

CASPIAN SERVICES INC  
Form 10-Q  
August 13, 2012

UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
Washington, DC 20549

FORM 10-Q

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

For the Quarterly Period Ended June 30, 2012

☐ 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 000-33215

CASPIAN SERVICES, INC.  
(Exact name of registrant as specified in its charter)

Nevada  
(State or other jurisdiction of  
incorporation or organization)

87-0617371  
(I.R.S. Employer  
Identification No.)

2319 Foothill Boulevard, Suite 160  
Salt Lake City, Utah  
(Address of principal executive offices)

84109  
(Zip Code)

(801) 746-3700  
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, 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 (Do not check if a smaller reporting company)  
☒ Smaller reporting company

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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 August 6, 2012, the registrant had 52,657,574 shares of common stock, par value \$0.001, issued and outstanding.

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CASPIAN SERVICES, INC. AND SUBSIDIARIES  
FORM 10-Q  
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## PART I - FINANCIAL INFORMATION

## Item 1. Financial Statements

CASPIAN SERVICES, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

(Dollars in thousands, except share and per share data)

	June 30, 2012	September 30, 2011
<b>ASSETS</b>		
Current Assets		
Cash	\$ 2,897	\$ 6,136
Trade accounts receivable, net of allowance of \$1,603 and \$2,915, respectively	9,529	13,899
Trade accounts receivable from related parties, net of allowance of \$3,263 and \$3,326, respectively	1,249	2,674
Other receivables, net of allowance of \$0 and \$18, respectively	1,185	943
Inventories	1,771	1,845
Inventories held for sale, net of allowance of \$1,791 and \$1,809, respectively	856	905
Prepaid taxes	2,299	1,832
Advances paid	1,540	647
Deferred tax assets	1,515	1,621
Prepaid expenses and other current assets	930	1,284
Total Current Assets	23,771	31,786
Vessels, equipment and property, net	60,066	66,063
Drydocking costs, net	51	258
Goodwill	230	232
Intangible assets, net	102	148
Long-term prepaid taxes	5,455	5,352
Investments	13	14
Long-term other receivables, net of current portion	1,154	1,206
Total Assets	\$ 90,842	\$ 105,059
<b>LIABILITIES AND EQUITY</b>		
Current Liabilities		
Accounts payable	\$ 2,694	\$ 4,923
Accounts payable to related parties	2	16
Accrued expenses	788	1,460
Taxes payable	1,330	2,317
Deferred revenue	51	587
Accelerated put option liability	17,318	15,817
Long-term debt - current portion	58,474	57,120
Total Current Liabilities	80,657	82,240
Long-term deferred revenue from related parties	2,920	3,072
Long-term deferred income tax liability	484	758
Total Long-Term Liabilities	3,404	3,830
Total Liabilities	84,061	86,070

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Equity			
Common stock, \$0.001 par value per share; 150,000,000 shares authorized;			
52,657,574 and 52,213,757 shares issued and outstanding, respectively	53		53
Additional paid-in capital	64,787		64,724
Accumulated deficit	(34,678)		(24,313)
Accumulated other comprehensive loss	(14,887)		(14,254)
Equity attributable to Caspian Services, Inc. Shareholders	15,275		26,210
Deficit attributable to noncontrolling interests	(8,494)		(7,221)
Total Equity	6,781		18,989
Total Liabilities and Equity	\$	90,842	\$ 105,059

See accompanying notes to the condensed consolidated financial statements.

CASPIAN SERVICES,  
INC. AND  
SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
(Unaudited)  
(Dollars in thousands,  
except per share data)

	For the Three Months Ended June 30, 2012		2011	For the Nine Months Ended June 30, 2012		2011		
Revenues								
Vessel revenues	\$	5,205	\$	7,928	\$	13,674	\$	23,021
Geophysical service revenues (which includes \$84 and \$4,070 from related parties for the three and nine months ended June 30, 2011, respectively)		2,393		143	6,028		10,597	
Marine base service revenues (which includes \$164 and \$448 from related parties for the three and nine months ended June 30, 2012, respectively and \$163 and \$457 from related parties for the three and nine months ended June 30, 2011, respectively)		223		282	741		876	
Total Revenues		7,821		8,353	20,443		34,494	
Operating Expenses								
Vessel operating costs		2,548		5,021	7,806		13,753	
Cost of geophysical service revenues		2,190		826	5,385		5,985	
Cost of marine base service revenues		252		298	511		637	
Depreciation and amortization		1,773		1,781	5,525		5,705	
Impairment loss		27		-	177		322	
General and administrative expense		2,997		3,059	7,919		8,311	
Total Costs and Operating Expenses		9,787		10,985	27,323		34,713	
Loss from Operations		(1,966)		(2,632)	(6,880)		(219)	

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Other Income					
(Expense)					
Interest expense	(1,865)		(1,740)	(5,228)	(5,951)
Foreign currency transaction income (loss)	(144)		456	(553)	637
Interest income	75		6	169	26
Other non-operating income, net	21		60	77	225
Net Other Expense	(1,913)		(1,218)	(5,535)	(5,063)
Loss from Continuing Operations Before Income Tax					
Benefit from (provision for) income tax	458		198	739	(1,159)
Loss from continuing operations	(3,421)		(3,652)	(11,676)	(6,441)
Loss from discontinued operations	-		(265)	-	(1,126)
Net loss	(3,421)		(3,917)	(11,676)	(7,567)
Net loss attributable to noncontrolling interests	794		459	1,311	1,536
Net loss attributable to Caspian Services, Inc	\$ (2,627)	\$ (3,458)	\$ (10,365)	\$ (6,031)	
Basic and Diluted Loss per Share from continuing operations					
Basic and Diluted Loss per Share from discontinued operations	-	(0.01)	-	(0.02)	
Basic and Diluted Loss per Share	\$ (0.06)	\$ (0.08)	\$ (0.22)	\$ (0.14)	
Weighted Average Shares Outstanding	52,657,574	52,213,757	52,657,574	52,213,757	
Amounts attributable to Caspian Services, Inc:					
Loss from continuing operations, net of tax	\$ (2,627)	\$ (3,193)	\$ (10,365)	\$ (4,905)	
Discontinued operations, net of tax	-	(265)	-	(1,126)	
Net loss	\$ (2,627)	\$ (3,458)	\$ (10,365)	\$ (6,031)	

See accompanying notes to the condensed consolidated financial statements.





CASPIAN SERVICES, INC AND SUBSIDIARIES  
 CONDENSED CONSOLIDATED STATEMENTS OF CASH  
 FLOWS (Unaudited)  
 (Dollars in thousands, except share and per share data)

For the Nine Months  
 Ended June 30,  
 2012 2011

Cash flows from operating activities:

Net loss	\$	(11,676)	\$	(7,567)
Adjustments to reconcile net loss to net cash provided by operating activities:				
Depreciation and amortization		5,525		5,705
Impairment loss		177		1,099
Accrued Interest on accelerated put option		1,681		1,553
Foreign currency transaction loss (gain)		553		(637)
Stock based compensation		63		88
Changes in current assets and liabilities:				
Trade accounts receivable		4,265		6,605
Trade accounts receivable from related parties		1,418		(3,083)
Other receivables		(403)		6
Inventories		55		(49)
Inventories held for sale		40		28
Prepaid taxes		(486)		(747)
Advances paid		(910)		(136)
Deferred tax assets		90		258
Prepaid expenses and other current assets		346		638
Long-term prepaid taxes		(160)		39
Long-term other receivables, net of current portion		41		46
Accounts payable		(2,225)		322
Accounts payable to related parties		(28)		(516)
Accrued expenses		3,354		3,469
Taxes payable		(972)		(587)
Deferred revenue		(535)		(1,551)
Long-term deferred revenue from related parties		(121)		-
Long-term deferred income tax liability		(268)		243
Net cash provided by (used in) operating activities	\$	(176)	\$	5,226

Cash flows from investing activities:

Investment in securities		-		(14)
Payments to purchase vessels, equipment and property		(827)		(2,275)
Net cash used in investing activities	\$	(827)	\$	(2,289)

Cash flows from financing activities:

Payments on long-term debt		(2,000)		(734)
Net cash used in financing activities	\$	(2,000)	\$	(734)
Effect of exchange rate changes on cash		(236)		893
Net change in cash		(3,239)		3,096
Cash at beginning of period		6,136		5,707
Cash at end of period	\$	2,897	\$	8,803

Supplemental disclosure of cash flow information:

Cash paid for interest	-	734
Cash paid for income tax	478	1,232

See accompanying notes to the condensed consolidated financial statements.

CASPIAN SERVICES, INC. AND SUBSIDIARIES  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
June 30, 2012 (UNAUDITED)  
(Dollars in thousands, except share and per share data)

NOTE 1 — THE COMPANY AND BASIS OF PRESENTATION

**Interim Financial Information** — The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and pursuant to the rules and regulations of the United States Securities and Exchange Commission (“SEC”). Accordingly, they are condensed and do not include all of the information and notes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments considered necessary for a fair and comparable presentation have been included and are of a normal recurring nature. The accompanying financial statements should be read in conjunction with the Caspian Services, Inc. (the “Company” or “CSI”) most recent annual financial statements included in its annual report on Form 10-K filed with the SEC on January 13, 2012. Operating results for the nine-month period ended June 30, 2012 are not necessarily indicative of the results that may be expected for the year ending September 30, 2012.

**Principles of Consolidation** — The accompanying condensed consolidated financial statements are presented in conformity with accounting principles generally accepted in the United States of America and include operations and balances of Caspian Services, Inc. and its wholly-owned subsidiaries: Caspian Services Group Limited (“CSGL”), Caspian Services Group LLP (“Caspian LLP”), TatArka LLP (“TatArka”), Caspian Real Estate, Ltd (“CRE”), Caspian Geophysics, Ltd (“CGEO”), Caspian Services Inc. Kazakhstan LLP (“Caspian Inc. Kazakhstan”), Caspian Services Group B.V. (“Caspian BV”) ; and include majority owned subsidiaries: Balykshi LLP (“Balykshi”) and Kazmorgeophysica CJSC (“KMG”), collectively “Caspian” or the “Company”. KMG owns a 50% non-controlling interest in Veritas-Caspian LLP (“Veritas-Caspian”) and 15% interest in a joint venture CaspyMorService LLP (“CaspyMorService”). Balykshi owns a 20% interest in a joint venture, Mangistau Oblast Boat Yard LLP (“MOBY”). Ownership of 20% to 50% non-controlling interests are accounted for by the equity method. Ownership of less than a 20% interest is accounted for at cost. Intercompany balances and transactions have been eliminated in consolidation.

**Business Condition** — In 2008 the Company entered into Facility agreements with Altima Central Asia (Master) Fund Ltd. (“Altima”) and Great Circle Energy Services, LLC (“Great Circle”). In June 2011 and July 2011 an otherwise unrelated individual (“Investor”) acquired all right, title and interest in and to the loans associated with the Facility agreements. On September 30, 2011 the Company executed an agreement to consolidate and restructure the loans associated with the Facility agreements (the “Loan Restructuring Agreement”) with the Investor.

Closing of the Loan Restructuring Agreement is subject to a number of closing conditions, including among other things, the Investor reaching agreement with the European Bank for Reconstruction and Development (“EBRD”) to restructure certain EBRD financing agreements, discussed in more detail below. Until the Closing of the Loan Restructuring Agreement the restructured loans will be treated as current liabilities.

CASPIAN SERVICES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2012 (UNAUDITED)

(Dollars in thousands, except share and per share data)

The Company funded a portion of the construction of its marine base through a combination of debt and equity financing agreements with EBRD pursuant to which EBRD provided \$18,600 of debt financing and made an equity investment in the marine base in the amount of \$10,000 in exchange for a 22% equity interest in Balykshi.

In connection with EBRD's 22% equity interest in Balykshi, the Company entered into a Put Option Agreement granting EBRD the right to require the Company to repurchase the 22% equity interest based on Balykshi's fair market value. The put option is exercisable between June 2013 and June 2017. This agreement also contains an acceleration feature that, should a triggering event occur, grants EBRD the right to require the Company to repurchase the \$10,000 equity investment at a 20% annual rate of return at any time following the triggering event.

In accordance with accounting principles generally accepted in the United States of America, the put option is an unconditional obligation and is measured at its fair value based on an estimate of the amount of cash that would be required to settle the liability. At the time of investment, the \$10,000 of proceeds from the equity financing was allocated to the put option which was classified as a long-term liability.

Under the terms of the EBRD Loan Agreement, as amended, Balykshi is required to repay the loan principal and accrued interest in eight equal semi-annual installments commencing November 20, 2011 and then occurring each May 20 and November 20 thereafter until fully repaid. The first two semi-annual repayment installments, due November 20, 2011 and May 20, 2012, were not made. The failure to pay the principal of, or interest on, the EBRD loan when due constitutes an event of default under the EBRD Loan Agreement. The EBRD financing agreements have acceleration right features that, in the event of default, allow EBRD to declare the loans and accrued interest immediately due and payable. As a result, the Company has included the EBRD loan and all accrued interest as current liabilities at June 30, 2012 and September 30, 2011. Additionally, this event of default may trigger the acceleration clause in the Put Option Agreement with EBRD which would allow EBRD to put its \$10,000 investment in Balykshi back to the Company. If EBRD were to accelerate its put right, the Company could be obligated to repay the initial investment plus a 20% annual rate of return. As a result, at September 30, 2011 the Company had accrued \$5,817 of interest expense representing the 20% rate of return on the \$10,000 investment and reclassified the liability from a long-term liability to a current liability. For the nine months ended June 30, 2012 the Company accrued an additional \$1,501 of interest expense to reflect the required return on investment for that period, increasing the value of the put option to \$17,318. EBRD also previously notified the Company that it believes the Company and Balykshi are in violation of certain other covenants of the EBRD financing agreements. As of the date of this quarterly report on Form 10-Q, to the Company's knowledge, EBRD has not sought to accelerate repayment of the loan or the put option.

Should EBRD determine to exercise its acceleration rights or should the Loan Restructuring Agreement not close, the Company currently has insufficient funds to repay these obligations individually or collectively and would be forced to seek other sources of funds to satisfy these obligations. Given our current and near-term anticipated operating results, the difficult credit and equity markets and the Company's current financial condition, the Company believes it would be very difficult to obtain new funding to satisfy these obligations. If the Company is unable to obtain funding to meet these obligations, the lenders could seek any legal remedies available to them to obtain repayment, including forcing the Company into bankruptcy, or in the case of the EBRD loan, which is collateralized by the assets, including the marine base, and bank accounts of Balykshi and CRE, foreclosure by EBRD on such assets and bank accounts.



CASPIAN SERVICES, INC. AND SUBSIDIARIES  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
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(Dollars in thousands, except share and per share data)

The ability of the Company to continue as a going concern is dependent upon, among other things, the Company's ability to reach agreement with EBRD to restructure the EBRD financing agreements and successfully close the Loan Restructuring Agreement or to repay its debt obligations by obtaining additional financing or selling business segments or assets. Uncertainty as to the outcome of these factors raises substantial doubt about the Company's ability to continue as a going concern. The accompanying condensed consolidated financial statements do not include any adjustments that might be necessary if the Company is unable to continue as a going concern.

**Discontinued Operations** – In April 2011, the Company sold its interest in Bauta to an unrelated third party. Upon determining to dispose of Bauta, all prior periods presented have been restated to separately account for the discontinued operations.

**Nature of Operations** —The Company's business consists of three major business segments:

**Vessel Operations** – Vessel operations consist of chartering a fleet of shallow draft offshore support vessels to customers performing oil and gas exploration activities in the Kazakhstan Sector of the North Caspian Sea.

**Geophysical Services** – Geophysical services consist of providing seismic data acquisition services to oil and gas companies operating both onshore in Kazakhstan and offshore in the Kazakhstan sector of the North Caspian Sea and the adjacent transition zone.

**Marine Base Services** – Marine Base Services consists of operating a marine base located at the Port of Bautino on the North Caspian Sea.

**Basic and Diluted Loss Per Share** — Basic loss per common share is calculated by dividing net loss attributable to Caspian Services by the weighted-average number of common shares outstanding. Diluted loss per common share is calculated by dividing net loss attributable to Caspian Services by the weighted-average number of common shares outstanding giving effect to potentially dilutive issuable common shares.

For the three and nine months ended June 30, 2012, the Company had 800,000 options outstanding, 735,785 non-vested restricted shares outstanding and 90,000,000 potential shares related to convertible debt that were not included in the computation of diluted loss per common share because they would be anti-dilutive.

For the three and nine months ended June 30, 2011, the Company had 800,000 options outstanding, 560,492 non-vested restricted shares outstanding and 18,576,467 potential shares related to convertible debt that were not included in the computation of diluted loss per common share because they would be anti-dilutive.

**Concentrations of Credit Risk** — The Company's vessel operations are contracted primarily to a North Caspian Operating Company ("NCOC") service provider. Loss of this customer could have a material negative effect on the Company. Some vessel charter services are provided under contracts with varying terms and through various dates in 2012. However, it is possible that a loss of business could occur in the short or long term. While management expects to renew the contracts periodically, there is no assurance that this customer will renew, or will renew on terms favorable to the Company.



CASPIAN SERVICES, INC. AND SUBSIDIARIES  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
June 30, 2012 (UNAUDITED)  
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Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of trade receivables, trade receivables from related parties and other receivables. The Company manages its exposure to risk through ongoing credit evaluations of its customers; however, the Company generally does not require collateral. In some cases when dealing with new customers the Company requires advance payments. The Company maintains an allowance for doubtful accounts for potential losses.

**Fair Value of Financial Instruments** — The carrying amounts reported in the accompanying condensed consolidated financial statements for other receivables, accounts receivables from related parties, accounts payable to related parties and accrued expenses approximate fair values because of the immediate nature or short-term maturities of these financial instruments. The carrying amount of long-term debts approximates fair value due to the stated interest rates approximating prevailing market rates. See Note 7 for discussion of the fair value of the long-term derivative put option liability.

**Accelerated Put Option Liability** — In connection with EBRD's \$10,000 equity investment to purchase a 22% equity interest in Balykshi, the Company entered into a Put Option Agreement granting EBRD the right to require the Company to repurchase the 22% equity interest. The put option is exercisable between June 2013 and June 2017. The put price is determined based on the fair market value of Balykshi as mutually agreed by the parties. If the put price together with any dividend received by EBRD generates an annual internal rate of return for EBRD in excess of 30% per annum rate (the "put price excess"), the put price shall be reduced by an amount representing half of the put price excess. If the parties are unable to agree upon a fair market valuation, the parties agree to hire a third party expert to determine the put price on the basis of the fair market value of Balykshi, as set forth in the Put Option Agreement. In the event there is a change in control of the Company, EBRD has the right to require the repurchase of the equity interest at its fair market value. The Put Option Agreement also contains an acceleration feature. Should Balykshi: (i) default on \$1,000 or more of debt; (ii) fail to meet the obligations of any of the agreements between Balykshi, the Company and EBRD; (iii) be found to have made false representations to EBRD; or (iv) be declared insolvent, EBRD has the right to accelerate the put option. If the put option is accelerated, EBRD can require the Company to repurchase the \$10,000 equity investment plus a 20% per annum rate of return, taking into account any dividend or other distributions received by EBRD, at any time following one of the events mentioned above. Due to the fact that certain events of default under the EBRD Loan Agreement have occurred and that such could trigger EBRD's accelerated put right, we have reflected an accelerated put option liability of \$17,318, although, as of the date of this quarterly report on Form 10-Q, EBRD has not sought to accelerate the put option.

**Revenue Recognition** — Vessel revenues are usually derived from time charter contracts on a rate-per-day of service basis; therefore, vessel revenues are recognized on a daily basis throughout the contract period. These time charter contracts are generally on a term basis, ranging from one month to three years. The base rate of hire for a contract is generally a fixed rate; however, these contracts often include clauses to recover specific additional costs and mobilization and demobilization costs which are billed on a monthly basis.



CASPIAN SERVICES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2012 (UNAUDITED)

(Dollars in thousands, except share and per share data)

Geophysical service revenue is recognized when services are rendered, accepted by the customer and collectability is reasonably assured. Direct costs are charged to each contract as incurred along with allocated indirect costs for the specific period of service. Losses on contracts are recognized during the period in which the loss first becomes probable and reasonably estimated. Due to the nature of some of the geophysical services provided, certain customers have prepaid their contract services. These prepayments have been deferred and are recognized as revenue as the services are provided.

Marine base service revenue is recognized when services are rendered, accepted by the customer and collectability is reasonably assured.

Receivables — In the normal course of business, the Company extends credit to its customers on a short-term basis. Our principal customers are major oil and natural gas exploration, development and production companies. Credit risks associated with these customers are considered minimal. Dealings with smaller, local companies, particularly with the current difficulties in equity and credit markets, pose the greatest risks. For new geophysical services customers, the Company typically requires an advance payment and it retains the seismic data generated from these services until payment is made in full. The Company routinely reviews its accounts receivable balances and makes provisions for doubtful accounts as necessary. Accounts are reviewed on a case by case basis and losses are recognized in the period if the Company determines it is likely that receivables will not be fully collected. The Company may also provide a general provision for accounts receivables based on existing economic conditions.

Impairment of Long-Lived Assets and Long-Lived Assets to be Disposed Of — Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount that the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell. At September 30, 2010 we concluded that there were indicators of impairment as it related to the marine base. We performed a valuation of the base which included discounted future cash flows from operations and discounted cash flows from the sale of partial ownership interest in the entity. We utilized both a market and income approach when deriving this value. Information was obtained from the most current data available related to the entity. As a result of the analysis, the Company recognized an impairment charge on the marine base. During the nine months ended June 30, 2011, the Company incurred some additional costs on the marine base and as a result of the impairment analysis, the Company concluded that these additional costs were impaired as well and recognized an additional \$322 of impairment. During the nine months ended June 30, 2012, the Company incurred more costs on the marine base, which were fully impaired. The amount of the additional impairment is \$177.

At September 30, 2011 we concluded that there were indicators of impairment as it relates to KMG goodwill. We performed a valuation of KMG assets which included discounted future cash flows from operations. As a result of this valuation we concluded that KMG goodwill was impaired.

CASPIAN SERVICES, INC. AND SUBSIDIARIES  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
June 30, 2012 (UNAUDITED)  
(Dollars in thousands, except share and per share data)

**Income Taxes** — Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences in assets and liabilities and their respective tax bases and attributable to operating loss carry forwards. Differences generally result from the calculation of income under accounting principles generally accepted in the United States of America and the calculation of taxable income calculated under Kazakhstan income tax regulations.

The current regime of penalties and interest related to reported and discovered violations of Kazakhstan's laws, decrees and related regulations can be severe. Penalties include confiscation of the amounts in question for currency law violations, as well as fines of generally 100% of the unpaid taxes. Interest is assessable at rates of generally 0.06% per day. As a result, penalties and interest can result in amounts that are multiples of any unreported taxes. No interest or penalties have been accrued as a result of any tax positions taken. In the event interest or penalties are assessed, we will include these amounts related to unrecognized tax benefits in income tax expense.

A deferred tax liability is not recognized for the following types of temporary differences unless it becomes apparent that those temporary differences will reverse in the foreseeable future:

- (a) An excess of the amount for financial reporting over the tax basis of an investment in a foreign subsidiary or a foreign corporate joint venture, that is essentially permanent in duration; or
- (b) Undistributed earnings of a domestic subsidiary or a domestic corporate joint venture that is essentially permanent in duration.

**Dry-docking Costs** — Our vessels must be periodically dry-docked and pass certain inspections to maintain their operating classification, as mandated by certain maritime regulations. Costs incurred to dry-dock the vessels for certification are deferred and amortized over the period until the next dry-docking, generally 24 months. Dry-docking costs are comprised of painting the vessels, hulls and sides, recoating cargo and fuel tanks, and performing other engine and equipment maintenance activities to bring the vessels into compliance with classification standards.

**Recent Accounting Pronouncements** — In December 2010 the FASB issued Accounting Standards Update No. 2010-28, When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts (ASU 2010-28). ASU 2010-28 amends the criteria for performing Step 2 of the goodwill impairment test for reporting units with zero or negative carrying amounts and requires performing Step 2 if qualitative factors indicate that it is more likely than not that a goodwill impairment exists. ASU 2010-28 becomes effective in fiscal 2012. The Company does not expect ASU 2010-28 to have a material impact on its financial statements.

In January 2010 the FASB issued Accounting Standards Update No. 2010-06, Improving Disclosures about Fair Value Measurements (ASU 2010-06). ASU 2010-06 adds additional disclosures about the different classes of assets and liabilities measured at fair value, the valuation techniques and inputs used, and the activity in Level 3 fair value measurements. Certain provisions of this update become effective in fiscal 2012. The Company does not expect this standard to have a material impact on its financial statements.

## CASPIAN SERVICES, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

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In June 2011 the FASB issued an ASU on presentation of comprehensive income to improve the comparability, consistency and transparency of financial reporting and to increase the prominence of items reported in other comprehensive income. This update changes the requirements for the presentation of other comprehensive income, eliminating the option to present components of other comprehensive income as part of the statement of stockholders' equity, among other items. The guidance requires that all non-owner changes in stockholders' equity be presented in either a single continuous statement of comprehensive income or in two separate but consecutive statements. In December 2011, FASB issued an ASU that deferred portions of the prior ASU relating to the presentation of reclassification adjustments. The remainder of the provision will be effective for the first quarter of fiscal 2013 and as the update only requires a change in presentation, the Company does not expect it to have a material impact on its financial statements.

## NOTE 2 — ATASH MARINE BASE

Construction of the Atash Marine Base located in Bautino Bay commenced in the first quarter of 2008 with the first phase of the project being completed and commissioned in November 2009. The second phase of the base was commissioned in July 2010 subject to agreement with local authorities that Balykshi complete additional dredging works. During the first fiscal quarter 2012 the Company entered into a contract to complete the dredging which is anticipated to cost around \$3,000 and paid \$1,000 as an advance. Currently, Balykshi has insufficient funds to complete the dredging project. If the dredging is not completed in a reasonable period of time, Balykshi could be subject to certain penalties, including the cancelation of permits and termination of operational activities at the marine base until the dredging is completed. The failure by Balykshi or the Company to provide financing for, or to complete, the dredging works could also constitute a default under the EBRD financing agreements.

## NOTE 3 — NOTES PAYABLE

Notes payable consists of the following:

	June 30, 2012	September 30, 2011
Non-negotiable promissory note payable to an investor; interest at 0.26%	\$ 10,821	\$ 10,800
Convertible consolidated promissory note payable to an investor; interest at 12%	26,679	24,446
Loan from investor, paid subsequent to September 30, 2011	-	2,000
EBRD loan and accrued interest at 7% due May 2015 secured by property and bank accounts	20,974	19,874
Total Long-term Debt	58,474	57,120
Less: Current Portion	58,474	57,120
Long-term Debt - Net of Current Portion	\$ -	\$ -



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During the nine months ended June 30, 2012 the Company paid \$2,000 to the Investor, which was credited as a reduction of principal due.

During the nine months ended June 30, 2012 the Company engaged in ongoing discussion with EBRD about restructuring the terms of the EBRD financing agreements. There is no guarantee the Company will be successful in restructuring the EBRD financing agreements.

Until the Company is successful in restructuring the EBRD financing agreements, the EBRD loan, the non-negotiable promissory note and the convertible consolidated promissory note payable to the Investor will be treated as current liabilities in the consolidated financial statements.

#### NOTE 4 — STOCK BASED COMPENSATION PLANS

In January 2012, Alexey Kotov, the Company's Chief Executive Officer and President was issued a restricted stock grant of 443,817 common shares pursuant to the terms of his employment agreement. Except upon the occurrence of certain events, as detailed in his employment agreement, this grant shall vest equally over a period of three years on the anniversary of his employment agreement (August 2), commencing on August 2, 2012.

The shares representing the restricted stock grant have been issued and are deemed outstanding. All unvested shares will be held in escrow by the Company for release in accordance with the vesting schedule. Vesting of the shares is also contingent upon Mr. Kotov's continued employment with the Company on the respective vesting dates.

Compensation expense charged against income for stock-based awards during the three and nine months ended June 30, 2012 was \$19 and \$63, respectively, as compared to \$28 and \$88 during the three and nine months ended June 30, 2011 and is included in general and administrative expense in the accompanying financial statements.

A summary of the non-vested stock under the Company's compensation plan at June 30, 2012 follows:

	Non-Vested Shares	Weighted Average Grant Date Fair Value Per Share
Non-vested at September 30, 2011	331,968	\$0.34
Stock granted	443,817	0.11
Stock vested	(40,000)	0.29
Non-vested at June 30, 2012	735,785	\$0.21

The value of the non-vested stock under the Company's compensation plan at June 30, 2012 is \$22. As of June 30, 2012 unrecognized stock-based compensation was \$44 and will be recognized over the weighted average remaining term of 1.26 years.



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NOTE 5 — COMMITMENTS AND CONTINGENCIES

**Economic Environment**—In recent years, Kazakhstan has undergone substantial political and economic change. As an emerging market, Kazakhstan does not possess a well-developed business infrastructure, which generally exists in a more mature free market economy. As a result, operations carried out in Kazakhstan can involve significant risks, which are not typically associated with those in developed markets. Instability in the market reform process could subject the Company to unpredictable changes in the basic business infrastructure in which it currently operates. Uncertainties regarding the political, legal, tax or regulatory environment, including the potential for adverse changes in any of these factors could affect the Company's ability to operate commercially. Management is unable to estimate what changes may occur or the resulting effect of such changes on the Company's financial condition or future results of operations.

Legislation and regulations regarding taxation, foreign currency translation, and licensing of foreign currency loans in the Republic of Kazakhstan continue to evolve as the central government manages the transformation from a command to a market-oriented economy. The various legislation and regulations are not always clearly written and their interpretation is subject to the opinions of the local tax inspectors. Instances of inconsistent opinions between local, regional and national tax authorities are not unusual.

NOTE 6 — RELATED PARTY TRANSACTIONS

**MOBY** – During October 2008 the Company entered into a lease agreement with MOBY for the lease of three hectares of space at the marine base to operate a vessel repair and drydock facility. Balykshi owns a 20% joint venture interest in MOBY. The lease agreement is for 20 years and calls for a fixed rent payment of \$290 per year. In November 2009, according to the agreement term, MOBY made a partial advance payment of \$3,347, which is being recognized over the 20 year lease term starting from May 2010. This prepayment has been recorded as long-term deferred revenue from related parties on the balance sheet.

The lease revenue recognized from MOBY for the three and nine months ended June 30, 2012 was \$164 and \$448, respectively.

The lease revenue recognized from MOBY for the three and nine months ended June 30, 2011 was \$163 and \$457, respectively.

**KazakhstanCaspiShelf** – During the three and nine months ended June 30, 2011, seismic services valued at \$84 and \$4,070, respectively, were performed for KazakhstanCaspiShelf ("KCS"), a company related through common ownership.

Accounts receivable from related parties as of June 30, 2012 and September 30, 2011 consisted of the following:

## CASPIAN SERVICES, INC. AND SUBSIDIARIES

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(Dollars in thousands, except share and per share data)

Related Party's Name	Description	June 30, 2012	September 30, 2011
Bolz LLP	Seismic services	\$ 3,263	\$ 3,308
MOBY	Marine base	1,249	381
Kazakhstancaspishelf	Equipment rental, services and fuel sales	-	2,308
Others	Services/Indirect costs	-	3
	Allowance for doubtful accounts	(3,263)	(3,326)
<b>TOTAL</b>		<b>\$ 1,249</b>	<b>\$ 2,674</b>

In February 2011 Bolz (a company related through common ownership) transferred its overdue obligations of \$3,263 to BMB Munai LLP (a non-related third party), however, BMB Munai LLP failed to pay the amount due, so during the nine months ended June 30, 2012 the balance was transferred back to Bolz, which is still liable to pay. Accordingly, the balance of \$3,263 and the corresponding allowance for doubtful accounts of (\$3,263) was moved from Trade Accounts Receivable to Accounts Receivable from related parties.

Long-term deferred revenue from related parties as of June 30, 2012 and September 30, 2011 consisted of the following:

Related Party's Name	Description	June 30, 2012	September 30, 2011
MOBY	Advance received for land rental	\$ 2,920	\$ 3,072
<b>TOTAL</b>		<b>\$ 2,920</b>	<b>\$ 3,072</b>

## NOTE 7 — FAIR VALUE MEASUREMENTS

The Company uses fair value to measure certain assets and liabilities on a recurring basis when fair value is the primary measure for accounting. This is done primarily for the put option liability. Fair value is used on a nonrecurring basis to measure certain assets when applying lower of cost or market accounting or when adjusting carrying values. Fair value is also used when evaluating impairment on certain assets, including goodwill, intangibles, and long-lived assets.

## Recurring basis:

At June 30, 2012 the Company had one liability measured at fair value on a recurring basis. The put option liability is a Level 3 measurement based on the underlying value of Balykshi using third party valuations and discounted cash flow analysis. The fair value of the put option liability was \$15,817 at September 30, 2011. As of June 30, 2012 the amount was valued at \$17,318, which is the amount the Company would have to pay if EBRD accelerated its put option. The \$1,501 increase during the nine months ended June 30, 2012 reflects the 20% rate of return.

## NOTE 8 — SEGMENT INFORMATION



Accounting principles generally accepted in the United States of America establish disclosures related to components of a company for which separate financial information is available and evaluated regularly by a company's chief operating decision makers in deciding how to allocate resources and in assessing performance. They also require segment disclosures about products and services as well as geographic area.

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(Dollars in thousands, except share and per share data)

The Company has operations in three segments of its business, namely: Vessel Operations, Geophysical Services and Marine Base Services. All of these operations are located in the Republic of Kazakhstan. Corporate administration is located in the United States of America and the Republic of Kazakhstan.

Further information regarding the operations and assets of these reportable business segments follows:

	For the Three Months Ended June 30,		For the Nine Months Ended June 30,	
	2012	2011	2012	2011
Capital Expenditures				
Vessel Operations	\$ 194	\$ 381	\$ 204	\$ 933
Geophysical Services	316	1,143	623	1,353
Marine Base Services	-	(1)	-	57
Total segments	510	1,523	827	2,343
Corporate assets	-	1	-	58
Less intersegment investments	-	-	-	-
Total consolidated	\$ 510	\$ 1,524	\$ 827	\$ 2,401

## CASPIAN SERVICES, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2012 (UNAUDITED)

(Dollars in thousands, except share and per share data)

	For the Three Months Ended June 30,		For the Nine Months Ended June 30,	
	2012	2011	2012	2011
<b>Revenues</b>				
Vessel Operations	\$ 5,201	\$ 7,928	\$ 13,674	\$ 23,021
Geophysical Services	2,392	143	6,028	10,597
Marine Base Services	267	353	984	1,070
Total segments	7,860	8,424	20,686	34,688
Corporate revenue	-	-	-	-
Less intersegment revenues	(39)	(71)	(243)	(194)
Total consolidated	\$ 7,821	\$ 8,353	\$ 20,443	\$ 34,494
<b>Depreciation and Amortization</b>				
Vessel Operations	\$ (724)	\$ (777)	\$ (2,407)	\$ (2,615)
Geophysical Services	(655)	(628)	(1,977)	(1,969)
Marine Base Services	(394)	(375)	(1,141)	(1,118)
Total segments	(1,773)	(1,780)	(5,525)	(5,702)
Corporate depreciation and amortization	-	(1)	-	(3)
Total consolidated	\$ (1,773)	\$ (1,781)	\$ (5,525)	\$ (5,705)
<b>Interest expense</b>				
Vessel Operations	\$ -	\$ -	\$ -	\$ -
Geophysical Services	(4)	-	(4)	(19)
Marine Base Services	(1,277)	(1,424)	(3,989)	(4,186)
Total segments	(1,281)	(1,424)	(3,993)	(4,205)
Corporate interest expense	(584)	(316)	(1,235)	(1,746)
Total consolidated	\$ (1,865)	\$ (1,740)	\$ (5,228)	\$ (5,951)
<b>Income/(Loss) Before Income Tax</b>				
Vessel Operations	\$ 480	\$ 328	\$ (1,096)	\$ 3,433
Geophysical Services	(1,594)	(2,018)	(3,390)	(91)
Marine Base Services	(2,010)	(1,918)	(6,242)	(6,315)
Total segments	(3,124)	(3,608)	(10,728)	(2,973)
Corporate loss	(755)	(242)	(1,687)	(2,309)
Total consolidated	\$ (3,879)	\$ (3,850)	\$ (12,415)	\$ (5,282)

## CASPIAN SERVICES, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2012 (UNAUDITED)

(Dollars in thousands, except share and per share data)

	For the Three Months Ended June 30,		For the Nine Months Ended June 30,	
	2012	2011	2012	2011
Benefit from (Provision for) Income Tax				
Vessel Operations	\$ 222	\$ (42)	\$ 414	\$ (579)
Geophysical Services	236	240	325	(580)
Marine Base Services	-	-	-	-
Total segments	458	198	739	(1,159)
Corporate provision for income tax	-	-	-	-
Total consolidated	\$ 458	\$ 198	\$ 739	\$ (1,159)
Loss/(Income) attributable to Noncontrolling Interests				
Vessel Operations	\$ -	\$ -	\$ -	\$ -
Geophysical Services	(54)	121	(353)	225
Marine Base Services	848	338	1,664	1,311
Total segments	794	459	1,311	1,536
Corporate noncontrolling interest	-	-	-	-
Total consolidated	\$ 794	\$ 459	\$ 1,311	\$ 1,536
Net Loss/(Income) attributable to Caspian Services Inc.				
Vessel Operations	\$ 702	\$ 286	\$ (682)	\$ 2,854
Geophysical Services	(1,412)	(1,657)	(3,418)	(446)
Marine Base Services	(1,162)	(1,845)	(4,578)	(6,130)
Total segments	(1,872)	(3,216)	(8,678)	(3,722)
Corporate loss	(755)	(242)	(1,687)	(2,309)
Total consolidated	\$ (2,627)	\$ (3,458)	\$ (10,365)	\$ (6,031)
	June 30,	September 30,		
Segment Assets	2012	2011		
Vessel Operations	\$ 19,382	\$ 34,300		
Geophysical Services	22,833	25,385		
Marine Base Services	48,135	49,780		
Total segments	90,350	109,465		
Corporate assets	86,734	86,161		
Less intersegment investments	(86,242)	(90,567)		
Total consolidated	\$ 90,842	\$ 105,059		



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

Unless otherwise indicated by the context, all dollar amounts stated in this Part I, Item 2, other than per share amounts, are presented in thousands and all references to dollar amounts (\$) refers to U.S. dollars.

The following discussion is intended to assist you in understanding our results of operations and our present financial condition. Our condensed consolidated financial statements and the accompanying notes included in this quarterly report on Form 10-Q should be read in conjunction with our annual report on Form 10-K for the year ended September 30, 2011 and our other filings with the Securities and Exchange Commission.

### Forward-Looking Information and Cautionary Statements

This quarterly report contains forward-looking statements as that term is defined in Section 27A of the United States Securities Act of 1933, as amended, (the "Securities Act") and Section 21E of the Securities Exchange Act of 1934, as amended, (the "Exchange Act"). These statements relate to future events or our future financial performance. In some cases, you can identify forward-looking statements by terminology such as "may", "should", "expects", "plans", "anticipates", "believes", "estimates", "predicts", "potential" or "continue" or the negative of these terms or other comparable terminology. Such statements are based on currently available financial and competitive information and are subject to various risks and uncertainties that could cause actual results to differ materially from our historical experience and our present expectations. Undue reliance should not be placed on such forward-looking statements as such statements speak only as of the date on which they are made. These statements are only predictions and involve known and unknown risks, uncertainties and other factors that may cause our or our industry's actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by these forward-looking statements.

Forward-looking statements are predictions and not guarantees of future performance or events. Forward-looking statements are based on current industry, financial and economic information, which we have assessed but which by its nature, is dynamic and subject to rapid and possibly abrupt changes. Our actual results could differ materially from those stated or implied by such forward-looking statements due to risks and uncertainties associated with our business. We hereby qualify all our forward-looking statements by these cautionary statements. These forward-looking statements speak only as of their dates and should not be unduly relied upon. We undertake no obligation to publicly update or revise these forward-looking statements (other than pursuant to reporting obligations imposed on registrants pursuant to the Exchange Act), whether as a result of new information, future events or otherwise.

## Business Review

We do not anticipate demand for our services to grow through fiscal 2012 or 2013. In fact, we expect demand will continue to soften during the next two fiscal years as development of the second phase of the Kashagan oil field development project continues to be delayed. Current projections place commencement of the second phase some time in 2018-2019. We do not anticipate growth in demand for our services until the second phase of the Kashagan development project ramps up.

During the nine months ended June 30, 2012, we operated three business segments: Vessel Operations, Geophysical Services and Marine Base Services.

	For the Three Months Ended June 30,				For the Nine Months Ended June 30,		
	2012	2011	% change		2012	2011	% change
<b>VESSEL OPERATIONS</b>							
Operating Revenue	\$ 5,201	\$ 7,928	-34%		\$ 13,674	\$ 23,021	-41%
Pretax Operating Income/(Loss)	480	328	46%		(1,096)	3,433	-132%
<b>GEOPHYSICAL SERVICES</b>							
Operating Revenue	\$ 2,392	\$ 143	1573%		\$ 6,028	\$ 10,597	-43%
Pretax Operating Loss	(1,594)	(2,018)	-21%		(3,390)	(91)	3625%
<b>MARINE BASE SERVICES</b>							
Operating Revenue	\$ 267	\$ 353	-24%		\$ 984	\$ 1,070	-8%
Pretax Operating Loss	(2,010)	(1,918)	5%		(6,242)	(6,315)	-1%
<b>CORPORATE ADMINISTRATION</b>							
Operating Revenue	\$ -	\$ -	n/a		\$ -	\$ -	n/a
Pretax Operating Loss	(755)	(242)	212%		(1,687)	(2,309)	-27%

## Summary of Operations

Three months ended June 30, 2012 compared to the three months ended June 30, 2011

Total revenue during the three months ended June 30, 2012 was \$7,821 compared to \$8,353 during the three months ended June 30, 2011, a decrease of 6%. Vessel revenues were down by \$2,723 as we generally completed our major contract with Saipem – during the third fiscal quarter 2012 we had only one vessel under charter to Saipem vs. eight vessels during the third fiscal quarter 2011. This decrease was partially off-set by geophysical revenue growth of \$2,250.

We were able to reduce our operating and administrative costs in line with the decrease in total revenue, which made our net loss attributable to Caspian Services, Inc. decrease to \$2,627 during the third fiscal quarter 2012 in comparison with a net loss attributable to Caspian Services, Inc. of \$3,458 during the comparable prior year period.

#### Vessel Operations

Third fiscal quarter 2012 revenue from vessel operations of \$5,205 was 34% lower than the comparable period of the prior year. The completion of most projects with Saipem during the beginning of the first fiscal quarter of the current fiscal year resulted in lower vessel utilization rates in comparison with the third fiscal quarter 2011. This also resulted in lower cash and trade accounts receivables attributable to vessel operations and a corresponding reduction in vessel operations assets. With the completion of most of our projects with Saipem we expect vessel revenues will continue to be lower and we do not expect significant growth in demand for our vessels during the current fiscal year or the next fiscal year in the Kazakhstan sector of the Caspian Sea. Therefore, we are investigating opportunities to utilize our vessel fleet outside of Kazakhstan.

During the three months ended June 30, 2012 vessel operating costs of \$2,548 were 49% lower than during the three months ended June 30, 2011 which resulted in improved operating margins from 37% during the third fiscal quarter 2011 to 51% during the third fiscal quarter 2012. This improvement was mostly attributable to a decrease in the vessel charter costs we were paying to Actamarine to hire its vessels as we no longer hire most of the Actamarine vessels previously used in our fleet. Those chartered vessels generally provided lower margins than our own vessels.

Increased operating margin meant our net income from vessel operations in the third fiscal quarter 2012 increased to \$702, compared to the income of \$286 in the third fiscal quarter of 2011. We expect decreased fleet activity throughout fiscal 2012 when compared to fiscal 2011 and therefore expect our results of vessel operations will correspondingly be worse in fiscal 2012 than in fiscal 2011.

#### Geophysical Services

During the third fiscal quarter 2011, our geophysical service revenues of \$143 were extremely sluggish, and we were able to increase it to \$2,393 during the third fiscal 2012. Given current expectations, we do not believe the increase in revenue experienced in the third fiscal quarter 2012 reflects a trend toward improving geophysical services revenue in upcoming quarters so much as it reflects a particularly sluggish third fiscal quarter 2011.

As a result of the increase in geophysical services provided, our operating costs increased by \$1,364. The major reason for that increase is the fact that we had to pay vacation allowance to dismissed production personnel and we could not significantly reduce our maintenance personnel during the third fiscal quarter 2011. Due to that fact, we realized a lower net loss from geophysical operations of \$1,412 during the third fiscal quarter 2012 compared to net loss of \$1,657 in the third fiscal quarter 2011.



We anticipate results of our geophysical services operations will be worse throughout the remainder of fiscal 2012 as compared to fiscal 2011 as the local market remains depressed by the difficult local credit market.

#### Marine Base Services

Our marine base services revenues during the third fiscal quarter 2012 were insufficient to cover our fixed costs, including depreciation. Additionally, interest expense of \$498 was accrued to reflect our liabilities on the EBRD loan and the potential accelerated put option. During the third fiscal quarter 2012 we realized a marine base services loss of \$1,162 compared to the loss of \$1,845 during the third fiscal quarter 2011.

Although we have been able to enter into agreements with some customers to use our base's services, we do not expect significant demand for the marine base until Kashagan field development and construction activity increases, which is currently anticipated to start in 2018 or 2019. Until activity in the Caspian Sea region increases, we do not expect the marine base to be able to service its current debt obligations or to operate profitably.

#### Corporate Administration

During the third fiscal quarter 2012 net loss from corporate administration was \$755 compared to \$242 during the third fiscal quarter 2011.

#### General and Administrative Expenses

During the third fiscal quarter 2012 general and administrative expenses of \$2,997 were in line with third fiscal quarter 2011 expenses. We anticipate general and administrative expenses to be in line with those realized in fiscal 2011 in the remaining upcoming quarter of fiscal 2012.

#### Depreciation

Depreciation expense of \$1,773 charged during the third fiscal quarter 2012 was in line with the depreciation expense charged in the third fiscal quarter of 2011.

#### Exchange Loss

During the third fiscal quarter 2012 we realized an exchange loss of \$144 compared to exchange income of \$456 during the third fiscal 2011. This was caused by significant USD and Euro fluctuations during our third fiscal quarter 2012. It is our policy to try and match Euro costs with Euro income and we were able to reduce some of the loss as Euro costs for vessel rental were also lower. It is not our business to speculate on currency movements and we have not historically engaged in currency hedging.

### Interest Expense

Interest expense of \$1,865 was 7% higher during the three months ended June 30, 2012 than for the same period ended June 30, 2011. This increase was the result of restructuring a portion of our outstanding loans.

### Net Other Expenses

Net other expenses increased 57% to \$1,913 during the third fiscal quarter 2012. This was mostly due to increased foreign exchange loss mentioned above.

### Benefit from (Provision for) Income Tax

During the three months ended June 30, 2012 we had a benefit from income tax of \$458 compared to a benefit from income tax of \$198 during the three months ended June 30, 2011. This difference was caused by TatArka and CSG LLP recognizing significant taxable losses during the three months ended June 30, 2012, while we had taxable income during the three months ended June 30, 2011. Each entity is taxed independently in Kazakhstan. Consistent with our expectations of lower revenues and net losses in the upcoming quarter, we anticipate we will continue to realize a benefit from income tax in the fourth fiscal quarter 2012.

### Net Loss Attributable to Caspian Services, Inc.

As a result of the aforementioned factors, during our third fiscal quarter 2012 we realized a net loss attributable to Caspian Services, Inc. of \$2,627 or \$0.06 per share on a basic and diluted basis. By comparison, during the third fiscal quarter 2011 we realized a net loss attributable to Caspian Services, Inc. of \$3,458 or \$0.07 per share on a basic and diluted basis.

### Nine months ended June 30, 2012 compared to the nine months ended June 30, 2011

Total revenue during the nine months ended June 30, 2012 was \$20,443 compared to \$34,494 during the nine months ended June 30, 2011, a decrease of 41%. Vessel revenues were down 41% as we generally completed our major contract with Saipem – during the nine months ended June 30, 2012 we had, on average, only two vessels under charter to Saipem vs. eight vessels during the nine months ended June 30, 2011. Geophysical revenues were down by 43% as the difficult credit situation in Kazakhstan continues to inhibit seismic financing.

Although, we were able to reduce our operating and administrative costs, our net loss attributable to Caspian Services, Inc. still increased to \$10,365 during the nine months ended June 30, 2012 compared to last year's net loss attributable to Caspian Services, Inc. of \$6,031.

### Vessel Operations

During the nine months ended June 30, 2012 revenue from vessel operations of \$13,674 was 41% lower than during the same period of the previous year. The completion of most projects with Saipem during the first fiscal quarter 2012 resulted in lower vessel utilization rates in comparison with the comparative period. With the completion of most of our projects with Saipem, we expect vessel revenues will continue to be lower and we do not expect significant growth in demand for our vessels during fiscal 2012 in the Kazakhstan sector of the Caspian Sea.

During the nine months ended June 30, 2012 vessel operating costs of \$7,806 were 43% lower than during the nine months ended June 30, 2011 in line with the reduction in vessel revenues. Decreased activity meant our loss from vessel operations during the nine months ended June 30, 2012 was \$682 compared to income of \$2,854 during the nine months ended June 30, 2011.

### Geophysical Services

As discussed above, seismic operations revenue was in line with our expectations of a sluggish market, and was 43% lower compared to the same period last year. Both the volume of work performed and rates charged to customers decreased significantly.

We have significantly reduced our variable operating and payroll costs as a result of the slowdown in our operating activity. Compared to the same period last year, cost of geophysical services was 10% lower. However, fuel and material prices increased significantly which limited our ability to reduce our costs in line with the reduction in revenue. As a result, the net loss attributable to Caspian Services, Inc. from geophysical operations was \$3,418 during the nine months ended June 30, 2012 compared to net loss attributable to Caspian Services, Inc. of \$446 during the nine months ended June 30, 2011.

### Marine Base Services

Our marine base services revenues during the nine months ended June 30, 2012 were insufficient to cover our fixed costs, including depreciation. Additionally, interest expense of \$1,501 was accrued to reflect our liabilities on the EBRD loan and the potential accelerated put option. During the nine months ended June 30, 2012 we realized a marine base services loss of \$4,578 compared to a loss of \$6,130 during the nine months ended June 30, 2011. This reduction in loss was the result of an impairment of Bauta's assets of \$1,042 recognized during the nine months ended June 30, 2011.

#### Corporate Administration

During the nine months ended June 30, 2012, net loss from corporate administration was \$1,687 compared to \$2,309 during the nine months ended June 30, 2011. Most of this decrease was attributable to decreased interest costs in connection with the restructuring of a portion of our outstanding loans.

#### General and Administrative Expenses

General and administrative expenses decreased 5% to \$7,919 during the nine months ended June 30, 2012. This decrease was mostly attributable to marine base property tax expenses of \$243, which were incurred during nine months ended June 30, 2011. This tax expense was a one-time expense and no such expense was incurred in the current fiscal year, due to tax exemption effective since January 1, 2011 under agreement with the Investment Committee.

#### Depreciation

Depreciation expense of \$5,525 charged during the nine months ended June 30, 2012 was 3% lower than the comparative period. This decrease was caused by the fact that a number of our properties were fully depreciated in fiscal 2012.

#### Interest Expense

Interest expense of \$5,228 was 12% lower during the nine months ended June 30, 2012 than during the nine months ended June 30, 2011. This decrease was the result of restructuring a portion of our outstanding loans.

#### Exchange Loss

During the nine months ended June 30, 2012 we realized an exchange loss of \$553 compared to an exchange income of \$637 during the same period of 2011. This was caused mainly by a decline in the value of the Euro during the nine months ended June 30, 2012, while during the comparative period of 2011 the Euro was more stable.

#### Net Other Expenses

Net other expenses increased 9% to \$5,535 during the nine months ended June 30, 2012. This increase was mostly due to the increase in exchange loss of \$1,190, which was partially offset by \$723 reduction in interest expense.

#### Benefit from (provision for) income tax

During the nine months ended June 30, 2012 we recognized a benefit from income taxes of \$739 compared to a provision for income taxes of \$1,159 during the nine months ended June 30, 2011. This difference was caused by the fact that significant taxable losses were recognized during the nine months ended June 30, 2012 by TatArka and CSG LLP while we had taxable income during the nine months ended June 30, 2011. Each entity is taxed separately in Kazakhstan.

#### Net Loss Attributable to Caspian Services, Inc.

As a result of the aforementioned factors, during the nine months ended June 30, 2012 net loss attributable to Caspian Services, Inc. increased 72% to \$10,365 or \$0.22 per share on a basic and diluted basis. By comparison, during the nine months ended June 30, 2011 we realized a net loss attributable to Caspian Services, Inc. of \$6,031 or \$0.12 per share on a basic and diluted basis.

#### Liquidity and Capital Resources

At June 30, 2012 we had cash on hand of \$2,897 compared to cash on hand of \$6,136 at September 30, 2011. At June 30, 2012 total current liabilities exceeded total current assets by \$56,886. This was mainly due to the EBRD loan and put option and the restructured loans being classified as current liabilities. We also have certain obligations under the EBRD financing agreements to assist Balykshi with its working capital needs and to complete dredging works which are estimated around \$3,000, of which we have already paid approximately \$1,000 as an advance. As discussed in more detail under the heading "Off-Balance Sheet Financing Arrangements" we may also be required to guarantee certain repayment obligations of Balykshi in connection with a loan made to MOBY.

As discussed above, under the terms of the EBRD Loan Agreement, as amended, the first two semi-annual repayment installments under the EBRD loan were due on November 20, 2011 and May 20, 2012. Those payments were not made, which constitutes an event of default under the EBRD Loan Agreement and may constitute a default under the Put Option Agreement. We are engaged in ongoing negotiations with EBRD about the possibility of restructuring our obligations to them. In connection with these discussions, we are investigating a number of potential solutions, including the availability of other funding sources to refinance our debt obligations, restructuring the repayment terms and obligations under the existing financing agreements, and the sale of Company assets and subsidiaries to generate funds to satisfy our obligations. At this time, we have not reached agreement with EBRD on any potential restructuring and there is no guarantee that we will be able to do so. As of the date of this quarterly report on Form 10-Q, EBRD has not sought to accelerate its loan or put option, but there is no guarantee EBRD will continue to forbear from so doing.

Should EBRD accelerate its loan or its put option, we would have insufficient funds to satisfy those obligations individually or collectively. If we are unable to satisfy those obligations, EBRD could seek any legal remedy available to it to obtain repayment, including forcing the Company into bankruptcy, or foreclosing on the loan collateral, which includes the marine base and other assets and bank accounts of Balykshi and CRE.

In addition to restructuring our obligations to EBRD, we hope to finalize the restructuring of our obligations to the Investor and to close the Loan Restructuring Agreement, including securing the restructured loans through the granting of first position security interests to the Investor in all or substantially all, (as allowed by applicable law), of our assets that are not currently pledged to EBRD and meeting the other closing conditions as more fully described in the Loan Restructuring Agreement.

For reasons detailed above, our operating revenues continue to fall. While we have made great efforts to correspondingly reduce our operating expenses, we continue to generate net losses. As noted above, we do not expect revenues from operations in the North Caspian Sea to improve significantly until the second phase of the Kashagan development ramps up, which at this time is projected to occur in 2018 or 2019. Unless we are able to exploit new markets outside of Kazakhstan for our services, there is no guarantee we will be able to continue to sustain net losses until that time.

Our ability to continue as a going concern is dependent upon, among other things, our ability to successfully restructure the EBRD financing agreements, complete the loan restructuring with the Investor and close the Loan Restructuring Agreement, increase our revenues and improve our operating results to a level that will allow us to service our debts or to attract a significant equity investment into the Company. Uncertainty as to the outcome of each of these events raises substantial doubt about our ability to continue as a going concern.

#### Cash Flows

We typically realize decreasing cash flows during our first fiscal quarter and limited cash flow during our second fiscal quarter as weather conditions in the North Caspian Sea dictate when oil and gas exploration and development work can be performed. Usually, the work season commences in late March or early April and continues until the Caspian Sea ices over in November. As a result, other than TatArka, which can continue to provide some onshore geophysical services between November and March and the receipt of winter standby rates on vessels, we generate very little revenue from November to March each year.

The following table provides an overview of our cash flow during the nine months ended June 30, 2012 and 2011.

	Period ended June 30,	
	2012	2011
Net cash provided by (used in) operating activities	\$ (176)	\$ 5,226
Net cash used in investing activities	(827)	(2,289)
Net cash used in financing activities	(2,000)	(734)
Effect of exchange rate changes on cash	(236)	893
Net Change in Cash	\$ (3,239)	\$ 3,096

Net cash flow from operations for the nine months ended June 30, 2012 was negative. This negative cash flow included, among other things, cash outflow to our vendors of \$2,225, advances paid of \$910, taxes payable of \$972 and prepaid taxes of \$486. This outflow was partially off-set by cash inflow from our customers of \$4,265.

Net cash used in investing activities for the nine months ended June 30, 2012 represents payments for geophysical machinery and equipment.

Net cash used in financing activities for the nine months ended June 30, 2012 represents the repayment to the Investor of part of the restructured loan.

#### Summary of Material Contractual Commitments

Contractual Commitments	Payment Period				
	Total	Less than 1 Year	1-3 Years	3-5 Years	After 5 years
Loans from an individual	\$ 37,500	\$ 37,500	\$ -	\$ -	\$ -
Loans from EBRD	20,974	20,974	-	-	-
Accelerated put option liability	17,318	17,318	-	-	-
Operating leases - vessels	1,252	1,252	-	-	-
Operating leases - other than vessels	137	137	-	-	-
Purchase commitments	1,682	1,682	-	-	-
Total	\$ 78,863	\$ 78,863	\$ -	\$ -	\$ -

#### Off-Balance Sheet Financing Arrangements

In January 2008 Balykshi, Kyran Holdings Limited and JSC “KazMorTransFlot” formed the MOBY joint venture, to operate a boat repair and drydocking services yard located at our marine base. Balykshi owns a 20% interest in MOBY. In August 2008 MOBY entered into a Loan Agreement with EBRD. The Loan Agreement provided that EBRD would loan MOBY \$10,300 (the “MOBY Loan”).

In June 2009 in connection with the Loan Agreement, EBRD required certain parties, including the Company, as the parent company of Balykshi, to execute a Deed of Guarantee and Indemnity (the “Guarantee”), which guarantees repayment of the MOBY Loan. The MOBY Loan funded and we became liable for the obligations under the Guarantee as of September 3, 2009. The Guarantee constitutes a direct financial obligation of the Company.

Pursuant to and in accordance with the Guarantee, we have agreed to guarantee payment to EBRD, on demand, all monies and liabilities which have been advanced or which shall become due, owing or incurred by MOBY to or in favor of EBRD when such shall become due. Our guarantee obligation is limited, however, to the "Caspian Pro-rata Percentage." The Caspian Pro-rata Percentage is an amount equal to our percentage ownership of Balykshi at any time multiplied by Balykshi's percentage ownership of MOBY, expressed as a percentage. Currently, we own a 78% interest in Balykshi and Balykshi owns a 20% interest in MOBY. Therefore, the Caspian Pro-rata Percentage is currently 15.6%, or \$1,866, including interest, at June 30, 2012.

We also agreed as a separate and independent obligation and liability to indemnify EBRD on demand against all losses, costs and expenses suffered or incurred by EBRD should any of the financing agreements between EBRD and MOBY be or become unlawful, void, voidable or unenforceable, ineffective or otherwise not recoverable on the basis of the guarantee, provided again our obligation is limited to the Caspian Pro-rata Percentage of such losses, costs and expenses.

As a guarantor, we agreed to advance to MOBY at any time on demand of EBRD any additional amount required by MOBY to enable it to comply with its obligations under the financing agreements and to carry out the project. Our obligation in this context is limited to 20% of the total amount.

Pursuant to and in accordance with the Guarantee, EBRD is not obliged before taking steps to enforce any of its rights and remedies under the Guarantee to make any demand or seek to enforce any right against MOBY or any other person, to obtain judgment in any court against MOBY or any other person or to file any claim in bankruptcy, liquidation or similar proceedings.

The Guarantee provides that each guarantor agrees to pay interest to EBRD on all unpaid sums demanded under the Guarantee at a rate of LIBOR plus 5.6%. The Guarantee also provides that each guarantor shall, on demand and on a full indemnity basis, pay to EBRD, the amount of all costs and expenses, including legal and out-of-pocket expenses and any VAT on such costs and expenses which EBRD incurs in connection with: a) the preparation, negotiation, execution and delivery of the Guarantee; b) any amendment, variation, supplement, waiver or consent under or in connection with the Guarantee; c) any discharge or release of the Guarantee; d) the preservation or exercise of any rights in connection with the Guarantee; and e) any stamping or registration of the Guarantee; provided that our obligation in this context is limited to the Caspian Pro-rata Percentage.

As of September 30, 2011 and June 30, 2012 MOBY was in violation of certain financial covenants under the MOBY Loan. To date, EBRD has not sought to accelerate repayment of the MOBY Loan; however, there is no guarantee EBRD will continue to forbear from accelerating the MOBY Loan in the future.

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

As a smaller reporting company, as defined in Rule 12b-2 promulgated under the Exchange Act and in Item 10(f)(1) of Regulation S-K, we are electing scaled disclosure reporting obligations and therefore are not required to provide the information requested by this Item.



#### Item 4. Controls and Procedures

##### Evaluation of Disclosure Controls and Procedures

Our management, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) or 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”)), as of the end of the period covered by this quarterly report on Form 10-Q. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that as of the end of the period covered by this quarterly report on Form 10-Q, our disclosure controls and procedures were effective in (1) recording, processing, summarizing and reporting, information required to be disclosed by us in the reports that we file or submit under the Exchange Act within the time periods specified by the SEC’s rules and forms and (2) ensuring that information disclosed by us in such reports is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

##### Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting during the quarter ended June 30, 2012 that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## PART II - OTHER INFORMATION

#### Item 1A. Risk Factors

We believe there are no additions to the risk factors disclosed in our annual report on Form 10-K for the year ended September 30, 2011 filed on January 13, 2012 and our quarterly report on Form 10-Q for the quarter ended December 31, 2011 filed on February 21, 2012.

#### Item 3. Defaults Upon Senior Securities

See Note 1 – Business Condition to the condensed consolidated financial statements included in this quarterly report on Form 10-Q.

#### Item 4. Mine Safety Disclosures

Not applicable.

## Item 6. Exhibits

Exhibits. The following exhibits are included as part of this report:

Exhibit No.	Description of Exhibit
Exhibit 31.1	Certification of Principal Executive Officer Pursuant to Rule 13a-14(a)*
Exhibit 31.2	Certification of Principal Financial Officer Pursuant to Rule 13a-14(a)*
Exhibit 32.1	Certification of Principal Executive Officer Pursuant to 18 U.S.C. Section 1350*
Exhibit 32.2	Certification of Principal Financial Officer Pursuant to 18 U.S.C. Section 1350*
Exhibit 101.INS	XBRL Instance Document**
Exhibit 101.SCH	XBRL Taxonomy Extension Schema Document**
Exhibit 101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document**
Exhibit 101.DEF	XBRL Taxonomy Definition Linkbase Document**
Exhibit 101.LAB	XBRL Taxonomy Extension Label Linkbase Document**
Exhibit 101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document**

\* Filed herewith

\*\* To be filed by amendment

SIGNATURES

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

CASPIAN SERVICES, INC.

Date: August 13, 2012

By: /s/ Alexey Kotov  
Alexey Kotov  
Chief Executive Officer

Date: August 13, 2012

By: /s/ Andrey Yuryev  
Andrey Yuryev  
Interim Chief Financial Officer