

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

GOLFGEAR INTERNATIONAL INC
Form 10QSB
August 19, 2002

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-QSB

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

For the Quarterly Period Ended June 30, 2002

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

For the transition period from _____ to _____

Commission File Number: 0-28007

GOLFGEAR INTERNATIONAL, INC.

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

Nevada

43-1627555

(State or other jurisdiction of
incorporation or organization)

(I.R.S. Employer
Identification Number)

5285 Industrial Drive, Huntington Beach, California 92649

(Address of principal executive offices)

(714) 899-4274

(Issuer's telephone number)

Not applicable

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

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

As of June 30, 2002, the Company had 34,511,454 shares of common stock issued and outstanding.

Transitional Small Business Disclosure Format: Yes No

Documents incorporated by reference: None.

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Consolidated Balance Sheets - June 30, 2002 (Unaudited) and December 31, 2001

Consolidated Statements of Operations (Unaudited) - Three Months and Six Months Ended June 30, 2002 and 2001

Consolidated Statements of Cash Flows (Unaudited) - Six Months Ended June 30, 2002 and 2001

Notes to Consolidated Financial Statements (Unaudited) - Six Months Ended June 30, 2002 and 2001

Item 2. Management's Discussion and Analysis or Plan of Operation

PART II. OTHER INFORMATION

Item 1 - Legal proceedings

Item 2 - Recent sales of unregistered securities

Item 6 - Exhibits and reports on form 8-K

SIGNATURES

EXHIBIT

2

GolfGear International, Inc. and Subsidiaries Consolidated Balance Sheets

	June 30, 2002	December 31, 2001
	-----	-----
	(Unaudited)	
ASSETS		
Current assets:		
Cash	\$1,135,782	\$ 120,135
Accounts receivable, net of allowance for doubtful accounts of \$60,261, and \$78,337 at June 30, 2002, and December 31, 2001, respectively	301,815	335,755
Inventories	642,033	691,265
Prepaid expenses	43,510	22,450
	-----	-----
Total current assets	2,123,140	1,169,605

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

Property and equipment, net of accumulated depreciation	105,119	128,754
Other assets:		
Patents and trademarks, net of accumulated amortization	73,828	83,922
Deferred financing costs, net	487,384	---
Infomercial costs	167,678	---
Deposits	7,770	12,400
	736,660	96,322
Total assets	\$2,964,919	\$ 1,394,681

(continued)

3

GolfGear International, Inc. and Subsidiaries
Consolidated Balance Sheets (continued)

	June 30, 2002	December 31, 2001
	-----	-----
	(Unaudited)	
LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)		
Current liabilities:		
Accounts payable and accrued expenses	\$ 821,654	\$ 1,127,427
Income tax payable	4,000	8,000
Accrued product warranties	110,234	101,593
Accrued interest payable	13,288	8,438
Accrued officers' compensation	70,065	90,961
Bank credit line payable	51,069	57,100
Notes payable to stockholders	---	97,166
Notes payable, current portion	83,177	69,091
Total current liabilities	1,153,487	1,559,776
Non-current liabilities:		
Note payable	---	50,000
Convertible debentures	2,040,000	---
Stockholders' equity (deficit):		
Common stock, \$0.001 par value;		
Authorized - 50,000,000 shares		
Issued and outstanding -		
34,586,454 shares and 17,989,454		
shares at June 30, 2002 and		
December 31, 2001, respectively	34,586	17,989

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

Additional paid-in capital	10,522,046	8,901,273
Accumulated deficit	(9,833,975)	(9,134,357)
	-----	-----
Total stockholders' equity (deficit)	696,407	(215,095)
	-----	-----
Common stock purchase receivable note	(924,975)	---
	-----	-----
	(228,568)	(215,095)
	-----	-----
Total liabilities and stockholders' equity (deficit)	\$ 2,964,919	\$ 1,394,681
	=====	=====

See accompanying notes to consolidated financial statements.

4

GolfGear International, Inc. and Subsidiaries
Consolidated Statements of Operations (Unaudited)

	Three Months Ended June 30,	
	2002	2001
	-----	-----
Sales	\$ 386,066	\$ 740,480
Cost of goods sold	347,959	365,511
	-----	-----
Gross profit	38,107	374,969
	-----	-----
Expenses:		
Selling and marketing	160,119	132,167
Tour and pro contracts	9,795	25,156
Provision for bad debts	11,582	57,777
General and administrative	352,207	344,717
Depreciation and amortization	16,474	31,046
	-----	-----
Total expenses	550,177	590,863
	-----	-----
Net loss from operations	(512,070)	(215,894)
Other income (expense):		
Gain on settlement of accounts payable	57,274	---
Interest income	6,712	523
Interest expense	(37,494)	(6,715)
	-----	-----
Net loss	\$ (485,578)	\$ (222,086)
	=====	=====
Net loss applicable to common stockholders:		
Net loss	\$ (485,578)	\$ (222,086)
Less dividends on Series A		

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

Senior Convertible Preferred Stock	---	(32,634)
	-----	-----
Net loss applicable to common stockholders	\$ (485,578)	\$ (255,720)
	=====	=====
Net loss per common share - Basic and diluted	\$ (0.02)	\$ (0.03)
	=====	=====
Weighted average number of common shares outstanding - basic and diluted	33,793,354	15,273,598
	=====	=====

See accompanying notes to consolidated financial statements.

5

GolfGear International, Inc. and Subsidiaries
Consolidated Statements of Operations (Unaudited)

	Six Months Ended June 30,	
	2002	2001
	-----	-----
Sales	\$ 763,846	\$ 1,311,526
Cost of goods sold	564,222	716,639
	-----	-----
Gross profit	199,624	594,887
	-----	-----
Expenses:		
Selling and marketing	273,458	216,780
Tour and pro contracts	18,666	55,064
Provision for bad debts	22,915	59,711
General and administrative	574,109	583,452
Depreciation and amortization	29,884	55,256
	-----	-----
Total expenses	919,032	970,263
	-----	-----
Net loss from operations	(719,408)	(375,376)
Other income (expense):		
Gain settlement of accounts payable	57,274	---
Interest income	6,712	929
Interest expense	(43,677)	(13,959)
Loss on disposal of assets	(26,769)	---
	-----	-----
Net loss	\$ (725,868)	\$ (388,406)
	=====	=====
Net loss applicable to common stockholders:		
Net loss	\$ (725,868)	\$ (388,406)

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

Less dividends on Series A Senior Convertible Preferred Stock	---	(66,414)
	-----	-----
Net loss applicable to common stockholders	\$ (725,868)	\$ (454,820)
	=====	=====
Net loss per common share - Basic and diluted	\$ (0.03)	\$ (0.03)
	=====	=====
Weighted average number of common shares outstanding - basic and diluted	25,875,571	15,273,598
	=====	=====

See accompanying notes to consolidated financial statements.

6

GolfGear International, Inc. and Subsidiaries
Consolidated Statements of Cash Flows (Unaudited)

	Six Months Ended June 30,	
	2002	2001
	-----	-----
Cash flows from operating activities:		
Net loss	\$ (725,868)	\$ (388,406)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	29,884	55,256
Provision for obsolete inventory	93,680	---
Amortization of financing costs	28,670	---
Provision for bad debts	22,915	59,711
Gain on settlement of accounts payable	(57,274)	---
Fair value of stock options and warrants issued to non-employees	---	46,065
Loss on disposal of assets	26,769	---
Changes in operating assets and liabilities:		
(Increase) decrease in:		
Accounts receivable	11,025	(207,430)
Inventories	(44,449)	362,122
Prepaid expenses	(21,059)	1,917
Deposits	4,630	12,217
Increase (decrease) in:		
Accounts payable and accrued expenses	222,249)	78,437
Accrued product warranties	8,641	10,208
Accrued interest payable	4,850	6,743
Accrued officer's compensation	(20,896)	12,000
	-----	-----
Net cash provided by (used in) operating activities	(864,731)	48,840

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

Cash flows from investing activities:		
Purchase of property and equipment	(22,924)	(90,881)
Infomercial costs	(167,678)	---
Net cash used in investing activities	(190,602)	(90,881)

(continued)

7

GolfGear International, Inc. and Subsidiaries
Consolidated Statements of Cash Flows (Unaudited) (continued)

	Six Months Ended June 30,	
	2002	2001
Cash flows from financing activities:		
Increase (decrease) in notes payable to stockholders	\$ (97,166)	\$20,666
Decrease in bank credit line	(6,031)	(1,182)
Proceeds from sale of convertible debentures	2,040,000	---
Deferred financing costs	(29,934)	---
Proceeds from short-term borrowings	---	40,000
Repayments of short-term borrowings	(35,914)	---
Proceeds from sale of common stock	200,025	---
Net cash provided by (used in) financing activities	2,070,980	65,484
Cash:		
Net increase	1,015,647	23,443
At beginning of period	120,135	39,754
At end of period	1,135,782	\$63,197
Non-cash Transactions:		
Deferred financial costs	\$ (486,120)	---
Settlement of accounts payable	\$ 183,524	---
New note issued	100,000	---
Value of stock issued	26,250	---
Gain on settlement of accounts payable	\$ 57,274	---
Other Cash Information:		
Interest paid	\$ 7,283	---

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

Taxes paid	\$	6,643	---
	=====	=====	=====

See accompanying notes to consolidated financial statements.

8

GolfGear International, Inc. and Subsidiaries
Notes to Consolidated Financial Statements (Unaudited)
Six Months Ended June 30, 2002 and 2001

1. Basis of Presentation

The accompanying consolidated financial statements have been prepared by GolfGear International, Inc. and subsidiaries (collectively, "GolfGear" or the "Company") pursuant to the rules and regulations of the Securities and Exchange Commission (the "SEC") for interim financial reporting. These consolidated financial statements are unaudited and, in the opinion of management, include all adjustments (consisting of normal recurring adjustments and accruals) necessary for a fair presentation of the balance sheets, operating results, and cash flows for the periods presented. Operating results for the three and six months ended June 30, 2002 are not necessarily indicative of the results that may be expected for the fiscal year ending December 31, 2002. Certain financial information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been omitted in accordance with the rules and regulations of the SEC. These consolidated financial statements should be read in conjunction with the audited consolidated financial statements, and accompanying notes, included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2001. The consolidated balance sheet at December 31, 2001 has been derived from the audited consolidated financial statements at that date.

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

9

Organization and Description of Business - The Company designs, develops and markets premium golf clubs and related golf products utilizing its proprietary forged face insert technology.

The golf club industry is highly seasonal, with most companies experiencing up to 60% of their annual sales between February and June, with an additional 20% of their annual sales occurring between October and December for the Christmas buying season.

The Company is attempting to increase revenues through various means, including expanding brands and product offerings, new marketing programs, and the production of an infomercial, which it hopes will air in late November or early December. These types of programs take time to develop and the results of any successful program may not be apparent in the Company's revenues for 2002.

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

The Company has raised \$2,240,025 in new capital, and is currently attempting to raise additional capital but there can be no assurances that the Company will be successful in this regard. To the extent that the Company is unable to secure the capital necessary to fund its future cash requirements on a timely basis and/or under acceptable terms and conditions, the Company may have to reduce its operations to a level consistent with its available working capital resources.

Principles of Consolidation - The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, GearFit Golf Company, Pacific Golf Holdings, Inc., Bel Air - Players Group, Inc. and Leading Edge Acquisition, Inc. All significant intercompany transactions and balances have been eliminated in consolidation.

Loss Per Share - Basic earnings per share are calculated by dividing net loss applicable to common shareholders by the weighted average number of common shares outstanding during the period. Diluted earnings per share reflects the potential dilution that would occur if stock options, and warrants were exercised. These potentially dilutive securities were anti-dilutive for all periods presented, and accordingly, basic and diluted earnings per share are the same for all periods presented. As of June 30, 2002 and 2001, potentially dilutive securities consisted of outstanding stock options and warrants to acquire 3,179,721 shares and 2,622,789 shares of common stock, respectively.

2. Convertible Debentures

On June 6, 2002, GolfGear International, Inc. (the "Company") completed the sale of \$2,000,000 of convertible debentures. The debentures are convertible into common stock at \$0.25 per share for a period of twelve (12) months commencing six (6) months after the initial sale of the debentures. The debentures are secured by the Company's patents. For each share of common stock issued upon conversion of the debentures, one (1) common stock purchase warrant will be issued, which will be exercisable for a period of eighteen (18) months at \$0.10

10

per share. The costs associated with the issuance of the Debentures have been capitalized and are being amortized over the 18 months. If the Debentures convert to equity prior to the 18 month term the unamortized portion will be debited to additional paid in capital. The Company has not recognized any expense for the warrants at this time because the warrants are only issued when and if the debentures convert to stock. At that point the company will treat the value of the warrants as a cost of equity.

Pursuant to the terms of this financing, on June 11, 2002 Wyngate's President, Peter H. Pocklington, was appointed as Chairman of the Board of Directors and Chief Executive Officer. The financing also provides for Wyngate to appoint a majority of the Board of Directors of the Company. To this end Wyngate has only appointed Roger Miller and Dean Rienmuth. With the resignation of Frank Mc Garvey the new appointees is only equal to the current number of sitting board members. Don Anderson, the Company's founder, remained with the Company as President and Chief Operating Officer.

3. Stockholders' Equity

For the three months ended June 30, 2001, 3,541 shares of Series A Senior Convertible Preferred Stock were issued as payment of dividends of \$33,634.

For the six months ended June 30, 2001, 6,992 shares of Series A Senior Convertible Preferred Stock were issued as payment of dividends of \$66,414.

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

During the three months ended June 30, 2002 the Company canceled 5,000 shares issued to a former employee.

During the six months ended June 30, 2002 the Company canceled 105,000 shares issued to a former employee and issued 5,000 shares in consideration for an extension granted on a certain note payable.

On March 23, 2002 the Company entered into an agreement for the sale of 15,000,000 shares of its common stock, for \$1,125,000, at which time \$200,025 was received in cash and \$924,975 in a promissory note with interest at 2.88% per annum. Pursuant to the promissory note, the balance is due and payable October 8, 2003. The promissory note is secured by a stock pledge agreement which pledges 12,333,000 shares of the common stock, which shall be held by the Company as security for payment of the promissory note.

On May 30, 2002, the Company entered into a settlement agreement and mutual general release (the "Settlement Agreement") with MC Corporation. The Settlement Agreement provided that the Company issue a total of 3,000,000 shares of common stock to MC Corporation, of which 2,450,330 shares have already been reflected as issued and outstanding in the Company's financial statements at December 31, 2001 and March 31, 2002. The additional 549,700 shares of common stock are reflected as issued and outstanding in the June 30 2002.

On June 6, 2002 the Company completed the sale of \$2,000,000 of convertible debentures. The debentures are convertible into common stock at \$0.25 per share for a period of twelve (12) months commencing six (6) months after the initial sale of the debentures. As part of this financing, the Company issued 1,072,000 shares of its common stock as a finders fee.

11

Effective June 30, 2002 the Company issued 75,000 shares of common stock as part of accounts payable settlement on a debt of \$183,524. The Company recorded note payable of \$100,000 and a gain of \$57,274. The Stock was valued at the current market price of \$26,250.

4. Segment and Geographic Information;

The Company operates in one business segment. The Company sells to customers in the United States, and the rest of the world. During the three months ended June 30, 2002, sales to customers in the United States, and the rest of the world were \$391,137, and \$13,724, respectively. During the three months ended June 30, 2001, sales to customers in the United States, and the rest of the world were \$712,303, and \$28,177 respectively.

During the six months ended June 30, 2002, sales to customers in the United States, and the rest of the world were \$689,719, and \$74,127, respectively. During the six months ended June 30, 2001, sales to customers in the United States, and the rest of the world were \$1,000,163, and \$311,363 respectively.

5. Inventories

At June 30, 2002 and December 31, 2001, inventories consist of the following:

	2002	2001
	-----	-----
Components parts	\$334,823	\$482,024
Finished goods	352,874	254,905
	-----	-----

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

	687,697	736,929
Reserve for obsolescence	(45,664)	(45,664)
	-----	-----
	\$642,033	\$691,265
	=====	=====

6. Legal Proceedings

On November 17, 2001, MC Corporation, a Japanese corporation, filed an action against the Company in the United States District Court, Central District of California. MC Corporation had purchased 210,526 shares of Series A Senior Convertible Preferred Stock in October 1999 for \$2,000,000 which, combined with the 34,504 shares of preferred stock received as dividends and pursuant to an anti-dilution provision, automatically converted into 2,450,300 shares of common stock in October 2001 pursuant to a subscription agreement dated September 1, 1999 (the "Subscription Agreement"). MC Corporation contended that it was entitled to approximately an additional 8,500,000 shares of common stock based on its interpretation of the reset provision contained in the Subscription Agreement. The Company filed a cross-complaint against MC Corporation for reformation of the Subscription Agreement to conform it to the mutual understanding of the parties at the time it was executed.

12

MC Corporation had also been the exclusive distributor of the Company's products in Japan since September 1999. Effective March 5, 2002, the Company terminated its distribution agreement with MC Corporation as a result of MC Corporation's failure to comply with the terms of the distribution agreement.

On May 30, 2002, the Company entered into a settlement agreement and mutual general release (the "Settlement Agreement") with MC Corporation, John Kura and Keizaikai USA, Inc. (hereinafter collectively referred to as the "MC Corporation parties"). The Settlement Agreement provides that the Company issue a total of 3,000,000 shares of common stock to MC Corporation, consisting of 2,450,300 shares of common stock for the conversion at (the specified ten to one conversion rate) of 245,030 shares of convertible preferred stock previously issued to MC Corporation, and an additional 549,700 shares of common stock for other consideration. The 2,450,330 shares have already been reflected as issued and outstanding in the Company's financial statements at December 31, 2001 and March 31, 2002. The additional 549,700 shares of common stock are reflected as issued and outstanding in the June 30 2002. The Company was given the right of first refusal to repurchase any shares of common stock owned by MC Corporation it may desire to sell in a private transaction for a period of eighteen (18) months from the date of execution of the Settlement Agreement. All stock options and warrants owned by the MC Corporation parties were cancelled and MC Corporation's anti-dilution rights arising under the Settlement Agreement were terminated. The Settlement Agreement also provides that MC Corporation's representative on the Company's Board of Directors will resign, and the Company's distribution agreement with MC Corporation was formally terminated.

The MC Corporation parties agreed to restrict the sale of their shares of common stock in a public transaction for a period of eighteen (18) months as follows: no sale of shares shall be made during the first six (6) months; during the second six (6) months, the MC Corporation parties agreed to sell no more than fifty percent (50%) of the limitation on volume restrictions contained in Rule 144(e) of the Securities Act of 1933, as amended; during the third six (6) month period, all sales must be made in compliance with the volume limitations contained in Rule 144(e).

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

Cautionary Statement Pursuant to Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995:

This Quarterly Report on Form 10-QSB for the quarterly period ended June 30, 2002 contains "forward-looking" statements within the meaning of Section 27A of the Securities Act of 1933, as amended, including statements that include the words "believes", "expects", "anticipates", or similar expressions. These forward-looking statements include, among others, statements concerning the Company's expectations regarding its working capital requirements, gross margin, results of operations, business, growth prospects, competition and other

13

statements of expectations, beliefs, future plans and strategies, anticipated events or trends, and similar expressions concerning matters that are not historical facts. The forward-looking statements included in this Quarterly Report on Form 10-QSB for the quarterly period ended June 30, 2002 involve known and unknown risks, uncertainties and other factors that could cause the actual results, performance or achievements of the Company to differ materially from those expressed in or implied by the forward-looking statements contained herein.

Overview:

The Company designs, develops and markets premium golf clubs and related golf products. The Company utilizes its proprietary forged face insert technology to offer a full line of golf equipment. The Company's patent portfolio with respect to insert technology is the largest and most comprehensive in the golf industry, with nine domestic and foreign patents issued related to forged face insert technology. These patents incorporate a wide variety of forged face insert materials, including titanium, beryllium copper, stainless steel, carbon steel, aluminum, and related alloys thereof, and include technology relating to varying the face thickness of the insert.

The Company operates in one business segment. The Company sells to customers in the United States, the Far East and Europe.

The golf club industry is highly seasonal, with most companies experiencing up to 60% of their annual sales between February and June, with an additional 20% of their annual sales occurring between October and December for the Christmas buying season.

The consolidated financial statements include the accounts of the Company and its direct and indirect wholly-owned subsidiaries, Gear Fit Golf Company, Pacific Golf Holdings, Inc., Bel Air-Players Group, Inc. and Leading Edge Acquisition, Inc. All significant inter-company transactions and balances have been eliminated in consolidation.

The Company is attempting to increase revenues through various means, including expanding brands and product offerings, new marketing programs, and the production of an infomercial, which it hopes will air in late November or early December. These types of programs take time to develop and the results of any successful program may not be apparent in the Company's revenues for 2002.

The Company has raised \$2,240,025 in new capital, and is currently attempting to raise additional capital but there can be no assurances that the Company will be successful in this regard. To the extent that the Company is unable to secure the capital necessary to fund its future cash requirements on a timely basis and/or under acceptable terms and conditions, the Company may have to

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

substantially reduce its operations to a level consistent with its available working capital resources.

Results of Operations

Three Months ended June 30, 2002 and 2001 -

14

Net sales decreased to \$386,066 in 2002 from \$740,480 in 2001, a decrease of \$354,414 or 47.9%. The Company's sales in the second and third quarter are generally re-orders. The lack of working capital in the first quarter delayed the production of inventory resulting in the loss of the initial sell-in. These initially lost sales result in the loss of re-orders significantly affecting the Company's second quarter sales. The Company also believes that the decline in sales to its major customers has been caused by the general economic slowdown and the softness in the equipment industry.

Gross profit decreased to \$38,107 in 2002 from \$374,969 in 2001, and decreased as a percentage of net sales to 9.9% in 2002 from 50.6% in 2001. The gross profit would have been \$169,483 or 43.9% if it had not been for several factors including a 10% increase in freight-in expense a result of the lack of working capital and the Company's inability to take advantage of greater lead times. The Company also chose to write-down older inventory - a total of \$93,681 or 24% of the gross profit. This was done in anticipation of the introduction of new product preventing the Company from recovering its cost on the older inventory.

Selling and marketing expenses increased to \$160,119 in 2002 (41.5% of sales) from \$132,167 in 2001 (17.8% of sales), an increase of \$27,952 or 21.1%. Selling and marketing expenses increased in 2002 as compared to 2001 as a result of the Company's continued efforts to increase sales in 2002.

Tour and pro contract expenses decreased to \$9,795 in 2002 (2.5% of sales) from \$25,156 in 2001 (3.4% of sales), a decrease of \$15,361 or 61.1%. Tour and pro contract expenses decreased in 2002 as compared to 2001 as previous obligations have expired and have not been renewed.

General and administrative expenses increased to \$352,207 in 2002 (91.2% of sales) from \$344,717 in 2001 (46.6% of sales), an increase of \$7,490 (2.2%).

Depreciation and amortization decreased to \$16,474 in 2002 from \$31,046 in 2001, a decrease of \$14,572 or 46.9%. The decrease is a result of the write off of Goodwill and certain other tangible assets at December 31, 2001.

Interest expense increased to \$37,494 in 2002 from \$6,715 in 2001, an increase of \$30,779. Interest expense increased in 2002 as compared to 2001 due to the sale of the convertible debenture. The debenture bears interest at seven percent (7%). The sales of the debenture resulted in \$487,348 in capitalized financing costs. These costs are being amortized over the 18-month life of the debenture.

Bad debt expense decreased to \$11,582 in 2002 from \$57,777 in 2001, a decrease of \$46,195. The allowance in 2002 is being calculated at 3% of sales where as in 2001 specific accounts were being reserved for.

Net loss was \$485,578 for the three months ended June 30, 2002, as compared to a net loss of \$222,086 for the three months ended June 30, 2001. An increased loss of \$263,492 or 118.6%. The main factor in the increased loss was the decrease in sales.

Net Loss Applicable to Common Stockholders. During the three months ended June

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

30, 2001, the Company recorded preferred stock dividends of \$32,634, which were reflected as a return to the preferred stockholder and as an increase in the loss to common stockholders. The Company did not have preferred stock in 2002.

15

Six Months ended June 30, 2002 and 2001 -

Net sales decreased to \$763,846 in 2002 from \$1,311,526 in 2001, a decrease of \$547,680 or 41.8%. The Company's sales in the second and third quarter are generally re-orders. The lack of working capital in the first quarter delayed the production of inventory resulting in the loss of the initial sell-in. These initially lost sales resulted in the loss of re-orders significantly affecting the Company's second quarter sales. In 2001 the Company sold \$243,915 in Japan but had no sales there in 2002. The Company terminated its distribution agreement with MC Corporation as a result of MC Corporation's failure to comply with the terms of the distribution agreement. Additionally the Company believes that the decline in sales to its major customers is a result of the general economic slowdown and the softness in the equipment industry.

Gross profit decreased to \$199,624 in 2002 from \$594,887 in 2001, but decreased as a percentage of net sales to 26.1% in 2002 from 45.4% in 2001. The gross profit would have been \$330,524 or 43.3% if it had not been for several factors including a 10% increase in freight-in expense a result of the lack of working capital and the Company's inability to take advantage of greater lead times. The Company also chose to write-down older inventory - a total of \$93,681 or 12% of the gross profit. This was done in anticipation of the introduction of new product preventing the Company from recovering its cost on the older inventory.

Selling and marketing expenses increased to \$273,458 in 2002 (35.8% of sales) from \$216,780 in 2001 (16.5% of sales), an increase of \$56,678 or 26.1%. Selling and marketing expenses increased in 2002 as compared to 2001 as a result of the Company's continued efforts to increase sales in 2002.

Tour and pro contract expenses decreased to \$18,666 in 2002 (2.4% of sales) from \$55,064 in 2001 (2.4% of sales), a decrease of \$36,398 or 66.1%. Tour and pro contract expenses decreased in 2002 as compared to 2001 as previous obligations have expired and have not been renewed.

General and administrative expenses decreased to \$574,109 in 2002 (75.2% of sales) from \$583,452 in 2001 (44.5% of sales), a decrease of \$9,343 (1.6%).

Depreciation and amortization decreased to \$29,884 in 2002 from \$55,256 in 2001, a decrease of \$25,372 or 45.9%. The decrease is a result of the write off of Goodwill and certain other tangible assets at December 31, 2001.

Interest expense increased to \$43,677 in 2002 from \$13,959 in 2001, an increase of \$29,718. Interest expense increased in 2002 as compared to 2001 due to the sale of the convertible debenture. The debenture bears interest at seven percent (7%). The sales of the debenture resulted in \$487,348 in capitalized financing costs. These costs are being amortized over the 18-month life of the debenture.

16

Bad debt expense decreased to \$22,915 in 2002 from \$59,711 in 2001, an decrease of \$36,796. The allowance in 2002 is being calculated at 3% of sales where as in 2001 specific accounts were being reserved for.

Net loss was \$725,868 for the six months ended June 30, 2002, as compared to a

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

net loss of \$388,406 for the six months ended June 30, 2001. An increased loss of \$337,462 or 86.9%. This increase was result of the decrease in sales, increased expenses and the write-down of selected inventory.

Net Loss Applicable to Common Stockholders. During the three months ended June 30, 2001, the Company recorded preferred stock dividends of \$66,414, which were reflected as a return to the preferred stockholder and as an increase in the loss to common stockholders. The Company did not have preferred stock in 2002.

Liquidity and Capital Resources - June 30, 2002:

The Company has financed its working capital requirements during the past few years principally from the private placement of its securities. Such funds have periodically been supplemented with short-term borrowings under the Company's bank line of credit and other private sources. The bank line of credit is unsecured, has a maximum borrowing level of \$70,000, and is personally guaranteed by the President of the Company.

Operating Activities. The Company's operations utilized cash of \$864,731 during the six months ended June 30, 2002, as compared to cash of \$48,840 provided by the six months ended June 30, 2001. The increase in cash utilized in operating activities in 2002 as compared to 2001 was primarily a result of a much greater loss. At June 30, 2002, cash had increased by \$1,015,647, to \$1,135,782, as compared to \$120,135 at December 31, 2001. The Company had working capital of \$969,653 at June 30, 2002, as compared to working capital deficit of \$390,171 at December 31, 2001, reflecting current ratios of 1.84:1 and 0.75:1 at June 30, 2002 and December 31, 2001, respectively.

Investing Activities. During the six months ended June 30, 2002 and 2001, net cash used in investing activities was \$190,602 and \$90,881, respectively. During the six months ended June 30, 2002 the Company invested \$167,678 in the production of an infomercial. The Company also invested \$22,924 in other fixed assets. During the six months ended 2001 the Company invested \$90,881 in fixed assets.

Financing Activities. During the six months ended June 30, 2002, the Company repaid certain shareholders and directors \$97,166. During the six months ended June 30, 2001, the Company borrowed \$26,164 net of payments on short-term notes from its shareholders and directors. During the six months ended June 30, 2002 and 2001, the Company reduced its bank line of credit by \$6,031 and \$1,182, respectively.

During the six months ended June 30, 2002, The Company sold \$2,040,000 in the form of a convertible debenture. The debentures are convertible into common stock at \$0.25 per share for a period of twelve (12) months commencing six (6) months after the initial sale of the debentures. The debentures are secured by the Company's patents. For each share of common stock issued upon conversion of the debentures, one (1) common stock purchase warrant will be issued, which will be exercisable for a period of eighteen (18) months at \$0.10 per share. The costs associated with the issuance of the Debentures have been capitalized and are being amortized over the 18 months. If the Debentures convert to equity prior to the 18 month term the unamortized portion will be debited to additional paid in capital.

Pursuant to the terms of this financing, on June 11, 2002 Wyngate's President, Peter H. Pocklington, was appointed as Chairman of the Board of Directors and Chief Executive Officer. The financing also provides for Wyngate to appoint a majority of the Board of Directors of the Company. To this end Wyngate has only appointed Roger Miller and Dean Rienmuth. With the resignation of Frank Mc

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

Garvey the new appointees is only equal to the current number of sitting board members. Don Anderson, the Company's founder, remained with the Company as President and Chief Operating Officer.

During the six months ended June 30, 2001 the Company borrowed \$40,000 under a short-term note from a related party. During the six months ended June 30, 2002, the Company repaid \$35,914 of short-term notes to unrelated parties.

On April 8, 2002, the Company entered into a stock purchase agreement (the "Agreement") with Wyngate Limited, a Jersey Limited Company ("Wyngate"), whereby Wyngate agreed to purchase 15,000,000 shares of the Company's common stock at \$0.075 per share for an aggregate purchase price of \$1,125,000. Of the purchase price, \$200,025 was paid upon execution of the Agreement and Wyngate executed a promissory note with interest at 2.88% per annum in favor of the Company for the balance of \$924,975. Pursuant to the promissory note, the balance is due and payable October 8, 2003. The promissory note is secured pursuant to a stock pledge agreement which pledges 12,333,000 shares of the common stock, which shall be held by the Company as security for payment of the promissory note.

Funds from this transaction will be used for working capital, sales and marketing, tour promotion, inventory purchases, accounts payable, patent development and general operating expenses.

On June 6, 2002, GolfGear International, Inc. (the "Company") completed the sale of \$2,000,000 of convertible debentures. The debentures are convertible into common stock at \$0.25 per share for a period of twelve (12) months commencing six (6) months after the initial sale of the debentures. The Company may sell up to an additional \$2,000,000 of convertible debentures in the near future. As part of this financing, the Company issued 532,000 shares of its common stock as a finders fee.

Critical Accounting Policies

Our financial statements are prepared in accordance with accounting principles generally accepted in the United States, which require management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements, the disclosure of contingent assets and liabilities, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. We believe the following critical accounting policies affect our more significant estimates and assumptions used in the preparation of our financial statements. Our significant estimates and assumptions are reviewed and any required adjustments are recorded on a quarterly basis.

18

The Company has an infomercial in production. The costs associated with the infomercial are being capitalized and will be amortized over the estimated useful life of the Infomercial.

The Company has obtained \$2,040,000 financing through a convertible debentures (Debentures). The costs associated with the issuance of the Debentures have been capitalized and are being amortized over the 18 months. If the Debentures convert to equity prior to the 18 month term the unamortized portion will be debited to additional paid in capital.

New Accounting Pronouncements:

In June 2001, the FASB issued SFAS No. 142, "Goodwill and Other Intangible Assets", which is effective January 1, 2002. SFAS No. 142 requires, among other

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

things, the discontinuance of goodwill amortization. In addition, SFAS No. 142 includes provisions for the reclassification of certain existing recognized intangibles as goodwill, reassessment of the useful lives of the existing recognized intangibles, reclassification of certain intangibles out of previously reported goodwill and the identification of reporting units for purposes of assessing potential future impairments of goodwill. SFAS No. 142 also requires the Company to complete a transitional goodwill impairment test six months from the date of adoption. The Company adopted SFAS No. 142 in December of 2001. It did not have any effect, its financial statement presentation or disclosures for this period.

In August 2001, the FASB issued SFAS No. 143, "Accounting for Asset Retirement Obligations". SFAS No. 143 addresses the diverse accounting practices for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. The Company will be required to adopt SFAS No. 143 effective January 1, 2003. The Company is reviewing SFAS No. 143 to determine what effect, if any, it will have on its financial statement presentation or disclosures. There was no effect on the financial statements or disclosures for this period.

In August 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets", which is effective January 1, 2002. SFAS No. 144 supersedes SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of", and a portion of APB Opinion No. 30, "Reporting the Results of Operations". SFAS No. 144 provides a single accounting model for long-lived assets to be disposed of and significantly changes the criteria that would have to be met to classify an asset as held-for-sale. Classification as held-for-sale is an important distinction since such assets are not depreciated and are stated at the lower of fair value or carrying amount. SFAS No. 144 also requires expected future operating losses from discontinued operations to be displayed in the period(s) in which the losses are incurred, rather than as of the measurement date as presently required. The Company does not anticipate that the adoption of SFAS No. 144 will have a material effect on the Company's financial statement presentation or disclosures.

19

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

On November 17, 2001, MC Corporation, a Japanese corporation, filed an action against the Company in the United States District Court, Central District of California. MC Corporation had purchased 210,526 shares of Series A Senior Convertible Preferred Stock in October 1999 for \$2,000,000 which, combined with the 34,504 shares of preferred stock received as dividends and pursuant to an anti-dilution provision, automatically converted into 2,450,300 shares of common stock in October 2001 pursuant to a subscription agreement dated September 1, 1999 (the "Subscription Agreement"). MC Corporation contended that it was entitled to approximately an additional 8,500,000 shares of common stock based on its interpretation of the reset provision contained in the Subscription Agreement. The Company filed a cross-complaint against MC Corporation for reformation of the Subscription Agreement to conform it to the mutual understanding of the parties at the time it was executed.

MC Corporation had also been the exclusive distributor of the Company's products in Japan since September 1999. Effective March 5, 2002, the Company terminated its distribution agreement with MC Corporation as a result of MC Corporation's failure to comply with the terms of the distribution agreement.

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

On May 30, 2002, the Company entered into a settlement agreement and mutual general release (the "Settlement Agreement") with MC Corporation, John Kura and Keizaikai USA, Inc. (hereinafter collectively referred to as the "MC Corporation parties"). The Settlement Agreement provides that the Company issue a total of 3,000,000 shares of common stock to MC Corporation, consisting of 2,450,300 shares of common stock for the conversion at (the specified ten to one conversion rate) of 245,030 shares of convertible preferred stock previously issued to MC Corporation, and an additional 549,700 shares of common stock for other consideration. The 2,450,330 shares have already been reflected as issued and outstanding in the Company's financial statements at December 31, 2001 and March 31, 2002. The additional 549,700 shares of common stock are reflected as issued and outstanding in the June 30 2002. The Company was given the right of first refusal to repurchase any shares of common stock owned by MC Corporation it may desire to sell in a private transaction for a period of eighteen (18) months from the date of execution of the Settlement Agreement. All stock options and warrants owned by the MC Corporation parties were cancelled and MC Corporation's anti-dilution rights arising under the Settlement Agreement were terminated. The Settlement Agreement also provides that MC Corporation's representative on the Company's Board of Directors will resign, and the Company's distribution agreement with MC Corporation was formally terminated.

20

The MC Corporation parties agreed to restrict the sale of their shares of common stock in a public transaction for a period of eighteen (18) months as follows: no sale of shares shall be made during the first six (6) months; during the second six (6) months, the MC Corporation parties agreed to sell no more than fifty percent (50%) of the limitation on volume restrictions contained in Rule 144(e) of the Securities Act of 1933, as amended; during the third six (6) month period, all sales must be made in compliance with the volume limitations contained in Rule 144(e).

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS

(c) Recent sales of unregistered securities

During the six months ended June 30, 2002 the Company canceled 105,000 and issued 16,702 shares of its common stock. The 105,000 shares had been granted to but never issued to former employees. 15,000,000 shares of common stock was sold and issued to Wyngate Limited - details found else where in this document. In connection with that sale of stock 1,072,000 shares were issued as a finders fee. 550,000 shares of stock have been issued to MC Corporation as part of a settlement agreement - see legal proceedings. Effective June 30, 2002 75,000 shares were issued as part of a settlement of a certain debt and 5,000 shares in consideration for the extension granted on a certain note payable.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits:

- 3.1 Articles of Incorporation(1)
- 3.2 Certificate of Amendment of Articles of Incorporation(1)
- 3.3 Certificate of Amendment of Articles of Incorporation(1)
- 3.4 Articles of Merger(1)
- 3.5 Bylaws(1)
- 4.3 Binding Subscription Agreement for Purchase of Equity Securities (M.C. Corporation) (1)
- 4.4 Certificate of Determination(1)
- 10.1 Distribution Agreement (M.C. Corporation) (1)

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

- 10.2 Distribution Agreement (GolfGear Korea, Ltd.)(1)
- 10.6 License Agreement (Wilson Sporting Goods Company)(1)
- 10.10 Employment Agreement (Donald A. Anderson)(1)(C)
- 10.11 GolfGear International, Inc. 1997 Stock Incent Plan(1)(C)
- 10.12 License Agreement (PowerBilt Golf)(1)
- 10.13 Property Lease Agreement(2)
- 10.14 Amended and Restated Agreement for Sale and Purchase of Assets between Bel Air Golf Company and GolfGear International, Inc.(2)
- 10.15 Agreement for Sale and Purchase of Assets - Leading Edge(3)
- 10.16 Personal Services Agreement - Peter Alliss(3)
- 10.17 Exclusive Distribution Agreement (4)

20

- 10.18 Subscription Agreement dated March 7, 2002(5)
- 10.19 Stock Purchase Agreement dated April 8, 2002(5)
- 10.20 Promissory Note dated April 8, 2002(5)
- 10.21 Stock Pledge Agreement dated April 8, 2002(5)
- 21 Subsidiaries of the Registrant(1)
- 99.1 Patents(1)
- 99.2 Trademarks (1)
- 99.3 Certification pursuant to 18 U.S.C Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002(contained within this document)

(b) Reports on Form 8-K - Six Months Ended June 30, 2002:

On April 8, 2002, GolfGear International, Inc. (the "Company") entered into a stock purchase agreement with Wyngate Limited, a Jersey Limited Company ("Wyngate"), whereby Wyngate agreed to purchase 15,000,000 shares of the Company's common stock.

On May 30, 2002, the Company entered into a settlement agreement and mutual general release (the "Settlement Agreement") with MC Corporation, John Kura and Keizaikai USA, Inc. (hereinafter collectively referred to as the "MC Corporation parties").

On June 6, 2002, GolfGear International, Inc. (the "Company") completed the sale of \$2,000,000 of convertible debentures. The debentures are convertible into common stock at \$0.25 per share for a period of twelve (12) months commencing six (6) months after the initial sale of the debentures. The debentures are secured by the Company's patents. For each share of common stock issued upon conversion of the debentures, one (1) common stock purchase warrant will be issued, which will be exercisable for a period of eighteen (18) months at \$0.10 per share.

21

SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

GOLFGEAR INTERNATIONAL, INC.

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

(Registrant)

Date: August 19, 2002 By: /s/ PETER H. POCKLINTON

PETER H. POCKLINGTON
Chief Executive Officer
(Duly Authorized Officer)

Date: August 19, 2002 By: /s/DANIEL C. WRIGHT

DANIEL C. WRIGHT
Chief Financial Officer
(Principal Financial Officer)