Sugarmade, Inc.
Form 10-Q
May 15, 2012

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

[X] QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended: March 31, 2012

[ ] TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from N/A to N/A

Commission file number: 000-23446

SUGARMADE, INC.

(Exact Name of Registrant as Specified in its Charter)

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

888-747-6233

(Registrant s telephone number, including area code)

Indicate by check mark whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act of 1934 during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No o
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨
Indicate by check mark whether registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer o

Accelerated filer o

Non-accelerated filer o (Do not check if a smaller reporting company)

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

At May 14, 2012 there were 10,238,000 shares outstanding of the issuer’s common, the only class of common equity.

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

SUGARMADE, INC.

FORM 10-Q

FOR THE PERIOD ENDED MARCH 31, 2012

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SPECIAL NOTE REGARDING FORWARD LOOKING STATEMENTS

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

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

Sugarmade, Inc. and Subsidiaries
Condensed Consolidated Balance Sheets

	March 31, 2012 (Unaudited)	June 30, 2011
Assets		
Current assets:		
Cash	$ 478,056	$ 1,606,764
Accounts receivable	56,331	8,081
Inventory, net of reserves for obsolescence of $ - ($15,321 at June 30, 2011)	121,751	-
Other current assets	255,367	-
Total current assets	911,505	1,614,845
Equipment, net	26,021	-
License and supply agreement with Sugar Cane Paper Co., Ltd., net of accumulated amortization of $44,473 ($30,671 at June 30, 2011)	323,584	337,386
Other assets	3,994	3,994
	$ 1,265,104	$ 1,956,225
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable and accrued liabilities, including amounts due to related parties of $5,800 ($7,668 at June 30, 2011)	$ 235,366	$ 143,070
Notes payable due to bank	50,000	-
Accrued compensation and personnel related payables	46,559	45,258
Total current liabilities	331,925	188,328
Stockholders equity:		
Preferred stock ($0.001 par value, 10,000,000 shares authorized, none issued and outstanding)	-	-
Common stock ($0.001 par value, 300,000,000 shares authorized, 10,738,000 shares issued and outstanding)	10,738	10,256
Additional paid-in capital	7,960,777	5,944,872
Prepaid stock compensation	-	(368,000)
Accumulated deficit	(7,038,336)	(3,819,231)

Total stockholders' equity	933,179	1,767,897
	$ 1,265,104	$ 1,956,225

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

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

	For the three months ended March 31,		For the nine months ended March 31,	
	2012	2011	2012	2011
Sales revenues, net	$ 84,498	$ 1,538	$ 123,996	$ 26,531
Cost of goods sold:				
Materials and freight costs	69,207	1,344	82,589	26,449
Provision for inventory obsolescence	-	15,195	-	32,634
	69,207	16,539	82,589	59,083
Gross margin	15,291	(15,001)	41,407	(32,552)
Operating expenses:				
Selling, general and administrative expenses	634,962	238,311	3,246,786	435,351
Amortization of license and supply agreement	4,601	4,601	13,802	13,802
Total operating expenses	639,563	242,912	3,260,588	449,153
Loss from operations	(624,272)	(257,913)	(3,219,181)	(481,705)
Nonoperating income (expense):				
Interest expense:				
Related parties	-	(4,341)	-	(14,223)
Other	(1,146)	(22,704)	(1,146)	(68,067)
Interest income:				
Interest income from shareholder note receivable	-	6,349	-	17,760
Other	-	-	1,222	15
Total nonoperating income (expense)	(1,146)	(20,696)	76	(64,515)
Net loss	$ (625,418)	$ (278,609)	$ (3,219,105)	$ (546,220)
Basic and diluted net loss per share	$ (0.06)	$ (0.18)	$ (0.31)	$ (0.35)
Basic and diluted weighted average common shares				

outstanding used in computing net loss per share	10,372,000	1,576,214	10,294,385	1,576,214

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

Sugarmade, Inc. and Subsidiaries
Condensed Consolidated Statements of Cash Flows (Unaudited)
For the nine months ended March 31, 2012 and 2011

	2012	2011
Cash flows from operating activities:		
Net loss	$ (3,219,105)	$ (546,220)
Adjustments to reconcile net loss to cash flows from operating activities:		
Amortization of license and supply agreement	13,802	13,802
Depreciation expense	1,122	-
Share based compensation	184,177	-
Issuance of common stock for services	1,590,950	-
Interest income from note receivable from stockholder	-	(17,760)
Changes in operating assets and liabilities:		
Accounts receivable	(48,250)	7,082
Inventory	(121,751)	54,618
Other assets	(255,367)	(17,796)
Accounts payable and accrued liabilities	92,296	142,268
Accrued interest	-	(7,176)
Accrued compensation and personnel related payables	1,301	21,457
Net cash used in operating activities	(1,760,825)	(349,725)
Cash flows from investing activities:		
Additions to property and equipment	(27,143)	-
Reductions to notes receivable from stockholder	-	6,001
Net cash (used in) provided by investing activities	(27,143)	6,001
Cash flows from financing activities:		
Proceeds from issuances of common stock and warrants	609,260	-
Escrowed prepayments for common stock	-	172,750
Additions to convertible notes payable	-	138,000
Additions to notes payable due to bank	50,000	-
Net cash provided by financing activities	659,260	310,750
Net change in cash during period	(1,128,708)	(32,974)
Cash, beginning of period	1,606,764	41,610
Cash, end of period	$ 478,056	$ 8,636

Supplemental disclosure of cash flow information:		
Cash paid during the period for:		
Interest	$ 1,146	$ 92,266
Noncash investing and financing transactions:		
Forgiveness of note payable and accrued interest due to shareholder	$ -	$ 62,800

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

Sugarmade, Inc.

Notes to Unaudited Condensed Consolidated Financial Statements

March 31, 2012

1.

Summary of significant accounting policies

Nature of business

Sugarmade, Inc. (hereinafter referred to as we or the/our Company) is a publicly traded company incorporated in the state of Delaware. Our previous legal name was Diversified Opportunities, Inc. On May 9, 2011 we completed the remaining conditions and closed an Exchange Agreement dated April 23, 2011 (the Exchange Agreement) with Sugarmade, Inc., a California corporation (Sugarmade-CA) and certain shareholders of Sugarmade-CA (the Sugarmade Acquisition). On June 24, 2011, we changed our legal name to Sugarmade, Inc. and on July 15, 2011 our ticker symbol changed and we began trading under the symbol SGMD .

On April 27, 2011, the Board of Directors of Sugarmade-CA declared a two-for-one stock dividend to the holders of its common stock, effective upon the successful completion of the Sugarmade Acquisition. All share amounts herein have been retroactively adjusted to reflect the effect of this stock dividend.

On October 26, 2009, Sugarmade-CA acquired all of the outstanding common stock of Sugarmade, Inc. (SMI) and during 2010 it began doing business as Sugarmade, Inc. On February 1, 2011, Sugarmade-CA changed its legal name to Sugarmade, Inc. and dissolved the SMI legal entity.

Our Company is principally engaged in the business of selling and distributing environmentally friendly non-tree-based paper products.

Basis of presentation

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

These financial statements should be read in conjunction with our Company s Annual Report on Form 10-K for the year ended June 30, 2011, which contains our audited financial statements and notes thereto, together with the

Management s Discussion and Analysis of Financial Condition and Results of Operation, for the period ended June 30, 2011. The interim results for the period ended March 31, 2012 are not necessarily indicative of the results for the full fiscal year.

Principles of consolidation

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

Going concern

Our condensed consolidated financial statements have been prepared assuming that we will continue as a going concern. Such assumption contemplates the realization of assets and satisfaction of liabilities in the normal course of business. However, our auditors raised concerns about our ability to continue as a going concern in their opinion on our financial statements at and for the year ended June 30, 2011. Additionally, we have incurred significant net losses through March 31, 2012. This factor and others raise a substantial doubt about our ability to continue as a going concern. We are dependent upon achieving sufficient future profitable operations and/or procuring additional debt financing or sales of equity securities in order to meet our operating cash requirements. Barring our generation of revenues in excess of our costs and expenses or our obtaining additional funds from equity or debt financing, we will not have sufficient cash to continue to fund the operations of our Company significantly beyond June 30, 2012. These condensed consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

Use of estimates

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

Sugarmade, Inc.

Notes to Unaudited Condensed Consolidated Financial Statements

March 31, 2012

Revenue recognition

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

During fiscal 2011, our Company changed the product packaging of its copy and printing paper, rendering the then existing inventory as obsolete and resulting in the write-off of the remaining inventory as of March 31, 2011. During the quarter ended September 30, 2011, our Company sold its remaining inventory as a one-time sale to a retailer specializing in the liquidation of excess inventory. As a result for the nine months ended March 31, 2012, our sales revenues and cost of goods sold reflect the sale of this liquidated inventory with no corresponding cost of goods sold.

Cash

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

Accounts receivable

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

From time to time, we may have a limited number of customers with individually large amounts due. Any unanticipated change in a customer s creditworthiness could have a material effect on our results of operations in the period in which such changes or events occurred. Accounts receivable at March 31, 2012 and June 30, 2011 were minimal and we had no allowance for doubtful accounts at either March 31, 2012 or June 30, 2011.

Inventory

Inventory consists of finished goods paper and paper-based products ready for sale and is stated at the lower of cost or market. We value inventories using the weighted average costing method. We regularly review inventory and consider forecasts of future demand, market conditions and product obsolescence. If the estimated realizable value of our inventory is less than cost, we make provisions in order to reduce its carrying value to its estimated market value. We had no valuation reserves against inventory at March 31, 2012 and such reserves totaled $15,321 at June 30, 2011 (the entire balance of inventory at June 30, 2011). Our Company consigns inventory to one of our customers on a consignment basis until ultimately sold to the consignee s customers. The value of consigned inventory is reflected in our Company s financial statements as inventory.

Other current assets

Other current assets consist mainly of funds prepaid for the purchase of inventory totaling $246,500 at March 31, 2012.

Equipment

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

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Sugarmade, Inc.

Notes to Unaudited Condensed Consolidated Financial Statements

March 31, 2012

Valuation of long-lived assets

We evaluate long-lived assets for impairment whenever events or changes in circumstances indicate their net book value may not be recoverable. When such factors and circumstances exist, we compare the projected undiscounted future cash flows associated with the related asset or group of assets over their estimated useful lives against their respective carrying amount. Impairment, if any, is based on the excess of the carrying amount over the fair value, based on market value when available, or discounted expected cash flows, of those assets and is recorded in the period in which the determination is made. Our management currently believes there is no impairment of our long-lived assets. There can be no assurance, however, that market conditions will not change or demand for our products under development will continue. Either of these could result in future impairment of long-lived assets.

Income taxes

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

Stock based compensation

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

Loss per share

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

Fair value of financial instruments

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

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

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

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

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

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Sugarmade, Inc.

Notes to Unaudited Condensed Consolidated Financial Statements

March 31, 2012

Intangible assets

We have intangible assets related to the exclusive license and supply agreement with Sugar Cane Paper Company. Our Company recorded the exclusivity agreement at fair value. The exclusivity agreement will be amortized on a straight line basis over the life of the agreement, or twenty years. Amortization expense recorded for each of the three and nine months ended March 31, 2012 was $4,601 and $13,802, respectively.

Advertising

To the extent present in the future, we will expense advertising costs as incurred. We have no existing arrangements under which we provide or receive advertising services from others for any consideration other than cash.

Customer concentration

During the three and nine months ended March 31, 2012, our Company s earned revenues of $84,498 and $123,996, respectively. A significant portion of the Company s revenue is derived from a small number of customers. For the three and nine months ended March 31, 2012, sales to five of the Company s customers accounted for 95% and 94% of net sales, respectively. Additionally, for the three and nine months ended March 31, 2012, no one customer accounted for more than 32% and 22% of net sales, respectively.

Litigation

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

Recently issued and adopted accounting pronouncements

Accounting standards promulgated by the Financial Accounting Standards Board (FASB) are subject to change. Changes in such standards may have an impact on our Company s future financial statements. The following are a summary of recent accounting developments.

In June 2011, the Financial Accounting Standards Board, or the FASB, issued Accounting Standards Update (ASU), 2011-05, Comprehensive Income: Presentation of Comprehensive Income, which requires an entity to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. It eliminates the option to present components of other comprehensive income as part of the statement of changes in stockholders' equity. The ASU does not change the items which must be reported in other comprehensive income, how such items are measured or when they must be reclassified to net income. This ASU is effective for interim and annual periods beginning after December 15, 2011. This ASU did not have a material impact on our condensed consolidated financial statements.

In May 2011, the FASB issued ASU 2011-04, Fair Value Measurement: Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs, which converges common fair value measurement and disclosure requirements in accordance with GAAP and International Financial Reporting Standards (IFRS). This ASU is effective for interim and annual periods beginning after December 15, 2011. Our adoption of this ASU did not have a material impact on our consolidated financial statements.

2.

Acquisition of Sugarmade-CA and related financing activities

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

Under the terms of the Exchange Agreement, Sugarmade-CA s shareholders exchanged all of their shares of stock on a one-for-one basis for a total of 8,864,108 shares of our common stock. In connection with the Exchange Agreement and effective at the closing of the Exchange transaction, our previous three principal shareholders agreed to enter into a Share Cancellation Agreement pursuant to

Sugarmade, Inc.

Notes to Unaudited Condensed Consolidated Financial Statements

March 31, 2012

which 8,762,500 shares held by them were canceled or redeemed in exchange for our Company s payment of $210,000, the issuance of 200,000 two-year warrants to purchase our common stock at $1.25 per share, and certain registration rights.

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

3.

Note payable due to bank

During October 2011, we entered into a revolving demand note (line of credit) arrangement with HSBC Bank USA, with a revolving borrowing limit of $150,000. The line of credit bears a variable interest rate of one quarter percent (0.25%) above the prime rate (3.25% as of March 31, 2012). This borrowing facility is renewed annually and our Company is required to maintain a separate demand deposit account with HSBC with a minimum balance equal to the outstanding borrowing. In the event the deposit account is not established or minimum balance maintained, HSBC can charge a higher rate of interest of up to 4.0% above prime rate. As of March 31, 2012, the loan s interest rate was three and one half percent (3.5%) and our Company has drawn down $50,000 loan balance on the line.

4.

Stockholders equity

Issuance of common stock and warrants for cash

On March 7, 2012, our Company s Board of Directors approved the sale of up to $1,500,000 of our Company s common stock and warrants to purchase common stock at $2.25 per unit. Each unit consists of (i) one share of our Company's common stock; and (ii) two-year term warrants to purchase the amount of shares of common stock equal to 80% of the number of units purchased. Each warrant was issued with a fixed exercise price of $.01 per share. As of March 31, 2012, our Company raised $607,500 through the sale of 270,000 units and the commensurate exercise of 176,000 warrants for additional cash proceeds totaling $1,760.

Issuance of common stock for services

In May 2011, we issued 500,000 shares of common stock to an individual as consideration for consulting services. We recorded a prepaid stock compensation in connection with the shares granted totaling $400,000 based on the estimated value of the underlying shares of stock at the time of their issuance to the consultant. The grant was originally scheduled to vest evenly on a monthly basis over two years through May 2013, however our Company vested all of the remaining unvested shares in December 2011. The prepaid stock compensation from the grant was charged to operations at the time that shares were vested at the fair market value of the vesting shares at the time of their vesting. Prepaid stock compensation was originally amortized proportionally over the expected vesting term of the shares at the time the shares were vested, with the difference being recorded as additional paid-in capital. During the nine months ended March 31, 2012, we recorded noncash charges totaling $1,547,000 in connection with this stock issuance which is included in selling, general and administrative expense in the accompanying statement of operations. No such expenses were incurred for this issuance for the three months ended March 31, 2012.

On January 19, 2012, our Company issued 36,000 shares of restricted common stock to one of its board members in exchange for additional advisory services in the area of finance and financial reporting. The shares vest over one year and any unvested shares are subject to repurchase by our Company should the recipient cease to provide for the contracted services. For the three and nine months ended March 31, 2012, the Company incurred a charge totaling $43,950 related to this issuance.

Stock options

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

Through March 31, 2012, we have a total of 1,131,462 incentive and nonqualified stock options granted and outstanding under the Plan. All of our outstanding options have terms of between five and ten years. During the three and nine months ended March 31, 2012, we recognized share based compensation expense totaling $66,695 and $119,337, respectively, related to stock options granted through that date.

Sugarmade, Inc.

Notes to Unaudited Condensed Consolidated Financial Statements

March 31, 2012

Other outstanding warrants

We have 2,185,600 outstanding warrants issued in connection with the sale of our common stock during the year ended June 30, 2011 and 40,000 outstanding warrants issued in connection with the sale of our common stock during the three months ended March 31, 2012.

Outstanding warrants from all sources have terms ranging from two to five years with certain of the warrants carrying registration rights of the underlying shares of common stock. The number of shares of common stock subject to exercise and the exercise price of all options and warrants outstanding at March 31, 2012 is as follows:

Shares Outstanding	Weighted Average Exercise Price	Shares Vested	Expiration Fiscal Period
2,805,600	$1.45	2,805,600	4th Qtr, 2013
200,000	1.25	200,000	4th Qtr, 2014
12,500	2.00	12,500	1st Qtr, 2015
40,000	0.01	40,000	3rd Qtr, 2015
30,000	1.25	30,000	4th Qtr, 2016
1,079,000	1.25	552,015	4th Qtr, 2021
175,000	3.73	-	1st Qtr, 2022
35,000	3.00	-	2nd Qtr, 2022
1,462	3.25	1,462	3rd Qtr, 2022
4,378,562		3,641,577	

Stock based compensation

Results of operations for the three and nine months ended March 31, 2012 include share based compensation costs totaling $71,476 and $184,177, respectively, charged to selling, general and administrative expenses. For purposes of accounting for stock based compensation, the fair value of each option and warrant award is estimated on the date of grant using the Black-Scholes-Merton option pricing formula. The following weighted average assumptions were utilized for the calculations during the three months ended March 31, 2012:

Expected life (in years)	4.93 years
Weighted average volatility	101.6%
Forfeiture rate	- %
Risk-free interest rate	2.06%
Expected dividend rate	- %

The weighted average expected option and warrant term for director and employee stock options granted reflects the application of the simplified method set out in SEC Staff Accounting Bulletin No. 110/107 as amended, *Share-Based Payment* (SAB 110/107 as amended). The simplified method defines the life as the average of the contractual term of the options and the weighted average vesting period for all options. We utilized this approach as our historical share option exercise experience does not provide a reasonable basis upon which to estimate an expected term. Expected volatilities are based on the historical volatility of our stock as well as those of a peer group. We estimated the forfeiture rate based on our expectation for future forfeitures and we currently expect substantially all options and warrants to vest. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield in effect at or near the time of grant. We have never declared or paid dividends and have no plans to do so in the foreseeable future.

As of March 31, 2012, $501,214 of unrecognized compensation cost related to unvested stock based compensation arrangements is expected to be recognized over a weighted-average remaining period of 11.95 months. The following is required disclosure in connection with stock options and warrants (which resulted in share based compensation charges) as of March 31, 2012: 1) weighted average exercise price - $1.51; 2) weighted average remaining contractual term vested and outstanding options 57.8 and 77.7 months, respectively; 3) aggregate intrinsic value of outstanding and exercisable options and warrants - $3,477,375 and $2,414,655, respectively; 4) weighted average grant date fair value of options and warrants granted - $2.20 per share; and 5) weighted average fair value of options and warrants vested - $0.18 per share.

Sugarmade, Inc.

Notes to Unaudited Condensed Consolidated Financial Statements

March 31, 2012

The exercise prices for options and warrants granted and outstanding (which resulted in stock based compensation charges) was as follows at March 31, 2012:

Exercise Price	Number of Options or Warrants
$1.25	1,709,000
1.50	20,000
2.00	12,500
3.00	35,000
3.25	1,462
3.73	175,000
	1,952,962

A summary of the status of our non-vested options and warrants as of March 31, 2012 and changes during the three months then ended is as follows:

	Shares
Non-vested outstanding, December 31, 2011	803,695
Granted	236,462
Vested	(303,172)
Non-vested outstanding, March 31, 2012	736,985

Common Shares Reserved for Future Issuance

The following table summarizes shares of our common stock reserved for future issuance at March 31, 2012:

Stock options outstanding	1,131,462
Stock options available for future grant under the 2011 Plan	368,538
Warrants	3,247,100

Total common shares reserved for future issuance	4,747,100

5.

Income taxes

We currently estimate our Company s book net operating loss carryforwards (NOL) and deferred tax asset balance to total approximately $6,800,000 and $2,700,000, respectively, as of March 31, 2012. We have recorded a valuation allowance against our entire deferred tax asset balance due to our lack of a history of earnings, the limitations on the use of our NOL as a result of the Sugarmade-CA acquisition and the future expiration of the NOL. These factors give rise to substantial uncertainty as to whether our net deferred tax assets will be realized. As a result of these factors, our utilization of the NOL will likely be severely limited and a substantial portion of the NOL will likely expire unused.

6.

Subsequent events

Effective May 11, 2012, the Company entered into a Share Cancellation Agreement with Clifton Leung, a director and shareholder of the Company, pursuant to which Mr. Leung agreed to the cancellation of 500,000 shares of Company common stock held by him. This summary of the Share Cancellation Agreement is qualified in its entirety by reference to the agreement which is filed as an exhibit to this report

Item 2 Management s Discussion and Analysis of Financial Condition and Results of Operations

This discussion and analysis may include statements regarding our expectations with respect to our future performance, liquidity, and capital resources. Such statements, along with any other non-historical statements in the discussion, are forward-looking. These forward-looking statements are subject to numerous risks and uncertainties, including, but not limited to, the risks and uncertainties described below in Part II, Item 1A and in our June 30, 2011 Annual Report on Form 10-K, as well as those factors listed in other documents we file with the Securities and Exchange Commission (SEC). We do not assume an obligation to update any forward-looking statement. Our actual results may differ materially from those contained in or implied by any of the forward-looking statements in this Form 10-Q.

Overview and Financial Condition

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

Results of Operations

Revenues

Our Company had revenues totaling $84,498 and $123,996 for the three and nine months ended March 31, 2012, respectively, compared to $1,538 and $26,531, respectively for the three and nine months ended March 31, 2011. Our third quarter fiscal 2012 increase in revenues reflected increased revenue from existing customers as well as several new customers. While we are experiencing revenue and customer growth, this is a relatively new product offering with significantly different characteristics compared with existing paper products on the market, and there can be no assurance about whether or when our products will generate sufficient sales volumes with adequate margins in order for our Company to be profitable.

Cost of goods sold

Our Company recorded cost of goods sold for the three months ended March 31, 2012 of $69,207 compared to negligible cost of sales for the three months ended March 31, 2011 (and an inventory obsolescence charge in 2011 of $15,195). For the nine months ended March 31, 2012, we recorded costs of goods sold of $82,589 compared to $26,449 for the nine months ended March 31, 2011 (excluding a provision for inventory obsolescence of $32,634). For the first fiscal quarter of 2012, we sold our remaining previously written off inventory as a one-time sale to a retailer specializing in the liquidation of excess inventory. As a result, our company did not record cost of sales for first fiscal quarter of 2012, resulting in lower than normal cost of sales for the nine months ended March 31, 2012.

Gross margin

Gross margin was $15,291 or 18% of sales for the three months ended March 31, 2012 compared to negative margins ($15,001) for the corresponding period in fiscal 2011 (consisting entirely of a $15,195 provision for inventory obsolescence). For the nine months ended March 31, 2012, gross margins totaled $41,407 compared to negative

margins of ($32,552) for the first nine months of fiscal 2011. The negative margin for the nine months ended March 31, 2011 consisted entirely of a provision for inventory obsolescence totaling $32,634. We do not believe that our gross margin percentage realized to date is indicative of anticipated future results due to relatively low product sales volumes experienced to date and the fact that a portion of our revenues in the early part of fiscal 2012 came from previously written off inventory.

Selling, general and administrative expenses

For the three and nine months ended March 31, 2012, selling, general and administrative expenses totaled $634,962 and $3.246,786 respectively, compared to $238,311 and $435,351 for the three and nine months ended March 31, 2011. The third fiscal quarter and year-to-date ending March 31, 2012 included non-cash related charges for stock compensation and consulting expenses of $115,426 and $1,775,127, respectively (no such expenses were incurred during the same periods in the prior fiscal year). Payroll and related expenses including noncash items totaled $328,976 and $908,677 during the three and nine months ended March 31, 2012, respectively, compared to $62,500 and $133,750 for the three and nine months ended March 31, 2011, respectively. Consulting expenses including noncash items totaling $119,135 and $1,879,680 during the three and nine months ended March 31, 2012, respectively, compared to $119,400 and $208,187 for the three and nine months ended March 31, 2011, respectively.

Legal and auditing expenses totaled $23,263 and $97,858 during the three and nine months ended March 31, 2012, respectively, while legal and auditing expenses for the three and nine months ended March 31, 2011 totaled $36,027 and $54,440, respectively. Travel expenses were $36,978 and $112,523 during the three and nine months ended March 31, 2012, respectively. For the three and nine months ended March 31, 2011, travel expenses totaled $12,108 and $17,254 respectively. The substantial increase in all of our expenses for the quarter and year-to-date periods ended March 31, 2012 as compared to corresponding periods in the prior fiscal year resulted primarily from our Company s non-cash charges for compensation and consulting, added infrastructure and the resulting increase of sales related activities.

Amortization of license and supply agreement

We recognized amortization of our license and supply agreement with Sugar Cane Paper Company (SCPC) totaling $4,601 and $13,802 during both the three and nine months ended March 31, 2012 and 2011, respectively. The amortization represented the recognition of the cost of the SCPC agreement over its initial twenty year term on a straight line basis.

Interest expense and interest income

Our Company incurred minimal interest expense during the three and nine months ended March 31, 2012 as compared to $27,045 and $82,290, respectively, for the three and nine months ended March 31, 2011. Interest expense in fiscal 2011 was primarily the result of amounts accrued and paid in cash under notes payable outstanding through April 2011. All notes payable outstanding during fiscal 2011 were either converted or paid off from the proceeds of an equity offering in fiscal 2011. Our Company had no interest income in the third quarter of fiscal 2012 and $1,222 during the nine months ended March 31, 2012. Interest income for the three and nine months ended March 31, 2011 totaled $6,349 and $17,775, respectively. Interest income in the third fiscal quarter and year-to-date period ending March 31, 2011 was derived almost exclusively from a note receivable due from a stockholder and former officer of our Company.

Net loss

Our net loss totaled $625,418 and $3,219,105, respectively, for the three and nine months ended March 31, 2012 compared to $278,609 and $546,220 for the corresponding periods in the prior year. As mentioned previously, noncash amounts included in our net loss for the three and nine months ended March 31, 2012 of $115,426 and $1,775,127, respectively, accounted for the majority of the our net loss. The remainder of our net loss was generated as our Company primarily focused its activities on establishing relationships with our supplier and potential customers, recruiting an executive management team and sales staff and instituting systems to control and grow our future operations.

Liquidity and Capital Resources

We have primarily financed our operations to date through the sale of unregistered equity, warrants and (prior to our acquisition of Sugarmade-CA) convertible notes payable. As of March 31, 2012, our Company had cash totaling $478,056, current assets totaling $911,505 and total assets of $1,265,104 (including $323,584 in net intangible assets related to the license and supply agreement with SCPC). Included in other assets was $246,500 of funds expended for prepaid inventory. We expect such funds to be returned to us from our operating credit facility with SCPC in the fourth quarter of fiscal 2012. We had total liabilities of $235,366 (all current) and working capital of $579,580. Stockholders equity totaled $933,179 at March 31, 2012.

Net cash used by operating activities was $1,760,825 for the nine months ended March 31, 2012, an increase of $1,411,100 from the $349,725 used during the nine months ended March 31, 2011. The increase of net cash used by operating activities was related to increased activities incurred in ramping up our business operations over the previous year.

There were $27,143 of net cash flows used for investing activities during the nine months ended March 31, 2012 related to our purchase of computer and testing equipment. The inflows for investment activities of $6,001 during the nine months ended March 31, 2011 related to additional advances to a shareholder and former officer under a note receivable totaling $169,000 (the balance of which along with related accrued interest was written off in April 2011).

For the nine months March 31, 2012, there were cash flows from financing activities totaling $659,260. These arose primarily due to proceeds from the sale of common stock and warrants to three investors for $609,260, as well as draws on our operating line of credit totaling $50,000. Inflows from financing activities for the nine months ended March 31, 2011 related to short term shareholder loans as well as additional convertible notes issued during this period.

As part of our license and supply agreement with SCPC, we have an operating credit facility whereby we estimate that we will be able to finance the purchase of substantially all of our Company s products for resale during fiscal 2012 from them on an interest-free basis. Qualifying orders placed with SCPC are not required to be paid for by our Company until up to thirty days after we receive payment from our customers. This operating credit facility is intended to allow us to grow our business quickly without the capital constraints posed by the need for financing our accounts receivables and inventory requirements. Material terms of our operating credit facility under our license and supply agreement with SCPC include: 1) a term expiring on December 31, 2030; 2) an initial ceiling to borrowings under the agreement of $2 million which may be increased by SCPC to a maximum of $20 million based upon the demonstration of our sales and operating performance and need; and 3) terms allowing payment to SCPC for product within 30 days of our Company s receipt of payment from its customer.

Our capital requirements going forward are expected to consist of financing our operations until we are able to reach a level of revenues and gross margins adequate to equal or exceed our ongoing operating expenses. Our Company currently has a line of credit with a bank for $150,000 in order to allow us access to short term operating capital. Other than the operating credit facility with SCPC and the bank line of credit, we do not have any credit arrangements or sources of liquidity immediately available to us.

As of the date of this report, we had a cash balance of approximately $270,000, not including $246,500 advanced as a refundable deposit for inventory that is expected to soon be reimbursed from our credit line with SCPC. We do not currently estimate that these funds are adequate to meet our ongoing cash requirements for the next twelve months. Our management is currently planning to raise additional equity prior to our fiscal year end on June 30, 2012. However, there are no arrangements in place for any such financing at this time. We cannot provide any assurances as to whether we will be able to secure any necessary equity or debt financing, or the terms of any such financing transaction if one were to occur. Should we be unable to secure any financing, the results could potentially threaten our plans for future growth or in more severe scenarios, threaten the continued operations of our Company.

Capital Expenditures

Our current plans do not call for our Company to expend significant amounts for capital expenditures for the foreseeable future beyond relatively insignificant expenditures for office furniture and information technology related equipment as we add employees to our Company. Third parties in China produce the products that we market and our U.S. based warehousing facilities are contracted for with third parties (and therefore do not require us to make capital purchases in this area).

Critical Accounting Policies Involving Management Estimates and Assumptions

Please see the notes to our financial statements.

Item 3 Quantitative and Qualitative Disclosures about Market Risk

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

Item 4 Controls and Procedures

Disclosure Controls and Procedures

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

As required by the Securities and Exchange Commission Rule 13a-15(e) and Rule 15d-15(e), we carried out an evaluation, under the supervision of and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by

this report. Based on the foregoing, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective at the reasonable assurance level.

Changes in Internal Controls over Financial Reporting

There have not been any changes in our internal controls over financial reporting during the quarter ended March 31, 2012 that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

Part II

Item 1 Legal Proceedings

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

Item 1A Risk Factors

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

RISKS RELATED TO OUR BUSINESS

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

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

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

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

Changes within the paper industry may adversely affect our financial performance. Changes in the identity, ownership structure and strategic goals of our competitors and the emergence of new competitors in our target markets may harm our financial performance. New competitors may include foreign-based companies and commodity-based domestic producers who could enter our specialty

markets if they are unable to compete in their traditional markets. The paper industry has also experienced consolidation of producers and distribution channels. Further consolidation could unite other producers with distribution channels through which we intend to sell our products, thereby limiting access to our target markets.

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

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

If we fail to maintain satisfactory relationships with our larger customers, our business may be harmed. We do not have and are unlikely to enter into long-term fixed quantity supply agreements with our customers. Due to competition or other factors, we could lose future business from our customers, either partially or completely. The future loss of one or more of our significant customers or a substantial future reduction of orders by any of our significant customers could harm our business and results of operations. Moreover, our customers may vary their order levels significantly from period to period and customers may not continue to place orders with us in the future at the same levels as in prior periods. In the event that in the future we lose any of our larger customers, we may not be able to replace that revenue source. This could harm our financial results.

Our Company is exposed to risks associated with a highly concentrated customer base. We sell our products to a large office supply company and regional distributors of paper and related products. For the first nine months ended March 31, 2012, five customers accounted for 94% of our net sales. In this environment, contracts or orders from a relatively limited number distributors or retailers have accounted for, and are expected to continue to account for, a substantial portion of our business, which may result in added complexities in managing customer relationships and transactions. In addition, the mix and type of customers, and sales to any single customer, may vary significantly from quarter-to-quarter and from year-to-year. If customers do not place orders, or they substantially reduce, delay or cancel orders, we may not be able to replace the business. Major customers may also seek, and on occasion receive, pricing, payment, or other commercial terms that are less favorable to our Company. These factors could have a material adverse effect on our business, financial condition and results of operations.

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

materials. Our consolidated financial condition, liquidity or results of operations may be adversely affected in the event that we were forced to absorb such costs.

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

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

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

FINANCIAL RISKS

Our current business plan requires that our Company raise additional equity in early 2012. We do not currently have sufficient revenues to cover our operating expenses and have never been profitable. We cannot be certain that our Company will ever generate sufficient revenues and gross margin to achieve profitability in the future. Our business plan requires that our Company needs to raise additional equity in early 2012. Although our Company has

started efforts to raise additional funds, we cannot provide any assurances as to whether we will be able to secure necessary financing, or the ultimate terms of any such financing transactions we may obtain. Our failure to raise sufficient additional capital would seriously harm our business and operating results. If we fail to raise sufficient additional capital in early 2012, our business will be materially and adversely affected and an investor could suffer the loss of a significant portion or all of his investment in our Company.

If we cannot establish profitable operations, we will need to raise additional capital to continue our operations, which may not be available on commercially reasonable terms, or at all, and which may dilute your investment. We incurred a net loss for the nine months ended March 31, 2012 of approximately $3,219,000 (including non-cash related charges for stock compensation and consulting expenses of $1,775,127) and had negative cash flows from operations totaling nearly $1,761,000. For the year ended June 30, 2011, we incurred a net loss in excess of $3.3 million and had negative cash flows from operations in excess of approximately $900,000. Achieving and sustaining profitability will require us to increase our revenues and manage our product, operating and administrative expenses. We cannot guarantee that we will be successful in achieving profitability. If we are unable to generate sufficient revenues to pay our expenses and our existing sources of cash and cash flows are otherwise insufficient to fund our activities, we will need to raise additional funds to continue our operations. We do not have any arrangements in place for additional funds. If needed, those funds may

not be available on favorable terms, or at all. Furthermore, if we issue equity or debt securities to raise additional funds, our existing stockholders may experience dilution, and the new equity or debt securities may have rights, preferences and privileges senior to those of our existing stockholders. If we are unsuccessful in achieving profitability and we cannot obtain additional funds on commercially reasonable terms or at all, we may be required to curtail significantly or cease our operations, which could result in the loss of all of your investment in our stock

We are dependent upon SCPC and our borrowing arrangement with them in order to fund our working capital and liquidity requirements. We have signed an agreement with SCPC to provide our Company favorable payment terms for sales made by our Company of their provided paper products. Our plans going forward are dependent upon SCPC s providing such financing upon the terms we have agreed to and there are currently no other alternate financing plans in place. Should there be an interruption in either SCPC s willingness or ability to provide such financing per the terms of the agreement, we could face a severe liquidity shortfall that could cause our Company s operations to fail and which could consequently result in the loss of an investor s investment with our Company.

Our financial statements have been prepared assuming that our Company will continue as a going concern. We have generated losses to date and have limited working capital. These factors raise substantial doubt about our ability to continue as a going concern. Our financial statements do not include any adjustments that might result from this uncertainty. The report of our independent registered public accounting firm included an explanatory paragraph expressing substantial doubt about our ability to continue as a going concern in their most recent audit report for the fiscal year ended June 30, 2011. If we cannot generate the required revenues and gross margin to achieve profitability or obtain additional capital on acceptable terms, we will need to substantially revise our business plan or cease operations and an investor could suffer the loss of a significant portion or all of his investment in our Company.

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

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

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

Our net operating loss (NOL) carry-forward is limited. We have recorded a valuation allowance amounting to our entire net deferred tax asset balance due to our lack of a history of earnings, possible statutory limitations on the use of tax loss carry-forwards

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

CORPORATE AND OTHER RISKS

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

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

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

our common stock.

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

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

CAPITAL MARKET RISKS

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

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

those prices and with consequent investor losses. The occurrence of these patterns or practices could increase the volatility of our share price.

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

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

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

Item 2 Unregistered Sales of Securities and Use of Proceeds

Between March 14, 2012 and May 11, 2012, the Company issued a total of 270,000 shares of common stock at $2.25 per share, and two-year warrants to purchase up to 216,000 shares of common stock at $.01 per share, to three accredited investors in exchange for gross proceeds totaling $607,500. Commensurate with the purchase, two of these accredited investors exercised their warrants to purchase 176,000 shares of common stock in exchange for gross proceeds totaling $1,760. The securities were issued in reliance upon the exemption from registration afforded by Section 4(2) of the Securities Act as transactions by an issuer not involving any public offering.

Item 3 Defaults upon Senior Securities

Not applicable.

Item 4 Mine Safety Disclosures

None

Item 5 Other Information

Effective May 11, 2012, the Company entered into a Share Cancellation Agreement with Clifton Leung, a director and shareholder of the Company, pursuant to which Mr. Leung agreed to the cancellation of 500,000 shares of Company common stock held by him. This summary of the Share Cancellation Agreement is qualified in its entirety by reference to the agreement which is filed as an exhibit to this report.

Item 6 Exhibits

Exhibit

Number

Description

10.12

Share Cancellation Agreement with Clifton Leung dated May 11, 2012 (1)

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Certification pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, for Chief

Executive Officer and Chief Financial Officer (1)

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Certification pursuant to 18 U.S.C. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, for Chief Executive Officer and Chief Financial Officer (1)

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(1)

Filed as an exhibit to this Report.

SIGNATURES

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

Sugarmade, Inc., a Delaware corporation

By: /s/ SCOTT LANTZ

Scott Lantz, , Chief Executive Officer, Chief Financial Officer (Principal Accounting Officer) and Director

May 14, 2012