

SYNTHESIS ENERGY SYSTEMS INC

FORM 10-Q (Quarterly Report)

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Address	THREE RIVERWAY, SUITE 300 HOUSTON, TX 77056
Telephone	713-579-0600
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Industry	Renewable Energy Equipment & Services
Sector	Energy
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2016

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: 001-33522

SYNTHESIS ENERGY SYSTEMS, INC.

(Exact name of registrant as specified in its charter)

Delaware
(State of Incorporation)

20-2110031
(I.R.S. Employer Identification No.)

Three Riverway, Suite 300, Houston, Texas
(Address of principal executive offices)

77056
(Zip code)

Registrant's telephone number, including area code: (713) 579-0600

Former name, former address and former fiscal year, if changed since last report: N/A

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 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 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.

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

As of October 31, 2016 there were 87,044,085 shares of the registrant's common stock, par value \$.01 per share, outstanding.

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PART I

Item 1. Financial Statements

SYNTHESIS ENERGY SYSTEMS, INC.
Consolidated Balance Sheets
(In thousands, except per share amount)

	September 30, 2016	June 30, 2016
	<u>(Unaudited)</u>	<u></u>
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 11,048	\$ 13,807
Accounts receivable, net	26	27
Prepaid expenses and other current assets	1,132	828
Inventory	42	43
Assets of discontinued operations	<u>12,003</u>	<u>12,662</u>
Total current assets	24,251	27,367
Property, plant and equipment, net	111	54
Intangible asset, net	884	898
Investment in joint ventures	26,201	26,201
Other long-term assets	<u>625</u>	<u>661</u>
Total assets	<u>\$ 52,072</u>	<u>\$ 55,181</u>
LIABILITIES AND EQUITY		
Current liabilities:		
Accrued expenses and accounts payable	\$ 1,588	\$ 1,655
Liabilities of discontinued operations	<u>12,997</u>	<u>13,337</u>
Total current liabilities	<u>14,585</u>	<u>14,992</u>
Commitment and contingencies (Note 9)		
Preferred stock, \$0.01 par value- 20,000 shares authorized – no shares issued and outstanding	—	—
Common stock, \$0.01 par value: 200,000 shares authorized: 87,044 and 86,984 shares issued and outstanding, respectively	870	870
Additional paid-in capital	261,508	261,225
Accumulated deficit	(229,885)	(226,938)
Accumulated other comprehensive income	<u>6,640</u>	<u>6,586</u>
Total shareholder's equity	39,133	41,743
Noncontrolling interests in subsidiaries	<u>(1,646)</u>	<u>(1,554)</u>
Total equity	<u>37,487</u>	<u>40,189</u>
Total liabilities and equity	<u>\$ 52,072</u>	<u>\$ 55,181</u>

See accompanying notes to the consolidated financial statements.

SYNTHESIS ENERGY SYSTEMS, INC.
Consolidated Statements of Operations
(In thousands, except per share amounts)
(Unaudited)

	Three Months Ended	
	September 30,	
	2016	2015
Revenue:		
Technology licensing and related services	\$ —	\$ 247
Total revenue	—	247
Costs and Expenses:		
Costs of sales and plant operating	—	177
General and administrative expenses	2,332	1,965
Stock-based expense	257	1,131
Depreciation and amortization	39	57
Total costs and expenses	2,628	3,330
Operating loss	(2,628)	(3,083)
Non-operating (income) expense:		
Foreign currency losses, net	26	119
Interest income	(5)	(10)
Loss from continuing operations	(2,649)	(3,192)
Loss from discontinued operations	(389)	(1,584)
Net Loss	(3,038)	(4,776)
Less: net loss attributable to noncontrolling interests	(91)	(194)
Net loss attributable to SES stockholders	\$ (2,947)	\$ (4,582)
Net loss attributable to SES stockholders:		
From continuing operations	(2,567)	(3,003)
From discontinued operations	(380)	(1,579)
Net loss attributable to SES stockholders	\$ (2,947)	\$ (4,582)
Net loss per share (Basic and diluted):		
From continuing operations	(0.03)	(0.03)
From discontinued operations	(0.00)	(0.02)
Net loss attributable to SES stockholders	\$ (0.03)	\$ (0.05)
Weighted average common shares outstanding:		
Basic and diluted	86,988	86,346

See accompanying notes to the consolidated financial statements.

SYNTHESIS ENERGY SYSTEMS, INC.
Consolidated Statements of Comprehensive Loss
(In thousands)
(Unaudited)

	Three Months Ended September 30,	
	2016	2015
Net loss	\$ (3,038)	\$ (4,776)
Currency translation adjustment	53	(620)
Comprehensive loss	(2,985)	(5,396)
Less comprehensive loss attributable to noncontrolling interests	(92)	(211)
Comprehensive loss attributable to the Company	\$ (2,893)	\$ (5,185)

See accompanying notes to the consolidated financial statements

SYNTHESIS ENERGY SYSTEMS, INC.
Consolidated Statements of Cash Flows
(In thousands)
(Unaudited)

	Three Months Ended	
	September 30,	
	2016	2015
Cash flows from operating activities:		
Net loss	\$ (3,038)	\$ (4,776)
Adjustments to reconcile net loss to net cash used in operating activities:		
Stock-based expense	257	1,131
Loss on disposal of property, plant and equipment	93	—
Depreciation and amortization	196	225
Foreign currency losses	—	246
Changes in operating assets and liabilities:		
Accounts receivable	—	561
Prepaid expenses and other current assets	(15)	(284)
Inventory	26	(920)
Other long-term assets	(16)	(14)
Accrued expenses and payables	(285)	1,966
Net cash used in operating activities	(2,782)	(1,865)
Cash flows from investing activities:		
Capital expenditures	(4)	(9)
Net cash used in investing activities	(4)	(9)
Cash flows from financing activities:		
Payments on long-term bank loan	—	—
Proceeds from exercise of stock options	26	279
Proceeds from issuance of common stock	—	1,000
Net cash provided by financing activities	26	1,279
Net decrease in cash	(2,760)	(595)
Cash and cash equivalents, beginning of period	13,819	22,217
Effect of exchange rates on cash	(11)	(150)
Cash and cash equivalents, end of period	\$ 11,048	\$ 21,472

See accompanying notes to the consolidated financial statements.

SYNTHESIS ENERGY SYSTEMS, INC.
Consolidated Statement of Equity
(In thousands)
(Unaudited)

	Common Stock		Additional Paid-in Capital	Deficit Accumulated During the Development Stage	Accumulated Other Comprehensive Income	Non- controlling Interest	Total
	Shares	Common Stock					
Balance at June 30, 2015	85,476	\$ 855	\$ 256,643	\$ (203,866)	\$ 6,179	\$ (1,038)	\$ 58,773
Net loss	—	—	—	(4,582)	—	(194)	(4,776)
Currency translation adjustment	—	—	—	—	(603)	(17)	(620)
Net proceeds from issuance of common stock	1,000	10	990	—	—	—	1,000
Exercise of stock options	372	3	276	—	—	—	279
Stock-based expense	—	—	1,131	—	—	—	1,131
Balance at September 30, 2015	<u>86,848</u>	<u>\$ 868</u>	<u>\$ 259,040</u>	<u>\$ (208,448)</u>	<u>\$ 5,576</u>	<u>\$ (1,249)</u>	<u>\$ 55,787</u>
Balance at June 30, 2016	86,984	\$ 870	\$ 261,225	\$ (226,938)	\$ 6,586	\$ (1,554)	\$ 40,189
Net loss	—	—	—	(2,947)	—	(91)	(3,038)
Currency translation adjustment	—	—	—	—	54	(1)	53
Exercise of stock options	40	—	26	—	—	—	26
Stock-based expense	20	—	257	—	—	—	257
Balance at September 30, 2016	<u>87,044</u>	<u>\$ 870</u>	<u>\$ 261,508</u>	<u>\$ (229,885)</u>	<u>\$ 6,640</u>	<u>\$ (1,646)</u>	<u>\$ 37,487</u>

See accompanying notes to the consolidated financial statements.

Note 1 — Summary of Significant Accounting Policies

(a) Organization and description of business

Synthesis Energy Systems, Inc. (“SES”), together with its wholly-owned and majority-owned controlled subsidiaries (collectively, the “Company”) is a global clean energy and gasification technology company that provides proprietary gasification technology systems and solutions to the energy and chemical industries. Our gasification technology is a flexible, efficient and economic technology for the production of synthesis gas, or syngas, a mixture of primarily hydrogen, carbon monoxide and methane. Syngas is a clean and versatile source of energy. Our technology is uniquely capable of manufacturing clean syngas from a wide variety of energy resources including most all existing forms of coal, biomass, municipal wastes and refuse derived fuels and petroleum coke. In doing so, our technology produces syngas which allows us to unlock the energy from these resources and transform the syngas into electric power as well as a natural gas substitute. Furthermore, our syngas can be used to produce a variety of chemical products, fertilizers and transportation fuels. Our proprietary fluidized bed technology is built on decades of research, development, demonstration and commercialization. At the present time, we have commercialized seven gasification units. In addition, we are in the process of commissioning five units and have two additional units under development. The Company’s headquarters is located in Houston, Texas and it has an additional administrative location for Chinese operations in Shanghai, China.

As noted in Note 2, in August 2016, the Company announced that it and Shandong Hai Hua Xecheng Energy (“Xuecheng Energy”) entered into a Definitive Agreement to restructure the ZZ Joint Venture. The agreement took full effect when the registration with the government was completed on October 31, 2016. During the second quarter of fiscal 2017, the Company will deconsolidate the ZZ Joint Venture and will account for our investment under the cost method. For purposes of these financials, the Company has classified all operations related to the ZZ Joint Venture as discontinued operations and have classified all assets and liabilities related to the ZZ Joint Venture as assets/liabilities of discontinued operations. Prior period results have been adjusted to reflect the current presentation.

(b) Basis of presentation and principles of consolidation

The consolidated financial statements for the periods presented are unaudited. Operating results for the three month period ended September 30, 2016 are not necessarily indicative of results to be expected for the fiscal year ending June 30, 2017.

The consolidated financial statements are in U.S. dollars. Non-controlling interests in consolidated subsidiaries in the consolidated balance sheets represents minority stockholders’ proportionate share of the equity in such subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation. These consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto reported in the Company’s Annual Report on Form 10-K for the year ended June 30, 2016. Significant accounting policies that are new or updated from those presented in the Company’s Annual Report on Form 10-K for the year ended June 30, 2016 are included below. The consolidated financial statements have been prepared in accordance with the rules of the United States Securities and Exchange Commission (“SEC”) for interim financial statements and do not include all annual disclosures required by generally accepted accounting principles in the United States.

(c) Accounting for Variable Interest Entities (“VIEs”) and Financial Statement Consolidation Criteria

The joint ventures which the Company enters into may be considered VIEs. The Company consolidates all VIEs where it is the primary beneficiary. This determination is made at the inception of the Company’s involvement with the VIE and is continuously assessed. The Company considers qualitative factors and forms a conclusion that the Company, or another interest holder, has a controlling financial interest in the VIE and, if so, whether it is the primary beneficiary. In order to determine the primary beneficiary, the Company considers who has the power to direct activities of the VIE that most significantly impacts the VIE’s performance and has an obligation to absorb losses from or the right to receive benefits of the VIE that could be significant to the VIE. The Company does not consolidate VIEs where it is not the primary beneficiary. The Company accounts for these unconsolidated VIEs using either the equity method of accounting if the Company has significant influence but not control, or the cost method of accounting and includes its net investment on its consolidated balance sheets. Under the equity method, the Company’s equity interest in the net income or loss from its unconsolidated VIEs is recorded in non-operating income (expense) on a net basis on its consolidated statements of operations. In the event of a change in ownership, any gain or loss resulting from an investee share issuance is recorded in earnings. Controlling interest is determined by majority ownership interest and the ability to unilaterally direct or cause the direction of management and policies of an entity after considering any third-party participatory rights.

The Company has determined that the ZZ Joint Venture is a VIE and has determined that the Company is the primary beneficiary. In making the initial determination, the Company considered, among other items, the change in profit distribution between the Company and Xuejiao (as defined in Note 2 – Current Projects) after 20 years. The expected negative variability in the fair value of the ZZ Joint Venture’s net assets was considered to be greater during the first 20 years of the ZZ Joint Venture’s life, which coincided with our original 95% profit/loss allocation, versus the latter 30 years in which the Company’s profit/loss allocation would be reduced to 10%. As the result of an amendment to the ZZ Joint Venture agreement in 2010, the profit distribution percentages will remain in place after the first 20 years, providing further support to the determination that the Company is the primary beneficiary.

As noted in Note 2, in August 2016, the Company announced that it and Shandong Hai Hua Xecheng Energy (“Xuecheng Energy”) entered into a Definitive Agreement to restructure the ZZ Joint Venture. The agreement took full effect when the registration with the government was completed on October 31, 2016. During the second quarter of fiscal 2017, the Company will deconsolidate the ZZ Joint Venture and will account for our investment under the cost method. For purposes of these financial statement, the Company has classified all operations related to the ZZ Joint Venture as discontinued operations and have classified all assets and liabilities related to the ZZ Joint Venture as assets/liabilities from discontinued operations. Prior period results have been adjusted to reflect the current presentation.

The Company has determined that the Yima Joint Ventures are VIEs and that Yima, the joint venture partner, is the primary beneficiary since Yima has a 75% ownership interest in the Yima Joint Ventures and has the power to direct the activities of the VIE that most significantly influence the VIE’s performance. The carrying value of our investment in the Yima Joint Ventures at both September 30, 2016 and June 30, 2016 was approximately \$26.2 million.

The Company has determined that the Tianwo-SES Joint Venture (as defined in Note 2 – Current Projects – Tianwo-SES Joint Venture) is a VIE and that STT, the joint venture partner, is the primary beneficiary since SST has a 65% ownership interest in the Tianwo-SES Joint Venture and has the power to direct the activities of the Tianwo-SES Joint Venture that most significantly influence its performance. Because of losses sustained by the Tianwo-SES Joint Venture, the carrying value of this joint venture is zero at both September 30, 2016 and June 30, 2016.

(d) Investment in joint ventures

We have equity investments in various privately held entities. We account for these investments either under the equity method or cost method of accounting depending on our ownership interest and level of influence. Investments accounted for under the equity method are recorded based upon the amount of our investment and adjusted each period for our share of the investee's income or loss. Investments are reviewed for changes in circumstance or the occurrence of events that suggest an other than temporary event where our investment may not be recoverable.

(e) Revenue Recognition

Revenue from sales of products, which has included the capacity fee and energy fee earned at the ZZ Joint Venture plant includes sale of methanol under the ZZ Cooperation Agreement, and sales of equipment are recognized when the following elements are satisfied: (i) there are no uncertainties regarding customer acceptance; (ii) there is persuasive evidence that an agreement exists; (iii) delivery has occurred; (iv) the sales price is fixed or determinable; and (v) collectability is reasonably assured. The Company records revenue net of any applicable value-added taxes.

Technology licensing revenue is typically received over the course of a project’s development as milestones are met. The Company may receive upfront licensing fee payments when a license agreement is entered into. Typically, the majority of a license fee is due once project financing and equipment installation occur. The Company recognizes license fees for the use of its gasification systems as revenue when the license fees become due and payable under the license agreement, subject to the deferral of the amount of the performance guarantee. Fees earned for engineering services, such as services that relate to integrating our technology to a customer’s project, are recognized using the percentage-of-completion method.

(f) Fair value measurements

Accounting standards require that fair value measurements be classified and disclosed in one of the following categories:

- 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; and
- Level 3 Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (i.e., supported by little or no market activity).

The Company's financial assets and liabilities are classified based on the lowest level of input that is significant for the fair value measurement. The following table summarizes the assets of the Company measured at fair value on a recurring basis as of September 30, 2016 and June 30, 2016 (in thousands):

	September 30, 2016			
	Level 1	Level 2	Level 3	Total
Assets:				
Certificates of Deposit	\$ —	\$ 50(1)	\$ —	\$ 50
Certificates of Deposit- Restricted	—	2,248(2)	—	2,248
Money Market Funds	10,509(3)	—	—	10,509

	June 30, 2016			
	Level 1	Level 2	Level 3	Total
Assets:				
Certificates of Deposit	\$ —	\$ 50(1)	\$ —	\$ 50
Certificates of Deposit- Restricted	—	2,262(2)	—	2,262
Money Market Funds	12,654(3)	—	—	12,654

- (1) Amount included in current assets on the Company's consolidated balance sheets.
- (2) Amount included in assets of discontinued operations on the Company's consolidated balance sheets.
- (3) Amount included in cash and cash equivalents on the Company's consolidated balance sheets.

The carrying values of the certificates of deposit and money market funds approximate fair value, which was estimated using quoted market prices for those or similar investments. The carrying value of the Company's other financial instruments, including accounts receivable, accounts payable and short-term debt approximate their fair values due to the short maturities on those instruments.

(g) Recently Issued Accounting Standards

In May 2014, the Financial Accounting Standards Board ("FASB") issued ASU No. 2014-09, which creates Accounting Standards Codification ("ASC") Topic 606, "Revenue from Contracts with Customers," and supersedes the revenue recognition requirements in Topic 605, "Revenue Recognition," including most industry-specific revenue recognition guidance throughout the Industry Topics of the Codification. In addition, ASU No. 2014-09 supersedes the cost guidance in Subtopic 605-35, "Revenue Recognition—Construction-Type and Production-Type Contracts," and creates new Subtopic 340-40, "Other Assets and Deferred Costs—Contracts with Customers." In summary, the core principle of Topic 606 is to recognize revenue when promised goods or services are transferred to customers in an amount that reflects the consideration that is expected to be received for those goods or services. Companies are allowed to select between two transition methods: (1) a full retrospective transition method with the application of the new guidance to each prior reporting period presented, or (2) a retrospective transition method that recognizes the cumulative effect on prior periods at the date of adoption together with additional footnote disclosures. The amendments in ASU No. 2014-09 are effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period, and early application is not permitted. In March 2016 and April 2016, the FASB issued ASU No. 2016-08 and ASU No. 2016-10, respectively. The amendments in ASU No. 2016-08 and ASU No. 2016-10 do not change the core principle of ASU No. 2014-09, but instead clarify the implementation guidance on principle versus agent considerations and identify performance obligations and the licensing implementation guidance, respectively. We are currently evaluating the impact the adoption of this guidance will have on our consolidated financial statements and have not made any decision on the method of adoption.

In November 2015, the FASB issued ASU No. 2015-17, which amends ASC Topic 740, “Income Taxes.” This amendment aligns the presentation of deferred income tax assets and liabilities with International Financial Reporting Standards. International Accounting Standard 1, *Presentation of Financial Statements*, requires deferred tax assets and liabilities to be classified as noncurrent in a classified statement of financial position. The current requirement that deferred tax liabilities and assets be offset and presented as a single amount is not affected by the amendments in this update. The standard is effective for interim and annual reporting periods beginning after December 15, 2016. The amendments in this update may be applied either prospectively to all deferred tax liabilities and assets or retrospectively to all periods presented. The adoption of this guidance did not have a material impact on our financial condition, results of operations, cash flows or financial disclosures.

In February 2016, the FASB issued ASU No. 2016-02, which creates ASC Topic 842, “Leases.” This update increases transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. This guidance is effective for interim and annual reporting periods beginning after December 15, 2018. We are evaluating what impact, if any, the adoption of this guidance will have on our financial condition, results of operations, cash flows or financial disclosures.

In March 2016, the FASB issued ASU No. 2016-09, which amends ASC Topic 718, “Compensation – Stock Compensation.” This amendment simplifies several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities and classification on the statement of cash flows. This guidance is effective for interim and annual reporting periods beginning after December 15, 2016. We are evaluating what impact, if any, the adoption of this guidance will have on our financial condition, results of operations, cash flows or financial disclosures.

In August 2016, the FASB issued an accounting standards update which provides additional clarity on the classification of specific events on the statement of cash flows. These events include: debt prepayment and extinguishment costs, settlement of zero-coupon debt instruments, contingent consideration payments made after a business combination, proceeds from settlement of insurance claims, distributions received from equity method investees, and beneficial interests in securitization transactions. The update is effective for annual reporting periods beginning after December 15, 2017, including interim periods within those annual reporting periods, with early application permitted. We are evaluating what impact, if any, the adoption of this guidance will have on our financial condition, results of operations, cash flows or financial disclosures.

Note 2 – Current Projects

Synthesis Energy Systems (Zao Zhuang) New Gas Company Ltd. (“ZZ Joint Venture”)

In July 2006, we entered into a cooperative joint venture contract Xuecheng Energy which established the ZZ Joint Venture, a joint venture company that has the primary purposes of:

- developing, constructing and operating a syngas production plant utilizing SGT in Zao Zhuang City, Shandong Province, China and
- producing and selling syngas and the various byproducts of the plant.

We initially owned 97.6% of the ZZ Joint Venture and Xuecheng Energy owned the remaining 2.4%. In June 2015, we entered into a Share Purchase and Investment Agreement (the “SPA”) with Rui Feng Enterprises Limited (“Rui Feng”), whereby Rui Feng will acquire a controlling interest in Synthesis Energy Systems Investments Inc. (“SESI”), and a wholly owned subsidiary, which owns our interest in the ZZ Joint Venture. Under the terms of the SPA, SESI originally agreed to sell an approximately 61% equity interest to Rui Feng in exchange for \$10 million. This amount was to be paid in four installments through December 2016, with the first installment of approximately \$1.6 million paid on June 26, 2015.

Rui Feng's second installment payment was due in December 2015 and the third installment was due on May 1, 2016, and neither of these installment payments has been made. With the restructuring of the ZZ Joint Venture discussed below, we do not anticipate that Rui Feng will make any additional installment payments under the SPA. If Rui Feng does not make the required installment payments, we would be entitled to terminate the agreement and Rui Feng would lose future rights to acquire additional interest in SESI and additional positions on the board of SESI.

Because Rui Feng has not made additional installment payments, as of September 30, 2016, we owned approximately 88.1% of the ZZ Joint Venture as of September 30, 2016.

ZZ Joint Venture Debt Agreements

In October 2014, the ZZ Joint Venture entered into a working capital loan agreement (the "ZZ Working Capital Loan") with Zaozhuang Bank Co., Ltd. ("ZZ Bank"), and received approximately \$3.3 million of loan proceeds, with a maturity of September 23, 2015. In September 2015, the Company refinanced the ZZ Working Capital Loan through August 2016 for approximately \$3.0 million. This amount was refinanced again in August 2016 through November 2016.

In October 2014, the ZZ Joint Venture entered two lines of credit with the ZZ Bank for a total of \$3.3 million (collectively, the "ZZ Line of Credit Agreement"). In April 2015, the Company repaid the ZZ Line of Credit Agreement and renewed the agreement for \$3.3 million under the same terms for an additional six months. In November 2015, the Company repaid \$3.3 million of the ZZ Line of Credit Agreement, and refinanced the ZZ Line of Credit Agreement with the ZZ Bank for \$3.7 million which matures in November 2016.

Agreement with Xuecheng Energy

In August 2016, we announced that we and Xuecheng Energy have entered into a definitive agreement to restructure the ZZ Joint Venture. Additionally, to dovetail with the Chinese government's widespread initiative to move industry into larger scale, commercial and environmentally beneficial industrial parks, the partners intend to evaluate a new ZZ syngas facility in the Zouwu Industrial Park in Shandong Province. We will retain an approximate nine percent ownership in the ZZ Joint Venture asset, and Xuecheng Energy has agreed to assume all outstanding liabilities of the ZZ Joint Venture, including payables related to the Cooperation Agreement with Xuecheng Energy signed in 2013. The definitive agreement took full effect when the registration with the government was completed on October 31, 2016. During the second quarter of fiscal 2017 we will deconsolidate the ZZ Joint Venture and will account for our investment under the cost method. For purposes of these financial statements, the Company has classified all operations related to the ZZ Joint Venture as discontinued operations and have classified all assets and liabilities related to the ZZ Joint Venture as assets/liabilities of discontinued operations. Prior period results have been adjusted to reflect the current presentation.

Yima Joint Ventures

In August 2009, we entered into amended joint venture contracts with the Yima Coal Industry Group Company ("Yima"), replacing the prior joint venture contracts entered into in October 2008 and April 2009. The joint ventures were formed for each of the gasification, methanol/methanol protein production, and utility island components of the plant (collectively the "Yima Joint Ventures"). The amended joint venture contracts provide that:

- We and Yima contribute equity of 25% and 75%, respectively, to the Yima Joint Ventures;
- Yima will guarantee the repayment of loans from third party lenders for 50% of the project's cost and, if debt financing is not available, Yima is obligated to provide debt financing via shareholder loans to the project until the project is able to secure third-party debt financing; and
- Yima will supply coal to the project from a mine located in close proximity to the project at a preferential price.

We own a 25% interest in each joint venture and Yima owns a 75% interest. Notwithstanding this, in connection with an expansion of the project, we have the option to contribute a greater percentage of capital for the expansion, such that as a result, we could expand through contributions, at our election, up to a 49% ownership interest in the Yima Joint Ventures.

The remaining capital for the project has been funded with project debt obtained by the Yima Joint Ventures. Yima agreed to guarantee the project debt in order to secure debt financing from domestic Chinese banking sources. We have agreed to pledge to Yima our ownership interests in the joint ventures as security for our obligations under any project guarantee. In the event that the necessary additional debt financing is not obtained, Yima has agreed to provide a loan to the joint ventures to satisfy the remaining capital needs of the project with terms comparable to current market rates at the time of the loan.

Under the terms of the joint venture agreements, the Yima Joint Ventures are to be governed by a board of directors consisting of eight directors, two of whom were appointed by us and six of whom were appointed by Yima. The joint ventures also have officers that are nominated by us, Yima and/or the board of directors pursuant to the terms of the joint venture contracts. We and Yima shall share the profits, and bear the risks and losses, of the joint ventures in proportion to our respective ownership interests. The term of the joint venture shall commence upon each joint venture company obtaining its business operating license and shall end 30 years after commercial operation of the plant.

We believe there is a consistent pattern of the Yima Joint Venture management not demonstrating an understanding of the methanol facility operations and not sourcing available expertise in China to improve the overall operations. We have witnessed operation of the gasifier systems at Yima with design and operating parameter deviations from our existing technology recommendations. We continue to experience a limited ability to influence the Yima Joint Ventures' operating performance.

As a result of the issues noted above, Yima restructured the management of the Yima Joint Ventures under the direction of the Henan Coal Gasification Company ("Henan"), which is an affiliated company reporting directly to Henan Coal and Energy Group Companies. The ownership of the Yima Joint Ventures is unchanged. Henan currently has full authority of day to day operational and personnel decisions at the Yima Joint Venture.

Since 2014, we have accounted for this joint venture under the cost method of accounting. Our conclusion to account for this joint venture under this methodology is based upon our lack of significant influence in the Yima Joint Venture. The lack of significant influence is determined based upon our interactions with the Yima Joint Ventures related to the start-up and operations and due to various other circumstances including limited participation in operating and financial policymaking processes and our limited ability to influence decisions which contribute to the financial success of the Yima Joint Ventures.

Current Yima Operating Description

Despite initiating methanol production in December 2012, the Yima Joint Ventures' plant continued its construction through the beginning of 2016. In March 2016, the Yima Joint Ventures completed the required performance testing of the SGT systems and successfully issued its Performance Test Certificate. Because of the extended construction period, the plant recently faced increasing regulatory scrutiny from the environmental and safety bureaus.

In June 2016, the local environmental bureau requested that the plant temporarily halt operations to address certain issues identified by the environmental bureau. After the plant shut down operations, the Yima plant experienced an accident during maintenance activities that were unrelated to the gasification units. The Yima Joint Ventures have been working with both the environmental and safety bureaus and is anticipated to return to operations in November 2016.

In 2009, the project was approved as three separate joint ventures. The approval for the original joint ventures was for the production of methanol protein, and methanol by-product. This has impacted the ability of the plant to sell pure methanol on the open market and has been an impediment to receive the permanent safety operating permit.

To resolve these issues, during the quarter ended June 30, 2016, the Yima Joint Ventures commenced an organizational restructuring to better streamline the operations of the Joint Ventures. This restructuring effort was a multi-step process, including first obtaining the operating license to sell methanol by combining the three joint ventures into a single operating entity, and finally obtaining the permanent safety and environmental permits. The Yima Joint Ventures received the operating permit in July 2016, and have made continued progress in completing the remaining items.

The Yima Joint Ventures also are experiencing certain liquidity concerns with a series of third party bank notes due prior to the end of December 2016. Yima, the 75% shareholder of the Yima Joint Ventures, has been routinely providing liquidity to the Yima Joint Ventures in the form of shareholder loans and during the first quarter Yima successfully refinanced, for one full year through October 2017, certain amounts which were to become due in October 2016. The Yima Joint Ventures are currently in discussion with the impacted third party lenders to seek additional extensions, refinancing or other alternative arrangements to avoid a default by the Yima Joint Ventures. While we believe Yima will continue to provide additional liquidity to the Yima Joint Ventures until the project is operating and producing income, we can make no assurances that Yima will continue to do this or on the outcome of the above mentioned negotiations.

Because of the situations detailed above, our management evaluated the current conditions of the Yima Joint Ventures to determine whether an other than temporary decrease in value had occurred for the year ended June 30, 2016. Management determined that the decrease in value due to the shutdown and liquidity situation were other than temporary in nature and therefore management conducted an impairment analysis utilizing a discounted cash flow fair market valuation with the assistance of a third party valuation expert. In this valuation, significant unobservable inputs were used to calculate the fair value of the investment. The valuation led to the conclusion that the investment in the Yima Joint Ventures was impaired as of June 30, 2016, and accordingly, we recorded an \$8.6 million impairment for the fiscal year ended June 30, 2016. Management determined that there was not an other than temporary impairment of value of our Yima investment during the quarter ended September 30, 2016. The carrying value of our Yima investment was approximately \$26.2 million as of both September 30, 2016 and June 30, 2016. We continue to monitor the Yima Joint Ventures and could take an additional impairment in the future if operating conditions do not meet our current expectations, or if the liquidity situation worsens.

Tianwo-SES Clean Energy Technologies Limited (the “Tianwo-SES Joint Venture”)

Joint Venture Contract

In February 2014, SES Asia Technologies Limited, one of our wholly owned subsidiaries, entered into a Joint Venture Contract (the “JV Contract”) with Zhangjiagang Chemical Machinery Co., Ltd., which subsequently changed its legal name to Suzhou Thvow Technology Co. Ltd. (“STT”), to form the Tianwo-SES Joint Venture. The purpose of the Tianwo-SES Joint Venture is to establish the Company’s gasification technology as the leading gasification technology in the Tianwo-SES Joint Venture territory (which is China, Indonesia, the Philippines, Vietnam, Mongolia and Malaysia) by becoming a leading provider of proprietary equipment and engineering services for the technology. The scope of the Tianwo-SES Joint Venture is to market and license our gasification technology via project sublicenses; procurement and sale of proprietary equipment and services; coal testing; and engineering, procurement and research and development related to the technology. STT contributed 53.8 million yuan in April 2014 and was required to contribute an additional 46.2 million yuan within two years of such date for a total contribution of 100 million yuan (approximately \$15.0 million) in cash to the Tianwo-SES Joint Venture, and owns 65% of the Tianwo-SES Joint Venture.

We have contributed certain exclusive technology sub-licensing rights into the Tianwo-SES Joint Venture for the territory pursuant to the terms of a Technology Usage and Contribution Agreement (the “TUCA”) entered into among the Tianwo-SES Joint Venture, STT and us on the same date and further described in more detail below. We own 35% of the Tianwo-SES Joint Venture. Under the JV Contract, neither party may transfer their interests in the Tianwo-SES Joint Venture without first offering such interests to the other party.

The JV Contract also includes a non-competition provision which requires that the Tianwo-SES Joint Venture be the exclusive legal entity within the Tianwo-SES Joint Venture territory for the marketing and sale of any gasification technology or related equipment that utilizes low quality coal feedstock. Notwithstanding this, STT has the right to manufacture and sell gasification equipment outside the scope of the Tianwo-SES Joint Venture within the Tianwo-SES Joint Venture territory. In addition, we have the right to develop and invest equity in projects outside of the Tianwo-SES Joint Venture within the Tianwo-SES Joint Venture territory. After the termination of the Tianwo-SES Joint Venture, STT must obtain written consent from us to market development of any gasification technology that utilizes low quality coal feedstock in the Tianwo-SES Joint Venture territory.

The JV Contract may be terminated upon, among other things: (i) a material breach of the JV Contract which is not cured, (ii) a violation of the TUCA, (iii) the failure to obtain positive net income within 24 months of establishing the Tianwo-SES Joint Venture or (iv) mutual agreement of the parties.

TUCA

Pursuant to the TUCA, we have contributed to the Tianwo-SES Joint Venture certain exclusive rights to our gasification technology in the Tianwo-SES Joint Venture territory, including the right to: (i) grant site specific project sub-licenses to third parties; (ii) use our marks for proprietary equipment and services; (iii) engineer and/or design processes that utilize our technology or our other intellectual property; (iv) provide engineering and design services for joint venture projects and (v) take over the development of projects in the Tianwo-SES Joint Venture territory that have previously been developed by us and our affiliates.

The Tianwo-SES Joint Venture will be the exclusive operational entity for business relating to our technology in the Tianwo-SES Joint Venture territory. If the Tianwo-SES Joint Venture loses exclusivity due to a breach by us, STT is to be compensated for direct losses and all lost project profits. We will also provide training for technical personnel of the Tianwo-SES Joint Venture through the second anniversary of the establishment of the Tianwo-SES Joint Venture. We will also provide a review of engineering works for the Tianwo-SES Joint Venture. If modifications are suggested by us and not made, the Tianwo-SES Joint Venture bears the liability resulting from such failure. If we suggest modifications and there is still liability resulting from the engineering work, it is our liability.

Any party making, whether patentable or not, improvements relating to our technology after the establishment of the Tianwo-SES Joint Venture, grants to the other party an irrevocable, non-exclusive, royalty free right to use or license such improvements and agrees to make such improvements available to us free of charge. All such improvements shall become part of our technology and both parties shall have the same rights, licenses and obligations with respect to the improvement as contemplated by the TUCA.

The Tianwo-SES Joint Venture is required to establish an Intellectual Property Committee, with two representatives from the Tianwo-SES Joint Venture and two from SES. This Committee shall review all improvements and protection measures and recommend actions to be taken by the Tianwo-SES Joint Venture in furtherance thereof. Notwithstanding this, each party is entitled to take actions on its own to protect intellectual property rights. As of September 30, 2016 that committee was still yet to be formed.

Any breach of or default under the TUCA which is not cured on notice entitles the non-breaching party to terminate. The Tianwo-SES Joint Venture indemnifies us for misuse of our technology or infringement of our technology upon rights of any third party.

Current relationship with STT

The second capital contribution from STT of 46.2 million yuan (approximately \$6.9 million) was not paid in April 2016 as required by our initial JV Contract and currently remains outstanding. We notified STT in writing to determine the status of the payment, and other contractual breaches related to the TUCA, and the JV Contract, and have continued to follow up on this issue. Should the payment or the other breaches of the TUCA not be cured, we will consider any and all legal actions to resolve these issues.

The following table presents summarized financial information for the Tianwo-SES Joint Venture (in thousands):

<u>Income Statement data:</u>	Three Months Ended September 30, 2016	Three Months Ended September 30, 2015
Revenue	\$ 2,370	\$ 4,098
Operating loss	(1,558)	(551)
Net loss	(1,558)	(551)

<u>Balance sheet data:</u>	As of September 30, 2016	As of June 30, 2016
Current assets	\$ 10,859	\$ 9,856
Noncurrent assets	7,112	7,366
Current liabilities	7,114	4,719
Noncurrent liabilities	—	—
Equity	10,857	12,503

The Tianwo-SES Joint Venture is accounted for under the equity method. The Company's capital contribution in the formation of the venture was the TUCA, which is an intangible asset. As such, the Company did not record a carrying value at the inception of the venture. Under the equity method of accounting, losses in the venture are not recorded if the losses cause the carrying value to be negative and there is no requirement of the Company to contribute additional capital.

As the Company is not required to contribute additional capital, the Company is not recognizing losses in the venture, as this would cause the carrying value to be negative. Had the Company recognized its share of the losses related to the venture, the Company would have recognized losses of approximately \$0.5 million and \$0.2 million for the three months ended September 30, 2016 and 2015, respectively, and \$1.9 million from inception to date.

CESI-SES Investment Platforms

In March 2016, we entered a strategic Joint Project Development and Investment Agreement with China Environment State Investment Co., Ltd. ("CESI"). CESI is a state-owned enterprise established in Beijing under the China Ministry of Environmental Protection that is charged with, and funded to, develop and invest in the energy conservation and environmental protection industry. We and CESI have agreed to develop, jointly invest, and build a total of no less than 20 projects using our gasification technology over the next five years. Further, we and CESI are targeting to bring a minimum of two projects through development within 12 months. Equity in the projects for investment by us and CESI is expected to be owned 51% by CESI, and 49% by us through our wholly owned Hong Kong subsidiary, SES Clean Energy Investment Holdings Limited. We and CESI have initially identified a pipeline of potential projects.

In July 2016, CESI's executive management changed related to a restructuring agreement and the entrance of a new shareholders. We have been in contact with the new management team and we have been told that CESI will evaluate the economics of the projects discussed above and will make its decision to continue in the projects based upon their views of the projects' economics. If CESI were to not continue to participate in these projects, it could cause delays as we seek replacement partners and alternative funding sources. We can provide no assurances as to the level of involvement which CESI will have in the projects in the future but we believe that we will be able to find a replacement partner should CESI decide to not participate.

Dongying Projects

In May 2016, we announced the first of our projects on the platform discussed above. The project will use SGT to produce lower-cost hydrogen in the Lijin County Binhai New District industrial park in Dongying, Shandong Province. The build-out consists of three projects completed in phases with an estimated preliminary total investment to be approximately 2 billion yuan (\$299.5 million). In June 2016, the Company signed an investment and cooperation agreement with Shandong Dongying Hekou District Government. The project will use SGT to produce lower-cost hydrogen needed for clean fuels production by refineries at the Hekou Blue Economy Industrial Park Project in Dongying City, Shandong Province. The build-out consists of multiple phases with an estimated preliminary total investment to be approximately 550 million yuan (\$82.4 million).

In May 2015, we established AFE together with Australian company Ambre Investments PTY Limited ("Ambre"). AFE is a development stage Australian company which is seeking to deploy SGT into projects in Australia where AFE or its affiliates would own equity and to secure ownership positions in low quality, low cost, coal resources such as unmarketable coal generally produced from coal mining operations in order to secure a long-term source of feedstock for the projects that would utilize SGT.

In forming AFE, we contributed conditional exclusive access to SGT limited to Australia through a master technology agreement in return for an ownership interest in AFE. In addition, we contributed certain early stage engineering support for AFE's business development through an engineering consulting agreement while Ambre contributed cash for the early stage business development. In connection with this agreement, in fiscal year 2016, we recognized approximately \$0.2 million in Related party consulting services. At September 30, 2016, we owned approximately 37% of AFE. Because of the early stage business development expenses incurred by AFE, the carrying value of AFE was zero as of both September 30, 2016 and June 30, 2016. Under the equity method of accounting, losses in the venture are not recorded if the losses cause the carrying value to be negative and there is no requirement of the Company to contribute additional capital. Had the Company recognized its share of the losses related to the venture, the Company would have recognized additional losses of approximately \$84,000 from inception to date.

Because of its early stage business development efforts associated with the Callide coal mine in Central Queensland, Australia, AFE created Batchfire. Batchfire was a spin-off company which was distributed to the shareholders of AFE in December 2015. Batchfire is registered in Australia and was formed for the purpose of purchasing the Callide thermal coal mine from Anglo-American plc ("Anglo-American"). On October 31, 2016, Batchfire announced that it had completed its acquisition of the Callide thermal coal mine from Anglo American. The Callide mine is a mature and significantly sized coal producer with substantial recoverable thermal coal reserves. After the transaction on October 31, 2016 the Company owns an approximately 11% interest in Batchfire. Because of the nature of our contribution, our carrying value of Batchfire was zero as of both September 30, 2016 and June 30, 2016.

Batchfire intends to operate the Callide mine and implement its planned improvements to increase output from the mine and lower the mining costs. AFE is currently evaluating project opportunities that would use SGT and utilize the unmarketable coal from the Callide mine to responsibly manufacture energy or chemical products.

Note 3- Discontinued Operation

As discussed in Note 2 above, in August 2016, the Company reached a definitive agreement with Xuecheng Energy to reduce its ownership in the ZZ Joint Venture to approximately 9%. The definitive agreement took full effect in October 2016, when the government approved our transfer. The ZZ Joint Venture will be deconsolidated during the second quarter of fiscal 2017. The Company reported the operations of the ZZ Joint Venture as discontinued operation on the Company's consolidated financial statements and classified the related assets and liabilities as assets/liabilities of discontinued operations.

The following table provides the results of operations from discontinued operations, the ZZ Joint Venture, for the three months ended September 30, 2016, and 2015.

	Three Months Ended	
	September 30,	
	2016	2015
Revenue:		
Product sales and other –related parties	\$ —	3,075
Related party consulting services	168	77
Total revenue from discontinued operation	168	3,152
Net loss from discontinued operations to SES stockholders	(380)	(1,579)
Net comprehensive loss from discontinued operations to SES stockholders	(355)	(2,092)

The carry value of the major categories of assets and liabilities of the ZZ Joint Venture classified as assets/liabilities of discontinued operations on the Company's balance sheet as of September 30, 2016 and June 30, 2016 were as follows:

	As of	As of
	September 30, 2016	June 30, 2016
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 10	\$ 12
Certificate of deposit- restricted	2,248	2,262
Prepaid expenses and other currents assets	26	329
Inventory	53	79
Total current assets of discontinued operation	2,337	2,682
Property, plant and equipment, net	8,611	8,948
Other long-term assets	1,055	1,032
Total assets of discontinued operations	12,003	12,662
LIABILITIES AND EQUITY		
Current liabilities:		
Accrued expenses and accounts payable	1,314	1,698
Accrued expenses and accounts payable- related party	4,942	4,853
Line of credit	3,746	3,770
Short-term bank loan	2,995	3,016
Total Current liabilities of discontinued operations	12,997	13,337

The following table provides the major categories of cash flows from discontinued operations, our ZZ Joint Venture, for the three months ended September 30, 2016 and 2015.

	Three Months Ended	
	September 30,	
	2016	2015
Cash flows from operating activities:		
Depreciation	155	166
Amortization	2	2
Cash flows from investing activities:		
Capital expenditures	(4)	(9)

There are no significant non cash transactions related to discontinued operations for both the three months ended September 30, 2016 and 2015.

Note 4 – GTI License Agreement

In November 2009, we entered into an Amended and Restated License Agreement, or the GTI Agreement, with GTI, replacing the Amended and Restated License Agreement between us and GTI dated August 31, 2006, as amended. Under the GTI Agreement, we maintain our exclusive worldwide right to license the U-GAS[®] technology for all types of coals and coal/biomass mixtures with coal content exceeding 60%, as well as the non-exclusive right to license the U-GAS[®] technology for 100% biomass and coal/biomass blends exceeding 40% biomass.

In order to sublicense any U-GAS[®] system, we are required to comply with certain requirements set forth in the GTI Agreement. In the preliminary stage of developing a potential sublicense, we are required to provide notice and certain information regarding the potential sublicense to GTI and GTI is required to provide notice of approval or non-approval within ten business days of the date of the notice from us, provided that GTI is required to not unreasonably withhold their approval. If GTI does not respond within that ten business day period, they are deemed to have approved of the sublicense. We are required to provide updates on any potential sublicenses once every three months during the term of the GTI Agreement. We are also restricted from offering a competing gasification technology during the term of the GTI Agreement.

For each U-GAS[®] unit which we license, design, build or operate for ourselves or for a party other than a sub-licensee and which uses coal or a coal and biomass mixture or biomass as the feedstock, we must pay a royalty based upon a calculation using the MMBtu per hour of dry syngas production of a rated design capacity, payable in installments at the beginning and at the completion of the construction of a project, or the Standard Royalty. If we invest, or have the option to invest, in a specified percentage of the equity of a third party, and the royalty payable by such third party for their sublicense exceeds the Standard Royalty, we are required to pay to GTI an agreed percentage split of third party licensing fees, or the Agreed Percentage, of such royalty payable by such third party. However, if the royalty payable by such third party for their sublicense is less than the Standard Royalty, we are required to pay to GTI, in addition to the Agreed Percentage of such royalty payable by such third party, the Agreed Percentage of our dividends and liquidation proceeds from our equity investment in the third party. In addition, if we receive a carried interest in a third party, and the carried interest is less than a specified percentage of the equity of such third party, we are required to pay to GTI, in our sole discretion, either (i) the Standard Royalty or (ii) the Agreed Percentage of the royalty payable to such third party for their sublicense, as well as the Agreed Percentage of the carried interest. We will be required to pay the Standard Royalty to GTI if the percentage of the equity of a third party that we (a) invest in, (b) have an option to invest in, or (c) receive a carried interest in, exceeds the percentage of the third party specified in the preceding sentence.

We are required to make an annual payment to GTI for each year of the term, with such annual payment due by the last day of January of the following year; provided, however, that we are entitled to deduct all royalties paid to GTI in a given year under the GTI Agreement from this amount, and if such royalties exceed the annual payment amount in a given year, we are not required to make the annual payment. We must also provide GTI with a copy of each contract that we enter into relating to a U-GAS[®] system and report to GTI with our progress on development of the technology every six months.

For a period of ten years, we and GTI are restricted from disclosing any confidential information (as defined in the GTI Agreement) to any person other than employees of affiliates or contractors who are required to deal with such information, and such persons will be bound by the confidentiality provisions of the GTI Agreement. We have further indemnified GTI and its affiliates from any liability or loss resulting from unauthorized disclosure or use of any confidential information that we receive.

While the core of our technology is the U-GAS[®] system, we have continued to innovate and modify the process to a point where we maintain certain intellectual property rights over SGT. Since the original licensing in 2004, we have maintained a strong relationship with GTI and continue to benefit from the resources and collaborative work environment that GTI provides us. It is in part for that reason, in May 2016, we exercised the first of our 10-year extensions and now maintain the exclusive license described above through 2026.

Note 5 – Equity

Preferred Stock

At the Annual Meeting of Stockholders of the Company on June 30, 2015, the Company's stockholders approved an amendment to the Company's certificate of incorporation to authorize a class of preferred stock, consisting of 20.0 million authorized shares, which may be issued in one or more series, with such rights, preferences, privileges and restrictions as shall be fixed by the Company's board of directors. No shares of preferred stock have been issued or outstanding since approved by the stockholders.

Stock-Based Compensation

As of September 30, 2016, the Company has outstanding stock option and restricted stock awards granted under the Company's 2015 Long Term Incentive Plan (the "2015 Incentive Plan") and Amended and Restated 2005 Incentive Plan (the "2005 Incentive Plan"), under which the Company's stockholders have authorized a total of 21.0 million shares of common stock for awards under the 2015 and 2005 Incentive Plan. The 2005 Incentive Plan expired as of November 7, 2015 and no future awards will be made thereunder. As of September 30, 2016, there were approximately 7.3 million shares authorized for future issuance pursuant to the 2015 Incentive Plan. Under the 2015 Incentive Plan, the Company may grant incentive and non-qualified stock options, stock appreciation rights, restricted stock units and other stock-based awards to officers, directors, employees and non-employees. Stock option awards generally vest ratably over a one to four year period and expire ten years after the date of grant.

Restricted stock activity during the three months ended September 30, 2016 was as follows:

	Restricted stock outstanding
Outstanding at June 30, 2016	275,096
Granted	—
Vested	(20,089)
Forfeited	—
Outstanding at September 30, 2016	<u>255,007</u>

Stock option activity during the three months ended September 30, 2016 was as follows:

	Shares of Common Stock Underlying Stock Options
Outstanding at June 30, 2016	10,215,447
Granted	—
Exercised	(40,000)
Forfeited	—
Outstanding at September 30, 2016	<u>10,175,447</u>
Exercisable at September 30, 2016	<u>9,431,510</u>

Stock warrants activity during the three months ended September 30, 2016 were as follows:

	Shares of Common Stock Underlying Warrants
Outstanding at June 30, 2016	9,914,832
Granted	—
Exercised	—
Forfeited	—
Outstanding at September 30, 2016	9,914,832
Exercisable at September 30, 2016	9,539,832

The Company recognizes the stock-based expense related to the 2005 and 2015 Incentive Plan awards and warrants over the requisite service period. The following table presents stock based compensation expense attributable to stock option awards issued under the 2005 and 2015 Incentive Plan and attributable to warrants issued to investors and consulting firms as compensation (in thousands):

	Three Months Ended September 30,	
	2016	2015
2005 and 2015 Incentive Plans	\$ 199	\$ 172
Warrants	58	959
Total stock-based expense	\$ 257	\$ 1,131

Note 6 – Net Loss Per Share

Historical net loss per share of common stock is computed using the weighted average number of shares of common stock outstanding. Basic loss per share, for both continuing and discontinuing operations, excludes dilution and is computed by dividing net loss available to common stockholders by the weighted average number of shares of common stock outstanding for the period. Stock options, warrants and unvested restricted stock are the only potential dilutive share equivalents the Company had outstanding for the periods presented. For the three months ended September 30, 2016 and 2015, options and warrants to purchase common stock excluded from the computation of diluted earnings per share, for both continuing and discontinuing operations, as their effect would have been anti-dilutive as the Company incurred net losses during those periods, amounted to 20.3 million and 17.9 million, respectively.

Note 7 – Risks and Uncertainties

As of September 30, 2016, we had \$11.1 million in cash and cash equivalents. We currently plan to use our available cash for: (i) commercializing our technology and securing orders and associated tasks with developing our business with a prime focus on the markets of syngas for direct replacement of natural gas, syngas for producing substitute natural gas and power; (ii) securing new partners for our technology business; (iii) technology product advancement for power applications and industrial syngas; (iv) general and administrative expenses; and (v) working capital and other general corporate purposes.

The actual allocation and timing of these expenditures will be dependent on various factors, including changes in our strategic relationships, commodity prices and industry conditions, and other factors that the Company cannot currently predict. In particular, any future decrease in economic activity in China or in other regions of the world in which the Company may in the future do business could significantly and adversely affect the Company's results of operations and financial condition. Operating cash flows from the Company's joint venture operating projects can be positively or negatively impacted by changes in coal and methanol prices. These are commodities where market pricing is often volatile in nature.

Any future decrease in economic activity in China, or in other regions of the world, in which the Company may in the future do business, could significantly and adversely affect its results of operations and financial condition in a number of other ways. Any decline in economic conditions may reduce the demand for prices from the products from our plants, thus the Company's ability to finance and develop its existing projects, commence any new projects and sell its products could be adversely impacted.

The Company's future success will depend on its relationships with its joint venture partners and any other strategic relationships that the Company may enter into. The Company can provide no assurances that it will satisfy the conditions required to maintain these relationships under existing agreements or that it can prevent the termination of these agreements. The Company also cannot provide assurances that it will be able to enter into relationships with future strategic partners on acceptable terms, including partnering its technology vertical. Further, the Company cannot provide assurances that its joint venture partners, including in the Yima Joint Ventures and the Tianwo-SES Joint Venture, will grow the joint venture or effectively meet their development objectives. Joint ventures typically involve a number of risks and present financial, managerial and operational challenges, including the existence of unknown potential disputes, liabilities or contingencies that arise after entering into the joint venture related to the counterparties to such joint ventures, with whom the Company shares control. The Company could experience financial or other setbacks if transactions encounter unanticipated problems due to challenges, including problems related to execution or integration. Continued economic uncertainty in China could also cause delays or make financing of operations more difficult.

The Company does not currently have all of the financial and human resources to fully develop and execute on all of its other business opportunities; however, the Company intends to finance their development through paid services, technology access fees, equity and debt financings and by securing financial and strategic partners focused on development of these opportunities. The Company can make no assurances that its business operations will provide it with sufficient cash flows to continue its operations. The Company may need to raise additional capital through equity and debt financing for any new ventures that are developed, to support its existing projects and possible expansions thereof and for its corporate general and administrative expenses. The Company is considering a full range of financing options in order to create the most value in the context of the increasing interest the Company is witnessing in its proprietary technology. The Company cannot provide any assurance that any financing will be available to it in the future on acceptable terms or at all. Any such financing could be dilutive to its existing stockholders. If the Company cannot raise required funds on acceptable terms, it may not be able to, among other things, (i) maintain its general and administrative expenses at current levels including retention of key personnel and consultants; (ii) successfully develop its licensing and related service businesses; (iii) negotiate and enter into new gasification plant development contracts and licensing agreements; (iv) make additional capital contributions to its joint ventures; (v) fund certain obligations as they become due; (vi) respond to competitive pressures or unanticipated capital requirements; or (vii) repay its indebtedness.

Fluctuations in exchange rates can have a material impact on the Company's costs of construction, operating expenses and the realization of revenue from the sale of commodities. The Company cannot be assured that it will be able to offset any such fluctuations and any failure to do so could have a material adverse effect on the Company's business, financial condition and results of operations. In addition, the Company's financial statements are expressed in U.S. dollars and will be negatively affected if foreign currencies depreciate relative to the U.S. dollar as has happened recently with the yuan. In addition, the Company's currency exchange losses may be magnified by exchange control regulations in China or other countries that restrict our ability to convert into U.S. dollars.

We own a 25% interest in the Yima Joint Ventures, however, as discussed in Note 2, we account for our investment at cost. While the Yima Joint Ventures commenced initial production in December 2012, the Yima Joint Ventures completed the required performance testing of the plants and received its Performance Test Certificate in March 2016 due to on-going modifications and construction delays. The formal acceptance of the test results was an important step for the plant. In June 2016, the local environmental bureau requested that the plant halt operations due to certain issues identified by the bureau. The Yima Joint Ventures have been working with the bureau to resolve the issues, complete its internal restructuring, and recommence operations during November 2016. The Yima Joint Ventures have also commenced an organizational restructuring to better streamline operations and allow the Yima Joint Ventures to obtain permanent safety and environmental permits. In July 2016 the Yima Joint Ventures obtained its own business license. Prior to this point the Yima Joint Ventures operated under a business license from its parent company. The Yima Joint Ventures are experiencing certain liquidity concerns related to a series of third party notes which are due prior to December 31, 2016 and are currently in discussions with the lenders to seek extensions, refinancing or other alternative arrangements to avoid default.

The Company can make no assurances that the plants will recommence operations as expected, that they will be able to successfully complete the organizational restructuring required to obtain the permanent safety and environmental permits for the plants or that they will be able to resolve its liquidity concerns. We continue to monitor the Yima Joint Ventures and could take an additional impairment in the future if operating conditions do not meet our current expectations, or if the liquidity situation worsens.

The Company is subject to concentration of credit risk with respect to our cash and cash equivalents, which it attempts to minimize by maintaining cash and cash equivalents with major high credit quality financial institutions. At times, the Company's cash balances in a particular financial institution exceed limits that are insured by the U.S. Federal Deposit Insurance Corporation or equivalent agencies in foreign countries and jurisdictions such as Hong Kong. As of September 30, 2016 the Company had \$11.0 million in cash and cash equivalents (of which \$10.6 million is located in the United States), and \$2.3 million in a restricted certificate of deposit in Chinese based bank accounts as part of our assets of discontinued operations. While the Company is generally able to pay intercompany obligations from these bank accounts, there are more stringent requirements on the distribution of earnings.

Note 8 – Segment Information

The Company's reportable operating segments have been determined in accordance with the Company's internal management reporting structure and include SES China, Technology Licensing and Related Services, and Corporate. The SES China reporting segment includes all of the assets and operations and related administrative costs for China including initial closing costs relating to our joint ventures. The Technology Licensing and Related Services reporting segment includes all of the Company's current operating activities outside of China. The Corporate reporting segment includes the executive and administrative expenses of the corporate office in Houston. The Company evaluates performance based upon several factors, of which a primary financial measure is segment operating income or loss.

The following table presents statements of continuing operations data and assets by segment (in thousands):

	Three Months Ended	
	September 30,	
	2016	2015
Revenue:		
SES China	\$ —	\$ —
Technology licensing and related services	—	247
Corporate & other	—	—
Total revenue	\$ —	\$ 247
Depreciation and amortization:		
SES China	\$ —	\$ 6
Technology licensing and related services	39	51
Corporate & other	—	—
Total depreciation and amortization	\$ 39	\$ 57
Operating loss:		
SES China	\$ (486)	\$ (571)
Technology licensing and related services	(649)	(244)
Corporate & other	(1,493)	(2,268)
Total operating loss	\$ (2,628)	\$ (3,083)

	As of September 30, 2016	As of June 30, 2016
Assets:		
SES China	\$ 36,423	\$ 37,188
Technology licensing and related services	830	892
Corporate & other	14,819	17,101
Total assets	<u>\$ 52,072</u>	<u>\$ 55,181</u>

Note 9 — Commitments and Contingencies

Litigation

The Company is currently not a party to any legal proceedings.

Operating leases

In February 2016, the Company extended its corporate office lease term for an additional 18 months ending December 31, 2017 with rental payments of approximately \$12,000 per month (monthly rent changes depending on actual utility usage each month).

Governmental and Environmental Regulation

The Company's operations are subject to stringent federal, state and local laws and regulations governing the discharge of materials into the environment or otherwise relating to environmental protection. Numerous governmental agencies, such as the U.S. Environmental Protection Agency, and various Chinese authorities, issue regulations to implement and enforce such laws, which often require difficult and costly compliance measures that carry substantial administrative, civil and criminal penalties or may result in injunctive relief for failure to comply. These laws and regulations may require the acquisition of a permit before operations at a facility commence, restrict the types, quantities and concentrations of various substances that can be released into the environment in connection with such activities, limit or prohibit construction activities on certain lands lying within wilderness, wetlands, ecologically sensitive and other protected areas, and impose substantial liabilities for pollution resulting from our operations. The Company believes that it is in substantial compliance with current applicable environmental laws and regulations and it has not experienced any material adverse effect from non-compliance with these environmental requirements.

Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations.

You should read the following discussion and analysis of our financial condition and results of operations together with our consolidated financial statements and the related notes and other financial information included elsewhere in this quarterly report. Some of the information contained in this discussion and analysis or set forth elsewhere in this quarterly report, including information with respect to our plans and strategy for our business and related financing, includes forward-looking statements that involve risks and uncertainties. You should review the “Risk Factors” section of our Annual Report on Form 10-K for the fiscal year ended June 30, 2016 for a discussion of important factors that could cause actual results to differ materially from the results described in or implied by the forward-looking statements contained in the following discussion and analysis.

Forward-Looking Statements

This Quarterly Report on Form 10-Q includes “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Exchange Act. All statements other than statements of historical fact are forward-looking statements and are subject to certain risks, trends and uncertainties that could cause actual results to differ materially from those projected. Among those risks, trends and uncertainties are the ability of our project with Yima to produce earnings and pay dividends; our ability to develop and expand business of the TSEC joint venture in the joint venture territory; our ability to successfully partner our technology business; our ability to develop our power business unit and marketing arrangement with GE and our other business verticals, including DRI steel, through our marketing arrangement with Midrex Technologies, and renewables; our ability to successfully develop the SES licensing business; the ability of the ZZ Joint Venture to retire existing facilities and equipment and build another SGT facility; the ability of Batchfire management to successfully grow and develop Callide operations; the economic conditions of countries where we are operating; events or circumstances which result in an impairment of our assets; our ability to reduce operating costs; our ability to make distributions and repatriate earnings from our Chinese operations; our ability to successfully commercialize our technology at a larger scale and higher pressures; commodity prices, including in particular natural gas, crude oil, methanol and power, the availability and terms of financing; our ability to obtain the necessary approvals and permits for future projects, our ability to raise additional capital, if any, our ability to estimate the sufficiency of existing capital resources; the sufficiency of internal controls and procedures; and our results of operations in countries outside of the U.S., where we are continuing to pursue and develop projects. Although we believe that in making such forward-looking statements our expectations are based upon reasonable assumptions, such statements may be influenced by factors that could cause actual outcomes and results to be materially different from those projected by us. We cannot assure you that the assumptions upon which these statements are based will prove to be correct.

When used in this Form 10-Q, the words “expect,” “anticipate,” “intend,” “plan,” “believe,” “seek,” “estimate” and similar expressions are intended to identify forward-looking statements, although not all forward-looking statements contain these identifying words. Because these forward-looking statements involve risks and uncertainties, actual results could differ materially from those expressed or implied by these forward-looking statements for a number of important reasons, including those discussed under “Risk Factors” in our Annual Report on Form 10-K for the year ended June 30, 2016, as well as in “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” and elsewhere in this Form 10-Q.

You should read these statements carefully because they discuss our expectations about our future performance, contain projections of our future operating results or our future financial condition, or state other “forward-looking” information. You should be aware that the occurrence of certain of the events described in this Form 10-Q could substantially harm our business, results of operations and financial condition and that upon the occurrence of any of these events, the trading price of our common stock could decline, and you could lose all or part of your investment.

We cannot guarantee any future results, levels of activity, performance or achievements. Except as required by law, we undertake no obligation to update any of the forward-looking statements in this Form 10-Q after the date hereof.

Business Overview

We are a global clean energy company that develops, builds and owns clean energy projects and we own proprietary gasification technology which we utilize to provide technology licenses and proprietary equipment to customers in the energy and chemical industries. Our Synthesis Energy Systems Gasification Technology (“SGT”) is a flexible, efficient and economic technology for the production of synthesis gas, or syngas, a mixture of primarily hydrogen, carbon monoxide and methane. Syngas is a versatile source of clean energy that can be used to create a variety of valuable products. Through our unique SGT, we offer an attractive economic alternative to expensive natural gas, imported LNG and crude oil for manufacturing many of the world’s energy and chemical products. We can do this because our technology is uniquely capable of manufacturing clean syngas from a wide variety of energy resources including most all existing forms of coal, biomass, municipal wastes and refuse derived fuels and petroleum coke. Our syngas can be efficiently converted into a wide variety of energy and chemical products such as industrial fuel gas, substitute natural gas, electricity, hydrogen, ammonia and methanol. Therefore, using our clean syngas enables a valuable alternative in many parts of the world where natural gas, LNG and crude oil are expensive or unavailable. Our SGT is built on decades of research, development, demonstration and we have deployed SGT in several commercial operating plants in China. At the present time, our technology is, or has been, operating commercially on eight gasification systems in four plant facilities. In addition, there are four SGT gasification systems in the commissioning phase at this time.

Our business strategy is focused upon generating growth and financial results from: i) our existing Chinese technology and gasification facilities joint ventures, ii) licensing our gasification technology and selling our proprietary equipment and services and iii) forming value accretive partnerships with low cost equity and debt financing capabilities which we use to build joint market segment and regional business platforms for developing, investing into, owning and monetizing clean energy projects. With these strategy components, we focus on leveraging our technology’s capability to create value. In implementing our strategy, we intend to diversify our geographic concentration from China by growing markets outside China where our unique technology capabilities can create value.

Our technology license and equipment package is a very low-capital intensive offering and we believe it has potential to generate attractive margins on license fees, equipment sales and services. We rely on a variety of regional, market segment and adjacent technology partners to extend our global sales reach for commercializing our technology and equipment. We believe the largest contributor to future earnings from our business strategy will be through our project investment partnerships and platforms. While this element of our strategy is more capital intensive, we intend to manage and minimize our equity requirements, achieve project financing debt support and minimize risk through the formation of joint business enterprises with partners which we call platforms. These project investment platforms are intended to develop multiple projects, raise low cost capital and debt, and build projects using SGT. We typically work with partners who have aligned business interest with SES related to value creation and who bring financial capabilities, such as debt guarantees and equity financing as well as local project implementation and operating expertise. In addition we anticipate that this element of our strategy will also grow our related technology license and equipment business as these platform projects would utilize our SGT licensing, engineering and equipment systems.

Our business relies on the unique capability of our SGT technology, which can convert the most challenging, and therefore lower cost, coal feedstocks, such as high ash coal and coal wastes, into syngas. We believe our feedstock flexibility exceeds all other commercially available gasification technologies. To demonstrate our technology capabilities, our initial joint venture operating projects were focused on the demonstration of our technology’s robustness via a modest scale plant at our ZZ joint venture, then later on a larger scale at our Yima Joint Ventures. Our three projects with the Aluminum Corporation of China (“CHALCO”), in connection with our Tianwo-SES Joint Venture, have further enhanced the commercial validation of our technologies’ capabilities and strengths. We believe these projects provide evidence of our technology’s capability to operate using coals with characteristics that would not be offered by our competitors. We continue to pursue a variety of additional global projects under development internally and by our customers who wish to use our proprietary gasification technology platform to convert low-cost, locally available feedstocks to high value products.

Our technology economically extracts carbon and hydrogen from all types of coal, coal wastes, renewable forms of biomass and municipal wastes in an environmentally friendly manner. The carbon and hydrogen are extracted by reacting the coal with oxygen, steam and utilize these energy building blocks to form syngas. Syngas can be used as a substitute for natural gas in many industries such as energy, steel, aluminum, ceramics, glass and others that combust natural gas to produce heat. In addition, syngas can be readily converted into a wide range of energy and chemical products. These products include, but are not limited to, the following:

- industrial fuel gas,
- hydrogen and its derivatives,
- electricity,
- substitute natural gas (“SNG”),
- transportation fuels such as gasoline, diesel and jet fuel,
- chemicals such as methanol, olefins, and glycols,
- fertilizers like ammonia and urea, and
- steel and direct reduction of iron (“DRI”),

Our technology is one of several which have been used successfully in these industrial applications for many years. However, our technology is meaningfully differentiated over other forms of gasification primarily through its feedstock flexibility, its ability to economically convert the lowest quality brown coals and lignites, high ash sub-bituminous coals, bituminous and anthracite coals as well as biomass and other renewable waste materials.

Our most recent product is the XL3000 gasification system introduced in October 2014. It is specifically targeted to provide high syngas capacity and delivery pressure with low capital costs, while maintaining high syngas generation efficiencies on all types of coal feedstock. The XL3000 is targeted to deliver the efficiency and economy required to meet the needs of the world's syngas projects: electricity, steelmaking, industrial chemicals, fertilizers, SNG, and transportation fuels. The XL3000 gasification system delivers approximately 250% syngas capacity (3,000 metric tons per day of coal feedstock) than our previous designs with syngas delivery pressures up to 55 bar.

As discussed in “-Current Operations and Projects” below, in August 2016, the Company announced that the Company and Shandong Hai Hua Xuecheng Energy Co., Ltd. (“Xuecheng Energy”) have entered into a Definitive Agreement to restructure the ZZ Joint Venture. The agreement took full effect when the registration with the government was completed on October 31, 2016. During the second quarter of fiscal 2017, the Company will deconsolidate the ZZ Joint Venture and will account for our investment under the cost method. For purposes of these financial statements, the Company has classified all operations related to the ZZ Joint Venture as discontinued operations and have classified all assets and liabilities related to the ZZ Joint Venture as assets/liabilities of discontinued operations. Prior period results have been adjusted to reflect the current presentation.

Outlook

We believe the ever increasing industrialization of developing countries will drive the need for additional and cleaner energy sources and we anticipate that there will be a preference to those companies who can provide these energy sources in an economical and environmentally efficient manner. We own rights to proprietary gasification technology which is capable of converting most of the world’s coal, including low-quality coal and coal waste and renewable sources such as biomass and municipal wastes, into a clean syngas. Because of our technology capability, the clean syngas produced by our technology provides what we believe is a compelling low cost alternative to using expensive natural gas and crude oil energy sources for the production of a wide variety of energy and chemical products. While the current economic environment poses challenges in some regions of the world where growth is slow or where natural gas and oil prices are very low, we believe the long-term outlook for our industry is quite strong.

To date our operations have focused on China which has seen dramatic growth over the past few years. Over the past two years we have successfully increased our installed base of gasifier systems from five to twelve, all of which are located in China. While we have seen a recent slowing in the Chinese economy, we expect China will continue provide a strong market for our technology as they continue to seek to become a dominant global economic player.

Globally, we have seen a shifting of the competitive landscape of gasification over the past months from more commonly deployed gasification technologies that rely on higher grade coals and utilize more water. This has generated an increasing global interest in our technology and its capabilities to produce syngas cleanly, efficiently and with lower water consumption for most all qualities of coal as well as biomass and municipal solid waste. We believe that our technology is well positioned to address the market needs of the changing global energy landscape.

We believe the largest contributor to earnings from our business strategy will be through our project investment partnerships and platforms. While this element of our strategy is more capital intensive, through partnering we intend to manage and minimize our equity requirements, achieve project financing debt support and minimize risk through the formation of joint business enterprises which we call platforms. These project investment platforms are intended to develop multiple projects, raise low cost capital and debt, and build projects using SGT. We typically work with partners who have aligned business interest with us related to value creation and who bring financial capabilities, such as debt guarantees and equity financing as well as local project implementation and operating expertise. In addition we anticipate that this element of our strategy will also grow our related technology license and equipment business as these platform projects would utilize our SGT licensing, engineering and equipment systems. The current global economic environment does provide a number of risks to our business. Our ability to access both debt and equity funding, at commercially reasonable returns, will be critical to achieving growth in the project investment side of our business.

We believe that this is a critical time in shaping the future of our company. We have spent a number of years commercializing our technology and our ZZ and Yima joint ventures combined with the latest licensed projects under our Tianwo-SES joint venture have provided the demonstration of our technical capabilities at commercial scale. Building on the results from these projects we believe we will achieve increasingly more efficient and reliable project operations which in turn will lead to better financial returns both to our shareholders and our joint venture partners. We believe the AFE and Batchfire projects are examples of the type of potential projects that we will pursue in the future as we seek to globalize our Company's operations.

We do not currently have all of the financial and human resources necessary to fully develop and execute on all of our business opportunities; however, we intend to finance our development through paid services, technology access fees, equity and debt financings, earnings from operations and by securing financial and strategic partners focused on the development of these opportunities. We can make no assurances that our business operations will provide us with sufficient cash flows to continue our operations. We are also seeking to raise capital through our strategic partnering activities. We may need to raise additional capital through equity and debt financing for any new ventures that are developed, to support our existing projects and possible expansions thereof and for our corporate general and administrative expenses. We may consider a full range of financing options in order to create the most value in the context of the increasing interest we are seeing in our technology. We cannot provide any assurance that any financing will be available to us in the future on acceptable terms or at all. Any such financing could be dilutive to our existing stockholders. If we cannot raise required funds on acceptable terms, we may not be able to, among other things, (i) maintain our general and administrative expenses at current levels including retention of key personnel and consultants; (ii) successfully implement our business strategy; (iii) make additional capital contributions to our joint ventures; (v) fund certain obligations as they become due; (vi) respond to competitive pressures or unanticipated capital requirements; or (vii) repay our indebtedness.

Results of Operations

Three Months Ended September 30, 2016 ("Current Quarter") Compared to the Three Months Ended September 30, 2015 ("Comparable Quarter")

Unless noted below the results of operations are comparing Current Quarter results of operations with the Comparable Quarter results from continuing operations.

Revenue. There were no revenues for the Current Quarter. During the Comparable Quarter total revenues were \$0.2 million, which resulted from engineering feasibility studies and coal testing services for two customers.

Costs of sales and plant operating expenses. There were no costs of sales during the Current Quarter. In the Comparable Quarter cost of sales totaled \$0.2 million, which related to the costs incurred for coal testing and engineering studies for two customers.

General and administrative expenses. General and administrative expenses was \$2.3 million in the Current Quarter compared with \$2.0 million for the Comparable Quarter. The \$0.3 million increase is due primarily to the engineering expenses and consulting fees incurred related to our engineering feasibility studies and technology development.

Stock-based expense . Stock-based expense decreased by \$0.8 million to \$0.3 million for the Current Quarter, compared to \$1.1 million for the Comparable Quarter. This decrease is due primarily to the modification and replacement of warrants in the prior year.

Depreciation and amortization. Depreciation and amortization expense for continuing operation was \$39,000 for the Current Quarter compared with \$57,000 for the Comparable Quarter, which primarily related to the amortization of our exclusive worldwide GTI license fee.

Foreign currency loss . Foreign currency loss for continuing operation was \$26,000 for the Current Quarter compared with a loss of \$0.1 million for the Comparable Quarter. The \$26,000 foreign currency loss for the Current Quarter primarily resulted from the 0.7% depreciation of the yuan relative to the U.S. Dollar from June to September 2016 as compared to a depreciation of the yuan relative to the U.S. Dollar of 4.0% during the comparable period.

Loss from discontinued operations . Loss from discontinued operations related to our ZZ Joint Venture was \$0.4 million for the Current Quarter compared with \$1.6 million for the Comparable Quarter. The decrease in loss was due primarily to the shutdown of the ZZ Joint Venture plant in October 2015.

Liquidity and Capital Resources

We have financed our operations to date through private placements and public offerings of our common stock and through lines of credit and working capital loans in our ZZ Joint Venture. We do not currently have all of the financial resources necessary to fully develop and execute on all of our business opportunities and may seek to raise additional capital through either additional equity or debt financing.

On May 13, 2016, we entered into an At The Market Offering Agreement (the “Offering Agreement”) with T.R. Winston & Company (“T.R. Winston”) to sell, from time to time, shares of our common stock having an aggregate sales price of up to \$20.0 million through an “at the marketing offering” program under which T.R. Winston would act as sales agent, which we refer to as the ATM Offering. The shares that may be sold under the Offering Agreement, if any, would be issued and sold pursuant to the Company’s \$75.0 million universal shelf registration statement on Form S-3 that was declared effective by the Securities and Exchange Commission on April 21, 2016. Through November 11, 2016, we have not sold any shares of our common stock in the ATM Offering. We have no obligation to sell any of our common stock under the Offering Agreement.

In June 2015, we entered into an SPA with Rui Feng, whereby Rui Feng was to acquire a controlling interest in SESI, a wholly owned subsidiary of which we owns our interest in the ZZ Joint Venture. Under the terms of the SPA, SESI will sell an approximately 61% equity interest to Rui Feng in exchange for \$10 million. Rui Feng’s second installment payment was due in December 2015 and the third installment was due on or before May 1, 2016. Neither of these installment payments have been made. It is not certain when or if Rui Feng will make any additional required installment payments under the SPA. Because Rui Feng has not made additional installment payments, they have not acquired additional ownership interest in the ZZ Joint Venture. As a result of our agreement with Xuecheng Energy discussed above, we do not anticipate additional installment payments from Rui Feng

As of September 30, 2016, we had \$11.0 million in cash and cash equivalents and \$9.7 million of working capital. Excluding our ZZ joint venture, we had approximately \$11.0 million in cash and cash equivalents and \$10.7 million of working capital. The following summarizes the sources and uses of cash during the Current Quarter:

- **Operating Activities:** During the Current Quarter, we used \$2.8 million in cash for operating activities compared to \$1.9 million during the Comparable Quarter. These funds were utilized to fund the ongoing operations of the ZZ Joint Venture, develop our technical licensing and related services and our general and administrative expenses.

- Investing Activities: During the Current Quarter, we used \$4,000 in investing activities for capital expenditures as compared to \$9,000 during the Comparable Quarter.
- Financing Activities: For the Current Quarter, we had a net source of cash of approximately \$26,000 as compared to a net source of cash of \$1.3 million in the Comparable Quarter. During the Current Quarter, we received proceeds of approximately \$26,000 from the exercise of stock options. During the Comparable Quarter, we received proceeds of \$1.0 million from the exercise of stock warrants from a warrant holder and \$0.3 million from the exercise of stock options.

We currently plan to use our available cash for: (i) expanding our technology and securing orders and associated tasks with developing our business with a prime focus on the markets of syngas for direct replacement of natural gas, syngas for producing substitute natural gas and power; (ii) securing new partners for our technology business; (iii) technology product advancement for power applications and industrial syngas; (iv) general and administrative expenses; and (v) working capital and other general corporate purposes.

Current Operations and Projects

Synthesis Energy Systems (Zao Zhuang) New Gas Company Ltd. (“ZZ Joint Venture”)

In July 2006, we entered into a cooperative joint venture contract with Xuecheng Energy which established the ZZ Joint Venture, a joint venture company that has the primary purposes of:

- developing, constructing and operating a syngas production plant utilizing SGT in Zao Zhuang City, Shandong Province, China and
- producing and selling syngas and the various byproducts of the plant.

We initially owned 97.6% of the ZZ Joint Venture and Xuecheng Energy owned the remaining 2.4%. In June 2015, we entered into a Share Purchase and Investment Agreement (the “SPA”) with Rui Feng Enterprises Limited (“Rui Feng”), whereby Rui Feng will acquire a controlling interest in Synthesis Energy Systems Investments Inc. (“SESI”), and a wholly owned subsidiary, which owns our interest in the ZZ Joint Venture. Under the terms of the SPA, SESI originally agreed to sell an approximately 61% equity interest to Rui Feng in exchange for \$10 million. This amount was to be paid in four installments through December 2016, with the first installment of approximately \$1.6 million paid on June 26, 2015.

Rui Feng’s second installment payment was due in December 2015 and the third installment was due on May 1, 2016, and neither of these installment payments has been made. With the restructuring of the ZZ Joint Venture discussed below, we do not anticipate that Rui Feng will make any additional installment payments under the SPA. If Rui Feng does not make the required installment payments, we are entitled to terminate the agreement and Rui Feng would lose future rights to acquire additional interest in SESI and additional positions on the board of SESI. Given our agreement with Xuecheng Energy discussed below, we do not anticipate any additional installment payments from Rui Feng.

Because Rui Feng has not made additional installment payments, as of September 30, 2016, we owned approximately 88.1% of the ZZ Joint Venture as of September 30, 2016.

ZZ Joint Venture Debt Agreements

In October 2014, the ZZ Joint Venture entered into a working capital loan agreement (the “ZZ Working Capital Loan”) with Zaozhuang Bank Co., Ltd. (“ZZ Bank”), and received approximately \$3.3 million of loan proceeds, with a maturity of September 23, 2015. In September 2015, the Company refinanced the ZZ Working Capital Loan through August 2016 for approximately \$3.0 million. This amount was refinanced again in August 2016 through November 2016.

In October 2014, the ZZ Joint Venture entered two lines of credit with the ZZ Bank for a total of \$3.3 million (collectively, the “ZZ Line of Credit Agreement”). In April 2015, the Company repaid the ZZ Line of Credit Agreement and renewed the agreement for \$3.3 million under the same terms for an additional six months. In November 2015, the Company repaid \$3.3 million of the ZZ Line of Credit Agreement, and refinanced the ZZ Line of Credit Agreement with the ZZ Bank for \$3.7 million which matures in November 2016.

Agreement with Xuecheng Energy

In August 2016, we announced that we and Xuecheng Energy have entered into a definitive agreement to restructure the ZZ Joint Venture. Additionally, to dovetail with the Chinese government's widespread initiative to move industry into larger scale, commercial and environmentally beneficial industrial parks, the partners intend to evaluate a new ZZ syngas facility in the Zouwu Industrial Park in Shandong Province. We will retain an approximate nine percent ownership in the ZZ Joint Venture asset, and Xuecheng Energy has agreed to assume all outstanding liabilities of the ZZ Joint Venture, including payables related to the Cooperation Agreement with Xuecheng Energy signed in 2013. The definitive agreement took full effect when the registration with the government was completed on October 31, 2016. With the closure of this transaction, SES does not anticipate any future liabilities related to the ZZ Joint Venture. During the second quarter of fiscal 2017 we will deconsolidate the ZZ Joint Venture and will account for our investment under the cost method. For purposes of these financial statements, the Company has classified all operations related to the ZZ Joint Venture as discontinued operations and have classified all assets and liabilities related to the ZZ Joint Venture as assets/liabilities of discontinued operations. Prior period results have been adjusted to reflect the current presentation.

In October 2016, together with Xuecheng Energy, we signed a cooperation agreement and the local government of Xuecheng District, ZaoZhuang City, Shandong Province signed a Moving Project Cooperative Agreement to relocate the ZZ Joint Venture to a new industrial zone for the Xuecheng District of ZaoZhuang. The intent of the agreement is for the project to be expanded and repurposed to produce 283 million Nm³ of syngas per year using three SGT systems.

Yima Joint Ventures

In August 2009, we entered into amended joint venture contracts with Yima, replacing the prior joint venture contracts entered into in October 2008 and April 2009. The joint ventures were formed for each of the gasification, methanol/methanol protein production, and utility island components of the plant (collectively the "Yima Joint Ventures"). The amended joint venture contracts provide that:

- we and Yima contribute equity of 25% and 75%, respectively, to the Yima Joint Ventures;
- Yima will guarantee the repayment of loans from third party lenders for 50% of the project's cost and, if debt financing is not available, Yima is obligated to provide debt financing via shareholder loans to the project until the project is able to secure third-party debt financing; and
- Yima will supply coal to the project from a mine located in close proximity to the project at a preferential price.

We own a 25% interest in each joint venture and Yima owns a 75% interest. Notwithstanding this, in connection with an expansion of the project, we have the option to contribute a greater percentage of capital for the expansion, such that as a result, we could expand through contributions, at our election, up to a 49% ownership interest in the Yima Joint Ventures.

The remaining capital for the project has been funded with project debt obtained by the Yima Joint Ventures. Yima agreed to guarantee the project debt in order to secure debt financing from domestic Chinese banking sources. We have agreed to pledge to Yima our ownership interests in the joint ventures as security for our obligations under any project guarantee. In the event that the necessary additional debt financing is not obtained, Yima has agreed to provide a loan to the joint ventures to satisfy the remaining capital needs of the project with terms comparable to current market rates at the time of the loan.

Under the terms of the joint venture agreements, the Yima Joint Ventures are to be governed by a board of directors consisting of eight directors, two of whom were appointed by us and six of whom were appointed by Yima. The term of the joint venture shall commence upon each joint venture company obtaining its business operating license and shall end 30 years after commercial operation of the plant.

We believe there is a consistent pattern of the Yima Joint Venture management not demonstrating an understanding of the methanol facility operations and not sourcing available expertise in China to improve the overall operations. We have witnessed operation of the gasifier systems at Yima with design and operating parameter deviations from our existing technology recommendations. We continue to experience a limited ability to influence the Yima Joint Ventures' operating performance.

As a result of the issues noted above, Yima restructured the management of the Yima Joint Ventures under the direction of the Henan Coal Gasification Company ("Henan"), which is an affiliated company reporting directly to Henan Coal and Energy Group Companies. By virtue of this acquisition, Henan placed the Yima Joint Ventures under one of its subsidiaries Henan Energy which currently supervises the operations and personnel decisions of the Yima Joint Ventures. The ownership of the Yima Joint Ventures remains unchanged.

Since 2014, we have accounted for this joint venture under the cost method of accounting. Our conclusion to account for this joint venture under this methodology is based upon our lack of significant influence in the Yima Joint Venture. The lack of significant influence is determined based upon our interactions with the Yima Joint Ventures related to our limited participation in operating and financial policymaking processes coupled with our limited ability to influence decisions which contribute to the financial success of the Yima Joint Ventures.

Current Yima Operating Description

Despite initiating methanol production in December 2012, the Yima Joint Ventures' plant continued its construction through the beginning of 2016. In March 2016, the Yima Joint Ventures completed the required performance testing of the SGT systems and successfully issued its Performance Test Certificate. Because of the extended construction period, the plant recently faced increasing regulatory scrutiny from the environmental and safety bureaus.

In June 2016, the local environmental bureau requested that the plant temporarily halt operations to address certain issues identified by the environmental bureau. After the plant shut down operations, the Yima plant experienced an accident during maintenance activities that were unrelated to the gasification units. The Yima Joint Ventures have been working with both the environmental and safety bureaus and is anticipated to return to operations in November 2016.

In 2009, the project was approved as three separate joint ventures. The approval for the original joint ventures was for the production of methanol protein, and methanol by-product. This has impacted the ability of the plant to sell pure methanol on the open market and has been an impediment to receive the permanent safety operating permit.

To resolve these issues, during the quarter ended June 30, 2016, the Yima Joint Ventures commenced an organizational restructuring to better streamline the operations of the Joint Ventures. This restructuring effort was a multi-step process, including first obtaining the operating license to sell methanol by combining the three joint ventures into a single operating entity, and finally obtaining the permanent safety and environmental permits. The Yima Joint Ventures received the operating permit in July 2016, and have made continued progress in completing the remaining items.

The Yima Joint Ventures also are experiencing certain liquidity concerns with a series of third party bank notes due prior to the end of December 2016. Yima, the 75% shareholder of the Yima Joint Ventures, has been routinely providing liquidity to the Yima Joint Ventures in the form of shareholder loans and during the first quarter Yima successfully refinanced, for one full year through October 2017, certain amounts which were to become due in October 2016. The Yima Joint Ventures are currently in discussion with the impacted third party lenders to seek additional extensions, refinancing or other alternative arrangements to avoid a default by the Yima Joint Ventures. While we believe Yima will continue to provide additional liquidity to the Yima Joint Ventures until the project is operating and producing income, we can make no assurances that Yima will continue to do this or on the outcome of the above mentioned negotiations.

Because of the situations detailed above, our management evaluated the current conditions of the Yima Joint Ventures to determine whether an other than temporary decrease in value had occurred for the year ended June 30, 2016. Management determined that the decrease in value due to the shutdown and liquidity situation were other than temporary in nature and therefore management conducted an impairment analysis utilizing a discounted cash flow fair market valuation with the assistance of a third party valuation expert. In this valuation, significant unobservable inputs were used to calculate the fair value of the investment. The valuation led to the conclusion that the investment in the Yima Joint Ventures was impaired as of June 30, 2016, and accordingly, we recorded an \$8.6 million impairment for the fiscal year ended June 30, 2016. Management determined that there was not an other than temporary impairment of value of our Yima investment during the quarter ended September 30, 2016. The carrying value of our Yima investment was approximately \$26.2 million as of both September 30, 2016 and June 30, 2016. We continue to monitor the Yima Joint Ventures and could take an additional impairment in the future if operating conditions do not meet our current expectations, or if the liquidity situation worsens.

Tianwo-SES Clean Energy Technologies Limited (the “Tianwo-SES Joint Venture”)

Joint Venture Contract

In February 2014, SES Asia Technologies Limited, one of our wholly owned subsidiaries, entered into a Joint Venture Contract (the “JV Contract”) with Zhangjiagang Chemical Machinery Co., Ltd., which subsequently changed its legal name to Suzhou Thvow Technology Co. Ltd. (“STT”), to form the Tianwo-SES Joint Venture. The purpose of the Tianwo-SES Joint Venture is to establish the Company’s gasification technology as the leading gasification technology in the Tianwo-SES Joint Venture territory (which is China, Indonesia, the Philippines, Vietnam, Mongolia and Malaysia) by becoming a leading provider of proprietary equipment and engineering services for the technology. The scope of the Tianwo-SES Joint Venture is to market and license our gasification technology via project sublicenses; procurement and sale of proprietary equipment and services; coal testing; and engineering, procurement and research and development related to the technology. STT contributed 53.8 million yuan in April 2014 and was required to contribute an additional 46.2 million yuan within two years of such date for a total contribution of 100 million yuan (approximately \$15.0 million) in cash to the Tianwo-SES Joint Venture, and owns 65% of the Tianwo-SES Joint Venture.

We have contributed certain exclusive technology sub-licensing rights into the Tianwo-SES Joint Venture for the territory pursuant to the terms of a Technology Usage and Contribution Agreement (the “TUCA”) entered into among the Tianwo-SES Joint Venture, STT and us on the same date and further described in more detail below. We own 35% of the Tianwo-SES Joint Venture. Under the JV Contract, neither party may transfer their interests in the Tianwo-SES Joint Venture without first offering such interests to the other party.

The JV Contract also includes a non-competition provision which requires that the Tianwo-SES Joint Venture be the exclusive legal entity within the Tianwo-SES Joint Venture territory for the marketing and sale of any gasification technology or related equipment that utilizes low quality coal feedstock. Notwithstanding this, STT has the right to manufacture and sell gasification equipment outside the scope of the Tianwo-SES Joint Venture within the Tianwo-SES Joint Venture territory. In addition, we have the right to develop and invest equity in projects outside of the Tianwo-SES Joint Venture within the Tianwo-SES Joint Venture territory. After the termination of the Tianwo-SES Joint Venture, STT must obtain written consent from us to market development of any gasification technology that utilizes low quality coal feedstock in the Tianwo-SES Joint Venture territory.

The JV Contract may be terminated upon, among other things: (i) a material breach of the JV Contract which is not cured, (ii) a violation of the TUCA, (iii) the failure to obtain positive net income within 24 months of establishing the Tianwo-SES Joint Venture or (iv) mutual agreement of the parties.

TUCA

Pursuant to the TUCA, we have contributed to the Tianwo-SES Joint Venture certain exclusive rights to our gasification technology in the Tianwo-SES Joint Venture territory, including the right to: (i) grant site specific project sub-licenses to third parties; (ii) use our marks for proprietary equipment and services; (iii) engineer and/or design processes that utilize our technology or our other intellectual property; (iv) provide engineering and design services for joint venture projects and (v) take over the development of projects in the Tianwo-SES Joint Venture territory that have previously been developed by us and our affiliates.

The Tianwo-SES Joint Venture will be the exclusive operational entity for business relating to our technology in the Tianwo-SES Joint Venture territory. If the Tianwo-SES Joint Venture loses exclusivity due to a breach by us, STT is to be compensated for direct losses and all lost project profits. We will also provide training for technical personnel of the Tianwo-SES Joint Venture through the second anniversary of the establishment of the Tianwo-SES Joint Venture. We will also provide a review of engineering works for the Tianwo-SES Joint Venture. If modifications are suggested by us and not made, the Tianwo-SES Joint Venture bears the liability resulting from such failure. If we suggest modifications and there is still liability resulting from the engineering work, it is our liability.

Any party making, whether patentable or not, improvements relating to our technology after the establishment of the Tianwo-SES Joint Venture, grants to the other party an irrevocable, non-exclusive, royalty free right to use or license such improvements and agrees to make such improvements available to us free of charge. All such improvements shall become part of our technology and both parties shall have the same rights, licenses and obligations with respect to the improvement as contemplated by the TUCA.

The Tianwo-SES Joint Venture is required to establish an Intellectual Property Committee, with two representatives from the Tianwo-SES Joint Venture and two from SES. This Committee shall review all improvements and protection measures and recommend actions to be taken by the Tianwo-SES Joint Venture in furtherance thereof. Notwithstanding this, each party is entitled to take actions on its own to protect intellectual property rights. As of September 30, 2016 that committee was yet to be formed.

Any breach of or default under the TUCA which is not cured on notice entitles the non-breaching party to terminate. The Tianwo-SES Joint Venture indemnifies us for misuse of our technology or infringement of our technology upon rights of any third party.

Current relationship with STT

The second capital contribution from STT of 46.2 million yuan (approximately \$6.9 million) was not paid in April 2016 as required by our initial JV Contract and currently remains outstanding. We notified STT in writing to determine the status of the payment, and other contractual breaches related to the TUCA, and the JV Contract, and have continued to follow up on this issue. Should the payment or the other breaches of the TUCA not be cured, we will consider any and all legal actions to resolve these issues.

CESI-SES Investment Platform

In March 2016, we entered a strategic Joint Project Development and Investment Agreement with China Environment State Investment Co., Ltd. (“CESI”). CESI is a state-owned enterprise established in Beijing under the China Ministry of Environmental Protection that is charged with, and funded to, develop and invest in the energy conservation and environmental protection industry. We and CESI have agreed to develop, jointly invest, and build a total of no less than 20 projects using our gasification technology over the next five years. Further, we and CESI are targeting to bring a minimum of two projects through development within 12 months. Equity in the projects for investment by us and CESI is expected to be owned 51% by CESI, and 49% by us through our wholly owned Hong Kong subsidiary, SES Clean Energy Investment Holdings Limited. We and CESI have initially identified a pipeline of potential projects.

In July 2016, CESI’s executive management changed related to a restructuring agreement and the entrance of a new shareholders. We have been in contact with the new management team and we have been told that CESI will evaluate the economics of the projects discussed above and will make its decision to continue in the projects based upon their views of the projects’ economics. If CESI were to not continue to participate in these projects, it could cause delays as we seek replacement partners and alternative funding sources. We can provide no assurances as to the level of involvement which CESI will have in the projects in the future but we believe that we will be able to find a replacement partner should CESI decide to not participate.

Dongying Projects

In May 2016, we announced the first of our projects on the platform discussed above. The project will use SGT to produce lower-cost hydrogen in the Lijin County Binhai New District industrial park in Dongying, Shandong Province. The build-out consists of three projects completed in phases with an estimated preliminary total investment to be approximately 2 billion yuan (\$299.5 million). In June 2016, we signed an investment and cooperation agreement with Shandong Dongying Hekou District Government. The project will use SGT to produce lower-cost hydrogen needed for clean fuels production by refineries at the Hekou Blue Economy Industrial Park Project in Dongying City, Shandong Province. The build-out consists of multiple phases with an estimated preliminary total investment to be approximately 550 million yuan (\$82.4 million).

Australian Future Energy Pty Ltd ("AFE") & Batchfire Resources Pty Ltd ("Batchfire")

In May 2015, we established AFE together with Australian company Ambre Investments PTY Limited ("Ambre"). AFE is a development stage Australian company which is seeking to deploy SGT into projects in Australia where AFE or its affiliates would own equity and to secure ownership positions in low quality, low cost, coal resources such as unmarketable coal generally produced from coal mining operations in order to secure a long-term source of feedstock for the projects that would utilize SGT.

In forming AFE, we contributed conditional exclusive access to SGT limited to Australia through a master technology agreement in return for an ownership interest in AFE. In addition, we contributed certain early stage engineering support for AFE's business development through an engineering consulting agreement while Ambre contributed cash for the early stage business development. In connection with this agreement, in fiscal year 2016, we recognized approximately \$0.2 million in Related party consulting services. At September 30, 2016, we owned approximately 37% of AFE. Because of the early stage business development expenses incurred by AFE, the carrying value of AFE was zero as of both September 30, 2016 and June 30, 2016.

Because of its early stage business development efforts associated with the Callide coal mine in Central Queensland, Australia, AFE created Batchfire. Batchfire was a spin-off company which was distributed to the shareholders of AFE in December 2015. Batchfire is registered in Australia and was formed for the purpose of purchasing the Callide thermal coal mine from Anglo-American plc ("Anglo-American"). On October 31, 2016, Batchfire announced that it had completed its acquisition of the Callide thermal coal mine from Anglo American. The Callide mine is a mature and significantly sized coal producer with substantial recoverable thermal coal reserves. After the transaction on October 31, 2016 the Company owns an approximately 11% interest in Batchfire. Because of the nature of our contribution, our carrying value of Batchfire was zero as of both September 30, 2016 and June 30, 2016.

Batchfire intends to operate the Callide mine and implement its planned improvements to increase output from the mine and lower the mining costs. AFE is currently evaluating project opportunities that would use SGT and utilize the unmarketable coal from the Callide mine to responsibly manufacture energy or chemical products.

GTI Agreement

In November 2009, we entered into an Amended and Restated License Agreement, or the GTI Agreement, with GTI, replacing the Amended and Restated License Agreement between us and GTI dated August 31, 2006, as amended. Under the GTI Agreement, we maintain our exclusive worldwide right to license the U-GAS[®] technology for all types of coals and coal/biomass mixtures with coal content exceeding 60%, as well as the non-exclusive right to license the U-GAS[®] technology for 100% biomass and coal/biomass blends exceeding 40% biomass.

In order to sublicense any U-GAS[®] system, we are required to comply with certain requirements set forth in the GTI Agreement. In the preliminary stage of developing a potential sublicense, we are required to provide notice and certain information regarding the potential sublicense to GTI and GTI is required to provide notice of approval or non-approval within ten business days of the date of the notice from us, provided that GTI is required to not unreasonably withhold their approval. If GTI does not respond within that ten business day period, they are deemed to have approved of the sublicense. We are required to provide updates on any potential sublicenses once every three months during the term of the GTI Agreement. We are also restricted from offering a competing gasification technology during the term of the GTI Agreement.

For each U-GAS[®] unit which we license, design, build or operate for ourselves or for a party other than a sub-licensee and which uses coal or a coal and biomass mixture or biomass as the feedstock, we must pay a royalty based upon a calculation using the MMBtu per hour of dry syngas production of a rated design capacity, payable in installments at the beginning and at the completion of the construction of a project, or the Standard Royalty. If we invest, or have the option to invest, in a specified percentage of the equity of a third party, and the royalty payable by such third party for their sublicense exceeds the Standard Royalty, we are required to pay to GTI an agreed percentage split of third party licensing fees, or the Agreed Percentage, of such royalty payable by such third party. However, if the royalty payable by such third party for their sublicense is less than the Standard Royalty, we are required to pay to GTI, in addition to the Agreed Percentage of such royalty payable by such third party, the Agreed Percentage of our dividends and liquidation proceeds from our equity investment in the third party. In addition, if we receive a carried interest in a third party, and the carried interest is less than a specified percentage of the equity of such third party, we are required to pay to GTI, in our sole discretion, either (i) the Standard Royalty or (ii) the Agreed Percentage of the royalty payable to such third party for their sublicense, as well as the Agreed Percentage of the carried interest. We will be required to pay the Standard Royalty to GTI if the percentage of the equity of a third party that we (a) invest in, (b) have an option to invest in, or (c) receive a carried interest in, exceeds the percentage of the third party specified in the preceding sentence.

We are required to make an annual payment to GTI for each year of the term, with such annual payment due by the last day of January of the following year; provided, however, that we are entitled to deduct all royalties paid to GTI in a given year under the GTI Agreement from this amount, and if such royalties exceed the annual payment amount in a given year, we are not required to make the annual payment. We must also provide GTI with a copy of each contract that we enter into relating to a U-GAS[®] system and report to GTI with our progress on development of the technology every six months.

For a period of ten years, we and GTI are restricted from disclosing any confidential information (as defined in the GTI Agreement) to any person other than employees of affiliates or contractors who are required to deal with such information, and such persons will be bound by the confidentiality provisions of the GTI Agreement. We have further indemnified GTI and its affiliates from any liability or loss resulting from unauthorized disclosure or use of any confidential information that we receive.

While the core of our technology is the U-GAS[®] system, we have continued to innovate and modify the process to a point where we maintain certain intellectual property rights over SGT. Since the original licensing in 2004, we have maintained a strong relationship with GTI and continue to benefit from the resources and collaborative work environment that GTI provides us. It is in part for that reason, in May 2016, we exercised the first of our 10-year extensions and now maintain the exclusive license described above through 2026.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Qualitative disclosure about market risk.

We are exposed to certain qualitative market risks as part of our ongoing business operations, including risks from changes in foreign currency exchange rates and commodity prices that could impact our financial position, results of operations and cash flows. We manage our exposure to these risks through regular operating and financing activities, and may, in the future, use derivative financial instruments to manage this risk. We have not entered into any derivative financial instruments to date.

Foreign currency risk

We conduct operations in China and our functional currency in China is the Chinese Renminbi Yuan ("RMB"). Our consolidated financial statements are expressed in U.S. Dollars ("USD") and will be negatively affected if foreign currencies, such as the RMB, depreciate relative to the USD. For example, there has recently been intense pressure on the RMB due to the devaluation by China's central bank. We cannot predict at this time when prices will stabilize or recover.

In addition, our currency exchange losses may be magnified by exchange control regulations in China or other countries that restrict our ability to convert RMB into USD. The People's Bank of China, the monetary authority in China, sets the spot rate of the RMB, and may also use a variety of techniques, such as intervention by its central bank or imposition of regulatory controls or taxes, to affect the exchange rate relative to the USD. In the future, the Chinese government may also issue a new currency to replace its existing currency or alter the exchange rate or relative exchange characteristics resulting in devaluation or revaluation of the RMB in ways that may be adverse to our interests.

Commodity price risk

Our business plan is to purchase coal and other consumables from suppliers and to sell commodities, such as syngas, methanol and other products. Coal is the largest component of our costs of product sales and in order to mitigate coal price fluctuation risk for future projects, we expect to enter into long-term contracts for coal supply or to acquire coal assets.

Historically, the majority of our revenues are derived from the sale of methanol in China. We do not have long term off take agreements for these sales, so revenues fluctuate based on local market spot prices, which have been under significant pressure, and we are unsure of how much longer this will continue. Our liquidity and capital resources may be materially adversely affected if markets remain under pressure, and we are unable to obtain satisfactory prices for these commodities or if prospective buyers do not purchase these commodities.

Hedging transactions may be available to reduce our exposure to these commodity price risks, but availability may be limited and we may not be able to successfully hedge this exposure at all. To date, we have not entered into any hedging transactions.

Customer credit risk

We are exposed to the risk of financial non-performance by customers. To manage customer credit risk, we monitor credit ratings of customers and seek to minimize exposure to any one customer where other customers are readily available.

Item 4. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures

The Company's management, including our Chief Executive Officer and our Chief Financial Officer, is responsible for establishing and maintaining adequate internal control over financial reporting for the Company, as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act. Under the supervision and with the participation of the Company's management, including the Company's principal executive and principal financial officers, the Company conducted an evaluation of the effectiveness of its internal control over financial reporting based on the framework in *Internal Control — Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (the "COSO Framework").

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the Company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements. A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of the annual or interim financial statements will not be prevented or detected on a timely basis.

Based on our evaluation under the COSO Framework, our management concluded that our internal control over financial reporting was not effective as of June 30, 2016, as a result of the identification of material weakness described below.

Internal control over the valuation of cost method investments- We did not maintain effective internal controls over the preparation and review of the impairment evaluation of our cost method investments. Specifically, we did not effectively operate controls over management's review of the impairment assessment, including its review of certain elements related to the valuation of our cost based investments. This material weakness resulted in errors that, if not corrected, would have resulted in a material misstatement of the amount of our impairment of our cost method investments.

In light of the material weakness described above, our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures were not effective at the reasonable assurance level as of September 30, 2016.

Management has taken immediate steps to address and improve our controls over our internal controls over the valuation of cost method investments and a remediation plan has been put into place. We have developed an implementation plan for the new processes and controls to remediate the material weakness identified. While we had the necessary controls as of September 30, 2016, we will not be able to conclude the material weakness has been remediated until we are able to test its operational effectiveness as we must maintain such effectiveness over multiple quarters to ensure full remediation. We expect to test the controls and conclude as to whether the material weakness has been remediated during the third quarter of fiscal year 2017.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Changes in Internal Control Over Financial Reporting

Outside of the remediation efforts discussed above, there have been no changes in our internal control over financial reporting during the three months ended September 30, 2016 that have materially affected, or that are reasonably likely to materially affect, our internal control over financial reporting.

PART II

Item 1. Legal Proceedings.

None.

Item 1A. Risk Factors.

There are numerous factors that affect our business and results of operations, many of which are beyond our control. In addition to information set forth in this quarterly report, you should carefully read and consider "Item 1A. Risk Factors" in Part I and "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations" in Part II of our annual report on Form 10-K for the year ended June 30, 2016, which contains descriptions of significant risks that might cause our actual results of operations in future periods to differ materially from those currently anticipated or expected. Except as discussed below, there have been no material changes from the risks previously disclosed in our annual report on Form 10-K for the year ended June 30, 2016.

We will require substantial additional funding, and our failure to raise additional capital necessary to support and expand our operations could reduce our ability to compete and could harm our business.

As of September 30, 2016, we had \$11.0 million in cash and cash equivalents. We currently plan to use our available cash for (i) expanding our technology and securing orders and associated tasks with developing our business with a prime focus on the markets of syngas for direct replacement of natural gas, syngas for producing substitute natural gas and power; (ii) securing new partners for our technology business; (iii) technology product advancement for power applications and industrial syngas; (iv) general and administrative expenses; and (v) working capital and other general corporate purposes.

We do not currently have all of the financial resources to fully develop and execute on all of our other business opportunities; however, we intend to finance our development through paid services, technology access fees, and equity financings and by securing financial and strategic partners focused on development of these opportunities. We can make no assurances that our business operations will provide us with sufficient cash flows to continue our operations. We will need to raise additional capital through equity and debt financing for any new ventures that are developed, to support our existing projects and possible expansions thereof and for our corporate general and administrative expenses. Uncertainty in the Chinese economy, including as related to the devaluation of the yuan, will have a significant impact on the ability of our partners to provide financing in China. We may consider a full range of financing options in order to create the most value in the context of the increasing interest we are witnessing in our proprietary technology.

We cannot provide any assurance that any financing will be available to us in the future on acceptable terms or at all. Any such financing could be dilutive to our existing stockholders. If we cannot raise required funds on acceptable terms, we may not be able to, among other things, (i) maintain our general and administrative expenses at current levels including retention of key personnel and consultants; (ii) successfully develop our licensing and related service businesses; (iii) fund certain obligations as they become due; (iv) negotiate and enter into new gasification plant development contracts and licensing agreements; (v) make additional capital contributions to our joint ventures; (vi) respond to competitive pressures or unanticipated capital requirements; or (vii) repay our indebtedness.

We may be subject to future impairment losses due to potential declines in the fair value of our assets .

During the fiscal year of 2015 and 2016, there was a significant decline in methanol prices in the China commodity market, which put significant pressure on our ZZ Joint Venture plant methanol production margins leading to a \$20.9 million impairment of that asset during the fiscal year ended June 30, 2015. Management evaluated the need to take an impairment of the ZZ Joint Venture plant as of June 30, 2016 and deemed no impairment was required. The net book value of the ZZ Joint Venture plant was approximately \$8.4 million as of September 30, 2016 and is included as part of our assets of discontinued operations.

Because of the current operating and liquidity concerns ongoing at the Yima Joint Ventures, our management evaluated its investment in the Yima Joint Ventures to determine whether an other than temporary decrease in value had occurred for the year ended June 30, 2016. Management determined that the decrease in value due to the shutdown and liquidity situation are other than temporary in nature and therefore management conducted an impairment analysis utilizing a discounted cash flow fair market valuation with the assistance of a third party valuation expert. In this valuation, significant unobservable inputs were used to calculate the fair value of the investment. The valuation led to the conclusion that the investment in the Yima Joint Ventures was impaired as of June 30, 2016 and accordingly we recorded an \$8.6 million impairment for the fiscal year ended June 30, 2016. The carrying value of our Yima investment was approximately \$26.2 million as of both September 30, 2016 and June 30, 2016. We continue to monitor the Yima Joint Ventures and could take an additional impairment in the future if operating conditions do not meet our current expectations, or if the liquidity situation worsens.

Should general economic, market or business conditions decline further, and continue to have a negative impact on our stock price or revenues, we may be required to record impairment charges in the future, which could materially and adversely affect financial condition and results of operation.

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

None

Item 3. Defaults Upon Senior Securities.

None.

Item 4. Mine Safety Disclosures

Not Applicable.

Item 5. Other Information.

None.

Item 6. Exhibits

<u>Number</u>	<u>Description of Exhibits</u>
10.1+	Amendment to Consulting Agreement between the Company and Robert Rigdon dated October 2, 2016 (incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K filed on October 5, 2016).
10.2+	Employment Letter between the Company and Scott Davis dated October 14, 2016 (incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K filed on October 19, 2016).
10.3+	Consulting Agreement between the Company and Roger Ondreko dated October 14, 2016 (incorporated by reference to Exhibit 10.4 to the Company's Current Report on Form 8-K filed on October 19, 2016).
31.1*	Certification of Chief Executive Officer of Synthesis Energy Systems, Inc. pursuant to Rule 13a-14(a) promulgated under the Securities Exchange Act of 1934, as amended.
31.2*	Certification of Chief Financial Officer of Synthesis Energy Systems, Inc. pursuant to Rule 13a-14(a) promulgated under the Securities Exchange Act of 1934, as amended.
32.1*	Certification of Chief Executive Officer of Synthesis Energy Systems, Inc. pursuant to Rule 13a-14(b) promulgated under the Securities Exchange Act of 1934, as amended, and Section 1350 of Chapter 63 of Title 18 of the United States Code.
32.2*	Certification of Chief Financial Officer of Synthesis Energy Systems, Inc. pursuant to Rule 13a-14(b) promulgated under the Securities Exchange Act of 1934, as amended, and Section 1350 of Chapter 63 of Title 18 of the United States Code.
101.INS	XBRL Instance Document.**
101.SCH	XBRL Taxonomy Extension Schema Document.**
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.**
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.**
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.**
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.**

+ Management contract or compensatory plan or arrangement.

* Filed herewith.

** In accordance with Rule 406T of Regulation S-T, the XBRL information in Exhibit 101 to this quarterly report on Form 10-Q shall not be deemed to be "filed" for purposes of Section 18 of the Securities Exchange Act of 1934, as amended ("Exchange Act"), or otherwise subject to the liability of that section, and shall not be incorporated by reference into any registration statement or other document filed under the Securities Act of 1933, as amended, or the Exchange Act, except as shall be expressly set forth by specific reference in such filing.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

SYNTHESIS ENERGY SYSTEMS, INC.

Date: November 14, 2016

By: /s/ DeLome Fair
DeLome Fair
President and Chief Executive Officer

Date: November 14, 2016

By: /s/ Scott Davis
Scott Davis
Chief Accounting Officer, Principal Financial
Officer and Corporate Secretary

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER PURSUANT TO RULE 13a-14(a)/15d-14(a) PROMULGATED UNDER THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED

I, DeLome Fair, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Synthesis Energy Systems, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 14, 2016

/s/ DeLome Fair

DeLome Fair

President and Chief Executive Officer

CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER PURSUANT TO RULE 13a-14(a) PROMULGATED UNDER THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED

I, Scott Davis, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Synthesis Energy Systems, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 14, 2016

/s/ Scott Davis

Chief Accounting Officer, Principal Financial
Officer and Corporate Secretary

**CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906
OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Synthesis Energy Systems, Inc. (the "Company") on Form 10-Q for the period ended September 30, 2016 (the "Report"), as filed with the Securities and Exchange Commission on the date hereof, I, DeLome Fair, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

1. The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ DeLome Fair

DeLome Fair

President and Chief Executive Officer

November 14, 2016

**CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER
PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906
OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Synthesis Energy Systems, Inc. (the "Company") on Form 10-Q for the period ended September 30, 2016 (the "Report"), as filed with the Securities and Exchange Commission on the date hereof, I, Scott Davis, Chief Accounting Officer of the Company, certify, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

1. The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Scott Davis

Scott Davis
Chief Accounting Officer, Principal Financial
Officer and Corporate Secretary
November 14, 2016