

CIRTRAN CORP  
Form 10-Q  
November 19, 2014

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-Q**

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

For the quarterly period ended September 30, 2014

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

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

Commission File Number 000-49654

**CirTran Corporation**

(Exact name of registrant as specified in its charter)

**Nevada**

(State or other jurisdiction of incorporation or organization)

**68-0121636**

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

**4125 South 6000 West, West Valley City, Utah 84128**

(Address of principal executive offices, including zip code)

**(801) 963-5112**

Edgar Filing: CIRTRAN CORP - Form 10-Q

(Registrant's telephone number, including area code)

**n/a**

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

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

YesNo

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

YesNo

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

Large accelerated filer  Accelerated filer   
Non-accelerated filer  Smaller reporting company

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

YesNo

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. **As of November 17, 2014, issuer had 4,498,891,910 outstanding shares of common stock, par value \$0.001.**

**CIRTRAN CORPORATION**

**FORM 10-Q**

**For the Quarterly Period Ended September 30, 2014**

**INDEX**

|   | <b>Page</b> |
|---|-------------|
| <br><b><u>PART I – FINANCIAL INFORMATION</u></b>  |             |
| Item 1 <u>Financial Statements (unaudited)</u>  |             |
| <u>Condensed Consolidated Balance Sheets</u>  | 3           |
| <u>Condensed Consolidated Statements of Operations</u>  | 4           |
| <u>Condensed Consolidated Statements of Cash Flows</u>  | 5           |
| <u>Notes to Condensed Consolidated Financial Statements</u>   | 6           |
| Item 2 <u>Management’s Discussion and Analysis of Financial Condition and Results of Operations</u> | 16          |
| Item 3 <u>Quantitative and Qualitative Disclosures About Market Risk</u>                            | 21          |
| Item 4 <u>Controls and Procedures</u>   | 21          |
| <br><b><u>PART II – OTHER INFORMATION</u></b>   |             |
| Item 6 <u>Exhibits</u>  | 22          |
| <u>Signatures</u>   | 23          |

**PART I – FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****CIRTRAN CORPORATION AND SUBSIDIARIES****CONDENSED CONSOLIDATED BALANCE SHEETS**

|  | <b>September<br/>30, 2014<br/>(Unaudited)</b> | <b>December<br/>31, 2013</b> |
|--|---|------------------------------|
| <b>ASSETS</b>  |   |                              |
| <b>Current assets</b>  |   |                              |
| Cash and cash equivalents  | \$200   | \$281                        |
| Trade accounts receivable, net of allowance for doubtful accounts of \$338,880 and \$832,093, respectively | 37,545  | 6,561                        |
| Inventory, net of reserve of \$2,255,041   | 173,903                                       | 188,634                      |
| Other  | 72,370  | 52,555                       |
| <b>Total current assets</b>  | <b>284,018</b>                                | <b>248,031</b>               |
| Investment in securities, at cost  | 300,000                                       | 300,000                      |
| Long-term receivable, net of allowance of \$1,582,895  | -   | -                            |
| Property and equipment, net  | 22,039  | 39,856                       |
| Other assets, net  | 45,441  | 40,733                       |
| <b>Total assets</b>  | <b>\$651,498</b>                              | <b>\$628,620</b>             |
| <b>LIABILITIES AND STOCKHOLDERS' DEFICIT</b>   |   |                              |
| <b>Current liabilities</b>   |   |                              |
| Checks written in excess of bank balance   | \$23,155                                      | \$41,925                     |
| Accounts payable   | 4,040,689                                     | 4,169,641                    |
| Related-party payable  | 1,374,566                                     | 1,193,901                    |
| Short-term advances payable - non-related parties  | 2,165,321                                     | 1,982,212                    |
| Short-term advances payable - related parties  | 786,382                                       | 766,939                      |
| Accrued liabilities  | 1,792,237                                     | 2,147,729                    |
| Accrued payroll and compensation expense   | 3,471,912                                     | 2,961,993                    |
| Accrued interest   | 1,872,031                                     | 1,482,181                    |
| Deferred revenue   | 2,586,136                                     | 2,592,170                    |
| Derivative liability   | 464,962                                       | 158,396                      |
| Convertible debenture  | 2,390,528                                     | 2,390,528                    |
| Current maturities of long-term debt   | 414,085                                       | 414,085                      |

Edgar Filing: CIRTRAN CORP - Form 10-Q

|  |              |              |
|--|--------------|--------------|
| Current liabilities to non-controlling interest holders  | 2,738,556    | 2,728,556    |
| Note payable to stockholders and members   | 151,833      | 151,833      |
| <b>Total current liabilities</b>   | 24,272,393   | 23,182,089   |
| <b>Total liabilities</b>   | 24,272,393   | 23,182,089   |
| <b>Stockholders' deficit</b>   |              |              |
| CirTran Corporation stockholders' deficit:   |              |              |
| Common stock, par value \$0.001; authorized 4,500,000,000 shares; issued and outstanding shares: 4,498,891,910 and 4,457,991,910 | 4,498,892    | 4,457,992    |
| Additional paid-in capital   | 29,246,170   | 29,270,710   |
| Subscription receivable  | (17,000 )    | (17,000 )    |
| Accumulated deficit  | (48,371,759) | (47,674,008) |
| Total CirTran Corporation and subsidiaries stockholders' deficit   | (14,643,697) | (13,962,306) |
| Non-controlling interest   | (8,977,198 ) | (8,591,163 ) |
| Total stockholders' deficit  | (23,620,895) | (22,553,469) |
| <b>Total liabilities and stockholders' deficit</b>   | \$651,498    | \$628,620    |

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

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

|  | <b>Three months ended<br/>September 30,</b> |               | <b>Nine months ended<br/>September 30,</b> |               |
|--|---|---------------|--|---------------|
|  | <b>2014</b>                                 | <b>2013</b>   | <b>2014</b>                                | <b>2013</b>   |
| Net sales  | \$200,871                                   | \$658,361     | \$1,100,484                                | \$2,623,204   |
| Cost of sales  | (6,965)                                     | (124,235)     | (87,380)                                   | (554,703)     |
| Royalty Expense  | -   | -             | -  | (37,494)      |
| Gross profit   | 193,906                                     | 534,126       | 1,013,104                                  | 2,031,007     |
| Operating expenses   |   |               |  |               |
| Selling, general and administrative expenses                           | 325,146                                     | 892,245       | 1,406,835                                  | 2,575,273     |
| Total operating expenses   | 319,513                                     | 892,245       | 1,406,835                                  | 2,575,273     |
| Loss from operations   | (125,607)                                   | (358,119)     | (393,731)                                  | (544,266)     |
| Other income (expense)   |   |               |  |               |
| Interest expense   | (146,617)                                   | (198,962)     | (441,076)                                  | (564,572)     |
| Gain on settlement of debt   | -   | 260,061       | 57,587                                     | 1,703,618     |
| Gain (loss) on derivative valuation                                    | 169,379                                     | 104,494       | (306,566)                                  | 475,560       |
| Total other expense, net   | 22,762                                      | 165,593       | (690,055)                                  | 1,614,606     |
| Net income (loss)  | (102,845)                                   | (192,526)     | (1,083,786)                                | 1,070,340     |
| Less net income (loss) attributable to non-controlling interest        | 112,399                                     | 343,264       | 386,035                                    | (494,004)     |
| Net income (loss) attributable to CirTran Corporation and subsidiaries | \$9,554                                     | \$150,738     | \$(697,751)                                | \$576,336     |
| Basic and diluted loss per common share                                | \$0.00                                      | \$0.00        | \$(0.00)                                   | \$0.00        |
| Basic and diluted weighted-average common shares outstanding           | 4,498,891,910                               | 3,996,671,346 | 4,489,608,265                              | 3,436,274,192 |

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

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

| <b>For the Nine Months Ended September 30,</b>                              | <b>2014</b>      | <b>2013</b>       |
|---|------------------|-------------------|
| <b>Cash flows from operating activities</b>                                 |                  |                   |
| Net income (loss)   | \$(1,083,786)    | \$1,070,340       |
| Adjustments to reconcile net loss to net cash used in operating activities: |                  |                   |
| Depreciation and amortization   | 17,817           | 38,118            |
| Inventory reserves  | -                | (755 )            |
| (Gain) Loss on derivative valuation   | 306,566          | (475,560 )        |
| Current liabilities to non-controlling interest holders                     | -                | 124,365           |
| (Gain) on settlement of debt  | (57,587 )        | (1,703,618)       |
| Non-cash compensation expense   | -                | 30,872            |
| Expenses paid by third-party on behalf of the company                       | 100,000          | -                 |
| Loan fees   | 25,000           | -                 |
| Changes in assets and liabilities:  |                  |                   |
| Trade accounts receivable   | (30,984 )        | (144,075 )        |
| Inventory   | 14,731           | (141,816 )        |
| Other current assets  | (19,815 )        | (19,785 )         |
| Other assets  | (4,708 )         | 199,128           |
| Accounts payable  | (13,620 )        | (287,793 )        |
| Related-party payable   | 180,665          | 180,128           |
| Accrued liabilities   | (355,492 )       | 251,463           |
| Accrued payroll and compensation expense                                    | 509,919          | 373,074           |
| Refundable customer deposits  | -                | 127,798           |
| Accrued interest  | 389,850          | 535,582           |
| Deferred revenue  | (6,034 )         | 66,700            |
| <b>Net cash provided by operating activities</b>                            | <b>(27,478 )</b> | <b>224,166</b>    |
| <b>Cash flows from financing activities</b>                                 |                  |                   |
| Checks written in excess of bank balance                                    | (18,770 )        | (17,118 )         |
| Proceeds from non-controlling interest                                      | -                | 200,000           |
| Proceeds from short-term advances non-related parties                       | 92,724           | 23,500            |
| Proceeds from short-term advances related parties                           | 106,800          | 224,558           |
| Payments on convertible debenture accrued interest                          | -                | (64,395 )         |
| Payments on short-term advances non-related parties                         | (76,000 )        | (312,903 )        |
| Payments on short-term advances related parties                             | (77,357 )        | (252,450 )        |
| <b>Net cash provided by (used in) financing activities</b>                  | <b>27,397</b>    | <b>(198,808 )</b> |
| <b>Net increase (decrease) in cash and cash equivalents</b>                 | <b>(81 )</b>     | <b>25,358</b>     |
| <b>Cash and cash equivalents at beginning of period</b>                     | <b>281</b>       | <b>7,883</b>      |
| <b>Cash and cash equivalents at end of period</b>                           | <b>\$200</b>     | <b>\$33,241</b>   |

**Supplemental disclosure of cash flow information:**

|  |          |             |
|--|----------|-------------|
| Cash paid during the period for interest   | \$38,000 | \$64,395    |
| <b>Noncash investing and financing activities:</b>   |          |             |
| Debt and accrued liabilities converted to equity   | \$16,360 | \$1,948,381 |
| Conversion of short-term advances, related parties for current liabilities to non-controlling interest holders | 10,000   | 350,000     |

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



**CIRTRAN CORPORATION AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)**

**as of September 30, 2014**

**NOTE 1 – BASIS OF PRESENTATION**

The accompanying unaudited condensed consolidated financial statements include the accounts of CirTran Corporation and its subsidiaries (the “Company”). These financial statements have been prepared in accordance with Article 10 of Regulation S-X promulgated by the Securities and Exchange Commission (“SEC”). Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) have been condensed or omitted pursuant to such rules and regulations. These statements should be read in conjunction with the Company’s annual financial statements included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2013. In particular, the Company’s significant accounting policies were presented as Note 2 to the consolidated financial statements in that Annual Report. In the opinion of management, all adjustments necessary for a fair presentation have been included in the accompanying condensed consolidated financial statements and consist of only normal recurring adjustments. The results of operations presented in the accompanying condensed consolidated financial statements for the three and nine months ended September 30, 2014, are not necessarily indicative of the results that may be expected for the 12 months ending December 31, 2014.

**NOTE 2 – REALIZATION OF ASSETS**

The accompanying condensed consolidated financial statements have been prepared on the assumption that the Company will continue as a going concern. The Company had a net loss of \$1,083,786 and net income of \$1,070,340 for the nine months ended September 30, 2014 and 2013, respectively. As of September 30, 2014, the Company had an accumulated deficit of \$48,371,759. In addition, the Company had cash provided by operations in the amount of \$36,917 during the nine months ended September 30, 2014, and cash provided by operations in the amount of \$224,166 during the nine months ended September 30, 2013. The Company also had a negative working capital deficit balance of \$23,988,375 as of September 30, 2014, and \$22,934,058 as of December 31, 2013. These conditions raise substantial doubt about the Company’s ability to continue as a going concern.

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

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

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

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

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

### NOTE 3 – INVENTORIES

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

|                     | <b>September<br/>30, 2014</b> | <b>December<br/>31, 2013</b> |
|---------------------|-------------------------------|------------------------------|
| Raw Materials       | \$1,689,854                   | \$1,682,099                  |
| Work in Process     | 278,788                       | 255,934                      |
| Finished Goods      | 460,302                       | 505,642                      |
| Allowance / Reserve | (2,255,041)                   | (2,255,041)                  |
| Totals              | \$173,903                     | \$188,634                    |

### NOTE 4 – RELATED-PARTY TRANSACTIONS

**Transactions Involving Officers, Directors, and Stockholders** - In 2007, the Company appointed Fadi Nora to its Board of Directors. In addition to compensation the Company normally pays to nonemployee members of the Board, Mr. Nora is entitled to a quarterly bonus equal to 0.5% of any gross sales earned by the Company directly through Mr. Nora's efforts. As of September 30, 2014, the Company owed \$134,330 under this arrangement. As of September 30, 2014, the Company owed Mr. Nora \$621,773 in the form of unsecured advances. These advances and short-term bridge loans were approved by the Board of Directors under a 5% borrowing fee. The borrowing fees on these loans were waived by Mr. Nora. In addition, the Company owed Mr. Nora \$233,731 in accrued liabilities as of September 30, 2014, for selling, general, and administrative expenses that were paid for by Mr. Nora on a personal credit card. As

of September 30, 2014, Mr. Nora had \$718,000 in accrued management fees for PlayBev, which is included in related-party payables. (see Note 5 under Employment Agreements).

The Company has agreed to issue 2,400,000 options to Mr. Nora as compensation for services provided as a Director of the Company. The terms of the director agreement require the Company to grant to Mr. Nora options to purchase 2,400,000 shares of the Company's stock each year, with the exercise price of the options being the market price of the Company's common stock as of the grant date. During the nine months ended September 30, 2014, the Company accrued for 2,400,000 stock options relating to the director agreement with Mr. Nora. The fair market value of the options was \$719, using the following assumptions: seven-year term, estimated volatility of 246.35%, and a discount rate of 0.0% (see also Note 12).

In 2007, the Company issued a 10% promissory note to a family member of the Company President in exchange for \$300,000. The note was due on demand after May 2008. During the three months ended September 30, 2014, the Company made no payments on the outstanding note. At September 30, 2014, the principal amount owing on the note was \$151,833. On March 31, 2008, the Company issued to this same family member, along with four other Company shareholders, promissory notes totaling \$315,000. The family member's note was for \$105,000. Under the terms of all the notes, the Company received total proceeds of \$300,000 and agreed to repay the amount received plus a 5% borrowing fee. The notes were due April 30, 2008, after which they were due on demand, with interest accruing at 12% per annum. During the nine months ended September 30, 2014, the Company made no payments on the outstanding notes. The principal balance owing on the promissory notes as of September 30, 2014, totaled \$72,466.

The Company has agreed to issue 6,000,000 options each year to the Company President as compensation for services provided as an officer of the Company. The terms of the employment agreement require the Company to grant to the Company President options to purchase 6,000,000 shares of the Company's stock each year, with the exercise price of the options being the market price of the Company's common stock as of the grant date. During the nine months ended September 30, 2014, the Company accrued for 6,000,000 stock options relating to the employee agreement with Mr. Hawatmeh. The fair market value of the options was \$1,798, using the following assumptions: estimated seven-year term, estimated volatility of 246.35%, and a discount rate of 0.0% (see also Note 12).

During the period ending September 30, 2014, the company President advanced \$61,800, was repaid \$47,357, assumed \$58,556 owed to a Company Director and exchanged \$10,000 of this amount for current liabilities to non-controlling interest holders. As a result of these transactions, as of September 30, 2014, the Company owed the Company President a total of \$126,609 in short-term advances payable and 42,000,000 stock options with an aggregated fair value at time of grant of \$166,496. These advances and short-term bridge loans were approved by the Board of Directors under a 5% borrowing fee. The borrowing fees on these loans were waived by the Company's President.

**Sublease** - In an effort to operate more efficiently and focus resources on higher margin areas of the Company's business, on March 5, 2010, the Company and Katana Electronics, LLC, a Utah limited liability company ("Katana"), entered into certain agreements (collectively, the "Agreements") to reduce the Company's costs. The Agreements include an Assignment and Assumption Agreement, an Equipment Lease, and a Sublease Agreement relating to the Company's property. Pursuant to the terms of the Sublease, the Company agreed to sublease a certain portion of the Company's premises to Katana, consisting of the warehouse and office space used as of the close of business on March 4, 2010. The term of the Sublease was for two months with automatic renewal periods of one month each. The base rent under the Sublease is \$8,500 per month. The Sublease contains normal and customary use restrictions, indemnification rights and obligations, default provisions, and termination rights. Under the Agreements signed, the Company continues to have rights to operate as a contract manufacturer in the future in the U.S. and offshore. On July 1, 2011, Katana had assumed the full lease payment, and the Company agreed to pay Katana \$5,000 per month for the use of office space and utilities. The Company recorded a rent expense of \$50,000 and \$30,000 for the nine months ended September 30, 2014 and 2013, respectively.

**NOTE 5 – COMMITMENTS AND CONTINGENCIES**

*Litigation and Claims* - Various vendors and service providers have notified the Company that they believe they have claims against the Company totaling approximately \$2,250,000. The Company has determined the probability of realizing any loss on these claims is remote. The Company has made no accrual for these claims and is currently in the process of negotiating the dismissal of these claims.

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

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

**YA Global Forbearance Agreements** - As of September 30, 2014, the Company had an outstanding Convertible Debenture (as defined below) issued to YA Global Investments, L.P., formerly known as Cornell Capital Partners, L.P. ("YA Global"), with an aggregate outstanding balance of \$2,390,528, including accrued interest of \$748,291, which was then in default.

The terms of the Company's outstanding Convertible Debenture are governed by a February 22, 2013, Ratification Agreement with YA Global (the "Ratification Agreement"). Under this Ratification Agreement, the Company ratified the obligations under three existing convertible debentures dated May 26, 2005, December 30, 2005, and August 23, 2006, and agreed to amend, restate, and consolidate the obligations evidenced thereby into the single Convertible Debenture.

Under the Ratification Agreement and Convertible Debenture payment schedule, the Company was required to make monthly payments, to be applied first to accrued interest and then to principal, in the amount of \$100,000 per month, commencing in April 2013. The convertible debentures and accrued interest are convertible into shares of the Company's common stock at the lowest bid price for the 20 trading days prior to conversion (\$0.0002 as of December 31, 2013). The amount of its required monthly cash payment would be reduced in an amount equal to the amount credited to the balance due under the debentures into common stock, as provided in the original convertible debentures as well as in the Convertible Debenture. Any amount credited against the debenture obligation in excess of \$100,000 per month would be credited against the amounts due in the next succeeding month, with the entire unpaid balance of principal and interest due on January 31, 2014.

During 2013, a total of \$1,284,412 was credited against required payments due YA Global for the conversion of indebtedness to common stock. Since 2009, the Company has not had insufficient funds to pay cash to YA Global and has had to rely exclusively on the conversion of the obligation to common stock. However, no further conversions can be effected because the Company has insufficient authorized but unissued common stock. Based on the prevailing market price for its common stock, which has ranged from a high bid of \$0.0006 to a low bid of \$0.0002 during the past six months, the terms of the Convertible Debenture would require a conversion price of \$0.001 per share, which

is lower than the per-share par value, so the Company would be obligated to issue shares at \$0.001 par value. The Convertible Debenture provides that the holder cannot convert indebtedness to common stock if, as a result of such conversion, the holder would own more than 9.99% of the Company's outstanding common stock. Sales of common stock that would reduce the holder's ownership would enable the holder to convert additional amounts due under the Convertible Debenture.

The obligation under the Company's Convertible Debentures is secured by liens and security interests in all of the Company's assets, so the continuation of the Company is dependent of meeting this obligation. If YA Global were to exercise its collection remedies and execute on its collateral, it could take all of the Company's assets and leave nothing for other creditors or shareholders.



During the nine months ended September 30, 2014, the Company did not issue any common stock against the required payments.

***Delinquent Payroll Taxes, Interest, and Penalties*** - In November 2004, the IRS accepted the Company's Amended Offer in Compromise (the "Offer") to settle delinquent payroll taxes, interest, and penalties. The acceptance of the Offer required the Company to pay \$500,000. Additionally, the Offer required the Company to remain current in its payment of taxes for five years and not claim any net operating losses for the years 2001 through 2015, or until the Company pays taxes on future profits in an amount equal to the taxes waived by the Offer of \$1,455,767. In June 2013, the Company entered into a partial installment agreement to pay \$768,526 in unpaid 2009 payroll taxes. The installment agreement requires the Company to pay the IRS 5% of cash deposits. The monthly payments are to continue until the account balances are paid in full or until the collection statute of limitation expires on October 6, 2020. As of September 30, 2014, this balance is \$445,983.

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

***Employment Agreements*** - On August 1, 2009, the Company entered into a new employment agreement with Mr. Hawatmeh, the Company's President. The term of the employment agreement continues until August 31, 2014, and automatically extends for successive one-year periods, with an annual base salary of \$345,000. The employment agreement also grants to Mr. Hawatmeh options to purchase a minimum of 6,000,000 shares of the Company's stock each year, with the exercise price of the options being the market price of the Company's common stock as of the grant date. The employment agreement also provides for health insurance coverage, cell phone, car allowance, life insurance, and director and officer liability insurance, as well as any other bonus approved by the Board. The employment agreement includes additional incentive compensation as follows: a quarterly bonus equal to 5% of the Company's earnings before interest, taxes, depreciation, and amortization for the applicable quarter; bonus(es) equal to 1.0% of the net purchase price of any acquisitions completed by the Company that are directly generated and arranged by Mr. Hawatmeh; and an annual bonus (payable quarterly) equal to 1% of the gross sales, net of returns and allowances, of all beverage products of the Company and its affiliates for the most recent fiscal year. During the nine months ended September 30, 2014 and 2013, the Company incurred \$1,798 and \$10,171, respectively, of noncash compensation expense related to accrual for employee stock options to be awarded per the employment contract with Mr. Hawatmeh.

Pursuant to the employment agreement, Mr. Hawatmeh's employment may be terminated for cause or upon death or disability, in which event, the Company is required to pay Mr. Hawatmeh any unpaid base salary and unpaid earned bonuses. In the event that Mr. Hawatmeh is terminated without cause, the Company is required to pay to Mr. Hawatmeh: (i) within 30 days following such termination, any benefit, incentive, or equity plan, program, or practice (the "Accrued Obligations") paid when such would have been paid to him if employed; (ii) within 30 days following such termination (or on the earliest later date as may be required by Internal Revenue Code Section 409A to the extent

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

On May 1, 2009, PlayBev, a consolidated variable interest entity, entered into compensation agreements with its managers, Mr. Hawatmeh and Mr. Nora. The agreed compensation consists of a monthly fee of \$10,000 for each manager, reimbursement of reasonable expenses on its behalf, and a car allowance for Mr. Nora of \$1,000 per month to cover the cost of use, fuel, and repairs. The Company has accrued \$1,368,000 in compensation, which is included in related-party payables as of September 30, 2014.

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

ABS entered into a subordination agreement subordinating the obligation under the ABS Forbearance Agreement in favor of the obligations and first-priority security interest of YA Global. The Company conveyed to ABS the trademarks and intellectual property previously conveyed by ABS to the Company.

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

Under the ABS Forbearance Agreement, the Company accrued \$90,000 as of December 31, 2011, and made payments of \$0 and \$70,000 during the nine months ended September 30, 2014 and 2013, respectively. The royalty accrual as of September 30, 2014 and 2013, was \$0 and \$20,000, respectively.

#### **NOTE 6 – NOTES PAYABLE**

Edgar Filing: CIRTRAN CORP - Form 10-Q

Notes payable to stockholders and members consisted of a promissory note to a stockholder due on demand with a 10% stated interest rate, unsecured, with interest due quarterly. The principal balance was \$151,833 as of September, 30, 2014, and December 31, 2013.

Notes payable consisted of the following at September 30, 2014, and December 31, 2013:

|  | <b>2014</b> | <b>2013</b> |
|--|-------------|-------------|
| Promissory notes to three investors, 12% stated interest, 5% borrowing fee, due on demand to related party, in default.        | \$72,465    | \$72,465    |
| Settlement note, 10 monthly payments, no interest, in default.   | 59,120      | 59,120      |
| Promissory note to a member of AfterBev Group LLC, 10% stated interest, interest payable quarterly. Due on demand, in default. | 75,000      | 75,000      |
| Promissory note to a member of PlayBev, 10% stated interest, interest payable quarterly, unsecured. Due on demand, in default. | 100,000     | 100,000     |
| Promissory note to an investor, 0% stated interest, interest payable quarterly, unsecured. Due on demand, in default.          | 100,000     | 100,000     |
| Promissory note to an investor, 10% stated interest, interest payable quarterly, unsecured. Due on demand.                     | 7,500       | 7,500       |
| Total  | 414,085     | 414,085     |
| Less current maturities  | (414,085)   | (414,085)   |
| Long-term portion of notes payable   | \$-         | \$-         |

As of September 30, 2014, and December 31, 2013, the Company had accrued interest owed on the notes payable in the amounts of \$369,679 and \$312,917, respectively. The Company recorded interest expense of \$56,763 and \$284,376 for the nine months September 30, 2014 and 2013, respectively. During the nine months ended September 30, 2014, the Company paid \$0 of accrued interest on the notes.

***Short-term advances payable***

As of September 30, 2014 and December 31, 2013, the Company had \$2,165,322 and \$1,982,212, respectively, in short-term advances payable to unrelated parties. The short-term advances to unrelated parties also had accrued interest expense of \$147,821 and \$79,864 as of September 30, 2014 and December 31, 2013, respectively.

During the nine months ended September 30, 2014, the Company made cash payments of \$76,000 and recorded a loss from settlement of short-term advances payable in the amount of \$41,385. The additional accrual is included in the loss on settlement of debt. The Company also increased short-term advances payable to unrelated parties by \$125,000 for expenses, \$25,000 of which relates to loan fees, paid on behalf of the company by outside parties and approximately \$93,000 for cash received from third parties.

During the nine months ended September 30, 2014, the Company recorded interest expense of \$82,957 and paid \$15,000 of accrued interest on the unrelated party short-term advances.

**NOTE 7 – CONVERTIBLE DEBENTURES**

Convertible Debenture consisted of the following as of September 30, 2014, and December 31, 2013:

|   | September<br>30, 2014 | December<br>31, 2013 |
|---|-----------------------|----------------------|
| Convertible debenture, 5% stated interest rate, secured by all of the Company's assets, due on December 31, 2014. | \$2,390,528           | \$2,390,528          |
|   | 2,390,528             | 2,390,528            |
| Less current maturities   | (2,390,528)           | (2,390,528)          |
| Long-term portion of convertible debentures   | \$-                   | \$-                  |

The convertible debentures and accrued interest are convertible into shares of the Company's common stock at the lowest bid price for the 20 trading days prior to conversion (\$0.0002 as of December 31, 2013). As of December 31, 2010, the Company was in default on the all three convertible debentures. On January 24, 2011, the Company entered into an Amended and Restated Forbearance Agreement that requires the Company to make payments according to the agreement (see Note 5). The Company subsequently defaulted under the terms of the agreement and the debenture holders are seeking their rights as secured creditors. See Note 12 regarding the actions taken by the holder of the convertible debentures in connection with the Company's noncompliance with the Amended and Restated Forbearance Agreement.

As of September 30, 2014 and December 31, 2013, the fair value of the conversion feature for the convertible debt and associated warrants was determined to be \$464,961 and \$158,396, respectively, which has been recorded as a derivative liability on the balance sheet.

As of September 30, 2014 and December, 2013, the fair value of the conversion feature for the convertible debt and associated warrants was determined to be \$464,961 and \$158,396, respectively which has been recorded as a derivative liability on the balance sheet.

#### **NOTE 8 – FINANCIAL INSTRUMENTS**

The Company has financial instruments that are considered derivatives or contain embedded features subject to derivative accounting. Embedded derivatives are valued separately from the host instrument and are recognized as derivative liabilities in the Company's balance sheet. The Company measures these instruments at their estimated fair value and recognizes changes in their estimated fair value in results of operations during the period of change. The Company has estimated the fair value of these embedded derivatives for convertible debentures and associated warrants using a multinomial lattice model as of September 30, 2014, and December 31, 2013. The fair values of the derivative instruments are measured each quarter, which resulted in a gain (loss) of (\$306,566) and \$475,560 during the nine months ended September 30, 2014 and 2013, respectively. As of September 30, 2014, and December 31, 2013, the fair market value of the derivatives aggregated \$464,962 and \$158,396, respectively, using the following assumptions: estimated 1.5-0.25-year term, estimated volatility of 419.37-32.87%, and a discount rate of 0.02-0.36%.

#### **NOTE 9 – FAIR VALUE MEASUREMENTS**

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

Level one — Quoted market prices in active markets for identical assets or liabilities;

Level two — Inputs other than level one inputs that are either directly or indirectly observable; and

Level three — Unobservable inputs developed using estimates and assumptions, which are developed by the reporting entity and reflect those assumptions that a market participant would use.

Liabilities measured at fair value on a recurring basis at September 30, 2014, are summarized as follows:

|                                  | <b>Level<br/>1</b> | <b>Level 2</b> | <b>Level<br/>3</b> | <b>Total</b> |
|----------------------------------|--------------------|----------------|--------------------|--------------|
| <b>Fair value of derivatives</b> | \$ -               | \$464,962      | \$ -               | \$464,962    |

Liabilities measured at fair value on a recurring basis at December 31, 2013, are summarized as follows:

|                                  | <b>Level<br/>1</b> | <b>Level 2</b> | <b>Level<br/>3</b> | <b>Total</b> |
|----------------------------------|--------------------|----------------|--------------------|--------------|
| <b>Fair value of derivatives</b> | \$ -               | \$158,396      | \$ -               | \$158,396    |



## **NOTE 10 – STOCKHOLDERS’ DEFICIT**

The Company’s stockholders’ deficit increased by \$681,391 as a result of the net loss attributable to CirTran Corporation for the nine months ended September 30, 2014. The Company’s noncontrolling interest in consolidated subsidiaries increased stockholders’ deficit by \$386,035 for the nine months ended September 30, 2014, due to the operating losses of the noncontrolled subsidiary.

**Loss Per Share** - Basic loss per share is calculated by dividing net loss available to common shareholders by the weighted-average number of common shares outstanding during each period. Diluted loss per share is similarly calculated, except that the weighted-average number of common shares outstanding would include common shares that may be issued subject to existing rights with dilutive potential when applicable. The Company had 3,210,783,000 and 3,186,357,000 in potentially issuable common shares at September 30, 2014, and December 31, 2013, respectively. These potentially issuable common shares were excluded from the calculation of diluted loss per share because the effects were antidilutive.

## **NOTE 11 – CAPITAL STOCK**

During the nine months ending September 30, 2014, the Company issued 40,900,000 shares of common stock for conversion of liabilities to multiple nonrelated parties for convertible notes and liabilities of \$16,360. This resulted in a gain of \$24,540.

## **NOTE 12 – STOCK OPTIONS AND WARRANTS**

**Stock Incentive Plans** - As of September 30, 2014, a total of 201,000,000 shares of common stock had been issued from the 2012 Stock Incentive Plan, out of which a maximum of 403,000,000 can be issued. The Company’s Board of Directors administers the plan and has discretion in determining the employees, directors, independent contractors, and advisors who receive awards, the type of awards (stock, incentive stock options, nonqualified stock options, or share purchase rights) granted, and the term, vesting, and exercise prices.

**Employee Options** - During the nine months ended September 30, 2014 and 2013, the Company did not grant any options to purchase shares of common stock to employees.

During 2013, the Company accrued for 18,800,000 employee options relating to the employment contract of the Company's president, directors, and officers. The fair market value of the options accrued aggregated \$28,423, using the following assumptions: seven-year term, volatility of 212.05%, and a discount rate of 1.31%.

During 2014, the Company accrued for 18,800,000 employee options relating to the employment contract of the Company's president, directors, and officers. The fair market value of the options accrued aggregated \$5,634, using the following assumptions: seven-year term, volatility of 246.35%, and a discount rate of 2.42%.

As of September 30, 2014, and December 31, 2013, the Company had a total of 125,600,000 and 106,800,000, respectively, in options not issued but accrued.

**Warrants** - In connection with the YA Global convertible debenture issued in August 2006, the Company issued three-year warrants to purchase 15,000,000 shares of the Company's common stock. The initial expiration date of the warrants was August 23, 2009. As part of the Forbearance Agreement (see Note 5), the life of the warrants was extended one year to August 23, 2010. The warrants had an exercise price of \$0.06 per share and vested immediately. On January, 24, 2011, as part of the Forbearance Agreement, a warrant to purchase 25,000,000 shares of common stock was issued to YA Global. The warrant had an exercise price of \$0.02 per share and vested immediately and expires December 2015.

**NOTE 13 – SEGMENT INFORMATION**

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

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

|  | Electronics<br>Assembly | Contract<br>Manufacturing | Marketing<br>and<br>Media | Beverage<br>Distribution | Total        |
|--|-------------------------|---------------------------|---------------------------|--------------------------|--------------|
| <u>Three Months Ended September 30, 2014</u>                             |                         |                           |                           |                          |              |
| Sales to external customers  | \$ -                    | \$ -                      | \$ -                      | \$ 200,871               | \$ 200,871   |
| Segment income (loss )   | 191,769                 | -                         | -                         | (369,614 )               | (177,845 )   |
| Segment as assets  | 38,159                  | (51,661 )                 | -                         | 665,000                  | 651,498      |
| Depreciation and amortization  | 3,059                   | 393                       | -                         | -                        | 3,452        |
| <u>Three Months Ended September 30, 2013 Sales to external customers</u> |                         |                           |                           |                          |              |
| Sales to external customers  | \$ -                    | \$ 501                    | \$ -                      | \$ 657,860               | \$ 658,361   |
| Segment income (loss )   | 95,113                  | (10,371 )                 | -                         | (277,268 )               | (192,526 )   |
| Segment assets   | 395,365                 | 41,346                    | -                         | 544,915                  | 981,626      |
| Depreciation and amortization  | 4,123                   | 6,997                     | -                         | -                        | 11,120       |
| <u>Nine Months Ended September 30, 2014</u>                              |                         |                           |                           |                          |              |
| Sales to external customers  | \$ -                    | \$ 148,960                | \$ -                      | \$ 951,524               | \$ 1,100,484 |
| Segment income (loss )   | (82,219 )               | 6,569                     | -                         | (1,083,136)              | (1,158,786)  |
| Segment assets   | 38,159                  | (51,661 )                 | -                         | 665,000                  | 651,498      |
| Depreciation and amortization  | 10,574                  | 7,243                     | -                         | -                        | 17,817       |
| <u>Nine Months Ended September 30, 2013</u>                              |                         |                           |                           |                          |              |
| Sales to external customers  | \$ -                    | \$ 57,713                 | \$ -                      | \$ 2,565,491             | \$ 2,623,204 |
| Segment income (loss )   | 393,426                 | 3,551                     | (25 )                     | 673,388                  | 1,070,340    |
| Segment assets   | 395,365                 | 41,346                    | -                         | 544,915                  | 981,626      |
| Depreciation and amortization  | 12,723                  | 25,395                    | -                         | -                        | 38,118       |

**NOTE 14 – GEOGRAPHIC INFORMATION**

The Company currently maintains \$7,842 of capitalized tooling costs in China. All other revenue-producing assets are located in the United States of America. Revenues are attributed to the geographic areas based on the location of the customers purchasing the products.

**NOTE 15 – RECLASSIFICATIONS**

Certain amounts have been reclassified in the 2013 financial statements to conform to the 2014 presentation, short-term advances payable – non-related parties of \$45,000 was reclassified to accrued liabilities.

**NOTE 16 – SUBSEQUENT EVENTS**

These financial statements considered subsequent events through November 19, 2014, the date the financial statements were available to be issued.

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

This discussion should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations included in our Annual Report on Form 10-K for the year ended December 31, 2013.

### Overview

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

We are engaged in the following business segments.

***Beverage Distribution*** (100% and 98% of total revenue during nine months ended September 30, 2014 and 2013, respectively):

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

***Contract Manufacturing*** (0% and 2% of total revenue during the nine months ended September 30, 2014 and 2013, respectively):

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

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

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

### **Forward-Looking Statements**

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

## Results of Operations

### *Comparison of the Three Months and Nine months Ended September 30, 2014 and 2013*

#### Sales and Cost of Sales

Gross profit decreased to \$193,906 for the three months ended September 30, 2014, as compared to \$534,126 for the three months ended September 30, 2013. Gross profit decreased to \$1,013,104 for the nine months ended September 30, 2014, as compared to \$2,031,007 for the nine months ended September 30, 2013. The decrease is primarily attributable to the disruption we experienced in 2013 and into 2014 with the unexpected bankruptcy proceedings initiated against PlayBev, the continuing uncertainty created by Playboy in relation to the interference with our beverage distributors, and our defenses against numerous lawsuits. Net sales in the contract manufacturing segment decreased \$501 in the three months ended September 30, 2014, as compared to the same period in 2013. Beverage distribution revenue decreased to \$200,871 for the three months ended September 30, 2014, as compared to \$657,860 for the quarter ended September 30, 2013. Net sales in the contract manufacturing segment increased \$91,247 in the nine months ended September 30, 2014, as compared to the same period in 2013. Beverage distribution revenue decreased to \$951,524 for the nine months ended September 30, 2014, as compared to \$2,565,491 for the quarter ended September 30, 2013. The decrease was driven by reductions in product sales and royalty revenues, as well as less recognition of deferred revenue. During each of the three months and nine months ended September 30, 2014, and 2013, we recognized no revenue from prepayments under contracts that were in default and/or were terminated due to nonperformance.

Cost of sales, including royalty expense, as a percentage of sales, decreased to 3% from 19% for the three months ended September 30, 2014, as compared to the three months ended September 30, 2013, respectively, and decreased to 19% from 21% for the nine months ended September 30, 2014, as compared to the nine months ended September 30, 2013, respectively. Consequently, the gross profit margin increased to 92% from 77%, for the nine months ended September 30, 2014 and 2013, respectively. The increase in gross profit margin is attributable to an increase in revenues from royalty agreements that have an overall lower cost and the settlement of royalty expense contracts during 2013.

The following charts present comparisons of sales, cost of sales, and gross profits generated by our two operating segments, beverage distribution and contract manufacturing, during the nine months ended September 30, 2014 and 2013:

#### Nine months Ended September 30:

| Segment                | Year | Sales     | Cost of Sales | Royalty Expense | Gross Loss / Margin |
|------------------------|------|-----------|---------------|-----------------|---------------------|
| Beverage Distribution  | 2014 | \$951,524 | \$ 87,380     | \$ -            | \$ 864,144          |
|                        | 2013 | 2,565,491 | 553,303       | 37,494          | 1,974,694           |
| Contract Manufacturing | 2014 | 148,960   | -             | -               | 148,960             |
|                        | 2013 | 57,713    | 1,400         | -               | 56,313              |

#### Three months Ended September 30:

| Segment                | Year | Sales     | Cost of Sales | Royalty Expense | Gross Loss / Margin |
|------------------------|------|-----------|---------------|-----------------|---------------------|
| Beverage Distribution  | 2014 | \$200,871 | \$ 6,965      | \$ -            | \$ 193,906          |
|                        | 2013 | 657,860   | 124,185       | -               | 533,675             |
| Contract Manufacturing | 2014 | -         | -             | -               | -                   |
|                        | 2013 | 501       | 50            | -               | 451                 |

#### Selling, General, and Administrative Expenses

During the nine months ended September 30, 2014, selling, general, and administrative expenses decreased by \$1,132,199 to \$1,401,202 from \$2,533,401 for the same period during 2013. The decrease in selling, general, and administrative expenses was driven primarily by reduced consulting and accounting fees of \$230,966, legal fees of \$414,537, sales commission expense of \$153,877, and travel expense of \$102,720, and an adjustment to inventory costs of \$217,914.

#### Noncash Compensation Expense

Compensation expense in connection with accounting for options owed or granted to employees to purchase common stock was \$0 for the three months ended September 30, 2014, as compared to \$11,000 for the three months ended



September 30, 2013, and \$5,633 for the nine months ended September 30, 2014, as compared to \$41,872 for the nine months ended September 30, 2013, as a result of the employee stock options accrued for pursuant to the respective employment agreements.

### **Other Income and Expense**

Interest expense for the three months ended September 30, 2014 was \$146,617, as compared to \$198,962 for the three months ended September 30, 2013, a decrease of 26.3%. Interest expense for the nine months ended September 30, 2014, was \$441,076, as compared to \$564,572 for the nine months ended September 30, 2013. The decrease in the combined interest expense was driven by the reduction in interest-bearing liabilities during the nine months ended September 30, 2014, and a decrease in the interest rate on the convertible debentures.

We recorded a gain of \$169,379 on our derivative valuation for the three months ending September 30, 2014, as compared to a gain of \$104,494 recorded for the three months ended September 30, 2013. We recorded a loss of \$306,566 on our derivative valuation for the nine months ended September 30, 2014, as compared to a gain of \$475,560 recorded for the nine months ended September 30, 2013. The swing in the derivative valuation is primarily the result of the change in estimating the fair value of convertible debentures and associated warrants from using the Black-Scholes model to a multinomial lattice model, together with the varying market values of our common stock.

We recorded a gain of \$57,587 on our settlement of debt for the nine months ended September 30, 2014.

We recorded no gain or loss on our settlement of debt for the three months ended September 30, 2014. This was a result of settling accounts payable and accrued liabilities with various vendors.

As a result of these factors, our overall net loss decreased to \$102,845 for the three months ended September 30, 2014, as compared to net loss of \$192,526 for the three months ended September 30, 2013. The net income attributable to the Company was \$9,554 for the three months ended September 30, 2014, and a net loss of \$112,399 was attributable to a non-controlling equity interest in PlayBev. Net loss increased to \$1,083,786 for the nine months ended September 30, 2014, as compared to net income of \$1,070,340 for the nine months ended September 30, 2013. The net loss attributable to the Company was \$697,751 for the nine months ended September 30, 2014, and net loss of \$386,035 was attributable to a non-controlling equity interest in PlayBev.

## **Liquidity and Capital Resources**

We have had a history of losses from operations, as our expenses have been greater than our revenues. Our accumulated deficit was \$48,371,759 at September 30, 2014, and \$47,674,008 at December 31, 2013. Our current liabilities exceeded our current assets by \$23,988,375 as of September 30, 2014, and by \$22,934,058 as of December 31, 2013.

### ***Cash***

The amount of cash provided by operating activities during the nine months ended September 30, 2014, decreased by \$187,249, driven primarily by deferred expenses and expenses paid by third-parties on our behalf. The amount of cash used in financing activities during the nine months ended September 30, 2014, increased by \$161,810, driven primarily from conversion of debt to equity and checks written in excess of our bank balance.

### ***Accounts Receivable***

Trade accounts receivable, net of allowance for doubtful accounts, increased \$30,984 during the nine months ended September 30, 2014. We continue to monitor individual customer accounts and are working to improve collections on trade accounts receivable. We eliminate the receivables associated with PlayBev as part of consolidation in

accordance with GAAP treatment as a variable interest entity.

***Accounts Payable and Accrued Liabilities***

During the nine months ended September 30, 2014, accounts payable, accrued liabilities, advances payable, interest payable, and short-term debt increased by \$798,542 to a combined balance of \$15,503,138 as of September 30, 2014. The increase includes a decrease of \$355,492 in accrued liabilities, a \$389,850 increase in interest payable, an increase of \$509,919 in accrued payroll and compensation, and a \$128,952 decrease in accounts payable. The decrease in accounts payable activity is a result of payments made by outside investors for continued PlayBev-related services performed during the nine months ended September 30, 2014, for beverage development, distribution, marketing, and legal services. At September 30, 2014, we owed \$2,165,321 to various investors from whom we had borrowed funds in the form of either unsecured or short-term advances.

### ***Capital Requirements***

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

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

### ***Convertible Debentures***

We had an outstanding Convertible Debenture with an aggregate outstanding balance of \$2,390,528 as of September 30, 2014, including accrued interest of \$748,291. We have entered into forbearance agreements following our previous defaults in payments in order to obtain extended payment terms. Under our most recent agreement reached with the lender in the second quarter of 2013, we were required to make monthly payments, to be applied first to accrued interest and then to principal, in the amount of \$100,000 per month, commencing in April 2013. The amount of our required monthly cash payments is reduced in an amount equal to the amount credited to the lender against the obligation as a result of the lender's exercise of the right to convert the outstanding balance due under the debentures into common stock. Any amount credited against the debenture obligation in excess of \$100,000 per month is credited against the amounts due in the next succeeding month.

During the nine months ended September 30, 2014, we did not issue any common stock against the required monthly payments because we had insufficient authorized but unissued common stock. Based on the prevailing market price for our common stock, which has ranged from a high bid of \$0.0006 to a low bid of \$0.0002 during the past six months, the terms of the Consolidated Debenture would require a conversion price of \$0.001 per share, which is lower than the per-share par value, so we would be obligated to issue shares at \$0.001 par value. As of September 30, 2014, we had only 81,016 authorized but unissued shares. The Consolidated Debenture provides that the holder cannot convert indebtedness to common stock if, as a result of such conversion, the holder would own more than 9.99% of the Company's outstanding common stock. We are seeking shareholder authorization of a recapitalization of the Company to provide additional shares to issue on conversion of the Convertible Debenture but cannot assure whether the stockholders will approve such amendment.

In the absence of an amendment to our articles to provide sufficient shares to issue on conversion of the Convertible Debenture, we would be required to pay the debenture in cash. The amount of cash required to meet our payment obligations under the Convertible Debenture will depend on the lender's decision to convert amounts to common stock, which will in turn depend on the trading market prices and volumes for our common stock, over which we have no control.

## **Critical Accounting Estimates**

### ***Revenue Recognition***

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

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

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

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

### ***Financial Instruments with Derivative Features***

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

## **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Not required.

#### **ITEM 4. CONTROLS AND PROCEDURES**

##### **Disclosure Controls and Procedures**

We carried out an evaluation, under the supervision and with the participation of management, including our Chief Executive Officer / Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) as of September 30, 2014. Based on our evaluation, our Chief Executive Officer / Chief Financial Officer has concluded that our disclosure controls and procedures were not effective at September 30, 2014, due to the fact that the material weaknesses in our internal control over financial reporting described in our Annual Report on Form 10-K for the fiscal year ended December 31, 2013, had not been remediated as of September 30, 2014.

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

### Changes in Internal Control over Financial Reporting

There was no change in our internal control over financial reporting that occurred in the third quarter of 2014 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

## PART II – OTHER INFORMATION

### ITEM 6. EXHIBITS

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

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

---

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





**SIGNATURE**

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

CIRTRAN CORPORATION  
(Registrant)

Date: November 19, 2014 By: */s/ Iehab Hawatmeh*  
Iehab Hawatmeh, President,  
Chief Financial Officer (Principal Executive Officer, Principal Financial Officer)

