

Fuse Science, Inc.
Form 10-Q
February 26, 2014

U.S. SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

Quarterly Report Pursuant to Section 13 or 15(d) of the
Securities Exchange Act of 1934

For Quarter Ended: December 31, 2013

Commission File Number: 000-22991

Fuse Science, Inc.

(Exact name of small business issuer as specified in its charter)

NEVADA

(State or other jurisdiction of
incorporation or organization)

87-0460247

(IRS Employer
Identification No.)

6135 NW 167 Street Suite E-21 Miami Lakes, FL 33015

(Address of principal executive office)

(305) 503-3873

(Issuer's telephone number)

Indicate by check mark whether the registrant (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 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 (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☒ No ☐

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

Large accelerated filer ☐ Accelerated filer ☐ Non-accelerated filer ☐ Smaller reporting company ☒

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

The number of shares outstanding of registrant's common stock, par value \$0.001 per share, as of February 19, 2014 was 399,915,143.

FUSE SCIENCE, INC.

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PART 1: FINANCIAL INFORMATION**ITEM 1: CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

FUSE SCIENCE, INC.
Condensed Consolidated Balance Sheets
December 31, 2013 (Unaudited) and September 30, 2013

	December 31, 2013	September 30, 2013
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 63,127	\$ 29,430
Accounts receivable	258,715	42,772
Inventory	1,250,023	1,336,513
Prepaid expenses and other assets	24,685	15,015
TOTAL CURRENT ASSETS	1,596,550	1,423,730
Other assets:		
Intellectual property, net	93,493	78,698
Fixed assets, net	137,732	143,447
TOTAL OTHER ASSETS	231,225	222,145
TOTAL ASSETS	\$ 1,827,775	\$ 1,645,875
LIABILITIES AND STOCKHOLDERS' DEFICIT		
LIABILITIES		
Accounts payable	\$ 1,763,748	\$ 1,694,589
Notes payable, net	237,086	174,395
Convertible notes payable, net	780,000	5,000
Accrued expenses	55,480	181,152
TOTAL CURRENT LIABILITIES	2,836,314	2,055,136
Warrants derivatives liabilities	58,994	252,210
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS' DEFICIT		
Preferred stock, \$0.001 par value; authorized 10,000,000 shares; no shares issued and outstanding; \$100 per share liquidation preference	-	-
Common stock, \$0.001 par value; authorized 400,000,000 shares; 377,215,464 and 276,944,231 shares issued and outstanding at December 31, 2013 and September 30, 2013, respectively	377,215	276,944
Additional paid-in capital	47,975,180	43,670,326
Non-controlling interest	(126,344)	(126,344)
Accumulated deficit	(49,293,584)	(44,482,397)
Total stockholders' deficit	(1,067,533)	(661,471)
Total liabilities and stockholders' deficit	\$ 1,827,775	\$ 1,645,875

See accompanying notes to condensed consolidated financial statements.

FUSE SCIENCE, INC.
Condensed Consolidated Statements of Operations
Three Months Ended December 31, 2013 and 2012
(Unaudited)

	2013	2012 Restated
Sales, net	\$ 313,993	\$ 40,711
Cost of sales	151,661	10,988
Gross margin	162,332	29,723
Expenses:		
Sales and marketing	553,185	748,318
General and administrative expense	1,226,153	1,476,519
Research and development	-	1,600
Total expenses	1,779,338	2,226,437
Loss from operations	(1,617,006)	(2,196,714)
Other expenses:		
Interest expense	(393,541)	(194,966)
Expense on inducement of warrant exchange	(170,616)	-
Change in fair value of warrant derivative liabilities	(2,630,024)	(1,672,804)
Total other expenses	(3,194,181)	(1,867,770)
Net loss	\$ (4,811,187)	\$ (4,064,484)
Loss per share, basic and diluted	\$ (0.01)	\$ (0.02)
Weighted average shares outstanding	328,542,287	176,794,628

See accompanying notes to condensed consolidated financial statements.

FUSE SCIENCE, INC.
Condensed Consolidated Statements of Changes in Stockholders' Deficit
Three Months Ended December 31, 2013
(Unaudited)

	Common Stock Shares	Par	Additional Paid-in Capital
Balance, September 30, 2013	276,944,231	\$ 276,944	\$ 43,670,326
Common stock issued for:			
Stock issued for consulting fees	18,275,000	18,275	591,918
Exercise of detachable warrants Cash	267,117	267	14,424
Exchange of warrants and inducement	81,729,116	81,729	88,887
Transfer from derivatives to equity			3,098,549
Amortization of stock options			511,076
Net loss			
Balance, December 31, 2013	377,215,464	377,215	47,975,180
	Non Controlling Interest	Accumulated Deficit	Total
Balance, September 30, 2013	\$ (126,344)	\$ (44,482,397)	\$ (661,471)
Common stock issued for:			
Stock issued for consulting fees			610,193
Exercise of detachable warrants Cash			14,691
Exchange of warrants and inducement			170,616
Transfer from derivatives to equity			3,098,549
Amortization of stock options			511,076
Net loss		(4,811,187)	(4,811,187)
Balance, December 31, 2013	\$ (126,344)	\$ (49,293,584)	\$ (1,067,533)

See accompanying notes to consolidated financial statements

FUSE SCIENCE, INC.
Condensed Consolidated Statements of Cash Flows
Three Months Ended December 31, 2013 and 2012
(Unaudited)

	2013	2012 Restated
Operating activities:		
Net loss	\$ (4,811,187)	\$ (4,064,484)
Adjustments to reconcile net loss from operations to net cash used in operating activities:		
Depreciation and amortization	6,020	3,462
Stock and stock option compensation	1,121,269	1,151,050
Inducement of warrant exchange	170,616	-
Amortization of discounts and financing fees	342,230	65,116
Change in fair value of warrant derivative liabilities	2,630,024	1,672,804
Changes in operating assets and liabilities:		
Inventory	86,490	(252,933)
Accounts receivable	(215,943)	9,573
Prepaid expenses and other assets	(73,902)	308,133
Accounts payable and accrued expenses	(56,511)	(273,692)
Net cash used in operating activities	(800,894)	(1,380,971)
Investing activities:		
Additions to fixed assets	-	(23,442)
Intellectual property	(15,100)	-
Net cash used in investing activities	(15,100)	(23,442)
Financing activities:		
Loan proceeds	835,000	250,000
Proceeds from warrant exercise	14,691	1,521,324
Financing charges paid	-	(122,578)
Net cash provided by investing activities	849,691	1,648,746
Net increase in cash and cash equivalents	33,697	244,333
Cash and cash equivalents, beginning of period	29,430	62,050
Cash and cash equivalents, end of period	\$ 63,127	\$ 306,383

See accompanying notes to condensed consolidated financial statements.

FUSE SCIENCE, INC.
Condensed Consolidated Statements of Cash Flows, Continued
Three Months Ended December 31, 2013 and 2012
(Unaudited)

	2013	2012 Restated
Supplemental Cash Flow Information:		
Non-cash investing and financing activities:		
Common stock issued for convertible notes payable and accrued interest	\$ -	\$ 138,001
Common stock issued for financing fees	\$ -	\$ 300,118
Transfers from derivative liability to additional paid in capital	\$ 3,098,548	\$ -

See accompanying notes to condensed consolidated financial statements.

FUSE SCIENCE, INC.
Notes to Condensed Consolidated Financial Statements

1. **NATURE OF BUSINESS**

ORGANIZATION

Fuse Science, Inc. (“**Company**”) was incorporated in Nevada on September 21, 1988. Since that time, the Company has engaged in a number of businesses as a private and subsequently a publicly held company, including developing and marketing data communications and networking infrastructure solutions for business, government and education (which business was sold in 2002) and as a “**business development company**” under the Investment Company Act of 1940, from 2007 to 2009. Since April 2011, the Company has been under new management with a singular focus on the development and commercialization of proprietary delivery technology focused on redefining the way humans receive energy, nutrition and medications today and in the future.

2. **SIGNIFICANT ACCOUNTING POLICIES**

CONSOLIDATION POLICY AND HISTORY OF BUSINESS

The consolidated financial statements of the Company include the accounts of the Company and its wholly owned subsidiaries, Fuse Science, Inc. (“**FSR&D**”), a Delaware Corporation, FSJV, LLC, a Florida limited liability company, FS Consumer Products Group, Inc., a Florida corporation [and its 60% owned subsidiary, Ultimate Social Network, Inc. (“**USN**”)]. All significant intercompany balances and transactions have been eliminated in consolidation.

BASIS OF PRESENTATION

The unaudited condensed consolidated financial statements included herein have been prepared by the Company, without audit, according to the rules and regulations of the Securities and Exchange Commission (“**SEC**”). Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America (“**GAAP**”) have been condensed or omitted pursuant to such rules and regulations. The information set forth in these interim condensed consolidated financial statements for the three months ended December 31, 2013 and 2012, is unaudited and reflects all adjustments, which include only normal recurring adjustments and which in the opinion of management are necessary to make the interim condensed consolidated financial statements not misleading. The September 30, 2013 year-end condensed consolidated balance sheet data was derived from audited financial statements, but does not include all disclosures required by GAAP. The Report of Independent Registered Public Accounting Firm on the September 30, 2013 consolidated financial statements contained an explanatory paragraph expressing substantial doubt about the Company’s ability to continue as a going concern. It is suggested that these condensed consolidated financial statements be read in conjunction with these financial statements and the notes thereto included in the Company’s latest stockholder’s annual report (Form 10-K) which were prepared assuming the Company will continue as a going concern.

USE OF ESTIMATES

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying disclosures. Although these estimates are based on management’s best knowledge of current events and actions the Company may undertake in the future, actual results could differ from these estimates.

REVENUE RECOGNITION

The Company records revenue net of discounts and allowances from the sale of Enerjel , Powerfuse and Electrofuse , when all of the following have occurred: (1) persuasive evidence of an arrangement exists, (2) product has been shipped or delivered, (3) the sales price to the customer is fixed or determinable, and (4) collectability is reasonably assured. The Company's customers may return ordered items for a refund. The Company also provides customers incentives to purchase products at a discount. For the three months ended December 31, 2013, we have recorded sales discounts, credits, and returns and allowances of \$246,091, which is netted against sales.

CASH CONCENTRATIONS

From time to time, the Company maintains cash with financial institutions in excess of federally insured limits.

ACCOUNTS RECEIVABLE

Accounts receivable are uncollateralized customer obligations due under normal trade terms. The carrying amount of accounts receivable may be reduced by an allowance that reflects management's best estimate of the amounts that will not be collected. Management individually reviews all accounts receivable balances and based on assessment of current credit worthiness, estimates the portion, if any, of the balance that will not be collected. All accounts or portions thereof determined to be uncollectible are written off to the allowance for doubtful accounts. No allowance for doubtful accounts was recorded as of December 31, 2013 and September 30, 2013.

SHIPPING AND HANDLING

Shipping and handling billed to customers is included in net sales and shipping and handling costs are recorded as a component of cost of sales.

INVENTORIES

Inventories consist of finished goods, which are manufactured by a contracted manufacturer on behalf of the Company, for resale. Inventories are valued at average cost and adjusted to reflect lower of cost or market. Provisions for inventory obsolescence are determined based upon the specific facts and circumstances and market conditions. As of December 31, 2013 and September 30, 2013, no obsolescence reserves were considered necessary.

FIXED ASSETS

Fixed assets are recorded at cost and depreciated using the straight-line method over the estimated useful life of 3-10 years. Repairs and maintenance are charged to expense as incurred.

FAIR VALUE MEASUREMENTS

Fair value is defined as the price that the Company would receive to sell an investment or pay to transfer a liability in a timely transaction with an independent counter-party in the principal market or in the absence of a principal market, the most advantageous market for the investment or liability. A three-tier hierarchy is established to distinguish between (1) inputs that reflect the assumptions market participants would use in pricing an asset or liability developed based on market data obtained from sources independent of the reporting entity (observable inputs) and (2) inputs that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing an asset or liability developed based on the best information available in the circumstances (unobservable inputs); and establishes a classification of fair value measurements for disclosure purposes.

The hierarchy is summarized in the three broad levels listed below:

Level 1 - quoted prices in active markets for identical assets and liabilities

Level 2 - other significant observable inputs (including quoted prices for similar assets and liabilities, interest rates, credit risk, etc.)

Level 3 - significant unobservable inputs (including the Company's own assumptions in determining the fair value of assets and liabilities).

In accordance with Accounting Standards Codification ("ASC") 815, the Company's warrant derivative liability is measured at fair value on a recurring basis, and is a level 3 measurement in the three-tier fair value hierarchy.

There were no transfers between the levels of the fair value hierarchy during the three months ended December 31, 2013 and 2012.

FAIR VALUE OF FINANCIAL INSTRUMENTS

The following methods and assumptions were used by the Company in estimating the fair values of each class of financial instruments disclosed herein:

Warrant Derivative Liability - These financial instruments are carried at fair value.

Notes Payable - Based upon the interest rates, current economic conditions, risk characteristics, collateral and other factors, the carrying amount of these financial instruments approximate market value (level 2 measurement).

DERIVATIVE LIABILITY

The Company issued warrants to purchase the Company's common stock in connection with the issuance of convertible debt, which contain certain ratchet provisions that reduce the exercise price of the warrants in certain circumstances. The Company determined that the warrants did not qualify for a scope exception under ASC 815 as they were determined not to be indexed to the Company's stock and accordingly are accounted for as derivatives and are recorded on the balance sheet at fair value with the changes in the fair value recognized in the consolidated statement of operations. Fair values are measured using a Black-Scholes valuation model, which approximates a binomial lattice valuation methodology utilizing Level 3 inputs.

INTELLECTUAL PROPERTY

Intellectual property is evaluated for impairment whenever events or changes in business circumstances indicate that the carrying value of our intellectual property may not be recoverable. Intellectual property is amortized on a straight-line basis over its estimated economic life of 15 years. We believe that the straight-line method of amortization reflects an appropriate allocation of the cost of the intangible assets to earnings in proportion to the amount of economic benefits obtained annually by the Company.

IMPAIRMENT OF LONG-LIVED ASSETS

The Company evaluates its long-lived assets and intangible assets for impairment whenever events change or if circumstances indicate that the carrying amount of any assets may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of the asset to the future net undiscounted cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is the excess of the carrying amount over the fair value of the asset.

INCOME TAXES

The Company accounts for income taxes under the liability method whereby deferred tax assets and liabilities are provided for the future tax consequences attributable to temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled.

Deferred tax assets, net of a valuation allowance, are recorded when management believes it is more likely than not that the tax benefits will be realized. Realization of the deferred tax assets is dependent upon generating sufficient taxable income in the future. The amount of deferred tax asset considered realizable could change in the near term if estimates of future taxable income are modified.

The Company assesses its tax positions in accordance with "Accounting for Uncertainties in Income Taxes" as prescribed by the Accounting Standards Codification, which provides guidance for financial statement recognition and measurement of uncertain tax positions taken or expected to be taken in a tax return for open tax years (generally a period of three years from the later of each return's due date or the date filed) that remain subject to examination by the Company's major tax jurisdictions. Generally, the Company is no longer subject to income tax examinations by major taxing authorities for years before September 30, 2010.

The Company assesses its tax positions and determines whether it has any material unrecognized liabilities for uncertain tax positions. The Company records these liabilities to the extent it deems them more likely than not to be incurred. Interest and penalties related to uncertain tax positions, if any, would be classified as a component of income tax expense in the accompanying consolidated statements of income.

The Company believes that it does not have any significant uncertain tax positions requiring recognition or measurement in the accompanying consolidated financial statements.

MARKETING, ADVERTISING AND PROMOTION COSTS

Marketing, advertising and promotion costs are charged to operations as incurred and are included in sales and marketing expenses in the accompanying consolidated statements of operations. The amounts charged for the three months ended December 31, 2013 and 2012 were approximately \$553,185 and \$748,318, respectively.

NON-CONTROLLING INTEREST

Non-controlling interest in the Company's consolidated financial statements represents the 40% interest not owned by the Company in USN. USN had no operations during the three months ended December 31, 2013 and 2012.

CONCENTRATION OF CREDIT RISK

One customer accounted for approximately 97% of the Company's net sales for the three months ended December 31, 2013 and approximately 86% of accounts receivable at December 31, 2013.

The Company obtains principally all of its inventory from one vender. In the event of loss of this supplier, it is reasonably possible that the Company would incur significant disruption to its operations, which could have a material adverse impact on the Company's financial position.

STOCK-BASED COMPENSATION

The Company accounts for stock options granted to employees and directors using the accounting guidance in ASC 718 “Stock Compensation” (“ASC 718”) and for stock options granted to consultants and endorers using the accounting guidance included in ASC 505-50 “Equity-Based Payments to Non-Employees” (“ASC 505-50”). In accordance with ASC 718, we estimate the fair value of service based options and performance based options on the date of grant, using the Black-Scholes pricing model. In accordance with ASC 505-50, we estimate the fair value of service based options and performance based options at each reporting period until a measurement date is reached using the Black-Scholes pricing model.

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because the Company’s options would have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management’s opinion, the existing models may not necessarily provide a reliable single measure of the fair value of the Company’s options, although they provide the best estimate currently.

LOSS PER SHARE

The Company’s loss per share is computed by dividing net loss by the weighted average number of common shares outstanding. Diluted losses per share reflects the potential dilution that could occur if stock options and or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the losses of the Company. All outstanding options and warrants are not included in the calculation of diluted loss per share as their effect would be antidilutive.

As described in Note 7 Payable, the Company had convertible notes and warrants outstanding during the three months ended December 31, 2013 and 2012. The convertible notes are reflected in the calculation of diluted earnings per share for the corresponding periods by application of the “if converted” method to the extent their effect is dilutive.

The following is a reconciliation of the numerator and denominator used for the computation of basic and diluted net loss per common shares:

		For the Three Months ended December 31,	
		2013	2012 Restated
Numerator:			
Net loss available to stockholders		\$ (4,811,187)	\$ (4,069,484)
Denominator:			
Weighted average number of common shares	Basic	328,542,287	176,794,628
Weighted average number of common shares	Diluted	328,542,287	176,794,628
Net loss per common share:			
Basic		\$ (0.01)	\$ (0.02)
Diluted		\$ (0.01)	\$ (0.02)

3. RESTATEMENT OF THE DECEMBER 31, 2012 BALANCES

As a result of certain adjustments affecting quarters of the fiscal year ended September 30, 2013, that were made as of September 30, 2013, the previously reported condensed consolidated statements of operations and cash flow for the three months ended December 31, 2012 have been restated. The restatements are a result of the following:

- Certain warrants with price protection features as described in Note 8, were not accounted for as derivatives for the quarter ended December 31, 2012. This resulted in an understatement of expenses by \$1,672,804.
- The Company incorrectly calculated the expense related to the issuance of stock options for the quarter ended December 31, 2012. This resulted in an understatement of general and administrative expense of \$286,506.

Detailed below are the account balances, which were reclassified to reflect the accounting for the previously described transactions.

	Three Months Ended December 31, 2012	Three Months Ended December 31, 2012	Effect of the
	Restated	(Originally Issued)	Change
General and administrative expense	\$ (1,476,519)	\$ (1,190,013)	\$ (286,506)
Change in fair value of warrant derivative liabilities	\$ (1,672,804)	\$ -	\$ (1,672,804)
Net loss	\$ (4,064,484)	\$ (2,105,174)	\$ (1,959,310)
Loss per share, basic and diluted	\$ (0.02)	\$ (0.01)	\$ (0.01)

Additionally, the impact of the restatements to the December 31, 2012 balance sheet would be increases in warrant derivative liabilities and total stockholders' deficit of approximately \$3.5 million.

4. GOING CONCERN

The Company has not established sources of revenue sufficient to fund the development of the business, projected operating expenses and commitments for the next twelve months and may be unable to obtain sufficient debt or equity financing. The Company has incurred net losses since inception, had a net loss of \$ (4,811,187) and used \$(800,894) in cash from operating activities during the three month period ended December 31, 2013. At December 31, 2013, current assets were \$1,596,550 and current liabilities were \$2,836,314. Further, at December 31, 2013, the accumulated deficit and total stockholders' deficit amounted to \$49,293,584 and \$1,067,533, respectively. These conditions raise substantial doubt about the Company's ability to continue as a going concern. No adjustments have been made as a result of this uncertainty.

The Company believes that the recent increases in the numbers of orders that it has shipped and its marketing plan will enable it to significantly increase its sales during 2014. In addition, the Company has already taken many steps to reduce the amount of operating expenses that it incurs on a monthly basis. Lastly, the Company believes that it will be able to complete additional fundraising with several of its current shareholders or debt holders that will enable it to meet its business plan.

5. INTELLECTUAL PROPERTY

In April 2011, the Company completed its acquisition of all the outstanding common stock of the Delaware corporation now known as FSR&D, which was a development stage company with no prior operations. As of December 31, 2013 and September 30, 2013 unamortized intellectual property relating to this acquisition amounted to \$93,492 and \$78,698, respectively.

6. FIXED ASSETS

Fixed Assets consisted of the following at December 31, 2013 and September 30, 2013:

	December 31, 2013	September 30, 2013
Equipment	\$ 108,821	\$ 108,821
Website	13,750	13,750
Display cases	42,245	42,245
Fixed assets	164,816	164,816

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Less: Accumulated depreciation	(27,084)	(21,369)
Fixed assets (net)	\$ 137,732	\$ 143,447

Depreciation and amortization expense amounted to \$6,020 and \$3,462 for the three months ended December 31, 2013 and 2012, respectively.

7.

NOTES PAYABLE

The Company had the following notes payable at December 31, 2013 and September 30, 2013.

	December 31, 2013	September 30, 2013
Convertible notes payable with interest at 12% (the "March 2013 Notes")	\$ 5,000	\$ 5,000
Convertible notes payable with interest at 10% (the "November 2013 Notes")	775,000	-
5% Six month secured promissory note due October 9, 2013	177,086	174,395
Two Week promissory note due January 7, 2014	60,000	-
	\$ 1,017,086	\$ 179,395
	December 31, 2013	September 30, 2013
Current	\$ 1,017,086	\$ 179,395
Long term	-	-
Total	\$ 1,017,086	\$ 179,395

November 2013 Notes

On November 7, 2013, we entered into a securities purchase agreement (the "**Purchase Agreement**") with a group of investors pursuant to which Fuse issued and sold 10% senior secured convertible notes in the aggregate original principal amount of \$775,000 (the "**Notes**") and warrants to purchase up to 25,830,750 shares of Fuse's common stock (the "**Warrants**"). The investor group consists of MusclePharm Corporation, Barry Honig, Michael Brauser, Melechdavid, Inc., Frost Gama Investments Trust, Jonathan Manela and Brian Tuffin, our Chief Executive Officer.

The indebtedness evidenced by the Notes bears interest at 10% per year, and accrues and is payable together with principal on the 60th day after Closing. The Notes may be converted, at the option of the holder, (i) into the Company's common stock, at any time following issuance at an exercise price of \$0.065 per share (subject to adjustment as provided in the Note) or (ii) if the Company consummates a subsequent financing generating gross proceeds of not less than \$4,000,000 (a "**Subsequent Financing**"), into the securities sold in the Subsequent Financing at a specified discount from the offering price of such securities. The Notes are secured by a first lien on substantially all of Fuse's assets pursuant to a pledge and security agreement (the "**Security Agreement**") among the parties.

Under the terms of the Warrants, the Holders are entitled to exercise the Warrants for a period of five (5) years following Closing at a price of \$0.065 per share (subject to adjustment as provided in the Warrant). The Company recorded a debt discount of \$275,309 and recorded the warrants as derivative liabilities at fair value. The discount is amortized over the life of the Notes using the interest method.

The fair value of the warrants on the due date was estimated using the Black-Scholes valuation model with the following assumptions:

Expected term	1 year	
Expected average volatility	106.00	%
Expected dividend yield	0	%
Risk-free interest rate	..12	%

In connection with the financing, Fuse granted piggy-back registration rights to the Holders with respect to the shares of common stock issuable upon conversion of the Notes and exercise of the Warrants.

The securities were issued pursuant to the exemption from registration afforded by Section 4(a)(2) of the Securities Act and Regulation D thereunder. In connection with these transactions, Fuse will pay a placement agent fee of \$43,400 to Dawson James Securities and will issue to the placement agent and their respective designees, placement agent warrants to purchase 7% of the number of shares of common stock that are issuable pursuant to the Notes and Warrants.

March 2013 Notes

On March 7, 2013, we sold (i) \$2,050,000 in combined principal amount of senior convertible and senior subordinated convertible notes (the “**March 2013 Notes**”) and (ii) warrants (the “**March 2013 Warrants**”), consisting of (a) series A warrants to purchase an aggregate of 12,058,828 (prior to conversion rate adjustment) shares of common stock (the “**Series A Warrants**”) and (b) series B warrants to purchase an aggregate of 12,058,828 (prior to conversion rate adjustment) shares of common stock (the “**Series B Warrants**”) at a purchase price of \$2,050,000, in a private placement to a group of institutional and accredited investors pursuant to a Securities Purchase Agreement, dated as of March 4, 2013. Prior to remeasurement, the March 2013 Notes are convertible into shares of the Company’s common stock at a conversion rate of \$0.17, and are entitled to earn interest which may be paid in cash or in shares of common stock. The March 2013 Warrants are exercisable into shares of common stock and have been accounted for as derivatives (See Note 7).

The March 2013 Notes are one (1) year senior convertible notes with an aggregate principal amount of \$1,500,000 (“**Series A Notes**”) and one (1) year senior subordinated convertible notes with an aggregate principal amount of \$550,000 (the “**Series B Notes**”). The March 2013 Notes will accrue interest at a rate of five percent (5%) per annum. The interest accrued is payable in interest shares, although the Company may, at its option and upon written notice to each note holder of the March 2013 Notes, make such interest payments in cash or in a combination of cash and interest shares.

The Series A Warrants have a term of five (5) years from the Closing Date and the Series B Warrants have a term of seven (7) months from the Closing Date. Each of the Series A Warrants and the Series B Warrants is immediately exercisable upon issuance into an aggregate of 12,058,828 (prior to remeasurement of the conversion rate) fully paid and non-assessable shares at an initial exercise price of \$0.21 per share in the case of the Class A Warrants and \$0.17 per share in the case of the Class B Warrants.

Any holder of the March 2013 Notes is entitled to convert the notes into conversion shares at any time by delivery of a notice of conversion to the Company. On or before the third trading day after receipt of the conversion notice, the Company must deliver to the note holder such number of conversion shares to which the note holder is entitled pursuant to the conversion. The number of conversion shares the note holder will receive upon conversion of the Notes will be determined by dividing the amount of principal being converted plus any accrued and unpaid interest by the conversion price effective at the time of the conversion. The March 2013 Notes have an initial conversion price of \$0.17 however it is subject to reset after a measurement period commencing upon effectiveness of a registration statement (Registration No. 333-187491) covering the shares underlying such securities. The registration statement was declared effective on May 22, 2013. As a result, this triggered a remeasurement of the conversion rate if the stock price falls below the initial conversion rate of \$0.17 on the tenth (10th) consecutive trading day following the registration statement and 80% of the average of the volume-weighted average prices for each of the preceding ten (10) complete consecutive trading days.

On June 6, 2013, the Company recomputed the conversion rate based on the 80% of the Company’s stock trading value for the 10 preceding days. As a result of the revision, the conversion rate was reduced to \$0.094. The exercise price of the Series A Warrants and Series B Warrants was also remeasured to \$0.149 and \$0.094, respectively. The remeasured conversion rate and exercise price increased the shares available for conversion to 21,808,510.

The Company received net proceeds in the amount of approximately \$1,794,000 after offering costs of \$256,000. In recording the transaction, the Company recorded a debt discount for the full face value of the Notes, and recorded the Series A and B Warrants as Derivative Liabilities at fair market value. The discount associated with the warrants is amortized over the life of the March 2013 Notes using the interest method. The value of the warrants was calculated using the Black-Scholes valuation model and totaled \$3,333,103 at issuance, resulting in a \$1,283,103 loss upon recording the warrant derivative liability.

During the quarter ending June 30, 2013, the noteholders of the March 2013 Notes converted substantially all the outstanding March 2013 Notes, reducing the Company debt associated with such convertible notes from \$2,105,000 to \$5,000 in exchange for approximately 22 million shares.

With respect to the March 2013 financing, the Company paid the co-placement agents a placement fee of \$164,000 and issued to the co-placement agents and their designees, five-year warrants to purchase an aggregate of 1,266,175 shares of common stock at an exercise price of \$0.21 per share and seven-month warrants to purchase an aggregate of 1,266,175 shares of common stock at an exercise price of \$0.17 per share. The total fair value of warrants and shares issued was approximately \$368,000. The conversion rate adjustment increased the shares issued to the Placement Agent. The series A Warrants increased to 1,818,253 and the series B Warrant increased to 2,299,873.

The fair value of each warrant on the date issued was estimated using the Black-Scholes valuation model. The following assumptions were used for the calculation of the warrants granted in March 2013.

	(Series A Warrants)		(Series B Warrants)	
Expected term	1 year		7 months	
Expected average volatility	120.00	%	120.00	%
Expected dividend yield	0	%	0	%
Risk-free interest rate	..80	%	..12	%

8. WARRANT DERIVATIVE LIABILITIES

The Company has warrants issued in connection with its convertible notes payable with price protection provisions that allow for the reduction in the exercise price of the warrants in the event the Company subsequently issues stock or securities convertible into stock at a price lower than the exercise price of the warrants. For certain warrants, simultaneously with any reduction to the exercise price, the number of shares of common stock that may be purchased upon exercise of each of these warrants shall be increased or decreased proportionately, so that after such adjustment the aggregate exercise price payable for the adjusted number of warrants shall be the same as the aggregate exercise price in effect immediately prior to such adjustment. The Company accounted for its warrants with price protection in accordance with FASB ASC Topic 815.

The Company's derivative warrant instruments have been measured at fair value at December 31, 2013 using the Black-Scholes model, which approximates a binomial or lattice model. The liability is revalued at each reporting period and changes in fair value are recognized currently in the consolidated statements of operations. The initial recognition and subsequent changes in fair value of the warrant derivative liability have no effect on the Company's cash flows.

The recognition and revaluation of the warrants at each reporting period resulting in the recognition of an expense of \$2,630,024 and \$1,672,804 for the three months ended December 31, 2013 and 2012, respectively. The fair value of the warrants at December 31, 2013 is \$58,994, which is reported on the consolidated balance sheet under the caption "Warrant Derivative Liabilities".

Fair Value Assumptions Used in Accounting for Warrant Derivative Liabilities

The Company has determined its warrant derivative liabilities to be a Level 3 fair value measurement and has used the Black-Scholes pricing model to calculate the fair value as of December 31, 2013. The Black-Scholes model requires six basic data inputs: the exercise or strike price, time to expiration, the risk free interest rate, the current stock price, the estimated volatility of the stock price in the future, and the dividend rate. Changes to these inputs could produce a significantly higher or lower fair value measurement. The key inputs used in the December 31, 2013 fair value calculations were as follows:

Stock Price	\$	0.02	
Volatility		108%-113	%
Strike Price	\$	0.065 0.25	
Risk-free Rate		0.10%-0.13	%
Dividend Rate		0	%
Expected Life	6 months	9 months	

At December 31, 2013, the estimated fair values of the liabilities measured on a recurring basis are as follows:

	Fair Value Measurements at December 31, 2013			
	Balance at September 30, 2013	Quoted Prices in Active Markets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Warrant derivative liabilities	\$ 58,994	\$ -	\$ -	\$ 58,994

The following table presents the activity for liabilities measured at estimated fair value using unobservable inputs for the three months ended December 31, 2013:

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3) Warrant Derivative Liabilities
Beginning balance at September 30, 2013	\$ 252,210
Issuance of warrant derivative liabilities	275,309
Changes in estimated fair value	2,630,024
Reclassification of derivative liability to additional paid-in capital	(3,098,549)
Ending balance at December 31, 2013	\$ 58,994

9. WARRANT EXCHANGE

On December 2, 2013, we concluded an exchange offer pursuant to which we repurchased our outstanding Series A Warrants (the “**Series A Warrants**”) and Exchange Warrants (the “**Exchange Warrants**”) from the holders thereof (the “**Holders**”). These Series A Warrants were originally issued on March 7, 2013 pursuant to a Securities Purchase Agreement dated March 4, 2013, among the Company and certain investors and were scheduled to expire on March 7, 2018. The Exchange Warrants were issued in a private exchange offer completed on March 14, 2013 and were scheduled to expire on March 14, 2018. The exchange offer reflects Fuse’s ongoing efforts to reduce market overhang.

Under Exchange Agreements entered into between the Company and the Holders, the Holders of Series A Warrants to purchase an aggregate of 19,808,930 shares of our common stock and Exchange Warrants to purchase an aggregate of 8,601,814 shares of our common stock agreed to exchange their Series A Warrants and/or their Exchange Warrants for an aggregate of 81,729,116 shares of our common stock (the “**Exchange Shares**”).

As a result of the exchange, the warrant derivative liability related to the Series A Warrants was reduced by \$3,098,549. An expense on inducement of warrant exchange in the amount of \$170,616 was recorded as a result of the exchange of the Exchange Warrants.

10. INCOME TAXES

The Company recorded no income tax benefit or expense for the losses for the three months ended December 31, 2013 and 2012 since management has determined that the realization is not assured and has created a valuation allowance for the full amount of deferred tax assets.

11. STOCKHOLDERS' EQUITY (DEFICIT)

Preferred stock

At December 31, 2013, the Company had 10,000,000 shares authorized and no shares issued and outstanding of its \$0.001 par value preferred stock.

Common stock

At December 31, 2013 and September 30, 2013, the Company had 400,000,000 shares authorized and 377,215,464 and 276,944,231 shares issued and outstanding, respectively, of its \$0.001 par value common stock.

Transactions during the three months ended December 31, 2013

Common Stock

During the three months ended December 31, 2013, the Company issued 18,275,000 shares of common stock to athletes and consultants for endorsement and consulting services valued at approximately \$610,000.

Warrants

During the three months ended December 31, 2013, the holders of the March 2013 Notes exercised 267,117 of series B Warrants issued in connection therewith for common stock which generated \$14,691 in cash.

On December 12, 2013, the Company reached agreements with the holders of the series A Warrants that were issued in conjunction with the March 2013 Notes, and the holders of the exchange warrants. The terms of the agreements resulted in the exchange of the . 19,808,930 series A Warrants and 8,601,814 exchange warrants for approximately 81,729,000 shares of common stock (see Note 9).

Transactions during the three months ended December 31, 2012

Common Stock

During the three months ended December 31, 2012, the Company issued 1,066,461 shares of common stock upon conversion of convertible notes payable with a principal balance and accrued interest totaling \$138,001.

During the three months ended December 31, 2012, the Company issued 1,250,000 shares of common stock to athletes and consultants for endorsement and consulting services valued at approximately \$518,000.

Warrants

During the three months ended December 31, 2012, the note holders of the February 2012 Notes exercised approximately 13,830,216 of Series B Warrants for common stock which generated \$1,521,324 in cash. In addition, during the period there were cashless exercises in the amount of 919,018 shares from our Series A warrants issued with our February 2012 Notes.

12. COMMITMENTS AND CONTINGENCIES

Consulting agreement - The Company entered into a consulting agreement with Mr. Durschlag in April 2010 under which he may receive royalty payments in accordance with the terms of his patent assignment and technology transfer agreement. The Company is currently in litigation proceedings with Mr. Durschlag as it does not believe that any of its products use the technology specified in the patent assignment and technology transfer agreement. If it is determined that Mr. Durschlag is entitled to royalties on Fuse Science, Inc. sales payment would be as follows:

Sales Range	Commission Rate	
\$0 - \$100,000	0.00	%
\$100,001 - \$10,000,000	5.00	%
\$10,000,001 - \$50,000,000	2.50	%

Employment agreements - The Company currently has an employment agreement with Brian Tuffin.

Effective December 28, 2012 the Company entered into a settlement agreement with the Company's former Chief Marketing Officer and Chief Information Officer, Aitan Zacharin for approximately 1,000,000 options to acquire common stock at exercise prices from \$0.12 to \$0.21 and \$58,000 over a period of seven months commencing January 1, 2013.

Endorsement agreements Several of our endorsement agreements require share or option compensation to be issued annually. In addition, additional shares may be granted in the event of certain performance milestones.

The Company also issued stock options as compensation under certain other endorsement agreements. These agreements have a term of one to five years with Company options to extend the agreements for one to three years at mutually agreeable terms.

13. SUBSEQUENT EVENTS:

(a) On January 3, 2014, we repurchased outstanding Advisory Warrants (the "**Advisory Warrants**") from the holders thereof (the "**Holders**") through an exchange offer. These Advisory Warrants were originally issued in 2011 and 2012 for investment banking services.

Under Exchange Agreements entered into between the Company and the Holders, the Holders of Advisory Warrants to purchase an aggregate of 828,249 shares of our common stock agreed to exchange their Advisory Warrants for an aggregate of 24,000,000 shares of our common stock (the "**Exchange Shares**").

The Exchange Shares are being issued to the Holders pursuant to the exemption from registration afforded by Section 3(a)(9) of the Securities Act of 1933, as amended (the "**Securities Act**").

(b) On January 3, 2014, we also entered into a securities purchase agreement (the "**Purchase Agreement**") with two (2) investors (the "**New Investors**") pursuant to which Fuse agreed to issue and sell senior secured convertible notes in the aggregate original principal amount of \$1,000,000 (the "**Senior Notes**") and warrants to purchase up to 50,000,000 shares of Fuse's common stock (the "**Warrants**"). The transaction is scheduled to close on or before January 6, 2014 ("**Closing**"). \$550,000 in principal amount of Senior Notes and Warrants to purchase 41,250,000 shares of our common stock will be issued at Closing. The balance of \$450,000 will be funded in four (4) monthly installments of \$100,000 in principal amount of Senior Notes and Warrants to purchase 7,500,000 shares of our common stock and a final installment of \$50,000 in principal amount of Senior Notes and Warrants to purchase 3,750,000 shares of our common stock, subject to satisfaction of customary conditions at the closing of each installment.

In addition to the foregoing, the holders of the \$775,000 in principal amount of our 10% senior secured convertible notes (the “**Exchange Investors**”), originally issued in private transactions in November and December 2013, agreed to exchange their notes for an equal principal amount of Senior Notes.

The indebtedness evidenced by the Senior Notes bears interest at 12% per year, payable when the Senior Notes become due and mature on the fifth (5th) anniversary from issuance, provided a holder of Senior Notes may require Fuse to redeem the holder’s Senior Notes at any time after the first (1st) anniversary of issuance. The principal amount of the Senior Notes will be payable on the maturity date or such earlier as the Senior Notes become due. The Senior Notes may be converted into the Company’s common stock, at the option of the holder, at any time following issuance at an initial conversion price of \$0.02 (the “**Fixed Conversion Price**”). From and after the sixth (6) month anniversary of the issuance of the Senior Notes, the conversion price of the Senior Notes will be equal to the lower of (i) the Fixed Conversion Price and (ii) sixty percent (60%) of the arithmetic average of the one (1) lowest weighted average price our common stock for the sixty (60) trading days immediately preceding any conversion of the Senior Notes (the “**Alternative Conversion Price**,” and together with the Fixed Conversion Price, the “**Conversion Price**”). The Conversion Price is also subject to anti-dilution adjustments as provided for in the Senior Notes. The Senior Notes are secured by a first lien on substantially all of Fuse’s assets pursuant to a pledge and security agreement (the “**Security Agreement**”) among the parties.

Under the terms of the Warrants, the Holders are entitled to exercise the Warrants for a period of seven (7) years from issuance at a price of \$0.0259 per share (subject to adjustment as provided in the Warrant).

As soon as practicable after the Closing Date but in no event later than twenty (20) days thereafter, the Company shall seek shareholder approval to cause (1) the increase of the number of authorized shares of common stock to 800 million shares and (2) authorize implementation of a reverse split of the common stock at a ratio of 200:1.

The securities issued to the Investor were issued pursuant to the exemption from registration afforded by Section 4(a)(2) of the Securities Act and Regulation D thereunder. The Notes issued to the Exchange Investors were issued to the Exchange Investors pursuant to the exemption from registration afforded by Section 3(a)(9) of the Securities Act. In connection with these transactions, Fuse will pay a placement agent fee equal to five percent (5%) of the principal amount of Senior Notes issued to the New Investors, to Dawson James Securities and will issue to the placement agent and their respective designees, placement agent warrants to purchase 7% of the number of shares of common stock that are issuable pursuant to the Senior Notes and Warrants issued to the New Investors.

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

Forward Looking Statements

This analysis of our results of operations should be read in conjunction with the accompanying financial statements, including notes thereto, contained in Item 8 of this Report. This Report contains certain forward-looking statements within the meaning of Section 27A of the Securities Act, and Section 21E of the Securities Exchange Act of 1934. Statements that are predictive in nature and that depend upon or refer to future events or conditions are forward-looking statements. Although we believe that these statements are based upon reasonable expectations, we can give no assurance that projections will be achieved. Please refer to the discussion of forward-looking statements included in Part I of this Report.

RESULTS OF OPERATIONS

Three Months Ended December 31, 2013 as Compared to Three Months Ended December, 2012.

Revenues and Gross Profit

	Three Months ended December 31,				
	2013	2012 Restated	\$ Change	% Change	
Sales, net	\$ 313,993	\$ 35,872	\$ 278,121	775	%
Cost of sales	151,661	10,960	140,701	1,284	%
Gross margin	\$ 162,332	\$ 24,912	\$ 137,420		

Sales

Net Sales were \$313,993 for the three months ended December 31, 2013, as compared to \$35,872 for the three months ended December 31, 2012. The increase in sales is due to the initial expansion of retail distribution nationally led by Walgreens, Discount Drug Mart, Golf Galaxy and others.

Gross Profit

Gross profit percentage during the three months ended December 31, 2013 was 52% compared to 69% for the three months ending December 31, 2012. Sales for the three months ended December 31, 2013 consisted of Enerjel ,

Powerfuse and Electrofuse. Sales for the three months ended December 31, 2012 only consisted of Enerjel. This change resulted in a larger portion of sales being sold at wholesale pricing versus direct to consumer. Additionally, the Company and Walgreens conducted a two-for-one promotion during the three months ended December 31, 2013 resulting in reduced sales prices and gross profit.

Operating Costs and Expenses

	Three Months ended December 31,		\$
	2013	2012 Restated	Change
General and administrative	\$ 1,226,153	\$ 1,476,519	\$ (250,366)
Sales and Marketing	553,185	748,318	(195,133)
	\$ 1,779,338	\$ 2,224,837	\$ (445,499)

Our operating expenses were \$1,779,338 and \$2,224,837 for the three months ended December 31, 2013 and December 31, 2012, respectively, a decrease of \$445,499 from 2012 to 2013, reflecting increased operations. For the three months ending December 31, 2013, \$1,121,269 was recorded for share-based compensation and amortization of deferred compensation. This compares with \$1,151,050 for share-based compensation and amortization of deferred compensation for the three months ending December 31, 2012. The deferred compensation expense in 2013 and 2012 represents the amortized fair value of stock and options issued for services to non-employees. The share-based compensation charges to operations in 2013 and 2012 were primarily for stock options granted under our 2011 Incentive Stock Plan to executive officers and were made so that their interests would be aligned with those of shareholders, providing incentive to improve Company performance on a long-term basis. Grants of stock options were also made to third parties for various services rendered and as additional compensation for financing agreements. Amortization of deferred compensation is recorded in general and administrative expenses. Share-based compensation expense is included in sales and marketing and general and administrative expenses.

General and Administrative Expenses

For the three months ended December 31, 2013 and 2012 general and administrative expenses were \$1,226,153 and \$1,476,519, respectively. The decrease of \$250,366 is primarily composed of decreases in non-cash stock-based compensation costs of \$30,000 and \$60,000 in compensation expenses to employees. General and administrative expenses consist primarily of compensation and support costs for management and administrative staff, and for other general and administrative costs, including professional fees related to accounting, finance, and legal services as well as other operating expenses.

	Three months ended December 31,	
	2013	2012 Restated
Professional fees	\$ 703,482	\$ 575,347
Salaries and benefits	431,527	494,541
Other general and administrative expense	91,143	406,631
	\$ 1,226,153	\$ 1,476,519

Professional Fees Expense

Professional fees expense increased to \$703,482 for the three months ended December 31, 2013, compared to \$576,347 for the three months ended December 31, 2012. This increase was due to the Company's requirements for legal, compliance, protection and accounting and consulting services related to the Company's ongoing day-to-day business dealings and execution of its business plan, including, accounting, financial reporting and SEC compliance.

Salary and Benefits

Salary and benefits amounted to \$431,527 for the three months ended December 31, 2013 compared to \$494,541 for the three months ended December 31, 2012. The decrease was due to a decrease in personnel headcount. Prior to April 1, 2012 the Company limited payments to employees and consultants based on cash availability resulting in underpayment of salaries.

Sales and Marketing

For three months ended December 31, 2013 and 2012, sales and marketing expenses were \$553,185 and \$748,318, respectively. In February 2012, the Company entered into a marketing and distribution agreement with Mission to

market the Company's products through their distribution channels. This agreement included comprehensive marketing services and heavy commercialization efforts during the first ten (10) months. The Company paid Mission approximately \$650,000 for these services, which is amortized over 10 months. Included in the decrease in 2013 is amortization of deferred compensation (non-cash) of approximately \$60,942 as of December 31, 2013 compared to \$274,481 as of December 31, 2012. The Company's products are endorsed by a number of professional athletes, which are remunerated cash and non-cash payments. The decrease in sales and marketing is also attributed to endorsement contracts with these professional athletes. Sales and marketing expenses consist primarily of compensation and support costs for sales and marketing personnel, professional services, promotional, marketing and related activities.

Research and Development

Included in our operating expenses for 2013 is approximately \$0 for research and development expenses compared to \$1,600 for 2012. Research and development expenses consist primarily of compensation for contractors engaged in internal research and product development activities, laboratory operations, and related expenses. The Company considers research and development of its technology and the science behind its products an important cornerstone of its continuing efforts. As the Company progresses it will continue to invest in research and development and anticipates increases year over year.

Other Expense

Other income (expense) consists of the following:

	Three months ended December 31,	2012
	2013	Restated
Expense on inducement of warrant exchange	\$ (170,616)	\$ -
Change in fair value warrant derivative liabilities	(2,630,024)	(1,672,804)
Interest expense	(393,541)	(194,966)
	\$ (3,194,181)	\$ (1,867,770)

Interest Expense

Interest expense is primarily attributable to convertible notes payable. During February of 2012, the Company issued \$3,169,359 of convertible notes bearing interest of 9%. On March 7, 2013, the Company issued similar notes with an aggregate face value of \$2,050,000 bearing interest of 12%. Interest expense amounted to \$393,541 for the three months ended December 31, 2013, as compared to interest expense of approximately \$194,966 for the three months ended December 31, 2012. Also included in interest expense is amortization of financing fees relating to the notes and amortization of note discounts on the balance of the outstanding notes.

LIQUIDITY AND CAPITAL RESOURCES**Liquidity**

The following table summarizes total current assets, liabilities and working capital at December 31, 2013 compared to September 30, 2013.

	December 31, 2013	September 30, 2013	Increase/(Decrease)
Current Assets	\$ 1,596,550	\$ 1,423,730	\$ 172,820
Current Liabilities	\$ 2,836,314	\$ 2,055,136	\$ 781,178
Working Capital (Deficit)	\$ (1,239,764)	\$ (631,406)	\$ (608,358)

As December 31, 2013, we had a working capital deficit of \$(1,239,764), as compared to a working capital deficit of \$(631,406) at September 30, 2013, an increase of \$608,358. The increase is primarily attributable to the Company's issuance of \$780,000 in convertible notes. The Company continues to devote significant resources to aggressively pursue markets for its products, new product introductions, advancement of its intellectual property and build out of its infrastructure and team.

Net cash (used for) operating activities for the three months ended December 31, 2013 and 2012 was \$(800,894) and \$(1,380,971), respectively. The net loss for the three months ended December 31, 2013 and 2012 was \$(4,811,187) and \$(4,064,484), respectively.

Net cash (used for) and provided by investing activities for the three months ended December 31, 2013 and 2012 respectively, was \$(15,100) and \$(23,442), respectively.

Net cash obtained through all financing activities for the three months ended December 31, 2013 and 2012 was \$849,691 and \$1,648,746, respectively.

Our primary source of operating cash during fiscal 2013 has been through private placements of our securities, principally convertible notes and warrants and the subsequent exercise of certain of those warrants.

Management estimates that it will need between \$3,500,000 and \$5,000,000 in capital during fiscal 2014 to continue to commercialize our products, license our technology and otherwise fully implement our business plan. We have no commitments to raise any such capital. If such capital is not available when needed on commercially reasonable terms or otherwise, we may have to scale down or delay implementation of our business plan in whole or in part and curtail its business activities, which would seriously harm the Company and its prospects.

Going Concern

The financial statements are prepared using the accrual method of accounting in accordance with accounting principles generally accepted in the United States of America and have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities in the normal course of business. However, the Company has incurred significant losses and experienced negative cash flow since its inception. At December 31, 2013, the Company had cash of \$63,127 and a working capital deficit of \$(1,239,764). Further, at December 31, 2013, the accumulated deficit amounted to \$49,293,584. As a result of the history of losses and unfavorable financial condition, there is substantial doubt about the ability of the Company to continue as a going concern.

The Company will require additional funding of between \$3,500,000 and \$5,000,000 during 2014 to finance the growth of its current and expected future operations as well as to achieve its strategic objectives. The Company believes its current available cash along with anticipated revenues may be insufficient to meet its cash needs for the near future. There can be no assurance that financing will be available in amounts or terms acceptable to the Company, if at all.

In response to these problems, management has taken the following actions:

- continue with the implementation of our business plan;
- generate new sales from expanded retail distribution of EnerJel , PowerFuse and ElectroFuse ;
- seeking additional third party debt and/or equity financing;
- continue facilitation of licensing efforts; and
- allocate sufficient resources to continue with advertising and marketing efforts.

A successful transition to attaining profitable operations is dependent upon obtaining sufficient financing to fund the Company's planned expenses and achieving a level of revenues adequate to support the Company's cost structure. Management plans to finance future operations through the use of cash on hand, increased revenues and capital raised through equity or debt financing. We also expect to receive proceeds from stock warrant exercises from existing shareholders. As the Company's product continues to gain market acceptance, the Company expects sales in 2014 and beyond to substantially increase.

There can be no assurances that the Company will be able to achieve its projected level of revenues in 2014 and beyond. If the Company is unable to achieve its projected revenues and is not able to obtain alternate additional financing of equity or debt, the Company would need to significantly curtail or reorient its operations during 2013, which could have a material adverse effect on the Company's ability to achieve its business objectives and as a result may require the Company to file for bankruptcy or cease operations. The financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or amounts classified as liabilities that might be necessary should the Company be forced to take any such actions.

Our future expenditures will depend on numerous factors, including: the rate at which we can introduce and sell products; the costs of filing, prosecuting, defending and enforcing any patent claims and other intellectual property rights; and market acceptance of our products and competing technological developments. We expect that we will incur between \$3,500,000 and \$5,000,000 in cash expenditures for our operating expenses during fiscal 2014. As we expand our activities and operations, our cash requirements are expected to increase at a rate consistent with revenue growth after we have achieved sustained revenue generation.

RECENT ACCOUNTING PRONOUNCEMENTS

New Accounting Standards

There are several new accounting pronouncements issued by the Financial Accounting Standards Board (“FASB”) which are not yet effective. Each of these pronouncements, as applicable, has been or will be adopted by the Company. Management does not believe any of these accounting pronouncements has had or will have a material impact on the Company’s financial position or operating results.

Critical Accounting Policies

The SEC issued “Cautionary Advice Regarding Disclosure about Critical Accounting Policies”; suggesting companies provide additional disclosure and commentary on their most critical accounting policies. The SEC defined the most critical accounting policies as the ones that are most important to the portrayal of a company’s financial condition and operating results, and require management to make its most difficult and subjective judgments, often as a result of the need to make estimates of matters that are inherently uncertain. Based on this definition our most critical accounting policies are in process of evolving while we move from the development stage to the operational stage of our business cycle.

Off-Balance Sheet Arrangements

None.

Tabular Disclosure Of Contractual Obligations

None.

ITEM 3: QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not applicable.

ITEM 4: CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Under the PCAOB standards, a control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control over financial reporting that is less severe than a material weakness, yet important enough to merit the attention by those responsible for oversight of the company's financial reporting. A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the company's annual or interim financial statements will not be prevented or detected on a timely basis.

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of our disclosure controls and procedures, as such term is defined under Rule 13a-15(e) and Rule 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended (Exchange Act), as of December 31, 2013. Our management has determined that, as of December 31, 2013, the Company's disclosure controls and procedures are not effective.

Management's Report on Internal Control over Financial Reporting

Management of the Company is responsible for establishing and maintaining effective internal control over financial reporting, as defined in Rule 13a-15(f) under the Exchange Act. The Company's internal control over financial reporting is designed to provide reasonable assurance to the Company's management and Board of Directors regarding the preparation and fair presentation of published financial statements in accordance with the United States' generally accepted accounting principles (US GAAP), including those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and disposition of the assets of the Company, (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with US GAAP and that receipts and expenditures are being made only in accordance with authorizations of management and directors of the Company, and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation.

Under the supervision and with the participation of our management, including our chief executive officer and our chief financial officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework established by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) as set forth in its Internal Control - Integrated Framework. Based on our evaluation under the framework in Internal Control - Integrated Framework, our management has concluded that our internal control over financial reporting was not effective as of December 31, 2013 in the following areas:

- The Company does not have adequate controls and procedures to detect errors in accounting for certain of its financing transactions, specifically related to the Company's issuance of convertible debt and warrants.

- The Company does not have adequate controls and procedures to detect errors in accounting for certain of its equity transactions, specifically related to recording stock options granted to employees, consultants and endorsers.

There were no significant changes in internal controls or in other factors that could significantly affect these controls during the quarter ended December 31, 2013.

PART II OTHER INFORMATION

ITEM 1 LEGAL PROCEEDINGS

On August 28, 2013, Maurice Edward Durschlag filed a state court lawsuit against the Company in Charlotte, North Carolina. Mr. Durschlag was formerly the president of Double Eagle Holdings, Inc. (n/k/a Fuse Science, Inc.), alleges breach of contract and unpaid royalty payments. On October 10, 2013, the Company learned that a default had been entered in this case. The Company has filed appropriate motions to set aside the default and compel arbitration as required under the subject Agreement. Based on conversations with our IP counsel, the Company believes that Mr. Durschlag's claims are without merit.

ITEM 1A RISK FACTORS

Not applicable.

ITEM 2 UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Not applicable.

ITEM 3 DEFAULTS UPON SENIOR SECURITIES

Not applicable.

ITEM 4 SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

Not applicable.

ITEM 5 OTHER INFORMATION

Not applicable.

ITEM 6 EXHIBITS

31.1 Certification pursuant to 18 U.S.C. Section 1350 Section 302 of the Sarbanes-Oxley Act of 2002

32.1 Certification pursuant to 18 U.S.C. Section 1350 Section 906 of the Sarbanes-Oxley Act of 2002

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

*Pursuant to Rule 406T of Regulation S-T, these interactive data files are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933 or Section 18 of the Securities Act of 1934 and otherwise are not subject to liability.

SIGNATURE

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.

FUSE SCIENCE, INC.

February 26, 2014

By: /s/Brian Tuffin
Brian Tuffin,
Chief Executive Officer and
Acting Chief Financial Officer