

NET 1 UEPS TECHNOLOGIES INC  
Form 8-K/A  
January 12, 2011

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

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**FORM 8-K/A**

**CURRENT REPORT**

**Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

Date of Report (Date of earliest event reported): **January 12, 2011 (October 29, 2010)**

**NET 1 UEPS TECHNOLOGIES, INC.**

(Exact name of registrant as specified in its charter)

**Florida**  
(State or other jurisdiction  
of incorporation)

**000-31203**  
(Commission  
File Number)

**98-0171860**  
(IRS Employer  
Identification No.)

**President Place, 4<sup>th</sup> Floor, Cnr. Jan Smuts Avenue and Bolton Road  
Rosebank, Johannesburg, South Africa**

(Address of principal executive offices) (ZIP Code)

Registrant's telephone number, including area code: **011-27-11-343-2000**

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions:

- Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)
- Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)
- Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))
- Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))
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**Explanatory Note**

On October 29, 2010, we acquired 98.73% of the issued share capital of KSNET, Inc. ( KSNET ) for a cash payment of KRW 270 billion (the Acquisition ), subject to an estimated post-closing working capital adjustment of \$2.1 million. Under the share purchase agreement, we were required to transfer the movement in net working capital (excluding deferred taxes) between June 30, 2010, and October 29, 2010 to the sellers.

On November 3, 2010, we filed a Current Report on Form 8-K (the Form 8-K ) under Item 2.01 to report the completion of the Acquisition. In response to parts (a) and (b) of Item 9.01 of the Form 8-K, we stated that we would file the required financial information by amendment, as permitted by Item 9.01. This Form 8-K/A is being filed to provide certain historical financial statements of KSNET and pro forma financial information .

**Item 9.01. Financial Statements and Exhibits.**(a) Financial statements of businesses acquired.

|   |             |
|---|-------------|
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(b) Pro forma financial information.

|  |             |
|--|-------------|
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(d) Exhibits

| <b>Exhibits</b> | <b>Description</b>                            |
|-----------------|---|
| <u>23.1</u>     | <u>Consent of Ernst &amp; Young Han Young</u> |

Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders  
KSNET, Inc.

We have audited the accompanying balance sheets of KSNET, Inc. (the Company ) as of December 31, 2009 and 2008, and the related statements of income, changes in equity and comprehensive income, and cash flows for each of the three years in the period ended December 31, 2009. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company at December 31, 2009 and 2008, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2009, in conformity with U.S. generally accepted accounting principles.

/s/ Ernst & Young Han Young  
Seoul, Republic of Korea  
January 10, 2011

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**KSNET, Inc.****BALANCE SHEETS****as of December 31, 2009 and 2008**(In thousands of Korean won,  
except share data)

|  | <b>2009</b>       | <b>2008</b>       |
|--|-------------------|-------------------|
| <b>ASSETS</b>  |                   |                   |
| <b>CURRENT ASSETS</b>  |                   |                   |
| Cash and cash equivalents (Note 6)   | 18,650,898        | 8,097,531         |
| Short-term financial instruments (Notes 3, 6 and 18)   | 2,228,000         | 5,738,000         |
| Accounts receivable, net (Notes 4 and 6)   | 10,911,842        | 7,693,116         |
| Inventory (Note 5)   | 961,153           | 1,029,647         |
| Deferred tax assets (Note 15)  | 482,053           | 729,238           |
| Other current assets (Notes 6, 11 and 20)  | 13,046,226        | 9,796,119         |
| Total current assets   | 46,280,172        | 33,083,651        |
| AVAILABLE-FOR-SALE SECURITIES (Note 6)   | 100,000           | 100,000           |
| PROPERTY AND EQUIPMENT, net (Note 9)   | 24,870,181        | 20,545,591        |
| INTANGIBLE ASSETS, net (Note 10)   | 23,385            | 30,772            |
| NON-CURRENT ACCOUNTS RECEIVABLE, net (Notes 4 and 6)   | 1,906,418         | 2,889,876         |
| NON-CURRENT DEFERRED TAX ASSETS (Note 15)  | -                 | 38,918            |
| OTHER NON-CURRENT ASSETS (Notes 3, 6 and 11)   | 5,568,270         | 5,751,657         |
| <b>TOTAL ASSETS</b>  | <b>78,748,426</b> | <b>62,440,465</b> |
| <b>LIABILITIES</b>   |                   |                   |
| <b>CURRENT LIABILITIES</b>   |                   |                   |
| Accounts payable (Note 6)  | 6,462,841         | 4,301,624         |
| Short-term borrowings (Note 6)   | -                 | 4,000,000         |
| Current portion of long-term debt (Notes 6 and 8)  | 10,000,000        | -                 |
| Other current liabilities (Notes 6, 7, 11 and 20)  | 16,744,433        | 13,617,056        |
| Total current liabilities  | 33,207,274        | 21,918,680        |
| LONG-TERM DEBT (Notes 6 and 8)   | -                 | 4,000,000         |
| ACCRUED SEVERANCE BENEFITS, net (Note 14)  | 749,779           | 733,989           |
| NON-CURRENT DEFERRED TAX LIABILITIES (Note 15)   | 389,488           | -                 |
| OTHER NON-CURRENT LIABILITIES (Notes 11 and 15)  | 963,778           | -                 |
| <b>TOTAL LIABILITIES</b>   | <b>35,310,319</b> | <b>26,652,669</b> |
| <b>EQUITY</b>  |                   |                   |
| COMMON STOCK (Note 13)   | 6,802,883         | 7,275,892         |
| Authorized shares: 36,500,000 with 500 par value at December 31, 2009 and 2008                       |                   |                   |
| Issued and outstanding shares: 13,605,766 and 14,551,784 at December 31, 2009 and 2008, respectively |                   |                   |
| ADDITIONAL PAID-IN-CAPITAL (Note 13)   | 33,568            | 33,568            |
| RETAINED EARNINGS  | 36,601,656        | 28,478,336        |
| <b>TOTAL EQUITY</b>  | <b>43,438,107</b> | <b>35,787,796</b> |
| <b>TOTAL LIABILITIES AND EQUITY</b>  | <b>78,748,426</b> | <b>62,440,465</b> |

See accompanying notes to financial statements.



**KSNET, Inc**  
**STATEMENTS OF INCOME**  
**for the years ended December 31, 2009, 2008 and 2007**

(In thousands of Korean won, except per share data)

|   | <b>2009</b> | <b>2008</b> | <b>2007</b> |
|---|-------------|-------------|-------------|
| <b>REVENUE</b>                                      |             |             |             |
| Services rendered                                   | 87,382,235  | 72,434,882  | 66,306,804  |
| Sale of merchandise (Note 20)                       | 2,657,854   | 3,260,281   | 4,025,601   |
| Others  | 196,260     | 345,838     | 47,707      |
|   | 90,236,349  | 76,041,001  | 70,380,112  |
| <b>EXPENSE</b>                                      |             |             |             |
| Cost of services rendered                           | 45,193,746  | 36,384,790  | 32,371,800  |
| Cost of merchandise sold (Note 20)                  | 2,694,231   | 3,411,359   | 4,167,976   |
| Selling, general and administrative expenses        | 23,804,823  | 1,759,563   | 21,571,238  |
| Depreciation and amortization                       | 3,057,302   | 3,072,933   | 2,741,552   |
|   | 74,750,102  | 64,628,645  | 60,852,566  |
| <b>OPERATING INCOME</b>                             | 15,486,247  | 11,412,356  | 9,527,546   |
| <b>INTEREST INCOME, net</b>                         | 209,430     | 1,152,529   | 3,154,316   |
| <b>OTHER INCOME (EXPENSE), net (Note 12)</b>        | 47,436      | (252,551)   | 158,596     |
| <b>INCOME BEFORE INCOME TAXES</b>                   | 15,743,113  | 12,312,334  | 12,840,458  |
| <b>INCOME TAX EXPENSE (Note 15)</b>                 | 3,851,074   | 3,135,605   | 4,274,357   |
| <b>NET INCOME</b>                                   | 11,892,039  | 9,176,729   | 8,566,101   |
| <b>Net income per share (Note 16)</b>               |             |             |             |
| Basic earnings attributable to KSNET shareholders   | 862         | 616         | 529         |
| Diluted earnings attributable to KSNET shareholders | 862         | 616         | 424         |

See accompanying notes to financial statements.

## KSNET, Inc.

## STATEMENTS OF CHANGES IN EQUITY AND COMPREHENSIVE INCOME (in thousands of Korean won, except share data)

for the years ended December 31, 2009, 2008 and 2007

|   |                  | Common stock |                |                            |                  | Preferred stock |                            |                   |
|---|------------------|--------------|----------------|----------------------------|------------------|-----------------|----------------------------|-------------------|
|   | Number of shares | Amount       | Treasury stock | Additional paid-in capital | Number of shares | Amount          | Additional paid-in capital | Retained earnings |
| Balance Jan. 1, 2007  | 16,355,138       | 8,177,569    | (329,156)      | 33,568                     | 4,000,000        | 2,000,000       | 40,701,975                 | 33,459,687        |
| Exercise of stock warrants                                  | 16,000           | 8,000        | -              | -                          | -                | -               | -                          | -                 |
| Comprehensive income:                                       | -                | -            | -              | -                          | -                | -               | -                          | -                 |
| Net income  | -                | -            | -              | -                          | -                | -               | -                          | 8,566,101         |
| Balance Dec. 31, 2007                                       | 16,371,138       | 8,185,569    | (329,156)      | 33,568                     | 4,000,000        | 2,000,000       | 40,701,975                 | 42,025,788        |
| Balance Jan. 1, 2008  | 16,371,138       | 8,185,569    | (329,156)      | 33,568                     | 4,000,000        | 2,000,000       | 40,701,975                 | 42,025,788        |
| Capital reduction common stock                              | (1,654,776)      | (827,388)    | -              | -                          | -                | -               | -                          | (6,327,289)       |
| Capital reduction preferred stock                           | -                | -            | -              | -                          | (4,000,000)      | (2,000,000)     | (40,701,975)               | (16,150,025)      |
| Stock retirement  | (164,578)        | (82,289)     | 329,156        | -                          | -                | -               | -                          | (246,867)         |
| Comprehensive income:                                       | -                | -            | -              | -                          | -                | -               | -                          | -                 |
| Net income  | -                | -            | -              | -                          | -                | -               | -                          | 9,176,729         |
| Balance Dec. 31, 2008                                       | 14,551,784       | 7,275,892    | -              | 33,568                     | -                | -               | -                          | 28,478,336        |
| Balance Jan. 1, 2009  | 14,551,784       | 7,275,892    | -              | 33,568                     | -                | -               | -                          | 28,478,336        |
| Adoption of FIN 48 -adjustment to opening retained earnings | -                | -            | -              | -                          | -                | -               | -                          | (154,210)         |
| Revised retained earnings                                   | -                | -            | -              | -                          | -                | -               | -                          | 28,324,126        |
| Capital reduction   | (946,018)        | (473,009)    | -              | -                          | -                | -               | -                          | (3,614,509)       |
| Comprehensive income:                                       | -                | -            | -              | -                          | -                | -               | -                          | -                 |

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|                          |            |           |   |        |   |   |   |            |
|--------------------------|------------|-----------|---|--------|---|---|---|------------|
| Net income               | -          | -         | - | -      | - | - | - | 11,892,039 |
| Balance Dec.<br>31, 2009 | 13,605,766 | 6,802,883 | - | 33,568 | - | - | - | 36,601,656 |

See accompanying notes to financial statements.

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**KSNET, Inc.****STATEMENTS OF CASH FLOWS****for the years ended December 31, 2009, 2008 and 2007**

|  | (In thousands of Korean won) |                  |                  |
|--|------------------------------|------------------|------------------|
|  | <b>2009</b>                  | <b>2008</b>      | <b>2007</b>      |
| <b>Cash flows from operating activities</b>                                      |                              |                  |                  |
| Net income   | 11,892,039                   | 9,176,729        | 8,566,101        |
| Adjustments to reconcile net income to net cash provided by operating activities |                              |                  |                  |
| Provision for severance benefits   | 795,660                      | 944,342          | 887,842          |
| Depreciation and amortization  | 9,893,357                    | 8,469,269        | 7,554,783        |
| Loss (gain) on disposal of property and equipment                                | (6,503)                      | 92,355           | 4,212            |
| Loss (gain) on valuation of derivatives  | (69,567)                     | 91,833           | -                |
| Gain on disposal of investment securities  | -                            | -                | (215,948)        |
| Bad debt expenses  | (138,328)                    | 204,459          | (269,892)        |
| Changes in operating assets and liabilities:                                     |                              |                  |                  |
| Decrease (increase) in long-term accounts receivable                             | 983,457                      | (343,593)        | (859,125)        |
| Increase in accounts receivable  | (3,109,970)                  | (1,184,438)      | (562,333)        |
| Decrease (increase) in other receivables   | 89,734                       | (102,420)        | (34,318)         |
| Decrease in accrued income   | 62,234                       | 511,817          | 18,662           |
| Decrease (increase) in advanced payments   | 1,558,187                    | (385,740)        | (2,027,581)      |
| Increase in prepaid expenses   | (4,938,925)                  | (3,311,860)      | (68,116)         |
| Decrease (increase) in inventory   | (12,002,583)                 | (7,752,580)      | (5,449,491)      |
| Decrease (increase) in guarantee deposits  | (153,487)                    | 1,432,905        | 343,8820         |
| Decrease in deferred tax assets  | 286,103                      | 74,500           | 99,355           |
| (Decrease) increase in deferred tax liabilities                                  | 389,488                      | (95,930)         | 95,930           |
| Decrease in accounts payable   | 2,161,217                    | 676,297          | 3,148,047        |
| Increase in other payables   | 90,457                       | (406,558)        | (2,307,639)      |
| (Decrease) increase in advances from customers                                   | (161,577)                    | (106,398)        | 106,349          |
| (Decrease) increase in value-added tax payable                                   | 317,233                      | 15,516           | (179,587)        |
| Increase in accrued expenses   | 28,398                       | 68,978           | 27,485           |
| Decrease in deposits received  | (190,156)                    | (20,869)         | (53,124)         |
| Increase in withholdings   | 3,439,170                    | 1,753,869        | 2,208,543        |
| Decrease in income taxes payable   | (326,582)                    | (91,536)         | (9,864)          |
| Increase in other non-current liabilities  | 809,567                      | -                | -                |
| (Decrease) increase in deposit for severance benefits                            | (448,515)                    | 294,600          | (318,622)        |
| insurance  |                              |                  |                  |
| Payment of severance benefits  | (331,355)                    | (1,368,019)      | (921,628)        |
| <b>Net cash provided by operating activities</b>                                 | <b>10,918,753</b>            | <b>8,637,528</b> | <b>9,783,861</b> |
| <b>Cash flows from investing activities</b>                                      |                              |                  |                  |
| Decrease in short-term financial instruments                                     | 3,510,000                    | 7,293,325        | 21,065,055       |
| Decrease in restricted cash  | -                            | 24,428           | -                |
| Proceeds from sale of investment securities                                      | -                            | -                | 329,240          |
| Decrease in short-term loans   | 43,140                       | 6,175            | 83,459           |
| Decrease in long-term loans  | 736,912                      | 554,111          | 567,992          |
| Decrease in other investment   | -                            | -                | 101,650          |
| Proceeds from the disposal of property and equipment                             | 174,112                      | 316,752          | 77,824           |
| Increase in restricted cash  | -                            | -                | (24,428)         |
| Increase in long-term financial instruments                                      | (6,000)                      | (6,000)          | (133,000)        |

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|  |                  |                  |                   |
|--|------------------|------------------|-------------------|
| Acquisition of investment securities                       | -                | (100,000)        | -                 |
| Increase in short-term loans                               | (53,000)         | -                | (35,000)          |
| Increase in long-term loans                                | (375,000)        | (826,880)        | (309,400)         |
| Increase in other investment                               | (942)            | (174,187)        | -                 |
| Acquisition of property and equipment                      | (2,307,090)      | (2,653,533)      | (3,619,765)       |
| <b>Net cash (used in) provided by investing activities</b> | <b>1,722,132</b> | <b>4,434,191</b> | <b>18,103,627</b> |

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**KSNET, Inc.****STATEMENTS OF CASH FLOWS (continued)**

for the years ended December 31, 2009, 2008 and 2007

|   | (In thousands of Korean won) |                     |                   |
|---|------------------------------|---------------------|-------------------|
|   | 2009                         | 2008                | 2007              |
| <b>Cash flows from financing activities</b>                 |                              |                     |                   |
| Proceeds from short-term borrowings                         | -                            | 4,000,000           | 8,000             |
| Proceeds from issuance of long-term debt                    | 6,000,000                    | 4,000,000           | -                 |
| Repayment of current portion of long-term debt              | -                            | -                   | (8,000)           |
| Repayment of short-term borrowings                          | (4,000,000)                  | -                   | (2,500)           |
| Capital reduction   | (4,087,518)                  | (66,006,677)        | -                 |
| <b>Net cash used in financing activities</b>                | <b>(2,087,518)</b>           | <b>(58,006,677)</b> | <b>(2,500)</b>    |
| <b>Net increase (decrease) in cash and cash equivalents</b> | <b>10,553,367</b>            | <b>(44,934,958)</b> | <b>27,884,988</b> |
| <b>Cash and cash equivalents beginning of year</b>          | <b>8,097,531</b>             | <b>53,032,489</b>   | <b>25,147,501</b> |
| <b>Cash and cash equivalents at end of year</b>             | <b>18,650,898</b>            | <b>8,097,531</b>    | <b>53,032,489</b> |

**Non cash transaction**

|   | 2009       | 2008      | 2007      |
|---|------------|-----------|-----------|
| Transfer from inventory to property and equipment | 12,071,077 | 7,259,169 | 5,546,053 |
| See accompanying notes to financial statements.   |            |           |           |

**KSNET, Inc.****Notes to the Financial Statements****for the years ended December 31, 2009, 2008 and 2007****(All amounts stated in thousands of Korean won, unless otherwise stated)****1. DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION****Description of business**

KSNET, Inc. (the Company) was established through split-off from Chosun I&C on December 30, 1999 and engages in providing Value Added Network (VAN) services and the sale of communication equipment in the Republic of Korea.

The Company's capital stock amounts to 6,802,883 thousand as of December 31, 2009 and the Company's shareholders and their ownership as of December 31, 2009 are as follows:

|                           | Number of shares | Ownership (%) |
|---------------------------|------------------|---------------|
| H&QNPS Van Investment     | 6,716,500        | 49.37         |
| Payment Services Asia LLC | 6,716,500        | 49.37         |
| Others                    | 172,766          | 1.26          |
|                           | 13,605,766       | 100.00        |

**Basis of presentation**

The Company maintains its accounting records in Korean won and the accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ( US GAAP ).

**2. SIGNIFICANT ACCOUNTING POLICIES****Use of estimates**

The preparation of the Company's financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant items subject to such estimates and assumptions include the useful lives of property and equipment; allowances for doubtful accounts; the valuation of derivatives, deferred tax assets, property and equipment, inventory, investment securities; and accrued severance benefits, income tax uncertainties and other contingencies.

**Cash and cash equivalents**

The Company considers cash equivalents as all highly liquid investments and short-term financial instruments, which are readily convertible to cash without significant transaction cost, and do not carry significant risk from changes in interest rates, and with maturities of three months or less when purchased. Cash and cash equivalents mainly consist of money market trust and checking deposits.

**Allowance for doubtful accounts**

Allowance for doubtful accounts is estimated based on an analysis and past experience of collections of

individual accounts such as accounts receivable, other receivables and loans. Allowance for doubtful accounts is presented as a deduction from receivables. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote.

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**KSNET, Inc.****Notes to the Financial Statements****for the years ended December 31, 2009, 2008 and 2007****(All amounts stated in thousands of Korean won, unless otherwise stated)****2. SIGNIFICANT ACCOUNTING POLICIES (continued)****Property and equipment**

Property and equipment are shown at cost less accumulated depreciation. Property and equipment are depreciated on the straight-line basis at rates which are estimated to depreciate the assets to their anticipated residual values over their useful lives. Within the following asset classifications, the expected economic lives are approximately:

|                               |              |
|-------------------------------|--------------|
| Buildings                     | 30 years     |
| Structures                    | 8 years      |
| Vehicles                      | 4 years      |
| Tools, furniture and fixtures | 3 to 4 years |
| Machinery and equipment       | 8 years      |
| Software                      | 5 years      |

The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognized in the statements of income.

Property and equipment do not require that an annual impairment test be performed; instead, they are tested for impairment upon the occurrence of a triggering event. Triggering events include the more likely than not disposal of a portion of such assets or the occurrence of an adverse change in the market involving the business employing the related assets. There were no impairment losses for the years ended December 31, 2009, 2008 and 2007.

**Sales taxes**

Revenues and expenses are presented net of value added taxes, as the case may be.

**Income taxes**

The Company provides for income taxes using the asset and liability method. This approach recognizes the amount of taxes payable or refundable for the current year, as well as deferred tax assets and liabilities for the future tax consequence of events recognized in the financial statements and tax returns. Deferred income taxes are adjusted to reflect the effects of changes in tax laws or enacted tax rates. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Under the Corporate Tax Act in the Republic of Korea, corporate taxpayers are subject to corporate income taxes on taxable income at 22% (10% is applicable to the first 200 million of taxable income) in 2009. On top of the corporate income tax, 10% resident surtax is also assessed; thus the statutory tax rate becomes 24.2% or 11% depending on the amount of taxable income; therefore, the income tax rate during the year ended December 31, 2009 was 24.2%. The income tax rate during the years ended December 31, 2008 and 2007 was 27.5% (including 10% resident surtax).

In establishing the appropriate income tax valuation allowances, the Company assesses the realizability of its net deferred tax assets, and based on all available evidence, both positive and negative, determines whether it is more likely than not that the net deferred tax assets or a portion thereof will be realized.

Effective January 1, 2009, the Company adopted the provisions of Accounting Standards Codification ( ASC ) 740, *Income Taxes*, which set outs a consistent framework to determine the appropriate level of tax reserve for uncertain tax positions. The Company uses a two-step approach wherein a tax benefit is recognized if a position is more-likely-than-not to be sustained. The amount of the benefit is then measured as the highest tax benefit which is greater than 50% likely to be realized. The difference between the benefit recognized for a position in accordance with ASC 740 and the tax benefit claimed on a tax return is referred to as an unrecognized tax benefit.

The Company s policy is to include interest related to unrecognized tax benefits in interest income, net and penalties in selling, general and administration in the statements of income.

## **KSNET, Inc.**

### **Notes to the Financial Statements**

**for the years ended December 31, 2009, 2008 and 2007**

**(All amounts stated in thousands of Korean won, unless otherwise stated)**

#### **2. SIGNIFICANT ACCOUNTING POLICIES (continued)**

##### **Intangible assets**

Intangible assets are shown at cost less accumulated amortization. Intangible assets are amortized over the following useful lives:

|            |          |
|------------|----------|
| Trademarks | 10 years |
|------------|----------|

Intangible assets are periodically evaluated for recoverability, and those evaluations take into account events or circumstances that warrant revised estimates of useful lives or that indicate an impairment exists.

##### **Research and development expenditures**

Research expenditures are charged to net income in the period in which they are incurred.

Costs in respect of the development of software for the Company's internal use are expensed as incurred, except to the extent that these costs are incurred during the application development stage. All other costs including those incurred in the project development and post-implementation stages are expensed as incurred. For the years ended December 31, 2009, 2008 and 2007, the amount of research and development expenditures charged to net income were 69,000 thousand, 86,800 thousand and 68,000 thousand, respectively.

##### **Inventory**

Inventory is stated at the lower of cost or market value. Cost is determined on a first-in, first-out basis and includes transport and handling costs.

##### **Investment securities**

The Company classifies its debt security into available-for-sale security. The Company classifies its equity securities that do not have readily determinable fair values as other investment securities and those securities are stated at cost.

The Company reviews its investment portfolio each reporting period to determine whether there are identified events or circumstances that would indicate there is a decline in the fair value that is considered to be other-than-temporary. For other securities which are stated at cost, if there are no identified events or circumstances that would have a material adverse effect on the fair value of the investment, then the fair value is not estimated. If an investment is deemed to have experienced an other-than-temporary decline below its cost basis, the Company reduces the carrying amount of the investment to its quoted or estimated fair value, as applicable, and establishes a new cost basis for the investment. There was no impairment loss on investment securities recognized for the years ended December 31, 2009, 2008 and 2007.

##### **Fair value measurements**

The Company applies fair value accounting for all financial assets and liabilities and non-financial assets and liabilities that are recognized or disclosed at fair value in the financial statements. The Company defines fair value as



the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities, which are required to be recorded at fair value, the Company considers the principal or most advantageous market in which the Company would transact and the market-based risk measurements or assumptions that market participants would use in pricing the asset or liability, such as inherent risk, transfer restrictions and credit risk. ASC 820, *Fair Value Measurements and Disclosure* ( ASC 820 ), establishes a framework for measuring fair value and expands disclosures about fair value measurements.

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## **KSNET, Inc.**

### **Notes to the Financial Statements**

**for the years ended December 31, 2009, 2008 and 2007**

**(All amounts stated in thousands of Korean won, unless otherwise stated)**

#### **2. SIGNIFICANT ACCOUNTING POLICIES (continued)**

##### **Derivatives**

The Company recognizes all derivative financial instruments in the balance sheets as either assets or liabilities at fair value.

For a derivative financial instrument not designated as a hedging instrument, the gain or loss is recognized in earnings in the period of change.

##### **Revenue recognition**

The Company recognizes revenue when:

- There is persuasive evidence of an agreement or arrangement;
- Delivery of products has occurred or services have been rendered;
- The seller's price to the buyer is fixed or determinable; and
- Collectability is reasonably assured.

The Company's revenue mainly consists of revenue from Card VAN, Banking VAN, Payment Gateway (PG) and sale of merchandise. The Company's revenue recognition methods for each component are as follows:

##### *Card VAN*

Card VAN services consist of services relating to authorization of credit card transactions including transmission of transaction details (Authorization Service), and collection of receipts associated with the credit card transactions (Collection Service). With its Authorization Service, the Company connects credit card companies with merchants online when a customer uses his/her credit card via terminals installed at merchants' sites and the Company's central processing server for approval of credit card transactions. Immediately after approval of credit card transactions, the Company transmits details of the transactions to credit card companies online for processing payments. Collection Service captures the transaction data and gathers receipts as documented evidences and provides them to credit card companies upon request. The Company earns service fees based on the number of processed transactions for credit card companies when services are rendered in accordance with the contracts entered into between credit card companies and the Company. The Company bills for its service charges to credit card companies each month. Each service could be provided either individually or collectively, based on terms of contracts.

The Company charges commission fee to credit card companies for the Authorization Service provided based on the number of approvals transferred. The right to receive fee for services rendered will take effect as credit card transactions are approved and details of the transactions are transmitted. Therefore, revenues from the Authorization Service are recognized when the credit card transactions are authorized and details of the transactions are transmitted. In the case of Collection Service, the Company is not allowed to receive its commission fees until it provides collected receipts to the credit card companies. Therefore, revenue from the Collection Service is recognized when the Company collects the receipts and provides them to the card companies.

For multi-element arrangements, the Company has identified two deliverables in arrangements. The first

deliverable is the Authorization Service, and the second deliverable is the Collection Service. The Company evaluates each deliverable in an arrangement to determine whether they represent separate units of accounting. A deliverable constitutes a separate unit of accounting when it has standalone value and there are no customer-negotiated refunds or return rights for the delivered elements. If the arrangement includes a customer-negotiated refund or return right relative to the delivered item and the delivery and performance of the undelivered item is considered probable and substantially in the Company's control, the delivered element constitutes a separate unit of accounting. In instances when the aforementioned criteria are not met, the deliverable is combined with the undelivered elements and the allocation of the arrangement consideration and revenue recognition is determined for the combined unit as a single unit. Allocation of the consideration is determined at arrangement inception on the basis of each unit's relative selling price. In such circumstances, the Company uses a hierarchy to determine the selling price to be used for allocating revenue to deliverables: (i) vendor-specific objective evidence of fair value ( VSOE ), (ii) third-party evidence of selling price ( TPE ), and (iii) best estimate of the selling price ( ESP ).

## **KSNET, Inc.**

### **Notes to the Financial Statements**

**for the years ended December 31, 2009, 2008 and 2007**

**(All amounts stated in thousands of Korean won, unless otherwise stated)**

#### **2. SIGNIFICANT ACCOUNTING POLICIES (continued)**

##### **Revenue recognition (continued)**

###### *Card VAN (continued)*

VSOE generally exists only when the Company sells the deliverable separately and is the price actually charged by the Company for that deliverable. ESPs reflect the Company's best estimates of what the selling prices of elements would be if they were sold regularly on a stand-alone basis. Because the Company has neither VSOE nor TPE for the two deliverables, the allocation of revenue has been based on the Company's ESPs. Amounts allocated to the Authorization and the Collection Service are recognized at the time of service provided the other conditions for revenue recognition have been met.

The Company's process for determining its ESP for deliverables without VSOE or TPE considers multiple factors that may vary depending upon the unique facts and circumstances related to each deliverable. Key factors considered by the Company in developing the ESPs include prices charged by the Company, historical pricing practices and controls, range of prices for various customers and the nature of the services. Consideration is also given to market conditions such as competitor pricing strategies and market perception.

###### *Banking VAN*

Banking VAN is a division supporting a Company's fund management business (large payment transfers, collections, etc.) by relaying financial transactions between client companies and financial institutions. Financial transactions between two or more business enterprises, or between business enterprises and their customers, are conducted through the transaction-processing network established between the Company and the banks. Revenue from the Banking Van service is recognized when the service is rendered by the Company.

###### *Payment Gateway service (PG service)*

With its PG service, the Company provides the Internet-based settlement service between on-line shopping mall and a credit card company when a customer uses his/her credit card, debit card or on-line payment to pay for goods or services. The Company receives fees for carrying out settlements for electronic transactions. Revenue from the PG service is recognized when the service is rendered by the Company.

###### *Sale of merchandise*

The Company buys terminals from manufacturers, and subsequently sells them through its subsidiary agencies. Revenue is recognized when significant risks and rewards of ownership of terminals have passed to the buyer, usually on delivery of the terminals to the buyer.

##### **Accrued severance benefits**

Employees and directors are entitled to receive a lump-sum payment upon termination of their employment with the Company, based on their length of service and rate of pay at the time of termination. Accrued severance benefits are estimated assuming all eligible employees were to terminate their employment at the balance sheet date. The

annual severance benefits expense charged to income is calculated based on the net change in the accrued severance benefits payable at the balance sheet date, plus the actual payments made during the year.

The contributions to the severance insurance deposit are deducted from accrued severance benefit liabilities. Contributed amounts are refunded from the insurance company to employees upon their retirement.

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## **KSNET, Inc.**

### **Notes to the Financial Statements**

**for the years ended December 31, 2009, 2008 and 2007**

**(All amounts stated in thousands of Korean won, unless otherwise stated)**

#### **2. SIGNIFICANT ACCOUNTING POLICIES (continued)**

##### **Commitments and contingencies**

Liabilities arising from claims, assessments, litigation, fines, and penalties and other sources, are recorded when it is probable that a liability has been incurred and the amount of the assessment and/or remediation can be reasonably estimated. Legal costs incurred in connection with loss contingencies are expensed as incurred.

##### **Earnings per share**

Basic earnings per share are computed by dividing net income by the weighted-average number of shares of common stock outstanding during the year. Diluted earnings per share are calculated by dividing net income by the weighted-average number of shares of common stock outstanding during the year plus the weighted-average number of common shares that would have been outstanding assuming the conversion of all dilutive potential common shares.

##### **Recent accounting pronouncements adopted**

In June 2009, the Financial Accounting Standards Board ( FASB ) issued the FASB Accounting Standards Codification (the Codification ) as the single source of authoritative GAAP recognized by the FASB to be applied by non-governmental entities. The Codification supersedes all existing non-SEC accounting and reporting standards. Following the issue of the Codification, the FASB has issued new guidance in the form of Accounting Standards Updates. This Codification is effective for financial statements issued for interim and annual periods ending after September 15, 2009. The Codification was effective for the Company from January 1, 2009. The Codification did not impact the Company's financial position or results of operations.

In September 2009, the FASB issued guidance on revenue recognition in multiple-deliverable revenue arrangements. The guidance amended the existing guidance on allocating consideration received between the elements in a multiple-deliverable arrangement and established a selling price hierarchy for determining the selling price of a deliverable. The selling price used for each deliverable will be based on vendor-specific objective evidence ( VSOE ) if available, third-party evidence if VSOE is not available, or estimated selling price if neither VSOE nor third-party evidence is available. The guidance replaced the term fair value in the revenue allocation with selling price to clarify that the allocation of revenue is based on entity specific assumptions rather than the assumptions of a market place participant. The guidance eliminates the residual method of allocation and requires that arrangement consideration be allocated using the relative selling price method. It also significantly expands the disclosures related to a vendor's multiple-deliverable revenue arrangements. Earlier application is permitted. The Company adopted these new accounting standards in the beginning of 2007.

In October 2009, the FASB issued guidance which amended the scope of existing software revenue recognition accounting. Tangible products containing software components and non-software components that function together to deliver the product's essential functionality would be scoped out of the accounting guidance on software and accounted for based on other appropriate revenue recognition guidance. This guidance must be adopted in the same period that the company adopts the amended guidance for arrangements with multiple deliverables described in the preceding paragraph. The adoption of this guidance did not have an impact on the Company's financial position or results of operations.



**KSNET, Inc.****Notes to the Financial Statements****for the years ended December 31, 2009, 2008 and 2007****(All amounts stated in thousands of Korean won, unless otherwise stated)****2. SIGNIFICANT ACCOUNTING POLICIES (continued)****Recent accounting pronouncements not yet adopted as of December 31, 2009**

In January 2010, the FASB issued Update 2010-06, *Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements*, ( Update 2010-06 ). Update 2010-06 amends ASC 820 and clarifies and provides additional disclosure requirements related to recurring and non-recurring fair value measurements and employers' disclosures about postretirement benefit plan assets. This Update became effective for us on January 1, 2010. The Company is currently evaluating the impact of the adoption of Update 2010-16.

In July 2010, the FASB issued amendments to the disclosure requirements about the credit quality of financing receivables and the allowance for credit losses. The purpose of the additional disclosures is to enable users of financial statements to better understand the nature of credit risk inherent in an entity's portfolio of financing receivables and how that risk is analyzed. For end of period balances, the new disclosures are required to be made in all interim and annual periods ending on or after December 15, 2010. For activity during a reporting period, the disclosures are required to be made in all interim and annual periods after January 1, 2011. These changes will not have an impact on the Company's financial results as this guidance only relates to additional disclosures.

**3. RESTRICTED FINANCIAL INSTRUMENTS**

The following table represents financial instruments which are restricted in use as of December 31, 2009 and 2008.

|                                  | <b>Restriction</b>   | <b>2009</b>    | <b>2008</b>   |
|----------------------------------|--|----------------|---------------|
| Short-term financial instruments | Pledge   | 658,000        | 738,000       |
| Long-term financial instruments  | Pledge, guarantee deposits<br>for checking account and<br>others | 3,000          | 3,000         |
| <b>Total</b>                     |  | <b>661,000</b> | <b>41,000</b> |

The amount of restricted short-term financial instrument above is included in short-term financial instruments and the amount of restricted long-term financial instrument above is included in other non-current assets on the balance sheets.

**4. ACCOUNTS RECEIVABLE**

The following table presents current and non-current accounts receivable at December 31, 2009 and 2008:

**Current accounts receivable, net**

|   | <b>2009</b>       | <b>2008</b>      |
|---|-------------------|------------------|
| Current accounts receivable             | 11,113,442        | 7,994,139        |
| Discount on current accounts receivable | (7,236)           | (9,336)          |
| Allowance for doubtful accounts         | (194,364)         | (291,687)        |
| <b>Current accounts receivable, net</b> | <b>10,911,842</b> | <b>7,693,116</b> |

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**KSNET, Inc.****Notes to the Financial Statements****for the years ended December 31, 2009, 2008 and 2007****(All amounts stated in thousands of Korean won, unless otherwise stated)****4. ACCOUNTS RECEIVABLE (continued)****Non-current accounts receivable, net**

|   | <b>2009</b>      | <b>2008</b>      |
|---|------------------|------------------|
| Non-current accounts receivable             | 2,132,551        | 3,275,848        |
| Discount on accounts receivable             | (204,807)        | (353,214)        |
| Allowance for doubtful accounts             | (21,326)         | (32,758)         |
| <b>Non-current accounts receivable, net</b> | <b>1,906,418</b> | <b>2,889,876</b> |

Non-current accounts receivable arose from installment sales of Point of Sale ( POS ) terminals for the three years to merchants. Non-current accounts receivable amounts are determined based on the present value using appropriate risk adjusted discount rate considering environment of counter-party.

**5. INVENTORY**

Inventory valuations as of December 31, 2009 and 2008 are summarized as follows:

|              | As of December 31, 2009 |                            |                        |
|--------------|-------------------------|----------------------------|------------------------|
|              | Cost                    | Lower of cost or<br>market | Valuation<br>allowance |
| Inventory:   |                         |                            |                        |
| Merchandise  | 961,153                 | 961,153                    | -                      |
| <b>Total</b> | <b>961,153</b>          | <b>961,153</b>             | <b>-</b>               |

|              | As of December 31, 2008 |                            |                        |
|--------------|-------------------------|----------------------------|------------------------|
|              | Cost                    | Lower of cost or<br>market | Valuation<br>allowance |
| Inventory:   |                         |                            |                        |
| Merchandise  | 1,029,647               | 1,029,647                  | -                      |
| <b>Total</b> | <b>1,029,647</b>        | <b>1,029,647</b>           | <b>-</b>               |

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**KSNET, Inc.****Notes to the Financial Statements****for the years ended December 31, 2009, 2008 and 2007****(All amounts stated in thousands of Korean won, unless otherwise stated)****6. FAIR VALUE MEASUREMENTS****Fair value of financial instruments**

The following table presents the carrying amounts and estimated fair values of the Company's financial instruments at December 31, 2009 and 2008.

|                                      | 2009              |                   | 2008              |                   |
|--------------------------------------|-------------------|-------------------|-------------------|-------------------|
|                                      | Carrying amount   | Fair value        | Carrying amount   | Fair value        |
| <b>Financial assets:</b>             |                   |                   |                   |                   |
| Cash and cash equivalents            | 18,650,898        | 18,650,898        | 8,097,531         | 8,097,531         |
| Short-term financial instruments     | 2,228,000         | 2,228,000         | 5,738,000         | 5,738,000         |
| Accounts receivable, net             | 10,911,842        | 10,911,842        | 7,693,116         | 7,693,116         |
| Short-term loans, net                | 28,129            | 28,129            | 10,925            | 10,925            |
| Non-current accounts receivable, net | 1,906,418         | 1,906,418         | 2,889,876         | 2,889,876         |
| Available-for-sale securities        | 100,000           | 100,000           | 100,000           | 100,000           |
| Other investment securities          | 222,693           | 222,693           | 222,693           | 222,693           |
| Long-term financial instruments      | 19,500            | 19,500            | 13,500            | 13,500            |
| Long-term loans, net                 | 1,049,387         | 971,654           | 1,393,203         | 1,326,410         |
| <b>Total financial assets</b>        | <b>35,116,867</b> | <b>35,039,134</b> | <b>26,158,844</b> | <b>26,092,051</b> |
| <b>Financial liabilities:</b>        |                   |                   |                   |                   |
| Accounts payable                     | 6,462,841         | 6,462,841         | 4,301,624         | 4,301,624         |
| Short-term borrowings                | -                 | -                 | 4,000,000         | 4,000,000         |
| Derivatives                          | 22,266            | 22,266            | 91,833            | 91,833            |
| Current portion of long-term debt    | 10,000,000        | 10,000,000        | -                 | -                 |
| Long-term debt                       | -                 | -                 | 4,000,000         | 3,716,744         |
| <b>Total financial liabilities</b>   | <b>16,485,107</b> | <b>16,485,107</b> | <b>12,393,457</b> | <b>12,110,201</b> |

The fair values of the financial instruments shown in the above table represent the amounts that would be received to sell those assets or that would be paid to transfer those liabilities in an orderly transaction between market participants at that date. Those fair value measurements maximize the use of observable inputs. However, in situations where there is little, if any, market activity for the asset or liability at the measurement date, the fair value measurement reflects the Company's own judgments about the assumptions that market participants would use in pricing the asset or liability. Those judgments are developed by the Company based on the best information available in the circumstances, including expected cash flows and appropriately risk adjusted discount rates, available observable and unobservable inputs.

## **KSNET, Inc.**

### **Notes to the Financial Statements**

**for the years ended December 31, 2009, 2008 and 2007**

**(All amounts stated in thousands of Korean won, unless otherwise stated)**

#### **6. FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)**

##### **Fair value of financial instruments (continued)**

The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

*Cash and cash equivalents, short-term financial instruments, long-term financial instruments, accounts receivable, short-term loans, non-current accounts receivable, accounts payable, short-term borrowings and current portion of long-term debt*

The carrying amounts, at face value or cost plus accrued interest, approximate fair value because of the short maturity of these instruments.

##### *Available for sale and other investment securities*

Debt securities classified as available-for-sale are measured using quoted market prices multiplied by the quantity held when quoted market prices are available. If quoted market prices for those debt securities are not available, the fair value is determined using an income approach valuation technique (present value using the discount rate adjustment technique) that considers, among other things, rates currently observed in publicly traded debt markets for debt of similar terms to companies with comparable credit risk, the issuer's credit spread, and illiquidity by sector and maturity. Equity securities that do not have readily determinable fair value are classified as other investment securities and measured at cost less any impairment.

##### *Long-term loans*

The fair value of the long-term loans is determined using an income approach valuation technique (present value using the discount rate adjustment technique) based on the present value of expected future cash flows which incorporates a risk premium to take into account the risks inherent in those expected cash flows. The long-term loans are recorded at their carrying value. The fair value is measured for disclosure purposes.

##### *Long-term debt*

The fair value of the Company's long term debt is measured using quoted offer side prices when quoted market prices are available. If quoted market prices are not available, the fair value is determined by discounting the future cash flows of each instrument at rates that reflect rates currently observed in publicly traded debt markets for debt of similar terms to companies with comparable credit risk. For long-term debt measurements, where there are no rates currently observable in publicly traded debt markets of similar terms to companies with comparable credit, the Company uses market interest rates and adjusts that rate for all necessary risks, including its own credit risk. In determining an appropriate spread to reflect its credit standing, the Company considers credit default swap spreads, bond yields of other long-term debt offered by the Company, and interest rates currently offered to the Company for similar debt instruments of comparable maturities by the Company's bankers as well as other banks that regularly compete to provide financing to the Company. The long-term debt is recorded at its carrying value. The fair value is measured for disclosure purposes.

*Derivatives*

All derivatives are recognized on the balance sheet at fair value based on quoted market prices, dealer or counterparty quotes, if available. If quoted market prices are not available, pricing or valuation models are applied to current market information to estimate the fair value.

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**KSNET, Inc.****Notes to the Financial Statements****for the years ended December 31, 2009, 2008 and 2007****(All amounts stated in thousands of Korean won, unless otherwise stated)****6. FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)****Fair value hierarchy**

Fair value is defined as the price that would be received upon sale of an asset or paid upon transfer of a liability in an orderly transaction between market participants at the measurement date and in the principal or most advantageous market for that asset or liability. The fair value should be calculated based on assumptions that market participants would use in pricing the asset or liability, not on assumptions specific to the entity. In addition, the fair value of liabilities should include consideration of non-performance risk including the Company's own credit risk.

Fair value measurements and inputs are categorized into a fair value hierarchy which prioritizes the inputs into three levels based on the extent to which inputs used in measuring fair value are observable in the market. Each fair value measurement is reported in one of the three levels which are determined by the lowest level input that is significant to the fair value measurement in its entirety.

These levels are:

- Level 1 inputs are based upon unadjusted quoted prices for identical instruments traded in active markets.
- Level 2 inputs are based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3 inputs are generally unobservable and typically reflect management's estimates of assumptions that market participants would use in pricing the asset or liability. The fair values are therefore determined using model-based techniques that include option pricing models, discounted cash flow models, and similar techniques.

The following table presents the Company's assets and liabilities measured at fair value on a recurring basis as of December 31, 2009:

|  | <b>Quoted price in<br/>active markets<br/>for<br/>identical assets<br/>(Level 1)</b> | <b>Significant<br/>other<br/>observable<br/>inputs<br/>(Level 2)</b> | <b>Significant<br/>unobservable<br/>inputs<br/>(Level 3)</b> | <b>Total</b>   |
|--|--|--|--|----------------|
| <b>Assets:</b>                         |  |  |  |                |
| Available-for-sale securities          | -  | 100,000  | -  | 100,000        |
| <b>Total assets at fair value</b>      | <b>-</b>   | <b>100,000</b>   | <b>-</b>   | <b>100,000</b> |
| <b>Liabilities:</b>                    |  |  |  |                |
| Derivatives                            | -  | 22,266   | -  | 22,266         |
| <b>Total liabilities at fair value</b> | <b>-</b>   | <b>22,266</b>  | <b>-</b>   | <b>22,266</b>  |

**value**

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**KSNET, Inc.****Notes to the Financial Statements****for the years ended December 31, 2009, 2008 and 2007****(All amounts stated in thousands of Korean won, unless otherwise stated)****6. FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)****Fair value hierarchy (continued)**

The following table presents the Company's assets and liabilities measured at fair value on a recurring basis as of December 31, 2008:

|  | Quoted price in<br>active markets<br>for<br>identical assets<br>(Level 1) | Significant<br>other<br>observable<br>inputs<br>(Level 2) | Significant<br>unobservable<br>inputs<br>(Level 3) | Total          |
|--|---|---|--|----------------|
| Assets:                                |   |   |  |                |
| Available-for-sale securities          | -   | 100,000   | -  | 100,000        |
| <b>Total assets at fair value</b>      | <b>-</b>  | <b>100,000</b>  | <b>-</b>   | <b>100,000</b> |
| Liabilities:                           |   |   |  |                |
| Derivatives                            | -   | 91,833  | -  | 91,833         |
| <b>Total liabilities at fair value</b> | <b>-</b>  | <b>91,833</b>   | <b>-</b>   | <b>91,833</b>  |

**7. DERIVATIVES**

The Company uses derivative financial instruments primarily to manage the risks associated with fluctuations in interest rates. In 2008, the Company used variable-rate Certificate of Deposit (CD) debt to finance its operations. The debt obligations expose the Company to variability in interest payments due to changes in interest rates. Management believed that it is prudent to limit the variability of a portion of its interest payments. To meet this objective, management entered into CD based interest rate swap agreements to manage fluctuations in cash flows resulting from changes in the benchmark interest rate of CD. This swap changes the variable rate cash flow exposure on the debt obligations to fixed cash flows. Under the terms of the interest rate swaps, the Company receives CD based variable interest rate payments (CD + 1.425%) and makes fixed interest rate payments of 6.625%, thereby creating the equivalent of fixed-rate debt for the notional amount ( 4,000 million) of its debt hedged. However, the Company did not designate the interest rate related derivatives as hedging instruments under ASC 815, Derivatives and Hedging, and therefore, any gains or losses on these derivatives are recognized in the current income.

The fair value of derivatives held as of December 31, 2009 and 2008 are as follows:

|  | 2009   | 2008   |
|--|--------|--------|
| Derivatives:   |        |        |
| Interest Rate Swap   | 22,266 | 91,833 |
| Total derivatives not designated as hedging instrument under ASC 815 | 22,266 | 91,833 |



The effects of derivatives instruments on income for the years ended December 31, 2009 and 2008 are summarized as follows:

|                             | 2009   | 2008   |
|-----------------------------|--------|--------|
| Derivatives:                |        |        |
| Gains (loss) on derivatives | 69,567 | 91,833 |

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**KSNET, Inc.****Notes to the Financial Statements****for the years ended December 31, 2009, 2008 and 2007****(All amounts stated in thousands of Korean won, unless otherwise stated)****8. LONG-TERM DEBT**

Long-term debt as of December 31, 2009 and 2008 are summarized as follows:

|   | <b>Maturity</b> | <b>2009</b>  | <b>2008</b>      |
|---|-----------------|--------------|------------------|
| Long-term debt:                         |                 |              |                  |
| (Annual interest rate: 5.08~6.63%)      | 2010            | 10,000,000   | 4,000,000        |
| Less: current portion of long-term debt |                 | (10,000,000) |                  |
| <b>Total</b>                            |                 | <b>-</b>     | <b>4,000,000</b> |

Long-term debt is subject to various restrictive covenants. These covenants typically include restrictions on the debt to equity ratio, credit rating, working capital ratio, and other similar financial ratios. The Company was in compliance with these financial covenants during all periods presented.

**9. PROPERTY AND EQUIPMENT**

Property and equipment as of December 31, 2009 and 2008 are summarized as follows:

|                                 | <b>2009</b> | <b>2008</b> |
|---------------------------------|-------------|-------------|
| Cost:                           |             |             |
| Land                            | 981,257     | 981,257     |
| Buildings                       | 625,943     | 625,943     |
| Structures                      | 203,350     | 203,350     |
| Vehicles                        | 40,629      | 56,999      |
| Tools, furniture and fixtures   | 70,381,043  | 56,821,824  |
| Machinery and equipment         | 6,054,301   | 6,054,301   |
| Software                        | 4,982,167   | 4,416,270   |
|                                 | 83,268,690  | 69,159,944  |
| Accumulated depreciation:       |             |             |
| Buildings                       | 125,893     | 105,028     |
| Structures                      | 126,527     | 101,108     |
| Vehicles                        | 40,629      | 56,999      |
| Tools, furniture and fixtures   | 48,963,351  | 40,128,396  |
| Machinery and equipment         | 5,384,975   | 4,944,946   |
| Software                        | 3,757,134   | 3,255,575   |
|                                 | 58,398,509  | 48,592,052  |
| Accumulated loss on impairment: |             |             |
| Tools, furniture and fixtures   | -           | 22,301      |
|                                 | -           | 22,301      |
| Carrying amount:                |             |             |
| Land                            | 981,257     | 981,257     |
| Buildings                       | 500,050     | 520,915     |
| Structures                      | 76,823      | 102,242     |
| Vehicles                        | -           | -           |
| Tools, furniture and fixtures   | 21,417,692  | 16,671,127  |

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|                              |                   |                   |
|------------------------------|-------------------|-------------------|
| Machinery and equipment      | 669,326           | 1,109,356         |
| Software                     | 1,225,033         | 1,160,694         |
| <b>Total carrying amount</b> | <b>24,870,181</b> | <b>20,545,591</b> |

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**KSNET, Inc.****Notes to the Financial Statements****for the years ended December 31, 2009, 2008 and 2007**

(All amounts stated in thousands of Korean won, unless otherwise stated)

**9. PROPERTY AND EQUIPMENT (continued)**

For the years ended December 31, 2009, 2008 and 2007, total depreciation expenses for the property and equipment were 9,886 million, 8,462 million, and 7,547 million, respectively. Total depreciation expenses include cost of sales in an amount of 6,836 million, 5,396 million and 4,813 million; and selling, general, administrative expenses of 3,050 million, 3,066 million and 2,734 million for the years ended December 31, 2009, 2008 and 2007, respectively.

**10. INTANGIBLE ASSETS**

Summarized below is the carrying value and accumulated amortization of intangible assets as of December 31, 2009 and 2008:

|                                 | <b>As of December 31, 2009</b> |                                 |                           |
|---------------------------------|--------------------------------|---------------------------------|---------------------------|
|                                 | <b>Gross carrying value</b>    | <b>Accumulated amortization</b> | <b>Net carrying value</b> |
| Finite-lived intangible assets: |                                |                                 |                           |
| Trademarks                      | 77,057                         | 53,672                          | 23,385                    |
| <b>Total</b>                    | <b>77,057</b>                  | <b>53,672</b>                   | <b>23,385</b>             |

|                                 | <b>As of December 31, 2008</b> |                                 |                           |
|---------------------------------|--------------------------------|---------------------------------|---------------------------|
|                                 | <b>Gross carrying value</b>    | <b>Accumulated amortization</b> | <b>Net carrying value</b> |
| Finite-lived intangible assets: |                                |                                 |                           |
| Trademarks                      | 77,057                         | 46,285                          | 30,772                    |
| <b>Total</b>                    | <b>77,057</b>                  | <b>46,285</b>                   | <b>30,772</b>             |

Amortization expenses charged for the years to December 31, 2009, 2008 and 2007 were 7.4 million, respectively.

Future estimated annual amortization expense for the next five fiscal years is presented in the table below. Actual amortization expense in future periods could differ from this estimate as a result of acquisitions, changes in useful lives and other relevant factors.

| <b>Year</b> | <b>Amount</b> |
|-------------|---------------|
| 2010        | 7,387         |
| 2011        | 7,387         |
| 2012        | 7,387         |
| 2013        | 1,224         |
| 2014        | -             |

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**KSNET, Inc.****Notes to the Financial Statements****for the years ended December 31, 2009, 2008 and 2007****(All amounts stated in thousands of Korean won, unless otherwise stated)****11. OTHER ASSETS AND LIABILITIES**

Details of other assets and liabilities as of December 31, 2009 and 2008 are as follows:

**Other current assets**

|                                 | <b>2009</b>       | <b>2008</b>      |
|---------------------------------|-------------------|------------------|
| Short-term loans                | 29,609            | 19,750           |
| Allowance for doubtful accounts | (1,480)           | (8,825)          |
| Other receivables               | 400,069           | 489,802          |
| Allowance for doubtful accounts | (17,724)          | (21,856)         |
| Accrued income                  | 57,912            | 120,146          |
| Advanced payments               | 2,240,175         | 3,798,362        |
| Prepaid expenses                | 10,337,665        | 5,398,740        |
| <b>Total</b>                    | <b>13,046,226</b> | <b>9,796,119</b> |

**Other non-current Assets**

|                                 | <b>2009</b>      | <b>2008</b>      |
|---------------------------------|------------------|------------------|
| Long-term financial instruments | 19,500           | 13,500           |
| Other investment securities     | 222,693          | 222,693          |
| Long-term loans (*)             | 1,104,618        | 1,466,530        |
| Allowance for doubtful accounts | (55,231)         | (73,327)         |
| Guarantee deposits (**)         | 3,238,209        | 3,084,722        |
| <b>Total</b>                    | <b>1,038,481</b> | <b>1,037,539</b> |
|                                 | <b>5,568,270</b> | <b>5,751,657</b> |

(\*) Long-term loans include loans to employees for mortgage in the amount of 788 million and 706 million as of December 31, 2009 and 2008, respectively.

(\*\*) Guarantee deposits consist of deposits for leased offices.

**Other current liabilities**

|                         | <b>2009</b>       | <b>2008</b>       |
|-------------------------|-------------------|-------------------|
| Other payables          | 2,536,737         | 2,446,280         |
| Advances from customers | 175,336           | 336,912           |
| Value-added tax payable | 1,086,111         | 768,878           |
| Withholdings (*)        | 11,011,153        | 7,571,983         |
| Other accrued expenses  | 419,696           | 391,298           |
| Deposits received       | 170,751           | 360,907           |
| Income taxes payable    | 1,322,383         | 1,648,965         |
| Derivatives             | 22,266            | 91,833            |
| <b>Total</b>            | <b>16,744,433</b> | <b>13,617,056</b> |

(\*) Withholdings are related to the Payment Gateway service for accounts received from the credit card companies withheld before they are passed to the on-line shopping mall.



**KSNET, Inc.****Notes to the Financial Statements****for the years ended December 31, 2009, 2008 and 2007****(All amounts stated in thousands of Korean won, unless otherwise stated)****11. OTHER ASSETS AND LIABILITIES (continued)****Other non-current liabilities**

|                                     | <b>2009</b>    | <b>2008</b> |
|-------------------------------------|----------------|-------------|
| Unrecognized tax benefits (Note 15) | 963,778        | -           |
| <b>Total</b>                        | <b>963,778</b> | <b>-</b>    |

**12. OTHER INCOME (EXPENSE), net**

Details of other income (expense), net for the years ended December 31, 2009, 2008 and 2007 are as follows:

|   | <b>2009</b>   | <b>2008</b>      | <b>2007</b>    |
|---|---------------|------------------|----------------|
| Gain (loss) on foreign currency transactions      | (121)         | (1)              | (33)           |
| Gain (loss) on disposal of property and equipment | 6,503         | (92,355)         | (4,212)        |
| Gain (loss) on disposal of investment securities  | -             | -                | 215,948        |
| Gain (loss) on valuation of derivatives           | 69,567        | (91,833)         | -              |
| Donations   | (28,420)      | (94,873)         | (87,564)       |
| Miscellaneous                                     | (93)          | 26,511           | 34,457         |
| <b>Total</b>                                      | <b>47,436</b> | <b>(252,551)</b> | <b>158,596</b> |

**13. EQUITY****Common stock**

The holder of each share of common stock has the right to one vote. The number of issued common shares as of December 31, 2009 and 2008 are 13,605,766 and 14,551,784 respectively. All common stock is issued at par value. Amount of capital stock and additional paid-in capital as of December 31, 2009 and 2008 are as follows:

|                             | <b>2009</b>      | <b>2008</b>      |
|-----------------------------|------------------|------------------|
| Capital stock:              |                  |                  |
| Common stock                | 6,802,883        | 7,275,892        |
| <b>Total</b>                | <b>6,802,883</b> | <b>7,275,892</b> |
| Additional paid-in capital: |                  |                  |
| Other                       | 33,568           | 33,568           |
| <b>Total</b>                | <b>33,568</b>    | <b>33,568</b>    |

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**KSNET, Inc.****Notes to the Financial Statements****for the years ended December 31, 2009, 2008 and 2007****(All amounts stated in thousands of Korean won, unless otherwise stated)****13. EQUITY (continued)****Common stock (continued)**

In 2000, the Company issued preferred stock at 11,000 (par value 500) and treated the amount of excess over par value less stock issuance costs as additional paid-in capital preferred stock. The preferred stock is non-cumulative and is convertible into common stock from the issuance date. The number of issued preferred shares as of December 31, 2007 was 4,000,000. There were no shares of preferred stock outstanding as of December 31, 2009 and 2008 due to capital reduction in 2008. Additional paid-in capital common stock of 33,568 thousand relates to the amount of excess fair value of net assets over common stock at the time of split off in 1999.

On February 15, 2008, the Company's shareholders approved an amendment to the Certificate of Incorporation decreasing the authorized shares from 42,400,000 to 36,500,000 shares, par value 500 per share.

**Stock retirement**

Total amount of common stocks and preferred stocks retired for the years ended December 31, 2009, 2008 and 2007 are as follows:

|                           | 2009           |                | 2008             |                  |
|---------------------------|----------------|----------------|------------------|------------------|
|                           | Shares         | Amount         | Shares           | Amount           |
| Common stock:             |                |                |                  |                  |
| Capital reduction         | 946,018        | 473,009        | 1,654,776        | 827,388          |
| Treasury stock retirement | -              | -              | 164,578          | 82,289           |
| Preferred stock:          |                |                |                  |                  |
| Capital reduction         | -              | -              | 4,000,000        | 2,000,000        |
| <b>Total</b>              | <b>946,018</b> | <b>473,009</b> | <b>5,819,354</b> | <b>2,909,677</b> |

According to ASC 505, Equity, if an entity's stock is retired, an excess of purchase price over par or stated value may be allocated between additional paid-in capital and retained earnings.

On February 15, 2008, the Company repurchased and retired all of its preferred shares. An excess of repurchase price over par value was allocated between additional paid-in capital preferred stock in an amount of 40,702 million and retained earnings in an amount of 16,150 million. On the same date, the Company reduced 1,654,776 shares of common stock by capital reduction and retired 164,578 shares of treasury stock.

On March 26, 2009, the Company repurchased and retired 946,018 shares of common stock and an excess of repurchase price over par value was allocated to retained earnings for amount of 3,615 million.



**KSNET, Inc.****Notes to the Financial Statements****for the years ended December 31, 2009, 2008 and 2007****(All amounts stated in thousands of Korean won, unless otherwise stated)****14. ACCRUED SEVERANCE BENEFITS**

Accrued severance benefits as of December 31, 2009 and 2008 are as follows:

|  | <b>2009</b>    | <b>2008</b>    |
|--|----------------|----------------|
| Balance at beginning of year             | 1,993,792      | 2,417,469      |
| Provision for severance benefits         | 795,660        | 944,342        |
| Severance payments during the year       | (331,355)      | (1,368,019)    |
| Balance at end of year                   | 2,458,097      | 1,993,792      |
| Deposit for severance benefits insurance | (1,708,318)    | (1,259,803)    |
| <b>Accrued severance benefits</b>        | <b>749,779</b> | <b>733,989</b> |

The severance benefits are funded approximately 69.5% and 63.2% as of December 31, 2009 and 2008, respectively through severance insurance deposits with the Shinhan Life Insurance Company and the Hana Bank for the payment of severance benefits. The Company has no additional liability once the amount has been contributed, thus the Company deducts contributions made to the severance insurance deposits from accrued severance benefit liabilities. The beneficiaries of the severance insurance deposit are the Company's employees.

The Company expects to pay the following severance benefits, which are currently accrued for the Company's obligation through December 31, 2009, to its employees. If they terminate upon their normal retirement age:

| <b>Year</b> | <b>Amount</b> |
|-------------|---------------|
| 2010        | -             |
| 2011        | -             |
| 2012        | -             |
| 2013        | -             |
| 2014        | -             |
| 2015 ~ 2019 | 235,392       |

The above amounts were determined based on the employees' current salary rates and the number of service years that will be accumulated upon their retirement date. These amounts do not include amounts that might be paid to employees that will cease working with the Company before their normal retirement age.

**KSNET, Inc.****Notes to the Financial Statements****for the years ended December 31, 2009, 2008 and 2007****(All amounts stated in thousands of Korean won, unless otherwise stated)****15. INCOME TAXES**

The statutory income tax rate, including tax surcharges, applicable to the Company was 27.5% in 2007 and 2008. In accordance with the amendment of Corporate Tax Act enacted in 2008, the statutory income tax rate was amended to 24.2% effective for fiscal year 2009 and 22.0% for fiscal years 2010 and thereafter. However, in 2009, Corporate Income Tax Law was further amended and the statutory income tax rate of 24.2% is effective for fiscal years 2009 until 2011 and 22% for fiscal years 2012 and thereafter. Accordingly, deferred income taxes as of December 31, 2009 were calculated based on the enacted rates of 24.2% and 22.0% ..

Actual income tax expense differs from the theoretical amount that would arise at the Korean statutory tax rate for the years ended December 31, 2009, 2008 and 2007 as follows:

|  | 2009             | 2008             | 2007             |
|--|------------------|------------------|------------------|
| Income tax expense at Korean statutory tax rate                | 3,785,377        | 3,355,549        | 3,517,933        |
| Nondeductible items  | 208,270          | 244,933          | 274,638          |
| Adjustments to uncertain and effectively settled tax positions | 806,625          | -                | -                |
| Income tax exemption   | (781,976)        | (557,483)        | (429,792)        |
| Tax investigation by National Tax Service                      | -                | -                | 786,280          |
| Others   | (167,222)        | 92,606           | 125,298          |
| <b>Income tax expense</b>                                      | <b>3,851,074</b> | <b>3,135,605</b> | <b>4,274,357</b> |

The following is a reconciliation of income taxes computed at the Korean tax rate to actual effective income tax provision:

|   | 2009         | 2008         | 2007         |
|---|--------------|--------------|--------------|
| Statutory income tax rate                 | 24.2%        | 27.5%        | 27.5%        |
| Expenses not deductible for tax purposes  | 1.3          | 2.0          | 2.14         |
| Tax exemptions                            | (5.0)        | (4.5)        | (3.3)        |
| FIN 48 tax contingencies and settlements  | 5.1          | -            | -            |
| Tax investigation by National Tax Service | -            | -            | 7.1          |
| Others                                    | (1.1)        | 0.5          | (0.1)        |
| <b>Effective income tax rate</b>          | <b>24.5%</b> | <b>25.5%</b> | <b>33.3%</b> |

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**KSNET, Inc.****Notes to the Financial Statements****for the years ended December 31, 2009, 2008 and 2007****(All amounts stated in thousands of Korean won, unless otherwise stated)****15. INCOME TAXES (continued)****Deferred tax assets and liabilities**

Deferred income taxes reflect the temporary differences between the amounts at which assets and liabilities are recorded for financial reporting purposes and the amounts utilized for tax purposes. The primary components of the temporary differences that gave rise to the Company's deferred tax assets and liabilities as of December 31, 2009 and 2008 and their classification were as follows:

**Deferred tax assets**

|                                  | <b>2009</b>      | <b>2008</b>      |
|----------------------------------|------------------|------------------|
| Investment securities            | 271,154          | 293,155          |
| Depreciation and amortization    | 77,616           | 36,158           |
| Derivatives                      | 4,899            | 20,203           |
| Other payables                   | 980,979          | 630,595          |
| Advances from customers          | 35,903           | 75,655           |
| Accrued severance benefits       | 445,332          | 382,271          |
| Bad debt                         | 154,048          | 176,836          |
| Other                            | 65,818           | 99,175           |
| <b>Total deferred tax assets</b> | <b>2,035,749</b> | <b>1,714,048</b> |

**Deferred tax liabilities**

|  | <b>2009</b>      | <b>2008</b>    |
|--|------------------|----------------|
| Accounts receivable                      | 965,937          | 640,596        |
| Other current assets                     | 13,545           | 28,139         |
| Deposit for severance benefits insurance | 375,830          | 277,157        |
| Other                                    | 587,872          | -              |
| <b>Total deferred tax liabilities</b>    | <b>1,943,184</b> | <b>945,892</b> |

**Reported as:**

|                                       | <b>2009</b>   | <b>2008</b>    |
|---------------------------------------|---------------|----------------|
| Current deferred tax assets           | 482,053       | 729,238        |
| Non-current deferred tax assets       | -             | 38,918         |
| Non-current deferred tax liabilities  | (389,488)     | -              |
| <b>Net deferred income tax assets</b> | <b>92,565</b> | <b>768,156</b> |

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**KSNET, Inc.****Notes to the Financial Statements****for the years ended December 31, 2009, 2008 and 2007****(All amounts stated in thousands of Korean won, unless otherwise stated)****15. INCOME TAXES (continued)****Uncertain tax positions**

On January 1, 2009, the Company adopted the provisions of ASC 740 which set out a consistent framework to determine the appropriate level of tax reserve for uncertain tax positions. ASC Subtopic 740-10 originally was effective for fiscal years beginning after December 15, 2006. The FASB issued ASC Subtopic 740-10 (FSP FIN 48-3, Effective date of FASB Interpretation No. 48 for Certain Nonpublic Enterprises), which deferred the effective date of ASC Subtopic 740-10 for nonpublic entities that had not already issued a complete set of annual financial statements fully reflecting ASC Subtopic 740-10's requirements or are consolidated entities of public entities that report in US GAAP. This means that ASC Subtopic 740-10 was required for such entities with fiscal years beginning after December 15, 2008 and accordingly, the Company adopted the provisions in 2009.

The following table is a reconciliation of the beginning and ending amount of the Company's gross unrecognized tax benefits for the year ended December 31, 2009:

|   | <b>2009</b>    |
|---|----------------|
| Beginning balance   | 154,210        |
| Gross increases/(decreases) tax positions in prior period | -              |
| Gross increases/(decreases) current period tax positions  | 809,568        |
| Settlements   | -              |
| Lapse of statute of limitations                           | -              |
| <b>Ending balance</b>                                     | <b>963,778</b> |

Upon adoption at January 1, 2009, the Company's decreased retained earnings by 154,210 thousand. For the year ended December 31, 2009, the unrecognized tax benefit increased by 809,568 thousand which all related to permanent differences. As of December 31, 2009, the Company's total unrecognized tax benefits that, if recognized, would affect the effective tax rate is 809,568 thousand. During the year ended December 31, 2009, the Company recognized approximately 2,942 thousand for the payment of interest and penalty. The Company had approximately 12,099 thousand and 14,403 thousand for the payment of interest and penalties accrued in the balance sheet as of December 31, 2009.

The Company files income tax returns in the Republic of Korea. In 2007, the Korea National Tax Service, or NTS, has effectively completed the examination of the Company's returns in the Republic of Korea related to years 2002 through 2006.

It is expected that the amount of unrecognized tax benefits will also change for other reasons in the next 12 months; however, the Company does not expect the change to have a significant impact on our financial position or results of operations.

**KSNET, Inc.****Notes to the Financial Statements****for the years ended December 31, 2009, 2008 and 2007****(All amounts stated in thousands of Korean won, unless otherwise stated)****16. EARNINGS PER SHARE**

Basic earnings per share of common stock is computed by dividing net income by the weighted average number of shares of common stock outstanding for the period, less the weighted average number of shares subject to stock retirement. Diluted earnings per share of common stock is computed using the weighted average number of shares of common stock outstanding plus the effect of common stock equivalents, unless the common stock equivalents are anti-dilutive. The calculation of diluted earnings per share includes the dilutive effect of an exercise of stock warrants.

The following details the computation of earnings per share of common stock as of December 31, 2009, 2008 and 2007:

|  | 2009       | 2008       | 2007       |
|--|------------|------------|------------|
| Net income   | 11,892,039 | 9,176,729  | 8,566,101  |
| Weighted average shares used in computing basic earnings per share   | 13,800,153 | 14,895,399 | 16,203,185 |
| Weighted average effect of dilutive securities: stock warrants       | -          | -          | 4,003,375  |
| Weighted average shares used in computing diluted earnings per share | 13,800,153 | 14,895,399 | 20,206,560 |
| <b>Basic earnings per share (in Korean won)</b>                      | <b>862</b> | <b>616</b> | <b>529</b> |
| <b>Diluted earnings per share (in Korean won)</b>                    | <b>862</b> | <b>616</b> | <b>424</b> |

**17. COMMITMENTS AND CONTINGENCIES**

The Company is involved in a total of four litigations that have arisen in the ordinary course of business, including matters involving price fixing. The results and timing of the ultimate resolutions of these proceedings are inherently unpredictable. The outcome of any claim, suit, assessment, investigation, or legal proceeding, individually or collectively will depend on a number of variables, including the nature, timing, and amount of any associated expenses, amounts paid in settlement, damages or other remedies or consequences. As of December 31, 2009, the Company did not accrue liabilities with respect to the pending litigations. The Company will accrue a liability when it believes that it is both probable that a liability has been incurred and that it can reasonably estimate the amount of the loss.

As of December 31, 2009, the Company has guarantees provided by non-related party for the Company as follows (Korean won in thousands):

| Providing by                        | Amount    | Description   |
|-------------------------------------|-----------|---|
| Seoul Guarantee Insurance Co., Ltd. | 3,078,047 | Payment guarantee provided by the insurance company |

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**KSNET, Inc.****Notes to the Financial Statements****for the years ended December 31, 2009, 2008 and 2007****(All amounts stated in thousands of Korean won, unless otherwise stated)****18. PLEDGED ASSETS**

Details of assets pledged by the Company as collateral for operating activities as of December 31, 2009 are as follows:

| <b>Pledged to</b>        | <b>Pledged assets</b>            | <b>Pledged amount</b> |
|--------------------------|----------------------------------|-----------------------|
| Kookmin Bank             | Short-term financial instruments | 400,000               |
| Industrial Bank of Korea | Short-term financial instruments | 100,000               |
| Hana Bank                | Short-term financial instruments | 158,000               |
| <b>Total</b>             |                                  | <b>658,000</b>        |

**19. SUPPLEMENTAL CASH FLOWS INFORMATION**

Supplemental cash flows information for the years ended December 31, 2009, 2008 and 2007 is as follows:

|                                | <b>2009</b> | <b>2008</b> | <b>2007</b> |
|--------------------------------|-------------|-------------|-------------|
| Cash paid during the year for: |             |             |             |
| Interest                       | 575,203     | 407,126     | 667         |
| Income taxes                   | 2,695,440   | 3,248,571   | 4,088,937   |

**20. RELATED PARTY TRANSACTIONS**

Significant transactions which occurred in the normal course of business with related companies for the years ended December 31, 2009, 2008 and 2007 are as follows:

| <b>Relationship</b> | <b>Name</b>          | <b>Transaction</b>   | <b>2009</b> | <b>2008</b> | <b>2007</b> |
|---------------------|----------------------|----------------------|-------------|-------------|-------------|
| (*)                 | Kooryoonsoft Co. Ltd | Sales and others     | 53,112      | 75,702      | 34,574      |
|                     |                      | Purchases and others | 476,930     | 1,958,473   | 1,943,201   |

Account balances with related companies as of December 31, 2009 and 2008 are as follows:

| <b>Relationship</b> | <b>Name</b>          | <b>2009</b>        |                 | <b>2008</b>        |                 |
|---------------------|----------------------|--------------------|-----------------|--------------------|-----------------|
|                     |                      | <b>Receivables</b> | <b>Payables</b> | <b>Receivables</b> | <b>Payables</b> |
| (*)                 | Kooryoonsoft Co. Ltd | 100,442            | 43,105          | 122,498            | 41,295          |

(\*) The Company's operating department manager is serving as a director of Kooryoonsoft. Co. Ltd.

**KSNET, Inc.****Notes to the Financial Statements****for the years ended December 31, 2009, 2008 and 2007****(All amounts stated in thousands of Korean won, unless otherwise stated)****21. CONCENTRATIONS OF CREDIT RISKS**

Financial instruments that potentially expose the Company to concentrations of credit risk consist primarily of cash, cash equivalents, restricted deposits, and accounts receivable. Substantially all of the Company's cash, cash equivalents, and short-term and long-term financial instruments are held at financial institutions that management believes to be of high credit quality.

A substantial portion of the Company's sales for the years ended December 31, 2009, 2008 and 2007 was made to credit card companies. Sales and accounts receivable from customers accounting for 10% or more of the Company's sales are as follows:

| <b>Major Customers</b>     | <b>Sales for the year ended<br/>December 31, 2009</b> | <b>Accounts receivable as of<br/>December 31, 2009</b> |
|----------------------------|---|--|
| BC Card                    | 18,910,505  | 2,353,548  |
| NTS (National Tax Service) | 5,845,391   | 2,044,259  |
| Shinhan Card               | 14,421,231  | 1,703,070  |
| Kookmin Card               | 12,318,036  | 1,432,215  |
|                            | 51,495,163  | 7,533,092  |

| <b>Major Customers</b> | <b>Sales for the year ended<br/>December 31, 2008</b> | <b>Accounts receivable as of<br/>December 31, 2008</b> |
|------------------------|---|--|
| BC Card                | 15,067,882  | 1,482,641  |
| Shinhan Card           | 10,540,921  | 1,295,034  |
| Kookmin Card           | 10,361,607  | 1,121,757  |
|                        | 35,970,410  | 3,899,432  |

| <b>Major Customers</b> | <b>Sales for the year ended<br/>December 31, 2007</b> | <b>Accounts receivable as of<br/>December 31, 2007</b> |
|------------------------|---|--|
| BC Card                | 16,302,366  | 1,313,688  |
| Shinhan Card           | 13,545,208  | 988,340  |
| Kookmin Card           | 10,802,548  | 935,356  |
| Hyundai Card           | 7,775,082   | 624,783  |
|                        | 48,425,204  | 3,862,167  |

**22. SUBSEQUENT EVENTS**

On September 16, 2010, Net 1 UEPS Technologies, Inc. announced that it had agreed to purchase 98.73% of the outstanding share capital of the Company for 270 billion in cash considerations, subject to a post-closing working capital adjustment. The acquisition was made by Net 1 Applied Technologies Korea, an indirect wholly-owned subsidiary of Net 1 UEPS Technologies, Inc., which was closed on October 29, 2010.

The Company has evaluated subsequent events through the date that the financial statements were issued on January 10, 2011.





**KSNET, Inc.**  
**UNAUDITED BALANCE SHEETS**  
**as of June 30, 2010 and 2009**

|  | (In thousands of Korean won,<br>except share data) |                   |
|--|--|-------------------|
|  | <b>2010</b>  | <b>2009</b>       |
| <b>ASSETS</b>  |  |                   |
| <b>CURRENT ASSETS</b>  |  |                   |
| Cash and cash equivalents (Note 6)   | 20,017,727   | 8,565,795         |
| Short-term financial instruments (Notes 3, 6 and 18)                       | 3,199,364  | 1,798,000         |
| Accounts receivable, net (Notes 4 and 6)                                   | 11,111,189   | 9,087,081         |
| Inventory (Note 5)   | 1,380,603  | 1,864,666         |
| Deferred tax assets (Note 15)  | -  | 175,164           |
| Other current assets (Notes 6, 11 and 20)                                  | 16,525,627   | 13,103,960        |
| Total current assets   | 52,234,510   | 34,594,666        |
| AVAILABLE-FOR-SALE SECURITIES (Note 6)                                     | 100,000  | 100,000           |
| PROPERTY AND EQUIPMENT, net (Note 9)                                       | 26,114,027   | 22,447,255        |
| INTANGIBLE ASSETS, net (Note 10)   | 19,691   | 27,078            |
| NON-CURRENT ACCOUNTS RECEIVABLE, net (Notes 4 and 6)                       | 1,505,297  | 2,043,439         |
| NON-CURRENT DEFERRED TAX ASSETS (Note 15)                                  | -  | 282,013           |
| OTHER NON-CURRENT ASSETS (Notes 3, 6 and 11)                               | 5,583,247  | 5,735,795         |
| <b>TOTAL ASSETS</b>  | <b>85,556,772</b>                                  | <b>65,230,246</b> |
| <b>LIABILITIES</b>   |  |                   |
| <b>CURRENT LIABILITIES</b>   |  |                   |
| Accounts payable (Note 6)  | 6,154,692  | 5,171,972         |
| Short-term borrowings (Note 6)   | 2,000,000  | -                 |
| Current portion of long-term debt (Notes 6 and 8)                          | 6,000,000  | 4,000,000         |
| Deferred tax liabilities (Note 15)   | 12,060   | -                 |
| Other current liabilities (Notes 6, 7, 11 and 20)                          | 17,061,849   | 10,959,742        |
| Total current liabilities  | 31,228,601   | 20,131,714        |
| LONG-TERM DEBT (Notes 6 and 8)   | -  | 6,000,000         |
| ACCRUED SEVERANCE BENEFITS, net (Note 14)                                  | 1,192,860  | 1,082,422         |
| NON-CURRENT DEFERRED TAX LIABILITIES (Note 15)                             | 152,536  | -                 |
| OTHER NON-CURRENT LIABILITIES (Note 15)                                    | 1,036,750  | 148,135           |
| <b>TOTAL LIABILITIES</b>   | <b>33,610,747</b>                                  | <b>27,362,271</b> |
| <b>EQUITY</b>  |  |                   |
| COMMON STOCK (Note 13)   | 6,802,883  | 7,275,892         |
| Authorized shares: 36,500,000 with 500 par value at June 30, 2010 and 2009 |  |                   |
| Issued and outstanding shares: 13,605,766 at June 30, 2010 and 2009        |  |                   |
| ADDITIONAL PAID-IN-CAPITAL (Note 13)                                       | 33,568   | 33,568            |
| RETAINED EARNINGS  | 45,109,574   | 31,031,524        |
| <b>TOTAL EQUITY</b>  | <b>51,946,025</b>                                  | <b>37,867,975</b> |
| <b>TOTAL LIABILITIES AND EQUITY</b>  | <b>85,556,772</b>                                  | <b>65,230,246</b> |
| See accompanying notes to financial statements.                            |  |                   |



**KSNET, INC.****UNAUDITED STATEMENTS OF INCOME****For the six months ended June 30, 2010 and 2009**(In thousands of Korean  
won,  
except share data)

|   | <b>2010</b> | <b>2009</b> |
|---|-------------|-------------|
| <b>REVENUE</b>                                    |             |             |
| Services rendered                                 | 51,359,503  | 40,176,730  |
| Sale of merchandise (Note 20)                     | 1,534,002   | 1,334,725   |
| Others  | 81,514      | 122,033     |
|   | 52,975,019  | 41,633,488  |
| <b>EXPENSE</b>                                    |             |             |
| Cost of services rendered                         | 26,783,173  | 20,383,587  |
| Cost of merchandise sold (Note 20)                | 1,453,776   | 1,304,229   |
| Selling, general and administrative expenses      | 12,475,505  | 10,582,655  |
| Depreciation and amortization                     | 1,607,823   | 1,524,479   |
|   | 42,320,277  | 33,794,950  |
| <b>OPERATING INCOME</b>                           | 10,654,742  | 7,838,538   |
| <b>INTEREST INCOME, net</b>                       | 86,710      | 139,695     |
| <b>OTHER INCOME (EXPENSE), net (Note 12)</b>      | (244,306)   | 7,496       |
| <b>INCOME BEFORE INCOME TAXES</b>                 | 10,497,146  | 7,985,729   |
| <b>INCOME TAX EXPENSE (Note 15)</b>               | 1,989,228   | 1,663,822   |
| <b>NET INCOME</b>                                 | 8,507,918   | 6,321,907   |
| <b>Net income per share (Note 16)</b>             |             |             |
| Basic earnings attributable to KSNET shareholders | 617         | 450         |

See accompanying notes to financial statements.

**KSNET, INC.**  
**UNAUDITED STATEMENTS OF CHANGES IN EQUITY AND COMPREHENSIVE INCOME (in**  
**thousands of won, except share data)**  
**For the six months ended June 30, 2010 and 2009**

|   | Number of shares | Common stock<br>Amount | Treasury<br>stock | Additional<br>paid-<br>in capital | Number<br>of shares | Preferred stock<br>Amount | Additional<br>paid-<br>in capital | Retained<br>earnings | Total<br>equity |
|---|------------------|------------------------|-------------------|-----------------------------------|---------------------|---------------------------|-----------------------------------|----------------------|-----------------|
| Balance Jan. 1, 2009  | 14,551,784       | 7,275,892              |                   | 33,568                            | -                   | -                         | -                                 | 28,478,336           | 35,787,796      |
| Adoption of FIN 48 -adjustment to opening retained earnings |                  |                        |                   |                                   |                     |                           |                                   | (154,210)            | (154,210)       |
| Revised retained earnings                                   |                  |                        |                   |                                   |                     |                           |                                   | 28,324,126           | 35,633,586      |
| Capital reduction   | (946,018)        | (473,009)              | -                 | -                                 | -                   | -                         | -                                 | (3,614,509)          | (4,087,518)     |
| Comprehensive income:                                       |                  |                        |                   |                                   |                     |                           |                                   |                      |                 |
| Net income  | -                | -                      | -                 | -                                 | -                   | -                         | -                                 | 6,321,907            | 6,321,907       |
| Balance Jun. 30, 2009                                       | 13,605,766       | 6,802,883              | -                 | 33,568                            | -                   | -                         | -                                 | 31,031,524           | 37,867,975      |
| Balance Jan. 1, 2010  | 13,605,766       | 6,802,883              | -                 | 33,568                            | -                   | -                         | -                                 | 36,601,656           | 43,438,107      |
| Comprehensive income:                                       |                  |                        |                   |                                   |                     |                           |                                   |                      |                 |
| Net income  | -                | -                      | -                 | -                                 | -                   | -                         | -                                 | 8,507,918            | 8,507,918       |
| Balance Jun. 30, 2010                                       | 13,605,766       | 6,802,883              | -                 | 33,568                            | -                   | -                         | -                                 | 45,109,574           | 51,946,025      |

See accompanying notes to financial statements.

**KSNET, INC.****UNAUDITED STATEMENTS OF CASH FLOWS****for the six months ended June 30, 2010 and 2009**

| <b>Cash flows from operating activities</b>                                       | (In thousands of Korean won) |                  |
|---|------------------------------|------------------|
|   | <b>2010</b>                  | <b>2009</b>      |
| Net income  | 8,507,918                    | 6,321,907        |
| Adjustments to reconcile net income to net cash provided by operating activities: |                              |                  |
| Provision for severance benefits  | 569,331                      | 405,862          |
| Depreciation and amortization   | 5,619,874                    | 4,658,789        |
| Gain on disposal of property and equipment  | (14,626)                     | (1,642)          |
| Gain on valuation of derivatives  | (22,266)                     | (21,427)         |
| Loss on impairment of property, plant and equipment                               | 12,359                       | -                |
| Bad debt expenses   | 85                           | (131,969)        |
| Changes in operating assets and liabilities:                                      |                              |                  |
| Decrease in long-term accounts receivable   | 401,122                      | 846,437          |
| Increase in accounts receivable   | (210,632)                    | (1,267,112)      |
| Decrease (Increase) in other receivables  | (182,222)                    | 50,623           |
| Decrease in accrued income  | 15,723                       | 75,010           |
| Increase in advanced payments   | (893,338)                    | (678,726)        |
| Increase in prepaid expenses  | (2,443,317)                  | (2,723,956)      |
| Increase in inventory   | (5,725,187)                  | (6,293,703)      |
| Decrease (Increase) in guarantee deposits   | 30,000                       | (132,949)        |
| Decrease in deferred tax assets   | 482,053                      | 310,978          |
| (Decrease) Increase in deferred tax liabilities                                   | (236,952)                    | -                |
| (Decrease) Increase in accounts payable   | (296,089)                    | 870,348          |
| Decrease in other payables  | (71,217)                     | (1,249,939)      |
| Decrease in advances from customers   | (41,236)                     | (76,202)         |
| (Decrease) Increase in value-added tax payable                                    | 12,581                       | (7,137)          |
| Increase in accrued expenses  | 32,324                       | 32,938           |
| Increase in deposits received   | -                            | 9,400            |
| (Decrease) Increase in withholdings   | 107,145                      | (1,110,863)      |
| (Decrease) Increase in income taxes payable                                       | 300,085                      | (234,084)        |
| (Decrease) Increase in other non-current liabilities                              | 72,972                       | (6,076)          |
| Decrease in deposits for severance benefits insurance                             | 196,854                      | 90,878           |
| Payment of severance benefits   | (323,104)                    | (148,307)        |
| <b>Net cash provided by (used in) operating activities</b>                        | <b>5,900,240</b>             | <b>(410,922)</b> |
| <b>Cash flows from investing activities</b>                                       |                              |                  |
| Decrease in short-term financial instruments                                      | -                            | 3,940,000        |
| Decrease in short-term loans  | 27,110                       | 6,333            |
| Decrease in long-term loans   | 271,866                      | 336,802          |
| Proceeds from disposal of property and equipment                                  | 54,584                       | 120,518          |
| Increase in short-term financial instruments                                      | (971,364)                    | -                |
| Increase in long-term financial instruments                                       | (194,000)                    | (3,000)          |
| Increase in short-term loans  | -                            | (40,000)         |
| Increase in long-term loans   | (115,000)                    | (177,000)        |
| Acquisition of property and equipment   | (1,358,607)                  | (867,450)        |
| Acquisition of intangible assets  | (248,000)                    | (349,500)        |
| <b>Net cash provided by (used in) investing activities</b>                        | <b>(2,533,411)</b>           | <b>2,966,703</b> |



**KSNET, INC.****UNAUDITED STATEMENTS OF CASH FLOWS (continued)**

for the six months ended June 30, 2010 and 2009

| <b>Cash flows from operating activities</b>          | (In thousands of Korean won) |                    |
|--|------------------------------|--------------------|
|  | <b>2010</b>                  | <b>2009</b>        |
| <b>Cash flows from financing activities</b>          |                              |                    |
| Proceeds from short-term borrowings                  | 2,000,000                    | -                  |
| Proceeds from issuance of long-term debt             | -                            | 6,000,000          |
| Repayment of current portion of long-term debt       | (4,000,000)                  | -                  |
| Repayment of short-term borrowings                   | -                            | (4,000,000)        |
| Capital reduction                                    | -                            | (4,087,517)        |
| <b>Net cash used in financing activities</b>         | <b>(2,000,000)</b>           | <b>(2,087,517)</b> |
| <b>Net increase in cash and cash equivalents</b>     | <b>1,366,829</b>             | <b>468,264</b>     |
| <b>Cash and cash equivalents beginning of year</b>   | <b>18,650,898</b>            | <b>8,097,531</b>   |
| <b>Cash and cash equivalents at end of year</b>      | <b>20,017,727</b>            | <b>8,565,795</b>   |
| <b>Non cash transaction</b>                          |                              |                    |
|  | <b>2010</b>                  | <b>2009</b>        |
| Transferred from inventory to property and equipment | 5,305,737                    | 5,458,685          |
| See accompanying notes to financial statements.      |                              |                    |

**KSNET, Inc.****Notes to the Unaudited Financial Statements****For the six months ended June 30, 2010 and 2009****(All amounts stated in thousands of Korean won, unless otherwise stated)****1. DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION****Description of business**

KSNET, INC. (the Company) was established through split off from Chosun I&C on December 30, 1999 and engages in the Value Added Network (VAN) service and sale of communication equipment in the Republic of Korea.

The Company's capital stock amounts to 6,802,883 thousand as of June 30, 2010 and the Company's shareholders and their ownership as of June 30, 2010 are as follows:

|                           | Number of shares | Ownership (%) |
|---------------------------|------------------|---------------|
| H&QNPS Van Investment     | 6,716,500        | 49.37         |
| Payment Services Asia LLC | 6,716,500        | 49.37         |
| Others                    | 172,766          | 1.26          |
|                           | 13,605,766       | 100.00        |

**Basis of presentation**

The Company maintains its accounting records in Korean Won and the accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ( US GAAP ).

**2. SIGNIFICANT ACCOUNTING POLICIES****Use of estimates**

The preparation of the Company's financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant items subject to such estimates and assumptions include the useful lives of property and equipment; allowances for doubtful accounts; the valuation of derivatives, deferred tax assets, property and equipment, inventory, investment securities; and accrued severance benefits, income tax uncertainties and other contingencies.

**Cash and cash equivalents**

The Company considers cash equivalents as all highly liquid investments and short-term financial instruments, which are readily convertible to cash without significant transaction cost, do not have significant risk from changes in interest rates, and with maturities of three months or less when purchased. Cash and cash equivalents mainly consist of money market trust and checking deposits.

**Allowance for doubtful accounts**

Allowance for doubtful accounts is estimated based on an analysis and past experience of collections of



individual accounts such as accounts receivable, other receivables and loans. Allowance for doubtful accounts is presented as a deduction from receivables. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote.

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**KSNET, Inc.****Notes to the Unaudited Financial Statements****For the six months ended June 30, 2010 and 2009****(All amounts stated in thousands of Korean won, unless otherwise stated)****2. SIGNIFICANT ACCOUNTING POLICIES (continued)****Property and equipment**

Property and equipment are shown at cost less accumulated depreciation. Property and equipment are depreciated on the straight-line basis at rates which are estimated to depreciate the assets to their anticipated residual values over their useful lives. Within the following asset classifications, the expected economic lives are approximately:

|                               |              |
|-------------------------------|--------------|
| Buildings                     | 30 years     |
| Structures                    | 8 years      |
| Vehicles                      | 4 years      |
| Tools, furniture and fixtures | 3 to 4 years |
| Machinery and equipment       | 8 years      |
| Software                      | 5 years      |

The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognized in the statements of income.

Property and equipment do not require that an annual impairment test be performed; instead, they are tested for impairment upon the occurrence of a triggering event. Triggering events include the more likely than not disposal of a portion of such assets or the occurrence of an adverse change in the market involving the business employing the related assets. For six months ended June 30, 2010 and 2009, the amount of impairment losses were 12,359 thousand and zero respectively.

**Sales taxes**

Revenues and expenses are presented net of value added taxes, as the case may be.

**Income taxes**

The Company provides for income taxes using the asset and liability method. This approach recognizes the amount of taxes payable or refundable for the current year, as well as deferred tax assets and liabilities for the future tax consequence of events recognized in the financial statements and tax returns. Deferred income taxes are adjusted to reflect the effects of changes in tax laws or enacted tax rates. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Under the Corporate Income Tax Law in the Republic of Korea, corporate taxpayers are subject to corporate income taxes on taxable income at 22% (10% is applicable to the first 200 million of taxable income) in 2010. On top of the corporate income tax, 10% resident surtax is also assessed; thus the statutory tax rate becomes 24.2% or 11% depending on the amount of taxable income; therefore, the income tax rate during the periods ended June 30, 2010 and 2009 was 24.2% .

In establishing the appropriate income tax valuation allowances, the Company assesses the realizability of its net deferred tax assets, and based on all available evidence, both positive and negative, determines whether it is more likely than not that the net deferred tax assets or a portion thereof will be realized.

Effective January 1, 2009, the Company adopted the provisions of Accounting Standards Codification ( ASC ) 740, *Income Taxes*, which set outs a consistent framework to determine the appropriate level of tax reserve for uncertain tax positions. The Company uses a two-step approach wherein a tax benefit is recognized if a position is more-likely-than-not to be sustained. The amount of the benefit is then measured as the highest tax benefit which is greater than 50% likely to be realized. The difference between the benefit recognized for a position in accordance with ASC 740 and the tax benefit claimed on a tax return is referred to as an unrecognized tax benefit. The Company s policy is to include interest related to unrecognized tax benefits in interest income, net and penalties in selling, general and administration in the statements of income.

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## **KSNET, Inc.**

### **Notes to the Unaudited Financial Statements**

#### **For the six months ended June 30, 2010 and 2009**

(All amounts stated in thousands of Korean won, unless otherwise stated)

#### **2. SIGNIFICANT ACCOUNTING POLICIES (continued)**

##### **Intangible assets**

Intangible assets are shown at cost less accumulated amortization. Intangible assets are amortized over the following useful lives:

|            |          |
|------------|----------|
| Trademarks | 10 years |
|------------|----------|

Intangible assets are periodically evaluated for recoverability, and those evaluations take into account events or circumstances that warrant revised estimates of useful lives or that indicate impairment exists.

##### **Research and development expenditures**

Research expenditures are charged to net income in the period in which they are incurred.

Costs in respect of the development of software for the Company's internal use are expensed as incurred, except to the extent that these costs are incurred during the application development stage. All other costs including those incurred in the project development and post-implementation stages are expensed as incurred. For six-month periods ended June 30, 2010 and 2009, the amount of research and development expenditures charged to net income were zero and 69,000 thousand, respectively.

##### **Inventory**

Inventory is stated at the lower of cost or market value. Cost is determined on a first-in, first-out basis and includes transport and handling costs.

##### **Investment securities**

The Company classifies its debt security into available-for-sale security. The Company classifies its equity securities that do not have readily determinable fair values as other investment securities and those securities are stated at cost.

The Company reviews its investment portfolio each reporting period to determine whether there are identified events or circumstances that would indicate there is a decline in the fair value that is considered to be other-than-temporary. For other securities which are stated at cost, if there are no identified events or circumstances that would have a material adverse effect on the fair value of the investment, then the fair value is not estimated. If an investment is deemed to have experienced an other-than-temporary decline below its cost basis, the Company reduces the carrying amount of the investment to its quoted or estimated fair value, as applicable, and establishes a new cost basis for the investment. There was no impairment loss on investment securities recognized for six-months periods ended June 30, 2010 and 2009.

##### **Fair value of financial instruments**

The Company applies fair value accounting for all financial assets and liabilities and non-financial assets and liabilities that are recognized or disclosed at fair value in the financial statements. The Company defines fair value as

the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities, which are required to be recorded at fair value, the Company considers the principal or most advantageous market in which the Company would transact and the market-based risk measurements or assumptions that market participants would use in pricing the asset or liability, such as inherent risk, transfer restrictions and credit risk. ASC 820, *Fair Value Measurements and Disclosure* ( ASC 820 ), establishes a framework for measuring fair value and expands disclosures about fair value measurements.

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## **KSNET, Inc.**

### **Notes to the Unaudited Financial Statements**

#### **For the six months ended June 30, 2010 and 2009**

**(All amounts stated in thousands of Korean won, unless otherwise stated)**

#### **2. SIGNIFICANT ACCOUNTING POLICIES (continued)**

##### **Derivatives**

The Company recognizes all derivative financial instruments in the balance sheets as either assets or liabilities at fair value.

For a derivative financial instrument not designated as a hedging instrument, the gain or loss is recognized in earnings in the period of change

##### **Revenue recognition**

The Company recognizes revenue when:

- There is persuasive evidence of an agreement or arrangement;
- Delivery of products has occurred or services have been rendered;
- The seller's price to the buyer is fixed or determinable; and
- Collectability is reasonably assured.

The Company's revenue is mainly consists of revenue from Card VAN, Banking VAN, Payment Gateway (PG) and Sale of Merchandise. The Company's revenue recognition methods for each component are as follows:

##### *Card VAN*

Card VAN services consist of services relating to authorization of credit card transactions including transmission of transaction details (Authorization Service), and collection of receipts associated with the credit card transactions (Collection Service). With its Authorization Service, the Company connects credit card companies with merchants online when a customer uses his/her credit card via terminals installed at merchants' sites and the Company's central processing server for approval of credit card transactions. Immediately after approval of credit card transactions, the Company transmits details of the transactions to credit card companies online for processing payments. Collection Service captures the transaction data and gathers receipts as documented evidences and provides them to credit card companies upon request. The Company earns service fees based on the number of processed transactions for credit card companies when services are rendered in accordance with the contracts entered into between credit card companies and the Company. The Company bills for its service charges to credit card companies each month. Each service could be provided either individually or collectively, based on terms of contracts.

The Company charges commission fee to credit card companies for the Authorization Service provided based on the number of approvals transferred. The right to receive fee for services rendered will take effect as credit card transactions are approved and details of the transactions are transmitted. Therefore, revenues from the Authorization Service are recognized when the credit card transactions are authorized and details of the transactions are transmitted. In the case of Collection Service, the Company is not allowed to receive its commission fees until it provides collected receipts to the credit card companies. Therefore, revenue from the Collection Service is recognized when the Company collects the receipts and provides them to the card companies.

For multi-element arrangements, the Company has identified two deliverables in arrangements. The first

deliverable is the Authorization Service, and the second deliverable is the Collection Service. The Company evaluates each deliverable in an arrangement to determine whether they represent separate units of accounting. A deliverable constitutes a separate unit of accounting when it has standalone value and there are no customer-negotiated refunds or return rights for the delivered elements. If the arrangement includes a customer-negotiated refund or return right relative to the delivered item and the delivery and performance of the undelivered item is considered probable and substantially in the Company's control, the delivered element constitutes a separate unit of accounting. In instances when the aforementioned criteria are not met, the deliverable is combined with the undelivered elements and the allocation of the arrangement consideration and revenue recognition is determined for the combined unit as a single unit. Allocation of the consideration is determined at arrangement inception on the basis of each unit's relative selling price. In such circumstances, the Company uses a hierarchy to determine the selling price to be used for allocating revenue to deliverables: (i) vendor-specific objective evidence of fair value ( VSOE ), (ii) third-party evidence of selling price ( TPE ), and (iii) best estimate of the selling price ( ESP ).

## **KSNET, Inc.**

### **Notes to the Unaudited Financial Statements**

#### **For the six months ended June 30, 2010 and 2009**

(All amounts stated in thousands of Korean won, unless otherwise stated)

#### **2. SIGNIFICANT ACCOUNTING POLICIES (continued)**

##### **Revenue recognition (continued)**

###### *Card VAN (continued)*

VSOE generally exists only when the Company sells the deliverable separately and is the price actually charged by the Company for that deliverable. ESPs reflect the Company's best estimates of what the selling prices of elements would be if they were sold regularly on a stand-alone basis. Because the Company has neither VSOE nor TPE for the two deliverables, the allocation of revenue has been based on the Company's ESPs. Amounts allocated to the Authorization and the Collection Service are recognized at the time of service provided the other conditions for revenue recognition have been met.

The Company's process for determining its ESP for deliverables without VSOE or TPE considers multiple factors that may vary depending upon the unique facts and circumstances related to each deliverable. Key factors considered by the Company in developing the ESPs include prices charged by the Company, historical pricing practices and controls, range of prices for various customers and the nature of the services. Consideration is also given to market conditions such as competitor pricing strategies and market perception.

###### *Banking VAN:*

Banking VAN is a division supporting a Company's fund management business (large payment transfers, collections, etc.) by relaying financial transactions between client companies and financial institutions. Financial transactions between two or more business enterprises, or between business enterprises and their customers, are conducted through the transaction-processing network established between the Company and the banks. The data is consolidated and transmitted to each bank batch/real time. Revenue from the Banking Van service is recognized when the service is rendered by the Company.

###### *Payment Gateway service (PG service)*

With its PG service, the Company provides the Internet-based settlement service between on-line shopping mall and a credit card company when a customer uses his/her credit card, debit card or on-line payment to pay for goods or services. The Company receives fees for carrying out settlements for electronic transactions. Revenue from the PG service is recognized when the service is rendered by the Company.

###### *Sale of Merchandise*

The Company buys terminals from manufacturers, and subsequently sells them through its subsidiary agencies. Revenue is recognized when significant risks and rewards of ownership of terminals have passed to the buyer, usually on delivery of the terminals to the buyer.

##### **Accrued severance benefits**

Employees and directors are entitled to receive a lump-sum payment upon termination of their employment with the Company, based on their length of service and rate of pay at the time of termination. Accrued severance benefits



are estimated assuming all eligible employees were to terminate their employment at the balance sheet date. The annual severance benefits expense charged to income is calculated based on the net change in the accrued severance benefits payable at the balance sheet date, plus the actual payments made during the year.

The contributions to the severance insurance deposit are deducted from accrued severance benefit liabilities. Contributed amounts are refunded from the insurance company to employees upon their retirement.

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## **KSNET, Inc.**

### **Notes to the Unaudited Financial Statements**

#### **For the six months ended June 30, 2010 and 2009**

**(All amounts stated in thousands of Korean won, unless otherwise stated)**

#### **2. SIGNIFICANT ACCOUNTING POLICIES (continued)**

##### **Commitments and contingencies**

Liabilities arising from claims, assessments, litigation, fines, and penalties and other sources, are recorded when it is probable that a liability has been incurred and the amount of the assessment and/or remediation can be reasonably estimated. Legal costs incurred in connection with loss contingencies are expensed as incurred.

##### **Earnings per share**

Basic earnings per share are computed by dividing net income by the weighted-average number of shares of common stock outstanding during the year. Diluted earnings per share are calculated by dividing net income by the weighted-average number of shares of common stock outstanding during the year plus the weighted-average number of common shares that would have been outstanding assuming the conversion of all dilutive potential common shares.

##### **Recent accounting pronouncements adopted**

In June 2009, the Financial Accounting Standards Board ( FASB ) issued the FASB Accounting Standards Codification (the Codification ) as the single source of authoritative GAAP recognized by the FASB to be applied by non-governmental entities. The Codification supersedes all existing non-SEC accounting and reporting standards. Following the issue of the Codification, the FASB has issued new guidance in the form of Accounting Standards Updates. This Codification is effective for financial statements issued for interim and annual periods ending after September 15, 2009. The Codification was effective for the Company from January 1, 2009. The Codification did not impact the Company's financial position or results of operations.

In September 2009, the FASB issued guidance on revenue recognition in multiple-deliverable revenue arrangements. The guidance amended the existing guidance on allocating consideration received between the elements in a multiple-deliverable arrangement and established a selling price hierarchy for determining the selling price of a deliverable. The selling price used for each deliverable will be based on vendor-specific objective evidence ( VSOE ) if available, third-party evidence if VSOE is not available, or estimated selling price if neither VSOE nor third-party evidence is available. The guidance replaced the term fair value in the revenue allocation with selling price to clarify that the allocation of revenue is based on entity specific assumptions rather than the assumptions of a market place participant. The guidance eliminates the residual method of allocation and requires that arrangement consideration be allocated using the relative selling price method. It also significantly expands the disclosures related to a vendor's multiple-deliverable revenue arrangements. Earlier application is permitted. The Company adopted these new accounting standards in the beginning of 2007.

In October 2009, the FASB issued guidance which amended the scope of existing software revenue recognition accounting. Tangible products containing software components and non-software components that function together to deliver the product's essential functionality would be scoped out of the accounting guidance on software and accounted for based on other appropriate revenue recognition guidance. This guidance must be adopted in the same period that the company adopts the amended guidance for arrangements with multiple deliverables described in the preceding paragraph. The adoption of this guidance did not have an impact on the Company's financial position or results of operations.

In January 2010, the FASB issued Update 2010-06, *Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements*, ( Update 2010-06 ). Update 2010-06 amends ASC 820 and clarifies and provides additional disclosure requirements related to recurring and non-recurring fair value measurements and employers' disclosures about postretirement benefit plan assets. This Update became effective for us on January 1, 2010. The adoption did not have a material impact on the Company's financial position or results of operations.

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**KSNET, Inc.****Notes to the Unaudited Financial Statements****For the six months ended June 30, 2010 and 2009**

(All amounts stated in thousands of Korean won, unless otherwise stated)

**2. SIGNIFICANT ACCOUNTING POLICIES (continued)****Recent accounting pronouncements not yet adopted as of December 31, 2009**

In July 2010, the FASB issued amendments to the disclosure requirements about the credit quality of financing receivables and the allowance for credit losses. The purpose of the additional disclosures is to enable users of financial statements to better understand the nature of credit risk inherent in an entity's portfolio of financing receivables and how that risk is analyzed. For end of period balances, the new disclosures are required to be made in all interim and annual periods ending on or after December 15, 2010. For activity during a reporting period, the disclosures are required to be made in all interim and annual periods after January 1, 2011. These changes will not have an impact on the Company's financial results as this guidance only relates to additional disclosures.

**3. RESTRICTED FINANCIAL INSTRUMENTS**

The following table represents financial instrument which are restricted in use as of June 30, 2010 and 2009.

|                                  | <b>Restriction</b>                                    | <b>2010</b>      | <b>2009</b>    |
|----------------------------------|---|------------------|----------------|
| Short-term financial instruments | Pledge, etc.  | 1,179,364        | 788,000        |
| Long-term financial instruments  | Pledge, Guarantee deposits for checking account, etc. | 197,000          | 3,000          |
| <b>Total</b>                     |   | <b>1,376,364</b> | <b>791,000</b> |

The entire amount of restricted short-term financial instrument is included in short-term financial instruments and the entire amount of restricted long-term financial instrument is included in other non-current assets in the balance sheet.

**4. ACCOUNTS RECEIVABLE**

The following table presents accounts receivable at June 30, 2010 and 2009:

**Current accounts receivable, net**

|   | <b>2010</b> | <b>2009</b> |
|---|-------------|-------------|
| Accounts receivable, gross              | 11,326,377  | 9,284,748   |
| Discount on current accounts receivable | (5,108)     | (23,066)    |
| Allowance for doubtful accounts         | (210,080)   | (174,601)   |
| Accounts receivable, net                | 11,111,189  | 9,087,081   |

**Non-current accounts receivable, net**

|  | <b>2010</b> | <b>2009</b> |
|--|-------------|-------------|
| Non-current accounts receivable, gross | 1,689,403   | 2,299,111   |
| Discount on accounts receivable        | (167,212)   | (232,681)   |
| Allowance for doubtful accounts        | (16,894)    | (22,991)    |
| Non-current accounts receivable, net   | 1,505,297   | 2,043,439   |

Non-current accounts receivable arose from installment sales of Point of Sale( POS ) terminals for the three years to merchants. Non-current accounts receivable amounts are determined based on the present value using appropriate

risk adjusted discount rate considering environment of counter-party.

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**KSNET, Inc.****Notes to the Unaudited Financial Statements****For the six months ended June 30, 2010 and 2009****(All amounts stated in thousands of Korean won, unless otherwise stated)****5. INVENTORY**

Inventory valuations as of June 30, 2010 and 2009 are summarized as follows:

|                   | <b>As of June 30, 2010</b> |                            |                        |
|-------------------|----------------------------|----------------------------|------------------------|
|                   | Cost                       | Lower of Cost or<br>Market | Valuation<br>Allowance |
| <b>Inventory:</b> |                            |                            |                        |
| Merchandise       | 1,380,603                  | 1,380,603                  | -                      |
| <b>Total</b>      | <b>1,380,603</b>           | <b>1,380,603</b>           | <b>-</b>               |

|                   | <b>As of June 30, 2009</b> |                            |                        |
|-------------------|----------------------------|----------------------------|------------------------|
|                   | Cost                       | Lower of Cost or<br>Market | Valuation<br>Allowance |
| <b>Inventory:</b> |                            |                            |                        |
| Merchandise       | 1,864,666                  | 1,864,666                  | -                      |
| <b>Total</b>      | <b>1,864,666</b>           | <b>1,864,666</b>           | <b>-</b>               |

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**KSNET, Inc.****Notes to the Unaudited Financial Statements****For the six months ended June 30, 2010 and 2009**

(All amounts stated in thousands of Korean won, unless otherwise stated)

**6. FAIR VALUE OF FINANCIAL INSTRUMENTS****Fair value of financial instruments**

The following table presents the carrying amounts and estimated fair values of the Company's financial instruments as of June 30, 2010 and 2009:

|                                      | 2010              |                   | 2009              |                   |
|--------------------------------------|-------------------|-------------------|-------------------|-------------------|
|                                      | Carrying amount   | Fair value        | Carrying amount   | Fair value        |
| <b>Financial assets</b>              |                   |                   |                   |                   |
| Cash and cash equivalents            | 20,017,727        | 20,017,727        | 8,565,795         | 8,565,795         |
| Short-term financial instruments     | 3,199,364         | 3,199,364         | 1,798,000         | 1,798,000         |
| Accounts receivable, net             | 11,111,189        | 11,111,189        | 9,087,081         | 9,087,081         |
| Short-term loans, net                | 2,375             | 2,375             | 43,320            | 43,320            |
| Non-current accounts receivable, net | 1,505,297         | 1,505,297         | 2,043,439         | 2,043,439         |
| Available-for-sale securities        | 100,000           | 100,000           | 100,000           | 100,000           |
| Other investment securities          | 222,693           | 222,693           | 222,693           | 222,693           |
| Long-term financial instruments      | 213,500           | 213,500           | 16,500            | 16,500            |
| Long-term loans, net                 | 900,364           | 833,153           | 1,241,392         | 1,136,150         |
| <b>Total financial assets</b>        | <b>37,272,509</b> | <b>37,205,298</b> | <b>23,118,220</b> | <b>23,012,978</b> |
| <b>Financial liabilities</b>         |                   |                   |                   |                   |
| Accounts payable                     | 6,154,692         | 6,154,692         | 5,171,972         | 5,171,972         |
| Short-term borrowings                | 2,000,000         | 2,000,000         | -                 | -                 |
| Derivatives                          | -                 | -                 | 70,406            | 70,406            |
| Current portion of long-term debt    | 6,000,000         | 6,000,000         | 4,000,000         | 4,000,000         |
| Long-term debt                       | -                 | -                 | 6,000,000         | 5,780,714         |
| <b>Total financial liabilities</b>   | <b>14,154,692</b> | <b>14,154,692</b> | <b>15,242,378</b> | <b>15,023,092</b> |

The fair values of the financial instruments shown in the above table represent the amounts that would be received to sell those assets or that would be paid to transfer those liabilities in an orderly transaction between market participants at that date. Those fair value measurements maximize the use of observable inputs. However, in situations where there is little, if any, market activity for the asset or liability at the measurement date, the fair value measurement reflects the Company's own judgments about the assumptions that market participants would use in pricing the asset or liability. Those judgments are developed by the Company based on the best information available in the circumstances, including expected cash flows and appropriately risk adjusted discount rates, available observable and unobservable inputs.

## **KSNET, Inc.**

### **Notes to the Unaudited Financial Statements**

#### **For the six months ended June 30, 2010 and 2009**

**(All amounts stated in thousands of Korean won, unless otherwise stated)**

#### **6. FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)**

##### **Fair value of financial instruments (continued)**

The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

*Cash and cash equivalents, short-term financial instruments, long-term financial instruments, accounts receivable, short-term loans, non-current accounts receivable, accounts payable, short-term borrowings and current portion of long-term debt*

The carrying amounts, at face value or cost plus accrued interest, approximate fair value because of the short maturity of these instruments.

##### *Available for sale and other investment securities*

Debt securities classified as available-for-sale are measured using quoted market prices multiplied by the quantity held when quoted market prices are available. If quoted market prices for those debt securities are not available, the fair value is determined using an income approach valuation technique (present value using the discount rate adjustment technique) that considers, among other things, rates currently observed in publicly traded debt markets for debt of similar terms to companies with comparable credit risk, the issuer's credit spread, and illiquidity by sector and maturity. Equity securities that do not have readily determinable fair value are classified as other investment securities and measured at cost less any impairment.

##### *Long-term loans*

The fair value of the long-term loans is determined using an income approach valuation technique (present value using the discount rate adjustment technique) based on the present value of expected future cash flows which incorporates a risk premium to take into account the risks inherent in those expected cash flows. The long-term loans are recorded at their carrying value. The fair value is measured for disclosure purposes.

##### *Long-term debt*

The fair value of the Company's long term debt is measured using quoted offer side prices when quoted market prices are available. If quoted market prices are not available, the fair value is determined by discounting the future cash flows of each instrument at rates that reflect rates currently observed in publicly traded debt markets for debt of similar terms to companies with comparable credit risk. For long-term debt measurements, where there are no rates currently observable in publicly traded debt markets of similar terms to companies with comparable credit, the Company uses market interest rates and adjusts that rate for all necessary risks, including its own credit risk. In determining an appropriate spread to reflect its credit standing, the Company considers credit default swap spreads, bond yields of other long-term debt offered by the Company, and interest rates currently offered to the Company for similar debt instruments of comparable maturities by the Company's bankers as well as other banks that regularly compete to provide financing to the Company. The long-term debt is recorded at its carrying value. The fair value is measured for disclosure purposes.



*Derivatives*

All derivatives are recognized on the balance sheet at fair value based on quoted market prices, dealer or counterparty quotes, if available. If quoted market prices are not available, pricing or valuation models are applied to current market information to estimate the fair value.

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**KSNET, Inc.****Notes to the Unaudited Financial Statements****For the six months ended June 30, 2010 and 2009****(All amounts stated in thousands of Korean won, unless otherwise stated)****6. FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)****Fair value hierarchy**

Fair value is defined as the price that would be received upon sale of an asset or paid upon transfer of a liability in an orderly transaction between market participants at the measurement date and in the principal or most advantageous market for that asset or liability. The fair value should be calculated based on assumptions that market participants would use in pricing the asset or liability, not on assumptions specific to the entity. In addition, the fair value of liabilities should include consideration of non-performance risk including the Company's own credit risk.

Fair value measurements and inputs are categorized into a fair value hierarchy which prioritizes the inputs into three levels based on the extent to which inputs used in measuring fair value are observable in the market. Each fair value measurement is reported in one of the three levels which are determined by the lowest level input that is significant to the fair value measurement in its entirety.

These levels are:

- Level 1 inputs are based upon unadjusted quoted prices for identical instruments traded in active markets.
- Level 2 inputs are based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3 inputs are generally unobservable and typically reflect management's estimates of assumptions that market participants would use in pricing the asset or liability. The fair values are therefore determined using model-based techniques that include option pricing models, discounted cash flow models, and similar techniques.

The following table presents the Company's assets and liabilities measured at fair value on a recurring basis as of June 30, 2010:

|  | Quoted price in<br>active markets<br>for<br>identical assets<br>(Level 1) | Significant<br>other<br>observable<br>inputs<br>(Level 2) | Significant<br>unobservable<br>inputs<br>(Level 3) | Total          |
|--|---|---|--|----------------|
| <b>Assets</b>                          |   |   |  |                |
| Available-for-sale securities          | -   | 100,000   | -  | 100,000        |
| <b>Total assets at fair value</b>      | -   | <b>100,000</b>  | -  | <b>100,000</b> |
| <b>Liabilities</b>                     |   |   |  |                |
| Derivatives                            | -   | -   | -  | -              |
| <b>Total liabilities at fair value</b> | -   | -   | -  | -              |

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**KSNET, Inc.****Notes to the Unaudited Financial Statements****For the six months ended June 30, 2010 and 2009**

(All amounts stated in thousands of Korean won, unless otherwise stated)

**6. FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)****Fair value hierarchy (continued)**

The following table presents the Company's assets and liabilities measured at fair value on a recurring basis as of June 30, 2009:

|  | Quoted Price in<br>Active Markets<br>for<br>Identical Assets<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) | <b>Total</b>   |
|--|---|---|--|----------------|
| <b>Assets</b>                          |   |   |  |                |
| Available-for-sale securities          | -   | 100,000   | -  | 100,000        |
| <b>Total assets at fair value</b>      | <b>-</b>  | <b>100,000</b>  | <b>-</b>   | <b>100,000</b> |
| <b>Liabilities</b>                     |   |   |  |                |
| Derivatives                            | -   | 70,406  | -  | 70,406         |
| <b>Total liabilities at fair value</b> | <b>-</b>  | <b>70,406</b>   | <b>-</b>   | <b>70,406</b>  |

**7. DERIVATIVES**

The Company uses derivative financial instruments primarily to manage the risks associated with fluctuations in interest rates. In 2008, the Company used variable-rate Certificate of Deposit (CD) debt to finance its operations. The debt obligations expose to the Company to variability in interest payments due to changes in interest rates. Management believed that it is prudent to limit the variability of a portion of its interest payments. To meet this objective, management entered into CD based interest rate swap agreements to manage fluctuations in cash flows resulting from changes in the benchmark interest rate of CD. This swap changes the variable rate cash flow exposure on the debt obligations to fixed cash flows. Under the terms of the interest rate swaps, the Company receives CD based variable interest rate payments (CD + 1.425%) and makes fixed interest rate payments of 6.625%, thereby creating the equivalent of fixed-rate debt for the notional amount ( 4,000 million) of its debt hedged. However, the Company did not designate the interest rate related derivatives as hedging instruments under ASC 815 and therefore, any gains or losses on derivatives are recognized in the current income.

The fair value of derivatives held as of June 30, 2010 and 2009 are as follows:

|   | Liability derivatives |             |
|---|-----------------------|-------------|
|   | <b>2010</b>           | <b>2009</b> |
| Derivatives:  |                       |             |
| Interest Rate Swap  | -                     | 70,406      |
| Total derivatives not designated as hedging instruments under ASC 815 | -                     | 70,406      |

The effects of derivatives instruments on income for the periods ended June 30, 2010 and 2009 are summarized as follows:

|                               | Gains (Losses) |        |
|-------------------------------|----------------|--------|
|                               | 2010           | 2009   |
| Gains (losses) on derivatives | 22,266         | 21,427 |
|                               | F-47           |        |

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**KSNET, Inc.****Notes to the Unaudited Financial Statements****For the six months ended June 30, 2010 and 2009**

(All amounts stated in thousands of Korean won, unless otherwise stated)

**8. LONG-TERM DEBT**

Long-term debt as of June 30, 2010 and 2009 are summarized as follows:

|                                    | <b>Maturity</b> | <b>2010</b> | <b>2009</b> |
|------------------------------------|-----------------|-------------|-------------|
| Long-term debt                     |                 |             |             |
| (Annual interest rate: 4.95~5.77%) | 2010            | 6,000,000   | 10,000,000  |
| Current portion of long-term debt  |                 | (6,000,000) | (4,000,000) |
| Total                              |                 | -           | 6,000,000   |

Long-term debt is subject to various restrictive covenants. These covenants typically include restrictions on the debt to equity ratio, credit rating, working capital ratio, and other similar financial ratios. The Company was in compliance with these financial covenants during all periods presented.

**9. PROPERTY AND EQUIPMENT**

Property and equipment as of June 30, 2010 and 2009 are summarized as follows:

|                                 | <b>2010</b>       | <b>2009</b>       |
|---------------------------------|-------------------|-------------------|
| Cost:                           |                   |                   |
| Land                            | 981,257           | 981,257           |
| Buildings                       | 625,943           | 625,943           |
| Structures                      | 203,350           | 203,350           |
| Vehicles                        | 25,350            | 40,629            |
| Tools, furniture and fixtures   | 76,993,018        | 62,986,908        |
| Machinery and equipment         | 6,054,301         | 6,054,301         |
| Software                        | 5,230,167         | 4,742,157         |
|                                 | <b>90,113,386</b> | <b>75,634,545</b> |
| Accumulated depreciation:       |                   |                   |
| Buildings                       | 136,326           | 115,461           |
| Structures                      | 139,236           | 113,817           |
| Vehicles                        | 25,350            | 40,629            |
| Tools, furniture and fixtures   | 54,123,608        | 44,224,728        |
| Machinery and equipment         | 5,558,521         | 5,169,204         |
| Software                        | 4,003,959         | 3,501,150         |
|                                 | <b>63,987,000</b> | <b>53,164,989</b> |
| Accumulated loss on impairment: |                   |                   |
| Tools, furniture and fixtures   | -                 | 22,301            |
| Machinery and equipment         | 12,359            | -                 |
|                                 | <b>12,359</b>     | <b>22,301</b>     |
| Carrying amount:                |                   |                   |
| Land                            | 981,257           | 981,257           |
| Buildings                       | 489,617           | 520,915           |
| Structures                      | 64,114            | 102,242           |
| Vehicles                        | -                 | -                 |

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|                               |                   |                   |
|-------------------------------|-------------------|-------------------|
| Tools, furniture and fixtures | 22,869,410        | 16,671,127        |
| Machinery and equipment       | 483,420           | 1,109,356         |
| Software                      | 1,226,208         | 1,160,694         |
|                               | <b>26,114,027</b> | <b>22,447,255</b> |

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**KSNET, Inc.****Notes to the Unaudited Financial Statements****For the six months ended June 30, 2010 and 2009**

(All amounts stated in thousands of Korean won, unless otherwise stated)

**9. PROPERTY AND EQUIPMENT (continued)**

For six-month periods ended June 30, 2010 and 2009, total depreciation expenses for the property and equipment were 5,620 million, and 4,659 million, respectively. Total depreciation expenses include cost of sales in an amount of 4,012 million and 3,135 million; and selling, general, administrative expenses of 1,608 million, and 1,524 million for six-month periods ended June 30, 2010 and 2009, respectively.

**10. INTANGIBLE ASSETS**

Summarized below is the carrying value and accumulated amortization of intangible assets as of June 30, 2010 and 2009:

|   | <b>As of June 30, 2010</b>  |                                 |                           |
|---|-----------------------------|---------------------------------|---------------------------|
|   | <b>Gross carrying value</b> | <b>Accumulated amortization</b> | <b>Net carrying value</b> |
| Finite-lived intangible assets:             |                             |                                 |                           |
| Trademarks                                  | 77,057                      | 57,366                          | 19,691                    |
| <b>Total finite-lived intangible assets</b> | <b>77,057</b>               | <b>57,366</b>                   | <b>19,691</b>             |

|   | <b>As of June 30, 2009</b>  |                                 |                           |
|---|-----------------------------|---------------------------------|---------------------------|
|   | <b>Gross carrying value</b> | <b>Accumulated amortization</b> | <b>Net carrying value</b> |
| Finite-lived intangible assets:             |                             |                                 |                           |
| Trademarks                                  | 77,057                      | 49,979                          | 27,078                    |
| <b>Total finite-lived intangible assets</b> | <b>77,057</b>               | <b>49,979</b>                   | <b>27,078</b>             |

Amortization expenses charged for the periods ended June 30, 2010 and 2009 were 3.7 million, respectively.

Future estimated annual amortization expense for the next five fiscal years is presented in the table below. Actual amortization expense in future periods could differ from this estimate as a result of acquisitions, changes in useful lives and other relevant factors.

| Year | Amount |
|------|--------|
| 2011 | 7,387  |
| 2012 | 7,387  |
| 2013 | 1,224  |
| 2014 | -      |
| 2015 | -      |

**KSNET, Inc.****Notes to the Unaudited Financial Statements****For the six months ended June 30, 2010 and 2009**

(All amounts stated in thousands of Korean won, unless otherwise stated)

**11. OTHER ASSETS AND LIABILITIES****Other Current Assets**

|                                 | 2010       | 2009       |
|---------------------------------|------------|------------|
| Short-term Loans                | 2,500      | 53,416     |
| Allowance for doubtful accounts | (125)      | (10,096)   |
| Other receivables               | 582,290    | 439,179    |
| Allowance for doubtful accounts | (15,723)   | (23,459)   |
| Accrued income                  | 42,190     | 45,136     |
| Advanced prepayments            | 3,133,513  | 4,477,088  |
| Prepaid expenses                | 12,780,982 | 8,122,696  |
|                                 | 16,525,627 | 13,103,960 |

**Other non-current Assets**

|                                 | 2010      | 2009      |
|---------------------------------|-----------|-----------|
| Long-term financial instruments | 213,500   | 16,500    |
| Other investment securities     | 222,693   | 222,693   |
| Long-term loans (*)             | 947,752   | 1,306,728 |
| Allowance for doubtful accounts | (47,388)  | (65,336)  |
| Guarantee deposits (**)         | 3,208,209 | 3,216,729 |
| Other investment                | 1,038,481 | 1,038,481 |
|                                 | 5,583,247 | 5,735,795 |

(\*) Long-term loans include loans to employees for mortgage in an amount of 765 million and 758 million as of June 30, 2010 and 2009, respectively.

(\*\*) Guarantee deposits consist of deposits for leased offices.

**Other current Liabilities**

|                         | 2010       | 2009       |
|-------------------------|------------|------------|
| Other payables          | 2,465,520  | 1,196,341  |
| Advances from customers | 134,099    | 260,710    |
| Value-added tax payable | 1,098,692  | 761,741    |
| Withholdings (*)        | 11,118,299 | 6,461,120  |
| Other accrued expenses  | 452,020    | 424,237    |
| Deposits received       | 170,751    | 370,307    |
| Income taxes payable    | 1,622,468  | 1,414,880  |
| Derivatives             | -          | 70,406     |
|                         | 17,061,849 | 10,959,742 |

(\*) Withholdings are related to the Payment Gateway Service for accounts received from the credit card companies withheld before they are passed to the on-line shopping mall.

**Other non-current Liabilities**

| 2010 | 2009 |
|------|------|
|------|------|



|                                   |           |         |
|-----------------------------------|-----------|---------|
| Unrecognized tax benefits(Note15) | 1,036,750 | 148,135 |
|                                   | 1,036,750 | 148,135 |
|                                   | F-50      |         |

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**KSNET, Inc.****Notes to the Unaudited Financial Statements****For the six months ended June 30, 2010 and 2009**

(All amounts stated in thousands of Korean won, unless otherwise stated)

**12. OTHER INCOME (EXPENSE), net**

| <b>Other income(expense), net</b>            | <b>2010</b> | <b>2009</b> |
|--|-------------|-------------|
| Loss on foreign currency transactions        | (104)       | (113)       |
| Gain on disposal of property and equipment   | 2,267       | 1,642       |
| Loss on impairment of property and equipment | (12,359)    | -           |
| Gain on valuation of derivatives             | 22,266      | 21,427      |
| Donations                                    | (267,611)   | (15,460)    |
| Miscellaneous                                | (1,124)     | -           |
|  | (244,306)   | 7,496       |

**13. EQUITY****Common stock**

The holder of each share of common stock has the right to one vote. The number of issued common shares as of June 30, 2010 and 2009 are 13,605,766, respectively. All common stock is issued at par value. Amount of capital stock and additional paid-in capital as of June 30, 2010 and 2009 are as follows:

|                             | <b>2010</b>      | <b>2009</b>      |
|-----------------------------|------------------|------------------|
| Capital stock:              |                  |                  |
| Common stock                | 6,802,883        | 6,802,883        |
| <b>Total</b>                | <b>6,802,883</b> | <b>6,802,883</b> |
| Additional paid-in capital: |                  |                  |
| Other paid-in capital       | 33,568           | 33,568           |
| <b>Total</b>                | <b>33,568</b>    | <b>33,568</b>    |

**Stock retirement**

Total amount of common stocks retired as of June 30, 2010 and 2009 are as follows:

|              | <b>2010</b> |          | <b>2009</b>    |                |
|--------------|-------------|----------|----------------|----------------|
|              | Shares      | Amount   | Shares         | Amount         |
| Common stock | -           | -        | 946,018        | 473,009        |
| <b>Total</b> | <b>-</b>    | <b>-</b> | <b>946,018</b> | <b>473,009</b> |

According to ASC 505, if an enterprise's stock is retired, an excess of purchase price over par or stated value may be allocated between additional paid-in capital and retained earnings. On March 26, 2009, the Company repurchased and retired 946,018 shares of common stock and an excess of repurchase price over par value was allocated to the retained earnings for amount of 3,615 million.

**KSNET, Inc.****Notes to the Unaudited Financial Statements****For the six months ended June 30, 2010 and 2009****(All amounts stated in thousands of Korean won, unless otherwise stated)****14. ACCRUED SEVERANCE BENEFITS**

Accrued severance benefits as of June 30, 2010 and 2009 are as follows:

|  | <b>2010</b>      | <b>2009</b>      |
|--|------------------|------------------|
| Balance at beginning of period           | 2,458,097        | 1,993,792        |
| Provision for severance benefits         | 569,331          | 405,862          |
| Severance payments during the period     | (323,104)        | (148,307)        |
| Balance at end of period                 | 2,704,324        | 2,251,347        |
| Deposit for severance benefits insurance | (1,511,464)      | (1,168,925)      |
| Accrued severance benefits               | <b>1,192,860</b> | <b>1,082,422</b> |

The severance benefits are funded approximately 55.9% and 51.9% as of June 30, 2010 and 2009, respectively through severance insurance deposits with the Shinhan Life Insurance Company and the Hana Bank for the payment of severance benefits. The Company has no additional liability once the amount has been contributed, thus the Company deducts contributions made to the severance insurance deposits from accrued severance benefit liabilities. The beneficiaries of the severance insurance deposit are the Company's employees.

The Company expects to pay the following severance benefits, which are currently accrued for the Company's obligation through June 30, 2010, to its employees. If they terminate upon their normal retirement age:

|           |         |
|-----------|---------|
| 2011      | -       |
| 2012      | -       |
| 2013      | -       |
| 2014      | -       |
| 2015      | -       |
| 2016~2020 | 235,392 |

The above amounts were determined based on the employees' current salary rates and the number of service years that will be accumulated upon their retirement date. These amounts do not include amounts that might be paid to employees who will cease working with the Company before their normal retirement age.

**15. INCOME TAXES**

In accordance with the amendment of Corporate Tax Act enacted in 2008, the statutory income tax rate was amended to 24.2% effective for fiscal year 2009 and 22.0% for fiscal years 2010 and thereafter. However, in 2009, Corporate Income Tax Law was further amended and the statutory income tax rate of 24.2% is effective for fiscal years 2009 until 2011 and 22% for fiscal years 2012 and thereafter. Accordingly, deferred income taxes as of December 31, 2009 were calculated based on the enacted rates of 24.2% and 22.0%.

**KSNET, Inc.****Notes to the Unaudited Financial Statements****For the six months ended June 30, 2010 and 2009****(All amounts stated in thousands of Korean won, unless otherwise stated)****15. INCOME TAXES (continued)**

Actual income tax expense differs from the theoretical amount that would arise at the Korean statutory tax rate for six months ended June 30, 2010 and 2009 as follows:

|  | <b>2010</b> | <b>2009</b> |
|--|-------------|-------------|
| Income tax expense at Korean statutory tax rate                | 2,526,580   | 1,920,220   |
| Nondeductible items  | 113,806     | (90,455)    |
| Adjustments to uncertain and effectively settled tax positions | (688,185)   | (276,014)   |
| Income tax exemption   | 68,283      | (5,524)     |
| Other  | (31,256)    | 115,595     |
| Income tax expense(benefit)                                    | 1,989,228   | 1,663,822   |

The following is a reconciliation of income taxes computed at the Korean tax rate to actual effective income tax provision:

|  | <b>2010</b> | <b>2009</b> |
|--|-------------|-------------|
| Statutory income tax rate                | 24.2%       | 24.2%       |
| Expenses not deductible for tax purposes | 1.1         | (1.1)       |
| Tax exemptions                           | (6.6)       | (3.5)       |
| FIN 48 tax contingencies and settlements | 0.6         | (0.1)       |
| Others                                   | (0.3)       | 1.3         |
| Effective income tax rate                | 19.0%       | 20.8%       |

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**KSNET, Inc.****Notes to the Unaudited Financial Statements****For the six months ended June 30, 2010 and 2009**

(All amounts stated in thousands of Korean won, unless otherwise stated)

**15. INCOME TAXES (continued)****Deferred tax assets and liabilities**

Deferred income taxes reflect the temporary differences between the amounts at which assets and liabilities are recorded for financial reporting purposes and the amounts utilized for tax purposes. The primary components of the temporary differences that gave rise to the Company's deferred tax assets and liabilities as of June 30, 2010 and 2009, and their classification, were as follows:

**Deferred tax assets**

|                                  | <b>2010</b>      | <b>2009</b>      |
|----------------------------------|------------------|------------------|
| Investment securities            | 271,154          | 293,155          |
| Depreciation and amortization    | 112,542          | 49,014           |
| Derivatives                      | -                | 15,489           |
| Advanced payments                | -                | 169,806          |
| Other payables                   | 487,232          | 379,238          |
| Advances from customers          | 21,341           | 51,398           |
| Accrued severance benefits       | 512,685          | 411,465          |
| Bad debt                         | 207,501          | 6,609            |
| Other                            | 113,492          | 121,679          |
| <b>Total deferred tax assets</b> | <b>1,725,947</b> | <b>1,497,853</b> |

**Deferred tax liabilities**

|  | <b>2010</b>      | <b>2009</b>      |
|--|------------------|------------------|
| Accounts receivable                      | 960,589          | 774,248          |
| Other current assets                     | 9,560            | 9,265            |
| Deposit for severance benefits insurance | 332,522          | 257,163          |
| Other                                    | 587,872          | -                |
| <b>Total deferred tax liabilities</b>    | <b>1,890,543</b> | <b>1,040,676</b> |

**Reported as:**

|  | <b>2010</b>      | <b>2009</b>    |
|--|------------------|----------------|
| Current deferred tax assets                        | -                | 175,164        |
| Non-current deferred tax assets                    | -                | 282,013        |
| Current deferred tax liabilities                   | 12,060           | -              |
| Non-current deferred tax liabilities               | 152,536          | -              |
| <b>Net deferred income tax assets(liabilities)</b> | <b>(164,596)</b> | <b>457,177</b> |

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**KSNET, Inc.****Notes to the Unaudited Financial Statements****For the six months ended June 30, 2010 and 2009**

(All amounts stated in thousands of Korean won, unless otherwise stated)

**15. INCOME TAXES (continued)****Uncertain tax positions**

On January 1, 2009, the Company adopted the provisions of ASC 740 which set out a consistent framework to determine the appropriate level of tax reserve for uncertain tax positions. ASC Subtopic 740-10 originally was effective for fiscal years beginning after December 15, 2006. The FASB issued ASC Subtopic 740-10 (FSP FIN 48-3, Effective date of FASB Interpretation No. 48 for Certain Nonpublic Enterprises), which deferred the effective date of ASC Subtopic 740-10 for nonpublic entities that had not already issued a complete set of annual financial statements fully reflecting ASC Subtopic 740-10's requirements or are consolidated entities of public entities that report in US GAAP. This means that ASC Subtopic 740-10 was required for such entities with fiscal years beginning after December 15, 2008 and accordingly, the Company adopted the provisions in 2009.

The following table is a reconciliation of the beginning and ending amount of the Company's gross unrecognized tax benefits for the six-month periods ended June 30, 2010 and 2009:

|   | <b>2010</b> |
|---|-------------|
| Beginning balance   | 963,778     |
| Gross increases/(decreases) tax positions in prior period | -           |
| Gross increases/(decreases) current period tax positions  | 72,972      |
| Settlements   | -           |
| Lapse of statute of limitations                           | -           |
| Ending balance  | 1,036,750   |
|   | <b>2009</b> |
| Beginning balance   | 154,210     |
| Gross increases/(decreases) tax positions in prior period | -           |
| Gross increases/(decreases) current period tax positions  | (6,075)     |
| Settlements   | -           |
| Lapse of statute of limitations                           | -           |
| Ending balance  | 148,135     |

Upon adoption at January 1, 2009, the Company's decreased retained earnings by 154,210 thousand. For the six-month periods ended June 30, 2009, the unrecognized tax benefit decreased by 6,075 thousand which all related to permanent differences. As of June 30, 2009, the Company's total unrecognized tax benefits that, if recognized, would affect the effective tax rate is 148,135 thousand. During the six-month periods ended June 30, 2009, the Company recognized approximately 82 thousand for the payment of interest and penalty. The Company had approximately 11,544 thousand and 5,661 thousand for the payment of interest and penalties accrued in the balance sheet as of June 30, 2009.

For the six-month periods ended June 30, 2010, the unrecognized tax benefit increased by 72,972 thousand which all related to permanent differences. As of June 30, 2010, the Company's total unrecognized tax benefits that, if recognized, would affect the effective tax rate is 1,036,750 thousand. During the six-month periods ended June 30, 2010, the Company recognized approximately 3,687 thousand for the payment of interest and penalty. The Company had approximately 18,090 thousand and 39,827 thousand for the payment of interest and penalties accrued in the balance sheet as of June 30, 2010.

The Company files income tax returns in the Republic of Korea. In 2007, the Korea National Tax Service, or NTS, has effectively completed the examination of the Company's returns in the Republic of Korea related to years 2002 through 2006.

It is expected that the amount of unrecognized tax benefits will also change for other reasons in the next 12 months; however, the Company does not expect the change to have a significant impact on our financial position or results of operations

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**KSNET, Inc.****Notes to the Unaudited Financial Statements****For the six months ended June 30, 2010 and 2009****(All amounts stated in thousands of Korean won, unless otherwise stated)****16. EARNINGS PER SHARE**

Basic earnings per share of common stock is computed by dividing net income by the weighted average number of shares of common stock outstanding for the period, less the weighted average number of shares subject to stock retirement.

The following details the computation of earnings per share of common stock for six months ended June 30, 2010 and 2009:

|  | <b>2010</b> | <b>2009</b> |
|--|-------------|-------------|
| Net income   | 8,507,918   | 6,321,908   |
| Weighted average shares used in computing basic earnings per share | 13,800,153  | 14,044,802  |
| <b>Basic earnings per share</b>                                    | <b>617</b>  | <b>450</b>  |

**17. COMMITMENTS AND CONTINGENCIES**

The Company is involved in a total of four litigations that have arisen in the ordinary course of business, including matters involving price fixing. The results and timing of the ultimate resolutions of these proceedings are inherently unpredictable. The outcome of any claim, suit, assessment, investigation, or legal proceeding, individually or collectively will depend on a number of variables, including the nature, timing, and amount of any associated expenses, amounts paid in settlement, damages or other remedies or consequences. As of June 30, 2010, the Company did not accrue liabilities with respect to the pending litigations. The Company will accrue a liability when it believes that it is both probable that a liability has been incurred and that it can reasonably estimate the amount of the loss.

As of June 30, 2010, the Company has guarantees provided by non-related party for the Company as follows:

| Providing by                        | Amount     | Description   |
|-------------------------------------|------------|---|
| Seoul Guarantee Insurance Co., Ltd. | 10,456,000 | Payment guarantee provided by the insurance company |

**18. PLEDGED ASSETS**

Details of assets pledged by the Company as collateral for operating activities as of June 30, 2010 are as follows

| Pledged to               | Pledged assets                   | Pledged amount |
|--------------------------|----------------------------------|----------------|
| Kookmin Bank             | Short-term financial instruments | 1,079,364      |
| Industrial Bank of Korea | Short-term financial instruments | 100,000        |
| Shinhan Bank             | Long-term financial instruments  | 194,000        |
|                          |                                  | 1,373,364      |



**KSNET, Inc.****Notes to the Unaudited Financial Statements****For the six months ended June 30, 2010 and 2009**

(All amounts stated in thousands of Korean won, unless otherwise stated)

**19. SUPPLEMENTAL CASH FLOWS INFORMATION**

Supplemental cash flows information for the periods ended June 30, 2010 and 2009 is as follows:

|                               | 2010      | 2009      |
|-------------------------------|-----------|-----------|
| Cash paid during the year for |           |           |
| Interest                      | 255,509   | 267,960   |
| Income taxes                  | 2,184,689 | 1,118,759 |
|                               | 2,440,198 | 1,386,719 |

**20. RELATED PARTY TRANSACTIONS**

Significant transactions which occurred in the normal course of business with related companies as of June 30, 2010 and 2009 are as follows:

| Relationship | Name                 | Transaction          | 2010    | 2009    |
|--------------|----------------------|----------------------|---------|---------|
| Other        | Kooryoonsoft Co. Ltd | Sales and others     | 15,336  | 38,540  |
|              |                      | Purchases and others | 242,965 | 202,207 |

Account balances with related companies as of June 30, 2010 and 2009 are as follows:

| Relationship | Name                 | 2010        |          | 2009        |          |
|--------------|----------------------|-------------|----------|-------------|----------|
|              |                      | Receivables | Payables | Receivables | Payables |
| Other        | Kooryoonsoft Co. Ltd | 21,191      | -        | 106,065     | 22,677   |

**21. CONCENTRATIONS OF CREDIT RISKS**

Financial instruments that potentially expose the Company to concentrations of credit risk consist primarily of cash, cash equivalents, restricted deposits, and accounts receivable. Substantially all of the Company's cash, cash equivalents, and short-term and long-term financial instruments are held at financial institutions that management believes to be of high credit quality.

A substantial portion of the Company's sales for six months ended June 30, 2010 and 2009 were made to credit card companies. Sales and accounts receivable from customers accounting for 10% or more of the Company's sales are as follows:

| Major Customers            | Sales for the period ended | Accounts receivable as of |
|----------------------------|----------------------------|---------------------------|
|                            | June 30, 2010              | June 30, 2010             |
| BC Card                    | 10,811,047                 | 1,995,160                 |
| NTS (National Tax Service) | 4,053,506                  | 2,371,165                 |
| Shinhan Card               | 8,792,240                  | 1,611,020                 |
| Kookmin Card               | 7,009,895                  | 1,261,050                 |

|            |           |
|------------|-----------|
| 30,666,688 | 7,238,395 |
|------------|-----------|

| <b>Major Customers</b>     | <b>Sales for the period<br/>ended<br/>June 30, 2009</b> | <b>Accounts receivable as<br/>of<br/>June 30, 2009</b> |
|----------------------------|---|--|
| BC Card                    | 10,275,047  | 2,353,548  |
| NTS (National Tax Service) | 2,462,656   | 1,448,175  |
| Shinhan Card               | 6,733,393   | 1,250,688  |
| Kookmin Card               | 5,919,433   | 1,064,968  |
|                            | 25,390,529  | 6,117,379  |

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**KSNET, Inc.**

**Notes to the Unaudited Financial Statements**

**For the six months ended June 30, 2010 and 2009**

**(All amounts stated in thousands of Korean won, unless otherwise stated)**

**22. SUBSEQUENT EVENTS**

On September 16, 2010, Net 1 UEPS Technologies, Inc. announced that it had agreed to purchase 98.73% of the outstanding share capital of the Company for 270 billion in cash, subject to a post-closing working capital adjustment. The acquisition closed on October 29, 2010 and the acquisition was made by Net 1 Applied Technologies Korea, an indirect wholly-owned subsidiary of Net 1 UEPS Technologies, Inc.

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**NET 1 UEPS TECHNOLOGIES, INC.**

**UNAUDITED PRO FORMA COMBINED FINANCIAL STATEMENTS**

**Overview**

The following unaudited pro forma combined financial statements have been prepared to give effect to the Acquisition. We have prepared these unaudited pro forma combined financial statements based on (a) our historical audited consolidated financial statements as of and for the year ended June 30, 2010 and (b) financial information for KSNET as of the same date and for the same period which has been derived as described below. The unaudited pro forma combined financial statements present the pro forma financial position and results of operations of the combined company based on the historical financial information and after giving effect to the Acquisition and certain adjustments which we believe to be factually supportable as described in the notes to the unaudited pro forma combined financial statements.

We have presented an unaudited pro forma combined balance sheet which combines the historical balance sheets of Net1 and KSNET, each as of June 30, 2010, as if the Acquisition had occurred on that date. We have presented an unaudited combined pro forma statement of operations of Net1 and KSNET which combines the historical statements of operations of Net1 for the year ended June 30, 2010, and financial information for KSNET for the same period, as if the Acquisition had occurred on July 1, 2009.

Our fiscal year ends on June 30 and KSNET's fiscal year ends on December 31. SEC rules require us to prepare the pro forma statement of operations by using our fiscal year end and bring KSNET's statement of operations up to within 93 days of our fiscal year end. Thus, we have prepared the pro forma combined statement of operations to coincide with our fiscal year end as follows:

We used KSNET's statement of operations for the year ended December 31, 2009, added the first six months of KSNET's 2010 fiscal year (i.e. the six months ended June 30, 2010) and deducted the comparable period of KSNET's 2009 fiscal year (i.e., the six months ended June 30, 2009).

The financial information of KSNET which has been derived as described above for the year ended June 30, 2010, was prepared in accordance with US GAAP, is unaudited, and is denominated in Korean Won ( KRW ). An exchange rate of \$1/KRW1,217.73 has been used to translate KSNET's historical balance sheet as of June 30, 2010, from KRW to U.S. dollars, based on the closing exchange rate as of June 30, 2010, as reported by an independent external source (www.oanda.com) ( Oanda ). An exchange rate of \$1/KRW1,183.33 has been used to translate KSNET's results of operations for the year ended June 30, 2010, from KRW to U.S. dollars, based on the average daily exchange rate for the year ended June 30, 2010, as reported by Oanda.

The Acquisition has been recorded using the purchase method of accounting. Under the purchase method of accounting, the aggregate consideration paid is allocated to the tangible and identifiable intangible assets acquired and liabilities assumed on the basis of their fair values on the transaction date. Any purchase price in excess of net assets acquired is recorded as goodwill. These unaudited pro forma combined financial statements have been prepared based on preliminary estimates of fair values. The actual amounts and the allocation between net tangible and intangible assets ultimately recorded may differ materially from the information presented in these unaudited pro forma combined financial statements, including property, plant and equipment, identifiable intangible assets and residual goodwill. The preliminary estimates of the fair values of the assets acquired and liabilities assumed reflected herein are subject to change based upon completion of the valuation of the assets acquired and liabilities assumed as of the closing date.

No account has been taken within these unaudited pro forma combined financial statements of any future changes in accounting policies or any synergies (including cost savings), all of which may or may not occur as a result

of the Acquisition. In addition, the impact of ongoing integration activities and other changes in KSNET's assets and liabilities could cause material differences in the information presented.

These unaudited pro forma combined financial statements are not necessarily indicative of the consolidated results of operations or financial position of the combined company that would have been reported had the Acquisition been completed as of the dates presented, and are not necessarily representative of future consolidated results of operations or financial condition of the combined company.

You should read these unaudited pro forma combined financial statements in conjunction with the historical audited consolidated financial statements and accompanying notes of KSNET included in Item 9.01(a) of this Form 8-K/A and our audited consolidated financial statements included in our Annual Report on Form 10-K. Certain KSNET balances have been reclassified to conform to the balance sheet and statement of operations presentation of Net1.

**UNAUDITED PRO FORMA COMBINED BALANCE SHEET**  
**(in thousands, except per share data or unless otherwise indicated)**  
**As of June 30, 2010**

|   | Net1           | KSNET         | KSNET         | Pro forma      | Notes | Pro forma      |
|---|----------------|---------------|---------------|----------------|-------|----------------|
|   | (USD<br>000)   | (KRW<br>M)    | (USD<br>000)  | adjustments    |       | (USD<br>000)   |
| <b>ASSETS</b>   |                |               |               |                |       |                |
| Current assets  |                |               |               |                |       |                |
| Cash and cash equivalents                               | 153,742        | 8,899         | 7,308         | (116,610)      | 3(a)  | 44,440         |
| Pre-funded social welfare grants receivable             | 6,660          | -             | -             |                |       | 6,660          |
| Accounts receivable, net                                | 41,854         | 27,637        | 22,695        |                |       | 64,549         |
| Finance loans receivable, net                           | 4,221          | -             | -             |                |       | 4,221          |
| Inventory   | 3,622          | 1,381         | 1,134         |                |       | 4,756          |
| Deferred income taxes                                   | 16,330         | -             | -             |                |       | 16,330         |
| Other current assets                                    | -              | 3,199         | 2,627         |                |       | 2,627          |
| Total current assets before settlement assets           | 226,429        | 41,116        | 33,764        | (116,610)      |       | 143,583        |
| Settlement assets                                       | 83,661         | 11,118        | 9,130         |                |       | 92,791         |
| Total current assets                                    | 310,090        | 52,234        | 42,894        | (116,610)      |       | 236,374        |
| Long term receivable,                                   | 7,423          | 100           | 82            |                |       | 7,505          |
| Property, plant and equipment, net                      | 7,286          | 26,114        | 21,445        |                |       | 28,731         |
| Equity-accounted investments                            | 2,598          | -             | -             |                |       | 2,598          |
| Goodwill  | 76,346         | -             | -             | 92,800         | 3(b)  | 169,146        |
| Intangible assets, net                                  | 68,347         | 20            | 16            | 117,691        | 3(c)  | 186,054        |
| Other long-term assets                                  | -              | 7,089         | 5,821         |                |       | 5,821          |
| <b>TOTAL ASSETS</b>                                     | <b>472,090</b> | <b>85,557</b> | <b>70,258</b> | <b>93,881</b>  |       | <b>636,229</b> |
| <b>LIABILITIES</b>                                      |                |               |               |                |       |                |
| Current liabilities                                     |                |               |               |                |       |                |
|   |                |               |               | 5,393          | 3(d)  |                |
| Trade payables  | 3,596          | 6,155         | 5,054         | 2,855          | 3(e)  | 16,898         |
| Other payables  | 50,855         | 5,369         | 4,409         | 592            | 3(f)  | 55,856         |
| Short-term borrowings                                   | -              | 2,000         | 1,642         |                |       | 1,642          |
| Current portion of long-term debt                       | -              | 6,000         | 4,927         | 6,672          | 3(g)  | 11,599         |
| Income taxes payable                                    | 3,476          | 1,622         | 1,332         |                |       | 4,808          |
| Total current liabilities before settlement obligations | 57,927         | 21,146        | 17,364        | 15,512         |       | 90,803         |
| Settlement obligations                                  | 83,661         | 11,118        | 9,130         |                |       | 92,791         |
| Total current liabilities                               | 141,588        | 32,264        | 26,494        | 15,512         |       | 183,594        |
| Deferred income taxes                                   | 38,858         | 153           | 125           | 26,494         | 3(c)  | 65,477         |
| Long-term debt  | 4,343          | -             | -             | 100,495        | 3(g)  | 104,838        |
| Accrued severance benefits                              | -              | 1,193         | 980           |                |       | 980            |
| <b>TOTAL LIABILITIES</b>                                | <b>184,789</b> | <b>33,610</b> | <b>27,599</b> | <b>142,501</b> |       | <b>354,889</b> |
| Common stock  | 59             | 6,803         | 5,587         | (5,587)        | 3(h)  | 59             |
| Additional paid-in-capital                              | 133,543        | 34            | 28            | (28)           | 3(h)  | 133,543        |
| Treasury shares   | (173,671)      | -             | -             |                |       | (173,671)      |
| Accumulated other comprehensive income                  | (66,396)       | -             | -             |                |       | (66,396)       |

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|                                     |         |        |        |          |      |         |
|-------------------------------------|---------|--------|--------|----------|------|---------|
|                                     |         |        |        | (5,393)  | 3(d) |         |
|                                     |         |        |        | (2,855)  | 3(e) |         |
|                                     |         |        |        | (592)    | 3(f) |         |
| Retained earnings                   | 392,343 | 45,110 | 37,044 | (37,044) | 3(h) | 383,503 |
| <b>TOTAL NET1 EQUITY</b>            | 285,878 | 51,947 | 42,659 | (51,499) |      | 277,038 |
| Non-controlling interest            | 1,423   | -      | -      | 2,879    |      | 4,302   |
| <b>TOTAL EQUITY</b>                 | 287,301 | 51,947 | 42,659 | (48,620) |      | 281,340 |
| <b>TOTAL LIABILITIES AND EQUITY</b> | 472,090 | 85,557 | 70,258 | 93,881   |      | 636,229 |

See accompanying notes to unaudited pro forma combined financial statements.

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**UNAUDITED PRO FORMA COMBINED STATEMENT OF OPERATIONS****(in thousands, except per share data or unless otherwise indicated)****For the year ended June 30, 2010**

|  | Net1<br>(USD 000) | KSNET<br>(KRW<br>M) | KSNET<br>(USD<br>000) | Pro forma<br>adjustments | Notes | Pro forma<br>(USD 000) |
|--|-------------------|---------------------|-----------------------|--------------------------|-------|------------------------|
| Revenue  | 280,364           | 101,578             | 85,841                |                          |       | 366,205                |
| <b>Expenses</b>  |                   |                     |                       |                          |       |                        |
| Cost of goods sold, IT<br>processing,<br>servicing and support               | 72,973            | 54,437              | 46,003                |                          |       | 118,976                |
|  |                   |                     |                       | 39                       | 3(e)  |                        |
|  |                   |                     |                       | 164                      | 3(f)  |                        |
| General and administration   | 80,854            | 25,902              | 21,889                | 202                      | 3(i)  | 103,148                |
| Depreciation and<br>amortization   | 19,348            | 3,141               | 2,654                 | 12,046                   | 3(c)  | 34,048                 |
| Impairment of goodwill   | 37,378            | -                   | -                     |                          |       | 37,378                 |
| Operating income (loss)  | 69,811            | 18,098              | 15,295                | (12,451)                 |       | 72,655                 |
|  |                   |                     |                       | (7,731)                  | 3(a)  |                        |
| Interest income (expense),<br>net  | 9,069             | 156                 | 132                   | (7,852)                  | 3(e)  | (6,382)                |
| Net income (loss) before<br>income taxes                                     | 78,880            | 18,254              | 15,427                | (28,034)                 |       | 66,273                 |
|  |                   |                     |                       | (2,671)                  | 3(a)  |                        |
|  |                   |                     |                       | (2,915)                  | 3(c)  |                        |
| Income tax expense (benefit)   | 40,822            | 4,176               | 3,529                 | 40                       | 3(f)  | 38,805                 |
| Net income (loss) before<br>earnings from<br>equity-accounted<br>investments | 38,058            | 14,078              | 11,898                | (22,488)                 |       | 27,468                 |
| Earnings from<br>equity-accounted<br>investments                             | 93                | -                   | -                     |                          |       | 93                     |
| Net income (loss)  | 38,151            | 14,078              | 11,898                | (22,488)                 |       | 27,561                 |
| Add: Net loss attributable to<br>non-controlling interest                    | (839)             | -                   | -                     |                          |       | (839)                  |
| Net income (loss)<br>attributable to Net1                                    | 38,990            | 14,078              | 11,898                | (22,488)                 |       | 28,400                 |



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|                         |      |  |      |
|-------------------------|------|--|------|
| Earnings per share:     |      |  |      |
| <i>Basic earnings</i>   | 0.84 |  | 0.61 |
| <i>Diluted earnings</i> | 0.84 |  | 0.61 |

|  |            |  |        |      |            |
|--|------------|--|--------|------|------------|
| Weighted-average number of outstanding shares of common stock used to calculate basic earnings per share | 46,244,609 |  | 60,000 | 3(i) | 46,304,609 |
|--|------------|--|--------|------|------------|

|  |            |  |        |      |            |
|--|------------|--|--------|------|------------|
| Weighted-average number of outstanding shares of common stock used to calculate diluted earnings per share | 46,434,608 |  | 60,000 | 3(i) | 46,494,608 |
|--|------------|--|--------|------|------------|

See accompanying notes to unaudited pro forma combined financial statements.

## NET 1 UEPS TECHNOLOGIES, INC.

## NOTES TO UNAUDITED PRO FORMA COMBINED FINANCIAL STATEMENTS

**1. Basis of presentation**

The accompanying unaudited pro forma combined financial statements present the pro forma financial position and results of operations of the combined company based on the historical financial information and after giving effect to the Acquisition and certain adjustments which we believe to be factually supportable, which are described in these notes. The Acquisition has been recorded using the purchase method of accounting, with Net1 as the acquirer. Please refer to *Overview* for further discussion of the basis of presentation of these unaudited pro forma combined financial statements.

Certain KSNET balances have been reclassified to conform to the balance sheet and statement of operations presentation of Net1 as described in Note 3(j).

**2. Acquisition of KSNET**

The following table sets forth the components of the purchase price for the Acquisition (using exchange rates applicable as of June 30, 2010 for cash paid at closing):

|   | <b>USD 000</b> |
|---|----------------|
| Cash paid at closing to former KSNET shareholders                                       | 221,724        |
| Cash payable to former KSNET shareholders resulting from the working capital adjustment | 2,053          |
| Total purchase price  | 223,777        |

The following table sets forth the preliminary allocation of the purchase price:

|  | <b>USD 000</b> |
|--|----------------|
| Cash and cash equivalents  | 7,308          |
| Accounts receivable, net   | 22,695         |
| Inventory  | 1,134          |
| Other current assets   | 2,627          |
| Settlement assets  | 9,130          |
| Long term receivable,  | 82             |
| Property, plant and equipment, net   | 21,445         |
| Goodwill   | 92,800         |
| Intangible assets, net   | 117,708        |
| Other long-term assets   | 5,821          |
| Trade payables   | (5,054)        |
| Other payables   | (4,409)        |
| Short-term borrowings  | (1,642)        |
| Current portion of long-term borrowings                                    | (4,927)        |
| Income taxes payable   | (1,332)        |
| Settlement obligations   | (9,130)        |
| Deferred income taxes - long-term liabilities                              | (26,620)       |
| Accrued severance benefits   | (980)          |
| Total net assets of KSNET attributable to shareholders, including goodwill | 226,656        |
| Less attributable to non-controlling interest                              | (2,879)        |
| Total purchase price   | 223,777        |



The preliminary purchase price allocation is based on management estimates as of January 12, 2011, and may be adjusted up to one year following the closing of the Acquisition. The purchase price allocation has not been finalized, as management has not yet analyzed in detail the assets acquired and liabilities assumed. We expect to finalize the purchase price allocation on or before June 30, 2011. The actual amounts and the allocation between net tangible and intangible assets ultimately recorded may differ materially from the information presented in these unaudited pro forma combined financial statements, including property, plant and equipment, identifiable intangible assets and residual goodwill.

### 3. Pro forma adjustments

The following are descriptions of each of the pro forma adjustments included in the unaudited pro forma combined financial statements:

(a) Reduction in cash and cash equivalents and interest income

Represents the estimated reduction in interest income of \$7.7 million on Net1's cash reserves of \$116.6 million for the year ended June 30, 2010, which was used to fund the a portion of the Acquisition at an assumed pre-tax South African interest rate of 6.63% . The tax effect of \$2.7 million related to this adjustment is included on the income tax expense line in the unaudited pro forma combined statement of operations.

(b) Goodwill

Represents the excess of the purchase price over the fair value of net assets acquired of \$133.8 million as presented within the preliminary purchase price allocation in Note 2 above.

(c) Acquired intangible assets and amortization expense

Represents the portion of the purchase price allocated to KSNET's intangible assets acquired, at estimated fair values based on management's estimates. As of June 30, 2010, these assets had a carrying value on KSNET's balance sheet of approximately \$1 million. As noted above, this identification and estimation of fair value is provisional and may change when the final purchase price allocation is made. Since the tax basis of these identifiable intangible assets is less than their accounting basis, the purchase price allocated to these assets results in additional deferred tax liabilities.

|  | Fair value<br>(KRW<br>million) | Fair value<br>(USD 000) | Estimated<br>useful life<br>(in years) | Annual<br>amortization<br>expense (1)<br>(USD 000) | Annual<br>tax effect<br>(USD 000) |
|--|--------------------------------|-------------------------|--|--|-----------------------------------|
| <b><i>Finite lived intangibles</i></b> |                                |                         |  |  |                                   |
| <b><i>assets</i></b>                   |                                |                         |  |  |                                   |
| Customer relationships                 | 106,624                        | 87,560                  | 15                                     | 5,837  | 1,413                             |
| Software                               | 33,032                         | 27,126                  | 5                                      | 5,425  | 1,313                             |
| Trade names                            | 4,860                          | 3,991                   | 20                                     | 443  | 107                               |
|  | 144,516                        | 118,677                 |  | 11,705   | 2,833                             |
| <b><i>Deferred tax liabilities</i></b> |                                |                         |  |  |                                   |
| Customer relationships                 | 23,692                         | 19,456                  |  |  |                                   |
| Software                               | 7,484                          | 6,146                   |  |  |                                   |
| Trade names                            | 1,087                          | 892                     |  |  |                                   |
|  | 32,263                         | 26,494                  |  |  |                                   |

- (1) Using the average exchange rate for the year ended June 30, 2010, the total annual amortization expense related to these intangible assets was \$12.0 million. The deferred tax effect of \$2.9 million related to this

adjustment is included on the income tax expense line in the unaudited pro forma combined statement of operations.

(d) Transaction costs incurred subsequent to June 30, 2010

Represents the Company's estimate of the expected KSNET acquisition costs of \$5.4 million owing to external professional advisors for services provided which are not reflected in Net1's June 30, 2010 consolidated balance sheet. These costs have been accrued as a current liability. We do not expect to deduct these expenses for tax purposes. Because we are required to expense these costs as they are incurred, we have charged them to retained earnings as of June 30, 2010. No adjustment has been made to the unaudited pro forma combined statement of operations for these costs as they are non-recurring.

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(e) Upfront fees, deferred financing costs and interest expense

On signing the Facilities Agreement, upfront fees and deferred financing costs of KRW 3.5 billion (equivalent of \$2.9 million) at the USD/ KRW exchange rate on June 30, 2010, were paid. Accordingly, an amount of \$2.9 million is included in accounts payable as of June 30, 2010.

Represents interest of \$7.5 million under the Facilities Agreement for the year ended June 30, 2010, using the Korea CD rate of 2.66% plus the margin of 4.10% . Amount also includes \$0.4 million which represents twelve months of amortization of the total deferred financing costs, or KRW 1.7 billion (equivalent of \$1.3 million) at the USD/ KRW exchange rate on July 1, 2009, on signing the Facilities Agreement.

A change of 1/8<sup>th</sup> of a percentage point in the CD rate results in a change of KRW 0.2 billion (equivalent of \$0.1 million) in the interest expense.

(f) Salary and cash incentive compensation

Represents the effect of the increase in the salary and cash incentive compensation of a member of KSNET 's management. We agreed to these compensation arrangements as a condition to the closing of the Acquisition, which became effective on closing and remain fixed until June 30, 2013. The expected incremental difference between the compensation expense included in KSNET 's historical statement of operations and the new compensation arrangements are reflected in the combined pro forma combined statement of operations.

(g) Long-term debt and current portion of long-term debt

Represents a loan in the principal amount of KRW 130.5 Billion, or \$107.2 million, translated at exchange rates prevailing on June 30, 2010, under the senior facilities agreement ( Facilities Agreement ) used to fund a portion of the Acquisition. Under the Facilities Agreement, \$6.7 million of the total \$107.2 million facility is repayable one year after the initial draw down of the facility. As a result, we have included this amount within current liabilities and the remainder in long-term debt in the unaudited pro forma combined balance sheet.

(h) Elimination of KSNET shareholders ' equity

Represents the elimination of KSNET 's common stock of \$5.6 million, additional paid in capital of \$0.03 million and retained earnings of \$37.0 million, acquired by Net1.

(i) Stock-based compensation

Represents the annual stock-based compensation charge of \$0.2 million related to 60,000 restricted shares of Net1 's common stock awarded to a member of KSNET 's management. The restricted stock vests on June 30, 2014, unless the recipient fails to receive a conditional incremental bonus for each of the fiscal years ended June 30, 2011, 2012, 2013 and 2014, in which event the restricted stock shall not vest. We have assumed that all 60,000 shares of restricted stock will vest on June 30, 2014. The restricted stock has been valued using the closing price, or \$12.33, of our common stock on October 29, 2010, the acquisition date, and the effective date of the restricted stock award agreement. We do not expect to deduct this stock-based compensation charge for tax purposes.

(j) Reclassifications

Certain balances have been reclassified from the financial statements of KSNET so their presentation would be consistent with Net1.

The following reclassifications have been made to the balance sheet as of June 30, 2010 (in millions):



KRW

***Cash and cash equivalents***

## KSNET:

|  |              |
|--|--------------|
| Cash and cash equivalents  | 20,017       |
| Reclassified to settlement assets                                    | (11,118)     |
| <b><i>KSNET cash and cash equivalents after reclassification</i></b> | <b>8,899</b> |

***Accounts receivable, net***

## KSNET:

|   |               |
|---|---------------|
| Accounts receivable, net  | 11,111        |
| Other current assets  | 16,526        |
| <b><i>KSNET accounts receivable, net after reclassification</i></b> | <b>27,637</b> |

***Other long-term assets, net***

## KSNET:

|  |              |
|--|--------------|
| Other long-term assets   | 5,583        |
| Non-current accounts receivable, net                                   | 1,506        |
| <b><i>KSNET other loan-term assets, net after reclassification</i></b> | <b>7,089</b> |

***Other current liabilities***

## KSNET:

|  |              |
|--|--------------|
| Other current liabilities  | 17,061       |
| Deferred tax liabilities   | 12           |
| Other non-current liabilities  | 1,036        |
| Reclassified to settlement obligations                               | (11,118)     |
| Reclassified to income taxes payable                                 | (1,622)      |
| <b><i>KSNET other current liabilities after reclassification</i></b> | <b>5,369</b> |

No significant reclassifications were made to the statement of operations for the year ended June 30, 2010.



**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

**NET 1 UEPS TECHNOLOGIES, INC.**

Date: January 12, 2011

By: /s/ Serge Belamant  
Dr. Serge C.P. Belamant  
Chief Executive Officer

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