

Net Medical Xpress Solutions, Inc.
Form 10-Q
November 12, 2014

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

FORM 10-Q

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

For the quarterly period ended September 30, 2014

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

For the transition period from _____ to _____

COMMISSION FILE No. 333-30176

NET MEDICAL EXPRESS SOLUTIONS, INC.

(Exact name of Registrant as specified in charter)

NEVADA
(State or other jurisdiction of
incorporation or organization)

91-1287406
(I.R.S. Employer Identification No.)

5021 Indian School Road, Suite 100
Albuquerque, New Mexico 87110
(Address of principal executive offices) (Zip Code)

(505) 255-1999

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(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES NO

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

Large accelerated filer
Non-accelerated filer

Accelerated filer
Smaller 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 number of shares outstanding of each of the issuer's classes of common stock at November 7, 2014 was 163,622,470.

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USE OF PRONOUNS AND OTHER WORDS

The pronouns we , us , our and the equivalent used in this annual report mean Net Medical Xpress Solutions, Inc. and consolidated subsidiaries. In the notes to our financial statements, the Company means Net Medical Xpress Solutions, Inc. and consolidated subsidiaries. The pronoun you means the reader of this quarterly report.

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS AND INFORMATION

This quarterly report on Form 10-Q, other reports we have file and will file pursuant to Section 15(d) of the Securities Exchange Act of 1934 and press releases we have issued and will issue will have contained and will contain, as the case may be, forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 and are intended to enjoy the benefits of that act. Unless the context is otherwise, we use words such as anticipate , assumption , believe , could , estimate , expect , forecast , intend , may , objective , outlook , plan and predict , project and projection , seek , should , will continue , will result and would , or other such words, w or pronouns and verbs or adverbs in the future tense and words and phrases that convey similar meaning and uncertainty of and information about future events or outcomes and statements about performance that is not an historical fact to identify these forward-looking statements. Such words and statements involve estimates, assumptions and uncertainties, which could cause actual results to differ materially from those expressed in them. Any forward-looking statements are qualified in their entirety by reference to the factors discussed throughout this document. All forward-looking statements concerning economic conditions, rates of growth, rates of income or values as may be included in this document are based on information available to us on the dates noted, and we assume no obligation to update any such forward-looking statements. It is important to note that our actual results may differ materially from those in such forward-looking statements due to fluctuations in interest rates, inflation, government regulations, economic conditions and competitive product and pricing pressures in the geographic and business areas in which we conduct operations, including our plans, objectives, expectations and intentions and other factors discussed elsewhere in this document.

There are a number of important factors beyond our control that could cause actual results to differ materially from the results anticipated by these forward-looking statements. For example, a few of the uncertainties that could affect the accuracy of forward-looking statements include the following:

·
Rapid changes in technology relating to the Internet

·
Continued growth and use of the Internet

.

Changes in government regulations

.

Changes in our business strategies

.

Hardware failure of a catastrophic proportion

.

Terrorist interference with the operation of the Internet or effects of terrorist activities on the economy

.

Difficulty recruiting and retaining staff of sufficient technical caliber to provide adequate and on-going customer support and product maintenance and development

.

Failure to successfully market our products through the Internet and our representatives

.

Inability to locate sources to retire our line of credit or to obtain alternative lending sources

.

Inability to solve cash flow problems

We make these forward-looking statements based our beliefs and on various factors and using numerous assumptions using information available at the time we make these statements. Forward-looking statements (i) are neither predictions nor guaranties of future events or circumstances, and (ii) the assumptions, beliefs, expectations, forecasts and projections about future events may differ materially from actual results. You have no assurance the factors and assumptions we have used as a basis for forward-looking statements will prove to be materially accurate when the events they anticipate actually occur in the future; and, you should not place undue reliance on any such forward-looking statements. We undertake no obligation to publicly update any forward-looking statement to reflect developments occurring after the date of this annual report or after the date of any previous or subsequent report or any press release after publication.

PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Net Medical Xpress Solutions, Inc.**Condensed Consolidated Balance Sheets****(Rounded to the nearest thousand)****(Unaudited)**

	September 30, 2014	December 31, 2013
Assets		
Current assets:		
Cash and equivalents	\$ 315,000	\$ 421,000
Accounts receivable, net of allowance of \$18,000 and \$29,000, respectively	883,000	606,000
Inventory	14,000	2,000
Prepaid expenses and other assets	108,000	66,000
Total current assets	1,320,000	1,095,000
Furniture, equipment and improvements, net of accumulated depreciation of \$656,000 and \$643,000, respectively	48,000	58,000
Security deposits	4,000	4,000
Goodwill	239,000	239,000
Total Assets	\$ 1,611,000	\$ 1,396,000
Liabilities and Stockholders' Equity (Deficit)		
Current liabilities:		
Accounts payable	\$ 784,000	\$ 676,000
Accrued expenses	145,000	79,000
Deferred revenue	165,000	2,000
Capital lease	8,000	7,000
Notes payable - related party	50,000	48,000
Total current liabilities	1,152,000	812,000
Long-term liabilities		
Notes payable - related party	2,000	2,000

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Capital lease - long-term portion	11,000	11,000
Total long-term liabilities	13,000	13,000
Total liabilities	1,165,000	825,000
Stockholders' equity (deficit):		
Preferred stock, \$0.001 par value, 500,000 shares authorized, 0 shares issued and outstanding, as of 9/30/14 and 12/31/13, respectively	-	-
Common stock, \$0.001 par value, 200,000,000 shares authorized, 163,622,470 and 160,622,470 shares issued and outstanding as of 9/30/14 and 12/31/13, respectively	163,000	160,000
Paid-in capital	15,738,000	15,466,000
Subscriptions payable	66,000	296,000
Deferred compensation	(25,000)	(40,000)
Accumulated deficit	(15,496,000)	(15,311,000)
Total stockholders' equity (deficit)	446,000	571,000
Total Liabilities and Stockholders' Equity (Deficit)	\$ 1,611,000	\$ 1,396,000

The accompanying notes are an integral part of these financial statements.

Net Medical Xpress Solutions, Inc.

Condensed Consolidated Statements of Operations

(Rounded to the nearest thousand)

(Unaudited)

	For the three months ended September 30,		For the nine months ended September 30,	
	2014	2013	2014	2013
Revenues				
Net Medical Xpress Services	823,000	911,000	2,738,000	2,863,000
Net Medical Xpress Specialists	157,000	118,000	399,000	348,000
Net Medical Xpress Solutions	\$ 90,000	\$ 99,000	\$ 311,000	\$ 344,000
Net Medical Xpress Staffing	21,000	101,000	88,000	101,000
Gross revenues	1,091,000	1,229,000	3,536,000	3,656,000
Cost of services	928,000	909,000	2,869,000	2,752,000
Gross profit	163,000	320,000	667,000	904,000
Operating costs and expenses:				
General and administrative	235,000	256,000	730,000	707,000
Depreciation and amortization	4,000	4,000	11,000	16,000
Research and development	29,000	45,000	99,000	106,000
Total operating costs and expenses	268,000	305,000	840,000	829,000
Net operating income (loss)	(105,000)	15,000	(173,000)	75,000
Other income (expense):				
Interest expense	(4,000)	(3,000)	(12,000)	(9,000)
Total other income (expense)	(4,000)	(3,000)	(12,000)	(9,000)
Net income (loss)	\$ (109,000)	\$ 12,000	\$ (185,000)	\$ 66,000
Income (loss) per share - basic	\$ (0.00)	\$ 0.00	\$ (0.00)	\$ 0.00
Income (loss) per share - diluted	\$ (0.00)	\$ 0.00	\$ (0.00)	\$ 0.00
Basic weighted average common shares outstanding	165,222,470	164,708,016	163,909,283	163,793,822
Diluted weighted average common shares outstanding	165,222,470	164,708,016	165,593,511	163,793,822

The accompanying notes are an integral part of these financial statements.

Net Medical Xpress Solutions, Inc.

Condensed Consolidated Statements of Cash Flows

(Rounded to the nearest thousand)

(Unaudited)

	For the nine months ended September 30,	
	2014	2013
Cash flows from operating activities		
Net income (loss)	\$ (185,000)	\$ 66,000
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Common stock issued for services to board members and officers	-	60,000
Common stock issued for services	15,000	25,000
Depreciation and amortization	10,000	19,000
Depreciation and amortization allocated to cost of goods sold	9,000	2,000
Changes in operating assets and liabilities:		
Accounts receivable	(277,000)	14,000
Inventory	(12,000)	(7,000)
Prepaid expenses and other assets	(42,000)	122,000
Accounts payable	108,000	44,000
Accrued expenses	66,000	(113,000)
Deferred revenue	163,000	(1,000)
Net cash provided (used) by operating activities	(145,000)	231,000
Cash flows from investing activities		
Assets purchased under capital lease	8,000	-
Acquisition of fixed assets	(9,000)	(8,000)
Net cash used by investing activities	(1,000)	(8,000)
Cash flows from financing activities		
Repayment of principal under capital lease	(7,000)	(2,000)
Proceeds from notes payable - related party	2,000	2,000
Net proceeds from the issuance of common stock for the exercise of options	45,000	45,000
Working capital received from MedTel Solutions, LLC transaction	-	36,000
Net cash provided by financing activities	40,000	81,000
Net increase in cash equivalents	(106,000)	304,000
Cash equivalents - beginning	421,000	109,000
Cash equivalents - ending	\$ 315,000	\$ 413,000
Supplemental disclosures:		
Interest paid	\$ 11,000	\$ 7,000

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Supplemental disclosures of non-cash financing activities:

Insurance contracts financed	\$ 166,000	\$ 179,000
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Assets purchased under capital lease	\$ 8,000	\$ -
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Supplemental disclosure of noncash investing and financing activities related to MedTel Solutions, LLC transaction:

Acquisition of goodwill through issuance of commons stock	\$ -	\$ 239,000
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The accompanying notes are an integral part of these financial statements.

Net Medical Xpress Solutions, Inc.

Notes to the Financial Statements

(Unaudited)

NOTE A - BASIS OF PRESENTATION

The interim financial statements included herein, presented in accordance with United States generally accepted accounting principles and stated in US dollars, 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 interim financial statements be read in conjunction with the financial statements of the Company for the year ended December 31, 2013 and notes thereto included in the Company's Form 10-K. The Company follows the same accounting policies in the preparation of interim reports.

Results of operations for the interim periods are not indicative of annual results.

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reclassification:

Certain reclassifications have been made to conform the 2013 amounts to the 2014 classifications for comparative purposes.

Principles of Consolidation:

The accompanying consolidated financial statements include the accounts Net Medical Xpress Solutions, Inc. (Formerly New Mexico Software, Inc.) and its wholly-owned subsidiaries, Telerad Service, Inc. and MedTel Solutions, LLC. Intercompany transactions and balances have been eliminated in consolidation.

Use of Estimates:

The preparation of 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 amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents:

The Company considers all highly liquid instruments purchased with a maturity of three months or less to be cash equivalents. At September 30, 2014, the Company did not have cash and equivalents that exceeded federally insured limits.

Trade Accounts Receivable:

The Company extends unsecured credit to customers under normal trade agreements which generally require payment within 30 - 45 days. Accounts not paid within 15 days after their original due date are considered delinquent. Unless specified by the customer, payments are applied to the oldest unpaid invoice. Accounts receivable are presented at the amount billed.

The Company also estimates an allowance for doubtful accounts, which amounted to \$18,000 and \$30,000 at September 30, 2014 and December 31, 2013, respectively. The estimate is based upon management's review of all accounts and an assessment of the Company's historical evidence of collections. Specific accounts are charged directly to the reserve when management obtains evidence of a customer's insolvency. Charge-offs, net of recoveries, for the nine months ended September 30, 2014 and 2013 totaled \$0 and \$1,000, respectively.

Net Medical Xpress Solutions, Inc.

Notes to the Financial Statements

(Unaudited)

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Property and Equipment:

Property and equipment are stated at cost. Major renewals and improvements are charged to the asset accounts while replacements, maintenance and repairs that do not improve or extend the lives of the respective assets are expensed. At the time property and equipment are retired or otherwise disposed of, the asset and related accumulated depreciation accounts are relieved of the applicable amounts. Gains or losses from retirements or sales are credited or charged to income.

Depreciation is computed on the straight-line and accelerated methods for financial reporting and income tax reporting purposes based upon the following estimated useful lives:

Software development	3 years
Equipment	5 years
Computer hardware	5 years
Office furniture	7 years

Long-Lived Assets:

The Company accounts for its long-lived assets in accordance with Accounting Standards Codification (ASC) Topic 360-10-05, Accounting for the Impairment or Disposal of Long-Lived Assets. ASC Topic 360-10-05 requires that long-lived assets be reviewed for impairment whenever events or changes in circumstances indicate that the historical cost carrying value of an asset may no longer be appropriate. The Company assesses recoverability of the carrying value of an asset by estimating the future net cash flows expected to result from the asset, including eventual disposition. If the future net cash flows are less than the carrying value of the asset, an impairment loss is recorded equal to the difference between the asset's carrying value and fair value or disposable value. The Company determined that none of its long-term assets at September 30, 2014 or December 31, 2013 were impaired.

Stock-Based Compensation:

The Company accounts for stock-based payments to employees in accordance with ASC 718, Stock Compensation (ASC 718). Stock-based payments to employees include grants of stock, grants of stock options and issuance of warrants that are recognized in the consolidated statement of operations based on their fair values at the date of grant.

The Company accounts for stock-based payments to non-employees in accordance with ASC 505-50, Equity-Based Payments to Non-Employees. Stock-based payments to non-employees include grants of stock, grants of stock options and issuances of warrants that are recognized in the consolidated statement of operations based on the value of the vested portion of the award over the requisite service period as measured at its then-current fair value as of each financial reporting date.

The Company calculates the fair value of option grants and warrant issuances utilizing the Binomial pricing model. The amount of stock-based compensation recognized during a period is based on the value of the portion of the awards that are ultimately expected to vest. ASC 718 requires forfeitures to be estimated at the time stock options are granted and warrants are issued to employees and non-employees, and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. The term forfeitures is distinct from cancellations or expirations and represents only the unvested portion of the surrendered stock option or warrant. The Company estimates forfeiture rates for all unvested awards when calculating the expense for the period. In estimating the forfeiture rate, the Company monitors both stock option and warrant exercises as well as employee termination patterns. The resulting stock-based compensation expense for both employee and non-employee awards is generally recognized on a straight-line basis over the period in which the Company expects to receive the benefit, which is generally the vesting period.

Net Medical Xpress Solutions, Inc.

Notes to the Financial Statements

(Unaudited)

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Stock-Based Compensation (continued):

During the nine months ended September 30, 2014 and 2013, the Company recognized stock-based compensation expense totaling \$15,000 and \$60,000, from the issuance of a total of 0 and 0 shares of its common stock to officers, directors, and consultants (See Note E).

Income Taxes:

The Company accounts for its income taxes under the provisions of ASC Topic 740, *Income Taxes*. The method of accounting for income taxes under ASC 740 is an asset and liability method. The asset and liability method requires the recognition of deferred tax liabilities and assets for the expected future tax consequences of temporary differences between tax bases and financial reporting bases of other assets and liabilities.

Gain (Loss) per Share:

The Company reports earnings (loss) per share in accordance with ASC Topic 260-10, "Earnings per Share." Basic earnings (loss) per share is computed by dividing income (loss) available to common shareholders by the weighted average number of common shares available. Diluted earnings (loss) per share is computed similar to basic earnings (loss) per share except that the denominator is increased to include the number of additional common shares that would have been outstanding if the potential common shares had been issued and if the additional common shares were dilutive.

Revenue Recognition:

The Company recognizes revenue in accordance with Statement of Position ASC Topic 985 *Software Revenue Recognition* as amended.

Revenue from proprietary software sales that does not require further commitment from the Company is recognized upon persuasive evidence of an arrangement as provided by agreements executed by both parties, delivery of the software, and determination that collection of a fixed or determinable fee is probable. These sales are generally direct purchases of a software product and there is no other involvement by the Company.

The Company offers with certain sales of its software products, software maintenance, upgrade and support arrangements. These contracts may be elements in a multiple-element arrangement or may be sold in a stand-alone basis. Revenues from maintenance and support services are recognized ratably on a straight-line basis over the term that the maintenance service is provided.

The Company typically charges 17% to 21% of the software purchase price for a 12-month maintenance contract with discounts available for longer-term agreements. The complexity of the software determines the percentage that is charged to any individual customer, and that percentage remains consistent upon renewal unless there is a change in the software or the terms of the agreement.

Charges for hosting are likewise spread ratably over the term of the hosting agreement, with the typical hosting agreement having a term of 12 months, with renewal on an annual basis. The Company sells some hosting contracts in conjunction with the sale of software, and some hosting contracts without an associated software sale. When the hosting arrangement is sold in conjunction with a software sale, the Company allocates a portion of the fee to the software license. Hosting services do not require the customer to purchase the software license, and for those hosting contracts that are sold without an associated software sale, the customer has neither the right nor the ability to operate the software on its own.

Net Medical Xpress Solutions, Inc.

Notes to the Financial Statements

(Unaudited)

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Revenue Recognition (continued):

Should the sale of software involve an arrangement with multiple elements (for example, the sale of a software license along with the sale of maintenance and support to be delivered over the contract period), the Company allocates revenue to each component of the arrangement using the residual value method based on the fair value of the undelivered elements. The Company defers revenue from the arrangement equivalent to the fair value of the undelivered elements and recognizes the remaining amount at the time of the delivery of the product or when all other revenue recognition criteria have been met. Fair values for the ongoing maintenance and support obligations are based upon separate sales of renewals of maintenance contracts. Fair value of services, such as training or consulting, is based upon separate sales of these services to other customers.

The Company follows the guidance in FASB ASC Topic 605, *Accounting for Performance of Construction-Type and Certain Production-Type Contracts* for custom software development arrangements that require significant production, customization or modification to its core software. Revenue is generally recognized for such arrangements under the percentage-of-completion method. Under percentage-of-completion accounting, both the product license and custom software development revenue are recognized as work progresses based on specific milestones in accordance with FASB ASC Topic 450. The Company believes that project milestones based on completion of specific tasks provide the best approximation of progress toward the completion of the contract. At September 30, 2014 and September 30, 2013, there were no custom software development arrangements in progress.

The Company also occasionally derives revenue from the sale of third party hardware, which is billed as a separate deliverable under consulting or custom development contracts. Revenue from radiological services, radiological quality assurance (QA) services, software installation, and any training or consulting services is recognized when the services are rendered. These revenues include services that are not essential to the functionality of the software. If these services are included in a software agreement with multiple elements, amounts are allocated to these categories based on the estimated number of hours required to complete the work, which is the same criteria used to bill for the services separately. License revenue is recognized ratably over the term of the license.

Amounts collected prior to satisfying the above revenue recognition criteria are included in deferred revenue.

The application of ASC 605, as amended, requires judgment, including a determination that collectability is probable and the fee is fixed and determinable.

The Company follows the guidance provided by SEC Staff Accounting Bulletin (SAB) No. 101, *Revenue Recognition in Financial Statements* and SAB No. 104, *Revenue Recognition*, which provide guidance on the recognition, presentation and disclosure of revenue in financial statements filed with the SEC.

Due to uncertainties inherent in the estimation process it is at least reasonably possible that completion costs for contracts in progress will be further revised in the near-term.

The cost of services, consisting of staff payroll, outside services, equipment rental, communication costs and supplies, is expensed as incurred.

Research and Development Expenses:

Costs of research and development activities are expensed as incurred.

Advertising Expenses:

The Company expenses advertising costs which consist primarily of direct mailings, promotional items and print media, as incurred. Advertising expenses amounted to \$0 and \$0 for the nine months ended September 30, 2014 and 2013, respectively.

Net Medical Xpress Solutions, Inc.

Notes to the Financial Statements

(Unaudited)

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Fair Value of Financial Instruments:

The Company adopted the Financial Accounting Standards Board (FASB) standard related to fair value measurement at inception. The standard defines fair value, establishes a framework for measuring fair value and expands disclosure of fair value measurements. The standard applies under other accounting pronouncements that require or permit fair value measurements and, accordingly, does not require any new fair value measurements. The standard clarifies that fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. The recorded values of long-term debt approximate their fair values, as interest approximates market rates. As a basis for considering such assumptions, the standard established a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value as follows:

Level 1: Observable inputs such as quoted prices in active markets;

Level 2: Inputs other than quoted prices in active markets that are observable either directly or indirectly; and

Level 3: Unobservable inputs in which there is little or no market data, which require the reporting entity to develop its own assumptions.

The Company's financial instruments consist of cash, accounts receivable, inventory, prepaid expenses, leasehold improvements, property and equipment, deposits, other assets, accounts payable, accrued expenses, deferred revenue, capital leases and notes payable. The recorded values of cash, accounts receivable, inventory, prepaid expenses, and accounts payable approximate fair values due to the short maturities of such instruments. Recorded values for notes payable and related liabilities approximate fair values, since their stated or imputed interest rates are commensurate with prevailing market rates for similar obligations.

Recent Pronouncements:

The Company's management has reviewed recent accounting pronouncements issued through the date of the issuance of these financial statements. In management's opinion, no pronouncements apply or will have a material effect on the Company's financial statements.

NOTE C - FURNITURE, EQUIPMENT, AND IMPROVEMENTS

Furniture, equipment, and improvements as of September 30, 2014 consisted of the following:

Computers	499,000
Furniture, fixtures and equipment	150,000
Automobiles	41,000
Leasehold improvements	20,000
	710,000
Accumulated depreciation	(662,000)
	\$ 48,000

Depreciation expense for the nine months ended September 30, 2014 and 2013 was \$11,000 and \$16,000, respectively.

Net Medical Xpress Solutions, Inc.

Notes to the Financial Statements

(Unaudited)

NOTE D - GOODWILL

On July 1, 2013, the Company completed its merger with MedTel Solutions, LLC (MedTel), an Alabama limited liability company, in accordance with its Merger Agreement dated June 28, 2013. MedTel was organized on June 13, 2012 for the purpose of engaging in and is now engaged in the business of providing licensed medical practitioners to perform services via telemedicine. Pursuant to the agreement, the Company authorized the issuance of 3,000,000 shares of its common stock in exchange for 100% of the outstanding membership interests of MedTel. The fair value of the consideration given up totaled \$275,000 of which \$36,000 has been allocated to the fair value of net identifiable assets and the remaining \$239,000 to goodwill.

In accordance with FASB ASC 350, Intangibles - Goodwill and Other, the Company performs goodwill impairment testing at least annually, unless indicators of impairment exist in interim periods. The impairment test for goodwill uses a two-step approach. Step one compares the estimated fair value of a reporting unit with goodwill to its carrying value. If the carrying value exceeds the estimated fair value, step two must be performed. Step two compares the carrying value of the reporting unit to the fair value of all of the assets and liabilities of the reporting unit (including any unrecognized intangibles) as if the reporting unit was acquired in a business combination. If the carrying amount of a reporting unit's goodwill exceeds the implied fair value of its goodwill, an impairment loss is recognized in an amount equal to the excess. As of September 30, 2014, there is no impairment of goodwill.

In connection with the merger, the Company also entered two employment agreements to the former holders of MedTel membership interests. Each agreement provides for bonus compensation of 2,000,000 shares of common stock to be earned equally upon attainment of quarterly sales and profitability goals. As of September 30, 2014, these goals have not been met.

NOTE E - CAPITAL TRANSACTIONS

Common stock:

During the nine month period ended September 30, 2014, the Company effected the following stock transactions:

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The Company received cash for the exercise of options valued at \$45,000. At September 30, 2014, the shares are authorized but not issued.

The Company issued a total of 3,000,000 shares of the Company's \$0.001 par value common stock for the purchase of MedTel Solutions, LLC on July 1, 2013.

The Company expensed \$15,000 during the nine months ended September 30, 2014 for compensation earned from shares issued during 2013.

Exercise prices and weighted-average contractual lives of stock options outstanding as of September 30, 2014, are as follows:

Exercise Prices	Options Outstanding			Options Exercisable	
	Number	Weighted Average Remaining Contractual Life	Weighted Average Exercise Prices	Number	Weighted Average Exercise Price
\$0.03-\$0.044	Outstanding 6,500,000	Life 2.63	\$0.03	Exercisable 6,500,000	\$0.03

Net Medical Xpress Solutions, Inc.

Notes to the Financial Statements

(Unaudited)

NOTE E - CAPITAL TRANSACTIONS (CONTINUED)

Summary of Options Granted and Outstanding:

	For the nine months ended	
	September 30, 2014	
	Shares	Weighted Average Exercise Price
Options:		
Outstanding at beginning of year	8,000,000	\$0.03
Granted	-	-
Cancelled	-	-
Exercised	1,500,000	-
Outstanding at end of period	6,500,000	\$0.03

NOTE F - MAJOR CUSTOMERS

During the nine month period ended September 30, 2014, two customers accounted for 36% or approximately \$1,269,000 of the Company's revenue.

As of September 30, 2014, balances due from three customers comprised 46% or approximately \$414,000 of total accounts receivable.

NOTE G - REPORTABLE SEGMENTS

Management has identified the Company's reportable segments based on separate lines of business. The parent company, Net Medical Xpress Solutions, derives revenues from the development and marketing of proprietary

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internet technology-based software. Net Medical Xpress Staffing, the Company's new division within the parent company, specializes in the recruitment and staffing of telemedicine physicians. The Company's wholly-owned subsidiary, Telerad Service, Inc., operates under the trade names Net Medical Xpress Services and Net Medical Xpress Specialists. Net Medical Xpress Services provides medical diagnostic reading services. Net Medical Xpress Specialists provides telemedicine services to hospitals and other medical entities.

Information related to the Company's reportable segments for the nine months ended September 30, 2014 is as follows:

	<u>Services</u>	<u>Specialists</u>	<u>Solutions</u>	<u>Staffing</u>	<u>TOTAL</u>
Revenue	\$2,689,000	\$448,000	\$311,000	\$88,000	\$3,536,000
Cost of Service	2,129,000	351,000	230,000	159,000	2,869,000
General & administrative	230,000	200,000	131,000	169,000	730,000
Depreciation	3,000	0	8,000	0	11,000
Research & development	0	8,000	3,000	88,000	99,000
Operating Income (loss)	\$327,000	\$(111,000)	\$(61,000)	\$(328,000)	\$(173,000)
Total assets	\$967,000	\$234,000	\$163,000	\$247,000	\$1,611,000

Net Medical Xpress Solutions, Inc.

Notes to the Financial Statements

(Unaudited)

NOTE G - REPORTABLE SEGMENTS (CONTINUED)

A reconciliation of the segments' operating loss to the consolidated net loss is as follows:

Segment s operating loss	\$ (173,000)
Other income (expense)	(12,000)
Consolidated net loss	\$ (185,000)

NOTE H - COMMITMENTS AND CONTINGENCIES

Leases:

The Company leases office space in New Mexico expiring on January 31, 2017. The Company also leases office and computer equipment. Future minimum lease payments as of September 30, 2014, are as follows:

<u>Year</u>	<u>Amount</u>
2014	\$23,000
2015	\$92,000
2016	\$94,000
2017	\$9,000

Rent expense for the nine months ended September 30, 2014 and 2013 amounted to \$61,000 and \$55,000, respectively.

Employment Agreement (Related Party):

During the first quarter of 2013, the Company entered into a new employment agreement with Mr. Govatski whereby agreeing to annual compensation of \$30,000 for a term of one year commencing on January 1, 2013. The agreement will automatically renew for one additional term unless terminated by either party. The non-compete agreement has remained intact and becomes effective only in the event of termination by either party and will remain in effect for a period of one year.

NOTE I - SUBSEQUENT EVENTS

The Company's wholly-owned subsidiary, Telerad Service, Inc., has filed suit against two customers for failure to make payments for services rendered in the amounts of approximately \$45,000 and \$39,000. At the date of this filing, no response has been received from either customer. The Company intends to vigorously pursue collection of the amounts owed.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION

OVERVIEW

We operate our business in four divisions.

Our Net Medical Xpress Services division provides medical diagnostic reading services for radiology and cardiology. We currently employ seventy licensed radiologists and twenty licensed cardiologists in this division. We use the same proprietary XR-EXpress software to provide these services to the customers of our Net Medical Xpress Solutions division.

Our Net Medical Xpress Specialists division provides telemedicine services to hospitals and other medical facilities. We currently employ fifteen credentialed specialists in the field of neurology in this division, which includes stroke and behavioral assessment. We facilitate real-time assessment of patients through a virtual examination via video conferencing, combined with our proprietary medical software. Revenues and costs in this division also include sales of our proprietary package of equipment necessary for our medical facility customers to initiate their participation in our specialists program.

Our Net Medical Xpress Solutions division derives revenues from the development and marketing of proprietary internet technology-based software. This division encompasses all revenues and costs from the software aspect of our business, including software usage, software hosting and maintenance, and custom programming (customization or modification to our core software products). Software usage and hosting include our customers who use our proprietary XR-EXpress software to provide their own radiological services. This division also occasionally derives revenue from scanning services and other services such as consulting, training and installation.

Our Net Medical Xpress Staffing division was formed as a result of the purchase of MedTel Solutions, LLC. This division specializes in the recruitment and staffing of telemedicine physicians. In addition, we are now offering home health care services - consultations with primary care physicians - in this division.

RESULTS OF OPERATIONS

TOTAL REVENUES:

For the Nine Months Ended September 30,

<u>2014</u>	<u>2013</u>	<u>Increase (Decrease)</u>	<u>Percent Inc (Dec)</u>
\$3,536,000	\$3,656,000	\$(120,000)	(3.3)%

These changes are a result of the following factors:

Net Medical Xpress Services Revenues

1. Radiological services:

For the Nine Months Ended September 30,

<u>2014</u>	<u>2013</u>	<u>Increase (Decrease)</u>	<u>Percent Inc (Dec)</u>
\$2,640,000	\$2,779,000	\$(139,000)	(5.0)%

The decrease in radiological services is due to two main factors: the loss of two medical facility customers during the third quarter accounts for approximately \$70,000 of the decrease, and a net decreased volume of reads for existing customers accounts for the remainder of the decrease.

2. Cardiological services:

For the Nine Months Ended September 30,

<u>2014</u>	<u>2013</u>	<u>Increase (Decrease)</u>	<u>Percent Inc (Dec)</u>
\$98,000	\$84,000	\$14,000	16.7%

The increase in cardiological services is due to a net increase in the volume of reads for existing customers. We have had no significant gains or losses in the number of customers for this service.

Net Medical Xpress Specialists Revenues

1. Neurological services:

For the Nine Months Ended September 30,

<u>2014</u>	<u>2013</u>	<u>Increase (Decrease)</u>	<u>Percent Inc (Dec)</u>
\$389,000	\$247,000	\$142,000	57.5%

The increase in neurological services revenue is due to the increased volume of consults from the new customers added during the second half of 2013 and the beginning of 2014. We expect this revenue to continue increasing during the remainder of 2014 as we continue to add new customers. One new development that will positively impact the revenues of this division during the fourth quarter and for the next three years is that the Center for Medicare and Medicaid Services (CMS) approved a \$15.1 million grant for the University of New Mexico, in conjunction with Net Medical Xpress, to establish a 30-hospital telehealth system in New Mexico over a three-year period. This project will help CMS study the impact of providing telemedicine for critical care services in rural areas. It will also help the participating hospitals to provide appropriate patient care in the local facility without needing patient transport to tertiary care hospitals by delivering critical cerebral emergency support services. Net Medical Xpress will supply the hardware and the software to facilitate the virtual neurological consultations.

2. Specialists program hardware sales:

For the Nine Months Ended September 30,

<u>2014</u>	<u>2013</u>	<u>Increase (Decrease)</u>	<u>Percent Inc (Dec)</u>
\$10,000	\$100,000	\$(90,000)	(90.0)%

The decrease in the specialists program hardware sales is due to the fact that we have added two new customers during the first nine months of 2014, as compared to the addition of several new customers during each quarter of 2013. The specialist program hardware sales are sales of our proprietary package of third-party equipment required for a customer to begin using our specialist services. This sale is generally a one-time event with each new customer.

Since the customers in this division are typically hospitals, the lead time required to bring on a new customer is approximately six months. This is nearly double the lead time required to bring on customers in our other divisions.

We do expect hardware sales to continue during the remainder of 2014 as we continue to add new customers. In addition, we anticipate receiving the final contract for the 30 hospitals participating in the grant described above during the fourth quarter of 2014. We will begin installing hardware in those hospitals at that time.

Net Medical Xpress Solutions Revenues

1. Software usage fees:

For the Nine Months Ended September 30,

<u>2014</u>	<u>2013</u>	<u>Increase (Decrease)</u>	<u>Percent Inc (Dec)</u>
\$270,000	\$302,000	\$(32,000)	(10.6)%

The decrease in software usage fees for the nine months ended September 30, 2014 as compared to the same period in 2013 is primarily due to variances in the volume of radiology reports generated for our existing customers. We have had no significant changes in the number of customers during 2014. These customers are using our XR-EXpress software to conduct their own businesses.

2. Software hosting and maintenance:

For the Nine Months Ended September 30,

<u>2014</u>	<u>2013</u>	<u>Increase (Decrease)</u>	<u>Percent Inc (Dec)</u>
\$40,000	\$41,000	\$(1,000)	(2.4)%

The decrease in software hosting and maintenance revenues for the nine months ended September 30, 2014 as compared to the same period in 2013 is due to rounding. Although we still have a few customers using our digital

filing cabinet (DFC) product, the majority of our customers and all of our new customers are using our XR-EXpress software. We generally charge usage fees based on radiological reports generated using XR-EXpress, which includes storage of the reports for later access by the customers, rather than monthly hosting fees. We may occasionally charge a monthly maintenance fee for new customers for the use of our XR-Express software. Software maintenance consists mainly of technical support for our medical software. We expect revenues in this category to stay relatively constant during 2014, as we continue to focus our efforts on growing our telemedicine business, particularly our specialists program.

3. Other revenues:

For the Nine Months Ended September 30,

	<u>2014</u>	<u>2013</u>	<u>Increase (Decrease)</u>	<u>Percent Inc (Dec)</u>
Bandwidth	\$1,000	\$1,000	\$0	0.0%

The bandwidth service is a charge for internet access for one customer that started during the second quarter of 2013. We do not anticipate that this service will be a major revenue generator for us in the future.

Net Medical Xpress Staffing Revenues

1. Recruiting and staffing services:

For the Nine Months Ended September 30,

<u>2014</u>	<u>2013</u>	<u>Increase (Decrease)</u>	<u>Percent Inc (Dec)</u>
\$67,000	\$101,000	\$(34,000)	(33.7)%

The decrease in recruiting and staffing revenues during the nine months ended September 30, 2014 as compared to the same period last year is due to the fact that the staffing division lost one customer during the first quarter of 2014, resulting in no revenue for the second and third quarters of 2014. This service involves locating and recruiting doctors for our customers to use in their telemedicine businesses; we then receive a fee for that service. At this time, we have recruited a significant pool of doctors that are available to provide telemedicine services. We are promoting the services of these doctors via our home health care program to potential customers such as insurance companies, human resource departments for employee programs, and underserved rural areas. Consequently, we will be focusing our efforts on growing the home health care program for the remainder of 2014 and during 2015. Therefore, we do not expect to see significant revenues solely from recruiting and staffing services in the near future.

2. Home health care services:

For the Nine Months Ended September 30,

<u>2014</u>	<u>2013</u>	<u>Increase (Decrease)</u>	<u>Percent Inc (Dec)</u>
\$21,000	\$0	\$21,000	Not meaningful

The increase in home health care service revenues during the nine months ended September 30, 2014 as compared to the same period last year is due to the fact that we started offering this service during the third quarter of 2014. In this program, we provide primary care doctors for video consultations. As mentioned above, we are marketing this program to a variety of potential customers. One area of emphasis will be to provide affordable primary care services to individuals with high-deductible insurance plans. We expect these revenues to increase during the remainder of 2014 and during 2015 as the existing new customers expand their businesses, and as we continue to add new customers.

COST OF SERVICES:

For the Nine Months Ended September 30,

<u>2014</u>	<u>2013</u>	<u>Increase (Decrease)</u>	<u>Percent Inc (Dec)</u>
\$2,869,000	\$2,752,000	\$117,000	4.3%

The increase in cost of services for both the quarter and the nine months ended September 30, 2014 as compared to the same periods last year is primarily due to the addition of the staffing division resulting from the purchase of MedTel Solutions, LLC on July 1, 2013. Approximately eighty percent of the costs of services for the first nine months of 2014 are direct costs related to the services, specialists and staffing divisions. These costs consist of radiologist fees, cardiologist fees, neurologist fees, as well as engineering and customer service staff expenses. The majority of these costs are directly related to revenues.

GENERAL AND ADMINISTRATIVE EXPENSES:

For the Nine Months Ended September 30,

<u>2014</u>	<u>2013</u>	<u>Increase (Decrease)</u>	<u>Percent Inc (Dec)</u>
\$730,000	\$707,000	\$23,000	3.3%

Approximately 50% of the increase in general and administrative expenses for both the three months and the nine months ended September 30, 2014 as compared to the same periods last year is due to increased legal fees related to the FDA audit of our XR-EXpress software. This is a standard compliance audit that is required periodically for our certification. The remaining 50% is due to the addition of a sales person for the specialists program beginning in the third quarter of 2013.

RESEARCH AND DEVELOPMENT COSTS:

For the Nine Months Ended September 30,

<u>2014</u>	<u>2013</u>	<u>Increase (Decrease)</u>	<u>Percent Inc (Dec)</u>
\$99,000	\$106,000	\$(7,000)	(6.6)%

The decrease in research and development costs for the second quarter of 2014 as compared to the same period in 2013 is due to our engineers spending the majority of their time on the FDA compliance audit instead of on research and development. The increase in research and development costs for the first nine months of 2014 compared to the same period in 2013 is due to increased outside programming costs to continue the development and expansion of the specialists program.

During the first nine months of 2014, approximately 90% of our research and development costs were a direct result of personnel costs. In the software industry, it is common for research and development costs to be ongoing, since development of the next version of the software begins as soon as the current version is completed. In addition, we are constantly developing new applications for our existing software. We anticipate research and development costs during 2014 will continue to focus on the development and expansion of software and services for our specialists program. As a result, these costs may remain somewhat higher than usual during the coming year.

DEPRECIATION:

For the Nine Months Ended September 30,

<u>2014</u>	<u>2013</u>	<u>Increase (Decrease)</u>	<u>Percent Inc (Dec)</u>
\$11,000	\$16,000	\$(5,000)	(31.3)%

The decrease in depreciation expense is due to assets being fully depreciated but not replaced.

OTHER EXPENSE:

For the Nine Months Ended September 30,

	<u>2014</u>	<u>2013</u>	<u>Increase (Decrease)</u>	<u>Percent Inc (Dec)</u>
Interest expense	\$12,000	\$9,000	\$3,000	33.3%

The increase in interest expense is a result of circumstances related to the purchase of MedTel Solutions, LLC during 2013.

REPORTABLE SEGMENTS

We believe gross profit is our key indicator of operating progress. Our four operating divisions generated the following gross profit, rounded to the nearest 1,000, during the first nine months of 2014:

	<u>Services</u>	<u>Specialists</u>	<u>Solutions</u>	<u>Staffing</u>	<u>TOTAL</u>
Revenue	\$ 2,689,000	\$ 448,000	\$ 311,000	\$ 88,000	\$ 3,536,000
Direct costs	2,129,000	351,000	230,000	159,000	2,869,000
Gross profit	\$ 560,000	\$ 97,000	\$ 81,000	\$(71,000)	\$667,000
Gross Profit Percent	21%	22%	26%	(81)%	19%

The Net Medical Xpress Services division's gross profit was \$560,000, or 21%. Approximately 81% of the direct costs in this division are physician fees, which are directly related to revenues. The gross profit percentage may change slightly as the mix of services changes. In general, the majority of our revenue in this division comes from the reading of plain film (x-rays). This service produces the lowest margin relative to our other services. However, because the volume of plain film reads is many times that of our other services such as ultrasounds, MRIs or cardiological services, it would require a significant increase in the volume of our other services and/or a significant decrease in our reads of plain films to produce any significant change in our margins. Therefore, we expect this percentage to remain relatively stable during 2014.

The Net Medical Xpress Specialists division's gross profit was \$97,000, or 22%. Approximately 60% of the direct costs in this division for the first nine months of 2014 consists of physician fees, which are directly related to revenues. The remaining 40% consists of staffing and other costs such as credentialing, licensing and insurance costs, which are relatively fixed. The percentage of fixed costs should decrease as revenues increase over the next few years. This ratio is the reason for the gradual increase in gross profit percentage from 2.6% at the end of 2013 to 22% at September 30, 2014. In general, we believe the gross profit percentage of this division will continue to increase during 2014 as the revenues grow, while the fixed costs remain stable.

The Net Medical Xpress Solutions division's gross profit was \$81,000, or 26%. The majority of the direct costs in this division are software engineering staff expenses. The gross profit percentage of this division has decreased slightly during 2014 due to compliance costs related to the FDA 510(k) clearance of our PACS system.

The Net Medical Xpress Staffing division's gross profit was \$(71,000), or 81%. The staffing division lost its only customer during the first quarter of 2014. We have several new customers on contract, and we began seeing revenues from these contracts during the third quarter of 2014. The majority of the direct costs in this division are staffing

expenses. We purchased the staffing company on July 1, 2013. Since this is a relatively new operation, we anticipate the gross profit for this division to increase in the coming years as new customers are added. However, we are currently developing new projects in this division that may involve additional direct costs such as physician fees. Such changes in the type of direct costs could cause inconsistencies in the future gross profit percentages.

We expect our general and administrative expenses to increase to approximately \$250,000 to \$300,000 per quarter for the remainder of 2014 due to several factors: the addition of the staffing division during 2013, the increased credentialing requirements in the specialists division, and the development of a sales and marketing program to facilitate growth and expansion of our services and customer base.

Information related to the Company's reportable segments for the nine months ended September 30, 2014 is as follows:

	<u>Services</u>	<u>Specialists</u>	<u>Solutions</u>	<u>Staffing</u>	<u>TOTAL</u>
Revenue	\$2,689,000	\$448,000	\$311,000	\$88,000	\$3,536,000
Cost of Service	2,129,000	351,000	230,000	159,000	2,869,000
General & administrative	230,000	200,000	131,000	169,000	730,000
Depreciation	3,000	0	8,000	0	11,000
Research & development	0	8,000	3,000	88,000	99,000
Operating Income (loss)	\$327,000	\$(111,000)	\$(61,000)	\$(328,000)	\$(173,000)
Total assets	\$967,000	\$234,000	\$163,000	\$247,000	\$1,611,000

A reconciliation of the segments' operating loss to the consolidated net loss is as follows:

Segment s operating los	\$ (173,000)
Other income (expense)	<u>(12,000)</u>
Consolidated net loss	<u>\$ (185,000)</u>

LIQUIDITY AND CAPITAL RESOURCES

Liquidity refers to our ability to generate adequate amounts of cash to meet our needs for cash. We believe we will have adequate liquidity to maintain current operations during 2014, but we may choose to locate additional sources of cash to facilitate growth and expansion.

We do not currently have material commitments for capital expenditures and do not anticipate entering into any such commitments during the next twelve months. Our current commitments consist primarily of lease obligations for office space, computer equipment and office equipment.

At September 30, 2014, we had a working capital surplus of \$168,000 as opposed to a working capital surplus of \$283,000 at the beginning of the period, a decrease of \$115,000. This decrease is due to a combination of factors.

The primary factors are: a decrease of \$106,000 in available cash, an increase in deferred revenues of \$163,000, and an increase in accounts payable of \$108,000. These are offset by an increase in accounts receivable of \$277,000. We may continue to sell equity securities and incur debt if needed to meet our operating needs and facilitate growth and expansion of our services during 2014.

We anticipate that our primary uses of cash in the next year will continue to be for general operating purposes and to facilitate growth and expansion by establishing a sales and marketing program. We anticipate our operating cash requirements for the next twelve months to be in the range of \$5,000,000 to \$7,000,000. Profitability remains our primary goal.

OFF-BALANCE SHEET ARRANGEMENTS

We currently have no off-balance sheet arrangements.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of our financial statements in conformity with accounting principles generally accepted in the United States (GAAP) requires our management to make certain 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. In accordance with GAAP, our actual realized results may differ from management's initial estimates as reported. A summary of our significant accounting policies is detailed in the notes to the financial statements, which are an integral component of this filing.

Revenue Recognition

With each sale of our enterprise-level products, the end user enters into a license agreement for which an initial license fee is paid. The license agreement also provides that in order to continue the license, the licensee must pay an annual software maintenance fee for which the licensee receives access to product upgrades and bug fixes or product patches. Software maintenance consists primarily of hosting and managing our customers' data on our servers, as well as technical support programs for our products. Software usage comprises any charges for actual usage of our software.

Currently, software usage in our Net Medical Xpress Solutions division consists of fees for the use of our XR-EXpress medical software by our customers who use it to provide their own radiological reading services, billed as a fee for each report generated by our software for the customer.

Our software revenue recognition policies are in accordance with the ASC Topic 985, *Software Revenue Recognition* as amended. Revenue is recognized when (a) persuasive evidence of an arrangement exists, (b) delivery has occurred, (c) the fee is fixed or determinable, and (d) collectability is probable. We follow the guidance in ASC Topic 605, *Accounting for Performance of Construction-Type and Certain Production-Type Contracts* for custom software development arrangements that require us to provide significant production, customization or modification to our core software. Revenue is generally recognized for such arrangements under the percentage of completion method. Amounts collected prior to satisfying the above revenue recognition criteria are included in deferred revenue.

We follow the guidance provided by SEC Staff Accounting Bulletin (SAB) No. 101, *Revenue Recognition in Financial Statements* and SAB No. 104 *Revenue Recognition* which provide guidance on the recognition, presentation and disclosure of revenue in financial statements filed with the SEC. Revenue in our services and specialists divisions, software installation, training and consulting services is recognized when the services are rendered.

Software Development Costs

We account for software development costs in accordance with ASC Topic 985, *Accounting for Costs of Computer Software to be Sold, Leased, or Otherwise Marketed*. Product research and development expenses consist primarily of personnel, outside consulting and related expenses for development, and systems personnel and consultants and are charged to operations as incurred until technological feasibility is established. We consider technological feasibility to be established when all planning, designing, coding and testing have been completed to design specifications. After technological feasibility is established, costs are capitalized. Historically, product development has been substantially completed with the establishment of technological feasibility and, accordingly, no costs have been capitalized.

See Note B to our Consolidated Financial Statements for a full discussion of our critical accounting policies and estimates.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not applicable.

ITEM 4. CONTROLS AND PROCEDURES

307 - Disclosure controls and procedures: As of September 30, 2014, we carried out an evaluation of the effectiveness of our disclosure controls and procedures, with the participation of our principal executive and principal financial officers. Disclosure controls and procedures are defined in Exchange Act Rule 15d-15(e) as controls and other procedures of an issuer that are designed to ensure that information required to be disclosed by the issuer in the reports that it files or submits under the Act (15 U.S.C. 78a *et seq.*) is recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms [and] include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the Act is accumulated and communicated to the issuer's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. Based on our evaluation, our President/Chief Executive Officer and Chief Financial Officer have concluded that, as of September 30, 2014, such disclosure controls and procedures were not effective. The primary reasons for management's conclusions are that we did not have a plan in place for implementing controls and procedures and insufficient personnel to implement checks and balances. We believe that we will not have sufficient funds available to develop a plan in the foreseeable future. We do not anticipate that our business will need sufficient personnel in the foreseeable future that are needed to implement checks and balances.

308(b) - Changes in internal control over financial reporting: Based upon an evaluation by our management of our internal control over financial reporting, with the participation of our principal executive and principal financial officers, there were no changes made in our internal control over financial reporting during the quarter ended September 30, 2014 that have materially affected or are reasonably likely to materially affect this control.

Limitations on the Effectiveness of Internal Control: Our management does not expect that our disclosure controls and procedures or our internal control over financial reporting will necessarily prevent all fraud and material errors. An internal control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations on all internal control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, and/or by management override of the control. The design of any system of internal control is also based in part upon certain assumptions about risks and the likelihood of future events, and there is no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in circumstances and the degree of compliance with the policies and procedures may deteriorate. Because of the inherent limitations in a cost-effective internal control system, financial reporting misstatements due to error or fraud may occur and not be detected on a timely basis.

PART II

ITEM 1. LEGAL PROCEEDINGS

We are not engaged in any legal proceedings at the date of this report.

ITEM 1A. RISK FACTORS

We do not believe we have experienced any material changes in our risk factors subsequent to our last annual report on Form 10-K.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

The following table sets forth information about our unregistered sales of common stock during the nine months ended September 30, 2014:

<u>Class of Purchaser</u>	<u>Aggregate Number of Shares</u>
Owners of MedTel Solutions, LLC (2)	3,000,000

(1) We issued these shares in payment for purchase of the company valued at \$275,000.

We did not pay and to our knowledge no one acting on our behalf paid any commissions or other compensation with respect to the sales identified in the foregoing table. We made the sale directly to each purchaser for the consideration stated in the table. We did not receive cash proceeds directly from these sales, which reduced our cash expenses and increased our working capital as a result of using the stock to pay current obligations. Each purchaser acknowledged the investment nature of the transaction and a legend was placed on each certificate, prohibiting public resale of the shares, except in compliance with Rule 144. We believe each purchaser has either (a) such relationship with us or (b) such knowledge and experience in business and financial transactions that he or she is able to understand and evaluate the risks and merits of investment in our common stock. We relied upon the exemption from the registration requirement of the Securities Act of 1933, as amended (the Act) provided in Section 4(2) of the Act and the rules and regulations thereunder, on grounds that these sales did not involve a public offering within the meaning of the Act.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

ITEM 4. MINE SAFETY DISCLOSURE

Not applicable.

ITEM 5. OTHER INFORMATION

Not applicable.

ITEM 6. EXHIBITS

The following exhibits are attached to this report:

- 31.1 Rule 15d-14 (a) Certification by Principal Executive Officer
- 31.2 Rule 15d-14 (a) Certification by Principal Financial Officer
- 32 Section 1350 Certification of Principal Executive Officer and Principal Financial Officer

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.

NET MEDICAL XPRESS SOLUTIONS, INC.

Date: November 12, 2014

By /s/ Richard F. Govatski
Richard F. Govatski, President (Principal
Executive Officer)

Date: November 12, 2014

By /s/ Teresa B. Dickey
Teresa B. Dickey, Treasurer (Principal
Financial Officer)

