ALTERNET SYSTEMS INC
Form 10-Q
November 14, 2014

# UNITED STATES
# SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

# FORM 10-Q

[X] Quarterly report pursuant section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended **September 30, 2014**

[ ] Transition report pursuant section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from ________________to ________________

Commission file number **000-31909**

# ALTERNET SYSTEMS, INC.

(Exact name of registrant as specified in its charter)

| | |
|---|---|
| **Nevada** | **88-0473897** |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |
| **2665 S Bayshore Drive Miami FL** | **33133** |
| (Address of principal executive offices) | (Zip Code) |

Registrant's telephone number, including area code: **786-265-1840**

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 last 90 days.
Yes [X] No [ ]

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

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

Large accelerated filer [ ]          Accelerated filer [ ]

Non-accelerated filer [ ]                    Smaller reporting company [X]

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

Indicate the number of shares outstanding of each of the registrant s classes of common stock as of the latest practicable date.

**98,233,064 as of September 30, 2014**

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## PART I FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS.

## ALTERNET SYSTEMS INC.

## CONSOLIDATED FINANCIAL STATEMENTS

**SEPTEMBER 30, 2014**
**UNAUDITED**

**ALTERNET SYSTEMS INC.**
**CONDENSED CONSOLIDATED BALANCE SHEETS**
**As at September 30, 2014 and December 31, 2013**

| | September 30, 2014 (Unaudited) | December 31, 2013 |
|---|---|---|
| | $ | $ |
| **ASSETS** | | |
| | | |
| **Current Assets** | | |
| Cash | 6,235 | - |
| Sale proceeds held in escrow | 667,264 | - |
| Deposits and other assets | 2,000 | 21,785 |
| Investment in digital currency | 122,671 | - |
| Current assets of discontinued operations | - | 2,048,824 |
| **Total current assets** | 798,170 | 2,070,609 |
| **Fixed assets, net** | - | 2,733 |
| | | |
| **TOTAL ASSETS** | **798,170** | **2,073,342** |
| | | |
| **LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIENCY)** | | |
| | | |
| **Current liabilities** | | |
| Checks issued in excess of bank balance | - | 168 |
| Accounts payable and accrued charges | 1,907,213 | 1,466,546 |
| Wages payable | 770,101 | 1,672,273 |
| Accrued payroll taxes | 171,427 | 1,671,353 |
| Deferred gain on sale | 667,264 | - |
| Other loans payable, net of beneficial conversion feature | 848,679 | 1,543,509 |
| Due to related parties | 65,668 | 102,464 |
| Current liabilities of discontinued operations | - | 783,145 |
| **Total current liabilities** | 4,430,352 | 7,239,458 |
| **Long term debt** | - | 312,667 |
| | 4,430,352 | 7,552,125 |
| **Stockholders' equity (deficiency)** | | |
| | | |
| Capital stock Authorized: 500,000,000 common stock with a par value of $0.00001 | 982 | 957 |
| Issued and outstanding: 98,233,055 common shares (2013 - 95,737,389) | | |
| Additional paid-in capital | 14,736,385 | 14,453,693 |
| Private placement subscriptions | 630,362 | 130,362 |
| Share subscription receivable | (375,000) | - |
| Obligation to issue shares | - | 2,800 |
| Deferred compensation | - | (113,125) |
| Accumulated other comprehensive income | (331,411) | (331,332) |
| Accumulated deficit | (18,293,500) | (17,939,881) |
| | (3,632,182) | (3,796,526) |

| | | |
|---|---|---|
| Non-controlling interest | - | (1,682,257) |
| | (3,632,182) | (5,478,783) |
| | | |
| **TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIENCY)** | **798,170** | **2,073,342** |

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

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**ALTERNET SYSTEMS INC.**
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**
**(Unaudited)**

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| | **2014** | **2013** | **2014** | **2013** |
| | $ | $ | $ | $ |
| **REVENUE** | - | 1,501 | - | 3,142 |
| **OPERATING EXPENSES** | | | | |
| Bad debts | - | 5,875 | - | 7,646 |
| Depreciation | - | 283 | 2,733 | 847 |
| Investor relations | 11,745 | 32,441 | 97,680 | 91,696 |
| Research and development | - | - | 500,000 | - |
| Management and consulting | 174,800 | 22,103 | 645,125 | 548,626 |
| Office and general | 32,536 | 10,468 | 122,347 | 35,004 |
| Professional fees | 52,183 | 14,987 | 270,078 | 183,929 |
| Rent | 6,784 | 8,038 | 20,772 | 26,086 |
| Payroll (recovery), net | (62,521) | 325,092 | (206,060) | 513,075 |
| Travel | 812 | 1,748 | 86,416 | 18,103 |
| | 216,339 | 421,035 | 1,539,091 | 1,425,011 |
| **NET LOSS BEFORE OTHER ITEMS** | (216,339) | (419,534) | (1,539,091) | (1,421,869) |
| **OTHER ITEMS** | | | | |
| Interest expense, net | (24,688) | (83,245) | (81,491) | (319,858) |
| Gain on foreign exchange | 31,654 | 5,984 | 32,486 | 54,931 |
| Unrealized loss on investment | (2,329) | - | (2,329) | - |
| Forgiveness and adjustment of accounts payable | - | 18,425 | - | 18,425 |
| | 4,637 | (58,836) | (51,334) | (246,502) |
| **NET LOSS FROM CONTINUING OPERATIONS** | (211,702) | (478,370) | (1,590,425) | (1,668,371) |
| **NON-CONTROLLING INTEREST FROM CONTINUING OPERATIONS** | 34,311 | (9,174) | 21,693 | (11,650) |
| **NET LOSS ATTRIBUTABLE TO ALTERNET SYSTEMS INC. FROM CONTINUING OPERATIONS** | (246,013) | (469,196) | (1,612,118) | (1,656,721) |
| **DISCONTINUED OPERATIONS** | 14,394 | (383,152) | 3,006,931 | (1,088,203) |

| | | | | |
|---|---|---|---|---|
| **TOTAL NET AND COMPREHENSIVE INCOME (LOSS) ATTRIBUTABLE TO ALTERNET SYSTEMS INC.** | **(231,619)** | **(852,348)** | **1,394,813** | **(2,744,924)** |

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

**ALTERNET SYSTEMS INC.**
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**
**(Unaudited)**

| | Nine months ended September 30, 2014 | 2013 |
|---|---|---|
| | $ | $ |
| **OPERATING ACTIVITIES** | | |
| Net income (loss) attributable to Alternet Systems Inc. | 1,394,813 | (2,744,924) |
| Non-controlling interest | 21,693 | (11,650) |
| Add items not affecting cash | | |
| Depreciation | 2,733 | 847 |
| Interest accrued | 34,234 | 175,009 |
| Bad debt expense | - | 7,646 |
| Shares for services | 249,917 | 253,041 |
| Unrealized loss on investments | 2,329 | - |
| Accretion of debt discount | - | 143,590 |
| Unrealized foreign exchange gain | (32,174) | (131,707) |
| Deferred compensation | 143,125 | 65,625 |
| Changes in non-cash working capital: | | |
| Accounts receivable | - | 11,587 |
| Deposits and other assets | 19,785 | - |
| Accounts payable and accrued charges | 440,667 | 671,552 |
| Wages payable | (786,380) | 814,619 |
| Accrued taxes | (1,499,926) | 735,276 |
| Due to related parties | (4,622) | 53,883 |
| Net cash (used in) provided by operating activities | (13,806) | 44,394 |
| | | |
| **FINANCING ACTIVITIES** | | |
| Proceeds from loans payable | 400,000 | 363,000 |
| Payments on loans payable | (1,129,064) | (54,338) |
| Payments on long term debt | (312,667) | - |
| Checks issued in excess of bank balance | (168) | (3,713) |
| Share issue costs | - | (21,000) |
| Net cash (used in) provided by financing activities | (1,041,899) | 283,949 |
| | | |
| **EFFECT OF EXCHANGE RATES ON CASH** | (79) | (23) |
| | | |
| **CASH FLOWS FROM CONTINUING OPERATIONS** | (1,055,783) | 328,320 |
| **CASH FLOWS FROM DISCONTINUED OPERATIONS** | 1,062,019 8 | (327,228) |
| **NET INCREASE IN CASH DURING THE PERIOD** | 6,235 | 1,092 |
| | | |
| **CASH, BEGINNING OF PERIOD** | - | - |
| | | |
| **CASH, END OF PERIOD** | **6,235** | **1,092** |

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

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**ALTERNET SYSTEMS INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**September 30, 2014**
**(Unaudited)**

## NOTE 1 NATURE OF OPERATIONS AND BASIS OF PRESENTATION

Alternet Systems Inc., through its subsidiaries ( Alternet or the Company ), plans to enter the digital currency space and provide end to end security for digital currencies, launch its digital currency bank, fully compliant with government regulations, foreign exchange capabilities, offer micro payment services to the unbanked and global diasporas, and alternative financial services to the retail industry emerging markets. Previously, the Company provided leading edge mobile financial solutions and mobile security and related solutions with the former being offered throughout the Western Hemisphere, but most actively in Central and South America and the Caribbean, and the latter being offered globally. As detailed in Note 7, Discontinued Operations, the Company, pursuant to the ATS Transaction, discontinued providing mobile financial solutions and mobile security.

These condensed consolidated financial statements have been prepared on the basis of a going concern, which contemplates the realization of assets and satisfaction of liabilities in the normal course of business. At September 30, 2014 the Company had a working capital deficiency of $3,632,182. The Company s continued operations are dependent on the successful implementation of its business plan, its ability to obtain additional financing as needed, continued support from creditors, settling its outstanding debts, and ultimately attaining profitable operations. The accompanying condensed consolidated financial statements do not include any adjustments that might be necessary if the Company is unable to continue as a going concern.

## NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### Interim Financial Statements

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America (GAAP) for interim financial information and the instructions to Form 10-Q and Rule 10-01 of Regulation S-X of the Securities and Exchange Commission (the SEC ). In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair statement of the results for interim periods have been included. Results for interim periods should not be considered indicative of results for a full year. These interim condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto contained in the company s Annual Report on Form 10-K/A for the year ended December 31, 2013, filed with SEC on June 17, 2014. The consolidated financial statements include the accounts of the Company and all of its subsidiaries in which a controlling interest is maintained.

### Principles of Consolidation

These condensed consolidated financial statements include the accounts of the following companies:

- Alternet Systems Inc.
- AI Systems Group, Inc., a wholly owned subsidiary of Alternet
- Tekvoice Communications, Inc., a wholly owned subsidiary of Alternet
- Alternet Transactions Systems, Inc. ( ATS ), a wholly owned subsidiary of Alternet (formerly a 51% owned subsidiary. See Note 7, Discontinued Operations)
- Utiba Guatemala, S.A., a wholly-owned subsidiary of Alternet Transactions Systems Inc.
- International Mobile Security ( IMS ), Inc, a wholly owned subsidiary of Alternet (formerly a 60% owned subsidiary)

- Megatecnica, S.A., a wholly owned subsidiary of International Mobile Security, Inc.
- OneMarket, Inc., a wholly owned subsidiary of Alternet
- Alternet Payment Solutions, LLC, a wholly owned subsidiary of Alternet.

The minority interests of ATS, IMS, and ATS s and IMS s wholly owned subsidiaries have been deducted from earnings and equity. All significant intercompany transactions and account balances have been eliminated.

**ALTERNET SYSTEMS INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**September 30, 2014**
**(Unaudited)**
**NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**Use of Estimates and Assumptions**

The preparation of financial statements in conformity with generally accepted accounting principles 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 financial statement date and the reported amounts of revenues and expenses during the reporting period. The Company regularly evaluates estimates and assumptions related to the useful life and recoverability of long-lived assets, fair value of convertible notes payable and derivative liabilities. The Company bases its estimates and assumptions on current facts, historical experience and various other factors that it believes to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities and the accrual of costs and expenses that are not readily apparent from other sources. The actual results experienced by the Company may differ materially and adversely from the Company s estimates. To the extent there are material differences between estimates and the actual results, future results of operations will be affected.

**Revenue Recognition**

Up to March 4, 2014, the Company entered into sales arrangements that may have provided for multiple deliverables to a customer. Software sales may have included the sale of a software license, implementation/customization services, and/or ongoing support services.

In order to treat deliverables in a multiple-deliverable arrangement as separate units of accounting, the deliverables must have standalone value upon delivery. If the deliverables have standalone value upon delivery, the Company accounts for each deliverable separately. Licenses, support fees, and hosted services have standalone value as such services are often sold separately. In determining whether implementation/customization services have standalone value, the Company considers the following factors for each agreement: availability of the services from other vendors, the nature of the services, the timing of when the services contract was signed in comparison to the services start date, and the contractual dependence of the customization service on the customer s satisfaction with the implementation/customization services work.

The Company concluded that all of the services included in multiple-deliverable arrangements executed had standalone values when multiple deliverables included in an arrangement are separated into different units of accounting. The arrangement consideration is allocated to the identified separate units based on a relative selling price hierarchy. The Company determines the relative selling price for a deliverable based on its vendor-specific objective evidence of selling price ( VSOE ), if available, or its best estimate of selling price ( BESP ), if VSOE is not available. The Company has determined that third-party evidence of selling price ( TPE ) is not a practical alternative due to differences in its service offerings compared to other parties and the availability of relevant third party pricing information. The amount of revenue allocated to delivered items is limited by contingent revenue, if any.

The Company has not established VSOE for a majority of its revenue due to lack of pricing consistency, the customer specific requests, and other factors. Accordingly, the Company used its BESP to determine the relative selling price.

The Company determined BESP by considering its overall pricing objectives and market conditions. Significant pricing practices taken into consideration include the Company s discounting practices, the size and volume of the Company s transactions, the geographic area where services are sold, its market strategy, historic contractually stated prices and prior relationships, and future service sales with certain customers. The determination of BESP is made through consultation with and approval by the Company s management, taking into consideration the market strategy. As the Company s market strategies evolve, the Company may modify its pricing practices in the future, which could result in changes in selling prices.

Revenue was recognized upon delivery or when services were performed, provided that persuasive evidence of a sales arrangement existed, both title and risk of loss passed to the customer, and collection was reasonably assured. Persuasive evidence of a sales arrangement existed upon execution of a written sales agreement or signed purchase order that constituted a fixed and legally binding commitment between the Company and the buyer. Specifically, revenue from the sale of licenses was recognized when the title of the license transferred to the customer while revenue from implementation/customization services performed was recognized upon successful completion of a User Acceptance Test ( UAT ). If a successful UAT was never achieved and the sales arrangement was cancelled, the Company recognized any deferred revenue not required to be refunded to the customer.

**ALTERNET SYSTEMS INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**September 30, 2014**
**(Unaudited)**
**NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**Revenue Recognition (continued)**

The Company s payment terms vary by client. To reduce credit risk in connection with software license and support sales, the Company may, depending upon the circumstances, require significant deposits prior to delivery. In some circumstances, the Company may require payment in full for its products prior to delivery. For support and hosted services, the Company sold customers service agreements that were recorded as deferred revenue and provided for payment in advance on either an annual or other periodic basis. Revenue for these support services was recognized ratable over the term of the agreement.

Subsequent to March 4, 2014 the Company implemented the criteria outlined in SAB 104 and recognizes revenue when:

- persuasive evidence of an arrangement exists;
- delivery has occurred or services have been rendered;
- the seller s price to the buyer is fixed or determinable; and
- collectability is reasonably assured.

**Research and Development**

The Company expenses costs when incurred for items associated with researching and developing new sources of revenue.

**Digital Currency Transactions**

The Company enters into transactions that are denominated in digital currency (Ven). These transactions result in digital currency denominated assets and liabilities that are revalued periodically. Upon revaluation, transaction gains and losses are generated and are reported as unrealized gains and losses in other gain (loss), net in the Condensed and Consolidated Statements of Operations. The Company determines fair value as of the balance sheet date based on Level I inputs which consist of quoted prices in active markets. The value of the Company s digital currency is $122,671, net of $2,329 of unrealized losses, as of September 30, 2014. Due to the uncertainty regarding the current and future accounting treatment and tax, legal and regulatory requirements relating to digital currencies or transactions utilizing digital currencies, such accounting, legal, regulatory and tax developments or other requirements may adversely affect us.

**Long-Lived Assets Including Other Acquired Intellectual Property**

Management monitors the recoverability of long-lived assets and intangibles based on estimates using factors such as current market value, future asset utilization, and future undiscounted cash flows expected to result from its investment or use of the related assets. The Company s policy is to record any impairment loss in the period when it the Company determines that the carrying amount of the asset may not be recoverable. Any impairment loss is calculated as the excess of the carrying value over estimated realizable value. The Company did not record any significant impairments on long-lived assets during the nine months ended September 30, 2014 and 2013. Intangible assets deemed to have an indefinite life are not amortized but are subject to impairment tests at each reporting date. The Company assesses the impairment of intangible assets on a quarterly basis or whenever events or changes in circumstances indicate that the fair value is less than its carrying value. If the carrying amount of the intangible asset exceeds its fair value, the intangible asset is considered impaired and the second step of the test is performed to determine the amount of impairment loss, if any. The Company did not recognize any impairment charges related to indefinite lived intangible assets during the nine months ended September 30, 2014 and 2013.

**Income (Loss) per Share**

The Company computes net income (loss) per share in accordance with ASC Topic 260, *Earnings Per Share*. Topic 260 requires presentation of both basic and diluted earnings per share (EPS). Basic EPS is computed by dividing net income (loss) available to common shareholders (numerator) by the weighted average number of common shares outstanding (denominator) during the period. Diluted EPS gives effect to all dilutive potential common shares outstanding during the period including warrants using the treasury stock method. Diluted EPS excludes all dilutive potential common shares if their effect is anti-dilutive.

At September 30, 2014 and December 31, 2013 the Company had no warrants or options outstanding to consider in the income (loss) per share calculations.

**ALTERNET SYSTEMS INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**September 30, 2014**
**(Unaudited)**
**NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**Stock-Based Compensation**

The Company accounts for its share-based compensation plans in accordance with the fair value recognition provisions of ASC 718 *Compensation-Stock Compensation*. The Company utilizes the Black-Scholes option pricing model as its method for determining the fair value of stock option grants. ASC 718 requires the fair value of all share-based awards that are expected to vest to be recognized in the statements of operations over the service or vesting period of each award. The Company uses the straight-line method of attributing the value of share-based compensation expense for all stock option grants over the requisite service period.

**Reclassification**

Certain comparative figures have been reclassified in order to conform to the current year s presentation.

**Recent Accounting Pronouncements**

In April 2014, the FASB issued ASU No. 2014-08, *Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity*. This ASU is to be applied prospectively for all disposals of an entity that occur within annual periods beginning on or after December 15, 2014, and interim periods beginning on or after December 15, 2015. Additionally, this ASU is to be applied to all business activated that, on acquisition, are classified as held for sale that occur within annual periods beginning on or after December 15, 2014, and interim periods within annual periods beginning on or after December 15, 2015. ASU No 2014-08 addresses concerns about the accounting for discontinued operations and the disposal of small groups of assets that are recurring in nature but qualify as discontinued operations under subtopic 205-20 Management does not anticipate that this accounting pronouncement will have any material future effect on our consolidated financial statements.

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606).* This ASU is effective for annual reporting periods beginning after December 15, 2016. ASU No 2014-09 addresses concerns about weaknesses and inconsistencies in revenue recognition across entities, industries, jurisdictions, and capital markets. Management does not anticipate that this accounting pronouncement will have any material future effect on our consolidated financial statements.

In June 2014, the FASB issued ASU No. 2014-12, *Compensation - Stock Compensation (Topic 718): Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period.* This ASU is effective for annual reporting periods beginning after December 15, 2015. ASU No 2014-12 clarifies the diverse accounting treatments used by entities to account for awards based on performance targets achieved after the requisite period. Management does not anticipate that this accounting pronouncement will have any material future effect on our consolidated financial statements.

In August 2014, the FASB issued ASU No. 2014-15, *Presentation of Financial Statements Going Concern (Topic 205): Disclosure of Uncertainties about an Entity s Ability to Continue as a Going Concern* This ASU is effective for annual reporting periods ending after December 15, 2016. ASU No 2014-15 provides guidance about management s responsibility to evaluate whether there is substantial doubt about an entity s ability to continue as a going concern and to provide related footnote disclosures. Management does not anticipate that this accounting pronouncement will have any material future effect on our consolidated financial statements. Other recent accounting pronouncements issued by the FASB (including its Emerging Issues Task Force), the American Institute of Certified Public Accountants, and the SEC did not, or are not believed by management to, have a material impact on the Company's present or future financial position, results of operations or cash flows.

**ALTERNET SYSTEMS INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**September 30, 2014**
**(Unaudited)**
**NOTE 3 FIXED ASSETS**

| | | **September 30, 2014** | |
|---|---|---|---|
| | Cost | Accumulated Depreciation | Net Book Value |
| | $ | **$** | **$** |
| Computer equipment | 320,933 | 320,933 | **-** |
| Computer software | 75,128 | 75,128 | **-** |
| Equipment | 10,576 | 10,576 | **-** |
| | | | |
| | 406,637 | 406,637 | **-** |

| | | **December 31, 2013** | |
|---|---|---|---|
| | Cost | Accumulated Depreciation | Net Book Value |
| | $ | **$** | **$** |
| Computer equipment | 320,933 | 319,700 | **1,233** |
| Computer software | 75,128 | 73,866 | **1,262** |
| Equipment | 10,576 | 10,338 | **238** |
| | | | |
| | 406,637 | 403,904 | **2,733** |

Depreciation expense for the nine months ended September 30, 2014 and 2013 was $2,733 and $847, respectively.

**NOTE 4 - CONVERTIBLE DEBENTURE NOTES AND OTHER LOANS PAYABLE**

**Convertible Debentures**

On August 29, 2012, the Company issued a note payable in the amount of $44,438. The note carries interest at the rate of 10% per annum and was due on February 28, 2013. Since the note was not repaid on maturity, the holder is entitled to convert all or any portion of the original principal face value of the note into shares of common stock of the Company at a conversion value of $0.075. The beneficial conversion feature discount resulting from the conversion price being $0.045 below the market price on August 29, 2012 of $0.12 provided a value of $26,663. During the nine months ended September 30, 2014, $Nil (September 30, 2013 $8,596) of the debt discount was amortized. As of September 30, 2014, $53,374 (December 31, 2013 - $50,051) of principal and accrued interest was included in other loans payable. The note is past due and continues to accrue interest at the rate of 10% per annum.

On September 26, 2012, the Company issued a note payable in the amount of $60,000. The note carries interest at the rate of 10% per annum and was due on March 31, 2013. Since the note was not repaid on maturity, the holder is entitled to convert all or any portion of the original principal face value of the note into shares of common stock of the Company at a conversion value of $0.075. The beneficial conversion feature discount resulting from the conversion price being $0.045 below the market price on September 26, 2012 of $0.12 provided a value of $36,000. During the nine months ended September 30, 2014, $Nil (September 30, 2013 - $17,419) of the debt discount was amortized. As of September 30, 2014, $71,605 (December 31, 2013 - $67,118) of principal and accrued interest was included in other loans payable. The note is past due and continues to accrue interest at the rate of 10% per annum.

On October 19, 2012, the Company issued a note payable in the amount of $80,000. The note carries interest at the rate of 10% per annum and was due on April 30, 2013. Since the note was not repaid on maturity, the holder is entitled to convert all or any portion of the original principal face value of the note into shares of common stock of the Company at a conversion value of $0.075. The beneficial conversion feature discount resulting from the conversion price being $0.085 below the market price on October 19, 2012 of $0.16 provided a value of $80,000. During the nine months ended September 30, 2014, $Nil (September 30, 2013 - $49,741) of the debt discount was amortized. As of September 30, 2014, $94,970 (December 31, 2013 - $88,986) of principal and accrued interest was included in other loans payable. The note is past due and continues to accrue interest at the rate of 10% per annum.

**ALTERNET SYSTEMS INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**September 30, 2014**
**(Unaudited)**
**NOTE 4 - CONVERTIBLE DEBENTURE NOTES AND OTHER LOANS PAYABLE (continued)**

**Convertible Debentures**

On January 25, 2013, the Company issued a note payable in the amount of $80,000. The note carries interest at the rate of 10% per annum and was due on October 22, 2013. Since the note was not repaid on maturity, the holder is entitled to convert all or any portion of the original principal face value of the note into shares of common stock of the Company at a conversion value of $0.075. The beneficial conversion feature discount resulting from the conversion price being $0.055 below the market price on January 25, 2013 of $0.13 provided a value of $58,667. During the nine months ended September 30, 2014, $Nil (September 30, 2013 - $53,886) of the debt discount was amortized. As of September 30, 2014, $93,458 (December 31, 2013 - $87,474) of principal and accrued interest was included in other loans payable. The note is past due and continues to accrue interest at the rate of 10% per annum.

On April 24, 2013, the Company issued a note payable in the amount of $50,000. The note carries interest at the rate of 10% per annum and was due on October 31, 2013. Since the note was not repaid on maturity, the holder is entitled to convert all or any portion of the original principal face value of the note into shares of common stock of the Company at a conversion value of $0.075. The beneficial conversion feature discount resulting from the conversion price being $0.025 below the market price on April 24, 2013 of $0.10 provided a value of $16,667. During the nine months ended September 30, 2014, $Nil (September 30, 2013 - $13,947) of the debt discount was amortized. As of September 30, 2014, $57,192 (December 31, 2013 - $53,452) of principal and accrued interest was included in other loans payable. The note is past due and continues to accrue interest at the rate of 10% per annum.

**Other Loans Payable**

On January 25, 2011, the Company signed a promissory note whereby the Company agreed to repay a director $20,000 plus interest at 10% per annum on April 25, 2011. This loan was not repaid on its maturity and has since been renewed several times with the unpaid principal and interest being capitalized to the loan balance on each renewal. On July 1, 2013, the director combined this loan with a total unpaid principal and interest balance of $2,864 with two other matured loans and extended the maturity date to December 29, 2013. All other terms remained the same. The combined loan was paid in full on September 22, 2014.

On February 9, 2011, the Company signed a promissory note whereby the Company agreed to repay a director $5,000 plus interest at 10% per annum on May 9, 2011. This loan was not repaid on its maturity and has since been renewed several times with the unpaid principal and interest being capitalized to the loan balance on each renewal. On July 1, 2013, the director combined this loan with a total unpaid principal and interest balance of $6,324 with two other matured loans and extended the maturity date to December 29, 2013. All other terms remained the same. The combined loan was paid in full on September 22, 2014.

On February 11, 2011, the Company signed a promissory note whereby the Company agreed to repay a director $8,988 plus interest at 10% per annum on May 11, 2011. This loan was not repaid on its maturity and has since been renewed several times with the unpaid principal and interest being capitalized to the loan balance on each renewal. On July 1, 2013, the director combined this loan with a total unpaid principal and interest balance of $11,365 with two other matured loans and extended the maturity date to December 29, 2013. All other terms remained the same. The combined loan was paid in full on September 22, 2014.

On July 1, 2013, the above three promissory notes to one director of the Company were combined which capitalized the unpaid principal and interest on the three separate promissory notes totaling $20,553 into one promissory note and extended the maturity date to December 29, 2013. All other terms remained the same. In April 2014, the note was renewed retroactively from December 29, 2013 until December 29, 2014 which included interest of $1,025 being capitalized to the principal. As of September 30, 2014, the Company has accrued $Nil (December 31, 2013 - $1,036) of interest relating to this loan. On September 22, 2014, the Company paid the director $23,156 as full repayment of the loan.

On February 1, 2012, the Company signed a promissory note whereby the Company agreed to repay a creditor $200,000 plus interest at 24% per annum on May 1, 2012. On May 1, 2012, the Company signed a new promissory note with the creditor which capitalized the unpaid principal and interest of $211,836 under the previous promissory note and extended the maturity date to September 30, 2012. On October 1, 2012, the Company signed a new promissory note with the creditor which capitalized the unpaid principal and interest of $233,147 under the previous promissory note and extended the maturity date to January 31, 2013. The note was not repaid by January 31, 2013; as a result, $18,856 of unpaid interest was capitalized to the principal resulting in a total principal balance outstanding of $252,003 which is incurring a late payment charge of 0.10% per day on any unpaid balances. As of December 31, 2013, the Company had accrued $75,507 of late payment charges which was included in the outstanding principal and interest balance of $309,274. On March 6, 2014, the Company paid the creditor $293,480 as full repayment of the loan and realized a gain of $15,794 which was recorded against interest expense.

**ALTERNET SYSTEMS INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**September 30, 2014**
**(Unaudited)**
**NOTE 4 - CONVERTIBLE DEBENTURE NOTES AND OTHER LOANS PAYABLE (continued)**

**Other Loans Payable (continued)**

On October 10, 2012, the Company signed a promissory note whereby the Company agreed to repay a creditor $50,000 plus interest at 10% per annum on April 8, 2013. On April 9, 2013, the Company signed a new promissory note with the creditor which capitalized the unpaid principal and interest of $52,479 under the previous promissory note and extended the maturity date to October 6, 2013. The note was not repaid by October 6, 2013 and continues to accrue interest at the rate of 10% per annum. As of September 30, 2014, the Company has accrued $7,764 (December 31, 2013 - $3,839) of interest relating to this loan.

On November 19, 2012, the Company signed a promissory note whereby the Company agreed to repay a creditor $100,000 plus interest at 10% per annum on May 18, 2013. The loan was not repaid by its maturity date; as such, a late payment charge is being accrued on the unpaid principal and interest of $104,959. On December 9, 2013, the Company paid the creditor $15,000 towards the late payment charges. As of December 31, 2013, the Company had accrued $13,260 of interest relating to this loan. On March 6, 2014, the Company paid the creditor $119,059 as full repayment of the loan.

On November 19, 2012, the Company signed a promissory note whereby the Company agreed to repay a creditor $100,000 plus interest at 10% per annum on May 18, 2013. The loan was not repaid by May 18, 2013 and continues to accrue interest at the rate of 10% per annum. On July 24, 2013, the creditor combined this loan with another matured loan and extended the maturity date to January 20, 2014. All other terms remained the same. Refer to the promissory note dated July 24, 2013 for further details. The combined loan was repaid in full on March 6, 2014.

On December 5, 2012, the Company signed a promissory note whereby the Company agreed to repay a creditor $25,000 plus interest at 10% per annum on June 3, 2013. On June 3, 2013, the Company signed a new promissory note with the creditor which capitalized the unpaid principal and interest of $26,240 under the previous promissory note and extended the maturity date to December 1, 2013. The note was not repaid by December 1, 2013 and continues to accrue interest at the rate of 10% per annum. As of September 30, 2014, the Company has accrued $3,479 (December 31, 2013 - $1,517) of interest relating to this loan.

On January 24, 2013, the Company signed a promissory note whereby the Company agreed to repay a creditor $50,000 plus interest at 10% per annum on July 23, 2013. On July 24, 2013, the creditor combined this loan with another matured loan and extended the maturity date to January 20, 2014. All other terms remained the same. Refer to the promissory note dated July 24, 2013 for further details. The combined loan was repaid on March 6, 2014.

On February 8, 2013, the Company signed a promissory note whereby the Company agreed to repay a creditor $100,000 plus interest at 10% per annum on August 7, 2013. This loan was not repaid on its maturity and has since been renewed several times with the unpaid principal and interest being capitalized to the loan balance on each renewal. All other terms remained the same. The loan matures on February 4, 2015. As of September 30, 2014, Company has accrued $7,183 (December 31, 2013 - $4,198) of interest on a principal balance of $110,164 (December 31, 2013 - $104,959).

On February 19, 2013, the Company signed a promissory note whereby the Company agreed to repay a creditor $33,000 plus interest at 10% per annum on May 20, 2013. The loan was not repaid by May 18, 2013 and continued to accrue interest at the rate of 10% per annum. On July 17, 2013, the Company paid the creditor $34,338 resulting in a full repayment of the loan.

On February 28, 2013, the Company signed a promissory note whereby the Company agreed to repay a creditor $50,000 plus interest at 10% per annum on August 27, 2013. This loan was not repaid on its maturity and has since been renewed several times with the unpaid principal and interest being capitalized to the loan balance on each renewal. All other terms remained the same. The loan matures on February 25, 2015. On June 11, 2014, the Company paid the creditor $50,000 of which $1,600 was applied to the accrued interest and $48,400 was applied to the principal outstanding. As of September 30, 2014, Company has accrued $298 (December 31, 2013 - $1,812) of interest on a principal balance of $6,682 (December 31, 2013 - $52,479).

On July 24, 2013, the Company signed a new promissory note with a creditor which capitalized the unpaid principal and interest on two separate loans totaling $164,295 under previous promissory notes and extended the maturity date to January 20, 2014. The note was not repaid by January 20, 2014 and continued to accrue interest at the rate of 10% per annum. As of December 31, 2013, the Company has accrued $7,247 of interest relating to this loan. On March 6, 2014, the Company paid the creditor $174,468 as full repayment of the loan.

**ALTERNET SYSTEMS INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**September 30, 2014**
**(Unaudited)**
**NOTE 4 - CONVERTIBLE DEBENTURE NOTES AND OTHER LOANS PAYABLE (continued)**

**Other Loans Payable (continued)**

On October 15, 2013, the Company signed a new promissory note with a creditor for a total of $500,000 which was disbursed to the Company in three tranches: Tranche A - $200,000 (received in November 2013); Tranche B - $150,000 (received in December 2013); and Tranche C - $150,000 (received in January 2014). The note had a maturity date of April 15, 2014 and bears interest at 5% per annum. In the event of default, the creditor is able to convert the unpaid principal and interest into common shares of ATS as is required in order for the shareholding of the creditor, when added to the 49% shareholding of Utiba, be equal to 52.57% of the entire issued share capital of ATS. As of December 31, 2013, the balance on the loan was $351,382 which includes $1,382 of accrued interest. On March 6, 2014, the Company paid the creditor $505,063 as full repayment of the loan.

On July 24, 2014, the Company signed a promissory note whereby the Company agreed to repay a creditor $250,000 plus interest at 10% per annum on January 24, 2015. As of September 30, 2014, Company has accrued $11,342 of interest.

**NOTE 5 LONG-TERM DEBT**

On August 5, 2013, the Company signed a new promissory note with a creditor for a total of $550,000 which was to be disbursed to the Company in three tranches: Tranche A - $100,000 (received in June 2013); Tranche B - $200,000 by August 31, 2013 (received $100,000 in August 2013 and $100,000 in September 2013); and Tranche C - $250,000 by September 30, 2013 (outstanding as it has not yet been received by the Company). The note had a maturity date of December 31, 2015 and bears interest at 10% per annum with 5% per annum being capitalized to the loan and 5% per annum being payable in cash at each disbursements respective anniversary date. In the event of default, the creditor is able to convert the unpaid principal and interest into common shares of ATS at two times the principal amount outstanding with an exercise price being equal to ATS s capital stock and paid in capital for the month immediately prior to the Event of Default divided by the total outstanding shares of ATS of the same month. As of December 31, 2013, the balance on the loan was $312,667 which included $12,667 of accrued interest. On March 6, 2014, the Company paid the creditor $318,084 as full repayment of the loan.

**NOTE 6 CAPITAL STOCK**

On September 25, 2014 the Company s Shareholders approved amending the Company s Articles of Incorporation to increase its authorized capital stock to 510,000,000 shares of which 500,000,000 shared are common stock and 10,000,000 sharesare preferred stock.

**Common Stock**

The Company is authorized to issue up to 500,000,000 shares of the Company s common stock with a par value of $0.00001. During the nine months ended September 30, 2014, the Company:

- issued 2,495,666 common shares valued at $252,717 for legal, consulting, and investor relations services rendered;
- issued 1,000,000 common shares valued at $80,000 for consulting services to be rendered over a twelve month period which were included in deferred compensation (see Note 9); and

- cancelled 1,000,000 common shares valued at $50,000 previously issued for investor relations to be released upon achieving certain benchmarks which were included in deferred compensation (see Note 9).

During the year ended December 31, 2013, the Company:

- issued 1,140,590 common shares valued at $145,388 for employment incentives in accordance with employment agreements;
- issued 2,840,596 common shares valued at $199,048 for legal, consulting, and investor relations services rendered;
- issued 700,000 common shares valued at $105,000 for investor relations to be rendered over a twelve month period which were included in deferred compensation (See Note 9); and
- issued 2,000,000 common shares valued at $100,000 for investor relations to be released upon achieving certain benchmarks which were included in deferred compensation (See Note 9).

**ALTERNET SYSTEMS INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**September 30, 2014**
**(Unaudited)**
**NOTE 6 CAPITAL STOCK (continued)**

As of September 30, 2014, the Company had $630,362 (December 31, 2013 - $130,362) in private placement subscriptions which are reported as private placement subscriptions within stockholders deficit.

**Preferred Stock**

The Company is authorized to issue up to 10,000,000 shares of the Company s preferred stock with a par value of $0.00001.

**Income (Loss) Per Share**

For the nine months ended September 30, 2014 and 2013, the Company had a weighted average of 97,124,452 and 90,646,892 common shares outstanding, respectively, resulting in basic and diluted net and comprehensive loss per common share from continuing operations of $(0.02) (September 30, 2013 - $(0.02)), basic and diluted net and comprehensive income (loss) per common share from discontinued operations of $0.03 (September 30, 2013 $(0.01)), and basic and diluted net and comprehensive income (loss) per common share of $0.01 (September 30, 2013 - $(0.03)) .

For the three months ended September 30, 2014 and 2013, the Company had a weighted average of 99,202,417 and 91,360,926 common shares outstanding, respectively, resulting in basic and diluted net and comprehensive loss per common share from continuing operations of $(0.00) (September 30, 2013 - $(0.01)), basic and diluted net and comprehensive income (loss) per common share from discontinued operations of $0.00 (September 30, 2013 $(0.00)), and basic and diluted net and comprehensive loss per common share of $(0.00) (September 30, 2013 - $(0.01)) .

**Stock Options and Restricted Stock**

Effective July 17, 2014, the Company adopted the 2014 Equity Incentive Plan (the Plan ) for the purpose of providing the Company with the means to compensate, in the form of common stock of the Company, directors, officer, consultants, advisors, and employees of the Company or any of its subsidiaries. The Plan was approved by the Company s stockholders at a special meeting held on September 25, 2014. The Plan will terminate on July 17, 2024 following which no new Options or Restricted Stock can be granted under the Plan. The Company is authorized to issue a maximum 5,000,000 common shares under the Plan, which will automatically increase each time the Company issues additional shares of common stock for a maximum of 5% of the total outstanding common stock.

As at September 30, 2014, the Company had no outstanding stock options or restricted stock units.

**NOTE 7 DISCONTINUED OPERATIONS**

On October 15, 2013 and subsequently amended in its entirety on January 6, 2014, the Company, Utiba Pte. Ltd. ( Utiba ), a non-controlling interest investor in ATS, ATS, and Utiba Guatemala entered into an Asset Purchase Agreement in order to effect the sale by ATS of all of its business and assets to Utiba, as described below (the ATS Transaction ). For such transaction to proceed, approval of the Company s shareholder was required, which approval was obtained on February 21, 2014.

*Overview of the ATS Transaction and Consideration Payable*

1 The sale pursuant to the Asset Purchase Agreement by ATS of substantially all of its business and assets to Utiba (including the assumption by Utiba of certain liabilities related to such business and assets), in consideration for up to $3,100,000 in cash (the "Cash Purchase Price") subject to certain adjustments related to certain net receivables or liabilities, as the case may be, and reduction to the extent of certain tax liabilities of ATS. The amount of $300,000 of the Cash Purchase Price will be held back to cover certain claims that may be made under the indemnification provisions of the Asset Purchase Agreement.

2 The entry by the Company into a non-compete covenant in favor of Utiba and its affiliates in the mobile payment, top up and mobile financial services industry for a period of 36 months, in consideration for a payment in cash on closing of the transactions contemplated by the Asset Purchase Agreement (the Closing ) of $2,200,000. The Company is recognizing the full amount as income on closing as it does not intend to compete in the this industry in the future.

**ALTERNET SYSTEMS INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**September 30, 2014**
**(Unaudited)**
**NOTE 7 DISCONTINUED OPERATIONS (continued)**

*Overview of the ATS Transaction and Consideration Payable (continued)*

3 The release by the Company of Utiba from all its obligations under the ATS Shareholders Agreement in consideration for a payment in cash on Closing of $200,000.

4 Upon Closing, Utiba shall transfer its 49% interest in ATS to the Company so that the Company will own 100% of ATS after Closing.

On March 4, 2014, the ATS Transaction closed pursuant to which the Company received $4,928,036 in proceeds. An additional $667,264 is being held in escrow to cover certain claims that may be made under the indemnification provisions of the Asset Purchase Agreement. The escrow funds are included in sale proceeds held in escrow and deferred gain on sale.

As of December 31, 2013, the associated assets and liabilities of the consolidated ATS business have been classified as discontinued operations and are presented below:

| | **December 31, 2013** |
|---|---|
| | $ |
| **ASSETS** | |
| Cash | 44,107 |
| Accounts receivable, net of allowance for doubtful accounts of $789,565 | 301,991 |
| Prepaid cost of sales | 25,056 |
| Deposits and other assets | 40,500 |
| Fixed assets, net of accumulated amortization of $119,006 | 137,170 |
| Intellectual property | 1,500,000 |
| **CURRENT ASSETS OF DISCONTINUED OPERATIONS** | **2,048,824** |
| **LIABILITIES** | |
| Accounts payable and accrued charges | 555,914 |
| Deferred income | 153,150 |
| Long-term debt | 69,039 |
| Capital leases | 5,042 |
| **CURRENT LIABILITIES OF DISCONTINUED OPERATIONS** | **783,145** |

**ALTERNET SYSTEMS INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**September 30, 2014**
**(Unaudited)**
**NOTE 7 DISCONTINUED OPERATIONS (continued)**

The following table summarizes the financial results of ATS s consolidated discontinued operations for the three and nine months ended September 30, 2014 and 2013:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | **2014** | **2013** | **2014** | **2013** |
| | $ | $ | $ | $ |
| Revenue | - | 124,070 | 155,036 | 1,078,987 |
| Cost of Sales | - | 159,165 | 142,441 | 810,996 |
| Gross Margin | - | (35,095) | 12,595 | 267,991 |
| Operating Expenses | (14,394) | 698,230 | 464,858 | 2,437,778 |
| Net Income (Loss) Before Other Items | 14,394 | (733,325) | (452,263) | (2,169,787) |
| Other Items | - | (17,954) | (12,119) | 36,055 |
| Non-Compete Income | - | - | 2,200,000 | - |
| Shareholder Release Income | - | - | 200,000 | - |
| Gain on Disposal of Assets | - | - | 867,653 | - |
| | | | | |
| Net Income (Loss) Before Non-Controlling Interest | 14,394 | (751,279) | 2,803,271 | (2,133,732) |
| Non-Controlling Interest | - | (368,127) | (203,660) | (1,045,529) |
| | | | | |
| **Discontinued Operations for Alternet Systems, Inc.** | **14,394** | **(383,152)** | **3,006,931** | **(1,088,203)** |

The Company will not have any taxes owing on the income earned from the discontinued operation as it has tax losses from prior years which are available to be utilized for tax purposes.

The table below details the Company s gain on disposal of assets at September 30, 2014:

| | **Nine Months Ended September 30, 2014** |
|---|---|
| | $ |
| Total funds received | 4,928,036 |
| Less: Funds relating to non-compete and shareholder release income | (2,400,000) |
| Net funds received | 2,528,037 |
| Liabilities assumed by the purchaser | 177,401 |
| Total proceeds | 2,705,438 |
| Assets sold | (1,837,785) |
| | |
| **Gain on disposal of assets** | **867,653** |

The following table summarizes the cash flow of ATS s consolidated discontinued operations for the nine months ended September 30, 2014 and 2013:

| | Nine Months Ended September 30, | |
|---|---|---|
| | **2014** | **2013** |
| | $ | $ |
| Operating Activities | (494,210) | (471,482) |
| Investing Activities | 1,630,311 | - |
| Financing Activities | (74,083) | 144,254 |
| **Cash Flows From Discontinued Operations** | **1,062,018** | **(327,228)** |

All other Notes to the consolidated financial statements that were impacted by this discontinued operation have been reclassified accordingly.

**ALTERNET SYSTEMS INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**September 30, 2014**
**(Unaudited)**

## NOTE 8 - RELATED PARTY TRANSACTIONS

As of September 30, 2014, a total of $577,583 (December 31, 2013 - $1,046,352) was payable to directors and officers of the Company of which $577,583 (December 31, 2013 $357,957) was non-interest bearing and had no specific terms of repayment, $Nil (December 31, 2013 - $21,589) related to loans detailed in Note 4, and $Nil (December 31, 2013 - $666,806) related to unpaid wages for prior years accruing interest at 10% per annum. Of the amount payable, $16,102 (December 31, 2013 - $73,950) was included in accounts payable for expense reimbursements, $558,125 (December 31, 2013 - $964,723) was included in wages payable for accrued fees and capitalized interest, and $3,356 (December 31, 2013 - $7,679) was included in due to related parties.

During the nine months ended September 30, 2014, a director of the Company and ATS and a director of IMS resigned from the respective Board of Directors. The amounts owing to these two individuals as at September 30, 2014 included $7,999 (December 31, 2013 - $71,279) for accounts payable for expense reimbursements and $160,809 (December 31, 2013 - $520,079) for accrued fees and capitalized interest of which $Nil (December 31, 2013 - $281,120) related to unpaid wages of prior years accruing interest at 10% per annum. Additionally, on September 30, 2014, the former director of IMS released the Company of its obligation to pay the director unpaid wages of $115,792.

During the nine months ended September 30, 2014, the Company expensed a total of $312,714 (September 30, 2013 - $796,250) in consulting fees and salaries paid to directors and officers of the Company. Of the amounts incurred, $151,669 (September 30, 2013 - $796,250) has been accrued and $161,041 (September 30, 2013 - $Nil) has been paid in cash.

As of September 30, 2014, the Company s discontinued operations held an accounts receivable from a company with a director in common with the Company for $789,565; 6,674,709 Venezuelan bolivar fuerte ( VEF ) (December 31, 2013 - $789,565; VEF 6,674,709) which the Company fully allowed for during the year ended December 31, 2013 due to collectability uncertainty caused by the uncertainty of obtaining foreign currency in Venezuela. In addition, the Company owes this company $62,610 (VEF 5,971,438) (December 31, 2013 - $94,784; VEF 5,971,438) which is non-interest bearing, has no specific terms of repayment, and is included in due to related parties.

## NOTE 9 - DEFERRED COMPENSATION

On February 15, 2013, the Company signed an investor relations agreement with a consultant to provide investor relations services for a term of one year. Under the agreement, the Company agreed to make monthly payments to the consultant of $5,000 if the Company was able to raise $1,000,000 by May 16, 2013. As the Company did not raise the $1,000,000 by May 16, 2013, the monthly payments of $5,000 did not commence. The Company also agreed to issue to the consultant 700,000 shares of common stock, in four equal tranches of 175,000 each on or before February 20, 2013, May 16, 2013, August 14, 2013, and November 12, 2013. On February 19, 2013, the Company issued 700,000 shares in the name of the consultant valued at $0.15 per share, the closing price of the stock on the issue date, for a total value of $105,000. As of December 31, 2013, all of the shares had been issued to the consultant. The value of the services is being expensed on a straight-line basis over the life of the contract. During the nine months ended September 30, 2014, the Company expensed $13,125 (September 30, 2013 - $65,625) to investor relations. The contract was expensed in full by February 15, 2014.

In October 2013, the Company signed an investor relations agreement with another consultant to provide investor relations services for a term of one year. Under the agreement, the Company agreed to make two monthly payments to the consultant of $10,000 from the date of signing (paid). The Company also agreed to issue to the consultant

2,000,000 shares of common stock based on certain benchmarks. On November 6, 2013, the Company issued 2,000,000 common shares in the name of the consultant valued at $0.05 per share, the closing price of the stock on the issue date, for a total value of $100,000 of which none have been delivered to the consultant. The 2,000,000 shares will be delivered to the consultant when the benchmarks of the contract have been met. If the contract is terminated and the consultant does not meet the stages of the benchmarks, the Company may cancel any shares not delivered to the consultant. The value of the services is being expensed when the benchmarks are met. As at September 30, 2014, two of the benchmarks were met (December 31, 2013 - none); as such, the Company issued 1,000,000 common shares (December 31, 2013 - Nil) to the consultant and expensed $50,000 to investor relations. In April 2014, the Company terminated the contract with the consultant and cancelled the remaining 1,000,000 common shares.

On February 18, 2014, the Company signed a consulting agreement with a consultant to provide strategic business consulting services for a term of one year. Under the agreement, the Company agreed to make monthly payments of $6,500 to the consultant and to issue the consultant 1,000,000 shares of common stock. On June 9, 2014, the Company issued the 1,000,000 common shares in the name of the consultant valued at $0.08 per share, the closing price of the stock on the issue date, for a total value of $80,000. The value of the services is being expensed on a straight-line basis over six months, the term stipulated in the contract. During the nine months ended September 30, 2014, the Company expensed $80,000 to consulting fees.

**ALTERNET SYSTEMS INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**September 30, 2014**
**(Unaudited)**
**NOTE 9 - DEFERRED COMPENSATION (continued)**

The Company recorded the aggregate fair value of the shares issued pursuant to the above agreements as deferred compensation. During the nine months ended September 30, 2014, the Company expensed $143,125 (nine months ended September 30, 2013 -$65,625) relating to the above contracts. The shares issued were all valued at their market price on the date of issuance.

**NOTE 10 OPERATING LEASES**

The Company leases its office facilities under a one-year lease agreement with a monthly cost of $1,800. The lease expires in March 2015 and can be renewed at such time for a similar or longer term. In the normal course of business, it is expected that this lease will be renewed or replaced by a lease on another property.

Lease expense totaled $12,600 and $12,576 during the nine months ended September 30, 2014 and 2013, respectively.

The Company is required to make $9,000 in future minimum rental payments under the operating lease agreement.

**NOTE 11 SUPPLEMENTAL DISCLOSURE WITH RESPECT TO CASH FLOWS**

| | **Nine months ended September 30,** | |
|---|---|---|
| | **2014** | **2013** |
| | $ | $ |
| Supplemental cash flow disclosures: | | |
| Interest paid | 90,532 | 10,760 |
| Cash paid for income taxes | - | - |
| | | |
| Supplemental non-cash disclosures: | | |
| Shares obligated to be issued | - | 52,800 |
| Shares issued for share issue costs | - | 21,000 |
| Shares issued for deferred compensation | 80,000 | 105,000 |
| Shares issued for wages and related benefits payable | - | 85,795 |
| Value of beneficial conversion feature | - | 75,333 |
| Deferred gain from funds held in escrow | 667,264 | - |
| Shares issued for investment in digital currency | 125,000 | - |
| Cancellation of shares issued for deferred compensation | 50,000 | - |

**NOTE 12 FAIR VALUE**

Fair value accounting establishes 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 are described below:

Level 1 Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;

Level 2

| | |
|---|---|
| | Quoted prices in markets that are not active, or inputs that are observable, either directly or indirectly, for substantially the full term of the asset or liability; |
| Level 3 | Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (supported by little or no market activity). |

The fair value of the Company s sale proceeds held in escrow, accounts payable and accrued liabilities, wages payable, accrued taxes, deferred gain on sale, other loans payable, and due to related parties approximates their carrying values. The Company s other financial instruments, being cash and investment in digital currency, are measured at fair value using Level 1 inputs.

**ALTERNET SYSTEMS INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**September 30, 2014**
**(Unaudited)**

**NOTE 13 LAWSUIT**

In January 2014, the Company received notice of a default judgment in the amount of $39,000 plus interest entered by the State of New York related to an unpaid service agreement entered into on February 11, 2009. The Company has filed a motion to vacate the foreign judgment or in the alternative stay the enforcement. The Company, until receipt of such notice, was unaware of any such demand. No prior notice had been served to the Company or its chief executive. As of September 30, 2014, no provision for this claim has been made.

**NOTE 14 SUBSEQUENT EVENTS**

- Effective October 23, 2014, the Company amended its articles to increase its authorized capital stock to 510,000,000 shares of which 500,000,000 are common stock with a par value of $0.00001 and 10,000,000 are preferred stock with a par value of $0.00001.

Events occurring after September 30, 2014 were evaluated through the date this Interim Report was issued, in compliance with FASB ASC Topic 855 Subsequent Events , to ensure that any subsequent events that met the criteria for recognition and/or disclosure in this report have been included

**ITEM 2. MANAGEMENT DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS:**

The following discussion contains forward-looking statements that reflect our plans, estimates and beliefs. Our actual results could differ materially from those discussed in the forward looking statements. Factors that could cause or contribute to such differences include, but are not limited to those discussed below and in our annual report on Form 10-K/A for the year ended December 31, 2013, filed with the Securities and Exchange Commission on June 17, 2014, particularly in the section entitled "Risk Factors .

***Overview***

In 2014 Alternet will seek to transform into an accelerator of high growth, emerging mobile and digital, technology and services companies, in the digital currency and the mobile and digital security fields. Our goal is to expand the horizons of individuals and organizations, by providing a growth and networking platform, empowering them to go beyond their expectations and goals.

The new vision of Alternet is to accelerate the future of money through the creation of a digital bank, building security around the digital monetary ecosystem, and providing an exchange that allows for the movement from virtual money to fiat currency.

Our new product and service will offer consumers and businesses the cost savings and speed associated with the internet in compliance with anti-money laundering procedures in place at US brokerage firms and banks.

The Company is entering into its next phase which will leverage the experience and knowledge in mobile technology and financial services to provide solutions in the digital currency and the mobile and digital security fields. Investments in these fields are underway.

Alternet s vision is based on the following principles

As of the date of this report, the Company has reached the following milestones:

- entered into arrangements with select digital currencies, with the first having taken place in February 2014 with Ven;
- became a full time member of the Bitcoin Foundation and DATA (Digital Asset Transfer Association);
- entered into a strategic joint venture with BIOMETRY for "BioME", which replaces passwords and PINs through the combination of dynamic facial and voice recognition in a unique ID system; to provide end to end security for digital currencies;
- signed a Letter of Intent with P2P Cash to launch the Digital Asset Exchange initiative under the OneMarket subsidiary, subject to approval of the license by the New York Department of Financial Services. Under this Letter of Intent, the Company plans to launch a digital currency exchange, fully compliant with government regulations and foreign exchange capabilities. The Company is actively pursuing and preparing to apply for a license with The New York Department of Financial Services to be allowed to receive, transmit, store, exchange, issue or convert virtual currency for Customers. The licensing process will most likely not be completed until 2015 as requirements are still being defined;
- entered into a strategic channel partner agreement with BitPay - the world leader in business solutions for the bitcoin digital currency;
- in October the Company completed a formal agreement with Wildcard Consulting Inc. ("Wildcard") to launch the first U.S. based Bitcoin debit card.

VEN is a global digital currency traded in international financial markets and originally used by members of a social network service, Hub Culture, to buy, share, and trade knowledge, goods, and services. The value of Ven is determined on the financial markets from a basket of currencies, commodities and carbon futures. It trades against major currencies at floating exchange rates.

In the first quarter of 2014, we entered into a relationship with VEN and Hub Culture to become a VEN Authority. This relationship will allow us to become an issuer of the VEN Currency on a global basis, leveraging the experience and the strength of this Digital Currency.

P2P Cash's technology and intellectual property provides a highly secure, real-time mobile payment solution to deliver cash transfers and remittance payments in developing countries through seamless international cash transfers. P2P Cash's proprietary platform is a unique method for the implementation of a mobile banking standard that can work with any wireless carrier and/or any bank worldwide.

In addition, he Company s financial services initiative will focus on bringing to market innovative consumer products, including a multi-asset debit and credit card. This initiative is the first of its kind with dynamic currency conversion from digital to physical currency, digital currency exchange and merchant acquisition solutions. All of these services will include the seamless integration of existing digital currencies, including Bitcoin, Ven, Ripple and others. The Company expects to have a global reach, initially launching in Latin America and the Caribbean, with expansion opportunities into Africa and Eastern Europe.

We will actively participate in the industry associations and promoting organizations. We will also seek speaking and industry show participation, promoting our new initiatives.

Digital and Mobile Security Software and Services

In 2013 International Mobile Security (IMS) was wound down. IMS is expected to be restructured in 2014 and be used as the vehicle to provide services and products securing financial transactions and digital currency.

**Results of Operations:**

**Three and nine months ended September 30, 2014 compared to three and nine months ended September 30, 2013**

The Company s results, on a consolidated basis, reflect its own results consolidated with its subsidiaries. For the remainder of this part, the term Company refers to both the Company and its wholly owned subsidiaries.

Upon closing of the ATS Transaction described in Note 7 of the financial statements, the Company acquired the 49% non-controlling interest in Alternet Transactions Systems, Inc. ( ATS ), doing business as Utiba Americas, increasing the Company s ownership to 100%.

On September 30, 2014, the minority interest holder of IMS assigned its 40% shareholding of IMS to Alternet resulting in the Company owning 100% of the issued common stock of IMS.

**Net Sales**

For the three months ended September 30, 2014 and 2013, the Company had net sales of $Nil and $1,501, respectively. For the nine months ended September 30, 2014 and 2013, the Company had net sales of $Nil and $3,142, respectively. The low sales were a result of the Company focusing its efforts on ATS, which was classified as a discontinued operation at December 31, 2013. All revenue earned by ATS up to March 4, 2014 is included in discontinued operations.

**Selling, General and Administrative Expenses**

The operating and administrative expenses for the three months ended September 30, 2014 and 2013 totaled $216,339 and $421,035, respectively. The table below details the major changes in administrative expenditures for the three months ended September 30, 2014 and 2013.

| Expenses | Increase / Decrease in Expenses | Explanation for Change Three Months Ended September 30, 2014 as Compared to the Three Months Ended September 30, 2013 |
|---|---|---|
| Investor relations | Decrease of $20,696 | The quarter ended September 30, 2013 included a contract with an investor relations consultant which accounted for $26,250 of the quarterly balance. This contract ended in early 2014 and was replaced by another firm. |
| Management and consulting | Increase of $152,697 | The Company incurred increased consulting fees relating to seeking out new business ventures. |
| Office and general | Increase of $22,068 | Increased online marketing due to the Company rebranding its image after the closing of the ATS Transaction. |
| Professional fees | Increase of $37,196 | Increased legal fees relating to increased legal oversight and SEC filings. |
| Payroll (recovery), net | Decrease of $387,613 | The quarter ended September 30, 2013 included an estimate for payroll tax penalties and interest of $313,878. The current quarter did not include any accrual as all payroll taxes were paid up to date. Additionally, the current quarter included a reversal of $68,800 of unpaid wages which were forgiven by a former employee of IMS. |

The operating and administrative expenses for the nine months ended September 30, 2014 and 2013 totaled $1,539,091 and $1,425,011, respectively. The table below details the major changes in administrative expenditures for the nine months ended September 30, 2014 and 2013.

| Expenses | Increase / Decrease in Expenses | Explanation for Change Nine Months Ended September 30, 2014 as Compared to Nine Months Ended September 30, 2013 |
|---|---|---|
| Research and development | Increase of $500,000 | In 2014, the Company paid a fee of $500,000 in connection with the ability to offer and promote digital currency. |
| Management and consulting | Increase of $96,499 | Increased consulting fees have also been incurred in the current period while the Company searches for new business ventures. Additionally, in the interim the Company has utilized more consultants rather than salaried employees. |
| Office and general | Increase of $87,343 | |

| | | |
|---|---|---|
| | | Increased online marketing due to the Company rebranding its image after the closing of the ATS Transaction. |
| Professional fees | Increase of $86,149 | Increased accounting fees relating to the filing of quarterly reports and payroll tax payments and increased legal fees relating to the digital currency exchange licensing process and increased legal oversight and SEC filings. |
| Payroll | Decrease of $719,134 | The period ended September 30, 2013 included an estimate for payroll tax penalties and interest of $425,977 while the quarter ended September 30, 2014 included a reversal of $206,600 of estimated interest on payroll taxes that was over accrued in fiscal 2013. Additionally, the period ended September 30, 2013 included a reversal of $68,800 of unpaid wages which were forgiven by a former employee of IMS. |
| Travel | Increase of $68,313 | Increased need for travel for meetings and due diligence on new initiatives being explored by the Company. |

**Interest and Other Expenses**

The Company s net interest expense decreased to $24,688 for the three months ended September 30, 2014 and $81,491 for the nine months ended September 30, 2014 compared to $83,245 and $319,858 for the three and nine months ended September 30, 2013, respectively. This was due to the decrease in loans outstanding during the period, reflecting the repayment of several loans payable.

**Net Income (Loss)**

For the three months ended September 30, 2014, the Company had a net and comprehensive loss attributable to Alternet System, Inc. from continuing operations of $(246,013) or $(0.00) per share and an overall net and comprehensive loss of $(231,619) or $(0.00) per share, a decrease of 47.57% and 72.83% respectively, when compared to the corresponding three months ended September 30, 2013 which had a net and comprehensive loss attributable to Alternet System, Inc. from continuing operations of $(469,196) or $(0.01) per share and an overall net and comprehensive loss of $(852,348) or $(0.01) per share.

For the nine months ended September 30, 2014, the Company had a net and comprehensive loss attributable to Alternet System, Inc. from continuing operations of $(1,612,118) or $(0.02) per share and an overall net and comprehensive income of $1,394,813 or $0.01 per share, a decrease of 2.7% and an increase of 150.8% respectively, when compared to the corresponding nine month period ended September 30, 2013 which had a net and comprehensive loss attributable to Alternet System, Inc. from continuing operations of $(1,656,721) or $(0.02) per share and an overall net and comprehensive loss of $(2,744,924) or $(0.03) per share.

The increased losses from continuing operations is mostly attributable to an Authority fee the Company was required to pay to be able to promote the Ven digital currency while the overall income is primarily attributable to the sale of ATS s Assets.

**Liquidity and Capital Resources**

As of September 30, 2014, the Company had $6,235 (December 31, 2013 $Nil) cash in the bank and sale proceeds held in escrow relating to the ATS Transaction of $667,264 (December 31, 2013 $Nil). At September 30, 2014, the Company had a working capital deficiency of $3,632,182 (December 31, 2013 $5,168,849). The Company is in discussion with investment bankers to raise additional capital to fund ongoing operations. The Company s ability to continue as a going concern will be negatively affected if it is unsuccessful.

Accounts payable were $1,907,213 at September 30, 2014 compared to accounts payable of $1,466,546 at December 31, 2013. As at September 30, 2014, the Company s current liabilities were $4,430,352, a reduction of $2,809,106 from the current liabilities of $7,239,458 at December 31, 2013.

**Critical Accounting Policies**

The discussion and analysis of our financial condition and results of operations are based upon our financial statements, which have been prepared in accordance with the accounting principles generally accepted in the United States of America. Preparing financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, and expenses. These estimates and assumptions are affected by management s application of accounting policies. We believe that understanding the basis and nature of the estimates and assumptions involved with the following aspects of our financial statements is critical to an understanding of our financial statements.

*Basis of Presentation and Consolidation*

The consolidated financial statements and related notes are presented in accordance with accounting principles generally accepted in the United States, and are expressed in United States dollars. The financial statements include the accounts of the Company and its wholly owned and majority owned subsidiaries. Our fiscal year-end is December 31.

The minority interests of ATS up to March 4, 2014, the date the Company gained 100% ownership, IMS, and ATS s and IMS s wholly owned subsidiaries have been deducted from earnings and equity. All significant intercompany transactions and account balances have been eliminated.

*Use of Estimates and Assumptions*

The preparation of financial statements in conformity with generally accepted accounting principles 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 financial statement date and the reported amounts of revenues and expenses during the reporting period. The Company regularly evaluates estimates and assumptions related to the useful life and recoverability of long-lived assets, fair value of convertible notes payable and derivative liabilities. The Company bases its estimates and assumptions on current facts, historical experience and various other factors that it believes to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities and the accrual of costs and expenses that are not readily apparent from other sources. The actual results experienced by the Company may differ materially and adversely from the Company s estimates. To the extent there are material differences between estimates and the actual results, future results of operations will be affected.

*Cash and Cash Equivalents*

The Company considers all liquid investments, with an original maturity of three months or less when purchased, to be cash equivalents.

*Accounts Receivable and Allowance for Doubtful Accounts*

Trade accounts receivable are stated at the amount the Company expects to collect. The Company maintains allowances for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. Management considers the following factors when determining the collectability of specific customer accounts: customer credit-worthiness, past transaction history with the customer, current economic industry trends, and changes in customer payment terms. Past due balances over 90 days and other higher risk amounts are reviewed individually for collectability. If the financial condition of the Company s customers were to deteriorate, adversely affecting their ability to make payments, additional allowances would be required. Based on management s assessment, the Company provides for estimated uncollectible amounts through a charge to earnings and a credit to a valuation allowance. Balances that remain outstanding after the Company has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable.

*Equipment*

Fixed assets are recorded at cost and depreciated at the following rates:

| | | |
|---|---|---|
| Computer equipment | - | 30% declining balance basis |
| Computer software | - | 30% declining balance basis |
| Equipment | - | 20% declining balance basis |

*Long-Lived Assets Including Other Acquired Intellectual Property*

Management monitors the recoverability of long-lived assets and intangibles based on estimates using factors such as current market value, future asset utilization, and future undiscounted cash flows expected to result from its investment or use of the related assets. The Company s policy is to record any impairment loss in the period when it is determined that the carrying amount of the asset may not be recoverable. Any impairment loss is calculated as the excess of the carrying value over estimated realizable value. The Company did not recognize an impairment charges related to long-lived assets during the nine months ended September 30, 2014 and 2013.

Intangible assets deemed to have an indefinite life are not amortized but are subject to impairment tests at each reporting date. The Company assesses the impairment of intangible assets on a quarterly basis or whenever events or changes in circumstances indicate that the fair value is less than its carrying value. If the carrying amount of the intangible asset exceeds its fair value, the intangible asset is considered impaired and the second step of the test is performed to determine the amount of impairment loss, if any. The Company did not recognized an impairment charges related to indefinite lived intangible assets during the nine months ended September 30, 2014 and 2013.

*Revenue Recognition*

Up to March 4, 2014, the Company entered into sales arrangements that may have provided for multiple deliverables to a customer. Software sales may have included the sale of a software license, implementation/customization services, and/or ongoing support services.

In order to treat deliverables in a multiple-deliverable arrangement as separate units of accounting, the deliverables must have standalone value upon delivery. If the deliverables have standalone value upon delivery, the Company accounts for each deliverable separately. Licenses, support fees, and hosted services have standalone value as such services are often sold separately. In determining whether implementation/customization services have standalone value, the Company considers the following factors for each agreement: availability of the services from other vendors, the nature of the services, the timing of when the services contract was signed in comparison to the services start date, and the contractual dependence of the customization service on the customer s satisfaction with the implementation/customization services work.

The Company concluded that all of the services included in multiple-deliverable arrangements executed had standalone values when multiple deliverables included in an arrangement are separated into different units of accounting. The arrangement consideration is allocated to the identified separate units based on a relative selling price hierarchy. The Company determines the relative selling price for a deliverable based on its vendor-specific objective evidence of selling price ( VSOE ), if available, or its best estimate of selling price ( BESP ), if VSOE is not available. The Company has determined that third-party evidence of selling price ( TPE ) is not a practical alternative due to differences in its service offerings compared to other parties and the availability of relevant third party pricing information. The amount of revenue allocated to delivered items is limited by contingent revenue, if any.

The Company has not established VSOE for a majority of its revenue due to lack of pricing consistency, the customer specific requests, and other factors. Accordingly, the Company used its BESP to determine the relative selling price.

The Company determined BESP by considering its overall pricing objectives and market conditions. Significant pricing practices taken into consideration include the Company s discounting practices, the size and volume of the Company s transactions, the geographic area where services are sold, its market strategy, historic contractually stated prices and prior relationships, and future service sales with certain customers. The determination of BESP is made through consultation with and approval by the Company s management, taking into consideration the market strategy. As the Company s market strategies evolve, the Company may modify its pricing practices in the future, which could result in changes in selling prices.

Revenue was recognized upon delivery or when services were performed, provided that persuasive evidence of a sales arrangement existed, both title and risk of loss passed to the customer, and collection was reasonably assured. Persuasive evidence of a sales arrangement existed upon execution of a written sales agreement or signed purchase order that constituted a fixed and legally binding commitment between the Company and the buyer. Specifically, revenue from the sale of licenses was recognized when the title of the license transferred to the customer while revenue from implementation/customization services performed was recognized upon successful completion of a User Acceptance Test ( UAT ). If a successful UAT was never achieved and the sales arrangement was cancelled, the Company recognized any deferred revenue not required to be refunded to the customer.

The Company s payment terms vary by client. To reduce credit risk in connection with software license and support sales, the Company may, depending upon the circumstances, require significant deposits prior to delivery. In some circumstances, the Company may require payment in full for its products prior to delivery. For support and hosted services, the Company sold customers service agreements that were recorded as deferred revenue and provided for payment in advance on either an annual or other periodic basis. Revenue for these support services was recognized ratable over the term of the agreement.

Subsequent to March 4, 2014 the Company implemented the criteria outlined in SAB 104 and recognizes revenue when:

- persuasive evidence of an arrangement exists;
- delivery has occurred or services have been rendered;
- the seller s price to the buyer is fixed or determinable; and
- collectability is reasonably assured.

*Research and Development*

The Company expenses costs when incurred for items associated with researching and developing new sources of revenue.

*Digital Currency Transactions*

The Company enters into transactions that are denominated in digital currency (Ven). These transactions result in digital currency denominated assets and liabilities that are revalued periodically. Upon revaluation, transaction gains and losses are generated and are reported as unrealized gains and losses in other gain (loss), net in the Condensed and Consolidated Statements of Operations. The Company determines fair value as of the balance sheet date based on Level I inputs which consist of quoted prices in active markets. The value of the Company s digital currency is $122,671, net of $2,329 of unrealized losses, as of September 30, 2014. Due to the uncertainty regarding the current and future accounting treatment and tax, legal and regulatory requirements relating to digital currencies or transactions utilizing digital currencies, such accounting, legal, regulatory and tax developments or other requirements may adversely affect us.

*Debt with Conversion Options*

The Company accounts for convertible debentures in accordance with ASC Topic 470-20, *Debt with Conversion and Other Options* , which applies to all convertible debt instruments that have a net settlement feature, which means instruments that by their terms may be settled either wholly or partially in cash upon conversion. Accordingly, the liability and equity components of convertible debt instruments that may be settled wholly or partially in cash upon conversion should be accounted for separately in a manner reflective of their issuer s nonconvertible debt borrowing rate. Conversion features determined to be beneficial to the holder are valued at fair value and recorded to additional paid in capital. Any discount derived from determining the fair value to the debenture conversion features is amortized to interest expense over the life of the debenture. The unamortized costs, if any, upon the conversion of the debentures is expensed to interest immediately.

*Leases*

The Company leased operating facilities which include switches, other network equipment, and premises. Rentals payable under operating leases were charged to the statements of operation on a straight line basis over the term of the relevant lease. For capital leases, the present value of future minimum lease payments at the inception of the lease was reflected as an asset and a liability in the statement of financial position. Amounts due within one year are classified as short-term liabilities and the remaining balance as long-term liabilities.

*Foreign Currency Translation*

The Company s functional currency and its reporting currency is the United States Dollar. Foreign denominated monetary assets and liabilities are translated to their United States dollar equivalents using foreign exchange rates which prevailed at the balance sheet date. Revenue and expenses are translated at average rates of exchange during the year. Related translation adjustments are reported as a separate component of stockholders equity (deficit), whereas gains or losses resulting from foreign currency transactions are included in the results of operations.

*Fair Value of Financial Instruments*

The Company has determined the estimated fair value of financial instruments using available market information and appropriate valuation methodologies. The carrying value of the Company s financial instruments, consisting of accounts receivable, checks in excess of bank balances, accounts payable and accrued liabilities, wages payable, accrued payroll taxes, other loans payable, stock-based compensation, warrants, and due to related parties, approximate their fair value due to the relatively short maturity of these instruments.

*Income Taxes*

The Company accounts for income taxes under a method which requires the Company to recognize deferred tax assets and liabilities for the expected future tax consequences of events that have been recognized in the Company s financial statements or tax returns. Under this method, deferred tax assets and liabilities are determined based on the difference between the financial statements carrying amounts and tax basis of assets and liabilities using enacted tax rates. The Company recognizes the tax benefit from an uncertain tax position only if it is more likely than not the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such positions are then measured based on the largest benefit that has a greater than 50% likelihood of being realized upon settlement.

*Stock-Based Compensation*

The Company accounts for its share-based compensation plans in accordance with the fair value recognition provisions of ASC 718 *Compensation-Stock Compensation* . The Company utilizes the Black-Scholes option pricing model as its method for determining the fair value of stock option grants. ASC 718 requires the fair value of all share-based awards that are expected to vest to be recognized in the statements of operations over the service or vesting period of each award. The Company uses the straight-line method of attributing the value of share-based compensation expense for all stock option grants over the requisite service period.

*Income (Loss) per Share*

The Company computes net earnings (loss) per share in accordance with ASC Topic 260, *Earnings Per Share*. Topic 260 requires presentation of both basic and diluted earnings per share (EPS). Basic EPS is computed by dividing net income (loss) available to common shareholders (numerator) by the weighted average number of common shares outstanding (denominator) during the period. Diluted EPS gives effect to all dilutive potential common shares outstanding during the period including warrants using the treasury stock method. Diluted EPS excludes all dilutive potential common shares if their effect is anti-dilutive.

At September 30, 2014 and December 31, 2013 the Company had no warrants or options outstanding to consider in income (loss) per share calculation.

*Recent Accounting Pronouncements*

In April 2014, the FASB issued ASU No. 2014-08, *Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity.* This ASU is to be applied prospectively for all disposals of an entity that occur within annual periods beginning on or after December 15, 2014, and interim periods beginning on or after December 15, 2015. Additionally, this ASU is to be applied to all business activated that, on acquisition, are classified as held for sale that occur within annual periods beginning on or after December 15, 2014, and interim periods within annual periods beginning on or after December 15, 2015. ASU No 2014-08 addresses concerns about the accounting for discontinued operations and the disposal of small groups of assets that are recurring in nature but qualify as discontinued operations under subtopic 205-20. Management does not anticipate that this accounting pronouncement will have any material future effect on our consolidated financial statements.

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606).* This ASU is effective for annual reporting periods beginning after December 15, 2016. ASU No 2014-09 addresses concerns about weaknesses and inconsistencies in revenue recognition across entities, industries, jurisdictions, and capital markets. Management does not anticipate that this accounting pronouncement will have any material future effect on our consolidated financial statements.

In June 2014, the FASB issued ASU No. 2014-12, *Compensation - Stock Compensation (Topic 718): Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period.*

This ASU is effective for annual reporting periods beginning after December 15, 2015. ASU No 2014-12 clarifies the diverse accounting treatments used by entities to account for awards based on performance targets achieved after the requisite period. Management does not anticipate that this accounting pronouncement will have any material future effect on our consolidated financial statements.

In August 2014, the FASB issued ASU No. 2014-15, *Presentation of Financial Statements Going Concern (Topic 205): Disclosure of Uncertainties about an Entity s Ability to Continue as a Going Concern.* This ASU is effective for annual reporting periods ending after December 15, 2016. ASU No 2014-15 provides guidance about management s responsibility to evaluate whether there is substantial doubt about an entity s ability to continue as a going concern and to provide related footnote disclosures. Management does not anticipate that this accounting pronouncement will have any material future effect on our consolidated financial statements. Other recent accounting pronouncements issued by the FASB (including its Emerging Issues Task Force), the American Institute of Certified Public Accountants, and the SEC did not, or are not believed by management to, have a material impact on the Company's present or future financial position, results of operations or cash flows.

**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

As a smaller reporting company , we are not required to provide the information required by this Item.

**Item 4. Controls and Procedures**

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our reports filed under the Securities Exchange Act of 1934, as amended (the Exchange Act ), is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to our management, including our president (also our principal executive officer) and our chief financial officer (also our principal financial officer) to allow for timely decisions regarding required disclosure. In designing and evaluating our disclosure controls and procedures, our management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and our management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

As of September 30, 2014, we carried out an evaluation, under the supervision and with the participation of our president (also our principal executive officer) and our chief financial officer (also our principal financial officer), of the effectiveness of the design and operation of our disclosure controls and procedures. Based on the foregoing, our president (also our principal executive officer) and our chief financial officer (also our principal financial officer) concluded that our disclosure controls and procedures were effective as of the end of the period covered by this quarterly report to ensure that information required to be disclosed in our reports that we file under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms.

***Changes in Internal Control over Financial Reporting***

There have been no changes in our internal controls over financial reporting that occurred during the three months ended September 30, 2014 that have materially or are reasonably likely to materially affect, our internal controls over financial reporting.

## PART II OTHER INFORMATION

### Item 1. Legal Proceedings

Other than as described below, management is not aware of any legal proceedings (either presently engaged in or contemplated) by any government authority or other party involving the Company, its properties or its products.

In January 2014, the Company received notice of a default judgment in the amount of $39,000 plus interest entered by the State of New York related to an unpaid service agreement entered into on February 11, 2009. The Company has filed a motion to vacate the foreign judgment or in the alternative stay the enforcement. The Company, until receipt of such notice, was unaware of any such demand. No prior notice had been served to the Company or its chief executive.

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

During the three months ended September 30, 2014, the Company issued 56,000 shares of common stock for investor relations services rendered.

In connection with the foregoing, the Company relied upon the exemption from registration provided by Section 4(a)(2) under the Securities Act of 1933, as amended, for transactions not involving a public offering.

### Item 3. Defaults upon Senior Securities

None.

### Item 4. Mine Safety Disclosures

Not applicable.

### Item 5. Other Information

None.

**Item 6. Exhibits**

**EXHIBIT INDEX**

| Number | Exhibit Description |
|---|---|
| 31.1 | Section 302 Certification of Chief Executive Officer |
| 31.2 | Section 302 Certification of Chief Financial Officer |
| 32.1 | Section 906 Certification of Chief Executive Officer |
| 32.2 | Section 906 Certification of Chief Financial Officer |
| 101.INS | XBRL INSTANCE DOCUMENT |
| 101.SCH | XBRL TAXONOMY EXTENSION SCHEMA DOCUMENT |
| 101.CAL | XBRL TAXONOMY EXTENSION CALCULATION LINKBASE |
| 101.DEF | XBRL TAXONOMY EXTENSION DEFINITION LINKBASE |
| 101.LAB | XBRL TAXONOMY EXTENSION LABELS LINKBASE |
| 101.PRE | XBRL TAXONOMY EXTENSION PRESENTATION LINKBASE |

**SIGNATURES**

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

**ALTERNET SYSTEMS INC.**

By:*/s/Henryk Dabrowski*
Henryk Dabrowski, President
(Principal Executive Officer)
November 14, 2014

By:*/s/ Michael T. Viadero*
Michael T. Viadero, Chief Financial Officer
(Principal Financial Officer and Principal Accounting
Officer)
November 14, 2014