

FREESTONE RESOURCES, INC.  
Form 10-Q  
February 14, 2013

**U.S. SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 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, 2012

**OR**

**TRANSITION REPORT UNDER SECTION 13 OF 15(d) OF THE EXCHANGE ACT OF 1934**

Commission File Number 000-28753

**FREESTONE RESOURCES, INC.**

(Exact name of small business issuer as specified in its charter)

Nevada 33-0880427  
(State or other jurisdiction of incorporation or organization) (IRS Employer Identification No.)

Republic Center, Suite 1350

325 N. St. Paul Street Dallas, TX 75201

(Address of principal executive offices)

(214) 880-4870

(Issuer's telephone number)

Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 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 is a large accredited filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accredited filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act:

Large Accredited Filer  Accelerated Filer   
Non-Accredited 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

As of February 12, 2013 there were 62,743,177 shares of Common Stock of the issuer outstanding.

**Freestone Resources, Inc.****(A Development Stage Company)****Consolidated Balance Sheets****As of December 31, 2012 and June 30, 2012**

## Assets

	(Unaudited) December 31, 2012	(Audited) June 30, 2012
Current Assets:		
Cash	\$ 152,419	\$ 147,635
Accounts receivable	10,584	—
Total Current Assets	163,003	147,635
Oil and gas properties used for research and development	23,000	23,000
Fixed assets, net of accumulated depreciation of \$46,545 and \$36,040	34,007	31,512
Total fixed assets, net	57,007	54,512
Investment in Aqueous Services	99,964	—
Other assets	—	600
Total Assets	\$ 319,974	\$ 202,747

## Liabilities and Stockholders' Equity

Current Liabilities:		
Accounts payable	\$ 2,939	\$ 6,200
Accrued expenses	9,282	6,908
Notes payable-related parties	—	6,691
Investment in Freestone Water		11,978
Derivative liability - warrants	278,273	—
Stock to be issued	—	23,000
Total Current Liabilities	290,494	54,777
Long-term Liabilities:		
Asset retirement obligations	40,915	40,915
Total Liabilities	331,409	95,692

Stockholders' Equity (Deficit):

Common stock, \$.001 par value, 100,000,000 shares authorized, 62,680,677 and 58,364,010 shares issued and outstanding, respectively	62,681	58,364
Additional paid in capital	17,509,748	17,038,065
Accumulated deficit	(17,583,864)	(16,989,374)
Stockholders' Equity (Deficit)	(11,435 )	107,055
Total Liabilities and Stockholders' Equity	\$319,974	\$202,747

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

**Freestone Resources, Inc.****(A Development Stage Company)****Consolidated Statements of Operations****For the Three and Six Months Ended December 31, 2012 and 2011****And for the Period Since Reentering the Development Stage (July 1, 2011 to December 31, 2012)****(unaudited)**

	Three Months Ended December 31, 2012	Three Months Ended December 31, 2011	Six Months Ended December 31, 2012	Six Months Ended December 31, 2011	Since Reentering Developing Stage (July 1, 2011 to December 31, 2012
Revenue:					
Oil and gas revenues resulting from research activities	\$8,983	\$161	\$8,983	\$4,918	\$55,552
Total revenue resulting from research activities	8,983	161	8,983	4,918	55,552
Operating expenses:					
Lease operating costs	2,446	5,839	8,959	8,539	57,298
Depreciation	5,253	5,252	10,505	10,504	42,759
Stock Based Compensation	0	0	0	0	1,145,100
General and administrative	231,725	46,980	305,678	122,281	868,488
Total operating expenses	239,424	58,071	325,142	141,324	2,113,645
Operating loss	(230,441 )	(57,910 )	(316,159 )	(136,406 )	(2,058,093)
Other income (expense):					
Warrant expense	(278,273 )	0	(278,273 )	0	(278,273 )
Interest income (expense)	0	0	(22 )	0	(2,295 )
Gain (Loss) on sale of asset	0	0	0	0	20,541
Other income related to the settlement of EOS litigation	0	0	0	0	1,665,834
Gain (Loss) on Equity Method Investment	(36 )	0	0	0	(12,014 )
Revision to ARO estimate	0	0	(36 )	0	(6,057 )
Total other income (expense)	(278,309 )	0	(278,331 )	0	1,387,736

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Net loss	\$ (508,750 )	\$ (57,910 )	\$ (594,490 )	\$ (136,406 )	\$ (670,357 )
Basic and diluted loss per share	\$ (0.01 )	\$ 0.00	\$ (0.01 )	\$ 0.00	
Weighted average shares outstanding:					
Basic and diluted	62,183,304	52,598,629	62,002,597	52,555,695	

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

**Freestone Resources, Inc.****(A Development Stage Company)****Consolidated Statement of Stockholders' Equity****For the Period Since Reentering the Development Stage (July 1, 2011 to September 30, 2012)****And the Six Months Ended December 31, 2012****(Unaudited)**

	Common Stock	Additional	Accumulated		
	Shares	Amount	Paid in Capital	Deficit	Total
Balance, June 30, 2011	52,512,760	\$ 52,513	\$ 16,538,716	\$(16,492,116)	\$99,113
Common stock issued for cash	3,701,250	3,701	310,399	—	314,100
Common stock issued for services	2,450,000	2,450	188,650	—	191,100
Common stock canceled for Hydrex agreement	(300,000 )	(300 )	300	—	----
Net loss	—	—	—	(497,258 )	(497,258)
Balance, June 30, 2012	58,364,010	\$ 58,364	\$ 17,038,065	\$(16,989,374)	\$ 107,055
Common stock issued for services	600,000	600	168,400	—	169,000
Common Stock Issued for cash	3,716,667	3,717	303,283	—	307,000
Net loss				(594,490 )	(594,490)
Balance, December 31, 2012	62,680,677	\$ 62,681	\$ 17,509,748	\$(17,583,864)	\$(11,435 )

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



**Freestone Resources, Inc.****(A Development Stage Company)****Consolidated Statements of Cash Flows****Six Months Ended December 31, 2012 and 2011****And for the Period Since Reentering the Development Stage (July 1, 2011 to December 31, 2012)****(Unaudited)**

	Six Months Ended December 31, 2012	Six Months Ended December 31, 2011	Since Reentering Developing Stage (July 1, 2010 to December 31, 2012
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Net income (loss)	\$(594,490	) \$(136,406	) \$(670,357
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:			
Depreciation and amortization	10,505	10,504	42,759
Shares issued for demonstration equipment	—	—	58,585
Warrant expense	278,273	—	278,273
(Gain) on sale of investment asset	—	—	(20,541
Stock based compensation	—	—	1,145,100
Decrease in revision of ARO estimate	—	—	6,057
Shares issued for services	169,000	—	193,000
Changes in operating assets and liabilities:			
Write-off in note receivable	—	—	—
Change in account receivable	(10,584	) 2,153	11,445
Change in inventory of Petrozene	—	—	—
Change in other assets	600	(600	) 2,787
Change in accounts payable	—	(5,379	) (244,569
Change in accounts payable – related party	—	—	(150,010
Change in accrued expenses	(887	) (1,329	) (6,538
Net cash provided used in operating activities	(147,583	) (131,057	) 645,991
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>			
Sale of investment asset	—	—	30,000

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Investment in Freestone Water Solutions	(11,978	) —	—	
Investment in Aqueous Services	(99,964	) —	(99,964	)
Purchases of fixed assets	(13,000	) —	(71,585	)
Net cash used in investing activities	(124,942	) —	(141,549	)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>				
Payments on note payable	—	—	—	
Payments on note payables – related party	(6,691	) (3,243	) (34,321	)
Proceeds from sale of stock	307,000	15,000	1,065,600	
Stock returned upon settlement of litigation	—	—	(1,261,364	)
Stock to be issued	(23,000	) 84,100	(150,000	)
Net cash provided by financing activities	277,309	95,857	(380,085	)
<b>NET CHANGE IN CASH</b>	<b>4,784</b>	<b>(35,200</b>	<b>) 124,357</b>	
<b>CASH AT BEGINNING OF PERIOD</b>	<b>147,635</b>	<b>93,015</b>	<b>28,062</b>	
<b>CASH AT END OF PERIOD</b>	<b>\$ 152,419</b>	<b>57,815</b>	<b>\$ 152,419</b>	
Supplemental cash flow information:				
Cash paid for interest	\$22	\$343	\$358	
Non-cash investing activities:				
Stock returned upon settlement of litigation	\$—	\$—	\$(1,261,364	)
Stock Based Compensation	\$—	\$—	\$1,145,100	

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

**Freestone Resources, Inc.**

**(A Development Stage Company)**

**Notes to Consolidated Financial Statements**

**December 31, 2012**

**(Unaudited)**

**NOTE 1 – NATURE OF ACTIVITIES AND SIGNIFICANT ACCOUNTING POLICIES**

Nature of Activities, History and Organization:

Freestone Resources, Inc. (“Freestone” or the “Company”) is an oil and gas technology development company. The Company is located in Dallas, Texas and is incorporated under the laws of the State of Nevada.

The Company’s primary business is the development of new technologies that allow for the utilization of oil and gas resources in an environmentally responsible and cost effective way, as well as the development of technologies that can be used in the environmental cleanup of oil-based contaminant byproducts.

On November 16, 2012 the Company entered into a Company Agreement of Aqueous Services, LLC (“Aqueous”), a Texas limited liability company, with International Aqueous Investments, LLC and Pajarito W&M, LP. Aqueous is a joint venture between the Company and the two aforementioned parties, whereas the Company owns a 33.33% interest in Aqueous. Aqueous is a full water management company with access to a fresh water well that has been permitted to up to one thousand five hundred acre-feet of water per annum. A facility is being constructed near the well that is owned and operated by Aqueous for the purpose of providing water for oil and gas activities in the Eagle Ford. This site includes a designated location for the recycling frac water and produced water. The Company will account for net income (losses) from Aqueous by the equity investment method.

Development Stage Company

The Company is a development-stage company as defined in FASB Accounting Standards Codification (“ASC”) 915 “*Development Stage Enterprises*”. As of July 1, 2010 the Company reentered the development stage entity because it is devoting substantially all of its efforts to raising capital and establishing its business and principal operations, and no sales have been derived to date from its principal operations. The Company reentered the development stage due to management's decision to cease any operations of the oil separation technology licensed by Earth Oil Services, Inc. Instead, the Company began development of its own oil separation technology. The development of the aforesaid technology resulted in the need to raise additional capital for the construction and development of a prototype Oil Recovery Unit.

Unaudited Interim Financial Statements:

The accompanying unaudited interim consolidated financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America and the rules of the Securities and Exchange Commission. These financial statements are unaudited and, in the opinion of management, include all adjustments (consisting of normal recurring accruals) necessary to present fairly the balance sheet, statement of operations, statement of stockholders' equity and statement of cash flows for the periods presented in accordance with accounting principles generally accepted in the United States. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted pursuant to SEC rules and regulations. It is presumed that users of this interim financial information have read or have access to the audited financial statements and footnote disclosure for the preceding fiscal year contained in the Company's Annual Report on Form 10-K. The results of operations for the six months ended December 31, 2012 are not necessarily indicative of the results of operations for the full year or any other interim period. The information included in this Form 10-Q should be read in conjunction with Management's Discussion and Analysis and Financial Statements and notes thereto included in the Company's June 30, 2012 Form 10-K.

Significant Accounting Policies:

The Company's management selects accounting principles generally accepted in the United States of America and adopts methods for their application. The application of accounting principles requires the estimating, matching and timing of revenue and expense. It is also necessary for management to determine, measure and allocate resources and obligations within the financial process according to those principles. The accounting policies used conform to generally accepted accounting principles which have been consistently applied in the preparation of these financial statements.

The financial statements and notes are representations of the Company's management which is responsible for their integrity and objectivity. Management further acknowledges that it is solely responsible for adopting sound accounting practices, establishing and maintaining a system of internal accounting control and preventing and detecting fraud. The Company's system of internal accounting control is designed to assure, among other items, that 1) recorded transactions are valid; 2) valid transactions are recorded; and 3) transactions are recorded in the proper period in a timely manner to produce financial statements which present fairly the financial condition, results of operations and cash flows of the Company for the respective periods being presented.

#### Basis of Presentation

The Company prepares its financial statements on the accrual basis of accounting. All intercompany balances and transactions are eliminated. Investments in subsidiaries, where the Company has a controlling interest, are reported using the equity method. For those businesses that the Company does not have a controlling interest, they are accounted through the Noncontrolling Interest method. Management believes that all adjustments necessary for a fair presentation of the results of the six months ended December 31, 2012 and 2011 have been made.

The Company consolidates its subsidiaries in accordance with ASC 810, "*Business Combinations*", (formally SFAS 141R) and specifically ASC 810-10-15-8 which states, "The usual condition for a controlling financial interest is ownership of a majority voting interest, and, therefore, as a general rule ownership by one reporting entity, directly or indirectly, or over 50% of the outstanding voting shares of another entity is a condition pointing toward consolidation."

#### Use of Estimates:

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

#### Recently Issued Accounting Pronouncements:

The Company does not expect the adoption of recently issued accounting pronouncements to have a significant impact on the Company's results of operations, financial position or cash flow.

Cash and Cash Equivalents:

Cash and cash equivalents includes cash in banks with original maturities of three months or less and are stated at cost which approximates market value, which in the opinion of management, are subject to an insignificant risk of loss in value.

Revenue Recognition:

The Company recognizes revenue from the sale of products in accordance with ASC 605-15 "Revenue Recognition", (formerly Securities and Exchange Commission Staff Accounting Bulletin No. 104, "*Revenue Recognition in Financial Statements*" ("SAB 104")). Revenue will be recognized only when all of the following criteria have been met:

1. Persuasive evidence of an arrangement exists;
2. Ownership and all risks of loss have been transferred to buyer, which is generally upon shipment;
3. The price is fixed and determinable; and
4. Collectability is reasonably assured.

Revenue is recorded net any of sales taxes charged to customers.

Income Taxes:

The Company has adopted ASC 740-10 "*Income Taxes*" (formerly SFAS No. 109), which requires the use of the liability method in the computation of income tax expense and the current and deferred income taxes payable.

Earnings per Share:

Basic earnings (loss) per share are computed by dividing net income (loss) by the weighted average number of common shares outstanding for the period. Diluted earnings (loss) per share include the effects of any outstanding options, warrants and other potentially dilutive securities. For the periods presented, as there was a net loss from operations, any potentially dilutive securities would be considered anti-dilutive and have been excluded from the fully diluted shares outstanding. Therefore, primary earnings per share equals fully diluted.

Fair Value Measurements:

ASC Topic 820, “*Fair Value Measurements and Disclosures*”, defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and requires certain disclosures about fair value measurements. In general, fair value of financial instruments are based upon quoted market prices, where available. If such quoted market prices are not available, fair value is based upon internally developed models that primarily use, as inputs, observable market based parameters. Valuation adjustments may be made to ensure that financial instruments are recorded at fair value. These adjustments may include amounts to reflect counterparty credit quality and the Corporation’s credit worthiness, among other things, as well as unobservable parameters. Any such valuation adjustments are applied consistently over time.

Accounts Receivable:

Accounts Receivable are carried at their face amount, less an allowance for doubtful accounts. On a periodic basis, the Company evaluates accounts receivable and establishes the allowance for doubtful accounts based on a combination of specific customer circumstances and credit conditions, based on a history of write offs and collections. The Company’s policy is generally not to charge interest on trade receivables after the invoice becomes past due. A receivable is considered past due if payments have not been received within agreed upon invoice terms. Write offs are recorded at a time when a customer receivable is deemed uncollectible. The Company had no bad debt accruals at December 31, 2012 and June 30, 2012.

Oil and Gas Properties:

Freestone is actively purchasing marginal oil and gas properties and leasing properties that will be used in the further research and development of its oil enhancement technologies. This research focuses on the types of formations that will benefit the most from the use of the solvent, as well as the various applications from production and storage to end cycle refinement.

Equipment:

Equipment is carried at the cost of acquisition or construction and depreciated over the estimated useful lives of the assets. Costs associated with repair and maintenance are expensed as incurred. Costs associated with improvements which extend the life, increase the capacity or improve the efficiency of our property and equipment are capitalized

and depreciated over the remaining life of the related asset. Gains and losses on dispositions of equipment are reflected in operations. Depreciation and amortization are provided using the straight-line method over the estimated useful lives of the assets, which are 3 to 30 years. Oil and gas properties were purchased primarily for product testing and are depreciated over their estimated useful lives of 3 years but not reduced below estimated salvage value.

#### Impairment of Long Lived Assets

The Company evaluates, on a periodic basis, long-lived assets to be held and used for impairment in accordance with the reporting requirements of ASC 360-10, “*Accounting for the Impairment or Disposal of Long-Lived Assets*”. The evaluation is based on certain impairment indicators, such as the nature of the assets, the future economic benefit of the assets, any historical or future profitability measurements, as well as other external market conditions or factors that may be present. If these impairment indicators are present or other factors exist that indicate that the carrying amount of the asset may not be recoverable, then an estimate of the discounted value of expected future operating cash flows is used to determine whether the asset is recoverable and the amount of any impairment is measured as the difference between the carrying amount of the asset and its estimated fair value. The fair value is estimated using valuation techniques such as market prices for similar assets or discounted future operating cash flows.

#### Asset Retirement Obligation:

The Company records the fair value of a liability for asset retirement obligations (“ARO”) in the period in which an obligation is incurred and records a corresponding increase in the carrying amount of the related long-lived asset. For Freestone Resources, asset retirement obligations primarily relate to the abandonment of oil and gas properties. The present value of the estimated asset retirement cost is capitalized as part of the carrying amount of oil and gas properties. The settlement date fair value is discounted at Freestone Resource’s credit adjusted risk-free rate in determining the abandonment liability. The abandonment liability is accreted with the passage of time to its expected settlement fair value. Revisions to such estimates are recorded as adjustments to ARO and capitalized asset retirement costs and are charged to operations in the period in which they become known. At the time the abandonment cost is incurred, Freestone Resources is required to recognize a gain or loss if the actual costs do not equal the estimated costs included in ARO.

The amounts recognized for ARO are based upon numerous estimates and assumptions, including future abandonment costs, future recoverable quantities of oil and gas, future inflation rates, and the credit adjusted risk free interest rate.



**NOTE 2 – FIXED ASSETS**

Fixed assets at December 31, 2012 and June 30, 2012 are as follows:

	December 31, 2012	June 30, 2012
Computers & office furniture	\$80,552	\$67,552
Oil and gas research and development equipment	23,000	23,000
Total fixed assets	103,552	90,552
Less: Accumulated depreciation	(46,545 )	(36,040)
Total fixed assets, net of accumulated depreciation	\$57,007	\$54,512

Depreciation expense was \$5,253 for the three months ended December 31, 2012 and \$5,252 for the three months ended December 31, 2011. Depreciation expense was \$10,505 for the six months ended December 31, 2012 and \$10,504 for the six months ended December 31, 2011.

**NOTE 3 – NOTES PAYABLE - RELATED PARTIES**

On May 26, 2009, the Company received a loan from Mike Doran (“Doran”), the Company’s CEO at that time, in the amount of \$25,000. A note payable was formally prepared by the Company but never executed by Doran. The terms of the loan included an interest rate of three and a half percent, and the payment of twelve monthly installments beginning on October 31, 2009. On July 8, 2009, an amended and restated promissory note with similar terms was executed to replace the original note payable, at which time the Company recorded a \$6,200 gain on extinguishment of debt. During the year ended June 30, 2009, the Company received an advance from Doran of \$20,000 which was repaid during the year. As of December 31, 2012 and June 30, 2012 the balance owed to Mr. Doran was \$0 and \$1,691 respectively.

On July 9, 2009, the Company received an advance from James Carter, a shareholder, in the amount of \$25,000. There are no terms on the advance and no interest is paid. At December 31, 2012 and June 30 2012 the balance owed was \$0 and \$5,000, respectively.

As of June 30, 2012 the Company had a related party receivable of \$15,000 from Freestone Water Solutions, (“FWS”) a joint venture between MEA Solutions, LLC and Freestone Resources, Inc., which was created in September of 2011. Freestone did not have a controlling equity position in FWS nor did Freestone control the board or management of FWS. FWS was in the business of recycling flow back water and produced water for subsequent reuse in the fracking process. MEA and Freestone advanced FWS certain short-term, start-up cash. Profits and losses from FWS will be accounted for under the equity method and reflected as an Investment in Freestone Water Solutions on the balance sheet. As discussed in Note 14 of our June 30, 2012, 10-K, on September 4, 2012, FWS was dissolved. The receivable was written off to bad debt expense in fiscal year 2012, as it was uncollectible. On August 13, 2012 the Company advanced FWS an additional \$12,000. This was written off as of September 4, 2012. As of June 30, 2012 the Company had a liability of \$11,978 related to its negative equity investment in FWS. On September 4, 2012 the Company wrote-off this liability against the \$12,000 advance resulting in a net \$22 of write-offs.

**NOTE 4 – INCOME TAXES**

The Company has adopted ASC 740-10, “*Income Taxes*”, which requires the use of the liability method in the computation of income tax expense and the current and deferred income taxes payable (deferred tax liability) or benefit (deferred tax asset). Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized.

During the six months ended December 31, 2012 the Company had a net loss of \$594,490, increasing the deferred tax asset approximately \$107,515 at the statutory tax rate of 34%. Deferred tax assets at December 31, 2012 and June 30, 2012 consisted of the following:

Deferred tax asset related to:

	December 31, 2012	June 30, 2012
Prior Year	\$1,308,755	\$1,139,687
Tax Benefit (Expense) for Current Period	202,126	169,068
Net Operating Loss Carryforward	\$1,510,881	\$1,308,755
Less: Valuation Allowance	(1,510,881)	(1,308,755)
Net Deferred Tax Asset	\$0	\$0

The net deferred tax asset generated by the loss carryforward has been fully reserved and will expire in the years 2019 through 2030. The realization of deferred tax benefits is contingent upon future earnings and is fully reserved at December 31, 2012 and June 30, 2012.

**NOTE 5 – ASSET RETIREMENT OBLIGATION**

The Company's asset retirement obligation ("ARO") primarily represents the estimated present value of the amount Freestone Resources will incur to plug, abandon and remediate sits producing properties at the end of their productive lives, in accordance with applicable state laws. Freestone Resources determines the ARO on its oil and gas properties by calculating the present value of estimated cash flows related to the liability. At December 31, 2012, the liability for ARO was \$40,915, all of which is considered long term. The asset retirement obligations are recorded as current or non-current liabilities based on the estimated timing of the anticipated cash flows. During 2012, the Company has not recognized accretion expense, as the properties were written down to salvage value as of June 30, 2009.

**NOTE 6 – COMMITMENTS AND CONTINGENCIES**

The Company leases office space under a non-cancelable operating lease that expires in July 2014. The lease requires fixed escalations and payment of electricity costs. Rent expense, included in general and administrative expenses, totaled approximately \$14,241 and \$11,349 for the six months ended December 31, 2012 and 2011 respectively.

**NOTE 7 – EQUITY TRANSACTIONS**

The Company is authorized to issue 100,000,000 common shares at a par value of \$0.001 per share. These shares have full voting rights. At December 31, 2012 and June 30, 2012, there were 62,680,677 and 58,364,010 respectively, common shares outstanding.

During the six months ended December 31, 2012 the Company sold 3,716,667 shares at an average price of \$.0824 for a total of \$307,000. All shares have been issued as of December 31, 2012.

On November 16, 2012 the Company entered into an agreement to form Aqueous Services, LLC, a joint venture between Freestone Resources, Inc., Pajarito W&M, LP. and International Aqueous Investment, LLC for the purpose of developing a shale oil and gas water management facility in Wilson County, Texas. Each JV partner has a one-third interest and the Company is not in a position of control and will therefore account for its interest under the equity method of accounting.

As part of the agreement the Company sold 300,000 shares of common stock to each partner at par value of .001 a share. The Company treated the difference between the selling price and the fair market value of the stock as consulting expense resulting in a \$168,400 expense in the second quarter. The Company also sold each of the JV partners 500,000 warrants to purchase shares of common stock at 80% of the closing price on the exercise date. The warrants vest immediately and have a three year term from the issuance date. The Company accounted for the transaction using the Black-Scholes option pricing model and given the variable settlement price and cash settlement terms recorded an expense of \$278,273 and a resulting derivative liability. All of the derivative instruments will be accounted for under the fair value method and changes in fair value will be reflected in earnings.

**NOTE 8 – FREESTONE TECHNOLOGIES, LLC**

On October 24, 2008. Freestone established Freestone Technologies, LLC (the “Subsidiary”) in the state of Texas. The Subsidiary is wholly owned by Freestone and has certain assets and liabilities relating to the purchase of oil wells. These wells were purchased as additional test wells for Petrozene and research and development for subsequent technologies. The assets and liabilities of the Subsidiary are included in the consolidated financial statements of Freestone.

**NOTE 9 – GOING CONCERN**

As reflected in the accompanying consolidated financial statements, Freestone incurred operating losses, and has a negative working capital position as of December 31, 2012. The above factors raise substantial doubt about Freestone's ability to continue as a going concern. Freestone's continued existence is dependent on its ability to obtain additional equity and/or debt financing to fund its operations. Freestone plans to raise additional financing and to increase sales volume. There is no assurance that Freestone will obtain additional financing or achieve profitable operations or cash inflows. The consolidated financial statements do not include any adjustments relating to the recoverability or classification of recorded asset amounts or the amount and classification of liabilities that might be necessary as a result of this uncertainty.

**NOTE 10 – FAIR VALUE MEASUREMENTS**

Cash, accounts receivable, accounts payable and other accrued expenses and other current assets and liabilities are carried at amounts which reasonably approximate their fair values because of the relatively short maturity of those instruments.

Accounting Standards Codification (“ASC”) Topic 820, “*Fair Value Measurements and Disclosures*” (formally SFAS No. 157), establishes a framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy under ASC 820 are described as follows:

Level 1 - Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Company has the ability to access.

Level 2 - Inputs to the valuation methodology include:

- quoted prices for similar assets or liabilities in active markets;
- quoted prices for identical or similar assets or liabilities in inactive markets;
- inputs other than quoted prices that are observable for the asset or liability;
- inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

Level 3 - Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The asset or liability’s fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

Asset retirement obligations are recorded based on the present value of the estimated cost to retire the oil and gas properties and are depleted over the useful life of the asset. The settlement date fair value is discounted at the Company’s credit adjusted risk-free rate in determining the abandonment liability.

On November 16, 2012, the Company sold 1,000,000 warrants to purchase shares of common stock at 80% of the closing price on the exercise date. The warrants vested immediately and have a three year term from the issuance date. The Company accounted for the transaction using the Black-Scholes and given the variable settlement price and cash settlement terms, and recorded a derivative liability. The Company's derivative instruments will be accounted for under the fair value method and changes in fair value will be reflected in earnings. Due to the unobservable inputs, it is reflected as a Level 3 in the fair value hierarchy.

The preceding method described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although the Company believes its valuation method is appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date. The following table sets forth by level, within the fair value hierarchy, the Company's liabilities at fair value as of December 31, 2012:

Liabilities at Fair Value as of December 31, 2012

	Level 1	Level 2	Level 3	Total
Asset retirement obligations	\$—	—	\$40,915	\$40,915
Derivative liability	—	—	278,273	278,273
Total – Liabilities	\$—	\$—	\$319,188	\$319,188

**NOTE 12 – SUBSEQUENT EVENTS**

On January 14, 2013 the Company issued 62,500 shares of common stock at \$.08 a share. No other reportable subsequent events were noted.



## **ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS**

**This report contains forward looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended and Section 21E of the Securities Exchange Act of 1934, as amended. The Company's actual results could differ materially from those set forth on the forward looking statements as a result of the risks set forth in the Company's filings with the Securities and Exchange Commission, general economic conditions, and changes in the assumptions used in making such forward looking statements.**

### **General**

Freestone Resources, Inc. ("Freestone" or the "Company") is an oil and gas technology development company. The Company is located in Dallas, Texas and is incorporated under the laws of the State of Nevada.

The Company's primary business is the development of new technologies that allow for the utilization of oil and gas resources in an environmentally responsible and cost effective way, as well as the development of technologies that can be used in the environmental cleanup of oil-based contaminant byproducts.

On November 16, 2012 the Company entered into a Company Agreement of Aqueous Services, LLC ("Aqueous"), a Texas limited liability company, with International Aqueous Investments, LLC and Pajarito W&M, LP. Aqueous is a joint venture between the Company and the two aforementioned parties, whereas the Company owns a 33.33% interest in Aqueous. Aqueous is a full water management company with access to a fresh water well that has been permitted to up to one thousand five hundred acre-feet of water per annum. A facility is being constructed near the well that is owned and operated by Aqueous for the purpose of providing water for oil and gas activities in the Eagle Ford. This site includes a designated location for the recycling frac water and produced water. The Company will account for net income (losses) from Aqueous by the equity investment method.

### **Results of Operations**

**Three and six months Ended December 31, 2012 compared to three and six months Ended December 31, 2011**

**Revenue** - Our revenue for the three months ended December 31, 2012 was \$8,983, compared to \$161 for the same period in 2011, and for the six months ended December 31, 2012 was \$8,983 and \$4,918 for the same period in 2011. Revenue increased in the second quarter and six months ended December 31, 2011, due to increased oil and gas revenue as there was more in-field research and development activity.

**Lease Operating Expense** - Lease operating expense for the three months ended December 31, 2012 was \$2,446 compared to \$5,839 for the same period in 2011 and \$8,959 for the six months ended December 31, 2012 compared to \$8,539 for the same period in 2011.

**Operating Expense** - Total operating expenses for the three months ended December 31, 2012 were \$5,253 of depreciation expense and \$231,725 of general and administrative expenses respectively, compared to \$5,252 depreciation expense and \$46,980 of general and administrative expenses for the same period in 2011. The increased costs (\$184,745) in the three months ended December 31, 2011 were related to consulting expense of \$167,400 recognized for the issuance of stock for services related to the formation of Aqueous Services, LLC.

Total operating expenses for the six months ended December 31, 2012 were \$10,505 of depreciation expense and \$305,678 of general and administrative expenses respectively, compared to \$10,504 depreciation expense and \$122,281 of general and administrative expenses for the same period in 2011. The increased costs (\$183,397) in the six months ended December 31, 2012 were related consulting expense of \$167,400 recognized for the issuance of stock for services related to the formation of Aqueous Services, LLC.

**Net Income (Loss)** - Net loss for the three months ended December 31, 2012 was \$508,750 compared to net loss of \$57,910 for the same period in 2011. Net loss for the six months ended December 31, 2012 was \$594,490 compared to \$136,406 for the same period in 2011. The change in loss in the three and six month periods ended December 31, 2011 is mainly related to the consulting expense mention above in warrant expense of \$278,273 included in other income and expense.

### **Liquidity and Capital Resources**

We have little cash reserves and liquidity to the extent we receive it from operations and from the sale of stock.

Net cash used of the Company was \$147,583 for the six months ended December 31, 2012 compared to cash used of \$131,057 for the same period in 2011. We continue to explore working capital options and in the short-term rely on our line-of-credit and advances/loans from shareholders. During the six months ended December 31, 2011, our cash and cash equivalent increased to \$152,419 from \$147,635 at June 30, 2012 due to sales of common stock.

### **Employees**

As of December 31, 2012, Freestone had two employees.

### **Need for Additional Financing**

No commitments to provide additional funds have been made by management or other stockholders. Our independent auditors included a going concern explanatory paragraph in their report included in our annual report on Form 10-K for the year ended June 30, 2012, which raises substantial doubt about our ability to continue as a going concern.

**ITEM 3: QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Not applicable.

**ITEM 4T: CONTROLS AND PROCEDURES**

**Evaluation of Disclosure Controls and Procedures**

We carried out an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of December 31, 2012. This evaluation was accomplished under the supervision and with the participation of our chief executive officer /principal executive officer, and chief financial officer/principal financial officer who concluded that our disclosure controls and procedures are not effective.

Based upon an evaluation conducted for the period ended December 31, 2012, our Chief Executive and Chief Financial Officer as of December 31, 2012 and as of the date of this Report, has concluded that as of the end of the periods covered by this report, we have identified the following material weakness of our internal controls:

Lack of sufficient accounting staff which results in a lack of segregation of duties necessary for a good system of internal control and financial statement presentation.

### **Changes in Internal Controls over Financial Reporting**

We have not yet made any changes in our internal controls over financial reporting that occurred during the period covered by this report on Form 10-Q that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

## **PART II**

Items No. 1, 3, 4, 5 - Not Applicable.

### **Item 6 - Exhibits and Reports on Form 8-K**

(a) During the six months ended December 31, 2012 the Company filed no Form 8-Ks.

(b) Exhibits

Exhibit Number

31.1 Certification of Chief Executive Officer, pursuant to Rule 13a-14(a) of the Exchange Act, as enacted by Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of Chief Financial Officer, pursuant to Rule 13a-14(a) of the Exchange Act, as enacted by Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of Chief Executive Officer and Chief Financial Officer, pursuant to 18 United States Code Section 1350, as enacted by Section 906 of the Sarbanes-Oxley Act of 2002.

## SIGNATURES

In accordance with the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized.

FREESTONE RESOURCES, INC.

By /s/ Clayton Carter

Clayton Carter, CEO

Date: February 8, 2013

