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Seven Arts Entertainment Inc.  
Form 10-Q  
May 21, 2012

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U.S. 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, 2012

OR

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

Commission File Number 001-34250

SEVEN ARTS ENTERTAINMENT, INC.  
(Exact name of small business issuer as specified in its charter)

Nevada  
(State or other jurisdiction of  
incorporation or organization)

45-3138068  
(IRS Employer Identification No.)

8439 Sunset Boulevard 4th Floor  
Los Angeles, CA 90069  
(Address of principal executive offices)

(323) 372-3080  
(Issuer's telephone number)

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

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

Indicate by check mark whether the Registrant is a large accredited filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accredited filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act:

Large Accredited Filer                            Accelerated Filer                        
Non-Accredited Filer                            Smaller Reporting

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Company

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

As of May 10, 2012 there were 68,090,174 shares of Common Stock of the issuer outstanding.

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SEVEN ARTS ENTERTAINMENT, INC.  
FORM 10-Q  
MARCH 31, 2012

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Seven Arts Entertainment, Inc.

(Formerly Seven Arts Pictures, Plc)  
 Consolidated Balance Sheets  
 As of March 31, 2012 and June 30, 2011

	March 31, 2012 (Unaudited)	June 30, 2011 (Audited)
<b>ASSETS</b>		
<b>CURRENT ASSETS:</b>		
Cash and cash equivalents	\$-	\$8,785
Accounts receivable, net of allowance for doubtful accounts of \$78,661 and \$195,623	274,862	431,891
Due from related parties, net	3,552,137	2,725,974
Other receivables and prepayments	3,771,179	1,620,895
Total current assets	7,598,178	4,787,545
Film costs, less accumulated amortization of \$3,830,952 and \$2,843,734	24,111,370	23,133,559
Music assets	9,540,859	-
Property and equipment, net of accumulated depreciation of \$111,232 and \$106,671	19,522	24,540
<b>TOTAL ASSETS</b>	<b>\$41,269,929</b>	<b>\$27,945,644</b>

**LIABILITIES AND SHAREHOLDERS' EQUITY**

<b>CURRENT LIABILITIES:</b>		
Bank overdraft	\$25,267	\$987
Accounts payable	1,648,933	2,569,275
Accrued liabilities	1,132,266	3,860,502
Shares to be issued	1,303,589	-
Participation and residuals	150,982	503,187
Other loans	3,645,669	1,755,250
Film & production loans	4,921,206	10,890,430
Deferred income	626,080	407,763
Provision for earnout	2,837,134	-
Total Current Liabilities	16,291,126	19,987,394
<b>TOTAL LIABILITIES</b>	<b>\$16,291,126</b>	<b>\$19,987,394</b>

**STOCKHOLDERS' EQUITY**

Convertible redeemable Series A preferred shares, \$10 par value, 125,125 issued and outstanding	\$1,251,250	\$-
Convertible redeemable Series B preferred shares, \$100 par value, 180,000 issued and outstanding	18,000	
Shares held in escrow	(12,000,000)	
Common stock; \$0.01 par value; 250,000,000 shares authorized; 41,968,972 and 2,643,131 issued and outstanding, respectively	419,690	-
Common stock; £0.25 par value; 20,527,360 shares authorized; 2,643,131 shares issued and outstanding	-	1,121,208
Deferred stock; £0.45 par value; 13,184,000 shares authorized; and 13,184,000 shares issued and outstanding	-	11,636,594
Deferred stock; £1.00 par value; 2,268,120		

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shares issued and outstanding	-	3,876,745
Additional paid in capital	13,130,377	9,880,782
Convertible debentures	3,432,450	3,432,450
Accumulated deficit	(3,664,072 )	(19,952,191)
Comprehensive income	4,409,108	(2,037,338 )
Shareholders' equity	24,978,803	7,958,250
<b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>	<b>\$41,269,929</b>	<b>\$27,945,644</b>

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

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(Formerly Seven Arts Pictures, Plc)  
 Consolidated Statements of Operations  
 For the Three and Nine Months Ended March 31, 2012 and 2011

	3 Months Ended March 31, 2012	3 Months Ended March 31, 2011	9 Months Ended March 31, 2012	9 Months Ended March 31, 2011
Revenue:				
Film revenue	\$ 187,793	\$ 272,703	987,220	1,510,655
Fee related revenue - related party	-	-	-	570,029
Total revenue	187,793	272,703	987,220	2,080,684
Cost of revenue				
Amortization and impairment of film costs	186,890	523,998	987,221	1,219,618
Other cost of revenue	262,041	18,208	561,330	268,296
Cost of revenue	448,931	542,206	1,548,551	1,487,914
Gross profit	(261,138 )	(269,503 )	(561,331 )	592,770
Operating expenses:				
General and administrative expenses	500,897	591,285	1,550,761	973,905
Bad debt expense	109,481	71,800	106,663	47,800
Total operating expenses	610,378	663,085	1,657,424	1,021,705
Income from operations	(871,516 )	(932,588 )	(2,218,755 )	(428,935 )
Non-operating income(expense)				
Other income	30,196	-	31,100	-
Interest expenses	(744,469 )	(40,448 )	(1,476,417 )	(722,282 )
Interest income	-	2	-	370
Total non-operating income (expense)	(714,273 )	(40,446 )	(1,445,317 )	(721,912 )
Income/(loss) before taxes	(1,585,789 )	(973,034 )	(3,664,072 )	(1,150,847 )
Change in debt derivative	-	-	-	(32,775 )
	(1,585,789 )	(973,034 )	(3,664,072 )	(1,183,622 )
Provision for income tax (benefit)	-	-	-	-
Net income (loss)	\$(1,585,789 )	\$(973,034 )	(3,664,072 )	(1,183,622 )
Comprehensive income (loss):				
Net income (loss)	(1,585,789 )	(973,034 )	(3,664,072 )	(1,183,622 )
Foreign exchange translation gain (loss)	-	-	-	-
Comprehensive income (loss)	(1,585,789 )	(973,034 )	(3,664,072 )	(1,183,622 )
Weighted average number of ordinary shares used in the profit (loss) per share calculation:				
Basic	30,421,315	1,717,451	17,665,221	1,717,451
Diluted	30,421,315	1,717,451	17,665,221	1,717,451
Basic profit/ (loss) per share	(0.05 )	(0.57 )	(0.21 )	(0.69 )
Diluted profit/ (loss) per share	(0.05 )	(0.57 )	(0.21 )	(0.69 )

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



Seven Arts Entertainment, Inc.  
(Formerly Seven Arts Pictures, Plc.)  
Consolidated Statements of Cash Flows  
Nine Months Ended March 31, 2012 and 2011  
(Unaudited)

	Nine Months Ended March 31, 2012	Nine Months Ended March 31, 2011
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net loss	\$ (3,664,072 )	\$ (1,183,622)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation	10,034	10,044
Amortization of film cost	987,221	1,219,618
Conversion of debt to equity	8,332,434	2,275,297
Stock for services	659,096	-
Bad debt	106,663	47,800
Forgiveness of interest by lender	(30,196 )	-
Foreign currency impact of movement of consolidated entity to related party	2,757,155	-
Issuance of share options	97,386	-
Changes in operating assets and liabilities:		
Trade receivables	157,029	(314,014 )
Due to and due from related parties, net	(826,163 )	(1,539,887)
Capitalized film assets	(1,965,032 )	(609,768 )
Receivables and prepayments	(2,150,284 )	(1,174,052)
Bank overdraft	(987 )	-
Accounts payable	(920,342 )	691,245
Deferred income	218,317	648,878
Stock to be issued	1,303,589	-
Participation and residuals	(352,205 )	22,336
Accrued liabilities	(2,728,236 )	(438,323 )
Net cash provided /(used in) operating activities	1,991,407	(344,448 )
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Purchase of property and equipment	(5,016 )	(9,765 )
Net cash used in investing activities	(5,016 )	(9,765 )
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Conversion of convertible notes payable	(6,665,175 )	-
Issuance of common stock		
Shares of common stock issued in satisfaction of debt	(1,667,259 )	-
Proceeds from notes payable	3,395,281	365,371
Payments on notes payable	(732,323 )	-
Shares held in escrow	(12,000,000)	-
Issuance of Preferred Stock	19,251,250	-
Issuance of stock for cash	1,000,000	-
Acquisition of music assets	(8,540,859 )	-



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Acquisition of Big Jake Music	(1,000,000 )	-
Fair value of earnout	2,837,134	-
Shares of common stock issued to PLC for assets	7,880,000	-
Stock issued in share exchange	64,866	-
Liabilities retained in PLC in share exchange	(5,837,707 )	
Net cash provided by financing activities	(2,014,792 )	365,371
Effect of exchange rate changes on cash	(4,664 )	(11,402 )
NET CHANGE IN CASH	(33,065 )	(244 )
CASH AT BEGINNING OF PERIOD	7,798	26,818
CASH AT END OF PERIOD	\$ (25,267 )	\$ 26,574
Supplemental cash flow information:		
Cash paid for interest	\$ 149,326	-
Shares of common stock issued to PLC for assets	7,880,000	-
Common and preferred stock to be issued	1,303,589	-
Stock issued in share exchange	64,866	-
Liabilities retained in PLC in share exchange	(5,877,361 )	-
Accounts receivable applied against loan set-off	-	1,334,561
Stock issued for services	659,096	-
Common stock issued in satisfaction of debt	8,332,434	-
Foreign currency impact of movement of consolidated entity to related party	2,757,155	-

Seven Arts Entertainment, Inc.

(Formerly Seven Arts Pictures, Plc.)  
Notes to Consolidated Financial Statements  
March 31, 2012  
(Unaudited)

## NOTE 1 – NATURE OF ACTIVITIES AND SIGNIFICANT ACCOUNTING POLICIES

### Nature of Activities, History and Organization

Seven Arts Entertainment, Inc. (herein referred to as “the Company”, “Seven Arts” or “SAE,”), a Nevada Corporation, is the continuation of the business and the successor of the NASDAQ listing to Seven Arts Pictures Plc., (“PLC”) which was founded in 2002 as an independent motion picture production and distribution company engaged in the development, acquisition, financing, production, and licensing of theatrical motion pictures for exhibition in domestic (i.e., the United States and Canada) and foreign theatrical markets, and for subsequent worldwide release in other forms of media, including home video and pay and free television. The Company currently owns interests in 33 completed motion pictures, subject in certain instances to the prior financial interests of other parties. As discussed herein, in early March 2012, the Company launched Seven Arts Music (“SAM”) and acquired 52 completed sound recordings with the rights to additional albums.

On June 11, 2010, Seven Arts Entertainment, Inc. (“SAE”), a Nevada Corporation, was formed and became a wholly owned subsidiary of Seven Arts Pictures Plc. As of June 11, 2010, the Company entered into an Asset Transfer Agreement, as amended on January 27, 2011 and again on August 31, 2011, to transfer all of the assets with a cost basis from PLC to SAE, in exchange for assumption by SAE of certain indebtedness and for one share of common stock of SAE for each ordinary share of PLC which have been distributed to shareholders. Additionally, 2,000,000 shares of SAE were issued to PLC in order to satisfy any remaining obligations. This transfer was approved by the PLC shareholders at an Extraordinary General Meeting on June 11, 2010. The purpose of this transfer was to eliminate our status as a foreign private issuer and to assume compliance with all obligations of a domestic issuer under all applicable state and Federal securities laws. Our intention in executing this transaction was to redomicile our business with no change in the economic interests of our shareholders.

On August 31, 2011, NASDAQ approved the substitution of one share of SAE, Inc. stock for the Company's NASDAQ listing, effective at the opening of trading on September 1, 2011. On that date, each of the Company's ordinary shares were exchanged for one share of common stock of SAE, and commenced trading on NASDAQ as the successor to the Company's NASDAQ listing. This transaction was approved by the Company's shareholders at the Company's Extraordinary General Meeting on June 11, 2010.

SAE's authorized capital consists of 250,000,000 shares of common stock, \$.01 par value per share.. As of March 31, 2012, there were 41,968,972 shares of common stock outstanding, all of which are fully paid and non-assessable. (including the 2,000,000 shares issued to SAP Plc as part of the asset transfer agreement approved by the SEC in January 2011). Each outstanding share of common stock entitles the holder thereof to one vote per share on matters submitted to a vote of stockholders.

125,125 Series A preferred shares with a \$10.00 par value per share, were issued to one shareholder in November 2011 for a transaction completed in August 2011. These shares have a conversion price to common stock of \$0.15/share. Two further tranches of 11,500 and 10,859 shares of Series A preferred have been subscribed for by the same shareholder, but have not yet been issued.

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180,000 Series B preferred shares \$100.00 par value per share have been issued to two shareholders and 120,000 of such shares are held in escrow subject to earnout provisions.

SAE is now a United States issuer and commenced regular quarterly reporting from the first quarter ended September 30, 2011.

On November 8, 2011, the Company's listing predecessor, PLC, was placed into involuntary creditors liquidation under English law (See Note 6 – Commitments and Contingencies). Certain indebtedness of PLC remained with PLC and will be subject to administration or payment in those administration proceedings. In accordance with the asset transfer agreement, PLC has been issued 2,000,000 shares of common stock of SAE in order to satisfy these obligations.

In March 2012, the Company acquired the music assets of David Michery and 100% of the stock of Big Jake Music, although the deals were negotiated by the listing predecessor. As a result, the Company is now also an independent distributor and producer of sound recordings.

The material assets that were acquired comprise 52 completed sound recordings including two completed albums with “DMX”, up to two additional albums from “DMX” and upto five albums from “Bone Thugs-N-Harmony”. The commitments and liabilities assumed were a promissory note dated June 15, 2010 in the amount of \$200,000, and outstanding recording costs of the performances of DMX in amounts to be approved by us but not to exceed \$140,000.

In connection with the acquisition of the music assets of David Michery, the Company issued 50,000 shares of our Series B convertible preferred stock, par value \$100, (convertible at approximately \$1.10 per share subject to amendment and adjustment, as defined in the agreement, as of September 30, 2012) to David Michery and his assigns and agreed to issue an additional 50,000 shares of our Series B convertible preferred stock to Mr. Michery and his assigns if two DMX albums and two Bone Thugs-N-Harmony albums generate an aggregate of net earnings before interest and taxes of \$5,000,000 during the next five fiscal years. The second 50,000 shares are currently held in escrow. Mr. Michery is the Chief Executive Officer of Seven Arts Music Inc., a wholly-owned subsidiary of the Company.

In connection with the acquisition of the stock of Big Jake Music, the Company issued 10,000 shares of our Series B convertible preferred stock, par value \$100, (convertible at approximately \$1.10 per share subject to amendment and adjustment, as defined in the agreement, as of September 30, 2012) to Jake Shapiro and his assigns and agreed to issue an additional 70,000 shares of our Series B convertible preferred stock to Mr. Shapiro and his assigns if certain specific terms are met 40,000 shares are subject to proving valuation of of certain advertising credits and 30,000 shares are subject to an earnout over a two year period. The 70,000 shares are currently held in escrow. Mr. Shapiro is the Chief Executive Officer of Big Jake Music., a wholly-owned subsidiary of the Company.

#### Unaudited Interim Financial Statements:

The accompanying unaudited interim consolidated financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America and the rules of the Securities and Exchange Commission. These financial statements are unaudited and, in the opinion of management, include all adjustments (consisting of normal recurring accruals) necessary to present fairly the balance sheet, statement of operations, statement of stockholders' equity and statement of cash flows for the periods presented in accordance with accounting principles generally accepted in the United States. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted pursuant to SEC rules and regulations. It is presumed that users of this interim financial information have read or have access to the audited financial statements and footnote disclosure for the preceding fiscal year contained in the Company's Annual Report on Form 20-F. The results of operations for the three and nine months ended March 31, 2012 are not necessarily indicative of the results of operations for the full year or any other interim period. The information included in this Form 10-Q should be read in conjunction with Management's Discussion and Analysis and Financial Statements and notes thereto included in the Company's predecessor's June 30, 2011 Form 20-F, which was filed in December 2011. The Company's predecessor,

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PLC, was considered a foreign filer as of its June 30, 2011 year-end, and therefore, required to file a Form 20-F by December 31, 2011. The 2011 comparatives for the nine months to March 31, 2011 have been derived from the June 30, 2011 20-F filing which was prepared prior to the Company's predecessor filing Quarterly reports.

#### Significant Accounting Policies:

The Company's management selects accounting principles generally accepted in the United States of America and adopts methods for their application. The application of accounting principles requires the estimating, matching and timing of revenue and expense. It is also necessary for management to determine, measure and allocate resources and obligations within the financial process according to those principles. The accounting policies used conform to generally accepted accounting principles which have been consistently applied in the preparation of these financial statements.

The financial statements and notes are representations of the Company's management which is responsible for their integrity and objectivity. Management further acknowledges that it is solely responsible for adopting sound accounting practices, establishing and maintaining a system of internal accounting control and preventing and detecting fraud. The Company's system of internal accounting control is designed to assure, among other items, that 1) recorded transactions are valid; 2) valid transactions are recorded; and 3) transactions are recorded in the proper period in a timely manner to produce financial statements which present fairly the financial condition, results of operations and cash flows of the Company for the respective periods being presented.

#### Basis of Presentation

The accompanying consolidated financial statements include the accounts of Seven Arts Entertainment, Inc. ("SAE"), and its wholly owned subsidiaries, Seven Arts Filmed Entertainment, Limited ("SAFE, Ltd."), Seven Arts Music, Inc. ("SAM") and Big Jake Music, Inc. ("BJM").

The Company consolidates its subsidiaries in accordance with Accounting Standards Codification ("ASC") 810, "Business Combinations", and specifically ASC 810-10-15-8 which states, "The usual condition for a controlling financial interest is ownership of a majority voting interest, and, therefore, as a general rule ownership by one reporting entity, directly or indirectly, or over 50% of the outstanding voting shares of another entity is a condition pointing toward consolidation." The Company does not have any variable interest or special purpose entities.

The Company prepares its financial statements on the accrual basis of accounting and in accordance with Generally Accepted Accounting Principles of the United States of America ("US GAAP"). All intercompany balances and transactions are eliminated. Management believes that all adjustments necessary for a fair presentation of the results of the three and nine months ended March 31, 2012 and 2011, respectively, have been made.

#### Use of Estimates:

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. The most significant estimates made by management in the preparation of the financial statements relate to ultimate revenue and costs of its films which are used in the amortization and impairment of film costs, estimates for allowances and income taxes. Accordingly, actual results could differ from those estimates.

#### Recently Issued Accounting Pronouncements:

The Company does not expect the adoption of recently issued accounting pronouncements to have a significant impact on the Company's results of operations, financial position or cash flow.



Revenue Recognition:

FILM

The Company recognizes revenue from the sale (minimum guarantee or non-refundable advances) or licensing arrangement (royalty agreements) of a film in accordance with ASC 605-15 "Revenue Recognition". Revenue will be recognized only when all of the following criteria have been met:

- a) Persuasive evidence of a sale or licensing arrangement with a customer exists.
- b) The film is complete and, in accordance with the terms of the arrangement, has been delivered or is available for immediate and unconditional delivery. (i.e. the "notice of delivery" ("NOD") has been sent and there is a master negative available for the customer).
- c) The license period of the arrangement has begun and the customer can begin its exploitation, exhibition, or sale.
- d) The arrangement fee is fixed or determinable.
- e) Collection of the arrangement fee is reasonably assured.

A written agreement with clients (purchase order, letter, contract, etc.), indicating the film name, territory and period is required for the recognition of revenue. Revenue is recognized when the performance criteria in the contracts have been met. The customer generally confirms agreement by their signature on the contract.

Minimum guarantee revenue (i.e., non-refundable advances) is recognized as and when the film is available for delivery to the respective territories. Cash deposits received on the signing of the contracts are recorded as deferred revenue until the film is available for delivery (as described above) at which point the deferred revenue is recognized. The Company does not recognize any revenues relating to minimum guarantee on any motion picture or amortization expenses on that picture until United States theatrical release if it has agreed with the licensees that delivery or payment of minimum guarantee will be delayed for any material period of time to permit such a theatrical release.

Royalty revenue, which equates to an agreed share of gross receipts of films, is recognized as income as and when the Company is notified of the amounts by the customers through their royalty reports. Revenue is recorded net any of sales or value added taxes charged to customers.

MUSIC

Revenue, which equates to an agreed share of gross receipts, is recognized as income as and when the Company is notified of the amounts by the distribution agent through their distribution reports.

Revenue is recorded

- a) net of any sales or value added taxes charged to customers and
- b) net of discounts agreed with customers and
- c) net of returns provision agreed with the distributor and
- d) grossed up for the distribution fee charged by the distribution agent.

Revenue from digital distribution will be reported by the various digital platforms such as iTunes in their periodic reports and posted as received.



#### Fee-related revenues

Many countries make tax credits available to encourage film production in the territory. Seven Arts benefits from tax credits in:

- a) the UK and several other European territories for their European productions
- b) Canada for their Canadian productions
- c) Louisiana for their US productions
- d) Tax preferred financing deals

In the majority of circumstances these tax credits are treated as a reduction in the capitalized costs of the film assets they are financing.

#### Foreign Currency Transactions and Comprehensive Income

The Company's functional currency, as well as the Company's subsidiary, SAFE, Ltd. is the US Dollar. The functional currency of the Company's predecessor, was the Pound Sterling ("GPB"), and some transactions which are generated in the United Kingdom are denominated in GBP.

Assets and liabilities generated in a currency other than the functional currency are translated at exchange rates as of the balance sheet date. Revenues and expenses are translated at average rates in effect for the periods presented. The cumulative translation adjustment is included in the accumulated other comprehensive gain (loss) within shareholders' equity (deficit). Foreign currency transaction gains and losses arising from exchange rate fluctuations on transactions denominated in a currency other than the functional currency are included in the consolidated results of operations.

Where possible, the Company seeks to match GBP income with GBP expenditures. To date, the Company has not hedged any transactional currency exposure but will keep such exposures under review and where appropriate may enter into such transactions in future.

#### Income Taxes:

The Company has adopted ASC 740-10 "Income Taxes", which requires the use of the liability method in the computation of income tax expense and the current and deferred income taxes payable.

#### Cash and Cash Equivalents:

Cash and cash equivalents includes cash in banks with original maturities of three months or less and are stated at cost which approximates market value, which in the opinion of management, are subject to an insignificant risk of loss in value. The cash and cash equivalents of the Company consisted of cash balances held on deposit with banks, including various accounts denominated in US Dollars, Pounds Sterling and Euros.

#### Accounts Receivable:

Accounts Receivable are carried at their face amount, less an allowance for doubtful accounts. On a periodic basis, the Company evaluates accounts receivable and establishes an allowance for doubtful accounts based on a combination of specific customer circumstances and credit conditions, and on a history of write offs and collections. The Company's policy is generally not to charge interest on trade receivables after the invoice becomes past due. A receivable is considered past due if payments have not been received within agreed upon invoice terms. Write offs are recorded at a time when a customer receivable is deemed uncollectible. The Company's allowance for doubtful accounts was \$78,661 and \$195,623 at March 31, 2012 and June 30, 2011, respectively. Substantially all of the trade receivables in the consolidated financial statements are pledged as security for borrowings by the Company.

#### Property & Equipment:

Equipment is carried at the cost of acquisition or construction and depreciated over the estimated useful lives of the assets. Costs associated with repair and maintenance are expensed as incurred. Costs associated with improvements which extend the life, increase the capacity or improve the efficiency of our property and equipment are capitalized and depreciated over the remaining life of the related asset. Gains and losses on dispositions of equipment are reflected in operations. Depreciation and amortization are provided using the straight-line method over the estimated useful lives of the assets, which are 3 to 5 years.

#### Other Receivables and Prepayments:

The Company has entered into contracts for investor relations and consulting services to assist in future fundraising activities. A portion of these services were prepaid with shares of common stock that vested immediately and will be amortized over the period the services are to be provided.

#### Film Costs:

Film costs include the unamortized costs of completed films which have been produced by the Company or for which the Company has acquired distribution rights, libraries acquired as part of acquisitions of companies and films in progress and in development. For films produced by the Company, capitalized costs include all direct production and financing costs, capitalized interest and production overhead.

Costs of acquiring and producing films are amortized using the individual-film-forecast method, whereby these costs are amortized and participations and residuals costs are accrued in the proportion that current year's revenue bears to management's estimate of ultimate revenue at the beginning of the current year expected to be recognized from the exploitation, exhibition or sale of the films. The majority of a film's costs (approximately 80% or more) are generally amortized within three years of the picture's initial release.

Ultimate revenue includes estimates over a period not to exceed ten years following the date of initial release. Film costs are stated at the lower of amortized cost or estimated fair value. Individual film costs are reviewed on a title-by-title basis, when an event or change in circumstances indicates that the fair value of a film is less than its unamortized cost. The fair value of the film is determined using management's future revenue and cost estimates and a discounted cash flow approach. Impairment is recorded in the amount by which the unamortized costs exceed the estimated fair value of the film. Estimates of future revenue involve measurement uncertainty, and it is therefore possible that reductions in the carrying value of investment in films may be required as a consequence of changes in management's future revenue estimates.

Films are included in the general “library” category when initial release dates are at least three years prior to the acquisition date.

Films in progress include the accumulated costs of productions which have not yet been completed. Films in development include costs of acquiring film rights to books, stage plays or original screenplays and costs to adapt such projects. Such costs are capitalized and, upon commencement of production, are transferred to production costs. Projects in development are written off at the earlier of the date they are determined not to be recoverable or when abandoned.

#### Music Costs/Assets

The initial material assets that were acquired comprise 52 completed sound recordings including two completed albums with “DMX”, up to two additional albums from “DMX” and upto five albums from “Bone Thugs-N-Harmony”.

Music assets include the unamortized costs of completed albums, singles and videos which have been produced by the Company or for which the Company has acquired distribution rights, libraries acquired as part of acquisitions and albums in progress and in development. For albums produced by the Company, capitalized costs include all direct production and financing costs, capitalized interest and production overhead.

Costs of acquiring and producing music assets will be amortized using the individual-album-forecast method, whereby these costs are amortized in the proportion that current year’s revenue bears to management’s estimate of ultimate revenue at the beginning of the current year expected to be recognized from the exploitation or sale of the music.

#### Impairment of Long Lived Assets:

The Company evaluates, on a periodic basis, long-lived assets to be held and used for impairment in accordance with the reporting requirements of ASC 360-10, “Accounting for the Impairment or Disposal of Long-Lived Assets”. The evaluation is based on certain impairment indicators, such as the nature of the assets, the future economic benefit of the assets, any historical or future profitability measurements, as well as other external market conditions or factors that may be present. If these impairment indicators are present or other factors exist that indicate that the carrying amount of the asset may not be recoverable, then an estimate of the discounted value of expected future operating cash flows is used to determine whether the asset is recoverable and the amount of any impairment is measured as the difference between the carrying amount of the asset and its estimated fair value. The fair value is estimated using valuation techniques such as market prices for similar assets or discounted future operating cash flows.

#### Earnings Per Share:

Basic earnings (loss) per share are computed by dividing net income (loss) by the weighted average number of common shares outstanding for the period. Diluted earnings (loss) per share include the effects of any outstanding options, warrants and other potentially dilutive securities. For the periods presented, there were no potentially dilutive securities outstanding, therefore basic earnings per share equals diluted earnings per share. Basic and diluted earnings per share (“EPS”) are based on weighted-average common shares and exclude shares that would have an anti-dilutive effect. In accordance with ASC 260-10-45-19, the Company did not consider any potential common shares in the computation of diluted EPS as of March 31, 2012 and 2011, due to the loss from continuing operations, as they would have an anti-dilutive effect on EPS.

#### Share Based Payments:

The Company accounts for share based payments using a fair value based method whereby compensation cost is measured at the grant date based on the value of the services received and is recognized over the service period. The Company uses the Black-Scholes pricing model to calculate the fair value of options and warrants issued. In calculating this fair value, there are certain assumptions used such as the expected life of the option, risk-free interest rate, dividend yield, volatility and forfeiture rate. The use of a different estimate for any one of these components could have a material impact on the amount of calculated compensation expense.



## Segment Reporting:

The Company now operates in two business segments as a motion picture producer and distributor and as a music label managing the assets of David Michery. The Company believes that its businesses should be reported as two business segments. (See Note 2 - Segment Reporting)

## Fair Value Measurements:

ASC Topic 820, "Fair Value Measurements and Disclosures", defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and requires certain disclosures about fair value measurements. In general, fair value of financial instruments are based upon quoted market prices, where available. If such quoted market prices are not available, fair value is based upon internally developed models that primarily use, as inputs, observable market based parameters. Valuation adjustments may be made to ensure that financial instruments are recorded at fair value. These adjustments may include amounts to reflect counterparty credit quality and the Corporation's credit worthiness, among other things, as well as unobservable parameters. Any such valuation adjustments are applied consistently over time.

## Derivative Instruments:

The Company's policy is not to use derivative or hedging financial instruments for trading or speculative purposes, except certain embedded derivatives derived from certain conversion features or reset provisions attached to the convertible debentures, as described in Note 9.

## NOTE 2 - SEGMENT INFORMATION

In accordance with ASC 280 Segment Reporting, operating segments are identified as components of an enterprise about which separate discrete financial information is available for evaluation by the chief operating decision maker, or decision-making group, in making decisions how to allocate resources and assess performance. Our chief decision maker, as defined under the FASB's guidance, is a combination of the Chief Executive Officer and the Chief Financial Officer.

In the quarter ended March 31, 2012, the Company formed a new subsidiary, Seven Arts Music, and acquired music assets from David Michery and purchased the stock of Big Jake Music. This is a new line of business for the Company, and therefore, will now have two reportable operating segments.

The table below presents the financial information for the two reportable segments for the nine months ended March 31, 2012. Comparable financial information for 2011 is not presented as the Company only had one segment during that time.

	Nine Months Ended March 31, 2012		
	Film	Music	Total
Revenues	\$ 987,220	\$ 0	\$ 987,220
Cost of revenues	(1,548,551)	0	(1,548,551)
Gross profit (loss)	(561,331)	0	(561,331)
Operating expenses	(1,378,895)	(278,529)	(1,657,424)
Loss from operations	\$ (1,940,226)	\$ (278,529)	\$ (2,218,755)



As of March 31, 2012, the Company had film and music assets of \$24,111,370 and \$9,540,859, respectively. As of December 31, 2011, all of the Company's assets were related to film.

#### NOTE 3 – FILM COSTS

Film costs as March 31, 2012 and June 30, 2011 are as follows:

	March 31, 2012	June 30, 2011
Film Costs, beginning of period	\$ 25,977,293	\$ 23,808,869
Additions to film costs during the period	1,965,029	2,168,424
Total film costs	27,942,322	25,977,293
Less: Accumulated amortization	(3,830,952)	(2,843,734)
Total film costs, net of accumulated amortization	\$ 24,111,370	\$ 23,133,559

Amortization of film costs was \$987,221 and \$689,618 for the nine months ended March 31, 2012 and 2011. The Company reviews capitalized film costs for impairment whenever events or changes in circumstances indicate that the carrying amounts of such assets may not be recoverable or at least once per year. Determination of recoverability is based on an estimate of future cash flows resulting from the use of the asset, and its eventual disposition. Measurement of an impairment loss for the assets is based on the fair value of the asset as estimated using a discounted cash flow model.

#### NOTE 4 – MUSIC ASSETS

Music assets at March 31, 2012 and June 30, 2011 are as follows:

	March 31, 2012	June 30, 2011
Music assets, beginning of period	\$ -	\$ -
Additions to music assets during the period	9,540,859	-
Total film costs	9,540,859	-
Less: Accumulated amortization	-	-
Total film costs, net of accumulated amortization	\$ 9,540,859	\$ -



The initial material assets that were acquired comprise 52 completed sound recordings including two completed albums with “DMX”, up to two additional albums from “DMX” and upto five albums from “Bone Thugs-N-Harmony”.

The music assets were valued at the value of the preferred stock issued, the fair value of Mr. Michery’s earnout and capitalized costs incurred in the production of the current albums .

Currently no earnout provision has been recorded for the acquisition of Big Jake Music, as the Company does not yet believe it has any basis for this earnout.

Amortization of music assets was \$0 and \$0 for the nine months ended March 31, 2012 and 2011 as the assets were acquired in March 2012. The Company reviews capitalized music assets for impairment whenever events or changes in circumstances indicate that the carrying amounts of such assets may not be recoverable or at least once per year. Determination of recoverability is based on an estimate of future cash flows resulting from the use of the asset, and its eventual disposition. Measurement of an impairment loss for the assets is based on the fair value of the asset as estimated using a discounted cash flow model.

**NOTE 5 – RELATED PARTY DUE TO/DUE FROM**

Seven Arts Pictures, Inc. (“SAP, Inc.”) directly or through related various Louisiana limited liability companies, have from time-to-time made non-interest bearing advances to the Company or its subsidiaries or have received advances back from the Company. The balances of these combined accounts due to the Company as of March 31, 2012 and June 30, 2011 were \$3,552,137and \$2,725,974, respectively. SAP, Inc. has pledged an interest in its shares of the Company’s stock to secure certain indebtedness for which SAP, Inc. and the Company are jointly liable such as the Apollo and Armadillo debts. The stock of SAP, Inc. was transferred to the listing predecessor of SAE on September 10, 2011.

**NOTE 6 – INCOME TAXES**

The Company has adopted ASC 740-10, “Income Taxes”, which requires the use of the liability method in the computation of income tax expense and the current and deferred income taxes payable (deferred tax liability) or benefit (deferred tax asset). Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized.

During the nine months ended March 31, 2012 the Company had a net loss of \$3,664,072 increasing the deferred tax asset approximately \$1,245,784 at the statutory tax rate of 34%. Deferred tax assets at March 31, 2012 consisted of the following:

Deferred tax asset related to:

	March 31, 2012
Prior Year	\$ -
Tax Benefit (Expense) for Current Period	1,245,784
Deferred Tax Asset	\$ 1,245,784
Less: Valuation Allowance	(1,245,784)
Net Deferred Tax Asset	\$ -



The net deferred tax asset generated by the loss carry forward has been fully reserved and will expire in 2019 through 2030. The realization of deferred tax benefits is contingent upon future earnings and therefore, is fully reserved at March 31, 2012.

#### NOTE 7 – EARNINGS PER SHARE

Basic and diluted earnings per share (“EPS”) are based on weighted-average common shares and generally exclude shares that would have an anti-dilutive effect. In accordance with ASC 260-10-45-19, the Company did not consider any potential common shares in the computation of diluted EPS as of March 31, 2012, due to the loss from continuing operations, as including them would have an anti-dilutive effect on EPS.

#### NOTE 8 – COMMITMENTS AND CONTINGENCIES

##### Creditors Liquidation of SAP Plc.

The Company’s listing predecessor Seven Arts Pictures Plc. (‘PLC’) was placed by the English Companies Court into compulsory liquidation on November 8, 2011. The Company’s CEO, Mr. Peter Hoffman, as a director of PLC had sought an administration order but this request was denied by the Courts as a result of inter alia the opposition of Parallel Pictures LLC (‘Parallel’). PLC’s principal creditors have appointed a liquidator for the orderly winding up of its remaining assets not transferred to us pursuant to the Asset Transfer Agreement, effective January 27, 2011.

Mr. Hoffman expects that the liquidator and PLC will pursue its substantial claims against Parallel and its defenses to Parallel’s claims. Parallel has claimed in the proceedings in England and the United States that the Asset Transfer Agreement between the Company and PLC was ‘fraudulent’ and may seek additional compensation or guarantees from Company. Management believes that the Asset Transfer Agreement is a valid agreement for value and not subject to attack and that Parallel will not prevail in its claims. Management believes it has the support of its creditors to resist these claims by Parallel which are disputed by the Company and as a result Parallel will not obtain any relief from the courts on this issue.

Based on discussions with the liquidator, our management believes this liquidation proceeding will have no material effect on the cost, business or market value of common stock

##### Further Share Issue to SAE Inc

On June 11, 2010, Seven Arts Entertainment, Inc. (“SAE”), a Nevada Corporation, was formed and became a 100% owned subsidiary of Seven Arts Pictures Plc. As of June 11, 2010, the Company entered into an Asset Transfer Agreement, as amended on January 27, 2011 and again on August 31, 2011, to transfer all of the assets with a cost basis from PLC to SAE, in exchange for assumption by SAE of certain indebtedness and for one share of common stock of SAE for each ordinary share of PLC which have been distributed to shareholders. Additionally, 2,000,000 shares of SAE were issued to PLC in order to satisfy any remaining obligations. There are several outstanding lawsuits which the liquidator of SAP Plc. will try to resolve as part of the liquidation proceedings . Any proceeds from these legal matters will also be used to pay off outstanding obligations within the PLC. If there is a shortfall in the proceeds to meet the obligations left in PLC. then SAE Inc. may well have to issue more stock to cover this shortfall .

#### 807 Esplanade Guarantee

Seven Arts Pictures Louisiana LLC, a related party and/or an affiliate of the Company, entered into a Credit Agreement with Advantage Capital Community Development Fund LLC dated October 11, 2007, for the acquisition and improvement of a production and post production facility located at 807 Esplanade Avenue in New Orleans, Louisiana ("807 Esplanade") for aggregate principal advances of up to \$3,700,000. This agreement was guaranteed by the Company's predecessor. Approximately \$3,700,000 plus interest has been drawn under the terms of this Credit Agreement, as of March 31, 2012. The Company has also guaranteed this amount. A construction loan of \$1,800,000 has also been guaranteed by the Company

#### Armadillo

There is a guarantee of a \$1,000,000 note plus interest due to Armadillo by the Employee Benefit Trust of the Company's listing predecessor resulting from the purchase of Seven Arts preferred shares from Armadillo.

#### Fireworks Litigation

The Company prevailed in a motion for summary adjudication on February 10, 2011 in an action against CanWest Entertainment and two of its affiliates ("CanWest") confirming the Company's ownership of five motion pictures "Rules of Engagement", "An American Rhapsody," "Who Is Cletis Tout," "Onegin," and "The Believer", (the "Copyrights"). The Company has filed an action in England against Content Media Corporation ("Content") and Paramount Picture Corp. ("Paramount") to recover the Copyrights and substantial damages for the use of the copyrighted works after their purported acquisition from CanWest. The Company may incur up to \$200,000 in legal expenses to pursue this claim but expects to recover those fees from Content.

#### Arrowhead Target Fund

Seven Arts Future Flow I ("SFF"), a limited liability Company owned by SAP Inc., a Company previously controlled by Mr. Hoffman, obtained financing from the Arrowhead Target Fund, Ltd. ("Arrowhead") of approximately \$8,300,000 (the "Arrowhead Loan"). SFF secured the Arrowhead Loan with liens on 12 motion pictures that generated revenues of \$820,026 in the fiscal year ended June 30, 2009, \$2,739,800 in the fiscal year ended March 31, 2008 and \$544,478 in the three month period ended June 30, 2009. The Company's only liability is to repay the Arrowhead Loan from the proceeds of the film assets pledged against the Arrowhead Loan. The Company is not required to repay the Arrowhead Loan from any of its other assets or revenues. SAE Inc's subsidiary, SAFE, Ltd. was the collateral agent of the film assets.

The Arrowhead Loan became due in February 2009 and SFF has not paid the outstanding principle and interest due thereon. Arrowhead has the right to foreclose on the pledged film assets, but has not done so at the present time. SFF has received a default notice to this effect and as a result Arrowhead is now collecting directly all sums receivable by the Company with respect to these motion pictures, and has appointed a new servicing agent for these motion pictures with the result that the Company no longer controls the licensing of these motion pictures. Failure to repay or refinance the Arrowhead Loan could result in a material disposition of assets through the loss of the Company's rights to the twelve motion pictures and related loss of revenues in amounts that are difficult to predict.

As a result of the foregoing, the Company has removed all assets accounts relating to the twelve motion pictures pledged to Arrowhead and has removed the corresponding limited recourse indebtedness from the Company's consolidated balance sheet at fiscal year ended June 30, 2009, due to the fact that the loan was a limited recourse loan and the Company had no further obligations to Arrowhead beyond the pledged film assets.

Arrowhead filed an action on September 22, 2010, which seeks recovery from the Company of the monies which the Company has retained under its interpretation of the relevant agreements with Arrowhead. In addition, Arrowhead makes substantial additional claims against the Company, Mr. Hoffman and SAP Inc. regarding claimed breaches of the terms of the operative agreements, including failure to properly account, failure to turn over materials, failure to remit monies collected, and similar matters. The claims against the Company for these breaches of warranties for damages are \$8,300,000 although Arrowhead states no basis for this amount.

The Company had moved to dismiss the action against all defendants other than Seven Arts Future Flows I LLC, which is not part of the Company. On August 9, 2011, the New York Supreme Court granted the Company's motion and dismissed all defendants except Seven Arts Filmed Entertainment Limited in its capacity as a collateral agent, which is not a material element of Arrowhead claim.

Arrowhead has purported to refile its claim against the Company and the other defendants. The Company will seek dismissal of these claims on the same grounds. The Company continues to believe that Arrowhead's claims against the Company are without substantial merit.

#### Arrowhead Capital Partners – AGC Loan

The Company's predecessor and several affiliates were named as defendants in an action by Arrowhead Capital Partners Ltd filed in the Supreme Court of New York County of New York State purportedly served on May 24, 2010, seeking to collect \$1,000,000 plus interest (the "ACG Loan") due to Arrowhead Consulting Group LLC ("ACG") as well as foreclosure on the collateral granted as part of the Cheyne Loan. The ACG Loan is fully subordinated to repayment of the Cheyne Loan, which has not been repaid, and a subsidiary of the Company has been assigned all Cheyne's rights under the subordination provision of the Cheyne Loan. As a result Management does not believe that ACG has the right to maintain this action to collect any monies or to foreclose on any collateral pursuant to the Cheyne Loan. The Company intends to vigorously defend against this action and has filed for summary judgement to dismiss it.

#### Investigation into Claim for Tax Credits (SAPLA)

The US Attorney in New Orleans is investigating claims for Louisiana film infrastructure tax credits including such tax credits to be claimed by an affiliate of the Company, Seven Arts Pictures Louisiana LLC and has issued subpoenas for discovery of documents in the possession of the Company related to their tax credits. This investigation appears to include investigation as to whether certain expenses claimed by this affiliate were improper or fraudulent. All such claimed expenses were audited by independent auditors in Louisiana and reviewed by counsel. None of these expenses or credits has been included in the Company's financial statements for any period. Management believes that this investigation will have no material adverse effect on the Company's operations or the total tax credits to be received by the Company's affiliates, but could result in charges against current or former employees of this affiliate based on prior audits, including Mr. Hoffman.

#### Parallel Action

On June 28, 2011, Seven Arts Pictures Plc. ("PLC") filed an action in the High Court of England against Parallel Media LLC ("Parallel") to collect sums due to PLC with respect to acquisition of distribution rights in Russia to four motion pictures and to confirm Parallel's obligations under both a signed and unsigned investment agreement with respect to the motion picture project Winter Queen. On the same day Parallel filed a petition to wind up and liquidate PLC in the Companies Courts of England based on its claim of repayment of \$1,000,000 of investment made by Parallel in Winter Queen. PLC is no longer part of the Company.

On September 19, 2011, Parallel filed a new action against PLC and SAE in the Superior Court of California, asserting the same claims as in the winding up petition and seeking to enjoin the proposed administration proceedings in England. A request for a preliminary injunction was denied by the Superior Court.



#### HMRC Investigation

On July 19, 2011 Officers of Her Majesty's Revenue & Customs ("HMRC") attended the offices of Seven Arts Pictures Plc. (the "Company") in London. Documents were retained appertaining to arrangements involving the subscription for shares in a number of companies which had lost value, resulting in subscribers making claims to tax relief.

The Company's participation in these transactions was limited to the Company's predecessor's transfer of rights to certain motion pictures to the investors in return for their investments in the production and release costs of those pictures and making available the provision of loans to fund a portion of those investments. The Company received no tax benefits from the transactions, which were made on arms-length terms. The Company believes that it is not a subject of the HMRC investigation.

In connection with the transactions, the Company did not make any representations or warranties to any party, including the investors, regarding any potential tax benefits related to the transactions. Prior to the closing of the transactions the investors obtained and made available to the Company, an opinion of prominent Queen's counsel, specializing in United Kingdom tax laws, that the transactions were permitted and acceptable under the terms of the applicable United Kingdom revenue laws. The Company remains confident that the transactions were permitted and acceptable under the terms of the applicable United Kingdom revenue laws.

HMRC has requested interviews with three officers of the Company to discuss whether those officers were involved in the arrangements for subscription of shares in the relevant companies. The Company is fully cooperating with the investigation. The Company believes there is no basis for any claim of responsibility of any of its officers or employees. Based on facts currently known by the Company, there is no need for it to record a contingent liability in its financial statements in connection with the investigation or the related transactions.

#### Earnout for David Michery

The Company's Asset Purchase Agreement with David Michery provided for 50,000 of the Company's \$100 par, Convertible Redeemable Series B Preferred Shares, be held in Escrow until the Net EBIT (as defined in the agreement) from distribution of the DMX Albums and two albums embodying the performance of Bone Thugs-n-Harmony exceeds \$5,000,000, as confirmed by the Company's independent auditor. At the end of five years, should the Net EBIT be less than \$5,000,000, the shares will be released on a fractional basis, as defined in the agreement. The Company has determined the fair value of the earnout as of the acquisition date to be \$2,837,134 and has reflected it as a liability as of March 31, 2012.

#### NOTE 9 – CONVERTIBLE NOTES PAYABLE

##### Existing Notes:

On January 27, 2012, the Company converted \$132,645 of the Runway debt and relevant interest into 1,211,219 shares of the Company's common stock. On January 31, 2012 an additional \$50,000 of debt was converted to 333,333 shares and the final \$50,000 was converted into 333,333 shares on February 15, 2012.

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New Notes:

The following table presents convertible notes payable entered into during this fiscal year. Each of these notes is convertible into shares of the company's common stock at the indicated fixed conversion rate.

Convertibles	Principal	Fixed conversion price	Start date	End date
FireRock	\$ 300,000	\$ 0.25	12/12/2011	12/06/2012
RBSM	\$ 150,000	\$ 0.46	Due now	
Hanover	\$ 62,660	\$ 0.25	11/19/2011	04/16/2012
Hanover	\$ 150,000	\$ 0.30	10/19/2011	11/19/2012
Hanover	\$ 445,000	\$ 0.20	02/23/2012	02/21/2013
Tripod/CMS etc	\$ 100,000	\$ 0.27	12/15/2011	06/30/2012
Tripod	\$ 50,000	\$ 0.24	02/01/2012	07/31/2012
Tripod	\$ 150,000	\$ 0.24	02/01/2012	02/01/2013
Michael Briskin	\$ 100,000	\$ 0.23	01/31/2012	07/31/2012
Beauvoir	\$ 50,000	\$ 0.20	04/14/2011	10/14/2011
Beauvoir	\$ 100,000	\$ 0.20	11/30/2011	03/31/2012
Beaufort	\$ 350,000	\$ 0.20	02/29/2012	08/26/2012
Rowett Capital	\$ 200,000	\$ 0.20	02/29/2012	08/26/2012
Runway	\$ 190,000	\$ 0.20	01/22/2012	09/30/2012
Sendero	\$ 250,000	\$ 0.20	01/24/2012	09/30/2012
	\$ 2,647,660			
Balance of S144/3a9 Debt Conversions				
Hanover/Magna –Blue Rider	\$ 900,000	\$ 0.20		
Magna – Palm	\$ 80,000	\$ 0.28		
Alpha/Olsen –Mark Betor	\$ 100,000	\$ 0.10		
	\$ 1,080,000			
TOTAL	\$ 3,727,660			

The Company has evaluated these convertible notes for embedded derivative features and has determined that no derivative liability exists. Assuming all notes are settled via common stock, the number of shares to be issued to satisfy approximately \$3,727,660 of debt plus accrued interest is approximately 17,653,000 shares of the company's common stock .



## NOTE 10 – LOANS PAYABLE

The Company has the following indebtedness as of March 31, 2012:

Lender	Start Date	Due date	Amount Outstanding	Applicable Interest Rate	Status
Film and Production Loans					
Palm Finance			\$ 3,588,435	18 %	Forebearance agreement
Palm Finance			\$ 1,101,986	18 %	Forebearance agreement
120db Film Finance LLC			\$ 4,425	Non stated	Due on demand
Cold Fusion Media Group LLC			\$ 610,360	10 %	Due on demand
Pledged shares			\$ (384,000 )		
Total Film and Production Loans			\$ 4,921,206		
Trafalgar Capital (in liquidation)	10/15/2008	08/31/2009	\$ 531,987	9 %	Due on demand
TCA - loan interest	03/31/2011	09/30/2011	\$ 75,770	10 %	Due on demand
Runway - Loan - \$190k	01/11/2012	09/30/2012	\$ 194,997	12 %	Due September 2012
Sendero - \$250k	01/24/2012	09/30/2012	\$ 255,507	12 %	Due September 2012
Isaac Organisation	01/20/2012	07/20/2012	\$ 255,836	12 %	Due July 2012
Tripod Group - \$150k loan	02/01/2012	02/01/2013	\$ 152,811	12 %	Due Feb 2012
Hanover Holding Loans	11/16/2011	02/16/2012	\$ 63,989	12 %	Due on demand
Beauvoir Capital Ltd	11/22/2011	03/31/2012	\$ 106,411	18 %	Due on demand
FireRock	12/12/2011	06/12/2012	\$ 310,849	12 %	Due June 2012
Briarwood Investment Inc-Eastside Holdings	10/25/2011	04/30/2012	\$ 208,658	10 %	Due April 2012
Aegis - Tripod	12/15/2011	06/30/2012	\$ 34,507	12 %	Due June 2012

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Aegis – CMS	12/15/2011	06/30/2012	\$ 34,506	12	% Due	June 2012
Aegis - Rachel	15/12/2011	06/30/2012	\$ 34,506	12	% Due	June 2012
Beauvoir Capital - \$50k	04/14/2011	10/14/2011	\$ 54,822	10	% Due	on demand
Hanover Holding Loan \$150k	10/19/2011	05/18/2012	\$ 156,740	10	% Due	May 2012
Tripod Group - \$50k loan	01/16/2012	06/30/2012	\$ 51,233	12	% Due	June 2012
Michael Briskin - Loan \$100k	02/03/2012	02/03/2013	\$ 101,874	12	% Due	February 2013
Hanover Loan \$445k	10/19/2011	10/19/2012	\$ 464,995	10	% Due	October 2012
Beaufort Loan \$350k	02/29/2012	08/26/2012	\$ 353,567	12	% Due	August 2012
Rowett Capital Loan \$200k	02/28/2012	09/30/2012	\$ 202,104	12	% Due	September 2012
Total Corporate Loans			\$ 3,645,669			
<b>TOTAL LOANS</b>			<b>\$ 8,566,875</b>			

The Company converted \$2,963,028 of the film and production loans into 5,989,349 shares of common stock during the three months ended September 30, 2011, \$906,000 of film and production loans for 3,490,385 shares of common stock in the 2nd quarter ended December 31, 2011 and \$943,580 of film and production loans for 6,749,658 shares of common stock in the 3 months to March 31, 2012.

NOTE 11 – EQUITY TRANSACTIONS

First quarter 2011/12

On August 31, 2011, NASDAQ approved the substitution of one share of SAE, Inc. stock for the Company's NASDAQ listing, effective at the opening of trading on September 1, 2011. On that date, each of the Company's ordinary shares were exchanged for one share of common stock of SAE, and commenced trading on NASDAQ as the successor to the Company's NASDAQ listing. This transaction was approved by the Company's shareholders at the Company's Extraordinary General Meeting on June 11, 2010.

The Company is authorized to issue 250,000,000 common shares at a par value of \$0.01 per share. These shares have full voting rights. At September 30, 2011 and June 30, 2011, there were 11,149,480 and 2,643,131 respectively, common shares outstanding. The Company's predecessor, PLC, had a 1:5 reverse stock split on May 9, 2011. The shareholders agreed to increase the authorized shares to 250,000,000 from 50,000,000 at the Company's shareholder meeting in February 2012.

During the three months ending September 30, 2011, Company issued 6,496,349 shares in satisfaction of \$3,188,028 of outstanding loans payable and accrued interest, consisting of \$225,000 of convertible notes payable and \$2,963,028 of film and production loans. The conversions were done at contractual share prices ranging from \$.20 to \$2.00 per share.

In July 2011, the Company also issued 10,000 shares for investor relations services valued at approximately \$10,000.

The Company did not assume the deferred stock of the listing predecessor which was outstanding at June 30, 2011. Deferred stock is subordinated to all other classes of stock.

As of September 30, 2011, \$1,986,722 of stock was fully paid but still to be issued, consisting of \$1,251,250 of Series A preferred stock and \$735,472 of debt that was being converted to equity. There were 11,149,480 shares were outstanding as of September 30, 2011.

Second Quarter 2011/12

Between October 1, 2011 and December 31, 2011 the Company issued 11,470,808 shares. The total number of shares outstanding on December 31, 2011 was 22,620,288.

4,639,049	common shares were issued in satisfaction of the \$612,336 of convertible debt shares at an average conversion price of \$0.13/share .
2,851,374	common shares were issued on the conversion of the Agua Alta, Sendero and Isaac convertible notes totalling \$427,706 at an average conversion price of \$0.15/ share.
3,490,385	common shares were issued in satisfaction of \$906,000 of corporate loans at an average conversion price of \$0.26/share.
400,000	common shares were issued as restricted stock for cash, \$250,000 to Fletcher and \$150,000 to Goldstrand at \$1.00/share
75,000	common restricted shares were issued for investor relations services at \$0.36/share
15,000	common restricted shares were issued to a director in lieu of compensation at \$0.50/share
11,470,808	



Third Quarter 2011/12

Between January 1, 2012 and March 31, 2012, the Company issued 19,348,684 shares at an average price of \$0.19 per share. The total number of shares outstanding on March 31, 2012 was 41,968,972. (See Subsequent Events Note 13 for stock issuances subsequent to March 31, 2011).

6,749,658	common shares were issued in satisfaction of the \$943,580 of newly converted film debt at an average conversion price of \$0.14/share .
4,566,589	common shares were issued in satisfaction of \$929,596 of overhead at an average conversion price of \$0.20/share
3,492,255	common shares were issued on the conversion of old notes including the final conversion of the Runway convertible notes, total debt of \$516,568 was converted at an average conversion price of \$0.15/ share.
3,074,962	common shares were issued in satisfaction of \$698,736 of film loans previously converted at an average conversion price of \$0.23/share.
1,200,000	common shares were issued as restricted stock for cash, to Blue Rider at \$0.50/share
265,220	common restricted shares were issued for consultancy services provided under the S-8 authority at \$0.28/share
19,348,684	

During the nine months ended March 31, 2012, the Company issued 100,000 options to the seven members of the board of directors. These options have a five year term and a strike price equal to the closing price of the Company's stock at the date of issue. Each director was issued 50,000 options with a strike price of \$0.44 on October 14, 2011 and 50,000 options with a strike price of \$0.39 on December 6, 2011. Half of the options vested on December 31, 2011 and the remaining half will vest on December 31, 2012.

During the quarter ended March 31, 2012, the Company issued 2,000,000 options to David Michery in conjunction with his employment agreement with the Company. These options have a strike price of \$0.18 and vest and shall be exercisable in equal monthly installments over the term of his employment agreement, which is February 22, 2012 through December 31, 2016.

During the quarter ended March 31, 2012, the Company has agreed to issue 50,000 options per year to Jake Shapiro in conjunction with his employment agreement with the Company. These options have a strike price equal to the closing price of the Company's stock at the date of issue, with the exception of the first year, which the strike price was set at \$0.79 per share. The Company measures compensation expense related to stock options with the Black Scholes option pricing model, and recognizes expense over the vesting period.

In January 2012, the Company filed a registration statement on Form S-8 in connection with the registration under the Securities Act of 1933, as amended, of 5,000,000 shares of the Company's common stock under the Company's 2012 Stock Incentive Plan.

Convertible Preferred Shares

125,125 shares of Series A Cumulative Convertible \$10.00 Preferred Stock with a dividend rate of 8% (payable quarterly) were issued in November 2011. The conversion price into common stock of the Company is \$0.15/share.

An additional \$115,000 was invested for another 11,500 Series A preferred stock which has not yet been issued. This amount is included in the shares to be issued number in accruals on the balance sheet as of March 31, 2011.

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A further 10,859 Series A shares have been subscribed for but not yet issued, as of March 31, 2012. This amount is included in the shares to be issued on the balance sheet as of March 31, 2011.

180,000 Series B convertible preferred shares, \$100.00 par value have been issued to two shareholders although 120,000 of such shares are held in escrow subject to earnout. The shares were issued to acquire music assets for the Company. These shares in escrow are shown on the balance sheet as a contra to equity.

The earnout provision on David Michery's \$5,000,000 or 50,000 Series B preferred shares has been calculated using the fair value of the \$5,000,000 over a 5 year term with a discount rate of 12% per year. No earn-out provision has been applied to Big Jake Music assets as the Company does not yet believe it has any basis for this earn-out at the moment.

#### NOTE 12 – RELATED PARTY TRANSACTIONS

The Company's Chief Executive Officer, Peter Hoffman, controls several companies, including Seven Arts Pictures, Inc. ("SAP, Inc.") that are not part of the Company but from which it obtains or transfers distribution rights or other assets related to the business and which control production of the motion pictures. The agreements with Mr. Hoffman, and the companies controlled by him, provide that all revenues related to the Company's business payable to Mr. Hoffman or any of these related party companies is due to the Company, except Mr. Hoffman's salary, bonus and stock ownership. None of these affiliates are variable interest or special purpose entities.

Pursuant to a related party agreement, SAP, Inc. holds ownership of limited liability corporations in the United States, with all distribution rights and profits thereof being due to SAFE, Ltd. In addition, they have also provided other services for Seven Arts Pictures Plc. and SAFE, Ltd. And SAE, Inc. at no fee other than Mr. Hoffman's salary and the direct third party costs of the Los Angeles office, all of which are reflected in the financial statements of SAFE, Ltd. These other services are any reasonable requests of the management of the Company including accounting services, audits of distribution statements, collection of accounts receivable, supervision of production of motion pictures and similar day-to-day aspects of the Company's business. Effective January 1, 2012 no further such transactions are intended.

The Company has made and received advances from and to SAP Inc. and various Louisiana limited liability companies referred to above, where the advances from and to these related parties do not bear interest. The balances of these combined accounts were \$3,552,137 and \$2,725,974 as of March 31, 2012 and June 30, 2011, respectively.

On February 28, 2012 the Company took out a convertible loan of \$200,000 from Rowett Capital Ltd. This was then loaned to 807 Esplanade to cover outstanding interest payments due on the construction loan.

#### NOTE 13 – FAIR VALUE MEASUREMENTS

Cash, accounts receivable, accounts payable and other accrued expenses and other current assets and liabilities are carried at amounts which reasonably approximate their fair values because of the relatively short maturity of those instruments.

ASC 820, "Fair Value Measurements and Disclosures", establishes a framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy under ASC 820 are described as follows:

Level 1 - Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Company has the ability to access.

Level 2 - Inputs to the valuation methodology include:

quoted prices for similar assets or liabilities in active markets;  
quoted prices for identical or similar assets or liabilities in inactive markets;

inputs other than quoted prices that are observable for the asset or liability;  
inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

Level 3 - Inputs to the valuation methodology are unobservable and significant to the fair value measurement.



The asset or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

The preceding method described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although the Company believes its valuation method is appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date. As of March 31, 2012 and June 30, 2011, all of the Company's assets and liabilities were considered current and due to the short maturity the carrying amounts are considered to approximate fair value.

#### NOTE 14 – RECENT ACCOUNTING PRONOUNCEMENTS

In May 2011, the FASB issued guidance intended to achieve common fair value measurements and related disclosures between U.S. GAAP and international accounting standards. The amendments primarily clarify existing fair value guidance and are not intended to change the application of existing fair value measurement guidance. However, the amendments include certain instances where a particular principle or requirement for measuring fair value or disclosing information about fair value measurements has changed. This guidance was effective for the periods beginning after December 15, 2011, and early application is prohibited. The Company adopted these amendments on January 1, 2012; and the requirements did not have a material effect.

In June 2011, the FASB issued Accounting Standards Update (“ASU”) No. 2011-05, “Comprehensive Income — Presentation of Comprehensive Income.” ASU No. 2011-05 eliminates the option to present the components of other comprehensive income as part of the statement of stockholders' equity. It requires an entity to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In December 2011, the FASB issued ASU 2011-12, “Comprehensive Income — Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in ASU 2011-05,” to defer the effective date of the specific requirement to present items that are reclassified out of accumulated other comprehensive income to net income alongside their respective components of net income and other comprehensive income. All other provisions of this update, which are to be applied retrospectively, were effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. The Company adopted these amendments on January 1, 2012; and the requirements did not have a material effect.

In December 2011, the FASB issued ASU No. 2011-11, “Balance Sheet — Disclosures about Offsetting Assets and Liabilities.” ASU 2011-11 requires entities to disclose information about offsetting and related arrangements of financial instruments and derivative instruments and will be applied retrospectively for all comparative periods presented. ASU 2011-11 is effective for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. The Company currently believes that this ASU will have no significant impact on its consolidated financial statements.

NOTE 15 – SUBSEQUENT EVENTS

The Company issued the following shares of common stock subsequent to March 31, 2012:

New Stock Issuances through May 10, 2012

14,442,472	common shares were issued in satisfaction of \$1,120,000 of film loans previously converted at an average conversion price of \$0.09/share. (high of \$.10 and low of \$.06)
7,638,890	common shares were issued in satisfaction of the \$625,000 of newly converted debt at an average conversion price of \$0.08/share. (high of \$.09 and low of \$.06)
2,757,789	common shares were issued for consultancy services provided under the S-8 authority at \$0.14/share (high of \$.20 and low of \$.12)
1,282,051	common shares were issued in satisfaction of \$100,000 of existing overhead liabilities at an average conversion price of \$0.08/share
26,121,202	

Total shares outstanding as of May 10, 2012 was 68,090,174. (including 2 million shares issued to SAP Plc.)

Additionally, the Company had the following new convertible debt acquired, which will be converted to equity, subsequent to March 31, 2012:

- (1) \$50,000 loan was issued on April 4, 2012 by Michael Briskin for conversion at \$0.09
- (2) \$60,000 loan was issued on April 17, 2012 by Michael Briskin for conversion at \$0.09
- (3) \$50,000 loan was issued on April 24 2012 by Michael Briskin for conversion at \$0.06

Creditors Liquidation of SAP Plc.

The Company's listing predecessor Seven Arts Pictures Plc. ('PLC') was placed by the English Companies Court into compulsory liquidation on November 8, 2011. The Company's CEO, Mr. Peter Hoffman, as a director of PLC had sought an administration order but this request was denied by the Courts as a result of inter alia the opposition of Parallel Pictures LLC ('Parallel'). PLC's principal creditors have appointed a liquidator for the orderly winding up of its remaining assets not transferred to the Company pursuant to the Asset Transfer Agreement, effective January 27, 2011.

Mr. Hoffman expects that the liquidator and PLC will pursue its substantial claims against Parallel and its defenses to Parallel's claims. Parallel has claimed in the proceedings in England and the United States that the Asset Transfer Agreement between the Company and PLC was 'fraudulent' and may seek additional compensation or guarantees from Company. Management believes that the Asset Transfer Agreement is a valid agreement for value and not subject to attack and that Parallel will not prevail in its claims. Management believes it has the support of its creditors to resist these claims by Parallel which are disputed by the Company and as a result Parallel will not obtain any relief from the courts on this issue.

Based on discussions with the liquidator, our management believes this liquidation proceeding will have no material effect on the cost, business or market value of common stock

Filing of S-8

In January 2012, the Company filed a registration statement on Form S-8 in connection with the registration under the Securities Act of 1933, as amended, of 5,000,000 shares of the Company's common stock under the Company's

2012 Stock Incentive Plan.

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## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS

### FORWARD-LOOKING STATEMENTS

Certain statements in this document might constitute "forward-looking statements". Some, but not all, forward-looking statements can be identified by the use of words such as "anticipate," "believe," "plan," "estimate," "expect," and "intend," statements that an action or event "may," "might," "could," "should," or "will" be taken or occur, or other similar expressions. Although the Company has attempted to identify important factors that could cause actual results to differ materially from expected results, such forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Company, or other future events, to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Such factors include, among others, the following risks: the need for additional financing; uncertainties and risks related to carrying on business in foreign countries; risks associated with third party infringement of copyrights and other intellectual property, especially the unauthorized duplication of motion picture DVDs and unauthorized distribution of motion pictures through the world wide web; risks associated with the lack of enforcement of applicable copyright and intellectual property laws, especially in foreign countries; risks associated with changing copyright and applicable intellectual property laws, especially in foreign countries; risks associated with changing distribution models for motion pictures, especially on the world wide web; risks associated with restrictions of motion picture content, especially in foreign countries; reliance on key personnel; the potential for conflicts of interest among certain officer, directors or promoters of the Company; the absence of dividends; currency fluctuations; competition; dilution; the volatility of the Company's ordinary share price and volume; and tax consequences to United States Shareholders. Except as required by law, the Company undertakes no obligation to revise any forward-looking statements because of new information, future events or otherwise.

## Company Overview

Our common stock is traded on NASDAQ under the symbol "SAPX".

## Film Company

We license distribution rights in our motion pictures in the United States and in most foreign territories prior to and during the production or upon the acquisition of rights to distribute a picture. We share in the commissions generated by the sales of the pictures. Sale of a license to distribute a motion picture prior to its delivery is termed a "pre-sale" and may occur at any time during the development and production process. In a typical license agreement, we license a picture to a distributor before it is produced or completed for an advance from the licensee, which advance is recoverable by the distributor from our share of the revenues generated by the distribution of the picture in the licensee's territory, after deduction of the distributor's expenses and distributor fee. The advance usually is in the form of a cash deposit plus a letter of credit or "bank letter" for the balance payable 10-20% on execution (i.e., the cash deposit) and the balance on delivery (i.e., the letter of credit or "bank letter"). The license grants the distributor the right to the post-theatrical release of the picture in all or certain media in their territory for a predetermined time period. After this time, the distribution rights revert back to us and we are then free to re-license the picture. The license specifies that the distributor is entitled to recoup its advance from the revenue generated by the release of the picture in all markets in its territory, as well as its release costs and distribution fees.

After the distributor has recouped its advance, costs, and fees, any remaining revenue is shared with us according to a predetermined formula. This is known as an "overage" and can be a significant source of revenue for us from successful films. However, a film's poor reception in one market does not preclude it from achieving success in another market and generating significant additional revenue for us in the form of an "overage" in that territory. In all of our licensing arrangements, we retain ownership of our films and maintain our control of each copyright. We intend to continue the practice of retaining underlying rights to our film projects in order to continue to build our motion picture library to license or sell in the future.

We create a separate finance plan for each motion picture we produce. Accordingly, the sources of the funds for production of each motion picture vary according to each finance plan. We utilize financing based on state and foreign country tax credits (e.g. Louisiana, United Kingdom and Hungary) and direct subsidies, "mezzanine" or "gap" funds, which are senior to our equity, and senior secured financing with commercial banks or private lenders, together in certain cases with a limited investment from us, which is customarily less than 10% of the production budget. Since each finance plan is unique to each motion picture, we cannot generalize as to the amount we will utilize any of these sources of funds for a particular motion picture. We generally obtain some advances or guarantees prior to commitment to production of a motion picture project, but those amounts may not be substantial on smaller budgeted motion picture (e.g., under \$10,000,000), and in certain cases we have committed to production with an insubstantial amount of advances and guarantees. Unless we can manage the risks of production through the use of these financing techniques, we will not likely commit to production of larger budget motion pictures (e.g., over \$15,000,000), and we have never in the past committed to such productions, without substantial advances or guarantees from third-party distributors, or the equivalent in "non-recourse" financings.

## Music Company

Seven Arts Music Inc ("SAM") became a wholly owned subsidiary of the Company at the beginning of March 2012, although set-up costs had been incurred as early as September 2011. Costs are currently being incurred in the delivery of the first of the DMX albums acquired from David Michery (currently planned for release in August 2012) and the initial costs in creating the first album for Bone Thugs-N-Harmony. Several other new artists are being considered by SAM.



## Company Outlook

The principal factors that affected our results of operations have been the number of motion pictures delivered in a fiscal period, the distribution rights of motion pictures produced by others acquired in a fiscal period, the choice of motion pictures produced or acquired by us, management's and talents' execution of the screenplay and production plan for each picture, the distribution and market reactions to the motion pictures once completed, management's ability to obtain financing and to re-negotiate financing on beneficial terms, the performance of our third-party distributors and our ability to take advantage of tax-incentivized financing. These factors will continue to be, in our opinion, the principal factors affecting future results of operation and our future financial condition. No particular factor has had a primary or principal effect on our operations and financial condition in the periods discussed below.

Our revenues principally consist of amounts we earned from third-party distributors of its motion pictures. We recognize revenue from license fees as and when a motion picture is delivered to the territory to which the license relates if we have a contractual commitment and the term of license has begun or upon receipt of a royalty statement or other reliable information from a distributor of the amounts due to us from distribution of that picture. A motion picture is "delivered" when we have completed all aspects of production and may make playable copies of the motion picture for exhibition in a medium of exhibition such as theatrical, video, or television distribution.

We also recognize revenue beyond an initial license fee from our share of gross receipts on motion pictures which we recognize as revenue when we are notified of the amounts that are due to us. In some fiscal periods, a significant portion of our revenue is derived from sources other than motion picture distribution, including the cancellation of debt and interest income on a financing transaction.

We have also benefited significantly from our ability to raise third party film equity investments such as in tax advantaged transactions under which we transfer to third party investor's tax benefits for motion picture production and distribution. These types of investments have enabled us to substantially reduce the cost basis of our motion pictures and even to record significant fee-related revenues.

## Results of Operations for the Three-Month Period Ended March 31, 2012 vs. 2011

We generated a net loss of \$1,585,789 for the three months ended March 31, 2012, compared to a net loss of \$973,034 for the three months ended March 31, 2011. Included in the quarter ended March 31, 2012 are \$278,529 of start up costs for Seven Arts Music Inc.

A discussion of the key components of our statements of operations and material fluctuations for the three months ended March 31, 2012 and 2011 is provided below removing the music company start-up costs.

Film revenues totalled \$187,793 for the three months ended March 31, 2012, compared to \$272,703 for the three months ended March 31, 2011. A comparison of the 2011 and 2010 sales is as follows:

The majority of the 2012 sales were on-going royalties on PoolBoys, Night of the Demons and Nine Miles Down  
The 2011 sales were from royalties spread over several titles but with the majority from Deal and Autopsy.  
No fee related revenues were earned in either quarter

The costs of acquiring and producing films are amortized using the individual-film-forecast method, whereby these costs are amortized and participations and residuals costs are accrued in proportion to that the current year's revenue bear's to management's estimates of ultimate revenue expected to be recognized from the exploitation or sale of the films. The amortisation in the first quarter of 2012 was mainly on Pool Boys in line with achieved sales while the 2011 charge was mainly against Deal, again in line with achieved sales for the period





Other costs of revenue in the period totalling \$262,041 versus \$18,208 in the same quarter in 2011. The charge in the current period was due to:

- \$154,276 media credit expenditure on the theatrical release of PoolBoys as a trial for the media credit assets to be acquired under the deal with Big Jake Music;
- a one time payment to producers of Drunkboat of \$64k and ;
- commissions payable to our sales agent of \$30,000 on cash receipts received in the period.

General and administrative expenses decreased from \$591,285 for the three months ended March 31, 2011 to \$222,368 (excluding \$278,529 of the music company expenses) for the three months ended March 31, 2012. The net decrease is primarily due to legal and professional fees in the quarter being reduced by the assumption of fees by the PLC, as the expense was related to cases that are PLC liabilities, the cost of the equity rbeing raised was reflected as a reduction of proceeds versus legal expense, and prepaid to a major on-going legal case, as the fees are anticipated to be recovered based upon a similar favorable judgement in another venue.

A bad debt write-off of \$109,481 was taken in the three months to March 31 2012 being contracts terminated for non-payment where replacement distributors have been found in the territory.

Interest charges have increased from \$722,282 in the three months to March 31, 2011 to \$1,476,417 in the three months to March 31, 2012 due mainly to the interest on the loans with Palm Finance. The movie, Pool Boys had not been released in the 2011 quarter therefore all interest charged was capitalized to film costs, which are now being expensed. Also a settlement was reached with Blue Rider on the Deal loan which incurred additional interest of \$100k.

No tax expense was recognized in either period.

#### Results of Operations for the Three-Month Period Ended December 31, 2011 vs. 2010

We generated a net loss of \$1,095,995 for the three months ended December 31, 2011, compared to net income of \$569,711 for the three months ended December 31, 2010. A discussion of the key components of our statements of operations and material fluctuations for the three months ended December 31, 2011 and 2010 is provided below.

Film revenues totalled \$207,790 for the three months ended December 31, 2011, compared to \$1,137,647 for the three months ended December 31, 2010. A comparison of the 2011 and 2010 sales is as follows:

The majority of 2011 sales came from the US digital release of the movie "The Pool Boys" in September 2011.

The majority of 2010 sales came from the US release of the movie "Deal".

In December 31, 2010, there was fee-related revenue of \$570,029 for additional producers fees associated with films produced in Louisiana. There was no fee income in the three months to December 31, 2011.

The costs of acquiring and producing films are amortized using the individual-film-forecast method, whereby these costs are amortized and participations and residuals costs are accrued in proportion to that the current year's revenue bear's to management's estimates of ultimate revenue expected to be recognized from the exploitation or sale of the films.

An amortization charge of \$336,527 was made in the period to December 31, 2011 mainly against the title "The Pool Boys" in line with revenue forecasts.

The equivalent amortization charge in December 31, 2010 was \$639,257 mainly against the title "Deal".

Other costs of revenue in the period totalling \$283,949 versus \$229,757 in the same quarter in 2010. The charge in the current period was due to the write-off of the costs of distribution of "The PoolBoys" while in the 2010 period related to the write-off of distribution costs on "Deal"

General and administrative expenses increased from (\$12,121) for the three months ended December 31, 2011 to \$354,367 for the three months ended December 31, 2010. The net increase is primarily due to the following:

\$228,661 of additional legal and professional costs related to:  
HMRC investigations of \$130,000  
Set-up of SAE Inc of \$20,000  
Investor Relation fees of \$60,000  
Transfer agent, HMRC fines and edgarising fees of \$90,000  
Content Media,Parallel Media and Nine Miles Down actions of \$60,000

Payroll has increased from (\$41,809) for the three months ended December 31, 2010 to \$326,746 in the three months to December 31, 2011 which is due to the reversal of an accrual in December 31, 2010, prior to quarterly reporting. We were not required to do quarterly filings in 2010 due to our status as a foreign filer at that time.

Interest charges have marginally increased from \$281,440 in the three months to December 31, 2010 to \$ 328,942 in the three months to December 31, 2011 due mainly to 50% of the loan interest being capitalized in 2010 as PoolBoys had not yet been released by December 2010.

No tax expense was recognized in either period.

#### Results of Operations for the Six-Month Period Ended December 31, 2011 vs. 2010

We generated a net loss of \$2,078,283 for the six months ended December 31, 2011, compared to a net loss of (\$209,265) for the six months ended December 31, 2010. A discussion of the key components of our statements of operations and material fluctuations for the six months ended December 31, 2011 and 2010 is provided below.

#### Revenue

1)Film revenues totaled \$800,331 for the six months ended December 31, 2011, compared to \$1,237,952 for the six months ended December 31, 2010. A comparison of the 2011 and 2010 revenue is as follows:

The majority of 2011 sales came from the US digital release of the movie "The Pool Boys" in September 2011. Significant sales to third party distributors were also made on the title in Canada and Australia during the period. \$150,000 of royalty income spread over several titles but mainly continuing income from "Deal"

was received during the period.

2010 sales were mainly distribution income earned from third parties on the film "Deal" in overseas television markets and a small amount of sales agency fees.

2) In the six months to December 31, 2010, there was fee-related revenue of \$570,029 being additional producers fees associated with films produced in Louisiana. No fee-related income was received in the six months to December 31, 2011.

## Cost of Revenue

The costs of acquiring and producing films are amortized using the individual-film-forecast method, whereby these costs are amortized and participations and residuals costs are accrued in proportion to that the current year's revenue bear's to management's estimates of ultimate revenue expected to be recognized from the exploitation or sale of the films.

An amortization charge of \$800,331 was made in the period to December 31, 2011 mainly against the title "The Pool Boys" in line with revenue forecasts.

The equivalent charge in December 31, 2010 was \$695,620, this was mainly against the title "Deal".

Other costs of sales in the period totalled \$299,289 versus \$250,088 in the same period in 2010. The charge in the current period was due the distribution costs for the release of "The PoolBoys" whilst the 2010 charge generally related to the on-going distribution of "Deal".

## General and administrative Costs

General and administrative expenses increased from \$338,358 for the six months ended December 31, 2010 to \$1,036,252 for the six months ended December 31, 2011. The net increase is primarily due to the following:

- \$362,115 of additional legal and professional costs mainly related to HMRC investigations of \$130,000
- Set-up of SAE Inc of \$20,000
- Investor Relation fees of \$60,000
- Transfer agent, HMRC fines and edgarising fees of \$90,000
- Content Media, Parallel Media and Nine Miles Down actions of \$60,000

Payroll for directors has increased by \$399,000 in the 2011 period compared to the 2010 period due to a director moving from a consultancy arrangement to payroll expense and the removal of the accrual for one executive director in 2010.

## Interest expense

Interest expense has increased from \$702,094 in the six months to December 31, 2010 to \$742,742 in the six months to December 31, 2011 due to the increase in corporate loans along with the full charge for Poolboys loan interest which was capitalised in the 2010 period, set off against the reduction in interest on the Palm Finance films due to the debt/equity swaps.

No tax expense was recognized in either period.

## Employees

As of March 31, 2012, Seven Arts had 10 employees and independent contractors, providing full time services. Our affiliates employ many part time employees for production of our motion pictures, but we do not engage temporary employees on any regular or material basis. We are not signatory to any labor union collective bargaining agreements, but our affiliates in the United States are signatory to the current Writer's Guild of America, Directors Guild of America and IATSE Low Budget Agreements and have in the past been signatory to the Screen Actors Guild Agreement. Our employees have ranged from a low of six to a high of fourteen over the last three fiscal years.



## Liquidity

As of March 31, 2012, our assets totaled \$41,269,929, which included, among other items, receivables totaling \$274,862, amounts due from related parties totaling \$3,552,137, and prepayments of \$3,771,179. Our working capital as of March 31, 2012 was (\$8,692,948), compared to (\$15,199,849) as of June 30, 2011. The large negative balances at June 30, 2011 were mainly due to film loans having to be treated as current debt. We have reduced our outstanding film debt from \$10,890,430 as at June 30, 2011 to \$4,921,206 as at March 31, 2012 due to a series of debt for equity swaps and the maturity and exercise of convertible debt. This has helped improve the working capital position.

Historically, we have successfully raised additional operating capital through private equity funding sources or loans from affiliates. However, no assurances can be given that we will be able to obtain sufficient working capital through the sale of common stock and/or borrowing or that the development and implementation of our business plan will generate sufficient future revenues to sustain ongoing operations.

## Off-Balance Sheet Arrangements

We have no off-balance sheet arrangements.

## Litigation

### Fireworks Litigation

The Company prevailed in a motion for summary adjudication on February 10, 2011 in an action against CanWest Entertainment and two of its affiliates ("CanWest") confirming the Company's ownership of five motion pictures "Rules of Engagement", "An American Rhapsody," "Who Is Cletis Tout," "Onegin," and "The Believer", (the "Copyrights"). The Company has filed an action in England against Content Media Corporation ("Content") and Paramount Picture Corp. ("Paramount") to recover the Copyrights and substantial damages for the use of the copyrighted works after their purported acquisition from CanWest. The Company may incur up to \$200,000 in legal expenses to pursue this claim but expects to recover those fees from Content.

### Jones Film

Seven Arts Pictures plc ("PLC"), the Company's listing predecessor, its then subsidiary Seven Arts Filmed Entertainment Limited ("SAFE"), and Seven Arts Pictures Inc. ("SAP"), were the subject of two arbitration awards of attorney fees totalling approximately \$900,000, with interest and charges, both of which were reduced to judgment in favour of Jones film ("JF"). PLC has accrued a provisional liability in the amount of \$800,000 including approximately \$100,000 of accrued interest at June 30, 2011. The Company paid approximately \$525,000, the amount of the first arbitration award plus interest and charges, in November, 2011, Management believes the Company has no further liability in this matter. JF asserts that the Company is liable as the "successor in interest" to PLC, which the Company denies.

### Arrowhead Target Fund

Seven Arts Future Flow I ("SFF"), a limited liability Company owned by SAP Inc., a Company previously controlled by Mr. Hoffman, obtained financing from the Arrowhead Target Fund, Ltd. ("Arrowhead") of approximately \$8,300,000 (the "Arrowhead Loan"). SFF secured the Arrowhead Loan with liens on 12 motion pictures that generated revenues of \$820,026 in the Fiscal Year Ended June 30, 2009, \$2,739,800 in the Fiscal Year Ended March 31, 2008 and \$544,478 in the three month period ended June 30, 2009. The Company's only liability is to repay the Arrowhead Loan from the proceeds of the film assets pledged against the Arrowhead Loan. The Company is not required to repay the

Arrowhead Loan from any of its other assets or revenues. SAE's subsidiary, SAFE, Ltd. was the collateral agent of the film assets.

The Arrowhead Loan became due in February 2009 and SFF has not paid the outstanding principle and interest due thereon. Arrowhead has the right to foreclose on the pledged film assets, but has not done so at the present time. SFF has received a default notice to this effect and as a result Arrowhead is now collecting directly all sums receivable by the Company with respect to these motion pictures, and has appointed a new servicing agent for these motion pictures with the result that the Company no longer controls the licensing of these motion pictures. Failure to repay or refinance the Arrowhead Loan could result in a material disposition of assets through the loss of the Company's rights to the twelve motion pictures and related loss of revenues in amounts that are difficult to predict.

As a result of the foregoing, the Company has removed all assets accounts relating to the twelve motion pictures pledged to Arrowhead and has removed the corresponding limited recourse indebtedness from the Company's consolidated balance sheet at fiscal year ended June 30, 2009, due to the fact that the loan was a limited recourse loan and the Company had no further obligations to Arrowhead beyond the pledged film assets.

Arrowhead filed an action on September 22, 2010 which seeks recovery from the Company of the monies which the Company has retained under its interpretation of the relevant agreements with Arrowhead. In addition, Arrowhead makes substantial additional claims against the Company, Mr. Hoffman and SAP Inc. regarding claimed breaches of the terms of the operative agreements, including failure to properly account, failure to turn over materials, failure to remit monies collected, and similar matters. The claims against the Company for these breaches of warranties for damages are \$8,300,000 although Arrowhead states no basis for this amount.

The Company had moved to dismiss the action against all defendants other than Seven Arts Future Flows I LLC, which is not part of the Company. On August 9, 2011, the New York Supreme Court granted the Company's motion and dismissed all defendants except Seven Arts Filmed Entertainment Limited in its capacity as a collateral agent, which is not a material element of Arrowhead claim. The Company continues to believe that Arrowhead's claims against the Company are without substantial merit.

Arrowhead has purported to refile its claims against the Company and the other defendants. The Company will seek dismissal of these claims on the same grounds. The Company continues to believe that Arrowhead's claims against the Company are without substantial merit.

#### Arrowhead Capital Partners – AGC Loan

The Company's predecessor and several affiliates were named as defendants in an action by Arrowhead Capital Partners Ltd filed in the Supreme Court of New York County of New York State purportedly served on May 24, 2010, seeking to collect \$1,000,000 plus interest (the "ACG Loan") due to Arrowhead Consulting Group LLC ("ACG") as well as foreclosure on the collateral granted as part of the Cheyne Loan described above in Note 13 under "Production Loans". The ACG Loan is fully subordinated to repayment of the Cheyne Loan, which has not been repaid, and a subsidiary of the Company has been assigned all Cheyne's rights under the subordination provision of the Cheyne Loan. As a result Management does not believe that ACG has the right to maintain this action to collect any monies or to foreclose on any collateral pursuant to the Cheyne Loan. The Company intends to vigorously defend against this action and has filed a motion for summary judgement to dismiss this action.

#### Investigation into Claim for Tax Credits (SAPLA)

The US Attorney in New Orleans is investigating claims for Louisiana film infrastructure tax credits including such tax credits to be claimed by an affiliate of the Company, Seven Arts Pictures Louisiana LLC and has issued subpoenas for discovery of documents in the possession of the Company related to their tax credits. This investigation appears to include investigation as to whether certain expenses claimed by this affiliate were improper or fraudulent. All such claimed expenses were audited by independent auditors in Louisiana and reviewed by counsel. None of these



expenses or credits have been included in the Company's financial statements for any period. Management believes that this investigation will have no material adverse effect on the Company's operations or the total tax credits to be received by the Company's affiliates, but could result in charges against current or former employees of this affiliate based on prior audits, including Mr. Hoffman.

#### Parallel Action

On June 28, 2011, Seven Arts Pictures Plc. ("PLC") filed an action in the High Court of England against Parallel Media LLC ("Parallel") to collect sums due to PLC with respect to acquisition of distribution rights in Russia to four motion pictures and to confirm Parallel's obligations under both a signed and unsigned investment agreement with respect to the motion picture project Winter Queen. On the same day Parallel filed a petition to wind up and liquidate PLC in the Companies Courts of England based on its claim of repayment of \$1,000,000 of investment made by Parallel in Winter Queen. PLC is no longer part of the Company. On September 19, 2011, Parallel filed a new action against PLC and SAE in the Superior Court of California, asserting the same claims as in the winding up petition and seeking to enjoin the proposed administration proceedings in England. A request for a preliminary injunction was denied by the Superior Court.

## HMRC Investigation

On July 19, 2011 Officers of Her Majesty's Revenue & Customs ("HMRC") attended the offices of Seven Arts Pictures Plc. (the "Company") in London. Documents were retained appertaining to arrangements involving the subscription for shares in a number of companies which had lost value, resulting in subscribers making claims to tax relief.

The Company's participation in these transactions was limited to the Company's predecessor's transfer of rights to certain motion pictures to the investors in return for their investments in the production and release costs of those pictures and making available the provision of loans to fund a portion of those investments. The Company received no tax benefits from the transactions, which were made on arms-length terms. The Company believes that it is not a subject of the HMRC investigation.

In connection with the transactions, the Company did not make any representations or warranties to any party, including the investors, regarding any potential tax benefits related to the transactions. Prior to the closing of the transactions the investors obtained and made available to the Company, an opinion of prominent Queen's counsel, specializing in United Kingdom tax laws, that the transactions were permitted and acceptable under the terms of the applicable United Kingdom revenue laws. The Company remains confident that the transactions were permitted and acceptable under the terms of the applicable United Kingdom revenue laws.

HMRC has requested interviews with three officers of the Company to discuss whether those officers were involved in the arrangements for subscription of shares in the relevant companies, the first of which is scheduled for March 6, 2012. The Company is fully cooperating with the investigation. The Company believes there is no basis for any claim of responsibility of any of its officers or employees. Based on facts currently known by the Company, there is no need for it to record a contingent liability in its financial statements in connection with the investigation or the related transactions.

## ITEM 3: QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not applicable to Smaller Reporting Companies

## ITEM 4T: CONTROLS AND PROCEDURES

### Evaluation of Disclosure Controls and Procedures

We carried out an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of December 31, 2011. This evaluation was accomplished under the supervision and with the participation of our chief executive officer /principal executive officer, and chief financial officer/principal financial officer who concluded that our disclosure controls and procedures are not effective.

Based upon an evaluation conducted for the period ended March 31, 2012, our Chief Executive and Chief Financial Officer as of March 31, 2011 and as of the date of this Report, has concluded that as of the end of the periods covered by this report, we have identified the following material weakness of our internal controls:

Lack of sufficient accounting staff which results in a lack of segregation of duties necessary for a good system of internal control and financial statement presentation.

### Changes in Internal Controls over Financial Reporting

We have not yet made any changes in our internal controls over financial reporting that occurred during the period covered by this report on Form 10-Q that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II

Items No. 1, 3, 4, 5 - Not Applicable.

ITEM 6 - EXHIBITS AND REPORTS ON FORM 8-K

(a) During the three months ended March 31, 2012 and subsequent to December 30, 2011, the Company filed Form 8-Ks:

On January 18 2012

On March 16 2012

An S-8 was filed on February 1 2012

A 14A was filed on February 24 2012 (revised on March 14 2012)

(b) Exhibits

Exhibit Number

31.1	Certification of Chief Executive Officer, pursuant to Rule 13a-14(a) of the Exchange Act, as enacted by Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer, pursuant to Rule 13a-14(a) of the Exchange Act, as enacted by Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer and Chief Financial Officer, pursuant to 18 United States Code Section 1350, as enacted by Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURES

In accordance with the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized.

SEVEN ARTS PICTURES, INC.

Date: May 21, 2012

By: /s/ Peter Hoffman  
Peter Hoffman, CEO