BLUE HOLDINGS, INC.
Form 10-Q/A
October 01, 2008

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

FORM 10-Q/A
(Amendment No. 2)

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

For the Quarterly Period Ended: September 30, 2007

Commission File Number: 000-33297

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

Nevada	**88-0450923**
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

4901 Zambrano St., Commerce, CA 90040
(Address of principal executive offices)

(323) 72 6-0297
(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 o

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.

Large Accelerated Filer o   Accelerated Filer o   Non-accelerated Filer x

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

As of November 13, 2007, 26,232,200 shares of the registrant's common stock were outstanding.

TABLE OF CONTENTS

EXPLANATORY NOTE

Blue Holdings, Inc. is filing this Amendment No. 2 to its Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2007 filed with the Securities and Exchange Commission on November 14, 2007 and amended on November 29, 2007 (the “Form 10-Q”). This filing amends and restates our unaudited condensed consolidated balance sheet as of September 30, 2007, and the condensed consolidated statements of operations, stockholders equity (deficiency), and cash flows for the three and nine month periods ending September 30, 2007 to reflect the Company’s failure to record $1,302,842 of inventory purchased from a vendor that was directly paid for by Mr. Guez, and rental expense for an office facility used by the Company that is owned by the living trust of Paul and Elizabeth Guez in the amount of $24,000. The Company has now agreed to a settlement with Mr. Guez relating to these disputed amounts. The effects of the settlement agreement on the previously filed Form 10-Q for the three and nine months ending September 30, 2007 are detailed at Note 1(d) of the accompanying restated condensed consolidated financial statements.

This Amendment No. 2 amends and restates the following items of the Form 10-Q as described above: (i) Part I, Item 1 - Financial Statements; (ii) Part I, Item 2 - Management’s Discussion and Analysis of Result of Operations and Financial Condition; (iii) Part I, Item 4 - Controls and Procedures and (iv) Part II, Item 6 - Exhibits.

All information in the Form 10-Q, as amended by this Amendment No. 2, speaks as to the date of the original filing of our Form 10-Q for such period and does not reflect any subsequent information or events except as noted in this Amendment No. 2. All information contained in this Amendment No. 2 is subject to updating and supplementing as provided in our reports, as amended, filed with the Securities and Exchange Commission subsequent to the date of the initial filing of the Form 10-Q.

PART I

ITEM 1. CONDENSED FINANCIAL STATEMENTS

BLUE HOLDINGS INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

ASSETS		September 30 2007 (As Restated) (Unaudited)		December 31, 2006
Current assets:				
Cash	$	221,202	$	109,031
Due from factor, net of reserves of $106,237 and $178,801, respectively		2,662,425		1,366,588
Accounts receivable, net of reserves of $1,193,000 and $901,941, respectively:				
- Purchased by factor with recourse		3,380,109		7,662,198
- Others		146,672		19,312
Inventories, net of reserves of $590,701 and $1,742,893 respectively		8,943,060		5,394,006
Due from related parties		-		-
Income taxes receivable		61,190		2,030,919
Deferred income taxes		884,101		2,488,082
Prepaid expenses and other current assets		1,120,502		396,810
Total current assets		17,419,261		19,466,946
Deferred income taxes		1,875,925		-
Property and equipment, net of accumulated depreciation		1,881,012		1,611,171
Total assets	$	21,176,198	$	21,078,117

LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIENCY)				
Current liabilities:				
Bank overdraft		903,804	$	266,788
Accounts payable		864,559		2,820,024
Short-term borrowings		14,463,317		10,026,814
Due to related parties		85,778		710,153
Advances from majority shareholder		1,326,842		1,876,991
Current portion of liability for unrecognized tax benefits		96,850		-
Current portion of convertible debt		-		
Accrued expenses and other current liabilities		2,042,379		2,133,932
Total current liabilities		19,783,529		17,834,702
Loan from majority shareholder		2,556,682		-

Non-current portion of liability for unrecognized tax benefits		231,592		-
Non-current portion of convertible debt		-		
Total liabilities		22,571,803		17,834,702
Stockholders' equity (deficiency):				
Preferred stock $0.001 stated value, 5,000,000 shares authorized, 1,000,000 Series A convertible shares issued with 6% cumulative dividend of the designated purchase price and initial conversion price of $0.7347 (note 12)				
Common stock $0.001 par value, 75,000,000 shares authorized, 26,232,200 and 26,057,200 shares issued and outstanding, respectively		26,232		26,057
Additional paid-in capital		5,445,904		4,964,091
Accumulated deficit		(6,867,741)		(1,746,733)
Total stockholders' equity (deficiency)		(1,395,605)		3,243,415
Total liabilities and stockholders' equity (deficiency)	$	21,176,198	$	21,078,117

SEE NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

4

BLUE HOLDINGS INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2007 (AS RESTATED) AND 2006

	Three Months Ending		Nine Months Ending	
	Sept. 30, 2007 (As Restated)	Sept. 30, 2006	Sept. 30, 2007 (As Restated)	Sept. 30, 2006
Net sales	$ 9,458,399	$ 14,551,581	$ 26,300,592	$ 41,610,112
Cost of goods sold	8,511,248	10,116,732	17,092,681	23,797,647
Gross profit	947,151	4,434,849	9,207,911	17,812,465
Selling, distribution & administrative expenses	4,492,960	4,281,467	13,070,619	13,204,554
Income (loss) before other expenses and provision for income taxes	(3,545,809)	153,382	(3,862,708)	4,607,911
Other expenses:				
Interest expense	453,302	257,997	1,205,835	643,759
Expenses relating to the acquisition of Long Rap, Inc.	-	500,887	-	500,887
Income (loss) before provision for income taxes	(3,999,111)	(605,502)	(5,068,543)	3,463,265
Provision (benefit) for income taxes	-	(184,642)	-	1,489,453
Net income (loss)	$ (3,999,111)	$ (420,860)	$ (5,068,543)	$ 1,973,812
Income (loss) per common share, basic and diluted	$ (0.15)	$ (0.02)	$ (0.19)	$ 0.08
Weighted average shares outstanding, basic and diluted	26,232,200	26,057,200	26,154,422	26,057,200

SEE NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

BLUE HOLDINGS INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY (DEFICIENCY)
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2007 (UNAUDITED) (RESTATED)

	Common Shares Issued Number	Par Value 0.001	Additional Paid In Capital	Accumulated Deficit	Total
Balance, January 1, 2007	26,057,200	$ 26,057	$ 4,964,091	$ (1,746,733)	$ 3,243,415
Fair value of vested stock options	-	-	254,488		254,488
Cumulative effect of adoption of FIN 48	-	-		(52,465)	(52,465)
Fair value of shares issued under co-branding agreement	175,000	175	227,325		227,500
Net loss for the period (as restated)	-	-	-	(5,068,543)	(5,068,543)
Balance, Setptember 30, 2007 (as restated)	26,232,200	$ 26,232	$ 5,445,904	$ (6,867,741)	$ (1,395,605)

SEE NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

BLUE HOLDINGS INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2007 AND 2006 (UNAUDITED)

		2007 (As Restated)		2006
Cash flows from operating activities:				
Net income (loss)	$	(5,068,543)	$	1,973,812
Adjustments to reconcile net income to cash used in operating activities:				
Depreciation and amortization		312,442		136,644
Fair value of vested stock options		254,488		356,528
Changes in assets and liabilities:				
Accounts receivable		4,154,729		(3,598,620)
Due from factor		(1,295,837)		(789,990)
Income taxes receivable		1,969,729		-
Inventories		(3,549,054)		(3,629,291)
Due to related parties		(624,375)		399,950
Due from related parties		-		15,974
Deferred income taxes		4,033		(235,423)
Prepaid expenses and other current assets		(496,192)		(740,641)
Income tax payable		-		(650,468)
Bank overdraft		637,016		(594,303)
Accounts payable		(1,955,466)		553,751
Other current liabilities		(91,553)		588,046
Net cash used in operating activities		(5,748,583)		(6,214,031)
Cash flows from investing activities:				
Purchase of equipment		(582,282)		(1,216,063)
Net cash used in investing activities		(582,282)		(1,216,063)
Cash flows from financing activities:				
Short-term borrowings		4,436,503		4,912,007
Advances from majority shareholder		2,006,533		2,412,025
Net cash provided by financing activities		6,443,036		7,324,032
Net (decrease) increase in cash		112,171		(106,062)
Cash at beginning of period		109,031		228,127
Cash at end of period	**$**	**221,202**	**$**	**122,065**

SUPPLEMENTAL CASH FLOW INFORMATION:

Cash paid for interest	$	1,205,835	$	643,759
Cash paid for income tax	$	-	$	2,551,605

SUPPLEMENTAL DISCLOSURE OF NON-CASH FINANCING AND INVESTING ACTIVITIES:

Cumulative effect of adoption of FIN 48	$	52,465	$	-
Increase in prepaids for fair value of stock issued under co-branding agreement	$	227,500	$	-

SEE NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

7

BLUE HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2007 (AS RESTATED) AND 2006

NOTE 1 – BASIS OF PRESENTATION, ORGANIZATION AND NATURE OF OPERATIONS

(a) Basis of Presentation

The interim condensed consolidated financial statements are unaudited, but in the opinion of management of the Company, contain all adjustments, which include normal recurring adjustments, necessary to present fairly the financial position at September 30, 2007 and the results of operations for the three and nine months ended September 30, 2007 and 2006 and cash flow for the nine months ended September 30, 2007 and 2006. The condensed consolidated balance sheet as of December 31, 2006 is derived from the Company's audited financial statements.

Certain information and footnote disclosures normally included in financial statements that have been presented in accordance with generally accepted accounting principles have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission with respect to interim financial statements, although management of the Company believes that the disclosures contained in these financial statements are adequate to make the information presented therein not misleading. For further information, refer to the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-KSB for the fiscal year ended December 31, 2006, as filed with the Securities and Exchange Commission.

The Company's results of operations for the three and nine months ended September 30, 2007 are not necessarily indicative of the results of operations to be expected for the full fiscal year ending December 31, 2007.

The condensed consolidated financial statements include the operations of Blue Holdings, Inc. and its wholly-owned subsidiaries. Intercompany transactions and balances are eliminated in consolidation.

(b) Organization

Blue Holdings, Inc. (the "Company") was incorporated in the State of Nevada on February 9, 2000 under the name Marine Jet Technology Corp. On April 14, 2005, Blue Holdings entered into an Exchange Agreement with Antik Denim, LLC ("Antik"). At the closing of the transactions contemplated by the Exchange Agreement, which occurred on April 29, 2005, Blue Holdings acquired all of the outstanding membership interests of Antik (the "Interests") from the members of Antik, and the members contributed all of their Interests to Blue Holdings. In exchange, Blue Holdings issued to the members 843,027 shares of Series A Convertible Preferred Stock, par value $0.001 per share, of Blue Holdings ("Preferred Shares"), which, on June 7, 2005, as a result of a change to Marine Jet Technology Corp.'s name to Blue Holdings, Inc. and a 1 for 29 reverse stock split, were converted into 24,447,783 shares of Blue Holding's common stock on a post-reverse stock split basis.

As such, immediately following the closing and upon the conversion of the Preferred Shares, the Antik members and Elizabeth Guez, our former Chief Operating Officer and wife of Paul Guez, owned approximately 95.8% of the total issued and outstanding common stock of Blue Holdings on a fully-diluted basis. Following completion of the exchange transaction, Antik became a wholly-owned subsidiary of Blue Holdings. The acquisition was accounted for as a reverse merger (recapitalization) in the accompanying financial statements with Antik deemed to be the accounting acquirer and Blue Holdings deemed to be the legal acquirer. As such, the financial statements herein include those of Antik since September 13, 2004 (the date of its inception). All assets and liabilities of Marine Jet Technology Corp. were assumed by the major shareholder of Blue Holdings, Inc. prior to the exchange transaction and were inconsequential to the merged companies.

8

BLUE HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2007 (AS RESTATED) AND 2006

On June 7, 2005, Marine Jet Technology Corp. changed its name to Blue Holdings, Inc., and increased its authorized number of shares of common stock to 75,000,000.

On October 31, 2005, the Company entered into an exchange agreement with Taverniti So Jeans, LLC, a California limited liability company ("Taverniti"), and the members of Taverniti (the "Taverniti Members"). Under the exchange agreement, the Company acquired all of the outstanding membership interests of Taverniti (the "Taverniti Interests") from the Taverniti Members, and the Taverniti Members contributed all of their Taverniti Interests to the Company. In exchange, the Company issued to the Taverniti Members, on a pro rata basis, an aggregate of 500,000 shares of the Common Stock, par value $0.001 per share, of the Company, and paid to the Taverniti Members, on a pro rata basis, an aggregate of Seven Hundred Fifty Thousand Dollars ($750,000). At the closing of the exchange transaction, Taverniti became a wholly-owned subsidiary of the Company. Paul Guez, the Company's Chairman and majority shareholder, was and remains the sole manager and was a member of Taverniti. Elizabeth Guez, Paul Guez's spouse and the Company's former Chief Operating Officer, was also a member of Taverniti. Two other members of Mr. and Mrs. Guez's family were the remaining members of Taverniti. The transaction was accounted for as a combination of entities under common control. As such, the financial statements herein have been presented to include the operations of Taverniti since September 13, 2004, the date of its inception, and the $750,000 payment was considered as a deemed distribution to the members of Taverniti upon the closing of the combination.

(c) Nature of Operations

The Company operates exclusively in the wholesale apparel industry. The Company designs, develops, markets and distributes high fashion jeans and accessories under the brand names *Antik Denim*, *Yanuk, Faith Connexion* and *Taverniti So Jeans*. The Company's products currently include jeans, jackets, belts, purses and T-shirts. The Company currently sells its products in the United States, Canada, and Japan directly to department stores and boutiques and through distribution arrangements in certain foreign jurisdictions. The Company is headquartered in Commerce, California and maintains showrooms in New York and Los Angeles. The Company opened a retail store in Los Angeles during August 2005 and another store in San Francisco in September 2006. These retail operations are not yet significant to the consolidated operations.

(d) Restatement of Condensed Consolidated Financial Statements

The Company has restated its unaudited condensed consolidated balance sheet as of September 30, 2007, and the condensed consolidated statements of operations, stockholders equity (deficiency), and cash flows for the three and nine month periods ending September 30, 2007.

From time to time Paul Guez, the Company's Chairman of the Board and majority stockholder, and his spouse Elizabeth Guez made advances to the Company to support its working capital needs. These advances are part of a line of credit agreement with Mr. Guez which allows the Company to borrow from him up to a maximum of $3,000,000 at an interest rate of 6% per annum (the "Revolving Line"). The Company may repay the advances in full or in part at any time until the Revolving Line expires and repayment is required on December 31, 2007. The Company also maintains several due/to from related party accounts with Mr. Guez and his affiliated companies where funds are advanced to cover certain operating expenses. These advances are unsecured, non-interest bearing with no formal terms of repayment.

BLUE HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2007 (AS RESTATED) AND 2006

In early May 2008, Mr. Guez informed the Company of claims for sums he believed were due and owing to him pursuant to advances made to and payments made on behalf of the Company during fiscal 2007 that were inaccurately recorded in the Company's previously filed financial statements for the three and nine month periods ended September 30, 2007.

The Audit Committee commenced a review of these potential errors and instructed management to review the Registrant's books and records to obtain a summary of transactions recorded and amounts owed per such records. These investigations revealed accounting errors in the Registrant's related party accounts pertaining to payables due Mr. Guez as of September 30, 2007. These errors related to the Company not recording $1,302,842 of inventory purchased from a vendor that was directly paid for by Mr. Guez, and rental expense for an office facility used by the Company that is owned by the living trust of Paul and Elizabeth Guez in the amount of $24,000. The Company has now agreed to a settlement with Mr. Guez relating to these disputed amounts.

In light of this dispute and settlement, the Audit Committee and Management of the Company have determined that the Company's unaudited condensed consolidated financial statements for the three and nine months ended September 30, 2007 need to be restated due to accounting errors in the Company's related party accounts. The effects of the settlement agreement on the previously filed Form 10-Q for the three and nine months ending September 30, 2007 are summarized as follows:

BLUE HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2007 (AS RESTATED) AND 2006

ASSETS	September 30 2007 (As initially reported)	September 30 2007 (Adjustment)		September 30 2007 (As restated)
Current assets:				
Cash	$ 221,202			$ 221,202
Due from factor, net of reserves	2,662,425			2,662,425
Accounts receivable, net of reserves:				
- Purchased by factor with recourse	3,380,109			3,380,109
- Others	146,672			146,672
Inventories, net of reserves	8,943,060			8,943,060
Due from related parties	-			-
Income taxes receivable	61,190			61,190
Deferred income taxes	868,011	16,090	(3)	884,101
Prepaid expenses and other current assets	1,120,502			1,120,502
Total current assets	17,403,171	16,090		17,419,261
Deferred income taxes	1,875,925			1,875,925
Property and equipment, net of accumulated depreciation	1,881,012			1,881,012
Total assets	$ 21,160,108	$ 16,090		$ 21,176,198
LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIENCY)				
Current liabilities:				
Bank overdraft	903,804			903,804
Accounts payable	864,559			864,559
Short-term borrowings	14,463,317			14,463,317
Due to related parties	85,778			85,778
Advances from majority shareholder	-	1,326,842	(1,2)	1,326,842
Current portion of liability for unrecognized tax benefits	96,850			96,850
Current portion of convertible debt	-			-
Accrued expenses and other current liabilities	2,042,379			2,042,379
Total current liabilities	18,456,687	1,326,842		19,783,529
Loan from majority shareholder	2,556,682			2,556,682
Non-current portion of liability for unrecognized tax benefits	231,592			231,592
Non-current portion of convertible debt	-	-		-
Total liabilities	21,244,961	1,326,842		22,571,803
Stockholders' equity (deficiency):				
Preferred stock $0.001 stated value, 5,000,000 shares authorized, 1,000,000				

Series A convertible shares issued with 6% cumulative dividend of the designated purchase price and initial conversion price of $0.7347 (note 12)			
Common stock $0.001 par value, 75,000,000 shares authorized	26,232		26,232
Additional paid-in capital	5,445,904		5,445,904
Accumulated deficit	(5,556,989)	(1,310,752)	(6,867,741)
Total stockholders' equity (deficiency)	(84,853)	(1,310,752)	(1,395,605)
Total liabilities and stockholders' equity (deficiency)	$ 21,160,108	$ 16,090	$ 21,176,198

11

BLUE HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2007 (AS RESTATED) AND 2006

	Three Months Ended				Nine Months Ended			
	Sept. 30, 2007 (As initially reported)	Sept. 30, 2007 (Adjustment)		Sept. 30, 2007 (As restated)	Sept. 30, 2007 (As initially reported)	Sept. 30, 2007 (Adjustment)		Sept. 30, 2007 (As restated)
Net sales	$ 9,458,399	-		$ 9,458,399	$ 26,300,592	-		$ 26,300,592
Cost of goods sold	8,511,248	-		8,511,248	15,789,839	1,302,842	(1)	17,092,681
Gross profit	947,151	-		947,151	10,510,753	(1,302,842)		9,207,911
Selling, distribution & administrative expenses	4,468,960	24,000	(2)	4,492,960	13,046,619	24,000	(2)	13,070,619
Income (loss) before other expenses and provision for income taxes	(3,521,809)	(24,000)		(3,545,809)	(2,535,866)	(1,326,842)		(3,862,708)
Other expenses:								
Interest expense	453,302	-		453,302	1,205,835	-		1,205,835
Expenses relating to the acquisition of Long Rap, Inc.				-				-
Income (loss) before provision for income taxes	(3,975,111)	(24,000)		(3,999,111)	(3,741,701)	(1,326,842)		(5,068,543)
Provision (benefit) for income taxes	(92,826)	92,826	(3)	-	16,090	(16,090)	(3)	-
Net income (loss)	$ (3,882,285)	$ (116,826)		$ (3,999,111)	$ (3,757,791)	$ (1,310,752)		$ (5,068,543)
Income (loss) per common share, basic and diluted	$ (0.15)	$ (0.00)	(4)	$ (0.15)	$ (0.14)	$ (0.05)	(4)	$ (0.19)
Weighted average shares outstanding, basic and diluted	26,232,200	-		26,232,200	26,154,422	-		26,154,422

BLUE HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2007 (AS RESTATED) AND 2006

	2007 (As initially reported)	2007 (Adjustment)		2007 (As restated)
Cash flows from operating activities:				
Net income (loss)	$ (3,757,791)	$ (1,310,752)		$ (5,068,543)
Adjustments to reconcile net income to cash used in operating activities:				
Depreciation and amortization	312,442			312,442
Fair value of vested stock options	254,488			254,488
Changes in assets and liabilities:				
Accounts receivable	4,154,729			4,154,729
Due from factor	(1,295,837)			(1,295,837)
Income taxes receivable	1,969,729			1,969,729
Inventories	(3,549,054)			(3,549,054)
Due to related parties	(624,375)			(624,375)
Deferred income taxes	20,123	(16,090)	(3)	4,033
Prepaid expenses and other current assets	(496,192)			(496,192)
Bank overdraft	637,016			637,016
Accounts payable	(1,955,466)			(1,955,466)
Other current liabilities	(91,553)			(91,553)
Net cash used in operating activities	(4,421,741)	(1,326,842)		(5,748,583)
Cash flows from investing activities:				
Purchase of equipment	(582,282)	-		(582,282)
Net cash used in investing activities	(582,282)	-		(582,282)
Cash flows from financing activities:				
Short-term borrowings	4,436,503	-		4,436,503
Advances from majority shareholder	679,691	1,326,842	(1,2)	2,006,533
Net cash provided by financing activities	5,116,194	1,326,842		6,443,036
Net (decrease) increase in cash	112,171	-		112,171
Cash at beginning of period	109,031	-		109,031
Cash at end of period	**$ 221,202**	**$ -**		**$ 221,202**
SUPPLEMENTAL CASH FLOW INFORMATION:				
Cash paid for interest	$ 1,205,835	$ -		$ 1,205,835
Cash paid for income tax	$ -	$ -		$ -

SUPPLEMENTAL DISCLOSURE OF NON-CASH FINANCING AND INVESTING ACTIVITIES:

Cumulative effect of adoption of FIN 48	$	52,465	$	-	$	52,465
Increase in prepaids for fair value of stock issued under co-branding agreement	$	227,500	$	-	$	227,500

BLUE HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2007 (AS RESTATED) AND 2006

Description of adjustments:

1. To reflect a $1,302,842 adjustment to cost of sales and to increase payable to Paul Guez at September 30, 2007 for inventory purchases paid directly to a vendor by Mr. Guez that were not previously recorded.

2. To reflect a $24,000 adjustment to selling distribution and administrative expenses for lease of an office facility to the Company by the living trust of Paul and Elizabeth Guez that was previously unrecorded.

3. To remove the previously recorded tax provision for the period.

4. To reflect change in loss per share based on adjustments.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) 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. On an ongoing basis, we evaluate estimates, including those related to returns, discounts, bad debts, inventories, intangible assets, income taxes, contingencies and litigation. We base our estimates on historical experience and on various 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.

(b) Revenue Recognition

Revenue is recognized when merchandise has been shipped against a customer’s written purchase order, the risk of ownership has passed, selling price has been fixed and determined and collectibility is reasonably assured either through payment received, or fulfillment of all the terms and conditions of the particular purchase order. Revenue is recorded net of estimated returns, charge backs and markdowns based on management’s estimates and historical experience.

(c) Advertising

Advertising costs are expensed as of the first date the advertisements take place. Advertising expenses included in selling expenses approximated $165,442 and $285,016 for the three and nine months ended September 30, 2007, respectively, as compared with $51,420 and $627,482 for the same respective periods last year.

BLUE HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2007 (AS RESTATED) AND 2006

(d) Shipping and Handling Costs

Freight charges are included in selling, distribution and administrative expenses in the statement of operations and approximated $187,731 and $484,966 for the three and nine months ended September 30, 2007, respectively, as compared to $263,881 and $588,672 for the same respective periods in the prior year.

(e) Major Suppliers

We purchase our fabric, thread and other raw materials from various industry suppliers within the United States and abroad. We do not currently have any long-term agreements in place for the supply of our fabric, thread or other raw materials. The fabric, thread and other raw materials used by us are available from a large number of suppliers worldwide. During the three months ended September 30, 2007, only three suppliers accounted for more than 10% of our purchases. Purchases from these suppliers were 12.9%, 11.2% and 10.7%, respectively. During the nine months ended September 30, 2007, two suppliers accounted for more than 10% of our purchases and purchases from these suppliers were 15.4% and 11.4% , respectively. During the three months ended September 30, 2006, three suppliers accounted for more than 10% of our purchases. Purchases from these suppliers were 31.5%, 13.0% and 11.8%, respectively. During the nine months ended September 30, 2006, two suppliers accounted for more than 10% of our purchases and purchases from these suppliers were 13.6% and 12.9%, respectively.

(f) Major Customers

During three months ended September 30, 2007, one customer accounted for more than 10% of the Company's sales and sales to that customer was 11.1%. For the nine months ended September 30, 2007, two customers accounted for more than 10% of the Company's sales and sales to those customers were 10.7% and 10.5%, respectively. During fiscal 2006, two customers accounted for more than 10% of the Company's sales. Sales to those customers were 30.3% and 11.6%, for the three months ended September 30, 2006 and 15.6% and 14.3% for the nine months ended September 30, 2006, respectively.

International sales accounted for approximately 17.9% and 20.9% of the Company's sales during the three and nine months ended September 30, 2007, respectively, including Japan which accounted for 9.7% and 12%, respectively, of our total sales. International sales accounted for approximately 25% and 30% of sales in the three and nine months ended September 30, 2006, respectively, including Japan which accounted for 16% and 17%, respectively, of our total sales.

As of September 30, 2007 and December 31, 2006, one customer accounted for 18% and 42% of total accounts receivable, respectively.

(g) Stock-Based Compensation

In December 2004, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards 123R, "Share-Based Payment" ("SFAS 123R"). This statement requires that the cost resulting from all share-based payment transactions be recognized in the financial statements. This statement establishes fair value as the measurement objective in accounting for share-based payment arrangements and requires all entities to apply a fair-value based measurement method in accounting for share-based payment transactions with employees except for equity instruments held by employee share ownership plans. Effective January 1, 2006, the Company adopted the fair value recognition provisions of SFAS 123R, using the modified prospective method. Under this method, the provisions of SFAS 123R apply to all awards granted or modified after the date of adoption and all previously granted awards not yet vested as of the date of adoption.

BLUE HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2007 (AS RESTATED) AND 2006

The fair value of options was estimated on the date of grant using the Black-Scholes option pricing model with the following weighted-average assumptions for the three months ended September 30, 2007 and 2006:

	September 30, 2007	September 30, 2006
Dividend yield	—	—
Risk-free interest rate	4.50%	4.50%
Expected volatility	48.20%	46.01%
Expected life of options	6 years	5 years

(h) Earnings per Share

Statement of Financial Accounting Standards No. 128, “Earnings per Share,” requires presentation of basic earnings per share (“Basic EPS”) and diluted earnings per share (“Diluted EPS”). Basic earnings (loss) per share are computed by dividing net income by the weighted average number of common shares outstanding during the period. Diluted earnings per share reflects the potential dilution, using the treasury stock method, that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the Company. In computing diluted earnings per share, the treasury stock method assumes that outstanding options and warrants are exercised and the proceeds are used to purchase common stock at the average market price during the period. Options and warrants will have a dilutive effect under the treasury stock method only when the average market price of the common stock during the period exceeds the exercise price of the options and warrants.

At September 30, 2007 and 2006, potentially dilutive securities consisted of outstanding common stock options to acquire 1,096,500 and 685,000 shares, respectively. These potentially dilutive securities were not included in the calculation of loss per share for the three and nine months ended September 30, 2007 as they were anti-dilutive for the periods in 2007 and insignificant to the calculation in 2006. Accordingly, basic and diluted earnings per share for each of the three and nine months ended September 30, 2007 and 2006 are the same.

Issued but unvested shares of common stock under forfeitable service agreements are excluded from the calculations of basic and diluted earnings per share until such shares are earned.

(i) Reclassifications

Certain prior year balance sheet items have been reclassified to conform to the current period presentation.

(j) Adoption of new accounting policy

Effective January 1, 2007, the Company adopted Financial Accounting Standards Board Interpretation No. 48, "Accounting for Uncertainty in Income Taxes ("FIN 48")—an interpretation of FASB Statement No. 109, Accounting for Income Taxes." The Interpretation addresses the determination of whether tax benefits claimed or expected to be claimed on a tax return should be recorded in the financial statements. Under FIN 48, we may recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position should be measured based on the largest benefit that has a greater than fifty percent likelihood of being realized upon ultimate settlement. FIN 48 also provides guidance on derecognition, classification, interest and penalties on income taxes, accounting in interim periods and requires increased disclosures. At the date of adoption, and as of September 30, 2007, the Company made a cumulative effect adjustment. See note 8.

The Company files income tax returns in the U.S. federal jurisdiction and various states. The Company is subject to U.S. federal or state income tax examinations by tax authorities for years after 2002. The Company's tax returns are currently under examination by the government. As of September 30, 2007, the taxing authorities have not proposed any significant adjustments to taxable income. The Company does not expect to receive any adjustments that would result in a material change to its final position.

The Company's policy is to record interest and penalties on uncertain tax provisions as income tax expense. See note 8.

(k) Recent accounting pronouncements

In February 2007, the Financial Accounting Standards Board (FASB) issued FASB Statement No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities — including an amendment of FASB Statement No. 115" (FAS 159). FAS 159, which becomes effective for the company on January 1, 2008, permits companies to choose to measure many financial instruments and certain other items at fair value and report unrealized gains and losses in earnings. Such accounting is optional and is generally to be applied instrument by instrument. The company does not anticipate that election, if any, of this fair-value option will have a material effect on its consolidated financial condition, results of operations, cash flows or disclosures.

In September 2006, the FASB issued FAS No. 157 ("FAS 157"), "Fair Value Measurements," which establishes a framework for measuring fair value in accordance with GAAP and expands disclosures about fair value measurements. FAS 157 does not require any new fair value measurements but rather eliminates inconsistencies in guidance found in various prior accounting pronouncements. FAS 157 is effective for fiscal years beginning after November 15, 2007. The Company is currently evaluating the impact this standard will have on its consolidated financial condition, results of operations, cash flows or disclosures.

NOTE 3 – DUE FROM FACTOR

We use a factor for working capital and credit administration purposes. Under the various factoring agreements entered into separately by Blue Holdings, Antik and Taverniti, the factor purchases all the trade accounts receivable assigned by the Company and its subsidiaries and assumes all credit risk with respect to those accounts approved by it.

The factor agreements provide that we can borrow an amount up to 90% of the value of our purchased customer invoices, less a reserve of 10% of unpaid accounts purchased and 100% of all such accounts which are disputed. The factor agreements provide for automatic renewal subject to 120 days' termination notice from any party. The factor also makes available to all three companies a combined line of credit up to the lesser of $2.4 million or 50% of the value of eligible raw materials and finished goods. As of September 30, 2007, borrowings under this line of credit were $14.5 million of which, the Company drew down $2.4 million of this credit line against inventory, $4.9 million against accounts receivable and $7.2 million against personal guarantees of Paul Guez, our Chairman and majority shareholder, and the living trust of Paul and Elizabeth Guez.

As of September 30, 2007, the factor holds $2,831,979 of accounts receivable purchased from us on a without recourse basis and has made advances to us of $63,315 against those receivables, resulting in a net balance amount Due from Factor of $2,662,425, net of reserves of $106,237, as of September 30, 2007. The Company has accounted for the sale of receivables to the factor in accordance with SFAS No. 140, "Accounting for the Transfers and Servicing of Financial Assets and Extinguishments of Liabilities."

As of September 30, 2007, the factor also held as collateral $3,380,109 of accounts receivable that were subject to recourse, against which the Company has provided reserves of $1,193,000 and as of September 30, 2007, the Company received advances totaling $14,463,000 against such receivables, eligible inventory, intangibles, and on the personal guarantee of Mr. Paul Guez. The Company has included the $3,114,334 in accounts receivable, and has reflected the $14,463,000 as short term borrowings on the accompanying balance sheet. The factor commission against such receivables is 0.4% and interest is charged at the rate of 1% over the factor's prime lending rate per annum.

The factor commission on receivables purchased on a without recourse basis is 0.75% if the aggregate amount of approved invoices is below $10 million per annum, 0.70% if between $10 million and $20 million and 0.65% if between $20 million and $30 million. The Company is contingently liable to the factor for merchandise disputes, customer claims and the like on receivables sold to the factor. To the extent that the Company draws funds prior to the deemed collection date of the accounts receivable sold to the factor, interest is charged at the rate of 1% over the factor's prime lending rate per annum. Factor advances are collateralized by the non-factored accounts receivable, inventories and the personal guarantees of Paul Guez, our Chairman and majority shareholder, and the living trust of Paul and Elizabeth Guez (see note 6).

BLUE HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2007 (AS RESTATED) AND 2006

NOTE 4 – RELATED PARTY TRANSACTIONS

Inventories at September 30, 2007 and December 31, 2006 are summarized as follows:

	September 30, 2007 (Unaudited)	December 31, 2006
Raw Materials	$ 3,027,735	$ 3,583,019
Work-in-Process	1,037,913	991,775
Finished Goods	5,468,113	2,562,105
	9,533,761	7,136,899
Less: Inventory valuation allowance	($590,701)	(1,742,893)
TOTAL	$ 8,943,060	$ 5,394,006

NOTE 5 – PROPERTY AND EQUIPMENT

Property and equipment at September 30, 2007 and December 31, 2006 are summarized as follows:

	September 30, 2007 (Unaudited)	December 31, 2006
Furniture	$ 33,316	$ 14,294
Leasehold Improvements	1,308,423	1,219,094
Computer Equipment	1,090,826	616,551
	2,432,565	1,849,939
Less: Accumulated depreciation and amortization	(551,553)	(238,768)
	$ 1,881,012	$ 1,611,171

Depreciation expense for the three months ended September 30, 2007 and 2006 was $124,763 and $59,174, respectively and for the nine months ended September 30, 2007 and 2006 was $312,442 and $136,644, respectively.

NOTE 6 – RELATED PARTY TRANSACTIONS

The Company purchased fabric at cost from Blue Concept, LLC an entity that is owned by Paul Guez, the Company's Chairman, for $1,502 and $184,830 during the three and nine months ended September 30, 2007, respectively, and $10,555 and $262,213 respectively, during the same periods in the prior year.

On January 1, 2006, the Company leased its facility at Commerce, California from Azteca Production International Inc., as a sub-tenant and is paying it $19,030 per month. Azteca is a company that is co-owned by Paul Guez. Rent expense includes $57,090 and $171,270, respectively, for the three and nine months ended September 30, 2007, paid under this lease.

On September 1, 2007, the Company began occupying a design and merchandising facility owned by the living trust of Paul and Elizabeth Guez. While there is no formal lease agreement between the Company and the living trust of Paul and Elizabeth Guez, the parties have agreed that the Company will pay the living trust of Paul and Elizabeth Guez $24,000 per month in rent on a month-to-month basis.

On July 5, 2005 the Company entered into a ten-year license agreement with Yanuk Jeans, LLC., an entity that is solely owned by Paul Guez. Under the terms of the agreement, the Company became the exclusive licensor for the design, development, manufacture, sale, marketing and distribution of the *Yanuk* brand products to the wholesale and retail trade. The Company pays to Yanuk Jeans, LLC a royalty of six percent of all net sales of the licensed products and a guaranteed minimum royalty on an annual basis. Yanuk has agreed to waive such royalties due for the three and nine months ended September 30, 2007, and has agreed to waive such royalties through December 31, 2008. Yanuk Jeans, LLC is solely owned by Paul Guez. In addition, during the term of the license agreement, the Company has the option to purchase from Yanuk Jeans, LLC the property licensed under the agreement. The royalties paid and payable for the three and nine months ended September 30, 2006, were $60,902 and $243,833, respectively.

On October 6, 2005, the Company entered into a five-year license agreement with Yanuk Jeans, LLC. Under the terms of the agreement, the Company became the exclusive licensor for the design, development, manufacture, sale, marketing and distribution of Yanuk Jeans, LLC's *U* brand products to the wholesale and retail trade. The Company pays to Yanuk Jeans, LLC a royalty of five percent of all net sales of the licensed products and shall pay a guaranteed minimum royalty on an annual basis. In addition, during the term of the license agreement, the Company has the option to purchase from Yanuk Jeans, LLC the property licensed under the agreement. The royalties for the three and nine months ended September 30, 2007 paid or payable to Yanuk Jeans, LLC for the *U* brand products was $0 and $0, respectively and $0 and $0, respectively, for the same period last year.

Paul Guez and the living trust of Paul and Elizabeth Guez have guaranteed all advances and ledger debt due to the Company's factor (see note 3).

BLUE HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2007 (AS RESTATED) AND 2006

On August 27, 2005, the Company opened a retail store on Melrose Avenue, Los Angeles, California and took over all the obligations of a 10-year property lease which was entered into by Blue Concept, LLC in April 2005. The lease will expire on March 15, 2015.

Taverniti is the exclusive licensee for the design, development, manufacture, sale, marketing and distribution of the *Taverniti So Jeans* trademark in the denim and knit sports wear categories for men and women. It is paying royalties to Taverniti Holdings, LLC in the ranges of 5-8 percent depending on the net sales of the licensed products pursuant to a license agreement with Taverniti Holdings, LLC. Taverniti Holdings, LLC is jointly owned by Paul Guez (60%) and Jimmy Taverniti (40%), the designer of the products for the brand, and Mr. Guez is the sole manager. The license agreement was signed in May 2004 and expires on December 31, 2015. Royalties paid or payable for the three months ended September 30, 2007 and 2006 were $77,878 and $217,728, respectively, and $289,634 and $874,254 for the nine months ended September 30, 2007 and 2006, respectively.

NOTE 7 – DUE FROM/TO RELATED PARTIES

The related parties are the Company's majority shareholder (who is also the Chairman, Chief Executive Officer and President of the Company) and limited liability companies that are either owned or co-owned by the majority shareholder. These amounts are all unsecured and non-interest bearing. All non-trade related advances from related parties have been repaid. Trade-related outstanding items follow regular payment terms as invoiced. As of September 30, 2007 and December 31, 2006, total trade-related items due to related parties amounted to $85,778 and $710,153, respectively.

From time to time, the Company's majority shareholder, Mr. Paul Guez, made advances to the Company to support its working capital needs. These advances were non-interest bearing and unsecured, with no formal terms of repayment. On July 1, 2006, Mr. Guez converted the advances to a line of credit in an agreement with the Company. The line of credit allows the Company to borrow from him up to a maximum of $3 million at an interest rate of 6% per annum. The Company may repay the advances in full or in part at any time until the credit line expires and repayment is required, on December 31, 2007. As of September 30, 2007 and December 31, 2006, the balance of these advances was $2,556,682 and $1,876,991 respectively and accrued interest thereon was $104,857 and $0, respectively. Interest expense includes $37,356 and $0, for three months ended September 30, 2007 and 2006, respectively, and $104,857 and $0, for nine months ended September 30, 2007 and 2006, respectively.

Subsequent to September 30, 2007 the Company agreed to issue convertible preferred shares valued at $2,556,682 to Mr. Guez in satisfaction of $2,556,682 of advances to the Company by the majority stockholder (see Note 12).

Subsequent to September 30, 2007, in early May, 2008, as detailed above at Note 1(d), the Company and Mr. Guez agreed that, as of September 30, 2007, Mr. Guez was in fact owed additional monies totaling $1,326,842, which had not previously been reflected in the Company's financial statements. Such monies were advanced under the same terms as the line of credit agreement described above and are reflected as a current liability in these restated financial statements.

BLUE HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2007 (AS RESTATED) AND 2006

NOTE 8 – INCOME TAX

The Company accounts for income taxes and the related accounts under the liability method. Deferred tax liabilities and assets are determined based on the difference between the financial statement and tax bases of assets and liabilities using enacted rates expected to be in effect during the year in which the basis differences reverse.

The Company's provision for income taxes, as restated, was $0 for the nine months ended September 30, 2007 compared to $1,489,453 for the same period of the prior year.

The provision for income taxes consists of the following for the periods ended September 30:

	2007 (As Restated)	2006
Current		
Federal	$ 0	$ 1,305,011
State	0	419,865
Deferred		
Federal	0	(189,462)
State	0	(45,961)
Provision for income tax expense	$ 0	$ 1,489,453

A reconciliation of the statutory federal income tax rate to the effective tax rate is as follows for the periods ended September 30:

	2007	2006
Statutory federal rate	34.0%	34.0%
State taxes, net of federal benefit	6.6%	7.1%
Income not taxed at Company level	0.0%	2.0%
Permanent differences	0.0%	-0.1%
Change in valuation reserve	-40.4%	0.0%
Unrecognized tax benefits	-0.3%	0.0%
Other	0.1%	0.0%
Effective tax rate	0.0%	43.0%

The Company and its subsidiaries files income tax returns in the U.S. federal jurisdiction and various state jurisdictions. With few exceptions, the Company is no longer subject to U.S. federal or state and local income tax examinations by tax authorities for years before 2003. The Internal Revenue Service (IRS) commenced an examination of the Company's U.S. income tax return for 2005 in the first quarter of 2007 that is anticipated to be completed by the end of 2007. As of September 30, 2007, the IRS has not proposed any adjustments.

The Company adopted the provisions of FASB Interpretation No.48, Accounting for Uncertainty in Income Taxes, on January 1, 2007. As a result of the implementation of Interpretation 48, the Company recognized a $52,465 increase in the liability for unrecognized tax benefits, which was accounted for as a reduction to the January 1, 2007 balance of retained earnings. A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows:

Balance at January 1, 2007	$	(310,458)
Additions based on tax positions related to the current year		-
Additions for tax positions of prior years		(17,984)
Reductions for tax positions of prior years		-
Settlements		-
Balance	$	(328,442)

Included in the balance at September 30, 2007 are $263,731 of tax positions for which the ultimate deductibility is highly certain but for which there is uncertainty about the timing of such deductibility. Because of the impact of deferred tax accounting, other than interest and penalties, the disallowance of the shorter deductibility period would not affect the annual effective tax rate but would accelerate the payment of cash to the taxing authority to an earlier period.

The Company recognizes accrued interest and penalties related to unrecognized tax benefits in income tax expense. During the period ended September 30, 2007, the Company recognized in income tax expense $ 0 for interest and penalties, as reflected in these restated financial statements. The Company included in its balance for unrecognized tax benefits at September 30, 2007 $61,489 for the payment of interest and penalties.

NOTE 9 – STOCK OPTIONS

Under the Company's 2005 Stock Incentive Plan (the "Company Plan"), the Company may grant qualified and nonqualified stock options and stock purchase rights to selected employees. The Company reserved 2,500,000 shares of common stock for issuance under the Company Plan.

BLUE HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2007 (AS RESTATED) AND 2006

At September 30, 2007, options outstanding are as follows:

	Number of options	Weighted average exercise price	Intrinsic Value
Balance at January 1, 2007	335,500	$5.75	-
Granted	925,000	$1.98	-
Exercised	-	-	-
Cancelled	(164,000)	$5.20	-
Balance at September 30, 2007	1,096,500	$2.27	-

Additional information regarding options outstanding as of June 30, 2007 is as follows:

		Options outstanding			Options exercisable	
	Exercise price	Number outstanding	Weighted average remaining contractual life (years)	Weighted average exercise price	Number exercisable	Weighted average exercise price
	$8.10	42,000	7.43	$8.10	22,000	$8.10
	$5.30	33,500	7.87	$5.30	33,500	$5.30
	$5.20	96,000	8.25	$5.20	35,500	$5.20
	$1.98	300,000	9.50	$1.98	100,000	$1.98
	$1.40	625,000	9.75	$1.40	125,000	$1.40
Total	$1.40 - $8.10	1,096,500	9.4			