FREESTONE RESOURCES, INC.
Form 10-Q
February 14, 2012

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

**Washington, D.C. 20549**

**FORM 10-Q**

(Mark One)

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

For the quarterly period ended December 31, 2011

**OR**

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

Commission File Number 000-28753

**FREESTONE RESOURCES, INC.**

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

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

Republic Center, Suite 1350

325 N. St. Paul Street Dallas, TX 75201

(Address of principal executive offices)

(214) 880-4870

(Issuer's telephone number)

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

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

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

Large Accredited Filer [ ] Accelerated Filer [ ]
Non-Accredited Filer [ ] Smaller Reporting Company [X]

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

As of February 12, 2012 there were 53,630,677 shares of Common Stock of the issuer outstanding.

1

**Freestone Resources, Inc.**

**(A Development Stage Company)**

**Consolidated Balance Sheets**

**As of December 31, 2011 and June 30, 2011**

Assets

| | (Unaudited) December 31, 2011 | (Audited) June 30, 2011 |
|---|---|---|
| Current Assets: | | |
| Cash | $57,815 | $93,015 |
| Accounts receivable | — | 2,153 |
| Deposits and other assets | — | — |
| Total Current Assets | 57,815 | 95,168 |
| | | |
| Oil and gas properties used for research and development | 26,000 | 26,000 |
| Fixed assets, net of accumulated depreciation of $25,536 and $15,032 | 42,016 | 52,520 |
| Total fixed assets, net | 68,016 | 78,520 |
| | | |
| Other assets | 3,687 | 3,087 |
| | | |
| Total Assets | $129,518 | $176,775 |

Liabilities and Stockholders' Equity

| | | |
|---|---|---|
| Current Liabilities: | | |
| Accounts payable | $17,668 | $23,047 |
| Accounts payable-related party | — | — |
| Accrued expenses | 6,908 | 8,237 |
| Notes payable-related parties | 18,218 | 21,461 |
| Stock to be issued | 84,100 | — |
| Total Current Liabilities | 126,894 | 52,745 |
| | | |
| Long-term Liabilities: | | |
| Asset retirement obligations | 24,917 | 24,917 |
| Total Liabilities | 151,811 | 77,662 |

| | | |
|---|---|---|
| Stockholders' Equity (Deficit): | | |
| Common stock, $.001 par value, 100,000,000 shares authorized, 52,612,760 and 52,512,760 shares issued and outstanding, respectively | 52,613 | 52,513 |
| Additional paid in capital | 16,553,616 | 16,538,716 |
| Accumulated deficit | (16,628,522) | (16,492,116) |
| Stockholders' Equity (Deficit) | (22,293) | 99,113 |
| Total Liabilities and Stockholders' Equity | $129,518 | $176,775 |

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

2

**Freestone Resources, Inc.**

**(A Development Stage Company)**

**Consolidated Statements of Operations**

**For the Three and Six Months Ended December 31, 2011 and 2010**

**And for the Period Since Reentering the Development Stage (July 1, 2010 to December 31, 2011)**

**(unaudited)**

| | Three Months Ended December 31, 2011 | Three Months Ended December 31, 2010 | Six Months Ended December 31, 2011 | Six Months Ended December 31, 2010 | Since Reentering Developing Stage (July 1, 2010 to December 31, 2011 |
|---|---|---|---|---|---|
| Revenue: | | | | | |
| Oil and gas revenues resulting from research activities | $161 | $9,235 | $4,918 | $18,408 | $45,782 |
| Total revenue resulting from research activities | 161 | 9,235 | 4,918 | 18,408 | 45,782 |
| Operating expenses: | | | | | |
| Lease operating costs | 5,839 | 8,127 | 8,539 | 18,151 | 35,267 |
| Depreciation | 5,252 | 370 | 10,504 | 741 | 21,750 |
| Impairment expense | 0 | 0 | 0 | 0 | 954,000 |
| General and administrative | 46,980 | 60,442 | 122,281 | 165,901 | 446,917 |
| Total operating expenses | 58,071 | 68,939 | 141,324 | 184,793 | 1,457,934 |
| Operating loss | (57,910) | (59,704) | (136,406) | (166,385) | (1,412,152) |
| Other income (expense): | | | | | |
| Interest income (expense) | 0 | 232 | 0 | (343) | (2,179) |
| Gain on sale of investment asset | 0 | 17,276 | 0 | 17,276 | 17,276 |
| Other income related to the settlement of EOS litigation | 0 | 0 | 0 | 0 | 1,665,834 |
| Revision to ARO estimate | 0 | 0 | 0 | 0 | 16,206 |
| Total other income (expense) | 0 | 17,508 | 0 | 16,933 | 1,697,137 |

| | | | | | |
|---|---|---|---|---|---|
| Net loss | $(57,910 ) | $(42,196 ) | $(136,406 ) | $(149,452 ) | $284,985 |
| Basic and diluted loss per share | $0.00 | $0.00 | $0.00 | $0.00 | |
| Weighted average shares outstanding: | | | | | |
| Basic and diluted | 52,598,629 | 72,618,994 | 52,555,695 | 72,442,907 | |

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

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**Freestone Resources, Inc.**

**(A Development Stage Company)**

**Consolidated Statement of Stockholders' Equity**

**For the Period Since Reentering the Development Stage (July 1, 2010 to September 30, 2011)**

**And the Six Months Ended December 31, 2011**

**(Unaudited)**

| | Common Stock Shares | Additional Amount | Accumulated Paid in Capital | Deficit | Total |
|---|---|---|---|---|---|
| Balance, June 30, 2010 | 71,718,994 | $71,719 | $16,299,789 | $(16,913,507) | $(541,999) |
| Common stock issued for cash | 3,712,500 | 3,713 | 440,787 | — | 444,500 |
| Common stock issued for Demo equipment | 100,000 | 100 | 58,485 | — | 58,585 |
| Common stock issued for services | 5,300,000 | 5,300 | 948,700 | — | 954,000 |
| Common stock issued for warrants | 500,000 | 500 | 23,500 | — | 24,000 |
| Common stock returned for EOS acquisition | (28,818,734) | (28,819) | (1,232,545) | — | (1,261,364) |
| Net loss | — | — | — | 421,391 | 421,391 |
| Balance, June 30, 2011 | 52,512,760 | $52,513 | $16,538,716 | $(16,492,116) | $99,113 |
| Common stock issued for cash | 100,000 | 100 | 14,900 | | 15,000 |
| Net loss | | | | (136,406) | (136,406) |
| Balance, December 31, 2011 | 52,612,760 | $52,613 | $16,553,616 | $(16,628,522) | $(22,293) |

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

**Freestone Resources, Inc.**

**(A Development Stage Company)**

**Consolidated Statements of Cash Flows**

**Six Months Ended December 31, 2011 and 2010**

**And for the Period Since Reentering the Development Stage (July 1, 2010 to December 31, 2011)**

**(Unaudited)**

| | Six Months EndedDecember 31, 2011 | Six Months Ended December 31, 2010 | Since Reentering Developing Stage (July 1, 2010 to December 31, 2011 |
|---|---|---|---|
| CASH FLOWS FROM OPERATING ACTIVITIES: | | | |
| Net income (loss) | $(136,406) | $(149,452) | $284,985 |
| Adjustments to reconcile net loss to net cash provided by (used in) operating activities: | | | |
| Depreciation and amortization | 10,504 | 741 | 21,750 |
| Shares issued for demonstration equipment | — | 58,585 | 58,585 |
| (Gain) on sale of investment asset | — | (17,276) | (17,276) |
| Stock based compensation | — | — | 954,000 |
| Decrease in revision of ARO estimate | — | — | (16,206) |
| Shares issued for warrants | — | — | 24,000 |
| Changes in operating assets and liabilities: | | | |
| Write-off in note receivable | — | — | — |
| Change in account receivable | 2,153 | 13,830 | 22,029 |
| Change in inventory of Petrozene | — | — | — |
| Change in other assets | (600) | (300) | (900) |
| Change in accounts payable | (5,379) | 15,849 | (233,101) |
| Change in accounts payable – related party | — | — | (4,322) |
| Change in accrued expenses | (1,329) | 1,879 | (151,339) |
| Net cash provided used in operating activities | (131,057) | (76,144) | 942,205 |

| | | | |
|---|---|---|---|
| CASH FLOWS FROM INVESTING ACTIVITIES: | | | |
| Sale of investment asset | — | 30,000 | 30,000 |
| Purchases of fixed assets | — | (58,585) | (58,585) |
| Net cash used in investing activities | — | (28,585) | (28,585) |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | | |
| Payments on note payable | — | — | — |
| Payments on note payables – related party | (3,243) | (9,763) | (16,103) |
| Proceeds from sale of stock | 15,000 | 200,000 | 459,500 |
| Stock returned upon settlement of litigation | — | — | (1,261,364) |
| Stock to be issued | 84,100 | (85,000) | (65,900) |
| Net cash provided by financing activities | 95,857 | 105,237 | (883,867) |
| NET CHANGE IN CASH | (35,200) | 508 | 29,753 |
| CASH AT BEGINNING OF PERIOD | 93,015 | 28,062 | 28,062 |
| CASH AT END OF PERIOD | $57,815 | 28,570 | $57,815 |
| Supplemental cash flow information: | | | |
| Cash paid for interest | $— | $343 | $242 |
| Non-cash investing activities: | | | |
| Stock returned upon settlement of litigation | $— | $— | $(1,261,364) |

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

**Freestone Resources, Inc.**

**(A Development Stage Company)**

**Notes to Consolidated Financial Statements**

**December 31, 2011**

**(Unaudited)**

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

Nature of Activities, History and Organization:

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

The Company's primary business is the development of new technologies that allow for the utilization of oil and gas resources in an environmentally responsible and cost effective way, as well as the development of technologies that can be used in the environmental cleanup of oil-based contaminant byproducts. In October 2011, the Company entered into a joint venture with MEA Solutions, LLC to deliver a total solution for water resource management in the oilfield services sector. An integral component of the service includes owning and operating water recycling systems. The joint venture, Freestone Water Solutions, LLC, will utilize specialized, proprietary technology designed to treat and recycle flowback water (frac water that immediately flows back to the surface), as well as produced water for subsequent reuse in the fracking process. It is anticipated that Freestone Water will not be consolidated in future reporting, as the Company will own less than 50% of the joint venture and will not have control of the board of directors.

The Company acquired one hundred percent (100%) of the issued and outstanding stock of Earth Oil Services, Inc., a Nevada corporation ("EOS"), in a stock based transaction on September 24, 2009 (the "EOS Agreement"). The Company issued 31,603,734 shares of restricted common stock of the Company in consideration for this transaction. EOS owns certain exclusive, territorial, license agreements to a proprietary technology that is a chemical solvent that can separate, extract and recycle hydrocarbon contaminants from ground soils, tar sands, vessels and other materials. EOS has engaged a fabricator to build a prototype machine (the "Prototype") designed to be used in conjunction with the solvent. EOS is indebted to the fabricator for its development of the Prototype. EOS is now a wholly owned subsidiary of Freestone and all intercompany accounts have been eliminated in consolidation. The Company filed a lawsuit seeking to rescind the EOS Agreement. On June 26, 2011 the Company entered into a Settlement Agreement (the "Settlement Agreement") with Enviro Serv, Shultz, David Feuerborn, an individual residing in Riverside County, California, and Thomas Jennings, an individual residing in Orange County, California (collectively the "Parties"). The Settlement Agreement permanently and irrevocably effectuates a final and binding global settlement and release of the Parties regarding the pending lawsuit between the Parties in the Northern District of Texas, Cause No. 3:10-CV-01349-O. Furthermore, the Settlement Agreement rescinds the Stock Purchase Agreement entered into by and between the Parties on September 24, 2009, and cancels 28,818,734 shares of Freestone's common stock of the 31,603,734 shares of Freestone common stock that was originally issued to Enviro Serv and Shultz, and returns said cancelled stock to the Company's treasury.

Development Stage Company

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

Unaudited Interim Financial Statements:

The accompanying unaudited interim consolidated financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America and the rules of the Securities and Exchange Commission. These financial statements are unaudited and, in the opinion of management, include all adjustments (consisting of normal recurring accruals) necessary to present fairly the balance sheet, statement of operations, statement of stockholders' equity and statement of cash flows for the periods presented in accordance with accounting principles generally accepted in the United States. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted pursuant to SEC rules and regulations. It is presumed that users of this interim financial information have read or have access to the audited financial statements and footnote disclosure for the preceding fiscal year contained in the Company's Annual Report on Form 10-K. The results of operations for the three months ended September 30, 2011 are not necessarily indicative of the results of operations for the full year or any other interim period. The information included in this Form 10-Q should be read in conjunction with Management's Discussion and Analysis and Financial Statements and notes thereto included in the Company's June 30, 2011 Form 10-K.

Significant Accounting Policies:

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

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

Basis of Presentation

The Company prepares its financial statements on the accrual basis of accounting. All intercompany balances and transactions are eliminated. Investments in subsidiaries, where the Company has a controlling interest, are reported using the equity method. For those businesses that the Company does not have a controlling interest, they are accounted through the Noncontrolling Interest method. Management believes that all adjustments necessary for a fair presentation of the results of the six months ended December 31, 2011 and 2010 have been made.

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

Use of Estimates:

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

Recently Issued Accounting Pronouncements:

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

Cash and Cash Equivalents:

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

Revenue Recognition:

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

1. Persuasive evidence of an arrangement exists;

2. Ownership and all risks of loss have been transferred to buyer, which is generally upon shipment;

3. The price is fixed and determinable; and

4. Collectability is reasonably assured.

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

Income Taxes:

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

Earnings per Share:

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

Fair Value Measurements:

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

Accounts Receivable:

Accounts Receivable are carried at their face amount, less an allowance for doubtful accounts. On a periodic basis, the Company evaluates accounts receivable and establishes the allowance for doubtful accounts based on a combination of specific customer circumstances and credit conditions, based on a history of write offs and collections. The Company's policy is generally not to charge interest on trade receivables after the invoice becomes past due. A receivable is considered past due if payments have not been received within agreed upon invoice terms. Write offs are recorded at a time when a customer receivable is deemed uncollectible. The Company had no bad debt accruals at December 31, 2011 and June 30, 2011.

Oil and Gas Properties:

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

Equipment:

Equipment is carried at the cost of acquisition or construction and depreciated over the estimated useful lives of the assets. Costs associated with repair and maintenance are expensed as incurred. Costs associated with improvements which extend the life, increase the capacity or improve the efficiency of our property and equipment are capitalized and depreciated over the remaining life of the related asset. Gains and losses on dispositions of equipment are reflected in operations. Depreciation and amortization are provided using the straight-line method over the estimated useful lives of the assets, which are 3 to 30 years. Oil and gas properties were purchased primarily for product testing and are depreciated over their estimated useful lives of 3 years but not reduced below estimated salvage value.

Impairment of Long Lived Assets

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

Asset Retirement Obligation:

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

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

**NOTE 2 – FIXED ASSETS**

Fixed assets at December 31, 2011 and June 30, 2011 are as follows:

| | December 31, 2011 | June 30, 2011 |
|---|---|---|
| Computers & office furniture | $67,552 | $67,552 |
| Oil and gas research and development equipment | 26,000 | 26,000 |
| Total fixed assets | 93,552 | 93,552 |
| Less: Accumulated depreciation | (25,536) | (15,032) |
| Total fixed assets, net of accumulated depreciation | $68,016 | $78,520 |

Depreciation expense was $10,504 for the six months ended December 31, 2011 and $741 for the six months ended December 31, 2010.

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

On May 26, 2009, the Company received a loan from Mike Doran (“Doran”), the Company’s CEO at that time, in the amount of $25,000. A note payable was formally prepared by the Company but never executed by Doran. The terms of the loan included an interest rate of three and a half percent, and the payment of twelve monthly installments beginning on October 31, 2009. On July 8, 2009, an amended and restated promissory note with similar terms was executed to replace the original note payable, at which time the Company recorded a $6,200 gain on extinguishment of debt. During the year ended June 30, 2009, the Company received an advance from Doran of $20,000 which was repaid during the year. As of December 31, 2011 and June 30, 2011 the balance owed to Mr. Doran was $3,218 and $6,461 respectively.

On July 9, 2009, the Company received an advance from James Carter, a shareholder, in the amount of $25,000. There are no terms on the advance and no interest is paid. At December 31, 2011 and June 30 2011 the balance owed was $15,000.

**NOTE 4 – INCOME TAXES**

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

During the six months ended December 31, 2011 the Company had a net loss of $136,406, increasing the deferred tax asset approximately $46,380 at the statutory tax rate of 34%. Deferred tax assets at December 31, 2011 and June 30, 2011 consisted of the following:

Deferred tax asset related to:

| | December 31, 2011 | June 30, 2011 |
|---|---|---|
| Prior Year | $1,139,687 | $1,282,960 |
| Tax Benefit (Expense) for Current Period | 46,380 | (143,273) |
| Net Operating Loss Carryforward | $1,186,067 | $1,139,687 |
| Less: Valuation Allowance | (1,186,067) | (1,139,687) |
| Net Deferred Tax Asset | $0 | $0 |

The net deferred tax asset generated by the loss carryforward has been fully reserved and will expire in the years 2019 through 2030. The realization of deferred tax benefits is contingent upon future earnings and is fully reserved at December 31, 2011 and June 30, 2011.

**NOTE 5 – ASSET RETIREMENT OBLIGATION**

The Company's asset retirement obligation ("ARO") primarily represents the estimated present value of the amount Freestone Resources will incur to plug, abandon and remediate sits producing properties at the end of their productive lives, in accordance with applicable state laws. Freestone Resources determines the ARO on its oil and gas properties by calculating the present value of estimated cash flows related to the liability. At December 31, 2011, the liability for ARO was $24,917, all of which is considered long term. The asset retirement obligations are recorded as current or non-current liabilities based on the estimated timing of the anticipated cash flows. During 2011, the Company has not recognized accretion expense, as the properties were written down to salvage value as of June 30, 2009.

**NOTE 6 – COMMITMENTS AND CONTINGENCIES**

The Company leases office space under a non-cancelable operating lease that expires in July 2014. The lease requires fixed escalations and payment of electricity costs. Rent expense, included in general and administrative expenses, totaled approximately $11,349 and $6,254 for the six months ended December 31, 2011 and 2010 respectively.

**NOTE 7 – EQUITY TRANSACTIONS**

The Company is authorized to issue 100,000,000 common shares at a par value of $0.001 per share. These shares have full voting rights. At December 31, 2011 and June 30, 2011, there were 52,612,760 and 52,512,760, respectively, common shares outstanding.

In June 2011, the Company issued a warrant to purchase 500,000 shares of common stock to Hydrex Technologies, ("Hydrex") in conjunction with the issuance of a License Agreement to Hydrex. The warrants were exercised on June 9, 2011 for $24,000, which, per the agreement, was 20% of the closing price on the last trading day prior to the exercise. The Company has a similar warrant agreement with Hydrex, in which the warrant is only granted and exercisable upon the completion of commercial-scale Oil Recovery Units within a stated period of time.

On September 29, 2011, the Company sold 100,000 shares to a stockholder at $0.15 per share. These shares were issued on October 28, 2011.

On December 6, 2011, the Company sold 200,000 shares to a stockholder at $.08 per share. The shares had not been issued as of December 31, 2011, and are recorded as $16,000 of "stock to be issued" on the Company's December 31, 2011 balance sheet.

On December 6, 2011, the Company sold 250,000 shares to a stockholder at $.08 per share. The shares had not been issued as of December 31, 2011, and are recorded as $20,000 of "stock to be issued" on the Company's December 31, 2011 balance sheet.

On December 7, 2011, the Company sold 250,000 shares to a stockholder at $.08 per share. The shares had not been issued as of December 31, 2011, and are recorded as $20,000 of “stock to be issued” on the Company’s December 31, 2011 balance sheet.

On December 21, 2011, the Company sold 101,250 shares to a stockholder at $.08 per share. The shares had not been issued as of December 31, 2011, and are recorded as $8,100 of “stock to be issued” on the Company’s December 31, 2011 balance sheet.

On December 6, 2011, the Company sold 50,000 shares to a stockholder at $.10 per share. The shares had not been issued as of December 31, 2011, and are recorded as $5,000 of “stock to be issued” on the Company’s December 31, 2011 balance sheet.

**NOTE 8 – FREESTONE TECHNOLOGIES, LLC**

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

**NOTE 9 – GOING CONCERN**

As reflected in the accompanying consolidated financial statements, Freestone incurred operating losses, and has a negative working capital position as of December 31, 2011. The above factors raise substantial doubt about Freestone's ability to continue as a going concern. Freestone's continued existence is dependent on its ability to obtain additional equity and/or debt financing to fund its operations. Freestone plans to raise additional financing and to increase sales volume. There is no assurance that Freestone will obtain additional financing or achieve profitable operations or cash inflows. The consolidated financial statements do not include any adjustments relating to the recoverability or classification of recorded asset amounts or the amount and classification of liabilities that might be necessary as a result of this uncertainty.

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**NOTE 10 – FAIR VALUE MEASUREMENTS**

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

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

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

Level 2 - Inputs to the valuation methodology include:
- quoted prices for similar assets or liabilities in active markets;
- quoted prices for identical or similar assets or liabilities in inactive markets;
- inputs other than quoted prices that are observable for the asset or liability;
- inputs that are derived principally from or corroborated by observable market data by correlation or other means.

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

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

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

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

The preceding method described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although the Company believes its valuation method is appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date. The following table sets forth by level, within the fair value hierarchy, the Company's liabilities at fair value as of December 31, 2011:

Liabilities at Fair Value as of December 31, 2011

| | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Asset retirement obligations | $ - | $ - | $ 24,917 | $24,917 |

**NOTE 12 – SUBSEQUENT EVENTS**

In accordance with ASC 855-10 an evaluation of subsequent events was performed through February 14, 2012, which is the date the financial statements were issued. No items requiring disclosure were noted.

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS

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

### General

On August 22, 2007, the Company changed its name to Freestone Resources, Inc. in anticipation of going into the oil and gas technology development business. Since that time Freestone began developing and acquiring rights to chemical solvents that can increase the production in oil and gas wells, decrease the viscosity of heavy oil, and extract hydrocarbons from various forms of matter. The Company has developed an Oil Recovery Unit ("ORU") that it has successfully licensed to Hydrex in order to chemically remove oil from oil sands and oil contaminated soils.

In October 2011, the Company entered into a joint venture with MEA Solutions, LLC to deliver a total solution for water resource management in the oilfield services sector. An integral component of the service includes owning and operating water recycling systems. The joint venture, Freestone Water Solutions, LLC, will utilize specialized, proprietary technology designed to treat and recycle flowback water (frac water that immediately flows back to the surface), as well as produced water for subsequent reuse in the fracking process.

**Results of Operations**

**Three and six months Ended December 31, 2011 compared to three and three and six months Ended December 31, 2010**

**Revenue** - Our revenue for the three months ended December 31, 2011 was $161, compared to $9,235 for the same period in 2010, and for the six months ended December 31, 2011 was $4,918 and $18,408 for the same period in 2010. Revenue decreased in the second quarter and six months ended December 31, 2011, due to reduced oil and gas revenue as there was less in-field research and development activity.

**Lease Operating Expense** - Lease operating expense for the three months ended December 31, 2011 was $5,839 compared to $8,127 for the same period in 2010 and $8,539 for the six months ended December 31, 2011 compated to $18,151 for the same period in 2010. The reduction in lease operating expenses is reflected in the reduced sales.

**Operating Expense** - Total operating expenses for the three months ended December 31, 2011 were $5,252 of depreciation expense and $46,980 of general and administrative expenses respectively, compared to $370 depreciation expense and $60,442 of general and administrative expenses for the same period in 2010. The reduced costs ($13,462) in the three months ended December 31, 2011 were related to reduced legal fees of $9,700 and lower royalties of $3,400 due to the reduced sales.

Total operating expenses for the six months ended December 31, 2011 were $10,504 of depreciation expense and $122,281 of general and administrative expenses respectively, compared to $741 depreciation expense and $165,901 of general and administrative expenses for the same period in 2010. The reduced costs ($43,620) in the three months ended December 31, 2011 were related to a consultants fee of $10,000 incurred in 2010, legal fees $18,000 (the lawsuit that was filed in July, 2010), engineering fees of $5,000, reduced royalties (lower sales) of $5,700 and general expenses of $4,000.

**Net Income (Loss)** - Net loss for the three months ended December 31, 2011 was $57,910 compared to net loss of $42,196 for the same period in 2010. Net loss for the six months ended December 31, 2011 was $136,406 compated eto $149,452 for the same period in 2010. The decrease in loss in the three and six month periods ended December 31, 2011 is mainly related to the reduced administrative expenses mentioned above.

**Liquidity and Capital Resources**

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

Net cash used of the Company was $131,057 for the six months ended December 31, 2011 compared to cash used of $76,144 for the same period in 2010. We continue to explore working capital options and in the short-term rely on our line-of-credit and advances/loans from shareholders. During the six months ended December 31, 2010, our cash and cash equivalent increased to $28,570 from $28,062 at June 30, 2010 due to sales of common stock.

**Employees**

As of December 31, 2011, Freestone had two employees.

**Need for Additional Financing**

No commitments to provide additional funds have been made by management or other stockholders. Our independent auditors included a going concern explanatory paragraph in their report included in our annual report on Form 10-K for the year ended June 30, 2011, which raises substantial doubt about our ability to continue as a going concern.

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

Not applicable.

**ITEM 4T: CONTROLS AND PROCEDURES**

**Evaluation of Disclosure Controls and Procedures**

We carried out an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of December 31, 2011. This evaluation was accomplished under the supervision and with the participation of our chief executive officer /principal executive officer, and chief financial officer/principal financial officer who concluded that our disclosure controls and procedures are effective.

Based upon an evaluation conducted for the period ended December 31, 2011, our Chief Executive and Chief Financial Officer as of December 31, 2011 and as of the date of this Report, has concluded that as of the end of the periods covered by this report, we have identified the following material weakness of our internal controls:

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

**Changes in Internal Controls over Financial Reporting**

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

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**PART II**

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

Item 6 - Exhibits and Reports on Form 8-K

(a) During the six months ended December 31, 2011 the Company filed no Form 8-Ks.

(b) Exhibits

Exhibit Number

| | |
|---|---|
| 31.1 | Certification of Chief Executive Officer, pursuant to Rule 13a-14(a) of the Exchange Act, as enacted by Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2 | Certification of Chief Financial Officer, pursuant to Rule 13a-14(a) of the Exchange Act, as enacted by Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32.1 | Certification of Chief Executive Officer and Chief Financial Officer, pursuant to 18 United States Code Section 1350, as enacted by Section 906 of the Sarbanes-Oxley Act of 2002. |

SIGNATURES

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

FREESTONE RESOURCES, INC.

By /s/ Clayton Carter

Clayton Carter, CEO

Date: February 14, 2011

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