

MusclePharm Corp  
Form 10-Q  
August 14, 2013

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-Q**

**x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended: **June 30, 2013**

OR

**.. TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: **000-53166**

**MUSCLEPHARM CORPORATION**

(Exact name of registrant as specified in its charter)

**Nevada** **77-0664193**  
(State or other jurisdiction of (I.R.S. Employer)

incorporation or organization) Identification No.)

**4721 Ironton Street, Building A**

**Denver, Colorado 80239**

(Address of principal executive offices and zip code)

**(303) 396-6100**

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by section 13 or 15(d) of the Securities Exchange Act of 1934 during the past 12 months, 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, or 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 August 13, 2013, there were 10,127,124 shares outstanding of the registrant's common stock.

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**Part I – FINANCIAL INFORMATION****Item 1. Financial Statements****MusclePharm Corporation and Subsidiary****Consolidated Balance Sheets**

	June 30, 2013 (unaudited)	December 31, 2012 (audited)
Assets		
Current Assets:		
Cash	\$8,655,761	\$ -
Cash – restricted	-	9,148
Accounts receivable – net	9,235,094	3,302,344
Inventory	1,168,348	257,975
Prepaid giveaways	101,680	358,800
Prepaid stock compensation	1,109,313	44,748
Prepaid sponsorship fees	581,877	6,249
Deferred equity costs	-	698,500
Other assets	896,671	272,117
Total current assets	21,748,744	4,949,881
Property and equipment – net	1,329,047	1,356,364
Debt issue costs – net	-	335,433
Other assets	172,994	125,049
Total Assets	\$23,250,785	\$ 6,766,727
Liabilities and Stockholders' Equity		
Current Liabilities:		
Accounts payable and accrued liabilities	\$8,173,356	\$ 11,721,205
Customer deposits	24,773	336,211
Debt – net	74,329	4,463,040
Derivative liabilities	2,369,032	-
Total current liabilities	10,641,490	16,520,456
Long Term Liabilities:		
Debt – net	-	4,523
Total Liabilities	10,641,490	16,524,979
Commitments and Contingencies		
Stockholders' Equity:		
Series A, Convertible Preferred Stock, \$0.001 par value; 5,000,000 shares authorized, none issued and outstanding	-	-

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Series B, Preferred Stock, \$0.001 par value; 51 shares authorized, issued and outstanding	-	-	
Series C, Convertible Preferred Stock, \$0.001 par value; 500 shares authorized, 190 and zero issued and outstanding	-	-	
Series D, Convertible Preferred Stock, \$0.001 par value; 1,600,000 shares authorized, 1,500,000 and none issued and 145,000 and none outstanding	145	-	
Common Stock, \$0.001 par value; 100,000,000 shares authorized, 7,766,759 and 2,778,404 issued and 7,716,838 and 2,747,308 outstanding	7,767	2,778	
Treasury Stock, at cost; 49,921 and 31,096 shares	(564,515	)	(460,978 )
Additional paid-in capital	87,061,004		54,817,341 )
Accumulated deficit	(73,893,265	)	(64,109,476 )
Accumulated other comprehensive loss	(1,841	)	(7,917 )
Total Stockholders' Equity	12,609,295		(9,758,252 )
Total Liabilities and Stockholders' Equity	\$23,250,785		\$ 6,766,727

See accompanying notes to unaudited financial statements.

**MusclePharm Corporation and Subsidiary****Consolidated Statements of Operations****(unaudited)**

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2013	2012	2013	2012
Sales – gross	\$ 28,515,483	\$ 18,869,103	\$ 53,439,519	\$ 38,171,872
Discounts and sales allowances	(3,035,424 )	(3,439,763 )	(5,398,293 )	(6,181,852 )
Sales – net	25,480,059	15,429,340	48,041,226	31,990,020
Cost of sales	17,566,718	12,942,605	31,963,124	25,837,767
Gross profit	7,913,341	2,486,735	16,078,102	6,152,253
General and administrative expenses	10,654,272	4,151,076	19,540,512	8,543,887
Income (loss) from operations	(2,740,931 )	(1,664,341 )	(3,462,410 )	(2,391,634 )
Other income (expense)				
Derivative expense	-	(1,029,541 )	(96,913 )	(2,486,451 )
Change in fair value of derivative liabilities	272,681	9,854,045	(5,771,963 )	1,496,874
Gain (loss) on settlement of accounts payable and debt	47,671	-	324,656	(2,941,826 )
Interest expense	(1,125 )	(976,686 )	(781,445 )	(3,547,202 )
Foreign currency transaction loss	(104 )	(1,573 )	(5,714 )	(1,573 )
Other income	-	-	10,000	18,423
Total other income (expense) - net	319,123	7,846,245	(6,321,379 )	(7,461,755 )
Net income (loss)	(2,421,808 )	6,181,904	(9,783,789 )	(9,853,389 )
Other comprehensive income				
Net change in Foreign currency translation	4,228	40,719	(1,841 )	40,719
Total other comprehensive income (loss)	4,228	40,719	(1,841 )	40,719
Total comprehensive income (loss)	\$ (2,417,580 )	\$ 6,222,623	\$ (9,785,630 )	\$ (9,812,670 )
Net income (loss) per share available to common stockholders – basic and diluted	\$ (0.34 )	\$ 3.78	\$ (1.72 )	\$ (6.44 )
Weighted average number of common shares outstanding during the period – basic and diluted	7,226,849	1,633,676	5,686,323	1,530,850

See accompanying notes to unaudited financial statements.

**MusclePharm Corporation and Subsidiary****Consolidated Statements of Cash Flows****(unaudited)**

	Six Months Ended June 30,	
	2013	2012
Cash Flows From Operating Activities:		
Net loss	\$(9,783,789 )	\$(9,853,389 )
Adjustments to reconcile net loss to net cash (used in) provided by operating activities:		
Depreciation	333,383	199,750
Bad debt	105,271	9,490
Amortization of prepaid stock and deferred compensation	3,419,698	456,903
Amortization of debt discount	-	3,083,437
Amortization of debt issue costs	335,433	184,031
(Gain) loss on settlement of accounts payable, debt and conversion of Series C preferred stock	(324,656 )	2,941,826
Derivative expense	96,913	2,486,451
Change in fair value of derivative liabilities	5,771,963	(1,496,874 )
Changes in operating assets and liabilities:		
(Increase) decrease in:		
Restricted cash balance	9,148	(52,744 )
Accounts receivable	(5,713,366 )	502,193
Prepaid and other	(1,242,246 )	186,725
Inventory	86,866	(219,276 )
Increase (decrease) in:		
Accounts payable and accrued liabilities	2,052,010	867,058
Customer deposits	(311,438 )	1,142,426
Net Cash (Used In) Provided by Operating Activities	(5,164,810 )	438,007
Cash Flows From Investing Activities:		
Purchase of property and equipment	(307,760 )	(544,859 )
Proceeds from disposal of property and equipment	1,694	-
Purchase of trademark	(47,500 )	(35,000 )
Net Cash Used In Investing Activities	(353,566 )	(579,859 )
Cash Flows From Financing Activities:		
Proceeds from issuance of debt	-	4,073,950
Debt issue costs	-	(106,950 )
Repayment of debt	(4,393,234 )	(4,058,442 )
Repurchase of common stock (treasury stock)	(103,537 )	(460,978 )
Proceeds from issuance of preferred stock	12,000,000	-
Proceeds from issuance of common stock and warrants	8,327,499	285,760
Stock issuance costs	(1,662,667 )	-

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Net Cash Provided by (Used In) Financing Activities	14,168,061	(266,660 )
Cash Flows From Equity Activities:		
Effect of exchange rates on cash and cash equivalents	6,076	40,719
Net Cash Provided by Equity Activities	6,076	40,719
Net increase (decrease) in cash	8,655,761	(367,793 )
Cash at beginning of period	-	659,764
Cash at end of period	\$8,655,761	\$291,971
Supplemental disclosures of cash flow information:		
Cash paid for interest	\$410,502	\$265,078
Cash paid for taxes	\$-	\$-
Supplemental disclosure of non-cash investing and financing activities:		
Stock issued for future services - third parties	\$4,409,897	\$200,000
Warrants issued in conjunction with equity issuances	\$8,175,459	\$427,759
Debt discount recorded on convertible and unsecured debt accounted for as a derivative liability	\$-	\$3,554,672
Stock issued to settle accounts payable and accrued expenses– third parties	\$5,484,947	\$4,667,764
Conversion of convertible debt and accrued interest for common stock	\$-	\$1,069,402
Stock issued for executive and board compensation	\$114,912	\$-
Reclassification of derivative liability to additional paid in capital	\$-	\$4,124,387
Stock issued to settle accrued liabilities	\$-	\$135,000
Stock issued to settle contracts	\$-	\$3,932

See accompanying notes to unaudited financial statements.



**MusclePharm Corporation and Subsidiary**

**Notes to Consolidated Financial Statements**

**(June 30, 2013)**

**(Unaudited)**

**Note 1: Nature of Operations and Basis of Presentation**

**Nature of Operations**

MusclePharm Corporation (the “Company”, “we”, “our”, or “MusclePharm”), was incorporated in the state of Nevada on August 4, 2006 under the name Tone in Twenty for the purpose of engaging in the business of providing personal fitness training using isometric techniques. The Company is headquartered in Denver, Colorado.

MusclePharm currently manufactures and markets a wide-ranging variety of high-quality sports nutrition products.

**Basis of Presentation**

The accompanying unaudited interim consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) and the rules and regulations of the U.S. Securities and Exchange Commission (“SEC”), as amended for interim financial information.

The financial information as of December 31, 2012 is derived from the audited financial statements presented in the Company’s Annual Report on Form 10-K for the year ended December 31, 2012 and filed with the SEC on April 1, 2013. The unaudited interim consolidated financial statements should be read in conjunction with the Company’s Annual Report on Form 10-K, which contains the audited financial statements and notes thereto, together with Management’s Discussion and Analysis of Financial Condition and Results of Operations, for the years ended December 31, 2012 and 2011.

Certain information or footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted, pursuant to the rules and regulations of the SEC for interim financial reporting. 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 interim results for the six months ended June 30, 2013 are not necessarily indicative of results for the full fiscal year.

## **Note 2: Summary of Significant Accounting Policies**

### **Principles of Consolidation**

The consolidated financial statements include the accounts of MusclePharm Corporation and its wholly-owned subsidiary MusclePharm Canada Enterprises Corp ("MusclePharm Canada"). MusclePharm Canada began operations in April of 2012. All intercompany accounts and transactions between MusclePharm Corporation and MusclePharm Canada have been eliminated upon consolidation.

### **Use of Estimates**

The preparation of financial statements in conformity with GAAP requires 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.

Making estimates requires management to exercise significant judgment. It is reasonably possible that the estimate of the effect of a condition, situation or set of circumstances that existed at the date of the financial statements, which management considered in formulating its estimate could change in the near term due to one or more future non-conforming events. Accordingly, the actual results could differ significantly from estimates.

### **Risks and Uncertainties**

The Company operates in an industry that is subject to rapid change and intense competition. The Company's operations will be subject to significant risk and uncertainties including financial, operational, technological, regulatory, industry adverse publicity and other risks, including the potential risk of business failure.



**MusclePharm Corporation and Subsidiary**

**Notes to Consolidated Financial Statements**

**(June 30, 2013)**

**(Unaudited)**

**Cash and Cash Equivalents**

The Company considers all highly liquid instruments purchased with an original maturity of three months or less and money market accounts to be cash equivalents. At June 30, 2013 and December 31, 2012, respectively, the Company had no cash equivalents.

**Accounts Receivable and Allowance for Doubtful Accounts**

Accounts receivable represents trade obligations from customers that are subject to normal trade collection terms. Prior to July 1, the accounts receivable were sent directly to the Company's third party manufacturer and netted with any outstanding liabilities to the manufacturer (see Note 11). Liabilities to the manufacturer totaled \$4,213,394 at June 30, 2013 and are included in accounts payable and accrued liabilities. The Company periodically evaluates the collectability of its accounts receivable and considers the need to establish an allowance for doubtful accounts based upon historical collection experience and specific customer information. Accordingly, the actual amounts could vary from the recorded allowances. There is also a review of customer discounts at the period end and an accrual made for discounts earned but not yet received by quarter end.

Management reserves for bad debt expense based on the aging of accounts receivable. Bad debt expense is classified under general & administrative expense in the Consolidated Statement of Operations.

The Company does not charge interest on past due receivables. Receivables are determined to be past due based on the payment terms of the original invoices. Accounts receivable consisted of the following at June 30, 2013 and December 31, 2012:

As of	As of
June 30, 2013	December 31, 2012

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Accounts receivable	\$ 10,492,646	\$ 4,416,193	
Less: allowance for discounts	(1,004,000 )	(1,088,720 )	
Less: allowance for doubtful accounts	(253,552 )	(25,129 )	
Accounts receivable – net	\$ 9,235,094	\$ 3,302,344	

At June 30, 2013 and December 31, 2012, the Company had the following concentrations of accounts receivable with significant customers:

Customer	As of June 30, 2013		As of December 31, 2012	
A	14	%	19	%
B	8	%	6	%
C	7	%	0	%

### Inventory

Inventory is valued at the lower of cost or market value. Product-related inventories are primarily maintained using the average cost method.

### Prepaid Giveaways

Prepaid giveaways represent non-inventory sample items, which are given away to aid in promotion of the brand.

### Prepaid Sponsorship Fees

Prepaid sponsorship fees represents fees paid in connection with future advertising to be received.

### Property and Equipment

Property and equipment are stated at cost and depreciated to their estimated residual value over their estimated useful lives. When assets are retired or otherwise disposed of, the assets and related accumulated depreciation are relieved from the accounts and the resulting gains or losses are included in operating income in the statements of operations. Repairs and maintenance costs are expensed as incurred. Depreciation is provided using the straight-line method for all property and equipment.



**MusclePharm Corporation and Subsidiary**

**Notes to Consolidated Financial Statements**

**(June 30, 2013)**

**(Unaudited)**

**Website Development Costs**

Costs incurred in the planning stage of a website are expensed, while costs incurred in the development stage are capitalized and amortized over the estimated useful life of the asset.

**Long-Lived Assets**

The Company reviews long-lived assets for impairment whenever events or changes in circumstances, such as service discontinuance or technological obsolescence, indicate that the carrying amount of the long-lived asset may not be recoverable. When such events occur, the Company compares the carrying amount of the asset to the undiscounted expected future cash flows related to the asset. If the comparison indicates that impairment is present, the amount of the impairment is calculated as the difference between the excess of the carrying amount over the fair value of the asset. If a readily determinable market price does not exist, fair value is estimated using discounted expected cash flows attributable to the asset. During the six months ended June 30, 2013 and 2012, the Company recorded no impairment expense.

**Fair Value of Financial Instruments**

The Company measures assets and liabilities at fair value based on an expected exit price which represents the amount that would be received on the sale of an asset or paid to transfer a liability, as the case may be, in an orderly transaction between market participants. As such, fair value may be based on assumptions that market participants would use in pricing an asset or liability. The authoritative guidance on fair value measurements contains a consistent framework for measuring fair value on either a recurring or nonrecurring basis whereby inputs, used in valuation techniques, are assigned a hierarchical level.

The following are the hierarchical levels of inputs to measure fair value:

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- Level 1: Observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.
- Level 2: Inputs reflect quoted prices for identical assets or liabilities in markets that are not active; quoted prices for similar assets or liabilities in active markets; inputs other than quoted prices that are observable for the assets or liabilities; or inputs that are derived principally from or corroborated by observable market data by correlation or other means.
- Level 3: Unobservable inputs reflecting the Company's assumptions incorporated in valuation techniques used to determine fair value. These assumptions are required to be consistent with market participant assumptions that are reasonably available.

The following are the major categories of liabilities measured at fair value on a recurring basis as of June 30, 2013 and December 31, 2012, using quoted prices in active markets for identical liabilities (Level 1); significant other observable inputs (Level 2); and significant unobservable inputs (Level 3):

	As of June 30, 2013	As of December 31, 2012
Derivative liabilities (Level 2)	\$ 2,369,032	\$ -

The Company's financial instruments consisted primarily of accounts receivable, accounts payable and accrued liabilities, and debt. The Company's debt approximates fair value based upon current borrowing rates available to the Company for debt with similar maturities. The carrying amounts of the Company's financial instruments generally approximated their fair values as of June 30, 2013 and December 31, 2012, respectively, due to the short-term nature of these instruments.

### Revenue Recognition

The Company records revenue when all of the following have occurred: (1) persuasive evidence of an arrangement exists, (2) product has been shipped or delivered, (3) the sales price to the customer is fixed or determinable, and (4) collectability is reasonably assured.

Depending on individual customer agreements, sales are recognized either upon shipment of products to customers or upon delivery. For all of our Canadian sales, which represent 3% of total sales, recognition occurs upon shipment.



**MusclePharm Corporation and Subsidiary**

**Notes to Consolidated Financial Statements**

**(June 30, 2013)**

**(Unaudited)**

The Company has determined that advertising related credits that are granted to customers fall within the guidance of ASC No. 605-50-55 (“*Revenue Recognition*” – *Customer Payments and Incentives – Implementation Guidance and Illustrations*). The guidance indicates that, absent evidence of benefit to the vendor, appropriate treatment requires netting these types of payments against revenues and not expensing as advertising expense.

The Company records sales allowances and discounts as a direct reduction of sales.

Sales for the three and six months ended June 30, 2013 and 2012 were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Sales	\$ 28,515,483	\$ 18,869,103	\$ 53,439,519	\$ 38,171,872
Discounts	(3,035,424 )	(3,439,763 )	(5,398,293 )	(6,181,852 )
Sales - Net	\$ 25,480,059	\$ 15,429,340	\$ 48,041,226	\$ 31,990,020

The Company has an informal seven day right of return for products. There were nominal returns for the three and six months ended June 30, 2013 and 2012.

For the six months ended June 30, 2013 and 2012, the Company had the following concentrations of revenues with significant customers:

	Six Months Ended June 30,			
Customer	2013		2012	
A	31	%	40	%
B	12	%	11	%

C 6 % 17 %

### **Licensing Income and Royalty Revenue**

On May 5, 2011, the Company granted an exclusive indefinite license to market, manufacture, design and sell the Company's existing apparel line. The licensee paid an initial fee of \$250,000 in June 2011, and will pay the Company a 10% net royalty based on its net income at the end of each fiscal year. To date, no royalty revenue has been earned by the Company.

### **Cost of Sales**

Cost of sales represents costs directly related to the production, manufacturing and freight of the Company's products.

### **Shipping and Handling**

Until March 1, 2013 MusclePharm used a manufacturer from Tennessee to ship directly to our customers, and after that date MusclePharm took control of the shipping and began shipping product to our customers from a previously leased 152,000 square foot distribution center in Franklin, Tennessee in close proximity of our manufacturer. Our products are transported from our manufacturer to the MusclePharm distribution center, but title does not pass from the manufacturer until loaded on the truck for shipment. Through June 30, 2013, MusclePharm does not take title to our products (see Note 11). The facility in Franklin, Tennessee is operated with the Company's equipment and employees. This transition away from having our Tennessee manufacturer ship product for us is an effort to reduce our costs and improve gross margins.

The Company also uses a manufacturer in New York for the manufacture of one of the Company's products. These orders are typically large and heavy and are drop shipped directly to our customers at the time of order.

Costs associated to the shipments are recorded in cost of sales. For Canadian sales, the product is shipped from our Canadian warehouse to our customers. Costs associated with the shipments are recorded as shipping.

**MusclePharm Corporation and Subsidiary**

**Notes to Consolidated Financial Statements**

**(June 30, 2013)**

**(Unaudited)**

**Advertising**

The Company expenses advertising costs when incurred.

Advertising expense for the three and six months ended June 30, 2013 and 2012 were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Advertising	\$ 3,275,200	\$ 2,044,005	\$ 5,592,577	\$ 3,976,840

**Beneficial Conversion Feature**

For conventional convertible debt where the rate of conversion is below market value, the Company records a “beneficial conversion feature” (“BCF”) and related debt discount.

When the Company records a BCF, the relative fair value of the BCF is recorded as a debt discount against the face amount of the respective debt instrument. The discount is amortized to interest expense over the life of the debt.

**Accounts payable and accrued liabilities**

Accounts payable and accrued liabilities consists of the Company’s trade payables as well as amounts estimated by management for future liability payments that relate to the current accounting period. Management reviews these

estimates periodically to determine their reasonableness and fair presentation.

## **Debt**

The Company defines short term debt as any debt payment due less than one year from the date of the financial statements. Long term debt is defined as any debt payment due more than one year from the date of the financial statements. Refer to Note 4 for further disclosure of debt liabilities.

## **Derivative Liabilities**

Fair value accounting requires bifurcation of embedded derivative instruments such as conversion features in equity instruments and warrants granted, and measurement of their fair value. In determining the appropriate fair value, the Company uses the Black-Scholes option-pricing model. In assessing the convertible equity instruments, management determines if the convertible equity instrument is conventional convertible equity and further if the beneficial conversion feature requires separate measurement.

Once derivative liabilities are determined, they are adjusted to reflect fair value at the end of each reporting period. Any increase or decrease in the fair value is recorded in results of operations as an adjustment to fair value of derivatives. In addition, the fair value of freestanding derivative instruments such as warrants, are also valued using the Black-Scholes option-pricing model. Once a derivative liability ceases to exist any remaining fair value is reclassified to additional paid in capital.

## **Deferred Equity Costs**

The Company may pay costs related to the underwriting and offering of equity securities. These costs are treated as a reduction to equity capital raised and recorded in equity when the share issuances are recorded. Until the shares are recorded or until offering is aborted, these costs will be held on the balance sheet as a deferred asset.

## **Debt Issue Costs and Debt Discount**

The Company may pay debt issue costs, and record debt discounts in connection with raising funds through the issuance of debt. These costs are amortized over the life of the debt to interest expense. If a conversion of the underlying debt occurs, a proportionate share of the unamortized amounts is immediately expensed.



**MusclePharm Corporation and Subsidiary**

**Notes to Consolidated Financial Statements**

**(June 30, 2013)**

**(Unaudited)**

**Original Issue Discount**

For certain convertible debt issued, the Company provides the debt holder with an original issue discount. The original issue discount is recorded to debt discount and additional paid-in capital at an amount not to exceed gross proceeds raised, reducing the face amount of the debt, and is amortized to interest expense over the life of the debt.

**Share-Based Payments**

Generally, all forms of share-based payments, including stock option grants, warrants and restricted stock grants and stock appreciation rights are measured at their fair value on the awards' grant date, based on estimated number of awards that are ultimately expected to vest. Share-based compensation awards issued to non-employees for services rendered are recorded at either the fair value of the services rendered or the fair value of the share-based payment, whichever is more readily determinable.

**Earnings (loss) Per Share**

Net earnings (loss) per share is computed by dividing net income (loss) for the period by the weighted average number of shares of common stock outstanding during each period. Diluted earnings (loss) per share is computed by dividing net income (loss) for the period by the weighted average number of shares of common stock, common stock equivalents and potentially dilutive securities outstanding during each period.

The Company uses an "if converted" method to determine whether there is a dilutive effect of outstanding option and warrant contracts. For the three months ended June 30, 2012, all of the Company's convertible debt options and 625,028 warrants had exercise prices below of the Company's period end market price of the common stock into which they convert. The adjusted dilutive net loss reflects the add back of approximately \$349 of interest expense related to the convertible debt and the reduction of \$9,449,050 of gains on derivative contracts for the three months ended June

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30, 2012. For the three months ended June 30, 2013 and six months ended June 30, 2013 and 2012, and the three months ended June 30, 2012 the Company reflected net loss and a dilutive net loss, respectively, and the effect of considering any common stock equivalents would have been anti-dilutive for these periods. Therefore, separate computation of diluted earnings (loss) per share is not presented.

The Company has the following common stock equivalents for the six months ended June 30, 2013 and 2012, respectively:

	Six Months Ended June 30,	
	2013	2012
Stock options (exercise price - \$425/share)	670	1,903
Warrants (exercise price \$4 – \$1,275/share)	330,089	84,820
Convertible debt (exercise price \$17/share)	-	2,471
Total common stock equivalents	330,759	89,194

In the above table, some of the outstanding instruments from 2013 and 2012 contain ratchet provisions that would cause variability in the exercise price at the balance sheet date. As a result, common stock equivalents could change at each reporting period.

### Foreign Currency

MusclePharm began operations in Canada in April of 2012. The Canadian Dollar was determined to be the functional currency as the majority of the transactions related to the day to day operations of the business are exchanged in Canadian Dollars. At the end of the period, the financial results of the Canadian operation are translated into United States Dollars, which is our reporting currency, and added to the U.S. operations for consolidated company financial results. The revenue and expense items are translated using the average rate for the period and the assets and liabilities at the end of period rate. Transactions that have completed the accounting cycle and resulted in a gain or loss related to translation are recorded in realized gain or loss due to foreign currency translation under other income expense on the income statement. Transactions that have not completed their accounting cycle but appear to have gain or loss due to the translation process are recorded as unrealized gain or loss due to translation and held in the equity section on the balance sheet until such date the accounting cycle of the transaction is complete and the actual realized gain or loss is recognized.

**MusclePharm Corporation and Subsidiary****Notes to Consolidated Financial Statements****(June 30, 2013)****(Unaudited)****Reclassification**

The Company has reclassified certain prior period amounts to conform to the current period presentation. These reclassifications had no effect on the financial position, results of operations or cash flows for the periods presented.

**Note 3: Property and Equipment**

Property and equipment consisted of the following at June 30, 2013 and December 31, 2012:

	As of June 30, 2013	As of December 31, 2012	Estimated Useful Life
Furniture, fixtures and gym equipment	\$ 1,591,642	\$ 1,323,998	From 36 to 60 months
Leasehold improvements	601,625	563,204	From 42 to 66 months
Vehicles	100,584	100,584	5 years
Displays	32,057	32,057	5 years
Website	11,462	11,462	3 years
Total	2,337,370	2,031,305	
Less: Accumulated depreciation and amortization	(1,008,323 )	(674,941 )	
	\$ 1,329,047	\$ 1,356,364	

**Note 4: Debt**

At June 30, 2013 and December 31, 2012, debt consists of the following:

As of June 30, 2013    As of December 31, 2012



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Auto loan - secured	\$ 9,729		15,380
Unsecured debt	64,600		4,452,183
Less: debt discount	-		-
Unsecured debt - net	64,600		4,452,183
Total debt	74,329		4,467,563
Less: current portion	(74,329	)	(4,463,040
Long term debt	\$ -		\$ 4,523

Debt in default of \$64,600 at June 30, 2013 and December 31, 2012 is included as a component of short-term debt.

Future annual principal payments for the above debt is as follows:

Years Ending December 31,	
2013 (6 months)	\$70,840
2014	3,489
Total annual principal payments	\$74,329

**MusclePharm Corporation and Subsidiary****Notes to Consolidated Financial Statements****(June 30, 2013)****(Unaudited)****Convertible Debt – Secured - Derivative Liabilities**

During the year ended December 31, 2012, the Company issued convertible debt totaling \$519,950. The convertible debt includes the following terms:

		Year Ended December 31, 2012 Amount of Principal Raised
Interest Rate		8% - 10%
Default interest rate		0% - 20%
Maturity		January 3, 2012 to October 11, 2014
Conversion terms 1	62% of lowest trade price for the last 7 trading days	100,000
Conversion terms 2	65% of the lowest trade price in the 30 trading days previous to the conversion	19,950
Conversion terms 3	35% multiplied by the average of the lowest three (3) trading prices (as defined below) for the common stock during the ten (10) trading day period ending on the latest complete trading day prior to the conversion date.	400,000
		\$ 519,950

The debt holders are entitled, at their option, to convert all or part of the principal and accrued interest into shares of the Company's common stock at the conversion prices and terms discussed above. The Company classifies embedded conversion features in these notes as a derivative liability due to management's assessment that the Company may not have sufficient authorized number of shares of common stock required to net-share settle or due to the existence of a ratchet due to an anti-dilution provision. See Note 5 regarding accounting for derivative liabilities.

**(A) Unsecured Debt**

Unsecured debt consisted of the following activity and terms:

Balance - December 31, 2012	\$4,452,183
Repayments	(4,387,583)
Balance – June 30, 2013	\$64,600

**(B) Vehicle Loan**

Vehicle loan account consisted of the following activity and terms:

		Interest Rate	Maturity
Balance - December 31, 2012	\$ 15,380	6.99 %	26 payments of \$1,008
Repayments	(5,651 )		
Balance – June 30, 2013	\$9,729		

**(C) Debt Issue Costs**

During the six months ended June 30, 2012, the Company paid debt issue costs totaling \$106,950.

For the year ended December 31, 2012, the Company issued 22,633 warrants as cost associated with a debt raise. The initial derivative liability value of \$427,759 was recorded as debt issue costs and derivative liability.

The following is a summary of the Company's debt issue costs for the six months ended June 30, 2013 and year ended December 31, 2012 as follows:

	2013	2012
Debt issue costs	\$335,433	\$851,923
Accumulated amortization of debt issue costs	(335,433)	(516,490)
Debt issue costs – net	\$-	\$335,433



**MusclePharm Corporation and Subsidiary**

**Notes to Consolidated Financial Statements**

**(June 30, 2013)**

**(Unaudited)**

During the six months ended June 30, 2013 and 2012, the Company amortized \$335,433 and \$184,031, respectively in debt issue costs.

**Note 5: Derivative Liabilities**

The Company identified conversion features embedded within consulting agreements and Series D Preferred Stock issued in 2013. The Company has determined that the features associated with the embedded conversion option should be accounted for at fair value as a derivative liability as the Company could not determine if a sufficient number of shares would be available to settle all transactions.

The fair value of the conversion feature is summarized as follows:

Derivative liability - December 31, 2012	\$-
Fair value at the commitment date for equity instruments	8,175,459
Fair value at the commitment date for warrants issued	96,913
Fair value mark to market adjustment for equity instruments	5,716,688
Fair value mark to market adjustment for warrants	55,275
Conversion instruments exercised	(11,675,303)
Derivative liability – June 30, 2013	\$2,369,032

The Company recorded the day 1 value of derivative contracts associated with the Series D preferred stock issuance against gross proceeds raised, and expensed immediately the remaining value of the derivative as it exceeded the gross proceeds of the offering. The Company recorded a derivative expense of \$96,913 and \$2,486,451 for the six months ended June 30, 2013 and 2012, respectively.

The fair value at the commitment and re-measurement dates for the Company's derivative liabilities were based upon the following management assumptions:

	Commitment Date	Re-measurement Date
Expected dividends	0	% 0
Expected volatility	118% - 123%	107
Expected term:	1 year	17 months – 1 year
Risk free interest rate	0.14% - 0.15%	0.15

**Note 6: Restricted Stock Units**

In November 2012, the Company granted the Executive Vice President and Co-Chairman, Mr. John H. Bluher, 70,589 restricted stock units through a restricted stock unit agreement. Each restricted stock unit represents a contingent right to receive one share of the Company's common stock upon vesting. The value of this award at the grant date was \$245,400 and will be amortized over the vesting periods such that each tranche of restricted stock units will be fully amortized at the date of vesting. The restricted stock units vest in one tranche of 23,529 on January 1, 2013 and two tranches of 23,530 shares on January 1, 2014 and December 1, 2014. As of June 30, 2013, 23,529 restricted stock units have vested and the unamortized portion of this award is \$123,036.

In November 2012, the Company granted the Chief Financial Officer, Mr. L. Gary Davis, 58,824 restricted stock units through a restricted stock unit agreement. Each restricted stock unit represents a contingent right to receive one share of the Company's common stock upon vesting. The value of this award at the grant date was \$204,500 and will be amortized over the vesting periods such that each tranche of restricted stock units will be fully amortized at the date of vesting. The restricted stock units vest in three tranches of 19,608 shares each on January 1, 2013 and 2014, and December 1, 2014. As of June 30, 2013, 19,608 restricted stock units have vested and the unamortized portion of this award is \$102,530.

**MusclePharm Corporation and Subsidiary**

**Notes to Consolidated Financial Statements**

**(June 30, 2013)**

**(Unaudited)**

**Note 7: Stockholders' Equity**

The Company has four separate series of authorized preferred stock:

On November 26, 2012, the Company (i) effected a 1-for-850 reverse stock split of our common stock, including a proportionate reduction in the number of authorized shares of our common stock from 2.36 billion shares to 2.8 million shares of common stock, and (ii) amended our articles of incorporation to increase the number of authorized shares of common stock (post reverse stock split) from 2,941,177 to 100 million effective November 27, 2012. All share and per share amounts in this document have been changed to give effect to the reverse stock split.

**(A) Series A Convertible Preferred Stock**

This class of stock has the following provisions:

Non-voting,  
No rights to dividends,  
No liquidation value, and  
Convertible into 200 shares of common stock.

**(B) Series B Preferred Stock (Related Parties)**

In August 2011, the Company issued an aggregate of 51 shares of Series B Preferred Stock to two of its officers. The Company accounted for the share issuance at par value as there was no future economic value that could be associated with the issuance.

This class of stock has the following provisions:

- Voting rights entitling the holders to an aggregate 51% voting control,
- No rights to dividends,
- Stated value of \$0.001 per share,
- Liquidation rights entitle the receipt of net assets on a pro-rata basis with the holders of our common stock; and
- Non-convertible.

**(C) Series C Convertible Preferred Stock**

In October 2011, the Company issued 190 shares of Series C Convertible Preferred Stock, having a fair value of \$190,000. Of the total shares issued, 100 shares were issued for \$100,000 (\$1,000 /share). The remaining 90 shares were issued for services rendered having a fair value of \$90,000 (\$1,000 /share), based upon the stated value per share. In March 2012, all 190 shares were converted into 22,353 shares of the Company's common stock at a conversion price of \$0.0085 per share and a loss of \$614,984.

This class of stock has the following provisions:

Stated Value - \$1,000 per share,

Non-voting,

· Liquidation rights entitle an amount equal to the stated value, plus any accrued and unpaid dividends, As long as any Series C, Convertible Preferred Stock is outstanding, the Company is prohibited from executing various corporate actions without the majority consent of the holders of Series C, Convertible Preferred Stockholders authorization; and

· Convertible at the higher of (a) \$0.01 or (b) such price that is a 50% discount to market using the average of the low two closing bid prices, five days preceding conversion.

Due to the existence of an option to convert at a variable amount, the Company treated this series of preferred stock as a derivative liability due to the potential for settlement in a variable quantity of shares. Additionally, the Company computed the fair value of the derivative liability at the commitment date and re-measurement date, which was \$293 and \$175, respectively, using the Black-Scholes assumptions below. This transaction is analogous to a dividend with a direct charge to retained earnings.



**MusclePharm Corporation and Subsidiary****Notes to Consolidated Financial Statements****(June 30, 2013)****(Unaudited)****(D) Series D Convertible Preferred Stock**

In January 2013 the board of directors authorized 1,600,000 shares of Series D convertible preferred stock. Between January 16, 2013 and February 4, 2013, the Company entered into separate subscription agreements with certain investors in connection with the offering, pursuant to which the Company sold an aggregate of 1,500,000 shares of Preferred Stock for aggregate gross proceeds of approximately \$12 million. Pursuant to the Certificate of Designation of the Series D Convertible Preferred Stock filed with the Nevada Secretary of State on January 11, 2013 (the "Certificate of Designation"), each share of Preferred Stock is convertible into two shares of common stock, subject to adjustment as set forth in the Certificate of Designation.

The shares of Series D have the following provisions:

- Voting rights based on number of common shares of conversion option;
- Initially no rights to dividends;
- Liquidation rights entitle an amount equal to the stated value, plus any accrued and unpaid dividends, Convertible into 2 shares of common stock, subject to adjustment.

**(E) Common Stock**

During the six months ended June 30, 2013, the Company issued the following common stock:

Transaction Type	Quantity (#)	Valuation (\$)	Range of Value per Share (\$)
Conversion of Series D preferred stock to common stock	2,710,000	11,675,481	2.80 – 7.54
Cash and warrants	953,236	8,059,330	8.26 – 9.32
Executive/Board of Director compensation	62,289	264,879	3.48 – 6.00

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Stock issued for services and to settle liabilities	1,262,830	9,894,844	4.02 – 12.99
Total	4,988,355	29,894,534	2.80 – 12.99

The fair value of all stock issuances above is based upon either the quoted closing trading price on the date of issuance, the value of derivative instrument at the date of conversion, contract value where the fair value was stated by the contract, or net proceeds from capital raised after giving effect to the cost of capital raised.

**(F) Stock Options**

The Company applied fair value accounting for all shares based payments awards. The fair value of each option granted is estimated on the date of grant using the Black-Scholes option-pricing model. The Black-Scholes assumptions used when the options were issued in the year ended December 31, 2010 are as follows:

Exercise price	\$425	
Expected dividends	0	%
Expected volatility	74.8	%
Risk free interest rate	1.4	%
Expected life of option	5 years	
Expected forfeiture	0	%

**MusclePharm Corporation and Subsidiary****Notes to Consolidated Financial Statements****(June 30, 2013)****(Unaudited)**

The following is a summary of the Company's stock option activity:

	Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Aggregate Intrinsic Value
Balance – December 31, 2012	1,847	\$ 425.00	2.25 years	-
Granted	-			
Exercised	-			
Forfeited/Cancelled	(1,177 )	\$ 425.00		
Balance – June 30, 2013 – outstanding	670	\$ 425.00	1.75 years	-
Balance – June 30, 2013 – exercisable	670	\$ 425.00	1.75 years	-
Outstanding options held by related parties – 2013	-			
Exercisable options held by related parties – 2013	-			

**(G) Stock Warrants**

All warrants issued during the six months ended June 30, 2013 were accounted for as derivative liabilities. See Note 5.

During the six months ended June 30, 2013, the Company entered into convertible equity agreements. As part of these agreements, the Company issued warrants to convert 1,500,000 shares of Series D preferred stock into 3,000,000 shares of common stock.

A summary of warrant activity for the Company for the six months ended June 30, 2013 is as follows:

	Number of Warrants	Weighted Average Exercise Price
Outstanding – December 31, 2012	89	\$ 1,275

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Granted	3,040,000		4.09
Exercised	(2,710,000	)	4.00
Balance as June 30, 2013	330,089	\$	5.13

Warrants Outstanding			Warrants Exercisable			
Range of Exercise Prices	Number Outstanding	Weighted Average Remaining Contractual Life (in years)	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price	Intrinsic Value
\$4 - \$1,275	330,089	0.95	\$ 5.13	330,089	\$ 5.13	1,340,000

**(H) Treasury Stock**

During the six months ended June 30, 2013, the Company repurchased 18,825 shares of its common stock for the total sum of \$260,000 as part of a settlement. Of this amount, 103,537 or \$5.50 per share was considered repurchase of securities and \$156,463 was recorded as a loss on settlement. The Company records the value of its common stock held in treasury at cost. The Company has not cancelled or retired these shares, and they remain available for reissuance. The Company has a stock repurchase plan in place but has suspended it indefinitely.

**(I) Consulting Agreement**

On July 19, 2012, we entered into a consulting agreement (the “Original GRQ Consulting Agreement”) with GRQ Consultants, Inc. (“GRQ”, and together with Melechdavid, collectively, the “Consultants”). The Original GRQ Consulting Agreement provides that the Company will issue to GRQ shares of common stock in an amount equal to 4.2% of the Company’s outstanding common stock on a fully diluted (as-converted) basis. Further, until July 12, 2014, the Company is required to ensure that GRQ shall maintain its 4.2% fully diluted equity position. The term of the Original GRQ Consulting Agreement is 12 months.

On April 2, 2013, the Company entered into a first amendment to the Original Melechdavid Consulting Agreement with Melechdavid, effective as of March 28, 2013 (the “Melechdavid Amended Agreement”). Pursuant to the Melechdavid Amended Agreement, Melechdavid agreed to cap the shares of the Company’s common stock, \$0.001 par value per share (the “Common Stock”) that it is entitled to receive under the Original Melechdavid Consulting Agreement to no more than 570,000 shares of Common Stock of the Company, after giving effect to the 1-for-850 reverse stock split of the Common Stock effected by the Company on November 26, 2012. In connection with the execution and delivery of the Melechdavid Amended Agreement, the Company issued Melechdavid an aggregate of 341,247 shares of Common Stock on March 29, 2013 and 228,753 shares of Common Stock on April 5, 2013 as full satisfaction of the Company’s obligations under the Original Melechdavid Consulting Agreement.

**MusclePharm Corporation and Subsidiary**

**Notes to Consolidated Financial Statements**

**(June 30, 2013)**

**(Unaudited)**

On April 2, 2013, the Company entered into a first amendment to the Original GRQ Consulting Agreement with GRQ, effective as of March 28, 2013 (the "GRQ Amended Agreement"). Pursuant to the GRQ Amended Agreement, GRQ agreed to cap the shares of the Company's Common Stock that it is entitled to receive under the Original GRQ Consulting Agreement to no more than 420,000 shares of Common Stock of the Company, after giving effect to the 1-for-850 reverse stock split of the Common Stock effected by the Company on November 26, 2012. In connection with the execution and delivery of the GRQ Amended Agreement, the Company issued GRQ an aggregate of 305,889 shares of Common Stock on March 29, 2013 and 78,753 shares of Common Stock on April 5, 2013 as full satisfaction of the Company's obligations under the Original GRQ Consulting Agreement. The Company had previously issued GRQ 35,359 shares of Common Stock pursuant to the Original GRQ Consulting Agreement.

During the three and six months period ending June 30, 2013, the Company recognized expense related to the GRQ and Melechdavid agreements of \$3,037,636 and \$6,591,816, respectively. These expenses are classified under General and Administrative Expenses in the Consolidated Statement of Operations. The Company's obligations under the GRQ and Melechdavid agreements were completely satisfied as of July 12, 2013 and the agreements have not been renewed or extended.

**Note 8: Commitments, Contingencies and Other Matters**

**(A) Operating Lease**

The Company has various non-cancelable leases with terms expiring through 2017.

Future minimum annual lease payments for the above leases are approximately as follows:

Years Ending December 31,

2013 (6 months)	\$246,608
2014	556,868
2015	391,069
2016	79,860
2017	19,965
Total minimum lease payments	\$ 1,294,370

Rent expense for the six months ended June 30, 2013 and 2012, was \$298,887 and \$117,247, respectively.

## **(B) Legal Matters**

From time to time, the Company is or may become involved in various legal proceedings that arise in the ordinary course of business or otherwise. Legal proceedings are subject to inherent uncertainties as to timing, outcomes, costs, expenses and time expenditures by the Company's management and others on behalf of the Company. Although there can be no assurance, based on information currently available the Company's management believes that the outcome of legal proceedings that are pending or threatened against the Company will not have a material effect on the Company's financial condition. However, the outcome of any of these matters is neither probable nor reasonably estimable.

As of June 30, 2013, the Company was a party defendant in the following legal proceedings, each of which the Company: (a) believes is without merit; and (b) intends to defend vigorously:

**MusclePharm Corporation and Subsidiary**

**Notes to Consolidated Financial Statements**

**(June 30, 2013)**

**(Unaudited)**

*The Tawnsaura Group, LLC v MusclePharm Corporation, Case No: 8:12-cv-01476-JVS-RNB in the United States District Court for the Central District of California.* Date instituted: September 12, 2012. Plaintiff alleges patent infringement for MusclePharm's use of Citrulline Malate in its products. To date, Plaintiff has filed against over 70 different manufacturers of dietary supplements and sports nutrition products. MusclePharm is part of a joint defense group and believes this case is without merit due to the existence of prior art.

*William Bossung and Bishop Equity Partners LLC v. MusclePharm Corporation,* Clark County, Nevada District Court. Date instituted: January 17, 2012. Plaintiff alleges that additional monetary payments are due in respect of a settlement for outstanding warrants.

*Nageen Dehesh v MusclePharm Corporation, Case No: SC120793 in the Superior Court of the State of California, County of Los Angeles West District.* Date instituted: May 30, 2012. Plaintiff alleges she is owed payment for introducing MusclePharm to investors and/or raising capital. Plaintiff is not a licensed broker dealer and there was no agreement between the parties.

As of June 30, 2013, the Company was a party plaintiff in the following legal matters:

*MusclePharm Corporation v. Swole Sports Nutrition, LLC,* United States District Court for the Southern District of Florida. Date instituted: March 15, 2012. The Company filed this action for trademark infringement against after the Defendant started marketing and selling a dietary supplement named "Turbo Shred". The Company has sold "Shred Matrix" since April 2, 2008, and the mark "MusclePharm Shred Matrix" was granted registration by the USPTO on September 21, 2010. The parties have reached a coexistence and settlement agreement whereby the case would be dismissed. The court dismissed the case on July 15, 2013.

**(C) Payroll Taxes**

As of June, 2013, accounts payable and accrued expenses included \$87,339 pertaining to accrued payroll taxes. The taxes represent employee withholdings that have yet to be remitted to the taxing agencies.

**(D) Product Liability**

As a manufacturer of nutritional supplements and other consumer products that are ingested by consumers, the Company may be subject to various product liability claims. Although we have not had any material claims to date, it is possible that current and future product liability claims could have a material adverse effect on our business or financial condition, results of operations or cash flows. The Company currently maintains product liability insurance with a deductible/retention of \$10,000 per claim with an aggregate cap on retained loss of \$5,000,000. At June 30, 2013 the Company had not recorded any accruals for product liability claims.

**(E) Other Liabilities and Regulatory Matters**

Subsequent to December 31, 2012, the Company determined that it may have potential liabilities related to the filing of certain informational returns required by governmental authorities. Management has developed a plan to address these matters and does not currently expect a significant adverse impact on its financial position or results of operations.

**Note 9: Defined Contribution Plan**

The Company established a 401(k) Plan (the "401(k) Plan") for eligible employees of the Company. Generally, all employees of the Company who are at least twenty-one years of age and who have completed one year of entry service are eligible to participate in the 401(k) Plan. The 401(k) Plan is a defined contribution plan that provides that participants may make voluntary salary deferral contributions, on a pretax basis, of up to \$17,000 for 2012 (subject to make-up contributions) in the form of voluntary payroll deductions. The Company may make discretionary contributions. During the six months ended June 30, 2013 and 2012 the Company's matching contribution was \$28,530 and \$18,251, respectively.



**MusclePharm Corporation and Subsidiary****Notes to Consolidated Financial Statements****(June 30, 2013)****(Unaudited)****Note 10: Related Party Transactions**

The Chief Executive Officer of one of our major customers is the brother of our Chief Marketing Officer. Our Chief Financial Officer also indirectly owns 1.75% of the equity interest in such customer. We do not offer preferential pricing of our products to this customer based on these relationships.

**Note 11: Subsequent Events****(A) Restricted Stock Grant**

On June 25, 2013, our board of directors (“Board”) approved restricted stock grants (the “Restricted Stock”) to certain key employees, including named executive officers and directors, conditioned upon the execution and delivery of certain restricted stock agreement between the Company and such employees, officers and directors (the “Restricted Stock Agreements”). The Restricted Stock Agreements were executed and delivered by the parties on July 5, 2013. The Board approved Restricted Stock grants of the Company’s common stock in the aggregate amount of 1,550,000 shares including shares of the Company’s restricted stock to the following named executive officers and directors in the following amounts:

<b>Name</b>	<b>Title</b>	<b>Number of Shares of Restricted Stock</b>
Brad J. Pyatt	Co-Chairman, CEO and President	350,000
L. Gary Davis	Chief Financial Officer	200,000
John H. Blucher	Co-Chairman and Executive Vice President	150,000
Richard Estalella	Chief Operating Officer	100,000
Jeremy R. DeLuca	Executive Vice President – Chief Marketing Officer	225,000
Cory J. Gregory	Executive Vice President	150,000
Michael Doron	Director	25,000
James Greenwell	Director	25,000
Donald W. Prosser	Director	25,000

Pursuant to the Restricted Stock agreements, seventeen percent (17%) of each individual grant shall vest on December 31, 2013, and the remaining 83% shall vest on December 31, 2015. The grants for all will vest immediately upon (i) a change of control, and are subject to, such executive and/or employees continued employment, and in the case of any director, such director's continued service on the Board, and (ii) an employee, who has an entered into an employment agreement with the Company, serving the duration of the term of such employment agreement in accordance with its terms. The total value on the date of the grant was \$17,065,500, and will be amortized over the vesting periods as described above with the exception of certain executives under employment agreements that terminate prior to December 31, 2015. Those executives' grants will be amortized over the remaining term of their employment agreements.

**(B)**

**Inventory**

On July 1, 2013, the Company substantially terminated a Distribution Agreement dated November 17, 2010 with one of our key product manufacturers in which the manufacturer received and fulfilled customer sales orders for a majority of our products as more fully discussed in the "Shipping and Handling" section of Note 2 above. In connection with the termination of the agreement, we purchased an aggregate \$4,664,421 of product inventory, and the Company took back control of customer order fulfillment through our Franklin, Tennessee warehouse.

**(C)**

**Endorsement Agreements**

On July 26, 2013, the Company entered into an Endorsement Licensing and Co-Branding Agreement by and among, the Company, Arnold Schwarzenegger, Marine MP, LLC, and Fitness Publications, Inc. Under the terms of the Agreement, Mr. Arnold Schwarzenegger will endorse the Company's products and a special Arnold Schwarzenegger product line of between 4 and 8 products will be marketed under Mr. Schwarzenegger's name and likeness. In connection with this agreement, the Company issued Marine MP, LLC 780,000 restricted shares of common stock.

**MusclePharm Corporation and Subsidiary**

**Notes to Consolidated Financial Statements**

**(June 30, 2013)**

**(Unaudited)**

**(D) Board of Directors and Corporate Officer Changes**

On August 6, 2013, our board of directors appointed both Richard Estalella and Daniel J. McClory to serve on the Company's Board of Directors. The Board of Directors has determined that Mr. McClory is an independent director pursuant to the rules of the NASDAQ stock market. Mr. Estalella joined the Company in April of 2013 and has served since that time as Chief Operating Officer.

There is no family relationship between either of Mr. Estalella or Mr. McClory and any of our other officers and directors. There are no understandings or arrangements between either of Mr. Estalella or Mr. McClory and any other person pursuant to which either was selected as an officer.

Except for the aforementioned arrangements, there has not been any transaction or currently proposed transaction, in which the Company was or is to be a participant and the amount involved exceeds \$120,000, and in which either of Mr. Estalella or Mr. McClory had or will have a direct or indirect material interest since the beginning of the Company's last fiscal year.

Additionally, on August 6, 2013, Jeremy R. DeLuca and the Company agreed that Mr. DeLuca's title with the Company would be changed from that of Executive Vice President and Chief Marketing Officer to President of Sales and Marketing. The Board of Directors voted to accept this new designation. Accordingly, Mr. DeLuca will no longer be a named executive officer, including for purposes of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). The change in Mr. DeLuca's title was not as a result of any disagreements between him and the Company including with respect to the Company's operations, policies or practices.

**(E) Private Placement of Stock**

On August 9, 2013 the Company closed a \$2.5 million common stock offering. MusclePharm entered into subscription agreements with accredited investors whereby it sold 238,096 restricted shares of its common stock at \$10.50 per share. At the time of filing this report on Form 10-Q, these shares had not been issued but will be issued in

the very near future.

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

The following discussion should be read in conjunction with the accompanying unaudited consolidated financial statements and related notes thereto, included elsewhere in this Quarterly Report on Form 10-Q and in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2012 that was filed with the SEC on April 1, 2013.

### **Forward-Looking Information**

Certain statements contained in this report on Form 10-Q are not statements of historical fact and constitute forward-looking statements within the meaning of the various provisions of the Securities Act of 1933, as amended, (the "Securities Act") and the Securities Exchange Act of 1934, as amended (the "Exchange Act"), including, without limitation, the statements specifically identified as forward-looking statements within this report. Many of these statements contain risk factors as well. In addition, certain statements in our future filings with the SEC, in press releases and in oral and written statements made by or with our approvals which are not statements of historical fact constitute forward-looking statements within the meaning of the Securities Act and the Exchange Act. Examples of forward-looking statements, include, but are not limited to: (i) projections of capital expenditures, revenues, income or loss, earnings or loss per share, capital structure, and other financial items, (ii) statements of our plans and objectives or our management or board of directors, (iii) statements of future economic performance and (iv) statements of assumptions underlying such statements. Words such as "believes," "anticipates," "expects," "intends," "targeted," "may," "will," and similar expressions are intended to identify forward-looking statements but are not the exclusive means of identifying such statements. Such forward-looking statements are subject to a number of risks and uncertainties, including those identified in the "Risk Factors" section of our Annual Report on Form 10-K for the year ended December 31, 2012 and filed with the SEC on April 1, 2013.

Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance, or achievements. Except as required by applicable law, including the securities laws of the United States, we do not intend to update any of the forward-looking statements to conform these statements to actual results.

Our financial statements are prepared in accordance with GAAP. These accounting principles require us to make certain estimates, judgments and assumptions. We believe that the estimates, judgments and assumptions upon which we rely are reasonable based upon information available to us at the time that these estimates, judgments and assumptions are made. These estimates, judgments and assumptions can affect the reported amounts of assets and liabilities as of the date of the financial statements as well as the reported amounts of revenues and expenses during the periods presented. Our financial statements would be affected to the extent there are material differences between

these estimates and actual results. In many cases, the accounting treatment of a particular transaction is specifically dictated by GAAP and does not require management's judgment in its application. There are also areas in which management's judgment in selecting any available alternative would not produce a materially different result. The following discussion should be read in conjunction with our consolidated financial statements and notes thereto appearing elsewhere in this report on Form 10-Q.

## **Business Overview**

We develop, market and sell athlete-focused, high quality nutritional supplements primarily to specialty resellers. Our products have been formulated to enhance active fitness regimens, including muscle building, weight loss and maintaining general fitness. Our nutritional supplements are available for purchase in over 10,000 U.S. retail outlets, including Dick's Sporting Goods, GNC, Vitamin Shoppe and Vitamin World. We also sell our products to over 100 online channels, including bodybuilding.com, amazon.com, gnc.com and vitacost.com. Internationally, our nutritional supplements are currently sold in over 110 countries, and we expect that international sales will be a significant part of our sales for the foreseeable future.

We started formulating our nutritional supplements in 2008 for consumption by active individuals, high performance athletes and fitness enthusiasts. We launched our sales and marketing programs in late 2008 through our internal sales executives and staff targeting specialty retail distributors.

Our wide-range variety of nutritional supplements, include Assault™, Combat Powder™, MusclePharm MuscleGel, MusclePharm Shred Matrix®, and Re-Con®. These products are comprised of amino acids, herbs, and proteins tested by our scientists for the overall health of athletes. We developed these nutritional supplements to enhance the effects of workouts, repair muscles, and nourish the body for optimal physical fitness.

## **Our Growth and Core Marketing Strategy**

Our primary growth strategy is to:

· increase our product distribution and sales through increased market penetrations both domestically and internationally;

· increase our margins by focusing on streamlining our operations and seeking operating efficiencies in all areas of our operations;



- continue to conduct additional testing of the safety and efficacy of our products and formulate new products; and
- increase awareness of our products by increasing our marketing and branding opportunities through endorsements, sponsorships and brand extensions.

Our core marketing strategy is to brand MusclePharm as the “must have” fitness brand for workout enthusiasts and elite athletes. We seek to be known as the athlete’s company, run by athletes who create their products for other athletes both professional and otherwise. We believe that our marketing mix of endorsers, sponsorships and providing sample products for our retail resellers to use is an optimal strategy to increase sales.

## Results of Operations

### For the Three Months Ended June 30, 2013 and 2012 (unaudited):

	Three Months Ended June 30,	
	2013	2012
Sales - gross	\$28,515,483	\$18,869,103
Discounts and sales allowances	(3,035,424 )	(3,439,763 )
Sales - net	25,480,059	15,429,340
Cost of sales	17,566,718	12,942,605
Gross profit	7,913,341	2,486,735
General and administrative expenses	10,654,272	4,151,076
Loss from operations	(2,740,931 )	(1,664,341 )
Other income - net	319,123	7,846,245
Net (Loss) Income	\$(2,421,808 )	\$6,181,904
Net (loss) income per share - basic and diluted	\$(0.34 )	\$3.78
Weighted average number of common shares outstanding during the period – basic and diluted	7,226,849	1,633,676

### *Sales - gross*

Gross sales increased approximately \$9.6 million or 51% to \$28,516,000 for the three months ended June 30, 2013, compared to \$18,869,000 for the three months ended June 30, 2012. The increase in sales was due primarily to increased awareness of our product brand, combined with hiring additional sales and marketing staff, and adding new products in an effort to expand our customer base. Since inception, we have focused on an aggressive marketing plan



to penetrate the market. As such, significant promotional expenditures have been made to increase product sales through adding new customers and expanding our product line.

In this quarter the Company launched a women's line named FitMiss. The momentum is beginning to show increasing sales for this new product line. The Company believes it has a good position for market share with a women's line of products. The Company is also considering other new products. Overall as a direct result of our aggressive marketing plan, our products are currently being offered in more retail stores, both domestically and internationally, receiving better shelf placement, and receiving recognized awards compared to the prior period. At the 2012 Bodybuilding.com Supplement Awards, we received three Awards of Excellence; (i) the "Brand of the Year" award, (ii) the "Packaging of the Year" award, and (iii) the "Pre-Workout Supplement of the Year" award for Assault™. Assault™ and MusclePharm remains the product of choice for the Ultimate Fighting Championship, UFC.

### *Discounts and sales allowances*

Discounts and sales allowances for the three months ended June 30, 2013 decreased to approximately \$3,035,000 or 10.6% of gross sales as compared to \$3,440,000 or 18.2% of gross sales for the three months ended June 30, 2012. This decrease in discounts and allowances is a result driven by continued efforts to place controls around discounting and greater efforts to define customer terms and allowances.

***Sales - net***

Net sales increased approximately \$10.1 million or 65% to \$25,480,000 for the three months ended June 30, 2013, compared to \$15,429,000 for the three months ended June 30, 2012. A significant growth area for the Company was nutritional product sales in international markets. International sales are included in the results of operations and increased approximately \$3.5 million or 56% to \$9,833,000 for the three months ended June 30, 2013, compared to \$6,302,000 for the three months ended June 30, 2012.

***Gross Profit***

Gross profit increased approximately \$5.4 million or 218% to \$7,913,000 for the three months ended June 30, 2013, compared to \$2,487,000 for the three months ended June 30, 2012. The gross profit percentage increased to approximately 31% of net sales during the three months ended June 30, 2013, from 16% for the three months ended June 30, 2012. This increase was primarily due to the reduction in discounts as a percentage of sales, new product pricing from our Tennessee manufacturer, and the reduction of shipping costs. As discussed in Note 2 of the financial statements for shipping, the Company is handling its own shipping and has decreased the cost to ship product to the customer thereby increasing gross profit. Shipping expense for the three months ended June 30, 2013 was 2.6% of net sales down from 3.2% of net sales for the three months ended June 30, 2012.

For the three months ended June 30, 2013 the discounts as a percentage of gross sales was 10.6% compared to the three months ended June 30, 2012 of 18.2%. We have also experienced a decrease in cost of goods sold as a result of improved product pricing. For the three months ended June 30, 2013 the cost of goods as a percentage to sales was 69% compared to the three months ended June 30, 2012 of 84%. We expect to focus on streamlining our operations and seek operating efficiencies in order to further improve our gross profit percentage.

***General and Administrative Expenses***

General and administrative (“G&A”) expenses for the three months ended June 30, 2013, increased to approximately \$10,654,000, compared to approximately \$4,151,000 for the three months ended June 30, 2012 a 157% increase. Part of the reason for this increase in G&A is two consulting contracts of GRQ and Melechdavid. These contracts, categorized in the table below as professional fees, were entered into by the Company to promote the growth and expansion necessary to expand and raise capital and repay the previous existing debt by which the Company was encumbered. The total amount booked as expense for these advisory contracts in the second quarter of 2013 totaled approximately \$3.0 million and these contracts were satisfied as explained in Note 7 Stockholder’s Equity. This expense represents 46% of the total increase in the general and administrative expenses. The Company’s obligations under the GRQ and Melechdavid agreements were completely satisfied as of July 12, 2013 and the agreements have

not been renewed or extended.

The 65% increase in sales necessitated increases in our general and administrative expenses and included \$1,231,000 in the area of advertising and promotions used to promote brand and product awareness. We expect as we continue to promote our brand and products, these areas and levels of promotion will hold steady or increase relative to overall efforts to increase product awareness and sales.

Another area of increase is consulting expenses of \$567,000 related to consulting on a variety of matters including investor relations, product research and development, product certifications, capital acquisition, and debt retirement.

The \$6.5 million increase in general and administrative expenses including the significant items listed above were partially offset by the decrease of \$182,000 in stock based compensation.

The following table provides an overview of expense categories and percentage of net revenue:

	Three Months Ended June 30,			
	2013	% of Revenue	2012	% of Revenue
Advertising Expense	\$3,275,200	12.90 %	\$2,044,005	13.20 %
Operating Expense	1,918,665	7.50 %	1,298,392	8.40 %
Professional & R&D Expense	3,862,997	15.10 %	612,239	4.00 %
Salary and Wage Expense	1,597,410	6.30 %	196,440	1.30 %
Total G&A Expense	\$10,654,272	41.80 %	\$4,151,076	26.90 %

### ***Loss from Operations***

The net loss from operations for the three months ended June 30, 2013, was approximately \$2,741,000, compared to a net loss of approximately \$1,664,000 for the three months ended June 30, 2012.

***Other Income (Expenses)***

Other income was \$319,000 for the three months ended June 30, 2013, compared to the \$7,846,000 for the three months ended June 30, 2012. Refer to Note 5 for further detail of costs related to derivative agreements.

	Three Months Ended	
	June 30, 2013	2012
Derivative expense	\$-	\$(1,029,541)
Change in fair value of derivative liabilities	\$272,681	\$9,854,045
Gain (loss) on settlement of accounts payable and debt	\$47,671	\$-
Interest expense	\$(1,125 )	\$(976,686 )
Other income	\$(104 )	\$(1,573 )
Total other expenses	\$319,123	\$7,846,245

***Net (Loss) Income***

For the foregoing reasons, we had a net loss of approximately \$2,422,000 for the three months ended June 30, 2013, compared to net income of approximately \$6,182,000 for the three months ended June 30, 2012.

Inflation did not have a material impact on our operations for the period. Other than the foregoing, management knows of no trends, demands, or uncertainties that are reasonably likely to have a material impact on our results of operations.

**For the Six Months Ended June 30, 2013 and 2012 (unaudited):**

	Six Months Ended	
	June 30, 2013	2012
Sales - gross	\$53,439,519	\$38,171,872
Discounts and sales allowances	(5,398,293 )	(6,181,852 )
Sales - net	48,041,226	31,990,020
Cost of sales	31,963,124	25,837,767

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Gross profit	16,078,102	6,152,253
General and administrative expenses	19,540,512	8,543,887
Loss from operations	(3,462,410 )	(2,391,634 )
Other income (expenses) - net	(6,321,379 )	(7,461,755 )
Net Loss	\$ (9,783,789 )	\$ (9,853,389 )
Net loss per share - basic and diluted	\$(1.72 )	\$(6.44 )
Weighted average number of common shares outstanding during the period – basic and diluted	5,686,323	1,530,850

***Sales - gross***

Gross sales increased approximately \$15.3 million or 40% to \$53,440,000 for the six months ended June 30, 2013, compared to \$38,172,000 for the six months ended June 30, 2012. The increase in sales was due primarily to increased awareness of our product brand, combined with hiring additional sales and marketing staff, and adding new products in an effort to expand our customer base. Since inception, we have focused on an aggressive marketing plan to penetrate the market. As such, significant promotional expenditures have been made to increase product sales through adding new customers and expanding our product line.

In this quarter the Company launched a women's line named FitMiss. The momentum is beginning to show increasing sales for this new product line. The Company believes it has a good position for market share with a women's line of products. The Company is also considering other new products. Overall as a direct result of our aggressive marketing plan, our products are currently being offered in more retail stores, both domestically and internationally, receiving better shelf placement, and receiving recognized awards compared to the prior period. At the 2012 Bodybuilding.com Supplement Awards, we received three Awards of Excellence; (i) the "Brand of the Year" award, (ii) the "Packaging of the Year" award, and (iii) the "Pre-Workout Supplement of the Year" award for Assault™ and MusclePharm remains the product of choice for the Ultimate Fighting Championship, UFC.

### ***Discounts and sales allowances***

Discounts and sales allowances for the six months ended June 30, 2013 decreased to approximately \$5,398,000 or 10.1% of gross sales as compared to \$6,182,000 or 16.2% of gross sales for the six months ended June 30, 2012. This decrease in discounts and allowances is a result driven by continued efforts to place controls around discounting and greater efforts to define customer terms and allowances.

### ***Sales - net***

Net sales increased approximately \$16.1 million or 50% to \$48,041,000 for the six months ended June 30, 2013, compared to \$31,990,000 for the six months ended June 30, 2012. A significant growth area for the Company was nutritional product sales in international markets. International sales are included in the results of operations and increased approximately \$7.5 million or 84% to \$16,456,000 for the six months ended June 30, 2013, compared to \$8,963,000 for the six months ended June 30, 2012.

### ***Gross Profit***

Gross profit increased approximately \$9.9 million or 161% to \$16,078,000 for the six months ended June 30, 2013, compared to \$6,152,000 for the six months ended June 30, 2012. The gross profit percentage increased to approximately 33% of net sales during the six months ended June 30, 2013, from 19% for the six months ended June 30, 2012. This increase was primarily due to the reduction in discounts as a percentage of sales, new product pricing from our Tennessee manufacturer, and the reduction of shipping costs. As discussed in Note 2 of the financial statements for shipping, the Company is handling its own shipping and has decreased the cost to ship product to the customer thereby increasing gross profit. Shipping expense for the six months ended June 30, 2013 was 2.3% of net sales down from 3.3% of net sales for the six months ended June 30, 2012.

For the six months ended June 30, 2013 the discounts as a percentage of gross sales was 10.1% compared to the six months ended June 30, 2012 of 16.2%. We have also experienced a decrease in cost of goods sold as a result of improved product pricing For the six months ended June 30, 2013 the cost of goods as a percentage to sales was 67% compared to the six months ended June 30, 2012 of 81%. We expect to focus on streamlining our operations and seek operating efficiencies in order to further improve our gross profit percentage.

### ***General and Administrative Expenses***

General and administrative (“G&A”) expenses for the six months ended June 30, 2013, increased to approximately \$19,541,000, compared to approximately \$8,544,000 for the six months ended June 30, 2012 a 129%, increase. A primary reason for this increase in G&A is two consulting contracts of GRQ and Melechdavid. These contracts, categorized in the table below as professional fees, were entered into by the Company to promote the growth and expansion necessary to expand and raise capital and repay the previous existing debt by which the Company was encumbered. The total amount booked as expense for these advisory contracts in the first half of 2013 totaled approximately \$6,592,000 and these contracts were satisfied as explained in Note 7 Stockholder’s Equity. This expense represents 60% of the total increase in the general and administrative expenses. The Company’s obligations under the GRQ and Melechdavid agreements were completely satisfied as of July 12, 2013 and the agreements have not been renewed or extended.

The 50% increase in sales necessitated increases in our general and administrative expenses and included \$1,616,000 in the area of advertising and promotions used to promote brand and product awareness. We expect as we continue to promote our brand and products, these areas and levels of promotion will hold steady or increase relative to overall efforts to increase product awareness and sales. This increase was partially offset by a decrease in apparel and athlete endorsement/sponsorship of \$307,000. Another area of increase is legal fees of \$276,000 related to efforts required to obtain financing and dispute resolutions.

The \$11 million increase in general and administrative expenses including the significant items listed above were partially offset by the decrease of \$342,000 in stock based compensation.

The following table provides an overview of expense categories and percentage of net revenue:

	Six Months Ended June 30,					
	2013	% of Revenue	2012	% of Revenue		
Advertising Expense	\$5,592,577	11.60	% \$3,976,840	12.40	%	
Operating Expense	3,064,221	6.40	% 2,004,595	6.30	%	
Professional & R&D Expense	8,022,846	16.70	% 894,798	2.80	%	
Salary and Wage Expense	2,860,868	6.00	% 1,667,654	5.20	%	
Total G&A Expense	\$19,540,512	40.70	% \$8,543,887	26.70	%	

### ***Loss from Operations***

Our net loss from operations for the six months ended June 30, 2013, was \$3,462,000, compared to \$2,392,000 for the six months ended June 30, 2012.

### ***Other Income (Expenses)***

Other expenses were \$6,321,000 for the six months ended June 30, 2013, compared to the \$7,462,000 for the six months ended June 30, 2012. During the six months ended June 30, 2013, the Company issued warrants to convert 1,500,000 shares of preferred stock into 3,000,000 shares of common stock. Refer to Note 5 for further detail of costs related to derivative agreements.

	Six Months Ended June 30,	
	2013	2012
Derivative expense	\$(96,913 )	\$(2,486,451)
Change in fair value of derivative liabilities	\$(5,771,963)	\$1,496,874
Gain (loss) on settlement of accounts payable and debt	\$324,656	\$(2,941,826)
Interest expense	\$(781,445 )	\$(3,547,202)
Other income	\$4,286	\$16,850
Total other expenses	\$(6,321,379)	\$(7,461,755)

### ***Net Loss***

For the foregoing reasons, we had a net loss of approximately \$9,784,000 for the six months ended June 30, 2013, compared to approximately \$9,853,000 for the six months ended June 30, 2012.



Inflation did not have a material impact on our operations for the period. Other than the foregoing, management knows of no trends, demands, or uncertainties that are reasonably likely to have a material impact on our results of operations.

### Liquidity and Capital Resources

The following table summarizes total current assets, liabilities and working capital at June 30, 2013, compared to December 31, 2012.

	June 30, 2013	December 31, 2012	Increase/Decrease
Current Assets	\$ 21,748,744	\$ 4,949,881	\$ 16,798,863
Current Liabilities	\$ 10,641,490	\$ 16,520,456	\$ (5,878,966 )
Working Capital (Deficit)	\$ 11,107,254	\$ (11,570,575 )	\$ 22,677,829

Our primary source of operating cash has been through the sale of equity and through the issuance of convertible secured promissory notes and other short-term debt as discussed below.

The Company's management believes current levels of liquidity are sufficient for current operations, but additional capital may be needed to execute the business plan, which includes buying more inventory. There can be no assurance that such capital will be available on acceptable terms or at all.

On March 27, 2013, MusclePharm sold an aggregate of 703,236 shares of its common stock, \$0.001 par value per share at a per share price of \$8.50 in a private placement to certain accredited investors for an aggregate purchase price of approximately \$5,977,506, thereby providing working capital.

The common stock was sold pursuant to subscription agreements dated March 27, 2013 between the Company and the Purchasers. The Subscription Agreements contained customary terms regarding, among other things, representations and warranties and indemnification.

On May 6, 2013, MusclePharm sold an aggregate of 100,000 shares of its common stock, \$0.001 par value per share at a per share price of \$8.50 in a private placement to certain accredited investors, thereby providing working capital.

The common stock was sold pursuant to subscription agreements dated May 6, 2013 between the Company and the Purchasers. The Subscription Agreements contained customary terms regarding, among other things, representations and warranties and indemnification.

On June 3, 2013, MusclePharm sold an aggregate of 150,000 shares of its common stock, \$0.001 par value per share at a per share price of \$10.00 in a private placement to certain accredited investors, for an aggregate purchase price of approximately \$1,398,139 thereby providing working capital.

The common stock was sold pursuant to subscription agreements dated June 3, 2013 between the Company and the Purchasers. The Subscription Agreements contained customary terms regarding, among other things, representations and warranties and indemnification.

At June 30, 2013, we had cash of \$8,656,000 and working capital of approximately \$11,107,000 compared to cash of \$0 and a working capital deficit of approximately \$11,571,000 at December 31, 2012. The working capital increase of approximately \$22,678,000 was primarily due to a net increase in cash of \$8,656,000, an increase in accounts receivable of \$5,933,000 and a decrease in current liabilities of \$5,879,000.

Cash used in operating activities was \$5,164,810 for the six months ended June 30, 2013, as compared to cash provided by operating activities of \$438,007 for the six months ended June 30, 2012. The increase in cash used in operating activities of approximately \$5.6 million for the six months ended June 30, 2013, compared to the six months ended June 30, 2012, was primarily due to an increase in accounts receivable and prepaid expense of approximately \$7.6 million, an increase in the amortization of prepaid stock compensation of \$2.9 million, a decrease in customer deposits of approximately \$1.5 million, a decrease in depreciation and amortization expense of approximately \$2.7 million, and a decrease on loss on settlement of approximately \$3.3 million offset by a decrease in derivative expense and change in fair value of derivatives of approximately \$4.9 million, a decrease in inventory of approximately \$0.3 million, a decrease in accounts payable and accrued liabilities of approximately \$1.2 million and a decrease in net loss of approximately \$70,000.

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Cash used in investing activities decreased to \$353,566 from \$579,859 for the six months ended June 30, 2013 and 2012, due to slightly lower spending on fixed assets. Future investments in property and equipment, as well as further development of our Internet presence will largely depend on available capital resources.

Cash flows provided by financing activities were \$14,168,061 for the six months ended June 30, 2013, compared to cash flows used in financing activities of \$266,660 for the six months ended June 30, 2012. The approximately \$14.4 million increase was due to primarily to the net increase of approximately \$18.4 million net proceeds from equity offerings, a decrease of approximately \$0.4 million in the repurchase of common stock and a decrease of approximately \$0.1 million in debt issue costs offset by a decrease of approximately \$4.1 million in proceeds from issuance of debt and an increase in debt repayment of approximately \$0.3 million.

Cash Flows From Financing Activities:	Six Months Ended	
	June 30, 2013	2012
Proceeds from issuance of debt	\$-	\$4,073,950
Repayment of debt	(4,393,234 )	(4,058,442)
Debt issuance costs	-	(106,950 )
Repurchase of common stock	(103,537 )	(460,978 )
Proceeds from issuance of common stock and warrants	8,327,499	285,760
Proceeds from issuance of preferred stock	12,000,000	-
Stock issuance costs	(1,662,667 )	-
Net Cash Provided By Financing Activities	\$14,168,061	\$(266,660 )

### Off-Balance Sheet Arrangements

Other than the operating leases, as of June 30, 2013, we did not have any off-balance sheet arrangements. We are obligated under an operating lease for the rental of office space. Future minimum rental commitments with a remaining term in excess of one year as of June 30, 2013 are as follows:

Years Ending December 31,

2013(6 months)	\$246,608
2014	556,868
2015	391,069
2016	79,860
2017	19,965
Total minimum lease payments	\$1,294,370

### Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with GAAP requires 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.

Making estimates requires management to exercise significant judgment. It is at least reasonably possible that the estimate of the effect of a condition, situation or set of circumstances that existed at the date of the financial statements, which management considered in formulating its estimate could change in the near term due to one or more future non-conforming events. Accordingly, the actual results could differ significantly from estimates.

### Accounts Receivable and Allowance for Doubtful Accounts

Accounts receivable represents trade obligations from customers that are subject to normal trade collection terms. We periodically evaluate the collectability of our accounts receivable and considers the need to establish an allowance for doubtful accounts based upon historical collection experience and specific customer information. Accordingly, the actual amounts could vary from the recorded allowances.

We perform ongoing evaluations of our customers' financial condition and generally do not require collateral. Management reviews accounts receivable periodically and reduces the carrying amount by a valuation allowance that reflects management's best estimate of amounts that may not be collectible. Allowances, if any, for uncollectible accounts receivable are determined based upon information available and historical experience.

We do not charge interest on past due receivables. Receivables are determined to be past due based on the payment terms of the original invoices.

### **Fair Value of Financial Instruments**

We measure assets and liabilities at fair value based on an expected exit price as defined by the authoritative guidance on fair value measurements, which represents the amount that would be received on the sale of an asset or paid to transfer a liability, as the case may be, in an orderly transaction between market participants. As such, fair value may be based on assumptions that market participants would use in pricing an asset or liability. The authoritative guidance on fair value measurements establishes a consistent framework for measuring fair value on either a recurring or nonrecurring basis whereby inputs, used in valuation techniques, are assigned a hierarchical level.

The following are the hierarchical levels of inputs to measure fair value:

·Level 1: Observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2: Inputs reflect quoted prices for identical assets or liabilities in markets that are not active; quoted prices for similar assets or liabilities in active markets; inputs other than quoted prices that are observable for the assets or liabilities; or inputs that are derived principally from or corroborated by observable market data by correlation or other means.

Level 3: Unobservable inputs reflecting our assumptions incorporated in valuation techniques used to determine fair value. These assumptions are required to be consistent with market participant assumptions that are reasonably available.

## Revenue Recognition

We record revenue when all of the following have occurred: (1) persuasive evidence of an arrangement exists, (2) product has been shipped or delivered, (3) the sales price to the customer is fixed or determinable, and (4) collectability is reasonably assured.

Depending on individual customer agreements, sales are recognized either upon shipment of products to customers or upon delivery. We record sales allowances and discounts as a direct reduction of sales.

We have determined that advertising related credits that were granted to customers fell within the guidance of ASC No. 605-50-55 ("*Revenue Recognition*" – *Customer Payments and Incentives – Implementation Guidance and Illustrations*). The guidance indicates that, absent evidence of benefit to the vendor, appropriate treatment requires netting these types of payments against revenues and not expensing as advertising expense.

We have an informal seven day right to return products. There were nominal returns at the six month periods ended June 30, 2013 and 2012.

## Foreign Currency

We began operations in Canada in April 2012. The Canadian Dollar was determined to be the functional currency as the majority of the transactions related to the day to day operations of the business are exchanged in Canadian Dollars. At the end of the period, the financial results of the Canadian operation are translated into United States Dollars, which is the reporting currency, and added to the U.S. operations for consolidated company financial results. The revenue and expense items are translated using the average rate for the period and the assets and liabilities at the end of period rate. Transactions that have completed the accounting cycle and resulted in a gain or loss related to translation are recorded in realized gain or loss due to foreign currency translation under other income expense on the income statement. Transactions that have not completed their accounting cycle but appear to have gain or loss due to the translation process are recorded as unrealized gain or loss due to translation and held in the equity section on the balance sheet until such date the accounting cycle of a transaction is complete and the actual realized gain or loss is recognized.

## Beneficial Conversion Feature

For conventional convertible debt where the rate of conversion is below market value, we record a “beneficial conversion feature” (“BCF”) and related debt discount.

When we record a BCF, the relative fair value of the BCF would be recorded as a debt discount against the face amount of the respective debt instrument. The discount would be amortized to interest expense over the life of the debt.

### **Derivative Liabilities**

Fair value accounting requires bifurcation of embedded derivative instruments such as conversion features in convertible debt or equity instruments, and measurement of their fair value for accounting purposes. In determining the appropriate fair value, we use the Black-Scholes option-pricing model. In assessing the convertible debt instruments, management determines if the convertible debt host instrument is conventional convertible debt and further if there is a beneficial conversion feature requiring measurement. If the instrument is not considered conventional convertible debt, we will continue our evaluation process of these instruments as derivative financial instruments.

Once determined, derivative liabilities are adjusted to reflect fair value at each reporting period end, with any increase or decrease in the fair value being recorded in results of operations as an adjustment to fair value of derivatives. In addition, the fair value of freestanding derivative instruments such as warrants, are also valued using the Black-Scholes option-pricing model.

### **Debt Issue Costs and Debt Discount**

We may pay debt issue costs, and record debt discounts in connection with raising funds through the issuance of convertible debt. These costs are amortized over the life of the debt to interest expense. If a conversion of the underlying debt occurs, a proportionate share of the unamortized amounts is immediately expensed.

### **Original Issue Discount**

For certain convertible debt issued, we provide the debt holder with an original issue discount. The original issue discount is recorded to debt discount and additional paid in capital at an amount not to exceed gross proceeds raised, reducing the face amount of the note and is amortized to interest expense over the life of the debt.





## Share-Based Payments

Generally, all forms of share-based payments, including stock option grants, warrants, restricted stock grants and stock appreciation rights are measured at their fair value on the awards' grant date, based on estimated number of awards that are ultimately expected to vest. Share-based compensation awards issued to non-employees for services rendered are recorded at either the fair value of the services rendered or the fair value of the share-based payment, whichever is more readily determinable.

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

Not Applicable.

### Item 4. Controls and Procedures.

#### *(a) Evaluation of Disclosure Controls and Procedures*

Based on their evaluation as of the end of the period covered by this Quarterly Report on Form 10-Q, our Principal Executive Officer and Principal Financial Officer have concluded that our disclosure controls and procedures (as defined in Rules 13a-15(c) and 15d-15(e) under the Securities Exchange Act of 1934 as amended (the "Exchange Act") were not effective to ensure that information required to be disclosed by us in report that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our Principal Executive Officer and Principal Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

#### *(b) Changes in Internal Control Over Financial Reporting*

There were no changes in our internal control over financial reporting, as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act, during our most recently completed fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.



## **PART II – OTHER INFORMATION**

### **Item 1. Legal Proceedings.**

Except as disclosed in Note 8: Commitments, Contingencies and Other Matters, to the Financial Statements contained herein, we are currently not involved in any new litigation that we believe could have a material adverse effect on our financial condition or results of operations. Except as disclosed in Note 8: Commitments, Contingencies and Other Matters, there is no action, suit, proceeding, inquiry or investigation before or by any court, public board, government agency, self-regulatory organization or body pending or, to the knowledge of the executive officers of our Company or any of our subsidiaries, threatened against or affecting our company, our common stock, any of our subsidiaries or of our companies or our subsidiaries' officers or directors in their capacities as such, in which an adverse decision could have a material adverse effect.

### **Item 1A. Risk Factors.**

We believe there are no changes that constitute material changes from the risk factors previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2012, filed with the SEC on April 1, 2013. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results.

### **Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.**

The Company has not issued securities in addition to what is reported in a Current Report on Form 8-K, during the six months ended June 30, 2013.

### **Item 3. Defaults Upon Senior Securities.**

There were no defaults upon senior securities during the six months ended June 30, 2013.

### **Item 4. Mine Safety Disclosures**

Not applicable.

**Item 5. Other Information.**

None.

**Item 6. Exhibits.**

**Exhibit No. Description**

31.1\* Rule 13 (A) – 14(A) Certification of Principal Executive Officer

31.2\* Rule 13 (A) – 14(A) Certification of Principal Financial Officer

32.1\* Section 1350 Certification of Principal Executive Officer

32.2\* Section 1350 Certification of Principal Financial Officer

101.INS\*\* XBRL Instance Document

101.SCH\*\* XBRL Taxonomy Extension Schema

101.CAL\*\* XBRL Taxonomy Extension Calculation Linkbase

101.DEF\*\* XBRL Taxonomy Extension Definition Linkbase

101.LAB\*\* XBRL Taxonomy Extension Label Linkbase

101.PRE\*\* XBRL Taxonomy Extension Presentation Linkbase

\*Filed Herewith

\*\* In accordance with Regulation S-T, the XBRL-related information on Exhibit No. 101 to this Quarterly Report on Form 10-Q shall be deemed “furnished” herewith and not “filed.”

**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.

**MUSCLEPHARM CORPORATION**

Date: August 14, 2013 By: /s/ Brad J. Pyatt  
Name: Brad J. Pyatt  
Title: Chief Executive Officer and  
President  
(Principal Executive Officer)

Date: August 14, 2013 By: /s/ L. Gary Davis  
Name: L. Gary Davis  
Title: Chief Financial Officer, Treasurer  
(Principal Financial Officer)  
(Principal Accounting Officer)