Net Element, Inc.
Form 10-Q/A
June 27, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q/A
(Amendment No. 1)

(Mark One)

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

For the quarterly period ended March 31, 2016

OR

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

For the transition period from __________ to __________

Commission file number: **001-34887**

Net Element, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**90-1025599**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

3363 NE 163rd Street, Suite 705	
North Miami Beach, Florida	**33160**
(Address of principal executive offices)	(Zip Code)

(305) 507-8808

(Registrant's telephone number, including area code)

Not applicable

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

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

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

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

Large accelerated filer ¨	Accelerated filer ¨
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company x

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

The number of outstanding shares of common stock, $.0001 par value, of the registrant as of May 11, 2016 was 11,425,247 (after giving effect to the registrant's one-for-ten reverse stock split effected May 25, 2016).

EXPLANATORY NOTE

This Amendment No. 1 on Form 10-Q/A (this “Amendment No. 1”) amends and restates in its entirety the Quarterly Report on Form 10-Q of Net Element, Inc. (the “Company”) for the quarter ended March 31, 2016 as originally filed with the Securities and Exchange Commission (the “Commission”) on May 16, 2016 (the “Original Filing”).

This Amendment No. 1 amends the Original Filing to (i) reflect to the Company’s one-for-ten reverse stock split effected May 25, 2016 as if it had occurred on January 1, 2015 (shares and per share amounts have been revised accordingly); and (ii) revise disclosure relating to the Company’s guarantee of the market value of shares issued in connection with the PayOnline (as defined herein) acquisition.

For ease of reference, revisions to the Original Filing have been made to the following sections:

- Part I, Item 1 – Financial Statements (and Notes to Unaudited Condensed Consolidated Financial Statements)

- Part I, Item 2 – Management’s Discussion and Analysis of Financial Condition and Results of Operations

In addition, the Company’s Chief Executive Officer and Chief Financial Officer have provided new certifications dated as of the date of this filing in connection with this Amendment No. 1 (Exhibits 31.1, 31.2 and 32.1), and the Company has provided its revised unaudited consolidated financial statements formatted in eXtensible Business Reporting Language (XBRL) in Exhibit 101.

Except as provided in this explanatory note, or as indicated in the applicable disclosure, this Amendment No. 1 has not been updated to reflect other events occurring after the filing of the Original Filing and does not modify or update information and disclosures in the Original Filing affected by subsequent events. Accordingly, this Amendment No. 1 should be read in conjunction with our filings with the Commission subsequent to the date on which we filed the Original Filing, together with any amendments to those filings.

Defined Terms

Net Element, Inc. is a corporation organized under the laws of the State of Delaware. As used in this Quarterly Report on Form 10-Q (this "Report"), unless the context otherwise requires, the terms "Company," "we," "us" and "our" refer to Net Element, Inc. and, as applicable, its majority-owned and consolidated subsidiaries. References in this Report to "PayOnline" refer, collectively, to PayOnline System LLC, Innovative Payment Technologies LLC, Polimore Capital Limited and Brosword Holding.

Forward-Looking Statements

This Report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Any statements contained in this Report that are not statements of historical fact may be deemed forward-looking statements. Forward-looking statements generally are identified by the words "expects," "anticipates," "believes," "intends," "estimates," "aims," "plans," "
"will," "continue," "seeks," "should," "believe," "potential" or the negative of such terms and similar expressions. Forward-loo
statements are based on current plans, estimates and projections, and therefore you should not place too much reliance on them. Forward-looking statements speak only as of the date they are made, and the Company undertakes no obligation to update any forward-looking statement in light of new information or future events, except as expressly required by law. Forward-looking statements involve inherent risks and uncertainties, most of which are difficult to predict and are generally beyond the Company's control. The Company cautions you that a number of important factors could cause actual results or outcomes to differ materially from those expressed in, or implied by, the forward-looking statements. These factors include, among other factors:

- the impact of any new or changed laws, regulations, card network rules or other industry standards affecting our business including the U.S. government decision to impose sanctions or other legal restrictions that may restrict our ability to do business in Russia;
- the impact of any significant chargeback liability and liability for merchant or customer fraud, which we may not be able to accurately anticipate and/or collect;
- our ability to secure or successfully migrate merchant portfolios to new bank sponsors if current sponsorships are terminated;
- our and our bank sponsors' ability to adhere to the standards of the Visa® and MasterCard® payment card associations;
- our reliance on third-party processors and service providers;
- our dependence on independent sales groups ("ISGs") that do not serve us exclusively to introduce us to new merchant accounts;
- our ability to pass along increases in interchange costs and other costs to our merchants;
- our ability to protect against unauthorized disclosure of merchant and cardholder data, whether through breach of our computer systems or otherwise;
-

- the effect of the loss of key personnel on our relationships with ISGs, card associations, bank sponsors and our other service providers;
- the effects of increased competition, which could adversely impact our financial performance;
- the impact of any increase in attrition due to an increase in closed merchant accounts and/or a decrease in merchant charge volume that we cannot anticipate or offset with new accounts;
- the effect of adverse business conditions on our merchants;
- our ability to adopt technology to meet changing industry and customer needs or trends;
- the impact of any decline in the use of credit cards as a payment mechanism for consumers or adverse developments with respect to the credit card industry in general;
- the impact of any adverse conditions in industries in which we obtain a substantial amount of our bankcard processing volume;
- the impact of seasonality on our operating results;
- the impact of any failure in our systems due to factors beyond our control;
- the impact of any material breaches in the security of third-party processing systems we use;
- the impact of any new and potential governmental regulations designed to protect or limit access to consumer information;
- the impact on our profitability if we are required to pay federal, state or local taxes on transaction processing or VAT on content;
- the impact on our growth and profitability if the markets for the services that we offer fail to expand or if such markets contract;
- our ability (or inability) to continue as a going concern;
- the willingness of the Company’s majority stockholders, and/or other affiliates of the Company, to continue investing in the Company’s business to fund working capital requirements;
- the Company’s ability (or inability) to obtain additional financing in sufficient amounts or on acceptable terms when needed;
- the impact on our operating results as a result of impairment of our goodwill and intangible assets;
- our material weaknesses in internal control over financial reporting and our ability to maintain effective controls over financial reporting in the future; and
- the other factors those described in Part I, Item 1A of our Annual Report on Form 10-K for the fiscal year ended December 31, 2015 and in Part II, Item 1A of this Report and our subsequent filings with the U.S. Securities and Exchange Commission (the “Commission”).

If these or other risks and uncertainties (including those described in Part I, Item 1A of our Annual Report on Form 10-K for the fiscal year ended December 31, 2015 and in Part II, Item 1A of this Report and the Company’s subsequent filings with the Commission) materialize, or if the assumptions underlying any of these statements prove incorrect, the Company’s actual results may be materially different from those expressed or implied by such statements. We undertake no obligation to publicly revise any forward-looking statement to reflect circumstances or events after the date of this Report to reflect the occurrence of unanticipated events. You should, however, review the factors and risks described in the reports we file from time-to-time with the Commission after the date of this Report.

World Wide Web addresses contained in this Report are for explanatory purposes only and they (and the content contained therein) do not form a part of and are not incorporated by reference into this Report.

Net Element, Inc.

Form 10-Q

For the Three Months Ended March 31, 2016

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PART I — FINANCIAL INFORMATION

NET ELEMENT, INC.

UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS

	March 31, 2016	December 31, 2015
ASSETS		
Current assets:		
Cash	$ 724,509	$ 1,025,747
Accounts receivable, net	4,424,761	5,198,993
Prepaid expenses and other assets	1,311,979	1,106,016
Total current assets, net	6,461,249	7,330,756
Fixed assets, net	151,212	162,123
Intangible assets, net	4,969,863	5,423,880
Goodwill	9,643,752	9,643,752
Other long term assets	389,680	353,050
Total assets	21,615,756	22,913,561
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	5,075,959	5,858,837
Deferred revenue	572,002	743,910
Accrued expenses	3,131,234	2,975,066
Notes payable (current portion)	570,017	518,437
Due to related parties	1,239,856	329,881
Total current liabilities	10,589,068	10,426,131
Notes payable (net of current portion)	3,469,983	3,446,563
Total liabilities	14,059,051	13,872,694
STOCKHOLDERS' EQUITY		
Series A Convertible Preferred stock ($.0001 par value, 1,000,000 shares authorized, no shares issued and outstanding at March 31, 2016 and December 31, 2015)	-	-
Common stock ($.0001 par value, 300,000,000 shares authorized and 11,316,869 and 11,261,960 shares issued and outstanding at March 31, 2016 and December 31, 2015, respectively)	1,132	1,126
Paid in capital	154,792,862	154,361,694
Accumulated other comprehensive loss	(1,595,563)	(1,565,822)
Accumulated deficit	(145,802,767)	(143,955,048)
Noncontrolling interest	161,041	198,917
Total stockholders' equity	7,556,705	9,040,867
Total liabilities and stockholders' equity	$ 21,615,756	$ 22,913,561

See accompanying notes to unaudited condensed consolidated financial statements.

NET ELEMENT, INC.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS

	Three months ended March 31,	
	2016	2015
Net revenues		
Service fees	$9,363,820	$5,540,207
Branded content	1,897,239	-
Total Revenues	11,261,059	5,540,207
Costs and expenses:		
Cost of service Fees	7,598,184	4,614,072
Cost of branded content	1,787,057	-
General and administrative (includes $360,984 and $601,371 of share based compensation for the three months ended March 31, 2016 and 2015 respectively)	2,449,297	2,637,469
Bad debt expense	251,741	9,331
Depreciation and amortization	888,118	438,769
Total costs and operating expenses	12,974,397	7,699,641
Loss from operations	(1,713,338)	(2,159,434)
Interest expense, net	(150,438)	(117,594)
Other (expense) income	(21,819)	29,073
Net loss before income taxes	(1,885,595)	(2,247,955)
Income taxes	-	-
Net loss	(1,885,595)	(2,247,955)
Net loss attributable to the noncontrolling interest	37,876	8,747
Net loss attributable to Net Element, Inc. stockholders	(1,847,719)	(2,239,208)
Foreign currency translation	(29,741)	(108,167)
Comprehensive loss attributable to common stockholders	$(1,877,460)	$(2,347,375)
Loss per share - basic and diluted	$(0.16)	$(0.49)
Weighted average number of common shares outstanding - basic and diluted	11,293,434	4,605,797

See accompanying notes to unaudited condensed consolidated financial statements.

NET ELEMENT, INC.

UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Three Months Ended March 31,	
	2016	2015
Cash flows from operating activities		
Net loss	$(1,847,719)	$(2,239,208)
Adjustments to reconcile net loss to net cash used in operating activities		
Non controlling interest	(37,876)	(8,747)
Share based compensation	360,984	601,371
Deferred revenue	(171,908)	(34,858)
Depreciation and amortization	888,118	438,769
Changes in assets and liabilities		
Accounts receivable	436,453	131,020
Prepaid expenses and other assets	334,291	278,319
Accounts payable	(865,158)	667,819
Accrued expenses	(44,186)	356
Net cash used in operating activities	(947,001)	(165,159)
Cash flows from investing activities		
Purchase of fixed and other assets	(396,819)	(6,849)
Net cash used in investing activities	(396,819)	(6,849)
Cash flows from financing activities		
Proceeds from indebtedness	75,000	650,000
Repayment of indebtedness	-	(8,710)
Related party advances	910,045	125,000
Net cash provided by financing activities	985,045	766,290
Effect of exchange rate changes on cash	57,537	(331,346)
Net (decrease) increase in cash	(301,238)	262,936
Cash at beginning of period	1,025,747	503,343
Cash at end of period	$724,509	$766,279
Supplemental disclosure of cash flow information		
Cash paid during the period for:		
Interest	$150,438	$118,910
Taxes	$86,770	$30,505

See accompanying notes to unaudited condensed consolidated financial statements.

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NET ELEMENT, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

Net Element, Inc. (“We”, “us”, “our” or the “Company”) is a financial technology-driven group specializing in mobile payments and other transactional services in emerging countries and in the United States. We have three reportable segments: (i) North America Transaction Solutions for electronic commerce, (ii) Mobile Solutions (primary Russian Federation and CIS) (iii) Online Solutions, which started up with our acquisition of PayOnline Solutions on May 20, 2015. We are differentiated by our proprietary technology which enables us to provide a broad suite of payment products, end-to-end transaction processing services and superior client support. We are able to deliver these services across multiple points of access, or “multi-channel,” including brick and mortar locations, software integration, e-commerce, mobile operator billing, mobile and tablet-based solutions. In the United States, via our U.S. based subsidiaries, we generate revenues from transactional services and other payment technologies for small and medium-sized businesses. Through TOT Group Russia and Net Element Russia, we provide transactional services, mobile payment transactions, online payment transactions and other payment technologies in emerging countries in the Russian Federation, CIS, Europe and Asia.

Business

Our transactional services business enables merchants to accept credit cards as well as other forms of payment, including debit cards, checks, gift cards, loyalty programs and alternative payment methods in traditional card-present or swipe transactions, as well as card-not-present transactions, such as those conducted over the phone or through the Internet or a mobile device. We market and sell our services through both independent sales groups (“ISGs”), which are non-employee, external sales organizations and other third party resellers of our products and services, and directly to merchants through electronic media, telemarketing and other programs, including utilizing partnerships with other companies that market products and services to local and international merchants. In addition, we partner with banks such as BMO Harris Bank, N.A. in the United States and VTB Bank, Bank of Moscow, Raiffeisen Bank, Kazkommertsbank, and Rietumu Bank in the Russian Federation, CIS, Europe and Asia to sponsor us for membership in Visa® , MasterCard® and/or other card associations and to settle transactions with merchants. We perform core functions for merchants such as application processing, underwriting, account set-up, risk management, fraud detection, merchant assistance and support, equipment deployment and chargeback services.

Our mobile payments business, Digital Provider, LLC (f/k/a Tot Money, LLC) (“Digital Provider”) provides carrier-integrated mobile payments solutions. Our relationships with mobile operators give us substantial geographic coverage, a strong capacity for innovation in mobile payments and messaging, and the ability to offer our clients in-app, premium SMS, online and carrier billing services. We also market our own branded content which is a new business line for our mobile commerce business.

PayOnline provides flexible high-tech payment solutions to companies doing business on the Internet or in the mobile environment. PayOnline specializes in integration and customization of payment solutions for websites and mobile apps. In particular, PayOnline arranges payment on the website of any commercial organization, which increases the convenience of using the website and helps maximize the number of successful transactions. In addition, PayOnline is focused on providing online and mobile payment acceptance services to the travel industry through direct integration with leading Global Distribution Systems, which includes Amadeus® and Sabre®. Key regions of the PayOnline company are the CIS, Eastern Europe, Central Asia, Western Europe, North America and Asia major sub regions. PayOnline offices are located in Russia and in the Republic of Cyprus. We included the results of PayOnline starting in May 20, 2015.

Aptito is a proprietary, next-generation, cloud-based payments platform for the hospitality industry, which creates an online consumer experience in offline commerce environments via tablet, mobile and all other cloud-connected devices. Aptito’s easy to use point-of-sale (“POS”) system makes things easier by providing comprehensive solution to the hospitality industry to help streamline management and operations. Orders placed tableside by customers directly speed up the ordering process and improve overall efficiency. Aptito's mobile POS system provides portability to the staff while performing all the same functions as a traditional POS system, and more.

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("U.S. GAAP") and reflect all adjustments, which are of a normal and recurring nature, that are, in the opinion of management, necessary for a fair presentation of our condensed consolidated financial position and results of operations for the related periods. All significant intercompany transactions and balances have been eliminated in consolidation. The consolidated results of operations for any interim periods are not necessarily indicative of results to be expected for the full year.

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities as of the balance sheet date and the reported amounts of expenses for the period presented. Actual results could differ from those estimates.

Significant estimates include (i) the valuation of acquired merchant portfolios, (ii) the recoverability of indeterminate-lived assets, (iii) the remaining useful lives of long-lived assets, and (iv) the sufficiency of merchant, aggregator, legal, and other reserves. On an ongoing basis, we evaluate the sufficiency and accuracy of our estimates. Actual results could differ from those estimates.

Cash and Cash Equivalents

We maintain our U.S. dollar-denominated cash in several non-interest bearing bank deposit accounts and we have no cash equivalents. At March 31, 2016 and December 31, 2015, the U.S. based bank balances did not exceed Federal Deposit Insurance Corporation (FDIC) insured institution limits of $250,000.

We maintain approximately $609,885 and $922,062 in uninsured bank accounts in Russia, Ukraine, Cyprus and the Cayman Islands at March 31, 2016 and December 31, 2015, respectively.

Accounts Receivable and Allowance for Doubtful Accounts

Receivables are stated net of allowance for doubtful accounts. We estimate an allowance based on experience with our service providers and judgment as to the likelihood of their ultimate payment. We also consider collection experience and make estimates regarding collectability based on payout trends of the customers. In Russia, the service providers are large telecommunication companies and their affiliates, so we do not reserve for these receivables given their financial strengths and historical experience. Allowance for doubtful accounts was $103,031 at March 31, 2016 and December 31, 2015 respectively.

Other Current Assets

We maintain an inventory of point of sale terminals (including iPads® used for mobile point of sale), which we use to service both merchants and independent sales agents. If the terminals are sold for a fee, we expense the cost of these terminals, plus any setup fees at the time of the sale. Often, we will provide the terminals as an incentive to such merchants and independent sales agents to enter into a merchant contract with us, which have an average length of three years. In such case, the cost of the terminal plus any setup fees will be amortized over the three years. If the merchants early terminate their contract with us, they are obligated to either return the terminal or pay for the terminal. We had $414,297 in terminals and related equipment at March 31, 2016 and $345,459 at December 31, 2015, of which $190,874 has been placed with merchants at March 31, 2016 and $268,501 at December 31, 2015. Amortization of these terminals amounted to $36,646 and $30,735 for the three months ended March 31, 2016 and 2015, respectively.

Fixed Assets

We depreciate our furniture and equipment over a term of three to ten years. Computers and software are depreciated over terms between two and five years. Leasehold improvements are depreciated over the shorter of the economic life or term of each lease. All of our assets are depreciated on a straight-line basis for financial statement purposes.

Expenditures for repairs and maintenance are charged to operating expense as incurred. Expenditures that increase the value or productive capacity of assets are capitalized. At the time of retirements, sales, or other dispositions of property and equipment, the original cost and related accumulated depreciation are removed from the respective accounts, and the gains or losses are presented as other expenses.

Impairment of Long-Lived Assets

We review our long-lived assets for impairment whenever events or changes indicate that the carrying amount of an asset or group of assets may not be recoverable. During the three months ended March 31, 2016 and 2015, we did not recognize any charges for impairment of goodwill and intangible assets.

Intangible Assets

Included in our intangible assets are merchant portfolios which represent the net carrying value of an acquired merchant customer base. Merchant portfolios are amortized on a straight-line basis over their respective useful lives, generally three to five years. Merchant portfolios are assessed for impairment if events or circumstances indicate that their respective carrying values are not recoverable from the future anticipated undiscounted net cash flows attributable to such assets. In such cases, the amount of any potential impairment would be measured as the excess, if any, of carrying value over the fair value of such assets.

We also capitalize direct expenses associated with filing of patents and patent applications, and amortize the capitalized intellectual property costs over five years beginning when the patent is approved.

Additionally, we capitalize the fair value of intangible assets acquired in business combinations. We obtain third party valuations of net assets acquired, and allocate the purchase price of each acquired business to its respective net tangible and intangible assets. Acquired intangible assets include: merchant portfolios, trade and domain names, non-compete agreements, customer relationships, technology and certain contracts.

Capitalized Customer Acquisition Costs, Net

Included in intangible assets are capitalized customer acquisition costs, which consist of up-front cash payments made to certain ISGs for the establishment of new merchant relationships. Capitalized customer acquisition costs represent incremental, direct customer acquisition costs that are recoverable through gross margins (future net cash flows) associated with merchant contracts. The up-front payment to the ISG is based on the estimated gross margin for the first year of the merchant contract. The deferred customer acquisition cost asset is recorded at the time of payment and the capitalized acquisition costs are primarily amortized on a straight-line basis over a period of three years.

Management evaluates the capitalized customer acquisition cost for impairment at each balance sheet date by comparing, on a pooled basis by vintage month of origination, the expected future net undiscounted cash flows from underlying merchant relationships to the carrying amount of capitalized customer acquisition costs. If the estimated future net cash flows are lower than the recorded carrying amount, indicating an impairment of the carrying value of the capitalized customer acquisition costs, the impairment loss is charged to operations.

Unamortized customer acquisition costs were $1,255,231 and $1,048,060 at March 31, 2016 and December 31, 2015, respectively, and are reflected as intangible assets in the accompanying unaudited condensed consolidated balance sheets. During the three months ended March 31, 2016, we capitalized customer acquisition costs of $350,475, and amortized $143,304 over the three months ended March 31, 2016. During the twelve months ended December 31, 2015, we capitalized customer acquisition costs of $878,085, and amortized $356,757 over the twelve months ended December 31, 2015.

Goodwill

Goodwill represents the excess of the cost of the Company's investment in the net assets of acquired companies over the fair value of the underlying identifiable net assets at the dates of acquisition. The Company attributes all goodwill associated with the acquisitions of Unified Payments and PayOnline.

Goodwill is not amortized but is tested, using the income approach, for impairment on an annual basis and between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of the related entity below its carrying value.

The income approach employs a cash flow model that takes into account (1) assumptions that market participants would use in their estimates of fair value, (2) current period actual results, and (3) budgeted results for future periods that have been vetted by senior management.

Accrued Residual Commissions

We pay agent commissions to ISGs and independent sales agents based on the processing volume of the merchants enrolled. The commission payments are based on varying percentages of the volume processed by us on behalf of the merchants. Percentages vary based on the program type and transaction volume of each merchant. We report commission payments as a cost of revenues in the accompanying condensed consolidated statements of operations and comprehensive loss.

At March 31, 2016 and December 31, 2015, the residual commissions payable to ISGs and independent sales agents were $702,526 and $1,205,751, respectively.

We pay agent commission on annual fees between January and April of each year. We amortize the annual fees paid in equal monthly amounts from date of payment to end of year. We pay our agent commissions for annual fees in advance of recognizing the associated revenue. We deferred $318,566 and $483,090 of agent commissions paid for annual fees at March 31, 2016 and December 31, 2015, respectively.

Prepaid agent commissions for annual fees are included in prepaid expenses, and commissions payable are included in accounts payable in the accompanying condensed consolidated balance sheets.

Fair Value Measurements

Our financial instruments consist primarily of cash, accounts receivable, accounts payable and debt instruments. The carrying values of cash, accounts receivable and trade payables are considered to be representative of their respective fair values due to the short-term nature of these instruments. The carrying amount of the debt instruments of $4,040,000 at March 31, 2016 and $3,965,000 at December 31, 2015 approximates fair value because our current borrowing rate does not materially differ from market rates for similar bank borrowings.