BIOLARGO, INC.
Form 10-Q
November 14, 2012

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

FORM 10-Q

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x QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2012.

or

¨ TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to
Commission File Number 000-19709

BIOLARGO, INC.
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	65-0159115 (I.R.S. Employer Identification No.)

16150 Heron Avenue
La Mirada, California 90638
(Address, including zip code, of principal executive offices)

(949) 643-9540
(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 or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ¨	Accelerated filer ¨
Non-accelerated filer ¨	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

The number of shares of the Registrant's Common Stock outstanding as of November 12, 2012 was 66,585,656 shares.

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PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

BIOLARGO, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS
AS OF DECEMBER 31, 2011 AND SEPTEMBER 30, 2012

	December 31, 2011	September 30, 2012 (unaudited)
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$128,498	$427,842
Accounts receivable, net of allowance	10,476	7,254
Inventory	61,865	52,331
Prepaid expenses	1,346	--
Total current assets	202,185	487,427
FIXED ASSETS		
Equipment, net	2,700	741
OTHER ASSETS	41,502	54,647
TOTAL ASSETS	$246,387	$542,815
LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)		
CURRENT LIABILITIES		
Accounts payable and accrued expenses	$706,688	$971,266
Convertible notes payable, current portion	670,410	413,775
Discount on convertible notes, current portion net ofamortization	(255,914)	(13,465)
Note payable	100,000	100,000
Deferred revenue	52,509	22,395
Customer deposit	100,000	100,000
Total Current Liabilities	1,373,693	1,593,971
LONG-TERM LIABILITIES		
Convertible notes payable, net of current portion	438,775	--
Discount on convertible notes, net of current portion and amortization	(48,484)	--
Total Long-term Liabilities	390,291	--

TOTAL LIABILITIES	1,763,984	1,593,971
COMMITMENTS, CONTINGENCIES AND SUBSEQUENT EVENTS (Note 12)		
STOCKHOLDERS' EQUITY (DEFICIT)		
Convertible Preferred Series A, $.00067 Par Value, 50,000,000 Shares Authorized, -0- Shares Issued and Outstanding, at December 31, 2011 and September 30, 2012.	—	—
Common Stock, $.00067 Par Value, 200,000,000 Shares Authorized, 59,242,220 and 66,310,618 Shares Issued, at December 31, 2011 and September 30, 2012.	39,737	44,495
Additional Paid-In Capital	65,907,960	69,982,637
Accumulated Deficit	(67,465,294)	(71,078,288)
Total Stockholders' Deficit	(1,517,597)	(1,051,156)
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)	$246,387	$542,815

See accompanying notes to unaudited condensed consolidated financial statements

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BIOLARGO, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE THREE AND NINE-MONTH PERIODS ENDED SEPTEMBER 30, 2011 AND 2012

	For the three-month periods ended September 30, 2011 (unaudited)	For the three-month periods ended September 30, 2012 (unaudited)	For the nine-month periods ended September 30, 2011 (unaudited)	For the nine-month periods ended September 30, 2012 (unaudited)
Revenue				
Licensing Fees	$ 109,720	$ --	$ 115,500	$ --
Product Sales	10,805	10,490	26,759	55,145
Total Revenue	120,525	10,490	142,259	55,145
Cost of goods sold	12,683	6,857	36,270	32,706
Gross profit (loss)	107,842	3,633	105,989	22,439
Costs and expenses				
Selling, general and administrative	580,507	828,354	2,453,038	3,064,792
Research and development	9,035	54,498	48,325	114,609
Amortization and depreciation	1,335	312	6,532	1,958
Total costs and expenses	590,877	883,164	2,507,895	3,181,359
Loss from operations	(483,035)	(879,531)	(2,401,906)	(3,158,920)
Interest expense, net	(228,639)	(36,137)	(642,088)	(454,074)
Net loss	$ (711,674)	$ (915,668)	$ (3,043,994)	$ (3,612,994)
Loss per common share – basic and diluted				
Loss per share	$ (0.01)	$ (0.01)	$ (0.06)	$ (0.06)
Weighted average common share equivalents outstanding	56,340,625	65,289,303	54,826,213	62,674,578

See accompanying notes to unaudited condensed consolidated financial statements

BIOLARGO, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY (DEFICIT)
FOR THE NINE-MONTH PERIOD ENDED SEPTEMBER 30, 2012
(UNAUDITED)

	Common Stock				
	Number of Shares	Par Value $.00067	Additional Paid-In Capital	Accumulated Deficit	Total
BALANCE DECEMBER 31, 2011	59,242,220	$ 39,737	$ 65,907,960	$ (67,465,294)	$ (1,517,597)
Conversion of a 2009 Spring Note and accrued interest obligations	1,340,820	898	736,553	—	737,451
Payment of accrued interest on Spring 2010 Notes	125,539	84	41,341	—	41,425
Conversion of a 2010 Spring Note and accrued interest obligations	47,017	32	27,002	—	27,034
Issuance of stock for cash received in Winter 2012 PPM	3,127,914	2,110	1,092,655	—	1,094,765
Issuance of stock for cash received in Summer 2012 PPM	1,925,214	1,295	768,791	—	770,086
Issuance of stock for cash received in Fall 2011 PPM	275,985	187	96,407	—	96,594
Issuance of stock for services to consultants and rent	225,908	152	88,346	—	88,498
Issuance of stock options to officer and Board of Directors	—	—	792,821	—	792,821
Issuance of stock options to consultants	—	—	334,876	—	334,876
Fair value of warrant extension	—	—	95,885	—	95,885
Net loss for the nine-month period ended September 30, 2012	—	—	—	(3,612,994)	(3,612,994)
BALANCE SEPTEMBER 30, 2012	66,310,618	$ 44,495	$ 69,982,637	$ (71,078,288)	$ (1,051,156)

See accompanying notes to unaudited condensed consolidated financial statements

BIOLARGO, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE NINE-MONTH PERIODS ENDED SEPTEMBER 30, 2011 AND 2012
(unaudited)

	For the nine-month periods ended September 30, 2011	2012
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Loss	$(3,043,994)	$(3,612,994)
Adjustments to Reconcile Net Loss to Net Cash Used in Operating Activities:		
Non-cash interest expense related to the amortization of the fair value of warrants issued in conjunction with our convertible notes	481,303	386,818
Non-cash expense related to options issued to officers and board of directors	135,905	779,821
Non-cash expense related to stock issued to our board of directors for settlement of obligations	163,998	—
Non-cash expense related to options issued to consultants	503,813	334,876
Non-cash expense related to stock issued to consultants	45,937	80,174
Amortization and depreciation expense	6,532	1,958
Increase (decrease) in cash from change in:		
Accounts receivable	5,882	3,222
Inventory	(61,616)	9,534
Prepaid expenses	2,469	1,346
Other assets	(26,345)	(13,145)
Accounts payable and accrued expenses	423,817	396,403
Deferred revenue	(54,652)	(30,114)
Customer deposits	82,500	—
Net Cash Used In Operating Activities	(1,334,451)	(1,662,101)
CASH FLOWS FROM INVESTING ACTIVITIES		
Funds used to purchase equipment	(3,740)	—
Net Cash Used In Investing Activities	(3,740)	—
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from the sale of stock	1,122,770	1,961,445
Payment of note payable	(20,000)	—
Net Cash Provided By Financing Activities	1,102,770	1,961,445
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(235,421)	299,344
CASH AND CASH EQUIVALENTS — BEGINNING	425,069	128,498
CASH AND CASH EQUIVALENTS — ENDING	$189,648	$427,842
SUPPLEMENTAL DISCLOSURES OF CASHFLOW INFORMATION		
Cash Paid During the Period for:		
Interest	$—	$—
Taxes	$4,868	$4,347

SUPPLEMENTAL DISCLOSURES OF NON-CASH OPERATING ACTIVITIES:		
Shares of the Company’s common stock issued for services:		
Consultant obligations	$—	$88,498
Board of Directors and officer obligations	$78,000	—
Option or warrant issued to purchase shares of the Company’s common stock:		
Consultant obligations	$192,834	$334,876
Board of Directors and officer obligations	$88,292	$792,821
SUPPLEMENTAL DISCLOSURES OF NON-CASH FINANCING AND INVESTING ACTIVITIES:		
Conversion of Noteholders to shares of the Company’s Common stock:		
Convertible Notes and related accrued interest	$989,676	$695,410
Convertible Noteholders’ accrued and unpaid interest	$191,402	$110,500
Fair value of warrant extension	$55,166	$95,885
Fees paid related to our private securities offerings	$--	$90,071

See accompanying notes to unaudited condensed consolidated financial statements

BIOLARGO, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

Note 1. Business and Organization

Outlook

The accompanying condensed consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities and commitments in the normal course of our business. As reflected in the accompanying financial statements, we had a net loss of $3,612,994 for the nine-month period ended September 30, 2012, and at September 30, 2012, we had negative working capital of $1,106,544, current assets of $487,427, and an accumulated stockholders' deficit of $71,078,288. The foregoing factors raise substantial doubt about our ability to continue as a going concern. Ultimately, our ability to continue as a going concern is dependent upon our ability to attract significant new sources of capital, attain a reasonable threshold of operating efficiencies and achieve profitable operations by licensing or otherwise commercializing products incorporating our BioLargo technology. The financial statements do not include any adjustments that might be necessary if we are unable to continue as a going concern.

We have been, and anticipate that we will continue to be, limited in terms of our capital resources. Our total cash and cash equivalents were $427,842 at September 30, 2012. We generated revenues of $55,145 in the nine-month period ended September 30, 2012, which amount was not sufficient to fund our operations. We generally have not had enough cash or sources of capital to pay our accounts payable and expenses as they arise, and have relied on the issuance of stock options and common stock, as well as extended payment terms with our vendors, consultants and officers, to continue to operate. We will be required to raise substantial additional capital to expand our operations, including without limitation, hiring additional personnel, additional scientific and third-party testing, costs associated with obtaining regulatory approvals and filing additional patent applications to protect our intellectual property, and possible strategic acquisitions or alliances, as well as to meet our liabilities as they become due for the next 12 months.

As of September 30, 2012, we had $513,775 aggregate principal amount outstanding on various promissory notes. We may pay the principal and interest due on these notes in cash or in stock, at our option, at maturity. In addition, as of September 30, 2012, we had $971,266 of outstanding accounts payable and accrued expenses, of which $43,395 relates to interest due on outstanding promissory notes, and $927,871 relates to accrued and unpaid payables. (See Note 10.)

During the nine-month period ended September 30, 2012, we received gross proceeds of $1,961,445 pursuant to our private securities offerings. (See Note 5.)

In the opinion of management, the accompanying condensed consolidated balance sheets and related condensed consolidated statements of operations, cash flows, and stockholders' equity include all adjustments, consisting only of normal recurring items, necessary for their fair presentation in conformity with accounting principles generally accepted in the United States of America. Preparing financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, and expenses. Actual results and outcomes may differ from management's estimates and assumptions. Estimates are used when accounting for stock-based transactions, account payables and accrued expenses and taxes, among others.

The unaudited condensed consolidated financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and pursuant to Rule 8-03 of Regulation S-X under the Securities Act of 1933, as amended. Accordingly, they do not include all of the information and notes required by generally accepted accounting principles for annual financial statements. In the opinion of management, all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair presentation have been included. We are still operating in the early stages of the sales and distribution process, and therefore our operating results for the nine-month period ended September 30, 2012 are not necessarily indicative of the results that may be expected for the year ended December 31, 2012, or for any other period. These unaudited condensed consolidated financial statements and notes should be read in conjunction with the Company's audited financial statements and accompanying notes included in the Annual Report on Form 10-K for the year ended December 31, 2011 filed with the Securities and Exchange Commission (the "SEC").

BIOLARGO, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

Note 2. Summary of Significant Accounting Policies

Inventory

Inventories are stated at the lower of cost or net realizable value using the average cost method. Inventories consisted of:

	December 31, 2011	September 30, 2012
Raw materials	$27,556	$37,069
Finished goods (see Note 4)	34,309	15,262
Total inventory	$61,865	$52,331

Equipment

Equipment is carried at cost and depreciated using the straight-line method over the estimated useful lives of the assets, which is three years. Equipment is stated on the balance sheet net of accumulated depreciation of $29,728 and $31,686 as of December 31, 2011 and September 30, 2012, respectively.

Other Assets

"Other Assets" consists of payments made to secure the patent rights to continue our efforts in commercializing the ISAN system.

We review long-lived assets using our best estimates based on reasonable assumptions and projections. An impairment loss to write such assets down to their estimated fair values is necessary if the carrying values of the assets exceed their related undiscounted expected future cash flows. We also determine impairment whenever events or changes in circumstances indicate that their carrying values may not be recoverable.

Stock Options and Warrants Issued for Services

All share-based payments to employees, including grants of employee stock options, are recognized in the financial statements based on their fair values.

For stock issued to consultants and other non-employees for services, we record the expense based on the fair market value of the securities as of the date of the stock issuance. The issuance of stock warrants or options to non-employees are valued at the time of issuance utilizing the Black Scholes calculation and the amount is charged to expense.

Non-Cash Transactions

We have established a policy relative to the methodology to determine the value assigned to each intangible we acquire, and/or services or products received for non-cash consideration of our common stock. The value is based on the market price of our common stock issued as consideration, at the date of the agreement of each transaction or when the service is rendered or product is received.

The methods, estimates and judgments we use in applying these most critical accounting policies have a significant impact on the results of our financial statements.

BIOLARGO, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

Revenue Recognition

Revenues are recognized as risk and title to products transfers to the customer (which generally occurs at the time shipment is made), the sales price is fixed or determinable, and collectability is reasonably assured. We also may generate revenues from royalties and license fees from our intellectual property. Licensees typically pay a license fee in one or more installments and ongoing royalties based on their sales of products incorporating or using our licensed intellectual property. License fees are recognized over the estimated period of future benefit to the average licensee.

Earnings (Loss) Per Share

We report basic and diluted earnings (loss) per share (“EPS”) for common and common share equivalents. Basic EPS is computed by dividing reported earnings by the weighted average shares outstanding. Diluted EPS is computed by adding to the weighted average shares the dilutive effect if stock options and warrants were exercised into common stock. For the nine-month periods ended September 30, 2011 and 2012, the denominator in the diluted EPS computation is the same as the denominator for basic EPS due to the anti-dilutive effect of the warrants and stock options on the Company’s net loss.

Recent Accounting

There was no recent accounting guidance issued where the adoption would have a material effect on our condensed consolidated financial statements.

Note 3. Customer Deposit

On March 24, 2011, we entered into a contract in which Central Garden & Pet Company (“Central”) was granted the exclusive worldwide right and license to sell, market, offer for sale, distribute import, export, and otherwise exploit products that contain the BioLargo technologies in the “pet supplies industry” (which is defined in the agreement, and does not include products for equine or livestock). The agreement provided that we are the exclusive provider of the product containing the BioLargo technologies, other than in certain limited conditions. The rights granted to Central are exclusive so long as Central meets “minimum purchase requirements” of product from the Company, as set forth in the agreement. The agreement terminates only upon uncured breach of material warranty or obligation.

Pursuant to the Central contract, we received a $100,000 deposit which will be credited against future orders. The Company has agreed to sell product to Central at a price equal to the manufacturing cost plus a “manufacturer’s margin”, in an amount to be agreed upon by the parties for each particular product. Central agreed to include a BioLargo trademark on the packaging of any products containing the BioLargo technologies.

Central shall have a right of first refusal to purchase Odor-No-More, Inc., or the Odor-No-More brand and/or intellectual property. The Company shall give notice of receipt of any offer to purchase, and Central may elect to match the terms of the offer. Central also has the right of first offer to acquire the right to commercialize new products based on BioLargo technologies in the “pet supplies industry”, following notice from the Company and a 90 day due diligence period. If Central declines to commercialize any such new product, the Company is free to commercialize such products under its own brand, but not under a third party’s brand.

The agreement also contains standard provisions typical of a license and supply agreement.

Through the date of the filing of this Quarterly Report, no product orders were received under the Central contract.

BIOLARGO, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

Note 4. Deferred Revenue

Horn Warehouse

Our distribution partner, Horn (formerly the E.T. Horn Company), warehouses our product and makes it available to us for later sales, and thus for revenue recognition purposes, certain sales to Horn are deferred until such time as the product is sold to retailers and/or end-users. As of September 30, 2012, a balance of $22,395 relating to the sale of Odor-No-More product to Horn remains as deferred revenue.

Sublicense to Isan USA

On March 29, 2010, we entered into a sublicense agreement (the “Isan USA Sublicense”) with Isan USA, Inc. (“Isan USA”) which grants Isan USA the exclusive rights to use, exploit, develop and commercialize the Isan System Technology in the United States, in particular fields of use. Pursuant to the Isan USA Sublicense, Isan USA paid to BioLargo a $100,000 initial license fee plus additional payments of $23,000. Of the amounts received from Isan USA, $109,720 was considered deferred revenue as of June 30, 2011. Isan USA was unable to secure financing, and has ceased making the monthly payments required by the Isan USA Sublicense agreement. Given the failure of Isan USA to secure financing, on August 12, 2011 we and Isan USA mutually agreed to terminate the Isan USA Sublicense. The remaining Isan USA deferred revenue balance of $109,720 was recorded as revenue during the three-month period ended September 30, 2011.

Note 5. Private Securities Offerings

Summer 2012 Offering

Pursuant to a private offering of our common stock at a price of $0.40 per share that commenced May 2012 (the “Summer 2012 Offering”), through September 30, 2012, we sold 1,925,214 shares of our common stock at $0.40 per share to seven accredited investors and received $770,086 gross, $744,515 net proceeds from the sales. Of these amounts, 1,147,500 shares were sold and $459,000 was received during the three-month period ended September 30, 2012. Each purchaser of stock in the Summer 2012 Offering will receive, for no additional consideration, a stock purchase warrant (the “Summer 2012 Warrant”) entitling the holder to purchase the same number of shares as purchased in the offering, for $0.55 per share until March 31, 2014. Subsequent to September 30, 2012, we amended the terms of this offering to lower the price per share and warrant exercise price (see Note 12 “Subsequent Events).

Winter 2012 Offering

Pursuant to a private offering of our common stock at a price of $0.35 per share that commenced January 2012 and closed May 2012 (the “Winter 2012 Offering”), we sold 3,127,914 shares of our common stock at $0.35 per share to 30 accredited investors and received $1,094,765 gross; $1,030,265 net proceeds from the sales.

Each purchaser of stock in the Winter 2012 Offering received, for no additional consideration, a stock purchase warrant (the “Winter 2012 Warrant”) entitling the holder to purchase the same number of shares as purchased in the offering, for $0.50 per share until January 31, 2013. (See Note 7.)

Fall 2011 Offering

Pursuant to a private offering of our common stock at a price of $0.35 per share that commenced September 2011 (the "Fall 2011 Offering"), we received subscriptions of $467,317 from 16 accredited investors for the purchase of an aggregate 1,335,201 shares of our common stock at $0.35 per share. In the year ended December 31, 2011, we received $370,723 gross proceeds and issued 1,059,215 shares of our common stock. In January 2012 we received the remaining $96,594 from subscriptions committed prior to the termination of the offering and issued 275,986 shares of our common stock.

Each purchaser of stock in the Fall 2011 Offering received, for no additional consideration, a stock purchase warrant (the "Fall 2011 Warrant") entitling the holder to purchase the same number of shares of common stock for $0.50 per share until December 31, 2012. (See Note 7.)

BIOLARGO, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

Winter 2011 Offering

Pursuant to a private offering of our common stock at a price of $0.35 per share that commenced January 2011 and terminated June 2011 (the "Winter 2011 Offering") we sold 2,765,070 shares of our common stock at $0.35 per share and received $967,768 gross proceeds from the sales.

Spring 2010 Offering

Pursuant to a private offering that commenced January 2010 (the "Spring 2010 Offering") and terminated July 2010, we sold $438,775 of our 10% convertible notes (the "Spring 2010 Notes"), which are due and payable on April 15, 2013, to 18 investors, the principal amount of which is convertible into an aggregate 763,235 shares of our common stock, at $0.575 per share. The Spring 2010 Notes can be converted voluntarily by the noteholder at any time prior to the maturity date. We can unilaterally convert the Spring 2010 Notes (i) on or after July 31, 2010, if we have received one or more written firm commitments, or have closed on one or more transactions, or a combination of the foregoing, of at least $3 million gross proceeds of equity or debt; or (ii) on the maturity date. Accordingly, the Spring 2010 Notes may be repaid in cash or may be converted, at our sole option, into shares of our common stock, on or before the April 15, 2013 maturity date.

Each purchaser of the Spring 2010 Notes received, for no additional consideration, two stock purchase warrants, each of which entitle the holder to purchase the number of shares of our common stock into which the holder's Spring 2010 Note is initially convertible. The first warrant (the "Spring 2010 Eighteen Month Warrant") was exercisable at a price of $0.75 per share and expired unexercised on July 15, 2011. The second warrant (the "Spring 2010 Thirty-Six Month Warrant") is exercisable at a price of $1.00 per share and expires on January 15, 2013. (See Note 7.)

All of these offerings and sales were made in reliance on the exemption from registration contained in Section 4(2) of the Securities Exchange Act and/or Regulation D promulgated thereunder as not involving a public offering of securities.

Note 6. Conversion of Notes

Spring 2010 Notes

On February 6, 2012, a holder of a convertible promissory note issued in our Spring 2010 Offering (see Note 5) elected to convert the principal balance of $25,000 and accrued unpaid interest of $2,034 into an aggregate 47,017 shares of our common stock, at a conversion price of $0.575.

Spring 2008 Notes

On March 31, 2011, per the terms of the Spring 2008 Notes, we elected to convert the remaining aggregate principal balance of $913,625 and $76,051 of accrued and unpaid interest into an aggregate 733,108 shares of our common stock at a conversion price of $1.35 per share.

Spring 2009 Notes

On their June 1, 2012 maturity date, we elected to convert the remaining aggregate principal balance of $670,410 and $67,041 of accrued and unpaid interest of our Spring 2009 Notes into an aggregate 1,340,820 shares of our common stock at a conversion price of $0.55 per share. As a result, the Spring 2009 Notes are fully paid.

On April 16, 2011, the holder of a note issued in our Spring 2009 Offering elected to convert the principal balance of $11,000, and accrued unpaid interest of $964, into an aggregate 21,754 shares of our common stock, at a conversion price of $0.55.

All of these offerings and sales were made in reliance on the exemption from registration contained in Section 4(2) of the Securities Exchange Act and/or Regulation D promulgated thereunder as not involving a public offering of securities.

BIOLARGO, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

Note 7. Warrants

We have certain warrants outstanding to purchase our common stock, at various prices, as described in the following tables:

	Number of Shares		Price Range
Outstanding as of December 31, 2010	6,894,215	$	0.125– 2.00
Issued	1,089,630	$	0.50– 0.75
Exercised	—	$	—
Expired	(2,403,922)	$	0.75– 2.00
Outstanding as of September 30, 2011	7,156,377	$	0.125– 2.00

	Number of Shares		Price Range
Outstanding as of December 31, 2011	7,280,683	$	0.125 –1.00
Issued	8,158,449	$	0.40 –1.00
Exercised	—	$	—
Expired	—	$	—
Outstanding as of September 30, 2012	15,439,132	$	0.125 –1.00

To determine interest expense related to our outstanding warrants issued in conjunction with debt offerings, the fair value of each award grant is estimated on the date of grant using the Black-Scholes option-pricing model and the calculated value is amortized over the life of the warrant. The determination of expense of warrants issued for services or settlement also uses the option-pricing model. The principal assumptions we used in applying this model were as follows:

	2011	2012
Risk free interest rate	1.87%	0.57%
Expected volatility	558%	489%
Expected dividend yield	N/A	N/A
Forfeiture rate	N/A	N/A
Expected life in years	3.00	5

The risk-free interest rate is based on U.S Treasury yields in effect at the time of grant. Expected volatilities are based on historical volatility of our common stock. The expected life in years is presumed to be the mid-point between the vesting date and the end of the contractual term.

Warrants issued as part of our Convertible Notes

We recorded $481,303 and $386,818 of non-cash interest expense related to the amortization of the fair value of warrants issued in conjunction with our convertible notes for the nine-month periods ended September 30, 2011 and

2012, respectively. These expenses related to convertible notes issued in our Spring 2010 and Spring 2009 offerings. We have not issued convertible notes since that time.

BIOLARGO, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

Warrant Extension

On June 1, 2012, the expiration date of the Spring 2009 Three-Year Warrant was extended nine months from June 1, 2012 to March 1, 2013. The fair value of the extension was an aggregate $95,885 and was recorded as interest expense upon issuance.

Summer 2012 Warrants

Pursuant to the terms of our Summer 2012 Offering (see Note 5), from inception of May 2012 through September 30, 2012, we issued warrants to purchase up to an aggregate 1,925,214 shares of our common stock to the investors in the Offering. These warrants are set to expire on March 31, 2014 and have an exercise price of $0.55 per share.

Winter 2012 Warrants

Pursuant to the terms of our Winter 2012 Offering (see Note 5), during the nine-month period ended September 30, 2012, we issued warrants to purchase up to an aggregate 3,127,914 shares of our common stock to the investors in the Offering. These warrants are set to expire on January 31, 2013 and have an exercise price of $0.50 per share. Subsequent to September 30, 2012, we lowered the exercise price of the warrants issued in this offering (see Note 12 “Subsequent Events).

Fall 2011 Warrants

Pursuant to the Fall 2011 Offering (see Note 5), we issued to the investors warrants to purchase an aggregate 1,335,201 shares of our common stock at $0.50 per share, which warrants are set to expire on December 31, 2012. Of that amount, in the year ended December 31, 2011, we issued warrants to purchase an aggregate 1,059,215 shares of our common stock, and in the nine-month period ended September 30, 2012, we issued warrants to purchase an aggregate 275,986 shares of our common stock.

Fall 2008 Warrants Extension

Pursuant to the terms of the Fall 2008 Offering, we issued “three-year” warrants to purchase up to an aggregate 1,446,000 shares at an exercise price of $1.00 per share (initially issued at $2.00 per share). On September 28, 2011, we extended the expiration date of the Fall 2008 Three-year Warrant by one year from October 15, 2011 to October 15, 2012 resulting in a fair value of $180,172. Of this amount, $30,029 was expensed during 2011 and the remaining $150,143 was recorded as interest expense during the three-month period ended March 31, 2012.

Other Warrants

On July 23, 2012, we issued a warrant to a consultant for services provided to purchase up to an aggregate 250,000 shares of our common stock at an exercise price of $0.40 per share, resulting in a fair value of $67,500. Of this amount $45,900 was recorded as selling, general and administrative expense during the three-month period September 30, 2012 and the remaining will be expensed ratably over the four-month vesting schedule. The warrant expires July 23, 2017.

On May 11, 2011, we issued a warrant to consultants for services provided to purchase up to an aggregate 183,545 shares of our common stock at an exercise price of $0.55 per share, resulting in a fair value of $100,950, which was recorded as selling, general and administrative expense during the three-month period June 30, 2011.The warrant expires May 11, 2016.

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Note 8. Stockholders’ Equity

Preferred Stock

Our certificate of incorporation authorizes our Board of Directors to issue preferred stock, from time to time, on such terms and conditions as they shall determine. As of December 31, 2011 and September 30, 2012 there were no outstanding shares of our preferred stock.

Common Stock

As of December 31, 2011 and September 30, 2012 there were 59,242,220 and 66,310,618 shares of common stock outstanding, respectively. The increase in shares during the nine-month period ended September 30, 2012 is comprised of the following stock issuances: (i) 1,340,820 shares of our common stock related to the conversion of our Spring 2009 Notes and related accrued and unpaid interest, (ii) 125,539 shares of our common stock related to the conversion of Spring 2010 Notes accrued and unpaid interest, (iii) 47,017 shares of our common stock as payment of a noteholder of our Spring 2010 Notes and related accrued interest, (iv) 3,127,914 shares of our common stock issued to investors in our Winter 2012 Offering, (v) 1,925,214 shares of our common stock issued to investors in our Summer 2012 Offering, (vi) 275,986 shares of our common stock issued to investors in our Fall 2011 Offering (vii) 225,908 shares as payment to consultants in lieu of accrued and unpaid obligations.

Note 9. Stock-Based Compensation and Other Employee Benefit Plans

2007 Equity Incentive Plan

On August 7, 2007, our Board of Directors adopted the BioLargo, Inc. 2007 Equity Incentive Plan, as amended April 29, 2011 (“2007 Plan”), as a means of providing our directors, key employees and consultants additional incentive to provide services. Both stock options and stock grants may be made under this plan. The Compensation Committee administers this plan. The 2007 Plan allows grants of common shares or options to purchase common shares. As plan administrator, the Compensation Committee has sole discretion to set the price of the options. The Compensation Committee may at any time amend or terminate the plan.

Extension of Options

On April 27, 2009, in an effort to preserve the Company’s cash and reduce outstanding payables, the Board offered to third parties, officers and board members an option (“Option”) to purchase common stock in lieu of cash payment to reduce amounts owed by the Company. The Options were issued pursuant to the Company’s 2007 Equity Incentive Plan with an exercise price of $0.50 cents a share, an amount which was $0.20 per share above the $0.30 per share closing price of the Company’s common stock on April 27, 2009, and had an expiration date of April 27, 2012. The Options issued to Board members Dennis P. Calvert and Kenneth R. Code were issued at an exercise price of $0.55 per share. In consideration of the circumstances in which the Options were issued, and the fact that the price of the Company’s common stock was less than the strike price of the Options, the Board extended the expiration date of the Options by a period of seven years, to expire on April 27, 2019. The fair value of the Option totaled $684,171 and was recorded as selling, general and administrative expense.

Vesting of Options

During the nine-month period ended September 30, 2012, a portion of the option to purchase 300,000 shares of common stock issued to our Chief Financial Officer in exchange for his services pursuant to the April 2012 extension of his engagement agreement vested, resulting in $70,000 of selling, general and administrative expense.

During the nine-month period ended September 30, 2012, a portion of the unvested options issued to consultants vested, resulting in $147,869 of selling, general and administrative expense.

Issuance of Options

During the nine-month period ended September 30, 2012, we recorded the issuance of an option to purchase an aggregate 46,667 shares of our common stock to our independent member of our Board of Directors, pursuant to the terms of the 2007 Equity Plan which calls for an automatic issuance of an option to any new independent director. The option vests after a period of one year from the date of grant, expires ten years from the date of issuance, and 6,667 is exercisable at $0.34 per share and 40,000 shares is exercisable at $0.32 per share, the price of our common stock on the grant date. The fair value of this option totaled $15,067 and was recorded as selling, general and administrative expense.

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On July 5, 2012, our independent board members were issued options to purchase an aggregate 435,161 shares of our common stock at $0.40 per share in exchange for a reduction of $104,439 in accrued and unpaid obligations for their services on the board of directors. The share price of our common stock on July 5, 2012 was $0.32 per share. These options are fully vested and expire ten years from the date of issuance, July 5, 2022. The fair value of the options was an aggregate $152,585, resulting in additional $48,146 of selling, general and administrative expense in the three-month period September 30, 2012.

On July 18, 2012, an option was issued to a consultant, in accordance with the service agreement, to purchase an aggregate 200,000 shares of our common stock. Of this amount 50,000 vested upon issuance exercisable at $0.50 per share; 50,000 vest January 18, 2013 at an exercise price of $0.75 per share; 50,000 vest July 18, 2013 at an exercise price of $1.00 per share; and the remaining 50,000 vest January 18, 2014 at an exercise price of $1.25 per share. The share price of our common stock on the date of issuance was $0.28 per share and resulted in a fair value of $56,000, of which $14,000 was recorded as selling, general and administrative expense during the three-month period ended September 30, 2012, and the remaining will be expensed ratably per the vesting schedule. These options expire ten years from the date of issuance, July 18, 2022.

Activity for our stock options under the 2007 Plan for the nine-month periods ended September 30, 2011 and 2012 is as follows:

As of September 30, 2011:	Options Outstanding	Shares Available	Price per share	Weighted Average Price per share
Balances as of December 31, 2010	4,797,223	1,202,777	$ 0.25 – 1.89	$ 0.51
Amendment to increase	—	6,000,000	—	—
Granted	1,805,593	(1,805,593)	$ 0.39 – 0.51	$ 0.43
Exercised	—	—	—	—
Expired	—	—	—	—
Balances as of September 30, 2011	6,602,816	5,397,184	$ 0.25 – 1.89	$ 0.49

As of September 30, 2012:	Options Outstanding	Shares Available	Price per share	Price per share
Balances as of December 31, 2011	7,739,258	4,260,742	$ 0.25 – 1.89	$ 0.45
Granted	981,828	(981,828)	0.34 – 0.35	0.35
Exercised	—	—	—	—
Expired	—	—	—	—
Balances as of September 30, 2012	8,721,086	3,278,914	$ 0.25 – 1.89	$ 0.45

We recognize compensation expense for stock option awards on a straight-line basis over the applicable service period of the award, which is the vesting period. Share-based compensation expense is based on the grant date fair value estimated using the Black-Scholes Option Pricing Model. The following methodology and assumptions were used to calculate share based compensation for the nine-month period ended September 30:

2007 Plan

	2011	2012
Risk free interest rate	2.08 – 2.82 %	1.45%
Expected volatility	906 %	951%
Expected dividend yield	—	—
Forfeiture rate	—	—
Expected life in years	5	7

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Expected price volatility is the measure by which our stock price is expected to fluctuate during the expected term of an option. Expected volatility is derived from the historical daily change in the market price of our common stock, as we believe that historical volatility is the best indicator of future volatility.

The risk-free interest rate used in the Black-Scholes calculation is based on the prevailing U.S Treasury yield as determined by the U.S. Federal Reserve. We have never paid any cash dividends on our common stock and do not anticipate paying cash dividends on our common stock in the foreseeable future.

We recognize compensation expense for stock option awards on a straight-line basis over the applicable service period of the award, which is the vesting period. Share-based compensation expense is based on the grant date fair value estimated using the Black-Scholes Option Pricing Model. Historically, we have not had significant forfeitures of unvested stock options granted to employees and Directors. A significant number of our stock option grants are fully vested at issuance or have short vesting provisions. Therefore, we have estimated the forfeiture rate of our outstanding stock options as zero.

Note 10. Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses included the following:

	December 31, 2011	September 30, 2012
Accounts payable and accrued expenses	$ 448,177	$ 522,870
Accrued interest	86,720	43,395
Officer and Board of Director Payables	171,791	405,001
Total Accounts Payable and Accrued Expenses	$ 706,688	$ 971,266

Payment of Consultant Fees

On January 31, 2012, we issued an aggregate 30,147 shares of our common stock, at a conversion price of $0.31, in lieu of $9,225 of rent expense.

On March 6, 2012, we issued 100,000 shares of our common stock at a conversion price of $0.35 per share, and recorded $35,000 of selling, general and administrative expense to a consultant in exchange for research and marketing services.

On July 1, 2012, we issued 80,000 shares of our common stock at a conversion price of $0.35 per share, and recorded $28,000 of selling, general and administrative expense to a consultant in exchange for research and marketing services.

On September 5, 2012 we issued 15,761 shares of our common stock at a conversion price of $0.31 per share, and recorded $4,693 of selling, general and administrative expense to a consultant in exchange for research and marketing services.

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Payment of Accrued Interest

On April 15, 2012, in accordance with terms of the Spring 2010 Notes (see Note 5), we paid accrued interest of $41,425 by the issuance of 125,539 shares of our common stock, at a conversion price of $0.33 per share, to the holders of the Spring 2005 Notes.

All of these offerings and sales were made in reliance on the exemption from registration contained in Section 4(2) of the Securities Exchange Act and/or Regulation D promulgated thereunder as not involving a public offering of securities.

Note 11. Notes Payable

On June 8, 2010, we received $100,000 and issued a promissory note with an initial maturity date of December 3, 2010, which accrues interest at a rate of 10%. The noteholder, for no additional consideration, received a stock purchase warrant entitling the holder to purchase 50,000 shares of our common stock, exercisable at $0.50 per share until June 3, 2013. (See Note 7.) The maturity date of the note was extended to December 3, 2011, and again, to December 3, 2012.

On August 3, 2009, we received $70,000 and issued a promissory note with a maturity date of October 31, 2009 which accrued interest at a rate of 10%. On October 31, 2009 the maturity date of this promissory note was extended to February 1, 2010. The maturity date was further extended to December 1, 2010, and in March 2010 a $20,000 payment on the note was made. On December 31, 2010 we converted $30,000 principal balance into an aggregate 100,000 shares of our common stock at $0.30, and agreed to extend the maturity date to March 1, 2011. On March 1, 2011, we paid the remaining principal amount of $20,000, and $9,590 of accrued interest, in full satisfaction of the note.

For the nine-month periods ended September 30, 2011 and 2012 we recorded $7,583 and $7,611 of interest expense related to these notes payable.

Note 12. Subsequent Events.

Management has evaluated subsequent events through the date of the filing of this Quarterly Report and management noted the following for disclosure.

Summer 2012 Offering

On October 23, 2012, we amended the terms of the Summer 2012 Offering (see Note 5) by reducing the price of the common stock sold from 40 cents to 35 cents, and reducing the exercise price of the Summer 2012 Warrant from 55 cents to 50 cents. As a result, we issued an additional 275,038 shares of common stock to the investors, and issued those investors amended warrants reflecting the new share amount and new exercise price.

Options issued under 2007 Equity Plan

On October 2, 2012, our independent board members were issued options to purchase an aggregate 168,750 shares of common stock at $0.40 cents per share in exchange for a reduction of $45,000 in accrued and unpaid obligations for their services on the board of directors.

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

This Quarterly Report on Form 10-Q of BioLargo, Inc. (the "Company") contains forward-looking statements. These forward-looking statements include predictions regarding, among other things:

- our business plan;
- the commercial viability of our technology and products incorporating our technology;
- the effects of competitive factors on our technology and products incorporating our technology;
- expenses we will incur in operating our business;
- our ability to end persistent operating losses and generate positive cash flow and operating income;
- our ability to identify potential applications of our technology in industries other than the animal health industry and to bring viable products to market in such industries;
- the application of our technology in the food and beverage industry;
- the willingness of other companies to incorporate our technology into new or existing products or services and provide continued support for such products or services;
- the ability of our licensees to successfully produce, advertise and market products incorporating our technology;
- the continued success and viability of our licensees holding the exclusive right to exploit our technology in particular fields;
- the sufficiency of our liquidity and working capital;
- our ability to finance product field testing, hiring of personnel, required regulatory approvals, and needed patent applications;
- continued availability and affordability of resources used in our technology and the production of our products and services; and
- whether we are able to complete additional capital or debt financings in order to continue to fund operations and continue as a going concern.

You can identify these and other forward-looking statements by the use of words such as "may", "will", "expects", "anticipates", "believes", "estimates", "continues", or the negative of such terms, or other comparable terminology. Forward-looking statements also include the assumptions underlying or relating to any of the foregoing statements.

Such statements, which include statements concerning future revenue sources and concentrations, selling, general and administrative expenses, research and development expenses, capital resources, additional financings and additional losses, are subject to risks and uncertainties, including, but not limited to, those discussed elsewhere in this Form 10-Q, that could cause actual results to differ materially from those projected.

Our actual results could differ materially from those anticipated in these forward-looking statements as a result of various factors, including those set forth under the heading "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2011. Unless otherwise expressly stated herein, all statements, including forward-looking statements, set forth in this Form 10-Q are as of September 30, 2012, unless expressly stated otherwise, and we undertake no duty to update this information.

As used in this Report, the term Company refers to BioLargo, Inc., a Delaware corporation, and its wholly-owned subsidiaries, BioLargo Life Technologies, Inc., a California corporation, Odor-No-More, Inc., a California corporation, and Clyra Medical Technologies, Inc., a California corporation.

The following discussion and analysis should be read in conjunction with our unaudited condensed consolidated financial statements and the related notes to the consolidated financial statements included elsewhere in this report.

Overview

By leveraging our suite of patented and patent-pending intellectual property, which we refer to as the BioLargo technology, our business strategy is to harness and deliver nature's best disinfectant – iodine – in a safe, efficient, environmentally sensitive and cost-effective manner. The centerpiece of our BioLargo technology is CupriDyne®, which works by combining minerals with water from any source and delivering "free-iodine" on demand, in controlled dosages, in order to balance efficacy of disinfectant or odor control performance with concerns about toxicity.

Our BioLargo technology delivers "Nature's Best Solution®" – iodine – to an array of problems, including odor and moisture control, disinfection, wound healing and contaminated water. Our technology enables us to deliver precise dosing of iodine in a variety of physical forms and delivery systems, which often include the combination of chemical reagents with other materials. We primarily focus on developing uses and/or applications for our technology for its use in products, in order for us to secure a licensing and/or supplier agreement with other companies, that will in turn, sell services or products to their customers within a specific industry segment. We believe that we should continually work to advance proofs of claims and commercial validations wherever possible to support our fundamental licensing strategy and improve the perceived value of our technology to potential licensees.

Armed with a solution to specific industry problems, our BioLargo technology has potential commercial applications within global industries, including animal health, oil and gas extraction, agriculture and livestock, beach and soil environmental remediation, consumer products, food processing, medical, and water industries. While we believe the potential applications are many, we have thus far commercially launched products in only one area -- the animal health industry, under the brand name "Odor-No-More". In March 2011, we entered into an exclusive license and supply agreement with Central Garden & Pet Company ("Central"), the industry leading producer of premium pet products in the United States. Many of Central's product brands are the industry leader and household names with more than 20 years of history, including Kaytee, Nylabone, Four Paws, and others. In September 2012, Central introduced our Odor-No-More cat litter additive to pet store retailers at SuperZoo 2012. Since that time, we have retained professionals to advise us in our marketing efforts and we are actively developing a comprehensive marketing plan and refined product messaging that focuses on developing consumer awareness to encourage increased acceptance across various media outlets and that can support numerous selling channels.

While we continue to advance our efforts to market and sell our Odor-No-More products, with the addition of key industry experts to our team, we are also actively seeking opportunities for product sales or licensing in the oil and gas industry, the food processing industry, and the medical products industry. We are in discussions with leading researchers that serve the food and agriculture industry to conduct a series of trials for both the Isan Sytem and Cupridyne based systems to help meet specific targeted needs within those industries. We hope to begin this work as soon as possible.

In December 2011 we announced that we had been selected as a founding member of a Canadian Natural Sciences and Engineering Research Council ("NSERC") "research chair", joined by globally leading oil companies, the regional water district in Alberta Canada and the University of Alberta. The Chair was formed to solve the contaminated water and tailings ponds problems associated with the oil sands industry and commenced in December of last year. The Canadian Oil Sands are the second largest deposit of oil in the world. Extracting oil from the Oil Sands creates high volumes of contaminated water (between 2 and 4.5 barrels of water to produce one barrel of synthetic crude oil), currently discharged in "tailings" ponds, sometimes for years, to separate the solids from the liquids for eventual recycling or safe discharge into the environment. With Canadian oil production estimated to increase from 1.9 million to over 6 million barrels of oil a day over the next 20 years, the released water from oil sands operations is estimated to reach one billion cubic meters in the Athabasca oils sands region by 2025. An innovative solution that can reduce the water treatment time, and thus the overall footprint and environmental impact of the tailings ponds, is required for Canada to meet its production goals. It is widely believed that the future of oil sands exploration, its social and economic contribution as the second largest oil reserve in the world, and its contribution to the public good of both Canada and the Unites States, hinges on industry's ability to manage the wastewater in tailings ponds. Our Chief Science Officer continues to support the efforts at the University of Alberta on a direct and active basis. We believe our work with the Chair is important for this industry, both the Canadian and Unites States national interests, and could impact the global industry as the Chair was organized to develop sustainable solutions for managing these natural resources and the associated water issues. We expect technical publications by the researchers in the near future.

In February 2011, we added to our team a recognized industry water treatment expert, Harry DeLonge. Having spent more than 40 years at Pepsi-Cola International, Mr. DeLonge is assisting us in our efforts to commercialize our BioLargo technology in the food and beverage industry. Within the food and beverage industry, we believe the BioLargo technologies are useful in a number of applications, including “clean-in-place” related uses, treating processed and wastewater, and for enhancing performance of certain filter and water treatment technologies. In addition, we believe that we have a cost effective solution for managing dangerous and/or odorless compounds common with this industry. Our efforts to develop new patents and other intellectual property, advancing proof of claim, pilot projects and seeking customers and/or licensing partners are continuing throughout 2012.

In August of 2011, we added a medical products expert to our management team to develop and exploit commercial opportunities within the medical industry. Since that time, in addition to organizing an internal team to champion products in this segment, we have developed prototype wound care and medical-use products incorporating our BioLargo technology for evaluation and proving basic product claims. We have engaged third party labs to validate basic product claims, and have successfully verified that our newly developed products meet required safety and efficacy benchmarks according to industry specific standards. This work is continuing as we refine and optimize our product designs. In May 2012, we formed a wholly owned subsidiary for the purpose of commercializing medical products, and have since retained the services of Tanya Rhodes, a former Vice President at Smith & Nephew, to assist in the efforts. We are actively engaged in discussions with potential strategic partners about forming a business relationship to initiate the required regulatory applications and ultimately introduce new products to market, but have also determined, based on the substantial work that has been accomplished by our team, to now take the necessary steps to fully develop market-ready wound care products, including obtaining required regulatory approvals as soon as we are able. As a result, we are currently negotiating with contract manufacturers to finalize specific product specifications and technical validations for the purposes of finalizing the claims and product designs in anticipation of making an FDA application for requisite approvals which are targeted for mid-2013.

Throughout 2012, we have continued our product development, formulation refinement and test marketing for a number of animal-health related products in the equine and pet industries. We believe the work in this area is complimented by our technical advances and proofs of claims for products associated with human wound care and that many of these animal health care products could be ready for market in early to mid-2013 depending on our human and financial resources and our capability.

Results of Operations—Comparison of the three and nine-month periods ended September 30, 2012 and 2011

Revenue

We generated $10,490 and $55,145 in revenues from product sales during the three and nine-month periods ended September 30, 2012 and revenues of $10,805 and $26,759 during the same periods for 2011. In addition, for the three and nine-month periods ended September 30, 2011, we recognized revenue of $109,720 and $115,500 related to the Isan USA license transaction (see Note 4). For 2012, all of our product revenues relate to our Odor-No-More products for which sales are primarily to retail establishments at wholesale prices.

Cost of Goods Sold

For the three and nine-month periods ended September 30, 2012, our cost of goods sold was $6,857, or 65% of revenues, and $32,706, or 59% or revenues versus $12,683 or 11% of revenues and $36,270 or 25% of revenues for the three and nine month periods ended September 30, 2011. In the 2011 periods, we recognized licensing revenue, which reduced our cost of goods sold as a percentage of revenue. As well, in the nine-month period ended September 30, 2011, we agreed to purchase back product shipped in 2010 to a customer, which resulted in an increased cost of goods sold related to our product sales as compared with 2012.

Our cost of goods sold includes costs of raw materials, contract manufacturing, and proportions of salaries and expenses related to the production of our Odor-No-More branded products. Because we have not achieved a large or consistent revenue base, the inclusion of the fixed costs related to the product development and manufacturing increases our cost of goods disproportionately, resulting in high percentage fluctuations.

Selling, General and Administrative Expense

Selling, General and Administrative expenses were $828,354 and $3,064,792 for the three and nine-month periods ended September 30, 2012, compared to $580,507 and $2,453,038 for the three and nine-month periods ended September 30, 2011, an increase of $247,847 and $611,754, respectively. The largest components of these expenses were:

a. Salaries and Payroll-related Expenses: These expenses were $219,291 and $1,047,400 for the three and nine-month periods ended September 30, 2012, compared to $206,484 and $875,670 for the three and nine-month periods ended September 30, 2011, increases of $12,807 and $171,730, respectively. The increase in the nine-month period is primarily related to the non-cash expense related to the fair value of stock options, the expiration dates for which were extended in April 2012 by five years. An additional portion of the increase is related to annual salary increases pursuant to contracts with our executive officers.

b. Consulting Expenses: These expenses were $319,607 and $892,110 for the three and nine-month periods ended September 30, 2012, compared to $179,494 and $657,301 for the three and nine-month periods ended September 30, 2011, an increase of $140,113 and $234,809, respectively. . The increases are primarily related to the non-cash expense incurred as a result of the five-year extension in April 2012 of the expiration dates for warrants and stock options issued to consultants.

c. Professional Fees: These expenses were $47,464 and $155,194 for the three and nine-month periods ended September 30, 2012, compared to $39,323 and $206,459 for the three and nine-month periods ended September 30, 2011, an increase of $8,141 and a decrease of $34,976, respectively. The increase is primarily related to the non-cash expense incurred as a result of the five-year extension in April 2012 of the expiration dates for warrants and stock options issued to professionals. The decrease for the nine-month period is primarily due to the fair value of warrants issued to professionals in 2011 that have not been incurred in 2012.

Research and Development

Research and development expenses were $54,497 and $114,609 for the three and nine-month periods ended September 30, 2012, compared to $9,034 and $48,325 for the three and nine-month periods ended September 30, 2011, an increase of $45,463 and $66,284. The increases are attributed to an increase in product development activities and patent application and prosecutions as compared to 2011.

Interest expense

Interest expense totaled $36,137 and $454,074 for the three and nine-month periods ended September 30, 2012, compared to $228,639 and $642,088 for the three and nine-month periods ended September 30, 2011, a decrease of $192,502 and $188,014. The decrease is primarily due to the repayment of $670,410 in convertible notes during 2012 (see Item 2, “Conversion of Spring 2009 Notes”, below) and amortization of the discount based on the fair value of the warrants issued in connection with our convertible debt offset by the fair value of the extension of warrants.

Net Loss

Net loss for the three and nine-month periods ended September 30, 2012 was $915,668 and $3,612,994, a loss of $0.01 and $0.06 per share, compared to a net loss for the three and nine-month periods ended September 30, 2011 of $711,671 and $3,043,994, a loss of $0.01 and $0.06 per share. Although the dollar amount of the loss has declined, the per share loss hasn't declined as much due to the issuance of additional shares for new capital and for compensation and other related expenses.

Liquidity and Capital Resources

We have been, and anticipate that we will continue to be, limited in terms of our capital resources. Until we are successful in commercializing products or negotiating and securing payments for licensing rights from prospective licensing candidates, we expect to continue to have operating losses. Cash and cash equivalents totaled $427,842 at September 30, 2012. We had negative working capital of $1,106,544 as of September 30, 2012, compared with negative working capital of $2,027,351 as of September 30, 2011. We had negative cash flow from operating activities of $1,662,101 for the nine-month period ended September 30, 2012, compared to a negative cash flow from operating activities of $1,334,451 for the nine-month period ended September 30, 2011. We used cash from financing activities to fund operations. Although we have reduced our negative working capital position in the nine-month period ended September 30, 2012, our cash position is insufficient to meet our continuing anticipated expenses or fund anticipated operating expenses. Accordingly, we will be required to raise significant additional capital to sustain operations and further implement our business plan and we may be compelled to reduce or curtail certain activities to preserve cash.

The accompanying condensed consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities and commitments in the normal course of our business. As reflected in the accompanying financial statements, we had a net loss of $3,612,994 for the nine-month period ended September 30, 2012, and an accumulated stockholders' deficit of $71,078,288 as of September 30, 2012. The foregoing factors raise substantial doubt about our ability to continue as a going concern. Ultimately, our ability to continue as a going concern is dependent upon our ability to attract significant new sources of capital, attain a reasonable threshold of operating efficiencies and achieve profitable operations by licensing or otherwise commercializing products incorporating our BioLargo technology. The accompanying condensed consolidated financial statements do not include any adjustments that might be necessary if we are unable to continue as a going concern.

As of September 30, 2012, we had $513,775 aggregate principal amount outstanding on various promissory notes. We may pay the principal and interest due on these notes in cash or in stock, at our option, at maturity. In addition, as of September 30, 2012, we had $971,266 of outstanding accounts payable and accrued expenses, of which $43,395 relates to interest due on outstanding promissory notes, and $927,871 relates to accrued and unpaid payables. (See Note 10.)

During the nine-month period ended September 30, 2012, we received $1,961,445 pursuant to our private securities offerings. (See Note 5.)

We will be required to raise substantial additional capital to expand our operations, including without limitation, hiring additional personnel, additional scientific and third-party testing, costs associated with obtaining regulatory approvals and filing additional patent applications to protect our intellectual property, and possible strategic acquisitions or alliances, as well as to meet our liabilities as they become due for the next 12 months. We may also be compelled to reduce or curtail certain activities to preserve cash.

In addition to the private securities offerings discussed above, we are continuing to explore numerous alternatives for our current and longer-term financial requirements, including additional raises of capital from investors in the form of convertible debt or equity. There can be no assurance that we will be able to raise any additional capital. No commitments are in place as of the date of the filing of this report for any such additional financings. Moreover, in light of the current unfavorable economic conditions, we do not believe that any such financing is likely to be in place in the immediate future.

It is also unlikely that we will be able to qualify for bank or other financial institutional debt financing until such time as our operations are considerably more advanced and we are able to demonstrate the financial strength to provide confidence for a lender, which we do not currently believe is likely to occur for at least the next 12 months or more.

If we are unable to raise sufficient capital, we may be required to curtail some of our operations, including efforts to develop, test, market, evaluate and license our BioLargo technology. If we were forced to curtail aspects of our operations, there could be a material adverse impact on our financial condition and results of operations.

Critical Accounting Policies

Our discussion and analysis of our results of operations and liquidity and capital resources are based on our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and disclosure of contingent assets and liabilities. On an ongoing basis, we evaluate our estimates and judgments, including those related to revenue recognition, valuation of intangible assets and investments, and share-based payments. We base our estimates on anticipated results and trends and on various other assumptions that we believe are reasonable under the circumstances, including assumptions as to future events. These estimates form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. By their nature, estimates are subject to an inherent degree of uncertainty. Actual results that differ from our estimates could have a significant adverse effect on our operating results and financial position. We believe that the following significant accounting policies and assumptions may involve a higher degree of judgment and complexity than others.

The methods, estimates and judgments the Company uses in applying these most critical accounting policies have a significant impact on the results of the Company reports in its financial statements.

We anticipate that revenue will come from two sources: sales of Odor-No-More products and from royalties and license fees from our intellectual property. Odor-No-More revenue is recognized upon shipment of the product and all other contingencies have been met. Licensees typically pay a license fee in one or more installments and ongoing royalties based on their sales of products incorporating or using our licensed intellectual property. License fees are recognized over the estimated period of future benefit to the average licensee.

The Company has established a policy relative to the methodology to determine the value assigned to each intangible acquired with or licensed by the Company and/or services or products received for non-cash consideration of the Company’s common stock. The value is based on the market price of the Company’s common stock issued as consideration, at the date of the agreement of each transaction or when the service is rendered or product is received, as adjusted for applicable discounts.

It the Company’s policy to expense share based payments as of the date of grant in accordance with Auditing Standard Codification Topic 718 “Share-Based Payment.” Application of this pronouncement requires significant judgment regarding the assumptions used in the selected option pricing model, including stock price volatility and employee exercise behavior. Most of these inputs are either highly dependent on the current economic environment at the date of grant or forward-looking expectations projected over the expected term of the award. As a result, the actual impact of adoption on future earnings could differ significantly from our current estimate.

Recent Accounting Pronouncements

Recent accounting pronouncements issued by FASB and the SEC did not or are not believed by management to have a material impact on the Company’s present or future consolidated financial statements.

Inflation

Inflation affects the cost of raw materials, goods and services we use. In recent years, inflation overall has been modest, but we believe inflation may increase our costs in the near future. Some of our products incorporate oil based polymers, which are subject to price fluctuations based on the price of crude oil, as well as shortages.

Item 4. Controls and Procedures

We conducted an evaluation, under the supervision and with the participation of 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) as of the end of the period covered by this Report.

Our procedures have been designed to ensure that the information relating to our company, including our consolidated subsidiaries, required to be disclosed in our SEC reports is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms, and is accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate to allow for timely decisions regarding required disclosure. Based on this evaluation, our chief executive officer and chief financial officer concluded that as of the evaluation date our disclosure controls and procedures are effective.

It should be noted that the design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions, regardless of how remote.

There was no change in our internal control over financial reporting that occurred during the period covered by this Quarterly Report on Form 10-Q that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II

OTHER INFORMATION

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Summer 2012 Offering

Pursuant to a private offering of our common stock at a price of $0.40 per share that commenced May 2012 (the "Summer 2012 Offering"), through September 30, 2012, we sold 1,925,214 shares of our common stock at $0.40 per share from seven accredited investors and received $770,086 gross proceeds and $744,515 net proceeds from the sales. Of these amounts, 1,147,500 shares were sold and $459,000 was invested during the three-month period ended September 30, 2012. Each purchaser of stock in the Summer 2012 Offering will receive, for no additional consideration, a stock purchase warrant (the "Summer 2012 Warrant") entitling the holder to purchase the same number of shares as purchased in the offering, for $0.55 per share until March 31, 2014.

On October 23, 2012, we amended the terms of the Summer 2012 Offering (see Note 5) by reducing the price of the common stock sold from 40 cents to 35 cents, and reducing the exercise price of the Summer 2012 Warrant from 55 cents to 50 cents. This change was applied retroactively to the investors of the offering. As a result, we issued an additional 275,038 shares of common stock to the investors, and issued those investors amended warrants reflecting the new share amount and new exercise price.

Winter 2012 Offering

Pursuant to a private offering of our common stock at a price of $0.35 per share that commenced January 2012 and closed May 2012 (the "Winter 2012 Offering"), we sold 3,127,914 shares of our common stock at $0.35 per share from 30 accredited investors and received $1,094,765 gross and $1,030,265 net proceeds from the sales.

Each purchaser of stock in the Winter 2012 Offering received, for no additional consideration, a stock purchase warrant (the "Winter 2012 Warrant") entitling the holder to purchase the same number of shares as purchased in the offering, for $0.50 per share until January 31, 2013.

Conversion of Spring 2010 Note

On February 6, 2012, a holder of a convertible promissory note issued in our Spring 2010 Offering (see Note 5) elected to convert the principal balance of $25,000, and accrued unpaid interest of $2,034, into an aggregate 47,017 shares of our common stock, at a conversion price of $0.575.

Conversion of Spring 2009 Notes

On the June 1, 2012 maturity date of the Spring 2009 Notes, we elected to convert the remaining aggregate principal balance of $670,410 and $67,041 of accrued and unpaid interest into an aggregate 1,340,820 shares of our common stock at a conversion price of $0.55 per share. As a result, the Spring 2009 Notes are fully paid.

Payment of Consultant Fees

On January 31, 2012, we issued an aggregate 30,147 shares of our common stock, at a conversion price of $0.31, in lieu of $9,225 of rent expense.

On March 6, 2012, we issued 100,000 shares of our common stock at a conversion price of $0.35 per share, and recorded $35,000 of selling, general and administrative expense to a consultant in exchange for research and marketing services.

On July 1, 2012, we issued 80,000 shares of our common stock at a conversion price of $.035 per share, and recorded $28,000 of selling, general and administrative expense to a consultant in exchange for research and marketing services.

On September 5, 2012 we issued 15,761 shares of our common stock at a conversion price of $.031 per share, and recorded $4,693 of selling, general and administrative expense to a consultant in exchange for research and marketing services.

Payment of Accrued Interest

On April 15, 2012, in accordance with terms of the Spring 2010 Notes (see Note 5), we paid accrued interest of $41,425 by the issuance of 125,539 shares of our common stock, at a conversion price of $0.33 per share, to the holders of the Spring 2010 Notes.

All of these offerings and sales were made in reliance on the exemption from registration contained in Section 4(2) of the Securities Exchange Act and/or Regulation D promulgated thereunder as not involving a public offering of securities.

Item 6. Exhibits

The exhibits listed below are attached hereto:

Exhibit No.	Description
4.1*	Form of Warrant issued in Summer 2012 Offering
31.1*	Certification of Chief Executive Officer of Quarterly Report Pursuant to Rule 13(a)-15(e) or Rule 15(d)-15(e).
31.2*	Certification of Chief Financial Officer of Quarterly Report Pursuant to 18 U.S.C. Section 1350
32**	Certification of Chief Executive Officer and Chief Financial Officer of Quarterly Report pursuant to Rule 13(a)-15(e) or Rule 15(d)-15(e).
101.INS**	XBRL Instance
101.SCH**	XBRL Taxonomy Extension Schema
101.CAL**	XBRL Taxonomy Extension Calculation
101.DEF**	XBRL Taxonomy Extension Definition
101.LAB**	XBRL Taxonomy Extension Labels
101.PRE**	XBRL Taxonomy Extension Presentation

* Filed herewith

** Furnished herewith

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.

	BIOLARGO, INC.
Date: November 14, 2012	By: /s/ DENNIS P. CALVERT Dennis P. Calvert Chief Executive Officer
Date: November 14, 2012	By: /s/ CHARLES K. DARGAN, II Chief Financial Officer

EXHIBIT INDEX

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101.INS**	XBRL Instance
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101.CAL**	XBRL Taxonomy Extension Calculation
101.DEF**	XBRL Taxonomy Extension Definition
101.LAB**	XBRL Taxonomy Extension Labels
101.PRE**	XBRL Taxonomy Extension Presentation

* Filed herewith

** Furnished herewith