

Recon Technology, Ltd
Form 10-Q
February 13, 2015

U. S. SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 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 December 31, 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 Number 001-34409

RECON TECHNOLOGY, LTD

(Exact name of registrant as specified in its charter)

Cayman Islands **Not Applicable**
(State or other jurisdiction of (I.R.S. employer

incorporation or organization) identification number)

1902 Building C, King Long International Mansion

No. 9 Fulin Road

Beijing 100107 China

(Address of principal executive offices and zip code)

+86 (10) 8494-5799

(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.

Large accelerated filer

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) 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

Indicate the number of shares outstanding of each of the issuer's classes of ordinary shares, as of the latest practicable date. The Company is authorized to issue 25,000,000 ordinary shares. As of February 6, 2015, the Company has issued and outstanding 4,726,711 shares.

RECON TECHNOLOGY, LTD

FORM 10-Q

INDEX

<u>Special Note Regarding Forward-Looking Statements</u>	ii
<u>Part I Financial Information</u>	2
Item 1. <u>Financial Statements (Unaudited).</u>	2
Item 2. <u>Management’s Discussion and Analysis of Financial Condition and Results of Operations.</u>	3
Item 3. <u>Quantitative and Qualitative Disclosures about Market Risk.</u>	21
Item 4. <u>Controls and Procedures.</u>	21
<u>Part II Other Information</u>	22
Item 1. <u>Legal Proceedings.</u>	22
Item 1A. <u>Risk Factors.</u>	22
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds.</u>	22
Item 3. <u>Defaults upon Senior Securities.</u>	22
Item 4. <u>Mine Safety Disclosures.</u>	22
Item 5. <u>Other Information.</u>	22
Item 6. <u>Exhibits.</u>	22

Special Note Regarding Forward-Looking Statements

This document contains certain statements of a forward-looking nature. Such forward-looking statements, including but not limited to projected growth, trends and strategies, future operating and financial results, financial expectations and current business indicators are based upon current information and expectations and are subject to change based on factors beyond the control of the Company. Forward-looking statements typically are identified by the use of terms such as “look,” “may,” “should,” “might,” “believe,” “plan,” “expect,” “anticipate,” “estimate” and similar words, although some forward-looking statements are expressed differently. The accuracy of such statements may be impacted by a number of business risks and uncertainties that could cause actual results to differ materially from those projected or anticipated, including but not limited to the following:

- the timing of the development of future products;
- projections of revenue, earnings, capital structure and other financial items;
- statements of our plans and objectives;
- statements regarding the capabilities of our business operations;
- statements of expected future economic performance;
- statements regarding competition in our market; and
- assumptions underlying statements regarding us or our business.

Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. The Company undertakes no obligation to update this forward-looking information. Nonetheless, the Company reserves the right to make such updates from time to time by press release, periodic report or other method of public disclosure without the need for specific reference to this report. No such update shall be deemed to indicate that other statements not addressed by such update remain correct or create an obligation to provide any other updates.

Part I Financial Information

Item 1. Financial Statements.

See the unaudited condensed consolidated financial statements following the signature page of this report, which are incorporated herein by reference.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

The following discussion and analysis of our company's financial condition and results of operations should be read in conjunction with our unaudited condensed consolidated financial statements and the related notes included elsewhere in this report. This discussion contains forward-looking statements that involve risks and uncertainties. Actual results and the timing of selected events could differ materially from those anticipated in these forward-looking statements as a result of various factors.

Overview

We are a company with limited liability incorporated in 2007 under the laws of the Cayman Islands. Headquartered in Beijing, we provide products and services to oil and gas companies and their affiliates through Nanjing Recon Technology Co. Ltd ("Nanjing Recon") and Beijing Recon BHD Petroleum Technology Co. Ltd ("BHD" and together with Nanjing Recon, our "Domestic Companies"). As the company contractually controlling the Domestic Companies, we are the center of strategic management, financial control and human resources allocation.

Our business is mainly focused on the upstream sectors of the oil and gas industry. We derive our revenues from the sales and provision of (1) hardware products, (2) software products, and (3) services. Our products and services involve most of the key procedures of the extraction and production of oil and gas, and include automation systems, equipment, tools and on-site technical services.

Our VIEs provide the oil and gas industry with equipment, production technologies, automation and services.

Nanjing Recon: Nanjing Recon is a high-tech company that specializes in automation services for oilfield companies. It mainly focuses on providing automation solutions to the oil exploration industry, including monitoring wells,

automatic metering to the joint station production, process monitor, and a variety of oilfield equipment and control systems.

BHD: BHD is a high-tech company that specializes in transportation equipment and stimulation productions and services. Possessing proprietary patents and substantial industry experience, BHD has built up stable and strong working relationships with the major oilfields in China.

Recent Developments

During this six-month period, affected by decreased oil prices and CAPEX expenditures of our clients, our finished projects were maintained at a lower level compared to the same period of last year. Management expects the volume of finished projects will recover and thus revenue will increase during the balance of fiscal year ending June 30, 2015. During this period, we have achieved some major accomplishments on our self-developed down-hole equipment and overseas business development.

Products and Services

We currently provide products and services to oil and gas field companies, which focus on the development and production of oil and natural gas. Our products and services described below correlate to the numbered stages of the oilfield production system graphical expression shown below.

Our products and services include:

Equipment for Oil and Gas Production and Transportation

High-Efficiency Heating Furnaces (*as shown above*). Crude petroleum contains certain impurities that must be removed before it can be sold, including water and natural gas. To remove the impurities and to prevent solidification and blockage in transport pipes, companies employ heating furnaces. BHD researched, developed and implemented a new oilfield furnace that is advanced, highly automated, reliable, easily operable, safe and highly heat-efficient (90% efficiency).

Burner (*as shown above*). We serve as an agent for the Unigas Burner, which is designed and manufactured by UNIGAS, a European burning equipment production company. The burner we provide has the following characteristics: high degree of automation, energy conservation, high turn-down ratio, high security and environmental safety.

Oil and Gas Production Improvement Techniques

Packers of Fracturing. This utility model is used in concert with the security joint, hydraulic anchor, and slide brushing of sand spray in the well. It is used for easy seat sealing and sand uptake prevention. The utility model reduces desilting volume and prevents sand-up, which makes the deblocking processes easier to realize. The back flushing is sand-stick proof.

Production Packer. At varying withdrawal points, the production packer separates different oil layers and protects the oil pipe from sand and permeation, promoting the recovery ratio.

Sand Prevention in Oil and Water Well. This technique processes additives that are resistant to elevated temperatures into “resin sand” which is transported to the bottom of the well via carrying fluid. The “resin sand” goes through the borehole, pilling up and compacting at the borehole and oil vacancy layer. An artificial borehole wall is then formed, functioning as a means of sand prevention. This sand prevention technique has been adapted to more than 100 wells, including heavy oil wells, light oil wells, water wells and gas wells, with a 100% success rate and a 98% effective

rate.

Water Locating and Plugging Technique. High water cut affects the normal production of oilfields. Previously, there was no sophisticated method for water locating and tubular column plugging in China. The mechanical water locating and tubular column plugging technique we have developed resolves the problem of high water cut wells. This technique conducts a self-sealing test during multi-stage usage and is reliable to separate different production sets effectively. The water location switch forms a complete set by which the water locating and plugging can be finished in one trip. The tubular column is adaptable to several oil drilling methods and is available for water locating and plugging in second and third class layers.

3

Fissure Shaper. This is our proprietary product that is used along with a perforating gun to effectively increase perforation depth by between 46% and 80%, shape stratum fissures, improve stratum diversion capability and, as a result, improve our ability to locate oilfields and increase the output of oil wells.

Fracture Acidizing. We inject acid to layers under pressure, which can form or expand fissures. The treatment process of the acid is defined as fracture acidizing. The technique is mainly adapted to oil and gas wells that are blocked up relatively deeply, or the ones in low permeability zones.

Electronic Break-Down Service. This service resolves block-up and freezing problems by generating heat from the electric resistivity of the drive pipe and utilizing a loop tank composed of an oil pipe and a drive pipe. This technique saves energy and is environmentally friendly. It can increase the production of oilfields that are in the middle and later periods.

Automation System and Services

Pumping Unit Controller. This controller functions as a monitor to the pumping unit and also collects data for load, pressure, voltage, and startup and shutdown control.

RTU Monitor. This monitor collects gas well pressure data.

Wireless Dynamometer and Wireless Pressure Gauge. These products replace wired technology with cordless displacement sensor technology. They are easy to install and significantly reduce the work load associated with cable laying.

Electric Multi-way Valve for Oilfield Metering Station Flow Control. This multi-way valve is used before the test separator to replace the existing three valve manifolds. It facilitates the electronic control of the connection of the oil lead pipeline with the separator.

Natural Gas Flow Computer System. The flow computer system is used in natural gas stations and gas distribution stations to measure flow.

Recon Supervisory Control and Data Acquisition System (“SCADA”). Recon SCADA is a system which applies to the oil well, measurement station, and the union station for supervision and data collection.

EPC Service of Pipeline SCADA System. This service technique is used for pipeline monitoring and data acquisition after crude oil transmission.

EPC Service of Oil and Gas Wells SCADA System. This service technique is used for monitoring and data acquisition of oil wells and natural gas wells.

EPC Service of Oilfield Video Surveillance and Control System. This video surveillance technique is used for controlling the oil and gas wellhead area and the measurement station area.

Technique Service for “Digital oilfield” Transformation. This service includes engineering technique services such as oil and gas SCADA system, video surveillance and control system and communication systems.

Factors Affecting Our Business

Business Outlook

The oilfield engineering and technical service industry is generally divided into five sections: (1) exploration, (2) drilling and completion, (3) testing and logging, (4) production, and (5) oilfield construction. Thus far our businesses have been involved in completion, production and construction processes. Our management still believe we need to expand our core business, move into new markets, and develop new businesses quickly for the coming years. Management anticipates great opportunities both in new markets and our existing markets. We also believe that many existing wells and oilfields need to improve or renew their equipment and service to maintain production and techniques and services like ours will be needed as new oil and gas fields are developed. In the next three years, we will focus on:

Measuring Equipment and Service. “Digital oil field” and the management of oil companies are highly regarded. We believe our oilfield SCADA and related technical support services will address the needs of the oil well automation system market, for which we forecast increasing demand in short term and strong needs in the long term.

Gathering and Transferring Equipment. With more new wells developed, our management anticipates that demand for our furnaces and burners will grow compared to last year, especially in the Jilin Oilfield and Xinjiang oilfield.

Fracturing service. We believe we cooperated well with Zhongyuan Oilfield in fiscal years 2013 and 2014 and expect to continue growing revenue from fracturing and related stimulation services in the coming years.

New business. Design and development of down-hole tools has always been an important technique for oilfield companies. Recently, this market has developed very rapidly. After a year long test project for our customers, we have developed experience with this technology and our customers have accepted our products and services. We expect revenue from this business in the coming year.

Growth Strategy

As a smaller company with our current customers mostly based in China, it is our basic strategy to focus on developing our onshore oilfield business, that is, the upstream of the industry. Due to the remote location and difficult environments of China’s oil and gas fields, foreign competitors rarely enter those areas.

Large domestic oil companies have historically focused on their exploration and development businesses to earn higher margins and keep their competitive advantage. With regard to private oilfield service companies, we estimate that approximately 90% specialize in the manufacture of drilling and production equipment. Thus, the market for technical support and project service is still in its early stage. Our management insists on providing high quality products and service in oilfields in which we have a geographical advantage. This will allow us to avoid conflicts of interest with bigger suppliers of drilling equipment and protect our position within the market segment. Our mission is to increase the automation and safety levels of industrial petroleum production in China and improve the underdeveloped working process and management mode by using advanced technologies. At the same time, we are always looking to improve our business and to increase our earning capability.

Recent Industry Developments

Despite uncertainty in the energy industry related to such matters as fluctuating prices and future opportunities for oil companies, our management believes there are still many factors to support our long-term development:

(1) The opening of the Chinese oil industry to participation by non-state owned service providers and vendors played an increasingly important role in the high-end oilfield service segment to allow competition based on efficiency and price. As oil and gas fields are depleted, it becomes more challenging to find and convert reserves into usable energy sources. As the industry has permitted competition by private companies and oil companies have formed separate service companies, high-tech service has gradually opened up to private companies.

(2) As worldwide oil and gas prices decreased, development transform and strict management have been recent subject of domestic oil companies. Technology reforms have been their first choice to achieve their goals about quality and efficiency upgrade. The construction of digital oilfield have also been one of oil companies' long term development strategies. Even though total capital expenditure is expected to be reduced, we believe investment in technology reform will maintain at a high level. We believe the Company will benefit from this trend.

Management is focused on these factors and will seek to extend our business on the industrial chain, including providing more integrated services and incremental measures and growing our business from a predominantly up-ground business to include some down-hole services as well.

Factors Affecting Our Results of Operations

Our operating results in any period are subject to general conditions typically affecting the Chinese oilfield service industry including:

Oil and gas price;

the amount of spending by our customers, primarily those in the oil and gas industry;

growing demand from large corporations for improved management and software designed to achieve such corporate performance;

the procurement processes of our customers, especially those in the oil and gas industry;

seasonality caused by our customers' capital expenditure planning and change of season. Generally speaking, the second quarter ending December 31 is our high season when the customers make payment to use up their budget for the calendar year; while the third quarter ending March 31 and the fourth quarter ending June 30 are generally our low seasons due to the cold weather in the oil field and the customers' pending approval of their expenditure.

competition and related pricing pressure from other oilfield service solution providers, especially those targeting the Chinese oil and gas industry;

the ongoing development of the oilfield service market in China; and

inflation and other macroeconomic factors.

Unfavorable changes in any of these general conditions could negatively affect the number and size of the projects we undertake, the number of products we sell, the amount of services we provide, the price of our products and services, and otherwise affect our results of operations.

Our operating results in any period are more directly affected by company-specific factors including:

our revenue growth, due to the high percentage of the proportion of our business dedicated to large state-owned oil and gas companies and our ability to successfully collect and recognize revenue from such large companies and develop, introduce and market new solutions and services;

our ability to increase our revenues from both old and new customers in the oil and gas industry in China;

our ability to effectively manage our operating costs and expenses; and

our ability to effectively implement any targeted acquisitions and/or strategic alliances so as to provide efficient access to markets and industries in the oil and gas industry in China.

Critical Accounting Policies and Estimates

Estimates and Assumptions

We prepare our unaudited condensed consolidated financial statements in conformity with accounting principles generally accepted in the United States of America (U.S. GAAP), which require us to make judgments, estimates and assumptions. We continually evaluate these estimates and assumptions based on the most recently available information, our own historical experience and various other assumptions that we believe to be reasonable under the circumstances. Since the use of estimates is an integral component of the financial reporting process, actual results could differ from those estimates. An accounting policy is considered critical if it requires an accounting estimate to be made based on assumptions about matters that are highly uncertain at the time such estimate is made, and if different accounting estimates that reasonably could have been used, or changes in the accounting estimates that are reasonably likely to occur periodically, could materially impact the consolidated financial statements. We believe that the following policies involve a higher degree of judgment and complexity in their application and require us to make significant accounting estimates. The following descriptions of critical accounting policies, judgments and estimates should be read in conjunction with our consolidated financial statements and other disclosures included in this quarterly report. Significant accounting estimates reflected in our Company's consolidated financial statements include revenue recognition, allowance for doubtful accounts, and useful lives of property and equipment.

Consolidation of VIEs

We recognize an entity as a VIE if it either (i) has insufficient equity to permit the entity to finance its activities without additional subordinated financial support or (ii) has equity investors who lack the characteristics of a controlling financial interest. We consolidate a VIE as its primary beneficiary when we have both the power to direct the activities that most significantly impact the entity's economic performance and the obligation to absorb losses or the right to receive benefits from the entity that could potentially be significant to the VIE. We perform ongoing assessments to determine whether an entity should be considered a VIE and whether an entity previously identified as a VIE continues to be a VIE and whether we continue to be the primary beneficiary.

Assets recognized as a result of consolidating VIEs do not represent additional assets that could be used to satisfy claims against our general assets. Conversely, liabilities recognized as a result of consolidating these VIEs do not represent additional claims on our general assets; rather, they represent claims against the specific assets of the consolidated VIEs.

Revenue Recognition

We recognize revenue when the following four criteria are met: (1) persuasive evidence of an arrangement exists, (2) delivery has occurred or services have been provided, (3) the sales price is fixed or determinable, and (4) collectability is reasonably assured. Delivery does not occur until products have been shipped or services have been provided to the customers and the customers have signed a completion and acceptance report, risk of loss has transferred to the customers, customer- acceptance-provisions have lapsed, or the Company has objective evidence that the criteria specified in customers' acceptance provisions have been satisfied. The sales price is not considered to be fixed or determinable until all contingencies related to the sale have been resolved.

Hardware

Revenue from hardware sales is generally recognized when the product is shipped to the customer and when there are no unfulfilled company obligations that affect the customer's final acceptance of the arrangement.

Software

The Company sells self-developed software. For software sales, the Company recognizes revenues in accordance with the provisions of Accounting Standards Codification, Topic 985-605, "Software Revenue Recognition," and related interpretations. Revenue from software is recognized according to project contracts. Contract costs are accumulated during the periods of installation and testing or commissioning. Usually this is short term. Revenue is not recognized until completion of the contracts and receipt of acceptance statements.

Services

The Company provides services to improve software functions and system requirements on separated fixed-price contracts. Revenue is recognized when services are completed and acceptance is determined by a completion report signed by the customer.

Deferred income represents unearned amounts billed to customers related to sales contracts.

Fair Values of Financial Instruments

The US GAAP accounting standards regarding fair value of financial instruments and related fair value measurements define fair value, establish a three-level valuation hierarchy that requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

The three levels of inputs are defined as follows:

Level 1 inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

Level 3 inputs to the valuation methodology are unobservable.

The carrying amounts reported in the consolidated balance sheets for trade accounts receivable, other receivables, advances to suppliers, trade accounts payable, accrued liabilities, advances from customers and notes payable approximate fair value because of the immediate or short-term maturity of these financial instruments. Long-term receivables and borrowings approximate fair value because their interest rates charged approximate the market rates for financial instruments with similar terms. The fair value of the warrants liability was determined using the Black-Scholes Model, as Level 2 inputs (See Note 13). Any changes in the assumptions that are used in the Black-Scholes Model may increase or decrease the warrants liability from quarter to quarter. Any change in adjustment would be charged to operations. Long-term investment is measured at fair value on a non-recurring basis at December 31, 2014, since the Company recorded an impairment loss during the year ended June 30, 2014. The fair value was determined to be zero using Level 2 inputs.

Receivables

Trade receivables are carried at original invoiced amount less a provision for any potential uncollectible amounts. Provisions are applied to trade receivables where events or changes in circumstances indicate that the balance may not be collectible. The identification of doubtful accounts requires the use of judgment and estimates of management. Our management must make estimates of the collectability of our accounts receivable. Management specifically analyzes accounts receivable, historical bad debts, customer creditworthiness, current economic trends and changes in our customer payment terms when evaluating the adequacy of the allowance for doubtful accounts. We believe based on the current economic condition and our history of collections on accounts and notes receivable, our allowance for doubtful accounts was adequate at December 31, 2014.

Deferred Tax Estimates

As part of the process of preparing our consolidated financial statements, we are required to estimate our income taxes in each of the tax jurisdictions in which we operate. This process involves using an asset and liability approach whereby deferred tax assets and liabilities are recorded for differences in the financial reporting bases and tax bases of our assets and liabilities. Deferred tax accounting requires that we evaluate net deferred tax assets by jurisdiction to determine if these assets will more likely than not be realized. This analysis requires considerable judgment and is subject to change to reflect future events and changes in the tax laws.

Valuation of Long-Lived Assets

We review the carrying values of our long-lived assets for impairment whenever events or changes in circumstances indicate that they may not be recoverable. When such an event occurs, we project undiscounted cash flows to be generated from the use of the asset and its eventual disposition over the remaining life of the asset. If projections indicate that the carrying value of the long-lived asset will not be recovered, we reduce the carrying value of the long-lived asset by the estimated excess of the carrying value over the projected discounted cash flows. In the past, we have not had to make significant adjustments to the carrying values of our long-lived assets, and we do not anticipate a need to do so in the future. However, circumstances could cause us to have to reduce the value of our capitalized assets more rapidly than we have in the past if our revenues were to significantly decline. Estimated cash flows from the use of the long-lived assets are highly uncertain and therefore the estimation of the need to impair these assets is reasonably likely to change in the future. Should the economy or acceptance of our assets change in the future, it is likely that our estimate of the future cash flows from the use of these assets will change by a material amount. There were no impairments at June 30, 2014 and December 31, 2014.

Share-Based Compensation

The Company accounts for share-based compensation in accordance with ASC Topic 718, Share-Based Payment. Under the fair value recognition provisions of this topic, share-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as expense with graded vesting on a straight-line basis over the requisite service period for the entire award. The Company has elected to recognize compensation expenses mainly using the Black-Scholes valuation model estimated at the grant date based on the award's fair value.

Recently enacted accounting pronouncements

In November 2014, The FASB issued Accounting Standards Update (ASU) No. 2014-17, "Business Combinations (Topic 805): Pushdown Accounting, a consensus of the FASB Emerging Issues Task Force, which was ratified by the Financial Accounting Standards Board (FASB) on Oct 8, 2014. ASU No. 2014-17 impacts the stand-alone financial statements of an acquired entity (subsidiary), however it does not change the requirement for an acquirer (parent) to apply business combination accounting and record its new basis in the acquired entity's assets, liabilities, and non-controlling interests in the acquirer's consolidated financial statements. The amendments in this Update are effective on November 18, 2014. After the effective date, an acquired entity can make an election to apply the guidance to future change-in-control events or to its most recent change-in-control event. Management believes this ASU No. 2014-17 does not have any significant impact on the Company's consolidated financial position and results of operations.

In January 2015, the FASB issued ASU 2015-01, "Income Statement—Extraordinary and Unusual Items (Subtopic 225-20), Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items ("ASU 2015-01"). ASU 2015-01 eliminates from GAAP the concept of extraordinary items. The amendments will eliminate the requirements in Subtopic 225-20 for reporting entities to consider whether an underlying event or transaction is extraordinary, the presentation and disclosure guidance for items that are unusual in nature or occur infrequently will be retained and will be expanded to include items that are both unusual in nature and infrequently occurring. The amendments in this Update are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. Early adoption is permitted. The impact upon adoption would not affect the Company's consolidated financial position or results of operations.

Results of Operations

The following consolidated results of operations include the results of operations of the Company and its variable interest entities (“VIEs”), BHD and Nanjing Recon.

Our historical reporting results are not necessarily indicative of the results to be expected for any future period.

Three Months Ended December 31, 2014 Compared to Three Months Ended December 31, 2013

During the three months ended December 31, 2014, we encountered worldwide decline of oil and gas prices and decreased CAPEX expense of our major clients. As a result, our projects were slowed and/or cancelled. Our operation and revenue were affected negatively.

Revenues

	For the Three Months Ended December 31,		Increase / (Decrease)	Percentage Change
	2013	2014		
Hardware - non-related parties	¥40,691,269	¥19,689,503	¥(21,001,766)	(51.6)%
Hardware - related parties	558,312	524,528	(33,784)	(6.1)%
Service	397,589	45,283	(352,306)	(88.6)%
Software - non-related parties	3,550,780	826,068	(2,724,712)	(76.7)%
Software - related parties	1,068,376	243,590	(824,786)	(77.2)%
Total revenues	¥46,266,326	¥21,328,972	¥(24,937,354)	(53.9)%

Our total revenues decreased by 53.9%, or approximately ¥24.9 million (\$4.1 million), from approximately ¥46.3 million for the three months ended December 31, 2013 to ¥21.3 million (\$3.5 million) for the same period of 2014. During the three months ended December 31, 2014, our largest customers CNPC and SINOPEC, continued to reduce their capitalized exploration and production expenditure. As a result, the number of projects we provided to these customers during this quarter decreased compared to the same period last year. In addition, we were not able to finish a number of our projects with these customers as they or their general contractors were not able to finish the overall projects which our projects are a part of. Therefore, finished projects also decreased compared to same period last year. The changes in our revenues for the three-month period were due to the following factors:

- (1) Hardware business - non related parties. During the three-month ended December 31, 2014, the decrease in hardware revenue was mainly caused by lower sales of furnaces, which are the majority of our hardware sales.

- (2) Hardware – related parties. After we achieved business entrance certification in the name of Recon and could directly enter into contract with oilfield customers directly two years ago, we no longer required the services of a related party with such certification and, accordingly, revenue from related-parties decreased. As long as the local agency continue purchasing automation products from Recon, we will continue to recognize revenue from related parties, but we anticipate that such hardware and software related party revenue is likely to fluctuate from year to year.

- (3) Service business - non related parties. Service revenue for three months ended December 31, 2014 consisted mainly of minor maintenance services, which were provided upon request by customers.

- Software business. The software sales to non-related parties decreased approximately ¥2.7 million (\$0.4 million). We record revenue as software sales if (1) the customer signs a separate software contract with us, or (2) the (4) customer accepts VAT invoices for software. The amount of our revenues categorized as software sales may fluctuate because certain software may be sold with hardware at times as a whole product and not separately priced.

Software business – related parties. During the quarter ended December 31, 2013, we recorded software revenue of ¥1.1 million to a related party. As mentioned above, we used to develop our Ji Dong oilfield business through a local agent that is a related party. Since we achieved business entrance certification by ourselves and could thus directly compete for projects, revenue through this related party decreased overall. So Software revenue from related party also decreased during this period. We reclassified some prior related party software sales to non-related because they are not a related party anymore.

Cost and Margin

	For the Three Months Ended December 31,		Increase / (Decrease)	Percentage Change
	2013	2014		
Total revenues	¥46,266,326	¥21,328,972	¥(24,937,354)	(53.9)%
Cost of revenues	29,741,914	12,351,041	(17,390,873)	(58.5)%
Gross profit	¥16,524,412	¥8,977,931	¥(7,546,481)	(45.7)%
Margin %	35.7%	42.1%	6.4%	—

Cost of revenues. Our cost of revenues includes raw materials and costs related to design, implementation, delivery and maintenance of products and services. All materials and components we need can be purchased or manufactured by subcontracts. Usually the prices of electronic components do not fluctuate dramatically due to market competition and will not significantly affect our cost of revenues. However, specialized equipment and incentive chemical products may be directly influenced by metal and oil price fluctuations. Additionally, the prices of some imported accessories mandated by our customers can also impact our cost.

Our cost of revenues decreased from approximately ¥29.7 million in the three months ended December 31, 2013 to approximately ¥12.3 million (\$2.0 million) for the same period of 2014, a decrease of approximately ¥17.4 million (\$2.8 million), or 58.5%. This decrease was mainly caused by lower revenue during the three months ended December 31, 2014 compared to the same period of 2013. As a percentage of revenues, our cost of revenues decreased from 64.3% in 2013 to 57.9% in 2014, mainly due to decreased hardware cost of revenue.

Gross profit. Our gross profit decreased to approximately ¥9.0 million (\$1.5 million) for the three months ended December 31, 2014 from approximately ¥16.5 million for the same period in 2013. Our gross profit as a percentage of revenue increased to 42.1% for the three months ended December 31, 2014 from 35.7% for the same period in 2013. This was mainly due to decreased hardware cost of revenue during the three months ended December 31, 2014 as compared to the same period last year.

In more detail:

	For the Three Months Ended December 31,		Increase / (Decrease)	Percentage Change
	2013	2014		
Total revenues-hardware and software- non related parties	¥44,242,049	¥20,515,571	¥(23,726,478)	(53.6)%
Cost of revenues -hardware and software- non related parties	29,480,982	12,334,279	(17,146,703)	(58.2)%
Gross profit	¥14,761,067	¥8,181,292	¥(6,579,775)	(44.6)%
Margin %	33.4	% 39.9	% 6.5	% —

The revenue decrease from hardware and software to non-related parties of ¥23.7 million was mainly due to the decrease from the furnaces sales and automation business in the three months ended December 31, 2014. The gross profit from the hardware and software sales to non-related parties decreased ¥6.6 million (\$1.1 million) compared to the same period of last year.

	For the Three Months Ended December 31,		Increase / (Decrease)	Percentage Change
	2013	2014		
Total revenues-hardware and software- related parties	¥1,626,688	¥768,118	¥(858,570)	(52.8)%
Cost of revenues -hardware and software - related parties	225,986	16,762	(209,224)	(92.6)%
Gross profit	¥1,400,702	¥751,356	¥(649,346)	(46.4)%
Margin %	86.1	% 97.8	% 11.7	% —

Revenue from related parties decreased was mainly due to reclassification. Besides, cost of revenue from hardware and software-related parties decreased as revenue decreased. While gross profit decreased was mainly because revenue decreased as we developed business directly with oilfield, rather than cooperation with some local agency, which used to be our related parties.

	For the Three Months Ended December 31,		Increase / (Decrease)	Percentage Change
	2013	2014		
Total revenues-service	¥397,589	¥45,283	¥(352,306)	(88.6)%
Cost of revenues -service	34,946	-	(34,946)	(100.0)%
Gross profit	¥362,643	¥45,283	¥(317,360)	(87.5)%
Margin %	91.2	% —	—	—

Service revenue for three months ended December 31, 2014 consisted mainly of minor maintenance services, which were provided upon request by customers. Our fracturing projects are still on process and not officially accepted by our clients, thus no revenue from fracturing was recorded this period.

Operating Expenses

	For the Three Months Ended December 31,		Increase /	Percentage	
	2013	2014	(Decrease)	Change	
Selling and distribution expenses	2,250,518	1,254,470	(996,048)	(44.3)	%
% of revenue	4.9 %	5.9 %	1.0 %	—	
General and administrative expenses	3,715,640	4,093,440	377,800	10.2	%
% of revenue	8.0 %	19.2 %	11.1 %	—	
Research and development expenses	2,661,397	1,243,228	(1,418,169)	(53.3)	%
% of revenue	5.8 %	5.8 %	0.1 %	—	
Operating expenses	¥8,627,555	¥6,591,138	¥(2,036,417)	(23.6)	%

Selling and distribution expenses. Selling and distribution expenses consist primarily of salaries and related expenditures of our sales and marketing organization, sales commissions, costs of our marketing programs including advertising and trade shows, and an allocation of our facilities and depreciation expenses. Selling expenses decreased by 44.3%, from approximately ¥2.3 million for the three months ended December 31, 2013 to approximately ¥1.3 million (\$0.2 million) for the same period of 2014. This decrease was primarily from decreased shipping fee, traveling expenses, and service fee. Selling expenses were 4.9% of total revenues in the three months ended December 31, 2013 and 5.9% of total revenues in the same period of 2014.

General and administrative expenses. General and administrative expenses consist primarily of costs in human resources, facilities costs, depreciation expenses, professional advisor fees, audit fees, option expenses stock based comprehensive expense and other miscellaneous expenses incurred in connection with general operations. General and administrative expenses increased by 10.2% or ¥0.4 million (\$61,000), from approximately ¥3.7 million in the three months ended December 31, 2013 to approximately ¥4.1 million (\$0.7 million) in the same period of 2014. General and administrative expenses were 8.0% of total revenues in 2013 and 19.2% of total revenues in 2014. The increase in general and administrative expenses was mainly due to increase in consulting fee, share-based compensation and traveling fees.

Research and development (“R&D”) expenses. Research and development expenses consist primarily of salaries and related expenditures of our research and development projects. Research and development expenses decreased from approximately ¥2.7 million for the three months ended December 31, 2013 to approximately ¥1.2 million (\$0.2 million) for the same period of 2014. This decrease was primarily due to the Company spending less research and development expense on furnaces.

Net Income

Edgar Filing: Recon Technology, Ltd - Form 10-Q

	For the Three Months Ended December 31,			
	2013	2014	Increase / (Decrease)	Percentage Change
Income from operations	¥7,896,857	¥2,386,793	¥(5,510,064)	(69.8)%
Interest and other income (expense)	(65,253)	3,991,943	4,057,196	(6,217.6)%
Income before income tax	7,831,604	6,378,736	(1,452,868)	(18.6)%
Provision for income tax	1,251,862	618,687	(633,175)	(50.6)%
Net income	6,579,742	5,760,049	(819,693)	(12.5)%
Less: Net income attributable to non-controlling interest	765,071	434,673	(330,398)	(43.2)%
Net income attributable to Recon Technology, Ltd	¥5,814,671	¥5,325,376	¥(489,295)	(8.4)%

Income from operations. Income from operations was approximately ¥2.4 million (\$0.4 million) for the three months ended December 31, 2014, compared to income of ¥7.9 million for the same period of 2013. This decrease in income from operations can be attributed primarily to the decreased revenue and increases in general and administrative expenses.

Interest and other income (expense). Interest and other income was approximately ¥4.0 million (\$0.7 million) for the three months ended December 31, 2014, compared to interest and other expense of ¥65,000 for the same period of 2013. The ¥4.1 million (\$0.7 million) increase in interest and other income was primarily due to changes in the fair value of warrant liability and a decrease in loss from investment.

Provision for income tax. Provision for income tax for the three months ended December 31, 2013 was approximately ¥1.3 million and ¥0.6 million (\$0.1 million) for the three months ended December 31, 2014. This decrease of provision for income tax was mainly due to the pre-consolidation income from operations in subsidiaries in China on which we must pay income tax decreased for the three months ended December 31, 2014.

Net income. As a result of the factors described above, net income was approximately ¥5.8 million (\$0.9 million) for the three months ended December 31, 2014, an decrease of approximately ¥0.9 million (\$0.1 million) from net income of ¥6.6 million for the same period of 2013.

Net income attributable to Recon Technology, Ltd. As a result of the factors described above, net income attributable to ordinary shareholders was approximately ¥5.3 million (\$0.9 million) for the three months ended December 31, 2014, an decrease of approximately ¥0.5 million (\$0.1 million) from net income attributable to ordinary shareholders of approximately ¥5.8 million for same period of 2013.

Six Months Ended December 31, 2014 Compared to Six Months Ended December 31, 2013

Revenues

	For the Six Months Ended December 31,		Increase / (Decrease)	Percentage Change
	2013	2014		
Hardware - non-related parties	¥49,865,284	¥22,709,371	¥(27,155,913)	(54.5)%
Hardware - related parties	674,785	524,528	(150,257)	(22.0)%

Edgar Filing: Recon Technology, Ltd - Form 10-Q

Service	397,589	103,774	(293,815)	100.0	%
Software - non-related parties	5,473,857	2,051,709	(3,422,148)	(62.5)%
Software - related parties	1,367,521	243,590	(1,123,931)	(82.0)%
Total revenues	¥57,779,036	¥25,632,972	¥(32,146,064)	(55.6)%

Our total revenues decreased by 55.6%, or approximately ¥32.1 million (\$5.2 million), from approximately ¥57.8 million for the six months ended December 31, 2013 to ¥25.6 million (\$4.2 million) for the same period of 2014. The changes in our revenues for the six-month period were due to the following factors:

(1) Hardware business - non related parties. During the six-month ended December 31, 2014, the decrease in hardware revenue was mainly caused by lower sales of furnaces and automation system.

Hardware – related parties. After we achieved business entrance certification in the name of Recon and could cooperate with oilfield customers directly two years ago, we no longer required the services of a related party with (2) such certification and, accordingly, revenue from related-parties decreased. As long as the local agency still purchases automation products from Recon, we will continue to recognize revenue from related parties, but we anticipate that such hardware and software related party revenue is likely to fluctuate from year to year.

(3) Service business - non related parties. Service revenue for six months ended December 31, 2014 consisted mainly of minor maintenance services, which were provided upon request by customers.

(4) Software business. The software sales to non-related parties decreased approximately ¥3.4 million (\$0.6 million), mainly caused by reclassification of some company to non-related.

Software business – related parties. During the six months ended December 31, 2013, we recorded software revenue of ¥1.4 million to a related party. We record revenue as software sales if (1) the customer signs a separate software (5) contract with us, or (2) the customer accepts VAT invoices for software. The amount of our revenues categorized as software sales may fluctuate because certain software may be sold with hardware at times as a whole product and not separately priced.

Cost and Margin

	For the Six Months Ended December 31,		Increase / (Decrease)	Percentage Change
	2013	2014		
Total revenues	¥57,779,036	¥25,632,972	¥(32,146,064)	(55.6)%
Cost of revenues	35,963,524	16,039,727	(19,923,797)	(55.4)%
Gross profit	¥21,815,512	¥9,593,245	¥(12,222,267)	(56.0)%
Margin %	37.8	% 37.4	% (0.3))% —

Cost of revenues. Our cost of revenues includes raw materials and costs related to design, implementation, delivery and maintenance of products and services. All materials and components we need can be purchased or manufactured

by subcontracts. Usually the prices of electronic components do not fluctuate dramatically due to market competition and will not significantly affect our cost of revenues. However, specialized equipment and incentive chemical products may be directly influenced by metal and oil price fluctuations. Additionally, the prices of some imported accessories mandated by our customers can also impact our cost.

Our cost of revenues decreased from approximately ¥36.0 million for the six months ended December 31, 2013 to approximately ¥16.0 million (\$2.6 million) for the same period of 2014, a decrease of approximately ¥19.9 million (\$3.2 million), or 55.4%. This decrease was mainly caused by lower revenue during the six months ended December 31, 2014 compared to the same period of 2013. As a percentage of revenues, our cost of revenues changed slightly from 62.2% in 2013 to 62.6% in 2014.

Gross profit. Our gross profit decreased to approximately ¥9.6 million (\$1.6 million) for the six months ended December 31, 2014 from approximately ¥21.8 million for the same period in 2013. Our gross profit as a percentage of revenue decreased to 37.4% for the six months ended December 31, 2014 from 37.8% for the same period in 2013. This was mainly due to decreased hardware revenue during the six months ended December 31, 2014 as compared to the same period last year when we had higher software revenue with higher gross margins during the six months ended December 31, 2013.

In more detail:

	For the Six Months Ended December 31,		Increase / (Decrease)	Percentage Change
	2013	2014		
Total revenues-hardware and software- non related parties	¥55,339,141	¥24,761,080	¥(30,578,061)	(55.3)%
Cost of revenues -hardware and software- non related parties	35,599,656	16,022,965	(19,576,691)	(55.0)%
Gross profit	¥19,739,485	¥8,738,115	¥(11,001,370)	(55.7)%
Margin %	35.7 %	35.3 %	(0.4)%	—

The revenue decrease from hardware and software to non-related parties of ¥30.6 million was mainly due to the decrease from the furnaces sales and automation business in the six months ended December 31, 2014. The gross profit from the hardware and software sales to non-related parties decreased ¥11.0 million (\$1.8 million) compared to the same period of last year.

	For the Six Months Ended December 31,		Increase / (Decrease)	Percentage Change
	2013	2014		
Total revenues-hardware and software - related parties	¥2,042,306	¥768,118	¥(1,274,188)	(62.4)%
Cost of revenues -hardware and software - related parties	328,922	16,762	(312,160)	(94.9)%
Gross profit	¥1,713,384	¥751,356	¥(962,028)	(56.1)
Margin %	83.9 %	97.8 %	13.9 %	—

Cost of revenue from hardware and software-related parties decreased as revenue decreased. The decrease in gross profit was mainly due to revenue decrease as we developed business directly with oilfield, rather than cooperation with the previous related party.

Edgar Filing: Recon Technology, Ltd - Form 10-Q

For the Six Months Ended
December 31,

	2013	2014	Increase / (Decrease)	Percentage Change	
Total revenues-service	¥397,589	¥103,774	¥(293,815)	(73.9)	%
Cost of revenues -service	34,946	-	(34,946)	100.0	%
Gross profit	¥362,643	¥103,774	¥(258,869)	(71.4)	%
Margin %	91.2	% —	—	—	

Service revenue for six months ended December 31, 2014 consisted mainly of minor maintenance services, which were provided upon request by customers.

Operating Expenses

	For the Six Months Ended		Increase / (Decrease)	Percentage	
	2013	2014		Change	
Selling and distribution expenses	3,604,440	1,955,260	(1,649,180)	(45.8))%
% of revenue	6.2	% 7.6	1.4	% —	
General and administrative expenses	6,457,563	7,796,731	1,339,168	20.7	%
% of revenue	11.2	% 30.4	19.2	% —	
Research and development expenses	3,353,997	1,899,957	(1,454,040)	(43.4))%
% of revenue	5.8	% 7.4	1.6	% —	
Operating expenses	¥13,416,000	¥11,651,948	¥(1,764,052)	(13.1))%

Selling and distribution expenses. Selling and distribution expenses consist primarily of salaries and related expenditures of our sales and marketing organization, sales commissions, costs of our marketing programs including advertising and trade shows, and an allocation of our facilities and depreciation expenses. Selling expenses decreased by 45.8%, from approximately ¥3.6 million for the six months ended December 31, 2013 to approximately ¥2.0 million (\$0.3 million) for the same period of 2014. This decrease was primarily from decreased service fee, shipping fee and traveling expenses. Selling expenses were 6.2% of total revenues in the six months ended December 31, 2013 and 7.6% of total revenues in the same period of 2014.

General and administrative expenses. General and administrative expenses consist primarily of costs in human resources, facilities costs, depreciation expenses, professional advisor fees, audit fees, option expenses stock based comprehensive expense and other miscellaneous. expenses incurred in connection with general operations. General and administrative expenses increased by 20.7%, or ¥1.3 million (\$0.2 million), from approximately ¥6.5 million in the six months ended December 31, 2013 to approximately ¥7.8 million (\$1.3 million) in the same period of 2014. General and administrative expenses were 11.2% of total revenues in 2013 and 30.4% of total revenues in 2014. The increase in general and administrative expenses was mainly due to increase in consulting fee, salaries, share-based compensation and traveling expenses.

Research and development (“R&D”) expenses. Research and development expenses consist primarily of salaries and related expenditures of our research and development projects. Research and development expenses decreased by 43.4%, from approximately ¥3.4 million for the six months ended December 31, 2013 to approximately ¥1.9 million (\$0.3 million) for the same period of 2014. This decrease was primarily due to the Company spending less research and development expenses on furnaces.

Net Income

	For the Six Months Ended December 31,		Increase / (Decrease)	Percentage Change
	2013	2014		
Income (loss) from operations	¥8,399,512	¥(2,058,703)	¥(10,458,215)	(124.5)%
Interest and other income (expense)	(154,227)	4,306,139	4,460,366	(2,892.1)%
Income before income taxes	8,245,285	2,247,436	(5,997,849)	(72.7)%
Provision for income taxes	1,459,189	648,932	(810,257)	(55.5)%
Net income	6,786,096	1,598,504	(5,187,592)	(76.4)%
Less: Net income attributable to non-controlling interest	924,981	434,673	(490,308)	(53.0)%
Net income attributable to Recon Technology, Ltd	¥5,861,115	¥1,163,831	¥(4,697,284)	(80.1)%

Income (loss) from operations. Loss from operations was approximately ¥2.1 million (\$0.3 million) for the six months ended December 31, 2014, compared to income of ¥8.4 million for the same period of 2013. This decrease in income from operations can be attributed primarily to the decreased revenue and increases in general and administrative expenses.

Interest and other income (expense). Interest and other income was approximately ¥4.3 million (\$0.7 million) for the six months ended December 31, 2014, compared to interest and other expense of ¥0.2 million for the same period of 2013. The ¥4.5 million (\$0.7 million) increase in interest and other income was primarily due to changes in the fair value of warrant liability and a decrease in loss from investment, offset by a decrease in subsidy income .

Provision for income tax. Provision for income tax for the six months ended December 31, 2013 was approximately ¥1.5 million and ¥0.6 million (\$0.1 million) for the six months ended December 31, 2014. This decrease of provision for income tax was mainly due to the pre-consolidation income from operations in subsidiaries in China on which we must pay income tax decreased for the six months ended December 31, 2014.

Net income . As a result of the factors described above, net income was approximately ¥1.6 million (\$0.3 million) for the six months ended December 31, 2014, a decrease of approximately ¥5.2 million (\$0.8 million) from net income of ¥6.8 million for the same period of 2013.

Net income attributable to Recon Technology, Ltd. As a result of the factors described above, net income attributable to ordinary shareholders was approximately ¥1.2 million (\$0.2 million) for the six months ended December 31, 2014, a decrease of approximately ¥4.7 million (\$0.8 million) from net income attributable to ordinary shareholders of approximately ¥5.9 million for same period of 2013.

Adjusted EBITDA

Adjusted EBITDA. We define adjusted EBITDA as net income (loss) adjusted for income tax expense, interest expense, loss from investment, non-cash stock compensation expense, depreciation and amortization. We think it is useful to an equity investor in evaluating our operating performance because: (1) it is widely used by investors in our industry to measure a company's operating performance without regard to items such as interest expense, depreciation and amortization, which can vary substantially from company to company depending upon accounting methods and book value of assets, capital structure and the method by which the assets were acquired; and (2) it helps investors more meaningfully evaluate and compare the results of our operations from period to period by removing the impact of our capital structure and asset base from our operating results.

Edgar Filing: Recon Technology, Ltd - Form 10-Q

	For the Six Months Ended December 31,			Increase / (Decrease)	Percentage Change
	2013 RMB	2014 RMB	2014 USD		
Reconciliation of Adjusted EBITDA to Net Income					
Net income	¥6,786,096	¥1,598,504	\$260,406	¥(5,187,592)	(76.4)%
Provision for income taxes	1,459,189	648,932	105,715	(810,257)	(55.5)%
Interest expense and foreign currency adjustment	599,040	489,836	79,796	(109,204)	(18.2)%
Change in fair value of warrants liability	(556)	(4,077,517)	(664,253)	(4,076,961)	733,266.4%
Loss from investment	735,080	-	-	(735,080)	(100.0)%
Restricted shares issued for consulting services	407,972	1,171,331	190,817	763,359	187.1%
Stock compensation expense	895,509	1,115,030	181,645	219,521	24.5%
Depreciation and amortization	301,341	274,511	44,720	(26,830)	(8.9)%
Adjusted EBITDA	¥11,183,671	¥1,220,627	\$198,846	¥(9,963,044)	(89.1)%

Adjusted EBITDA decreased by approximately ¥10 million (\$1.6 million) to approximately income of ¥1.2 million (\$0.2 million) for the six months ended December 31, 2014 compared to approximately of ¥11.2 million income for the same period in 2013. This was due to decreased revenue and increased expenses.

Adjusted Net Income and Adjusted Earnings Per Share

	For the Six Months Ended December 31,		
	2013 RMB	2014 RMB	2014 USD
Reconciliation of Net Income attributable to Recon Technology, Ltd to Adjusted Net Income (loss) attributable to Recon Technology, Ltd			
Net income attributable to Recon Technology, Ltd	¥5,861,115	¥1,163,831	\$189,595
Noncash items ^(A) :			
Change in fair value of warrants liability	(556)	(4,077,517)	(664,253)
Loss from investment	735,080	-	-
Restricted shares issued for consulting services	407,972	1,171,331	190,817
Stock compensation expense	895,509	1,115,030	181,645
Adjusted net income(loss) attributable to Recon Technology, Ltd	¥7,899,120	¥(627,325)	\$(102,196)
Reconciliation of U.S. GAAP Earnings (loss) Per Share to Non U.S. GAAP Adjusted Earnings (loss) Per Share			
U.S. GAAP earnings per share	¥1.44	¥0.24	\$0.04
Impact of special items on earnings per share	0.50	(0.37)	(0.06)
Non U.S. GAAP adjusted earnings per share	¥1.94	¥(0.13)	\$(0.02)
Weighted - average shares -diluted	4,056,963	4,846,270	4,846,270

(A) Noncash items are certain expenses that are included in our U.S. GAAP reported results. There was no income tax benefit associated with the noncash items. The non-GAAP financial measures are provided to enhance investors' overall understanding of Recon's current financial performance.

(A) Noncash items are certain non-cash expenses that are included in our U.S. GAAP reported results. There was no income tax benefit associated with the special items. The non-GAAP financial measures are provided to enhance investors' overall understanding of Recon's current financial performance.

Liquidity and Capital Resources

Cash and Cash Equivalents. Cash and cash equivalents are comprised of cash on hand, demand deposits and highly liquid short-term debt investments with stated maturities of no more than six months. As of December 31, 2014, we had cash and cash equivalents in the amount of approximately ¥5.0 million (\$0.8 million).

Indebtedness. As of December 31, 2014, except for approximately ¥9.6 million (\$1.6 million) of short-term borrowings from related parties, and ¥8.0 million (\$1.3 million) in commercial loans from local banks, we did not have any finance leases or purchase commitments, guarantees or other material contingent liabilities.

Holding Company Structure. We are a holding company with no operations of our own. All of our operations are conducted through our Domestic Companies. As a result, our ability to pay dividends and to finance any debt that we may incur is dependent upon the receipt of dividends and other distributions from the Domestic Companies. In addition, Chinese legal restrictions permit payment of dividends to us by our Domestic Companies only out of their respective accumulated net profits, if any, determined in accordance with Chinese accounting standards and regulations. Under Chinese law, our Domestic Companies are required to set aside a portion (at least 10%) of their after-tax net income (after discharging all cumulated loss), if any, each year for compulsory statutory reserve until the amount of the reserve reaches 50% of our Domestic Companies' registered capital. These funds may be distributed to shareholders at the time of each Domestic Company's wind up.

Off-Balance Sheet Arrangements. We have not entered into any financial guarantees or other commitments to guarantee the payment obligations of any third parties. In addition, we have not entered into any derivative contracts that are indexed to our own shares and classified as shareholders' equity, or that are not reflected in our financial statements. Furthermore, we do not have any retained or contingent interest in assets transferred to an unconsolidated entity that serves as credit, liquidity or market risk support to such entity. Moreover, we do not have any variable interest in an unconsolidated entity that provides financing, liquidity, market risk or credit support to us or engages in leasing, hedging or research and development services with us.

Capital Resources. To date we have financed our operations primarily through cash flows from operations, bank loans and short-term borrowings. As of December 31, 2014, we had total assets of approximately ¥156.1 million (\$25.4 million), which includes cash of approximately ¥5.0 million (\$0.8 million), net accounts receivable from third parties of approximately ¥50.3 million (\$8.2 million), and net accounts receivable from related parties of approximately ¥3.0

million (\$0.5 million). Working capital amounted to approximately ¥87.1 million (\$14.2 million), and shareholders' equity amounted to approximately ¥98.4 million (\$16.0 million).

Cash from Operating Activities. Net cash used in operating activities was approximately ¥15.4 million (\$2.5 million) for the six months ended December 31, 2014. This was a decrease of approximately ¥8.6 million (\$1.4 million) compared to net cash used in operating activities of approximately ¥6.8 million for the six months ended December 31, 2013. In more detail:

Net cash used in operating activities totaled approximately ¥15.4 million for the six months ended December 31, 2014, are primarily attributable to net income adjusted to reconcile to net cash provided by operating activities of ¥1.6 million, which primarily included a ¥1.2 million of restricted shares issued to consulting firm, a ¥1.1 million of share based compensation and an adjustment for a ¥4.1 million change in fair value of warrant liability. Net cash used in changes in operating assets and liabilities resulted in a net cash use of ¥15.4 million, which mainly due to a ¥4.8 million change in inventory, a ¥6.2 million change in other receivable, a ¥3.0 million change in notes receivable, a ¥1.9 million change in prepaid expense, a ¥2.5 million change in accounts receivable and a ¥1.2 million change in deferred income, offset by a ¥2.6 million change in purchase advance and a ¥1.3 million change in trade payable and other payable. Our net cash used in operating activities were primarily for purchase of inventories for projects in the upcoming quarters.

Cash from Investing Activities. Net cash used in investing activities was approximately ¥0.2 million (\$28,000) for the six months ended December 31, 2014, an increase of ¥0.1 million (\$22,000) from ¥36,000 for the same period of 2013. The increase was due to an increase in the purchase of property and equipment and offset by the proceeds from disposal of equipment.

Cash from Financing Activities. Net cash provided by financing activities amounted to ¥2.4 million (\$0.4 million) for the six months ended December 31, 2014, compared to cash flows provided by financing activities of approximately ¥16.1 million for the same period in 2013. During the six-month period ended December 31, 2014, we repaid ¥2.0 million (\$0.3 million) in short term bank loans and received ¥4.4 million (\$0.7 million) net proceeds from a related party.

Working Capital. Total working capital as of December 31, 2014 amounted to approximately ¥87.1 million (\$14.2 million), compared to approximately ¥83.1 million as of June 30, 2014. Total current assets as of December 31, 2014 amounted to approximately ¥136.1 million (\$22.2 million), an increase of approximately ¥2.7 million (\$0.4 million) compared to approximately ¥133.4 million at June 30, 2014. The increase in total current assets at December 31, 2014 compared to June 30, 2014 was mainly due to an increase in trade accounts receivable, inventory and other receivables. We expect that our current working capital is sufficient to maintain our routine operation for the next twelve months without extraordinary business expansion.

Current liabilities amounted to approximately ¥49.0 million (\$8.0 million) at December 31, 2014, in comparison to approximately ¥50.3 million at June 30, 2014. This decrease of liabilities was attributable mainly to a decrease in warrant liability and short-term bank loans, offset by an increase in trade accounts payable and short-term borrowings – related party.

Item 3. Quantitative and Qualitative Disclosures about Market Risk.

Not applicable.

Item 4. Controls and Procedures.

Disclosure Controls and Procedures

As of December 31, 2014, the company carried out an evaluation, under the supervision of and with the participation of management, including our Company's chief executive officer and chief financial officer, of the effectiveness of the

design and operation of our Company's disclosure controls and procedures. Based on the foregoing, the chief executive officer and chief financial officer concluded that our Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) were ineffective in timely alerting them to information required to be included in the Company's periodic Securities and Exchange Commission filings.

Changes in Internal Control over Financial Reporting

Management continues to focus on internal control over financial reporting. As of December 31, 2014, the Company has completed the necessary documentation of our internal controls and implemented the following remedial initiatives:

- Improved the documentation related to multiple levels of review over financial statements included in our SEC filings;

- Expanded the design and assessment test work over the monitoring function of entity level controls;
- Enhanced documentation retention policies over test work related to continuous management assessments of internal control effectiveness; and
- Expanded documentation practices and policies related to various key controls to provide support and audit trails for both internal management assessment as well as external auditor testing.

There were no changes in the Company's internal control over financial reporting (as defined in Rule 13a-15(f) of the Securities Exchange Act of 1934) during the three months ended December 31, 2014 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting, except as disclosed above.

Part II Other Information

Item 1. Legal Proceedings.

None.

Item 1A. Risk Factors.

Not applicable.

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

(a)None

(b)None

(c)None

Item 3. Defaults upon Senior Securities.

None.

Item 4. Mine Safety Disclosures.

Not applicable.

Item 5. Other Information.

None.

Item 6. Exhibits.

The following exhibits are filed herewith:

22

Exhibit Number	Document
3.1	Amended and Restated Articles of Association of the Registrant ⁽¹⁾
3.2	Amended and Restated Memorandum of Association of the Registrant ⁽¹⁾
4.1	Specimen Share Certificate ⁽¹⁾
10.1	Translation of Exclusive Technical Consulting Service Agreement between Recon Technology (Jining) Co., Ltd. and Beijing BHD Petroleum Technology Co., Ltd. ⁽¹⁾
10.2	Translation of Power of Attorney for rights of Chen Guangqiang in Beijing BHD Petroleum Technology Co., Ltd. ⁽¹⁾
10.3	Translation of Power of Attorney for rights of Yin Shenping in Beijing BHD Petroleum Technology Co., Ltd. ⁽¹⁾
10.4	Translation of Power of Attorney for rights of Li Hongqi in Beijing BHD Petroleum Technology Co., Ltd. ⁽¹⁾
10.5	Translation of Exclusive Equity Interest Purchase Agreement between Recon Technology (Jining) Co. Ltd., Chen Guangqiang and Beijing BHD Petroleum Technology Co., Ltd. ⁽¹⁾
10.6	Translation of Exclusive Equity Interest Purchase Agreement between Recon Technology (Jining) Co. Ltd., Yin Shenping and Beijing BHD Petroleum Technology Co., Ltd. ⁽¹⁾
10.7	Translation of Exclusive Equity Interest Purchase Agreement between Recon Technology (Jining) Co. Ltd., Li Hongqi and Beijing BHD Petroleum Technology Co., Ltd. ⁽¹⁾
10.8	Translation of Equity Interest Pledge Agreement between Recon Technology (Jining) Co., Ltd., Chen Guangqiang and Beijing BHD Petroleum Technology Co., Ltd. ⁽¹⁾
10.9	Translation of Equity Interest Pledge Agreement between Recon Technology (Jining) Co., Ltd., Yin Shenping and Beijing BHD Petroleum Technology Co., Ltd. ⁽¹⁾
10.10	Translation of Equity Interest Pledge Agreement between Recon Technology (Jining) Co., Ltd., Li Hongqi and Beijing BHD Petroleum Technology Co., Ltd. ⁽¹⁾
10.11	Translation of Exclusive Technical Consulting Service Agreement between Recon Technology (Jining) Co., Ltd. and Jining ENI Energy Technology Co., Ltd. ⁽¹⁾
10.12	Translation of Power of Attorney for rights of Chen Guangqiang in Jining ENI Energy Technology Co., Ltd. ⁽¹⁾
10.13	Translation of Power of Attorney for rights of Yin Shenping in Jining ENI Energy Technology Co., Ltd. ⁽¹⁾

Edgar Filing: Recon Technology, Ltd - Form 10-Q

- 10.14 Translation of Power of Attorney for rights of Li Hongqi in Jining ENI Energy Technology Co., Ltd. ⁽¹⁾
- 10.15 Translation of Exclusive Equity Interest Purchase Agreement between Recon Technology (Jining) Co. Ltd., Chen Guangqiang and Jining ENI Energy Technology Co., Ltd. ⁽¹⁾
- 10.16 Translation of Exclusive Equity Interest Purchase Agreement between Recon Technology (Jining) Co. Ltd., Yin Shenping and Jining ENI Energy Technology Co., Ltd. ⁽¹⁾
- 10.17 Translation of Exclusive Equity Interest Purchase Agreement between Recon Technology (Jining) Co. Ltd., Li Hongqi and Jining ENI Energy Technology Co., Ltd. ⁽¹⁾

23

- 10.18 Translation of Equity Interest Pledge Agreement between Recon Technology (Jining) Co., Ltd., Chen Guangqiang and Jining ENI Energy Technology Co., Ltd. ⁽¹⁾
- 10.19 Translation of Equity Interest Pledge Agreement between Recon Technology (Jining) Co., Ltd., Yin Shenping and Jining ENI Energy Technology Co., Ltd. ⁽¹⁾
- 10.20 Translation of Equity Interest Pledge Agreement between Recon Technology (Jining) Co., Ltd., Li Hongqi and Jining ENI Energy Technology Co., Ltd. ⁽¹⁾
- 10.21 Translation of Exclusive Technical Consulting Service Agreement between Recon Technology (Jining) Co., Ltd. and Nanjing Recon Technology Co., Ltd. ⁽¹⁾
- 10.22 Translation of Power of Attorney for rights of Chen Guangqiang in Nanjing Recon Technology Co., Ltd. ⁽¹⁾
- 10.23 Translation of Power of Attorney for rights of Yin Shenping in Nanjing Recon Technology Co., Ltd. ⁽¹⁾
- 10.24 Translation of Power of Attorney for rights of Li Hongqi in Nanjing Recon Technology Co., Ltd. ⁽¹⁾
- 10.25 Translation of Exclusive Equity Interest Purchase Agreement between Recon Technology (Jining) Co. Ltd., Chen Guangqiang and Nanjing Recon Technology Co., Ltd. ⁽¹⁾
- 10.26 Translation of Exclusive Equity Interest Purchase Agreement between Recon Technology (Jining) Co. Ltd., Yin Shenping and Nanjing Recon Technology Co., Ltd. ⁽¹⁾
- 10.27 Translation of Exclusive Equity Interest Purchase Agreement between Recon Technology (Jining) Co. Ltd., Li Hongqi and Nanjing Recon Technology Co., Ltd. ⁽¹⁾
- 10.28 Translation of Equity Interest Pledge Agreement between Recon Technology (Jining) Co., Ltd., Chen Guangqiang and Nanjing Recon Technology Co., Ltd. ⁽¹⁾
- 10.29 Translation of Equity Interest Pledge Agreement between Recon Technology (Jining) Co., Ltd., Li Hongqi and Nanjing Recon Technology Co., Ltd. ⁽¹⁾
- 10.30 Employment Agreement between Recon Technology (Jining) Co., Ltd. and Mr. Yin Shenping ⁽¹⁾
- 10.31 Employment Agreement between Recon Technology (Jining) Co., Ltd. and Mr. Chen Guangqiang ⁽¹⁾
- 10.32 Employment Agreement between Recon Technology (Jining) Co., Ltd. and Mr. Li Hongqi ⁽¹⁾
- 10.33 Operating Agreement among Recon Technology (Jining) Co. Ltd., Nanjing Recon Technology Co., Ltd. and Mr. Yin Shenping, Mr. Chen Guangqiang and Mr. Li Hongqi ⁽¹⁾
- 10.34 Operating Agreement among Recon Technology (Jining) Co. Ltd., Jining ENI Energy Technology Co., Ltd., and Mr. Yin Shenping, Mr. Chen Guangqiang and Mr. Li Hongqi ⁽¹⁾
- 10.35 Operating Agreement among Recon Technology (Jining) Co. Ltd., Beijing BHD and Mr. Yin Shenping, Mr. Chen Guangqiang and Mr. Li Hongqi ⁽¹⁾

10.36 Form of Warrant Exchange Agreement by and among the Company and certain warrant holders dated February 13, 2015.(3)

21.1 Subsidiaries of the Registrant ⁽²⁾

99.1 Stock Option Plan ⁽¹⁾

24

99.2 Code of Business Conduct and Ethics ⁽¹⁾

31.1 Certifications pursuant to Rule 13a-14(a) or 15d-14(a) under the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. ⁽³⁾

31.2 Certifications pursuant to Rule 13a-14(a) or 15d-14(a) under the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. ⁽³⁾

32.1 Certifications pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. ⁽³⁾

32.1 Certifications pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. ⁽³⁾

101.INS XBRL Instance Document ⁽³⁾

101.SCH XBRL Taxonomy Extension Schema Document ⁽³⁾

101.CAL XBRL Taxonomy Extension Calculation Linkbase Document ⁽³⁾

101.LAB XBRL Taxonomy Extension Label Linkbase Document ⁽³⁾

101.PRE XBRL Taxonomy Extension Presentation Linkbase Document ⁽³⁾

101.DEF XBRL Taxonomy Extension Definition Linkbase Document ⁽³⁾

⁽¹⁾Incorporated by reference to the Company's Registration Statement on Form S-1, Registration No. 333-152964.

⁽²⁾Incorporated by reference to the Company's Quarterly Report on Form 10-Q/A, filed on January 31, 2012.

⁽³⁾Filed herewith.

SIGNATURES

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

RECON TECHNOLOGY, LTD

February 13, 2015 By: /s/ Liu Jia

Liu Jia

Chief Financial Officer

(Principal Financial and Accounting Officer)

SIGNATURES

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

**RECON TECHNOLOGY,
LTD**

February 13, 2015 By: /s/ Yin Shen ping
Yin Shen ping
Chief Executive Officer

RECON TECHNOLOGY, LTD

INDEX TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS	PAGE
<u>Unaudited Condensed Consolidated Balance Sheets as of June 30, 2014 and December 31, 2014</u>	F-2
<u>Unaudited Condensed Consolidated Statements of Operations and Comprehensive Income for the six and three months ended December 31, 2013 and 2014</u>	F-3
<u>Unaudited Condensed Consolidated Statements of Cash Flows for the six months ended December 31, 2013 and 2014</u>	F-4
<u>Notes to Unaudited Condensed Consolidated Financial Statements</u>	F-5

RECON TECHNOLOGY, LTD**UNaudited condensed Consolidated Balance Sheets**

	As of June 30, 2014 RMB	As of December 31, 2014 RMB	As of December 31, 2014 U.S. Dollars
ASSETS			
Current assets			
Cash and cash equivalents	¥ 18,094,586	¥ 4,947,964	\$ 806,054
Notes receivable	-	2,977,565	485,064
Trade accounts receivable, net	43,553,737	50,350,533	8,202,416
Trade accounts receivable- related parties, net	7,479,298	2,980,821	485,594
Inventories, net	14,336,602	19,170,009	3,122,914
Other receivables, net	18,293,043	27,201,739	4,431,333
Other receivables- related parties	1,414,433	-	-
Purchase advances, net	25,759,065	22,116,442	3,602,906
Purchase advances- related parties	394,034	394,034	64,191
Prepaid expenses	2,634,664	4,762,485	775,840
Prepaid expenses - related parties	230,000	-	-
Deferred tax asset	1,209,961	1,237,938	201,668
Total current assets	133,399,423	136,139,530	22,177,980
Property and equipment, net	1,321,538	1,368,636	222,959
Long-term trade accounts receivable, net	-	14,545,865	2,369,612
Long-term trade accounts receivable-related party, net	14,456,317	-	-
Long-term other receivable	5,353,104	4,053,933	660,411
Total Assets	¥ 154,530,382	¥ 156,107,964	\$ 25,430,962
LIABILITIES AND EQUITY			
Current liabilities			
Short-term bank loans	¥ 10,000,000	¥ 8,000,000	\$ 1,303,250
Trade accounts payable	11,413,505	12,602,016	2,052,947
Other payables	1,765,079	1,627,676	265,159
Other payable- related parties	3,306,024	3,596,762	585,935
Deferred revenue	4,419,824	3,196,427	520,718
Advances from customers	801,385	384,200	62,589
Accrued payroll and employees' welfare	417,624	284,937	46,418
Accrued expenses	203,051	212,378	34,597
Taxes payable	7,589,846	8,369,413	1,363,430
Short-term borrowings- related parties	5,207,728	9,631,504	1,569,032
Deferred tax liability	180,186	180,186	29,353
Warrants liability	5,021,621	930,480	151,581
Total current liabilities	50,325,873	49,015,979	7,985,009

Commitments and Contingency

Equity

Common stock, (\$ 0.0185 U.S. dollar par value, 25,000,000 shares authorized; 4,717,336 and 4,726,711 shares issued and outstanding as of June 30, 2014 and December 31, 2014, respectively)	616,865	617,943	100,665
Additional paid-in capital	83,061,058	84,343,979	13,740,161
Appropriated retained earnings	4,148,929	4,631,899	754,565
Unappropriated retained earnings	8,431,453	9,112,314	1,484,453
Accumulated other comprehensive loss	(279,275)	(274,549)	(44,727)
Total shareholders' equity	95,979,030	98,431,586	16,035,117
Non-controlling interest	8,225,479	8,660,399	1,410,836
Total equity	104,204,509	107,091,985	17,445,953
Total Liabilities and Equity	¥ 154,530,382	¥ 156,107,964	\$ 25,430,962

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

RECON TECHNOLOGY, LTD**UNaudited condensed Consolidated Statements of OPERATIONS and Comprehensive Income**

	For the six months ended December 31,			For the three months ended December 31,		
	2013 RMB	2014 RMB	2014 USD	2013 RMB	2014 RMB	2014 USD
Revenues						
Hardware and software	¥55,339,141	¥24,761,080	\$4,033,735	¥44,242,049	¥20,515,571	\$3,342,115
Service	397,589	103,774	16,905	397,589	45,283	7,377
Hardware and software - related parties	2,042,306	768,118	125,131	1,626,688	768,118	125,131
Total revenues	57,779,036	25,632,972	4,175,771	46,266,326	21,328,972	3,474,623
Cost of revenues						
Hardware and software	35,599,656	16,022,965	2,610,241	29,480,982	12,334,279	2,009,331
Service	34,946	-	-	34,946	-	-
Hardware and software - related parties	328,922	16,762	2,731	225,986	16,762	2,731
Total cost of revenues	35,963,524	16,039,727	2,612,972	29,741,914	12,351,041	2,012,062
Gross profit	21,815,512	9,593,245	1,562,799	16,524,412	8,977,931	1,462,561
Selling and distribution expenses	3,604,440	1,955,260	318,524	2,250,518	1,254,470	204,361
General and administrative expenses	6,457,563	7,796,731	1,270,136	3,715,640	4,093,440	666,847
Research and development expenses	3,353,997	1,899,957	309,515	2,661,397	1,243,228	202,530
Operating expenses	13,416,000	11,651,948	1,898,175	8,627,555	6,591,138	1,073,738
Income (loss) from operations	8,399,512	(2,058,703)	(335,376)	7,896,857	2,386,793	388,823
Other income (expenses)						
Subsidy income	1,018,313	484,318	78,898	684,601	269,615	43,922
Interest income	204,970	157,468	25,653	101,769	74,436	12,126
Interest expense	(479,648)	(468,956)	(76,396)	(258,389)	(227,112)	(36,998)
Loss from investment	(735,080)	-	-	(360,466)	-	-
Change in fair value of warrants liability	556	4,077,517	664,253	556	3,803,118	619,552
Loss from foreign currency exchange	(119,392)	(20,880)	(3,401)	(213,692)	(18,806)	(3,064)
Other expense	(43,946)	76,672	12,490	(19,632)	90,692	14,774
Income before income tax	8,245,285	2,247,436	366,121	7,831,604	6,378,736	1,039,135

Edgar Filing: Recon Technology, Ltd - Form 10-Q

Provision for income tax	1,459,189	648,932	105,715	1,251,862	618,687	100,788
Net Income	6,786,096	1,598,504	260,406	6,579,742	5,760,049	938,347
Less: Net income attributable to non-controlling interest	924,981	434,673	70,811	765,071	434,673	70,811
Net Income attributable to Recon Technology, Ltd	¥5,861,115	¥1,163,831	\$189,595	¥5,814,671	¥5,325,376	\$867,536
Comprehensive income						
Net income	¥6,786,096	¥1,598,504	\$260,406	¥6,579,742	¥5,760,049	\$938,347
Foreign currency translation adjustment	77,277	4,726	770	82,881	5,528	901
Comprehensive income	6,863,373	1,603,230	261,176	6,662,623	5,765,577	939,248
Less: Comprehensive income attributable to non-controlling interest	932,709	434,920	70,851	773,360	434,961	70,858
Comprehensive income attributable to Recon Technology, Ltd	¥5,930,664	¥1,168,310	\$190,325	¥5,889,263	¥5,330,616	\$868,390
Earnings per common share - basic	¥1.44	¥0.25	\$0.04	¥1.40	¥1.13	\$0.18
Earnings per common share - diluted	¥1.44	¥0.24	\$0.04	¥1.38	¥1.10	\$0.18
Weighted - average shares -basic	4,056,963	4,741,911	4,741,911	4,162,115	4,726,711	4,726,711
Weighted - average shares -diluted	4,056,963	4,846,270	4,846,270	4,224,560	4,820,817	4,820,817

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

RECON TECHNOLOGY, LTD**unaudited condensed Consolidated Statements of Cash Flows**

	For six months ended December 31,		
	2013	2014	2014
	RMB	RMB	U.S. Dollars
Cash flows from operating activities:			
Net income	¥6,786,096	¥1,598,504	\$260,406
Adjustments to reconcile net income to net cash used in operating activities:			
Depreciation	301,341	274,511	44,720
Gain from disposal of equipment	-	(149,480)	(24,351)
Provision for doubtful accounts	378,584	104,589	17,038
Share based compensation	895,509	1,115,030	181,645
Loss from investment	735,080	-	-
Deferred tax benefit	(32,211)	(27,977)	(4,558)
Change in fair value of warrants liability	(556)	(4,077,517)	(664,253)
Restricted shares issued for services	407,972	1,171,331	190,817
Changes in operating assets and liabilities:			
Notes receivable	2,578,855	(2,977,565)	(485,064)
Trade accounts receivable	(27,881,579)	(8,572,529)	(1,396,519)
Trade accounts receivable-related parties	610,501	6,104,734	994,499
Inventories	(8,799,658)	(4,833,407)	(787,392)
Other receivable, net	1,830,372	(7,635,508)	(1,243,873)
Other receivables related parties, net	147,224	1,414,433	230,420
Purchase advance, net	472,846	2,641,583	430,330
Tax recoverable	575,650	-	-
Prepaid expense	1,223,568	(2,127,821)	(346,635)
Prepaid expense - related party, net	-	230,000	37,468
Trade accounts payable	15,717,487	1,188,511	193,616
Trade accounts payable-related parties	(3,994,718)	-	-
Other payables	(556,242)	(137,403)	(22,384)
Other payables-related parties	(723,453)	290,738	47,363
Deferred income	544,754	(1,223,397)	(199,299)
Advances from customers	83,462	(417,185)	(67,962)
Accrued payroll and employees' welfare	(1,639,401)	(132,687)	(21,616)
Accrued expenses	269,270	9,327	1,519
Taxes payable	3,292,976	779,567	126,996
Net cash used in operating activities	(6,776,271)	(15,389,618)	(2,507,069)
Cash flows from investing activities:			
Purchase of property and equipment	(36,495)	(514,009)	(83,735)
Proceeds from disposal of equipment	-	341,880	55,694
Net cash used in investing activities	(36,495)	(172,129)	(28,041)

Edgar Filing: Recon Technology, Ltd - Form 10-Q

Cash flows from financing activities:			
Proceeds from short-term bank loans	15,400,000	-	-
Repayments of short-term bank loans	(6,040,000)	(2,000,000)	(325,812)
Proceeds from short-term borrowings-related parties	-	9,400,000	1,531,319
Repayment of short-term borrowings	(110,375)	-	-
Repayment of short-term borrowings-related parties	(5,303,279)	(5,000,000)	(814,531)
Proceeds from sale of common stock, net of issuance costs	12,132,882	-	-
Net cash provided by financing activities	16,079,228	2,400,000	390,976
Effect of exchange rate fluctuation on cash and cash equivalents	116,711	15,125	2,467
Net ncrease (decrease) in cash and cash equivalents	9,383,173	(13,146,622)	(2,141,667)
Cash and cash equivalents at beginning of period	12,350,392	18,094,586	2,947,721
Cash and cash equivalents at end of period	¥21,733,565	¥4,947,964	\$806,054
Supplemental cash flow information			
Cash paid during the period for interest	¥689,828	¥510,956	\$83,238
Cash paid during the period for taxes	¥-	¥203,073	\$33,082
Non-cash investing and financing activities			
Cancellation of prior issuance of 40,625 shares of common stock for professional services	-	1,002,721	163,350

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

RECON TECHNOLOGY, LTD

NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1. ORGANIZATION AND NATURE OF OPERATIONS

Organization – Recon Technology, Ltd (the “Company”) was incorporated under the laws of the Cayman Islands on August 21, 2007 as a company with limited liability. The Company provides oilfield specialized equipment, automation systems, tools, chemicals and field services to petroleum companies in the People’s Republic of China (the “PRC”). Its wholly owned subsidiary, Recon Technology Co., Limited (“Recon-HK”) was incorporated on September 6, 2007 in Hong Kong. Other than the equity interest in Recon-HK, the Company does not own any assets or conduct any operations. On November 15, 2007, Recon-HK established one wholly owned subsidiary, Jining Recon Technology Ltd. (“Recon-JN”) under the laws of the PRC. Other than the equity interest in Recon-JN, Recon-HK does not own any assets or conduct any operations. On November 19, 2011, the Company established one wholly owned subsidiary, Recon Investment Ltd. (“Recon-IN”) under the laws of HK. Other than the equity interest in Recon-IN, The Company does not own any assets or conduct any operations.

The Company conducts its business through the following PRC legal entities that were consolidated as variable interest entities (“VIEs”) and operate in the Chinese oilfield equipment & service industry:

1. Beijing BHD Petroleum Technology Co., Ltd. (“BHD”), and
2. Nanjing Recon Technology Co., Ltd. (“Nanjing Recon”).

Nature of Operations – The Company engaged in (1) providing equipment, tools and other hardware related to oilfield production and management, including simple installations in connection with some projects; (2) service to improve production and efficiency of exploited oil wells, and (3) developing and selling its own specialized industrial automation control and information solutions. The products and services provided by the Company include:

High-Efficiency Heating Furnaces - High-Efficiency Heating Furnaces are designed to remove the impurities and to prevent solidification blockage in transport pipes carrying crude petroleum. Crude petroleum contains certain impurities including water and natural gas, which must be removed before the petroleum can be sold.

Multi-Purpose Fissure Shaper - Multipurpose fissure shapers improve the extractors' ability to test for and extract petroleum which requires perforation into the earth before any petroleum extractor can test for the presence of oil.

Horizontal Multistage Fracturing related Service - The Company mainly uses Baker Hughes FracPoint™ system and provides related service to oilfield companies. The Baker Hughes FracPoint™ system provided a completion method using packers to isolate sections of the wellbore (stages) and frac sleeves to direct the frac treatment to the desired stage. The use of this type of completion eliminated the need for cementing the liner, coiled tubing operations, and wireline operations, while significantly reducing overall pumping time.

Supervisory Control and Data Acquisition System ("SCADA") - SCADA is an industrial computerized process control system for monitoring, managing and controlling petroleum extraction. SCADA integrates underground and aboveground activities of the petroleum extraction industry. This system can help to manage the oil extraction process in real-time to reduce the costs associated with extraction.

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation - The accompanying unaudited condensed consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America for interim financial information pursuant to the rules of the SEC and have been consistently applied. In the opinion of the management, all adjustments (consisting only normal recurring accruals) considered necessary for a fair presentation have been included. These financial statements should be read in conjunction with the audited financial statements and notes thereto included in the Company's Form 10-K for the fiscal year ended June 30, 2014. The results of operations for the interim periods presented may not be indicative of the operating results to be expected for the Company's fiscal year ending June 30, 2015.

Variable Interest Entities - A VIE is an entity that either (i) has insufficient equity to permit the entity to finance its activities without additional subordinated financial support or (ii) has equity investors who lack the characteristics of a controlling financial interest. A VIE is consolidated by its primary beneficiary. The primary beneficiary has both the power to direct the activities that most significantly impact the entity's economic performance and the obligation to absorb losses or the right to receive benefits from the entity that could potentially be significant to the VIE. We perform ongoing assessments to determine whether an entity should be considered a VIE and whether an entity previously identified as a VIE continues to be a VIE and whether we continue to be the primary beneficiary.

RECON TECHNOLOGY, LTD

NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Assets recognized as a result of consolidating VIEs do not represent additional assets that could be used to satisfy claims against the Company's general assets. Conversely, liabilities recognized as a result of consolidating these VIEs do not represent additional claims on the Company's general assets; rather, they represent claims against the specific assets of the consolidated VIEs.

Currency Translation - The Company's functional currency is the Chinese Yuan ("RMB") and the accompanying consolidated financial statements have been expressed in Chinese Yuan. The statements as of and for the six months period ended December 31, 2014 have been translated into United States dollars ("U.S. dollars") solely for the convenience of the readers. The translation has been made at the rate of ¥6.1385 = US\$1.00, the approximate exchange rate prevailing on December 31, 2014. These translated U.S. dollar amounts should not be construed as representing Chinese Yuan amounts or that the Chinese Yuan amounts have been or could be converted into U.S. dollars.

Estimates and assumptions- The preparation of the consolidated financial statements in conformity with U.S. GAAP requires that management make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Estimates are adjusted to reflect actual experience when necessary. Significant estimates include revenue recognition, allowance for doubtful accounts, the useful lives of property and equipment and the fair value of stock based payments. Since the use of estimates is an integral component of the financial reporting process, actual results could differ from those estimates.

Fair Values of Financial Instruments - The US GAAP accounting standards regarding fair value of financial instruments and related fair value measurements define fair value, establish a three-level valuation hierarchy that requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

The three levels of inputs are defined as follows:

Level 1 inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

Level 3 inputs to the valuation methodology are unobservable.

The carrying amounts reported in the consolidated balance sheets for trade accounts receivable, other receivables, purchase advances, trade accounts payable, accrued liabilities, advances from customers, short-term bank loan and short-term borrowings approximate fair value because of the immediate or short-term maturity of these financial instruments. Long-term borrowings approximate fair value because the interest rate charged approximates the market rate. Long-term other receivables approximate fair value because interest rate approximates the market rate. Long-term investment is carried at less than fair value, with fair value determined using level 1 inputs. (See Note 8.)

The fair value of the warrants liability was determined using the Black-Scholes Model, as Level 2 inputs (See Note 13).

Cash and Cash Equivalents - Cash and cash equivalents are comprised of cash on hand, demand deposits and highly liquid short-term debt investments with stated original maturities of no more than three months. Since a majority of the bank accounts are located in the PRC, those bank balances are uninsured.

Trade Accounts and Other Receivables - Accounts receivable are carried at original invoiced amount less a provision for any potential uncollectible amounts. Accounts are considered past due when the related receivables are more than a year old. Provision is made against trade accounts and other receivables to the extent they are considered to be doubtful. Accounts are written off after extensive efforts at collection. Other receivables arise from transactions with non-trade customers.

RECON TECHNOLOGY, LTD

NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Purchase Advances - Purchase advances are the amounts prepaid to suppliers for purchases of inventory and are recognized as inventory when the final amount is paid to the suppliers and the inventory is delivered.

Inventories - Inventories are stated at the lower of cost or market value, on a weighted average basis for BHD. Inventories are stated at the lower of cost or market value, on a first-in-first-out basis for Nanjing Recon and ENI. The methods of determining inventory costs are used consistently from year to year. Allowance for inventory obsolescence is provided when the market value of certain inventory items are lower than the cost.

Property and Equipment - Property and equipment are stated at cost. Depreciation on motor vehicles and office equipment is computed using the straight-line method over the estimated useful lives of the assets, which range from two to ten years. Leasehold improvements are amortized over the shorter of the lease term or the estimated useful life of the assets.

Long-Lived Assets - The Company applies the ASC Topic 360 "Property, plant and equipment." ASC Topic 360 requires that long-lived assets, such as property and equipment be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset or asset group may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated undiscounted future cash flows, an impairment charge is recognized for the amount by which the carrying amount of the asset exceeds the fair value of the asset. Fair value is determined based on the estimated discounted future cash flows expected to be generated by the asset. There were no impairments at June 30, 2014 and December 31, 2014.

Revenue Recognition - The Company recognizes revenue when the following four criteria are met: (1) persuasive evidence of an arrangement, (2) delivery has occurred or services have been provided, (3) the sales price is fixed or determinable, and (4) collectability is reasonably assured. Delivery does not occur until products have been shipped or services have been provided to the customers and the customers have signed a completion and acceptance report, risk of loss has transferred to the customers, customers acceptance provisions have lapsed, or the Company has objective evidence that the criteria specified in customers' acceptance provisions have been satisfied. The sales price is not considered to be fixed or determinable until all contingencies related to the sale have been resolved.

Hardware:

Edgar Filing: Recon Technology, Ltd - Form 10-Q

Revenue from hardware sales is generally recognized when the product is shipped to the customer and when there are no unfulfilled company obligations that affect the customer's final acceptance of the arrangement.

Software:

The Company sells self-developed software. For software sales, the Company recognizes revenues in accordance with ASC Topic 985 - 605 "Software Revenue Recognition". Revenue from software is recognized according to project contracts. Contract costs are accumulated during the periods of installation and testing or commissioning. Usually this is short term. Revenue is not recognized until completion of the contracts and receipt of acceptance statements.

Service:

The Company provides services to improve software function and system operation on separated fixed-price contracts. Revenue is recognized on the completed contract method when acceptance is determined by a completion report signed by the customer.

Deferred revenue represents unearned amounts billed to customers related to sales contracts.

Subsidy Income - Grants are given 1) by the government to support local software companies' operation and research and development and 2) by some local government to support development of selected middle and small-sized enterprises. Grants related to research and development projects are recognized as subsidy income in the unaudited condensed consolidated statements of operations when received. Grants in the form of value-added-tax refund for software products are recognized when received.

RECON TECHNOLOGY, LTD

NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Share-Based Compensation - The Company accounts for share-based compensation in accordance with ASC Topic 718, *Share-Based Payment*. Under the fair value recognition provisions of this topic, share-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as expense with graded vesting on a straight-line basis over the requisite service period for the entire award. The Company has elected to recognize compensation expenses mainly using the Black-Scholes valuation model estimated at the grant date based on the award's fair value.

Income Taxes - Income taxes are provided based upon the liability method of accounting pursuant to ASC Topic 740, *Accounting for Income Taxes*. Provisions for income taxes are based on taxes payable or refundable for the current year and deferred taxes. Deferred taxes are provided on differences between the tax bases of assets and liabilities and their reported amounts in the financial statements, and tax carry forwards. Deferred tax assets and liabilities are included in the financial statements at currently enacted income tax rates applicable to the period in which the deferred tax assets and liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes. The Company has not been subject to any income taxes in the United States or the Cayman Islands.

Under ASC Topic 740, the Company may recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position would be measured based on the largest benefit that has a greater than fifty percent likelihood of being realized upon ultimate settlement. Income tax returns for the years prior to 2010 are no longer subject to examination by tax authorities.

Earnings per Share ("EPS") - Basic EPS is computed by dividing net income attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding. Diluted EPS are computed by dividing net income attributable to ordinary shareholders by the weighted-average number of ordinary shares and dilutive potential ordinary share equivalents outstanding.

Potentially dilutive ordinary shares consist of ordinary shares issuable upon the conversion of ordinary stock options, restricted shares and warrants (using the treasury stock method). For the six months ended December 31, 2014, there were 104,359 restricted shares included in the weighted average dilutive shares calculation. For the three months ended December 31, 2013 and 2014, there were 62,445 and 94,106 restricted shares included in the weighted average dilutive shares calculation, respectively. The effect from options, restricted shares and warrants would have been anti-dilutive due to the fact that the exercise prices were higher than the average stock price during the six months ended December 31, 2013.

Recently Issued Accounting Pronouncements -

In November 2014, The FASB issued Accounting Standards Update (ASU) No. 2014-17, “Business Combinations (Topic 805): Pushdown Accounting, a consensus of the FASB Emerging Issues Task Force, which was ratified by the Financial Accounting Standards Board (FASB) on Oct 8, 2014. ASU No. 2014-17 impacts the stand-alone financial statements of an acquired entity (subsidiary), however it does not change the requirement for an acquirer (parent) to apply business combination accounting and record its new basis in the acquired entity’s assets, liabilities, and non-controlling interests in the acquirer’s consolidated financial statements. The amendments in this Update are effective on November 18, 2014. After the effective date, an acquired entity can make an election to apply the guidance to future change-in-control events or to its most recent change-in-control event. Management believes this ASU 2014-17 does not have any significant impact on the Company’s consolidated financial statements.

F-8

RECON TECHNOLOGY, LTD

NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

In December 2014, The FASB issued Accounting Standards Update (ASU) No. 2014-18, “Business Combinations (Topic 805): accounting for identifiable intangible assets in a business combination (a consensus of the private company council)”. ASU No. 2014-18 affects all entities except for public business entities and not-for-profit entities as defined in the Master Glossary of the FASB Accounting Standards Codification®. An entity within the scope of this Update that elects the accounting alternative to recognize or otherwise consider the fair value of intangible assets as a result of any in-scope transactions should no longer recognize separately from goodwill (1) customer-related intangible assets unless they are capable of being sold or licensed independently from the other assets of the business and (2) noncompetition agreements. The decision to adopt the accounting alternative in this Update must be made upon the occurrence of the first transaction within the scope of this accounting alternative in fiscal years beginning after December 15, 2015, and the effective date of adoption depends on the timing of that first in-scope transaction. If the first in-scope transaction occurs in the first fiscal year beginning after December 15, 2015, the elective adoption will be effective for that fiscal year’s annual financial reporting and all interim and annual periods thereafter. If the first inscope transaction occurs in fiscal years beginning after December 15, 2016, the elective adoption will be effective in the interim period that includes the date of that first in-scope transaction and subsequent interim and annual periods thereafter. Early application is permitted for any interim and annual financial statements that have not yet been made available for issuance.

In January 2015, the FASB issued ASU 2015-01, “Income Statement—Extraordinary and Unusual Items (Subtopic 225-20), Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items (“ASU 2015-01”). ASU 2015-01 eliminates from GAAP the concept of extraordinary items. The amendments will eliminate the requirements in Subtopic 225-20 for reporting entities to consider whether an underlying event or transaction is extraordinary, the presentation and disclosure guidance for items that are unusual in nature or occur infrequently will be retained and will be expanded to include items that are both unusual in nature and infrequently occurring. The amendments in this Update are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. Early adoption is permitted. The impact upon adoption would not affect our consolidated financial position or results of operations.

RECON TECHNOLOGY, LTD**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

NOTE 3. Notes receivable

Notes receivable consisted of the following:

	June 30, 2014	December 31, 2014	December 31, 2014
	RMB	RMB	U.S. Dollars
Notes receivable	¥ -	¥ 2,977,565	\$ 485,064
Total Notes receivable	¥ -	¥ 2,977,565	\$ 485,064

Notes receivable represents trade accounts receivable due from various customers where the customers' banks have guaranteed the payment. The notes are non-interest bearing and normally paid within three to six months. The Company has collected ¥2,777,565 (\$452,483) on January 22, 2015.

NOTE 4. TRADE ACCOUNTS RECEIVABLE, NET

Accounts receivable consisted of the following:

	June 30, 2014	December 31, 2014	December 31, 2014
Third Party	RMB	RMB	U.S. Dollars
Trade accounts receivable	¥ 48,284,531	¥ 55,151,305	\$ 8,984,492
Allowance for doubtful accounts	(4,730,794)	(4,800,772)	(782,076)
Total - third- party, net	¥ 43,553,737	¥ 50,350,533	\$ 8,202,416

	June 30, 2014	December 31, 2014	December 31, 2014
Third Party – long-term	RMB	RMB	U.S. Dollars
Beijing Yabei Nuoda Science and Technology Co. Ltd.	¥ -	¥ 16,162,072	\$ 2,632,902
Allowance for doubtful accounts	-	(1,616,207)	(263,290)

Edgar Filing: Recon Technology, Ltd - Form 10-Q

Total - long-term trade accounts receivable, net ¥ - ¥ 14,545,865 \$ 2,369,612

The receivable from Yabei Nuoda was recognized primarily from the sale of automation system and services based on written contracts. Based on the repayment agreement signed on August 27, 2014, the outstanding balance will be collected in four years beginning 2016, with each installment of ¥4,015,644.

	June 30, 2014	December 31, 2014	December 31, 2014
	RMB	RMB	U.S. Dollars
Related Party			
Beijing Yabei Nuoda Science and Technology Co. Ltd.*	¥ 5,441,498	¥ -	\$ -
Beijing Langchen Construction Company	726,800	817,821	133,227
Xiamen Huangsheng Hitek Computer Network Co.Ltd.	100,000	100,000	16,291
Xiamen Henda Hitek Computer Network Co. Ltd.	1,211,000	2,063,000	336,076
Total - related-parties, net	¥ 7,479,298	¥ 2,980,821	\$ 485,594

RECON TECHNOLOGY, LTD**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

	June 30, 2014	December 31, 2014	December 31, 2014
	RMB	RMB	U.S. Dollars
Related Party – long-term			
Beijing Yabei Nuoda Science and Technology Co. Ltd.	¥16,062,574	¥ -	\$ -
Allowance for doubtful accounts	(1,606,257)	-	-
Total - long-term trade accounts receivable, net	14,456,317	-	-

* One of the Founders, Mr. Yin Shenping, was the legal representative of Beijing Yabei Nuoda before December 2013 and Chairman as of September 30, 2014. On October 30, 2014, Mr. Yin resigned from the chairman position and thus Yabei Nuoda ceased to be a related party of the Company after October 30, 2014.

Mr. Yin does not have any equity interest in this company currently.

NOTE 5. OTHER RECEIVABLES, NET

Other receivables consisted of the following:

Third Party	June 30, 2014	December 31, 2014	December 31, 2014
Current Portion	RMB	RMB	U.S. Dollars
Due from ENI (A)	¥2,523,145	¥2,573,113	\$ 419,176
Loans to third parties (B)	8,979,408	14,728,760	2,399,407
Business advance to staff (C)	6,371,923	9,071,177	1,477,751
Deposits for projects	495,961	1,071,555	174,563
Others	373,622	234,131	38,141
Allowance for doubtful accounts	(451,016)	(476,997)	(77,705)
Total	¥18,293,043	¥27,201,739	\$ 4,431,333

Third Party	June 30, 2014	December 31, 2014	December 31, 2014
Non-Current Portion	RMB	RMB	U.S. Dollars
Due from ENI (A)	¥ 5,353,104	¥ 4,053,933	\$ 660,411
Total	¥ 5,353,104	¥ 4,053,933	\$ 660,411

Edgar Filing: Recon Technology, Ltd - Form 10-Q

- After Jining ENI Energy Technology Co. Ltd (“ENI”) ceased to be a VIE of the Company in [], ENI in January 2012 agreed to repay the loan on a payment schedule, with interest accrued during the period at an annual rate of 4%. In accordance with the payment schedule, the principal plus accrued interest is required to be repaid over approximately three years on a quarterly basis beginning March 2012. The first four payments are RMB 1.2 million each. In March, June, September and December of 2012, the Company received RMB 4.8 million. Starting March 2013, installments for each quarter would be ¥1,777,653. The Company received the payments on time in March and June, 2013. On September 30, 2013, ENI proposed to extend the payment period and signed a new contract with the Company. According to the new arrangement, the then remaining balance of this loan will be repaid by June 2017 with quarterly installments of ¥699,147. The has Company received the payments timely under the new agreement.
- (A)
- (B) Loans to third parties are mainly used for short-term funding to support cooperative companies. These loans are due on demand bearing no interest.
- (C) Business advance to staff represents advances for business travel and sundry expenses related to oilfield or on-site installation and inspection of products through customer approval and acceptance.

F-11

RECON TECHNOLOGY, LTD**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

Other receivables - related parties represent loans to related parties for working capital advances to related entities. Such advances are due-on-demand and non-interest bearing.

Below is a summary of other receivables - related parties which consisted of the following:

Related Party	June 30, 2014	December 31, 2014	December 31, 2014
Name of Related Party	RMB	RMB	U.S. Dollars
Beijing Yabei Nuoda Science and Technology Co. Ltd. *	500,000	-	-
Beijing Langchen Construction Company	913,780	-	-
Other-travel advances	653	-	-
Total	¥ 1,414,433	¥ -	\$ -

* Not a related party after October 31, 2014 (See Note 3).

NOTE 6. PURCHASE ADVANCES

The Company purchased products and services from a third-party and a related party during the normal course of business. Purchase advances consisted of the following:

Third Party	June 30, 2014	December 31, 2014	December 31, 2014
	RMB	RMB	U.S. Dollars
Prepayment for inventory purchase	¥ 27,119,326	¥ 23,475,382	\$ 3,824,286
Allowance for doubtful accounts	(1,360,261)	(1,358,940)	(221,380)
Total	¥ 25,759,065	¥ 22,116,442	\$ 3,602,906

Below is a summary of purchase advances to related party.

Edgar Filing: Recon Technology, Ltd - Form 10-Q

	June 30, 2014	December 31, 2014	December 31, 2014
Related Party	RMB	RMB	U.S. Dollars
Xiamen Huasheng Hitek Computer Network Co. Ltd. (A)	¥ 394,034	¥ 394,034	\$ 64,191
Total	¥ 394,034	¥ 394,034	\$ 64,191

The Company entered into a purchase agreement with Xiamen Huasheng Hitek in September, 2014 and planned to offset the purchase advance. At September 30, 2014, remaining amount to be paid was ¥797,585, which was included in accounts payable-related party. In October, 2014, the Company didn't offset the advance payment and paid the whole contract amount in cash.

One of the Founders and a family member collectively own 57% of Xiamen Huasheng Hitek Computer Network (A) Co. Ltd. Current ending balance of the purchase advances to Xiamen Huasheng Hitek is expect to be settled within one year.

RECON TECHNOLOGY, LTD**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

NOTE 7. INVENTORIES

Inventories consisted of the following:

	June 30, 2014	December 31, 2014	December 31, 2014
	RMB	RMB	U.S. Dollars
Small component parts	¥ 55,262	¥ 55,262	\$ 9,003
Purchased goods and raw materials	272,416	165,251	26,920
Work in process	1,665,447	1,860,073	303,018
Finished goods	12,343,477	17,089,423	2,783,973
Total inventories	¥ 14,336,602	¥ 19,170,009	\$ 3,122,914

There was no inventory obsolescence reserve at June 30, 2014 and December 31, 2014.

NOTE 8. PROPERTY AND EQUIPMENT, NET

Property and equipment consisted of the following:

	June 30, 2014	December 31, 2014	December 31, 2014
	RMB	RMB	U.S. Dollars
Motor vehicles	¥ 2,314,296	¥ 2,291,947	\$ 373,372
Office equipment and fixtures	709,165	793,923	129,335
Total property and equipment	3,023,461	3,085,870	502,707
Less: Accumulated depreciation	(1,701,923)	(1,717,234)	(279,748)
Property and equipment, net	¥ 1,321,538	¥ 1,368,636	\$ 222,959

Depreciation expense was ¥150,973 and ¥153,164 (\$24,951) for the three months ended December 31, 2013 and 2014, respectively.

Depreciation expense was ¥301,341 and ¥274,511 (\$44,720) for the six months ended December 31, 2013 and 2014, respectively.

NOTE 9. LONG-TERM INVESTMENT

On June 28, 2013, the Company purchased 2,800,000 restricted shares of Avalon Oil and Gas, Inc. ("Avalon") for \$0.089 per share, or approximately ¥1.5 million (\$250,000). Since the restriction for the shares is for two years, the Company was able to acquire the shares at 50% of the market value. The investment was accounted for using the equity method and no gain or loss from equity investment was recorded for the year ended June 30, 2013 due to immateriality. As of June 30, 2014 and December 31, 2014, Recon owned 24.02% and 23.61% of Avalon's outstanding shares, respectively. Avalon is an independent US domestic oil and natural gas producer listed on the OTCBB under the ticker symbol AOGN. Avalon is building a portfolio of oil and gas producing properties to generate asset growth. However, the stock is not actively traded and, based on available information and discussion with the management team of Avalon, we believe Avalon's operating loss would not be recovered in the foreseeable future, therefore, the Company believes the investment was impaired and recorded an investment loss of ¥1,535,250 (\$250,000) for the year ended June 30, 2014 to write its investment own to zero.

RECON TECHNOLOGY, LTD**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****NOTE 10. OTHER PAYABLES**

Other payables consisted of the following:

	June 30, 2014	December 31, 2014	December 31, 2014
	RMB	RMB	U.S. Dollars
Third Party			
Consulting services	¥ 777,863	¥ 412,599	\$ 67,215
Distributors and employees	973,707	1,126,265	183,476
Others	13,509	88,812	14,468
Total	¥ 1,765,079	¥ 1,627,676	\$ 265,159

	June 30, 2014	December 31, 2014	December 31, 2014
	RMB	RMB	U.S. Dollars
Related Party			
Due to related parties (1)	¥ 2,560,648	¥ 2,499,347	\$ 407,159
Expenses paid by the major shareholders	439,071	676,322	110,177
Due to family member of one owner on behalf of Recon	50,000	170,000	27,694
Due to management staff on behalf of Recon	256,305	251,093	40,905
Total	¥ 3,306,024	¥ 3,596,762	\$ 585,935

(1) Includes an advance from Xiamen Henda Haitek for RMB 2,499,347 to supplement the Company's working capital. The advances are payable on demand and non-interest bearing.

NOTE 11. TAXES PAYABLE

Taxes payable consisted of the following:

June 30, 2014

Edgar Filing: Recon Technology, Ltd - Form 10-Q

		December 31, 2014	December 31, 2014
	RMB	RMB	U.S. Dollars
VAT payable	¥ 3,412,759	¥ 2,967,332	\$ 483,397
Enterprise income tax payable	4,134,210	5,375,919	875,771
Other taxes payable	42,877	26,162	4,262
Total taxes payable	¥ 7,589,846	¥ 8,369,413	\$ 1,363,430

NOTE 12. SHORT-TERM BANK LOANS

Short-term bank loans consisted of the following:

	June 30, 2014	December 31, 2014	December 31, 2014
	RMB	RMB	U.S. Dollars
Industrial and commercial bank, floating interest rate at 5.6%, due on December 24, 2014	¥ 2,000,000	¥ -	-
Industrial and commercial bank, floating interest rate at 6.0%, due on June 24, 2015	8,000,000	8,000,000	1,303,250
Total short-term bank loans	¥ 10,000,000	¥ 8,000,000	\$ 1,303,250

RECON TECHNOLOGY, LTD**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

Interest expense was ¥257,085 and ¥80,667 (\$13,141) for the three months ended December 31, 2013 and 2014, respectively.

Interest expense was ¥476,757 and ¥238,178 (\$38,801) for the six months ended December 31, 2013 and 2014, respectively.

NOTE 13. SHORT-TERM BORROWINGS DUE TO RELATED PARTIES

Short-term borrowings due to related parties are generally extended upon maturity and consisted of the following:

	June 30, 2014	December 31, 2014	December 31, 2014
	RMB	RMB	U.S. Dollars
Short-term borrowings due to related parties:			
Short-term borrowing from a Founder, 6.6% annual interest, due on December 25, 2014	¥ 5,007,728	¥ -	-
Short-term borrowing from a Founder, 7.0% annual interest, due on October 20, 2015	-	6,014,400	979,783
Short-term borrowing from a Founder, 6.0% annual interest, due on October 2, 2015	-	3,417,104	556,668
Short-term borrowings from Xiamen Huasheng Haitian Computer Network Co. Ltd., no interest, due on November 14, 2015	200,000	200,000	32,581
Total short-term borrowings due to related parties	¥ 5,207,728	¥ 9,631,504	\$ 1,569,032

Interest expense for short-term borrowings due to related parties was ¥910 and ¥146,445 (\$23,857) for the three months ended December 31, 2013 and 2014, respectively.

Interest expense for short-term borrowings due to related parties was ¥1,441 and ¥230,778 (\$37,595) for the six months ended December 31, 2013 and 2014, respectively.

Note 14 –WARRANT LIABILITY

In connection with the stock offering in November 2013, the Company issued warrants to certain institutional investors and placement agent to purchase 218,600 ordinary shares (see details in Note 14).

According to ASC 815-40, if the strike price of the warrants is denominated in a currency other than the Company's functional currency, the warrants are not considered indexed to the entity's own stock. The Company's functional currency is RMB and the strike price of the warrants is denominated in USD, as a result, the warrants are classified as liabilities with all future changes in the fair value of these warrants recognized in earnings until such time as the warrants are exercised or expired.

These common stock purchase warrants do not trade in an active securities market, and as such, their fair value is estimated by using the Black-Scholes Option Pricing Model using the following assumptions:

RECON TECHNOLOGY, LTD**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

	December 31, 2014	June 30, 2014		
Annual dividend yield	-	-		
Exercised price	5.38	5.38		
Underlying stock price at valuation date	1.97	3.86		
Expected life (years)	1.92	2.42		
Risk-free interest rate	1.10	% 0.88	%	%
Expected volatility	113	% 220	%	%

Expected volatility is based on the historical volatility of the Company's common stock. The Company has no reason to believe future volatility over the expected remaining life of these warrants is likely to differ materially from historical volatility. The expected life is based on the remaining term of the warrants. The risk-free interest rate is based on U.S. Treasury securities according to the remaining term of the warrants. The expected dividend yield was based on the Company's current and expected dividend policy.

The following table sets forth by level within the fair value hierarchy the warrants liability that was accounted at fair value on a recurring basis.

	Fair Value Measurement at June 30, 2014			Carrying Value at June 30, 2014	Carrying Value at June 30, 2014
	Level 1	Level 2	Level 3	RMB	USD
Warrants liability	¥-	¥5,021,621	¥-	¥ 5,021,621	\$ 815,834

	Fair Value Measurement at December 31, 2014			Carrying Value at December 31, 2014	Carrying Value at December 31, 2014
	Level 1	Level 2	Level 3	RMB	USD
Warrants liability	¥-	¥930,480	¥-	¥ 930,480	\$ 151,581

The following is a reconciliation of the beginning and ending balance of the warrant liability measured at fair value on a recurring basis for six months ended December 31, 2014:

Edgar Filing: Recon Technology, Ltd - Form 10-Q

	Change of warrants liability	
	RMB	USD
Beginning balance - June 30, 2014	¥5,021,621	\$815,834
Change of warrant liability	(4,091,141)	(664,253)
Ending balance -December 31, 2014	¥930,480	\$151,581

F-16

RECON TECHNOLOGY, LTD

NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 15. SHAREHOLDERS' EQUITY

Stock offering – On November 25, 2013, the Company entered into a securities purchase agreement (“Purchase Agreement”) with certain institutional investors for the sale of 546,500 ordinary shares in a registered direct offering at the price of \$4.81 per ordinary share (amended to \$4.30 per ordinary share on November 29, 2013). The net cash proceeds received from the stock offering, after deducting underwriter commission and other associated fees, were ¥12,132,882 (approximately \$2.0 million). In addition, warrants to purchase 163,950 ordinary shares in the aggregate were issued to the investors. The warrants will be exercisable immediately as of the date of issuance at an exercise price of \$6.01 per ordinary share (amended to \$5.38 per ordinary share on November 29, 2013) and expire three years from the date of issuance. The Company also issued warrants to purchase 54,650 ordinary shares to the placement agent (“Placement Agent Warrant”). The Placement Agent Warrants are on substantially the same terms as the warrants issued pursuant to the Purchase Agreement, except that these warrants are not exercisable for a period of six months and will expire three years from the initial exercise date in 2016.

In addition to the above warrants issued to the placement agent, the Company granted warrants for 170,000 shares in connection with its IPO offering, and none of these warrants was exercised during this period.

Appropriated Retained Earnings - According to the Memorandum and Articles of Association, the Company is required to transfer a certain portion of its net profit, as determined under PRC accounting regulations, from current net income to the statutory reserve fund. In accordance with the PRC Company Law, companies are required to transfer 10% of their profit after tax, as determined in accordance with PRC accounting standards and regulations, to the statutory reserves until such reserves reach 50% of the registered capital or paid-in capital of the companies. As of June 30, 2014 and December 31, 2014, the balance of total statutory reserves was ¥4,148,929 and ¥4,631,899 (\$754,565).

NOTE 16. STOCK-BASED COMPENSATION

Stock-Based Awards Plan

Edgar Filing: Recon Technology, Ltd - Form 10-Q

2009 Options Plan - The Company granted options to purchase 293,000 ordinary shares under the Stock Incentive 2009 Plan to its employees and non-employee directors on July 29, 2009. The options have an exercise price of \$6.00, equal to the IPO price of the Company's ordinary shares, and will vest over a period of five years, with the first 20% vesting on July 29, 2010. The options expire ten years after the date of grant, on July 29, 2019. The fair value was estimated on July 29, 2009 using the Binomial Lattice valuation model, with the following weighted-average assumptions:

Stock price at grant date	\$6.00
Exercise price (per share)	\$6.00
Risk free rate of interest***	4.6118 %
Dividend yield	0.0 %
Life of option (years)**	10
Volatility*	78 %
Forfeiture rate****	0 %

* Volatility is projected using the performance of PHLX Oil Service Sector index.

** The life of options represents the period the option is expected to be outstanding.

*** The risk-free interest rate is based on the Chinese international bond denominated in U.S. dollar, with a maturity that approximates the life of the option.

**** Forfeiture rate is the estimated percentage of options forfeited by employees by leaving or being terminated before vesting.

The Company recognizes compensation cost for awards with graded vesting on a straight-line basis over the requisite service period for the entire award. The grant date fair value of the options was ¥30.17 (\$4.42) per share.

RECON TECHNOLOGY, LTD**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

2012 Options Plan – The Company granted options to purchase 415,000 ordinary shares to its employees and non-employee director on March 26, 2012. The options have an exercise price of \$2.96, which was equal to the share price of the Company's ordinary shares at March 26, 2012, and will vest over a period of five years, with the first 20% vesting on March 26, 2013. The options expire ten years after the date of grant, on March 26, 2022.

The Company recognizes compensation cost for awards with graded vesting on a straight-line basis over the requisite service period for the entire award. The grant date fair value of the options was ¥10.06 (\$1.49) per share.

The following is a summary of the stock options activity:

Stock Options	Shares	Weighted Average Exercise Price Per Share
Outstanding as of July 1, 2014	415,600	\$ 4.37
Granted	-	-
Forfeited	-	-
Exercised	-	-
Outstanding as of December 31, 2014	415,600	\$ 4.37

The following is a summary of the status of options outstanding and exercisable at December 31, 2014:

Outstanding Options			Exercisable Options		
Average Exercise Price	Exercise Number	Average Remaining Contractual life (Years)	Average Exercise Price	Exercise Number	Average Remaining Contractual life (Years)
\$6.00	193,000	4.58	\$6.00	193,000	4.58
\$2.96	222,600	7.24	-	-	-

Edgar Filing: Recon Technology, Ltd - Form 10-Q

During the six months December 31, 2014, the Company has granted restricted ordinary shares as follows:

On July 19, 2014, the Company granted 50,000 restricted shares to a non-affiliate as compensation for certain consulting service. The fair value of the restricted shares was \$190,000 based on the closing stock price \$3.8 at July 18, 2014.

On August 7, 2014, the Company canceled 40,625 restricted shares, which was issued to Expert Asia Investment Ltd. on May 8, 2014, as the services were not provided pursuant to the agreement it had with the Company.

On December 13, 2013, the Company granted 95,181 restricted shares to Mr. Yin Shenping and 135,181 restricted shares to Mr. Chen Guangqiang at an aggregate value of ¥4,207,496 (\$688,782), based on the stock closing price of \$2.99 at December 13, 2013. These restricted shares will vest over three years with one third of the shares vesting every year from the grant date. The first one third was vested on December 13, 2014 and are now non-restricted.

The Share-based compensation expense recorded for restricted shares granted were ¥66,229 and ¥705,612 (\$114,949) for the six months ended December 31, 2013 and 2014, respectively. Total unrecognized share-based compensation expense for these shares as of December 31, 2014 was approximately ¥2.8 million (\$0.4 million), which are expected to be recognized over a weighted average period of approximately 1.95 years.

RECON TECHNOLOGY, LTD

NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The Share-based compensation expense recorded for stock options granted were ¥414,326 and ¥409,418 (\$66,697) for the six months ended December 31, 2013 and 2014, respectively. The total unrecognized share-based compensation expense for stock options as of December 31, 2014 was approximately ¥1.9 million (\$0.3 million), which is expected to be recognized over a weighted average period of approximately 2.24 years.

Following is a summary of the restricted stock grants:

Restricted stock grants	Shares
Nonvested as of June 30, 2014	230,362
Granted	50,000
No vested adjustment	40,625
Cancelled	(40,625)
Vested	(126,787)
Nonvested as of December 31, 2014	153,575

NOTE 17. INCOME TAX

The Company is not subject to any income taxes in the United States or the Cayman Islands and had minimal operations in jurisdictions other than the PRC domestic companies. The Company follows Implementing Rules for the Enterprise Income Tax Law (“Implementing Rules”), which took effect on January 1, 2008 and unified the income tax rate for domestic-invested and foreign-invested enterprises at 25%.

The Company reapplied for high-technology enterprise approval and has passed all relevant reviews. Thus, for the calendar years 2013 and 2014, Nanjing Recon is subject to an income tax rate of 15%.

As approved by the domestic tax authority in the PRC, BHD was recognized as a government-certified high technology company on November 25, 2009 and is subject to an income tax rate of 15% through November 2015.

Deferred tax assets are comprised of the following:

Edgar Filing: Recon Technology, Ltd - Form 10-Q

	June 30, 2014	December 31, 2014	December 31, 2014
	RMB	RMB	U.S. Dollars
Allowance for doubtful receivables	¥ 1,209,961	¥ 1,237,938	\$ 201,668
Total deferred income tax assets	¥ 1,209,961	¥ 1,237,938	\$ 201,668

Deferred tax liability is comprised of the following:

	June 30, 2014	December 31, 2014	December 31, 2014
	RMB	RMB	U.S. Dollars
Income tax cost due to unpayable accounts	¥ 180,186	¥ 180,186	\$ 29,353
Total deferred income tax liability	¥ 180,186	¥ 180,186	\$ 29,353

F-19

RECON TECHNOLOGY, LTD**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

The Company's tax provision (benefit) is comprised of the following:

	For the three months ended		
	December 31,		
	2013	2014	2014
	RMB	RMB	U.S. Dollars
Current income tax	¥1,295,941	¥644,630	\$105,014
Deferred income taxes	(44,079)	(25,943)	(4,226)
Provision	¥1,251,862	¥618,687	\$100,788

	For the six months ended		
	December 31,		
	2013	2014	2014
	RMB	RMB	U.S. Dollars
Current income taxes	¥1,491,400	¥676,909	\$110,273
Deferred income taxes	(32,211)	(27,977)	(4,558)
Provision	¥1,459,189	¥648,932	\$105,715

NOTE 18. NON-CONTROLLING INTEREST

Non-controlling interest consisted of the following:

	As of June 30, 2014			
	BHD	Nanjing Recon	Total	Total
	RMB	RMB	RMB	U.S. Dollars
Paid-in capital	¥1,651,000	¥200,000	¥1,851,000	\$299,118
Unappropriated retained earnings	3,152,687	3,250,513	6,403,200	869,812
Accumulated other comprehensive loss	(16,868)	(11,853)	(28,721)	(5,265)
Total non-controlling interest	¥4,786,819	¥3,438,660	¥8,225,479	\$1,163,665

Edgar Filing: Recon Technology, Ltd - Form 10-Q

	As of December 31, 2014			
	BHD	Nanjing Recon	Total	Total
	RMB	RMB	RMB	U.S. Dollars
Paid-in capital	¥1,651,000	¥200,000	¥1,851,000	\$301,539
Unappropriated retained earnings	3,388,114	3,449,759	6,837,873	1,113,932
Accumulated other comprehensive loss	(16,621)	(11,853)	(28,474)	(4,635)
Total non-controlling interest	¥5,022,493	¥3,637,906	¥8,660,399	\$1,410,836

F-20

RECON TECHNOLOGY, LTD

NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 19. CONCENTRATIONS

For the three months ended December 31, 2013 and 2014, our two largest customers, China National Petroleum Corporation (“CNPC”) and China Petroleum & Chemical Corporation Limited (“SINOPEC”), represented 50.7%, 14.0% and 58.83%, 10.35% of the Company’s revenue, respectively.

For the six months ended December 31, 2013 and 2014, our two largest customers, China National Petroleum Corporation (“CNPC”) and China Petroleum & Chemical Corporation Limited (“SINOPEC”), represented 48.04%, 18.01% and 56.79%, 8.89% of the Company’s revenue, respectively.

For the three months ended December 31, 2013, four major suppliers accounted for 52.7% of the company’s total purchase. For the three months ended December 31, 2014, one major suppliers accounted for 20% of the company’s total purchases.

For the six months ended December 31, 2013, four major suppliers accounted for 48.8% of the company’s total purchase. For the six months ended December 31, 2014, one major suppliers accounted for 14% of the company’s total purchases.

NOTE 20. COMMITMENTS AND CONTINGENCY

(a) Office Leases

The Company leased three offices in Beijing (two for BHD; one for Recon-JN), and one office in Nanjing for Nanjing Recon. Future payments under such leases are as follows as December 31, 2014:

Twelve months ending
December 31,

	Office lease payment	
	RMB	U.S. Dollars
2015	¥1,188,333	\$193,587
2016	90,000	14,662
Total	¥1,278,333	\$208,249

In January 2015, BHD renewed its lease agreements amounted to ¥840,000 (\$136,841) for one more year.

(b) Contingency

The Labor Contract Law of the PRC requires employers to assure the liability of severance payments if employees are terminated and have been working for the employers for at least two years prior to January 1, 2008. The employers will be liable for one month of severance pay for each year of the service provided by the employees. As of December 31, 2014, the Company estimated its severance payments of approximately ¥1.5 million (\$0.2 million) which has not been reflected in its unaudited condensed consolidated financial statements because the Company has determined that the likelihood to make these payments is remote.

NOTE 21. RELATED PARTY TRANSACTIONS AND BALANCES

Sales to related parties – sales to related parties consisted of the following:

	For the three months ended		
	December 31,		
	2013	2014	2014
	RMB	RMB	U.S. Dollars
Beijing Yabei Nuoda Science and Technology Co. Ltd. *	¥1,242,073	¥-	\$-
Xiamen Henda Haitian computer network Inc	384,615	768,118	125,131
Revenues from related parties	¥1,626,688	¥768,118	\$125,131

RECON TECHNOLOGY, LTD**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

	For the six months ended		
	December 31,		
	2013	2014	2014
	RMB	RMB	U.S. Dollars
Beijing Yabei Nuoda Science and Technology Co. Ltd. *	¥1,358,546	¥-	\$-
Xiamen Henda Haitian computer network Inc	683,760	768,118	125,131
Revenues from related parties	¥2,042,306	¥768,118	\$125,131

* Not a related party after October 31, 2014, (See Note 3).

Purchases from related parties – purchases from related parties consisted of the following:

	For the six months ended		
	December 31,		
	2013	2014	2014
	RMB	RMB	U.S. Dollars
Xiamen Hengda Hitek Computer Network Co. Ltd.	¥-	¥797,585	\$129,932
Purchase from related parties	¥-	¥797,585	\$129,932

There was no purchase from related parties for the three months ended December 31, 2014.

Leases from related parties - The Company has various agreements for the lease of office space owned by the Founders and their family members. The terms of the agreement state that the Company will continue to lease the property for two years at a monthly rent of ¥95,000 with the annual rental expense at approximately ¥1.1 million (\$0.2 million). The two-year lease agreements between Nanjing Recon and Mr. Yin and his family member started from July 10, 2014, the one-year lease agreements between BHD and Mr. Chen Guangqiang and his family member started from January 1, 2014 and the annual lease between the Company and Mr. Chen Guangqiang's family member started from July 1, 2013.

Short-term borrowings from related parties - The Company borrowed ¥5,207,728 and ¥9,631,504 (\$1,569,032) from the Founders, their family members and senior officers as of June 30, 2014 and December 31, 2014, respectively. For the specific terms and interest rates of the borrowings, please see Note 12.

Expenses paid by the owner on behalf of Recon - One owner of Nanjing Recon, Mr. Yin and the major owner of BHD, Mr. Chen paid certain operating expense for the Company. As of June 30, 2014 and December 31, 2014, ¥284,370 and ¥676,322 (\$110,177) was due to them, respectively.

NOTE 22. Variable Interest Entities

The Company reports its VIEs' portion of consolidated net income and stockholders' equity as non-controlling interests in the condensed consolidated financial statements.

RECON TECHNOLOGY, LTD**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

Summary information regarding consolidated VIEs is as follows:

	June 30, 2014	December 31, 2014	December 31, 2014
	RMB	RMB	U.S. Dollars
ASSETS			
Current Assets			
Cash and cash equivalents	¥14,021,653	¥1,186,734	\$ 193,326
Trade accounts receivable, net	51,033,035	53,331,354	8,688,011
Purchase advances	24,600,379	22,510,477	3,667,097
Other assets	34,097,774	51,981,630	8,468,132
Total current assets	¥123,752,841	¥129,010,195	\$ 21,016,566
Non-current assets	15,758,115	15,897,211	2,589,755
Total Assets	¥139,510,956	¥144,907,406	\$ 23,606,321
LIABILITIES			
Trade accounts payable	¥11,413,505	¥12,602,016	\$ 2,052,948
Taxes payable	7,589,846	8,369,413	1,363,430
Other liabilities	21,878,699	25,685,691	4,184,360
Total current liabilities	40,882,050	46,657,120	7,600,738
Total Liabilities	¥40,882,050	¥46,657,120	\$ 7,600,738

The financial performance of VIEs reported in the condensed consolidated statement of income and comprehensive income for the three months ended December 31, 2014 includes revenues of ¥21,328,972 (\$3,474,623), gross profit of ¥8,977,931 (\$1,462,561), operating expenses of ¥3,63,239 (\$588,619), other income of ¥119,650(\$19,492) and a net income of ¥4,865,655(\$792,646).

The financial performance of VIEs reported in the condensed consolidated statement of income and comprehensive income for the six months ended December 31, 2014 includes revenues of ¥25,632,972 (\$4,175,771), gross profit of ¥9,593,245 (\$1,562,799), operating expenses of ¥6,124,974 (\$997,797), other income of ¥87,925(\$14,323) and a net income of ¥2,907,263 (\$473,611).

NOTE 23. SUBSEQUENT EVENTS

On January 12, 2015 the Company borrowed ¥1.6 million from its Chief Operating Officer to supplement the Company's working capital. This loan is due on October 12, 2015 with an annual interest rate of 6.16%.

On January 28, 2015, the Company entered into an engagement agreement with Maxim Group LLC ("Maxim") who shall serve as the exclusive agent for the Company in connection with the Company's offering of up to \$10,000,000 of its registered shares.

On January 29, 2015, the Company's shareholders approved an increase of its authorized shares from 25,000,000 shares to 100,000,000 shares. The shareholders also approved the Company's 2015 Equity Incentive Plan.

On January 31, 2015, the Company granted 150,000 restricted shares to Mr. Yin Shenping and 150,000 restricted shares to Mr. Chen Guangqiang under the Company's 2015 Incentive Plan. These restricted shares will vest over three years with one third of the shares vesting every year from the grant date. The Company also granted 400,000 options to management and staff. Exercise price for each warrant is \$1.65 per share and will vest over three years with one third of the warrants vesting every year from the grant date.

On February 2, 2015, the Company entered into an engagement agreement with Maxim who shall serve as the exclusive financial advisor and investment banker for the Company. Either party may terminate this engagement agreement at any time upon 30 days prior written notice after the 6 months anniversary of this agreement. Pursuant to this agreement, the Company issued 24,000 restricted shares to Maxim.

On February 13, 2015, the Company entered into certain warrants exchange agreements with certain holders (the "Holders") of warrants to purchase 163,950 ordinary shares of the Company (the "Warrants") issued in the Company's November 2013 registered offering. These Holders agreed to exchange the Warrants for 204,938 of ordinary shares (the "Exchange Shares") equal to one hundred twenty five percent (125%) of the shares issuable upon exercise of the Warrants. The Exchange Shares will be issued to the Holders in exchange for the Warrant and without the payment of any other consideration by the Holders. Upon completion of the transaction contemplated in the Exchange Agreement, the Warrants shall will be automatically canceled and terminated.