

SPO Global Inc  
Form 10-Q  
August 14, 2014

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**WASHINGTON, D.C. 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 June 30, 2014 or

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from \_\_\_\_\_ to \_\_\_\_\_

*COMMISSION FILE NUMBER: 0-11772*

**SPO GLOBAL INC.**

(Exact name of registrant specified in its charter)

Delaware  
(State or other jurisdiction of incorporation or  
organization)

25-1411971  
(I.R.S. Employer Identification No.)

**3 Gavish Street, POB 2454, Kfar Saba, Israel**

(Address of principal executive offices, including zip code)

972-9-966-2520

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) 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

(Do not check if a smaller reporting company)

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

As of August 14, 2014, SPO Global Inc. had outstanding 6,418,368 shares of common stock, par value \$0.01 per share.

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## **PART I - FINANCIAL INFORMATION**

### **FORWARD LOOKING STATEMENTS**

THE FOLLOWING DISCUSSION SHOULD BE READ IN CONJUNCTION WITH THE FINANCIAL STATEMENTS AND RELATED NOTES CONTAINED ELSEWHERE IN THIS FORM 10-Q. CERTAIN STATEMENTS MADE IN THIS DISCUSSION ARE "FORWARD-LOOKING STATEMENTS" WITHIN THE MEANING OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995. FORWARD-LOOKING STATEMENTS CAN BE IDENTIFIED BY TERMINOLOGY SUCH AS "MAY," "WILL," "SHOULD," "EXPECTS," "INTENDS," "ANTICIPATES," "BELIEVES," "ESTIMATES," "PREDICTS," OR "CONTINUE" OR THE NEGATIVE OF THESE TERMS OR OTHER COMPARABLE TERMINOLOGY AND INCLUDE, WITHOUT LIMITATION, STATEMENTS BELOW REGARDING: THE COMPANY'S ABILITY TO CONTINUE AS A GOING CONCERN; THE COMPANY'S BUSINESS PLANS; EXPECTATIONS AS TO PRODUCT PERFORMANCE; EXPECTATIONS AS TO MARKET ACCEPTANCE OF THE COMPANY'S PRODUCT LINES; AND BELIEF AS TO THE SUFFICIENCY OF CASH RESERVES. BECAUSE FORWARD-LOOKING STATEMENTS INVOLVE RISKS AND UNCERTAINTIES, THERE ARE IMPORTANT FACTORS THAT COULD CAUSE ACTUAL RESULTS TO DIFFER MATERIALLY FROM THOSE EXPRESSED OR IMPLIED BY THESE FORWARD-LOOKING STATEMENTS. THESE FACTORS INCLUDE, BUT ARE NOT LIMITED TO, SUFFICIENCY OF CASH RESERVES, THE COMPANY'S ABILITY TO OBTAIN ADDITIONAL NEEDED FINANCING; GOING CONCERN QUALIFICATIONS; ORDER BACKLOG RESULTING IN REVENUES; MARKET ACCEPTANCE OF THE COMPANY'S PRODUCT LINES; THE COMPETITIVE ENVIRONMENT GENERALLY AND IN THE COMPANY'S SPECIFIC MARKET AREAS; CHANGES IN TECHNOLOGY; INFLATION; ECONOMIC CONDITIONS IN GENERAL AND IN THE COMPANY'S SPECIFIC MARKET AREAS; DEMOGRAPHIC CHANGES; CHANGES IN FEDERAL, STATE AND /OR LOCAL GOVERNMENT LAW AND REGULATIONS AFFECTING THE TECHNOLOGY; CHANGES IN OPERATING STRATEGY OR DEVELOPMENT PLANS; AND THE ABILITY TO ATTRACT AND RETAIN QUALIFIED PERSONNEL. ALTHOUGH THE COMPANY BELIEVES THAT EXPECTATIONS REFLECTED IN THE FORWARD-LOOKING STATEMENTS ARE REASONABLE, IT CANNOT GUARANTEE FUTURE RESULTS, PERFORMANCE OR ACHIEVEMENTS. MOREOVER, NEITHER THE COMPANY NOR ANY OTHER PERSON ASSUMES RESPONSIBILITY FOR THE ACCURACY AND COMPLETENESS OF THESE FORWARD-LOOKING STATEMENTS. THE COMPANY IS UNDER NO DUTY TO UPDATE ANY FORWARD-LOOKING STATEMENTS AFTER THE DATE OF THIS REPORT TO CONFORM SUCH STATEMENTS TO ACTUAL RESULTS.

**SPO GLOBAL INC.****CONDENSED INTERIM CONSOLIDATED BALANCE SHEETS****U.S. dollars in thousands (except share and per share data)**

	June 30, 2014 (Unaudited)	December 31, 2013	
<b>ASSETS</b>			
<b>CURRENT ASSETS</b>			
Cash and cash equivalents	\$137	\$286	
Prepaid expenses and other accounts receivable	213	61	
	350	347	
<b>LONG TERM INVESTMENTS</b>			
Severance pay fund	172	168	
<b>PROPERTY AND EQUIPMENT, NET</b>	<b>20</b>	<b>22</b>	
Total net assets	\$542	\$537	
<b>LIABILITIES AND STOCKHOLDERS' DEFICIENCY</b>			
<b>Current Liabilities</b>			
Short-term loans	\$1,366	\$700	
Trade payables	37	38	
Employees and Payroll accruals	869	774	
Accrued expenses and other liabilities	543	531	
	2,815	2,043	
<b>Long-Term Liabilities</b>			
Long-Term Loans	464	882	
Accrued severance pay	283	271	
	747	1,153	
<b>COMMITMENTS AND CONTINGENT LIABILITIES</b>			
<b>STOCKHOLDERS' DEFICIENCY</b>			
Preferred stock \$0.01 par value			
Authorized - 2,000,000 shares, issued and outstanding - 100 Series A shares at June 30, 2014 and December 31, 2013, respectively	—	(*) —	(*)
Common stock \$0.01 par value-			

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Authorized - 100,000,000 shares, issued and outstanding - 6,127,599 and 5,305,608 shares as at June 30, 2014 and December 31, 2013, respectively (**)	62	53
Additional paid-in capital	18,975	18,971
Accumulated deficit	(22,057)	(21,683 )
	(3,020 )	(2,659 )
Total liabilities and stockholders' deficiency	\$ 542	\$ 537

(\*) Less than \$1

(\*\*) The number of shares have been adjusted retroactively to reflect the one for twenty reverse split of our common stock dated October 7, 2013.

The accompanying notes to these financial statements are an integral part thereof.

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**SPO GLOBAL INC.****CONDENSED INTERIM CONSOLIDATED STATEMENTS OF OPERATIONS**

U.S. dollars in thousands (except share and per share data)

	Three months ended June 30, 2014 (Unaudited)		Six months ended June 30, 2014 (Unaudited)	
	2013 (Unaudited)	2014 (Unaudited)	2013 (Unaudited)	2014 (Unaudited)
Revenues	\$22	\$100	\$50	\$249
Cost of revenues	0	85	2	210
Gross profit	22	15	48	39
Operating expenses				
Research and development	—	—	6	—
Selling and marketing	16	17	32	17
General and administrative	115	97	236	213
Total operating expenses	131	114	274	230
Operating loss	(109 )	(99 )	(226 )	(191 )
Financial expense, net	(92 )	(83 )	(148 )	(138 )
Net Loss for the period	\$(201 )	\$(182 )	\$(374 )	\$(329 )
Basic and diluted loss per share (*)	\$(0.03 )	\$(0.05 )	\$(0.07 )	\$(0.10 )
Weighted average number of shares outstanding used in computation of basic loss per share (*)	5,931,176	3,543,055	5,726,514	3,271,111

(\*) The number of shares have been adjusted retroactively to reflect the one for twenty reverse split of our common stock dated October 7, 2013.

The accompanying notes to these financial statements are an integral part thereof.

**SPO GLOBAL INC.****CONDENSED INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS****U.S. dollars in thousands (except share and per share data)**

	Six months ended June 30, 2014      2013 (Unaudited)(Unaudited)	
<b>Cash Flows from Operating Activities</b>		
Net Loss for the period	\$ (374 )	\$ (329 )
Adjustments to reconcile loss to net cash used in operating activities:		
Depreciation	2	—
Non-cash expenses related to convertible debt	28	61
Non-cash (income) related to warrants to issue shares	—	(18 )
Changes in assets and liabilities:		
Increase in accrued interest payable on loans	58	31
(Increase) in accounts receivables	—	(1 )
(Increase) in prepaid expenses and other receivables	(152 )	(15 )
(Decrease) Increase in trade payables	(1 )	54
Increase in accrued severance pay, net	8	10
Increase in accrued expenses and other liabilities	107	109
Net cash used in operating activities	(324 )	(98 )
<b>Cash Flows from Financing Activities</b>		
Proceeds from sale of shares and warrants, net of issuance costs	—	227
Payments of loans	—	(13 )
Proceeds from loan	175	104
Net cash provided by financing activities	175	318
Increase (decrease) in cash and cash equivalents	(149 )	220
Cash and cash equivalents at the beginning of the period	286	24
Cash and cash equivalents at the end of the period	\$ 137	\$ 244
<b>Non cash transactions</b>		
Conversion of convertible debt to shares	\$ 13	\$ 67
Exercise of warrants in consideration of concession of debt	\$ —	\$ 24
Discount on convertible notes recognized to beneficial conversion feature	\$ —	\$ 80
<b>Supplemental Disclosure of Cash Flow Information:</b>		
Cash paid during the period for:		
Interest	\$ 59	\$ 34



The accompanying notes to these financial statements are an integral part thereof.

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**SPO GLOBAL INC.**

**NOTES TO THE CONDENSED INTERIM FINANCIAL STATEMENTS**

**U.S. dollars in thousands (except share data)**

**NOTE 1 - GENERAL**

SPO Global Inc. (hereinafter referred to as "SPO" or the "Company") is engaged in the design, development and marketing of non-invasive pulse oximetry technologies to measure blood oxygen saturation and heart rate. The applications are marketed in the following sectors; professional medical care, homecare, sports, safety and search & rescue.

The Company was originally incorporated under the laws of the State of Delaware in September 1981 under the name "Applied DNA Systems, Inc." On November 16, 1994, the Company changed its name to "Nu-Tech Bio-Med, Inc." On December 23, 1998, the Company changed its name to "United Diagnostic, Inc." Effective April 21, 2005, the Company acquired (the "Acquisition Transaction") 100% of the outstanding capital stock of SPO Medical Equipment Ltd., a company incorporated under the laws of the State of Israel ("SPO Ltd."), pursuant to a Capital Stock Exchange Agreement dated as of February 28, 2005 between the Company, SPO Ltd. and the shareholders of SPO Ltd., as amended and restated on April 21, 2005 (the "Exchange Agreement"). In exchange for the outstanding capital stock of SPO Ltd., the Company issued to the former shareholders of SPO Ltd. a total of 5,769,106 shares of the Company's common stock, par value \$0.01 per share ("Common Stock"), representing approximately 90% of the Common Stock then issued and outstanding after giving effect to the Acquisition Transaction. As a result of the Acquisition Transaction, SPO Ltd. became a wholly owned subsidiary of the Company as of April 21, 2005 and, subsequent to the Acquisition Transaction, the Company changed its name to "SPO Medical Inc." Upon consummation of the Acquisition Transaction, the Company effectuated a forward subdivision of the Company's Common Stock issued and outstanding on a 2.65285:1 basis.

The merger between UNDI and the SPO Ltd was accounted for as a reverse merger. As the shareholders of SPO Ltd received the largest ownership interest in the Company, SPO Ltd was determined to be the "accounting acquirer" in the reverse acquisition. As a result, the historical financial statements of the Company were replaced with the historical financial statements of the SPO Ltd.

The Company and its subsidiary, SPO Ltd., are collectively referred to as the "Company". In January 2010, the Company restructured its operations to focus primarily on licensing its core technology for non-medical market applications. Following the restructure, the Company ceased its previous operations associated with the distribution of the PulseOx line in the medical field. In February 2011, the Company transferred research and development activities to subcontractors, thereby ceasing all internal research and development activities.

Effective October 4, 2013, the Company changed its corporate name to “SPO Global Inc.”.

The Company implemented a 1-for-20 reverse stock split on October 7, 2013. All share and per share amounts and calculations in these financial statements have been retroactively adjusted to reflect the effects of the reverse stock split.

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**NOTE 2 - GOING CONCERN**

As reflected in the accompanying financial statements, the Company's operations for the six months ended June 30, 2014, resulted in a net loss of \$374, and the Company's balance sheet reflects a net stockholders' deficit of \$3,020. The Company's ability to continue operating as a "going concern" is dependent on its ability to raise sufficient additional working capital. These matters raise substantial doubt about the Company's ability to continue as a going concern. The financial statements have been prepared on a going concern basis, which contemplates realization of assets and liquidation of liabilities in the ordinary course of business. As disclosed in previous filings with the Securities and Exchange Commission, management has been attempting to raise additional cash from current and potential stockholders and plans to continue these efforts. There can be no assurance that this capital will be available and if it is not, the Company may be forced to substantially curtail or cease operations and development expenditures. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

**NOTE 3 - SIGNIFICANT ACCOUNTING POLICIES**

The accompanying un-audited condensed consolidated interim financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with Rule 8-03 of Regulation S-X. These financial statements reflect all adjustments, consisting of normal recurring adjustments and accruals, which are, in the opinion of management, necessary for a fair presentation of the financial position of the Company as of June 30, 2014 and the results of operations and cash flows for the interim periods indicated in conformity with generally accepted accounting principles applicable to interim periods. Accordingly, certain information and footnote disclosures normally included in annual financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted. Operating results for the six months ended June 30, 2014, are not necessarily indicative of the results that may be expected for the year ended December 31, 2014.

Certain prior years' amounts have been reclassified in conformity with current year's financial statements.

**NOTE 4 - PROPERTY AND EQUIPMENT**

	June	December
	30,	31,
	2014	2013
Cost:		
Office furniture and equipment	\$ 5	\$ 5

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Automobile	\$ 24	\$ 24
Less accumulated depreciation:	\$ 9	\$ 7
Property and Equipment, net	\$ 20	\$ 22

Depreciation expense for the period ended June 30, 2014 amounted to \$2.

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**NOTE 5 - LOANS PAYABLE**

On April 12, 2013, the Company entered into a Convertible Note Agreement pursuant to which the Company received a loan in the principal amount of \$32.5 from an investor. The note was originally scheduled to mature on March 19, 2014. As of June 30, 2014, \$27 of the loan principal was converted into 1,008,095 shares of Common Stock and the remaining balance in the amount of \$5.5 was due and owing. The outstanding and unpaid principal amount continues to accrue interest at a per annum rate of 22%. The outstanding and unpaid principal together with the interest accrued continue to be convertible, at the election of the holder, into shares of the Company's Common Stock at a conversion rate equal to 55% of the average of the five lowest closing sale prices during the ten days preceding the conversion date.

On May 23, 2014, the Company entered into a loan agreement with investor pursuant to which the Company received a loan in the principal amount of \$175 to be used for order financing. The loan is interest-free. The principle amount of the loan with a \$10 fee is repayable by September 30, 2014 and may be pre-paid, at the option of the Company, without notice or penalty. If the loan is not repaid by the scheduled maturity date, the principle amount of the loan shall begin to accrue interest at a rate of 12% per annum from the maturity date until repayment in full.

**NOTE 6 - FINANCIAL INCOME (EXPENSE)**

Financial income (expense) is comprised of the following:

	<b>Six Months Ended June 30, 2014</b>	<b>Six Months Ended June 30, 2013</b>
Non-cash expenses related to convertible debt	\$ (28 )	\$ (61 )
Non-cash expenses related to warrants to issue shares	(1 )	18
Interest in respect of debt instruments and liabilities	(117 )	(65 )
Exchange rate differences caused by fluctuations in the exchange rate with the New Israeli Shekel ("NIS") on liabilities denominated in NIS held by the subsidiary	(2 )	(30 )
	<b>\$ (148 )</b>	<b>\$ (138 )</b>

**NOTE 7 - SUBSEQUENT EVENTS**

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On July 17, 2014, the Company entered into a loan agreement with an investor pursuant to which the Company received a loan in the principal amount of \$50 to be used for order financing. The loan is interest-free. The principle amount of the loan with a \$4 fee is repayable by November 30, 2014 and may be pre-paid, at the option of the Company, without notice or penalty. If the loan is not repaid by the maturity date, the interest with respect to the unpaid principle amount of the loan shall begin to accrue at a rate of 12% per annum from the maturity date until repayment in full.

On August 6, 2014, the Company issued 290,769 shares of its common stock upon conversion of convertible debt of approximately \$2.

On August 7, 2014, the Company entered into a loan agreement with an investor pursuant to which the Company received a loan in the principal amount of \$200 to be used for order financing. The loan is interest-free. The principle amount of the loan with a \$16 fee is repayable by November 30, 2014 and may be pre-paid, at the option of the Company, without notice or penalty. If the loan is not repaid by the maturity date, the interest with respect to the unpaid principle amount of the loan shall begin to accrue at a rate of 12% per annum from the maturity date until repayment in full.

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

THE FOLLOWING DISCUSSION SHOULD BE READ IN CONJUNCTION WITH OUR FINANCIAL STATEMENTS AND THE NOTES RELATED TO THOSE STATEMENTS. SOME OF OUR DISCUSSION IS FORWARD-LOOKING AND INVOLVES RISKS AND UNCERTAINTIES. FOR INFORMATION REGARDING RISK FACTORS THAT COULD HAVE A MATERIAL ADVERSE EFFECT ON OUR BUSINESS, REFER TO THE RISK FACTORS SECTION OF THE ANNUAL REPORT ON FORM 10-K FOR THE YEAR ENDED DECEMBER 31, 2013.

### **OVERVIEW**

SPO Global Inc. (“we” or the “Company”) is engaged in the design, development and marketing of non-invasive pulse oximetry technologies to measure blood oxygen saturation and heart rate. We have developed and patented proprietary technology that enables the measurement of heart rate and oxygen saturation levels in the blood, which is known as Reflectance Pulse Oximetry (RPO). Using RPO, a sensor can be positioned on various body parts, hence minimizing problems from motion artifacts and poor perfusion. The unique design features contribute to substantially lower power requirements and enhance wireless, stand-alone configurations facilitating expanded commercial possibilities. As of August 2014, we held 12 patents issued by the United States Patent and Trademark Office (“USPTO”) covering various aspects of our technologies. Our technologies are currently applied to products that are designed for use in the homecare, professional medical care, sports, safety and search and rescue markets.

We are primarily engaged in developing, manufacturing and licensing our technology to third parties for integration with products in the general wellness, recreational, baby monitoring and sports monitoring fields. We pursue joint ventures, OEM type arrangements, research and or subcontracting agreements relating to our oximetry technology with respect to the general wellness, recreational, baby monitoring and sports monitoring fields. Since August 2012, we have partnered with HoMedics LLC, a distributor and manufacturer of leading brands in an array of consumer health, wellness and electronic lifestyle categories throughout the Americas, Europe, the Asia-Pacific region, Africa and the Middle-East, for the distribution of a private labeled, over the counter pulse oximeter for non-medical consumer wellness applications.

We are currently focused on exploiting the sports and wellness markets by developing cutting edge products based on our proprietary technology.



The SPO sports watch has been designed to measure continuous heart-rate wirelessly, without the need to wear a conventional chest strap. This is a major and unique practical advantage over current products that we believe exist in the general leisure and wellness market. As importantly, the sports watch will be able to read the heart rate without the sports enthusiast ceasing his physical activity. This will be made possible through the use of SPO's patented reflectance technology. Subject to raising significant additional funds, of which no assurance can be provided, we anticipate that the product should become commercially available through an OEM arrangement with a strategic market partner during 2015.

In addition to the sports watch, we launched an innovative wellness watch that measures the number of activities and calories burned by an individual performs on a given day. The watch, designed for both children and adults, features a display function to continuously measure the number of daily activities against preset recommended goals. SPO has designed and patented the functionality of the watch to be an affordable, simple-to-use, fashion accessory to encourage users to increase their mobility and overall wellness and to wear it with pride.

In addition, we are developing an innovative home-baby monitoring device for continuous measurement of wellness information to the parent or caregiver, while the baby is sleeping. This parental reassurance tool gives the company a technological competitive edge in providing an innovative, high performance solution for a market application that is applicable to most family homes. Subject to raising significant additional funds, of which no assurance can be provided, we believe that the product could become commercially available through an OEM arrangement with a strategic market partner during 2015.

### **Current Operational Highlights**

We recorded revenues of \$556,000 for the year ended December 2013 and \$50,000 for the six months ended June 30, 2014. As of August 14, 2014, we had a backlog of approximately \$692,000, consisting of orders for additional units of our wellness product that we expect to deliver during 2014.

Since August 2012, we have partnered with HoMedics LLC, a distributor and manufacturer of leading brands in an array of consumer health, wellness and electronic lifestyle categories throughout the Americas, Europe, the Asia-Pacific region, Africa and the Middle-East, for the distribution of a private labeled, over the counter pulse oximeter for non-medical consumer wellness applications.

Revenues to date have resulted primarily from the initial shipments of a new consumer wellness product to mass-market retailers based in the United States. We have generated significant operating losses since inception and we have a limited operating history upon which an evaluation of our prospects can be made. Our prospects must therefore be evaluated in light of the problems, expenses, delays and complications associated with a development stage company.

However, we need to raise additional funds on an immediate basis in order to realize our business plan as well as pay outstanding loans in the approximate amount of \$1,830,000, of which \$1,366,000 is due or matures by June 30, 2015. In January 2010, we restructured our operations in an attempt to focus primarily on our core technology for non-medical market operations. As of August 14, 2014, we had two employees working on a full-time basis. In addition, all research and development activities are performed on a sub-contracted basis. If we are unable to raise capital on an immediate basis, it may be necessary for us to take further cost cutting measures to reduce our cash burn including laying-off additional personnel and/or cease operations entirely. No assurance can be given that we will be able to raise the needed capital. These conditions raise substantial doubt about our ability to continue as a going concern.

### **CRITICAL ACCOUNTING POLICIES**

The discussion and analysis of our financial condition and results of operations are based upon our unaudited consolidated financial statements, which have been prepared in accordance with generally accepted accounting principles in the United States. The preparation of these financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, we evaluate our estimates, including those related to revenue recognition, bad debts, intangible assets and income taxes. Our estimates are based on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. Actual results may differ from these estimates.

We have identified the accounting policies below as critical to our business operations and the understanding of our results of operations.

## **REVENUE RECOGNITION**

We generate revenues principally from product manufacturing. Revenues generated from product manufacturing are recognized when such products are shipped; subcontracted research and development services are recognized when such services are performed.

## **USE OF ESTIMATES**

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

## **RESULTS OF OPERATIONS**

### **COMPARISON OF THE THREE AND SIX MONTHS ENDED JUNE 30, 2014 AND THE THREE AND SIX MONTHS ENDED JUNE 30, 2013.**

**REVENUES.** Revenues for the three and six months ended June 30, 2014 were \$22,000 and \$50,000, respectively, as compared to \$100,000 and \$249,000, respectively for the corresponding periods in 2013. The decrease in revenues for the three and six months ended June 30, 2014 as compared to the corresponding periods in 2013 is attributable to a decline in deliverable purchase orders.

**COSTS OF REVENUES.** Costs of revenues include all costs related to subcontracted manufacturing and product delivery. Cost of Revenues for the three and six months ended June 30, 2014 were \$0 and \$2,000, respectively, as compared to \$85,000 and \$210,000, respectively for the corresponding periods in 2013. The decrease in cost of revenues for the three and six months ended June 30, 2014 as compared to the corresponding periods in 2013 is attributable to the manufacturing costs associated with product sales in the quarter.

**RESEARCH AND DEVELOPMENT EXPENSES, NET.** Research and development expenses, net, consist primarily of expenses incurred in the design, development and testing of our products. These expenses consist primarily of subcontractor services, contract design and testing services, supplies used and consulting fees paid to third parties. Research and development expenses were \$0 and \$6,000 for the three and six months ended June 30, 2014, respectively. No research and development expenses were recorded for the corresponding periods in 2013. The increase in research and development expenses for the six months ended June 30, 2014 as compared to the corresponding period in 2013 is primarily attributable to activities relating to new product development.

**SELLING AND MARKETING EXPENSES.** Selling and marketing expenses consist primarily of costs relating to compensation attributable to consultants for the provision of public relations, promotion and marketing services geared to the recreational sports and wellness markets. Selling and marketing expenses were \$16,000 and \$32,000, respectively, as compared to \$17,000 and \$17,000, respectively for the corresponding periods in 2013. The increase in selling and marketing expenses during the six months ended June 30, 2014 as compared to the corresponding period in 2013 is primarily attributable to activities relating to evaluating the potential of product sales in new territories.

**GENERAL AND ADMINISTRATIVE EXPENSES.** General and administrative expenses primarily consist of salaries and other related costs for personnel in executive and other administrative functions. Other significant costs include professional fees for legal and accounting services. General and administrative expenses for the three and six months ended June 30, 2014 were \$115,000 and \$236,000, respectively, as compared to \$97,000 and \$213,000, respectively, for the corresponding periods in 2013. The increase in general and administrative expenses during the three and six months ended June 30, 2014 as compared to the corresponding periods in 2013 is primarily attributable to increased professional fees and insurance expenses.

**FINANCIAL EXPENSE, NET.** Finance expense, net for the three and six months ended June 30, 2014 were \$92,000 and \$148,000, respectively, as compared to \$83,000 and \$138,000, respectively, for the corresponding periods in 2013. The increase in finance expenses during the three and six months ended June 30, 2014 as compared to the corresponding periods in 2013 is primarily attributable to the net effects of increased loans payable and variations of estimated fair values of warrants and conversion features.

**NET LOSS.** Net loss for the three and six months ended June 30, 2014 were \$201,000 and \$374,000, respectively, as compared to \$182,000 and \$329,000, respectively, for the corresponding periods in 2013. The increased net loss during the three and six months ended June 30, 2014 as compared to the corresponding periods in 2013 is primarily attributable to an increase in research and development, marketing, general and administrative expenses.

## **LIQUIDITY AND CAPITAL RESOURCES**

We need to raise additional funds in order to meet our on-going operating requirements, pay outstanding loans in the aggregate approximate amount of \$1,830,000 and to realize our restructured business plan. We believe that our currently existing cash resources are sufficient to satisfy our operating requirements through December 31, 2014. If we are unable to raise additional capital through a financial raise or revenues, it may be necessary for us to take further measures to reduce our cash burn including laying-off additional personnel, or ceasing operations entirely. No assurance can be given that we will be able to raise the needed capital. These conditions raise substantial doubt about our ability to continue as a going concern. Such “going concern” qualification may make it more difficult for us to raise funds if and when needed. In addition, any additional equity financings is likely to be dilutive to holders of our Common Stock and debt financing, if available, may require us to be bound by significant repayment obligations and covenants that restrict our operations.

As of June 30, 2014, we had \$136,528 in cash and cash equivalents available to us.

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We generated negative cash flow from operating activities of approximately \$324,000 during the six months ended June 30, 2014 compared to \$98,000 for the 2013 corresponding period.

To date, we have financed our operations primarily from debt financing and the sale of our securities. See Notes 5 and 9 in our consolidated financial statements accompanying our Annual Report on Form 10-K for the year ended December 31, 2013 filed on April 9, 2014 and Notes 5 and 7 in our consolidated financial statements accompanying this Quarterly Report on Form 10-Q. In May, July and August 2014, we borrowed, on a short-term basis, \$425,000 for working capital purposes to fund our backlog of purchase orders, of which \$175,000 is repayable by September 30, 2014 and the remaining \$250,000 by November 30, 2014.

#### **ITEM 4. CONTROLS AND PROCEDURES**

**EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES.** We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to management, including our Chief Executive Officer, as appropriate, to allow timely decisions regarding required disclosure based closely on the definition of "disclosure controls and procedures" in Rule 13a-14(c).

As of the end of the period covered by this report, we carried out an evaluation, under the supervision and with participation of management, including our Chief Executive Officer, who serves as our principal executive officer and principal financial and accounting officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based on the foregoing, our Chief Executive Officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report to provide reasonable assurance that material information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms.

Management is aware that there is a lack of segregation of duties due to the small number of employees dealing with general administrative and financial matters. However, at this time, management has decided that considering the employees involved, the control procedures in place, and the outsourcing of certain financial functions, the risks associated with such lack of segregation are low and the potential benefits of adding additional employees to clearly segregate duties do not justify the expenses associated with such increases. Management will periodically reevaluate this situation. If the volume of the business increases and sufficient capital is secured, it is our intention to increase staffing to mitigate the current lack of segregation of duties within the general administrative and financial functions.

A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of the inherent limitations in all control systems no evaluation of controls can provide absolute assurance that all control issues, if any, within a company have been detected. Such limitations include the fact that human judgment in decision-making can be faulty and that breakdowns in internal control can occur because of human failures, such as simple errors or mistakes or intentional circumvention of the established process.

**CHANGES IN INTERNAL CONTROLS OVER FINANCIAL REPORTING.** During the quarter ended June 30, 2014, there were no changes in our internal controls over financial reporting that have materially affected, or are reasonably likely to materially affect, these controls.



**PART II - OTHER INFORMATION**

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES.**

We first disclosed in the quarterly report on Form 10-Q for the three months ended March 31, 2008, that we had not repaid principal and accrued interest that became due during the quarterly period covered by such report. We disclosed in subsequent quarterly reports on Form 10-Q additional amounts that became due in ensuing quarterly periods and the results of our efforts to resolve these matters. As of June 30, 2014, principal and accrued interest in the aggregate amount of approximately \$620,000 continues to remain outstanding. We continue to hold discussions with certain of the holders of the outstanding debt in an attempt to resolve this matter; no assurance can be provided that we will be successful in concluding any mutually acceptable resolution of this matter.

**ITEM 6. EXHIBITS.**

- 3.1 Certificate of Amendment of the Amended and Restated Certificate of Incorporation.
- 31 Rule 13a - 14(a) Certification of Principal Executive Officer (and Principal Financial and Accounting Officer)
- 32 Section 1350 Certification of Principal Executive Officer (and Principal Financial and Accounting Officer)
- 101.INS XBRL Instance Document
- 101.SCH XBRL Taxonomy Extension Schema
- 101.CAL XBRL Taxonomy Extension Calculation Linkbase
- 101.DEF XBRL Taxonomy Extension Definition Linkbase
- 101.LAB XBRL Taxonomy Extension Label Linkbase
- 101.PRE XBRL Taxonomy Extension Presentation Linkbase

**SIGNATURES**

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

DATE: August 14, 2014 /s/ Michael Braunold

Michael Braunold

Chief Executive Officer (Principal Executive

Officer and Principal Financial and Accounting Officer) and Director

