Net Medical Xpress Solutions, Inc.
Form 10-Q
August 08, 2013

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

[X]

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

For the quarterly period ended June 30, 2013

[ ]

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

For the transition period from _____________ to _____________

COMMISSION FILE No. 333-30176

NET MEDICAL EXPRESS SOLUTIONS, INC.

(Exact name of Registrant as specified in charter)

| NEVADA | 91-1287406 |
|---|---|
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |

5021 Indian School Road, Suite 100

Albuquerque, New Mexico 87110

(Address of principal executive offices) (Zip Code)

(505) 255-1999

(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 [X] 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 [X] NO [ ] |

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

| | |
|---|---|
| Large accelerated filer [ ] | Accelerated filer [ ] |
| Non-accelerated filer [ ] | Smaller reporting company [X] |

| | |
|---|---|
| Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). | YES [ ] NO [X] |

The number of shares outstanding of each of the issuer s classes of common stock at August 14, 2013 was 157,122,470

TABLE OF CONTENTS

**ITEM 1. FINANCIAL STATEMENTS**

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

| | June 30, 2013 (Unaudited) | December 31, 2012 |
|---|---|---|
| **Assets** | | |
| Current assets: | | |
| Cash and equivalents | $ 184,000 | $ 109,000 |
| Accounts receivable, net of allowance of $30,000 and $31,000, respectively | 742,000 | 653,000 |
| Inventory | 9,000 | 5,000 |
| Prepaid expenses and other assets | 164,000 | 61,000 |
| Total current assets | 1,099,000 | 828,000 |
| Furniture, equipment and improvements, net of accumulated depreciation of $632,000 and $627,000, respectively | 44,000 | 55,000 |
| Security deposits | 4,000 | 4,000 |
| **Total Assets** | $ 1,147,000 | $ 887,000 |
| **Liabilities and Stockholders' Equity** | | |
| Current liabilities: | | |
| Accounts payable | $ 642,000 | $ 632,000 |
| Accrued expenses | 177,000 | 85,000 |
| Deferred revenue | 8,000 | 8,000 |
| Capital lease | 2,000 | 3,000 |
| Notes payable - related party | 46,000 | 45,000 |
| Total current liabilities | 875,000 | 773,000 |
| Long-term liabilities | | |
| Notes payable - related party | 2,000 | 2,000 |
| Capital lease - long-term portion | | 1,000 |
| Total long-term liabilities | 2,000 | 3,000 |
| Total liabilities | 877,000 | 776,000 |
| Stockholders' equity (deficit): | | |
| Preferred stock, $0.001 par value, 500,000 shares authorized, 0 shares issued and outstanding as of 6/30/13 | - | - |

| | | | | |
|---|---|---|---|---|
| Common stock, $0.001 par value, 200,000,000 shares authorized, 160,322,471 and 156,987,310 shares issued and outstanding as of 6/30/13 and 12/31/12, respectively | | 160,000 | | 157,000 |
| Paid-in capital | | 15,466,000 | | 15,354,000 |
| Subscriptions payable | | 21,000 | | 21,000 |
| Deferred compensation | | (90,000) | | (80,000) |
| Accumulated deficit | | (15,287,000) | | (15,341,000) |
| Total stockholders' equity | | 270,000 | | 111,000 |
| **Total Liabilities and Stockholders' Equity** | $ | 1,147,000 | $ | 887,000 |

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

**Net Medical Xpress Services, Inc.**
**Consolidated Statements of Operations**
**(Rounded to the nearest thousand)**
**(Unaudited)**

| | For the three months ended June 30, 2013 | For the three months ended June 30, 2012 | For the six months ended June 30, 2013 | For the six months ended June 30, 2012 |
|---|---|---|---|---|
| Revenues | | | | |
| Net Medical Xpress Solutions | $ 116,000 | $ 112,000 | $ 245,000 | $ 210,000 |
| Net Medical Xpress Services | 973,000 | 819,000 | 1,952,000 | 1,635,000 |
| Net Medical Xpress Specialists | 117,000 | 29,000 | 230,000 | 38,000 |
| Gross revenues | 1,206,000 | 960,000 | 2,427,000 | 1,883,000 |
| Cost of services | 927,000 | 743,000 | 1,843,000 | 1,460,000 |
| Gross profit | 279,000 | 217,000 | 584,000 | 423,000 |
| Operating costs and expenses: | | | | |
| General and administrative | 225,000 | 206,000 | 451,000 | 408,000 |
| Depreciation and amortization | 4,000 | 4,000 | 12,000 | 9,000 |
| Research and development | 45,000 | 16,000 | 61,000 | 36,000 |
| Total operating costs and expenses | 274,000 | 226,000 | 524,000 | 453,000 |
| Net operating income (loss) | 5,000 | (9,000) | 60,000 | (30,000) |
| Other income (expense): | | | | |
| Interest expense | (4,000) | (3,000) | (6,000) | (5,000) |
| Total other income (expense) | (4,000) | (3,000) | (6,000) | (5,000) |
| Net income (loss) | $ 1,000 | $ (12,000) | $ 54,000 | $ (35,000) |
| Income (loss) per share - fully diluted and basic | $ 0.00 | $ (0.00) | $ 0.00 | $ (0.00) |
| Weighted average number of common shares outstanding - fully diluted and basic | 167,172,961 | 155,173,109 | 165,205,143 | 151,123,798 |

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

**Net Medical Xpress Services, Inc.**
**Consolidated Statements of Cash Flows**
**(Rounded to the nearest thousand)**
**(Unaudited)**

| | For the six months ended June 30, 2013 | 2012 |
|---|---|---|
| **Cash flows from operating activities** | | |
| Net income (loss) | $ 54,000 | $ (35,000) |
| Adjustments to reconcile net income (loss) to net cash provided (used) by operating activities: | | |
| Common stock issued for services to board members and officers | 40,000 | 40,000 |
| Common stock issued for services | 20,000 | - |
| Executive services donated | - | 35,000 |
| Depreciation and amortization | 15,000 | 10,000 |
| Depreciation and amortization allocated to cost of goods sold | 1,000 | 4,000 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (89,000) | (133,000) |
| Inventory | (4,000) | (15,000) |
| Prepaid expenses and other assets | 76,000 | 45,000 |
| Accounts payable | 10,000 | (33,000) |
| Accrued expenses | (87,000) | 11,000 |
| Customer deposits | - | 9,000 |
| Deferred revenue | - | (2,000) |
| Net cash provided (used) by operating activities | 36,000 | (64,000) |
| **Cash flows from investing activities** | | |
| Acquisition of fixed assets | (5,000) | (5,000) |
| Net cash used by investing activities | (5,000) | (5,000) |
| **Cash flows from financing activities** | | |
| Proceeds from notes payable - related party | 1,000 | 25,000 |
| Repayment of notes payable | - | (31,000) |
| Repayment of principal under capital lease | (2,000) | (7,000) |
| Net proceeds from the issuance of common stock for the exercise of options | 45,000 | 45,000 |
| Net cash provided by financing activities | 44,000 | 32,000 |
| Net increase (decrease) in cash equivalents | 75,000 | (37,000) |
| Cash equivalents - beginning | 109,000 | 100,000 |
| Cash equivalents - ending | $ 184,000 | $ 63,000 |
| Supplemental disclosures: | | |
| Interest paid | $ 4,000 | $ 3,000 |
| Insurance contracts financed | $ 179,000 | $ 153,000 |

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

**Net Medical Xpress Services, Inc.**

Notes to the Financial Statements

(Unaudited)

**NOTE A BASIS OF PRESENTATION**

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

These statements reflect all adjustments, consisting of normal recurring adjustments, which, in the opinion of management, are necessary for fair presentation of the information contained therein. It is suggested that these interim financial statements be read in conjunction with the financial statements of the Company for the year ended December 31, 2012 and notes thereto included in the Company's Form 10-K. The Company follows the same accounting policies in the preparation of interim reports.

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

**NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Reclassification:**

Certain reclassifications have been made to conform the 2012 amounts to the 2013 classifications for comparative purposes.

**Principles of Consolidation:**

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

**Use of Estimates:**

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

**Cash and Cash Equivalents**:

The Company considers all highly liquid instruments purchased with a maturity of three months or less to be cash equivalents. At June 30, 2013, the Company did not have cash and equivalents that exceeded federally insured limits.

**Trade Accounts Receivable:**

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

**Net Medical Xpress Services, Inc.**

Notes to the Financial Statements

(Unaudited)

**NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Trade Accounts Receivable, continued:**

The Company also estimates an allowance for doubtful accounts, which amounted to $30,000 and $31,000 at June 30, 2013 and December 31, 2012, respectively. The estimate is based upon management s review of all accounts and an assessment of the Company s historical evidence of collections. Specific accounts are charged directly to the reserve when management obtains evidence of a customer s insolvency. Charge-offs, net of recoveries, for the six months ended June 30, 2013 and 2012 totaled $1,000 and $0, respectively.

**Property and Equipment:**

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

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

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

**Long-Lived Assets:**

The Company accounts for its long-lived assets in accordance with Accounting Standards Codification ( ASC ) Topic 360-10-05, Accounting for the Impairment or Disposal of Long-Lived Assets. ASC Topic 360-10-05 requires that long-lived assets be reviewed for impairment whenever events or changes in circumstances indicate that the historical cost carrying value of an asset may no longer be appropriate. The Company assesses recoverability of the carrying value of an asset by estimating the future net cash flows expected to result from the asset, including eventual disposition. If the future net cash flows are less than the carrying value of the asset, an impairment loss is recorded equal to the difference between the asset s carrying value and fair value or disposable value. The Company determined that none of its long-term assets at June 30, 2013 or December 31, 2012 were impaired.

**Stock-Based Compensation:**

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

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



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**Net Medical Xpress Services, Inc.**

Notes to the Financial Statements

(Unaudited)

**NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Stock-Based Compensation, continued:**

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

During the six months ended June 30, 2013 and 2012, the Company recognized stock-based compensation expense totaling $40,000 and $40,000, from the issuance of a total of 0 and 8,000,000 shares of its common stock to officers, directors, and consultants (See Note E).

**Income Taxes:**

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

**Earnings (Loss) per Share:**

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

**Revenue Recognition:**

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

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

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

**Net Medical Xpress Services, Inc.**

Notes to the Financial Statements

(Unaudited)

**NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Revenue Recognition, continued:**

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

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

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

The Company follows the guidance in FASB ASC Topic 605, *Accounting for Performance of Construction-Type and Certain Production-Type Contracts* for custom software development arrangements that require significant production, customization or modification to its core software. Revenue is generally recognized for such arrangements under the percentage-of-completion method. Under percentage-of-completion accounting, both the product license and custom software development revenue are recognized as work progresses based on specific milestones in accordance with FASB ASC Topic 450. The Company believes that project milestones based on completion of specific tasks provide the best approximation of progress toward the completion of the contract. At June 30, 2013 and June 30, 2012, there were no custom software development arrangements in progress.

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

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

**Net Medical Xpress Services, Inc.**

Notes to the Financial Statements

(Unaudited)

**NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Revenue Recognition, continued:**

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

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

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

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

**Research and Development Expenses:**

Costs of research and development activities are expensed as incurred.

**Advertising Expenses:**

The Company expenses advertising costs which consist primarily of direct mailings, promotional items and print media, as incurred. Advertising expenses amounted to $0 and $0 for the six months ended June 30, 2013 and 2012, respectively.

**Fair Value of Financial Instruments:**

Financial accounting standards Statement No. 107, Disclosure About Fair Value of Financial Instruments , requires the Company to disclose, when reasonably attainable, the fair market values of its assets and liabilities which are deemed to be financial instruments. The carrying amounts and estimated fair values of the Company s financial instruments approximate their fair value due to the short-term nature.

**Recent Pronouncements:**

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

**NOTE C GOING CONCERN**

The accompanying financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. The Company has incurred cumulative net losses of approximately $15,287,000 since its inception and requires capital for its contemplated operational and marketing activities to take place. The Company s ability to raise additional capital through the future issuances of the common stock is unknown. The obtainment of additional financing, the successful development of the Company s contemplated plan of operations, and its transition, ultimately, to the attainment of profitable operations are necessary for the Company to continue operations. The ability to successfully resolve these factors raise substantial doubt about the Company s ability to continue as a going concern. The financial statements of the Company do not include any adjustments that may result from the outcome of these aforementioned uncertainties.

**Net Medical Xpress Services, Inc.**

Notes to the Financial Statements

(Unaudited)

## NOTE D - FURNITURE, EQUIPMENT, AND IMPROVEMENTS

Furniture, equipment, and improvements as of June 30, 2013 consisted of the following:

| | |
|---|---|
| Computers | 483,000 |
| Furniture, fixtures and equipment | 132,000 |
| Automobiles | 41,000 |
| Leasehold improvements | 20,000 |
| | 676,000 |
| Accumulated depreciation | (632,000) |
| | $ 44,000 |

Depreciation expense for the six months ended June 30, 2013 and 2012 was $12,000 and $9,000, respectively.

## NOTE E CAPITAL TRANSACTIONS

Common stock:

During the six month period ended June 30, 2013, the Company effected the following stock transactions:

The Company issued a total of 2,000,000 shares of the Company s $0.001 par value common stock to two neurologists in exchange for services for 2013, 2014 and 2015 valued at $60,000. Accordingly, deferred compensation of $60,000 was recorded as of June 30, 2013. The Company expensed $10,000 during the six months ended June 30, 2013.

The Company issued a total of 1,500,000 shares of the Company s $0.001 par value common stock to one director for the exercise of options valued at $45,000.

The Company issued a total of 135,160 shares of the Company s $0.001 par value common stock to one contractor in return for services valued at $10,000.

Warrants:

During the six month period ended June 30, 2013, there were no warrants issued and none were exercised.

There are no warrants outstanding as of June 30, 2013.

Stock options:

Stock options employees and directors During the quarters ended June 30, 2013 and 2012, the Company made no grants of stock options to employees or directors.

Stock options non-employees and directors During the quarters ended June 30, 2013 and 2012, the Company made no grants of stock options for services.

**Net Medical Xpress Services, Inc.**

Notes to the Financial Statements

(Unaudited)

**NOTE E CAPITAL TRANSACTIONS (CONTINUED)**

Exercise prices and weighted-average contractual lives of stock options outstanding as of June 30, 2013, are as follows:

| | Options Outstanding | | | Options Exercisable | |
|---|---|---|---|---|---|
| Exercise Prices | Number Outstanding | Weighted Average Remaining Contractual Life | Weighted Average Exercise Prices | Number Exercisable | Weighted Average Exercise Price |
| $0.03 | 9,500,000 | 3.4 | $0.03 | 9,500,000 | $0.03 |
| $0.06 | 1,053,920 | 0.2 | $0.06 | 1,053,920 | $0.06 |

Summary of Options Granted and Outstanding:

| | For the six months ended June 30, 2013 | |
|---|---|---|
| | Shares | Weighted Average Exercise Price |
| Options: | | |
| Outstanding at beginning of year | 10,553,920 | $0.03 |
| Granted | - | - |
| Cancelled | - | - |
| Exercised | - | - |
| Outstanding at end of period | 10,553,920 | $0.03 |

**NOTE F - MAJOR CUSTOMERS**

During the six month period ended June 30, 2013, two customers accounted for 35% or approximately $843,000 of the Company's revenue.

As of June 30, 2013, balances due from two customers comprised 35% or approximately $273,000 of total accounts receivable.

**NOTE G - REPORTABLE SEGMENTS**

Management has identified the Company's reportable segments based on separate lines of business. The parent company, Net Medical Xpress Solutions, derives revenues from the development and marketing of proprietary internet technology-based software.   The Company  s wholly-owned subsidiary, Telerad Service, Inc., operates under the trade names Net Medical Xpress Services and Net Medical Xpress Specialists.  Net Medical Xpress Services provides medical diagnostic reading services.  Net Medical Xpress Specialists provides telemedicine services to hospitals and other medical entities.

**Net Medical Xpress Services, Inc.**

Notes to the Financial Statements

(Unaudited)

**NOTE G - REPORTABLE SEGMENTS (CONTINUED)**

Information related to the Company's reportable segments for the quarter ended June 30, 2013 is as follows:

| | Solutions | Services | Specialists | TOTAL |
|---|---|---|---|---|
| Revenue | $ 115,000 | $ 1,009,000 | $ 82,000 | $ 1,206,000 |
| Cost of services | 72,000 | 752,000 | 103,000 | 927,000 |
| General and administrative | 64,000 | 100,000 | 61,000 | 225,000 |
| Depreciation | 2,000 | 2,000 | - | 4,000 |
| Research and development | 8,000 | - | 37,000 | 45,000 |
| Operating income (loss) | $ (31,000) | $ 155,000 | $ (119,000) | $ 5,000 |

Information related to the Company's reportable segments for the six months ended June 30, 2013 is as follows:

| | Solutions | Services | Specialists | TOTAL |
|---|---|---|---|---|
| Revenue | $ 245,000 | $ 1,952,000 | $ 230,000 | $ 2,427,000 |
| Cost of services | 124,000 | 1,515,000 | 204,000 | 1,843,000 |
| General and administrative | 180,000 | 160,000 | 111,000 | 451,000 |
| Depreciation | 4,000 | 8,000 | - | 12,000 |
| Research and development | 24,000 | - | 37,000 | 61,000 |
| Operating income (loss) | $ (87,000) | $ 269,000 | $ (122,000) | $ 60,000 |
| Total assets | $ 315,000 | $ 608,000 | $ 224,000 | $ 1,147,000 |

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

| | |
|---|---|
| Segment s operating income | $ 60,000 |

| | |
|---|---|
| Other income (expense) | (6,000) |
| Consolidated net income | $ 54,000 |

**NOTE H COMMITMENTS AND CONTINGENCIES**

Leases:

The Company leases office space in New Mexico expiring on April 30, 2014. The Company also leases computer equipment with lease expiration dates ranging from November 2012 to March 2013, and office equipment with a lease expiration date of June 2014. Future minimum lease payments as of June 30, 2013, are as follows:

| Year | Amount |
|---|---|
| 2013 | $31,000 |
| 2014 | $21,000 |

**Net Medical Xpress Services, Inc.**

Notes to the Financial Statements

(Unaudited)

**NOTE H COMMITMENTS AND CONTINGENCIES (CONTINUED)**

Rent expense for the six months ended June 30, 2013 and 2012 amounted to $37,000 and $32,000, respectively.

**Employment Agreement (Related Party):**

On January 1, 2010, the Company entered into an employment and non-compete agreement with Mr. Govatski to continue in the capacity of President and CEO for an original term ended December 31, 2012. The agreement allowed for a one-year renewal option unless terminated by either party. During the year ended December 31, 2012, Mr. Govatski elected to terminate his agreement in order to increase the cash available for development of the Company s business activities.

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

**NOTE I SUBSEQUENT EVENTS**

On July 1, 2013, the Company agreed to purchase MedTel Solutions, LLC, an Alabama limited liability company that provides medical recruiting and staffing services. The Company agreed to issue 3,000,000 shares upon completion of the purchase agreement, with additional shares to be issued as outlined in the agreement based upon performance goals during the next three years.

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

OVERVIEW

We operate our business in three divisions.

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

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

Our Net Medical Xpress Specialists division provides telemedicine services to hospitals and other medical facilities. We currently employ fifteen credentialed specialists in the field of neurology in this division, which includes stroke assessment. We facilitate real-time assessment of patients through a virtual examination via video conferencing, combined with our proprietary medical software. In addition to stroke assessments, we performed our first behavioral medicine consultations during the second quarter of 2013. Revenues and costs in this division also include sales of our proprietary package of equipment necessary for our medical facility customers to initiate their participation in our specialists program.

We believe gross profit is our key indicator of operating progress. Our three operating divisions generated the following gross profit, rounded to the nearest 1,000, during the first six months of 2013:

| | Solutions | Services | Specialists | TOTAL |
|---|---|---|---|---|
| Revenue | $ 245,000 | $ 1,952,000 | $ 230,000 | $ 2,427,000 |
| Direct costs | 124,000 | 1,515,000 | 204,000 | 1,843,000 |

| | | | | |
|---|---|---|---|---|
| Gross profit | $ 121,000 | $ 437,000 | $ 26,000 | $584,000 |
| Percent | 49% | 22% | 11% | 24% |

Net Medical Xpress Solutions gross profit was $121,000 and 49% of total gross profit during the first six months of 2013, compared to $84,000 and 40% of total gross profit during the same period in 2012. The majority of the direct costs in this division are staffing expenses, which have decreased during 2013 due to less emphasis on this business line and greater emphasis on developing and expanding our specialists program. We expect the percentage of gross profit this division contributes to total gross profit to stabilize at about fifty percent during 2013.

Net Medical Xpress Services gross profit was $437,000 and 22% of total gross profit during the first six months of 2013, compared to $336,000 and 21% of total gross profit during the same period in 2012. Approximately 81% of the direct costs in this division are doctor fees, which are directly related to revenues. The gross profit percentage may change slightly as the mix of services changes. We expect this percentage to remain relatively stable during 2013.

Net Medical Xpress Specialists gross profit was $26,000 and 11% of total gross profit during the first six months of 2013, compared to $3,000 and 8% of total gross profit during the same period in 2012. Approximately 30% of the direct cost in this division consists of relatively fixed costs at this time. The percentage of fixed costs should decrease as revenues increase over the next few years. Approximately 25% of direct costs currently are hardware costs related to the sales of equipment necessary for new customers, which produces a very small gross profit. As the revenues generated by established customers increases, these hardware costs should become less of a factor. In general, we believe the gross profit percentage of this division will increase during 2013 as the revenues grow, while the fixed costs remain stable.

Our normal general and administrative expenses continue to be approximately $200,000 to $250,000 per quarter.

RESULTS OF OPERATIONS

TOTAL REVENUES:

For the Three Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $1,206,000 | $960,000 | $246,000 | 25.6% |

For the Six Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $2,427,000 | $1,883,000 | $544,000 | 28.9% |

These changes are a result of the following factors:

Net Medical Xpress Solutions Revenues

1. Software usage fees:

For the Three Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $102,000 | $90,000 | $12,000 | 13.3% |

For the Six Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $217,000 | $175,000 | $42,000 | 24.0% |

The increase in software usage fees both for the three months and six months ended June 30, 2013 as compared to the same periods in 2012 is primarily due to the increased volume of radiology reports generated for our existing customers, coupled with a slight increase in number of customers. These customers are using our XR-EXpress software to conduct their own businesses.

2. Software hosting and maintenance:

For the Three Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $13,000 | $11,000 | $2,000 | 18.2% |

For the Six Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $27,000 | $22,000 | $5,000 | 22.7% |

This increase is mainly due to the addition of maintenance fees for one new XR-Express customer. Although we still have a few customers using our digital filing cabinet (DFC) product, the majority of our customers and all of our new customers are using our XR-EXpress software. We generally charge usage fees based on radiological reports generated using XR-EXpress, which includes storage of the reports for later access by the customers, rather than monthly hosting fees. We may occasionally charge a monthly maintenance fee for new customers for the use of our XR-Express software. Software maintenance now consists mainly of technical support for our medical software. We expect revenues in this category to stay relatively constant during 2013, as we continue to focus our efforts on growing our telemedicine business, particularly our specialists program.

3. Other revenues:

For the Three Months Ended June 30,

| | 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|---|
| Custom programming | $0 | $11,000 | $(11,000) | (100.0)% |
| Bandwidth | $1,000 | $0 | $1,000 | 100.0% |

For the Six Months Ended June 30,

| | 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|---|
| Custom programming | $0 | $13,000 | $(13,000) | (100.0)% |
| Bandwidth | $1,000 | $0 | $1,000 | 100.0% |

We performed one small custom programming project during the first quarter of 2012. We anticipate undertaking a few small and medium-sized projects that may generate a modest increase in revenues in this category during 2013. We continue to offer programming services for customer database integration, and for other projects for our existing and new customers.

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

Net Medical Xpress Services Revenues

1. Radiological services:

For the Three Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $940,000 | $798,000 | $142,000 | 17.8% |

For the Six Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $1,892,000 | $1,602,000 | $290,000 | 18.1% |

Most of the increase in radiological services (approximately 88%) is due to increased volume of reads by existing customers. The remainder is due to the net addition of new customers.

2. Cardiological services:

For the Three Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $33,000 | $21,000 | $12,000 | 57.1% |

For the Six Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $60,000 | $33,000 | $27,000 | 81.8% |

The increase in cardiological services is due to increased volume of reads for existing customers.

Net Medical Xpress Specialists Revenues

1. Neurological services:

For the Three Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $81,000 | $13,000 | $55,000 | 611.1% |

For the Six Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $145,000 | $22,000 | $55,000 | 611.1% |

Our specialists program began operations during the first quarter of 2012 with a neurology/stroke assessment program at a regional hospital in New Mexico. We have added several new hospitals since that time, and are in the process of adding additional hospitals during 2013. Therefore, we anticipate that revenues in this division will continue to grow during 2013.

2. Behavioral medicine services:

For the Three Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $1,000 | $0 | $1,000 | Not meaningful |

For the Six Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $1,000 | $0 | $1,000 | Not meaningful |

We began providing behavioral medicine consults during the second quarter of 2013.

3. Specialists program hardware sales:

For the Three Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $35,000 | $16,000 | $49,000 | Not meaningful |

For the Six Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $84,000 | $16,000 | $49,000 | Not meaningful |

The specialist program began operations during the first quarter of 2012, with the first hardware sales occurring during the second quarter of 2012. The specialist program hardware sales are sales of our proprietary package of third-party equipment required for a customer to begin using our specialist services. We consider the specialist program to still be in in the startup phase. We expect hardware sales to increase as we add new customers, as well as expand the program to include other services during 2013. Therefore, we anticipate that revenues in this division will continue to grow during 2013. Hardware sales are typically a one-time event with each new customer.

COST OF SERVICES:

For the Three Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $927,000 | $743,000 | $184,000 | 24.8% |

For the Six Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $1,843,000 | $1,460,000 | $383,000 | 26.2% |

Approximately eighty percent of the costs of services for the first three months and six months of 2013 are direct costs related to the services and specialists divisions. These costs consist of radiologist fees, cardiologist fees, neurologist fees, behavioral medicine doctor fees, professional credentialing, professional licenses, professional liability insurance costs, and costs of hardware associated with the specialists program. The majority of these costs are directly related to revenues; as a result, they have increased as the services and specialists revenues have increased.

GENERAL AND ADMINISTRATIVE EXPENSES:

For the Three Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $225,000 | $206,000 | $19,000 | 9.2% |

For the Six Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $451,000 | $408,000 | $43,000 | 10.5% |

The increase in general and administrative expenses is primarily due to increased staffing costs needed to provide additional administrative support for the expanded medical services.

RESEARCH AND DEVELOPMENT COSTS:

For the Three Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $45,000 | $16,000 | $29,000 | 181.3% |

For the Six Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $61,000 | $36,000 | $25,000 | 69.4% |

The increase in research and development costs for the second quarter of 2013 compared to the second quarter of 2012 is due to increased programming costs to continue the development and expansion of the specialists program.

During the first six months of 2013, approximately 90% of our research and development costs were a direct result of staffing.  In the software industry, it is common for research and development costs to be ongoing, since development of the next version of the software begins as soon as the current version is completed.  In addition, we are constantly developing new applications for our existing software.  We anticipate research and development costs during 2013 will continue to focus on the development and expansion of software and services for our specialists program.  As a result, these costs may remain somewhat higher than usual during the coming year.

DEPRECIATION:

For the Three Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $4,000 | $4,000 | $0 | 0.0% |

For the Six Months Ended June 30,

| 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|
| $12,000 | $9,000 | $3,000 | 33.3% |

The increase in depreciation expense is due to a one-time adjustment to the depreciation for capital leases.

OTHER EXPENSE:

For the Three Months Ended June 30,

| | 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|---|
| Interest expense | $4,000 | $3,000 | $1,000 | 33.3% |

For the Six Months Ended June 30,

| | 2013 | 2012 | Increase (Decrease) | Percent Inc (Dec) |
|---|---|---|---|---|
| Interest expense | $6,000 | $5,000 | $2,000 | 40.0% |

There was no significant change in the factors contributing to interest expense during the first six months of 2013 as compared to the first six months of 2012.

REPORTABLE SEGMENTS

We have identified our reportable segments based on separate lines of business, as described in the Overview section above. Net Medical Xpress Solutions derives revenues from the development and marketing of proprietary internet technology-based software. Net Medical Xpress Services provides medical diagnostic reading services. Net Medical Xpress Specialists provides telemedicine services to remote hospitals and other medical entities.

Information about our reportable segments for the quarter ended June 30, 2013 is as follows:

| | Solutions | Services | Specialists | TOTAL |
|---|---|---|---|---|
| Revenue | $ 115,000 | $ 1,009,000 | $ 82,000 | $ 1,206,000 |
| Cost of services | 72,000 | 752,000 | 103,000 | 927,000 |
| General and administrative | 64,000 | 100,000 | 61,000 | 225,000 |
| Depreciation | 2,000 | 2,000 | - | 4,000 |
| Research and development | 8,000 | - | 37,000 | 45,000 |
| Operating income (loss) | $ (31,000) | $ 155,000 | $ (119,000) | $ 5,000 |

Information about our reportable segments for the six months ended June 30, 2013 is as follows:

| | Solutions | Services | Specialists | TOTAL |
|---|---|---|---|---|
| Revenue | $ 245,000 | $ 1,952,000 | $ 230,000 | $ 2,427,000 |
| Cost of services | 124,000 | 1,515,000 | 204,000 | 1,843,000 |
| General and administrative | 180,000 | 160,000 | 111,000 | 451,000 |
| Depreciation | 4,000 | 8,000 | - | 12,000 |
| Research and development | 24,000 | - | 37,000 | 61,000 |

| | | | | |
|---|---|---|---|---|
| Operating income (loss) | $ (87,000) | $ 269,000 | $ (122,000) | $ 60,000 |
| Total assets | $ 312,000 | $ 608,000 | $ 224,000 | $ 1,144,000 |

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

| | |
|---|---|
| Segment s operating income | $ 60,000 |
| Other income (expense) | (6,000) |
| Consolidated net income | $ 54,000 |

LIQUIDITY AND CAPITAL RESOURCES

Liquidity refers to our ability to generate adequate amounts of cash to meet our needs for cash. We believe we will have adequate liquidity during the balance of 2013. As of June 30, 2013, cash and cash equivalents totaled $184,000, representing a $75,000 increase from December 31, 2012. This increase in available cash was due to the following factors during the period:

Operating activities:

For the Six Months Ended June 30,

| 2013 | 2012 | Inc (Dec) in available cash |
|---|---|---|
| provided $36,000 | used $64,000 | $100,000 |

The increase in available cash from operations is mainly due to a combination of the following factors:

- a $55,000 decrease in available cash due to the net decrease in accounts payable and accrued expenses of $77,000 during the first six months of 2013 as compared to a net decrease of $22,000 during the first six months of 2012. The changes in accounts payable are mainly due to changes in doctors fees that vary with revenues throughout the year. The changes in accrued expenses are mainly due to variances in insurance contracts throughout the year.

- a $86,000 increase in available cash due to net income of $51,000 during the first six months of 2013 as compared to net loss of $35,000 during the first quarter of 2012.

- a $44,000 increase in available cash due to the net increase in accounts receivable of $89,000 during the first six months of 2013 as compared to a net increase in accounts receivable of $133,000 during the first six months of 2012. The changes in accounts receivable are mainly due to changes in revenues throughout the year.

- a $34,000 increase in available cash due to the net decrease in prepaid expenses of $79,000 during the first six months of 2013 as compared to a net decrease of $45,000 during the first six months of 2012. The changes in prepaid expenses are mainly the result of variances in insurance contracts throughout the year.

- several small factors combined to net with the above factors, resulting in the $100,000 increase in available cash from operating activities during the first six months of 2013.

Investing activities:

For the Six Months Ended June 30,

| 2013 | 2012 | Inc (Dec) in available cash |
|---|---|---|
| used $5,000 | used $5,000 | $0 |

We purchased $5,000 of computer equipment during the first quarter of 2012 and during the second quarter of 2013.

Financing activities:

For the Six Months Ended June 30,

| 2013 | 2012 | Inc (Dec) in available cash |
|---|---|---|
| provided $44,000 | provided $32,000 | $12,000 |

The changes in financing activities are primarily due to the proceeds from a note payable and the repayment of a note payable during the first six months of 2012.

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

At June 30, 2013, we had a working capital surplus of $221,000 as opposed to a working capital surplus of $55,000 at the beginning of the period, an increase of $166,000.  Although we generated a net profit at the end of 2012, and we expect to increase that profit by the end of 2013, we may continue to sell equity securities and incur debt if needed to meet our operating needs during 2013.

We anticipate that our primary uses of cash in the next year will continue to be for general operating purposes.  We anticipate our operating cash requirements for the next twelve months again to be in the range of $4,000,000 to $5,000,000, although this may increase as the specialists program grows.  This level of cash flow will allow us to maintain our current level of operations and allow for modest growth.  Profitability remains our primary goal.

OFF-BALANCE SHEET ARRANGEMENTS

We currently have no off-balance sheet arrangements.

FORWARD-LOOKING STATEMENTS

This report contains statements that plan for or anticipate the future. Forward-looking statements include statements about the future of operations involving the marketing and maintenance of products which manage large volumes of media or digital material, statements about our future business plans and strategies, and most other statements that are not historical in nature. In this report forward-looking statements are generally identified by the words anticipate, plan, believe, expect, estimate, and the like. Although management believes that any forward-looking statements it makes in this report are reasonable, because forward-looking statements involve future risks and uncertainties, there are factors that could cause actual results to differ materially from those expressed or implied. For example, a few of the uncertainties that could affect the accuracy of forward-looking statements include the following:

.

Rapid changes in technology relating to the Internet

.

Continued growth and use of the Internet

.

Changes in government regulations

.

Changes in our business strategies

.

Hardware failure of a catastrophic proportion

.

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

.

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

.

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

.

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

.

Inability to solve cash flow problems

In light of the significant uncertainties inherent in the forward-looking statements made in this report, particularly in view of our early stage of operation, the inclusion of this information should not be regarded as a representation by us or any other person that our objectives and plans will be achieved.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of our financial statements in conformity with accounting principles generally accepted in the United States (GAAP) requires our management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period.  In accordance with GAAP, our actual realized results may differ from management s initial estimates as reported.  A summary of our significant accounting policies is detailed in the notes to the financial statements, which are an integral component of this filing.

***Revenue Recognition***

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

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

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

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

***Software Development Costs***

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

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

**Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Not applicable.

**Item 4. CONTROLS AND PROCEDURES**

*307 - Disclosure controls and procedures:* As of June 30, 2013, we carried out an evaluation of the effectiveness of our disclosure controls and procedures, with the participation of our principal executive and principal financial officers. Disclosure controls and procedures are defined in Exchange Act Rule 15d 15(e) as controls and other procedures of an issuer that are designed to ensure that information required to be disclosed by the issuer in the reports that it files or submits under the Act (15 U.S.C. 78a *et seq.*) is recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms [and] include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the Act is accumulated and communicated to the issuer's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. Based on our evaluation, our President/Chief Executive Officer and Chief Financial Officer have concluded that, as of June 30, 2013, such disclosure controls and procedures were not effective. The primary reasons for management s conclusions are that we did not have a plan in place for implementing controls and procedures and insufficient personnel to implement checks and balances. We believe that we will not have sufficient funds available to develop a plan in the foreseeable future. We do not anticipate that our business will need sufficient personnel in the foreseeable future that are needed to implement checks and balances.

*308(b) - Changes in internal control over financial reporting:* Based upon an evaluation by our management of our internal control over financial reporting, with the participation of our principal executive and principal financial officers, there were no changes made in our internal control over financial reporting during the quarter ended June 30, 2013 that have materially affected or are reasonably likely to materially affect this control.

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

## PART II

### ITEM 1. LEGAL PROCEEDINGS

Not applicable

### ITEM 1A. RISK FACTORS

Not applicable

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

The following table sets forth information about our unregistered sales of common stock during the six months ended June 30, 2013:

| Class of Purchaser | Aggregate Number of Shares |
|---|---|
| Doctors (1) | 2,000,000 |
| Directors (2) | 1,500,000 |
| Contractors (3) | 135,160 |

(1)

We issued these shares in payment for services valued at $60,000.

(2)

We issued these shares in payment for the exercise of options valued at $45,000.

(3)

We issued these shares in payment for services valued at $10,000.

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

## ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

**ITEM 4. MINE SAFETY DISCLOSURE**

Not applicable.

**ITEM 5. OTHER INFORMATION**

Not applicable.

**ITEM 6. EXHIBITS**

The following exhibits are attached to this report:

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

## SIGNATURES

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

NET MEDICAL XPRESS SOLUTIONS, INC.

| | |
|---|---|
| Date: August 7, 2013 | By /s/ Richard F. Govatski<br>Richard F. Govatski, President (Principal Executive Officer) |
| Date: August 7, 2013 | By /s/ Teresa B. Dickey<br>Teresa B. Dickey, Treasurer (Principal Financial Officer) |