

True Drinks Holdings, Inc.
Form 10-Q
May 13, 2014

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2014

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

For the transition period from _____ to _____

Commission file number 001-32420

TRUE DRINKS HOLDINGS, INC.
(Exact Name of Registrant as Specified in Its Charter)

Nevada
(State or Other Jurisdiction of
Incorporation
or Organization)

84-1575085
(IRS Employer Identification No.)

18552 MacArthur Blvd., Suite 325
Irvine, CA 92612
(Address of Principal Executive Offices)

(949) 203-3500
(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 No

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer,

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or a smaller reporting company. See definitions of “large accelerated filer,” “accelerated filer,” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

| | | | |
|-------------------------|--------------------------|---------------------------|-------------------------------------|
| Large accelerated filer | <input type="checkbox"/> | Accelerated filer | <input type="checkbox"/> |
| Non-accelerated filer | <input type="checkbox"/> | Smaller reporting company | <input checked="" type="checkbox"/> |

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

The number of shares of Common Stock, with \$0.001 par value, outstanding on May 13, 2014 was 34,476,822.

TRUE DRINKS HOLDINGS, INC.

QUARTERLY REPORT ON FORM 10-Q
FOR THE QUARTER ENDED MARCH 31, 2014

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PART I

ITEM 1. FINANCIAL STATEMENTS

TRUE DRINKS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

| ASSETS | March 31, 2014 (Unaudited) | December 31, 2013 |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------|----------------------|
| Current Assets: | | |
| Cash | \$ 2,928,222 | \$ 3,136,766 |
| Accounts receivable, net | 307,920 | 175,068 |
| Inventory | 1,236,794 | 1,056,756 |
| Prepaid expenses and other current assets | 549,069 | 591,434 |
| Total Current Assets | 5,022,005 | 4,960,024 |
| Restricted Cash | 133,065 | 133,065 |
| Property and Equipment, net | 7,218 | 8,399 |
| Patents, net | 1,317,647 | 1,352,941 |
| Trademarks, net | 36,016 | 48,516 |
| Goodwill | 3,474,502 | 3,474,502 |
| Total Assets | \$ 9,990,453 | \$ 9,977,447 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current Liabilities: | | |
| Accounts payable and accrued expenses | \$ 938,450 | \$ 1,222,404 |
| Convertible notes payable, net | 25,000 | 680,000 |
| Term loan | 1,666,667 | 1,916,667 |
| Derivative liabilities | 4,360,969 | 1,619,021 |
| Total Current Liabilities | 6,991,086 | 5,438,092 |
| Commitments and Contingencies (Note 5) | | |
| Stockholders' Equity: | | |
| Common Stock, \$0.001 par value, 40,000,000 shares authorized, 34,476,822 and 27,855,587 shares outstanding at March 31, 2014 and December 31, 2013, respectively | 34,477 | 27,886 |
| Preferred Stock – Series B (liquidation preference of \$4 per share), \$0.001 par value, 2,750,000 shares authorized, 2,082,870 and 1,776,923 shares outstanding at March 31, 2014 and December 31, 2013, respectively | 2,082 | 1,777 |
| Additional paid in capital | 16,808,055 | 14,751,170 |
| Accumulated deficit | (13,845,247) | (10,241,478) |
| Total Stockholders' Equity | 2,999,367 | 4,539,355 |
| Total Liabilities and Stockholders' Equity | \$ 9,990,453 | \$ 9,977,447 |

The accompanying notes are an integral part of these financial statements.

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TRUE DRINKS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

| | Three Months Ended March 31, | |
|---------------------------------------------------------------|---------------------------------|----------------|
| | 2014 | 2013 |
| Net Sales | \$ 650,532 | \$ 410,801 |
| Cost of Sales | 529,301 | 263,950 |
| Gross Profit | 121,231 | 146,851 |
| Operating Expenses | | |
| Selling and marketing | 570,528 | 430,486 |
| General and administrative | 991,806 | 1,045,064 |
| Total operating expenses | 1,562,334 | 1,475,550 |
| Operating Loss | (1,441,103) | (1,328,699) |
| Other Expense | | |
| Change in fair value of derivative liabilities | (2,125,537) | - |
| Interest expense | (37,129) | (228,199) |
| | (2,162,666) | (228,199) |
| NET LOSS | \$ (3,603,769) | \$ (1,556,898) |
| Declared dividends on Preferred Stock | 133,204 | - |
| Net loss attributable to common stockholders | \$ (3,736,973) | \$ (1,556,898) |
| Loss per common share, basic and diluted | (0.13) | (0.06) |
| Weighted average common shares outstanding, basic and diluted | 27,902,154 | 26,810,744 |

The accompanying notes are an integral part of these financial statements.

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TRUE DRINKS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

| | Three Months Ended March 31, | |
|----------------------------------------------------------------------------|---------------------------------|----------------|
| | 2014 | 2013 |
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Net loss | \$ (3,603,769) | \$ (1,556,898) |
| Adjustments to reconcile net loss to net cash used in operating activities | | |
| Depreciation | 3,530 | 6,226 |
| Amortization | 47,794 | 47,795 |
| Change in estimated fair value of derivative | 2,125,537 | - |
| Fair value of stock issued for services | 39,875 | 195,600 |
| Stock based compensation | 123,364 | 436,403 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (132,852) | (50,775) |
| Inventory | (180,038) | 303,205 |
| Prepaid expenses and other current assets | 42,365 | (17,367) |
| Accounts payable and accrued expenses | (287,219) | (251,319) |
| Net cash used in operating activities | (1,821,413) | (887,130) |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Change in restricted cash | - | 262 |
| Purchase of property and equipment | (2,349) | - |
| Net cash (used in) provided by investing activities | (2,349) | 262 |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Dividends paid | (2,194) | - |
| Proceeds from issuance of Series B Preferred Stock, net | 1,887,412 | - |
| Proceeds from convertible notes payable | - | 1,049,000 |
| Repayments on convertible notes payable | (20,000) | (135,000) |
| Repayments on term loan | (250,000) | - |
| Net cash provided by financing activities | 1,615,218 | 914,000 |
| NET (DECREASE) INCREASE IN CASH | (208,544) | 27,132 |
| CASH – beginning of period | 3,136,766 | 4,449 |
| CASH – end of period | \$ 2,928,222 | \$ 31,581 |
| SUPPLEMENTAL DISCLOSURES | | |
| Interest paid in cash | \$ 7,944 | \$ 13,795 |
| Non-cash financing and investing activities: | | |
| Conversion of preferred stock to Common Stock | \$ 6,033 | \$ 25,304 |
| Conversion of notes payable and accrued interest to Common Stock | \$ 764,938 | \$ - |
| Dividends declared but unpaid | \$ 133,204 | \$ - |
| Warrants issued in connection with Series B Preferred Offering | \$ 616,411 | \$ - |

The accompanying notes are an integral part of these financial statements.

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TRUE DRINKS HOLDINGS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
March 31, 2014

NOTE 1 — ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization and Business

Overview

True Drinks Holdings, Inc. (the "Company", "us" or "we") was incorporated in the state of Nevada in January 2001 and is the holding company for True Drinks, Inc. ("True Drinks"), formed on January 19, 2012 in Delaware to create and commercialize all-natural, vitamin-enhanced drinks. Our primary business is the development, marketing, sale and distribution of our flagship product, AquaBall™ Naturally Flavored Water, a vitamin-enhanced, naturally flavored water drink packaged in our patented stacking spherical bottles. We distribute AquaBall™ nationally through select retail channels, such as grocery stores, mass merchandisers, drug stores and online. We also market and distribute Bazi® All Natural Energy, a liquid nutritional supplement drink, which is currently distributed through select retail channels, online, and through our existing database of customers.

Our principal place of business is 18552 MacArthur Boulevard, Suite 325, Irvine, California, 92612. Our telephone number is (949) 203-2500. Our corporate website address is <http://www.truedrinks.com>. Our Common Stock, par value \$0.001 ("Common Stock") is currently listed for quotation on the Over-the-Counter marketplace ("OTCQB") under the symbol TRUU.

Developments During the Quarter

On February 5, 2014, the Company completed a private offering of shares of Series B Convertible Preferred Stock ("Series B Preferred") for \$4.00 per share, and five-year warrants (the "Warrants"), exercisable for \$0.30 per share (the "Series B Offering"). Over the course of the Series B Offering, the Company and certain accredited investors entered into Securities Purchase Agreements to purchase 2.0 million shares of Series B Preferred and Warrants to purchase approximately 9.3 million shares of Common Stock for net proceeds to the Company of \$7,370,556.

Basis of Presentation and Going Concern

The accompanying condensed consolidated balance sheet as of December 31, 2013, which has been derived from audited financial statements included in Form 10-K for the year ended December 31, 2013, and the accompanying interim condensed consolidated financial statements as of March 31, 2014, for the three-month periods ended March 31, 2014 and 2013, have been prepared by management pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC") for interim financial reporting. These interim condensed consolidated financial statements are unaudited and, in the opinion of management, include all adjustments (consisting only of normal recurring adjustments and accruals) necessary to fairly present the Company's financial condition, results of operations and cash flows as of and for the periods presented in accordance with accounting principles generally accepted in the United States of America ("GAAP"). Operating results for the three-month period ended March 31, 2014 are not necessarily indicative of the results that may be expected for the year ending December 31, 2014, or for any other interim period during such year. Certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been omitted in accordance with the rules and regulations of the SEC, although the Company believes that the disclosures made are adequate to make the information not misleading. The accompanying condensed consolidated financial statements should be read in conjunction with the audited

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consolidated financial statements and notes thereto contained in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2013 filed with the SEC on March 31, 2014.

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The accompanying financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America, which contemplates continuation of the Company as a going concern. As of and for the three months ended March 31, 2014, the Company incurred a net loss of \$3,603,769, has negative working capital of \$1,969,081, and an accumulated deficit of \$13,845,247. Although the Company had \$3,061,287 in cash at March 31, 2014, \$133,065 of our cash is restricted, as discussed below. The Company may require additional capital to execute its business, marketing and operating plan, and therefore sustain operations, which capital may not be available on favorable terms, if at all. The accompanying condensed consolidated financial statements do not include any adjustments that might result in the event the Company was unable to generate sufficient cash from operations, execute its business, marketing or operating plan, or obtain additional working capital, if necessary.

Principles of Consolidation

The accompanying financial statements include the accounts of the Company and its wholly owned subsidiaries True Drinks, Bazi, Inc. and GT Beverage Company, LLC. All inter-company accounts and transactions have been eliminated in the preparation of these condensed consolidated financial statements.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant estimates made by management include, among others, derivative liabilities, provision for losses on accounts receivable, allowances for obsolete and slow moving inventory, stock compensation, deferred tax asset valuation allowances, and the realization of long-lived and intangible assets, including goodwill. Actual results could differ from those estimates.

Restricted Cash

The Company has \$133,065 in restricted cash with a financial institution securing a letter of credit. The letter of credit matures in August 2015 and was issued as part of contractual obligations related to one of our licensing agreements with Disney Consumer Products, Inc.

Accounts Receivable

We maintain an allowance for doubtful accounts, which is analyzed on a periodic basis to ensure that it is adequate to the best of management's knowledge. Management develops an estimate of the allowance for doubtful accounts receivable based on the perceived likelihood of ultimate payment. Although the Company expects to collect amounts due, actual collections may differ from these estimated amounts. The allowance for doubtful accounts was approximately \$210,000 at March 31, 2014 and December 31, 2013, respectively.

Concentrations

The Company has no significant off-balance sheet concentrations of credit risk such as foreign exchange contracts, options contracts or other foreign hedging arrangements. The Company maintains the majority of its cash balances with two financial institutions. There are funds in excess of the federally insured amount, or that are subject to credit risk, and the Company believes that the financial institutions are financially sound and the risk of loss is minimal.

We utilized a variety of suppliers to purchase raw materials for the AquaBall™ Naturally Flavored Water during the three-months ended March 31, 2014 and the year ended December 31, 2013.

During 2013, we relied significantly on one supplier for 100% of our purchases of certain raw materials for Bazi®. Bazi, Inc. has sourced these raw materials from this supplier since 2007 and we do not anticipate any issues with the supply of these raw materials.

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A significant portion of our revenue comes from sales of the AquaBall™ Naturally Flavored Water with the remaining sales coming from Bazi® All Natural Energy. For the three-months ended March 31, 2014, sales of AquaBall™ accounted for 91% of our sales, compared to 65% for the corresponding period in 2013.

Inventory

Inventory is stated at the lower of cost or market on a FIFO (first-in first-out) basis. Provisions are made to reduce excess or obsolete inventory to the estimated net realizable value. The Company purchases for resale a vitamin-enhanced flavored water beverage and a liquid dietary supplement.

Management reviews the carrying value of inventory in relation to its sales history and industry trends to determine an estimated net realizable value. Changes in economic conditions or customer demand could result in obsolete or slow moving inventory that cannot be sold or must be sold at reduced prices and could result in an inventory reserve. No inventory reserves were considered necessary as of March 31, 2014 and December 31, 2013.

Inventory is comprised of the following:

| | March 31, 2014 (unaudited) | December 31, 2013 |
|---------------------|----------------------------------|----------------------|
| Purchased materials | \$ 740,347 | \$ 659,835 |
| Finished goods | 496,447 | 396,921 |
| Total | \$ 1,236,794 | \$ 1,056,756 |

Long-Lived Assets

The Company reviews its long-lived assets for impairment whenever changes in circumstances indicate that the carrying amount of an asset may not be recoverable. For purposes of evaluating the recoverability of long-lived assets, the recoverability test is performed using undiscounted net cash flows estimated to be generated by the asset. No impairment was deemed necessary during the quarter ended March 31, 2014.

Intangible Assets

Intangible assets consists of the direct costs incurred for application fees and legal expenses associated with trademarks on the Company's products, customer list, and the estimated value of GT Beverage Company, LLC's interlocking spherical bottle patent. The Company's intangible assets are amortized over their estimated remaining useful lives. The Company evaluates the useful lives of its intangible assets annually and adjusts the lives according to the expected useful life. No impairment was deemed necessary during the quarter ended March 31, 2014.

Goodwill

Goodwill represents the future economic benefits arising from other assets acquired that are individually identified and separately recognized. Goodwill and intangible assets acquired in a purchase business combination and determined to have an indefinite useful life are not amortized, but are tested for impairment at least annually, typically in the fourth quarter. No impairment indicators were noted during the quarter ended March 31, 2014.

Income Taxes

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For the quarters ended March 31, 2014 and 2013, the Company incurred tax net operating losses, and accordingly, had no income tax provision. At March 31, 2014, the Company had tax net operating loss carryforwards and a related deferred tax asset, which had a full valuation allowance.

Stock-Based Compensation

For the three-month periods ended March 31, 2014 and 2013, general and administrative expenses included stock based compensation expense of \$123,364 and \$436,403, respectively.

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The Company uses a Black-Scholes option-pricing model (the “Black-Scholes Model”) to estimate the fair value of outstanding stock options and warrants. The use of a valuation model requires the Company to make certain assumptions with respect to selected model inputs. Expected volatility is calculated based on the historical volatility of the Company’s stock price over the contractual term of the option or warrant. The expected life is based on the contractual term of the option or warrant and expected exercise and, in the case of options, post-vesting employment termination behavior. Currently, our model inputs are based on the simplified approach provided by SAB 110. The risk-free interest rate is based on U.S. Treasury zero-coupon issues with a remaining term equal to the expected life assumed at the date of the grant (see Note 3, “Stock Options and Warrants”).

Derivative Instruments

A derivative is an instrument whose value is “derived” from an underlying instrument or index such as a future, forward, swap, option contract, or other financial instrument with similar characteristics, including certain derivative instruments embedded in other contracts (“embedded derivatives”) and for hedging activities. As a matter of policy, the Company does not invest in financial derivatives or engage in hedging transactions. However, the Company has entered into complex financing transactions that involve financial instruments containing certain features that have resulted in the instruments being deemed derivatives or containing embedded derivatives. The Company may engage in other similar complex debt transactions in the future, but not with the intention to enter into derivative instruments. Derivatives and embedded derivatives, if applicable, are measured at fair value using the binomial lattice (“Binomial Lattice”) pricing model and marked to market and reflected on our condensed consolidated statement of operations as other (income) expense at each reporting period. However, such new and/or complex instruments may have immature or limited markets. As a result, the pricing models used for valuation of derivatives often incorporate significant estimates and assumptions, which may impact the level of precision in the financial statements. Furthermore, depending on the terms of a derivative or embedded derivative, the valuation of derivatives may be removed from the financial statements upon conversion of the underlying instrument into some other security.

Net Loss Per Share

Earnings per share requires presentation of both basic earnings per common share and diluted earnings per common share. Since the Company has a net loss for all periods presented, Common Stock equivalents are not included in the weighted average calculation since their effect would be anti-dilutive. At March 31, 2014 and 2013, the Company had 90,832,975 and 26,536,428 shares of Common Stock equivalents outstanding, respectively.

Research and Development

Research and development costs are expensed as incurred.

Recent Accounting Pronouncements

The Company has reviewed all recently issued, but not yet effective accounting pronouncements and has concluded that there are no recently issued, but not yet effective pronouncements that may have a material impact on the Company’s future financial statements.

Subsequent Events

Management has evaluated subsequent events through the date the accompanying condensed consolidated financial statements were filed with the SEC, and noted no other significant subsequent events not elsewhere disclosed herein.

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NOTE 2 — SHAREHOLDERS' EQUITY

Series B Convertible Preferred Stock

We are currently authorized to issue up to 5,000,000 shares of preferred stock, of which 2,750,000 shares are currently designated as Series B Convertible Preferred Stock. Each share of Series B Preferred has a stated value of \$4.00 per share ("Stated Value") and accrues annual dividends equal to 5% of the Stated Value, payable by the Company in quarterly installments, in either cash or shares of Common Stock. The Company declared a dividend totaling \$133,204 and paid previously declared dividends of \$2,194 during the quarter ended March 31, 2014. The cumulative unpaid dividends on the Series B Preferred Stock are \$133,204 and \$2,194 at March 31, 2014 and December 31, 2013, respectively. Each share of Series B Preferred is convertible, at the option of the holder, into that number of shares of Common Stock equal to the Stated Value, divided by \$0.25 per share (the "Conversion Shares"). The Company also has the option to require the conversion of the Series B Preferred into Conversion Shares in the event: (i) there are sufficient authorized shares of Common Stock reserved as Conversion Shares; (ii) the Conversion Shares are registered under the Securities Act of 1933, as amended (the "Securities Act"), or the Conversion Shares are freely tradable, without restriction, under Rule 144 of the Securities Act; (iii) the daily trading volume of the Company's Common Stock, multiplied with the closing price as reported by the OTCBB, equals at least \$250,000 for 20 consecutive trading days; and (iv) the average closing price of the Company's Common Stock is at least \$0.62 per share for 10 consecutive trading days.

Over the course of the Series B Offering, between November 2013 and February 2014, the Company offered and sold 2.0 million shares of Series B Preferred to certain accredited investors in exchange for a total of \$8,000,000 in cash, less cash fees of \$659,440. The investors also received Warrants to purchase an aggregate total of 9,333,334 shares of the Company's Common Stock for \$0.30 per share. The Company also issued Warrants to purchase 1,946,721 shares of Common Stock to certain placement agents assisting with the Series B Offering. Each Warrant contains a price-protection feature that adjusts the exercise price in the event of certain dilutive issuances of securities. Such price-protection feature is determined to be a derivative liability and, as such, the value of all Warrants issued during the Series B Offering, or \$1,534,007, was recorded to derivative liabilities.

In January 2014, the Company repaid \$25,750 in outstanding principal, lender's fees and interest on certain convertible notes payable.

Between February 2014 and March 2014, holders of 402,230 shares of the Series B Preferred converted those shares into 6,435,680 shares of Common Stock.

In February 2014, holders of \$789,938 in outstanding principal, lender's fees and interest on certain convertible notes payable exchanged this total for 197,487 shares of Series B Preferred and Warrants to purchase 921,596 shares of Common Stock for \$0.30 per share.

In March 2014, the Company issued 145,000 shares of Common Stock in connection with two consulting agreements. The Company expensed the fair value of the Common Stock issued of \$39,875 to consulting expense.

NOTE 3 — STOCK OPTIONS AND WARRANTS

Warrants

A summary of the Company's warrant activity for the three months ended March 31, 2014 is presented below:

| Warrants | Weighted |
|----------|----------|
|----------|----------|

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| | Outstanding | Average Exercise Price |
|--------------------------------|-------------|------------------------------|
| Outstanding, December 31, 2013 | 12,590,467 | \$ 0.55 |
| Granted | 3,989,117 | 0.30 |
| Exercised | - | - |
| Expired | - | - |
| Outstanding, March 31, 2014 | 16,579,584 | \$ 0.49 |

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As of March 31, 2014, the Company had the following outstanding warrants to purchase shares of its Common Stock:

| Warrants Outstanding | Weighted Average Exercise Price Per Share | Weighted Average Remaining Life (Yrs.) |
|----------------------|-------------------------------------------|----------------------------------------|
| 62,453 | \$ 30.00 | 1.81 |
| 57,500 | \$ 25.00 | 0.26 |
| 3,038,243 | \$ 0.25 | 4.31 |
| 13,421,388 | \$ 0.30 | 4.71 |
| 16,579,584 | \$ 0.55 | 4.61 |

Non-Qualified Stock Options

The Company granted 2,457,390 non-qualified stock options to employees during the three months ended March 31, 2014.

Stock option activity during the three months ended March 31, 2014 is summarized as follows:

| | Options Outstanding | Weighted-Average Exercise Price |
|------------------------------------------|---------------------|---------------------------------|
| Options outstanding at December 31, 2013 | 3,993,258 | \$ 0.70 |
| Exercised | - | - |
| Granted | 2,457,390 | 0.25 |
| Forfeited | - | - |
| Expired | - | - |
| Options outstanding at March 31, 2014 | 6,450,648 | \$ 0.53 |

The following table summarizes information about the Company's stock options outstanding as of March 31, 2014:

| Range of Exercise Prices | Outstanding Options | | | Exercisable Options | | |
|--------------------------|---------------------|-----------------------------------------------------|---------------------------|---------------------|---------------------------|--|
| | Number | Weighted Average Remaining Contractual Life (Years) | Aggregate Intrinsic Value | Number | Aggregate Intrinsic Value | |
| \$ 0.61 | 3,133,173 | 1.29 | \$ - | 1,310,610 | \$ - | |
| \$ 1.02 | 614,346 | 1.45 | \$ - | 184,305 | \$ - | |
| \$ 1.10 | 245,739 | 2.25 | \$ - | - | \$ - | |
| \$ 0.25 | 2,457,390 | 9.86 | \$ 368,609 | 637,752 | \$ 95,663 | |
| Totals | 6,450,648 | 4.61 | \$ 368,609 | 2,132,667 | \$ 95,663 | |

NOTE 4 — CONVERTIBLE NOTES

A summary of convertible notes payable as of March 31, 2014, is as follows:

| | Amount |
|--------------------------------|------------|
| Outstanding, December 31, 2013 | \$ 680,000 |
| Notes issued | - |

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| | |
|---------------------------------|-----------|
| Notes repaid | (20,000) |
| Notes converted to Common Stock | (635,000) |
| Outstanding, March 31, 2014 | \$ 25,000 |

In January 2014, the Company repaid \$25,750 in outstanding principal, lender's fees and interest of certain notes payable.

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In February 2014, holders of bridge financing notes issued in totaling \$789,938 in outstanding principal, lender's fees and interest converted their notes into the Company's Series B Offering.

Term Loan

In November 2013, the Company secured a commercial term loan in the amount of \$2.0 million from Avid Bank. The loan has a term of two years, accrues interest at 2.75% above prime, is secured by virtually all of the Company's assets, and requires an asset coverage ratio of assets to outstanding principal of 1.5. As of March 31, 2014, the Company was in compliance with the asset coverage ratio of the Term Loan.

NOTE 5 — COMMITMENTS AND CONTINGENCIES

The Company has entered in a number of agreements with various consultants. Termination of any of these agreements could result in termination fees.

The Company leases its corporate office in Irvine, California on a one-year term, which term was most recently renewed in July 2013. Total rent expense related to the Company's operating lease for the three months ended March 31, 2014 was \$15,568. Total remaining payments on the lease through July 31, 2014 are \$14,728.

The Company maintains employment agreements with certain key members of management. The agreements provide for minimum base salaries, eligibility for stock options, performance bonuses and severance payments.

Legal Proceedings

From time to time, claims are made against the Company in the ordinary course of business, which could result in litigation. Claims and associated litigation are subject to inherent uncertainties and unfavorable outcomes could occur. In the opinion of management, the resolution of these matters, if any, will not have a material adverse impact on the Company's financial position or results of operations.

On July 1, 2011, a lawsuit was filed in the United States District Court, the Southern District of Ohio, Cincinnati Division, against GT Beverage Company, LLC ("GT LLC") by Dominion Liquid Technologies, LLC. The lawsuit alleges that GT LLC breached terms of a 2010 co-packing agreement, which governed the relationship between the parties. In February 2013, Dominion amended its complaint to add the Company as a defendant in the case. Dominion is seeking monetary damages in an amount exceeding \$800,000. GT LLC has filed its answer denying all of Dominion's claims and expects to vigorously defend the suit. A trial will likely be set in the second or third quarter of 2014.

On April 22, 2014, a lawsuit was filed in the Superior Court of California, County of Orange, against True Drinks by Advantage Sales and Marketing, LLC. The lawsuit is for an open book balance of \$92,064. The Company disputes some of the charges in the open book balance and is looking to settle the case for an amount that more fairly represents the work performed by Advantage Sales and Marketing on behalf of True Drinks.

NOTE 6 – FAIR VALUE MEASUREMENTS

The application of fair value measurements may be on a recurring or nonrecurring basis depending on the accounting principles applicable to the specific asset or liability or whether management has elected to carry the item at its estimated fair value. FASB ASC 820-10-35 specifies a hierarchy of valuation techniques based on whether the inputs to those techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's market assumptions. These two types of inputs create the

following fair value hierarchy:

- Level 1: Observable inputs such as quoted prices in active markets;
- Level 2: Inputs, other than the quoted prices in active markets, that are observable either directly or indirectly; and
- Level 3: Unobservable inputs in which there is little or no market data, which require the reporting entity to develop its own assumptions.

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This hierarchy requires the Company to use observable market data, when available, and to minimize the use of unobservable inputs when estimating fair value.

The Company assesses its recurring fair value measurements as defined by FASB ASC 810. Liabilities measured at estimated fair value on a recurring basis include derivative liabilities. Transfers between fair value classifications occur when there are changes in pricing observability levels. Transfers of financial liabilities among the levels occur at the beginning of the reporting period. There were no transfers between Level 1, Level 2 and/or Level 3 during the quarter ended March 31, 2014. The Company had no Level 1 or 2 fair value measurements at March 31, 2014 or December 31, 2013.

The following table presents the estimated fair value of financial liabilities measured at estimated fair value on a recurring basis included in the Company's financial statements as of March 31, 2014:

| | Total carrying value | Level 1 Quoted market prices in active markets | Level 2 Internal Models with significant observable market parameters | Level 3 Internal models with significant unobservable market parameters |
|------------------------|----------------------------|---------------------------------------------------------------|--------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------|
| Derivative liabilities | \$ 4,360,969 | \$ - | \$ - | \$ 4,360,969 |

The following table presents the changes in recurring fair value measurements included in net loss for the quarter ended March 31, 2014:

| | Recurring Fair Value Measurements Changes in Fair Value Included in Net Loss For the Quarter Ended March 31, 2014 | | |
|------------------------|----------------------------------------------------------------------------------------------------------------------------|----------|--------------|
| | Revenues | Expenses | Total |
| Derivative liabilities | \$ 2,125,537 | \$ - | \$ 2,125,537 |

The table below sets forth a summary of changes in the fair value of our Level 3 financial liabilities for the quarter ended March 31, 2014:

| | December 31, 2013 | Recorded New Derivative Liabilities | Write off of Derivative Liabilities | Change in Estimated Fair Value Recognized in Results of Operations | March 31, 2014 |
|------------------------|----------------------|----------------------------------------------|----------------------------------------------|--------------------------------------------------------------------------------------|-------------------|
| Derivative liabilities | \$ 1,619,021 | \$ 616,411 | \$ - | \$ 2,125,537 | \$ 4,360,969 |

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

Forward-Looking Statements

This Quarterly Report on Form 10-Q contains "forward-looking" statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. We intend to identify forward-looking statements in this report by using words such as "believes," "intends," "expects," "may," "will," "should," "plan," "projected," "contemplates," "anticipates," "estimates," "predicts," "potential," "continue," or similar terms. These statements are based on our beliefs as well as assumptions we made using information currently available to us. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise. Because these statements reflect our current views concerning future events, these statements involve risks, uncertainties, and assumptions. Actual future results may differ significantly from the results discussed in the forward-looking statements. These risks include changes in demand for our products, changes in the level of operating expenses, our ability to expand our network of customers, changes in general economic conditions that impact consumer behavior and spending, product supply, the availability, amount, and cost of capital to us and our use of such capital, and other risks discussed in this report. Additional risks that may affect our performance are discussed under "Risk Factors" in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2013.

The following discussion of the financial condition and results of operations should be read in conjunction with the condensed consolidated financial statements included elsewhere within this Quarterly Report. Fluctuations in annual and quarterly results may occur as a result of factors affecting demand for our products such as the timing of new product introductions by us and by our competitors and our customers' political and budgetary constraints. Due to such fluctuations, historical results and percentage relationships are not necessarily indicative of the operating results for any future period.

Overview

True Drinks Holdings, Inc. (the "Company", "us" or "we") was incorporated in the state of Nevada in January 2001 and is the holding company for True Drinks, Inc. ("True Drinks"), a beverage company incorporated in the state of Delaware in January 2012 that specializes in all-natural, vitamin-enhanced drinks. Our primary business is the development, marketing, sale and distribution of our flagship product, AquaBall™ Naturally Flavored Water, a vitamin-enhanced, naturally flavored water drink packaged in our patented stacking spherical bottles. We distribute the AquaBall™ nationally through select retail channels, such as grocery stores, mass merchandisers, drug stores and online. We also market and distribute Bazi® All Natural Energy, a liquid nutritional supplement drink, which is currently distributed online and through our existing database of customers.

Our principal place of business is 18552 MacArthur Boulevard, Suite 325, Irvine, California, 92612. Our telephone number is (949) 203-2500. Our corporate website address is <http://www.truedrinks.com>. Our Common Stock, par value \$0.001 ("Common Stock") is currently listed for quotation on the Over-the-Counter marketplace ("OTCQB") under the symbol TRUU.

Critical Accounting Policies and Estimates

Discussion and analysis of our financial condition and results of operations are based upon financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, we

evaluate our estimates; including those related to collection of receivables, inventory obsolescence, sales returns and non-monetary transactions such as stock and stock options issued for services. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. With the exception of derivative instruments below, we believe there have been no changes to our critical accounting policies subsequent to the filing of our annual report on Form 10-K for the year ended December 31, 2013.

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Derivative Instruments

We evaluate free-standing derivative instruments (or embedded derivatives) to properly classify such instruments within equity or liabilities in our consolidated financial statements.

The classification of a derivative instrument is reassessed at each reporting date. If the classification changes as a result of events during a reporting period, the instrument is reclassified as of the date of the event that caused the reclassification. There is no limit on the number of times a contract may be reclassified.

Instruments classified as derivative liabilities are remeasured each reporting period (or upon classification) and the change in fair value is recorded on our consolidated statement of operations in other (income) expense.

Comparison of the Three Months Ended March 31, 2014 to the Three Months Ended March 31, 2013.

Net Sales

Net sales for the three months ended March 31, 2014 were \$650,532, compared with sales of \$410,801 for the three months ended March 31, 2013. The increase in sales is due to greater market penetration in 2014 particularly in the grocery channel. Sales in March 2014 accounted for approximately 50% of the sales for the quarter.

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

| Product Category | Three Months Ended March 31, 2014 (% of Sales) |
|------------------|------------------------------------------------------|
| AquaBall™ | 91% |
| Bazi® | 9% |

Gross Profit

Gross profit for the three months ended March 31, 2014 was \$121,231, compared to \$146,851 for the three months ended March 31, 2013. Gross profit as a percentage of revenue (gross margin) during three months ended March 31, 2014 was 19%. Gross margin was affected by one-time tooling and plate charges related to the introduction of six-packs of AquaBall™ Naturally Flavored Water in four flavors.

Sales, General and Administrative Expense

Sales, general and administrative expenses were \$1,562,334 for the three months ended March 31, 2014, as compared to \$1,475,550 for the three months ended March 31, 2013. This increase is due to increases in salaries, slotting fees and stock-based compensation.

Change in Fair Value of Derivative Liabilities

The Company recorded an expense for the change in fair value of derivative liabilities for the three months ended March 31, 2014 of \$2,125,537. This figure is the result of an increase in the price of the Company's Common Stock during the quarter, causing an increase in the value of warrants issued by the Company.

Interest Expense

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Interest expense for the three months ended March 31, 2014 was \$37,130, as compared to \$228,199 for the three months ended March 31, 2013.

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Income Taxes

There is no income tax expense recorded for the three months ended March 31, 2014 and 2013, due to the Company's net losses. As of March 31, 2014, the Company has tax net operating loss carryforwards and a related deferred tax asset, offset by a full valuation allowance.

Net Loss

Our net loss for the three months ended March 31, 2014 was \$3,603,769, as compared to a net loss of \$1,556,898 for the three months ended March 31, 2013. On a per share basis, our loss was \$0.13 and \$0.06 per share for the three months ended March 31, 2014 and 2013, respectively.

Liquidity and Capital Resources

Our auditors have included a paragraph in their report on our consolidated financial statements, included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2013, indicating that there is substantial doubt as to the ability of the Company to continue as a going concern. The accompanying condensed consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America, which contemplates continuation of the Company as a going concern. As of and for the quarter ended March 31, 2014, the Company incurred a net loss of \$3,603,769, has negative working capital of \$1,961,081 and an accumulated deficit of \$13,845,247. While subsequent to December 31, 2013, the Company raised approximately \$1,860,000 resulting from the sale of shares of its Series B Convertible Preferred Stock ("Series B Preferred"), additional capital may be necessary to advance the marketability of the Company's products to the point at which the Company can sustain operations. Management's plans are to continue to contain expenses, expand distribution and sales of its AquaBall™ Naturally Flavored Water as rapidly as economically possible, and, if necessary, raise capital through equity and debt offerings in the event additional capital is necessary to execute the Company's business, marketing and operating plan, and achieve profitability from continuing operations. The accompanying condensed consolidated financial statements do not include any adjustments that might result in the event the Company is unsuccessful in its plans.

The Company has financed its operations through sales of equity and, to a lesser degree, cash flow provided by sales of AquaBall™. Despite recent sales of debt securities as described below, funds generated from sales of our Common Stock, shares of Series B Preferred and cash flow provided by AquaBall™, sales may be insufficient to fund our operating requirements for the next twelve months. As a result we may require additional capital to continue operating as a going concern. No assurances can be given that we will be successful.

Series B Offering

On November 25, 2013, the Company commenced a private offering of up to 2.0 million shares of Series B Preferred for \$4.00 per share ("Purchase Price"), and five-year warrants ("Warrants"), exercisable for \$0.30 per share (the "Exercise Price"), to purchase that number of shares of the Company's Common Stock equal to 35% of the Purchase Price, divided by the Exercise Price. The Company completed the Series B Offering in February 2014, and, over the course of the offering, offered and sold approximately 2.0 million shares of Series B Preferred and Warrants to purchase approximately 9.3 million shares of Common Stock to certain accredited investors.

Term Loan and Note Conversion

On November 29, 2013, the Company executed a Loan and Security Agreement and other ancillary documents for a \$2.0 million term loan from Avid Bank (the "Bank") (the "Term Loan"), which Term Loan accrues

interest at a rate of prime plus 2.75% and matures on November 29, 2015. The Company's repayment of the Term Loan is secured by a continuing security interest in substantially all of the Company's assets. Proceeds from the Term Loan, together with a portion of the proceeds from the Series B Offering were used to repay certain Notes (defined below) issued during the Note Offering (defined below), totaling approximately \$2.5 million in principal and accrued interest (the "Note Repayment").

In addition to the Note Repayment, holders of the remaining Notes issued during the Note Offering agreed to cancel Notes totaling \$739,706 in principal and accrued interest in exchange for 205,476 shares of Series B Preferred and Warrants to purchase 862,995 shares of Common Stock for \$0.30 per share, on substantially the same terms offered in the Series B Offering (the "Note Conversion").

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On November 29, 2013, the Company repaid approximately \$400,000 in principal, accrued interest and fees from certain promissory notes issued prior to the Note Offering. In addition to this repayment, certain holders of Notes agreed to cancel such Notes totaling \$235,729 in principal and accrued interest in exchange for 58,947 shares of Series B Preferred and Warrants to purchase 275,075 shares of Common Stock for \$0.30 per share, on substantially the same terms offered in the Series B Offering.

Note Offering

On June 20, 2013 the Company commenced a private offering of: (i) convertible promissory notes (the “Notes”) in the aggregate principal amount of up to \$3.3 million; and (ii) and five-year warrants to purchase shares of the Company’s Common Stock at an exercise price of \$1.10 per share to certain accredited investors (the “Note Offering”). During the year ended December 31, 2013, the Company issued Notes in the aggregate principal amount of \$3,126,000, which amount included \$600,000 issued as consideration for the exchange of the outstanding principal and accrued interest of certain promissory notes previously issued by the Company. As of November 29, 2013, all Notes issued during the Offering were either paid in full as a result of the Note Repayment, or exchanged for shares of Series B Preferred and Warrants in connection with the Note Conversion.

Off-Balance Sheet Items

We had no off-balance sheet items as of March 31, 2014.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

A smaller reporting company is not required to provide the information required by this item.

ITEM 4. CONTROLS AND PROCEDURES

(a) Evaluation of disclosure controls and procedures.

We maintain disclosure controls and procedures (as defined in Rule 13a-15(e) and Rule 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”)) that are designed to ensure that information required to be disclosed in our periodic reports filed under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC, and that this information is accumulated and communicated to our management, including our principal executive and financial officers, to allow timely decisions regarding required disclosure.

Our management, with the participation and supervision of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Quarterly Report on Form 10-Q. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. In addition, the design of disclosure controls and procedures must reflect the fact that there are resource constraints and that management is required to apply its judgment in evaluating the benefits of possible controls and procedures relative to their costs.

Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were not effective based on our material weakness in the form of lack of segregation of duties, which stems from our early stage status and limited capital resources to hire additional financial and administrative staff.

(b) Changes in internal controls over financial reporting.

The Company's Chief Executive Officer and Chief Financial Officer have determined that there have been no changes, in the Company's internal control over financial reporting during the period covered by this report identified in connection with the evaluation described in the above paragraph that have materially affected, or are reasonably likely to materially affect, Company's internal control over financial reporting.

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PART II

ITEM 1. LEGAL PROCEEDINGS

From time to time, claims are made against the Company in the ordinary course of business, which could result in litigation. Claims and associated litigation are subject to inherent uncertainties and unfavorable outcomes could occur. In the opinion of management, the resolution of these matters, if any, will not have a material adverse impact on the Company's financial position or results of operations.

On July 1, 2011, a lawsuit was filed in the United States District Court, the Southern District of Ohio, Cincinnati Division, against GT Beverage Company, LLC ("GT LLC") by Dominion Liquid Technologies, LLC. The lawsuit alleges that GT LLC breached terms of a 2010 co-packing agreement, which governed the relationship between the parties. In February 2013, Dominion amended its complaint to add the Company as a defendant in the case. Dominion is seeking monetary damages in an amount exceeding \$800,000. GT LLC has filed its answer denying all of Dominion's claims and expects to vigorously defend the suit. A trial will likely be set in the second or third quarter of 2014.

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ITEM 1A. RISK FACTORS

Our results of operations and financial condition are subject to numerous risks and uncertainties described in our Annual Report on Form 10-K for our fiscal year ended December 31, 2013, filed on March 31, 2014. You should carefully consider these risk factors in conjunction with the other information contained in this Quarterly Report. Should any of these risks materialize, our business, financial condition and future prospects could be negatively impacted. As of March 31, 2014, there have been no material changes to the disclosures made in the above-referenced Form 10-K.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

None.

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ITEM 6. EXHIBITS

| (a) | EXHIBITS |
|---------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 31.1 | Certification of the Principal Executive Officer pursuant to Rule 13a-14(a) and 15d-14(a) |
| 31.2 | Certification of the Principal Financial and Accounting Officer pursuant to Rule 13a-14(a) and 15d-14(a) |
| 32.1 | Certification by the Principal Executive Officer pursuant to 18 U.S.C. 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |
| 32.2 | Certification by the Principal Financial and Accounting Officer pursuant to 18 U.S.C. 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |
| 101.INS | XBRL Instance Document |
| 101.SCH | XBRL Taxonomy Extension Schema |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase |

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SIGNATURES

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

Date: May 13, 2014

TRUE DRINKS HOLDINGS, INC.

By: /s/ Lance Leonard
Lance Leonard
President, Chief Executive Officer, and
Director
(Principal Executive Officer)

Date: May 13, 2014

By: /s/ Daniel Kerker
Daniel Kerker
Chief Financial Officer
(Principal Financial and Accounting
Officer)