LOT78, INC.
Form 10-Q
February 27, 2014

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended December 31, 2013

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

Commission File Number 000-54816

LOT78, INC.

(Exact name of registrant as specified in its charter)

Nevada	**26-2940624**
(State of incorporation)	(I.R.S. Employer Identification No.)

65 Alfred Road

Studio 209

London W2 5EU

(Address of principal executive offices)

00447801480109

(Registrant's telephone number)

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

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large Accelerated Filer	**Accelerated Filer**
Non-accelerated Filer	**Smaller Reporting Company**

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

As of February 27, 2014, there were 237,570,283 shares of the registrant's $0.001 par value common stock issued and outstanding.

LOT78, INC.*

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Special Note Regarding Forward-Looking Statements

Information included in this Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (“Securities Act”), and Section 21E of the Securities Exchange Act of 1934, as amended (“Exchange Act”). This information may involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of Lot78, Inc., formerly known as Bold Energy Inc. (the “Company”), to be materially different from future results, performance or achievements expressed or implied by any forward-looking statements. Forward-looking statements, which involve assumptions and describe future plans, strategies and expectations of the Company, are generally identifiable by use of the words “may,” “will,” “should,” “expect,” “anticipate,” “estimate,” “believe,” “intend,” or “project” or the negative of these words or other variations on these words comparable terminology. These forward-looking statements are based on assumptions that may be incorrect, and there can be no assurance that these projections included in these forward-looking statements will come to pass. Actual results of the Company could differ materially from those expressed or implied by the forward-looking statements as a result of various factors. Except as required by applicable laws, the Company has no obligation to update publicly any forward-looking statements for any reason, even if new information becomes available or other events occur in the future.

**Please note that throughout this Quarterly Report, and unless otherwise noted, the words "we," "our," "us," the "Company," or "LOTE" refers to Lot78, Inc. and its wholly owned subsidiary Lot78 UK Limited.*

<u>PART I - FINANCIAL INFORMATION</u>

ITEM 1. FINANCIAL STATEMENTS

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LOT78, INC.

CONSOLIDATED BALANCE SHEET

(unaudited)

	December 31, 2013	**September 30, 2013**
ASSETS		
Current assets:		
Cash and cash equivalents	$ 49,947	$ 274,312
Accounts receivable	85,528	132,422
Prepaid expenses and other current assets	106,490	63,735
Inventory, net	16,107	61,460
Total current assets	258,072	531,929
Property and equipment, net	3,116	3,614
Patents, net	21,964	22,457
Total assets	$ 283,152	$ 558,000
LIABILITIES AND STOCKHOLDERS' DEFICIT		
Current liabilities:		
Accounts payable and accrued liabilities	$ 274,318	$ 280,535
Accounts payable – related party	41,797	26,850
Debt due to third parties	186,314	137,156
Debt due to related parties	32,976	32,272
Derivative liabilities	192,214	434,464
Convertible debt due to shareholders	89,838	124,610
Due to shareholders	329,760	322,594
Total current liabilities	1,147,217	1,358,481
Long term debt due to shareholders	320,659	313,813
Convertible debt, net of discount of $437,458 and $437,500	12,542	12,500
Total long term liabilities	333,201	326,313
Total liabilities	$ 1,480,418	1,684,794
Stockholders' deficit		
Preferred stock, $0.001 par value per share, 10,000,000 shares authorized, none issued and outstanding	-	-
Common stock, $0.001 par value per share, 350,000,000 shares authorized, 237,570,283 and 237,403,616 shares issued and outstanding	237,570	237,404
Additional paid-in capital	877,673	865,340
Accumulated other comprehensive income (loss)	17,017	42,134
Accumulated deficit	(2,329,526)	(2,271,672)
Total stockholders' deficit	(1,197,266)	(1,126,794)
Total liabilities and stockholders' deficit	$ 283,152	558,000

The accompanying notes are an integral part of the consolidated unaudited financial statements

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LOT78, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

AND OTHER COMPREHENSIVE LOSS

(unaudited)

	Three Months Ended December 31, 2013	**Three Months Ended December 31, 2012**
Revenue, net	$ 55,730	$ 58,695
Cost of sales	69,409	75,384
Gross Loss	(13,679)	(16,689)
Expenses		
Selling, general and administrative expenses	$ 273,576	$ 124,350
Depreciation and amortization	1,531	1,034
Total expenses	275,107	125,384
Other income (expense)		
Interest expense	(11,318)	(10,401)
Gain on derivative liabilities	242,250	-
Total other income (expense)	230,932	(10,401)
Net loss	(57,854) $	$ (152,474)
Foreign currency translation adjustments	(25,118)	(57)
Comprehensive income (loss)	(82,972)	(152,531)
Basic and diluted loss per share	$ (0.00)	$ (13.24)
Weighted average shares of common stock outstanding – basic	237,477,892	11,510

The accompanying notes are an integral part of the consolidated unaudited financial statements

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LOT78, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited)

	Three months Ended December 31, 2013	**Three months Ended December 31, 2012**
Cash flows from operating activities		
Net loss	$(57,854)	$ (152,474)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation	964	77
Amortization	567	957
Gain on derivative liabilities	(242,250)	-
Debt discount amortization	42	-
Stock based compensation	12,500	-
Change in operating assets/liabilities:		
Accounts receivable	48,862	96,151
Prepaid expenses and other current assets	(40,608)	13,423
Inventory	45,840	671
Accounts payable and accrued expenses	11,293	(34,033)
Net cash provided by (used in) operating activities	(220,644)	(75,228)
Cash flows from financing activities		
Proceeds from issuance of debt	45,322	77,656
Repayment of convertible debt to shareholders	(40,573)	
Net cash flows provided by financing activities:	4,749	77,656
Effect of foreign currency on cash and cash equivalents	(8,470)	14
	$(224,365)	$2,442
Net increase (decrease) in cash		
Cash- beginning of period	274,312	-
Cash- end of period	$49,947	$ 2,442
Cash paid for interest	$1,347	$ -
Cash paid for income taxes	$-	$ -
Supplementary Non-Cash Information		
Debt discount due to derivative liabilities	-	-

The accompanying notes are an integral part of the consolidated unaudited financial statements

Lot78, Inc.

Notes to CONSOLIDATED Financial Statements

Unaudited

1. BASIS OF PRESENTATION & ORGANIZATION

Basis of presentation

The accompanying unaudited interim financial statements of Lot78, Inc. (the “Company”) have been prepared in accordance with accounting principles generally accepted in the United States of America and the rules of the Securities and Exchange Commission (“SEC”), and should be read in conjunction with the audited financial statements and notes thereto of the Company contained in Form 10-K filed with the SEC on January 21, 2014.

In the opinion of management, all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation of financial position and the results of operations for the interim periods presented have been reflected herein. The results of operations for the interim periods are not necessarily indicative of the results to be expected for the full year. Notes to the financial statements that would substantially duplicate the disclosures contained in the audited financial statements for the fiscal year ended September 30, 2013 as reported in the Company’s Form 10-K have been omitted.

Our business is subject to seasonal fluctuations. Historically, sales of our products have been higher during the second and fourth quarters. As a result, our quarterly and annual operating results and comparable sales may fluctuate significantly as a result of seasonality. Accordingly, results for any one quarter or year are not necessarily indicative of results to be expected for any other quarter or for any year, and comparable sales for any particular future period may decrease.

2. GOING CONCERN

The Company’s financial statements are prepared in conformity with accounting principles generally accepted in the United States of America (“U.S. GAAP”) applicable to a going concern which contemplates the realization of assets and liquidation of liabilities in the normal course of business. The Company has not yet established an ongoing source of revenues sufficient to cover its operating costs and allow it to continue as a going concern. The Company has an accumulated deficit since inception to December 31, 2013, of $2,329,526 which raises substantial doubt about the Company’s ability to continue as a going concern. The ability of the Company to continue as a going concern is dependent on the Company obtaining adequate capital to fund operating losses until it becomes profitable. If the Company is unable to obtain adequate capital, it could be forced to cease operations.

In order to continue as a going concern, the Company will need, among other things, additional capital resources. Management's plan is to obtain such resources for the Company through debt and/or equity financing from third parties.

3. DEBT – THIRD PARTIES AND RELATED PARTIES

At December 31, 2013 and September 30, 2013 debt consists of the following:

	December 31, 2013	September 30, 2013
Loans - CI LLC	$ 186,314	$ 137,156
Loans – Related parties	32,976	32,272
Loans - David Hardcastle – Shareholder ($329,760 short term)	650,419	636,407
Total Debt to shareholders and related parties	$ 869,709	$ 805,835

During the three months ended December 31, 2013, the Company received $45,322 from CI LLC as a short term loan.

Short term loans from CI LLC ("CIL") are unsecured and interest free.

Other differences in the loan values between September 30, 2013 and December 31, 2013 are due to foreign exchange translations.

Long-term loans from David Hardcastle are unsecured and are currently non-interest bearing. However, once the Company secures significant external financing, the long term loans begin accruing interest at bank rate plus 2% per annum and will be payable in quarterly installments over a 3 year period.

4. CONVERTIBLE DEBT, DERIVATIVE LIABILITIES & FAIR VALUE MEASUREMENTS

Convertible Debt – IIMG

Loans from Iceberg Investment Management Group ("IIMG") are unsecured and accrue interest at a rate of 2.5% per annum. During the three months ended December 31, 2013, the Company repaid $40,573 to IIMG ..

If the loans remain unpaid by the maturity date, all amounts are convertible into common stock of the Company at 80% of the Company's volume weighted average price ("VWAP") for the 5 previous days prior to execution of the promissory note.

Convertible Debt – Embedded Derivatives

On August 30, 2013, the Company entered into an Unsecured Senior Convertible Promissory Note (the "Note") with Banque Benedict Hentsch & Cie SA ("Banque Benedict") for the principal sum of Three Hundred and Fifty Thousand Dollars ($350,000) plus simple interest thereon at the rate of ten percent (10%) per annum. Banque Benedict has the option at any time to convert the Note in whole into shares of the common stock of the Company at the conversion rate of $0.125 per share. Unless the Note is earlier converted, the total principal and unpaid interest is due on September 1, 2016.

On September 9, 2013, the Company entered into an Unsecured Senior Convertible Promissory Note (the "Note") with Monument Assets & Resources Company Ltd ("Monument Assets") for the principal sum of One Hundred Thousand Dollars ($100,000) plus simple interest thereon at the rate of ten percent (10%) per annum. Monument Assets has the option at any time to convert the Note in whole into shares of the common stock of the Company at the conversion rate of $0.125 per share. Unless the Note is earlier converted, the total principal and unpaid interest is due on September 1, 2016.

The above conversion notes contain a reset provision whereby the conversion price on the notes can be reduced based on future equity transactions of the Company. As a result, the conversion options were classified as derivative liabilities at their fair value on the date of issuance. The fair value of the derivative liabilities exceeded the principal amount of the notes, resulting in a full debt discount of $450,000, $12,542 of which has been amortized to interest expense from the date of the issuance to December 31 2013.

As defined in FASB ASC 820, fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (exit price). The Company utilized the market data of similar entities in its industry or assumptions that market participants would use in pricing the asset or liability, including assumptions about risk and the risks inherent in the inputs to the valuation technique. These inputs can be readily observable, market corroborated, or generally unobservable. The Company classifies fair value balances based on the observability of those inputs. FASB ASC 820 establishes a fair value hierarchy that prioritizes the inputs 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 measurement) and the lowest priority to unobservable inputs (level 3 measurement).

The three levels of the fair value hierarchy are as follows:

Level 1 –	Quoted prices are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions for the asset or liability occur in sufficient frequency and volume to provide pricing information on an ongoing basis. Level 1 primarily consists of financial instruments such as exchange-traded derivatives, marketable securities and listed equities.

Level 2 –	Pricing inputs are other than quoted prices in active markets included in level 1, which are either directly or indirectly observable as of the reported date.

Level 3 –	Pricing inputs include significant inputs that are generally less observable from objective sources. These inputs may be used with internally developed methodologies that result in management’s best estimate of fair value.

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The following table sets forth by level within the fair value hierarchy the Company's financial assets and liabilities that were accounted for at fair value as at December 31, 2013.

Recurring Fair Value Measures		**Level 1**	**Level 2**	**Level 3**	**Total**
LIABILITIES:					
Derivative liabilities net	September 30, 2013	$ -	$ -	$ 434,464	$ 434,464
Derivative liabilities net	December 31, 2013	$ -	$ -	$ 192,214	$ 192,214

The following table summarizes the changes in the derivative liabilities during the period ended December 31, 2013:

Fair value as of October 1, 2013	$ 434,464
Change in fair value	242,250
Ending balance as of December 31, 2013	**$192,214**

The gain on derivative liabilities of $242,250 in the accompanying consolidated statement of operations consists of the change in fair value of $242,250 noted above.

The Company uses the Black-Scholes option pricing model to value the derivative liability and subsequent re-measurements. Included in the model are the following assumptions: stock price at valuation date of $0.0547, exercise price of $0.125, dividend yield of zero, years to maturity of 2.67, risk free rate of 0.09 – 0.8 percent, and annualized volatility of 292.63 – 478.27 percent.

5. RELATED PARTY TRANSACTIONS

As of December 31, 2013, the Company owed an officer $41,797 for accounting and consultancy fees.

6. EQUITY

During the three months ended December 31, 2013 the Company issued 166,667 shares of common stock valued at $12,500 for services rendered.

7. COMMITMENTS AND CONTINGENCIES

In November 2012, Anio Limited (now named Lot 78 UK Limited) entered into a Consulting and Services Agreement with Iceberg Investments Management Group Limited , a British Virgin Islands corporation. This document includes a provision that Lot78 UK Ltd would pay a success fee of USD$770,000 on the closing of any financing in the amount exceeding $3,000,000. The amount of the success fee purportedly payable reduces if the financing is less than $3,000,000. For these purposes, Iceberg have confirmed that no success fee would be payable if the financing is less than $1,450,000 and $500,000 whether by equity or loan raised from or introduced by Banque Benedict Hentsch & CIE SA is excluded. If Iceberg is not successful in obtaining financing for the Company within 18 months of a potential merger or transaction there are provisions that Lot78 UK Ltd provide a convertible promissory note.

The Company is taking legal advice on this document, the enforceability of its provisions and reserves its position as to whether such fees will be payable under or pursuant to this document.

8. SUBSEQUENT EVENTS

On 2nd January 2014, the Company opened a Letter of Credit with Bibby Financial Services amounting to $305,085 for it's Spring/Summer 14 production. This Letter of Credit was covered by the forward orders received from our customers and the total amount outstanding as of date of issuance of the financial statements is $5,509.

eND OF NOTES TO FINANCIALS

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION OR PLAN OF OPERATION

FORWARD-LOOKING STATEMENTS

This Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) contains forward-looking statements that involve known and unknown risks, significant uncertainties and other factors that may cause our actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed, or implied, by those forward-looking statements. You can identify forward-looking statements by the use of the words may, will, should, could, expects, plans, anticipates, believes, estimates, predicts, intends, potential, proposed, or continue or the negative of those terms. These statements are only predictions. In evaluating these statements, you should consider various factors which may cause our actual results to differ materially from any forward-looking statements. Although we believe that the exceptions reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. Therefore, actual results may differ materially and adversely from those expressed in any forward-looking statements. We undertake no obligation to revise or update publicly any forward-looking statements for any reason.

Overview

Lot78, Inc. (the “Company”) designs, markets, distributes, and sells apparel under the brand name "Lot78" to fashion-conscious consumers on four continents, including North America, Europe, Asia, and South America. We seek to be a trend setting leader in the design, marketing, distribution and sale of luxury street apparel. Our current collection is a full men’s and women’s contemporary ready-to-wear line which includes leather jackets, t-shirts, sweats, knitwear, accessories, jeans, chinos, and wool coats. We operate in three distinct but integrated segments: Wholesale, Consumer Direct and Core Services. Our Wholesale segment sells our products to industry-leading high-end global department stores, specialty retailers and boutiques; our Consumer Direct segment consists of e-commerce sales through our branded website located at www.lot78.com; and our Core Services segment provides product design, distribution, marketing and other overhead resources to the other segments.

Executive Summary

Our results for the current quarter were in line with expectations. Historically, we rely on re orders and online sales for revenues in our first and third quarters with the bulk of our revenue being generated in the second and fourth quarters co-inciding with the Spring/Summer and Fall/Winter seasons.

We are in the process of looking to have pre seasonal deliveries to our customers which if successful will generate greater revenues in our first and third quarters.

Plan of Operation

As of December 31, 2013, we had $49,947 of cash on hand. We incurred operating expenses in the amount of $273,576 during the period ended December 31, 2013. These operating expenses were comprised of general and administrative expenses, professional fees, directors' and consulting fees, and other miscellaneous expenses.

Our current cash holdings will not satisfy our liquidity requirements and we will require additional financing to pursue our planned business activities. We are in the process of seeking equity and or debt financing to fund our operations over the next 12 months.

If we cannot generate sufficient revenues to continue operations, we will suspend or cease our operations.

We do not expect the purchase or sale of any significant equipment and have no current material commitments.

Management believes that if subsequent placements are successful, we will generate sufficient sales revenue to cover our operating costs within the following twelve months thereof. However, additional equity and or debt financing may not be available to us on acceptable terms or at all, and thus we could fail to satisfy our future cash requirements.

Revenues

We earned revenues of $55,730 for the period ended December 31, 2013 compared to revenues of $58,695 for the period ended December 31, 2012. The decrease in revenues for the period ended December 31, 2013 can be attributed to our end of season Fall/Winter 13 stock being sold after the quarter end in February 2014 whereas our old stock for Fall/Winter 12 was sold in December 2012.

Cost of Goods Sold

Cost of goods sold for the period ended December 31, 2013 were $69,409 compared to $75,384 for the period ended December 31, 2012. Cost of goods sold represented 125% of sales for the period ended December 31, 2013 as compared to 128% for the period ended December 31, 2012. For the period ended December 31, 2013 the decrease can be attributed to a lower write down off stock for Fall/Winter 13 compared to Fall/Winter 12.

Expenses

For the period ended December 31, 2013, total general and administrative expenses increased $149,226, or 120%, to $273,576. This increase can be attributed to increased professional fees related to regulatory filings, increased travel costs for Fall/Winter 2013 sales, PR costs, employing an Italian Consultant for liasing with factories, increase in design team staff and salaries of the CEO and CFO whose costs were not incurred in the December 2012 quarter. We have also incurred one off costs relating to professional fees of $12,500, pertaining to preparation of filing of an S-1 document.

Working Capital

At

December 31, At

2013