

Labor Smart, Inc.
Form 10-Q
May 15, 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 March 31, 2014

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

Commission file number **000-54654**

LABOR SMART, INC.

(Exact name of registrant as specified in its charter)

Nevada

(State or other jurisdiction of incorporation or organization)

45-2433287

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

5604 Wendy Bagwell Parkway, Suite 223

Hiram, GA

(Address of principal executive offices)

30141

(Zip Code)

(770) 222-5888

(Registrant's telephone number, including area code)

Indicate by check mark whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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 definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer
Non-accelerated filer

Accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

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

Number of shares of issuer's common stock outstanding as of May 12, 2014 was 22,567,807

LABOR SMART, INC.

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Table of Contents**PART I – FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****LABOR SMART, INC.****BALANCE SHEETS****(UNAUDITED)**

	March 31, 2014	December 31, 2013
Assets		
Current assets		
Cash	\$723,884	\$178,539
Accounts receivable, net	1,973,334	1,941,437
Prepaid expense	54,628	45,497
Deferred financing costs	39,251	57,748
Marketable securities	40,200	4,972
Other assets	71,835	11,591
Total current assets	2,903,132	2,239,784
Deposits	20,014	20,014
Fixed assets, net	40,480	7,894
Customer relationships, net	203,855	228,028
Total long-term assets	264,349	255,936
Total assets	\$3,167,481	\$2,495,720
Liabilities and Stockholders' Deficit		
Current liabilities		
Accounts payable and accrued liabilities	\$241,452	\$135,524
Loan payable to factor	763,335	865,321
Payroll taxes payable	1,397,063	1,487,907
Notes payable, related party	37,306	44,806
Convertible note payable, net of unamortized discount of \$1,409,585 and \$578,848, respectively	2,383,552	1,057,679
Convertible note payable derivative liability	122,506	20,701
Total current liabilities	4,945,214	3,611,938
Contingent liability	37,145	79,221
Total liabilities	4,982,359	3,691,159

Stockholders' deficit

Common stock; \$0.001 par value; 75,000,000 shares authorized,
22,239,315 and 20,982,740 issued and outstanding as of
March 31, 2014 and December 31, 2013, respectively.

	22,239	20,982
Additional paid-in capital	2,419,704	1,978,043
Accumulated deficit	(4,258,286)	(3,193,778)
Accumulated other comprehensive income	1,465	(686)
Total stockholder's deficit	(1,814,878)	(1,195,439)
Total liabilities and stockholders' deficit	\$3,167,481	\$2,495,720

See Accompany Notes to Financial Statements

Table of Contents**LABOR SMART, INC.****STATEMENT OF OPERATIONS AND COMPREHENSIVE INCOME****(UNAUDITED)**

	For the three months March 31, 2014	For the three months March 31, 2013
Revenues	\$4,792,941	\$2,503,872
Cost of sales	3,685,229	2,152,476
Gross profit	1,107,712	351,396
Operating expenses		
Professional fees	92,597	62,500
Stock-based compensation for services	57,156	250,616
Payroll expenses	443,654	160,076
Bad debt expense	11,982	—
Loss on sale of receivables	—	35,522
General and administrative expense	778,598	249,167
Total operating expenses	1,383,987	757,881
Operating loss	(276,275)	(406,485)
Other income (expenses)		
Interest and finance expense	(798,446)	(241,376)
Interest income	—	73
Gain on change in fair value in derivative liability	10,656	—
Loss on sale of securities	(443)	(1,355)
Total other income (expenses)	(788,233)	(242,658)
Net loss	\$(1,064,508)	\$(649,143)
Other comprehensive income:		
Unrealized gain on marketable securities	2,151	2,381
Other comprehensive income	2,151	2,381
Comprehensive loss	\$(1,062,357)	\$(646,762)
Basic loss per common share	\$(0.05)	\$(0.04)
Basic weighted average common		

shares outstanding	21,454,557	18,029,377
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See Accompany Notes to Financial Statements

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Table of Contents**LABOR SMART, INC.****STATEMENT OF CASH FLOWS****(UNAUDITED)**

	For the three months March 31, 2014	For the three months March 31, 2013
Cash flows from operating activities:		
Net loss	\$(1,064,508)	\$(649,143)
Adjustments to reconcile net loss to net cash used in operating activities:		
Stock-based compensation	57,156	250,616
Interest and financing costs	695,918	233,746
Depreciation and amortization	28,212	—
Loss on sale of securities	443	1,355
Gain on change in fair value of derivative liability	(10,656)	—
Changes in operating assets and liabilities:		
Increase in off-balance sheet receivable factoring	—	206,821
Increase in accounts receivables	(31,897)	(581,639)
Increase (decrease) in prepaid expense	(9,131)	6,270
Increase in other assets	(60,244)	(14,718)
Increase in accounts payable and accrued liabilities	105,928	27,003
Increase (decrease) in accrued liabilities, related party	0	3,872
Increase in payroll taxes payable	(90,844)	244,725
Net cash used by operating activities	(379,623)	(271,092)
Cash flows from investing activities:		
Purchase of fixed assets	(36,625)	—
Proceeds from sale of marketable securities	21,805	92,453
Purchase of marketable securities	(55,325)	(92,453)
Net cash used by investing activities	(70,145)	—
Cash flows from financing activities:		
Proceeds from common stock	—	50,000
Proceeds from convertible notes payable	1,237,395	270,000
Payment on convertible note payable	(89,000)	—
Payment on notes payable	—	(5,054)
Payment on notes payable - related party	(7,500)	(43,000)
Payments on loan to factor	(101,986)	—
Payments on contingent liability	(43,796)	—
Net cash provided by financing activities	995,113	271,946
Net change in cash	545,345	854

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Cash, beginning of period	178,539	124,888
Cash, end of period	\$723,884	\$125,742
Supplemental disclosure of cash flow information:		
Interest paid	\$102,528	\$—
Taxes paid	\$—	\$—
Non-cash interest and financing activities		
Warrants issued as part of deferred finance costs	\$—	\$125,445
Shares issued for prepaid services	\$—	\$236,685
Finance costs included in convertible note value	\$—	\$14,500
Shares issued for convertible notes	\$210,000	\$268,062

See Accompany Notes to Financial Statements

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LABOR SMART, INC.

NOTES TO FINANCIAL STATEMENTS

NOTE 1 – NATURE OF OPERATIONS

Nature of Business

Labor Smart, Inc. (the “Company”) was incorporated in the State of Nevada on May 31, 2011. Labor Smart, Inc. provides temporary blue-collar staffing services. It supplies general laborers on demand to the light industries, including manufacturing, logistics, and warehousing, skilled trades’ people, and general laborers to commercial construction industries.

NOTE 2 – GOING CONCERN

The accompanying financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. The Company requires capital for its contemplated operational and marketing activities. The Company’s ability to raise additional capital through the future issuances of common stock is unknown. Accordingly, the Company had a net loss of \$1,064,508 for the three months ended March 31, 2014. Additionally, the operating activities of the Company used \$379,623 net cash during the same three month period. The obtainment of additional financing and increasingly profitable operations are necessary for the Company to continue operations. The ability to successfully resolve these factors raise substantial doubt about the Company’s ability to continue as a going concern. These 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 result from this uncertainty.

NOTE 3 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

These financial statements are presented in United States dollars and have been prepared in accordance with generally accepted accounting principles in the United States of America. The Company has adopted a December 31 fiscal year end.

In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair statement of results in accordance with US GAAP have been included and properly prepared within reasonable limits of materiality and within the framework of the significant accounting policies summarized below:

Fair Value of Financial Instruments

As required by the Fair Value Measurements and Disclosures Topic of the FASB ASC (“ASC 820-10”), fair value is measured based on a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value as follows: (Level 1) observable inputs such as quoted prices in active markets; (Level 2) inputs, other than the quoted prices in active markets, that are observable either directly or indirectly; and (Level 3) unobservable inputs in which there is little or no market data, which require the reporting entity to develop its own assumptions.

The three levels of the fair value hierarchy are described below:

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- Level 1 Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;
- Level 2 Quoted prices in markets that are not active, or inputs that are observable, either directly or indirectly, for substantially the full term of the asset or liability;
- Level 3 Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (supported by little or no market activity).

Pursuant to ASC 825, the fair value of cash and marketable securities is determined based on “Level 1” inputs, which consist of quoted prices in active markets for identical assets. The Company believes that the recorded values of cash, accounts receivables, marketable securities, accounts payable and accrued liabilities, and notes payable approximate their current fair values because of their nature and respective relatively short maturity dates or durations.

Assets measured at fair value on a recurring basis were presented on the Company’s balance sheets as of March 31, 2014 and December 31, 2013 as follows:

Fair Value Measurements as of March 31, 2014 Using:

	<u>Total Carrying Value as of 03/31/14</u>	<u>Quoted Market Prices in Active Markets (Level 1)</u>	<u>Significant Other Observable Inputs (Level 2)</u>	<u>Significant Unobservable Inputs (Level 3)</u>
Assets:				
Equity securities	\$ 40,200	\$ 40,200	\$ 0	\$ 0
Total	\$40,200	\$ 40,200	\$ 0	\$ 0
Liabilities:				
Derivative liability	\$ 122,506	\$ 0	\$ 122,506	\$ 0
Contingent liability	37,145	0	0	37,145
Total	\$159,651	\$0	\$122,506	\$37,145

Fair Value Measurements as of December 31, 2013 Using:

	<u>Total Carrying Value as of 12/31/13</u>	<u>Quoted Market Prices in Active Markets (Level 1)</u>	<u>Significant Other Observable Inputs (Level 2)</u>	<u>Significant Unobservable Inputs (Level 3)</u>
Assets:				
Equity securities	\$ 4,972	\$ 4,972	\$ 0	\$ 0
Total	\$4,972	\$ 4,972	\$ 0	\$ 0
Liabilities:				

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Derivative liability	\$ 20,701	\$ 0	\$ 20,701	\$ 0
Contingent liability	79,221	0	0	79,221
Total	\$99,922	\$0	\$20,701	\$79,221

Cash and Cash Equivalents

Cash and cash equivalents consist of cash and short-term investments with original maturities of less than 90 days. Cash equivalents are placed with high credit quality financial institutions and are primarily in money market funds. The carrying value of those investments approximates fair value.

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Revenue Recognition

The Company recognizes revenues and the related costs when persuasive evidence of an arrangement exists, delivery and acceptance has occurred or service has been rendered, the price is fixed or determinable, and collection of the resulting receivable is reasonably assured. Amounts invoiced or collected in advance of product delivery or providing services are recorded as deferred revenue. The Company accrues for customer credits, bad debts, and other allowances based on its historical experience. Staffing revenue is recognized as the services are performed. Revenue also includes billable travel and other reimbursable costs and is record net of sales tax.

Deferred Financing Costs

Deferred financing costs consist of costs incurred to obtain debt financing, including legal fees, origination fees and administration fees. Costs associated with the Convertible Promissory Note are deferred and amortized in our accompanying statement of operations using the straight-line method, which approximates the effective interest method, over the terms of the respective financing instrument.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires the Company to make estimates and judgments that affect the reported amounts of assets and liabilities, revenues and expenses, and related disclosures of contingent assets and liabilities. These estimates and judgments are based on historical information, information that is currently available to the Company, and on various other assumptions that the Company believes to be reasonable under the circumstances. Actual results could differ from those estimates.

Factoring Agreement and Accounts Receivable

On July 31, 2013 the Company entered into a Purchase and Sale Agreement with Transfac Capital, Inc. (“Transfac”). Advances to the Company from Transfac are with recourse and are secured by assets of the Company and are treated as a secured financing arrangement. As of March 31, 2014 and December 31, 2013, factored accounts receivable total \$763,335 and \$865,321, respectively.

Allowance for Doubt