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 December 31, 2010

☐ 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 | 95-4627685 |
| (State or other Jurisdiction of Incorporation or Organization) | (I.R.S. Employer NO.) |

23901 Calabasas Road, Suite 2072, 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 ☐ | Accelerated Filer ☐ |
| Non-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 51,083,285 shares of its $.001 par value Common Stock and no shares of Series A 7% Cumulative Convertible Preferred Stock issued and outstanding as of February 8, 2011.

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

| | As of December 31, 2010 | As of June 30, 2010 |
|---|---|---|
| **ASSETS** | | |
| **Current assets:** | | |
| Cash and cash equivalents | $ 5,856,152 | $ 4,075,546 |
| Restricted Cash | 5,700,000 | 5,700,000 |
| Accounts receivable, net of allowance for doubtful accounts | 15,059,935 | 12,280,331 |
| Revenues in excess of billings | 11,001,000 | 9,477,278 |
| Other current assets | 1,762,098 | 1,821,661 |
| Total current assets | 39,379,185 | 33,354,816 |
| **Investment under equity method** | 58,269 | 200,506 |
| **Property and equipment**, net of accumulated depreciation | 10,950,969 | 9,472,917 |
| **Intangibles:** | | |
| Product licenses, renewals, enhancements, copyrights, trademarks, and tradenames, net | 21,320,814 | 19,002,081 |
| Customer lists, net | 415,645 | 666,575 |
| Goodwill | 9,439,285 | 9,439,285 |
| Total intangibles | 31,175,745 | 29,107,941 |
| **Total assets** | $ 81,564,168 | $ 72,136,180 |
| | | |
| **LIABILITIES AND STOCKHOLDERS' EQUITY** | | |
| **Current liabilities:** | | |
| Accounts payable and accrued expenses | $ 4,752,181 | $ 4,890,921 |
| Due to officers | - | 10,911 |
| Current portion of loans and obligations under capitalized leases | 6,509,412 | 7,285,773 |
| Other payables - acquisitions | 103,226 | 103,226 |
| Unearned revenues | 3,616,186 | 2,545,314 |
| Deferred liability | 32,066 | 47,066 |
| Convertible notes payable , current portion | 4,087,109 | 3,017,096 |
| Loans payable, bank | 2,321,047 | 2,327,476 |
| Common stock to be issued | 263,825 | 239,525 |
| Total current liabilities | 21,685,053 | 20,467,308 |
| **Obligations under capitalized leases,** less current maturities | 483,221 | 204,620 |
| **Convertible notes payable less current maturities** | - | 4,066,109 |
| **Long term loans;** less current maturities | 580,262 | 727,336 |
| **Lease abandonment liability; long term** | 867,583 | 867,583 |
| **Total liabilities** | 23,616,118 | 26,332,956 |
| **Commitments and contingencies** | | |
| **Stockholders' equity:** | | |
| Common stock, $.001 par value; 95,000,000 shares authorized; 49,685,342 & 37,103,396 issued and outstanding | 49,686 | 37,104 |
| Additional paid-in-capital | 93,244,355 | 86,002,648 |
| Treasury stock | (396,008) | (396,008) |
| Accumulated deficit | (36,356,313) | (39,859,030) |
| Stock subscription receivable | (2,105,960) | (2,007,960) |
| Other comprehensive loss | (7,880,946) | (8,396,086) |
| Non-controlling interest | 11,393,236 | 10,422,557 |
| **Total stockholders' equity** | 57,948,049 | 45,803,224 |
| **Total liabilities and stockholders' equity** | $ 81,564,168 | $ 72,136,180 |

See accompanying notes to these unaudited consolidated financial statements.

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

| | For the Three Months Ended December 31, 2010 | For the Three Months Ended December 31, 2009 | For the Six Months Ended December 31, 2010 | For the Six Months Ended December 31, 2009 |
|---|---|---|---|---|
| **Net Revenues:** | | | | |
| License fees | $ 3,129,063 | $ 3,318,936 | $ 6,606,856 | $ 5,870,529 |
| Maintenance fees | 2,023,509 | 1,780,336 | 3,693,428 | 3,588,053 |
| Services | 5,272,675 | 4,420,535 | 8,528,035 | 7,683,299 |
| Total revenues | 10,425,247 | 9,519,808 | 18,828,319 | 17,141,881 |
| **Cost of revenues:** | | | | |
| Salaries and consultants | 2,127,280 | 2,005,845 | 4,114,168 | 4,019,598 |
| Travel | 238,776 | 329,007 | 470,388 | 389,207 |
| Repairs and maintenance | 71,459 | 69,112 | 128,517 | 136,723 |
| Insurance | 31,087 | 36,030 | 62,079 | 72,709 |
| Depreciation and amortization | 679,284 | 573,268 | 1,310,225 | 1,071,772 |
| Other | 348,859 | 585,157 | 591,997 | 1,467,495 |
| Total cost of revenues | 3,496,745 | 3,598,418 | 6,677,374 | 7,157,503 |
| **Gross profit** | 6,928,503 | 5,921,390 | 12,150,945 | 9,984,378 |
| **Operating expenses:** | | | | |
| Selling and marketing | 1,002,877 | 526,751 | 1,486,847 | 1,020,381 |
| Depreciation and amortization | 267,861 | 418,023 | 534,303 | 930,384 |
| Bad debt expense | (353) | 212,840 | 254,279 | 212,840 |
| Salaries and wages | 736,898 | 743,970 | 1,657,162 | 1,468,665 |
| Professional services, including non-cash compensation | 151,276 | 210,795 | 290,361 | 306,901 |
| Lease abandonment charges | - | 1,076,347 | - | 1,076,347 |
| General and adminstrative | 873,569 | 1,042,172 | 2,006,088 | 2,132,183 |
| Total operating expenses | 3,032,128 | 4,230,898 | 6,229,041 | 7,147,701 |
| **Income (loss) from operations** | 3,896,375 | 1,690,492 | 5,921,904 | 2,836,677 |
| **Other income and (expenses)** | | | | |
| Loss on sale of assets | (792) | (89,119) | (15,586) | (89,101) |
| Interest expense | (291,475) | (372,273) | (607,119) | (840,887) |
| Interest income | 9,958 | 33,752 | 94,419 | 151,562 |
| Gain (loss) on foreign currency exchange transactions | (400,658) | (3,247) | 673,236 | 380,577 |
| Share of net loss from equity investment | (71,799) | - | (142,236) | - |
| Beneficial conversion feature | (118,163) | (595,215) | (295,574) | (893,214) |
| Other income (expense) | (1,748) | (50,825) | (57,301) | (81,975) |
| Total other income (expenses) | (874,677) | (1,076,927) | (350,162) | (1,373,038) |
| **Net income before non-controlling interest in subsidiary and income taxes** | 3,021,698 | 613,565 | 5,571,742 | 1,463,639 |
| **Income taxes** | (3,168) | (32,526) | (11,724) | (37,543) |
| **Net income after income tax but before non-controlling interest in subsidiary** | 3,018,530 | 581,039 | 5,560,018 | 1,426,096 |
| **Non-controlling interest** | (1,082,792) | (1,028,917) | (2,057,301) | (2,137,892) |
| ***Net income (loss) attibutable to NetSol*** | 1,935,737 | (447,878) | 3,502,718 | (711,796) |
| | | | | |
| **Other comprehensive income (loss):** | | | | |
| Translation adjustment | 784,153 | (538,141) | 515,139 | (854,005) |
| **Comprehensive income (loss)** | $ 2,719,890 | $ (986,019) | $ 4,017,857 | $ (1,565,801) |
| | | | | |
| **Net income (loss) per share:** | | | | |
| Basic | $ 0.04 | $ (0.01) | $ 0.08 | $ (0.02) |
| Diluted | $ 0.04 | $ (0.01) | $ 0.08 | $ (0.02) |
| Weighted average number of shares outstanding | | | | |
| Basic | 48,366,323 | 34,447,142 | 43,955,210 | 33,041,760 |
| Diluted | 51,058,140 | 34,447,142 | 46,647,027 | 33,041,760 |

See accompanying notes to these unaudited consolidated financial statements.

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

| | For the Six Months Ended December 31, 2010 | 2009 |
|---|---|---|
| **Cash flows from operating activities:** | | |
| Net income | $ 5,560,018 | $ 1,426,096 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 1,844,528 | 2,002,157 |
| Provision for bad debts | 254,279 | 212,840 |
| Loss on foreign currency exchange transaction | - | 19,582 |
| Share of net loss from investment under equity method | 142,236 | - |
| Loss on sale of assets | 15,586 | 89,101 |
| Stock issued for notes payable and related interest | 35,808 | 27,825 |
| Stock issued for services | 577,943 | 300,329 |
| Fair market value of warrants and stock options granted | 175,341 | 651,018 |
| Beneficial conversion feature | 295,574 | 893,214 |
| **Changes in operating assets and liabilities:** | | |
| Increase/ decrease in accounts receivable | (1,863,668) | 237,431 |
| Increase/ decrease in other current assets | (1,377,332) | (1,632,327) |
| Increase/ decrease in accounts payable and accrued expenses | (353,493) | 147,556 |
| **Net cash provided by operating activities** | 5,306,822 | 4,374,821 |
| **Cash flows from investing activities:** | | |
| Addition to property and equipment | (2,450,222) | (1,085,787) |
| Disposal of property and equipment | 19,988 | 227,773 |
| Purchase of non-controlling interest in subsidiary | (180,000) | - |
| Short-term investments held for sale | (256,706) | - |
| Increase in intangible assets | (3,127,234) | (3,118,094) |
| **Net cash used in investing activities** | (5,994,175) | (3,976,108) |
| **Cash flows from financing activities:** | | |
| Proceeds from sale of common stock | 2,566,750 | 514,539 |
| Proceeds from the exercise of stock options and warrants | 667,300 | 33,750 |
| Proceeds from convertible notes payable | - | 2,000,000 |
| Redemption of preferred stock | - | (1,920,000) |
| Dividend Paid | - | (44,090) |
| Bank overdraft | (156,849) | (221,382) |
| Proceeds from bank loans | 2,588,773 | 2,727,657 |
| Payments on bank loans | (44,455) | (352,887) |
| Payments on capital lease obligations & loans - net | (3,035,240) | (2,183,189) |
| **Net cash provided by financing activities** | 2,586,278 | 554,399 |
| **Effect of exchange rate changes in cash** | (118,318) | (145,201) |
| **Net increase in cash and cash equivalents** | 1,780,607 | 807,911 |
| Cash and cash equivalents, beginning of period | 4,075,546 | 4,403,762 |
| **Cash and cash equivalents, end of period** | $ 5,856,152 | $ 5,211,674 |

See accompanying notes to the unaudited consolidated financial statements.

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

| | For the Six Months Ended December 31, 2010 | 2009 |
|---|---|---|
| SUPPLEMENTAL DISCLOSURES: | | |
| Cash paid during the period for: | | |
| Interest | $ 597,347 | $ 357,400 |
| Taxes | $ 1,729 | $ 95,111 |
| | | |
| NON-CASH INVESTING AND FINANCING ACTIVITIES: | | |
| Stock issued for the conversion of Notes Payable | $ 1,900,598 | $ 1,200,000 |
| Purchase of property and equipment under capital lease | $ - | $ 101,376 |

See accompanying notes to the unaudited consolidated financial statements.

**NETSOL TECHNOLOGIES, INC. AND SUBSIDIARIES**
**NOTES TO UNAUDITED 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 consolidated condensed 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, 2010. 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 North America, Inc. ("NTNA")
NetSol Technologies Limited ("NetSol UK")
NetSol Connect (Private), Ltd. ("Connect)
NetSol-Abraxas Australia Pty Ltd. ("Abraxas")
NetSol Technologies Europe Limited ("NTE")
NTPK (Thailand) Co. Limited ("NTPK Thailand")

Majority-owned Subsidiaries
NetSol Technologies, Ltd. ("NetSol PK")
NetSol Innovation (Private) Limited ("NetSol Innovation")

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

## NOTE 2 - 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.

## NOTE 3 - NEW ACCOUNTING PRONOUNCEMENTS:

In October 2009, the FASB amended guidance related to revenue recognition that will be effective for the Company beginning July 1, 2010. Under the new guidance on arrangements that include software elements, tangible products that have software components that are essential to the functionality of the tangible product will no longer be within the scope of the software revenue recognition guidance, and software-enabled products will now be subject to other relevant revenue recognition guidance. Additionally, the FASB amended guidance on revenue arrangements with multiple deliverables that are outside the scope of the software revenue recognition guidance. Under the new guidance, when vendor specific objective evidence or third party evidence for deliverables in an arrangement cannot be determined, a best estimate of the selling price is required to separate deliverables and allocate arrangement consideration using the relative selling price method. The new guidance includes new disclosure requirements on how the application of the relative selling price method affects the timing and amount of revenue recognition. Adoption of the new guidance did not have a material impact on our financial statements.

In December 2009, the FASB amended guidance related to fair value measurements and Disclosures, which was effective beginning the 2nd quarter of the Company's 2010 fiscal year, December 31, 2009. These amendments prescribe new disclosures and clarify certain existing disclosure requirements related to fair value measurements. The objective of the amendments was to improve these disclosures and, thus, increase the transparency in financial reporting. The adoption of these amendments did not have a material impact on the Company's consolidated financial statements.

In February 2010, the FASB amended guidance related to disclosure of subsequent events, which was effective upon issuance. These amendments prescribe that entities that are SEC filers are required to evaluate subsequent events through the date that the financial statements are issued. The adoption of these amendments did not have a material impact on the Company's consolidated financial statements.

**NOTE 4 – EARNINGS/(LOSS) PER SHARE:**

Basic earnings per share is 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, and stock awards.

The components of basic and diluted earnings per share for the six months ended December 31, 2010 and 2009 were as follows:

| For the period ended December 31, 2010 | Net Income | Shares | Per Share |
|---|---|---|---|
| Basic income per share: | $ 3,502,718 | 43,955,210 | $ 0.08 |
| Dividend to preferred shareholders | - | | |
| Net income available to common shareholders | | | |
| Effect of dilutive securities* | | | |
| Stock options | | 1,271,378 | |
| Warrants | | 1,420,439 | |
| Convertible Note -1 | | - | |
| Diluted (loss) per share | $ 3,502,718 | 46,647,027 | $ 0.08 |

| For the period ended December 31, 2009 | Net Loss | Shares | Per Share |
|---|---|---|---|
| Basic (loss) per share: | $ (711,796) | 33,041,760 | $ (0.02) |
| Dividend to preferred shareholders | - | | $ - |
| Net income available to common shareholders | | | |
| Effect of dilutive securities* | | | |
| Stock options | | - | |
| Warrants | | - | |
| Convertible Note | | - | |
| Diluted (loss) per share | $ (711,796) | 33,041,760 | $ (0.02) |

* As there is a loss, these securities are anti-dilutive. The basic and diluted loss per share is the same for the six months ended December 31, 2009.

1 During the period ended December 31, 2010, convertible notes payable were not included in the computation of diluted earnings per share because the effect of conversion would be antidilutive.

**NOTE 5 – OTHER COMPREHENSIVE INCOME & FOREIGN CURRENCY:**

The accounts of NetSol UK and NTE use the British Pound; NetSol PK, Connect, and NetSol Innovation use Pakistan Rupees; NTPK Thailand uses Thai Baht and Abraxas uses the Australian dollar as the functional currencies. NetSol Technologies, Inc., and subsidiary, NTNA, 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 are classified as an item of accumulated other comprehensive loss in the stockholders' equity section of the consolidated balance sheet were $7,880,946 and $8,396,086 as of December 31, 2010 and June 30, 2010 respectively. During the six months ended December 31, 2010 and 2009, comprehensive loss in the consolidated statements of operations included translation gain of $515,139 and loss of $854,005 respectively.

**NOTE 6 - OTHER CURRENT ASSETS**

Other current assets consist of the following at December 31, 2010 and June 30, 2010:

| | As of December 31 2010 | As of June 30 2010 |
|---|---|---|
| Prepaid Expenses | $ 147,310 | $ 237,702 |
| Advance Income Tax | 507,078 | 422,028 |
| Employee Advances | 47,662 | 57,113 |
| Security Deposits | 172,311 | 131,229 |
| Tender Money Receivable | 141,873 | 252,826 |
| Other Receivables | 566,838 | 535,981 |
| Other Assets | 179,026 | 184,782 |
| Total | $ 1,762,098 | $ 1,821,661 |

**NOTE 7 - PROPERTY AND EQUIPMENT**

Property and equipment, net, consist of the following at December 31, 2010 and June 30, 2010:

| | As of December 31 2010 | As of June 30 2010 |
|---|---|---|
| Office furniture and equipment | $ 1,053,258 | $ 1,041,326 |
| Computer equipment | 8,450,059 | 8,038,033 |
| Assets under capital leases | 1,959,954 | 1,838,217 |
| Building | 2,307,688 | 2,314,080 |
| Land | 560,557 | 562,109 |
| Capital work in progress | 3,561,367 | 1,925,207 |
| Autos | 834,343 | 744,586 |
| Improvements | 162,993 | 163,365 |
| Subtotal | 18,890,219 | 16,626,923 |
| Accumulated depreciation | (7,939,250) | (7,154,005) |
| | $ 10,950,969 | $ 9,472,917 |

For the six months ended December 31, 2010 and 2009, depreciation expense totaled $765,004 and $742,864 respectively. Of these amounts, $537,424 and $520,981 respectively, are reflected as part of cost of goods sold.

**NOTE 8 - INTANGIBLE ASSETS:**

Intangible assets consist of the following at December 31, 2010 and June 30, 2010:

| | Product Licenses | Customer Lists | Total |
|---|---|---|---|
| Intangible assets - June 30, 2009 – cost | $ 25,042,331 | $ 5,804,057 | $ 30,846,388 |
| Additions | 7,652,707 | - | 7,652,707 |
| Effect of translation adjustment | (2,734,235) | - | (2,734,235) |
| Accumulated amortization | (10,958,723) | (5,137,482) | (16,096,205) |
| Net balance - June 30, 2010 | $ 19,002,080 | $ 666,575 | $ 19,668,655 |
| | | | |
| Intangible assets - December 31, 2010 - cost | $ 29,960,803 | $ 5,804,057 | $ 35,764,860 |
| Additions | 3,151,774 | - | 3,151,774 |
| Effect of translation adjustment | 21,251 | - | 21,251 |
| Accumulated amortization | (11,813,014) | (5,388,412) | (17,201,426) |
| Net balance - December 31, 2010 | $ 21,320,814 | $ 415,645 | $ 21,736,459 |
| | | | |
| Weighted average amortization period | 7.80 | 5.00 | 7.39 |
| | | | |
| Amortization expense for: | | | |
| Six months ended December 31, 2010 | $ 828,578 | $ 250,930 | $ 1,079,508 |
| Six months ended December 31, 2009 | $ 876,674 | $ 382,618 | $ 1,259,292 |

**(A) Product Licenses**

Product licenses include original license issue, renewals, enhancements, copyrights, trademarks, and trade names. Product licenses included unamortized software development and enhancement costs of $14,557,253.

**(B) Customer Lists**

On October 31, 2008, the Company entered into an agreement to purchase the rights to the customer list of Ciena Solutions, LLC, a California limited liability company ("Ciena"). Under the terms of the agreement, the total consideration for these rights included an initial payment of $350,000 (plus interest of $2,963), and deferred consideration to be paid in cash and the Company's common stock based on the operational results of Ciena, and certain other factors, over a four-year fiscal period. Each fiscal period is measured from July 1 to June 30 with fiscal period one being the period from July 1, 2008 to June 30, 2009. No other assets or liabilities were acquired by the Company as a result of this transaction.

As a result of operational losses of Ciena in the first two fiscal periods, 2009 and 2010, respectively, the first two annual deferred consideration installment payments were determined to be zero.

**(C) Amortization**

Software development amortization expense was $772,784 and $550,796 for the periods ended December 31, 2010 and December 31, 2009, respectively, and is recorded in cost of revenues.

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

| | FISCAL YEAR ENDING | | | | | | |
|---|---|---|---|---|---|---|---|
| Asset | 12/31/11 | 12/31/12 | 12/31/13 | 12/31/14 | 12/31/15 | Thereafter | TOTAL |
| Product Licences | $ 1,404,700 | $ 1,053,660 | $ 904,260 | $ 667,208 | $ 667,208 | $ 16,623,777 | $ 21,320,814 |
| Customer Lists | 286,226 | 70,592 | 58,827 | - | - | - | 415,645 |
| | | | | | | | |
| | $ 1,690,926 | $ 1,124,252 | $ 963,087 | $ 667,208 | $ 667,208 | $ 16,623,777 | $ 21,736,459 |

**NOTE 9 – GOODWILL**

Goodwill represents the excess of the aggregate purchase price over the fair value of the net assets acquired in prior period businesses combinations. Goodwill is comprised of the following amounts as of December 31, 2010 and June 30, 2010:

| | As of December 31, 2010 | As of June 30, 2010 |
|---|---|---|
| Asia Pasific | $ 1,303,372 | $ 1,303,372 |
| Europe | 3,471,813 | 3,471,813 |
| North America | 4,664,100 | 4,664,100 |
| Total | $ 9,439,285 | $ 9,439,285 |

There was no impairment of the goodwill for the periods ended December 31, 2010 and June 30, 2010.

**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. The joint venture was accounted for as an equity method investment as the Company has not established control over the affairs of Atheeb NetSol Saudi Company Ltd. due to its minority representation on the board of directors.

The Company's investment in equity for the period ended December 31, 2010 is as follows:

| | |
|---|---|
| Initial investment in Atheeb at cost | $ 268,000 |
| Net loss for the period | (134,719) |
| NetSol's share (50.1%) | (67,494) |
| Net book value at June 30, 2010 | $ 200,506 |
| Net loss for the half year ended December 31, 2010 | (283,905) |
| NetSol's share (50.1%) | (142,236) |
| Net book value at December 31, 2010 | $ 58,269 |

**NOTE 11 - ACCOUNTS PAYABLE AND ACCRUED EXPENSES**

Accounts payable and accrued expenses consist of the following at December 31, 2010 and June 30, 2010:

| | As of December 31 2010 | As of June 30 2010 |
|---|---|---|
| Accounts Payable | $ 1,064,280 | $ 1,321,212 |
| Accrued Liabilities | 2,449,327 | 2,369,153 |
| Accrued Payroll | 182,576 | 158,392 |
| Accrued Payroll Taxes | 287,554 | 299,908 |
| Interest Payable | 627,419 | 602,614 |
| Deferred Revenues | 2,351 | 6,472 |
| Taxes Payable | 138,675 | 133,169 |
| Total | $ 4,752,181 | $ 4,890,921 |

**NOTE 12 - DEBTS**

**(A) LOANS AND LEASES PAYABLE**

Notes payable consist of the following at December 31, 2010 and June 30, 2010:

| Name | As of December 31 2010 | Current Maturities | Long-Term Maturities |
|---|---|---|---|
| Habib Bank Line of Credit | $ 5,363,131 | $ 5,363,131 | $ - |
| Bank Overdraft Facility | 51,243 | 51,243 | - |
| Term Finance Facility | 1,015,458 | 435,196 | 580,262 |
| Subsidiary Capital Leases | 1,143,063 | 659,842 | 483,221 |
| Lease abandonment liability | 867,583 | - | 867,583 |
| | $ 8,440,478 | $ 6,509,412 | $ 1,931,066 |

| Name | As of June 30 2010 | Current Maturities | Long-Term Maturities |
|---|---|---|---|
| D&O Insurance | $ 12,122 | $ 12,122 | $ - |
| E&O Insurance | 7,046 | 7,046 | - |
| Habib Bank Line of Credit | 5,677,533 | 5,677,533 | - |
| Bank Overdraft Facility | 202,712 | 202,712 | - |
| HSBC Loan | 43,306 | 43,306 | - |
| Term Finance Facility | 1,163,738 | 436,402 | 727,336 |
| Subsidiary Capital Leases | 1,111,271 | 906,651 | 204,620 |
| | 867,583 | - | 867,583 |
| | $ 9,085,311 | $ 7,285,773 | $ 1,799,538 |

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 0.49% as of December 31, 2010 and June 30, 2010. Interest paid during the quarter-ended December 31, 2010 and 2009 was nominal.

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 2% and 3.23% as of December 31, 2010 and June 30, 2010, respectively. Interest paid during the six months ended December 31, 2010 and 2009 was $64,718 and $92,733, respectively.

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 £200,000. The annual interest rate is 3.25% over the bank's sterling base rate, which was 5.00% as of December 31, 2010 and June 30, 2010, respectively.

In August 2007, the Company's subsidiary, NetSol UK, entered into an agreement with HSBC Bank whereby the line of credit outstanding of £500,000 or approximately $773,550 was converted into a loan payable with a maturity of three years. The interest rate is 7.5% with monthly payments of £14,436 or approximately $22,334. The Parent has guaranteed payment of the loan in the event the subsidiary should default. Interest paid during the quarter ended December 31, 2010 and 2009 was $216 and $10,592, respectively. As of December 31, 2010, this loan was paid off in full.

The Company's subsidiary, NetSol PK, entered into a term finance facility from Askari Bank to finance the construction of a new building. The total amount of the facility is Rs. 100,000,000 or approximately $1,163,738 (secured by the first of Rs. 580 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 on June 30, 2010, the subsidiary had used Rs. 100,000,000 or approximately $1,163,738 of which $727,336 was shown as long term liabilities and the remainder of $436,402 as current maturity. As of the six months ended December 31, 2010, the Company paid back the first installment of Rs. 12,500,000 reducing the outstanding principal amount to Rs. 87,500,000 or approximately $1,015,458 of which $580,262 is shown as long term liabilities and the remainder of $435,196 as current maturity.

The Company leases various fixed assets under capital lease arrangements expiring in various years through 2014. 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 six months ended December 31, 2010 and 2009.

Following is the aggregate minimum future lease payments under capital leases as of December 31, 2010 and June 30, 2010:

| | As of December 31 2010 | As of June 30 2010 |
|---|---|---|
| Minimum Lease Payments | | |
| Due FYE 12/31/11 | $ 693,496 | $ 941,406 |
| Due FYE 12/31/12 | 235,423 | 189,155 |
| Due FYE 12/31/13 | 165,361 | 27,481 |
| Due FYE 12/31/14 | 100,990 | - |
| Total Minimum Lease Payments | 1,195,270 | 1,158,042 |
| Interest Expense relating to future periods | (52,208) | (46,771) |
| Present Value of minimum lease payments | 1,143,063 | 1,111,271 |
| Less: Current portion | (659,842) | (906,651) |
| Non-Current portion | $ 483,221 | $ 204,620 |

Following is a summary of fixed assets held under capital leases as of December 31, 2010 and June 30, 2010:

| | As of December 31 2010 | As of June 30 2010 |
|---|---|---|
| Computer Equipment and Software | $ 584,255 | $ 473,033 |
| Furniture and Fixtures | 830,575 | 830,942 |
| Vehicles | 242,909 | 232,026 |
| Building Equipment | 302,216 | 302,216 |
| Total | 1,959,954 | 1,838,217 |
| Less: Accumulated Depreciation | (788,900) | (621,567) |
| Net | $ 1,171,054 | $ 1,216,650 |

In 2008, the Company's subsidiary, NTNA, had acquired an office space in Emeryville on a long term lease. However, due to the unprecedented recession experienced in 2009, the company decided to vacate the office space and terminate the lease in October 2009. The Company recorded a lease abandonment charge of $1,076,347 in the quarter-ended December 31, 2009. However, the office space was leased by another company during the quarter-ended March 31, 2010 and the lease abandonment charge was reduced by $208,764 to $867,583 as of December 31, 2010 and June 30, 2010. The liability as of December 31, 2010 and June 30, 2010 was determined using fair value level 2 methodology and assumptions.

**(B) LOANS PAYABLE- BANK**

The Company's subsidiary, NetSol PK, has a loan with a bank, secured by the company's assets. This loan consists of the following as of December 31, 2010 and June 30, 2010:

For the period ended December 31, 2010:

| TYPE OF LOAN | MATURITY DATE | INTEREST RATE | BALANCE USD |
|---|---|---|---|
| Export Refinance | Every 6 months | 10.00% | $ 2,321,047 |
| Total | | | $ 2,321,047 |

For the year ended June 30, 2010:

| TYPE OF LOAN | MATURITY DATE | INTEREST RATE | BALANCE USD |
|---|---|---|---|
| Export Refinance | Every 6 months | 9.00% | $ 2,327,476 |
| Total | | | $ 2,327,476 |

**(C) OTHER PAYABLE – ACQUISITION**

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 1,712,332 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 period-ended December 31, 2010 and June 30, 2010, the remaining cash due of $103,226 is shown as "Other Payable – Acquisition" and the remaining stock to be issued of 46,704 shares at an average price of $1.89 is shown in "Shares to be issued" in the accompanying consolidated financial statements. Amounts payable represent the remaining McCue shareholders that have not been located as of the date of this report.

**(D) DUE TO OFFICERS**

The officers of the Company, from time to time, loan funds to the Company. The balance due to officers as of December 31, 2010 and June 30, 2010 was Nil and $10,911 respectively.

**NOTE 13 – CONVERTIBLE NOTES PAYABLE**

The net outstanding balance of convertible notes as of December 31, 2010 and June 30, 2010 is as follows:

| Issue Date | Balance net of BCF @ 12/31/10 | Current Portion | Long Term | Maturity Date |
|---|---|---|---|---|
| Jul-08 | 2,587,109 | 2,587,109 | - | Jul-11 |
| Mar-10 | 1,500,000 | 1,500,000 | - | Mar-11 |
| Total | 4,087,109 | 4,087,109 | - | |

| Issue Date | Balance net of BCF @ 6/30/10 | Current Portion | Long Term | Maturity Date |
|---|---|---|---|---|
| Jul-08 | 4,066,108 | | 4,066,108 | Jul-11 |
| Aug-09 | 1,517,096 | 1,517,096 | | Aug-10 |
| Mar-10 | 1,500,000 | 1,500,000 | | Mar-11 |
| Total | 7,083,204 | 3,017,096 | 4,066,108 | |

For the periods ended December 31, 2010 and 2009, the interest expense on convertible notes was $355,828 and $413,083, respectively.

**(A) 2008 CONVERTIBLE DEBT**

In July 2008, the Company issued $6,000,000 of 7% convertible debt maturing in 3 years (the "2008 Notes"), with a conversion price of $3.00 per share.

In January 2009, the 2008 Notes were amended to remove certain anti-dilution protection provisions and participation rights in future filings in exchange for a reduction in the conversion rate to $0.78, and $1,000,000 in cash, payable to the debt holders in 4 quarterly installments. Pursuant to the terms of the amendment, the Company recorded a beneficial conversion feature ("BCF") in the amount of $230,769 which is being amortized as a component of interest expense over the maturity period. The related liability of $1,000,000 was recorded as a component of interest expense for the year-ended June 30, 2009.

In August 2009, the Company amended the 2008 Notes by reducing the conversion rate to $0.63, and recorded an additional BCF of $715,518, which is being amortized as a component of interest expense over the maturity period.

During the year-ended June 30, 2010, Holders of the 2008 Notes elected to convert principal and interest due thereon into a total of 2,513,112 shares of common stock. These conversions reduced the total principal of the 2008 Notes to $4,450,000.

During the six months ended December 31, 2010, Holders of the 2008 Note further elected to convert the principal and interest due thereon into a total of 2,744,042 shares of common stock. These conversions reduced the principal of the 2008 Note to $2,758,330.

**(B) 2009 CONVERTIBLE DEBT**

In August 2009, the Company issued $2,000,000 of 9% convertible debt maturing in 1 year (the "2009 Notes") with a conversion price of $0.63 per share, in exchange for the redemption of preferred shares outstanding. The associated BCF of $1,428,571 is being amortized as a component of interest expense through maturity.

During the year-ended June 30, 2010, Holders of the 2009 Notes elected to convert principal and interest due thereon into a total of 645,556 shares of common stock. This conversion reduced the total principal of the 2009 Notes to $1,600,000.

During the quarter ended September 30, 2010, Holders of the 2009 Note further elected to convert the remaining principal and interest due thereon into a total of 2,613,333 shares of common stock. These conversions reduced the principal of the 2009 Note to nil.

**(C) 2010 CONVERTIBLE DEBT**

In March 2010, the Company issued $1,500,000 of 8% convertible debt maturing in 1 year (the "2010 Notes"), with a conversion price of $1.15 per share. The maturity date of these notes may be extended an additional year upon agreement of both parties. In August, 2010, the note conversion prices were adjusted to $.0.85 per share.

## NOTE 14 - STOCKHOLDERS' EQUITY:

### (A) TREASURY STOCK

On March 24, 2008, the Company announced that it had authorized a stock repurchase program permitting the Company to repurchase up to 1,000,000 of its shares of common stock over the next 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. During the year ended June 30, 2008, the Company had repurchased a total of 13,600 shares on the open market valued at $25,486. The balance as of June 30, 2008 was $35,681. In September 2008, the stock repurchase plan was extended an additional 6 months. During the year ended June 30, 2009, the Company purchased an additional 208,900 shares on the open market valued at $360,328. The balance as of December 31, 2010 and June 30, 2010 was $396,008. The stock repurchase plan expired on March 24, 2009.

On July 27, 2010, the Company announced that it had authorized a stock repurchase program permitting the Company to repurchase up to 2,000,000 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 did not repurchase any shares of common stock during the six months ended December 31, 2010. The stock repurchase plan expired on January 27, 2011.

### (B) SHARES ISSUED FOR SERVICES TO RELATED PARTIES

During the six months period ended December 31, 2010, and year ended June 30, 2010, the Company issued a total of 420,000 and 187,500 shares of restricted common stock for services rendered by the officers of the company. The issuances were approved by both the compensation committee and the board of directors. These shares were valued at the fair market value of $476,700 and 163,125, as of December 31, 2010 and June 30, 2010, respectively.

During the six months period ended December 31, 2010, and year ended June 30, 2010, the Company issued a total of 60,000 and 90,000 shares of restricted common stock for services rendered by the independent members of the Board of Directors as part of their board compensation. The issuances were approved by both the compensation committee and the board of directors. These shares were valued at the fair market value of $66,600 and $78,900, as of December 31, 2010 and June 30, 2010, respectively.

During the six months period ended December 31, 2010 and year ended June 30, 2010, the Company issued a total of 32,699 and 139,881 shares of its common stock to employees as required according to the terms of their employment agreements valued at $33,300 and $130,500, respectively.

### (C) SHARE-BASED PAYMENT TRANSACTIONS

During the period ended December 31, 2010, and year ended June 30, 2010, the Company issued a total of 337,857 and 501,931 shares of its common stock for provision of services to unrelated consultants valued at $152,543 and $275,019, respectively.

**NOTE 15 - INCENTIVE AND NON-STATUTORY STOCK OPTION PLAN**

Common stock purchase options and warrants consisted of the following as of December 31, 2010:

| **OPTIONS:** | # shares | Exercise Price | Aggregated Intrinsic Value |
|---|---|---|---|
| Outstanding and exercisable, June 30, 2009 | 7,706,917 | $0.30 to $5.00 | $ - |
| Granted | 300,000 | $ 0.75 | |
| Exercised | (300,000) | $ 0.75 | |
| Expired | - | | |
| Outstanding and exercisable, June 30, 2010 | 7,706,917 | $0.30 to $5.00 | $ 146,047 |
| Granted | 1,021,000 | $0.65 to $1.25 | |
| Exercised | (636,000) | $0.65 to $1.25 | |
| Expired | - | | |
| Outstanding and exercisable, December 31, 2010 | 8,091,917 | $0.30 to $5.00 | $ 2,427,620 |
| **WARRANTS:** | | | |
| Outstanding and exercisable, June 30, 2009 | 1,777,617 | $1.65 to $3.70 | $ - |
| Granted | 3,274,682 | $ 0.31 | |
| Exercised | - | | |
| Expired | (288,980) | 3.3 | |
| Outstanding and exercisable, June 30, 2010 | 4,763,319 | $0.31 to $3.70 | $ 1,698,387 |
| Granted | | | |
| Exercised | (2,253,226) | $ 0.31 | |
| Expired | | | |
| Outstanding and exercisable, December 31, 2010 | 2,510,093 | $0.31 to $3.70 | $ 2,775,290 |

The average life remaining on the options and warrants as of December 31, 2010 is as follows:

| Exercise Price | Number Outstanding and Exercisable | Weighted Average Remaining Contractual Life | Weighted Ave Exericse Price |
|---|---|---|---|
| ***OPTIONS:*** | | | |
| $0.01 - $0.99 | 2,191,000 | 6.67 | 0.65 |
| $1.00 - $1.99 | 2,045,917 | 4.59 | 1.88 |
| $2.00 - $2.99 | 3,055,000 | 4.30 | 2.69 |
| $3.00 - $5.00 | 800,000 | 3.32 | 4.24 |
| Totals | 8,091,917 | 4.91 | 2.08 |
| ***WARRANTS:*** | | | |
| $0.31 - $1.99 | 2,497,593 | 3.53 | 0.71 |
| $3.00 - $5.00 | 12,500 | 0.77 | 3.70 |
| Totals | 2,510,093 | 3.51 | 0.72 |

All options and warrants granted are vested and are exercisable as of December 31, 2010, except 375,000 options which will vest in the next two quarters.

**(A) INCENTIVE AND NON-STATUTORY STOCK OPTION PLAN**

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 December 31, 2009, the Company granted 250,000 options to two employees with an exercise price of $0.75 per share and an expiration date of 1 year, vesting immediately. Using the Black-Scholes method to value the options, the Company recorded $71,238 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 | 1.56% |
| Expected life | 1 year |
| Expected volatility | 56% |

During the quarter ended June 30, 2010, the Company granted 50,000 options to two employees with an exercise price of $0.75 per share and an expiration date of 1 month, vesting immediately. Using the Black-Scholes method to value the options, the Company recorded $3,652 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 | 1.08% |
| Expected life | 1 month |
| Expected volatility | 39% |

During the quarter ended September 30, 2010, the Company granted 750,000 options to five employees with an exercise price of $0.65 per share and an expiration date of 1 Year, vesting quarterly. Using the Black-Scholes method to value the options, the Company recorded $52,210 per quarter 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 | 2.01% |
| Expected life | 1 year |
| Expected volatility | 90% |

During the quarter ended September 30, 2010, the Company granted 10,000 options to one employee with an exercise price of $0.65 per share and an expiration date of 1 Year, vesting immediately. Using the Black-Scholes method to value the options, the Company recorded $2,785 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 | 2.01% |
| Expected life | 1 year |
| Expected volatility | 90% |

During the quarter ended September 30, 2010, the Company granted 242,000 options to seven employees with an exercise price of $0.65 per share and an expiration date of 4 months, vesting immediately. Using the Black-Scholes method to value the options, the Company recorded $43,441 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 | 1.81% |
| Expected life | 4 months |
| Expected volatility | 90% |

During the quarter ended December 31, 2010, the Company granted 15,000 options to one employee with an exercise price of $0.65 per share and an expiration date of 1 month, vesting immediately. Using the Black-Scholes method to value the options, the Company recorded $11,717 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 | 1.65% |
| Expected life | 1 month |
| Expected volatility | 99% |

During the quarter ended December 31, 2010, the Company granted 4,000 options to one employee with an exercise price of $1.25 per share and an expiration date of 1 month, vesting immediately. Using the Black-Scholes method to value the options, the Company recorded $1,040 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 | 1.65% |
| Expected life | 1 month |
| Expected volatility | 99% |

**WARRANTS**

During the year ended June 30, 2010, the Company amended the terms of warrant agreements associated with common stock issued in October, 2007. Pursuant to the terms of the amendment, the exercise price was reduced to $0.31 from $0.63, resulting in a corresponding increase in the number of shares of common stock underlying the warrants by 3,274,682. The above holders exercised 1,000,000 warrants and 1,253,226 warrants through a cashless exercise, resulting in 998,401 shares issued.

**(B) EQUITY INCENTIVE PLAN**

In May 2008, the shareholders approved the 2008 Equity Incentive Plan (the "2008 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 2008 Plan is 1,000,000 (the Share Reserve). The 2008 Plan contemplates the issuance of common stock upon exercise of options or other awards granted to eligible persons under the 2008 Plan. Shares issued under the 2008 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 2008 Plan, in whole or in part, the number of shares of common stock subject to such award again become available for grant under the 2008 Plan. Any shares of restricted stock forfeited as described below will become available for grant. The maximum number of shares that may be granted to any one participant in any calendar year may not exceed 500,000 shares. All options issued pursuant to the Plan are nontransferable and subject to forfeiture.

**STOCK OPTIONS**

Options granted under the 2008 Plan are not generally transferable and 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. The maximum term of any option granted under the 2008 Plan is ten years, provided that an incentive stock option granted to a Ten Percent Shareholder must have a term not exceeding five years.

**PERFORMANCE AWARDS**

Under the 2008 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 our 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 our 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 2008 Plan, which are 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 December 31, 2010, 864,500 shares have been issued under this plan.

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

## 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 intracompany 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 six months ended December 31:

| | 2010 | 2009 |
|---|---|---|
| Revenues from unaffiliated customers: | | |
| North America | $ 2,231,691 | $ 3,192,642 |
| Europe | 4,576,771 | 3,371,716 |
| Asia - Pacific | 12,019,857 | 10,577,523 |
| Consolidated | $ 18,828,319 | $ 17,141,881 |
| | | |
| Operating income (loss): | | |
| Corporate headquarters | $ (1,902,704) | $ (2,395,926) |
| North America | 324,948 | (538,810) |
| Europe | 2,394,818 | 1,047,738 |
| Asia - Pacific | 5,104,842 | 4,723,675 |
| Consolidated | $ 5,921,904 | $ 2,836,677 |
| | | |
| Net income (loss) after taxes and before minority interest: | | |
| Corporate headquarters | $ (2,699,654) | $ (3,816,443) |
| North America | 310,018 | (584,832) |
| Europe | 2,332,303 | 1,001,041 |
| Asia - Pacific | 5,617,352 | 4,826,330 |
| Consolidated | $ 5,560,018 | $ 1,426,096 |
| | | |
| Identifiable assets: | | |
| Corporate headquarters | $ 16,839,002 | $ 17,135,602 |
| North America | 2,620,231 | 2,887,026 |
| Europe | 6,003,011 | 4,194,899 |
| Asia - Pacific | 56,101,924 | 42,001,111 |
| Consolidated | $ 81,564,168 | $ 66,218,638 |
| | | |
| Depreciation and amortization: | | |
| Corporate headquarters | $ 307,171 | $ 709,833 |
| North America | 264,698 | 270,742 |
| Europe | 356,337 | 301,025 |
| Asia - Pacific | 916,323 | 720,556 |
| Consolidated | $ 1,844,528 | $ 2,002,156 |
| | | |
| Capital expenditures: | | |
| Corporate headquarters | $ - | $ - |
| North America | 40,310 | 10,712 |
| Europe | 905 | 16,892 |
| Asia - Pacific | 2,409,007 | 1,058,183 |
| Consolidated | $ 2,450,222 | $ 1,085,787 |

Net revenues by our various products and services provided for the period ended December 31, are as follows:

| | 2010 | 2009 |
|---|---|---|
| Licensing Fees | $ 6,606,856 | $ 5,870,529 |
| Maintenance Fees | 3,693,428 | 3,588,053 |
| Services | 8,528,035 | 7,683,299 |
| Total | $ 18,828,319 | $ 17,141,881 |

**NOTE 17 – NON-CONTROLLING INTEREST IN SUBSIDIARY**

The Company had non-controlling interests in several of its subsidiaries. The balance of non-controlling interest as of December 31, 2010 and June 30, 2010 was as follows:

| SUBSIDIARY | Non Controlling Interest % | Non-Controlling Interest at December 31, 2010 |
|---|---|---|
| NetSol PK | 42.04% | $ 10,422,545 |
| NetSol-Innovation | 49.90% | 970,691 |
| Total | | $ 11,393,236 |

| SUBSIDIARY | Non Controlling Interest % | Non-Controlling Interest at June 30, 2010 |
|---|---|---|
| NetSol PK | 42.04% | $ 9,133,392 |
| NetSol-Innovation | 49.90% | 1,291,057 |
| Connect | 49.90% | (1,891) |
| Total | | $ 10,422,557 |

**(A) NETSOL TECHNOLOGIES, LIMITED ("NETSOL PK")**

For the six months ended December 31, 2010 and 2009, NetSol Technologies Ltd. ("NetSol PK") had net income of $4,356,397 and $4,734,953. The related non-controlling interest was $1,831,429 and $1,990,574, respectively.

In April 2009, NetSol PK issued 6,223,209 shares of common stock to the Company in fulfillment of an outstanding loan balance of $1,879,672 provided by the Company.

During the fiscal year-ended June 2009, the Company disposed of 3,132,255 shares of NetSol PK in the open market with a value of $558,536. A net gain of $351,522 was recorded as "Other Income" in the consolidated financial statements. As a result of the sale, the corresponding non-controlling interest increased from 41.32% to 42.04%.

During the six months ended December 31, 2010, NetSol PK declared and paid a cash dividend of $1,125,733, of which the Company's interest was $653,905. The amount attributable to the minority holders was $471,828.

**(B) NETSOL INNOVATION (PRIVATE) LIMITED ("NETSOL INNOVATION")**

For the six months ended December 31, 2010 and 2009, NetSol Innovation (Private) Limited ("NetSol Innovation") had net income of $452,648 and $318,759. The related non-controlling interest was $225,871 and $159,061, respectively.

**(C) NETSOL CONNECT ("CONNECT")**

As on July 01, 2010, the Company acquired the non-controlling interest in NetSol Connect against a payment of $180,000.The balance of non-controlling interest as on June 30, 2010 (the acquisition date) was ($1,891). Per Para 33 of SFAS 160 company adjusted the additional paid in capital by $181,891.

**NOTE 18 - SUBSEQUENT EVENTS**

Holders of warrants with an exercise price of $.31 per share exercised warrants for a total of 930,443 shares of common stock.

Accredited investors who participated in an offering of shares of common stock which commenced in August 2010 were issued 270,000 shares of common stock as part of the final issuances due in this raise. Consideration and stock purchase agreements were received during the previous quarter but the shares of common stock were not issued until after the close of the quarter. The per share price of this offering was $.65 based on the offering commencement date of August 9, 2010.

Employees of the company exercised options to acquire 197,500 shares of common stock valued at $128,375.

**Item 2. Management's Discussion and Analysis Or 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 December 31, 2010.

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.

**INTRODUCTION**

NetSol Technologies, Inc. (“NetSol” or the “Company”) (NasdaqCM: NTWK) (NasdaqDubai: NTWK) is a worldwide provider of IT solutions to the global financing and leasing industry, with world class enterprise software and services. As a CMMI level 5 company, a distinction shared by few companies worldwide, NetSol uses its BestShoring® practices and highly-experienced resources in analysis, development, quality assurance, and implementation to deliver high-quality, cost-effective solutions. The Company is organized into two main revenue areas, consisting of its enterprise solutions (NetSol Financial Solutions “NFS™”) for the global financing and leasing industry and its portfolio of IT based global business services (“GBS”). NetSol’s GBS offerings include portfolio management systems for the financial services industry and, consulting, custom development, systems integration, and technical services for the global healthcare, insurance, real estate and technology markets. NetSol's commitment to quality is demonstrated by its achievement of the ISO 9001, ISO 279001, and SEI (Software Engineering Institute, Carnegie Mellon University, USA) CMMI (Capability Maturity Model) Level 5 assessments, a distinction shared by fewer than 100 companies worldwide. NetSol’s clients include Fortune 500 manufacturers, global automakers, financial institutions, technology providers, and governmental agencies.

Founded in 1996, NetSol is headquartered in Calabasas, California. NetSol also has operations and/or offices in: Horsham, United Kingdom; Alameda, California, USA; Beijing, China; Lahore, Islamabad and Karachi, Pakistan; Adelaide, Australia; Bangkok, Thailand; and, Riyadh, Kingdom of Saudi Arabia.

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, not only with lowest cost blended rates from its design centers and campuses located around the world, but also with the guarantee of localized program 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 focus on “Solutions” serves to ensure the most favorable pricing while delivering in-depth domain experience. NetSol currently has locations in Bangkok, Beijing, Lahore, London, the San Francisco Bay Area, and Adelaide to best serve its clients and partners worldwide. This provides 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; NetSol Defense Division; 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. NFS™ is a result of more than eight years of effort resulting in over 60 modules grouped in five comprehensive applications. These five applications are complete systems in themselves and can be used independently to exhaustively address specific sub-domains of the leasing/financing cycle. When used together, they fully automate the entire leasing / financing cycle.

The NetSol Financial Suite™ 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 product 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.

Our product offerings and services also include: LeaseSoft Portals and Modules through our European operations; LeasePak 6.0b of our NFS™ product suite; enterprise wide information systems, such as or LRMIS, MTMIS and Hospital Management Systems; Accounting Outsourcing Services, and, NetSol Technology Institute, our specialized career and technology program in Pakistan.

To further bolster NetSol's Solutions capabilities, in October 2008, NetSol acquired Ciena Solutions, a preferred SAP and Business Objects integration firm. The Ciena Solutions practice is now integrated into our wholly owned subsidiary, NetSol Technologies North America, Inc. This acquisition expanded NetSol's domain and subject matter expertise to include integration and consulting services for:

- SAP R/3 System deployments
- NetWeaver
- Exchange Infrastructure Portals
- MySAP Business Suite
- Supplier Relationship Management Module
- Client Relationship Management Module
- SAP/Business Objects Products and related Services

In addition to this expansion of SAP-centric integration consulting and services, this practice has developed proprietary intellectual property in the form of designs and source code focused on enhancing SAP-centric procurement activities.

The introduction of a major new product, smartOCI™, has emerged from this integration. smartOCI™ is a new search engine technology developed by NetSol which provides corporate buyers and shoppers a simple and intuitive user interface to search multiple supplier catalogs simultaneously within the SAP SRM application. The launch of smartOCI™ at the SAP SAPPHIRE Conference in Orlando, Florida, targeting approximately 1,000 SAP SRM platform customers has the strengthened NetSol's presence in the global SAP Services market.

The Company continues its efforts to reduce redundancy and cohesively present services and product operations on a global basis. This consolidation enables the Company to coordinate and streamline product, service and marketing while taking further advantage of the cost arbitrage offered by our highly trained, highly productive, Pakistani resources. This consolidation follows the successful integration of the operations acquired in the United Kingdom and the San Francisco Bay Area in California and facilitates the use of these regional offices as platforms for presenting an expanding services offering, relying on the experience and resources in Pakistan and our product offerings in North America and Europe.

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, California for North America and the parent headquarters in Calabasas, California; Horsham, United Kingdom, for Europe; and, our "center of excellence" operation in Lahore, Pakistan for Asia Pacific. The Company continues to maintain services or products and specific sales offices in Australia, China, Thailand, Kingdom of Saudi Arabia and Pakistan and in any other country on an as needed basis.

*Marketing and Business Development Activities:*

Management undertook major steps to sustain growth in the global markets:

- The Company strategically positioned the global delivery model by leveraging the 'Center of Excellence' technology campus in Lahore. This facility is fully integrated with three proximity development centers or PDC in San Francisco, London and Beijing to effectively support and service our clients in global markets. By implementing this model, the Company has mitigated the risk of dependence on any one particular location. The global delivery model has further streamlined the cost base as well as optimized utilization of the NetSol Center of Excellence, CMMI Level 5, technology campus, translating into better and more competitive pricing modules for our customers.

- The remarkable success and demand of NFS™ in China has led to long term planning to expand in the Chinese market. The overall steady economic growth in China and historic transformation of the auto sector (China outsold cars against the United States in number of units in 2009) combined with growing consumer spending, warrants the hire of additional local Chinese staff and infrastructure improvement. Management is poised to create a 'proximity development center' or PDC and clients support team to better serve our growing customers base.

- Consistent with our rapid expansion strategy and plans in China, we have started the process of forming a wholly foreign owned enterprise in Beijing, China. The NetSol subsidiary in China will be wholly owned by NetSol Technologies, Inc. In addition, we are moving into a larger office in Beijing effective March 1, 2011.

- In addition to further penetrating auto captive market in China, NetSol has entered a new segment of big ticket leasing with the successful implementation of NFS™ at Minsheng Financial leasing. Minsheng is the 4th largest big ticket leasing company in China. The three major sectors of focus in China will be banking, auto finance and equipment finance.

- Thailand is a new emerging market for banking and auto finance. NetSol has a modest presence in Bangkok and is operating under NetSol Thai, a recently formalized wholly owned subsidiary of NTI. The management has started to grow the region by adding a few Thai nationals as staff members and experienced business executives from within NetSol. The pipeline of new customers is growing from the markets in Japan, South Korea and India. These markets will be serviced and supported from the Thailand office. We are accommodating the foreseeable growth in the banking and lending software market by moving adding additional local staff and moving to a larger office space.

- NetSol North American operation has taken critical steps to further enhance the service levels of the local technical team with effective integration of the NetSol PK center of excellence. This strategy has impressively added accretive revenue and interest from current major customers. While the overall market is still going through consolidation and correction, the NetSol team in the US is successfully executing on efforts to grow from its existing client base.

- NetSol in North America has effectively established a relationship with senior management in SAP to build smartOCI™, a new search engine procurement technology for major corporations. In addition, NetSol is pursuing major alliances to grow the NFS™ business through this relationship in various global markets.

- Marketing and branding efforts will be resumed to generate new leads and demand of NetSol offerings in both matured and emerging markets. During the recession in 2008-2009, most of these activities were abandoned. We believe the time is ripe for aggressive marketing efforts towards exposure in major forums and enhanced lead generation.

- We anticipate hiring new sales executives and business developers in both the North America and Asia Pacific markets to take full advantage of new opportunities that our footprint has created.

NetSol marketing activities will continue to:

- Encourage organic revenue growth in the Chinese market in the automobile, banking, manufacturing and captive leasing sectors.
- Expand the Beijing office with new local Chinese staff and senior business development and project management teams.
- Further penetrate the Asia Pacific markets by selling NetSol offerings in the key and robust markets of Australia, New Zealand, Singapore, Thailand, South Korea, and Japan.
- Expand Thailand operations with the aim of making it a second hub, after China. A few senior business development teams have been mobilized and relocated in Thailand to support the new business development efforts in the APAC region.
- While consolidating the development and sales teams, further build and expand in the North America market. As the most mature and largest market for the Company's solutions, North America will remain key to new revenue in the coming years. NetSol's existing product line including LeasePak and its modules will remain as a primary offering to support our existing customers.
- NetSol SAP practice will enhance the revenue and add new customers for SAP consulting service, staffing & proprietary bolt-on software offerings.
- Expand and support the new and innovative road map of more capable and robust solutions to the existing 30 plus US customers.
- Increase marketing activities by participating in major forums such as ELFA (the Equipment Leasing & Finance Association) in North America and many other selected international forums to grow NetSol business and image.
- Test market NFS™ new generation products with key global customers.
- Expand and win new customers in the Middle Eastern markets through a recently formed joint venture with Atheeb Group in the Kingdom of Saudi Arabia (KSA). This will include sectors in leasing, banking, defense and public areas.

*Funding and Investor Relations:*

Management anticipates, but there is no guaranty, that as the price of the Company's shares of common stock will rise, as quoted on the NASDAQ Capital Market. Management believes that a rising price will make available prudent ways of injecting new capital to grow the business to be used in support of important activities such as:

- Expansion in China, Thailand and other emerging markets including Latin America.

- Support of bigger IT related public and defense sectors projects in the Kingdom of Saudi Arabia with our joint venture partner.

- Capital Expenditures for our next generation products, technology and infrastructure.

Capital may be injected through: continued officer exercises of options that are in the money; new debt and stock offerings with "friends and family" investors who typically hold for long term investment and can be raised without the necessity of placement agent fees; such other capital raising methods that are both reasonable in terms and beneficial to the Company.

Investor Relations efforts will include:

- With the help of our IR and PR firm we will aggressively present the Company to grow our institutional investor base.
- Sharing the NetSol story with sell side analysts, funds, portfolio managers and the financial media.
- Aggressively positioning NetSol in front of major investors' conferences and road shows to be organized by RedChip and other major institutions.
- Utilizing US mainstream media to highlight NetSol's image and 'niche' business offering.
- Founding management's anticipated continued investment in the Company displaying management's belief in NetSol's potential to new investors.
- Dedicating and focusing efforts to improve shareholder value.

**Improving the Bottom Line:**

Management believes that these measures will improve the bottom line on an ongoing basis:

- Improve pricing, sales volume and fee structures.
- Continue consolidation and reevaluating operating margins as ongoing activities.
- Streamline further cost of goods sold to improve gross margins to historical levels over 70%, as sales ramp up.
- Generate higher revenues per employee, enhance productivity and lower cost per employee.
- Optimize the utilization of NetSol PK resources, infrastructure, processes and disciplines to maximize the bottom-line and fully leverage the cost arbitrage.
- Grow process automation and leverage the best practices of CMMI level 5. Global delivery concept and integration will further improve both gross and net margins.
- Cost efficient management of every operation and continue further consolidation to improve bottom line.
- Implement SAAS model in mature markets to improve visibility and cash flow.
- Retire Debt to reduce the interest cost significantly and to make every effort to avoid any one time charges.

Management continues to be focused on building 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.

In a quest to continuously improve its quality standards, 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. 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. The quest for quality standards is imperative to NetSol's overall sustainability and success. In 2008, NetSol became ISO 27001 certified, a global standard and a set of best practices for Information Security Management.

**MATERIAL TRENDS AFFECTING NETSOL**

Management has identified the following material trends affecting NetSol.

Positive trends:

- The global recession and consolidations have opened doors for low cost solution providers such as NetSol. The BestShoring® model of NetSol is a catalyst in today's environment.

- The global economic pressures and recession has shifted IT processes and technology to utilize both offshore and onshore solutions providers, to control the costs and improve ROIs.

- The new generation of NFS "R2" demonstrations and workshops with key global clients and partners is being very well received. Hence, the outlook for the new generation solution appears to show much promise.

- GMAC – China, the implementation of first R2 for Wholesale Finance (WFS) is on track setting a strong foundation for growth. Two other key modules (CMS / CAP) are in the development stage and are expected to be marketed in fiscal 2012.

- China has become the second largest economy and has grown to over 9% GDP a year while other industrial nations have declined or grown marginally.

- China's automobile and banking sectors have been unaffected by the global meltdown and in fact have outgrown all other economies with their recent automobile sales statistics.

- As reported by the Associated Press, China surpassed the US as the number one automobile market in auto sales. JD Powers & Associates anticipated further strong growth in auto sales for the upcoming years. It is anticipated that this market opportunity will result in further penetration by NetSol into China's burgeoning leasing and finance market.

- The surviving IT companies, such as NetSol, with price advantage and a global presence, will gain further momentum as economic indicators turn positive. The bigger customers and targeted verticals are much more cost conscious and are seeking a better rate of return on investments in IT services. NetSol has an edge due to its BestShoring® model and proven track record of delivery and implementations worldwide.

- The Kingdom of Saudi Arabia is investing billions in healthcare, education, IT, infrastructure and many other new sectors. This makes it a most promising market for the Atheeb NetSol joint venture.

- Noticeable new interest emanating from the Latin America markets for NFS™.

- NetSol has never lost a product customer despite the recent severe recession. The dependency of our blue chip clients on NetSol solutions has further elevated new enhancements and services orders in the US.

- Improved outlook and earnings of bell weather technology companies in USA, reflecting the turnaround of this sector after recession.

- The aid and support of trade in Pakistan from countries like the US, China, Saudi Arabia and other western and friendly countries seems to be growing recently. This will positively affect NetSol, local employees and customers worldwide. Pakistan has every potential to rise up as the plans for energy, power, agriculture and infrastructures (including 12 new dams to be built by Chinese companies) create a much better outlook and growth for Pakistan.

- US AID and many other western agencies are diligently assisting the Pakistani people to improve literacy, education, poverty alleviation and healthcare programs. These initiatives will necessarily result in more graduates in science and technology areas.

- Global opportunities to diversify delivery capabilities in new emerging economies that offer geopolitical stability and low cost IT resources reducing dependency upon Lahore technology campus.

- Our global multi-national clients have continued to pursue deeper relationships in newer regions and countries. This reflects our customers' dependencies and satisfaction with our NetSol Financial Suite of products.

- The levy of Indian IT sector excise tax of 35% (NASSCOM) on software exports is very positive for NetSol. In Pakistan there is a 15 year tax holiday on IT exports of services. There are 7 more years remaining on this tax incentive.

Negative trends:

- Geopolitical unrest due to extremism in the regions of Pakistan and Afghanistan.
- Recent political developments in the Arab world might delay activities and plans.
- The flooding disaster in Pakistan, due to heavy monsoon rainfall, has affected more than 20 million people. The rebuilding of the affected areas will distract the government of Pakistan and major resources will be diverted to deal with the aftermath of this disaster. Accordingly, management expects delays in major public and defense projects.
- The emergence of many smaller players offering IT solutions in China has resulted in competition in pricing.
- The sluggish European market, due to debt crisis, could lead to our European business suffering.
- Dramatic and deep global recession has created a serious decline in business spending causing significant budget cuts for many of the Company's target verticals.
- Tightened liquidity and credit restrictions in consumer spending has either delayed or reduced spending on business solutions and systems squeezing IT budgets and elongating decision making cycles.

- Tighter internal processes and budgets will cause delays in the receivables from few clients.
- Anticipated worsening US deficit and rise in inflation in coming years would further put stress on consumers and business spending.
- Unrest and growing war in Afghanistan could increase the migration of both refugees and extremists to Pakistan, thus creating domestic and regional challenges.

## 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 RECOGNTION

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 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 over three years.

**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.

**CASH RESOURCES**

The company had $5.856 million worldwide in cash as on December 31, 2010.

**CHANGES IN FINANCIAL CONDITION**

**Quarter Ended December 31, 2010 as compared to the Quarter Ended December 31, 2009**:

Net revenues for the quarter ended December 31, 2010 and 2009 are broken out among the subsidiaries as follows:

| | 2010 | | 2009 | |
|---|---|---|---|---|
| | Revenue | % | Revenue | % |
| Corporate headquarters | $ - | 0.00% | $ - | 0.00% |
| North America: | | | | |
| NTNA | 988,708 | 9.48% | 1,468,688 | 15.43% |
| | 988,708 | 9.48% | 1,468,688 | 15.43% |
| Europe: | | | | |
| Netsol UK | - | 0.00% | - | 0.00% |
| NTE | 2,486,792 | 23.85% | 2,441,922 | 25.65% |
| | 2,486,792 | 23.85% | 2,441,922 | 25.65% |
| Asia-Pacific: | | | | |
| Netsol PK | 5,419,981 | 51.99% | 4,889,617 | 51.36% |
| Netsol-Innovation | 729,012 | 6.99% | 544,099 | 5.72% |
| Netsol Connect | 186,470 | 1.79% | 138,852 | 1.46% |
| Netsol-Abraxas Australia | 16,284 | 0.16% | 36,630 | 0.38% |
| Netsol-Thailand | 598,000 | 5.74% | - | 0.00% |
| | 6,949,747 | 66.66% | 5,609,198 | 58.92% |
| Total | $10,425,247 | 100.00% | $9,519,808 | 100.00% |

The following table sets forth the items in our unaudited consolidated statement of operations for the three months ended December 31, 2010 and 2009 as a percentage of revenues.

| | For the Three Months Ended December 31, 2010 | | 2009 | |
|---|---|---|---|---|
| **Net Revenues:** | | % | | % |
| License fees | $ 3,129,063 | 30.01% | $ 3,318,936 | 34.86% |
| Maintenance fees | 2,023,509 | 19.41% | 1,780,336 | 18.70% |
| Services | 5,272,675 | 50.58% | 4,420,535 | 46.44% |
| Total revenues | 10,425,247 | 100.00% | 9,519,808 | 100.00% |
| **Cost of revenues:** | | | | |
| Salaries and consultants | 2,127,280 | 20.41% | 2,005,845 | 21.07% |
| Travel | 238,776 | 2.29% | 329,007 | 3.46% |
| Repairs and maintenance | 71,459 | 0.69% | 69,112 | 0.73% |
| Insurance | 31,087 | 0.30% | 36,030 | 0.38% |
| Depreciation and amortization | 679,284 | 6.52% | 573,268 | 6.02% |
| Other | 348,859 | 3.35% | 585,157 | 6.15% |
| Total cost of revenues | 3,496,745 | 33.54% | 3,598,418 | 37.80% |
| **Gross profit** | 6,928,503 | 66.46% | 5,921,390 | 62.20% |
| **Operating expenses:** | | | | |
| Selling and marketing | 1,002,877 | 9.62% | 526,751 | 5.53% |
| Depreciation and amortization | 267,861 | 2.57% | 418,023 | 4.39% |
| Bad debt expense | (353) | 0.00% | 212,840 | 2.24% |
| Salaries and wages | 736,898 | 7.07% | 743,970 | 7.81% |
| Professional services, including non-cash compensation | 151,276 | 1.45% | 210,795 | 2.21% |
| Lease abandonment charges | - | 0.00% | 1,076,347 | 11.31% |
| General and adminstrative | 873,569 | 8.38% | 1,042,172 | 10.95% |
| Total operating expenses | 3,032,128 | 29.08% | 4,230,898 | 44.44% |
| **Income from operations** | 3,896,375 | 37.37% | 1,690,492 | 17.76% |
| **Other income and (expenses)** | | | | |
| Loss on sale of assets | (792) | -0.01% | (89,119) | -0.94% |
| Interest expense | (291,475) | -2.80% | (372,273) | -3.91% |
| Interest income | 9,958 | 0.10% | 33,752 | 0.35% |
| (Loss) on foreign currency exchange transactions | (400,658) | -3.84% | (3,247) | -0.03% |
| Share of net loss from equity investment | (71,799) | -0.69% | - | 0.00% |
| Beneficial conversion feature | (118,163) | -1.13% | (595,215) | -6.25% |
| Other income (expense) | (1,748) | -0.02% | (50,825) | -0.53% |
| Total other income (expenses) | (874,677) | -8.39% | (1,076,927) | -11.31% |
| **Net income before non-controlling interest in subsidiary and income taxes** | 3,021,698 | 28.98% | 613,565 | 6.45% |
| **Income taxes** | (3,168) | -0.03% | (32,526) | -0.34% |
| **Non-controlling interest** | (1,082,792) | -10.39% | (1,028,917) | -10.81% |
| ***Net income (loss) attributable to NetSol*** | 1,935,737 | 18.57% | (447,878) | -4.70% |

Net revenues for the quarter ended December 31, 2010 were $10,425,247 as compared to $9,519,808 for the quarter ended December 31, 2009. This reflects an increase of $905,440 or 9.51% in the current quarter as compared to the quarter ended December 31, 2009. Year over year, revenue from license income reduced slightly, by $189,873. Services revenue, which also includes consulting and implementation, increased to $5,272,675 as compared to $4,420,535 last year. This is an increase by 19.28%. In addition to services from new customers, this increase is mainly attributable to certain enhancements and consultancy work from the existing customers. Maintenance fees also increased by $243,173. As we are selling more licenses, this fee is expected to further increase in future.

The gross profit was $6,928,503 in the quarter ending December 31, 2010 as compared with $5,921,390 for the same quarter of the previous year. This is an increase of 17.01% or $1,007,113. The gross profit percentage for the quarter increased approximately 4.26% to 66.46% from 62.20% in the quarter ended December 31, 2009. The cost of sales was $3,496,745 in the current quarter compared to $3,598,418 in the comparable quarter of fiscal 2010. As a percentage of sales it decreased from 37.8% for the quarter ended December 31, 2009 to 33.54% in the current quarter. Salaries and consultant fees increased by $121,435, from $2,005,845, in the prior comparable quarter to $2,127,280. However as a percentage of sales, it slightly decreased by 0.67% from 21.07% in the prior comparable quarter to 20.41% in the current quarter. Besides increase in revenues, the improvement in gross profit margin is also due to management's efforts for globalization of delivery of products using the BestShoring® model.

Operating expenses were $3,032,128 for the quarter ending December 31, 2010 as compared to $4,230,898, for the corresponding period last year for a decrease of 28.33% or $1,198,770. As a percentage of sales it significantly decreased by 15.36% from 44.44% to 29.08%. Main reason of this significant decrease is provision of $1,076,347 made for lease abandonment charges in corresponding period last year. Depreciation and amortization expense amounted to $267,861 and $418,023 for the quarter ended December 31, 2010 and 2009, respectively. Combined salaries and wage costs were $736,898 and $743,970 for the comparable periods, respectively. As a percentage of sales, these costs slightly decreased from 7.81% to 7.07%. General and administrative expenses were $873,569 and $1,042,172 for the quarters ended December 31, 2010 and 2009, respectively, a decrease of $168,604 or 2.57%. As a percentage of sales, these expenses were 8.38% in the current quarter compared to 10.95% in the comparable quarter. The decrease is mainly attributable due to control over some non-cash expense on share based compensation.

Selling and marketing expenses were $1,002,877 and $526,751, in the quarter ended December 31, 2010 and 2009, respectively. The increase is due to focus on aggressive marketing efforts in different geographies of the world. The result of this investment in sales and marketing is also reflected in the increasing demand of our flagship product "NetSol Financial Suit and as well as the increasing revenues of the company. Professional services expense decreased 28.24% to $151,276 in the quarter ended December 31, 2010, from $210,795 in the corresponding period last year.

Income from operations was $3,896,375 compared to $1,690,492 for the quarters ended December 31, 2010 and 2009, respectively. This represents an increase of $2,205,883 for the quarter compared with the comparable period in the prior year. As a percentage of sales, net income from operations was 37.37% in the current quarter compared to 17.76% in the prior period.

Net income was $1,935,737 compared to a loss of $447,878 for the quarters ended December 31, 2010 and 2009, respectively. This is an increase of $2,383,616 compared to the prior year. Included in this income is foreign currency exchange loss of $400,658 (December 2009, $3,247) due to depreciation of Euro and Pound Sterling in the current quarter against Pakistan Rupee. The current fiscal quarter amount includes a net reduction of $1,082,792 compared to $1,028,917 in the prior period for the 49.9% non-controlling interest in NetSol Innovation owned by other parties, and the 42.04% non-controlling interest in NetSol PK. Interest expense was $291,475 in the current quarter as compared to $372,273 in the comparable period. Net income per share, basic and diluted, was $0.04 as compared to loss of $0.01 for the quarters ended December 31, 2010 and 2009.

The net EBITDA income was $3,177,525 compared to $948,211 for the quarters ended December 31, 2010 and 2009, after amortization and depreciation charges of $947,145 and $991,291, income taxes of $3,168 and $32,526, and interest expense of $291,475 and $372,273, respectively. The EBITDA earning per share, basic and diluted was $0.07 and $0.06 for the quarter ended December 31, 2010 and, $0.03 for the quarter ended December 31, 2009. As a percentage of revenues EBITDA was 30.48% compared to 9.96% for the quarters ended December 31, 2010 and 2009, 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 the Company's historical operating results nor is it intended to be predictive of potential future results.

**Six Month Period Ended December 31, 2010 as compared to the Six Month Period Ended December 31, 2009**:

Net revenues for the six months ended December 31, 2010 and 2009 are broken out among the subsidiaries as follows:

| | 2010 | | 2009 | |
|---|---|---|---|---|
| | Revenue | % | Revenue | % |
| Corporate headquarters | $ - | 0.00% | $ - | 0.00% |
| | | | | |
| North America: | | | | |
| NTNA | 2,231,691 | 11.85% | 3,192,642 | 18.62% |
| | 2,231,691 | 11.85% | 3,192,642 | 18.62% |
| Europe: | | | | |
| Netsol UK | - | 0.00% | - | 0.00% |
| NTE | 4,576,771 | 24.31% | 3,371,716 | 19.67% |
| | 4,576,771 | 24.31% | 3,371,716 | 19.67% |
| Asia-Pacific: | | | | |
| Netsol PK | 9,484,435 | 50.37% | 9,032,571 | 52.69% |
| Netsol-Innovation | 1,395,817 | 7.41% | 1,198,416 | 6.99% |
| Netsol Connect | 318,745 | 1.69% | 293,182 | 1.71% |
| Netsol-Abraxas Australia | 19,128 | 0.10% | 53,354 | 0.31% |
| Netsol-Thailand | 801,732 | 4.26% | - | 0.00% |
| | | | | |
| | 12,019,857 | 63.84% | 10,577,523 | 61.71% |
| | | | | |
| Total | $18,828,319 | 100.00% | $17,141,881 | 100.00% |

The following table sets forth the items in our unaudited consolidated statement of operations for the six months ended December 31, 2010 and 2009 as a percentage of revenues:

| | For the Half Year Ended December 31, 2010 | % | 2009 | % |
|---|---|---|---|---|
| **Net Revenues:** | | % | | % |
| License fees | $ 6,606,856 | 35.09% | $ 5,870,529 | 34.25% |
| Maintenance fees | 3,693,428 | 19.62% | 3,588,053 | 20.93% |
| Services | 8,528,035 | 45.29% | 7,683,299 | 44.82% |
| Total revenues | 18,828,319 | 100.00% | 17,141,881 | 100.00% |
| **Cost of revenues:** | | 0.00% | | 0.00% |
| Salaries and consultants | 4,114,168 | 21.85% | 4,019,598 | 23.45% |
| Travel | 470,388 | 2.50% | 389,207 | 2.27% |
| Repairs and maintenance | 128,517 | 0.68% | 136,723 | 0.80% |
| Insurance | 62,079 | 0.33% | 72,709 | 0.42% |
| Depreciation and amortization | 1,310,225 | 6.96% | 1,071,772 | 6.25% |
| Other | 591,997 | 3.14% | 1,467,495 | 8.56% |
| Total cost of revenues | 6,677,374 | 35.46% | 7,157,503 | 41.75% |
| **Gross profit** | 12,150,945 | 64.54% | 9,984,378 | 58.25% |
| **Operating expenses:** | | 0.00% | | 0.00% |
| Selling and marketing | 1,486,847 | 7.90% | 1,020,381 | 5.95% |
| Depreciation and amortization | 534,303 | 2.84% | 930,384 | 5.43% |
| Bad debt expense | 254,279 | 1.35% | 212,840 | 1.24% |
| Salaries and wages | 1,657,162 | 8.80% | 1,468,665 | 8.57% |
| Professional services, including non-cash compensation | 290,361 | 1.54% | 306,901 | 1.79% |
| Lease abandonment charges | - | 0.00% | 1,076,347 | 6.28% |
| General and adminstrative | 2,006,088 | 10.65% | 2,132,183 | 12.44% |
| Total operating expenses | 6,229,041 | 33.08% | 7,147,701 | 41.70% |
| **Income (loss) from operations** | 5,921,904 | 31.45% | 2,836,677 | 16.55% |
| **Other income and (expenses)** | | 0.00% | | 0.00% |
| Loss on sale of assets | (15,586) | -0.08% | (89,101) | -0.52% |
| Interest expense | (607,119) | -3.22% | (840,887) | -4.91% |
| Interest income | 94,419 | 0.50% | 151,562 | 0.88% |
| Gain on foreign currency exchange transactions | 673,236 | 3.58% | 380,577 | 2.22% |
| Share of net loss from equity investment | (142,236) | -0.76% | - | 0.00% |
| Beneficial conversion feature | (295,574) | -1.57% | (893,214) | -5.21% |
| Other income (expense) | (57,301) | -0.30% | (81,975) | -0.48% |
| Total other income (expenses) | (350,162) | -1.86% | (1,373,038) | -8.01% |
| **Net income (loss) before non-controlling interest in subsidiary and income taxes** | 5,571,742 | 29.59% | 1,463,639 | 8.54% |
| **Income taxes** | (11,724) | -0.06% | (37,543) | -0.22% |
| **Non-controlling interest** | (2,057,301) | -10.93% | (2,137,892) | -12.47% |
| ***Net income (loss) attributable to NetSol*** | 3,502,718 | 18.60% | (711,796) | -4.15% |

Net revenues for the six months ended December 31, 2010 were $18,828,319 as compared to $17,141,881 for the six months ended December 31, 2009. This reflects an increase of $1,686,438 or 9.84%. Revenue from license income increased to $6,606,856 from $5,870,529 in the corresponding half year of fiscal 2010. This is an increase of $736,328 or 12.54%. The company manages to sell more new licenses of its product NetSol Financial Suite resulting in increased license income. Services revenue, which also includes consulting and implementation, increased to $8,528,035 as compared to $7,683,299 last year. In addition to services from new customers, this increase is also attributable to certain enhancements and consultancy work from the existing customers. Maintenance fees also increased by $105,375 from $3,588,053 last year to $3,693,428 in the current first half of fiscal 2011. As we are selling more licenses, this fee is expecting to further increase in future.

The gross profit was $12,150,945 in the six months ending December 31, 2010 as compared with $9,984,378 for the same period of the previous year or an increase of 21.7% or $2,166,567. The gross profit percentage for the six months increased approximately 6.29% to 64.54% from 58.25% in the six months ended December 31, 2009. The cost of sales was $6,677,374 in the current period compared to $7,157,503 in the comparable period of fiscal 2010. As a percentage of sales it decreased from 41.75% for the six months ended December 31, 2009 to 35.46% in the current period. Salaries and consultant fees increased by $94,570 from $4,019,598 in the prior comparable period to $4,114,168. However as a percentage of sales, it decreased by 1.6% from 23.45% in the prior comparable period to 21.85% in the current period. The improvement in gross profit margin is due to management's efforts for globalization of delivery of products using the BestShoring® model.

Operating expenses were $6,229,041 for the six months ending December 31, 2010 as compared to $7,147,701, for the corresponding period last year or a decrease of 12.85% or $918,660. As a percentage of sales it decreased by 8.61% from 41.7% to 33.08%.Main reason of this decrease is the provision of $1,076,347 made for lease abandonment charges in corresponding period last year. Depreciation and amortization expense amounted to $534,303 and $930,384 for the six months ended December 31, 2010 and 2009, respectively. Combined salaries and wage costs were $1,657,162 and $1,468,665 for the comparable periods, respectively. As a percentage of sales, these costs increased from 8.57% to 8.80%. General and administrative expenses were $2,006,088 and $2,132,183 for the six months ended December 31, 2010 and 2009, respectively, a decrease of $126,095 or 5.91%. As a percentage of sales, these expenses were 10.65% in the current period compared to 12.44% in the comparable period. The decrease is mainly attributable due to control over some non-cash expense on share based compensation.

Selling and marketing expenses were $1,486,847 and $1,020,381 in the six months ended December 31, 2010 and 2009, respectively. The increase is due to focus on aggressive marketing efforts in different geographies of the world. The result of this investment in sales and marketing is also reflected in the increasing demand of our flagship product, NetSol Financial Suite, as well as the increasing revenues of the company. Professional services expense decreased 5.39% to $290,361 in the six months ended December 31, 2010, from $306,901 in the corresponding period last year.

Income from operations was $5,921,904 compared to $2,836,677 for the six months ended December 31, 2010 and 2009, respectively. This represents an increase of $3,085,227 for the six months compared with the comparable period in the prior year. As a percentage of sales, net income from operations was 31.45% in the current period compared to 16.55% in the prior period.

Net income was $3,502,718 compared to a loss of $711,796 for the six months ended December 31, 2010 and 2009, respectively. This is an increase of $4,214,513 compared to the prior year. Included in this income is foreign currency exchange gain of $673,236 (December 2009, $380,577) due to appreciation of Euro, US$ and Pound Sterling in the current half year period against Pakistan Rupee. The current fiscal period amount includes a net reduction of $2,057,301 compared to $2,137,892 in the prior period for the 49.9% non-controlling interest in NetSol Innovation owned by other parties, and the 42.04% non-controlling interest in NetSol PK. Interest expense was $607,119 in the current six months as compared to $840,887 in the comparable period. Net income per share, basic and diluted, was $0.08 as compared to loss of $0.02 for the periods ended December 31, 2010 and 2009.

The net EBITDA income was $5,966,090 compared to $2,168,792 for the periods ended December 31, 2010 and 2009, after amortization and depreciation charges of $1,844,528 and $2,002,156, income taxes of $11,724 and $37,543, and interest expense of $607,119 and $840,887 respectively. The EBITDA earning per share, basic and diluted was $0.14 and $0.13 for the period ended December 31, 2010 and $0.07 and $0.06 for the period ended December 31, 2009. As a percentage of revenues EBITDA was 31.69% compared to 12.65% for the periods ended December 31, 2010 and 2009, 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 the Company's historical operating results nor is it intended to be predictive of potential future results.

## LIQUIDITY AND CAPITAL RESOURCES

We note that the Company's cash position was $5,856,152 at December 31, 2010, compared to $5,211,674 at December 31, 2009.

Net cash provided by operating activities amounted to $5,306,822 for the six months ended December 31, 2010, as compared to $4,374,822 for the comparable period last fiscal year. The increase is mainly due to an increase in both net profits of the Company, accounts receivable and other current assets. The increase in the overall revenues of the company due to the signing of new deals has resulted in an increase in accounts receivables and other current assets, including revenues in excess of billings. The average collection cycle for accounts receivables ranges between three to six months from the date of invoicing. The average days sales outstanding, for the period ended December 31, 2010, was 144 days as compared with 129 days in same period of fiscal 2010.

Net cash used by investing activities amounted to $5,994,175 for the six months ended December 31, 2010, as compared to $3,976,108 for the comparable period last fiscal year. The Company had net purchases of property and equipment of $2,450,222 compared to $1,085,787 for the comparable period last fiscal year. The Company also purchased non-controlling interest in NetSol Connect using $180,000 in current period. The short term investment held for sales used $256,706 in current period as compared to $Nil in corresponding previous year. The increase in intangible assets which represents amounts capitalized for the development of new products was $3,127,234 and $3,118,094 for the comparable periods.

Net cash provided by financing activities amounted to $2,586,278 and $554,399 for the six months ended December 31, 2010, and 2009, respectively. The Company generated $2,566,750 through sale of its common stock whereas in the corresponding period of fiscal 2010, the cash generated through sale of common stock was $514,539. The six months ended December 31, 2010 included the cash inflow of $667,300 from the exercising of stock options and warrants compared to $33,750 in six months ended December 31, 2009. In the current fiscal period, the Company had net payments on account of bank loans, loans and capital leases of $3,035,240 as compared to $2,183,189 in the comparable period last year. The Company is operating in varying 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. 12 of the annexed financial statements. The company and all its subsidiaries 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. The Company anticipates to pay 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, European 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 the Company, we will be very cautious and prudent about any new capital raise given the global market declines. However, the Company is very conscious of the dilutive effect and price pressures in raising equity-based capital.

**Item 3. Quantitative and Qualitative Disclosures About Market Risks.**

None.

**Item 4. Controls and Procedures**

**Disclosure Controls and Procedures**

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of the end of the period covered by this Report (December 31, 2010). Based on such evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of such period, the Company's disclosure controls and procedures are effective in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act and are effective in ensuring that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

**Changes in Internal Control Over Financial Reporting**

There have been no changes in the Company's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the second quarter of fiscal year 2010 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## 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.

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

In October 2010, the Company issued a total of 210,000 shares of restricted common stock to executive employees as part of their compensation agreements. These share issuances were further reported on the employees annual form 5 filings. These shares were issued in reliance on an exemption from registration available under section 4(2) of the Securities Act of 1933, as amended. All of the executive employees in this transaction have direct knowledge, experience, and access to the Company’s financial and business information. Finally, the executives are all accredited investors and can bear the economic risk of the issued securities, if any.

In October 2010, an employee of the Company was issued 10,000 shares of restricted common stock which was required to be issued according to the terms of his employment agreement. The shares were issued in reliance on an exemption from registration under Section 4(2) of the Securities Act of 1933, as amended. The executive employee in this transaction has direct knowledge, experience and access to the Company’s financial and business information. Finally, the executive employee is an accredited investor and can bear the economic risk of the issued securities, if any.

In October 2010, shares of restricted common stock totaling 1,974,384 shares were issued to 13 accredited investors who all had a pre-existing investor relationship with the Company as part of an offering of common stock at $.65 per share that was commenced in August 2010. The shares were issued in reliance on an exemption from registration under Regulation S of the Securities Act of 1933, as amended.

In October 2010, the Company issued 233,000 shares of common stock to a consultant. The shares were due as part of its agreement with the Company. The consultant is an accredited and sophisticated investor. The shares were issued in reliance on an exemption from registration under section 4(2) of the Securities Act of 1933, as amended. The consultant is a business consultant that is familiar with the Company. The consultant has had the opportunity to review the Company’s financial and business materials.

In October 2010, holders of warrants were issued a total of 3,153,082 shares of common stock as a result of the exercise of warrants issued in June and October 2007. This transaction was initially reported at the time of the acquisition of the shares of common stock and associated warrants in 2007. The shares were issued in reliance on an exemption from registration under Regulation S of the Securities Act of 1933, as amended. The investors are sophisticated, accredited and non-US investor and otherwise qualify under the exemption.

In November 2010, the four independent directors were issued a total of 30,000 shares as compensation for their service on the board of directors for the quarter ended September 30, 2010. These shares are issued as part of the Company’s 2008 Equity Incentive Plan. These share issuances were reported in the holders’ annual Form 5 filing. These shares were issued in reliance on exemptions from registration under section 4(2) of the Securities Act of 1933, as amended. All board members have direct and continuous access to the Company’s financial and business materials and filings and are able to identify any risks that may be related with the shares. In addition, the board members have continuous and direct contact with the senior executives of the Company who may clarify any questions that they may have surrounding the shares. All of the independent directors are accredited investors and can bear the economic risk of loss, if any.

In November 2010, the Company issued 25,000 shares of common stock to a consultant. The shares were due as part of its agreement with the Company. The consultant is an accredited and sophisticated investor. The shares were issued in reliance on an exemption from registration under section 4(2) of the Securities Act of 1933, as amended. The consultant is a business consultant that is familiar with the Company. The consultant has had the opportunity to review the Company’s financial and business materials.

In November 2010, the Company issued 54,857 shares of common stock to a consultant. The shares were payment in exchange for services rendered as a business travel logistic consultant. The consultant is an accredited and sophisticated investor. The shares were issued in reliance on an exemption from registration under section 4(2) of the Securities Act of 1933, as amended. The consultant is a business consultant that is familiar with the Company. The consultant has had the opportunity to review the Company's financial and business materials.

In November 2010, one of the holders of our $6 million convertible note converted $402,741.02 worth of principal and interest there on from the note into 639,272 shares of common stock. This transaction was originally reported on an 8-K at the time of the issuance of the Note in July 2008. The shares were issued in reliance on an exemption from registration under Regulation S of the Securities Act of 1933, as amended. The investor is a sophisticated, accredited and non-US investor and otherwise qualifies under the exemption.

In December 2010, an employee of the Company was issued 7,267 shares of restricted common stock which was required to be issued according to the terms of his employment agreement. The shares were issued in reliance on an exemption from registration under Section 4(2) of the Securities Act of 1933, as amended. The executive employee in this transaction has direct knowledge, experience and access to the Company's financial and business information. Finally, the executive employee is an accredited investor and can bear the economic risk of the issued securities, if any.

STOCK REPURCHASE PLAN

No purchases were made in the repurchase plan approved by the Board of Directors in July 2010 from the date of the inception of the plan through December 31, 2010. The maximum number of shares that may be purchased under the plan remains at 2,000,000. The repurchase plan expired in January 2011.

**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: | February 10, 2011 | /s/ Najeeb Ghauri<br>NAJEEB GHAURI<br>Chief Executive Officer |
| Date: | February 10, 2011 | /s/Boo-Ali Siddiqui<br>BOO-ALI SIDDIQUI<br>Chief Financial Officer<br>Principal Accounting Officer |

Certification Pursuant to 18 U.S.C. Section 1350
As Adopted Pursuant to
Section 302 of the Sarbanes-Oxley Act of 2002

I, Najeeb Ghauri, certify that:

(1) I have reviewed this quarterly report on Form 10-Q for the fiscal quarter ended December 31, 2010 of NetSol Technologies, Inc., ("Registrant").

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

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

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

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

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

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

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

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

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

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

Date: February 10, 2011

/s/Najeeb Ghauri
Najeeb Ghauri,
Chief Executive Officer
Principal executive officer

Certification Pursuant to 18 U.S.C. Section 1350
As Adopted Pursuant to
Section 302 of the Sarbanes-Oxley Act of 2002

I, Boo-Ali Siddiqui, certify that:

(1) I have reviewed this quarterly report on Form 10-Q for the fiscal quarter ended December 31, 2010 of NetSol Technologies, Inc., ("Registrant").

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

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

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

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

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

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

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

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

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

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

Date: February 10, 2011

/s/ Boo-Ali Siddiqui
Boo-Ali Siddiqui
Chief Financial Officer
Principal Accounting Officer

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

In connection with the Quarterly Report of NetSol Technologies, Inc. on Form 10-Q for the period ending December 31, 2010, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, Najeeb Ghauri, Chief Executive Officer of the Company, certifies, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to ss. 906 of the Sarbanes-Oxley Act of 2002, that:

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

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

Date: February 10, 2011

/s/ Najeeb Ghauri
Najeeb Ghauri,
Chief Executive Officer
Principal Executive Officer

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

In connection with the Quarterly Report of NetSol Technologies, Inc. on Form 10-Q for the period ending December 31, 2010, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, Boo-Ali Siddiqui, Chief Financial Officer, and Principal Accounting Officer of the Company, certifies, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to ss. 906 of the Sarbanes-Oxley Act of 2002, that:

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

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

Date: February 10, 2011

/s/ Boo-Ali Siddiqui
Boo-Ali Siddiqui,
Chief Financial Officer
Principal Accounting Officer