FRANKLIN WIRELESS CORP
Form 10-Q
February 16, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

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

For the quarterly period ended December 31, 2015

OR

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

For the transition period from to .

Commission file number: 001-14891

FRANKLIN WIRELESS CORP.

(Exact name of Registrant as specified in its charter)

Nevada	**95-3733534**

(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
9707 Waples Street **Suite 150** **San Diego, California** (Address of principal executive offices)	**92121** (Zip code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

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

Large accelerated filer o   Accelerated filer o   Non-accelerated filer o   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 x No o

The Registrant has 10,403,869 shares of common stock outstanding as of February 16, 2016.

FRANKLIN WIRELESS CORP.

FORM 10-Q

FOR THE QUARTERLY PERIOD ENDED DECEMBER 31, 2015

INDEX

		Page
PART I – Financial Information		
Item 1:	Consolidated Financial Statements (unaudited)	
	Consolidated Balance Sheets as of December 31, 2015 (unaudited) and June 30, 2015	**4**
	Consolidated Statements of Comprehensive Income (unaudited) for the three and six months ended December 31, 2015 and 2014	**5**
	Consolidated Statements of Cash Flows (unaudited) for the six months ended December 31, 2015 and 2014	**6**
	Notes to Consolidated Financial Statements	**7**
Item 2:	Management’s Discussion and Analysis of Financial Condition and Results of Operations	**17**
Item 3:	Quantitative and Qualitative Disclosures About Market Risk	**21**
Item 4:	Controls and Procedures	**21**
PART II – Other Information		
Item 1:	Legal Proceedings	**22**
Item 1A:	Risk Factors	**22**
Item 2:	Unregistered Sales of Equity Securities and Use of Proceeds	**22**
Item 3:	Defaults Upon Senior Securities	**22**
Item 4:	Mine Safety Disclosures	**22**
Item 5:	Other Information	**22**
Item 6:	Exhibits	**22**
Signatures		**23**

NOTE ON FORWARD LOOKING STATEMENTS

You should keep in mind the following points as you read this Report on Form 10-Q:

The terms “we,” “us,” “our,” “Franklin,” “Franklin Wireless,” or the “Company” refer to Franklin Wireless Corp.

This Report on Form 10-Q contains statements which, to the extent they do not recite historical fact, constitute “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. Forward looking statements are used under the caption “Management’s Discussion and Analysis of Financial Condition and Results of Operation,” and elsewhere in this Quarterly Report on Form 10-Q. You can identify these statements by the use of words like “may,” “will,” “could,” “should,” “project,” “believe,” “anticipate,” “expect,” “plan,” “estimate,” “forecast,” “potential,” “intend,” “continue,” and variations of t or comparable words. Forward looking statements do not guarantee future performance and involve risks and uncertainties. Actual results may differ substantially from the results that the forward looking statements suggest for various reasons, including those discussed under the caption “Risk Factors” in Item 1A of our Annual Report on Form 10-K for the year ended June 30, 2015. These forward looking statements are made only as of the date of this Report on Form 10-Q. We do not undertake to update or revise the forward looking statements, whether as a result of new information, future events or otherwise.

3

PART I – FINANCIAL INFORMATION

ITEM 1. Financial Statements

FRANKLIN WIRELESS CORP.

CONSOLIDATED BALANCE SHEETS

	December 31, 2015 (unaudited)	**June 30, 2015**
ASSETS		
Current assets:		
Cash and cash equivalents	$14,657,624	$11,822,620
Accounts receivable	14,945,041	5,464,182
Other receivables, net	166,265	143,384
Inventories, net	4,572,075	2,281,667
Prepaid expenses and other current assets	13,601	60,339
Prepaid income taxes	–	1,055,788
Deferred tax assets, current	206,902	206,902
Advance payments to vendors	118,806	62,321
Total current assets	34,680,314	21,097,203
Property and equipment, net	256,869	314,492
Intangible assets, net	1,339,193	1,042,281
Deferred tax assets, non-current	1,768,588	1,860,347
Goodwill	273,285	273,285
Other assets	133,912	129,859
TOTAL ASSETS	$38,452,161	$24,717,467
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$20,648,002	$7,362,075
Advance payments from customers	87,002	693,317
Accrued liabilities	457,961	238,619
Income tax payable	91,744	–
Short-term borrowings	148,295	148,295
Total current liabilities	21,433,004	8,442,306
Total liabilities	21,433,004	8,442,306

Commitments and contingencies (Note 8)

Stockholders' equity:		
Parent Company stockholders' equity		
Preferred stock, par value $0.001 per share, authorized 10,000,000 shares; No preferred stock issued and outstanding as of December 31, 2015 and June 30, 2015	–	–
Common stock, par value $0.001 per share, authorized 50,000,000 shares; 10,403,869 and 10,533,869 shares issued and outstanding as of December 31, 2015 and June 30, 2015, respectively	13,806	13,806
Additional paid-in capital	7,280,767	7,305,767
Retained earnings	13,996,257	13,361,091
Treasury stock, 3,472,286 and 3,342,286 shares as of December 31, 2015 and June 30, 2015, respectively	(4,513,479)	(4,279,479)
Accumulated other comprehensive loss	(695,270)	(664,722)
Total Parent Company stockholders' equity	16,082,081	15,736,463
Non-controlling interests	937,076	538,698
Total stockholders' equity	17,019,157	16,275,161
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$38,452,161	$24,717,467

See accompanying notes to consolidated financial statements.

FRANKLIN WIRELESS CORP.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

	Three Months Ended December 31,		Six Months Ended December 31,	
	2015	2014	2015	2014
Net sales	$20,163,481	$12,494,687	$32,111,947	$26,110,764
Cost of goods sold	17,000,575	10,006,962	26,986,034	21,307,439
Gross profit	3,162,906	2,487,725	5,125,913	4,803,325
Operating expenses:				
Selling, general and administrative	1,256,806	1,225,254	2,411,682	2,632,784
Research and development	793,609	740,508	1,516,178	1,515,903
Total operating expenses	2,050,415	1,965,762	3,927,860	4,148,687
Income from operations	1,112,491	521,963	1,198,053	654,638
Other income (loss), net:				
Interest income	3,431	3,020	5,708	5,655
Other income (loss), net	25,062	201,227	(20,228)	378,008
Total other income (loss), net	28,493	204,247	(14,520)	383,663
Income before provision for income taxes	1,140,984	726,210	1,183,533	1,038,301
Income tax provision	144,924	152,000	149,989	210,000
Net income	996,060	574,210	1,033,544	828,301
Non-controlling interests in net income of subsidiary at 48.2%	(378,841)	(149,730)	(398,378)	(120,673)
Net income attributable to Parent Company	$617,219	$424,480	$635,166	$707,628
Basic earnings per share attributable to Parent Company stockholders	$0.06	$0.04	$0.06	$0.07
Diluted earnings per share attributable to Parent Company stockholders	$0.06	$0.04	$0.06	$0.07
Weighted average common shares outstanding – basic	10,511,012	10,533,869	10,522,503	10,533,869
Weighted average common shares outstanding – diluted	10,678,039	10,661,879	10,689,530	10,661,879
Comprehensive income				
Net income	$996,060	$574,210	$1,033,544	$828,301
Translation adjustments	1,314	(81,376)	(30,548)	(126,144)
Comprehensive income	997,374	492,834	1,002,996	702,157
Comprehensive income attributable to non-controlling interest	(378,841)	(149,730)	(398,378)	(120,673)
Comprehensive income attributable to controlling interest	$618,533	$343,104	$604,618	$581,484

See accompanying notes to consolidated financial statements.

FRANKLIN WIRELESS CORP.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Six Months Ended December 31,	
	2015	2014
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$1,033,544	$828,301
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	99,347	121,318
Amortization of intangible assets	484,047	653,510
Deferred tax	91,759	63,001
Share-based compensation	(25,000)	42,951
Gain on forgiven debt	–	(40,664)
Gain on debt extinguishment	–	(331,601)
Increase (decrease) in cash due to change in:		
Accounts receivable	(9,503,740)	547,471
Inventories	(2,290,408)	173,117
Prepaid expenses and other current assets	46,738	65,958
Prepaid income taxes	1,055,788	147,000
Advance payments to vendors	(56,484)	20,233
Other assets	(4,053)	7,194
Accounts payable	13,285,927	69,811
Advance payments from customers	(606,315)	1,566,645
Accrued liabilities	219,341	(20,661)
Income tax payable	91,744	–
Net cash provided by operating activities	3,922,235	3,913,584
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment	(41,724)	(29,643)
Payments for capitalized development costs	(603,577)	(81,591)
Purchases of intangible assets	(177,382)	(6,802)
Receipt of loan repayments from an employee	–	7,128
Net cash used in investing activities	(822,683)	(110,908)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Repurchase of common stock	(234,000)	–
Net cash used in financing activities	(234,000)	–
Effect of foreign currency translation	(30,548)	(126,144)
Net increase in cash and cash equivalents	2,835,004	3,676,532
Cash and cash equivalents, beginning of period	11,822,620	8,240,595

Cash and cash equivalents, end of period	$14,657,624	$11,917,127
Supplemental disclosure of cash flow information:		
Cash paid (received) during the periods for:		
Interest	$–	$4,869
Income taxes	$(1,090,181)	$–

See accompanying notes to consolidated financial statements.

FRANKLIN WIRELESS CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1 – BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements of Franklin Wireless Corp. ("the Company") have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP") for interim financial information and are presented in accordance with the requirements of Form 10-Q. In the opinion of management, the financial statements included herein contain all adjustments, including normal recurring adjustments, considered necessary to present fairly the financial position, the results of operations and comprehensive income (loss) and cash flows of the Company for the periods presented. These financial statements and notes hereto should be read in conjunction with the financial statements and notes thereto for the fiscal year ended June 30, 2015 included in the Company's Form 10-K filed on September 28, 2015. The operating results or cash flows for the interim periods presented herein are not necessarily indicative of the results to be expected for any other interim period or the full year.

NOTE 2 – BUSINESS OVERVIEW

We are a provider of intelligent wireless solutions including mobile hotspots, routers and modems as well as innovative hardware and software products that support machine-to-machine (M2M) applications and the Internet of Things (IoT). Our M2M and IoT solutions include embedded modules, modems and gateways built to deliver reliable always-on connectivity supporting a broad spectrum of applications. These products are designed to solve wireless connectivity challenges in a variety of vertical markets including video surveillance, digital signage, home security, oil and gas exploration, kiosks, fleet management, smart grid, vehicle diagnostics, telematics and many more.

We have a majority ownership position in Franklin Technology Inc. (FTI), a research and development facility located in Seoul, South Korea. FTI primarily provides design and development services to us for our wireless products.

Our products are generally marketed and sold directly to wireless operators, and indirectly through strategic partners and distributors. Our global customer base extends primarily from the United States to countries in South America, the Caribbean, Europe, the Middle East and Africa ("EMEA") and Asia.

NOTE 3 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and a subsidiary with a majority voting interest of 51.8% (48.2% is owned by non-controlling interests) as of December 31, 2015 and June 30, 2015. In the preparation of consolidated financial statements of the Company, intercompany transactions and balances are eliminated and net earnings are reduced by the portion of the net earnings of the subsidiary applicable to non-controlling interests.

Non-controlling Interest in a Consolidated Subsidiary

As of December 31, 2015, the non-controlling interest was $937,076, which represents a $398,378 increase from $538,698 as of June 30, 2015. The increase was due to the net income of subsidiary of $825,828 for the six months ended December 31, 2015, of which 48.2% was attributable to the non-controlling interests.

Segment Reporting

Accounting Standards Codification (“ASC”) 280, “Segment Reporting,” requires public companies to report financial and descriptive information about their reportable operating segments. We identify our operating segments based on how management internally evaluates separate financial information, business activities and management responsibility. We have one reportable segment, consisting of the sale of wireless access products.

We generate revenues from four geographic areas, consisting of the United States, the Caribbean and South America, EMEA and Asia. The following enterprise-wide disclosure is prepared on a basis consistent with the preparation of the consolidated financial statements. The following table contains certain financial information by geographic area:

	Three Months Ended December 31,		Six Months Ended December 31,	
Net sales:	2015	2014	2015	2014
United States	$15,360,582	$8,816,503	$25,470,917	$19,725,646
Caribbean and South America	7,000	1,257,352	100,000	1,415,052
Europe, the Middle East and Africa ("EMEA")	4,743,238	1,357,015	6,485,441	1,363,398
Asia	52,661	1,063,817	55,589	3,606,668
Totals	$20,163,481	$12,494,687	$32,111,947	$26,110,764

Long-lived assets, net (property and equipment and intangible assets):	December 31, 2015		June 30, 2015	
United States	$	1,139,870	$	785,144
Asia		456,192		571,629
Totals	$	1,596,062	$	1,356,773

Estimates

The preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the 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 materially differ from those estimates.

Fair Value of Financial Instruments

The carrying amounts of financial instruments such as cash equivalents, accounts receivable, accounts payable and debt approximate the related fair values due to the short-term maturities of these instruments. We invest our excess cash into financial instruments which management believes are readily convertible into cash, such as money market funds and certificates of deposit.

Allowance for Doubtful Accounts

Based upon our review of our collection history as well as the current balances associated with all significant customers and associated invoices, we do not believe an allowance for doubtful accounts was necessary as of December 31, 2015 and June 30, 2015.

Revenue Recognition

We recognize revenue in accordance with ASC 605, "Revenue Recognition," when persuasive evidence of an arrangement exists, the price is fixed or determinable, collection is reasonably assured and delivery of products has occurred or services have been rendered. Accordingly, we recognize revenues from product sales upon shipment of the products to customers or when the products are received by the customers in accordance with shipping or delivery terms. We provide a warranty for one year from the shipment date, which is covered by our vendors pursuant to purchase agreements. Any net warranty related expenditures made by us have not historically been material. Under our sales return policy, customers may generally return products that are under warranty for repair or replacement.

Cost of Goods Sold

All costs associated with our contract manufacturers, as well as distribution, fulfillment and repair services are included in our cost of goods sold. Cost of goods sold also includes amortization expense associated with capitalized product development costs associated with complete technology.

Capitalized Product Development Costs

Accounting Standards Codification ("ASC") Topic 350, "Intangibles – Goodwill and Other" includes software that is part of a product or process to be sold to a customer and shall be accounted for under Subtopic 985-20. Our products contain embedded software internally developed by our Korea-based subsidiary, Franklin Technology Inc. ("FTI"), which is an integral part of these products because it allows the various components of the products to communicate with each other and the products are clearly unable to function without this coding.

The costs of product development that are capitalized once technological feasibility is determined (noted as Technology in progress in the Intangible Assets table) include payroll, employee benefits, and other headcount-related expenses associated with product development. Related licenses and certification costs are also capitalized. We determine that technological feasibility for our products is reached after all high-risk development issues have been resolved. Once the products are available for general release to our customers, we cease capitalizing the product development costs and any additional costs, if any, are expensed. The capitalized product development costs are amortized on a product-by-product basis using the greater of straight-line amortization or the ratio of the current gross revenues to the current and anticipated future gross revenues. The amortization begins when the products are available for general release to our customers.

As of December 31, 2015 and June 30, 2015, capitalized product development costs in progress were $603,577 and $0, respectively, and these amounts are included in intangible assets in our consolidated balance sheets. During the three months and six months ended December 31, 2015, we incurred $464,665 and $603,577 in capitalized product development costs, and such amounts are primarily comprised of certifications and licenses. All costs incurred before technological feasibility is reached are expensed and included in our consolidated statements of comprehensive income (loss).

Research and Development Costs

Costs associated with research and development are expensed as incurred. Research and development costs were $793,609 and $740,508 for the three months ended December 31, 2015 and 2014, respectively, and $1,516,178 and $1,515,903 for the six months ended December 31, 2015 and 2014, respectively.

Warranties

We provide a warranty for one year which is covered by our vendors and manufacturers under purchase agreements between the Company and the vendors. In general, our products are shipped directly from our vendors to our customers. As a result, we believe we do not have any net warranty exposure and do not accrue any warranty expenses. Historically, the Company has not experienced any material net warranty expenditures.

Shipping and Handling Costs

Costs associated with product shipping and handling are expensed as incurred. Shipping and handling costs, which are included in selling, general and administrative expenses on the consolidated statements of comprehensive income, were $456,868 and $322,838 for the three months ended December 31, 2015 and 2014, respectively, and $671,428 and $675,578 for the six months ended December 31, 2015 and 2014, respectively.

Cash and Cash Equivalents

For purposes of the consolidated statements of cash flow, we consider all highly liquid investments purchased with original maturities of three months or less to be cash equivalents.

Inventories

Our inventories consist of finished goods and are stated at the lower of cost or market, cost being determined on a first-in, first-out basis. We assess the inventory carrying value and reduce it, if necessary, to its net realizable value based on customer orders on hand, and internal demand forecasts using management's best estimates given information currently available. Our customer demand is highly unpredictable, and can fluctuate significantly caused by factors beyond the control of the Company. We may write down our inventory value for potential obsolescence and excess inventory. As of December 31, 2015 and June 30, 2015, we have recorded an inventory reserve in the amount of $120,867 for inventories that we have identified as obsolete or slow-moving.

Property and Equipment

Property and equipment are recorded at cost. Significant additions or improvements extending useful lives of assets are capitalized. Maintenance and repairs are charged to expense as incurred. Depreciation is computed using the straight-line method over the estimated useful lives as follows:

Machinery	6 years
Office equipment	5 years
Molds	3 years
Vehicles	5 years
Computers and software	5 years
Furniture and fixtures	7 years
Facilities	5 years or life of the lease, whichever is shorter

Goodwill and Intangible Assets

Goodwill and certain intangible assets were recorded in connection with the FTI acquisition in October 2009, and are accounted for in accordance with ASC 805, "Business Combinations." Goodwill represents the excess of the purchase price over the fair value of the tangible and intangible net assets acquired. Intangible assets are recorded at their fair value at the date of acquisition. Goodwill and other intangible assets are accounted for in accordance with ASC 350, "Goodwill and Other Intangible Assets." Goodwill and other intangible assets are tested for impairment at least annually and any related impairment losses are recognized in earnings when identified. No impairment was recognized during the periods ended December 31, 2015 and June 30, 2015.

The definite lived intangible assets consisted of the following as of December 31, 2015:

Definite lived intangible assets:	**Expected Life**	**Average Remaining life**	**Gross Intangible Assets**	**Accumulated Amortization**	**Net Intangible Assets**
Complete technology	3 years	–	$490,000	$ 490,000	$–
Complete technology	3 years	–	1,517,683	1,517,683	–
Complete technology	3 years	–	281,714	281,714	–
Complete technology	3 years	–	361,249	361,249	–
Complete technology	3 years	–	174,009	174,009	–
Complete technology	3 years	0.1 years	909,962	884,685	25,277
Complete technology	3 years	1.3 years	65,000	37,917	27,083
Complete technology	3 years	2.0 years	2,402	800	1,602
Complete technology	3 years	2.3 years	6,405	1,602	4,803
Supply and development agreement	8 years	1.8 years	1,121,000	875,781	245,219
Technology in progress	Not Applicable	–	603,577	–	603,577
Software	5 years	1.6 years	214,065	180,671	33,394
Patents	10 years	7.5 years	58,390	1,710	56,680
Certifications and licenses	3 years	2.2 years	1,943,561	1,602,003	341,558
Total as of December 31, 2015			$7,749,017	$ 6,409,824	$1,339,193

The definite lived intangible assets consisted of the following as of June 30, 2015:

Definite lived intangible assets:	**Expected Life**	**Average Remaining life**	**Gross Intangible Assets**	**Accumulated Amortization**	**Net Intangible Assets**
Complete technology	3 years	–	$490,000	$ 490,000	$–
Complete technology	3 years	–	1,517,683	1,517,683	–
Complete technology	3 years	–	281,714	281,714	–
Complete technology	3 years	–	361,249	361,249	–
Complete technology	3 years	0.3 years	174,009	159,508	14,501
Complete technology	3 years	0.5 years	909,962	733,025	176,937
Complete technology	3 years	1.8 years	65,000	27,083	37,917
Complete technology	3 years	2.5 years	2,402	400	2,002
Complete technology	3 years	2.8 years	6,405	534	5,871
Supply and development agreement	8 years	2.3 years	1,121,000	805,719	315,281
Technology in progress	Not Applicable	–	–	–	–
Software	5 years	1.1 years	197,418	158,284	39,134
Patents	10 years	6.8 years	57,655	1,005	56,650
Certifications and licenses	3 years	0.4 years	1,783,561	1,389,573	393,988
Total as of June 30, 2015			$6,968,058	$ 5,925,777	$1,042,281

Amortization expense recognized during the three months ended December 31, 2015 and 2014 was $229,701 and $321,280, respectively, and during the six months ended December 31, 2015 and 2014 was $484,047 and $653,510, respectively.

Long-lived Assets

In accordance with ASC 360, "Property, Plant, and Equipment," we review for impairment of long-lived assets and certain identifiable intangibles whenever events or circumstances indicate that the carrying amount of assets may not be recoverable. We consider the carrying value of assets may not be recoverable based upon our review of the following events or changes in circumstances: the asset’s ability to continue to generate income from operations and positive cash flow in future periods; loss of legal ownership or title to the asset; significant changes in our strategic business objectives and utilization of the asset; or significant negative industry or economic trends. An impairment loss would be recognized when estimated future cash flows expected to result from the use of the asset are less than its carrying amount.

As of December 31, 2015, we are not aware of any events or changes in circumstances that would indicate that the long-lived assets are impaired.

Stock-based Compensation

The Company’s employee share-based awards result in a cost that is measured at fair value on an award’s grant date, based on the estimated number of awards that are expected to vest. Stock-based compensation is recognized on a straight-line basis over the award’s vesting period. The Company estimates the fair value of stock options using a Black-Scholes option pricing model. Transactions with non-employees in which goods or services are the consideration received for the issuance of equity instruments are accounted for based on the fair value of the consideration received or the fair value of the equity instrument issued, whichever is more reliably measurable. The measurement date of the fair value of the equity instrument issued is the earlier of the date on which the counterparty's performance is complete or the date on which it is probable that performance will occur. Stock-based compensation costs are reflected in the accompanying consolidated statements of comprehensive income based upon the underlying recipients' roles within the Company.

Income Taxes

The Company uses the asset and liability method of accounting for income taxes. Accordingly, deferred tax assets and liabilities are determined based on the difference between the financial statement and income tax bases of assets and liabilities, using enacted tax rates in effect for the year in which the differences are expected to reverse. A valuation allowance is recorded to reduce the carrying amount of deferred tax assets, unless it is more likely than not such assets will be realized. Current income taxes are based on the year’s taxable income for federal and state income tax reporting purposes and the annual change in deferred taxes.

The Company assesses its income tax positions and records tax benefits based upon management’s evaluation of the facts, circumstances, and information available at the reporting date. For those tax positions where it is more likely than not that a tax benefit will be sustained, the Company records the largest amount of tax benefit with a greater than 50% likelihood of being realized upon ultimate settlement with a taxing authority having full knowledge of all relevant information. For those income tax positions where it is not more likely than not that a tax benefit will be sustained, no tax benefit is recognized in the financial statements. The Company classifies interest and penalties associated with such uncertain tax positions as a component of income tax expense.

As of December 31, 2015, we have no material unrecognized tax benefits. We recorded an income tax provision of $144,924 and $149,989 for the three and six months ended December 31, 2015, respectively, and an increase in income tax payable of $86,679 and $91,744 for the three and six months ended December 31, 2015, respectively.

11

Net Loss per Share Attributable to Common Stockholders

Basic net loss per share is calculated by dividing the net loss by the weighted-average number of common shares that were outstanding for the period, without consideration for potential common shares. Diluted net loss per share is calculated by dividing the net loss by the sum of the weighted-average number of dilutive potential common shares outstanding for the period determined using the treasury-stock method or the as-converted method. Potentially dilutive shares are comprised of common stock options outstanding under our stock plan.

Concentrations

We extend credit to our customers and perform ongoing credit evaluations of such customers. We evaluate our accounts receivable on a regular basis for collectability and provide for an allowance for potential credit losses as deemed necessary. No reserve was required or recorded for any of the periods presented.

Substantially all of our revenues are derived from sales of wireless data products. Any significant decline in market acceptance of our products or in the financial condition of our existing customers could impair our ability to operate effectively.

A significant portion of our revenue is derived from a small number of customers. For the six months ended December 31, 2015, sales to our two largest customers accounted for 78.2% and 19.4% of our consolidated net sales and 94.6% and 0.6% of our accounts receivable balance, as of December 31, 2015. In the same period in 2014, sales to our two largest customers accounted for 63%, and 12% of our consolidated net sales and 61% and 11% of our accounts receivable balance as of December 31, 2014. No other customers accounted for more than ten percent of total net sales for the six months ended December 31, 2015 and 2014 and no other customers accounted for more than ten percent of total accounts receivable for the six months ended December 31, 2015 and 2014.

For the six months ended December 31, 2015, we purchased the majority of our wireless data products from one manufacturing company located in Asia. If this manufacturing company were to experience delays, capacity constraints or quality control problems, product shipments to our customers could be delayed, or our customers could consequently elect to cancel the underlying product purchase order, which would negatively impact the Company's revenue. For the six months ended December 31, 2015, we purchased wireless data products from this manufacturer in the amount of $28,887,185, or 98.9% of total purchases, and had related accounts payable of $19,469,976 as of December 31, 2015. For the six months ended December 31, 2014, we purchased wireless data products from two manufacturing companies in the amount of $16,506,938, or 81% of total purchases, and had related accounts payable of $4,162,219 as of December 31, 2014.

We maintain our cash accounts with established commercial banks. Such cash deposits exceed the Federal Deposit Insurance Corporation insured limit of $250,000 for each financial institution. However, we do not anticipate any losses on excess deposits.

Recently Issued Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2014-09, Revenue from Contracts with Customers. This amendment addresses revenue from contracts with customers, which clarifies existing accounting literature relating to how and when a company recognizes revenue. Under the update, a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods and services. ASU 2015-14 delayed the effective date of this update to annual reporting periods beginning after December 15, 2017, and the amendment is to be applied retrospectively or the cumulative effect as of the date of adoption. Management is currently evaluating the impact ASU 2014-09 will have on the consolidated financial statements and related disclosures.

In August 2014, the FASB issued ASU 2014-15, Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern. This ASU introduces an explicit requirement for management to assess if there is substantial doubt about an entity's ability to continue as a going concern, and to provide related footnote disclosures in certain circumstances. In connection with each annual and interim period, management must assess if there is substantial doubt about an entity's ability to continue as a going concern within one year after the issuance date. Disclosures are required if conditions give rise to substantial doubt. ASU 2014-15 is effective for all entities in the first annual period ending after December 15, 2016. Management does not believe the potential effects of this ASU on the consolidated financial statements will be material.

In April 2015, the FASB issued ASU 2015-03, Interest—Imputation of Interest: Simplifying the Presentation of Debt Issuance Costs. The update requires debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of the related debt liability instead of being presented as an asset. Debt disclosures will include the face amount of the debt liability and the effective interest rate. The update requires retrospective application and represents a change in accounting principle. ASU 2015-15 was issued subsequently to permit costs associated with a line of credit arrangement to be presented as assets and amortized ratably over the term of the arrangement. These updates will be effective for the Company on July 1, 2016. Management does not believe that these updates will materially impact the Company's consolidated financial statements.

In July 2015, the FASB issued ASU 2015-11, Inventory—Simplifying the Measurement of Inventory. ASU 2015-11 requires inventory to be subsequently measured using the lower of cost and net realizable value, thereby eliminating the market value approach. Net realizable value is defined as the "estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal and transportation." ASU 2015-11 is effective for

the Company beginning on July 1, 2017 and is applied prospectively. Early adoption is permitted. The Company is currently evaluating the impact that this guidance will have on its consolidated financial statements and disclosure.

NOTE 4 – PROPERTY AND EQUIPMENT

Property and equipment consisted of the following as of:

	December 31, 2015	June 30, 2015
Machinery and facility	$303,520	$300,650
Office equipment	381,927	373,554
Molds	808,130	775,499
Construction-in progress	–	2,150
	1,493,577	1,451,853
Less accumulated depreciation	(1,236,708)	(1,137,361)
Total	$256,869	$314,492

Depreciation expense associated with property and equipment was $47,714 and $57,264 for the three months ended December 31, 2015 and 2014, respectively, and $99,347 and $121,318 for the six months ended December 31, 2015 and 2014, respectively.

NOTE 5 – ACCRUED LIABILITIES

Accrued liabilities consisted of the following as of:

	December 31, 2015	June 30, 2015
Accrued salaries, severance	$113,313	$140,820
Accrued salaries, payroll deductions owed to government entities	9,444	8,434
Accrued vacation	69,946	75,477
Payroll taxes	9,512	10,823
Other accrued liabilities	255,746	3,065
Total	$457,961	$238,619

NOTE 6 – SHORT-TERM BORROWINGS

Short-term borrowings consisted of the following as of:

	December 31, 2015	June 30, 2015
Loan dated June 2011, due to a financial institution, with monthly interest payments (interest rate of 8.90% per annum), and the principal balance due March 2016 (interest rate of 5.025% per annum as extended)	$148,295	$148,295

The short-term borrowings of $148,295 as of December 31, 2015 and June 30, 2015, resulted from the consolidation of FTI's debt.

NOTE 7 – EARNINGS PER SHARE

We report earnings per share in accordance with ASC 260, "Earnings Per Share." Basic earnings per share are computed using the weighted average number of shares outstanding during the period. Diluted earnings per share represent basic earnings per share adjusted to include the potentially dilutive effect of outstanding stock options. The weighted average number of shares outstanding used to compute earnings per share is as follows:

	Three Months ended December 31,		Six Months Ended December 31,	
	2015	2014	2015	2014
Net income attributable to Parent Company	$617,219	$424,480	$635,166	$707,628
Weighted-average shares of common stock outstanding:				
Basic shares outstanding	10,511,012	10,533,869	10,522,503	10,533,869
Dilutive effect of common stock equivalents arising from stock options	167,027	128,010	167,027	128,010
Diluted shares outstanding	10,678,039	10,661,879	10,689,530	10,661,879
Basic earnings per share	$0.06	$0.04	$0.06	$0.07
Diluted earnings per share	$0.06	$0.04	$0.06	$0.07

13

NOTE 8 – COMMITMENTS AND CONTINGENCIES

Leases

We leased approximately 11,318 square feet of office space located in San Diego, California, at a monthly rent of $16,576; although the lease expired on August 31, 2015, we continued to occupy the premises with the consent of the landlord through October 27, 2015. On September 9, 2015, we signed a lease for new office space consisting of approximately 12,775 square feet, also located in San Diego, California, at a monthly rent of $23,115, which commenced on October 28, 2015. In addition to monthly rent, the new lease includes payment for certain common area costs. The term of the lease for the new office space is four years from the lease commencement date. Our facility is covered by an appropriate level of insurance and we believe it to be suitable for our use and adequate for our present needs. Rent expense related to these leases was $70,764 and $49,728 for the three months ended December 31, 2015 and 2014, respectively, and $131,080 and $99,456 for the six months ended December 31, 2015 and 2014, respectively.

Our Korea-based subsidiary, Franklin Technology, Inc. (“FTI”), leases approximately 10,000 square feet of office space in Seoul, Korea, at a monthly rent of approximately $8,000, and the lease expires on September 1, 2017. Beginning on June 12, 2015, FTI leased additional office space consisting of approximately 2,682 square feet, also located in Seoul, Korea, at a monthly rent of approximately $2,700, and the lease expires on September 1, 2017. In addition to monthly rent, the lease provides for periodic cost of living increases in the base rent and payment for certain common area costs. These facilities are covered by an appropriate level of insurance and we believe them to be suitable for our use and adequate for our present needs. Rent expense related to these leases was approximately $32,100 and $24,000 for the three months ended December 31, 2015 and 2014, respectively, and $64,200 and $48,000 for the six months ended December 31, 2015 and 2014, respectively.

We lease one corporate housing facility for our vendors and employees who travel, under a non-cancelable operating lease that expired on September 13, 2015 and was extended to September 5, 2016. Rent expense related to this lease was $2,460 and $2,597 for the three months ended December 31, 2015 and 2014, respectively, and $4,896 and $5,380 for the six months ended December 31, 2015 and 2014, respectively.

Litigation

We are from time to time involved in certain legal proceedings and claims arising in the ordinary course of business.

C-Motech Co., Ltd.

On July 27, 2010, we entered into a Common Stock Repurchase Agreement with C-Motech (the "Agreement"), under which we agreed to repurchase 3,370,356 shares of our Common Stock from C-Motech for $3,500,000. A total of 1,803,684 shares were repurchased on the date of the Agreement in exchange for non-cash consideration in the amount of $1,873,065, which represented amounts owed to the Company by C-Motech for certain marketing funds as well as the settlement of a price dispute for products previously purchased by the Company from C-Motech. Under the Agreement, the remaining 1,566,672 shares were to be repurchased by us upon payment of the balance, $1,626,935, on or before December 31, 2010.

On January 28, 2011 (the "Amendment Date") the Agreement was amended to reflect (1) a change in the date the 1,566,672 shares are to be repurchased from C-Motech from December 31, 2010 to March 31, 2011, and (2) a change to the non-cash consideration of $1,873,065. In exchange for the 1,803,684 shares, we were to pay cash to C-Motech (in the same amount) for the shares, by March 31, 2011. In addition, in a separate agreement dated January 28, 2011, C-Motech agreed to pay us $1,873,065, for amounts owed, by March 31, 2011. The purpose of these revisions was to more clearly differentiate each party's payment obligations to the other with respect to this transaction. Following the Amendment Date, we paid C-Motech $1,873,065 in exchange for the 1,803,684 shares previously transferred to us by C-Motech, and C-Motech paid us $1,873,065 for amounts owed, of which $1,581,457 was booked to other income and $291,608 was booked to cost of goods sold. The repurchase of the remaining 1,566,672 shares from C-Motech was not completed. We have provided formal notification to C-Motech that it is in breach of its obligations and we have also provided a demand to sell the shares back to us. We have attempted to tender payment for the shares without results. We were previously advised that two individuals, Cheng-Ji Zhu and Ok-Nam Yun, claim to have purchased the shares from C-Motech through its former CEO; however, the authority of the former CEO to agree to the sale of the shares was disputed by C-Motech. The ownership of the shares was the subject of litigation involving Cheng-Ji Zhu and Ok-Nam Yun and C-Motech in U.S. and Korean courts. On April 1, 2015 the Circuit Court of Cook County, Illinois County Department, Chancery Division issued an Order with respect to the matter of Cheng-Ji Zhu and Ok-Nam Yun, plaintiffs, v. Integrity Stock Transfer and Registrar, Mountain Share Transfer, Inc. and C-Motech Company Ltd., defendants. The Order recognizes and enforces the plaintiff's Motion to Recognize and Enforce Foreign Judgment in which the plaintiffs previously prevailed over C-Motech with respect to the ownership of the 1,566,672 shares of Franklin Wireless Common Stock in an action that took place in Korea.

On May 7, 2013, we filed a lawsuit against C-Motech in the Superior Court of California for the County of San Diego for breach of the Agreement and breach of other contracts between the parties relating to indemnification and other obligations. On February 25, 2014, C-Motech answered the complaint and on February 26, 2014, C-Motech filed a Notice of Removal from the Superior Court of the State of California for the County of San Diego to the United States District Court for the Southern District of California. On June 19, 2014, C-Motech filed a voluntary petition for relief under Chapter 15 of the U.S. Bankruptcy Code and on June 27, 2014, C-Motech filed a Motion for Recognition of a Foreign Main Proceeding under Chapter 15 of the U.S. Bankruptcy Code and Further Relief. On July 10, 2014, this motion was heard in the U.S. Bankruptcy Court for the Southern District of California during which the Court ordered that C-Motech's bankruptcy proceeding in South Korea was recognized as a foreign main proceeding and that our lawsuit against C-Motech in the U.S. District Court is stayed. The effect of this ruling is that we must participate in C-Motech's bankruptcy proceeding in South Korea if we wish to pursue our various claims against C-Motech.

On September 9, 2015, registered ownership of the shares was transferred from C-Motech to Cheng-Ji Zhu (838,350 shares) and Ok-Nam Yun (728,322 shares). Subsequently, on December 30, 2015, the Company repurchased 130,000 of the shares from Ok-Nam Yun.

Novatel Wireless, Inc.

On December 10, 2010, Novatel Wireless, Inc. and Novatel Wireless Solutions, Inc. ("Novatel") filed a complaint in the United States District Court for the Southern District of California, against us and one other defendant. The complaint alleges that certain products, including, but not limited to, mobile data hot spots and data modems, infringe on U.S. Patent Nos. 5,129,098; 7,318,225; 7,574,737 and 7,319,715. On April 13, 2012, the plaintiff filed a Second Amended Complaint which amended certain claims and added U.S. Patent No. 7,944,901 to the original complaint. On April 27, 2012, we filed a Motion to Dismiss the Second Amended Complaint as to certain of the claims. On July 6, 2012, the Court held oral argument on the Motion to Dismiss and on July 19, 2012, the Court issued an order granting in part and denying in part the Motion to Dismiss. On August 2, 2012, we answered the complaint and an Early Neutral Evaluation Conference took place on October 31, 2012 and a follow-up Settlement Conference was held on June 12, 2013. A claim construction hearing took place on October 9, 2014. On November 25, 2014, the Court granted plaintiff's Joint Motion to Joinder of Required Party, which added Nova Intellectual Solutions, LLC ("NIS") as a plaintiff to this litigation. Novatel had previously assigned the patents-in-suit to Strategic Intellectual Solutions, LLC, which is the parent company of NIS.

On April 24, 2015, NIS filed a complaint in the United States District Court for the Southern District of California, against us and FTI. The complaint alleges that one of the Company's products infringes on U.S. Patent No. 7,944,901.

On July 20, 2015, a Settlement Conference took place during which we and NIS agreed to settle this matter and an agreement governing the settlement was executed on October 20, 2015.

On October 1, 2015, we and Novatel filed a Joint Motion For Dismissal With Prejudice as to the patent infringement claims made by Novatel against us. On October 28, 2015, we and NIS filed a Joint Motion For Dismissal With Prejudice as to the patent infringement claims made by it against the Company and FTI.

Adaptix, Inc.

In October 2015 we were notified that on June 12, 2015, Adaptix, Inc. filed a complaint in the United States District Court for the Eastern District of Texas, Tyler Division against one of our customers. The complaint alleges that certain wireless devices, including one device provided by the Company, infringe on U.S. Patent No. 8,934,375. As of December 31, 2015, this legal proceeding is pending, but we do not believe that this action will have a material effect on the Company.

Change of Control Agreements

On September 21, 2009 we entered into Change of Control Agreements with OC Kim, our President, Yun J. (David) Lee, our Chief Operating Officer, and Yong Bae Won, our Vice President, Engineering. Each Change of Control Agreement provides for a lump sum payment to the officer in case of a change of control of the Company. The term includes the acquisition of Common Stock of the Company resulting in one person or company owning more than 50% of the outstanding shares, a significant change in the composition of the Board of Directors of the Company during any 12-month period, a reorganization, merger, consolidation or similar transaction resulting in the transfer of ownership of more than fifty percent (50%) of the Company's outstanding Common Stock, or a liquidation or dissolution of the Company or sale of substantially all of the Company's assets.

The Change of Control Agreement with Mr. Kim calls for a payment of $5 million upon a change of control; the agreement with Mr. Lee calls for a payment of $2 million upon a change of control; and the agreement with Mr. Won was for two years and called for a payment of $1 million upon a change of control.

The Board of Directors has approved extension of the Change of Control Agreements with Mr. Kim and Mr. Lee, through September 21, 2017. The Change of Control Agreement with Mr. Won expired on September 21, 2014 and was not renewed or extended.

NOTE 9 – LONG-TERM INCENTIVE PLAN AWARDS

We adopted the 2009 Stock Incentive Plan ("2009 Plan") on June 11, 2009, which provided for the grant of incentive stock options and non-qualified stock options to our employees and directors. Options granted under the 2009 Plan generally have a term of ten years and generally vest and become exercisable at the rate of 33% after one year and 33% on the second and third anniversaries of the option grant dates. Historically, some stock option grants have included shorter vesting periods ranging from one to two years.

The estimated forfeiture rate considers historical turnover rates stratified into employee pools in comparison with an overall employee turnover rate, as well as expectations about the future. We periodically revise the estimated forfeiture rate in subsequent periods if actual forfeitures differ from those estimates. Compensation expense recorded under this method for the three and six months ended December 31, 2015 was ($12,500) and ($25,000), respectively. The expense credits for the three and six months ended December 31, 2015 resulted from the reversal of expenses booked in prior periods for stock options for a small number of employees that were cancelled. This amount increased income from operations and income before provision for income taxes by the same amount by decreasing compensation expense recognized in selling, general and administrative expense.

A summary of the status of our stock options is presented below:

Options	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Life (In Years)	Aggregate Intrinsic Value
Outstanding as of June 30, 2015	850,337	$ 1.24	4.36	$ 306,583
Granted	–			
Exercised	–			
Cancelled	–			
Forfeited or Expired	–			

Outstanding as of December 31, 2015	850,337	$ 1.24	3.86	$ 816,782
Exercisable as of December 31, 2015	850,337	$ 1.24	3.86	$ 816,782

The aggregate intrinsic value in the preceding table represents the total pretax intrinsic value, based upon the Company's closing stock price of $2.20 as of December 31, 2015, which would have been received by the option holders had all option holders exercised their options as of that date. The weighted-average grant-date fair value of stock options outstanding as of December 31, 2015, in the amount of 850,337 shares, was $1.15 per share.

As of December 31, 2015, there was no unrecognized compensation cost related to non-vested stock options granted.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our financial statements and related notes included elsewhere in this report. This report contains certain forward-looking statements relating to future events or our future financial performance. These statements are subject to risks and uncertainties which could cause actual results to differ materially from those discussed in this report. You are cautioned not to place undue reliance on this information, which speaks only as of the date of this report. We are not obligated to publicly update this information, whether as a result of new information, future events or otherwise, except to the extent we are required to do so in connection with our obligation to file reports with the SEC. For a discussion of the important risks to our business and future operating performance, see the discussion under the caption “Item 1A. Risk Factors” and under the caption “Factors That May Influence Future Results of Operations” in the Company’s Form 10-K for the year ended June 30, 2015, filed on September 28, 2015. In light of these risks, uncertainties and assumptions, the forward-looking events discussed in this report might not occur.

BUSINESS OVERVIEW

We are a provider of intelligent wireless solutions including mobile hotspots, routers and modems as well as innovative hardware and software products that support machine-to-machine (M2M) applications and the Internet of Things (IoT). Our M2M and IoT solutions include embedded modules, modems and gateways built to deliver reliable always-on connectivity supporting a broad spectrum of applications. These products are designed to solve wireless connectivity challenges in a variety of vertical markets including video surveillance, digital signage, home security, oil and gas exploration, kiosks, fleet management, smart grid, vehicle diagnostics, telematics and many more.

We have a majority ownership position in Franklin Technology Inc. (FTI), a research and development facility located in Seoul, South Korea. FTI primarily provides design and development services to us for our wireless products.

Our products are generally marketed and sold directly to wireless operators, and indirectly through strategic partners and distributors. Our global customer base extends primarily from the United States to countries in South America, the Caribbean, EMEA and Asia.

FACTORS THAT MAY INFLUENCE FUTURE RESULTS OF OPERATIONS

We believe that our revenue growth will be influenced largely by (1) the successful maintenance of our existing customers, (2) the rate of increase in demand for wireless data products, (3) customer acceptance of our new products, (4) new customer relationships and contracts, and (5) our ability to meet customers' demands.

We have entered into and expect to continue to enter into new customer relationships and contracts for the supply of our products, and this may require significant demands on our resources, resulting in increased operating, selling, and marketing expenses associated with such new customers.

CRITICAL ACCOUNTING POLICIES

Our discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which are prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). The preparation of these financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingencies at the date of the financial statements, as well as the reported amounts of revenues and expenses during the reporting periods. Management evaluates these estimates and assumptions on an ongoing basis. Our estimates and assumptions have been prepared on the basis of the most current reasonably available information. The results of these estimates form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results could differ from these estimates under different assumptions and conditions.

We have several critical accounting policies, which were described in our Annual Report on Form 10-K for the year ended June 30, 2015, that are both important to the portrayal of our financial condition and results of operations and require management's most difficult, subjective and complex judgments. Typically, the circumstances that make these judgments difficult, subjective and complex have to do with making estimates about the effect of matters that are inherently uncertain. There were no material changes to our critical accounting policies during the three months ended December 31, 2015.

RESULTS OF OPERATIONS

The following table sets forth, for the three and six months ended December 31, 2015 and 2014, our statements of comprehensive income including data expressed as a percentage of sales:

	Three Months Ended		Six Months Ended	
	December 31,		December 31,	
	2015	2014	2015	2014
Net sales	100.0%	100.0%	100.0%	100.0%
Cost of goods sold	84.3%	80.1%	84.0%	81.6%
Gross profit	15.7%	19.9%	16.0%	18.4%
Operating expenses	10.2%	15.7%	12.2%	15.9%
Income from operations	5.5%	4.2%	3.8%	2.5%
Other income, net	0.2%	1.6%	0.1%	1.5%
Net income before income taxes	5.7%	5.8%	3.7%	4.0%
Income tax provision	0.7%	1.2%	0.5%	0.8%
Net income	5.0%	4.6%	3.2%	3.2%
Non-controlling interest in net income of subsidiary	(1.9%)	(1.2%)	(1.2%)	(0.5%)
Net income attributable to Parent Company stockholders	3.1%	3.4%	2.0%	2.7%

THREE MONTHS ENDED DECEMBER 31, 2015 COMPARED TO THREE MONTHS ENDED DECEMBER 31, 2014

NET SALES – Net sales increased by $7,668,794, or 61.4%, to $20,163,481 for the three months ended December 31, 2015 from $12,494,687 for the corresponding period of 2014. For the three months ended December 31, 2015, net sales by geographic regions, consisting of the United States, South America and the Caribbean, EMEA and Asia, were $15,360,582 (76.2% of net sales), $7,000 (0.0% of net sales), $4,743,238 (23.5% of net sales) and $52,661 (0.3% of net sales), respectively. For the three months ended December 31, 2014, net sales by geographic regions, consisting of the United States, South America and the Caribbean, EMEA and Asia, were $8,816,503 (70.6% of net sales), $1,257,352 (10.0% of net sales), $1,357,015 (10.9% of net sales) and $1,063,817 (8.5% of net sales), respectively.

Net sales in the United States increased by $6,544,079, or 74.2%, to $15,360,582 for the three months ended December 31, 2015 from $8,816,503 for the corresponding period of 2014. The increase in net sales was primarily due to increased demand for one of the Company's products from a carrier customer. Net sales in the South American and Caribbean regions decreased by $1,250,352, or 99.4%, to $7,000 for the three months ended December 31, 2015 from $1,257,352 for the corresponding period of 2014. The decrease in net sales was primarily due to the general nature of sales in these regions, which often fluctuate significantly from period to period due to timing of orders placed by a relatively small number of customers. Net sales in EMEA increased by $3,386,223, or 249.5%, to

$4,743,238 for the three months ended December 31, 2015 from $1,357,015 for the corresponding period of 2014. The increase in net sales was due to timing of orders placed by a carrier customer in Africa. Net sales in Asia decreased by $1,011,156, or 95.0%, to $52,661 for the three months ended December 31, 2015 from $1,063,817 for the corresponding period of 2014. The decrease in net sales was primarily due to lower product and component sales generated by FTI, which typically vary from period to period.

GROSS PROFIT – Gross profit increased by $675,181, or 27.1%, to $3,162,906 for the three months ended December 31, 2015 from $2,487,725 for the corresponding period of 2014. The gross profit in terms of net sales percentage was 15.7% for the three months ended December 31, 2015 compared to 19.9% for the corresponding period of 2014. The increase in gross profit was primarily due to the change in net sales as described above. The decrease in gross profit in terms of net sales percentage was primarily due to variations in customer and product mix, competitive selling prices and product costs which generally vary from period to period and region to region.

OPERATING EXPENSES – Operating expenses increased by $84,653, or 4.3%, to $2,050,415 for the three months ended December 31, 2015 from $1,965,762 for the corresponding period of 2014. The increase was primarily due to higher shipping and handling costs resulting from the volume increase in product shipments and increases in administrative office rent and share-based compensation expense, which were partially offset by lower travel related expenses and amortization and depreciation expense.

OTHER INCOME, NET – Other income, net decreased by $175,754, or 86.0%, to $28,493 for the three months ended December 31, 2015 from $204,247 for the corresponding period of 2014. The decrease was primarily due to expenses that were reversed associated with certain marketing related activities accrued in prior periods which expired during the three months ended December 31, 2014. During the three months ended December 30, 2015, no expenses were reversed or expired.

SIX MONTHS ENDED DECEMBER 31, 2015 COMPARED TO SIX MONTHS ENDED DECEMBER 31, 2014

NET SALES – Net sales increased by $6,001,183, or 23.0%, to $32,111,947 for the six months ended December 31, 2015 from $26,110,764 for the corresponding period of 2014. For the six months ended December 31, 2015, net sales by geographic regions, consisting of the United States, South America and the Caribbean, EMEA and Asia, were $25,470,917 (79.3% of net sales), $100,000 (0.3% of net sales), $6,485,441 (20.2% of net sales) and $55,589 (0.2% of net sales), respectively. For the six months ended December 31, 2014, net sales by geographic regions, consisting of the United States, South America and the Caribbean, EMEA and Asia, were $19,725,646 (75.6% of net sales), $1,415,052 (5.4% of net sales), $1,363,398 (5.2% of net sales) and $3,606,668 (13.8% of net sales), respectively.

Net sales in the United States increased by $5,745,271, or 29.1%, to $25,470,917 for the six months ended December 31, 2015 from $19,725,646 for the corresponding period of 2014. The increase in net sales was primarily due to increased demand for one of the Company's products from a carrier customer. Net sales in the South American and Caribbean regions decreased by $1,315,052, or 92.9%, to $100,000 for the six months ended December 31, 2015 from $1,415,052 for the corresponding period of 2014. The decrease in net sales was primarily due to the general nature of sales in these regions, which often fluctuate significantly from period to period due to timing of orders placed by a relatively small number of customers. Net sales in EMEA increased by $5,122,043, or 375.7%, to $6,485,441 for the six months ended December 31, 2015 from $1,363,398 for the corresponding period of 2014. The increase in net sales was due to timing of orders placed by a carrier customer in Africa. Net sales in Asia decreased by $3,551,079, or 98.5%, to $55,589 for the six months ended December 31, 2015 from $3,606,668 for the corresponding period of 2014. The decrease in net sales was primarily due to lower product and component sales generated by FTI, which typically vary from period to period.

GROSS PROFIT – Gross profit increased by $322,588, or 6.7%, to $5,125,913 for the six months ended December 31, 2015 from $4,803,325 for the corresponding period of 2014. The gross profit in terms of net sales percentage was 16.0% for the six months ended December 31, 2015 compared to 18.4% for the corresponding period of 2014. The increase in gross profit was primarily due to the change in net sales as described above. The decrease gross profit in terms of net sales percentage was primarily due to variations in customer and product mix, competitive selling prices and product costs which generally vary from period to period and region to region.

OPERATING EXPENSES – Operating expenses decreased by $220,827, or 5.3%, to $3,927,860 for the six months ended December 31, 2015 from $4,148,687 for the corresponding period of 2014. The decrease was primarily due to lower share-based compensation expense, amortization and depreciation expense and expenses associated with research and development, legal and travel.

OTHER INCOME (LOSS), NET – Other income (loss), net decreased by $398,183 to ($14,520) for the six months ended December 31, 2015 from $383,663 for the corresponding period of 2014. The decrease was primarily due to expenses that were reversed associated with certain marketing related activities accrued in prior periods which expired during the six months ended December 31, 2014. During the six months ended December 30, 2015, no expenses were reversed or expired.

LIQUIDITY AND CAPITAL RESOURCES

Our historical operating results, capital resources and financial position, in combination with current projections and estimates, were considered in management's plan and intentions to fund our operations over a reasonable period of time, which we define as the twelve month period ending December 31, 2016. For purposes of liquidity disclosures, we assess the likelihood that we have sufficient available working capital and other principal sources of liquidity to fund our operating activities and obligations as they become due.

Our principal source of liquidity as of December 31, 2015 consisted of cash and cash equivalents of $14,657,624. We believe we have sufficient available capital to cover our existing operations and obligations through at least December 31, 2016. Our long-term future cash requirements will depend on numerous factors, including our revenue base, profit margins, product development activities, market acceptance of our products, future expansion plans and ability to control costs. If we are unable to achieve our current business plan or secure additional funding that may be required, we would need to curtail our operations or take other similar actions outside the ordinary course of business in order to continue to operate as a going concern.

OPERATING ACTIVITIES – Net cash provided by operating activities for the six months ended December 31, 2015 and 2014 were $3,922,235 and $3,913,584, respectively.

The $3,922,235 in net cash provided by operating activities for the six months ended December 31, 2015 was primarily due to the increase in accounts payable and the decrease in prepaid income taxes of $13,285,927 and $1,055,788, respectively, as well as our operating results (net income adjusted for depreciation, amortization and other non-cash charges), which were partially offset by the increases in accounts receivable and inventories of $9,503,740 and $2,290,408, respectively. The $3,913,584 in net cash provided by operating activities for the six months ended December 31, 2014 was primarily due to the increase in advance payments from customers and the decrease in accounts receivable of $1,566,645 and $547,471, respectively, as well as our operating results (net income adjusted for depreciation, amortization and other non-cash charges).

INVESTING ACTIVITIES – Net cash used in investing activities for the six months ended December 31, 2015 and 2014 were $822,683 and $110,908, respectively.

The $822,683 in net cash used in investing activities for the six months ended December 31, 2015 was primarily due to the payments for capitalized product development and purchases of intangible assets of $603,577 and $177,382, respectively. The $110,908 in net cash used in investing activities for the six months ended December 31, 2014 was primarily due to the payments for capitalized product development of $81,591.

FINANCING ACTIVITIES – Net cash used in financing activities for the six months ended December 31, 2015 and 2014 were $234,000 and $0, respectively. The $234,000 in net cash used in financing activities for the six months ended December 31, 2015 was due to the repurchase of 130,000 shares of our common stock from a shareholder.

CONTRACTUAL OBLIGATIONS AND OTHER COMMITMENTS

Leases

We leased approximately 11,318 square feet of office space located in San Diego, California, at a monthly rent of $16,576; although the lease expired on August 31, 2015, we continued to occupy the premises with the consent of the landlord through October 27, 2015. On September 9, 2015, we signed a lease for new office space consisting of approximately 12,775 square feet, also located in San Diego, California, at a monthly rent of $23,115, which commenced on October 28, 2015. In addition to monthly rent, the new lease includes payment for certain common area costs. The term of the lease for the new office space is four years from the lease commencement date. Our facility is covered by an appropriate level of insurance and we believe it to be suitable for our use and adequate for our present needs. Rent expense related to these leases was $70,764 and $49,728 for the three months ended December 31, 2015 and 2014, respectively, and $131,080 and $99,456 for the six months ended December 31, 2015 and 2014, respectively.

Our Korea-based subsidiary, Franklin Technology, Inc. (“FTI”), leases approximately 10,000 square feet of office space in Seoul, Korea, at a monthly rent of approximately $8,000, and the lease expires on September 1, 2017. Beginning on June 12, 2015, FTI leased additional office space consisting of approximately 2,682 square feet, also located in Seoul, Korea, at a monthly rent of approximately $2,700, and the lease expires on September 1, 2017. In addition to monthly rent, the lease provides for periodic cost of living increases in the base rent and payment for certain common area costs. These facilities are covered by an appropriate level of insurance and we believe them to be suitable for our use and adequate for our present needs. Rent expense related to these leases was approximately $32,100 and $24,000 for the three months ended December 31, 2015 and 2014, respectively, and $64,200 and $48,000 for the six months ended December 31, 2015 and 2014, respectively.

We lease one corporate housing facility for our vendors and employees who travel, under a non-cancelable operating lease that expired on September 13, 2015 and was extended to September 5, 2016. Rent expense related to this lease was $2,460 and $2,597 for the three months ended December 31, 2015 and 2014, respectively, and $4,896 and $5,380 for the six months ended December 31, 2015 and 2014, respectively.

Recently Issued Accounting Pronouncements

Refer to NOTE 3 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES in the Consolidated Financial Statements.

OFF-BALANCE SHEET ARRANGEMENTS

None.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As a “smaller reporting company,” the Company is not required to respond to this item.

ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

The Company’s President and Chief Financial Officer have concluded, based on an evaluation of the Company’s disclosure controls and procedures (as defined in the Securities Exchange Act of 1934 Rules 13a-15(e) and 15(d)-15(e)), that such disclosure controls and procedures were effective as of the end of the period covered by this report.

Changes in Internal Control Over Financial Reporting

There has been no change in the Company’s internal control over financial reporting during the three months ended December 31, 2015 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We have provided information about legal proceedings in which we are involved in Note 8 of the notes to consolidated financial statements for the six months ended December 31, 2015, contained within this Quarterly Report on Form 10-Q.

ITEM 1A. RISK FACTORS

Our Annual Report on Form 10-K for the fiscal year ended June 30, 2015, filed with the SEC on September 28, 2015 (the “Annual Report”), includes a detailed discussion of our risk factors under the heading “PART I, ITEM 1A – RISK FACTORS.” You should carefully consider the risk factors discussed in our Annual Report, as well as other information in this quarterly report. Any of these risks could cause our business, financial condition, results of operations and future growth prospects to suffer. We are not aware of any material changes from the risk factors previously disclosed.

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

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

None.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURES

In accordance with Section 13 of 15(d) of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Franklin Wireless Corp.

By: /s/ OC Kim
OC Kim

President

(Principal Executive Officer)

By: /s/ Richard T. Walker
Richard T. Walker

Chief Financial Officer

(Principal Financial Officer)

Dated: February 16, 2016