

CIRTRAN CORP
Form 10-Q
November 19, 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 September 30, 2013

.. 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 000-49654

CirTran Corporation

(Exact name of registrant as specified in its charter)

Nevada

(State or other jurisdiction of incorporation or organization)

68-0121636

(I.R.S. Employer Identification No.)

4125 South 6000 West, West Valley City, Utah 84128
(Address of principal executive offices, including zip code)

(801) 963-5112

(Registrant's telephone number, including area code)

n/a

(Former name, former address and former fiscal year, if changed since last report)

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

Yes

No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes

No

Edgar Filing: CIRTRAN CORP - Form 10-Q

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

Large accelerated filer
Non-accelerated filer

Accelerated filer
Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).

Yes

No

Indicate the number of shares outstanding of each of the issuer’s classes of common stock, as of the latest practicable date. **As of November 19, 2013, issuer had 4,439,018,984 outstanding shares of common stock, par value \$0.001.**

CIRTRAN CORPORATION

FORM 10-Q

For the Quarterly Period Ended September 30, 2013

INDEX

| | <u>Page</u> | |
|---------------------------------------|---|----|
| PART I – FINANCIAL INFORMATION | | |
| Item 1 | Financial Statements (unaudited) | |
| | Condensed Consolidated Balance Sheets | 4 |
| | Condensed Consolidated Statements of Operations | 5 |
| | Condensed Consolidated Statements of Cash Flows | 6 |
| | Notes to Condensed Consolidated Financial Statements | 7 |
| Item 2 | Management’s Discussion and Analysis of Financial Condition and Results of Operations | 19 |
| Item 3 | Quantitative and Qualitative Disclosures About Market Risk | 24 |
| Item 4 | Controls and Procedures | 24 |
| PART II – OTHER INFORMATION | | |
| Item 1 | Legal Proceedings..... | 24 |
| Item 5 | Other Information..... | 24 |
| Item 6 | Exhibits..... | 25 |
| Signatures | | 26 |

PART I – FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

3

**CIRTRAN CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS**

| | September 30, 2013 (Unaudited) | De |
|---|---|-----------|
| ASSETS | | |
| Current assets | | |
| Cash and cash equivalents | \$ 33,241 | \$ |
| Trade accounts receivable, net of allowance for doubtful accounts of \$832,093 and \$832,093, respectively | 306,543 | |
| Inventory, net of reserve of \$2,255,644 and \$2,256,399, respectively | 240,914 | |
| Other | 27,651 | |
| Total current assets | 608,349 | |
| Investment in securities, at cost | 300,000 | |
| Long-term receivable, net of allowance of \$1,582,895 | - | |
| Property and equipment, net | 47,916 | |
| Other assets | 25,361 | |
| Total assets | \$ 981,626 | \$ |
| LIABILITIES AND STOCKHOLDERS' DEFICIT | | |
| Current liabilities | | |
| Checks written in excess of bank balance | \$ - | \$ |
| Accounts payable | 4,363,821 | |
| Related-party payable | 1,135,784 | |
| Short-term advances payable | 2,750,850 | |
| Accrued liabilities | 1,858,139 | |
| Accrued payroll and compensation expense | 2,935,607 | |
| Accrued interest | 1,926,141 | |
| Deferred revenue | 3,050,819 | |
| Derivative liability | 251,906 | |
| Convertible debenture | 2,215,528 | |
| Refundable customer deposits | 200,000 | |
| Current maturities of long-term debt | 214,085 | |
| Current liabilities to non-controlling interest holders | 2,544,365 | |
| Note payable to stockholders and members | 251,833 | |
| Total current liabilities | 23,698,878 | |
| Total liabilities | 23,698,878 | |
| Stockholders' deficit | | |
| CirTran Corporation stockholders' deficit: | | |
| Common stock, par value \$0.001; authorized 4,500,000,000 shares; issued and outstanding shares: 4,367,991,910 and 2,541,502,289 | 4,367,992 | |
| Additional paid-in capital | 29,335,710 | |

| | |
|--|----------------------|
| Subscription receivable | (17,000) |
| Accumulated deficit | (47,938,460) |
| Total CirTran Corporation and subsidiaries stockholders' deficit | (14,251,758) |
| Non-controlling interest | (8,465,494) |
| Total stockholders' deficit | (22,717,252) |
| Total liabilities and stockholders' deficit | \$ 981,626 \$ |

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

CIRTRAN CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)

| | Three months ended | | Nine months |
|---|---------------------------|---------------------|--------------------|
| | September 30, | | September |
| | 2013 | 2012 | 2013 |
| Net sales | \$ 658,361 | \$ 653,127 | \$ 2,623,204 |
| Cost of sales | (124,235) | (68,226) | (554,703) |
| Royalty expense | - | (39,594) | (37,494) |
| Gross profit | 534,126 | 545,307 | 2,031,007 |
| Operating expenses | | | |
| Selling, general and administrative expenses | 881,245 | 873,490 | 2,533,403 |
| Non-cash compensation expense | 11,000 | 16,331 | 41,872 |
| Total operating expenses | 892,245 | 889,821 | 2,575,275 |
| Income (loss) from operations | (358,119) | (344,514) | (544,266) |
| Other income (expense) | | | |
| Interest expense | (198,962) | (344,517) | (564,572) |
| Gain on settlement of debt | 260,061 | 108,864 | 1,703,618 |
| Gain (loss) on derivative valuation | 104,494 | 34,348 | 475,560 |
| Other income | - | (1,060) | - |
| Total other income (expense), net | 165,593 | (202,365) | 1,614,606 |
| Net income (loss) | (192,526) | (546,879) | 1,070,340 |
| Net loss (income) attributable to non-controlling interest | 343,264 | 222,685 | (494,004) |
| Net income (loss) attributable to CirTran Corporation and subsidiaries | \$ 150,738 | \$ (324,194) | \$ 576,336 |
| Basic and diluted income (loss) per common share | \$ 0.00 | \$ (0.00) | \$ 0.00 |
| Basic weighted-average common shares outstanding | 3,996,671,346 | 1,925,060,683 | 3,436,274,192 |
| Diluted weighted-average common shares outstanding | 6,343,999,346 | 1,925,060,683 | 5,783,602,192 |

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

CIRTRAN CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

| For the Nine Months Ended September 30, | 2013 | 2012 |
|---|------------------|------------------|
| Cash flows from operating activities | | |
| Net income (loss) | \$ 1,070,340 | \$ (2,540,462) |
| Adjustments to reconcile net income (loss) to net cash provided (used) in operating activities: | | |
| Depreciation and amortization | 38,118 | 68,225 |
| Inventory allowance | (755) | - |
| Change in valuation of derivative | (475,560) | 132,183 |
| Current liabilities to non-controlling interest holders | 124,365 | 170,666 |
| Gain on the settlement of debt | (1,703,618) | - |
| Non-cash compensation expense | 30,872 | 127,616 |
| Expenses paid by third-party on behalf of the company | - | 5,000 |
| Changes in assets and liabilities: | | |
| Trade accounts receivable | (144,075) | (472,160) |
| Inventories | (141,816) | 236,457 |
| Other current assets | (19,785) | (668) |
| Other assets | 199,128 | (21,204) |
| Accounts payable | (287,793) | 662,927 |
| Related-party payable | 180,128 | 162,600 |
| Accrued liabilities | 251,463 | (159,682) |
| Accrued payroll and compensation expense | 373,074 | 614,046 |
| Refundable customer deposits | 127,798 | (810,633) |
| Accrued interest | 535,582 | 803,497 |
| Deferred revenue | 66,700 | 1,205,704 |
| Net cash provided by (used in) operating activities | 224,166 | 184,112 |
| Cash flows from financing activities | | |
| Proceeds from non-controlling interest holders | 200,000 | 25,000 |
| Checks written in excess of bank balance | (17,118) | (182,095) |
| Proceeds from short-term advances | 248,058 | 234,350 |
| Payments on convertible debenture accrued interest | (64,395) | (165,000) |
| Payments on short-term advances | (565,353) | (230,650) |
| Net cash provided by (used in) financing activities | (198,808) | (318,395) |
| Net increase (decrease) in cash and cash equivalents | 25,358 | (134,283) |
| Cash and cash equivalents at beginning of period | 7,883 | 173,780 |
| Cash and cash equivalents at end of period | \$ 33,241 | \$ 39,497 |
| Supplemental disclosure of cash flow information: | | |
| Cash paid during the period for interest | \$ 64,395 | \$ 170,000 |
| Noncash investing and financing activities: | | |
| Common stock issued in exchange for forgiveness of | | |

Edgar Filing: CIRTRAN CORP - Form 10-Q

| | | | | |
|--|----|-----------|----|--------|
| Settlement of debt and liabilities | \$ | 1,948,381 | \$ | - |
| Conversion of current liabilities to non-controlling interests | \$ | 350,000 | \$ | 55,000 |
| Related party payable | \$ | - | \$ | 55,000 |
| Account receivable written off | \$ | - | \$ | 88,045 |

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

CIRTRAN CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

NOTE 1 – BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements include the accounts of CirTran Corporation and its subsidiaries (the “Company”). These financial statements have been prepared in accordance with Article 10 of Regulation S-X promulgated by the Securities and Exchange Commission (“SEC”). Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) have been condensed or omitted pursuant to such rules and regulations. These statements should be read in conjunction with the Company’s annual financial statements included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2012. In particular, the Company’s significant accounting policies were presented as Note 2 to the consolidated financial statements in that Annual Report. In the opinion of management, all adjustments necessary for a fair presentation have been included in the accompanying condensed consolidated financial statements and consist of only normal recurring adjustments. The results of operations presented in the accompanying condensed consolidated financial statements for the nine months ended September 30, 2013, are not necessarily indicative of the results that may be expected for the 12 months ending December 31, 2013.

NOTE 2 - REALIZATION OF ASSETS

The accompanying condensed consolidated financial statements have been prepared on the assumption that the Company will continue as a going concern. The Company had a net income of \$1,070,340 and a net loss of \$2,540,462 for the nine months ended September 30, 2013 and 2012, respectively. As of September 30, 2013, the Company had an accumulated deficit of \$47,938,460. In addition, the Company had cash from operations in the amount of \$224,166 and 184,112 during the nine months ended September 30, 2013 and 2012, respectively. The Company, however, had a negative working capital balance of \$23,090,529 as of September 30, 2013, and \$26,458,490 as of December 31, 2012. These conditions raise substantial doubt about the Company’s ability to continue as a going concern.

The Company’s ability to continue energy drink distribution, its principal source of revenue, is subject to interruption or termination because of ongoing disputes respecting the status of the Play Beverages, LLC, or PlayBev, license to market Playboy-licensed energy drinks. The Company is continuing its suit against Playboy Enterprises, Inc., or Playboy, in Illinois in an effort to enjoin Playboy’s termination of the license so the Company will be able to continue its beverage distribution segment. If the Playboy licensing dispute is not resolved satisfactorily through a negotiated

settlement or litigation in such proceeding, PlayBev would be required to terminate its beverage distribution activities, which are currently the principal source of the Company's revenues. Such termination may require the Company to cease its activities and seek protection from creditors.

In view of the matters described in the preceding paragraphs, recoverability of a major portion of the recorded asset amounts shown in the accompanying consolidated balance sheets is dependent upon continued operations of the Company, which in turn is dependent upon the Company's ability to meet its financing requirements on a continuing basis, to maintain or replace present financing, to acquire additional capital from investors, and to succeed in its future operations. The financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or amounts and classification of liabilities that might be necessary should the Company be unable to continue in existence.

The Company believes that its beverage business segment has the potential to have a substantial impact on its overall business. The Company plans to focus on the beverage business and the contract manufacturing business. For the beverage business, the Company plans to sell existing products to a globally expanding market and develop new products under the license agreement with Playboy. With regard to contract manufacturing, the Company's goal is to provide customers with manufacturing solutions for both new and more mature products, as well as across product generations.

The Company provides product marketing services to the direct response and retail markets for both proprietary and nonproprietary products. This segment provides campaign management and marketing services for the beverage distribution, direct response, and retail markets. The Company intends to continue to provide marketing and media services to support its own product efforts and offer to customers marketing service in channels involving television, radio, print media, and the Internet. The Company intends to serve the electronics assembly and manufacturing industries, although it anticipates that its focus will shift more to providing services on a subcontract basis.

NOTE 3 - INVENTORIES

Inventories are stated at the lower of average cost or market and consisted of the following:

| | September 30, 2013 | | December 31, 2012 |
|---------------------|-------------------------------|----|------------------------------|
| Raw Materials | \$ 1,729,054 | \$ | 1,691,500 |
| Work in Process | 222,461 | | 221,225 |
| Finished Goods | 545,043 | | 442,017 |
| Allowance / Reserve | (2,255,644) | | (2,256,399) |
| Totals | \$ 240,914 | \$ | 98,343 |

NOTE 4 – RELATED-PARTY TRANSACTIONS

Transactions Involving Officers, Directors, and Stockholders - In 2007, the Company appointed Fadi Nora to its Board of Directors. In addition to compensation the Company normally pays to nonemployee members of the Board, Mr. Nora is entitled to a quarterly bonus equal to 0.5% of any gross sales earned by the Company directly through Mr. Nora's efforts. As of September 30, 2013, the Company owed \$65,967 under this arrangement. As of September 30, 2013, the Company owed Mr. Nora \$1,034,929 in the form of unsecured advances. These advances and short-term bridge loans were approved by the Board of Directors under a 5% borrowing fee. The borrowing fees were waived by Mr. Nora on these loans. In addition, the Company owed Mr. Nora \$321,982 in accrued liabilities as of September 30, 2013, for selling, general, and administrative expenses that were paid for by Mr. Nora on a personal credit card.

The Company has agreed to issue 2,400,000 options to Mr. Nora as compensation for services provided as a Director of the Company. The terms of the director agreement require the Company to grant to Mr. Nora options to purchase 2,400,000 shares of the Company's stock each year, with the exercise price of the options being the market price of the Company's common stock as of the grant date. During the nine months ended September 30, 2013, the Company accrued for 2,400,000 stock options relating to the director agreement with Mr. Nora. The fair market value of the options was \$4,069, using the following assumptions: 7.0-year term, estimated volatility of 224.82%, and a discount rate of 0.0% (see also Note 11).

In 2007, the Company issued a 10% promissory note to a family member of the Company President in exchange for \$300,000. The note was due on demand after May 2008. During the nine months ended September 30, 2013, the Company made no payments towards the outstanding note. At September 30, 2013, the principal amount owing on the note was \$151,833. On March 31, 2008, the Company issued to this same family member, along with four other Company shareholders, promissory notes totaling \$315,000. The family member's note was for \$105,000. Under the terms of all the notes, the Company received total proceeds of \$300,000 and agreed to repay the amount received plus a 5% borrowing fee. The notes were due April 30, 2008, after which they were due on demand, with interest accruing at 12% per annum. During the nine months ended September 30, 2013, the Company made no payments towards the outstanding notes. The principal balance owing on the promissory notes as of September 30, 2013, totaled \$72,465.

On April 2, 2009, the Company President and a Director of the Company borrowed from a third party a total of \$890,000 in the form of four short-term promissory notes. The Company President and the Director of the Company signed personally for the notes. Because the loans were used to pay obligations of the Company, the Company has assumed full responsibility for the notes. Two of the notes were for a term of 60 days, with a 60-day grace period; a third note was for a term of 90 days; and a fourth note was for 24 days. Loan fees totaling \$103,418 were incurred with the issuance of the notes and are payable upon maturity of the notes. At September 30, 2013, two of the notes had a combined remaining balance of \$270,000 and comprised a portion of short-term advances payable of \$2,750,850. As of September 30, 2013, these notes were in default and are accruing interest at the default rate of 36% per year.

The Company has agreed to issue 6,000,000 options each year to the Company President as compensation for services provided as an officer of the Company. The terms of the employment agreement require the Company to grant to the Company President options to purchase 6,000,000 shares of the Company's stock each year, with the exercise price of the options being the market price of the Company's common stock as of the grant date. During the nine months ended September 30, 2013, the Company accrued for 6,000,000 stock options relating to the employee agreement with Mr. Hawatmeh. The fair market value of the options was \$10,171, using the following assumptions: estimated 7.0-year term, estimated volatility of 224.82%, and a discount rate of 0.0% (see also Note 11).

As of September 30, 2013, the Company owed the Company President a total of \$88,564 in short-term advances payable and 36,000,000 stock options with an aggregated fair value at time of grant of \$154,537. These advances and short-term bridge loans were approved by the Board of Directors under a 5% borrowing fee. The borrowing fees were waived by the Company's President on these loans.

Sublease - In an effort to operate more efficiently and focus resources on higher margin areas of the Company's business, on March 5, 2010, the Company and Katana Electronics, LLC, a Utah limited liability company ("Katana"), entered into certain agreements (collectively, the "Agreements") to reduce the Company's costs. The Agreements include an Assignment and Assumption Agreement, an Equipment Lease, and a Sublease Agreement relating to the Company's property. Pursuant to the terms of the Sublease, the Company agreed to sublease a certain portion of the Company's premises to Katana, consisting of the warehouse and office space used as of the close of business on March 4, 2010. The term of the Sublease was for two months with automatic renewal periods of one month each. The base

rent under the Sublease is \$8,500 per month. The Sublease contains normal and customary use restrictions, indemnification rights and obligations, default provisions, and termination rights. Under the Agreements signed, the Company continues to have rights to operate as a contract manufacturer in the future in the U.S. and offshore. On July 1, 2011, Katana had assumed the full lease payment, and the Company agreed to pay Katana \$5,000 per month for the use of office space and utilities. The Company recorded a rent expense of \$30,000 and \$45,000 for the nine months ended September 30, 2013 and 2012, respectively.

NOTE 5 - COMMITMENTS AND CONTINGENCIES

Litigation and Claims - In the ordinary course of business, the Company and its subsidiaries are from time to time parties to pending and threatened legal actions and proceedings. In certain of these actions and proceedings, claims are asserted against the Company and its subsidiaries.

In view of the inherent difficulty of predicting the outcome of such matters, the Company cannot state with confidence what the eventual outcome of the pending matters will be, what the timing of the ultimate resolution of these matters will be or what the eventual loss related to each pending matter may be. Based on current knowledge, management does not believe that liabilities, if any, arising from pending litigation or regulatory matters will have a material adverse effect on the consolidated financial position or liquidity of the Company, but may be material to the Company's operating results for any particular reporting period.

Registration Rights Agreements - In connection with the Company's issuance of convertible debentures to YA Global Investments, L.P., formerly known as Cornell Capital Partners, L.P. ("YA Global"), the Company granted to YA Global certain registration rights, pursuant to which the Company agreed to file a registration statement to register the resale of shares of the Company's common stock issuable upon conversion of the debentures. The Company agreed to keep the registration statement effective until all of the shares issuable upon conversion of the debenture have been sold. The Company has not accrued a liability for potential losses.

Previously, YA Global agreed to extensions of the filing deadlines inherent in the terms of the convertible debentures mentioned above. On January 24, 2011, the Company and YA Global entered into a forbearance agreement related to the convertible debentures issued by the Company to YA Global or its predecessor entities (the "2011 Forbearance Agreement"), as discussed below.

YA Global Forbearance Agreements - On September 25, 2010, YA Global filed a lawsuit against the Company asserting claims for breach of contract, breaches of the uniform commercial code, and replevin. YA Global sought a judgment in the amount of \$4,193,380, plus interest and attorneys' fees, as well as a writ of replevin to compel the Company to turn over equipment and other property that YA Global claims was pledged as collateral to secure obligations owing to YA Global.

On January 24, 2011, the Company entered into confession of judgment in favor of YA Global. On February 23, 2011, the court entered judgment based on the confession of judgment against the Company in the principal amount of \$3,161,354, plus interest of \$825,858.

On July 22, 2011, YA Global filed a motion in the Advanced Beauty Solutions, or ABS, lawsuit (discussed below) seeking an order clarifying its position with respect to ABS and staying enforcement of that court's order that the Company pay approximately \$35,000 in legal fees to ABS. In its motion, YA Global notified the Company that it intended to conduct a secured party's public auction of all of the Company's assets. YA Global also informed the Company that it had defaulted under the 2011 Forbearance Agreement and declared that all of the Company's obligations to YA Global were immediately due and owing. Further, YA Global stated that it intended to commence action to collect on the Company's obligations and instructed it to assemble its assets.

At a hearing held on August 3, 2011, in the ABS reorganization proceeding on YA Global's motion to stay enforcement, YA Global noted that the date of the proposed secured party's public auction was August 30, 2011. At the same time, YA Global notified the Company that the proposed sale of assets would be held on August 30, 2011.

At the hearing in the ABS matter, the Bankruptcy Court denied YA Global's motion to stay the payment of attorneys' fees by the Company. Subsequently, the parties to the January 2011 settlement with YA Global entered into an agreement whereby YA Global agreed to cancel the proposed asset sale without waiver.

On September 30, 2011, YA Global directed the Company to assemble the collateral in order to enable it to take possession on or before October 6, 2011. Following negotiations with YA Global, the Company confirmed its indebtedness to YA Global and arranged for it to take possession of collateral on October 17, 2011, on which date, all accounts receivable, collections, and other proceeds and products of the collateral would be held in trust by the Company for YA Global and immediately forwarded to it. Before the Company was required to surrender possession of the collateral, it initiated negotiations to obtain YA Global's forbearance from collection.

On March 22, 2012, the Company entered into a formal forbearance agreement with YA Global, dated as of March 1, 2012 (the "2012 YA Global Forbearance Agreement"), in which it ratified its previous obligations under the debentures and agreed to pay the debentures under the following payment plan: \$25,000 at signing the 2012 YA Global Forbearance Agreement, \$25,000 per month in March through September 2012, \$50,000 per month in July through September 2012, \$75,000 in the months of October and November 2012, \$100,000 per month in the months of December 2012 through May 2013, \$125,000 per month in the months of September through December 2013, and the balance in December 2014 (the "Extended Termination Date"). In addition to the above minimum payments to YA Global, the Company is required to pay monthly excess cash flow, to the extent cumulatively available, consisting of consolidated earnings before interest, taxes, depreciation and amortization, less cash deposits for product orders received but not yet shipped, actual cash taxes paid, actual cash principal and interest paid, and reasonable out-of-pocket cash paid together with reasonable cash reserves in an amount not to exceed 5% of total net sales, provided that such excess cash flow payments shall not exceed \$50,000 in March 2012 and \$25,000 per month in April through September 2012.

The Company continues to have the right, subject to the consent of YA Global, to pay all or any portion of the payments listed above in common stock, with the conversion price to be used to determine the number of shares being equal to the lowest closing bid price of the Company's common stock during the 20 trading days prior to the payment date. The amount applied as a payment on the note and accrued interest will be adjusted to the value of the actual proceeds from the sale of the stock by YA Global, less costs associated with the sale.

YA Global agreed to forbear from enforcing its rights and remedies as a result of the existing defaults and/or converting the debentures into shares of the Company's common stock, until the earlier of the Company's default under the 2012 YA Global Forbearance Agreement or the Extended Termination Date.

On February 22, 2013, the Company entered into a Ratification Agreement with YA Global (the "2013 Ratification Agreement"). Under the 2013 Ratification Agreement, the Company ratified the obligations under three existing Convertible Debentures dated May 26, 2005, December 30, 2005, and August 23, 2006, and agreed to amend, restate,

and consolidate the obligations evidenced thereby into a Consolidated Debenture.

The 2013 Ratification Agreement also provides for a new payment schedule under the Consolidated Debenture that replaces the payment schedule that had been agreed to in the 2012 YA Global Forbearance Agreement among the parties. Under the 2013 Ratification Agreement payment schedule, the Company is required to make monthly payments, to be applied first to accrued interest and then to principal, in the amount of \$100,000 per month, commencing in April 2013. The amount of the Company's required monthly cash payment shall be reduced in an amount equal to the amount credited to the lender against the obligation as a result of the lender's exercise of the right to convert the outstanding balance due under the debentures into common stock, as provided in the original convertible debentures as well as in the Consolidated Debenture. Any amount credited against the debenture obligation in excess of \$100,000 per month shall be credited against the amounts due in the next succeeding month.

During the nine months ended September 30, 2013, the Company converted \$1,948,381, of debt into 653,613,621 shares of common stock, valued at \$244,763, resulting in a gain on conversion of \$1,703,618.

Delinquent Payroll Taxes, Interest, and Penalties - In November 2004, the IRS accepted the Company's Amended Offer in Compromise (the "Offer") to settle delinquent payroll taxes, interest, and penalties. The acceptance of the Offer required the Company to pay \$500,000. Additionally, the Offer required the Company to remain current in its payment of taxes for five years and not claim any net operating losses for the years 2001 through 2015 or until the Company pays taxes on future profits in an amount equal to the taxes waived by the Offer of \$1,455,767. In June 2013, the Company entered into a partial installment agreement to pay \$768,526 in unpaid 2009 payroll taxes. The installment agreement requires the Company to pay the IRS 5% of cash deposits. The monthly payments are to continue until the account balances are paid in full or until the collection statute of limitation expires on October 6, 2020.

Disputed Account Payable - The Company is in disagreement with its former legal counsel over the amount due to this provider for billed services, charges, and interest expense. The Company is vigorously working with this provider to settle the outstanding balance. Management assesses the likelihood to be remote that it will not be able to settle the balance at or below the currently accrued balance.

Employment Agreements - On August 1, 2009, the Company entered into a new employment agreement with Mr. Hawatmeh, the Company President. The term of the employment agreement continues until August 31, 2014, and automatically extends for successive one-year periods, with an annual base salary of \$345,000. The employment agreement also grants to Mr. Hawatmeh options to purchase a minimum of 6,000,000 shares of the Company's stock each year, with the exercise price of the options being the market price of the Company's common stock as of the grant date. The employment agreement also provides for health insurance coverage, cell phone, car allowance, life insurance, and director and officer liability insurance, as well as any other bonus approved by the Board. The employment agreement includes additional incentive compensation as follows: a quarterly bonus equal to 5% of the Company's earnings before interest, taxes, depreciation, and amortization for the applicable quarter; bonus(es) equal to 1.0% of the net purchase price of any acquisitions completed by the Company that are directly generated and arranged by Mr. Hawatmeh; and an annual bonus (payable quarterly) equal to 1% of the gross sales, net of returns and allowances, of all beverage products of the Company and its affiliates for the most recent fiscal year. During the nine months ended September 30, 2013 and 2012, the Company incurred \$10,171 and \$5,852, respectively, of noncash compensation expense related to accrual for employee stock options to be awarded per the employment contract with the president of the Company.

Pursuant to the employment agreement, Mr. Hawatmeh's employment may be terminated for cause or upon death or disability, in which event, the Company is required to pay Mr. Hawatmeh any unpaid base salary and unpaid earned bonuses. In the event that Mr. Hawatmeh is terminated without cause, the Company is required to pay to Mr. Hawatmeh: (i) within 30 days following such termination, any benefit, incentive, or equity plan, program, or practice (the "Accrued Obligations") paid when the amount would have been paid Mr. Hawatmeh if employed; (ii) within 30 days following such termination (or on the earliest later date as may be required by Internal Revenue Code Section

409A to the extent applicable), a lump sum equal to 30 months of annual base salary; (iii) bonus(es) owing under the employment agreement for the two-year period after the date of termination (net of bonus amounts paid as Accrued Obligations) based on actual results for the applicable quarters and fiscal years; and (iv) within 12 months following such termination (or on the earliest later date as may be required by Internal Revenue Code Section 409A to the extent applicable), a lump sum equal to 30 months of annual base salary; provided that if Mr. Hawatmeh is terminated without cause in contemplation of, or within one year after, a change in control, then two times such annual base salary and bonus payment amounts.

On May 1, 2009, PlayBev, a consolidated variable interest entity, entered into compensation agreements with its managers, Mr. Hawatmeh and Mr. Nora. The agreed compensation consists of a monthly fee of \$10,000 for each manager, reimbursement of reasonable expenses on its behalf, and a car allowance for Mr. Nora of \$1,000 per month to cover the cost of use, fuel, and repairs. The Company has accrued \$1,135,784 in compensation, which is included in related-party payables as of September 30, 2013.

Advanced Beauty Solutions, LLC - In connection with prior litigation with ABS, ABS claimed nonperformance by the Company and filed an adversary proceeding in its bankruptcy case proceeding in the United States Bankruptcy Court, Central District of California, San Fernando Valley Division. On March 17, 2009, the Bankruptcy Court entered judgment in favor of ABS and against the Company in the amount of \$1,811,667, plus interest. On September 11, 2009, the Bankruptcy Court denied the Company's motion to set aside the judgment.

On September 8, 2010, the Company executed an Assignment of Copyrights, thereby assigning Copyright Registration No. TX-6-064-955, Copyright Registration No. TX-6-064-956, and Copyright to the True Ceramic Pro - Live Ops (TCPS) infomercial and related master tapes (collectively the "Copyrights") to ABS, without reservation or exclusion, making ABS the owner of the Copyrights.

On February 23, 2011, the Company filed a Motion to Declare Judgment Fully Satisfied or Alternatively to Recoup Mutual Debts, requesting that the court determine that its assignment of the Copyrights resulted in full satisfaction of the ABS judgment. On March 3, 2011, ABS brought a Motion for Order to Show Cause re Civil Contempt alleging that the Company had failed to make payments on ABS's judgment in violation of the court's orders. At the hearing on April 6, 2011, the court denied the motion to declare the judgment fully satisfied and granted ABS's motion, but did not hold the Company in civil contempt. The court also set a hearing on the ABS Motion for the Order to Show Cause for July 8, 2011, regarding the Company's compliance with collection orders, which the parties stipulated should be postponed until August 3, 2011. The parties attended mediation on July 11, 2011, but no formal settlement resulted. At the hearing in August, the court found that a basis existed to hold the Company in contempt and set an evidentiary hearing for October 6, 2011, to determine whether to issue a contempt citation. The Company appealed the denial of its motion to declare judgment satisfied.

On March 22, 2012, the Company and ABS entered into a formal forbearance agreement, dated as of March 1, 2012 (the "ABS Forbearance Agreement"), whereby ABS agreed to take no further judgment enforcement actions in consideration of the payment of \$25,000 upon execution of the definitive ABS Forbearance Agreement and satisfaction of applicable conditions precedent. The ABS Forbearance Agreement calls for the Company to pay \$7,500 per month for 46 consecutive months (except for a payment of \$15,000 in December 2012), commencing in March 2012, with the unpaid balance, as finally determined as provided below, due and payable in January 2016. No interest on the principal would accrue unless the note is in default, in which case, it would bear interest at 10% per annum from the date of the ABS Forbearance Agreement. In addition, the Company stipulated to an additional judgment for attorney's fees incurred in negotiating the ABS Forbearance Agreement and entering into the related definitive agreements and in related post-judgment collection efforts. The obligation to pay \$1,835,000 under the ABS Forbearance Agreement would be secured by an encumbrance on all of the Company's assets, subject to a prior

lien and encumbrance in favor of YA Global.

The principal amount of \$1,835,000 due under the ABS Forbearance Agreement would be reduced by the greater of the amount of credit granted in the bankruptcy proceedings for the value of the intellectual property the Company previously conveyed to ABS and the amount received by ABS from the sale of such intellectual property to a third party during the term of the ABS Forbearance Agreement, plus the amount of any distribution to which the Company is entitled as a creditor of ABS, provided, however, that in no event would the amount due under the ABS Forbearance Agreement be reduced below \$90,000, which is the amount payable during the first 12 months under the ABS Forbearance Agreement. ABS entered into a subordination agreement subordinating the obligation under the ABS Forbearance Agreement in favor of the obligations and first-priority security interest of YA Global. The Company conveyed to ABS the trademarks and intellectual property previously conveyed by ABS to the Company.

The Company's appeal of the approximately \$1.8 million judgment has been remanded in the ABS bankruptcy proceedings to conclusively determine the amount of credit due the Company for the conveyance of the intellectual property. Except for the determination of the fair market value of the intellectual property and any enforcement or collection proceedings that may be required under the ABS Forbearance Agreement, all litigation and disputes between ABS and its affiliates, on the one hand, and the Company and its affiliates, on the other hand, would be dismissed, including the pending order to show cause regarding contempt against the Company, its subsidiaries, and its President.

The Company has assigned to ABS its creditor claim against the estate of ABS, to the extent of the balance due under the ABS Forbearance Agreement. Any distribution from the ABS estate in excess of the adjusted amounts due under the ABS Forbearance Agreement will be paid to the Company. Pending the determination of the amount of the credit due for the value of the intellectual property conveyed, the Company accrued a balance of \$90,000 for the minimum required payment under the ABS Forbearance Agreement. It is reasonably possible that this estimate may change in the near future based on the events of the ABS settlement.

As part of ABS Forbearance Agreement, among other things, the Company agreed to a settlement amount that is to be reduced by any distribution to which the Company was entitled as a creditor of ABS. Under the ABS Forbearance Agreement the minimum amount due ABS is \$90,000, which is the amount payable during the first 12 months under the ABS Forbearance Agreement. The Company accrued \$90,000 as of December 31, 2012, and made payments of \$70,000. The royalty accrual as of September 30, 2013, was \$20,000.

Play Beverages, LLC, et al., v. Warner K. Depuy, et al. - PlayBev alleged tortious interference with contractual relations, breaches of fiduciary duty, and fraud and negligent misrepresentations and sought a declaratory judgment determining the rights of the parties, damages to be determined at trial, costs, and attorney's fees. A default certificate was filed by the plaintiffs for the failure of the defendants to respond and then withdrawn. Under a settlement and release agreement in April 2013, the parties exchanged mutual general releases without the payment by any party of any amounts to any other. Accordingly, PlayBev was relieved of approximately \$1.4 million in amounts due LIB-MP without any payment.

NOTE 6 - NOTES PAYABLE

For the nine-months ended September 30, 2013, the Company received short-term advances payable of \$248,058, from various private lenders. Payments on these notes can be called at any time and yield no interest. Further, the Company made payments in the amount of \$565,353 on short-term advances.

For the nine-months ended September 30, 2013, the Company received proceeds of \$200,000 and had \$124,365 of expenses paid for by non-controlling interest holders. The Company entered into demand notes yielding an interest rate of 10% for these transactions. See Note 10 below for conversions of certain amounts of notes payable during the period.

NOTE 7 - FINANCIAL INSTRUMENTS

The Company has financial instruments that are considered derivatives or contain embedded features subject to derivative accounting. Embedded derivatives are valued separately from the host instrument and are recognized as derivative liabilities in the Company's balance sheet. The Company measures these instruments at their estimated fair value and recognizes changes in their estimated fair value in results of operations during the period of change. The Company has estimated the fair value of these embedded derivatives for convertible debentures and associated warrants using a multinomial lattice model as of September 30, 2013, and December 31, 2012. The fair values of the derivative instruments are measured each quarter, which resulted in a gain (loss) of \$475,560 and \$(132,182) during the nine months ended September 30, 2013 and 2012, respectively. As of September 30, 2013, and December 31, 2012, the fair market value of the derivatives aggregated \$251,906 and \$426,900, respectively.

NOTE 8 - FAIR VALUE MEASUREMENTS

For asset and liabilities measured at fair value, the Company uses the following hierarchy of inputs:

- Level one -- Quoted market prices in active markets for identical assets or liabilities;
- Level two -- Inputs other than level one inputs that are either directly or indirectly observable; and
- Level three -- Unobservable inputs developed using estimates and assumptions, which are developed by the reporting entity and reflect those assumptions that a market participant would use.

Liabilities measured at fair value on a recurring basis at September 30, 2013, are summarized as follows:

| | Level 1 | | Level 2 | | Level 3 | | Total |
|---------------------------|----------------|---|----------------|---------|----------------|---|--------------|
| Fair value of derivatives | \$ | - | \$ | 251,906 | \$ | - | \$ 251,906 |

Liabilities measured at fair value on a recurring basis at December 31, 2012, are summarized as follows:

| | Level 1 | | Level 2 | | Level 3 | | Total |
|---------------------------|----------------|---|----------------|---------|----------------|---|--------------|
| Fair value of derivatives | \$ | - | \$ | 829,090 | \$ | - | \$ 829,090 |

NOTE 9 - STOCKHOLDERS' DEFICIT

The Company's stockholders' deficit decreased by \$576,336 as a result of the net income attributable to CirTran Corporation for the nine months ended September 30, 2013. Non-controlling interest in consolidated subsidiaries decreased stockholders' deficit by \$494,004 for the nine months ended September 30, 2013, due to the operating income of the non-controlling subsidiary.

Income (Loss) Per Share - Basic income (loss) per share is calculated by dividing net income (loss) available to common shareholders by the weighted-average number of common shares outstanding during each period. Diluted income (loss) per share is similarly calculated, except that the weighted-average number of common shares outstanding would include common shares that may be issued subject to existing rights with dilutive potential when applicable.

For the three and nine months ending September 30, 2013, the Company had 2,347,328 in potentially issuable common shares. These potentially issuable common shares were included in the calculation of diluted income (loss) per share.

For the three and nine months ending September 30, 2012, the Company had 124,600,000 in potentially issuable common shares. These potentially issuable common shares were excluded from the calculation of diluted income (loss) per share because the effects were antidilutive.

NOTE 10 – CAPITAL STOCK

During the nine months ending September 30, 2013, the Company issued 1,651,489, shares of common stock for conversion of convertible notes payable and liabilities to multiple non related parties for convertible notes and liabilities of \$1,948,381.

During the nine months ending September 30, 2013, the Company converted \$350,000 of contractual liabilities for ownership in non-controlling interests. This amount has been recorded as capital contributions to non-controlling interest as of September 30, 2013.

NOTE 11 - STOCK OPTIONS AND WARRANTS

Stock Incentive Plans - As of September 30, 2013, a total of 446,200,000 shares of common stock had been issued from the 2012 Stock Incentive Plan, out of which a maximum of 458,000,000 can be issued. The Company's Board of Directors administers the plan and has discretion in determining the employees, directors, independent contractors, and advisors who receive awards, the type of awards (stock, incentive stock options, nonqualified stock options, or share purchase rights) granted, and the term, vesting, and exercise prices.

Employee Options - During the nine months ended September 30, 2013 and 2012, the Company did not grant options to purchase shares of common stock to employees.

A summary of the stock option activity under the plans as of September 30, 2013, and changes during the nine months then ended is presented below:

| | Shares | Weighted- Average Exercise Price | Weighted- Average Remaining Contractual Life | Aggregate Intrinsic Value | |
|-----------------------------------|---------------|---|---|--|---|
| Outstanding at December 31, 2012 | 3,600,000 | \$ 0.0123 | 0.013 | \$ | - |
| Granted | - | - | | | |
| Exercised | - | - | | | |
| Expired | (3,600,000) | 0.0123 | | | - |
| Outstanding at September 30, 2013 | - | \$ - | - | \$ | - |
| Exercisable at September 30, 2013 | - | \$ - | - | \$ | - |

As of September 30, 2013, and December 31, 2012, the Company had a total of 106,800,000 and 88,000,000 options accrued but not issued, respectively.

Warrants - On January, 24, 2011, as part of the 2011 Forbearance Agreement, a warrant to purchase 25,000,000 shares of common stock was issued to YA Global. The warrant had an exercise price of \$0.02 per share and vested immediately.

The Company currently has an insufficient number of authorized shares to enable warrant holders to fully exercise their warrants, assuming all warrants holders desired to do so. Accordingly, the warrants are subject to derivative accounting treatment and are included in the derivative liability related to the convertible debentures (see Note 8).

NOTE 12 - SEGMENT INFORMATION

Segment information has been prepared in accordance with ASC 280-10, Disclosure about Segments of an Enterprise and Related Information. The Company has four reportable segments: electronics assembly, contract manufacturing, marketing and media, and beverage distribution. The electronics assembly segment manufactures and assembles circuit boards and electronic component cables. The contract manufacturing segment manufactures, either directly or through foreign subcontractors, various products under manufacturing and distribution agreements. The marketing and media segment provides marketing services to online retailers, along with beverage development and promotional services to PlayBev. The beverage distribution segment manufactures, markets, and distributes Playboy-licensed energy drinks domestically and internationally.

The accounting policies of the segments are consistent with those described in the summary of significant accounting policies. The Company evaluates performance of each segment based on earnings or loss from operations. Selected segment information is as follows:

Three and nine months ended September 30, 2013 and 2012

| | Electronics Assembly | Contract Manufacturing | Marketing and Media | Beverage Distribution | Total |
|--|-------------------------|---------------------------|------------------------|--------------------------|------------|
| <u>Three Months Ended September 30, 2013</u> | | | | | |
| Sales to external customers | \$ - | \$ 501 | \$ - | \$ 657,860 | \$ 658,361 |
| Segment income (loss) | 95,113 | (10,371) | - | (277,268) | (192,526) |
| Segment assets | 395,365 | 41,346 | - | 544,915 | 981,626 |
| Depreciation and amortization | 4,123 | 6,997 | - | - | 11,120 |
| <u>Three Months Ended September 30, 2012</u> | | | | | |
| Sales to external customers | \$ - | \$ 49,177 | \$ - | \$ 603,950 | \$ 653,127 |
| Segment income (loss) | (132,229) | 29,370 | - | (444,020) | (546,879) |
| Segment assets | 352,022 | 75,653 | - | 794,457 | 1,222,132 |
| Depreciation and amortization | 4,857 | 13,523 | - | - | 18,380 |

Edgar Filing: CIRTRAN CORP - Form 10-Q

Nine Months Ended September 30, 2013

| | | | | | |
|-------------------------------|---------|-----------|------|--------------|--------------|
| Sales to external customers | \$ - | \$ 57,713 | | \$ 2,565,491 | \$ 2,623,204 |
| Segment income (loss) | 393,426 | 3,551 | (25) | 673,388 | 1,070,340 |
| Segment assets | 395,365 | 41,346 | | 544,915 | 981,626 |
| Depreciation and amortization | 12,723 | 25,395 | | | 38,118 |

Nine Months Ended September 30, 2012

| | | | | | |
|-------------------------------|-----------|------------|------|--------------|--------------|
| Sales to external customers | \$ - | \$ 104,802 | \$ - | \$ 1,482,780 | \$ 1,587,582 |
| Segment income (loss) | (434,760) | 14,637 | - | (2,120,339) | (2,540,462) |
| Segment assets | 352,022 | 75,653 | - | 794,457 | 1,222,132 |
| Depreciation and amortization | 15,178 | 53,047 | - | - | 68,225 |

17

NOTE 13 - GEOGRAPHIC INFORMATION

The Company currently maintains \$18,652 of capitalized tooling costs in China. All other revenue-producing assets are located in the United States of America. Revenues are attributed to the geographic areas based on the location of the customers purchasing the products.

NOTE 14 - SUBSEQUENT EVENTS

On October 14, 2013, the Company issued a promissory note as payment for services rendered by a third-party. The amount owed the creditor for the services is \$20,000. Upon the execution of the agreement, the creditor agreed to return the agreement to the Company in exchange for 20,000,000 shares. Since September 30, 2013, the Company has issued 20,000,000 shares to the creditor.

On October 14, 2013, the Company provided issued a promissory note as payment for services rendered. The amount owed the creditor for the services is \$30,000. Upon the execution of the agreement, the creditor agreed to return the agreement to the Company in exchange for 30,000,000 shares. Since September 30, 2013, the Company has issued 30,000,000 shares to the creditor.

On October 14, 2013, the Company issued 20,000,000 shares of unrestricted S-8 shares for service rendered by a consultant.

These financial statements considered subsequent events through November 19, 2013, the date the financial statements were available to be issued.

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

This discussion should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations included in our Annual Report on Form 10-K for the year ended December 31, 2012.

Overview

We manufacture, market, and distribute domestically and internationally an energy drink under a license, now in dispute, with Playboy Enterprises, Inc., or Playboy, and in the U.S., we provide a mix of high- and medium-volume turnkey manufacturing services and products using various high-tech applications for leading electronics OEMs (original equipment manufacturers) in the communications, networking, peripherals, gaming, law enforcement, consumer products, telecommunications, automotive, medical, and semiconductor industries. Our services include pre-manufacturing, manufacturing, and post-manufacturing services. Our goal is to offer customers the significant competitive advantages that can be obtained from manufacture outsourcing.

We are engaged in the following business segments.

Beverage Distribution (98% and 94% of total revenue during nine months ended September 30, 2013 and 2012, respectively)

CirTran Beverage manufactures, markets, and distributes Playboy-branded energy drinks in accordance with an agreement it entered into with Play Beverages, LLC, or PlayBev, a consolidated variable interest entity, which holds the Playboy license.

Contract Manufacturing (2% and 6% of total revenue during the nine months ended September 30, 2013 and 2012, respectively)

CirTran Products pursues contract-manufacturing relationships in the U.S. consumer products markets, including licensed merchandise sold in the sports and entertainment markets.

CirTran Asia manufactures and distributes electronics, consumer products, and general merchandise to companies selling in international markets.

Prior to 2012, we also conducted activities in the marketing and media and electronics assembly operating segments, which may be reactivated.

Forward-Looking Statements

The statements contained in this report that are not purely historical are considered to be “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995 and Section 21E of the Securities Exchange Act. These statements represent our expectations, hopes, beliefs, anticipations, commitments, intentions, and strategies regarding the future. They may be identified by the use of words or phrases such as “believes,” “expects,” “anticipates,” “should,” “plans,” “estimates,” and “potential,” among others. Forward-looking statements include, but are not limited to, statements contained in Management’s Discussion and Analysis of Financial Condition and Results of Operations regarding our financial performance, revenue, and expense levels in the future and the sufficiency of our existing assets to fund future operations and capital spending needs. Readers are cautioned that actual results could differ materially from the anticipated results or other expectations that are expressed in these forward-looking statements. The forward-looking statements contained in this report are made as of the date of this report, and we assume no obligation to update them or to update the reasons why our actual results could differ from those that we have projected in such forward-looking statements. We expressly disclaim any obligation or intention to update any forward-looking statement.

Results of Operations

Comparison of the Three Months and Nine Months Ended September 30, 2013 and 2012

Sales and Cost of Sales

Net sales increased to \$658,361 for the three months ended September 30, 2013, as compared to \$653,127 for the three months ended September 30, 2012. Net sales increased to \$2,623,204 for the nine months ended September 30, 2013, as compared to \$1,587,582 for the nine months ended September 30, 2012. The increases are primarily attributable to our ability to manage the disruption we experienced in 2012 and into 2013 with the unexpected bankruptcy proceedings initiated against PlayBev, the continuing uncertainty created by Playboy in relation to the interference with our beverage distributors, and defense against numerous lawsuits.

Cost of sales, including royalty expense, as a percentage of sales, decreased 100% from 6% for the three months ended September 30, 2013, as compared to the three months ended September 30, 2012, respectively, and decreased to 99% from 35% for the nine months ended September 30, 2013, as compared to the nine months ended September 30, 2012, respectively. Consequently, the gross profit margin decreased to 81% from 83%, for the three months ended September 30, 2013 and 2012, and increased to 77% from 45% for the nine months ended September 30, 2013 and 2012, respectively. The decrease in gross profit margin is attributable to an increase in revenues from product sales that have an overall higher cost than revenues from royalty agreements.

The following charts present comparisons of sales, cost of sales, and gross profits generated by our two operating segments, beverage distribution and contract manufacturing, during the nine months ended September 30, 2013 and 2012:

Nine months Ended September 30:

| <u>Segment</u> | <u>Year</u> | <u>Sales</u> | <u>Cost of Sales</u> | <u>Royalty Expense</u> | <u>Gross Loss / Margin</u> |
|----------------|-------------|--------------|----------------------|------------------------|--------------------------------|
| Beverage | 2013 | \$ 2,565,491 | \$ 553,303 | \$ 37,494 | \$ 1,974,694 |
| Distribution | 2012 | 1,482,780 | 314,712 | 565,609 | 602,459 |
| Contract | 2013 | 57,713 | 1,400 | | 56,313 |
| Manufacturing | 2012 | 104,802 | 478 | - | 104,324 |

Three months Ended September 30:

| <u>Segment</u> | <u>Year</u> | <u>Sales</u> | <u>Cost of Sales</u> | <u>Royalty Expense</u> |
|----------------|-------------|--------------|----------------------|------------------------|
|----------------|-------------|--------------|----------------------|------------------------|

Edgar Filing: CIRTRAN CORP - Form 10-Q

| | | | | | <u>Gross Loss /</u> |
|-----------------------|------|------------|------------|--------|----------------------------|
| | | | | | <u>Margin</u> |
| Beverage Distribution | 2013 | \$ 657,860 | \$ 124,185 | \$ - | \$ 533,675 |
| | 2012 | 603,950 | 67,949 | 39,594 | 496,407 |
| Contract | 2013 | 501 | 50 | - | 451 |
| Manufacturing | 2012 | 49,177 | 277 | - | 48,900 |
| 20 | | | | | |

Selling, General, and Administrative Expenses

During the nine months ended September 30, 2013, selling, general, and administrative expenses increased by \$248,564 to \$2,533,401 from \$2,284,837 for the same period during 2012. The increase in selling, general, and administrative expenses was driven primarily by an increase in legal fees.

Noncash Compensation Expense

Noncash compensation expense in connection with accounting for options owed or granted to employees to purchase common stock was \$11,000 for the three months ended September 30, 2013, as compared to \$16,331 for the three months ended September 30, 2012, and \$41,872 for the nine months ended September 30, 2013, as compared to \$55,411 for the nine months ended September 30, 2012, as a result of the employee stock options accrued for employment agreements.

Other Income and Expense

Interest expense for the three months ended September 30, 2013, was \$198,962, compared to \$344,517 for the three months ended September 30, 2012, a decrease of 42%. Interest expense for the nine months ended September 30, 2013, was \$564,572, as compared to \$882,619 for the nine months ended September 30, 2012. The decrease in the combined interest expense was driven by the reduction in interest-bearing liabilities during the nine months ended September 30, 2013, and a decrease in the interest rate on the convertible debentures.

We recorded a gain of \$104,494 on our derivative valuation for the three months ending September 30, 2013, as compared to a gain of \$34,348 recorded for the three months ended September 30, 2012. We recorded a gain of \$260,061 on our derivative valuation for the nine months ended September 30, 2013, as compared to a loss of \$132,182 recorded for the nine months ended September 30, 2012. The swing in the derivative valuation is primarily the result of the change in estimating the fair value of convertible debentures and associated warrants from using the Black-Scholes model to a multinomial lattice model, together with the varying market values of our common stock.

We recorded a gain of \$1,703,618 on our settlement of debt for the nine months ended September 30, 2013. We recorded a gain of \$475,560 on our settlement of debt for the three months ended September 30, 2013. This was a result of settling payable, accrued liabilities and debt for equity and relief of about \$1.4 million in amounts due LIB-MP. See Notes 5 and 10, in the notes to the unaudited financial statements above for more details.

As a result of these factors, our overall net loss decreased to \$192,526 for the three months ended September 30, 2013, of which a \$343,264 net profit was attributable to non-controlling interests and net income of \$150,738 was attributable to our shareholders. This compares to a net loss of \$546,879 for the three months ended September 30, 2012, of which a net profit of \$222,685 was attributable to non-controlling interests and a net loss of \$324,194 was attributable to our shareholders. Accordingly, the net profit attributable to our shareholders of \$150,738 for the three months ended September 30, 2013, represents a \$474,932 improvement over the same quarter a year earlier. For the nine months ended September 30, 2013, we had net income of \$1,070,340, of which a loss of \$494,004 was attributable to non-controlling interest and a net profit of \$576,336 was attributable to our shareholders. This compares to a net loss of \$2,540,462 for the nine months ended September 30, 2012, of which a net profit of \$492,625 was attributable to non-controlling interest and a net loss of \$2,047,837 was attributable to our shareholders. The net profits attributable to our shareholders of \$576,336 for the nine months ended September 30, 2013, constitutes a \$2,624,173 improvement in net income attributable to our shareholders over the same period in the preceding year.

Liquidity and Capital Resources

We have had a history of losses from operations, as our expenses have been greater than our revenues. Our accumulated deficit was \$47,938,460 at September 30, 2013, and \$48,514,796 at December 31, 2012. Net income attributed to us for the nine months ended September 30, 2013, was \$576,336, as compared to a net loss attributed to us of \$2,047,837 for the nine months ended September 30, 2012. Our current liabilities exceeded our current assets by \$23,090,529 as of September 30, 2013, and by \$26,458,490 as of December 31, 2012.

Cash

The amount of cash provided by operating activities during the nine months ended September 30, 2013, increased by \$40,054 over the prior year period, driven primarily by gains recognized on settlement of debts. The amount of cash used in financing activities during the nine months ended September 30, 2013, decreased by \$119,587 over the prior year period, driven primarily by increased proceeds from non-controlling interest holders and short-term advances and payments on short-term advances.

Accounts Receivable

Trade accounts receivable, net of allowance for doubtful accounts, increased \$0 during the nine months ended September 30, 2013. We continue to monitor individual customer accounts and are working to improve collections on trade accounts receivable. We eliminated the receivables associated with PlayBev as part of consolidation in accordance with GAAP treatment as a variable interest entity.

Accounts Payable and Accrued Liabilities

During the nine months ended September 30, 2013, accounts payable, accrued liabilities, accrued payroll and compensation expense and accrued interest decreased by \$1,059,940 to a combined balance of \$11,087,708 as of September 30, 2013. The decrease includes decreases of \$317,293, \$587,074, and \$491,693 in accounts payable, accrued liabilities, and accrued interest, which more than offset a \$336,074 increase in accrued payroll. The significant decreases in liabilities is due to improved operations.

Capital Requirements

In conjunction with our efforts to improve our results of operations, we are also actively seeking infusions of capital from investors and are seeking sources to repay our existing convertible debentures. In our current financial condition and with ongoing activities substantially dependent on the outcome of the Playboy litigation, it is unlikely that we will be able to obtain additional debt financing. Even if we did acquire additional debt, we would be required to devote additional cash flow to servicing the debt and securing the debt with assets. Accordingly, we are looking to obtain equity financing to meet our anticipated capital needs. We cannot assure that we will be successful in obtaining such capital. If we issue additional shares for debt and/or equity, this will dilute the value of our common stock and existing shareholders' positions.

We cannot assure that we will be successful in obtaining more debt and/or equity financing in the future or that our results of operations will materially improve in either the short or the long term. If we fail to obtain such financing and improve our results of operations, we will be unable to meet our obligations as they become due. These conditions raise substantial doubt about our ability to continue as a going concern.

Convertible Debentures

We had outstanding convertible debentures with an aggregate outstanding balance of \$2,215,528 as of September 30, 2013, including accrued interest of \$800,978. We have entered into forbearance agreements following our previous defaults in payments in order to obtain extended payment terms. Under our most recent agreement reached with the lender in the second quarter of 2013, we are required to make monthly payments, to be applied first to accrued interest and then to principal, in the amount of \$100,000 per month, commencing in April 2013. The amount of our required monthly cash payments is reduced in an amount equal to the amount credited to the lender against the obligation as a result of the lender's exercise of the right to convert the outstanding balance due under the debentures into common stock. Any amount credited against the debenture obligation in excess of \$100,000 per month is credited against the amounts due in the next succeeding month. During the nine months ended September 30, 2013, we issued common stock valued at \$800,712, which includes common stock valued at \$675,176 towards the required monthly payments. The amount of cash required to meet our payment obligations under the debentures will depend on the lender's decision to convert amounts to common stock, which will in turn depend on the trading market prices and volumes for our common stock, over which we have no control.

Critical Accounting Estimates

Revenue Recognition - Revenue is recognized when products are shipped. Title passes to the customer or independent sales representative at the time of shipment. Returns for defective items are repaired and sent back to the customer. Historically, expenses associated with returns have not been significant and have been recognized as incurred.

Shipping and handling fees are included as part of net sales. The related freight costs and supplies directly associated with shipping products to customers are included as a component of cost of goods sold.

We sold our Salt Lake City, Utah, building in a sale/leaseback transaction and reported the gain on the sale as deferred revenue to be recognized over the term of lease pursuant to Financial Accounting Standards Board Accounting Standards Codification, or ASC, 840-10, Accounting for Leases. The lease agreement was terminated during 2011 and the remainder of the deferred revenue was recognized upon this termination event.

We have entered into a Manufacturing, Marketing and Distribution Agreement with PlayBev, a consolidated variable interest entity, whereby we are the vendor of record in providing initial development, promotional, marketing, and distribution services. Accordingly, all amounts billed to PlayBev in connection with the development and marketing of its new energy drink have been eliminated in consolidation.

Financial Instruments with Derivative Features - We do not hold or issue derivative instruments for trading purposes. However, we have financial instruments that are considered derivatives or contain embedded features subject to derivative accounting. Embedded derivatives are valued separately from the host instrument and are recognized as derivative liabilities in our balance sheet. We measure these instruments at their estimated fair value and recognize changes in their estimated fair value in results of operations during the period of change. We have estimated the fair value of these embedded derivatives using the Black-Scholes model. The fair values of the derivative instruments are measured each quarter.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not required.

ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

We carried out an evaluation, under the supervision and with the participation of management, including our Chief Executive Officer / Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) as of September 30, 2013. Based on our evaluation, our Chief Executive Officer / Chief Financial Officer has concluded that our disclosure controls and procedures were not effective at September 30, 2013, due to the fact that the material weaknesses in our internal control over financial reporting described in our Annual Report on Form 10-K for the fiscal year ended December 31, 2012, had not been remediated as of September 30, 2013.

These weaknesses are continuing. Management and the Board of Directors are aware of these weaknesses that result because of limited resources and staff. Efforts to design and implement controls and processes have been put on hold due to limited resources, but we anticipate a renewed focus on this effort in the near future. Due to our limited financial and managerial resources, we cannot assure when we will be able to implement effective internal controls over financial reporting.

Changes in Internal Control over Financial Reporting

There was no change in our internal control over financial reporting that occurred in the second quarter of 2013 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

No material developments.

ITEM 5. OTHER INFORMATION

As of July 31, 2013, YA Global Investments, L.P., and its assigns converted an aggregate of \$333,700 in amounts due under outstanding convertible debentures originally issued to YA Global's predecessor-in-interest in 2005 and 2006, and subsequently amended, restated, and consolidated, to 333,700,000 shares of our common stock at the conversion price set forth in the debentures.

In each of the above transactions, the convertible debentures exchanged for the common stock issued had been issued as restricted securities taken for investment with a restrictive legend to the effect that such securities were restricted. The issuance of the original securities was effected in reliance on the exemption from registration provided in Section 4(a)(2) of the Securities Act of 1933 as transactions not involving any public offering. The issuance of the common stock in exchange for such previously issued debt securities was effected in reliance on the exemption from registration provided in Section 3(a)(9) of the Securities Act for any security exchanged by the issuer with its existing securities holders when no commission or other remuneration is paid or given directly or indirectly for soliciting such exchange.

As a result of all of the foregoing transactions, as of November 19, 2013, CirTran Corporation had an aggregate of 4,439,018,984 shares issued and outstanding.

ITEM 6. EXHIBITS

The following exhibits are filed as a part of this report:

| Exhibit Number* | Title of Document | Location |
|-------------------------|--|-----------------|
| Item 31 31.01 | Rule 13a-14(a)/15d-14(a) Certifications Certification of Principal Executive Officer and Principal Financial Officer Pursuant to Rule 13a-14 | This filing. |
| Item 32 32.01 | Section 1350 Certifications Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Chief Executive Officer and Chief Financial Officer) | This filing. |
| Item 101 101 | Interactive Data File Interactive Data File | This filing |

* All exhibits are numbered with the number preceding the decimal indicating the applicable SEC reference number in Item 601 and the number following the decimal indicating the sequence of the particular document.

SIGNATURE

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

CIRTRAN CORPORATION
(Registrant)

Date: November 19, 2013

By: /s/ Iehab Hawatmeh
Iehab Hawatmeh, President,

Chief Financial Officer (Principal Executive
Officer, Principal Financial Officer)