | \$ 44,411 | \$ - |
| Habib Bank Line of Credit | (2) | 2,211,822 | 2,211,822 | - |
| Bank Overdraft Facility | (3) | 420,231 | 420,231 | - |
| HSBC Loan | (4) | 1,032,253 | 321,270 | 710,983 |
| Term Finance Facility | (5) | 703,103 | 351,552 | 351,551 |
| Subsidiary Capital Leases | (6) | 665,359 | 311,102 | 354,257 |
| | | \$ 5,077,179 | \$ 3,660,388 | \$ 1,416,791 |

| Name | | As of June 30 2013 | Current Maturities | Long-Term Maturities |
|---------------------------|------|-----------------------|-----------------------|-------------------------|
| D&O Insurance | (1) | \$ 88,292 | \$ 88,292 | \$ - |
| Habib Bank Line of Credit | (2) | 1,785,237 | 1,785,237 | - |
| Bank Overdraft Facility | (3) | 312,139 | 312,139 | - |
| HSBC Loan | (4) | 1,047,014 | 336,339 | 710,675 |
| Term Finance Facility | (5) | 867,195 | 495,540 | 371,655 |
| Subsidiary Capital Leases | (6) | 638,800 | 308,918 | 329,882 |
| | | \$ 4,738,677 | \$ 3,326,465 | \$ 1,412,212 |

(1) The Company finances Directors' and Officers' ("D&O") liability insurance as well as Errors and Omissions ("E&O") liability insurance, for which the total balances are renewed on an annual basis and as such are recorded in current maturities. The interest rate on the insurance financing was 0.40% and 0.40% as of September 30, 2013 and June 30, 2013, respectively. Interest paid during the three months ended September 30, 2013 and 2012 was nominal.

(2) In April 2008, the Company entered into an agreement with Habib American Bank to secure a line of credit to be collateralized by Certificates of Deposit held at the bank. The interest rate on this line of credit is variable and was 1.5% as of September 30, 2013 and June 30, 2013, respectively. In June 2012, the Company's subsidiary, NTNA entered into an agreement with Habib American Bank to secure a line of credit up to \$500,000 to be collateralized by Certificates of Deposit of same value held at the bank. The interest rate on this line of credit is variable and was 1.90% as of September 30, 2013 and June 30, 2013, respectively. Interest expense during the three months ended September 30, 2013 and 2012 was \$7,296 and \$3,772, respectively.

In February 2012, the Company entered into agreement with HSBC for the issuance of stand by letter of credit worth \$90,000 in favor of landlord against the new office space. The Company has deposited \$90,000 in a saving account with HSBC as collateral against this letter of credit.

(3) During the year ended June 30, 2008, the Company's subsidiary, NTE entered into an overdraft facility with HSBC Bank plc whereby the bank would cover any overdrafts up to £300,000, or approximately \$484,290. The annual

interest rate is 4.25% over the bank's sterling base rate, which was 4.75% and 5.20% as of September 30, 2013 and June 30, 2013, respectively. Interest expense during the three months ended September 30, 2013 and 2012 was \$22,442 and \$18,524, respectively.

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(4) In October 2011, the Company's subsidiary, NTE, entered into a loan agreement with HSBC Bank to finance the acquisition of 51% of controlling interest in Virtual Leasing Services Limited. HSBC Bank guaranteed the loan up to a limit of £1,000,000, or approximately \$1,614,300 for a period of 5 years with monthly payments of £18,420, or approximately \$29,735. The interest rate was 4% which is 3.5% above the bank sterling base rate. The loan is securitized against debenture comprising of fixed and floating charges over all the assets and undertakings of NTE including all present and future freehold and leasehold property, book and other debts, chattels, goodwill and uncalled capital, both present and future. As of June 30, 2013, the subsidiary has used this facility up to \$1,047,015, of which \$710,675, was shown as long term and the remaining \$336,339, as current maturity. As of September 30, 2013, the subsidiary has used this facility up to \$1,032,253, of which \$710,983, was shown as long term and the remaining \$321,270, as current maturity. Interest expense, for the three months ended September 30, 2013 and 2012, was \$18,849, and \$21,665, respectively.

(5) The Company's subsidiary, NetSol PK, entered into two different term finance facilities from Askari Bank to finance the construction of a new building. The total aggregate amount of these facilities is Rs. 112,500,000 or approximately \$1,054,655 (secured by the first charge of Rs. 580 million or approximately \$5.44 million over the land, building and equipment of the company). The interest rate is 2.75% above the six-month Karachi Inter Bank Offering Rate. As of the year ended June 30, 2013, the Company has used a total of Rs.87,500,000 or approximately \$867,195 of which \$371,655 is shown as long term liabilities and the remainder of \$495,540 as current maturity. As of September 30, 2013, the company has used a total of Rs.75,000,000, or approximately \$703,103, of which \$351,551, is shown as long term liabilities and the remainder of \$351,552, as current maturity. Interest expense during the three months ended September 30, 2013 and 2012 was \$22,123 and \$37,202, respectively.

(6) The Company leases various fixed assets under capital lease arrangements expiring in various years through 2018. The assets and liabilities under capital leases are recorded at the lower of the present value of the minimum lease payments or the fair value of the asset. The assets are depreciated over the lesser of their related lease terms or their estimated useful lives and are secured by the assets themselves. Depreciation of assets under capital leases is included in depreciation expense for the three months ended September 30, 2013 and 2012.

Following is the aggregate minimum future lease payments under capital leases as of September 30, 2013:

| | As of September 30, 2013 |
|---|-----------------------------|
| Minimum Lease Payments | |
| Due FYE 9/30/14 | \$ 368,052 |
| Due FYE 9/30/15 | 247,621 |
| Due FYE 9/30/16 | 105,153 |
| Due FYE 9/30/17 | 37,957 |
| Total Minimum Lease Payments | 758,783 |
| Interest Expense relating to future periods | (93,424) |
| Present Value of minimum lease payments | 665,359 |
| Less: Current portion | (311,102) |
| Non-Current portion | \$ 354,257 |

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Following is a summary of fixed assets held under capital leases as of September 30, 2013 and June 30, 2013:

| | As of September 30, 2013 | As of June 30, 2013 |
|---------------------------------|-----------------------------|------------------------|
| Computer Equipment and Software | \$ 533,813 | \$ 454,002 |
| Furniture and Fixtures | 900 | 951 |
| Vehicles | 675,816 | 671,907 |
| Total | 1,210,529 | 1,126,860 |
| Less: Accumulated Depreciation | (380,738) | (350,048) |
| Net | \$ 829,791 | \$ 776,812 |

Interest expense for the three months ended September 30, 2013 and 2012 was \$18,980, and \$18,621, respectively.

(B) LOANS PAYABLE - BANK

The Company's subsidiary, NetSol PK, has a loan with Askari Bank Limited, secured by the Company's assets. This is a revolving loan that matures every six months. The balance of the loan at September 30, 2013 and June 30, 2013 was \$1,874,941, and \$1,982,161, respectively. The interest rate for the loans was 9.40% and 9.40% at September 30, 2013 and June 30, 2013, respectively. Interest expense for the three months ended September 30, 2013, and 2012 was \$44,100 and \$57,406, respectively.

NOTE 13 – OTHER PAYABLE AND COMMON STOCK TO BE ISSUED

On June 30, 2006, the Company acquired McCue Systems, Inc. ("McCue"), a California corporation (subsequently renamed as NetSol Technologies North America, Inc.) The total purchase price was \$7,080,385, including \$3,784,635 of cash and 171,233 shares of the Company's common stock. Of the total purchase price, the accompanying consolidated financial statements include certain amounts payable to McCue shareholders that have not been located as of the date of this report.

As of the periods ended September 30, 2013 and June 30, 2013, the remaining cash due of \$103,226 is shown as "Other Payable" and the remaining stock to be issued of 4,670 shares at an average price of \$18.90 is shown in "Common stock to be issued" in the accompanying consolidated financial statements.

NOTE 14 - STOCKHOLDERS' EQUITY

(A) Treasury Stock

On November 11, 2011, the Company announced that it had authorized a stock repurchase program permitting the Company to repurchase up to 250,000 of its shares of common stock over the following 6 months. The shares are to be repurchased from time to time in open market transactions or privately negotiated transactions in the Company's discretion. The Company repurchased 4,430 shares of common stock from open market against cash consideration of \$19,417. The repurchase plan expired by its own terms in May, 2012. The balance of treasury stock as of September 30, 2013 and June 30, 2013 was \$415,425.

(B) Share-Based Payment Transactions

The Company recorded an expense of \$213,600 for the services rendered by officers during the three months ended September 30, 2013 in shares to be issued.

The Company recorded an expense of \$18,412 for services rendered by the independent members of the Board of Directors as part of their board compensation during the three months ended September 30, 2013.

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During the three months ended September 30, 2013, the Company issued a total of 6,500 shares of its common stock to employees pursuant to the terms of their employment agreements valued at \$69,420.

During the three months ended September 30, 2013, the Company issued a total of 2,400 shares of its common stock for provision of services to unrelated consultants valued at \$9,210.

The Company recorded an expense of \$69,420 as part of compensation to employees as required according to the terms of their employment agreements during the three months ended September 30, 2013.

NOTE 15 - INCENTIVE AND NON-STATUTORY STOCK OPTION PLAN

Common stock purchase options and warrants consisted of the following:

OPTIONS:

| | # of shares | Weighted Average Exercise Price | Weighted Average Remaining Contractual Life (in years) | Aggregated Intrinsic Value |
|---|-------------|--|---|----------------------------------|
| Outstanding and exercisable, June 30, 2013 | 311,462 | \$ 15.65 | 3.3 | |
| Granted | 52,500 | \$ 7.82 | | |
| Exercised | (52,500) | \$ 7.82 | | |
| Expired / Cancelled | (9,000) | \$ 32.70 | | |
| Outstanding and exercisable, September 30, 2013 | 302,462 | \$ 15.14 | 3.11 | \$ 517,621 |

WARRANTS:

| | | | | |
|---|---------|---------|------|------------|
| Outstanding and exercisable, June 30, 2013 | 163,124 | \$ 7.29 | 3.44 | |
| Granted / adjusted | - | - | | |
| Exercised | - | - | | |
| Expired | - | - | | |
| Outstanding and exercisable, September 30, 2013 | 163,124 | \$ 7.29 | 2.94 | \$ 446,625 |

The average life remaining on the options and warrants as of September 30, 2013 is as follows:

| Exercise Price | Number Outstanding and Exercisable | Weighted Average Remaining Contractual Life | Weighted Average Exercise Price |
|----------------|---|---|--|
| \$0.10 | - | \$9.90 | 183,462 |
| \$10.00 | - | \$19.90 | 14,000 |
| \$20.00 | - | \$29.90 | 91,000 |
| | | | 3.71 |
| | | | 2.35 |
| | | | 2.45 |
| | | | 7.21 |
| | | | 18.18 |
| | | | 25.31 |

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| | | | | | |
|---------------|---|---------|----------------|-------------|--------------|
| \$30.00 | - | \$50.00 | 14,000 | 0.40 | 50.00 |
| Totals | | | 302,462 | 3.11 | 15.14 |

WARRANTS:

| | | | | | |
|---------------|---|--------|----------------|-------------|-------------|
| \$3.10 | - | \$7.73 | 163,124 | 2.94 | 7.29 |
| Totals | | | 163,124 | 2.94 | 7.29 |

All options and warrants granted are vested and are exercisable as of September 30, 2013.

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Below is the table summarizing stock grants awarded as compensation:

| Issued by the Company | # of shares | Weighted Average Grant Date Fair Value (\$) |
|------------------------------|-------------|---|
| Unvested, June 30, 2012 | - | - |
| Granted | 3,750 | \$ 5.48 |
| Vested | (3,750) | \$ 5.48 |
| Unvested, June 30, 2013 | - | - |
| Granted | 86,899 | \$ 10.68 |
| Vested | (21,724) | \$ 10.68 |
| Unvested, September 30, 2013 | 65,175 | \$ 10.68 |

(A) INCENTIVE AND NON-STATUTORY STOCK OPTION PLANS

The Company maintains several Incentive and Non-Statutory Stock Option Plans (“Plans”) for its employees and consultants. Options granted under these Plans to an employee of the Company become exercisable over a period of no longer than ten (10) years and no less than twenty percent (20%) of the shares are exercisable annually. Options are not exercisable, in whole or in part, prior to one (1) year from the date of grant unless the Board specifically determines otherwise, as provided.

Two types of options may be granted under these Plans: (1) Incentive Stock Options (also known as Qualified Stock Options) which may only be issued to employees of the Company and whereby the exercise price of the option is not less than the fair market value of the common stock on the date it was reserved for issuance under the Plan; and (2) Non-statutory Stock Options which may be issued to either employees or consultants of the Company and whereby the exercise price of the option is less than the fair market value of the common stock on the date it was reserved for issuance under the plan. Grants of options may be made to employees and consultants without regard to any performance measures. All options issued pursuant to the Plan are nontransferable and subject to forfeiture.

OPTIONS

During the quarter ended September 30, 2013, the Company granted 47,500 options to four employees with an exercise price of \$8 per share and an expiration date of 3 months, vesting immediately. Using the Black-Scholes method to value the options, the Company recorded \$106,486 in compensation expense for these options in the accompanying consolidated financial statements. The Black-Scholes option pricing model used the following assumptions:

- Risk-free interest rate - 0.05%
- Expected life - 3 months
- Expected volatility - 45.99%
- Expected dividend - 0%

During the quarter ended September 30, 2013, the Company granted 5,000 options to one employee with an exercise price of \$6.10 per share and an expiration date of 1 month, vesting immediately. Using the Black-Scholes method to

value the options, the Company recorded \$18,551 in compensation expense for these options in the accompanying consolidated financial statements. The Black-Scholes option pricing model used the following assumptions:

- Risk-free interest rate - 0.02%
- Expected life - 1 month
- Expected volatility - 23.13%
- Expected dividend - 0%

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(B) EQUITY INCENTIVE PLAN

In May 2013, the shareholders approved the 2013 Equity Incentive Plan (the "2013 Plan") which provides for the grant of equity-based awards, including options, stock appreciation rights, restricted stock awards or performance share awards or any other right or interest relating to shares or cash, to eligible participants. The aggregate number of shares reserved and available for award under the 2013 Plan is 1,250,000 (the Share Reserve). The 2013 Plan is administered by the Compensation Committee of the Board of Directors ("The Committee"), which shall consist of two or more "outside directors" as that term is used in Section 162 of the Code and the regulations promulgated thereunder. The 2013 Plan contemplates the issuance of common stock upon exercise of options or other awards granted to eligible persons under the 2013 Plan. Shares issued under the 2013 Plan may be both authorized and unissued shares or previously issued shares acquired by the Company. Upon termination or expiration of an unexercised option, stock appreciation right or other stock-based award under the 2013 Plan, in whole or in part, the number of shares of common stock subject to such award again becomes available for grant under the 2013 Plan. Any shares of restricted stock forfeited as described below will become available for grant. The aggregate Fair Market Value (determined at the time of the award) of all shares of Stock with respect to which Incentive Stock Options are first exercisable by a Participant in any calendar year may not exceed \$100,000. All options issued pursuant to the Plan are nontransferable and subject to forfeiture.

Stock Options

Options granted under the 2013 Plan are not generally transferable and the term shall be set by The Committee but must be exercised within 10 years, subject to earlier termination upon termination of the option holder's employment, but in no event later than the expiration of the option's term. The exercise price of each option may not be less than the fair market value of a share of the Company's common stock on the date of grant (except in connection with the assumption or substitution for another option in a manner qualifying under Section 424(a) of the Internal Revenue Code of 1986, as amended (the Code). Incentive stock options granted to any participant who owns 10% or more of the Company's outstanding common stock (a Ten Percent Shareholder) must have an exercise price equal to or exceeding 110% of the fair market value of a share of our common stock on the date of the grant and must not be exercisable for longer than five years. Options become vested and exercisable at such times or upon such events and subject to such terms, conditions, performance criteria or restrictions as specified by the Committee.

Performance Awards

Under the 2013 Plan, a participant may also be awarded a "performance award," which means that the participant may receive cash, stock or other awards contingent upon achieving performance goals established by the Committee. The Committee may also make "deferred share" awards, which entitle the participant to receive the Company's stock in the future for services performed between the date of the award and the date the participant may receive the stock. The vesting of deferred share awards may be based on performance criteria and/or continued service with the Company. A participant who is granted a "stock appreciation right" under the Plan has the right to receive all or a percentage of the fair market value of a share of stock on the date of exercise of the stock appreciation right minus the grant price of the stock appreciation right determined by the Committee (but in no event less than the fair market value of the stock on the date of grant). Finally, the Committee may make "restricted stock" awards under the 2013 Plan, which is subject to such terms and conditions as the Committee determines and as are set forth in the award agreement related to the restricted stock. As of September 30, 2013, Nil shares have been issued under this plan to non-officers employees.

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NOTE 16 – SEGMENT AND GEOGRAPHIC AREAS

The Company has identified three global regions or segments for its products and services; North America, Europe, and Asia-Pacific. Our reportable segments are business units located in different global regions. Each business unit provides similar products and services; license fees for leasing and asset-based software, related maintenance fees, and implementation and IT consulting services. Separate management of each segment is required because each business unit is subject to different operational issues and strategies due to their particular regional location. We account for intra-company sales and expenses as if the sales or expenses were to third parties and eliminate them in the consolidation. The following table presents a summary of operating information and certain balance sheet information for the three months ended September 30:

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| | 2013 | 2012 |
|--|----------------|-----------------|
| Revenues from unaffiliated customers: | | |
| North America | \$1,218,012 | \$ 1,713,190 |
| Europe | 1,208,682 | 1,506,001 |
| Asia - Pacific | 6,630,622 | 7,852,709 |
| Consolidated | \$9,057,316 | \$ 11,071,900 |
| Operating income (loss): | | |
| Corporate headquarters | \$(1,122,311) | \$ (900,725) |
| North America | (39,517) | (233,685) |
| Europe | (427,564) | (23,805) |
| Asia - Pacific | 66,440 | 2,660,161 |
| Consolidated | \$(1,522,952) | \$ 1,501,946 |
| Net income (loss) after taxes and before non-controlling interest: | | |
| Corporate headquarters | \$(1,149,908) | \$ (1,503,819) |
| North America | (39,740) | (233,936) |
| Europe | (553,718) | (34,970) |
| Asia - Pacific | 1,280,418 | 3,034,129 |
| Consolidated | \$(462,948) | \$ 1,261,404 |
| Identifiable assets: | | |
| Corporate headquarters | \$14,506,503 | \$ 14,163,394 |
| North America | 2,867,929 | 3,242,885 |
| Europe | 4,666,802 | 5,989,190 |
| Asia - Pacific | 80,305,880 | 73,165,459 |
| Consolidated | \$102,347,114 | \$ 96,560,928 |
| Depreciation and amortization: | | |
| Corporate headquarters | \$34,652 | \$ 33,889 |
| North America | 159,345 | 159,901 |
| Europe | 220,726 | 226,983 |
| Asia - Pacific | 1,058,563 | 879,379 |
| Consolidated | \$1,473,286 | \$ 1,300,152 |
| Capital expenditures: | | |
| Corporate headquarters | \$2,097 | \$ 720 |
| North America | 7,987 | 36,646 |
| Europe | 77,580 | 13,370 |
| Asia - Pacific | 2,603,402 | 1,406,398 |
| Consolidated | \$2,691,066 | \$ 1,457,134 |
| Interest expense: | | |
| Corporate headquarters | \$7,883 | \$ 229,228 |
| North America | 299 | 564 |
| Europe | 44,347 | 40,189 |

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| | | |
|---------------------|----------|--------------|
| Asia - Pacific | 16,688 | 22,408 |
| Consolidated | \$69,217 | \$ 292,389 |
| Income tax expense: | | |
| Europe | \$- | \$ (29,024) |
| Asia - Pacific | 11,131 | 43,020 |
| Consolidated | \$11,131 | \$ 13,996 |

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NOTE 17 – NON-CONTROLLING INTEREST IN SUBSIDIARY

The Company had non-controlling interests in several of its subsidiaries. The balance of non-controlling interest was as follows:

| SUBSIDIARY | Non Controlling Interest % | Non-Controlling Interest at September 30, 2013 |
|-------------------|----------------------------------|---|
| NetSol PK | 35.77 % | \$ 15,062,396 |
| NetSol-Innovation | 49.90 % | 1,341,402 |
| VLS | 49.00 % | 454,162 |
| Vroozi | 9.09 % | 3,216 |
| Total | | \$ 16,861,176 |

| SUBSIDIARY | Non Controlling Interest % | Non-Controlling Interest at June 30, 2013 |
|-------------------|----------------------------------|--|
| NetSol PK | 34.81 % | \$ 15,593,585 |
| NetSol-Innovation | 49.90 % | 1,161,649 |
| VLS | 49.00 % | 481,121 |
| Vroozi | 9.09 % | 34,908 |
| Total | | \$ 17,271,263 |

(A) NETSOL TECHNOLOGIES, LIMITED

NetSol PK is majority owned by the Company. For the three months ended September 30, 2013 and 2012, NetSol PK had net income of \$1,286,605 and \$606,090, respectively. The related non-controlling interest was \$460,219 and \$239,284, respectively. For the same period the Comprehensive loss attributable to non-controlling interest was \$1,167,688, and \$237,743, respectively.

Employees of the company also exercised options to acquire 1,174,000 shares of the subsidiary valued at \$176,280.

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(B) NETSOL INNOVATION (PRIVATE) LIMITED

For the three months ended September 30, 2013 and 2012, NetSol Innovation had net income of \$501,344 and \$256,535. The related non-controlling interest was \$250,171 and \$128,011, respectively. For the same period the Comprehensive loss attributable to non-controlling interest was \$70,418 and \$12,356 respectively.

(C) VIRTUAL LEASE SERVICES

For the three months ended September 30, 2013 and 2012, VLS had a net loss of \$90,879 and \$64,620. The related, non-controlling interest was \$44,531 and \$31,664, respectively. For the same period the comprehensive income attributable to non-controlling interest was \$17,572 and \$17,543 respectively.

(D) VROOZI®, INC.

During the quarter ended March 31, 2013, the subsidiary company issued shares worth of \$100,000 to one employee against his services. As a result, the status of the subsidiary has been changed from wholly owned subsidiary to majority owned subsidiary. For the three months ended September 30, 2013 Vroozi® had a net loss of \$348,648, of which \$31,692 has been recorded as non-controlling interest.

NOTE 18 - SUBSEQUENT EVENTS

Pursuant to ASC 855-10, the Company has evaluated all events or transactions from September 30, 2013, through the filing with SEC. The Company did not have any material recognizable subsequent events during this period.

Item 2. Management's Discussion and Analysis of Plan of Operation

The following discussion is intended to assist in an understanding of the Company's financial position and results of operations for the quarter ending September 30, 2013.

Forward-Looking Information

This report contains certain forward-looking statements and information relating to the Company that is based on the beliefs of its management as well as assumptions made by and information currently available to its management. When used in this report, the words "anticipate", "believe", "estimate", "expect", "intend", "plan", and similar expressions as they relate to the Company or its management, are intended to identify forward-looking statements. These statements reflect management's current view of the Company with respect to future events and are subject to certain risks, uncertainties and assumptions. Should any of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those described in this report as anticipated, estimated or expected. The Company's realization of its business aims could be materially and adversely affected by any technical or other problems in, or difficulties with, planned funding and technologies, third party technologies which render the Company's technologies obsolete, the unavailability of required third party technology licenses on commercially reasonable terms, the loss of key research and development personnel, the inability or failure to recruit and retain qualified research and development personnel, or the adoption of technology standards which are different from technologies around which the Company's business ultimately is built. The Company does not intend to update these forward-looking statements.

NetSol Technologies, Inc. (NasdaqCM: NTWK) (NasdaqDubai: NTWK) is a worldwide provider of IT and enterprise application solutions, NetSol Technologies, Inc. executes its mission of focusing technology on the operational needs of its clients. NetSol's services and solutions enable businesses to streamline their operations and compete more effectively.

The Company is organized into two main revenue areas, consisting of enterprise solutions – NetSol Financial Suite (NFS™) – for the global financing, leasing and lending industry, and a portfolio of managed services, including customized application development, systems integration, and business process engineering. In addition, NetSol's solutions portfolio includes the smartOCI®, e-Procurement search engine for SAP SRM users.

NetSol's clients include Dow-Jones 30 Industrials and Fortune 500 manufacturers and financial institutions, global vehicle manufacturers, and enterprise technology providers, all of which are serviced by NetSol delivery locations across the globe.

Founded in 1997, NetSol is headquartered in Calabasas, California. While the Company follows a global strategy for sales and delivery of its portfolio of solutions and services, it continues to maintain regional offices in the San Francisco Bay Area, for North America; the London Metropolitan area for Europe; and Bangkok, Thailand, Beijing, China and Lahore, Pakistan for Asia Pacific. The Company continues to maintain services, solutions and/or sales specific offices in Australia, China, Pakistan, Thailand, the United Kingdom, the United States, and through alliances in the Kingdom of Saudi Arabia and Japan.

In today's highly competitive marketplace, business executives with labor or services-centric budgetary responsibilities are not just encouraged but, in fact, obliged to engage in "Make or Buy" decision process when contemplating how to support and staff new development, testing, services support and delivery activities. The Company business offerings are aligned as a BestShoring® solutions strategy. Simply defined, BestShoring® is NetSol Technologies' ability to draw upon its global resource base and construct the best possible solution and price for each and every customer. Unlike traditional outsourcing offshore vendors, NetSol draws upon an international workforce and delivery capability to ensure a "BestShoring® delivers BestSolution™" approach.

NetSol combines domain expertise with competitive cost blended rates from its “center of excellence” delivery center in Pakistan and other global centers located in the USA, UK, Thailand and China, Our model also provides localized programs in key markets and project management while minimizing any implementation risk associated with a single service center. Our BestShoring® approach, which we consider a unique and cost effective global development model, is leading the way, providing value added solutions for Global Business Services™ through a win-win partnership, rather than the traditional outsourced vendor framework. Our global locations provide NetSol customers with the optimum balance of subject matter expertise, in-depth domain experience, and cost effective labor, all merged into a scalable solution. In this way, “BestShoring® delivers BestSolution™”.

Information technology services are valuable only if they fulfill the business strategy and project objectives set forth by the customer. NetSol’s expert consultants have the technical knowledge and business experience to ensure the optimization of the development process in alignment with basic business principles. The Company offers a broad array of professional services to clients in the global commercial markets and specializes in the application of advanced and complex IT enterprise solutions to achieve its customers' strategic objectives. Its service offerings include IT consulting & services; business intelligence, information security, independent system review, outsourcing services and software process improvement consulting; maintenance and support of existing systems; and, project management.

In addition to services, our product offerings are fashioned to provide a Best Product for Best Solution model. Our offerings include our flagship global solution, NetSol Financial Suite (NFS™). NFS™, a robust suite of five software applications, is an end-to-end solution for the lease and finance industry covering the complete leasing and finance cycle starting from quotation origination through end of contract. The five software applications under NFS™ have been designed and developed for a highly flexible setting and are capable of dealing with multinational, multi-company, multi-asset, multi-lingual, multi-distributor and multi-manufacturer environments. Each application is a complete system in itself and can be used independently to address specific sub-domains of the leasing/financing cycle.

On October 24, NetSol announced the introduction and global release of NFS Ascent™, the company's next generation platform, offering the most technologically advanced solution for the auto and equipment finance and leasing industry. NFS Ascent™ architecture and user interfaces were designed based on the company's collective experience with global Fortune 500 companies over the past 30 years. The platform's framework allows auto captive and asset finance companies to rapidly transform legacy dependent information technology into a state-of-the-art IT and business process environment. At the core of the NFS Ascent™ platform is a lease accounting and contract processing engine, which allows for an array of interest calculation methods, as well as robust accounting of multi-billion dollar lease portfolios under various types of generally accepted accounting principles (GAAP), as well international financial reporting standards (IFRS). NFS Ascent™, with its distributed and clustered deployment across parallel application and high volume data servers, enables finance companies to process voluminous data in a hyper speed environment.

NFS Ascent™ has been developed using the latest tools and technologies and its n-tier SOA architecture allows the system to dramatically improve in various areas like scalability, performance, fault tolerance and security to name a few. We are excited about the transition from R1 to NFS Ascent™ for the following reasons:

- Improvement in overall productivity and throughout the delivery organization:

The new architecture and design of the system allows the delivery team to deliver more with less i.e. deliver more projects in a given financial year thereby increasing the revenue generation capacity of our organization. A few examples are given below

- oThe modules like Business Process Manager, Workflow Engine and Business Rule Engine will give a lot of flexibility to our clients allowing them to configure certain parts of the application themselves rather than requesting for customization.
- oThe powerful NFS Ascent™ platform and the SOA architecture allow us to develop Portals and Mobile applications rather quickly by utilizing our existing services.
- oIntegration with other systems will also be very easy and quick as we can expose our services to the external world for consumption.
- oThe n-tier architecture allows us to better distribute the tasks among various team members and because of the loose coupling between various modules and layers, the risk of regression in other parts of the system as a result of changes made in one part of the system goes down tremendously.

- Improvement in talent acquisition and retention:

Because NFS Ascent™ has been developed using the latest technologies and tools available in the market, it is helping us in attracting the top engineers and keeping them motivated compared to when we had to hire people for older technologies.

- Better customer satisfaction:

As a result of the powerful NFS Ascent™ platform and improvement in the talent acquisition and retention, the quality of our deliverables has gone up remarkably. This, in conjunction with the reduced delivery times, will allow us to have thoroughly satisfied customers.

NFS™ also includes LeasePak. LeasePak provides the leasing technology industry with the development of Web-enabled and Web-based tools to deliver superior customer service, reduce operating costs, streamline the lease

management lifecycle, and support collaboration with origination channel and asset partners. LeasePak can be configured to run on HP-UX, SUN/Solaris or Linux, as well as for Oracle and Sybase users. In terms of scalability, NetSol Technologies North America offers the basic solutions as well as a collection of highly specialized add on modules for systems, portfolios and accrual methods for virtually all sizes and complexities of operations. These solutions provide the equipment and vehicle leasing infrastructure at leading Fortune 500 banks and manufacturers, as well as for some of the industry's leading independent lessors.

NetSol's IP, smartOCI®, now part of Vroozii®, Inc., develops innovative e-commerce solutions for all business sizes and industry verticals which help companies search, source, negotiate, and order goods and services from suppliers electronically optimizing organization's procurement and supply chain operations. Vroozii's business to business search engine, collaborative commerce, and electronic marketplace applications are deployed On Demand and can integrate seamlessly with major ERP vendor systems such as SAP or deployed independently on the Internet.

Vroozii's first product to market is smartOCI®; a new search engine technology and buy-side content marketplace provider which enables corporate buyers and shoppers a simple and intuitive user interface to search multiple supplier catalogs simultaneously within the SAP procurement application. The smartOCI® technology was officially released to the market in 2011 at the SAP SAPHIRE Conference in Orlando, Florida, and has strengthened NetSol's presence in the global SAP Services market.

NetSol global operation is broken down into three regions: North America, Europe and Asia Pacific. All of the subsidiaries are seamlessly integrated to function effectively in terms of global delivery capabilities, cross selling to multinational captives' finance companies, centralized marketing organization and a network of employees connected across the globe to support local and global customers and partners.

The following discussion is intended to assist in an understanding of NetSol's financial position and results of operations for the quarter ended September 30, 2013. It should be read together with our consolidated financial statements and related notes included herein.

A few of NetSol's major successes achieved in the first three months of fiscal year 2014 were:

- Implementation of NetSol's mPOS (mobile point of sale) solution by a global luxury car manufacturer across its dealer network in China. Subsequent implementations in other markets are also being planned as per the agreement between NetSol and customer.
- Launch of NetSol's mobility products, which optimize productivity and improve the responsiveness of global sales teams. The applications seamlessly integrate with the company's flagship platform, the NetSol Financial Suite (NFS),
- The appointment of Roger K. Almond as the Company's Chief Financial Officer and Boo Ali Siddiqui, the Company's former Chief Financial Officer, as the PK subsidiary CFO and the Company's Chief Accounting Officer.
- NetSol PK signed an agreement to implement NetSol Financial Suite at a leading auto captive finance company in China.
- NetSol Technologies was awarded "First Rate and Best Selling Leasing and Finance Solution" at this year's China Leasing Summit for its flagship product, NetSol Financial Suite.
- NetSol Technologies Europe and Virtual Lease Services developed a Business Process Outsource service to address the broker market for own book management. In collaboration with funders, the service will form part of the funding approval sanction, which will generate a significant increase in sales opportunities.
- VLS signed new contracts with Investec and another European bank for providing due diligence and audit services.
- NTE concluded two license upgrades of its product LeaseSoft.
- Atheeb NetSol Saudi Company Limited recently won three projects in the area of network security, ISO/standard implementation of cyber security and consulting for local group of hospitals, Governmental security department and a construction group.
- Vroozzi® released new supplier purchase order pickup module, Vroozzi Purchase Manager.
- Vroozzi® released new vroozzi® Buy Route functionality in beta to global customer.

The success of the Company, in the near term, will depend, in large part, on the Company's ability to: (a) continue to grow revenues and improve profits; (b) adequately capitalize for growth in various markets and verticals; (c) make progress in the North American markets and, (d) continue to streamline sales and marketing efforts in every market we operate. However, management's outlook for the continuing operations, which has been consolidated and has been streamlined, remains optimistic.

Marketing and Business Development Activities

Management has developed, and the board of directors has ratified, an aggressive 3-5 year growth strategy aimed at increasing competitiveness and financial strength.

A focus of the marketing plan centers around the Global Launch of NFS Ascent™, the next generation of NFS that the company has been developing for nearly four years. Announced on October 24, 2013, NetSol has commenced a soft, regional launch with selected customers in APAC to test the readiness for the global markets. A formal launch of the global marketing plan is expected for all of our key markets of North America, Europe and APAC.

This plan is designed to:

- Achieve double digit revenue growth for the next 5 years
- Achieve 55% to 60% gross margins in 2014 and maintain 60% or better for the next three years
- Ramp up license revenues for NFS Ascent™

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The plan contemplates the following enhanced activities and initiatives to accomplish these goals:

- Grow delivery and sales capacity in APAC and the USA from approximately 600 NFS™ domain experts to over 1,000 within 18 months.
- Continue to build the delivery capacity. NetSol has hired over 100 new personnel in Quarter 1, 2014 to train and develop them to meet the long term growth outlook. This activity will continue until an optimum level of 1,000 NFS domain experts is achieved.
- Continue to advance infrastructure and systems in Lahore and Bangkok
- Strengthen the NetSol brand in the Americas and penetration in APAC markets such as China, Thailand, Indonesia, Australia and New Zealand.
- Hire and retain the best available talent to develop the next line of managers for our growing demand.
- Develop the sales and delivery capabilities for the Americas markets, in particular the growth in the US auto and banking sectors. A shift in revenue contribution from the Americas market would improve both gross and net operating margins due to the volume and size of US contracts
- Further position NetSol to deliver and support the new growth and technology dimensions in IT services, maintenance, mobile apps and cloud based solutions.

Management continues to be focused on scaling up its delivery capability and has achieved key milestones in that respect. Key projects are being delivered on time and on budget, quality initiatives are succeeding, especially in maturing internal processes. CMMI level companies are reassessed every three years by independent consultants under the standards of the Carnegie Mellon University to maintain its CMMI Level 5 quality certification. As required, NetSol was reassessed in 2010 and was successfully recertified as CMMI Level 5. While we believe this quality certification will be renewed, our current reassessment due for August 2013 is currently pending. We believe that the CMMI standards are a key reason in NetSol's demand surge worldwide. We remain convinced that this trend will continue for all NetSol offerings promoting further beneficial alliances and increasing the number and quality of our global customers.

MATERIAL TRENDS AFFECTING NETSOL

Management has identified the following material trends affecting NetSol.

Positive trends:

- Improving sales trends in US auto and banking sectors.
- Miliken Institute projects global economic growth in excess of 3% globally, 8% GDP growth for China, 2% GDP growth for the US over the next two years.
 - Slowly improving economic environment in the UK and major European economies.
 - The declining IT outsourcing from India gives strength to NetSol APAC delivery centers.
- New emerging markets and IT destinations in Thailand, Malaysia, Indonesia, Mexico, Australia, and some African nations.
 - Launch of NetSol Ascent™.
- Continued robustness of China's automobile and banking sectors. China's passenger vehicle sales rose 49% in December 2012, while China's total vehicle sales, including trucks and buses, are projected to accelerate this year and surpass 20 million for the first time according to Bloomberg News, February 7, 2013.

- Growing interest in Japan for IT services and NFS™ applications within banking, equipment finance and general leasing industries.
- Investment by the Kingdom of Saudi Arabia in healthcare, education, defense, cyberspace securities, IT, infrastructure and many other new sectors. This makes it one of the most promising markets for the Atheeb NetSol joint venture.
- Vroozi® provides a strong entry in the e-commerce and cloud by way of developing and marketing a new IP with the Vroozi® Shopping Platform and smartOCI® and landing Fortune 500 US customers.
- The dependency of our blue chip clients on NetSol solutions has further deepened; creating new enhancements, new modules, and services orders in the US.

Negative trends:

- Closure of United States government causing uncertainty in global US business decisions.
- Geopolitical unrest in the Middle East and in regions of Pakistan and Afghanistan.
- Continued strains in US-Pakistan relations.
- Despite efforts of newly elected government, security issues continue in Pakistan, causing concern for western customers, investors and media.
- The delays of CBRC licenses at least for another year in China.
- Emergence of smaller players offering IT solutions in China resulting in greater price competition.
- Continued sluggish European market could adversely affect our European business.
- Tightened liquidity and credit restrictions in consumer spending has either delayed or reduced spending on business solutions and systems, squeezing IT budgets and extending decision making cycles.
- Restricted liquidity and financial burden due to tighter internal processes and limited budgets might cause delays in the receivables from some clients.
- The threats of conflict between the US and other nations and Syria could potentially create volatility in oil prices causing readjustments of corporate budgets and consumer spending slowing global auto sales.
- Continued conflicts in Afghanistan could increase the migration of both refugees and extremists to Pakistan, thus creating domestic and regional challenges
- Our relatively low trading share volume makes the Company's stock price susceptible to market fluctuations.

CRITICAL ACCOUNTING POLICIES

Our financial statements and accompanying notes are prepared in accordance with accounting principles generally accepted in the United States ("U.S. GAAP"). Preparing financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, and expenses. These estimates and assumptions are affected by management's application of accounting policies. Critical accounting policies for us include revenue recognition and multiple element arrangements, intangible assets, software development costs, and goodwill.

REVENUE RECOGNITION

The Company recognizes revenue from license contracts without major customization when a non-cancelable, non-contingent license agreement has been signed, delivery of the software has occurred, the fee is fixed or determinable, and collectability is probable. Revenue from the sale of licenses with major customization, modification, and development is recognized on a percentage of completion method. Revenue from the implementation of software is recognized on a percentage of completion method.

Revenue from consulting services is recognized as the services are performed for time-and-materials contracts. Revenue from training and development services is recognized as the services are performed. Revenue from

maintenance agreements is recognized ratably over the term of the maintenance agreement, which in most instances is one year.

MULTIPLE ELEMENT ARRANGEMENTS

We may enter into multiple element revenue arrangements in which a customer may purchase a number of different combinations of software licenses, consulting services, maintenance and support, as well as training and development (multiple element arrangements).

VSOE of fair value for each element is based on the price for which the element is sold separately. We determine the VSOE of fair value of each element based on historical evidence of our stand-alone sales of these elements to third-parties or from the stated renewal rate for the elements contained in the initial software license arrangement. When VSOE of fair value does not exist for any undelivered element, revenue is deferred until the earlier of the point at which such VSOE of fair value exists or until all elements of the arrangement have been delivered. The only exception to this guidance is when the only undelivered element is maintenance and support or other services, then, the entire arrangement fee is recognized ratably over the performance period.

INTANGIBLE ASSETS

Intangible assets consist of product licenses, renewals, enhancements, copyrights, trademarks, trade names, and customer lists. Intangible assets with finite lives are amortized over the estimated useful life and are evaluated for impairment at least on an annual basis and whenever events or changes in circumstances indicate that the carrying value may not be recoverable. We assess recoverability by determining whether the carrying value of such assets will be recovered through the undiscounted expected future cash flows. If the future undiscounted cash flows are less than the carrying amount of these assets, we recognize an impairment loss based on the excess of the carrying amount over the fair value of the assets.

SOFTWARE DEVELOPMENT COSTS

Costs incurred to internally develop computer software products or to enhance an existing product are recorded as research and development costs and expensed when incurred until technological feasibility for the respective product is established. Thereafter, all software development costs are capitalized and reported at the lower of unamortized cost or net realizable value. Capitalization ceases when the product or enhancement is available for general release to customers.

The Company makes on-going evaluations of the recoverability of its capitalized software projects by comparing the amount capitalized for each product to the estimated net realizable value of the product. If such evaluations indicate that the unamortized software development costs exceed the net realizable value, the Company writes off the amount which the unamortized software development costs exceed net realizable value. Capitalized and purchased computer software development costs are being amortized ratably based on the projected revenue associated with the related software or on a straight-line basis.

STOCK-BASED COMPENSATION

Our stock-based compensation expense is estimated at the grant date based on the award's fair value as calculated by the Black-Scholes-Merton (BSM) option pricing model and is recognized as expense over the requisite service period. The BSM model requires various highly judgmental assumptions including expected volatility and expected term. If any of the assumptions used in the BSM model changes significantly, stock-based compensation expense may differ materially in the future from that recorded in the current period. In addition, we are required to estimate the expected forfeiture rate and only recognize expense for those shares expected to vest. We estimate the forfeiture rate based on historical experience and our expectations regarding future pre-vesting termination behavior of employees. To the extent our actual forfeiture rate is different from our estimate; stock-based compensation expense is adjusted accordingly.

GOODWILL

Goodwill represents the excess of the aggregate purchase price over the fair value of the net assets acquired in a purchase businesses combination. Goodwill is reviewed for impairment on an annual basis, or more frequently if events or changes in circumstances indicate that the carrying amount of goodwill may be impaired. The goodwill impairment test is a two-step test. Under the first step, the fair value of the reporting unit is compared with its carrying value (including goodwill). If the fair value of the reporting unit is less than its carrying value, an indication of goodwill impairment exists for the reporting unit and the enterprise must perform step two of the impairment test (measurement). Under step two, an impairment loss is recognized for any excess of the carrying amount of the reporting unit's goodwill over the implied fair value of that goodwill. The implied fair value of goodwill is determined by allocating the fair value of the reporting unit in a manner similar to a purchase price allocation. The residual fair value after this allocation is the implied fair value of the reporting unit goodwill. Fair value of the reporting unit is determined using a discounted cash flow analysis. If the fair value of the reporting unit exceeds its carrying value, step

two does not need to be performed.

RECENT ACCOUNTING PRONOUNCEMENTES

For information with respect to recent accounting pronouncements and the impact of these pronouncements on our consolidated financial statements, see Note 2 of Notes to Condensed Consolidated Financial Statements included elsewhere in this Quarterly Report.

AVAILABLE INFORMATION

Through the company's web sites, its customers, both existing and potential, and investors can access a wide range of information about its product offerings, and support and technical matters.

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Our website is located at www.netsoltech.com, and our investor relations website is located at <http://www.netsoltech.com/IR/>. The following filings are available through our investor relations website after we file with the SEC: Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, and our Proxy Statements for our annual meetings of stockholders. These filings are also available for download free of charge on our investor relations website. We also provide a link to the section of the SEC's website at www.sec.gov that has all of our public filings, including Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, all amendments to those reports, our Proxy Statements and other ownership related filings. Further, a copy of this Quarterly Report on Form 10-Q is located at the SEC's Public Reference Room at 100 F Street, NE, Washington D.C. 20549. Information on the operation of the Public Reference Room can be obtained by calling the SEC at 1-800-SEC-0330.

We webcast our earnings calls and certain events we participate in or host with members of the investment community on our investor relations website. Additionally, we provide notifications of news or announcements regarding our financial performance, including SEC filings, investor events, press and earnings releases, and blogs as part of our investor relations website. Investors and others can receive notifications of new information posted on our investor relations website by signing up for e-mail alerts. Further corporate governance information, including our committee charters and code of conduct, is also available on our investor relations website at <http://www.netsoltech.com/us/investors/corporate-governance>. The content of our websites are not intended to be incorporated by reference into this 10-Q or in any other report or document we file with the SEC, and any references to our websites are intended to be inactive textual references only.

CHANGES IN FINANCIAL CONDITION

Quarter Ended September 30, 2013 as compared to the Quarter Ended September 30, 2012

Net revenues for the quarter ended September 30, 2013 and 2012 are broken out among the subsidiaries as follows:

| | 2013 | | 2012 | |
|------------------------|-------------|----------|--------------|----------|
| | Revenue | % | Revenue | % |
| Corporate headquarters | \$- | 0.00 % | \$- | 0.00 % |
| North America: | | | | |
| NTNA | 1,081,618 | 11.94 % | 1,279,721 | 11.56 % |
| Vroozii | 136,394 | 1.51 % | 433,469 | |
| | 1,218,012 | 13.45 % | 1,713,190 | 15.47 % |
| Europe: | | | | |
| Netsol UK | - | 0.00 % | - | 0.00 % |
| NTE | 777,693 | 8.59 % | 1,117,915 | 10.10 % |
| VLS | 430,989 | 4.76 % | 388,086 | 3.51 % |
| HAFL | - | 0.00 % | - | 0.00 % |
| | 1,208,682 | 13.34 % | 1,506,001 | 13.60 % |
| Asia-Pacific: | | | | |
| NetSol PK | 4,787,147 | 52.85 % | 3,793,002 | 34.26 % |
| Netsol-Innovation | 967,543 | 10.68 % | 804,509 | 7.27 % |
| Connect | 196,380 | 2.17 % | 169,243 | 1.53 % |
| Abraxas | 70,271 | 0.78 % | 751,889 | 6.79 % |
| NTPK Thailand | 387,467 | 4.28 % | 2,334,066 | 21.08 % |
| NetSol Beijing | 221,814 | 2.45 % | - | 0.00 % |
| | 6,630,622 | 73.21 % | 7,852,709 | 70.92 % |
| Total | \$9,057,316 | 100.00 % | \$11,071,900 | 100.00 % |

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The following table sets forth the items in our unaudited consolidated statement of operations for the three months ended September 30, 2013 and 2012 as a percentage of revenues.

| | For the Three Months Ended September 30, | | | |
|--|---|----------|--------------|----------|
| | 2013 | % | 2012 | % |
| Net Revenues: | | | | |
| License fees | \$ 2,252,567 | 24.87 % | \$ 3,241,501 | 29.28 % |
| Maintenance fees | 2,380,409 | 26.28 % | 2,045,706 | 18.48 % |
| Services | 4,424,340 | 48.85 % | 5,784,693 | 52.25 % |
| Total net revenues | 9,057,316 | 100.00 % | 11,071,900 | 100.00 % |
| Cost of revenues: | | | | |
| Salaries and consultants | 3,456,604 | 38.16 % | 3,385,668 | 30.58 % |
| Travel | 396,784 | 4.38 % | 325,294 | 2.94 % |
| Repairs and maintenance | 175,821 | 1.94 % | 127,997 | 1.16 % |
| Insurance | 39,554 | 0.44 % | 37,719 | 0.34 % |
| Depreciation and amortization | 1,046,669 | 11.56 % | 958,151 | 8.65 % |
| Other | 544,337 | 6.01 % | 921,858 | 8.33 % |
| Total cost of revenues | 5,659,769 | 62.49 % | 5,756,687 | 51.99 % |
| Gross profit | 3,397,547 | 37.51 % | 5,315,213 | 48.01 % |
| Operating expenses: | | | | |
| Selling and marketing | 1,071,412 | 11.83 % | 762,963 | 6.89 % |
| Depreciation and amortization | 426,617 | 4.71 % | 342,001 | 3.09 % |
| Bad debt expense | 251,673 | 2.78 % | - | 0.00 % |
| Salaries and wages | 1,441,132 | 15.91 % | 1,153,873 | 10.42 % |
| Professional services, including non-cash compensation | 306,663 | 3.39 % | 206,502 | 1.87 % |
| General and administrative | 1,423,002 | 15.71 % | 1,347,928 | 12.17 % |
| Total operating expenses | 4,920,499 | 54.33 % | 3,813,267 | 34.44 % |
| (Loss) income from operations | (1,522,952) | -16.81 % | 1,501,946 | 13.57 % |
| Other income and (expenses) | | | | |
| (Loss) gain on sale of assets | (13,795) | -0.15 % | 14,296 | 0.13 % |
| Interest expense | (69,217) | -0.76 % | (292,389) | -2.64 % |
| Interest income | 32,854 | 0.36 % | 24,167 | 0.22 % |
| Gain on foreign currency exchange transactions | 1,111,423 | 12.27 % | 395,156 | 3.57 % |
| Share of net income from equity investment | 9,192 | 0.10 % | - | 0.00 % |
| Amortization of financing costs | - | 0.00 % | (367,744) | -3.32 % |
| Other income | 678 | 0.01 % | (32) | 0.00 % |
| Total other income (expenses) | 1,071,135 | 11.83 % | (226,546) | -2.05 % |
| Net (loss) income before income taxes | (451,818) | -4.99 % | 1,275,400 | 11.52 % |
| Income taxes | (11,131) | -0.12 % | (13,996) | -0.13 % |
| Net (loss) income after tax | (462,949) | -5.11 % | 1,261,404 | 11.39 % |
| Non-controlling interest | (634,167) | -7.00 % | (332,279) | -3.00 % |
| Net (loss) income attributable to NetSol | (1,097,116) | -12.11 % | 929,125 | 8.39 % |

Net revenues for the quarter ended September 30, 2013 were \$9,057,316, as compared to \$11,071,900 for the quarter ended September 30, 2012. This reflects a decrease of \$2,014,584, or 18.20% in the current quarter as compared to the corresponding quarter last year. Year over year, revenue from license income decreased by \$988,934. The

company has recently launched its next generation platform “NFS Ascent™” and some of the deals in pipeline for the legacy product have been delayed as the customers are now looking for the next generation. Revenue from the license sales of our legacy product “NetSol Financial Suite™” as well as services associated with the new sales have been impacted in the current quarter. Management is expecting sales of the legacy product to remain under pressure for at least two to three quarters until the time that we begin recognizing revenues for NFS Ascent™. Services revenue, which also includes consulting and implementation, decreased to \$4,424,340, as compared to \$5,784,693 last year. Maintenance fees increased by \$334,703, to \$2,380,409 in the current quarter, as compared to \$2,045,706 in the comparable period. The increase in maintenance fees is due to re-negotiation of rates with some of the customers.

The gross profit was \$3,397,547, in the quarter ending September 30, 2013 as compared with \$5,315,213 for the same quarter of the previous year. This is a decrease of 36.08% or \$1,917,666. The gross profit percentage for the quarter also decreased to 37.51% from 48.01% in the quarter ended September 30, 2012 mainly due to reduction in total revenues. The cost of sales was \$5,659,769 in the current quarter compared to \$5,756,687 in the comparable quarter of fiscal 2013. As a percentage of sales it increased from 51.99% for the quarter ended September 30, 2012 to 62.49% in the current quarter. Salaries and consultant fees slightly increased by \$70,936; from \$3,385,668, in the prior comparable quarter, to \$3,456,604. As a percentage of sales, it increased from 30.58% in the prior comparable quarter to 38.16% in the current quarter. Depreciation and amortization expense increased to \$1,046,669 compared to \$958,151 in the corresponding quarter last year or an increase of \$88,518.

Operating expenses were \$4,920,499 for the quarter ending September 30, 2013 as compared to \$3,813,267, for the corresponding period last year or an increase of 29.04% or \$1,107,232. As a percentage of sales, it increased from 34.44% to 54.15%. Depreciation and amortization expense amounted to \$426,617 and \$342,001 for the quarter ended September 30, 2013 and 2012, respectively. Combined salaries and wage costs were \$1,441,132 and \$1,153,873 for the comparable periods, respectively. As a percentage of sales, these costs increased from 10.42% to 15.86%. The combined salaries and wages also include non-cash expense on exercise of options. General and administrative expenses were \$1,423,002 and \$1,347,928 for the quarters ended September 30, 2013 and 2012, respectively, an increase of \$75,074 or 5.57%. As a percentage of sales, these expenses were 15.66% in the current quarter compared to 12.17% in the comparable quarter.

Selling and marketing expenses were \$1,071,412 and \$762,963, in the quarter ended September 30, 2013 and 2012, respectively. We are marketing our products in different geographies of the world and have hired more professional resources for business development. Also the aggressive marketing of smartOCI® and other Vrooz® products in North America and Europe has increased the sales and marketing expenses. Professional services expense increased by 48.50% to \$306,663 in the quarter ended September 30, 2013, from \$206,502 in the corresponding period last year.

Loss from operations was \$1,522,952, compared to income of \$1,501,946, for the quarters ended September 30, 2013 and 2012, respectively. This represents a decrease of \$3,024,898 for the quarter compared with the comparable period in the prior year. As a percentage of sales, net loss from operations was 16.81% in the current quarter compared to income of 13.57% in the prior period.

Net loss was \$1,097,116, compared to income of \$929,125, for the quarters ended September 30, 2013 and 2012, respectively. This is a decrease of \$2,026,241 compared to the prior year. Included in this income is foreign currency exchange gain of \$1,111,423 compared to \$395,156 in the same reporting period last year, mainly due to appreciation of the USD, Euro and Pound in the prior period against the Pakistan Rupee. Also included in the net income is the share of net income of \$9,192 from an associated company as compared to \$Nil in the corresponding period. The current fiscal quarter amount includes a net reduction of \$634,167, compared to \$332,279 in the prior period, for the 49.9% non-controlling interest in NetSol Innovation owned by other parties, the 35.77% non-controlling interest in NetSol PK, 49% non-controlling interest in VLS and 9.09% non-controlling interest in Vrooz®. Interest expense was \$69,217 in the current quarter as compared to \$292,389 in the comparable period. The reduction in interest expense is due to conversion of all the convertible notes into equity. Net loss per share, basic and diluted, was \$0.12 as compared to net income \$0.12 for the quarters ended September 30, 2013 and 2012, respectively.

The net EBITDA income was \$423,665 compared to \$2,511,495 for the quarters ended September 30, 2013 and 2012, after amortization and depreciation charges of \$1,473,286 and \$1,300,152, income taxes of \$11,131 and \$13,996, interest expense of \$69,217 and \$292,389, and interest income of \$32,854 and \$24,167 respectively. The EBITDA earning per share, basic and diluted was \$0.05 for the quarter ended September 30, 2013 as compared to \$0.33 for the quarter ended September 30, 2012. As a percentage of revenues, EBITDA was 4.68% compared to 22.68% for the quarters ended September 30, 2013 and 2012, respectively. Although the net EBITDA income is a non-GAAP measure of performance, we are providing it because we believe it to be an important supplemental measure of our

performance that is commonly used by securities analysts, investors, and other interested parties in the evaluation of companies in our industry. It should not be considered as an alternative to net income, operating income or any other financial measures calculated and presented, nor as an alternative to cash flow from operating activities as a measure of our liquidity. It may not be indicative of our historical operating results nor is it intended to be predictive of potential future results.

LIQUIDITY AND CAPITAL RESOURCES

We note that our cash position was \$6,755,950 at September 30, 2013, compared to \$8,019,788 at September 30, 2012.

Net cash provided by operating activities amounted to \$2,756,269 for the three months ended September 30, 2013, as compared to \$2,898,831 for the comparable period last fiscal year. At September 30, 2013, we had current assets of \$41,870,013 and current liabilities of \$14,445,088. We had accounts receivable of 18,535,948 and revenues in excess of billings of \$11,435,167. Our revenues in excess of billings will be reclassified to accounts receivable pursuant to billing requirements detailed in each contract. Accounts payable and accrued expenses amounted to \$4,498,965 and \$3,660,388, respectively at September 30, 2013.

Net cash used by investing activities amounted to \$3,972,805 for the three months ended September 30, 2013, as compared to \$2,488,599 for the comparable period last fiscal year. We had net purchases of property and equipment of \$2,671,222 compared to \$1,457,134 for the comparable period last fiscal year. The increase in intangible assets which represents amounts capitalized for the development of new products was \$1,362,026 and \$1,091,966 for the comparable periods.

Net cash provided by financing activities amounted to \$630,382 and \$171,628 for the three months ended September 30, 2013, and 2012, respectively. The three months ended September 30, 2013 included the cash inflow of \$560,500 from the exercising of stock options and warrants compared to \$252,900 in the three months ended September 30, 2012. In the current fiscal period, we had net payments on account of bank loans and capital leases of \$198,853 as compared to \$1,160,684 in the comparable period last year. We are operating in various geographical regions of the world through its various subsidiaries. Those subsidiaries have financial arrangements from various financial institutions to meet both their short and long term funding requirements. These loans will become due at different maturity dates the detail of which is given in Note No. 13 of the annexed financial statements. We are in compliance with the covenants of the financial arrangements and there is no default, whatsoever, which may lead to early payment of these obligations. We anticipate paying back all these obligations on their respective due dates from its own sources.

We remain open to strategic relationships that would provide value added benefits. The focus will remain on continuously improving cash reserves internally and reduced reliance on external capital raise.

As a growing company, we have on-going capital expenditure needs based on our short term and long term business plans. Although our requirements for capital expenses vary from time to time, for the next 12 months, we anticipate needing working capital of \$5.0 to \$7.0 million for US, Europe and UAE, new business development activities and infrastructure enhancements.

While there is no guarantee that any of these methods will result in raising sufficient funds to meet our capital needs or that even if available will be on terms acceptable to us, we will be very cautious and prudent about any new capital raise given the global market uncertainties. However, we are very conscious of the dilutive effect and price pressures in raising equity-based capital.

Financial Covenants

Our UK based subsidiary, NetSol Technologies Europe Limited (NTE) has an approved overdraft facility of £200,000 which requires that the aggregate amount of invoiced trade debtors (net of provisions for bad and doubtful debts and excluding intra-group debtors) of NTE, not exceeding 90 days old, will not be less than an amount equal to 200% of the facility. NTE had been granted another credit facility of £1,000,000 for the acquisition VLS. This facility requires that NTE's adjusted tangible net worth would not be less than £600,000. For this purpose, adjusted tangible net worth

means shareholders' funds less intangible assets plus non-redeemable preference shares. In addition, NTE's cash debt service coverage would not fall below 150% of the aggregate debt service cost. The Pakistani subsidiary, NetSol Technologies Limited (NTPK) has an approved facility for both export refinance and term finance from Askari Bank Limited amounting to Rupees 312.5 million (\$3,097,126) which requires NTPK to maintain a long term debt equity ratio of 60:40 and the current ratio of 1:1.

As of the date of this report, we are in compliance with the financial covenants associated with our borrowings. The maturity dates of the borrowings of respective subsidiaries may accelerate if they do not comply with these covenants. In case of any change in control in subsidiaries, they may have to repay their respective credit facilities.

Item 3. Quantitative and Qualitative Disclosures about Market Risks.

None.

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Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures pursuant to Rule 13a-15 under the Exchange Act, as of the end of the period covered by this Quarterly Report on Form 10-Q. Based upon that evaluation, the Chief Financial Officer and Chief Executive Officer concluded that our disclosure controls and procedures were not effective.

Management's Report on Internal Control over Financial Reporting

Our management has the responsibility to establish and maintain adequate internal controls over our financial reporting, as defined in Rule 13a-15(f) under the Securities and Exchange Act of 1934. Our internal controls are designed to provide reasonable assurance regarding the reliability of our financial reporting and the preparation of our external financial statements in accordance with generally accepted accounting principles (GAAP).

Due to inherent limitations of any internal control system, management acknowledges that there are limitations as to the effectiveness of internal controls over financial reporting and therefore recognize that only reasonable assurance can be gained from any internal control system. Accordingly, our internal control system may not detect or prevent material misstatements in our financial statements and projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Under the supervision and participation of management, including the Chief Executive Officer and Chief Financial Officer, we have performed an assessment of the effectiveness of our internal controls over financial reporting as of September 30, 2013. This assessment was based on the criteria established in Internal Control-Integrated Framework, issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on the results of our assessment, the Company has determined that as of September 30, 2013, there was a material weakness in the Company's internal control over financial reporting. Specifically, while in the performance of this assessment, management identified that its core accounting staff does not have necessary technical accounting training relating to accounting for complex U.S. GAAP matters. Based on this evaluation, management concluded that our internal control over financial reporting was not effective as of September 30, 2013. Notwithstanding the existence of such material weakness in our internal controls over financial reporting, our management, including our Chief Executive Officer, believes that the financial statements included in this report fairly present in all material respects our financial condition, results of operations and cash flows for the periods presented.

On September 9, 2013, the Company appointed Roger Almond, C.P.A. to act as Chief Financial Officer of NetSol. Management believes that Mr. Almond's appointment as CFO results in the requisite technical accounting knowledge and training relating to accounting for complex U.S. GAAP matters. Management believes that Mr. Almond's appointment will result in the removal of the material weakness in subsequent quarters.

Changes in Internal Control over Financial Reporting

Except for the hiring of a new Chief Financial Officer on September 9, 2013, there have been no changes in our internal controls over financial reporting during the first quarter of fiscal year 2014, that have materially affected, or are reasonable likely to materially affect, the Company's internal control over financial reporting (as defined in Exchange Act Rules 13a – 15(f) and 15d – 15(f)).

PART II OTHER INFORMATION

Item 1. Legal Proceedings

To the best knowledge of Company's management and counsel, there is no material litigation pending or threatened against the Company.

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Item 1A. Risk Factors

The Announcement Of Our New Generation Product, NFS Ascent™, May Result In A Reduction In New License Sales For Our Earlier Generation Product And Accordingly A Drop In Revenues.

On October 24, 2013, the Company announced the introduction and global release of NFS Ascent™, the company's next generation platform. While the Company believes that the new product will be well-received and is positioned to generate more lucrative license and related services revenues, we anticipate that new licenses for the old product will diminish in numbers larger than new product licenses, resulting in a drop in revenues until the new product gains traction in the market.

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

Item 3. Defaults Upon Senior Securities

None.

Item 4. Submission Of Matters To A Vote Of Security Holders

None.

Item 5. Other Information

None.

Item 6. Exhibits

31.1 Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (CEO)

31.2 Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (CFO)

32.1 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (CEO)

32.2 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (CFO)

SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

NETSOL TECHNOLOGIES, INC.

Date: November 8, 2013

/s/ Najeeb Ghauri

NAJEEB GHOURI
Chief Executive Officer

Date: November 8, 2013

/s/Roger Almond

ROGER K. ALMOND
Chief Financial Officer
Principal Accounting Officer