Sugarmade, Inc.
Form 10-Q
May 15, 2013

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)
þ QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended: March 31, 2013

o TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from N/A to N/A

Commission file number: 000-23446

SUGARMADE, INC.
(Exact Name of Registrant as Specified in its Charter)

Delaware (State or jurisdiction of incorporation or organization)	94-3008888 (I.R.S. Employer Identification No.)
2280 Lincoln Avenue, Suite 200, San Jose CA (Address and of principal executive offices)	95125 (Zip Code)

888-747-6233
(Registrant's telephone number, including area code)

Indicate by check mark whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act of 1934 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 þ No o

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ No o

Indicate by check mark whether 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	o	Accelerated filer	o
Non-accelerated filer	o (Do not check if a smaller reporting company)	Smaller reporting company	þ

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

At May 13, 2013 there were 9,238,526 shares outstanding of the issuer’s common, the only class of common equity.

Transitional Small Business Disclosure Format (Check one): Yes o No þ

SUGARMADE, INC.
FORM 10-Q
FOR THE PERIOD ENDED MARCH 31, 2013

TABLE OF CONTENTS

SPECIAL NOTE REGARDING FORWARD LOOKING STATEMENTS

In addition to historical information, this Quarterly Report on Form 10-Q includes forward-looking statements. Forward-looking statements are those that predict or describe future events or trends and that do not relate solely to historical matters. You can generally identify forward-looking statements as statements containing the words "believe," "expect," "will," "anticipate," "intend," "estimate," "project," "plan," "assume" or other similar expressions, or negatives of those expressions, although not all forward-looking statements contain these identifying words. All statements contained or incorporated by reference in this quarterly report regarding our future strategy, future operations, projected financial position, estimated future revenues, projected costs, future prospects, the future of our industry and results that might be obtained by pursuing management's current plans and objectives are forward-looking statements.

You should not place undue reliance on our forward-looking statements because the matters they describe are subject to known and unknown risks, uncertainties and other unpredictable factors, many of which are beyond our control. Our forward-looking statements are based on the information currently available to us and speak only as of the date on the cover of this quarterly report, or, in the case of forward-looking statements in documents incorporated by reference, as of the date of the date of the filing of the document that includes the statement. New risks and uncertainties arise from time to time, and it is impossible for us to predict these matters or how they may affect us. Over time, our actual results, performance or achievements will likely differ from the anticipated results, performance or achievements that are expressed or implied by our forward-looking statements, and such difference might be significant and materially adverse to our security holders. We do not undertake and specifically decline any obligation to update any forward-looking statements or to publicly announce the results of any revisions to any statements to reflect new information or future events or developments.

We have identified some of the important factors that could cause future events to differ from our current expectations and they are described in this quarterly report under the caption "Risk Factors," below, and elsewhere in this quarterly report which you should review carefully. Please consider our forward-looking statements in light of those risks as you read this quarterly report.

TABLE OF CONTENTS

Sugarmade, Inc. and Subsidiary
Condensed Consolidated Balance Sheets

	March 31, 2013 (Unaudited)	June 30, 2012
Assets		
Current assets:		
Cash	$158,335	$192,100
Accounts receivable, net	28,820	18,700
Inventory, net	262,432	88,798
Other current assets	19,130	45,125
Total current assets	468,717	344,723
Equipment, net	3,788	5,257
Other assets	3,994	3,994
Total assets	$476,499	$353,974
Liabilities and Stockholders' Deficit		
Current liabilities:		
Note payable due to bank	$150,000	$150,000
Accounts payable and accrued liabilities	361,798	221,020
Accrued interest, including amounts due to related parties of $29,195	55,892	-
Notes payable due to shareholder	86,000	-
Accrued compensation and personnel related payables	343,339	43,722
Production line of credit	284,000	-
Total current liabilities	1,281,029	414,742
Convertible notes payable, net	363,413	-
Convertible notes payable to related parties, net	118,621	-
Total liabilities	1,763,063	414,742
Stockholders' deficit:		
Preferred stock ($0.001 par value, 10,000,000 shares authorized, none issued and outstanding)	-	-
Common stock ($0.001 par value, 300,000,000 shares authorized, 10,538,526 and 10,288,526 shares issued and outstanding at March 31, 2013 and June 30, 2012, respectively)	10,539	10,289
Additional paid-in capital	8,406,610	8,069,581
Accumulated deficit	(9,703,713)	(8,140,638)
Total stockholders' deficit	(1,286,564)	(60,768)

Total liabilities and stockholders’ deficit	$476,499	$353,974

The accompanying notes are an integral part of these condensed consolidated financial statements

4

TABLE OF CONTENTS

Sugarmade, Inc. and Subsidiary
Condensed Consolidated Statements of Operations (Unaudited)

	For the three months ended March 31,		For the nine months ended March 31,	
	2013	2012	2013	2012
Revenues, net	$51,645	$84,498	$165,569	$123,996
Cost of goods sold:				
Materials and freight costs	36,161	69,207	111,162	82,589
Provision for inventory obsolescence	-	-	40,851	-
Total cost of goods sold	36,161	69,207	152,013	82,589
Gross margin	15,484	15,291	13,556	41,407
Operating expenses:				
Selling, general and administrative expenses	327,870	634,962	1,442,549	3,246,786
Amortization	-	4,601	-	13,802
Total operating expenses	327,870	639,563	1,442,549	3,260,588
Loss from operations	(312,386)	(624,272)	(1,428,993)	(3,219,181)
Non-operating income (expense):				
Interest expense:				
Related parties	(35,349)	-	(53,004)	-
Other	(44,684)	(1,146)	(81,468)	(1,146)
Total Interest Expense	(80,033)	(1,146)	(134,472)	(1,146)
Interest income:				
Other	124	-	390	1,222
Total non-operating income (expense)	(79,909)	(1,146)	(134,082)	76
Net loss	$(392,295)	$(625,418)	$(1,563,075)	$(3,219,105)
Basic and diluted net loss per share	$(0.04)	$(0.06)	$(0.15)	$(0.31)
Basic and diluted weighted average common shares outstanding used in computing net loss per share	10,538,526	10,372,000	10,492,906	10,294,385

The accompanying notes are an integral part of these condensed consolidated financial statements

TABLE OF CONTENTS

Sugarmade, Inc. and Subsidiary
Condensed Consolidated Statements of Cash Flows (Unaudited)
For the nine months ended March 31, 2013 and 2012

	2013	2012
Operating activities:		
Net loss	$(1,563,075)	$(3,219,105)
Adjustments to reconcile net loss to cash flows from operating activities:		
Amortization	-	13,802
Depreciation	1,469	1,122
Share based compensation	142,191	184,177
Issuance of common stock for services	98,545	1,590,950
Issuance of warrants with convertible notes	96,543	-
Changes in operating assets and liabilities:		
Accounts receivable	(10,120)	(48,250)
Inventory	(173,634)	(121,751)
Other assets	25,995	(255,367)
Accounts payable and accrued liabilities	140,778	92,296
Accrued interest	55,892	-
Accrued compensation and personnel related payables	299,617	1,301
Net cash used in operating activities	(885,799)	(1,760,825)
Investing activities:		
Purchase of equipment	-	(27,143)
Net cash flows used in investing activities	-	(27,143)
Financing activities:		
Proceeds from issuances of common stock and warrants	-	609,260
Borrowings from note payable to bank	-	50,000
Borrowings from production line of credit	284,000	-
Proceeds from issuance of convertible notes payable	363,413	-
Proceeds from issuance of convertible notes payable to related parties	118,621	-
Issuance of notes payable	86,000	-
Net cash provided by financing activities	852,034	659,260
Net decrease in cash	(33,765)	(1,128,708)
Cash, beginning of period	192,100	1,606,764
Cash, end of period	$158,335	$478,056
Supplemental disclosure of cash flow information:		
Cash paid during the period for:		
Interest	$25,003	$1,146

The accompanying notes are an integral part of these condensed consolidated financial statements

TABLE OF CONTENTS

Sugarmade, Inc. and Subsidiary
Notes to Unaudited Condensed Consolidated Financial Statements
March 31, 2013

1. Summary of significant accounting policies

Nature of business

Sugarmade, Inc. (hereinafter referred to as "we", "us" or "the/our Company") is a publicly traded company incorporated in the state of Delaware. Our previous legal name was Diversified Opportunities, Inc. Our Company, Sugarmade, Inc. operates through our subsidiary, Sugarmade, Inc., a California corporation ("Sugarmade-CA"). Our Company is principally engaged in the business of marketing and distributing environmentally friendly non-tree-based paper products. We are parties to an Exclusive License and Supply Agreement ("LSA") with Sugar Cane Paper Company ("SCPC"), a company located in the People's Republic of China. SCPC is one of Sugarmade's original contract manufacturers and SCPC is a holder of intellectual property rights and patents in the area of developing and manufacturing paper from non-wood sources. We also obtained the rights (within the designated territories) to the Sugarmade™ brand name and trademarks. Historically, Sugarmade has leveraged this relationship and corresponding agreement to initially insure production and management of its products. Presently, Sugarmade has been able to diversify its manufacturing and process management options to include other third party contract manufacturers. Sugarmade-CA's primary product is 100% tree-free copy paper in various sizes, however our Company plans to offer other tree-free paper products in the future.

Basis of presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America and the rules and regulations of the United States Securities and Exchange Commission for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all the information and footnotes necessary for a comprehensive presentation of financial position, results of operations, or cash flows. It is management's opinion however, that all material adjustments (consisting of normal recurring adjustments) have been made which are necessary for a fair financial statement presentation. The results for the interim period are not necessarily indicative of the results to be expected for the full year.

These condensed consolidated financial statements should be read in conjunction with our Company's Annual Report on Form 10-K for the year ended June 30, 2012, which contains our audited consolidated financial statements and notes thereto, together with the Management's Discussion and Analysis of Financial Condition and Results of Operation, for the period ended June 30, 2012. The interim results for the period ended March 31, 2013 are not necessarily indicative of the results for the full fiscal year.

Principles of consolidation

The condensed consolidated unaudited financial statements include the accounts of our Company and its wholly-owned subsidiary, Sugarmade-CA. All significant intercompany transactions and balances have been eliminated in consolidation.

Going concern

The Company sustained continued operating losses during the nine months ended March 31, 2013 and for the year ended June 30, 2012. The Company's continuation as a going concern is dependent on its ability to generate sufficient cash flows from operations to meet its obligations, in which it has not been successful, and/or obtaining additional financing from its shareholders or other sources, as may be required.

Our condensed consolidated financial statements have been prepared assuming that we will continue as a going concern. Such assumption contemplates the realization of assets and satisfaction of liabilities in the normal course of business. However, our auditors raised concerns about our ability to continue as a going concern in their opinion on our financial statements at and for the year ended June 30, 2012. These condensed consolidated financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amounts and classifications of liabilities that may result should the Company be unable to continue as a going concern.

TABLE OF CONTENTS

Sugarmade, Inc. and Subsidiary
Notes to Unaudited Condensed Consolidated Financial Statements
March 31, 2013

Management is endeavoring to increase revenue generating operations. While priority is on generating cash from operations through the sale of the Company's products, management is also seeking to raise additional working capital through various financing sources, including the sale of the Company's equity and/or debt securities, which may not be available on commercially reasonable terms to our Company, or which may not be available at all. If such financing is not available on satisfactory terms, we may be unable to continue our business as desired and our operating results will be adversely affected. In addition, any financing arrangement may have potentially adverse effects on us and/or our stockholders. Debt financing (if available and undertaken) will increase expenses, must be repaid regardless of operating results and may involve restrictions limiting our operating flexibility. If we issue equity securities to raise additional funds, the percentage ownership of our existing stockholders will be reduced and the new equity securities may have rights, preferences or privileges senior to those of the current holders of our common stock.

Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires our management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ significantly from those estimates.

Revenue recognition

We recognize revenue in accordance with Financial Accounting Standards Board Accounting Standards Codification ("FASB ASC") No. 605, Revenue Recognition. Revenue is recognized when we have evidence of an arrangement, a determinable fee, and when collection is considered to be probable and products are delivered. This generally occurs upon shipment of the merchandise, which is when legal transfer of title occurs. In the event that final acceptance of our product by the customer is uncertain, revenue is deferred until all acceptance criteria have been met. We currently have a consignment arrangement with two of our customers. We record revenue on consignment goods when the consigned goods are sold by the consignee and all other above mentioned revenue recognition criteria have been satisfied. Cash deposits received in connection with the sales of our products prior to their being delivered is recorded as deferred revenue.

During the year ended June 30, 2012, we became aware of quality issues surrounding our copy paper products. We were able to trace the reported problems with paper quality back to manufacturing issues with our third party contract manufacturer. Our Company has since implemented additional quality assurance procedures both during and at the completion of the production processes. During the nine months ended March 31, 2013, our Company had limited sales as we continued producing and delivering replacement product, in addition to disposing of the product containing the quality issues. For the three months ended March 31, 2013, we sold the remaining sub-quality paper to a third party wholesaler specializing in the liquidation of excess inventory. This sale represented approximately 18% of our revenue for the quarter. As we had recorded an inventory reserve for this product, we recognized revenue with no corresponding cost of goods sold.

Cash

From time to time, we may maintain bank balances in interest bearing accounts in excess of the $250,000 currently insured by the Federal Deposit Insurance Corporation for interest bearing accounts (there is currently no insurance limit for deposits in noninterest bearing accounts). We have not experienced any losses with respect to cash. Management believes our Company is not exposed to any significant credit risk with respect to its cash.

Accounts receivable

Accounts receivable are carried at their estimated collectible amounts, net of any estimated allowances for doubtful accounts. We grant unsecured credit to our customers deemed credit worthy. Ongoing credit evaluations are performed and potential credit losses estimated by management are charged to operations on a regular basis. At the time any particular account receivable is deemed uncollectible, the balance is charged to the allowance for doubtful accounts. Since we cannot necessarily predict future changes in the financial stability of our customers, we cannot guarantee that our allowance for doubtful accounts will be adequate.

From time to time, we may have a limited number of customers with individually large amounts due. Any unanticipated change in a customer's creditworthiness could have a material effect on our results of operations in the period in which such changes or events occurred. Accounts receivable at March 31, 2013 and June 30, 2012 was $28,820 and $18,700 (net of allowance for doubtful accounts of $1,220), respectively, all of which we expect to be collectible.

Sugarmade, Inc. and Subsidiary
Notes to Unaudited Condensed Consolidated Financial Statements
March 31, 2013

Inventory

Inventory consists of finished goods paper and paper-based products ready for sale and is stated at the lower of cost or market. We value our inventory using the weighted average costing method. Our Company's policy is to include as a part of inventory any freight incurred to ship the product from our contract manufactures to our warehouses. Outbound freights costs related to shipping costs to our customers are considered period costs and reflected in selling, general and administrative expenses. Outbound freight costs to customers totaled $16,019 and $50,628 for the three and nine months ended March 31, 2013, respectively, and $26,888 and $39,288 for the three and nine months ended March 31, 2012. We regularly review inventory and consider forecasts of future demand, market conditions and product obsolescence. If the estimated realizable value of our inventory is less than cost, we make provisions in order to reduce its carrying value to its estimated market value. During the fourth quarter of fiscal 2012, our Company became aware of quality issues surrounding its copy paper products. As a result of these quality issues, we determined that the historical inventory values were not realizable and we recorded a reserve for inventory obsolescence. We completed our review of impacted inventory during the second quarter of fiscal 2013, and recorded additional reserves at that time. For the three months ended March 31, 2013, we continued to dispose of reserved inventory either through sales to a third party liquidator or where it was impractical to sell the inventory, we donated the product to third party charitable organizations. There were no additional reserves recorded during the third quarter ended March 31, 2013. As of March 31, 2013 and June 30, 2012, the balance for the inventory obsolescence reserve totaled $37,708 and $195,880, respectively.

Other current assets

Other current assets consist mainly of prepaid insurance, deposits and other related expenses.

Equipment

Equipment is stated at cost, less accumulated depreciation. Expenditures for maintenance and repairs are charged to expense as incurred. Items of equipment with costs greater than $1,500 are capitalized and depreciated on a straight-line basis over their estimated useful lives ranging from 3-7 years.

Intangible assets

We had intangible assets related to the exclusive license and supply agreement ("LSA") with Sugar Cane Paper Company. During the year ended June 30, 2012, we performed a review of the LSA including estimations of the likely future cash flows to be derived from the LSA. Upon completing the review, it was management's assessment that due to changes in our Company's manufacturing process, enhancements to the product formulation and the limitations on the credit facility, the fair value of the intangible asset had been impaired to the level that the asset has negligible remaining value. As such, our Company recorded an impairment charge totaling $318,983 for the remaining value of the license and supply agreement as of June 30, 2012.

Valuation of long-lived assets

We evaluate long-lived assets for impairment whenever events or changes in circumstances indicate their net book value may not be recoverable. When such factors and circumstances exist, we compare the projected undiscounted future cash flows associated with the related asset or group of assets over their estimated useful lives against their respective carrying amount. Impairment, if any, is based on the excess of the carrying amount over the fair value, based on market value when available, or discounted expected cash flows, of those assets and is recorded in the period in which the determination is made. As noted above, for the year ended June 30, 2012, it was determined that the carrying value of our intangible assets should be zero and we recorded an impairment charge for the full carrying value.

Income taxes

We provide for federal and state income taxes currently payable, as well as for those deferred due to timing differences between reporting income and expenses for financial statement purposes versus tax purposes. Deferred tax assets and liabilities are recognized 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 income tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect of a change in income tax rates is recognized as income or expense in the period that includes the enactment date.

The accounting guidance for uncertainties in income tax prescribes a comprehensive model for the financial statement recognition, measurement, presentation, and disclosure of uncertain tax positions taken or expected to be taken in income tax returns. The Company recognizes a tax benefit from an uncertain tax position in the financial statements only when it is more likely than not that the position will be sustained upon examination, including resolution of any related appeals or litigation processes, based on the technical merits and a consideration of the relevant taxing authority's widely understood administrative practices and precedents.

TABLE OF CONTENTS

Sugarmade, Inc. and Subsidiary
Notes to Unaudited Condensed Consolidated Financial Statements
March 31, 2013

Stock based compensation

Stock based compensation cost is measured at the date of grant, based on the calculated fair value of the stock-based award, and will be recognized as expense over the employee's requisite service period (generally the vesting period of the award). We estimate the fair value of employee stock options granted using the Black-Scholes-Merton Option Pricing Model. Key assumptions used to estimate the fair value of stock options will include the exercise price of the award, the fair value of our common stock on the date of grant, the expected option term, the risk free interest rate at the date of grant, the expected volatility and the expected annual dividend yield on our common stock. We use comparable public company data among other information to estimate the expected price volatility and the expected forfeiture rate. Non-employee stock grant costs are measured and recognized upon completion of performance and tied to the contractual obligations of the parties we transact with.

Loss per share

We calculate basic loss per share ("EPS") by dividing our net loss by the weighted average number of common shares outstanding for the period, without considering common stock equivalents. Diluted EPS is computed by dividing net loss by the weighted average number of common shares outstanding for the period and the weighted average number of dilutive common stock equivalents, such as options and warrants. Options and warrants are only included in the calculation of diluted EPS when their effect is dilutive.

Fair value of financial instruments

The Company follows guidance for accounting for fair value measurements of financial assets and financial liabilities and for fair value measurements of nonfinancial items that are recognized or disclosed at fair value in the financial statements on a recurring basis. Additionally, the Company adopted guidance for fair value measurement related to nonfinancial items that are recognized and disclosed at fair value in the financial statements on a nonrecurring basis. The guidance establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to measurements involving significant unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company has the ability to access at the measurement date.

Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3 inputs are unobservable inputs for the asset or liability.

The level in the fair value hierarchy within which a fair measurement in its entirety falls is based on the lowest level input that is significant to the fair value measurement in its entirety.

Advertising

We expense advertising costs as incurred. Advertising and promotion totaled $2,292 and $9,001 during the three and nine months ended March 31, 2013. For the three and nine months ended March 31, 2012, advertising and promotions totaled $17,253 and $26,692, respectively. We have no existing arrangements under which we provide or receive advertising services from others for any consideration other than cash.

Concentration

Customers

For the three and nine months ended March 31, 2013, our Company earned net revenues of $51,645 and $165,569, respectively. A significant portion of our Company's revenue is derived from a small number of customers. For the three and nine months ended March 31, 2013, sales to three of our Company's customers accounted for 73% and 84% of net sales, respectively.

Suppliers

For the three and nine months ended March 31, 2013, all of our tree free paper products were purchased from SCPC and their contract manufacturers.

TABLE OF CONTENTS

Sugarmade, Inc. and Subsidiary
Notes to Unaudited Condensed Consolidated Financial Statements
March 31, 2013

Litigation

From time to time, we may become involved in disputes, litigation and other legal actions. We estimate the range of liability related to any pending litigation where the amount and range of loss can be estimated. We record our best estimate of a loss when the loss is considered probable. Where a liability is probable and there is a range of estimated loss with no best estimate in the range, we record a charge equal to at least the minimum estimated liability for a loss contingency when both of the following conditions are met: (i) information available prior to issuance of the financial statements indicates that it is probable that an asset had been impaired or a liability had been incurred at the date of the financial statements and (ii) the range of loss can be reasonably estimated.

Recent Developed Accounting Pronouncements

Effective January 2013, we adopted FASB ASU No. 2011-11, Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities (ASU 2011-11). The amendments in ASU 2011-11 require the disclosure of information on offsetting and related arrangements for financial and derivative instruments to enable users of its financial statements to understand the effect of those arrangements on its financial position. Amendments under ASU 2011-11 will be applied retrospectively for fiscal years, and interim periods within those years, beginning after January 1, 2013. The adoption of this update did not have a material impact on the consolidated financial statements.

Effective January 2013, we adopted FASB ASU No. 2013-02, Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive (ASU 2013-02). This guidance is the culmination of the FASB's deliberation on reporting reclassification adjustments from accumulated other comprehensive income (AOCI). The amendments in ASU 2013-02 do not change the current requirements for reporting net income or other comprehensive income. However, the amendments require disclosure of amounts reclassified out of AOCI in its entirety, by component, on the face of the statement of operations or in the notes thereto. Amounts that are not required to be reclassified in their entirety to net income must be cross-referenced to other disclosures that provide additional detail. This standard is effective prospectively for annual and interim reporting periods beginning after December 15, 2012. The adoption of this update did not have a material impact on the consolidated financial statements.

New Accounting Pronouncements Not Yet Adopted

In February 2013, the FASB issued ASU No. 2013-04, Liabilities (Topic 405): Obligations Resulting from Joint and Several Liability Arrangements for Which the Total Amount of the Obligation Is Fixed at the Reporting Date. The amendments in ASU 2013-04 provide guidance for the recognition, measurement, and disclosure of obligations resulting from joint and several liability arrangements for which the total amount of the obligation within the scope of this Update is fixed at the reporting date, except for obligations addressed within existing guidance in U.S. GAAP. The guidance requires an entity to measure those obligations as the sum of the amount the reporting entity agreed to pay on the basis of its arrangement among its co-obligors and any additional amount the reporting entity expects to pay on behalf of its co-obligors. The guidance in this Update also requires an entity to disclose the nature and amount of the obligation as well as other information about those obligations. The amendments in this standard are effective retrospectively for fiscal years, and interim periods within those years, beginning after December 15, 2013. We are evaluating the effect, if any, adoption of ASU No. 2013-04 will have on our consolidated financial statements.

In March 2013, the FASB issued ASU No. 2013-05, Foreign Currency Matters (Topic 830): Parent's Accounting for the Cumulative Translation Adjustment upon Derecognition of Certain Subsidiaries or Groups of Assets within a

Foreign Entity or of an Investment in a Foreign Entity. The amendments in ASU No. 2013-05 resolve the diversity in practice about whether Subtopic 810-10, Consolidation—Overall, or Subtopic 830-30, Foreign Currency Matters—Translation of Financial Statements, applies to the release of the cumulative translation adjustment into net income when a parent either sells a part or all of its investment in a foreign entity or no longer holds a controlling financial interest in a subsidiary or group of assets that is a nonprofit activity or a business (other than a sale of in substance real estate or conveyance of oil and gas mineral rights) within a foreign entity. In addition, the amendments in this Update resolve the diversity in practice for the treatment of business combinations achieved in stages (sometimes also referred to as step acquisitions) involving a foreign entity. The amendments in this standard are effective prospectively for fiscal years, and interim reporting periods within those years, beginning December 15, 2013. We are evaluating the effect, if any, adoption of ASU No. 2013-05 will have on our consolidated financial statements.

In April 2013, the FASB issued ASU No. 2013-07, Presentation of Financial Statements (Top 205): Liquidation Basis of Accounting. The objective of ASU No. 2013-07 is to clarify when an entity should apply the liquidation basis of accounting and to provide principles for the measurement of assets and liabilities under the liquidation basis of accounting, as well as any required disclosures. The amendments in this standard is effective prospectively for entities that determine liquidation is imminent during annual reporting periods beginning after December 15, 2013, and interim reporting periods therein. We are evaluating the effect, if any, adoption of ASU No. 2013-07 will have on our consolidated financial statements.

TABLE OF CONTENTS

Sugarmade, Inc. and Subsidiary
Notes to Unaudited Condensed Consolidated Financial Statements
March 31, 2013

2. Acquisition of Sugarmade-CA and related financing activities

On April 23, 2011, we entered into the Exchange Agreement with Sugarmade-CA. Under the terms of the Exchange Agreement, we acquired all of the outstanding stock of Sugarmade-CA (the "Exchange"). Upon the closing of the Exchange on May 9, 2011, Sugarmade-CA became a wholly-owned subsidiary of our Company.

Under the terms of the Exchange Agreement, Sugarmade-CA's shareholders exchanged all of their shares of stock on a one-for-one basis for a total of 8,864,108 shares of our common stock. In connection with the Exchange Agreement and effective at the closing of the Exchange transaction, our previous three principal shareholders agreed to enter into a Share Cancellation Agreement pursuant to which 8,762,500 shares held by them were canceled or redeemed in exchange for our Company's payment of $210,000, the issuance of 200,000 two-year warrants to purchase our common stock at $1.25 per share, and certain registration rights.

Prior to the closing of the Exchange, our Company had no operations and was a "shell" company. Accordingly, the transaction was accounted as a reverse-merger and our financial statements reflect the financial position and operations of Sugarmade-CA for all periods presented as if it was the acquiring entity in the Exchange.

3. Note payable due to bank

During October 2011, we entered into a revolving demand note (line of credit) arrangement with HSBC Bank USA, with a revolving borrowing limit of $150,000. The line of credit bears a variable interest rate of one quarter percent (0.25%) above the prime rate (3.25% as of March 31, 2013). This borrowing facility is renewed annually and our Company is required to maintain a separate demand deposit account with HSBC with a minimum balance equal to the outstanding borrowing. In the event the deposit account is not established or minimum balance maintained, HSBC can charge a higher rate of interest of up to 4.0% above prime rate. As of March 31, 2013, the loan's interest rate was three and one half percent (3.5%) and HSBC has advanced $150,000. The note is payable on demand.

4. Production Line of Credit

As part of our agreement with SCPC for a production line of credit, SCPC has provided our Company with access to a portion of the overall credit line to allow us to purchase product for inventory purposes, without the need for customer purchase orders as a requirement to order product from its contract manufacturer. This portion production line of credit will initially be set at $300,000, bear interest at 5% interest per quarter and a 4% usage charge, and require payment 30 days after receipt of funds from our customer. The same repayment terms will remain in effect. As of March 31, 2013, the balance on the credit line totaled $284,000.

5. Convertible note payables, net

Between August 17, 2012 and March 31, 2013, our Company issued a total of $525,000 in convertible promissory notes to eleven accredited investors, one of which is a member of our Board of Directors and another was a former member of our Board of Directors. The convertible promissory notes must be repaid by our Company within 9 months from the date of issuance; accrue interest at the rate of 14%; and are subject to conversion at the election of the investors at such time as our Company has raised a minimum of $500,000 in a subsequent equity financing. The conversion price will be the lower of 80% of the per share purchase price paid for by the new investors in the subsequent financing, or $0.50 per share. Unless these promissory notes are converted or repaid earlier, our Company must pay the noteholders the amount of the then accrued interest on the three, nine, and nine month anniversaries of the issue date.

In connection with the issuance of the promissory notes, the investors in the aggregate received two-year warrants to purchase up to a total of 78,750 shares of common stock at $0.50 per share, and two-year warrants to purchase up to a total of 131,250 shares of common stock at $0.01 per share. For purposes of accounting for the detachable warrants issued in connection with the convertible notes, the fair value of the warrants was estimated using the Black-Scholes-Merton option pricing formula. The value of all warrants granted at the date of issuance totaled $96,543 and was recorded as a discount to the notes payable. The amount will be amortized over the nine month term of the respective convertible note as additional interest expense.

For the three and nine month periods ended March 31, 2013, the Company recorded interest expense related to convertible notes payable (including discount amortization) of $50,024, and $85,111, respectively.

Sugarmade, Inc. and Subsidiary
Notes to Unaudited Condensed Consolidated Financial Statements
March 31, 2013

6. Related party transactions

On January 19, 2012, our Board of Directors approved a grant of 36,000 shares of our Company's common stock (subject to a 1 year repurchase option by our Company) to Ed Roffman, a former director, for the provision of services to our Company in the areas of finance and public reporting. During the year ended June 30, 2012, our company recorded share based consulting expense totaling $66,900. The monthly expense was based on exercise prices ranging from $1.90 per share to $4.25 per share. The shares were issued in reliance upon the exemption from registration afforded by Section 4(2) of the Securities Act as transactions by an issuer not involving any public offering.

Effective May 11, 2012, our Company entered into a Share Cancellation Agreement with Clifton Leung, a director and shareholder of our Company, pursuant to which Mr. Leung agreed to the cancellation of 500,000 shares of Company common stock held by him. In consideration for the cancellation, our Company agreed to pay Mr. Leung $5,000 representing a price of $0.01 per share of common stock. Our Company accounted for this transaction as a purchase and immediate retirement of treasury shares. Effective June 30, 2012, Mr. Leung forgave the amount owed to him from the share cancellation agreement.

On August 17, 2012, the company issued a convertible note with warrants to Jim Jensen, a former director, in exchange for $25,000 short term loan to our Company. In connection with the issuance of the promissory note, Mr. Jensen received two-year warrants to purchase up to a total of 3,750 shares of common stock at $0.50 per share, and two-year warrants to purchase up to a total of 6,250 shares of common stock at $0.01 per share. The convertible promissory note must be repaid by our Company within 9 months from the date of issuance; accrues interest at the rate of 14%; and is subject to conversion at the election of the noteholder at such time as our Company has raised a minimum of $500,000 in a subsequent equity financing. The conversion price will be the lower of 80% of the per share purchase price paid for by the new investors in the subsequent financing, or $0.50 per share. Unless these promissory notes are converted or repaid earlier, our Company must pay the noteholder the amount of the then accrued interest on the three, nine, and nine month anniversaries of the issue date.

On September 6, 2012, our Company's Board of Directors approved the repricing of options and warrants granted to employees, consultants and board members. The repriced options and warrants had exercise prices ranging from $1.25 to $3.73. A total of 1,245,000 vested and unvested options and warrants were amended to reduce the exercise price to $0.52 per share, based on the most recent closing price for our Company's common stock prior to the approval of the re-pricing, which was deemed to be the fair market value as of that date. One current and two former members of our board had a total of 325,000 options repriced to the lower exercise price. The Company incurred additional share based compensation costs totaling $6,250 related to the repriced options and will recognized over the options vesting period.

On November 29, 2012, the Company entered into a Share Cancellation Agreement with Scott Lantz pursuant to which Mr. Lantz agreed to the cancellation of 354,722 of his shares of Company common stock. Mr. Lantz is the Chief Executive Officer, Chief Financial Officer and a Director of the Company.

On November 30, 2012, our Company issued a convertible promissory note in the amount of $100,000 to Jonathan Leong, one of our directors, as part of a financing involving eleven accredited investors. The convertible promissory note must be repaid by our Company within 9 months from the date of issuance; accrues interest at the rate of 14%; and is convertible at the election of the note holder at such time as our Company has raised a minimum of $500,000 in equity in a subsequent equity financing, at the conversion price which is the lower of 80% of the per share purchase price paid for the securities by the investors in the subsequent financing, or $.50 per share. Unless this promissory note is converted or repaid earlier, our Company must pay the note holder the amount of the then accrued interest on the three month anniversary, nine month anniversary, and nine month anniversary of the issue date. In connection with the issuance of the promissory notes, Mr. Leong received two-year warrants to purchase 15,000 shares of common stock at $.50 per share, and two-year warrants to purchase 25,000 shares of common stock at $.01 per share.

On February 22, 2013, our Company issued a promissory note in the amount of $25,000 to Sandy Salzberg, one of our directors, for short term financing. The note has a term of 30 days and bears interest at a rate of 25% per annum. As of March 31, 2013, the note remained outstanding and had accrued interest totaling $660.

7. Stockholders' Deficit

Issuance of common stock and warrants for cash

On March 7, 2012, our Company's Board of Directors approved the sale of our Company's common stock and warrants to purchase common stock at $2.25 per unit. Each unit consisted of (i) one share of our Company's common stock; and (ii) two-year term warrants to purchase the amount of shares of common stock equal to 80% of the number of units purchased. Each warrant was issued with a fixed exercise price of $0.01 per share. As of June 30, 2012, our Company raised $657,500 through the sale of 292,222 units and the commensurate exercise of 193,778 warrants for additional cash proceeds totaling $1,938. For the nine months ended March 31, 2013, there were no additional stock issuances for cash.

TABLE OF CONTENTS

Sugarmade, Inc. and Subsidiary
Notes to Unaudited Condensed Consolidated Financial Statements
March 31, 2013

Issuance of common stock for services

In May 2011, we issued 500,000 shares of common stock subject to repurchase provisions to an individual as consideration for consulting services. We recorded a prepaid stock compensation in connection with the shares granted totaling $400,000 based on the estimated value of the underlying shares of stock at the time of their issuance to the consultant. The grant was originally scheduled to vest evenly on a monthly basis over two years through May 2013, however our Company vested all of the remaining unvested shares in December 2011. The prepaid stock compensation from the grant was charged to operations at the fair market value of the vesting shares at the time of their vesting since the consultant's performance was tied to the contractual vesting terms. Prepaid stock compensation was originally amortized proportionally over the expected vesting term of the shares at the time the shares were vested, with the difference being recorded as additional paid-in capital. For the year ended June 30, 2012, we recorded noncash charges totaling $1,547,000 in connection with this stock issuance.

On January 19, 2012, our Company issued 36,000 shares of restricted common stock to one of its former board members in exchange for additional advisory services in the area of finance and financial reporting. The shares vest over one year and any unvested shares are subject to repurchase by our Company should the recipient cease to provide for the contracted services. For the nine months ended March 31, 2013, our Company incurred a charge totaling $13,545 related to this issuance.

On May 31, 2012, we issued 10,526 shares of restricted common stock to a public relations firm as part of their compensation for services in the area of public relations related strategy, processes and tactics. For the year ended June 30, 2012, our Company recorded noncash charges totaling $20,000 related to this issuance.

On September 20, 2012, our Company issued 250,000 shares to a third party consultant in consideration for its services under the terms of a consulting agreement for investor relations and public communications services. For the three months ended March 31, 2013, we recorded noncash charges totaling $85,000 in connection with this stock issuance based on previous day's closing price for our common stock, which is deemed the fair market value as of that date.

Share surrender and cancellation

Effective May 11, 2012, our Company entered into a Share Cancellation Agreement with Clifton Leung, a director and shareholder of our Company, pursuant to which Mr. Leung agreed to surrender 500,000 shares of Company common stock held by him. In consideration for the surrender, our Company agreed to pay Mr. Leung $5,000 representing a price of $0.01 per share of common stock. Our Company accounted for this transaction as a repurchase and cancellation of common stock. Effective June 30, 2012, Mr. Leung forgave the amount owed to him from the share cancellation agreement.

On November 29, 2012, the Company entered into a Share Cancellation Agreement with Scott Lantz pursuant to which Mr. Lantz agreed to the cancellation of 354,722 of his shares of Company common stock. Mr. Lantz is the Chief Executive Officer, Chief Financial Officer and a Director of the Company. In consideration for the surrender, our Company agreed to pay Mr. Lantz $10. Our Company accounted for this transaction as a repurchase of common stock previously issued to Mr. Lantz and recorded treasury stock on the date of the agreement. The shares were concurrently issued to certain third party investors who previously participated in the Company's sale of common stock and warrants during the March-May 2012 fundraising. The Company measured the issuance based on the previous day's closing market price of the common stock of $0.3210 per share and recorded $113,866 as contributed shares with a corresponding entry to additional paid in capital.

Stock options

On April 27, 2011, our Company's Board of Directors approved the adoption of the 2011 Stock Option/Stock Issuance Plan (the "2011 Plan") and reserved 1,500,000 shares of common stock for issuance under the 2011 Plan. The 2011 Plan provides for the issuance of both non-qualified stock options and incentive stock options ("ISOs"), and permitted grants to employees, non-employee directors and consultants of our Company. Generally, stock option grants under the 2011 Plan will vest over a period of up to four years and have a term not to exceed 10 years, although the Plan Administrator has the discretion to issue option grants with varying terms and vesting periods.

As of March 31, 2013, we have a total of 1,133,462 incentive and nonqualified stock options granted and outstanding under the Plan. All of our outstanding options have terms of between five and ten years. During the three and nine months ended March 31, 2013, we recognized share based compensation expense totaling $32,105– and $105,797, respectively, related to stock options granted through that date.

TABLE OF CONTENTS

Sugarmade, Inc. and Subsidiary
Notes to Unaudited Condensed Consolidated Financial Statements
March 31, 2013

Other outstanding warrants

We issued warrants to purchase up to 2,185,600 of our common stock in connection with the sale of our common stock during the year ended June 30, 2011 and issued warrants to purchase up to 40,000 shares of our common stock in connection with the sale of our common stock during the year ended June 30, 2012. We also have warrants to purchase 921,500 of our common stock outstanding as of March 31, 2013, issued to individuals providing consulting and advisory services to our Company. During the three and nine months ended March 31, 2013, we recognized share based compensation expense related to these warrants totaling $5,056 and $36,395, respectively.

Between August 17, 2012 and March 31, 2013, our Company issued a total of 210,000 warrants in conjunction with $525,000 in convertible promissory notes to eleven accredited investors, one of which was a member of our Board of Directors and another who is a former member of our Board of Directors. In connection with the issuance of the promissory notes, the investors in the aggregate received two-year warrants to purchase up to a total of 78,750 shares of common stock at $0.50 per share, and two-year warrants to purchase up to a total of 131,250 shares of common stock at $0.01 per share. The value of all warrants granted at the date of issuance totaled $96,543 and was recorded as a discount to the notes payable. The amount will be amortized over the nine month term of the respective convertible note as additional interest expense. For the three and nine months ended March 31, 2013, we amortized $31,661 and $53,577, respectively, of discounts on note payable as interest expense.

Outstanding warrants from all sources have terms ranging from two to five years with certain of the warrants carrying registration rights of the underlying shares of common stock. The number of shares of common stock subject to exercise and the exercise price of all options and warrants outstanding at March 31, 2013 is as follows:

Shares Outstanding		Weighted Average Exercise Price	Shares Vested	Expiration Fiscal Period
2,805,600	$	1.45	2,805,600	4th Qtr, 2013
40,000		0.01	40,000	3rd Qtr, 2014
200,000		1.25	200,000	4th Qtr, 2014
108,500		0.40	108,500	1st Qtr, 2015
104,000		0.19	104,000	2nd Qtr. 2015
10,000		0.19	10,000	3rd Qtr. 2015
30,000		0.53	30,000	4th Qtr, 2016
50,000		0.50	50,000	1st Qtr, 2017
50,000		0.50	50,000	2nd Qtr. 2017
1,079,000		0.55	803,265	4th Qtr, 2021
125,000		0.53	46,872	1st Qtr, 2022
35,000		0.53	12,395	2nd Qtr, 2022
1,462		3.25	1,462	3rd Qtr, 2022
52,000		0.75	-	1st Qtr, 2023
4,690,562			4,262,094	

Stock based compensation

Results of operations for the three and nine months ended March 31, 2013 include share based compensation costs totaling $37,161 and $142,191, respectively, charged to selling, general and administrative expenses. For purposes of accounting for stock based compensation, the fair value of each option and warrant award is estimated on the date of grant using the Black-Scholes-Merton option pricing formula. The following weighted average assumptions were used for the calculations during the three months ended March 31, 2013:

Expected life (in years)	3.74 years	
Weighted average volatility	135.89	%
Forfeiture rate	20.00	%
Risk-free interest rate	1.06	%
Expected dividend rate	-	%

TABLE OF CONTENTS

Sugarmade, Inc. and Subsidiary
Notes to Unaudited Condensed Consolidated Financial Statements
March 31, 2013

The weighted average expected option and warrant term for director and employee stock options granted reflects the application of the simplified method set out in SEC Staff Accounting Bulletin No. 110. The simplified method defines the life as the average of the contractual term of the options and the weighted average vesting period for all options. We utilized this approach as our historical share option exercise experience does not provide a reasonable basis upon which to estimate an expected term. Expected volatilities are based on the historical volatility of our stock as well as those of a peer group. We estimated the forfeiture rate based on our expectation for future forfeitures and we currently expect substantially all options and warrants to vest. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield in effect at or near the time of grant. We have never declared or paid dividends and have no plans to do so in the foreseeable future.

As of March 31, 2013, $297,822 of unrecognized compensation cost related to unvested stock based compensation arrangements is expected to be recognized over a weighted-average remaining period of 4.36 months. The following is required disclosure in connection with stock options and warrants (which resulted in share based compensation charges) as of March 31, 2013: 1) weighted average exercise price - $0.77; 2) weighted average remaining contractual term vested and outstanding options – 55.5 and 63.3 months, respectively; 3) aggregate intrinsic value of outstanding and exercisable options and warrants - $––––––298,900 and $216,079, respectively; 4) weighted average grant date fair value of options and warrants granted - $0.26 per share; and 5) weighted average fair value of options and warrants vested - $0.26 per share.

On September 6, 2012, our Company's Board of Directors approved the repricing of options and warrants granted to employees, active consultants and board members. The repriced options and warrants had exercise prices ranging from $1.25 to $3.73. A total of 1,245,000 options and warrants were amended to reduce the exercise price to $0.52 per share, based on the most recent closing price for our Company's common stock, which is deemed the fair market value as of that date. As a result of the repriced options and warrants, our company will be incurring additional stock based compensation totaling $31,450, recognized in the current and future periods over the remaining vesting periods related to the respective securities. For the three and nine months ended March 31, 2013, we recorded additional stock based compensation expense totaling $2,245 and $18,348, respectively, related to the repriced options and warrants.

The exercise prices for options and warrants granted and outstanding which resulted in stock based compensation charges was as follows at March 31, 2013:

	Exercise Price Range	Number of options or warrants
$	0.25 - $0.50	100,000
$	0.51 – $0.75	1,297,000
$	0.76 - $1.00	-
$	1.01 - $1.25	624,000
$	1.26 - $2.00	32,500
$		-

	2.01 - $3.00	
$	3.01 - $4.00	1,462
		2,054,962

A summary of the status of our non-vested options and warrants as of March 31, 2013 and changes during the three months then ended is as follows:

	Shares
Non-vested outstanding, December 31, 2012	498,675
Granted	152,000
Vested	(222,207)
Cancelled	-
Non-vested outstanding, March 31, 2013	428,468

16

TABLE OF CONTENTS

Sugarmade, Inc. and Subsidiary
Notes to Unaudited Condensed Consolidated Financial Statements
March 31, 2013

Common Shares Reserved for Future Issuance

The following table summarizes shares of our common stock reserved for future issuance at March 31, 2013:

Stock options outstanding	1,133,462
Stock options available for future grant under the 2011 Plan	366,538
Warrants	3,557,100
Total common shares reserved for future issuance	5,057,100

8. Income taxes

We currently estimate our Company's book net operating loss carryforwards ("NOL") and deferred tax asset balance to total approximately $9,257,000 and $3,731,000, respectively, as of March 31, 2013. Internal Revenue Code Section 382 and similar California rules place a limitation on the amount of taxable income that can be offset by NOL's after a change in control (generally greater than a 50% change in ownership). Transactions such as planned future sales of our common stock may be included in determining such a change in control. These factors give rise to uncertainty as to whether the net deferred tax assets are realizable. Our in NOL will begin to expire in 2024 for federal and state purposes and could be limited for use under IRC Section 382. We have recorded a valuation allowance against the entire net deferred tax asset balance due because we believe there exists a substantial doubt that we will be able to realize the benefits due to our lack of a history of earnings and due to possible limitations under IRC Section 382.

We file income tax returns in the U.S. and in the state of California with varying statutes of limitations. Our policy is to recognize interest expense and penalties related to income tax matters as a component of our provision for income taxes. There were no accrued interest and penalties associated with uncertain tax positions as of March 31, 2013. All operations are in California and the Company believes it has no tax positions which could more-likely-than not be challenged by tax authorities. We have no unrecognized tax benefits and thus no interest or penalties included in the financial statements.

9. Subsequent events

On April 22, 2013, our Company issued a convertible promissory note to an accredited investor totaling $100,000. The note has a term of 2 years, and bears interest at a rate of 15% per annum, with 5% payable in cash and the remaining 10% per annum payable in stock at the conversion rate of seventy cents per share; both on a quarterly basis. The note holder will also have the option to convert the outstanding balance into stock at any time during the term of the Note at an exercise price of seventy cents per share.

Effective April 29, 2013, our Company has appointed Clifton Leung as the Chief Executive Officer of the Company. Mr. Leung is also currently a member of the Board of Directors of the Company. In addition, Mr. Leung was the original President and CEO of the Company's wholly-owned subsidiary, Sugarmade, Inc., as a private company in 2009, prior to when the Company acquired it on May 9, 2011. Also effective April 29, 2013, Scott Lantz resigned as the Chief Executive Officer. Mr. Lantz continues in his roles as President, Chief Financial Officer and a member of the Board of Directors.

On May 9, 2013, the Company entered into a Share Cancellation Agreement with Scott Lantz pursuant to which Mr. Lantz agreed to the cancellation of 1,300,000 of his shares of Company common stock. Mr. Lantz is the President, Chief Financial Officer and a Director of the Company. In consideration for the surrender, our Company agreed to pay Mr. Lantz $130.

TABLE OF CONTENTS

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

This discussion and analysis may include statements regarding our expectations with respect to our future performance, liquidity, and capital resources. Such statements, along with any other non-historical statements in the discussion, are forward-looking. These forward-looking statements are subject to numerous risks and uncertainties, including, but not limited to, the risks and uncertainties described below in Part II, Item 1A and in our June 30, 2012 Annual Report on Form 10-K/A, amendment number 2, as well as those factors listed in other documents we file with the Securities and Exchange Commission (SEC). We do not assume an obligation to update any forward-looking statement. Our actual results may differ materially from those contained in or implied by any of the forward-looking statements in this Form 10-Q. See "SPECIAL NOTE REGARDING FORWARD LOOKING STATEMENTS" above.

Overview and Financial Condition

Discussions with respect to our Company's operations included herein refer to our operating subsidiary, Sugarmade-CA. Our Company purchased Sugarmade-CA on May 9, 2011. We have no operations other than those of Sugarmade-CA. Information with respect to our Company's nominal operations prior to the Sugarmade Acquisition is not included herein.

Results of Operations

Revenues

Our Company had revenues totaling $51,645 and $165,569 for the three and nine months ended March 31, 2013, respectively, compared to $84,498 and $123,996, respectively, for the three and nine months ended March 31, 2012. The comparative periods in the prior year reflected sales to customers that later received credits in the fourth quarter of 2012 as a result of quality issues with our paper. The first three quarters of fiscal 2013 reflected building sales as new and replacement product was received into the U.S. During the fourth quarter of fiscal 2012, we became aware of quality issues surrounding our copy paper products. We were able to trace the reported problems with paper quality back to manufacturing issues with our third party contract manufacturer. Our Company has since implemented additional quality assurance procedures both during and at the completion of the production processes and believes that all known issues have been addressed. As a result of the production difficulties, we issued full refunds to our customers during the prior year and have replaced our customer's product supplies. For the three months ended March 31, 2013, we sold the remaining sub-quality paper to a third party wholesaler specializing in the liquidation of excess inventory. This sale represented approximately 18% of our revenue for the quarter.

Cost of goods sold

For the three and nine months ended March 31, 2013, our Company reported cost of goods sold totaling $36,161 and $152,013, respectively, inclusive of a provision for inventory obsolescence of $40,851 for the nine months ended March 31, 2013. The provision was recorded after we completed our full assessment of all remaining product with our customers. This process was completed in the second quarter of fiscal 2013. Cost of goods sold for material and freight costs reflect sub-quality product sold to a third party wholesaler which was fully reserved, resulting in a zero cost of goods sold for this product. Excluding the effects of the fully reserved product, cost of goods sold reflected higher than normal freight charges due to industry surcharges assessed by the shipping carriers to companies using their ocean freight services. As we ship our product from China, these surcharges negatively impact our profit margins. We are managing our freight costs closely in an attempt mitigate some of these costs by using pre-purchased freight, alternative routes and /or longer lead times. Cost of goods sold for the three and nine months ended March 31, 2012 totaled $69,207 and $82,589, reflecting costs correlating to the increasing sales during the period.

Gross margin (loss)

Gross margin was $15,484 and $13,556 for the three and nine months ended March 31, 2013, respectively. For the third quarter of fiscal 2013, gross margin included the positive impact of sales of fully reserved product to a third party wholesaler. Without the benefit of these sales, gross margin as a percentage of sales would have been 14.6% as compared to the current margins of 29.9%. For the nine months ended March 31, 2013, the margin was impacted negatively due to the provision for inventory obsolesces on the remaining inventory from the sub-quality production in fiscal 2012. Higher margins for the nine months ended March 31, 2012 related to the sales of previously written off inventory.

TABLE OF CONTENTS

Selling, general and administrative expenses

For the three and nine months ended March 31, 2013, selling, general and administrative expenses totaled $327,870 and $1,442,549 respectively, compared to $634,962 and $3,246,786 for the three and nine months ended March 31, 2012. The third fiscal quarter and year-to-date ending March 31, 2013 included non-cash related charges for stock compensation and consulting expenses of $37,161 and $240,736 respectively, compared of $115,426 and $1,775,127, respectively, for the same periods in the prior fiscal year. Payroll and related expenses including noncash items totaled $37,161 and $142,191 during the three and nine months ended March 31, 2013, respectively, compared to $328,976 and $908,677 for the three and nine months ended March 31, 2012, respectively. Consulting expenses including noncash items totaled none and $98,545 during the three and nine months ended March 31, 2013, respectively, compared to $119,135 and $1,879,680 for the three and nine months ended March 31, 2012, respectively. Legal and auditing expenses totaled $19,573 and $74,663 during the three and nine months ended March 31, 2013, respectively while legal and auditing expenses for the three and nine months ended March 31, 2012 totaled $23,263 and $97,858, respectively. In an effort to further lower our expenses, during the third quarter of fiscal 2013 we reduced our headcount by 2 more people (in addition to the 5 people in the second quarter of Fiscal 2013), resulting in a 63% headcount reduction.. For the 9 months ended March 31, 2013, we cut costs in many areas as we continued to bring down our overhead operating expenses.

Interest expense and interest income

Interest expense totaled $80,033 and $134,472, respectively, for the three and nine months ended March 31, 2013 compared to negligible amounts for the same period in 2012. The increase in interest expense resulted from the increase in our debt in the form of convertible notes and our Production line of credit. Interest expense related to the convertible notes includes the amortization of discount on the note payable, which totaled $31,661 and $53,577 for the three and nine months ended March 31, 2013, respectively. The remaining accrued interest related to the note payable for the three and nine months ended March 31, 2013 totaled $18,363 and $31,884, respectively. Interest expense related to the SCPC Production line of credit for the third quarter of Fiscal 2013 and the nine months ended March 31, 2013 totaled $25,502and $37,299, respectively.

Net loss

Net loss totaled $392,295 and $1,563,075, respectively, for the three and nine months ended March 31, 2013, compared to $625,418 and $3,219,105 respectively, for the three and nine months ended March 31, 2012. The higher losses in the prior fiscal periods related to the non-cash charges discussed above.

Liquidity and Capital Resources

We have primarily financed our operations through the sale of unregistered equity, warrants and convertible notes payable. As of March 31, 2013, our Company had cash totaling $158,335, current assets totaling $468,717 and total assets of $476,499. We had current liabilities totaling $1,281,029 and total liabilities of $1,763,063, with a negative working capital of $812,312. The increase in negative working capital resulted from the increased debt burden the company has incurred during the three quarters of fiscal 2013. Stockholders’ equity reflected a deficit of $1,286,564.

Net cash used by operating activities was $885,799 for the nine months ended March 31, 2013, a decrease of $875,026 from the comparable figure of $1,760,825 for the nine months ended March 31, 2012. The decrease of net cash flows used in operating activities resulted from our decreased net loss and the increase in our liabilities and accrued compensation costs.

For the nine months ended March 31, 2013, we did not have cash flows from investing activities, and only uses of cash activities totaling $27,143 related to furniture and equipment purchases for the nine months ended March 31, 2012l.

Net cash provided by financing activities totaled $852,034 for nine months ended March 31, 2013 as compared to $659,260 for the first nine months of fiscal 2012. The net cash provided by financing activities for the period was mainly attributable to proceeds from the issuances of notes payable and convertible notes payables, as well as the funds provided by the SCPC production line of credit.

On October 1, 2012, our Company obtained a production line of credit line from Norco Sourcing (Hong Kong) Company Ltd (“Norco”) that allows our Company to draw up to $3 million dollars on the line. One of our directors, Clifton Leung, has a forty-five percent (45%) ownership interest in Norco. The line of credit will bear interest at 9% per annum. If we were to draw the maximum amount on the line, our Company would have to issue 300,000 shares of Common stock and warrants to purchase 300,000 shares of the Company’s common stock at an exercise price of $0.01 per share. The line of credit constitutes an oral agreement between Norco and the Company and has not been memorialized in a written agreement executed between the parties. The Company has not received any funds under the line of credit as of the date of this report.

TABLE OF CONTENTS

Our capital requirements going forward will consist of financing our operations until we are able to reach a level of revenues and gross margins adequate to equal or exceed our ongoing operating expenses. Other than the notes payable discussed above, borrowings from our bank and the production credit facility with our suppliers, we do not have any credit agreement or source of liquidity immediately available to us.

Given estimates of our Company's future operating results and our credit arrangements with our suppliers, we are currently forecasting that we will need to secure additional financing to obtain adequate financial resources to reach profitability. As of the date of this report, we estimate that the cash necessary to implement our current business plan for the next twelve months is approximately $1,500,000. This amount does not include funds for the production of our paper products which we expect to be satisfied by our production line of credit. Similarly, the funds from the production line of credit cannot be used for operational needs. As of March 31, 2013, we had a cash balance of approximately $158,335. However, we cannot provide any assurances that we will be able to raise additional funds to meet our cash needs; that the cash required to implement our current plan will not exceed our estimated amount of $1,500,000; or that we can achieve profitability with the estimated amounts we determined above, or that we will ever achieve profitability. We also cannot provide any assurances that we will be able to receive additional funds under our production line of credit.

Based on our need to raise additional funds to implement our business plans for the next twelve months, we have included a discussion concerning the presentation of our financial statements on a going concern basis in the notes to our financial statements and our independent public accountants have included a similar discussion in their opinion on our financial statements through June 30, 2012. We will be required in the near future to issue debt or sell our Company's equity securities in order to raise additional cash, although there are no firm arrangements in place for any such financing at this time. We cannot provide any assurances as to whether we will be able to secure the necessary financing, or the terms of any such financing transaction if one were to occur. The failure to secure such financing could severely curtail our plans for future growth or in more severe scenarios, the continued operations of our Company.

Capital Expenditures

Our current plans do not call for our Company to expend significant amounts for capital expenditures for the foreseeable future beyond relatively insignificant expenditures for office furniture and information technology related equipment as we add employees to our Company. We are however continually evaluating the production processes of our third party contract manufacturers to determine if there are investments we could make in their processes to achieve manufacturing improvements and significant cost savings. Any such desired investments would require additional cash above our current forecast requirements.

Critical Accounting Policies Involving Management Estimates and Assumptions

Please see the notes to our financial statements.

ITEM 3 – QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Intentionally omitted pursuant to Item 305(e) of Regulation S-K.

TABLE OF CONTENTS

ITEM 4 – CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

We maintain disclosure controls and procedures and internal controls that are designed to provide reasonable assurance that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized, and reported within the time periods specified in the Securities and Exchange Commission's rules and forms and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures and internal controls, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable, and not absolute, assurance of achieving the desired control objectives. In reaching a reasonable level of assurance, management necessarily was required to apply its judgment in evaluating the cost benefit relationship of possible controls and procedures and internal controls. Our disclosure controls and procedures are designed to provide reasonable assurance of achieving their objectives.

As required by the Securities and Exchange Commission Rule 13a-15(e) and Rule 15d-15(e), we carried out an evaluation, under the supervision of and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this report. Based on the foregoing, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective at the reasonable assurance level.

Changes in Internal Controls over Financial Reporting

There have not been any changes in our internal controls over financial reporting during the quarter ended March 31, 2013 that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

TABLE OF CONTENTS

PART II

ITEM 1 – LEGAL PROCEEDINGS

From time to time and in the course of business, we may become involved in various legal proceedings seeking monetary damages and other relief. The amount of the ultimate liability, if any, from such claims cannot be determined. However, in the opinion of our management, there are no legal claims currently pending or threatened against us that would be likely to have a material adverse effect on our financial position, results of operations or cash flows.

ITEM 1A – RISK FACTORS

Investment in our common stock involves a high degree of risk. You should carefully consider the risks described below together with all of the other information included in this herein before making an investment decision. If any of the following risks actually occur, our business, financial condition or results of operations could suffer. In that case, the market price of our common stock could decline, and you may lose all or part of your investment. You should also read the section entitled "Special Notes Regarding Forward-Looking Statements" below for a discussion of what types of statements are forward-looking statements as well as the significance of such statements in the context of this report.

RISKS RELATED TO OUR BUSINESS

We have a very limited operating history. Prior to the Sugarmade Acquisition, our Company was a “shell” company with no or nominal operations. Sugarmade-CA recently completed its funding and the related acquisition with our Company. Sugarmade-CA was formed in 2009 to market paper products manufactured from tree-free materials. Sugarmade-CA does not currently have significant operating revenues and has a very limited operating history. Because Sugarmade-CA has a limited operating history, we do not have any historical financial data upon which to base planned operations.

The segments of the paper industry in which we operate are highly competitive and increased competition could affect our sales and profitability. We compete in different markets within the paper industry on the basis of the uniqueness of our products, the quality of our products, customer service, price and distribution. All of our markets are highly competitive. Our competitors vary in size and many have greater financial and marketing resources than we do. While we believe that our products offer unique advantages because of their tree-free composition, if we cannot maintain quality and pricing that are comparable to traditional products we may not be able to develop, or may lose, market share. In some of our markets, the industry’s capacity to make products exceeds current demand levels. Competitive conditions in some of our segments may cause us to incur lower net selling prices, reduced gross margins and net earnings.

Our tree-free products could encounter low consumer acceptance in our primary target markets, including our initial target market of North America. The tree-free paper market in North America is relatively young with little publically available data on the size of the market in relation to the overall paper industry. There is only anecdotal data referencing the growing demand in the United States and abroad for paper products from tree-free sources. Our product is relatively new to consumers and does not have a significant sales history in many of our target markets. Should our tree-free products not be accepted by consumers in these markets, particularly in the markets of our initial focus in North America, we could experience sales and operating results substantially less than we expect to achieve. Such results could jeopardize our Company’s financial well-being and subject an investor to the loss of all or a portion of his investment in our Company.

Our business and financial performance may be adversely affected by downturns in the target markets that we serve or reduced demand for the types of products we sell. Demand for our products is often affected by general economic conditions as well as product-use trends in our target markets. These changes may result in decreased demand for our products. The occurrence of these conditions is beyond our ability to control and, when they occur, they may have a significant impact on our sales and results of operations. Our products are comparably priced with paper products comprised of 30% recycled materials. Both our products and paper products comprised of 30% recycled materials are typically higher in cost than paper products made from virgin pulp wood. The inability or unwillingness of our customers to pay a premium for our products due to general economic conditions or a downturn in the economy may have a significant adverse impact on our sales and results of operations.

Changes within the paper industry may adversely affect our financial performance. Changes in the identity, ownership structure and strategic goals of our competitors and the emergence of new competitors in our target markets may harm our financial performance. New competitors may include foreign-based companies and commodity-based domestic producers who could enter our specialty markets if they are unable to compete in their traditional markets. The paper industry has also experienced consolidation of producers and distribution channels. Further consolidation could unite other producers with distribution channels through which we intend to sell our products, thereby limiting access to our target markets.

TABLE OF CONTENTS

Any interruption in delivery from our suppliers will impair our ability to distribute our products and generate revenues. We are dependent on third party contract manufacturers for the production of our products. We have no manufacturing facilities and we rely on third party contract manufacturers to provide us with an adequate and reliable supply of products on a timely basis. Any interruption in the distribution from these suppliers could affect our ability to distribute our products. Additionally, our suppliers are located in the People's Republic of China ("PRC"). Any legislation or consumer preferences in the United States or other countries requiring products which are made in the United States or such other countries may have a material adverse impact on our sales and results of operations.

Uncertainties with respect to the PRC legal system could limit the legal protections available for us to pursue any claim against our third party contract manufacturers, and therefore our ability to protect our contract rights. We rely on third party contract manufacturers for our supply of products. These third party suppliers operate entirely within the PRC. The PRC legal system continues to rapidly evolve, the interpretations of many laws, regulations and rules are not always uniform and enforcement of these laws, regulations and rules involve uncertainties, which may limit legal protections available to us in the event that we needed to bring a claim against our suppliers. Courts in the PRC may recognize and enforce foreign judgments in accordance with the requirements of the PRC Civil Procedures Law based on treaties between China and the country where the judgment is made or on reciprocity between jurisdictions. The PRC does not have any treaties or other arrangements that provide for the reciprocal recognition and enforcement of foreign judgments with the United States. So it is uncertain whether a PRC court would enforce a judgment rendered by a court in the United States. Any litigation we may try to bring in the PRC may be protracted and result in substantial costs and diversion of resources and management attention.

If we fail to maintain satisfactory relationships with our larger customers, our business may be harmed. We do not have and are unlikely to enter into long-term fixed quantity supply agreements with our customers. Due to competition or other factors, we could lose future business from our customers, either partially or completely. Additionally, during our last fiscal year we produced certain batches of paper which did not meet the quality standards required by our customers which resulted in dissatisfaction by those customers. This dissatisfaction may have also harmed our reputation and ability to sell our products to those customers and other customers in the future. The future loss of one or more of our significant customers or a substantial future reduction of orders by any of our significant customers, or the unwillingness of a customer to purchase our products again due to concerns over the quality of the paper they previously purchased could harm our business and results of operations. Moreover, our customers may vary their order levels significantly from period to period and customers may not continue to place orders with us in the future at the same levels as in prior periods. In the event that in the future we lose any of our larger customers, we may not be able to replace that revenue source. This could harm our financial results.

The costs of complying with environmental regulations may increase substantially and adversely affect our consolidated financial condition, liquidity or results of operations. Our Company's third party contract manufacturers are subject to various environmental laws and regulations that govern discharges into the environment and the handling and disposal of hazardous substances and wastes. Environmental laws impose liabilities and clean-up responsibilities for releases of hazardous substances into the environment. However, many PRC laws and regulations are uncertain in their scope, and the implementation of such laws and regulations in different localities could have significant differences. In certain instances, local implementation rules and/or the actual implementation are not necessarily consistent with the regulations at the national level. We cannot assure you that the relevant PRC government authorities will not determine that our suppliers have failed to comply with certain laws or regulations. Our Company's suppliers will likely continue to incur substantial capital and operating expenses in order to comply with current laws. Any future changes in these laws or their interpretation by government agencies or the courts may significantly increase our suppliers' capital expenditures and operating expenses and decrease the amount of funds available for investment in other areas of their operations. In addition, our Company's suppliers may be required to eliminate or mitigate any adverse effects on the environment caused by the release of hazardous materials, whether or not SCPC's suppliers had knowledge of or were responsible for such release. Our suppliers may also incur liabilities for personal injury and property damages as a result of discharges into the environment. If costs or liabilities related to environmental compliance increase significantly for our suppliers, such costs could be passed along to us in the form of higher prices paid for supplied materials. Our consolidated financial condition, liquidity or results of operations may be adversely affected in the event that we were forced to absorb such costs.

If our third party contract manufacturers were to suffer a catastrophic loss, unforeseen or recurring operational problems at any of its facilities, we could suffer significant product shortages, sales declines and/or cost increases. The paper making and converting facilities of our third party suppliers as well as their distribution warehouses could suffer catastrophic loss due to fire, flood, terrorism, mechanical failure or other natural or human caused events. If any of these facilities were to experience a catastrophic loss, it could disrupt our supply of products for sale, delay or reduce shipments and reduce our revenues. These expenses and losses may not be adequately covered by property or business interruption insurance. Even if covered by insurance, our inability to deliver our products to customers, even on a short-term basis, may cause us to lose market share on a more permanent basis.

Our ability to protect the intellectual property and proprietary technology related to the production of our products is uncertain. Our future success may depend on our ability to protect the proprietary rights and the intellectual property upon which our tree-free products are based. SCPC holds several patents in the People's Republic of China related to the production of tree-free paper, and under the terms of our supply agreement with SCPC, we have the right to request SCPC to file for counterpart patent protection in Sugarmade's territories and for copyright protection for the name "Sugarmade," but we have not yet made such requests. Should we make such a request to SCPC, any patent applications may not be issued as patents, or may not be issued in a form that will be advantageous to us, or we may not be able to obtain copyright protection for the name "Sugarmade". Additionally, our Company is in the process of applying for a provisional patent in the US to protect its new formulation and process for its most recent tree free pulp and paper product. The provisional patent application which the Company plans to file is intended to allow us to establish an early effective filing date with the United States Patent and Trademark Office (USPTO) for the filing of the planned final non-provisional patent for our paper product. However, we may not be able to file the provisional patent application or the planned final non-provisional patent for our paper product. Additionally, any patents obtained in the future may be challenged by re-examination or otherwise invalidated or eventually be found unenforceable. Both the patent application process and the process of managing patent disputes can be time consuming and expensive. Even if any patents were to be granted, competitors may attempt to challenge or invalidate the patents, or may be able to design alternative techniques or devices that avoid infringement of the patents, or develop products with functionalities that are comparable to the tree-free products which we sell. In the event a competitor infringes upon our intellectual property rights, litigation to enforce such rights or to defend patents granted (or to be granted) against challenge, even if successful, could be expensive and time consuming and could require significant time and attention from our management. We may not have sufficient resources to enforce our intellectual property rights.

We may become involved in claims concerning intellectual property rights, and we could suffer significant litigation or related expenses in defending our or SCPC's intellectual property rights or defending claims that we infringed the rights of others. We consider our licensed intellectual property to be a material asset. We may lose market share and suffer a decline in our revenue and net earnings if we cannot successfully defend one or more trademarks or patents we have secured or licensed. We do not believe that any of our products infringe the valid intellectual property rights of third parties. However, we may be unaware of intellectual property rights of others that may cover some of our products or services. In that event, we may be subject to significant future claims for damages. Any litigation regarding patents or other intellectual property could be costly and time-consuming and could divert our management and key personnel from our business operations. Claims of intellectual property infringement might also require us to enter into licensing agreements which would reduce our operating margins, or in some cases, we may not be able to obtain license agreements on terms acceptable to us.

FINANCIAL RISKS

Our current business plan requires that our Company raise additional equity by the end of fiscal year 2013. We do not currently have sufficient revenues to cover our operating expenses and have never been profitable. We cannot be certain that our Company will ever generate sufficient revenues and gross margin to achieve profitability in the future. Our business plan requires that our Company needs to raise additional equity by the end of our 2013 fiscal year end.

However, there are no arrangements in place for any such financing at this time. We cannot provide any assurances as to whether we will be able to secure any necessary financing, or the terms of any such financing transaction if one were to occur. Our failure to raise additional capital would seriously harm our business and operating results. If we fail to raise additional capital by the end of fiscal 2013, our business will be materially and adversely affected and an investor could suffer the loss of a significant portion or all of his investment in our Company.

If we cannot establish profitable operations, we will need to raise additional capital to continue our operations, which may not be available on commercially reasonable terms, or at all, and which may dilute your investment. We incurred a net loss for the nine months ended March 31, 2013 in excess of $1,563,000 and had negative cash flows from operations of nearly of $886,000. For the nine months ended March 31, 2012 we incurred a net loss in excess of $3,219,000 and had negative cash flows from operations of nearly $1,761,000. Achieving and sustaining profitability will require us to increase our revenues and manage our product, operating and administrative expenses. We cannot guarantee that we will be successful in achieving profitability. If we are unable to generate sufficient revenues to pay our expenses and our existing sources of cash and cash flows are otherwise insufficient to fund our activities, we will need to raise additional funds to continue our operations. We do not have any arrangements in place for additional funds. If needed, those funds may not be available on favorable terms, or at all. Furthermore, if we issue equity or debt securities to raise additional funds, our existing stockholders may experience dilution, and the new equity or debt securities may have rights, preferences and privileges senior to those of our existing stockholders. If we are unsuccessful in achieving profitability and we cannot obtain additional funds on commercially reasonable terms or at all, we may be required to curtail significantly or cease our operations, which could result in the loss of all of your investment in our stock.

TABLE OF CONTENTS

We are dependent upon our production credit borrowing arrangement with SCPC and Norco Sourcing (Hong Kong) Co. Ltd in order to fund our working capital and liquidity requirements. We have signed an agreement with SCPC, and have secured a verbal agreement for a line of credit with Norco Sourcing (Hong Kong) Co. Ltd (“Norco”), to provide our Company with credit facilities to fund the production of our paper products. Our plans going forward are dependent upon SCPC and Norco in providing such financing upon the terms we have agreed to and there are currently no other alternate financing plans in place. Should there be an interruption in either SCPC’s or Norco willingness or ability to provide such financing per the terms of the agreements, we could face a severe liquidity shortfall that could cause our Company’s operations to fail and which could consequently result in the loss of an investor’s investment with our Company.

We may not have the ability to pay our convertible notes when due. Between August 17, 2012 and March 31, 2013, our Company has issued convertible promissory notes totaling $525,000 which must be repaid by our Company within 9 months after their date of issuance. Our Company does not have sufficient capital to repay the notes as of the date of this report, and may not have sufficient capital to repay the notes when due. Our Company is in discussions with several of the note holders to obtain an extension on the due date, or to have the note holders convert their balances into shares of Company common stock. Our Company’s inability to obtain an extension on the due date from the note holders, or our inability to repay the notes when due, would permit the noteholders to exercise their default remedies against our Company which could have a material adverse effect on our Company.

Conversion of our convertible notes into common stock could result in additional dilution to our stockholders. Upon satisfaction of certain conversion conditions (including conditions outside of our control, such as the closing of a financing), the notes may be converted into shares of Company common stock by the noteholders. If shares of our common stock are issued due to conversion of some or all of the convertible notes, the ownership interests of existing stockholders would be diluted.

Our financial statements have been prepared assuming that our Company will continue as a going concern. We have generated losses to date and have limited working capital. These factors raise substantial doubt about our ability to continue as a going concern. Our financial statements do not include any adjustments that might result from this uncertainty. The report of our independent registered public accounting firm included an explanatory paragraph expressing substantial doubt about our ability to continue as a going concern in their recent audit report for the fiscal year ended June 30, 2012. If we cannot generate the required revenues and gross margin to achieve profitability or obtain additional capital on acceptable terms, we will need to substantially revise our business plan or cease operations and an investor could suffer the loss of a significant portion or all of his investment in our Company.

Fluctuations in exchange rates could adversely affect our cost of goods sold and consequently our profit margins. The price we pay for product from our third party suppliers in China will be directly affected by the foreign exchange rate between U.S. dollars and the Chinese Renminbi ("RMB") and between those currencies and other currencies in which our sales may be denominated. Because substantially all of our product purchases will be from our suppliers in China, fluctuations in the exchange rate between the U.S. dollar and the RMB will affect the prices that we effectively pay for product. Since July 2005, the RMB has no longer been pegged to the U.S. dollar. Although the People's Bank of China regularly intervenes in the foreign exchange market to prevent significant short-term fluctuations in the exchange rate, the RMB may appreciate or depreciate significantly in value against the U.S. dollar in the medium to long term. Moreover, it is possible that in the future PRC authorities may lift restrictions on fluctuations in the RMB exchange rate and lessen intervention in the foreign exchange market. Very limited hedging transactions are available in China to reduce our exposure to exchange rate fluctuations. To date, we have not entered into any hedging transactions. While we may enter into hedging transactions in the future, the availability and effectiveness of these transactions may be limited, and we may not be able to successfully hedge our exposure at all.

As we transition from a Company with insignificant revenues to what we hope will be a Company generating substantial revenues, we may not be able to manage our growth effectively, which could adversely affect our operations and financial performance. The ability to manage and operate our business as we execute our growth strategy will require effective planning. Significant rapid growth could strain our internal resources, leading to a lower quality of customer service, reporting problems and delays in meeting important deadlines resulting in loss of market share and other problems that could adversely affect our financial performance. Our efforts to grow could place a significant strain on our personnel, management systems, infrastructure and other resources. If we do not manage our growth effectively, our operations could be adversely affected, resulting in slower growth and a failure to achieve or sustain profitability.

TABLE OF CONTENTS

We do not expect to pay dividends for the foreseeable future, and we may never pay dividends and, consequently, the only opportunity for investors to achieve a return on their investment is if a trading market develops and investors are able to sell their shares for a profit or if our business is sold at a price that enables investors to recognize a profit. We currently intend to retain any future earnings to support the development and expansion of our business and do not anticipate paying cash dividends for the foreseeable future. Our payment of any future dividends will be at the discretion of our Board of Directors after taking into account various factors, including but not limited to our financial condition, operating results, cash needs, growth plans and the terms of any credit agreements that we may be a party to at the time. In addition, our ability to pay dividends on our common stock may be limited by state law. Accordingly, we cannot assure investors any return on their investment, other than in connection with a sale of their shares or a sale of our business. At the present time there is a limited trading market for our shares. Therefore, holders of our securities may be unable to sell them. We cannot assure investors that an active trading market will develop or that any third party will offer to purchase our business on acceptable terms and at a price that would enable our investors to recognize a profit.

Our net operating loss (“NOL”) carry-forward is limited. We have recorded a valuation allowance amounting to our entire net deferred tax asset balance due to our lack of a history of earnings, possible statutory limitations on the use of tax loss carry-forwards generated in the past and the future expiration of our NOL. This gives rise to uncertainty as to whether the net deferred tax asset is realizable. Internal Revenue Code Section 382, and similar California rules, place a limitation on the amount of taxable income that can be offset by carry-forwards after a change in control (generally greater than a 50% change in ownership). As a result of these provisions, it is likely that given our acquisition of Sugarmade-CA, future utilization of the NOL will be severely limited. Our inability to use our Company’s historical NOL, or the full amount of the NOL, would limit our ability to offset any future tax liabilities with its NOL.

CORPORATE AND OTHER RISKS

Limitations on director and officer liability and indemnification of our Company’s officers and directors by us may discourage stockholders from bringing suit against an officer or director. Our Company’s certificate of incorporation and bylaws provide, with certain exceptions as permitted by governing state law, that a director or officer shall not be personally liable to us or our stockholders for breach of fiduciary duty as a director, except for acts or omissions which involve intentional misconduct, fraud or knowing violation of law, or unlawful payments of dividends. These provisions may discourage stockholders from bringing suit against a director for breach of fiduciary duty and may reduce the likelihood of derivative litigation brought by stockholders on our behalf against a director.

We are responsible for the indemnification of our officers and directors. Should our officers and/or directors require us to contribute to their defense, we may be required to spend significant amounts of our capital. Our certificate of incorporation and bylaws also provide for the indemnification of our directors, officers, employees, and agents, under certain circumstances, against attorney's fees and other expenses incurred by them in any litigation to which they become a party arising from their association with or activities on behalf of our Company. This indemnification policy could result in substantial expenditures, which we may be unable to recoup. If these expenditures are significant, or involve issues which result in significant liability for our key personnel, we may be unable to continue operating as a going concern.

Our executive officers, directors and insider stockholders beneficially own or control a substantial portion of our outstanding common stock, which may limit your ability and the ability of our other stockholders, whether acting alone or together, to propose or direct the management or overall direction of our Company. Additionally, this concentration of ownership could discourage or prevent a potential takeover of our Company that might otherwise result in an investor receiving a premium over the market price for his shares. A substantial portion of our outstanding shares of common stock is beneficially owned and controlled by a group of insiders, including our directors and executive officers. Accordingly, any of our existing outside principal stockholders together with our directors, executive officers and insider shareholders would have the power to control the election of our directors and the approval of actions for which the approval of our stockholders is required. If you acquire shares of our common stock, you may have no effective voice in the management of our Company. Such concentrated control of our Company may adversely affect the price of our common stock. Our principal stockholders may be able to control matters requiring approval by our stockholders, including the election of directors, mergers or other business combinations. Such concentrated control may also make it difficult for our stockholders to receive a premium for their shares of our common stock in the event we merge with a third party or enter into different transactions which require stockholder approval. These provisions could also limit the price that investors might be willing to pay in the future for shares of our common stock.

Certain provisions of our Certificate of Incorporation may make it more difficult for a third party to effect a change-of-control. Our certificate of incorporation authorizes the Board of Directors to issue up to 10,000,000 shares of preferred stock. The preferred stock may be issued in one or more series, the terms of which may be determined at the time of issuance by the Board of Directors without further action by the stockholders. These terms may include preferences as to dividends and liquidation, conversion rights, redemption rights and sinking fund provisions. The issuance of any preferred stock could diminish the rights of holders of our common stock, and therefore could reduce the value of such common stock. In addition, specific rights granted to future holders of preferred stock could be used to restrict our ability to merge with, or sell assets to, a third party. The ability of the Board of Directors to issue preferred stock could make it more difficult, delay, discourage, prevent or make it more costly to acquire or effect a change-in-control, which in turn could prevent our stockholders from recognizing a gain in the event that a favorable offer is extended and could materially and negatively affect the market price of our common stock.

TABLE OF CONTENTS

We are dependent for our success on a few key executive officers. Our inability to retain those officers would impede our business plan and growth strategies, which would have a negative impact on our business and the value of your investment. Our success depends on the skills, experience and performance of key members of our management team. Each of those individuals may voluntarily terminate his employment with our Company at any time. Were we to lose one or more of these key executive officers, we would be forced to expend significant time and money in the pursuit of a replacement, which would result in both a delay in the implementation of our business plan and the diversion of limited working capital. We do not maintain a key man insurance policy on any of our executive officers.

CAPITAL MARKET RISKS

Our common stock is thinly traded, so you may be unable to sell at or near ask prices or at all if you need to sell your shares to raise money or otherwise desire to liquidate your shares. There is limited market activity in our stock and we are too small to attract the interest of many brokerage firms and analysts. We cannot give you any assurance that a broader or more active public trading market for our common stock will develop or be sustained. While we are trading on OTCMarkets, the trading volume we will develop may be limited by the fact that many major institutional investment funds, including mutual funds, as well as individual investors follow a policy of not investing in OTC stocks and certain major brokerage firms restrict their brokers from recommending OTC stocks because they are considered speculative, volatile, thinly traded and the market price of the common stock may not accurately reflect the underlying value of our Company. The market price of our common stock could be subject to wide fluctuations in response to quarterly variations in our revenues and operating expenses, announcements of new products or services by us, significant sales of our common stock, including “short” sales, the operating and stock price performance of other companies that investors may deem comparable to us, and news reports relating to trends in our markets or general economic conditions.

The application of the “penny stock” rules to our common stock could limit the trading and liquidity of the common stock, adversely affect the market price of our common stock and increase your transaction costs to sell those shares. As long as the trading price of our common stock is below $5 per share, the open-market trading of our common stock will be subject to the “penny stock” rules, unless we otherwise qualify for an exemption from the “penny stock” definition. The “penny stock” rules impose additional sales practice requirements on certain broker-dealers who sell securities to persons other than established customers and accredited investors (generally those with assets in excess of $1,000,000 or annual income exceeding $200,000 or $300,000 together with their spouse). These regulations, if they apply, require the delivery, prior to any transaction involving a penny stock, of a disclosure schedule explaining the penny stock market and the associated risks. Under these regulations, certain brokers who recommend such securities to persons other than established customers or certain accredited investors must make a special written suitability determination regarding such a purchaser and receive such purchaser’s written agreement to a transaction prior to sale. These regulations may have the effect of limiting the trading activity of our common stock, reducing the liquidity of an investment in our common stock and increasing the transaction costs for sales and purchases of our common stock as compared to other securities. The stock market in general and the market prices for penny stock companies in particular, have experienced volatility that often has been unrelated to the operating performance of such companies. These broad market and industry fluctuations may adversely affect the price of our stock, regardless of our operating performance. Stockholders should be aware that, according to Securities and Exchange Commission (“SEC”) Release No. 34-29093, the market for penny stocks has suffered in recent years from patterns of fraud and abuse. Such patterns include 1) control of the market for the security by one or a few broker-dealers that are often related to the promoter or issuer; 2) manipulation of prices through prearranged matching of purchases and sales and false and misleading press releases; 3) boiler room practices involving high-pressure sales tactics and unrealistic price projections by inexperienced sales persons; 4) excessive and undisclosed bid-ask differential and markups by selling broker-dealers; and 5) the wholesale dumping of the same securities by promoters and broker-dealers after prices have been manipulated to a desired level, along with the resulting inevitable collapse of those prices and with consequent investor losses. The occurrence of these patterns or practices could increase the volatility of our share price.

We may not be able to attract the attention of major brokerage firms, which could have a material adverse impact on the market value of our common stock. Security analysts of major brokerage firms may not provide coverage of our common stock since there is no incentive to brokerage firms to recommend the purchase of our common stock. The absence of such coverage limits the likelihood that an active market will develop for our common stock. It will also likely make it more difficult to attract new investors at times when we require additional capital.

TABLE OF CONTENTS

We may be unable to list our common stock on NASDAQ or on any securities exchange. Although we may apply to list our common stock on NASDAQ or the American Stock Exchange in the future, we cannot assure you that we will be able to meet the initial listing standards, including the minimum per share price and minimum capitalization requirements, or that we will be able to maintain a listing of our common stock on either of those or any other trading venue. Until such time as we qualify for listing on NASDAQ, the American Stock Exchange or another trading venue, our common stock will continue to trade on OTC Markets or another over-the-counter quotation system where an investor may find it more difficult to dispose of shares or obtain accurate quotations as to the market value of our common stock. In addition, rules promulgated by the SEC impose various practice requirements on broker-dealers who sell securities that fail to meet certain criteria set forth in those rules to persons other than established customers and accredited investors. Consequently, these rules may deter broker-dealers from recommending or selling our common stock, which may further affect the liquidity of our common stock. It would also make it more difficult for us to raise additional capital.

Future sales of our equity securities could put downward selling pressure on our securities, and adversely affect the stock price. There is a risk that this downward pressure may make it impossible for an investor to sell his or her securities at any reasonable price, if at all. Future sales of substantial amounts of our equity securities in the public market, or the perception that such sales could occur, could put downward selling pressure on our securities, and adversely affect the market price of our common stock.

ITEM 2 –UNREGISTERED SALES OF SECURITIES AND USE OF PROCEEDS

On April 22, 2013, our Company issued a convertible promissory note to an accredited investor totaling $100,000. The note has a term of 2 years, and bears interest at a rate of 15% per annum, with 5% payable in cash and the remaining 10% per annum payable in stock at the conversion rate of seventy cents per share; both on a quarterly basis. The note holder will also have the option to convert the outstanding balance into stock at any time during the term of the Note at an exercise price of seventy cents per share. The issuance of notes and warrants to the investors was made in reliance on the exemption provided by Section 4(2) of the Securities Act of 1933, as amended (the “Securities Act”) for the offer and sale of securities not involving a public offering, and Regulation D promulgated under the Securities Act. This summary of the convertible promissory notes is qualified in its entirety by reference to the form of convertible promissory note which is attached as an exhibit to this Quarterly Report.

The Company’s reliance upon Section 4(2) of the Securities Act in issuing the securities was based upon the following factors: (a) the issuance of the securities was an isolated private transaction by us which did not involve a public offering; (b) there was only three investors; (c) there were no subsequent or contemporaneous public offerings of the securities by the Company; (d) the securities were not broken down into smaller denominations; and (e) the negotiations for the issuance of the securities took place directly between the investors and the Company.

ITEM 3 – DEFAULTS UPON SENIOR SECURITIES

Not applicable.

ITEM 4 – MINE SAFETY DISCLOSURES

None.

ITEM 5 – OTHER INFORMATION

On May 9, 2013, the Company entered into a Share Cancellation Agreement with Scott Lantz pursuant to which Mr. Lantz agreed to the cancellation of 1,300,000 of his shares of Company common stock. Mr. Lantz is the President, Chief Financial Officer and a Director of the Company. In consideration for the surrender, our Company agreed to pay Mr. Lantz $130. This summary of the Share Cancellation Agreement is qualified in its entirety by reference to the full text of the Share Cancellation Agreement which is attached as an exhibit to this Quarterly Report.

ITEM 6 – EXHIBITS

Exhibit Number	Description
10.18	Form of Convertible Promissory Note (1)
10.19	Share Cancellation Agreement with Scott Lantz dated May 9, 2013(1)
31.1	Certification pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, for Chief Executive Officer (1)
31.2	Certification pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, for Chief Financial Officer (1)
32.1	Certification pursuant to 18 U.S.C. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, for Chief Executive Officer (1)
32.2	Certification pursuant to 18 U.S.C. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, for Chief Financial Officer (1)

(1) Filed as an exhibit to this Report.

TABLE OF CONTENTS

SIGNATURES

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

	Sugarmade, Inc., a Delaware corporation	
May 13, 2013	By:	/s/ Clifton Leung Clifton Leung Chief Executive Officer and Director