Genius Brands International, Inc.
Form 10-Q
May 15, 2013

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2013

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

For the transition period from ___________ to ___________

Commission file number: 000-54389

GENIUS BRANDS INTERNATIONAL, INC.

(Exact name of registrant as specified in its charter)

Nevada	**20-4118216**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
3111 Camino del Rio North, Suite 400 San Diego, California	**92108**
(Address of principal executive offices)	(Zip Code)

(858) 450-2900

(Registrant's telephone number, including area code)

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

Large accelerated filer	¨	Accelerated filer	¨
Non-accelerated filer (Do not check if a smaller reporting company)	¨	Smaller reporting company	x

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 72,383,205 shares of common stock, par value $0.001, were outstanding as of May 15, 2013.

GENIUS BRANDS INTERNATIONAL, INC.

FORM 10-Q

For the Quarterly Period Ended March 31, 2013

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PART I — FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited).

Genius Brands International, Inc.

Balance Sheets

March 31, 2013 (unaudited) and December 31, 2012 (audited)

ASSETS	3/31/2013	12/31/2012
Current Assets:		
Cash	$179,835	$447,548
Accounts Receivable, net	557,332	1,084,233
Inventory	344,946	326,072
Prepaid and Other Assets	110,458	139,983
Total Current Assets	1,192,571	1,997,836
Property and Equipment, net	21,141	23,736
Capitalized Product Development in Process	320,306	246,617
Intangible Assets, net	319,493	356,070
Debenture Issuance Costs	159,623	191,762
Total Assets	$2,013,134	$2,816,021
LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)		
Current Liabilities:		
Accounts Payable	$883,423	$971,097
Accrued Expenses	349,420	496,662
Accrued Salaries and Wages	614,991	516,083
Accrued Interest - Debentures	45,716	45,716
Derivative Liability	161,824	68,962
Notes Payable - short term portion	250,000	–
Total Current Liabilities	2,305,374	2,098,520
Long Term Liabilities:		
Notes Payable (Net of Discount of $404,025 and $485,147, respectively)	345,975	514,853
Notes Payable and Accrued Interest – Related Parties	454,614	447,891
Total Liabilities	3,105,963	3,061,264
Stockholders' Equity (Deficit)		

Common Stock, $0.001 par value, 250,000,000 shares authorized; 72,383,205 and 71,912,617 shares issued and outstanding, respectively	72,383	71,913
Additional Paid in Capital	9,988,677	9,890,868
Accumulated Deficit	(11,153,889)	(10,208,024)
Total Genius Brands International, Inc. Stockholders' Equity (Deficit)	(1,092,829)	(245,243)
Total Liabilities & Stockholders' Equity (Deficit)	$2,013,134	$2,816,021

See accompanying notes to consolidated financial statements

Genius Brands International, Inc.

Statements of Operations

Periods Ending March 31, 2013 and 2012 (unaudited)

	3/31/2013	3/31/2012
Revenues:		
Product Sales	$702,812	$1,001,251
Licensing & Royalties	31,427	29,696
Total Revenues	734,239	1,030,947
Cost of Sales (Excluding Depreciation)	647,309	734,131
Gross Profit	86,930	296,816
Operating Expenses:		
Product Development	26,991	5,680
Professional Services	64,506	73,875
Rent Expense	6,947	9,432
Marketing & Sales	54,719	189,557
Depreciation & Amortization	39,172	38,715
Salaries and Related Expenses	471,147	409,364
Stock Compensation Expense	58,279	61,960
Other General & Administrative	56,205	75,404
Total Operating Expenses	777,966	863,987
Loss from Operations	(691,036)	(567,171)
Other Income (Expense):		
Other Income	16	85
Interest Expense	(155,259)	(1,160)
Interest Expense – Related Parties	(6,724)	(32,055)
Gain (loss) on derivative valuation	(92,862)	–
Net Other Income (Expense)	(254,829)	(33,130)
Loss before Income Tax Expense and Noncontrolling Interest	(945,865)	(600,301)
Income Tax Expense	–	–
Net Loss	(945,865)	(600,301)
Net Loss attributable to Noncontrolling Interest	–	(5,366)
Net Loss attributable to Genius Brands International, Inc.	$(945,865)	$(605,667)

Net Loss per common share	$(0.01)	$(0.01)
Weighted average shares outstanding	72,215,885	60,698,815

See accompanying notes to consolidated financial statements

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Genius Brands International, Inc.

Statements of Stockholders' Equity (Deficit)

	Common Stock		Additional	Noncontrolling	Accumulated	
	Shares	Amount	Paid in Capital	Interest	Deficit	Total
Balance, December 31, 2011 (audited)	60,698,815	$60,699	$6,959,083	$ (5,366)	$(8,135,049)	$(1,120,633)
Common Stock Issued for Cash	1,000,000	1,000	199,000	–	–	200,000
Common Stock Issued for Services	1,486,070	1,486	323,228	–	–	324,714
Common Stock Issued in exchange for repayment of Note Payable	8,727,732	8,728	1,736,818	–	–	1,745,546
Warrants Granted for Debenture Issuance Costs	–	–	28,929	–	–	28,929
Warrants Granted for Debt Discount	–	–	379,688	–	–	379,688
Stock Compensation Expense	–	–	264,122	–	–	264,122
Acquisition of Noncontrolling Interest	–	–	–	5,366	(5,366)	–
Net Loss	–	–	–	–	(2,067,609)	(2,067,609)
Balance, December 31, 2012 (audited)	71,912,617	$71,913	$9,890,868	$ –	$(10,208,024)	$(245,243)
Common Stock Issued for Interest	470,588	470	39,530	–	–	40,000
Stock Compensation Expense			58,279			58,279
Net Loss					(945,865)	(945,865)
Balance, March 31, 2013 (unaudited)	72,383,205	$72,383	$9,988,677	$ –	$(11,153,889)	$(1,092,829)

See accompanying notes to financial statements

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Genius Brands International, Inc.

Statements of Cash Flows (unaudited)

Cash Flows from Operating Activities:	**3/31/2013**	**3/31/2012**
Net Loss	$(945,865)	$(600,301)
Adjustments to reconcile net loss to net cash provided in operating activities:		
Depreciation Expense	2,595	3,070
Amortization Expense	36,577	35,645
Issuance of Common Stock for Interest	40,000	–
Accretion of Discount on Convertible Debenture	81,121	–
Stock Compensation Expense	58,279	61,960
Gain on Derivative Valuation	92,862	–
Decrease (increase) in operating assets:		
Accounts Receivable	526,901	338,922
Inventory	(18,874)	69,895
Prepaid Expenses & Other Assets	29,525	(22,682)
Increase (decrease) in operating liabilities:		
Accounts Payable	(87,674)	(2,617)
Accrued Salaries	98,908	123,237
Accrued Interest – Related Party	6,724	32,055
Other Accrued Expenses	(147,242)	12,017
Net cash provided/(used) in operating activities	(226,163)	51,201
Cash Flows from Investing Activities:		
Investment in Intangible Assets	(73,689)	(27,771)
Net cash provided/(used) by investing activities	(73,689)	(27,771)
Cash Flows from Financing Activities:		
Issuance Costs on Debenture	32,139	–
Net cash provided/(used) by financing activities	32,139	–
Net increase/(decrease) in cash	(267,713)	23,430
Beginning Cash Balance	447,548	405,341
Ending Cash Balance	$179,835	$428,771
Supplemental disclosures of cash flow information:		
Cash paid for income taxes	$–	$–
Cash paid for interest	$–	$1,160
Schedule of non-cash financing and investing activities:		

Related Party Note converted to Common Stock	$–	$1,745,546

See accompanying notes to financial statements

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Genius Brands International, Inc.

Notes to Financial Statements

March 31, 2013 (unaudited)

Note 1: The Company and Significant Accounting Policies

Organization and Nature of Business

Genius Brands International, Inc. (“we”, “us”, “our” or the “Company”), *f/k/a* Pacific Entertainment Corporation, creates and distributes music-based products which we believe are entertaining, educational and beneficial to the well-being of infants and young children under our brands, including Baby Genius. We create, market and sell children’s videos, music, books and other products in the United States by distribution at wholesale to retail stores and distributors, direct to consumers through various “deal for a day” sites and through digital platforms using intellectual property developed and owned by us. We license the use of our intellectual property, both domestically and internationally, to others to manufacture, market and sell products based on our characters and brand, whereby we receive advances and royalties. The Company also obtains rights to the content of other studios for distribution through our warehouse facility to our customers, for which we either pay royalty fees or earn distribution fees. We have licensing agreements with other companies under which we produce music-based products using their characters and brands and for which we pay a royalty.

The Company commenced operations in January 2006, assuming all of the rights and obligations of its Chief Executive Officer, Klaus Moeller, under an Asset Purchase Agreement between the Company and Genius Products, Inc., in which we obtained all rights, copyrights, and trademarks to the brands “Baby Genius,” “Little Genius,” “Kid Genius,” “123 Favorite Music” and “Wee Worship,” and all then existing productions under those titles. On October 17, 2011 and October 18, 2011, Genius Brands International, Inc., filed Articles of Merger with the Secretary of State of the State of Nevada and with the Secretary of State of the State of California, respectively. As previously described on the Company’s Schedule 14C Information Statement, filed with the Securities and Exchange Commission on September 21, 2011, by filing the Articles of Merger, the Company (i) changed its domicile to Nevada from California, and (ii) changed its name to Genius Brands International, Inc. from Pacific Entertainment Corporation (the “Reincorporation”). Pursuant to the Articles of Merger, Pacific Entertainment Corporation, a California corporation, merged into Genius Brands International, Inc., a Nevada corporation that, prior to the Reincorporation, was the wholly owned subsidiary of Pacific Entertainment Corporation. Genius Brands International, the Nevada corporation, is the surviving corporation. In connection with the Reincorporation, on October 12, 2011, the Company filed an Issuer Company-Related Action Notification Form with the Financial Industry Regulatory Authority (“FINRA”) and on November 29, 2011 our trading symbol changed from “PENT” to “GNUS”.

On January 11, 2011, the Company signed a five-year, world-wide license agreement with Tollytots® for a new toy line to be distributed world-wide. As a result of the agreement, Tollytots® immediately began development on a comprehensive line of musical and early learning toys, incorporating the music, characters and themes associated with our *Baby Genius* series of videos and music CDs. The toy line covers a broad range of exclusive categories including learning and developmental toys, most plush toys, and musical toys which Tollytots® has the sole right to manufacture, market and distribute on a world-wide basis. It also allows Tollytots® a non-exclusive right to manufacture, market and distribute products in several non-exclusive categories, including board games, puzzles, electronic learning aids and amusement plush toys, where we may already have other licenses who produce similar products or may grant licenses for such products to new parties in addition to Tollytots®. We have received recoupable advances and will receive quarterly royalty payments in excess of the advances, if applicable, from sales of products developed under the agreement by Tollytots®. The Company will have rights to sell product developed under the license agreement directly via its website subject to availability of inventory from Tollytots®. The agreement provides for certain guaranteed minimum payments to the Company for each contract year. The agreement is subject to early termination by the Company in specified territories in the event minimum sales requirements in those territories have not been met in any contract year. Currently, Tollytots® has several toys developed for the line, including musical and early learning toys, and the toys were available for retail sales beginning in the third quarter of 2012. The new toy line has not produce additional royalty revenue subsequent to its launch at retail in the third quarter of 2012 in excess of the guaranteed minimum payments and there is no guarantee that it will produce additional revenue in the future.

The Company also obtains licenses for other select brands we feel we can market and sell through our distribution channels.

On September 20, 2010, the Company entered into a joint venture agreement with Dr. Shulamit Ritblatt to form Circle of Education, LLC ("COE"), a California limited liability company, for the purpose of creation and distribution of a curriculum to promote school readiness for children ages 2-5 years. The Company actively participated in a research study into the use of music-based curriculum through a major university for three years based on certain unregistered copyrights and trademarks, confidential information, designs, ideas, discoveries, inventions, processes, research results and work product it had developed. In March 2012, the Company and Dr. Ritblatt agreed to terminate the joint venture agreement. COE transferred equal right of ownership in the intellectual property developed as of the date of termination ("IP") to each of the Company and Dr. Ritblatt, and in exchange for the rights to the IP, Dr. Ritblatt transferred her units of COE to the Company. Each party will have the right to continue development of the IP and products based on the IP with no further obligation to the other party. Subject to certain limitations for specific channels of distribution reserved for each party for a period of twelve months from the execution of the agreements, both parties have non-exclusive and non-restrictive rights to the use, sublicense or sale of the IP and products created based on the IP.

The Company has developed the Ready!Play!Learn!™ program based partially on the intellectual property discussed above, which we anticipate will be available for distribution in the second quarter of 2013. The program includes a curriculum book and music aimed at parents and caregivers of preschool aged children to assist them in preparing their children for kindergarten.

In 2012, the Company began development of an application based on our content and characters. The initial application includes digital video and music delivery, with games and puzzles based on our characters, which is scheduled to be available in the second quarter of 2013. Future enhancements include a variety of tools, including lesson plans, curriculum and songs designed to assist parents teach academic subjects and socialization skills to their children ages 2-5 years in preparation for attending kindergarten.

The Company launched a line of classic movies and television programs, "Pacific Entertainment Presents". Initially consisting of seven titles, each focusing on a specific genre such as Horror, Western, SciFi, Action, Mystery, War, and Gangster, an additional six titles were added in late 2010 expanding the line with the Super Hero's collection as well as Family Favorites. During 2011, the Company also signed distribution agreements with five studios whereby we sell their existing products through our channels of distribution. The agreements range in length from three to five years.

The Company's Financial Statements are prepared in accordance with accounting principles generally accepted in the United States of America. These require the use of estimates and assumptions that affect the assets, liabilities, revenues and expenses reported in the financial statements, as well as amounts included in the notes thereto, including discussion and disclosure of contingent liabilities. Although the Company uses its best estimates and judgments, actual results could differ from these estimates as future confirming events occur.

Liquidity

Historically, the Company has incurred net losses. As of March 31, 2013, the Company had an accumulated deficit of $11,153,889 and a total stockholders' deficit of $1,092,829. At March 31, 2013, the Company had current assets of $1,192,571, including cash of $179,835, and current liabilities of $2,305,374, resulting in a working capital deficit of $1,112,803. For the three months ended March 31, 2013, the Company reported a net loss of $945,865 and net cash used by operating activities of $226,163. Management believes that its increasing sales, cash provided by operations, together with funds available from deferred officers' salaries and short term financing, will be sufficient to fund planned operations for the next twelve months. However, there can be no assurance that operations and operating cash flows will continue at the current levels or improve in the near future. If the Company is unable to obtain profitable operations and positive operating cash flows sufficient to meet scheduled debt obligations, it may need to seek additional funding or be forced to scale back its development plans or to significantly reduce or terminate operations.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods.

Cash Equivalents

The Company considers all highly liquid debt instruments with initial maturities of three months or less to be cash equivalents.

Significant Accounting Policies

Revenue Recognition - The Company recognized revenue related to product sales when (i) the seller's price is substantially fixed, (ii) shipment has occurred causing the buyer to be obligated to pay for product, (iii) the buyer has economic substance apart from the seller, and (iv) there is no significant obligation for future performance to directly bring about the resale of the product by the buyer as required by FASB Accounting Standards Codification ("ASC") Topic 605 - Revenue Recognition.

Revenues associated with the sale of products, are recorded when shipped to customers pursuant to approved customer purchase orders resulting in the transfer of title and risk of loss. Cost of sales, rebates and discounts are recorded at the time of revenue recognition or at each financial reporting date.

The Company's licensing and royalty revenue represent variable payments based on net sales from brand licensees for content distribution rights. These license agreements are held in conjunction with third parties that are responsible for collecting fees due and remitting to the Company its share after expenses. Revenue from licensed products is recognized when realized or realizable based on royalty reporting received from licensees.

Shipping and Handling - The Company records shipping and handling expenses in the period in which they are incurred and are included in the Cost of Goods Sold.

Inventories - Inventories are stated at the lower of cost (average) or market and consist of finished goods such as DVDs, CDs and other products. A reserve for slow-moving and obsolete inventory is established for all inventory deemed potentially non-saleable by management in the period in which it is determined to be potentially non-saleable. The current inventory is considered properly valued and saleable. The Company concluded that there was an appropriate reserve for slow moving and obsolete inventory of $60,474 and $57,305 established as of March 31, 2013 and December 31, 2012, respectively.

Property and Equipment - Property and equipment are recorded at cost. Depreciation on property and equipment is computed using the straight-line method over the estimated useful lives of the assets, which range from 5 to 39 years. Maintenance, repairs, and renewals, which neither materially add to the value of the assets nor appreciably prolong their lives, are charged to expense as incurred. Gains and losses from dispositions of property and equipment are reflected in the statement of operations.

Intangible Assets –Intangible Assets acquired, either individually or with a group of other assets, are initially recognized and measured based on fair value. In the acquisition of the assets from Genius Products, fair value was calculated using a discounted cash flow analysis of the revenue streams for the estimated life of the assets.

The Company develops new video, music, books and digital applications, in addition to adding content, improved animation and songs/features to their existing productions. The costs of new product development and significant improvement to existing products are capitalized while routine and periodic alterations to existing products are expensed as incurred. The Company begins amortization of new products when it is available for general release. Annual amortization cost of intangible assets are computed based on the straight-line method over the remaining economic life of the product, generally such deferred costs are amortized over five years.

The Company reviews all intangible assets periodically to determine if the value has been impaired by recent financial transactions using the discounted cash flow analysis of revenue stream for the estimated life of the assets.

Stock Based Compensation - As required ASC 718 - Stock Compensation, the Company recognizes an expense related to the fair value of our stock-compensation awards, including stock options, using the Black-Scholes calculation as of the date of grant.

Advertising Costs- The Company's marketing and sales costs are primarily related to advertising, trade shows, public relation fees and production and distribution of collateral materials. In accordance with ASC 720 regarding Advertising Costs, the Company expenses advertising costs in the period in which the expense is incurred. Marketing and Sales costs incurred by licensees are borne fully by the licensee and are not the responsibility of the Company. Advertising expense for the three months ended March 31, 201 and March 31, 2012 was $13,500 and $16,560, respectively.

Allowance for Sales Returns - An Allowance for Sales Returns is estimated based on average sales during the previous year. Based on experience, sales growth, and our customer base, the Company concluded that the allowance for sales returns at March 31, 2013 and December 31, 2012 should be $43,000 and $53,000, respectively.

Fair value of financial instruments - The carrying amounts of cash, receivables and accrued liabilities approximate fair value due to the short-term maturity of the instruments.

Note 2: Plant, Property, and Equipment and Intangible Assets

The Company has plant, property and equipment and other intangible assets used in the creation of revenue as follows as of March 31, 2013 and December 31, 2012:

	3/31/2013	12/31/2012
Furniture and Equipment	$89,159	$89,159
Less Accumulated Depreciation	(68,018)	(65,423)
Net Fixed Assets	$21,141	$23,736
Trademarks	$129,831	$129,831
Product Masters	3,279,369	3,279,369
Other Intangible Assets	290,161	290,161

Less Accumulated Amortization	(3,379,868)	(3,343,291)
Net Intangible Assets	$319,493	$356,070

Pursuant to FASB Accounting Standards Codification regarding Topic 350, Intangible Assets, intangible asset(s) acquired, either individually or with a group of other assets shall be initially recognized and measured based on fair value. In the acquisition of the assets from Genius Products, fair value was calculated using a discounted cash flow analysis of the revenue streams for the estimated life of the assets. As this resulted in a fair market value in excess of the purchase price, the assets were recorded at $2,489,082, the total purchase price discounted with the imputed interest rate of 10%.

The Company reviews all intangible assets periodically to determine if the value has been impaired by recent financial transactions using the discounted cash flow analysis of revenue stream for the estimated life of the assets. At March 31, 2013 and December 31, 2012, it was determined that no impairment existed.

The Company continues to develop new videos, music, books and digital applications in addition to adding content, improved animation and bonus songs/features to its existing product catalog. In accordance with FASB Accounting Standards Codification regarding ASC 350 - Intangible Assets and ASC 730 - Research and Development*,* the costs of new product development and significant improvement to existing products are capitalized while routine and periodic alterations to existing products are expensed as incurred. As of March 31, 2013, the Company has $320,306 in Capitalized Product Development in Process representing video, music, website, digital application and preschool preparation program development projects not yet completed.

Note 3: Accrued Liabilities

Accrued but unpaid salaries and vacation benefits total $614,991 and $516,083 as of March 31, 2013 and December 31, 2012, respectively. Debenture Interest accrued and unpaid is $45,716 at both March 31, 2013 and December 31, 2012. Other accrued liabilities totaling $349,420 and $496,662 as of March 31, 2013 and December 31, 2102 are as follows:

	3/31/2013	12/31/2012
Allowance for Sales Returns	$ 43,000	$ 53,000
Distribution Arrangements Payable	184,351	217,858
Deferred Revenue	63,102	110,177
Royalties Payable	33,395	59,033
Other Accrued Expenses	25,572	56,594
Total Accrued Expenses	$ 349,420	$ 496,662

The Company recognized a derivative liability for the conversion feature and warrants for the $1.0 million senior secured debenture issued on June 27, 2012 as an embedded derivative. It was valued on the respective transaction dates of June 27, 2012 for issuance of the debentures and the period ended March 31, 2013 using a Black-Scholes pricing model. The conversion feature may be exercised at any time and are thus reported as current liabilities. Warrants to purchase 5,000,000 shares of common stock were issued to Hillair as part of the debenture and 380,952 warrants to purchase shares of common stock were issued to National Securities Corporation and several of its employees, who acted as placement agent to the Company in connection with the Debenture. These warrants have a cashless exercise provision effective six months after the issuance date. In accordance with ASC 815-10-25, we measured the subsequent derivative valuation using a Black-Scholes pricing model on December 31, 2012 and recorded the additional derivative liability as of that date. See Note 6: Stockholders' Equity for additional information on the warrants issued. At the end of each quarterly reporting date the values are evaluated and adjusted to current market value. The amount recorded as of March 31, 2013 and December 31, 2012 was $161,824 and $68,962, respectively.

Derivative liability activity for the three months ending March 31, 2013 was as follows:

March 31, 2013	December 31, 2012	(Gain) Loss on Derivative, 3 Months Ending March 31, 2013
$ 50,570	$ 15,743	$ 34,827

Conversion feature of the June 27, 2012 Securities Purchase Agreement (see note 4)			
5,000,000 Warrants	103,377	49,491	53,886
380,952 Warrants	7,877	3,728	4,149
Total	$161,824	$ 68,962	$ 92,862

Fair market values of the Company's derivatives as of March 31, 2013 were based on the Black Scholes valuation using the following assumptions:

	Conversion Feature	Warrants
Risk-free interest rate	0.14%	0.77%
Expected life in years	1.24	4.24
Dividend yield	0	0
Expected volatility	79.38%	68.41%

The Company recorded a loss on the derivative valuation for the debenture in the amounts of $92,862 and $0 for the three months ended March 31, 2013 and 2012, respectively.

Note 4: Notes Payable

On June 27, 2012, the Company entered into a Securities Purchase Agreement with Hillair Capital Investments L.P. ("Hillair") whereby the Company issued and sold (i) a $1,000,000 16% senior secured convertible debenture due June 27, 2014 (the "Debenture"), and (ii) a common stock purchase warrant (the "Debenture Warrant") to purchase up to 5,000,000 shares of the Company's common stock. The initial closing of the Debenture and Warrant Transaction occurred on June 27, 2012 ("Original Issue Date"). The Company issued to Hillair the Debenture and the Debenture Warrant for the purchase price of $1,000,000. The Debenture is convertible, in whole or in part, into shares of Common Stock upon notice by Hillair to the Company, subject to certain conversion limitations set forth in the Debenture. The conversion price for the Debenture is $0.21 per share, subject to adjustments. Interest on the Debenture accrues at the rate of 16% annually and is payable quarterly on February 1, May 1, August 1 and November 1, beginning on November 1, 2012, on any redemption, conversion and at maturity. Interest is payable in cash or at the Company's option in shares of the Company's common stock; provided certain conditions are met. Commencing on December 27, 2013, the Company will be obligated to redeem a certain amount under the Debenture on a quarterly basis, in an amount equal to $250,000 on each of December 27, 2013 and March 27, 2014 and $500,000 on June 27, 2014, until the Debenture's maturity date of June 27, 2014. Accrued interest was recorded as of March 31, 2013 and December 31, 2012 in the amounts of $45,716 and $45,716, respectively.

Debt Discount was recorded in the aggregate amount of $648,972 for the issuance of warrants and the derivative value of the convertible feature of the debenture at inception.

The warrants were valued in the amount of $379,688, based on the Black-Scholes valuation using the following assumptions:

Risk-free interest rate	0.73%
Expected life in years	5
Dividend yield	0
Expected volatility	63.65%

Debt Discount for the convertible feature of the debenture was valued in the amount of $269,284 using the Black-Scholes calculation with the following assumptions:

Risk-free interest rate	0.31%
Expected life in years	2
Dividend yield	0
Expected volatility	60.01%

Interest expense for the amortization of the debt discount for the warrants and convertible feature of the debenture is calculated on a straight-line basis over the two year life of the debenture. For the periods ended March 31, 2013 and December 31, 2012, amortization of the debt discount was recorded in the amounts of $81,121 and $163,825, respectively, for a debt discount balance of $404,025 and $485,147, respectively.

To secure the Company's obligations under the Debenture, the Company granted a security interest in certain of its property to secure the prompt payment, performance and discharge in full of all of the Company's obligations under the Debenture.

National Securities Corporation acted as placement agent to the Company in connection with the Debenture and Warrant Transaction and received commissions of 8% of the gross proceeds and a five year warrant to purchase up to 380,952 shares of the company's common stock at a price of $0.33 per share, which warrant contained terms substantially similar to the Debenture Warrants.

Additional information regarding the Debenture may be found in the Form 8-K filed by the Company on July 2, 2012.

Debenture Interest accrued and unpaid for the 2006 issuance of $2.5 million is $19,049 as of March 31, 2013 and December 31, 2012. Interest on this series of debentures was terminated effective July 24, 2009 in accordance with the conversion agreement upon establishment of a secondary trading market for our common stock.

As of March 31, 2013 and December 31, 2012, the Company had the following notes payable and accrued interest balances outstanding:

	3/31/2013	12/31/2012
Debenture - $1,000,000 16% senior secured convertible	$1,000,000	$1,000,000
Debt Discount	(404,025)	(485,147)
Total Notes Payable	595,975	514,853
Less: Current Portion	250,000	–
Long Term Portion	$345,975	$514,853
Accrued Interest		
Debenture - $1,000,000 16% senior secured convertible Issued June 27,2012	$26,667	$26,667
Debenture - $2,500,000 Terminated June 2009	19,049	19,049
Accrued Interest - Current Portion	$45,716	$45,716

Maturities requirements on long-term debt subject to mandatory redemption are as follow:

2013	$250,000
2014	750,000
2015	–
2016	–
2017	–
Total	$1,000,000

Note 5: Notes Payable and Accrued Interest - Related Parties

As of March 31, 2013 and December 31, 2012, the Company had the following notes payable and accrued interest balances outstanding:

	3/31/2013	12/31/2012
Officer Loans to Company	$194,163	$ 194,163
Accrued Interest on Officer Loans to Company	52,754	49,087
Subordinated Officer Loans to Company	159,753	159,753
Accrued Interest on Subordinated Loans	47,944	44,888
Total Notes Payable and Accrued Interest	454,614	447,891
Less: Current Portion	–	–
Long Term Portion	$454,614	$ 447,891

Throughout 2009, 2008 and 2007, the Company borrowed funds from Messrs. Moeller, Meader, Larry Balaban and Howard Balaban in the aggregate principal amounts of $4,000, $280,000 and $444,500, respectively. The proceeds from all officer loans were used to pay operating obligations of the Company. Subsequent agreements amended the stated interest rate to 6% per annum and extended the maturity to January 15, 2015. Repayments were made on February 2, 2011 and April 27, 2011 in the aggregate amounts of $66,000 and $30,000, respectively. On March 7, 2012, the four Officers agreed to execute extension agreements to change the maturity date on their respective notes to January 15, 2015, with no change in the terms. For the three months ended March 31, 2013 compared to the same period of 2012, interest expenses for these loans were recorded in amounts of $3,666 and $3,454, respectively.

On February 1, 2008, Isabel Moeller, sister of our Chief Executive Officer, Klaus Moeller, loaned $310,000 to the Company at an interest rate equal to 8% per annum. The funds were borrowed from Ms. Moeller in order to reduce outstanding obligations due to Genius Products, Inc. at that time. Subsequent agreements extended the maturity date to January 15, 2015 and reduced the stated interest rate to six (6%) percent per annum. Repayments on the principal balance were made in the aggregate of $24,000 during February and April 2011. On April 1, 2011, Ms. Moeller agreed to convert $200,000 of the outstanding balance to shares of common stock of the Company. On March 31 2012, Ms. Moeller agreed to convert the remaining balance of outstanding principal and interest, in the amount of $173,385, to shares of common stock of the Company. Interest expense for the three months ended March 31, 2013 and March 31, 2012 was $0 and $2,562, respectively. The note is paid in full.

On March 31, 2011, four of the Company's officers agreed to convert accrued but unpaid salaries through December 31, 2010 to subordinated long term notes payable. In February 2011, as a result of an agreement by each of the four officers to retroactively decrease the amount of the annual salary for 2010 from $125,000 per annum per officer to $80,000, the amount of the notes were reduced to an aggregate of $1,620,137. In March 2012, the officers agreed to convert the aggregate sum of $1,572,161 to shares of common stock of the Company. The remaining note, with a principal balance of $159,753, has a maturity of January 15, 2015 and a stated interest rate of six percent (6%) per annum. For the three month periods ended March 31, 2013 and 2012, interest expense was recorded in the amounts $3,057 and $26,038, respectively. The decrease in expense was due to conversion of a majority of the outstanding balance to common stock on March 31, 2012.

Maturities requirements on long-term debt subject to mandatory redemption are as follow:

2013	$–
2014	–
2015	353,919
2016	–
2017	–
Total	$353,919

Note 6: Stockholders' Equity

As part of the Reincorporation, the total number of authorized shares of common stock was changed to 250,000,000 shares of $0.001 par value. The common stock and additional paid in capital accounts were restated as of December 31, 2012, and for the years then ended, to recognize the change from no par common stock to a par value of $0.001 per share. As of March 31, 2013 and December 31, 2012, there were 72,383,205 and 71,912,617 shares of common stock outstanding, respectively.

The Company has 10,000,000 shares of preferred stock authorized with a par value of $0.001. The Board of Directors is authorized, subject to any limitations prescribed by law, without further vote or action by our stockholders, to issue from time to time shares of preferred stock in one or more series. Each series of preferred stock will have such number of shares, designations, preferences, voting powers, qualifications and special or relative rights or privileges as shall be determined by our board of directors, which may include, among others, dividend rights, voting rights, liquidation preferences, conversion rights and preemptive rights. As of March 31, 2013 and December 31, 2012, no shares were outstanding and the Board of Directors has not authorized issuance of preferred shares.

On February 1, 2013, the Company issued 470,588 shares of common stock in exchange for interest payable on the debenture due on that date in the amount of $40,000, or $0.085 per share. Hillair agreed to waive any anti-dilutive provisions contained in the debenture for this transaction.

On June 27, 2012, a senior secured convertible debenture was issued in the face value of $1,000,000 with a stated conversion price of $0.21, subject to certain adjustments, and 5,000,000 warrants, which is equal to the total face value divided by the stated warrant conversion price of $0.20. The debenture warrants may be exercised at any time on or after June 27, 2012 and on or prior to the close of business on June 27, 2017, at an exercise price of $0.33 per share, subject to adjustments upon certain events. The warrants contain full anti-dilution protection and do not limit the amount the Company would be required to pay or the number of shares the Company could be required to issue. The Company is required to reserve shares equal to the total outstanding debentures divided by seventy-five percent (75%) of the conversion price plus the outstanding warrants. As of March 31, 2013, we have reserved 11,349,206 shares of common stock for the debenture conversion provision and warrants issued to Hillair.

The Company has warrants outstanding to purchase up to 5,852,060 and 5,852,060 shares of our common stock at March 31, 2013 and December 31, 2012, respectively.

Warrants were issued on June 27, 2012 to various holders as part of the debenture. These warrants have an exercise price of $0.33 and will expire on July 26, 2017. All common stock underlying the warrants will be restricted when issued.

Previous warrants had been issued with an exercise price of $0.40 per share and expire on November 18, 2013. All common stock underlying the warrants will be restricted when issued.

Either the exercise price or the number of shares purchasable under the warrant may be adjusted in the event of any split of the common stock, reclassification, capital reorganization or change in the outstanding common stock, or declaration of a common stock dividend. In the event of any such adjustment, the Company will notify the holders of the warrants of the exercise price and number of shares purchasable under the warrant following adjustment, the facts requiring the adjustment and the method of calculation of any increase or decrease in price or purchasable shares. No adjustment will be required, however, unless the adjustment would require an increase or decrease in the exercise price of at least 1%.

Note 7: Income Taxes

The Company accounts for income taxes in accordance with Accounting Standards Codification Topic 740, Income Taxes ("Topic 740"), which requires the recognition of deferred tax liabilities and assets at currently enacted tax rates for the expected future tax consequences of events that have been included in the financial statements or tax returns. A valuation allowance is recognized to reduce the net deferred tax asset to an amount that is more likely than not to be realized.

Topic 740 provides guidance on the accounting for uncertainty in income taxes recognized in a company's financial statements. Topic 740 requires a company to determine whether it is more likely than not that a tax position will be sustained upon examination based upon the technical merits of the position. If the more-likely-than-not threshold is met, a company must measure the tax position to determine the amount to recognize in the financial statements.

At the adoption date of January 1, 2008, the Company had no unrecognized tax benefit which would affect the effective tax rate if recognized.

The Company includes interest and penalties arising from the underpayment of income taxes in the statements of operation in the provision for income taxes. As of March 31, 2013 and December 31, 2012, the Company had no accrued interest or penalties related to uncertain tax positions.

The Company files income tax returns in the U.S. federal jurisdiction and in the state of California. The Company is currently subject to U.S. federal, state and local, or non-U.S. income tax examinations by tax authorities since inception of the Company.

Note 8: Lease Commitments

The Company has no capital leases subject to the Capital Lease guidelines in the FASB Accounting Standards Codification. Rental expenses incurred for operating leases during the three months ended March 31, 2013 and March 31, 2012 were $6,947 and $9,432, respectively. The Company continues to occupy an office in San Diego on a month to month basis. Warehouse space of approximately 2,000 square feet in Rogers, Minnesota is rented on a month to month basis. In November 2012, the Company signed a six month lease to occupy three offices in San Diego, California, which terminated as of April 30, 2013.

Note 9: Recent Accounting Pronouncements

The Company reviews all of the Financial Accounting Standard Board's updates periodically to ensure the Company's compliance of its accounting policies and disclosure requirements to the Codification Topics. The Company has determined there were no new accounting pronouncements issued during the three months ended March 31, 2013 that the Company believes are applicable or would have a material impact on the financial statements of the Company.

Note 10: Stock Options

The Company has adopted the provisions of ASC 718 – Compensation which requires companies to measure the cost of employee services received in exchange for equity instruments based on the grant date fair value of those awards and to recognize the compensation expense over the requisite service period during which the awards are expected to vest.

On December 29, 2008, the Company adopted the Pacific Entertainment Corporation 2008 Stock Option Plan (the "Plan"), which provides for the issuance of qualified and non-qualified stock options to officers, directors, employees and other qualified persons. The Plan is administered by the Board of Directors of the Company or a committee appointed by the Board of Directors. The number of shares of the Company's common stock initially reserved for issuance under the Plan was 11 million. On September 2, 2011, the shareholders holding a majority of the Company's outstanding common stock adopted an amendment to the Company's 2008 Stock Option Plan to increase the number of shares of common stock issuable under the plan to 50 million.

As of March 31, 2013, options to purchase up to 120,000 shares of the Company's common stock previously issued in 2009 through 2012 expired due to the termination of employees.

The following schedule summarizes the changes in the Company's stock option plan for the three months ended March 31, 2013:

	Options Outstanding		Weighted Average		Weighted Average
	Number of Shares	Exercise Price per Share	Remaining Contractual Life	Aggregate Intrinsic Value	Exercise Price per Share
Balance at December 31, 2012	15,845,000	$0.06-0.55	3.55 years	–	$ 0.42
Options Granted	–	–	–	–	–
Options Exercised	–	–	–	–	–
Options Expired	(120,000)	0.34-0.55	–	–	0.44
Balance at March 31, 2013	15,725,000	$0.06-0.55	3.30 years	–	$ 0.42
Exercisable March 31, 2013	13,925,000	$0.06-0.55	2.92 years	–	$ 0.41

Note 11: Warrants

In connection with the sale of shares of its common stock in 2010 the Company issued warrants to purchase a total of 471,108 shares of its common stock at $0.40 per share exercisable for a three-year period.

Warrants to purchase up to 5,380,952 shares of common stock were issued on June 27, 2012 to various holders as part of the debenture disclosed on the Form 8-K filed by the Company on July 3, 2012. These warrants have an exercise price of $0.33 and will expire on June 27, 2017. All common stock underlying the warrants will be restricted when issued.

The following schedule summarizes the changes in the Company’s warrants during the three months ended March 31, 2013:

	Number of Warrants	**Exercise Price per Share**	**Weighted Average Exercise Price per Share**
Balance at December 31, 2012	5,852,060	$0.33 - 0.40	$ 0.34
Warrants Granted	–	–	–
Warrants Exercised	–	–	–
Warrants Expired	–	–	–
Balance at March 31, 2013	5,852,060	0.33 - 0.40	0.34
Exercisable at March 31, 2013	5,852,060	$0.33 - 0.40	$ 0.34

The following schedule summarizes the outstanding warrants at March 31, 2013:

Number of Warrants Outstanding at March 31, 2013	**Number of Warrants Exercisable at March 31, 2013**	**Expiration Date**	**Exercise Price**
471,108	471,108	2013	$ 0.40
5,380,952	5,380,952	2017	$ 0.33

Note 12: Fair Value Measurements

We adopted ASC Topic 820 (originally issued as SFAS 157, "Fair Value Measurements") as of January 1, 2008 for financial instruments measured at fair value on a recurring basis. ASC Topic 820 defines fair value, establishes a framework for measuring fair value in accordance with accounting principles generally accepted in the United States and expands disclosures about fair value measurements.

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC Topic 820 establishes a three-tier fair value hierarchy which prioritizes the inputs used in measuring fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements). These tiers include:

- Level 1, defined as observable inputs such as quoted prices for identical instruments in active markets;
- Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable such as quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in markets that are not active; and
- Level 3, defined as unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions, such as valuations derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable.

We measure certain financial instruments at fair value on a recurring basis. Assets and liabilities measured at fair value on a recurring basis are as follows at March 31, 2013:

	Total	(Level 3)

		(Level 1)	(Level 2)	
Assets	$–	$ –	$ –	$–
Total assets measured at fair value	–	–	–	–
Liabilities				
Derivative Liability	161,824	–	–	161,824
Convertible Debenture, net of discount	345,975	–	–	345,975
Total liabilities measured at fair value	$507,799	$ –	$ –	$507,799

Note 13: Employment Agreements

On April 26, 2011, the Company and each of Messrs. Moeller, Meader, Larry Balaban and Howard Balaban (the "Executives") agreed to terminate all then existing employment agreements for the Executives and enter into new five-year employment agreements unless written termination is provided by either party. Each employment agreement provides for a graduated base salary beginning at $165,000 per annum retroactive to March 20, 2011, continuing to December 31, 2011, increasing to $195,000 for 2012 and $225,000 for 2013. After 2013, the agreement provides for base salary increases at the discretion of the Board of Directors, with a minimum 5% increase. In addition to base salary, each Executive will receive an annual car allowance of $11,400, and four weeks paid vacation per annum.

On January 10, 2013, Messrs. Moeller, Meader and Howard Balaban agreed to reduce the amount of payments for salary effective January 1, 2013 through January 19, 2013 to $165,000 and a further reduction to $140,000 commencing January 20, 2013, continuing until further notice by each one to the Board of Directors. The agreements with each of Messrs. Moeller, Meader and Howard Balaban include the accrual of unpaid salary, the right to convert any or all of the accrued but unpaid salary to common stock of the Company at a conversion price of $0.21 per share and an amendment to all outstanding stock option grant notices to allow each to retain all rights until the expiration date upon termination unless for cause, as defined in the employment agreement.

On March 28, 2013, Mr. Meader voluntarily resigned his position as President effective April 1, 2013. The Company agreed to the retention of all stock options granted to Mr. Meader as of the date of termination, vesting and expiration dates in accordance with the original grant notices in exchange for a general release of all claims against the Company. The Company has entered into a consulting agreement with Mr. Meader to provide continued services for an initial period of twelve months.

On May 2, 2012, the Company entered into a five-year “at will” employment agreement with Jeanene Morgan to serve as the Company’s Chief Financial Officer. The agreement provides a base salary of $165,000 per annum from January 1, 2012 to December 31, 2012, increasing to $190,000 on January 1, 2013 and $215,000 on January 1, 2014. After 2014, the agreement provides for base salary increases at the discretion of the Board of Directors with a minimum 5% increase. The board of directors, in its sole discretion, may grant Ms. Morgan a year-end bonus with a value of no less than 2% of EBITDA of the Company (assuming a positive figure) and up to 100% of Ms. Morgan’s base salary. Ms. Morgan shall be granted an option to purchase 200,000 shares of the Company’s common stock. Ms. Morgan shall be permitted to participate in all benefit plans of the Company and receive 4 weeks paid vacation.

On January 10, 2013, Ms. Morgan agreed to defer the payment of the salary increase which would have become effective January 1, 2013. The deferral will continue until further notice by Ms. Morgan to the Board of Directors. The agreement includes the accrual of unpaid salary, the right to convert any or all of the accrued but unpaid salary to common stock of the Company at a conversion price of $0.21 per share and an amendment to all outstanding stock option grant notices to allow Ms. Morgan to retain all rights until the expiration date upon termination unless for cause, as defined in the employment agreement.

The following is a schedule by year of the future minimum salary payments related to these employment agreements:

2013	$727,211
2014	923,750
2015	969,939
2016	432,389
Total	$3,053,289

Note 14: Subsequent Events

The Company evaluated subsequent events pursuant to ASC 855 and has determined there are no events to disclose.

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

The following discussion and analysis of our results of operations, financial condition and liquidity and capital resources should be read in conjunction with our unaudited financial statements and related notes for the three months ended March 31, 2013 and 2012. In addition to historical financial information, the following discussion contains forward-looking statements that reflect our plans, estimates and beliefs. Our actual results could differ materially from those discussed in the forward-looking statements.

Forward Looking Statements

This report on Form 10-Q contains forward-looking statements which involve assumptions and describe our future plans, strategies and expectations. When used in this statement, the words “may,” “will,” “expect,” “anticipate,” “continue,” “estimate,” “project,” “intend,” and similar expressions are intended to identify forward-looking statements regarding events, conditions, and financial trends that may affect the Company’s future plans of operations, business strategy, operating results, and financial position. These statements are expressed in good faith and based upon a reasonable basis when made, but there can be no assurance that these expectations will be achieved or accomplished.

Persons reviewing this report are cautioned that any forward-looking statements are not guarantees of future performance and are subject to risks and uncertainties and actual results may differ materially from those included within the forward looking statements as a result of various factors. Such factors include, among other things, uncertainties relating to our success in judging consumer preferences, financing our operations, entering into strategic partnerships, engaging management, seasonal and period-to-period fluctuations in sales, failure to increase market share or sales, inability to service outstanding debt obligations, dependence on a limited number of customers, increased production costs or delays in production of new products, intense competition within the industry, inability to protect intellectual property in the international market for our products, changes in market condition and other matters disclosed by us in our public filings from time to time. Forward-looking statements speak only as to the date they are made. The Company does not undertake to update forward-looking statements to reflect circumstances or events that occur after the date the forward-looking statements are made.

Overview

The MD&A is based on our financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires us to make certain estimates and judgments that affect the reported amounts of assets, liabilities and expenses and related disclosure of contingent assets and liabilities. Management bases its 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 and conditions.

Our Business

Genius Brands International, Inc. ("we", "us", "our" or the "Company"), *f/k/a* Pacific Entertainment Corporation, creates and distributes music-based products which we believe are entertaining, educational and beneficial to the well-being of infants and young children under our brands, including Baby Genius. We create, market and sell children's videos, music, books and other products in the United States by distribution at wholesale to retail stores, direct to consumers through various "deal for a day" sites and through digital platforms using intellectual property developed and owned by us. We license the use of our intellectual property, both domestically and internationally, to others to manufacture, market and sell products based on our characters and brand, whereby we receive advances and royalties. The Company also obtains rights to the content of other studios for distribution through our warehouse facility to our customers, for which we either pay royalty fees or earn distribution fees. We have licensing agreements with other companies under which we produce music-based products using their characters and brands and for which we pay a royalty.

The Company commenced operations in January 2006, assuming all of the rights and obligations of its Chief Executive Officer, Klaus Moeller, under an Asset Purchase Agreement between the Company and Genius Products, Inc., in which we obtained all rights, copyrights, and trademarks to the brands “Baby Genius,” “Little Genius,” “Kid Genius,” “123 Favorite Music” and “Wee Worship,” and all then existing productions under those titles. On October 17, 2011 and October 18, 2011, Genius Brands International, Inc., filed Articles of Merger with the Secretary of State of the State of Nevada and with the Secretary of State of the State of California, respectively. As previously described on the Company’s Schedule 14C Information Statement, filed with the Securities and Exchange Commission on September 21, 2011, by filing the Articles of Merger, the Company (i) changed its domicile to Nevada from California, and (ii) changed its name to Genius Brands International, Inc. from Pacific Entertainment Corporation (the “Reincorporation”). Pursuant to the Articles of Merger, Pacific Entertainment Corporation, a California corporation, merged into Genius Brands International, Inc., a Nevada corporation that, prior to the Reincorporation, was the wholly owned subsidiary of Pacific Entertainment Corporation. Genius Brands International, the Nevada corporation, is the surviving corporation. In connection with the Reincorporation, on October 12, 2011, the Company filed an Issuer Company-Related Action Notification Form with the Financial Industry Regulatory Authority (“FINRA”) and on November 29, 2011 our trading symbol changed from “PENT” to “GNUS”.

In addition to the distribution of our products, we have developed and will continue to develop multiple revenue streams which include worldwide licensing and merchandising opportunities for toys and other customer products that have been inspired by our brands or which we feel we can market and sell through our distribution channels. The Company is committed to providing the very best in children’s education and developmental entertainment, as well as quality items based on our brand and licensed characters.

The Company believes that the distribution of products is changing from the traditional brick and mortar retail store to an increasing emphasis on digital delivery whereby the owners of content will be able to reach customers directly through a digital delivery platform. In 2013, we began creation of a digital delivery application and anticipate the initial completion date in the second quarter of 2013. We also self-distribute products through direct relationships with customers, both retail and wholesale, from our warehouse facility in Rogers, Minnesota.

Following is a summary of our revenues, assets and net losses for our two most recent fiscal years ended March 31, 2013 and March 31, 2012:

	Three Months Ended March 31,	
	2013	2012
Total Revenue	$734,239	$1,030,947
Net Loss	$(945,865)	$(605,667)
Total Assets	$2,013,134	$2,278,608

Total Liabilities	$3,105,963	$2,192,036
Accumulated Deficit	$(11,153,889)	$(8,740,716)

Products

Our products consist primarily of family and children's videos, music, books and other entertainment products. The products are manufactured and sold under brand names such as "Baby Genius", "Little Genius", "Kid Genius", "Wee Worship" and "123 Favorite Music". The Company has created eleven videos, five hundred songs and twelve books which are owned by us and we continue to add content to the library. Some Baby Genius products are bilingual in English and Spanish versions. Our Baby Genius brand products are designed primarily for ages from 0 – 5 years and our Little Genius products focus on children up to age 8 years.

We also license our Baby Genius brand and characters for various product lines including toys, sunglasses, games and puzzles, sippy cups, and early learning aids, as well as others, and receive advances and royalties based on sales of these products.

On January 11, 2011, the Company signed a five-year, world-wide license agreement with Tollytots® for a new toy line to be distributed world-wide. As a result of the agreement, Tollytots® immediately began development on a comprehensive line of musical and early learning toys, incorporating the music, characters and themes associated with our *Baby Genius* series of videos and music CDs. As described above under “Distribution”, the toy line covers a broad range of exclusive categories including learning and developmental toys, most plush toys, and musical toys which Tollytots® has the sole right to manufacture, market and distribute on a world-wide basis. It also allows Tollytots® a non-exclusive right to manufacture, market and distribute products in several non-exclusive categories, including board games, puzzles, electronic learning aids and amusement plush toys, where we may already have other licenses who produce similar products or may grant licenses for such products to new parties in addition to Tollytots®. We have received recoupable advances and will receive quarterly royalty payments in excess of the advances, if applicable, from sales of products developed under the agreement by Tollytots®. The Company will have rights to sell product developed under the license agreement directly via its website subject to availability of inventory from Tollytots®. The agreement provides for certain guaranteed minimum payments to the Company for each contract year. The agreement is subject to early termination by the Company in specified territories in the event minimum sales requirements in those territories have not been met in any contract year. Currently, Tollytots® has several toys developed for the line, including musical and early learning toys, and the toys were available for retail sales beginning in the third quarter of 2012. The new toy line has not produce additional royalty revenue subsequent to its launch at retail in the third quarter of 2012 in excess of the guaranteed minimum payments and there is no guarantee that it will produce additional revenue in the future.

We will continue to explore the potential for derivative products under the Baby Genius brand to expand brand awareness and sales. For instance, we have created custom products using the Baby Genius brand for several book and music premiums, including Wendy’s, Taco Bell and Gerber. For example, through an agreement with a third party licensee, we created small books based on our characters specifically for Wendy’s which were inserted as a gift in Under 3 kids meals purchased at Wendy’s locations throughout 2012.

On September 20, 2010, the Company entered into a joint venture agreement with Dr. Shulamit Ritblatt to form Circle of Education, LLC (“COE”), a California limited liability company, for the purpose of creation and distribution of a curriculum to promote school readiness for children ages 2-5 years. The Company actively participated in a research study into the use of music-based curriculum through a major university for three years based on certain unregistered copyrights and trademarks, confidential information, designs, ideas, discoveries, inventions, processes, research results and work product it had developed. In March 2012, the Company and Dr. Ritblatt agreed to terminate the joint venture agreement. COE transferred equal right of ownership in the intellectual property developed as of the date of termination (“IP”) to each of the Company and Dr. Ritblatt, and in exchange for the rights to the IP, Dr. Ritblatt transferred her units of COE to the Company. Each party will have the right to continue development of the IP and products based on the IP with no further obligation to the other party. Subject to certain limitations for specific channels of distribution reserved for each party for a period of twelve months from the execution of the agreements, both parties have non-exclusive and non-restrictive rights to the use, sublicense or sale of the IP and products created based on the IP.

The Company has developed the Ready!Play!Learn!™ program based partially on the intellectual property discussed above, which we anticipate will be available for distribution in the second quarter of 2013. The program includes a curriculum book and music aimed at parents and caregivers of preschool aged children to assist them in preparing their children for kindergarten.

In 2013, the Company signed agreements to develop an application based on our content and characters. The initial application includes digital video and music delivery, with games and puzzles based on our characters, which is scheduled to be available in the second quarter of 2013. Future enhancements include a variety of tools, including lesson plans, curriculum and songs designed to assist parents teach academic subjects and socialization skills to their children ages 2-5 years in preparation for attending kindergarten.

We created a set of early learning cards “Numbers and Alphabet” using our characters which were made available in 2012 and are currently developing additional products for addition to our catalog in 2013.

We have third party licensing agreements under which we developed musical products under other brands. Through an exclusive licensing agreement with the San Diego Zoological Society, we created a series of Baby Genius DVD’s featuring footage from the San Diego Zoo and San Diego Wild Animal Park. We will continue to investigate partnerships which may lead to additions to our product lines.

Our business has reacted to seasonal influence, such as the holiday season. We generally anticipate increased sales in the third and fourth quarters principally due to sales from the holiday season. Due to the seasonality of our sales, we expect quarterly results to fluctuate. Our results of operations may also fluctuate significantly as a result of a variety of other factors, including changing consumer tastes and the marketing efforts of our distributors.

Results of Operations

Three Month Period Ended March 31, 2013 Compared to March 31, 2012

Our summary results of operations are presented below:

	Three Months Ended March 31,			
	2013	2012	Change	% Change
Revenues	$734,239	$1,030,947	$(296,708)	-28.8 %
Costs and Operating Expenses	(1,386,103)	(1,559,403)	173,300	-11.1 %
Depreciation and Amortization	(39,172)	(38,715)	(457)	1.2 %
Loss from Operations	(691,036)	(567,171)	(123,865)	21.8 %
Other Income	16	85	(69)	-81.2 %
Interest Expense	(161,983)	(33,215)	(128,768)	387.7 %
Gain on settlement of debt	–	–	–	100.0 %
Gain on derviative valuation	(92,862)	–	(92,862)	100.0 %
Net Other Income (Expense)	(254,829)	(33,130)	(221,699)	669.2 %
Net Loss	(945,865)	(600,301)	(345,564)	57.6 %
Net Loss attributable to Noncontrolling Interest	–	(5,366)	5,366	-100.0 %
Net Loss attributable to Genius Brands International, Inc.	$(945,865)	$(605,667)	$(340,198)	56.2 %
Net Loss per common share	$(0.01)	$(0.01)		
Weighted average shares outstanding	72,215,885	60,698,815		

Revenues. Revenues by product segment and for the Company as a whole were as follows:

	Three Months Ended March 31,			
	2013	2012	Change	% Change
Genius Brands Product Sales	$216,523	$522,023	$(305,500)	-58.5 %
Licensed and Distributed Products	486,290	479,228	7,062	1.5 %
Royalty Revenue	31,426	29,696	1,730	5.8 %
Total Revenue	$734,239	$1,030,947	$(296,708)	-28.8 %

Genius Brands product sales represent items in which the Company holds the copyrights and/or trademarks to the characters and content which are manufactured and sold by the Company directly, either at wholesale to retail stores and outlets or direct to consumers through daily deal sites and our website. The decrease of $305,500 (58.5%) for the three months ended March 31, 2013 compared to the three months ended March 31, 2012, was due to a decrease in sales at wholesale to retail customers, returns from distributors and a reduction in sales directly to consumers. Management believes that the Company is on target to increase direct product sales volumes over 2012, although economic and retail conditions in the market could impact our future sales in a negative manner and we are unable to guarantee increased sales. We continue to explore additional sales opportunities with retail and distribution customers; however, there is no guarantee that our products will be accepted by these new customers.

The licensed and distributed product sales category includes items for which we license rights from other companies to copyrights and trademarks of select brands we felt would do well within our distribution channels, product acquired from other studios through distribution agreements, and overstock inventory from other studios which we sell. For the three months ended March 31, 2013, the category increased by $7,062 (1.5%) over the same period in 2012 as a result of an increase in outside overstock studio product acquired and sold. The timing of the sales of overstock product is intermittent and unpredictable as it is determined by the availability of excess inventory from outside studios and the product margin is minimal. As a result, the Company has discontinued the sales of overstock effective at the end of the first quarter of 2013. We intend to focus all our resources on our core product categories of family and children's entertainment and education products and will phase out unrelated products over the next six months.

Royalty revenue is income for our characters and brands licensed to others to manufacture and/or market, both internationally and domestically. For the three months ended March 31, 2013 compared to the same period in 2013, this category increased $1,730 (5.8%). There may be fluctuation in licensing revenue due to economic conditions in the sales territory.

Our products compete in the pre-school music, books, DVDs, and toy categories. We believe we compare favorably in the quality of our products, as well as competitive price point. We continue to market direct to retailers and are exploring new domestic and international licensing opportunities. We are investigating additional relevant external brands to license, adding to the diversity of our product line, while maintaining the integrity of our core mission of educating and entertaining children.

The Company's business is subject to the effects of seasonality, causing revenues to fluctuate with consumer purchasing behavior, competition, and the timing of holiday periods.

The 2013 economic outlook remains challenging, however, we anticipate sales growth through our actions to improve our existing products, maintaining highly competitive price points, increasing our digital product revenue and adding content to our product catalog.

Costs. Costs and expenses, excluding depreciation and amortization, consisting of cost of sales, marketing and sales expenses, and general and administrative costs, decreased $173,300 (11.1%) for the three months ended March 31, 2013 compared to the three months ended March 31, 2012.

	Three Months Ended March 31,			
	2013	2012	Change	% Change

Cost of Sales	$647,309	$734,131	$(86,822)	-11.8	%
General and Administrative	657,084	630,035	27,049	4.3	%
Marketing and Sales	54,719	189,557	(134,838)	-71.1	%
Product Development	26,991	5,680	21,311	375.2	%
Total Costs and Operating Expenses	$1,386,103	$1,559,403	$(173,300)	-11.1	%

Cost of sales decreased $86,822 (11.8%) during the three months ended March 31, 2013 compared to the three months ended March 31, 2012, as a result of decreased sales volumes, offset by product mix variations and increased shipping costs due to the larger volume of direct to consumer shipments.

Operating expenses predominately consists of salaries, employee benefits and stock based compensation as well as other expenses associated with executive management, finance, legal, facilities, marketing, rent, and other professional services. Costs associated with these categories are detailed as follows:

General and administrative costs increased $27,049 (4.3%) for the three months ended March 31, 2013 compared to the three months ended March 31, 2012. This is the result of increases in salaries and related expenses of $61,781 offset by a decrease in investor relations of $26,589.

Marketing and sales expenses include trade shows, public relations firms, sales and royalty commissions and personal contact. Marketing expenses exhibit some fluctuation due to timing of trade shows attended. For the three months ended March 31, 2013 compared to the same period in the prior year the total expense decreased $134,838 (71.1%), due to reductions of commission expense for outside sales on direct to consumer products.

Product development expenses are for routine and periodic alterations to existing products. For the three months ended March 31, 2013 compared to the three months ended March 31, 2012, these expenses increased $21,311 (375.2%). All costs for new product development and significant improvements to existing products are capitalized in accordance with FASB Accounting Standards Codification Topic 350, Intangible Assets and Topic 730, Research and Development.

Operating expenditures are not generally seasonal and require consistent cash outflows.

Interest Expense. Interest expense primarily resulted from the debenture and related party loans.

The Company borrowed funds from four of the Officers of the Company during the years 2007 to 2009 and issued promissory notes in favor of the Officers. The proceeds from the notes were used to pay operating obligations of the Company. Interest expense was recorded in the three months ended March 31, 2013 and 2012 in the amounts of $3,666 and $3,454, respectively.

On February 1, 2008, Isabel Moeller, sister of our Chief Executive Officer, Klaus Moeller, loaned $310,000 to the Company at an interest rate equal to 8% per annum. The funds were borrowed from Ms. Moeller in order to reduce outstanding obligations due to Genius Products, Inc. at that time. Subsequent agreements extended the maturity date to January 15, 2015 and reduced the stated interest rate to six (6%) percent per annum. Repayments on the principle balance were made in the aggregate of $24,000 during February and April 2011. On April 1, 2011, Ms. Moeller agreed to convert $200,000 of the outstanding balance to shares of common stock of the Company. On March 31 2012, Ms. Moeller agreed to convert the remaining balance of outstanding principal and interest, in the amount of $173,385, to shares of common stock of the Company. The interest expense for the three months ended March 31, 2013 and March 31, 2012 was $0 and $2,562, respectively. The note is paid in full.

On March 31, 2011, four of the Officers agreed to convert accrued but unpaid salaries through December 31, 2010 to subordinated long term notes payable. In February 2011, as a result of an agreement by each of the four Officers to retroactively decrease the amount of the annual salary for 2010 from $125,000 per annum per Officer to $80,000, the amount of the notes were reduced to an aggregate of $1,620,137. In March 2102, the Officers agreed to convert the aggregate sum of $1,572,161 to shares of common stock of the Company. The remaining note, with a principal balance of $159,753, has a maturity of January 15, 2015 and a stated interest rate of six percent (6%) per annum. For the three months ended March 31, 2013 and March 31, 2012, interest expense was recorded in the amount of $3,057 and $26,038, respectively.

Liquidity and Capital Resources

Three and Three Months Ended March 31, 2013 Compared to March 31, 2012

To date, we have relied on a combination of revenue, loans from officers, the debenture issued in June 2012 and private offerings of stock to meet our cash requirements. Currently, our principal source of liquidity is cash in the bank. Management believes that its increasing revenues and cash generated by operations, together with funds available from deferred officers salaries and short term financing, will be sufficient to fund planned operations for the next twelve months. However, there can be no assurance that operations and operating cash flows will continue at the current levels or improve in the near future. If the Company is unable to obtain profitable operations and positive operating cash flows sufficient to meet scheduled debt obligations, it may need to seek additional funding through equity and related party loans or be forced to scale back its development plans or to significantly reduce or terminate operations.

Cash totaled $179,835 and $428,771 at March 31, 2013 and March 31, 2012, respectively. The change in cash is as follows:

	Three Months Ended March 31,		
	2013	2012	Change
Cash provided (used) by operations	$(226,163)	$51,201	$(277,364)
Cash provided (used) in investing activities	(73,689)	(27,771)	(45,918)
Cash provided (used) in financing activities	32,129	–	32,129
Increase (decrease) in cash	$(267,723)	$23,430	$(291,153)

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Our cash flow is very seasonal and a vast majority of our sales historically occur in the last two quarters of the year as retailers expand inventories for the holiday selling season. Cash provided by operations in the three months ended March 31, 2013, compared to 2012, increased by $277,364 due to increased net loss, a decrease in the accounts payable and other accrued expenses balances offset by decreases in accounts receivable and accrued salaries to officers. Cash used in the same periods for investing activities relates to investment in additional music, DVD and digital application projects.

Notes were issued in favor of four of the Officers for loans to the Company at various times during the years 2007 through 2009. Interest expense was recorded in the three months ended March 31, 2013 and 2012 in the amounts of $3,666 and $3,454, respectively.

On March 31, 2011, four of the Officers agreed to convert accrued but unpaid salaries through March 31, 2011 to subordinated long term notes payable in an aggregate of $1,620,137. In March 2012, the Officers agreed to convert the sum of $1,572,161 to shares of common stock of the Company. The remaining note, with a principal balance of $159,753, has a maturity of January 15, 2015 and a stated interest rate of six percent (6%) per annum. For the three months ended March 31, 2013 and March 31, 2012, interest expense was recorded in the amount of $3,057 and $26,038, respectively.

On June 27, 2012, the Company entered into a Securities Purchase Agreement with Hillair Capital Investments L.P. whereby the Company issued and sold (i) a $1,000,000 16% senior secured convertible debenture due June 27, 2014. The Company recorded interest expense payable to the holder in cash or stock for the three months ended March 31, 2013 and March 31, 2012 in the amounts of $40,000 and $0, respectively.

Critical Accounting Policies

The Company's accounting policies are described in Note 1: The Company and Significant Accounting Policies of the notes to the Company's financial statements in Item 1 above. Below is a summary of the critical accounting policies, among others, that management believes involve significant judgments and estimates used in the preparation of its financial statements.

Revenue Recognition **–** The Company recognizes revenue related to product sales when (i) the seller's price is substantially fixed, (ii) shipment has occurred causing the buyer to be obligated to pay for product, (iii) the buyer has economic substance apart from the seller, and (iv) there is no significant obligation for future performance to directly bring about the resale of the product by the buyer as required by Revenue Recognition Topic 605 of the FASB Accounting Standards Codification.

Revenues associated with the sale of branded CDs, DVDs and other products, are recorded when shipped to customers pursuant to approved customer purchase orders resulting in the transfer of title and risk of loss. Cost of sales, rebates and discounts are recorded at the time of revenue recognition or at each financial reporting date.

The Company's licensing and royalty revenue represent variable payments based on net sales from brand licensees for exclusive content distribution rights. Revenue from licensed products is recognized when realized or realizable based on royalty reporting received from licensees.

Other Estimates – The Company estimates reserves for future returns of product based on an analysis that considers historical returns, changes in customer demand and current economic trends. The Company regularly reviews the outstanding accounts receivable balances for each account and monitors delinquent accounts for collectability. The Company reviews all intangible assets periodically to determine if the value has been impaired by recent financial transactions using the discounted cash flow analysis of revenue stream for the estimated life of the assets.

Item 3. Quantitative and Qualitative Disclosures about Market Risk.

Not applicable

Item 4. Controls and Procedures.

Disclosure Controls and Procedures

We carried out an evaluation, under the supervision and with the participation of our management, including our chief executive officer and chief financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the ‘‘Exchange Act’’). Disclosure controls and procedures include, without limitation, controls and procedures that are designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the Exchange Act is accumulated and communicated to the issuer’s management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. Based upon our evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures are effective, for the three months ended March 31, 2013, in ensuring that information that we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission rules and forms.

Internal Control Over Financial Reporting

There were no changes in our system of internal controls over financial reporting during the three months ended March 31, 2013 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION

Item 1. Legal proceedings.

There are presently no material pending legal proceedings to which the Company is a party or as to which any of its property is subject, and no such proceedings are known to the Company to be threatened or contemplated against it.

Item 1a. Risk factors.

As a "smaller reporting company" as defined by Item 10 of Regulation S-K, the Company is not required to provide information required by this Item.

Item 2. Unregistered sales of equity securities and use of proceeds.

On February 1, 2013, the Company issued 470,588 shares of common stock in exchange for interest payable on the debenture due on that date in the amount of $40,000, or $0.085 per share. Hillair agreed to waive any anti-dilutive provisions contained in the debenture for this transaction.

Item 3. Defaults upon senior securities.

There were no reportable events under this Item 3 during the three months ended March 31, 2013.

Item 4. Mine Safety Disclosures.

Not applicable.

Item 5. Other information.

None.

Item 6. Exhibits.

Exhibit No.	Description
31.1	Section 302 Certification of Chief Executive Officer.
31.2	Section 302 Certification of Chief Financial Officer.
32.1	Section 906 Certification of Chief Executive Officer.
32.2	Section 906 Certification of Chief Financial Officer
101.INS	XBRL Instance Document
101.SCH	XBRL Schema Document
101.CAL	XBRL Calculation Linkbase Document
101.DEF	XBRL Definition Linkbase Document
101.LAB	XBRL Label Linkbase Document
101.PRE	XBRL Presentation Linkbase Document

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.

GENIUS BRANDS INTERNATIONAL, INC.

Date: May 15, 2013

By: *<u>/s/ Klaus Moeller</u>*

Klaus Moeller, Chief Executive Officer