

XELR8 HOLDINGS, INC.  
Form 10QSB  
November 02, 2007

# UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

## FORM 10-QSB

**Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the quarterly period ended September 30, 2007

Or

**Transition Report Pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934**

Commission file No. 000-50875

## XELR8 HOLDINGS, INC.

(Exact name of small business issuer as specified in its charter)

**Nevada**  
(State of incorporation)

**84-1575085**  
(I.R.S. Employer Identification Number)

**480 South Holly Street**

**Denver, CO 80246**

(Address of principal executive offices)

(303)-316-8577

(Issuer's telephone number)

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

YES  NO

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

YES  NO

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

YES  NO

As of October 31, 2007 the Company had 15,197,170 shares of its \$.001 par value common stock issued and outstanding.

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**Part I FINANCIAL INFORMATION****Item 1 CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS****XELR8 HOLDINGS, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS**

	September, 30 2007 (unaudited)	December, 31 2006
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 2,473,233	\$ 76,147
Accounts receivable, net of allowance for doubtful accounts of \$ 19,827 and \$10,706, respectively	7,662	4,785
Inventory, net of allowance for obsolescence of \$ 95,414 and \$41,655, respectively	613,134	411,364
Prepaid expenses and other current assets	321,429	259,292
Total current assets	3,415,458	751,588
Intangible assets, net	10,176	11,212
Property and equipment, net	93,228	123,943
Deferred offering and loan costs		133,889
Total assets	\$ 3,518,862	\$ 1,020,632
<b>LIABILITIES AND SHAREHOLDERS EQUITY (DEFICIT)</b>		
Current liabilities:		
Accounts payable and accrued expenses	\$ 841,017	\$ 1,160,916
Short-term note payable		250,000
Total Liabilities	841,017	1,410,916
<b>Commitments and Contingencies</b>		
<b>SHAREHOLDERS EQUITY (DEFICIT) (Note 2):</b>		
Preferred stock, authorized 5,000,000 shares, \$.001 par value, none issued or outstanding		
Common stock, authorized 50,000,000 shares, \$.001 par value, 15,197,170 and 10,097,170 shares issued and outstanding respectively	15,197	10,097
Additional paid in capital	22,513,097	16,849,900
Accumulated (deficit)	(19,850,449)	(17,250,281)
Total shareholders equity (deficit)	2,677,845	(390,284)
Total liabilities and shareholders equity	\$ 3,518,862	\$ 1,020,632

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

**XELR8 HOLDINGS, INC.****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)**

Three and Nine Months Ended September 30, 2007 and 2006

	For the Three Months Ended September 30, 2007	For the Three Months Ended September 30, 2006	For the Nine Months Ended September 30, 2007	For the Nine Months Ended September 30, 2006
Net sales	\$ 1,432,220	\$ 608,111	\$ 3,687,690	\$ 1,724,252
Cost of goods sold	342,233	211,513	1,014,765	622,841
Gross profit	1,089,987	396,598	2,672,925	1,101,411
Operating expenses:				
Selling and marketing expenses	820,080	571,160	2,417,200	2,214,842
General and administrative expenses	642,930	577,456	2,429,738	2,136,506
Research and development expenses	3,214	20,246	8,342	64,180
Depreciation and amortization	11,716	11,779	45,992	54,554
Total operating expenses	1,477,940	1,180,641	4,901,272	4,470,082
Net (loss) from operations	(387,953)	(784,043)	(2,228,347)	(3,368,671)
Other income (expense)				
Interest income	32,674	5,099	67,716	32,757
Interest (expense)			(439,537)	
Total other income (expense)	32,674	5,099	(371,821)	32,757
Net (loss)	\$ (355,279)	\$ (778,944)	\$ (2,600,168)	\$ (3,335,914)
Net (loss) per common share				
Basic and diluted net (loss) per share	\$ (0.02)	\$ (0.08)	\$ (0.19)	\$ (0.35)
Weighted average common shares outstanding, basic and diluted	15,197,170	9,697,170	13,544,596	9,660,897

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

**XELR8 HOLDINGS, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)****Nine Months Ended September 30, 2007 and 2006**

	September 30 2007	September 30 2006
<b>Cash flows from operating activities:</b>		
Net income (loss)	\$ (2,600,168)	\$ (3,335,914)
Adjustments to reconcile		
Depreciation and amortization	45,992	54,554
Stock and stock options issued for services	1,188,848	527,332
Interest expense and amortization related to bridge loan financing	428,889	
Change in allowance for doubtful accounts	9,121	6,865
Change in allowance for inventory obsolescence	53,760	90,402
Change in allowance for product returns	30,866	24,718
Changes in assets and liabilities:		
Accounts receivable	(11,998)	(4,269)
Inventory	(255,530)	109,995
Other current assets	(62,137)	(10,392)
Accounts payable and accrued expenses	214,235	157,661
Net cash (used) by operating activities	(958,122)	(2,379,048)
<b>Cash flows from investing activities:</b>		
Proceeds from maturity of investments		110,000
Capital expenditures	(14,241)	(71,846)
Net cash (used) by investing activities	(14,241)	38,154
<b>Cash flow from financing activities:</b>		
Proceeds from bridge loan financing	250,000	
Repayments of bridge financing	(500,000)	
Issuance of common stock	3,619,449	
Net cash provided from financing activities	3,369,449	
NET INCREASE (DECREASE) IN CASH	2,397,086	(2,340,894)
CASH AND CASH EQUIVALENTS, BEGINNING OF THE PERIOD	76,147	2,805,021
CASH AND CASH EQUIVALENTS, END OF THE PERIOD	\$ 2,473,233	\$ 464,127
<b>SUPPLEMENTAL CASH FLOW DISCLOSURE</b>		
Cash paid for interest	\$ 13,425	\$
Stock issued for satisfaction of accrued compensation expense	\$ 540,000	\$
Deferred offering costs applied against proceeds from offering	\$ 25,000	\$

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





**XELR8 HOLDINGS, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**Note 1 - ORGANIZATION, OPERATIONS AND BASIS OF PRESENTATION**

**Organization and Business**

The consolidated financial statements include those of XELR8 Holdings, Inc. (formerly VitaCube Systems Holdings, Inc.), and its wholly owned subsidiaries, VitaCube Systems, Inc., XELR8, Inc. (formerly VitaCube Network, Inc.) and XELR8 International, Inc. Collectively, they are referred to herein as the the Company.

The Company is in the business of selling, marketing and distributing nutritional supplement products and functional foods. Our product lines consist of a sports hydration drink, a protein shake, a sports energy drink, a meal replacement drink, a functional food snack and a full product line of vitamins and minerals in the form of tablets, softgels or capsules, all of which are manufactured using our proprietary product formulations. In January 2007, we added a new product, BAZI , a dietary supplement beverage.

The Company sells and markets the products primarily through a direct selling channel, in which independent distributors sell our products through a network of customers and other distributors. These activities are conducted through XELR8, Inc., a wholly owned Colorado corporation formed on July 9, 2003, and XELR8 International, a wholly owned Colorado corporation formed on July 19, 2007. In addition, we sell our products directly to professional and Olympic athletes and professional sports teams through VitaCube Systems, Inc.

Our independent auditors have noted in their reports on our financial statements as of December 31, 2006 and 2005 and for the years then ended, that there is substantial doubt regarding our ability to continue as a going concern. To date this contingency has not affected our ability to secure funding for our operations; however, going forward, in the event this uncertainty is not resolved, we may experience more difficulty in raising funds to operate our Company if we are required to raise such capital. In March 2007, we completed a private sale of common stock of the Company for gross proceeds of \$2,000,000, and in May 2007 we completed a second private sale of common stock shares of the Company for additional gross proceeds of \$2,000,000.

**Basis of Presentation**

The condensed interim financial statements included herein have been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations, although the Company believes that the disclosures made are adequate to make the information presented not misleading. The condensed interim financial statements and notes thereto should be read in conjunction with the financial statements and the notes thereto, included in the Company's Annual Report to the Securities and Exchange Commission for the fiscal year ended December 31, 2006, filed on Form 10-KSB on

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March 30, 2007.

The accompanying condensed interim financial statements have been prepared, in all material respects, in conformity with the standards of accounting measurements set forth in Accounting Principles Board Opinion No. 28 and reflect, in the opinion of management, all adjustments necessary to summarize fairly the financial position and results of operations for such periods in accordance with accounting principles generally accepted in the United States of America. All adjustments are of a normal recurring nature. The results of operations for the most recent interim period are not necessarily indicative of the results to be expected for the full year.

### **Principles of Consolidation**

The accompanying financial statements include the accounts of the Company and its wholly owned subsidiaries VitaCube Systems, Inc., XELR8, Inc. and XELR8 International, Inc. All inter-company accounts and transactions have been eliminated in the preparation of these consolidated statements.

**Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Management believes that the estimates utilized in the preparation of financial statements are prudent and reasonable. Actual results could differ from these estimates.

**Revenue Recognition**

The Company ships its products by common carrier and receives payment in the form of cash, credit card payment or approved credit terms. The Company offers a 60-day money back guarantee on orders placed by first-time customers and distributors, for their initial enrollment pack. Additional products purchased during their first 60 days are refundable for 100% of the sales price if returned in resalable condition. After 60 days and for all subsequent orders placed by customers and distributors, the Company allows resalable products to be returned within 12 months of the purchase date for a 100% sales price refund, subject to a 10% restocking fee. During the nine months ended September 30, 2007 and for the nine months ended September 30, 2006, returns as a percentage of net sales were 2.3% and 6.3%, respectively. Sales revenue and estimated returns are recorded when the merchandise is shipped since performance by the Company is considered met when products are in the hands of the common carrier. Amounts received for unshipped merchandise are recorded as customer deposits and are included in accrued liabilities. Additionally, up to December 31, 2006 the Company collected an annual website fee from Distributors that was deferred on receipt and recognized as income on a straight-line basis over the subsequent twelve-month period.

**Inventory**

Inventory is stated at the lower of cost or market on a FIFO (first-in first-out) basis. Provision is made to reduce excess or obsolete inventory to the estimated net realizable value. The Company purchases for resale a dietary supplement beverage, sports energy drink, a protein shake, an appetite suppressant chew and other vitamins and nutritional supplements, which it packages in various forms and containers.

Inventory is comprised of the following:

	<b>September 30, 2007</b>		<b>December 31, 2006</b>	
Raw materials	\$	61,523	\$	245,447
Finished goods		647,026		207,572
Provision for obsolete inventory		(95,414)		(41,655)
	\$	613,135	\$	411,364

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A summary of the reserve for obsolete and excess inventory is as follows:

	September 30, 2007		December 31, 2006	
Balance as of January 1	\$	41,655	\$	16,879
Addition to provision		122,771		123,511
Write-off of obsolete inventory		(69,012)		(98,735)
	\$	95,414	\$	41,655

### Stock-Based Compensation

Effective January 1, 2006, the Company adopted SFAS No. 123 (revised 2004), *Share-Based Payment* (SFAS 123R), which requires compensation costs related to share-based transactions, including employee stock options, to be recognized in the financial statements based on fair value. SFAS 123R revises SFAS No. 123, *Accounting for Stock-Based Compensation*, (SFAS 123) and supersedes Accounting Principles Board Opinion (APB) No. 25, *Accounting for Stock Issued to Employees*. In March 2005, the Securities and Exchange Commission (the SEC) issued Staff Accounting

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Bulletin No. 107 (SAB 107) regarding the SEC's interpretation of SFAS 123R and the valuation of share-based payments for public companies. The Company has applied the provisions of SAB 107 in its adoption of SFAS 123R.

The Company adopted the provisions of SFAS 123R using the modified prospective transition method. In accordance with this transition method, the Company's consolidated financial statements for prior periods have not been restated to reflect the impact of SFAS 123R. Under the modified prospective transition method, share-based compensation expense for the first quarter of 2006 includes compensation expense for all share-based compensation awards granted prior to, but for which the requisite service has not yet been performed as of January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of SFAS 123. Share-based compensation expense for all share-based compensation awards granted after January 1, 2006 is based on the grant date fair value estimated in accordance with the provisions of SFAS 123R. The Company recognizes compensation costs net of an assumed forfeiture rate and recognizes the compensation costs for nonqualified stock options expected to vest on a straight-line basis over the requisite service period of the award. The Company estimates the forfeiture rate based on its historical experience.

Total share-based compensation expense, for all of the Company's share-based awards recognized for the nine months ended September 30, 2007, was \$1,188,848 or \$0.08 per share basic and diluted compared with the \$527,332 or \$0.06 per share for the nine months ended September 30, 2006.

The Company uses a Black-Scholes option-pricing model (Black-Scholes model) to estimate the fair value of the stock option grant. The use of a valuation model requires the Company to make certain assumptions with respect to selected model inputs. Expected volatility was calculated based on the historical volatility of the Company's stock price. In the future the average expected life will be based on the contractual term of the option and expected employee exercise and post-vesting employment termination behavior. Currently it is based on the simplified approach provided by SAB 107. The risk-free interest rate is based on U.S. Treasury zero-coupon issues with a remaining term equal to the expected life assumed at the date of the grant. The following were the factors used in the Black Scholes model in the quarters to calculate the compensation cost:

	Nine months ended September 30, 2007		Nine months ended September 30, 2006	
Stock price volatility	97.6	98.7%	92.9 to 94.1%	
Risk-free rate of return	4.05	4.95%	4.76 to 5.27%	
Annual dividend yield		0%		0%
Expected life	1.5 to 4.5 Years		3 to 5 Years	

### Net Loss Per Share

Earnings per share require presentation of both basic earnings per common share and diluted earnings per common share. Since the Company has a net loss for all periods presented since inception, common stock equivalents are not included in the weighted average calculation since their effect would be anti-dilutive.

### **NOTE 2 - SHAREHOLDERS EQUITY**

On November 21, 2006, the Company entered into a Bridge Financing Agreement with Asset Protection Fund (APF), whereby APF loaned the Company \$250,000. The term of the loan was the shorter of when the Company completed a Private Placement Offering or six months from the loan origination date and it accrued interest at a rate of 10% per annum. Additionally, the Company issued APF 400,000 shares of restricted common stock as a loan fee. The Company recorded a deferred loan cost of \$140,000 based on the Company's closing common stock price on the day that the loan was funded. The deferred loan cost was amortized over the term of the loan and recorded as additional interest expense. On March 27, 2007, the Company completed the private placement transaction and repaid the loan to Asset Protection Fund of \$250,000 plus accrued interest of \$8,630. In the nine months ended September 30, 2007, the Company recognized \$108,000 of interest expense related to the

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amortization of the deferred loan costs.

On December 12, 2006, the Company entered into a Bridge Financing Agreement with Global Project Finance AG ( GPF ), whereby GPF loaned the Company the amount of \$250,000 which was funded on January 16, 2007. The term of the loan was the shorter of when the Company completed a Private Placement Offering or six months from the loan origination date and it accrued interest at a rate of 10% per annum. Additionally, the Company issued GPF 400,000 shares of restricted common stock as a loan fee. The Company recorded, as interest expense, an amount based on the

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Company's closing common stock price on the day that the loan was funded, and the Company recorded \$320,000 representing the fair value of the stock provided. This deferred loan cost was to be amortized over the term of the loan and recorded as an additional interest expense. On March 27, 2007 the Company repaid the loan plus accrued interest of \$4,795. In the nine months ended September 30, 2007, the Company recognized \$320,000 of interest expense in connection with this transaction.

On December 18, 2006, the Company entered into an agreement with Lighthouse Capital for the referral of APF and GPF, or other potential financing contacts to the Company. The term of this Agreement was for a period of sixty days from the date of the Agreement and the Company would pay a fee in the amount of 200,000 restricted shares of the Company's common stock to the referral representative upon funding received from any one or more referrals in the total aggregate amount of \$500,000. On January 16, 2007, GPF funded the Company \$250,000, to aggregate \$500,000 received by the Company from the referrals of Lighthouse Capital. Per the terms of the Agreement, the Company issued Lighthouse Capital 200,000 shares and recorded an expense of \$160,000 based on the closing market price on the date of the funding.

On March 5, 2007, the Company announced that it had completed the sale of two million units in a private placement transaction for gross proceeds of \$2,000,000. The placement was sold to accredited individual and institutional investors. The units were sold under the exemption provided in Regulation D of Rule 506 and Section 415 of the Securities Act. The terms of the private placement provided for a unit offering at \$1.00 per unit. Each unit was comprised of one share and one half of a warrant to purchase a share of common stock at an exercise price of \$1.50 per share. The shares of common stock and the shares underlying the warrants have been registered under the Securities Act of 1933, as amended, and may be offered or sold in the United States. On March 7, 2007, the shareholders approved the placement transaction, and on March 27, the Company closed the transaction. The Company incurred \$221,907 of offering expenses in connection with the offering, netting the Company \$1,778,094 in proceeds. Additionally, the Company engaged a number of selling agents in connection with the sale of the private placement and paid compensation of 108,500 warrants for their efforts.

On March 7, 2007, at the annual shareholder meeting, the shareholder approved an increase in the number of shares issuable under the 2003 Stock Incentive Plan to 2,200,000 shares of our Common Stock. During the three months ended September 30, 2007 the Company recorded an expense of \$172,574 related to options issued to athletes, consultants, employees and executives of the Company. Additionally, at the shareholder meeting, the stockholders of the Company approved the creation of the 2006 Distributor Option Plan and reserved thereunder options to purchase 500,000 shares of common stock. The Company recorded an expense of \$5,142 for the three months ended September 30, 2007, in connection with the issuance of options under this plan.

On March 26, 2007, the Company entered into an amended employment contract ( Employment Agreement ) with Sanford Greenberg to provide for the assignment of the benefits and obligations of the Employee Agreement from XELR8 Holdings, Inc. to XELR8, Inc. The amendment provides that Mr. Greenberg will receive annual compensation of \$1. Additionally, Mr. Greenberg waives any and all rights to participate in any incentive executive bonus plan of the Company, but will receive a bonus equal to one percent (1%) of the gross sales of XELR8, Inc. from November 1, 2006, for a period of 12 years. Further, Mr. Greenberg shall receive 1,500,000 restricted shares of the Company, and he agreed to waive and forfeit options for 250,000 shares of the Company's common stock that were granted on April 1, 2004. The 1,500,000 restricted shares were issued on March 27, 2007, in satisfaction of the obligation of \$540,000 which was recorded in the year ended December 31, 2006 financial statements. The fair value was determined based on the closing market value of the Company share price on the date that the Company and Mr. Greenberg agreed to the amendment, subject to shareholder approval, of November 17, 2006.

On April 6, 2007, a principal shareholder of the Company granted 200,000 shares of common stock to the employees of the Company. Under the guidance issued by the SEC in Staff Accounting Bulletin 107 (SAB 107), share-based payments issued to an employee of a reporting entity by a related party or other holder of economic interest in the entity as compensation for services provided to the entity are to be recorded as a compensation expense by the entity. As a principal shareholder, Mr. Greenberg, is a holder of an economic interest in the entity, and therefore the Company is required to record an expense of \$350,000 in stock based compensation and an off-setting entry directly to additional paid in capital based on the share price on the date of the grant.

On May 8, 2007, the Company announced that it had completed the sale of one million units in a private placement transaction for gross proceeds of \$2,000,000. The placement was sold to an accredited individual and institutional investors. The units were sold under the exemption provided in Regulation D of Rule 506 and Section 415 of

the Securities Act. The terms of the private placement provided for a unit offering at \$2.00 per unit. Each unit was comprised of one share of common stock, half of a Class E warrant to purchase common stock and half of a Class F warrant to purchase common stock. The Class E warrants have an exercise price of \$2.00 and are for a five year period with a call provision by the Company when the Company's share price trades above \$4.50 for twenty consecutive days. The Class F warrants have an exercise price of \$2.00 and a five year term, with no call provision. The shares of common stock and the shares underlying the warrants have been registered under the Securities Act of 1933, as amended, and may be offered or sold in the United States. The Company incurred \$158,645 of offering expenses in connection with the offering, netting the Company \$1,841,355 in proceeds. Additionally, the Company engaged a number of selling agents in connection with the sale of the private placement and paid compensation of 55,000 warrants for their efforts.



## Item 2 MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

### Cautionary Note Regarding Forward-Looking Statements

This report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 and is subject to the safe harbor created by those sections. We intend to identify forward-looking statements in this report by using words such as believes, intends, expects, may, will, should, plan, projected, contemplates, anticipates, potential, continue, or similar terminology. These statements are based on our beliefs as well as assumptions we made using information currently available to us. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise. Because these statements reflect our current views concerning future events, these statements involve risks, uncertainties, and assumptions. Actual future results may differ significantly from the results discussed in the forward-looking statements. These risks include changes in demand for our products, changes in the level of operating expenses, our ability to expand our network of distributors, changes in general economic conditions that impact consumer behavior and spending, product supply, the availability, amount, and cost of capital to us and our use of such capital, and other risks discussed in this report. Additional risks that may affect our performance are discussed under Risk Factors Associated with Our Business in our Registration Statement Form SB-2 declared effective April 5, 2005 and in Registration Statements on Form S-3 declared effective on June 11, 2007 and July 20, 2007. Readers are cautioned not to place undue reliance on the forward-looking statements contained in this report.

### Overview

We are in the business of developing, selling, marketing and distributing nutritional supplement products and functional foods. We market our products primarily through direct selling or network marketing, in which independent distributors sell our products. In addition, we sell our products directly to professional and Olympic athletes and professional sports teams.

Our product lines consist of four powdered beverages, 12 individual supplements packaged in our VitaCube®, and a functional food chew. Our PEAK PERFORMANCE System is a packaged product that consists of a protein drink, hydration drink and vitamin support pack all of which can be purchased as a system or individually. The SUPPORT pack has the vitamins for each serving individually packaged. The VitaCube® is an easy to use, compartmentalized box with instructions for which supplements to take and the proper times to take them. Our EAT, DRINK and SNACK System (EDS) is a packaged product that consists of functional foods and energy drinks that can be purchased as a whole system or individually. On January 12, 2007, we introduced our newest product offering, *Bazi*, a nutritional dietary supplement drink which includes eight different fruits and berries, including the Chinese jujube, plus 12 vitamins and 68 minerals.

During the third quarter of 2003, we initiated a transition of our sales and marketing efforts from sales to retail outlets and in-house telemarketing to direct selling through independent distributors and we launched our direct sales program in the second quarter of 2004. As of September 30, 2007, we had 4,940 independent distributors and 2,214 customers (excluding professional athletes and sports teams) who had purchased our products within the prior twelve months.

We maintain an inventory of our products to insure that we can timely fill our customer orders. We can have large increases in inventory levels if we have multiple product reorders in the same period. In addition, our manufacturers typically may take up to 12 weeks to deliver products after we place an order, and they have minimum order requirements, which also adds to higher inventory levels. Our inventory, net of our allowance for obsolescence, was \$613,135 at September 30, 2007, an increase from \$411,364 at December 31, 2006.

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The increase of inventory resulted from an increased portion of our sales coming from our new product *Bazi* product, and the higher anticipated demand for the *Bazi* product and the volume discounts available for purchases of higher quantities, which was offset by the resultant lower inventory requirements for our EDS and Peak Performance Systems. We believe our inventory is appropriately classified as a current asset based on the current sales levels as well as ongoing implementation of our new *Bazi* marketing plan which is designed to increase our distributor base and sales.

As a result of the launch of the *Bazi* product in January 2007 and the marketing approach to the INVITE TASTE AND FOLLOW UP , we have a charge against operations for obsolete inventory of \$122,771. Our allowance for

obsolete inventory was increased from \$41,655 at December 31, 2006 compared to \$95,414 at September 30, 2007. We believe our reserve for obsolescence is reasonable because (i) substantially all of our inventory has been recently purchased, (ii) the shelf life of our products averages three years for the legacy products and one year for Bazi™, and (iii) we have no current plans to eliminate any of our products, instead choosing to repackage them in connection with our new product branding strategy.

Our network marketing program is designed to provide an incentive for independent distributors to build, maintain and motivate a sales organization of customers and other independent distributors to enhance earning potential. Our independent distributors are compensated with commissions and bonuses on sales generated through their downline organization. Independent distributors advance in distributor levels as they develop their sales organization and increase their sales volume, which increases their compensation.

We recognize revenue when products are shipped to our customers. Revenue is reduced by product returns at the time we take the product either back into inventory or dispose of it. In addition, we estimate a reserve total for future returns. We also collect an annual website fee from distributors that is deferred on receipt and recognized as income on a straight-line basis over the subsequent twelve-month period. Cost of our sales consists of expenses directly related to the production and distribution of the products and certain sales materials. Included in the sales and marketing expenses are independent distributor commissions, bonus and incentives along with other general selling expenses. We expect our independent distributor expenses, as a percentage of net revenues, to decrease as independent distributors require less additional incentives and rely on the incentives in our direct sales program. General and administrative expenses include salaries and benefits, rent and building expenses, legal, accounting, telephone and professional fees.

Our revenue will depend on the number and productivity of our independent distributors, who purchase products and sales materials from us for resale to their customers or for personal use. Because we will distribute substantially all of our products through our independent distributors, our failure to retain our existing distributors and recruit additional distributors could have an adverse effect on our revenue.

Due to the recent start-up of our direct sales program we believe that the number of our distributors is an important indicator to monitor. In addition, we will monitor the sales generated per independent distributor as well as the success of our independent distributors in recruiting new independent distributors.

With respect to industry and market factors that may affect us directly, we believe that industry credibility in both direct selling and nutritional supplements will be critical elements in whether we can increase revenues and become profitable. Any adverse developments in either of these two areas, to us or in our industry, could lead to a lower number of our independent distributors and reduced sales and recruiting efforts by existing distributors, as well as a loss or no increase in the number of sports celebrity endorsers of our products. We do not know what industry growth was for 2006 or will be for 2007, nor do we have enough experience in the direct sales channel to determine whether a slower industry growth rate, which occurred for several years leading up to 2003 and which has subsequently been slow, will adversely affect us.

Our operating plan for 2007 is focused on increasing the number of independent distributors, growing revenues, and generating gross profits with a focus on the Bazi product. Due to the relatively recent commencement of our direct selling program through independent distributors, we cannot predict our revenue, gross profit, net income or loss or use of cash and cash equivalents; however, we expect net losses will continue for at least the next 3 months.

Our independent auditors have noted in their reports on our financial statements as of December 31, 2006 and 2005 and for the years then ended, that there is substantial doubt regarding our ability to continue as a going concern. To date this contingency has not affected our ability to secure funding for our operations; however, going forward, in the event this uncertainty is not resolved, we may experience more difficulty in raising funds to operate our Company if we are required to raise such capital. In March 2007, we completed a private sale of common stock of the Company for gross proceeds of \$2,000,000 and in May 2007 completed a second private sale of common stock of the Company for additional

gross proceeds of \$2,000,000.

**Critical Accounting Policies and Estimates**

Discussion and analysis of our financial condition and results of operations are based upon financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of

assets, liabilities, revenue and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, we evaluate our estimates; including those related to collection of receivables, inventory obsolescence, sales returns and non-monetary transactions such as stock and stock options issued for services and beneficial conversion features of notes payable. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. We believe the following critical accounting policies affect our more significant judgments and estimates used in the preparation of our financial statements.

**Revenue Recognition.** In accordance with Staff Accounting Bulletin 104 Revenue Recognition in Financial Statements, revenue is recognized at the point of shipment, at which time title is passed. Net sales include sales of products, sales of marketing tools to independent distributors and freight and handling charges. With the exception of approved professional sports teams, we receive the net sales price from all of our orders in the form of cash or credit card payment prior to shipment. Professional sports teams with approved credit have been extended payment terms of net 30 days.

**Allowances for Product Returns.** Allowances for product returns are recorded at the time product is shipped. These accruals are based upon the historical return rate since the inception of our network marketing program in the third quarter of 2003, and the specific historical return patterns by product. Our return rate since the third quarter of 2003 has varied from 0.7% to 7.7% of our net sales.

We offer a 60-day, 100% money back unconditional guarantee to all customers and independent distributors who have never before purchased products from us, for their initial enrollment pack. Additional products purchased during their first 60 days are refundable for 100% of the sales price if returned in resalable condition. As of September 30, 2007, orders shipped that are subject to our 60-day money back guarantee were approximately \$344,671. All other product may be returned to us by any customer or independent distributor if it is unopened and undamaged for a 100% sales price refund, less a 10% restocking fee, provided the product is returned within 12 months of purchase and is being sold by us at the time of return. We are not able to estimate the amount of revenue we have recognized that is held by these buyers of product and which is returnable, because it is not possible to determine the amount of product that is unopened and undamaged. Product damaged during shipment is replaced wholly at our cost, which historically has been negligible.

We monitor our return estimate on an ongoing basis and may revise allowances to reflect our experience. Our reserve for product returns at September 30, 2007 and December 31, 2006 was \$76,193 and \$45,327, respectively. To date, product expiration dates have not played any role in product returns, and we do not expect they will in the future because it is unlikely that we will ship product with an expiration date earlier than the latest allowable product return date.

**Inventory Valuation.** Inventories are stated at the lower of cost or market on a first-in first-out basis. A reserve for inventory obsolescence is maintained and is based upon assumptions about current and future product demand, inventory whose shelf life has expired and market conditions. A change in any of these variables may require additional reserves to be taken. We reserved \$95,414 for obsolete inventory as of September 30, 2007 and \$41,655 as of December 31, 2006.

**Stock Based Compensation.** Many equity instrument transactions are valued based on pricing models such as Black-Scholes-Merton, which require judgments by us. Values for such transactions can vary widely and are often material to the financial statements.

Effective January 1, 2006, we adopted SFAS No. 123 (revised 2004), Share-Based Payment (SFAS 123R), which requires compensation costs related to share-based transactions, including employee stock options, to be recognized in the financial statements based on fair value. SFAS 123R revises SFAS No. 123, Accounting for Stock-Based Compensation, (SFAS 123) and supersedes Accounting Principles Board Opinion

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(APB) No. 25, Accounting for Stock Issued to Employees. In March 2005, the Securities and Exchange Commission (the SEC) issued Staff Accounting Bulletin No. 107 (SAB 107) regarding the SEC's interpretation of SFAS 123R and the valuation of share-based payments for public companies. We have applied the provisions of SAB 107 in its adoption of SFAS 123R. We adopted the provisions of SFAS 123R using the modified prospective transition method. In accordance with this transition method, the company's consolidated financial statements for prior periods have not been restated to reflect the impact of SFAS 123R. Under the modified prospective transition method, share-based compensation expense for the first quarter of 2006

includes compensation expense for all share-based compensation awards granted prior to, but for which the requisite service has not yet been performed as of January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of SFAS 123. Share-based compensation expense for all share-based compensation awards granted after January 1, 2006 is based on the grant date fair value estimated in accordance with the provisions of SFAS 123R.

## Results of Operations

**For the three months ended September 30, 2007 compared to the three months ended September 30, 2006.**

*The discussion below first presents the results of the quarter ended September 30, 2007 followed by the results of the quarter ended September 30, 2006*

*Net sales.* Net sales were \$1,432,220 an increase of 136% compared to \$608,111. The increase in net sales can be attributed to launch of the Bazi product on January 12, 2007 and the resultant increase in the number of independent distributors and customers.

The percentage that each product category represented of our net sales is as follows:

Product Category	Three Months Ended September 30,	
	2007 % of Sales	2006 % of Sales
Bazi™	86%	1%
EAT	1%	17%
DRINK	3%	31%
SNACK	0%	9%
HYDRATE	2%	12%
Vitamins and minerals, including SUPPORT	2%	12%
BUILD	1%	5%
Other-educational materials, apparel	5%	14%

*Gross Profit.* Gross profit increased to \$1,089,987 compared to \$396,598, an increase of 175%. Gross profit as a percentage of revenue (gross margin) increased to 76% from 65%. The increase in the gross margin was a result of the increased sales of the new Bazi product that has a higher gross margin as compared to the legacy products. The increase was offset as a result of the scrap and obsolescence charges resulting from new marketing materials for Bazi compared with the XELR8 WHAT MOVES YOU® marketing materials.

*Sales and marketing expenses.* Sales and marketing expenses increased to \$820,080 from \$571,160, an increase of 44%. The increase in sales and marketing expenses is a result of the increased payments to our independent distributors as a result of increased sales. The increase was also the result of the additional staff in the customer service center.

*General and administrative expenses.* General and administrative expenses were \$642,930, an increase of 11% compared to \$577,456. The increase is a result of higher expenses in the current year, principally related to public company costs, including costs to comply with the requirements of the Sarbanes Oxley Act.

*Research and development expenses.* Research and development expenses decreased to \$3,214 from \$20,246 a decrease of 84%. While we are continuing to research and develop ingredients and manufacturing technologies for our product line internally, the expense in the prior year was primarily from the expense related to our technology provider. The Company terminated this agreement in October 2006.

*Depreciation and Amortization Expense.* The expense was \$11,716 compared to \$11,779, a decrease of 1%. The decrease is a result of the full depreciation of certain assets.



*Net Loss.* Our net loss was \$355,279 or (\$0.02) per share, compared to \$778,944 or (\$0.08) per share, a decrease of net loss of \$.06 per share or 71%, respectively. The decrease in net loss is associated with the increase in sales and gross margin.

**For the nine months ended September 30, 2007 compared to the nine months ended September 30, 2006.**

*The discussion below first presents the results of the nine months ended September 30, 2007 followed by the results of the nine months ended September 30, 2006*

*Net sales.* Net sales were \$3,687,690, an increase of 114% compared to \$1,724,252. The increase in net sales can be attributed to the launch of the Bazi product on January 12, 2007 and the resultant increase in the number of independent distributors and customers.

The percentage that each product category represented of our net sales is as follows:

Product Category	Nine Months Ended September 30,	
	2007 % of Sales	2006 % of Sales
Bazi™	80%	1%
EAT	1%	18%
DRINK	4%	26%
SNACK	1%	10%
HYDRATE	2%	12%
Vitamins and minerals, including SUPPORT	3%	13%
BUILD	2%	5%
Other-educational materials, apparel	7%	16%

*Gross Profit.* Gross profit increased to \$2,672,925 compared to \$1,101,411, an increase of 143%. Gross profit as a percentage of revenue (gross margin) increased to 72% from 64%. The increase in the gross margin was a result of the increased sales of the new Bazi product that has a higher gross margin as compared to the legacy products. The increase was offset by the costs related to the scrap and obsolescence charges resulting from new marketing materials for Bazi compared with the XELR8 WHAT MOVES YOU marketing materials.

*Sales and marketing expenses.* Sales and marketing expenses increased to \$2,417,200 from \$2,214,842, an increase of 9%. Sales and marketing expenses consist primarily of distributor commissions, costs associated with attracting experienced field leaders for our distributor network, and events and training for the distributors. There were additional increases for salaries related to our customer service department, and for the national event in March, and the leadership event in September.

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*General and administrative expenses.* General and administrative expenses were \$2,429,738, an increase of 14% compared to \$2,136,506. Our general and administrative expenses consist primarily of employee and compensation for executives and administrative personnel, legal and accounting fees, business consultants, rent and associated building costs, costs associated with being a public company, business insurance and office costs such as telephone, supplies, computer hardware and software and hosting fees. The increase is a result of \$661,132 in stock based compensation that we paid to the referral agent in connection with the short term loan financing and executive compensation and a charge of \$350,000 in stock based compensation that the Company recorded for the grant of stock by a principal shareholder, Mr. Greenberg, to the employees of the Company. Under the guidance issued by the SEC in Staff Accounting Bulletin 107 (SAB 107), share-based payments issued to an employee of a reporting entity by a related party or other holder of economic interest in the entity as compensation for services provided to the entity are to be recorded as a compensation expense by the entity. This increase was offset by lower compensation as a result of the restructured employment agreement with Mr. Greenberg, and the departure of Mr. Mathis, our former Chief Executive Officer, and Mr. Litt, our former Vice-President of Sales, as compared with the prior year.

*Research and development expenses.* Research and development expenses decreased to \$8,342 from \$64,180. We are continuing to research and develop ingredients and manufacturing technologies for our product line internally, the expense in the prior year was primarily from the expense related to our technology provider. The Company terminated this agreement in October 2006.

*Depreciation and Amortization Expense.* The expense was \$45,992 compared to \$54,554, a decrease of 16%. As a result of the continued success of the *Bazi* product we evaluated the carrying value of the trademarks associated with the legacy products that the Company had and fully amortized these intangible balances.

*Net Loss.* Our net loss was \$2,600,168 or (\$0.19) per share, compared to \$3,335,914 or (\$0.35) per share. Our net loss decreased by 22% as a result of higher revenue and gross margin which was partially offset by increased expenses for Sales and Marketing and General and Administrative related to Stock Based Compensation. The change in net loss per share is also attributable to the increase in the weighted number of shares outstanding.

### **Liquidity and Capital Resources**

To date, our operating funds have been provided primarily from sales of our common stock (\$14,913,421), and by loans from our founder and by various stockholders (\$3,989,209), through September 30, 2007, and to a lesser degree, cash flow provided by sales of our products.

On November 21, 2006, we obtained a \$250,000 short-term loan from an unrelated party. We were also able to obtain a commitment for an additional \$250,000 from an unrelated party that funded in January 2007. Each loan provided for the issuance of 400,000 restricted shares and interest at 10% per annum. The loans matured at the earlier of six months from funding or the final closing of a private placement.

On March 5, 2007, we announced that the Company had raised \$2,000,000 in gross proceeds in a private placement transaction, which would close subject to shareholder and American Stock Exchange approval. On March 7, 2007, the shareholders approved the private placement transaction, and on March 27, we closed the transaction. At the time of closing, we paid in full the short-term loans of \$500,000 plus accrued interest of \$13,425 leaving us with no short-term or long-term debt at this time, other than trade accounts payable and other accrued liabilities.

On May 8, 2007, the Company announced that it had completed the sale of one million units in a private placement transaction resulting in gross proceeds of \$2,000,000, which would close subject to American Stock Exchange approval. On May 24, 2007, we closed the transaction.

We used \$958,122 of cash for operations in the nine months ended September 30, 2007, compared to \$2,379,048 of cash for operations in the nine months ended September 30, 2006. The use of cash in our operations results from incurring and accruing expenses to suppliers necessary to generate business and service our customers at a time when revenues did not keep pace with expenses. As of September 30, 2007, we had \$2,473,233 in cash and cash equivalents available to fund future operations. Net working capital increased from (\$409,382) at December 31, 2006, to \$2,574,441 at September 30, 2007.

Our independent auditors have noted in their reports on our financial statements as of December 31, 2006 and 2005 and for the years then ended, that there is substantial doubt regarding our ability to continue as a going concern. To date this contingency has not affected our ability to secure funding for our operations; however, going forward, we may experience more difficulty in raising additional funds to operate our Company.

In the event that we are successful in completing our business plan of increasing the number of distributors, sales levels and consequently increased profitability, we believe that our cash resources will be sufficient to fund our operations for the next 24 months. If our business operations do not result in increased product sales, our business viability, financial position, results of operations and cash flows will likely be adversely affected. Further, if we are not successful in achieving profitability, additional capital will be required to conduct ongoing operations. We cannot predict the terms upon which we could raise such capital or if any capital would be available at all.

### **Customer Concentrations**

We had no single customer that accounted for any substantial portion of our revenues.

*Off-Balance Sheet Items*

We have no off-balance sheet items as of September 30, 2007.

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**Item 3 CONTROLS AND PROCEDURES**

Prior to the filing of this report, the Company's management carried out an evaluation, under the supervision and with the participation of its Chief Executive Officer and the Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures as of the end of the period covered by this report. Based on this evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the Company's controls and procedures were effective to ensure that information required to be disclosed by the Company in the reports filed by it under the Securities and Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and include controls and procedures designed to ensure that information required to be disclosed by the Company in such reports is accumulated and communicated to the Company's management, including the Chief Executive Officer and the Chief Financial Officer of the Company, as appropriate to allow timely decisions regarding required disclosure.

There has been no change in the Company's internal control over financial reporting that occurred during the Company's most recent fiscal quarter that has materially affected or is reasonably likely to materially affect its internal control over financial reporting.

**Part II OTHER INFORMATION**

**Item 1. LEGAL PROCEEDINGS**

None.

**Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

None.

**Item 3. DEFAULTS UPON SENIOR SECURITIES**

None.

**Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

None.

**Item 5. OTHER INFORMATION**

None.

**Item 6. EXHIBITS**

<b>Exhibit No</b>	<b>Description</b>
31.1	Certification of CEO as Required by Rule 13a-14(a/15d-14)
31.2	Certification of CFO as Required by Rule 13a-14(a/15d-14)

**Item 1. LEGAL PROCEEDINGS**

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- 32.1 Certification of CEO as Required by Rule 13a-14(a and Rule 15d-14(b) (17 CFR 240.15d-14(b and Section 1350 of Chapter 63 of Title 18 of the United States Code)
- 32.2 Certification of CFO as Required by Rule 13a-14(a and Rule 15d-14(b) (17 CFR 240.15d-14(b and Section 1350 of Chapter 63 of Title 18 of the United States Code)
- 99.1 Press Release

**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, in the City and County of Denver, State of Colorado, on November 2, 2007.

**XELR8 HOLDINGS, INC.**

By */s/ John D. Pougnet.*  
John D. Pougnet  
Chief Executive Officer  
Chief Financial Officer (Principal Accounting Officer)