

BIOLARGO, INC.  
Form 10-Q  
May 17, 2010  
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

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FORM 10-Q

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

For the quarterly period ended March 31, 2010.

or

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
Commission File Number 000-19709

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

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Delaware  
(State or other jurisdiction of  
incorporation or organization)

65-0159115  
(I.R.S. Employer  
Identification No.)

16333 Phoebe Avenue  
La Mirada, California 90638  
(Address, including zip code, of principal executive offices)

(949) 643-9540  
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Exchange Act: None  
Securities registered pursuant to Section 12(g) of the Exchange Act: Common Stock, \$0.0067 par  
value.

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer. See definition of “accelerated filer and large accelerated filer” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated  
filer  Smaller reporting company

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

The number of shares of the Registrant’s Common Stock outstanding as of May 14, 2010 was 43,510,642 shares.

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## PART I – FINANCIAL INFORMATION

## Item 1. Financial Statements

BIOLARGO, INC. AND SUBSIDIARIES  
CONSOLIDATED BALANCE SHEETS  
AS OF DECEMBER 31, 2009 AND MARCH 31, 2010

	December 31, 2009	March 31, 2010 (unaudited)
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash and cash equivalents	\$ 135,350	\$ 109,629
Accounts receivable	14,607	7,007
Inventory	9,678	7,002
Prepaid expenses	4,586	38,815
<b>Total current assets</b>	<b>164,221</b>	<b>162,453</b>
<b>FIXED ASSETS</b>		
Equipment, net	16,390	13,999
<b>Total fixed assets</b>	<b>16,390</b>	<b>13,999</b>
<b>TOTAL ASSETS</b>	<b>\$ 180,611</b>	<b>\$ 176,452</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>CURRENT LIABILITIES</b>		
Accounts payable and accrued expenses	\$ 1,273,028	\$ 1,593,037
Accrued option compensation expense	679,210	1,105,319
Convertible notes payable, current portion	1,913,625	1,913,625
Discount on convertible notes, current portion net of amortization	(470,822 )	(378,830 )
Note payable	70,000	
Deferred revenue	—	100,000
<b>Total Current Liabilities</b>	<b>3,465,041</b>	<b>4,383,151</b>
<b>LONG-TERM LIABILITIES</b>		
Convertible notes payable, net of current portion	1,372,410	1,601,410
Discount on convertible notes, net of current portion and amortization	(793,523 )	(824,890 )

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Total Long-term Liabilities	578,887	776,520
<b>TOTAL LIABILITIES</b>	<b>4,043,928</b>	<b>5,159,671</b>
<b>COMMITMENTS, CONTINGENCIES AND SUBSEQUENT EVENTS</b>		
<b>STOCKHOLDERS' EQUITY</b>		
Convertible Preferred Series A, \$.00067 Par Value, 50,000,000 and 25,000,000 Shares Authorized, -0- Shares Issued and Outstanding, at March 31, 2010 and December 31, 2009.	—	—
Common Stock, \$.00067 Par Value, 200,000,000 Shares Authorized, 43,510,642 and 43,196,355 Shares Issued, at March 31, 2010 and December 31, 2009, respectively	28,969	29,180
Additional Paid-In Capital	53,876,278	54,769,918
Accumulated Deficit	(57,768,564 )	(59,782,317 )
<b>Total Stockholders' Equity (Deficit)</b>	<b>(3,863,317 )</b>	<b>(4,983,219 )</b>
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<b>\$ 180,611</b>	<b>\$ 176,452</b>

See accompanying notes to unaudited consolidated financial statements

BIOLARGO, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF OPERATIONS  
FOR THE THREE-MONTH PERIODS ENDED MARCH 31, 2009 AND 2010  
(unaudited)

	For the three-month periods ended March 31,	
	2009	2010
Revenue	\$ —	\$ 10,733
Cost of goods sold	—	8,539
Gross Profit	—	2,194
Costs and expenses		
Selling, general and administrative	991,790	1,588,487
Amortization and depreciation	279,192	2,391
Research and development	36,929	43,145
Total costs and expenses	1,307,911	1,634,023
Loss from operations	(1,307,911 )	(1,631,829 )
Other income and (expense)		
Interest expense	(403,526 )	(381,924 )
Other income	3,021	—
Net other income and (expense)	(400,505 )	(381,924 )
Net loss	\$ (1,708,416 )	\$ (2,013,753 )
Loss per common share — basic and diluted		
Loss per share	\$ (0.04 )	\$ (0.05 )
Weighted average common share equivalents outstanding	42,325,788	43,503,658

See accompanying notes to unaudited consolidated financial statements

BIOLARGO, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY (DEFICIT)  
FOR THE THREE-MONTH PERIOD ENDED MARCH 31, 2010 (UNAUDITED)

	Common Stock Number of Shares	Par Value \$.00067	Additional Paid-In Capital	Retained Earnings (Deficit)	Total
BALANCE DECEMBER 31, 2009	43,196,355	\$28,969	\$53,876,278	\$(57,768,564)	(3,863,317)
Issuance of warrants as part of convertible note offering	—	—	229,000	—	229,000
Issuance of a warrant to a consultant	—	—	25,000	—	25,000
Issuance of stock options to Board of Directors	—	—	344,500	—	344,500
Issuance of stock options to consultants	—	—	115,000	—	115,000
Issuance of stock for services to board of directors	114,287	77	79,923	—	80,000
Issuance of stock for services	200,000	134	100,217	—	100,351
Net loss for the three-month period ended March 31, 2010	—	—	—	(2,013,753 )	(2,013,753)
BALANCE MARCH 31, 2010	43,510,642	\$29,180	\$54,769,918	\$(59,782,317)	\$(4,983,219)

See accompanying notes to unaudited consolidated financial statements

BIOLARGO, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
FOR THREE-MONTH PERIODS ENDED MARCH 31, 2009 AND 2010  
(unaudited)

	For the three-month periods ended March 31,	
	2009	2010
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net Loss	\$ (1,708,416 )	\$ (2,013,753 )
Adjustments to Reconcile Net Loss to Net Cash Used in Operating Activities:		
Non-cash accrued option compensation expense	329,909	426,109
Non-cash expense related to options issued to officers and board of directors	—	344,500
Non-cash interest expense related to the amortization of the fair value of warrants issued in conjunction with our convertible notes	353,891	289,625
Non-cash expense related to options issued to consultants	201,000	115,000
Non-cash expense related to stock issued to consultants and professionals for settlement of obligations	28,383	100,351
Non-cash expense related to stock issued to our board of directors for settlement of obligations	—	20,000
Increase in accounts payable and accrued expenses	249,570	405,009
Increase in deferred revenue	—	100,000
Decrease in accounts receivable	—	7,600
Amortization and depreciation expense	279,192	2,391
Decrease in inventory	—	2,676
Increase in prepaid expenses	(7,096 )	(34,229 )
<b>Net Cash Used In Operating Activities</b>	<b>(273,567 )</b>	<b>(234,721 )</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Proceeds from convertible notes	400,000	229,000
Payments on note payable	—	(20,000 )
<b>Net Cash Provided By Financing Activities</b>	<b>400,000</b>	<b>209,000</b>
<b>NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS</b>	<b>126,433</b>	<b>(25,721 )</b>
<b>CASH AND CASH EQUIVALENTS — BEGINNING</b>	<b>90,384</b>	<b>135,350</b>
<b>CASH AND CASH EQUIVALENTS — ENDING</b>	<b>\$ 216,817</b>	<b>\$ 109,629</b>
<b>SUPPLEMENTAL DISCLOSURES OF CASHFLOW INFORMATION</b>		
Cash Paid During the Period for:		
Interest	\$ —	\$ —
Taxes	\$ 1,600	\$ 2,371



Conversion of accrued expenses to shares of the Company's common stock:

Board of Directors and officer obligations incurred in 2009	\$ —	\$ 60,000
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Conversion of accrued expenses to an option to purchase shares of the Company's common stock:

Board of Directors and officer obligations incurred in 2009	\$10,000	\$—
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**SUPPLEMENTAL DISCLOSURES OF NON-CASH FINANCING AND**

**INVESTING ACTIVITIES:**

Fair value of the issuance of warrants in conjunction with convertible note offerings	\$400,000	\$229,000
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Repriced warrants in conjunction with convertible note offering	\$52,967	\$—
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See accompanying notes to unaudited consolidated financial statements

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

Note 1. Business and Organization

Outlook

The financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities and commitments in the normal course of our business. As reflected in the accompanying financial statements, we had a net loss of \$2,013,753 for the three-month period ended March 31, 2010, and an accumulated stockholders' deficit of \$59,782,317 as of March 31, 2010. The foregoing factors raise substantial doubt about our ability to continue as a going concern. Ultimately, our ability to continue as a going concern is dependent upon our ability to attract significant new sources of capital, attain a reasonable threshold of operating efficiencies and achieve profitable operations by licensing or otherwise commercializing products incorporating our BioLargo technology. The financial statements do not include any adjustments that might be necessary if we are unable to continue as a going concern.

We have been, and anticipate that we will continue to be, limited in terms of our capital resources. Our total cash and cash equivalents was \$109,629 at March 31, 2010. We generated revenues of \$10,733 in the three-month period ended March 31, 2010, which amount was not sufficient to fund our operations, and we incurred negative cash flow from operating activities of \$234,721 for the three-month period ended March 31, 2010. We had negative working capital of \$4,220,698 for the three-month period ended March 31, 2010. Our accounts payable and accrued expenses increased by \$320,009 during three-month period ended March 31, 2010 and were \$1,593,017 at March 31, 2010. We do not have enough cash or source of capital to pay our accounts payable and expenses as they arise, and have relied on the issuance of stock options and common stock, as well as extended payment terms with our vendors, to continue to operate. Additionally, our officers are continuing to finance operations by delaying the receipt of their salary and by incurring expenses which have not been reimbursed.

As of March 31, 2010 we had \$3,565,035 aggregate principal amount, together with \$404,428 accrued and unpaid interest, outstanding on various promissory notes. We may pay all of these amounts in cash or in stock, at our option, at maturity. In addition, as of March 31, 2010, we had \$1,038,609 in accrued and unpaid payables (see Note 11) and \$150,000 in accrued and unpaid interest to New Millennium Capital Partners, LLC, an entity controlled by Dennis P. Calvert, our President and Chief Executive Officer. (See Note 14.)

On January 15, 2010 we commenced a private offering of our convertible promissory notes, and through March 31, 2010, we sold \$229,000 principal amount of convertible notes and issued warrants to purchase up to an aggregate 398,266 shares of our common stock. (See Notes 4 and 15.)

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

The unaudited consolidated financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and pursuant to Rule 8-03 of Regulation S-X under the Securities Act of 1933, as amended. Accordingly, they do not include all of the

information and notes required by generally accepted accounting principles for annual financial statements. In the opinion of management, all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair presentation have been included. We have less than a year of historical operating revenues, and therefore our operating results for the three-month period ended March 31, 2010 are not necessarily indicative of the results that may be expected for the year ended December 31, 2010, or for any other period. These unaudited consolidated financial statements and notes should be read in conjunction with the Company's audited financial statements and accompanying notes included in the Annual Report on Form 10-K for the year ended December 31, 2009 filed with the Securities and Exchange Commission (the "SEC").

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

Organization

We were initially organized under the laws of the State of Florida in 1989 as Repossession Auction, Inc. In 1991, we merged into a Delaware corporation bearing the same name. In 1994, we changed our name to Latin American Casinos, Inc. to reflect our new focus on the gaming and casino business in South and Central America, and in 2001 we changed our name to NuWay Energy, Inc. to reflect our new emphasis on the oil and gas development industry. During October 2002, we changed our name to NuWay Medical, Inc. coincident with the divestiture of our non-medical assets and the retention of new management. In March 2007, in connection with the approval by our stockholders of the acquisition of the BioLargo technology, we changed our name to BioLargo, Inc.

Business Overview

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

In addition to our BioLargo technology, in 2008 we acquired the rights to market an iodine based water disinfection system (the “Isan system”) from Ioteq IP Pty. Ltd., an Australian company, and its U.S. affiliate Ioteq Inc., and recently licensed the rights to commercialize the Isan system from Ioteq. The Isan system is an automated water disinfection system that substantially reduces the incidence of fungal growth, spoilage, organisms and pathogens in water and on food. On March 29, 2010, we licensed the rights to commercialize the Isan system from Ioteq, and sublicensed those rights to a third party, in particular fields of use. (See Note 4.)

Both our BioLargo technology and the Isan system have potential commercial applications within global industries, including but not limited to agriculture, animal health, beach and soil environmental remediation, consumer products, food processing, medical, and water industries. While we believe the potential applications are many, we are currently focused in two primary areas – the development of certain products designed for the animal health industry, and agriculture.

First, in 2009, we launched our first products incorporating our BioLargo technology under the brand name “Odor-No-More”, in the animal health industry. The primary benefits of the products are odor and moisture control, and customers using our animal bedding additive experience a net savings on total bedding costs. We have focused our efforts on building wholesale distribution, and in 2010, we intend to expand our marketing efforts into new industries, as well as continue evaluating new product opportunities within the same industry.

Second, we are actively seeking to secure strategic partners to either license or partner with to exploit commercial opportunities for CupriDyne™ and for the Isan system. In March 2010, we entered into a series of transactions whereby we licensed the Isan system technology from Ioteq, and then sublicensed the technology to a third party for commercialization in the United States in certain fields of use. We are still actively marketing the Isan system for opportunities outside the United States pursuant to our marketing agreement with Ioteq, and in the United States through an agency agreement with Isan USA. We continue research and product development for our CupriDyne™ technology, and continue to work with a number of global companies who are engaged in technology evaluation and testing processes. Simultaneously, we are also actively seeking to identify and negotiate regional or global partnerships to exploit commercial opportunities for both CupriDyne™ and the Isan technologies. No such regional or

global partnerships have been formed at this time, and we can make no representation about our ability to successfully conclude such arrangements.

Although we are focused primarily on odor control products and agriculture, we also intend to continue to advance our intellectual property, product designs and licensing opportunities for our technology for use in other industries, as capital resources are available to support these efforts. We continue to market both our BioLargo technology and the Isan system to various companies for licensure in numerous industry segments.

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**BIOLARGO, INC. AND SUBSIDIARIES**  
**NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS**

Note 2. Summary of Significant Accounting Policies

Principles of Consolidation

As of March 31, 2010, we had two subsidiaries, BioLargo Life Technologies, Inc. (“BLTI”) and Odor-No-More, Inc. (“ONM”). The consolidated balance sheets include the accounts of BioLargo, Inc. and BLTI and ONM. All significant inter-company balances have been eliminated in consolidation.

Cash and Cash Equivalents

We consider all highly liquid investments with original maturities of three months or less or money market funds from substantial financial institutions to be cash equivalents. We place substantially all of our cash and cash equivalents in interest bearing demand deposit accounts with one financial institution.

Accounts Receivable

Trade accounts receivable are recorded net of allowances for doubtful accounts. Estimates for allowances for doubtful accounts are determined based on payment history and individual customer circumstances. The allowance for doubtful accounts was zero at March 31, 2010.

We consider all other accounts receivable to be fully collectible.

Inventory

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

	December 31, 2009	March 31, 2010
Raw Materials	\$ 4,241	\$ 6,221
Finished Goods	5,437	781
<b>Total</b>	<b>\$ 9,678</b>	<b>\$ 7,002</b>

Equipment

Equipment is carried at cost and depreciated using the straight-line method over the estimated useful lives of the assets, which is three years. Equipment is stated on the balance sheet net of accumulated depreciation of \$14,690 as of March 31, 2010. Depreciation expense for the three-month periods ended March 31, 2009 and 2010 was \$2,391 and \$2,391, respectively.

Earnings (Loss) Per Share

We report basic and diluted earnings (loss) per share (“EPS”) for common and common share equivalents. Basic EPS is computed by dividing reported earnings by the weighted average shares outstanding. Diluted EPS is computed by adding to the weighted average shares the dilutive effect if stock options and warrants were exercised into common stock. For the three-month periods ended March 31, 2009 and 2010, the denominator in the diluted EPS computation

is the same as the denominator for basic EPS due to the anti-dilutive effect of the warrants and stock options on the Company's net loss.

#### Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and revenues and expenses during the period reported. Actual results could differ from those estimates. Estimates are used when accounting for stock-based transactions, uncollectible accounts receivable, asset depreciation and amortization, and taxes, among others.

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

Stock Options and Warrants issued for Services

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

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

Non-Cash Transactions

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

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

Revenue Recognition

We recognize revenues based upon contract terms and completion of the sales process in accordance the SEC codification of revenue recognition.

We also generate revenues from royalties and license fees from our intellectual property. Licensees typically pay a license fee in one or more installments and ongoing royalties based on their sales of products incorporating or using our licensed intellectual property. License fees are recognized over the estimated period of future benefit to the average licensee.

Recent Accounting Pronouncements

Only July 1, 2009, the Financial Accounting Standards Board (FASB) launched the FASB Accounting Standards Codification as the single source of authoritative nongovernmental U.S. generally accepted accounting principles (GAAP). The Codification is effective for interim and annual periods ending after September 15, 2009. All existing accounting standards documents are superseded as described in FASB Statement No. 168, The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles. All other accounting literature not included in the Codification is nonauthoritative.

Other recent accounting updates issued by FASB and the SEC did not or are not believed by management to have a material impact on the Company's present or future consolidated financial statements.

Note 3. Intangible Assets/Long-lived Assets and Impairment

Amortization expense for the intangible assets for the three-month periods ended March 31, 2009 and 2010 was \$276,801 and \$0.



Management performed its assessment of the fair value of the intangible assets for the year ended December 31, 2009. In our undertaking we analyzed the projected cash flow from the assets discounted at appropriate rates, the length of time to full development of the cash flow potential and the current recessionary state of the world-wide economy. We determined after this analysis that it was appropriate for us to record an impairment charge of \$8,781,133 consisting of \$8,610,940, which was the remaining net book value of our licensing rights acquired from IOWC Technologies, Inc., in March 2007, and \$170,193, which was the remaining net book value of certain agreements assigned to us as part of the acquisition of the BioLargo technology from IOWC Technologies, Inc., in March 2007. The impairment charge reduced the net book value of the asset to zero.

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

Note 4. Deferred Revenue

Sublicense to Isan USA

On March 29, 2010, BioLargo and Isan USA, Inc. (“Isan USA”) entered into a sublicense agreement (the “Isan USA Sublicense”) which grants Isan USA the exclusive rights to use, exploit, develop and commercialize the Isan System Technology in the United States, in particular fields of use.

Pursuant to the Isan USA Sublicense, Isan USA paid to BioLargo a \$100,000 initial license fee, of which the full amount is recorded as deferred revenue as of March 31, 2010.

Note 5. Private Security Offerings

Spring 2010 Offering

Pursuant to a private offering that commenced January 2010 (the “Spring 2010 Offering”) and continued through March 31, 2010, we sold \$229,000 of our 10% convertible notes (the “Spring 2010 Notes”), which are due and payable on April 15, 2013, to ten investors, convertible into an aggregate 398,266 shares of our common stock. The Spring 2010 Notes are convertible into shares of our common stock at an initial conversion price of \$0.575 per share. The Spring 2010 Notes can be converted voluntarily by the noteholders at any time prior to the maturity date. We can unilaterally convert the Spring 2010 Notes (i) on or after July 31, 2010, if we have received one or more written firm commitments, or have closed on one or more transactions, or a combination of the foregoing, of at least \$3 million gross proceeds of equity or debt; or (ii) on the maturity date. Accordingly, the Spring 2010 Notes may be repaid in cash or may be converted, at our sole option, into shares of our common stock, on or before the April 15, 2013 maturity date.

Each purchaser of the Spring 2010 Notes received, for no additional consideration, two stock purchase warrants, each of which entitle the holder to purchase the number of shares of our common stock into which the holder’s Spring 2010 Note is initially convertible. The first warrant (the “Spring 2010 Eighteen Month Warrant”) is exercisable at a price of \$0.75 per share and expires on July 15, 2011. The second warrant (the “Spring 2010 Thirty-Six Month Warrant”) is exercisable at a price of \$1.00 per share and expires on January 15, 2013. (See Note 8.)

Spring 2009 Offering

Pursuant to a private offering that commenced April 2009 (the “Spring 2009 Offering”) and terminated November 2009, we sold \$681,410 of our 10% convertible notes (the “Spring 2009 Notes”), which are due and payable on June 1, 2012, to 23 investors, convertible into an aggregate 1,238,935 shares of our common stock. The Spring 2009 Notes are convertible into shares of our common stock at an initial conversion price of \$0.55 per share. The Spring 2009 Notes can be converted voluntarily by the noteholders at any time prior to the maturity date. We can unilaterally convert the Spring 2009 Notes (i) on or after December 15, 2009, if we have received one or more written firm commitments, or have closed on one or more transactions, or a combination of the foregoing, of at least \$3 million gross proceeds of equity or debt; or (ii) on the maturity date. Accordingly, the Spring 2009 Notes may be repaid in cash or may be converted, at our sole option, into shares of our common stock, on or before the June 1, 2012 maturity date.

Each purchaser of the Spring 2009 Notes received, for no additional consideration, two stock purchase warrants, each of which entitle the holder to purchase the number of shares of our common stock into which the holder’s Spring 2009

Note is initially convertible. The first warrant (the "Spring 2009 One-Year Warrant") is exercisable at a price of \$0.75 per share and expires on June 1, 2010. The second warrant (the "Spring 2009 Three-Year Warrant") is exercisable at a price of \$1.00 per share and expires on June 1, 2012. (See Note 8.)

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

Fall 2008 Offering

Pursuant to a private offering that commenced October 2008 (the “Fall 2008 Offering”) and terminated March 2009, we sold \$723,000 of our 10% convertible notes (the “Fall 2008 Notes”), which are due and payable October 15, 2011, to 18 investors, convertible into an aggregate 1,446,000 shares of our common stock. As originally offered, the Fall 2008 Notes were convertible into shares of our common stock at an initial conversion price of \$1.00 per share. The Fall 2008 Notes can be converted voluntarily by the noteholders at any time prior to the maturity date. We can unilaterally convert the Fall 2008 Notes (i) on or after April 30, 2009, if we have received one or more written firm commitments, or have closed on one or more transactions, or a combination of the foregoing, of at least \$3 million gross proceeds of equity or debt; or (ii) on the maturity date. Accordingly, the Fall 2008 Notes may be repaid in cash or may be converted, at the noteholders’ option or our option, into shares of our common stock, on or before the October 15, 2011 maturity date.

Each purchaser of the Fall 2008 Notes received, for no additional consideration, two stock purchase warrants (a one-year warrant and a three-year warrant), each of which entitled the holder to purchase the number of shares of our common stock into which the holder’s Fall 2008 Note is initially convertible. As originally offered, the first warrant (the “Fall 2008 One-Year Warrant”) was exercisable at \$1.00 per share and was due to expire on October 15, 2009. The second warrant (the “Fall 2008 Three-Year Warrant” and together with the One-Year Warrant, the “Fall 2008 Warrants”) was exercisable at \$2.00 per share and was due to expire on October 15, 2011. (See Note 8.)

On January 16, 2009, our Board of Directors amended the terms of the Offering as follows: (i) the initial conversion price of the Fall 2008 Notes was reduced from \$1.00 per share to \$0.50 per share; (ii) the exercise price of the Fall 2008 One-Year Warrant was reduced from \$1.00 per share to \$0.75 per share; (iii) the exercise price of the Fall 2008 Three-Year Warrant was reduced from \$2.00 per share to \$1.00 per share; and the number of shares of our common stock for which the Fall 2008 One-Year Warrants and the Fall 2008 Three-Year Warrants may be exercised is being increased from one share per dollar invested to two shares for each dollar invested. The Fall 2008 One-Year Warrants expired unexercised on October 15, 2009.

Spring 2008 Offering

Pursuant to a private offering that commenced March 2008 (the “Spring 2008 Offering”) and terminated August 2008, we sold \$913,625 of our 10% convertible notes (the “Spring 2008 Notes”), which are due and payable on March 31, 2010, to 30 investors, convertible into an aggregate 676,775 shares of our common stock. The Spring 2008 Notes are convertible into shares of our common stock at an initial conversion price of \$1.35 per share. The Spring 2008 Notes can be converted voluntarily by the noteholders at any time prior to the maturity date. We can unilaterally convert the Spring 2008 Notes (i) on or after September 30, 2008, if we have received one or more written firm commitments, or have closed on one or more transactions, or a combination of the foregoing, of at least \$3 million gross proceeds of equity or debt; or (ii) on the maturity date. Accordingly, the Spring 2008 Notes may be repaid in cash or may be converted, at our sole option, into shares of our common stock, on or before the maturity date.

Each purchaser of the Spring 2008 Notes received, for no additional consideration, two stock purchase warrants (a one-year warrant and a three-year warrant), each of which entitled the holder to purchase the number of shares of our common stock into which the holder’s Spring 2008 Note is initially convertible. The “Spring 2008 One-Year Warrants” expire on March 31, 2009 and were exercisable at \$0.50 (originally \$1.50) per share. The “Spring 2008 Three-Year Warrants” are exercisable at an initial exercise price of \$2.00 per share and expire on March 31, 2011. On September 19, 2008, our Board of Directors reduced the exercise price of the Spring 2008 One-Year Warrants from

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\$1.50 per share (the original exercise price pursuant to the terms of the Spring 2008 Offering) to \$1.00 per share. On January 16, 2009, our Board of Directors reduced the exercise price of the Spring 2008 One-Year Warrants from \$1.00 per share to \$0.50 per share. The Spring 2008 One-Year Warrants expired unexercised on March 31, 2009.

On March 30, 2010, our board accepted proposals from the holders of the Spring 2008 Notes to extend the maturity date of the notes by one year, such that the Spring 2008 Notes mature on March 31, 2011. (See Note 15.)

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

2007 Offering

Pursuant to a private offering that commenced May 2007 (the “2007 Offering”) and terminated December 2007, we sold \$1,000,000 of our convertible notes (the “2007 Notes”), which were initially due and payable on June 30, 2009 (extended by one year to June 30, 2010, see Note 6) to 21 investors, convertible into an aggregate 1,428,582 shares of our common stock. The 2007 Notes bear interest at a rate of 10% compounding annually, such interest to be paid, at our option, in cash or stock at a conversion rate of \$0.70 per share. The 2007 Notes are convertible into shares of the Company’s common stock at an initial conversion price of \$0.70 per share, and can be converted voluntarily by the noteholders at any time. We can elect to convert the 2007 Notes (i) on or after September 30, 2007, if we have received one or more written firm commitments, or have closed on one or more transactions, or a combination of the foregoing, of at least \$3 million gross proceeds of equity or debt; or (ii) on the maturity date. Accordingly, on the maturity date, we may repay the 2007 Notes in cash or choose to convert the notes, at our sole option, into shares of our common stock.

Each purchaser of the 2007 Notes received, for no additional consideration, a stock purchase warrant (the “2007 Warrants”) entitling the holder to purchase a number of shares of our common stock equal to the number of shares of our common stock into which the principal amount of the investor’s 2007 Note is convertible. The 2007 Warrants are exercisable at \$1.30 per share and expire on June 30, 2010.

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

Note 6. Extension of Maturity Date of 2007 Offering

On June 30, 2009, we and the holders of the 2007 Notes (see Note 5) agreed to extend, by one year, the maturity dates of the 2007 Notes, in an aggregate principal amount of \$1,000,000. The 2007 Notes now mature on June 30, 2010.

Note 7. Issuance of Securities in exchange for payment of payables

Payment of Officer Salaries and Board of Director Fees

On January 4, 2010, we issued an aggregate 114,287 shares of our common stock, at a conversion price of \$0.70, which was the closing price of our common stock on the day of issuance, to two members of our board of directors in lieu of \$80,000 in accrued and unpaid payables for their services as a director. Of this amount \$60,000 related to payables accrued and unpaid as of December 31, 2009. On February 1, 2010, we issued an aggregate 200,000 shares of our common stock, at a conversion price of \$0.50, which was the closing price of our common stock on the day of issuance, to a consultant for services provided. We recorded \$100,351 in consulting expense for the three-month period March 31, 2010 related to that issuance.

Note 8. Warrants

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

Number of	Price
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	Shares		Range
Outstanding as of December 31, 2009	9,766,456	\$	0.125 – 2.00
Issued	846,532	\$	0.75 – 1.00
Exercised	—	\$	—
Expired	—	\$	—
Outstanding as of March 31, 2010	10,612,988	\$	0.125 – 2.00

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

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

	2009	2010
Risk free interest rate	1.83 – 2.49%	0.45 – 1.47%
Expected volatility	203 – 615%	269 – 470 %
Expected dividend yield	—	—
Forfeiture rate	—	—
Expected life in years	0.50 – 3.00	0.50 – 3.00

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

The aggregate fair value of the warrants issued and outstanding as of March 31, 2010 totaled \$4,665,724. Of this total, \$77,500 was related to warrants issued to a consultant of which \$35,000 was expensed during the three-month period ended March 31, 2010 and \$52,500 was expensed during the three-month period March 31, 2009. The remaining fair value of \$4,588,224 was issued in conjunction with our convertible notes and is recorded on our balance sheet as discount on convertible notes net of amortization of \$3,384,504. We recorded \$353,891 and \$289,625 of interest expense related to the amortization of the discount on convertible notes for the three-month periods ended March 31, 2009 and 2010, respectively.

#### Spring 2010 Warrants

From the inception of our Spring 2010 Offering on January 15, 2010, through March 31, 2010, we issued warrants to purchase up to an aggregate 796,532 shares of our common stock to purchasers of our Spring 2010 Notes, consisting of Spring 2010 Eighteen Month Warrants to purchase up to an aggregate 398,266 shares which expire July 15, 2011, at an exercise price of \$0.75 per share, and Spring 2010 Thirty-Six Month Warrants to purchase up to an aggregate 398,266 shares which expire January 15, 2013, at an exercise price of \$1.00 per share. (See Note 5.)

#### Spring 2009 Warrants

From April 2009 through November 2009, we issued warrants to purchase up to an aggregate 2,477,870 shares of our common stock to purchasers of our Spring 2009 Notes, consisting of Spring 2009 One-Year Warrants to purchase up to an aggregate 1,238,935 shares which expire June 1, 2010, at an exercise price of \$0.75 per share, and Spring 2009 Three-Year Warrants to purchase up to an aggregate 1,238,935 shares which expire June 1, 2012, at an exercise price of \$1.00 per share.

#### Fall 2008 Warrants

From January 2009 through June 2009, we issued warrants to purchase up to an aggregate 2,652,000 shares of our common stock to purchasers of our Fall 2008 Notes, consisting of Fall 2008 One-Year Warrants to purchase an aggregate 1,326,000 shares which expire October 15, 2009, at an exercise price of \$0.75 per share (initially issued at



\$1.00 per share), and Fall 2008 Three-Year Warrants to purchase up to an aggregate 1,326,000 shares which expire October 15, 2011, at an exercise price of \$1.00 per share (initially issued at \$2.00 per share).

On January 16, 2009, the exercise price of the Fall 2008 One-Year Warrants was reduced from \$1.00 to \$0.75, and the exercise price of the Fall 2008 Three-Year Warrants was reduced from \$2.00 to \$1.00, resulting in additional fair value totaling \$52,967, which was recorded as interest expense.

From October 2008 through December 2008, we issued warrants to purchase up to an aggregate 240,000 shares of our common stock to purchasers of our Fall 2008 Notes, consisting of Fall 2008 One-Year Warrants to purchase an aggregate 120,000 shares which expire October 15, 2009, at an exercise price of \$0.75 per share (initially issued at \$1.00 per share), and Fall 2008 Three-Year Warrants to purchase up to an aggregate 120,000 shares which expire October 15, 2011, at an exercise price of \$1.00 per share (initially issued at \$2.00 per share).

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

Other Warrants

On February 5, 2010 we issued a warrant to a consultant for services provided to purchase up to an aggregate 50,000 shares of our common stock at an exercise price of \$0.50 per share.

Note 9. Stockholders' Equity

Preferred Stock

Our certificate of incorporation authorizes our Board of Directors to issue preferred stock, from time to time, on such terms and conditions as they shall determine. As of March 31, 2010 and December 31, 2009 there were no outstanding shares of our preferred stock.

Common Stock

As of December 31, 2009 and March 31, 2010 there were 43,196,355 and 43,510,642 shares of common stock outstanding, respectively. The increase in shares during the three-month period ended March 31, 2010 is comprised of the following stock issuances: (i) 200,000 shares of our common stock to a consultant for services provided, and (ii) 114,287 shares of our common stock to two directors in exchange for their services as a director.

Note 10. Stock-Based Compensation and Other Employee Benefit Plans

2007 Equity Incentive Plan

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

Under this plan, 6,000,000 shares of our common stock are reserved for issuance under awards. Any shares that are represented by awards under the 2007 Plan that are forfeited, expire, or are canceled or settled in cash without delivery of shares, or that are forfeited back to us or reacquired by us after delivery for any reason, or that are tendered to us or withheld to pay the exercise price or related tax withholding obligations in connection with any award under the 2007 Plan, will again be available for awards under the 2007 Plan. Only shares actually issued under the 2007 Plan will reduce the share reserve. If we acquire another entity through a merger or similar transaction and issue replacement awards under the 2007 Plan to employees, officers and directors of the acquired entity, those awards, to the extent permitted under applicable laws and securities exchange rules, will not reduce the number of shares reserved for the 2007 Plan.

The 2007 Plan imposes additional maximum limitations, which limitations will be adjusted to take into account stock splits, reverse stock splits and other similar occurrences. The maximum aggregate fair market value of stock that may be issued in connection with incentive stock options granted to any one person in any calendar year intended to qualify under Internal Revenue Code Section 422 is \$100,000. The maximum number of shares that may be subject to stock options or stock appreciation rights granted to any one person in any calendar year is 200,000 shares, except that

this limit is 400,000 shares if the grant is made in the year of the recipient's initial employment. The maximum number of shares that may be subject to restricted stock or restricted stock units granted to any one person in any calendar year is 200,000 shares.

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**BIOLARGO, INC. AND SUBSIDIARIES**  
**NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS**

The maximum number shares that may be subject to awards granted to any one Participant in any calendar year of (i) performance shares, and/or performance units (the value of which is based on the Fair Market Value of a share of our common stock), is 200,000 shares; and (ii) of performance units (the value of which is not based on the Fair Market Value of a share of our common stock) that could result a payment of more than \$500,000.

During the three-month period ended March 31, 2010, we granted options to purchase an aggregate 30,000 shares of our common stock to our Chief Financial Officer, pursuant to the terms of our engagement agreement with him. These options are exercisable at various exercise prices ranging between \$0.45 and \$0.50 depending upon their respective dates of grant. The fair value of these option issuances was an aggregate \$14,500 and was recorded as selling, general and administrative expense as of March, 31, 2010. Each option is fully vested upon grant and is exercisable for ten years from its respective date of grant.

On February 1, 2010, the Company's Compensation Committee issued options pursuant to the Company's 2007 Equity Incentive Plan to certain employees, outside consultants and professionals who have and continue to provide services to the Company, consistent with management's recommendations to the committee.

In total, options to purchase an aggregate 1,060,000 shares of the Company's common stock were issued, at an exercise price of \$0.575 per share, which price was \$0.075 more than the \$0.50 closing price of the Company's common stock on the date of grant. Of the options issued, 400,000 were issued to third party consultants for their respective roles within the Company and the remaining 660,000 options were issued to the Company's principal executive officer, principal financial officer, and named executive officers, as set forth in the following table:

Name	Position	Number of Shares Underlying Options
Dennis P. Calvert	President and Chief Executive Officer	200,000
Charles K. Dargan II	Chief Financial Officer	60,000
Kenneth R. Code	Chief Technology Officer	200,000
Joseph L. Provenzano	Secretary, VP of Operations	200,000
	Total	660,000

With one exception, the options issued expire ten years from the date of grant (the option issued to Mr. Code expires five years from the date of grant).

During the three-month periods ended March 31, 2009 and 2010 we recorded an aggregate \$439,202 and \$483,667 in option compensation expense related to options issued pursuant to the 2007 Plan.

Activity for our stock options under the 2007 Plan for the three-month period ended March 31, 2010 is as follows:

	Options Outstanding	Shares Available	Price per share	Weighted Average Price per share
Balances, December 31, 2009	1,667,135	4,332,865	\$ 0.28 – \$1.89	\$ 0.75
Granted	910,000	(910,000)	\$ 0.33 – 0.50	\$ 0.53
Exercised	—	—	—	—

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Canceled

Balances, March 31, 2010	2,577,135	3,422,865	\$	0.28	–	\$1.89	\$	0.69
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BIOLARGO, INC. AND SUBSIDIARIES  
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

The following table summarizes the stock options issued under the 2007 Equity Plan outstanding at March 31, 2010.

Options Outstanding at March 31, 2010	Exercise Price	Weighted		Currently Exercisable	
		Average Remaining Contractual Life	Weighted Average Exercise Price	Number of Shares at March 31, 2010	Weighted Average Exercise Price
20,000	\$ 0.40	8	\$ 0.40	20,000	\$ 0.40
	\$ 0.94 –				
605,000	1.03	8	\$ 0.97	105,000	\$ 0.94
50,000	\$ 1.89	9	\$ 1.89	50,000	\$ 1.89
	\$ 0.35 –				
110,000	1.65	4	\$ 1.04	110,000	\$ 1.04
	\$ 0.28 -				
120,000	0.50	10	\$ 0.40	120,000	\$ 0.40
20,000	\$ 0.33	10	\$ 0.33	20,000	\$ 0.33
557,035	\$ 0.50	3	\$ 0.50	557,035	\$ 0.50
155,100	\$ 0.55	3	\$ 0.55	155,100	\$ 0.55
30,000	\$ 0.57	5	\$ 0.57	30,000	\$ 0.57
20,000	\$ 0.33	10	\$ 0.33	20,000	\$ 0.33
	\$ 0.45 –				
30,000	0.50	10	\$ 0.48	30,000	\$ 0.48
200,000	\$ 0.50	5	\$ 0.50	200,000	\$ 0.50
600,000	\$ 0.50	10	\$ 0.50	600,000	\$ 0.50

#### Stock Options Issued Outside the 2007 Equity Incentive Plan

We recognize compensation expense for stock option awards on a straight-line basis over the applicable service period of the award, which is the vesting period. Share-based compensation expense is based on the grant date fair value estimated using the Black-Scholes Option Pricing Model. The following methodology and assumptions were used to calculate share based compensation for the three-month period ended March 31, 2010:

	Non plan Option	2007 Plan
Risk free interest rate	—%	0.45 – 1.47%
Expected volatility	—%	766%
Expected dividend yield	—	—
Forfeiture rate	—	—
Expected life in years	—	5

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

Following the SEC guidance, we use the “shortcut” method to determine the expected term of plain vanilla options issued to employees and Directors. The expected term is presumed to be the mid-point between the vesting date and the end of the contractual term.

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

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

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

## Note 11. Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses included the following:

	December 31, 2009	March 31, 2010
Accounts payable and accrued expenses	\$ 479,034	\$ 719,110
Accrued interest	462,129	554,428
Officer and board of director payable	331,865	319,499
Total Accounts Payable and Accrued Expenses	\$ 1,273,028	\$ 1,593,037

## Accrued Interest

Accrued interest as of December 31, 2008, includes \$380,658 of accrued and unpaid interest related to a note previously held by New Millennium Capital Partners, LLC (“New Millennium”), a related party. On April 27, 2009, New Millennium agreed to accept from the Company an option to purchase common stock as payment of \$230,658 of the outstanding \$380,658 in accrued but unpaid interest. New Millennium further agreed to extend the due date for the remaining \$150,000 accrued and unpaid interest to April 30, 2010. (See Note 14.) The remaining \$404,428 of accrued and unpaid interest relates to outstanding convertible promissory notes issued by the Company pursuant to private securities offerings. (See Note 5.)

During the three-month periods ended March 31, 2009 and 2010, we recorded \$49,635 and \$92,299 of interest expense related to the convertible notes outstanding, respectively.

## Officer and Board of Director payable

Officer and Board of Director payables were reduced as certain board members agreed to accept common stock as payment of an aggregate \$80,000, of which \$60,000 was outstanding as of December 31, 2009, and the balance of \$20,000 related to expenses incurred in the three-month period ended March 31, 2010.

## Note 12. Note Payable

On August 3, 2009, we received \$70,000 and issued a promissory note with a maturity date of October 31, 2009 which accrued interest at a rate of 10%. For the three-month period ended March 31, 2010 we recorded \$4,104 of interest expense. On October 31, 2009 the maturity date of this promissory note was extended to February 1, 2010. The maturity date was further extended to June 1, 2010, and in March 2010 a \$20,000 payment on the note was made.

## Note 13. Related Party Transactions

## New Millennium

On April 13, 2007, New Millennium Capital Partners LLC (“New Millennium”), a limited liability company controlled and owned in part by the Company’s CEO and president, Dennis P. Calvert, converted a promissory note (the “Note”) in principal amount of \$900,000 into 1,636,364 shares of our common stock, at a price of \$0.55 per share, which was the last bid price on the date of conversion. Accrued but unpaid interest in the amount of \$380,658 as of the conversion



date of April 13, 2007 remained outstanding on the Note, which amount was due to be paid on January 15, 2008. We did not make such payment on such date. On November 12, 2008, we and New Millennium agreed to extend the date on which interest would be paid to April 30, 2009. On April 27, 2009, New Millennium agreed to accept as payment of \$230,658 of the outstanding \$380,658 in accrued but unpaid interest an option to purchase 691,974 shares of our common stock, exercisable at \$0.55 cents per share. This option will expire April 24, 2012. New Millennium further agreed to extend the due date for the remaining \$150,000 unpaid interest to April 30, 2010, which date has been further extended to October 31, 2010. (See Notes 7 and 11.)

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

Note 14. Commitments and Contingencies

Litigation

We are not currently a party to any litigation.

Engagement of Charles K. Dargan, II as Chief Financial Officer

On February 1, 2010, we extended the engagement agreement dated February 1, 2008 (the "Engagement Agreement", which had been previously extended by one year by agreement dated February 23, 2009), pursuant to which Mr. Dargan served as the Company's Chief Financial Officer for a period of two years, and which expired January 31, 2010. The extension agreement dated as of February 1, 2010 (the "Engagement Extension Agreement") provides for an additional one-year term January 31, 2011 (the "Extended Term"). During the Extended Term, Mr. Dargan will continue to receive a fee of \$4,000 per month, which amount will be increased to \$8,000 or more in months during which the Company files its periodic reports with the Securities and Exchange Commission.

In addition to the cash compensation specified above, Mr. Dargan will be issued stock options over the Extended Term. Each option will allow Mr. Dargan to purchase 10,000 shares of the Company's common stock, and will be granted on the last business day of each month commencing February 2010 and ending January 2011, provided that the Engagement Extension Agreement with Mr. Dargan has not been terminated prior to each such grant date, at an exercise price equal to the closing price of a share of the Company's common stock on each grant date, each such option to be fully vested upon grant.

Mr. Dargan will continue to be reimbursed for business expenses he incurs in connection with the performance of his services as our Chief Financial Officer. All other provisions of the Engagement Agreement not expressly amended pursuant to the Engagement Extension Agreement remain the same, including provisions regarding indemnification and arbitration of disputes.

Note 15. Subsequent Events

Spring 2010 Private Securities Offering

On January 15, 2010 we commenced a private offering (the Spring 2010 Offering). Subsequent to March 31, 2010, we (i) sold \$138,250 principal amount of Spring 2010 Notes convertible at \$0.575 per share, (ii) issued warrants to purchase up to 240,437 shares of our common stock at \$0.75 per share which expire July 15, 2011, and (iii) issued warrants to purchase up to an additional 240,437 shares of our common stock at \$1.00 per share which expire January 15, 2013.

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

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

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

- our business plan;
- the commercial viability of our technology and products incorporating our technology;
- the effects of competitive factors on our technology and products incorporating our technology;
- expenses we will incur in operating our business;
- our liquidity and sufficiency of existing cash; and
- the success of our financing plans.

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

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

Our actual results could differ materially from those anticipated in these forward-looking statements as a result of various factors, including those set forth under the heading "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2009. Unless otherwise expressly stated herein, all statements, including forward-looking statements, set forth in this Form 10-Q are as of March 31, 2010, unless expressly stated otherwise, and we undertake no duty to update this information.

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

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

### Overview

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

In addition to our BioLargo technology, in 2008 we acquired the rights to market an iodine based water disinfection system (the "Isan system") from Ioteq IP Pty. Ltd., an Australian company, and its U.S. affiliate Ioteq Inc. ("Ioteq"). The Isan system is an automated water disinfection system that substantially reduces the incidence of fungal growth, spoilage, organisms and pathogens in water and on food. Capable of treating high volumes of water flow, the Isan

system is a combination of electrodes for measuring iodine levels in the target water stream, a control unit which automatically controls the running of the system, iodine canisters to deliver the iodine, and resin canisters to collect by-products after disinfection has been completed. The Isan system is registered with the APVMA (Australian Pesticides and Veterinary Medicines Authority) and FSANZ (Food Standards Australia and New Zealand) in Australia and New Zealand, where it has approximately 150 customer installations currently operating.

Both our BioLargo technology and the Isan system have potential commercial applications within global industries, including but not limited to agriculture, animal health, beach and soil environmental remediation, consumer products, food processing, medical, and water industries. While we believe the potential applications are many, we are currently focused in two primary areas – the development of certain products designed for the animal health industry, and agriculture.

First, in 2009, we launched our first products incorporating our BioLargo technology under the brand name “Odor-No-More”, in the animal health industry. The primary benefits of the products are odor and moisture control, and customers using our animal bedding additive experience a net savings on total bedding costs. We have focused our efforts on building wholesale distribution, and in 2010, we intend to expand our marketing efforts into new industries, as well as continue evaluating new product opportunities within the same industry.

Second, we are actively seeking to secure strategic partners to either license or partner with to exploit commercial opportunities for CupriDyne™ and for the Isan system. In March 2010, we entered into a series of transactions whereby we licensed the Isan system technology from Ioteg, and then sublicensed the technology to a third party for commercialization in the United States in certain fields of use. We are still actively marketing the Isan system for opportunities outside the United States pursuant to our marketing agreement with Ioteg, and in the United States through an agency agreement with Isan USA. We continue research and product development for our CupriDyne™ technology, and continue to work with a number of global companies who are engaged in technology evaluation and testing processes. Simultaneously, we are also actively seeking to identify and negotiate regional or global partnerships to exploit commercial opportunities for both CupriDyne™ and the Isan technologies. No such regional or global partnerships have been formed at this time, and we can make no representation about our ability to successfully conclude such arrangements.

#### Results of Operations—Comparison of the three-month periods ended March 31, 2010 and 2009

We generated revenues of \$10,733 during the three-month period ended March 31, 2010, as compared with no revenues during the three-month period ended March 31, 2009. During the last two quarters, rather than focus our efforts on direct selling activities, we focused our efforts on establishing and training a network of wholesale to retail distributors. As a result, our sales revenues have declined during each of the last two quarters. During the three-month period ended March 31, 2010, we used cash in operations of \$234,721, and incurred a net loss of \$2,013,753. Of this amount, \$1,305,585 consists of non-cash expenses related to the issuances of stock options, warrants and stock for services.

#### Revenue

We generated \$10,733 and \$0 in revenues from operations during the three-month periods ended March 31, 2010 and 2009. The revenues consist entirely of sales of our Odor-No-More products.

#### Selling, General and Administrative Expense

Selling, General and Administrative expenses were \$1,588,487 for the three-month period ended March 31, 2010, compared to \$991,790 for the three-month period ended March 31, 2009, an increase of \$596,697. The largest components of these expenses were:

a. Salaries and Payroll-related Expenses: These expenses were \$885,923 for the three-month period ended March 31, 2010, compared to \$492,529 for the three-month period ended March 31, 2009, an increase of \$393,394. The increase is related to the non-cash stock option compensation expense incurred in the three-month period ended March 31, 2010.

b. Consulting Expenses: These expenses were \$481,588 for the three-month period ended March 31, 2010, compared to \$276,063 for the three-month period ended March 31, 2009, an increase of \$205,525. The increase is primarily attributable to non-cash stock option compensation expense and stock issued for services incurred in the three-month period ended March 31, 2010 that were not issued in 2009.

c. Professional Fees: These expenses were \$124,318 for the three-month period ended March 31, 2010, compared to \$86,195 for the three-month period ended March 31, 2009, an increase of \$38,123. The increase is primarily attributable to non-cash stock option compensation expense.

d. Other Expense: These expenses were \$60,000 for the three-month period ended March 31, 2010, compared to \$50,000 for the three-month period ended March 31, 2009. The expenses incurred in 2009 and 2010 were the result of the obligations pursuant to the Marketing Agreement with Ioteq.

#### Interest expense

Interest expense totaled \$381,924 for the three-month period ended March 31, 2010, compared to \$403,526 for the three-month period ended March 31, 2009, a decrease of \$21,602. The decrease in the three-month period ended March 31, 2010 is primarily attributable to \$52,966 of expense incurred in the three-month period March 31, 2009 related to the fair value of the repricing of warrants that was not completed in the three-month period ended March 31, 2010. This was offset by an increase of interest expense related to the fair value amortization of our warrants and that we have increased our note payables outstanding resulting in additional interest expense.

#### Amortization and depreciation expense

Amortization and depreciation expense totaled \$2,391 for the three-month period ended March 31, 2010, compared to \$279,192 for the three-month period ended March 31, 2009, a decrease of \$276,801. The decrease is attributable to the impairment expense recorded December 31, 2009, related to our intangible assets which included Licensing rights and Assignment agreements acquired from IOWC in April 2007. Management performed its assessment of the fair value of the intangible assets for the year ended December 31, 2009. In our undertaking we analyzed the projected cash flow from the assets discounted at appropriate rates, the length of time to full development of the cash flow potential and the current recessionary state of the world-wide economy. We determined that after this detailed analysis that it was appropriate for us to record an impairment charge.

#### Research and Development

Research and development expenses were \$43,145 for the three-month period ended March 31, 2010, compared to \$36,929 for the three-month period ended March 31, 2009, an increase of \$6,216 which is related to patent application and prosecutions.

#### Net Loss

Net loss for the three-month period ended March 31, 2010 was \$2,013,753, a loss of \$0.05 per share, compared to a net loss for the three-month period ended March 31, 2009 of \$1,708,416, a loss of \$0.04 per share. The increase in net loss for the three-month period ended March 31, 2009 is primarily attributable to the non-cash option expense from the issuance of options to the management team and to consultants for services provided, recorded in the three-month period March 31, 2010.

#### Liquidity and Capital Resources

We have been, and anticipate that we will continue to be, limited in terms of our capital resources. Until we are successful in commercializing products or negotiating and securing payments for licensing rights from prospective licensing candidates, we expect to continue to have operating losses. Cash and cash equivalents totaled \$109,629 at March 31, 2010. We had negative working capital of \$4,220,698 for the three-month period ended March 31, 2010, compared with negative working capital of \$3,019,907 for the three-month period ended March 31, 2009. We negative cash flow from operating activities of \$234,721 three-month period ended March 31, 2010, compared to a negative cash flow from operating activities of \$273,567 for the three-month period ended March 31, 2009. We used cash from financing activities to fund operations. Our cash position is insufficient to meet our continuing anticipated expenses or fund anticipated operating expenses. Accordingly, we will be required to raise significant additional

capital to sustain operations and further implement our business plan and we may be compelled to reduce or curtail certain activities to preserve cash.

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The financial statements accompanying this report have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities and commitments in the normal course of our business. As reflected in the accompanying financial statements, we had a net loss of \$2,013,753 for the three-month period ended March 31, 2010, and an accumulated stockholders' deficit of \$59,782,317 as of March 31, 2010. The foregoing factors raise substantial doubt about our ability to continue as a going concern. Ultimately, our ability to continue as a going concern is dependent upon its ability to attract significant new sources of capital, attain a reasonable threshold of operating efficiencies and achieve profitable operations by licensing or otherwise commercializing products incorporating our BioLargo technology. The financial statements do not include any adjustments that might be necessary if we are unable to continue as a going concern.

As of March 31, 2010 we had \$3,565,035 aggregate principal amount, together with \$404,428 accrued and unpaid interest, outstanding on various promissory notes. We may pay all of these amounts in cash or in stock, at our option, at maturity. In addition, as of March 31, 2010, we had \$1,038,609 in accrued and unpaid payables (see Note 11) and \$150,000 in accrued and unpaid interest to New Millennium Capital Partners, LLC, an entity controlled by Dennis P. Calvert, our President and Chief Executive Officer. (See Note 14.)

We continue to be limited in terms of our capital resources. During the three-month period ended March 31, 2010, we received gross and net proceeds of \$229,000 pursuant to a private offering of our securities. Subsequent to March 31, 2010, we received an additional \$138,250 pursuant to a private offering of our securities.

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

In addition to the private securities offerings discussed above, we are continuing to explore numerous alternatives for our current and longer-term financial requirements, including additional raises of capital from investors in the form of convertible debt or equity. To fully implement our business plan, we believe that we must raise up to an additional \$10 million in financing. There can be no assurance that we will be able to raise any additional capital. No commitments are in place as of the date of the filing of this report for any such additional financings. Moreover, in light of the current unfavorable economic conditions, we do not believe that any such financing is likely to be in place in the immediate future.

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

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

#### Obligation to New Millennium Capital Partners, LLC

On April 13, 2007, New Millennium Capital Partners LLC ("New Millennium"), a limited liability company controlled and owned in part by the Company's CEO and president, Dennis P. Calvert, converted a promissory note (the "Note") in principal amount of \$900,000 into 1,636,364 shares of our common stock, at a price of \$0.55 per share, which was the last bid price on the date of conversion. Accrued but unpaid interest in the amount of \$380,658 as of the conversion date of April 13, 2007 remained outstanding on the Note, which amount was due to be paid on January 15, 2008. We

did not make such payment on such date. On November 12, 2008, we and New Millennium agreed to extend the date on which interest would be paid to April 30, 2009. On April 27, 2009, New Millennium agreed to accept as payment of \$230,658 of the outstanding \$380,658 in accrued but unpaid interest an option to purchase 691,974 shares of our common stock, exercisable at \$0.55 cents per share. This option will expire April 24, 2012. New Millennium further agreed to extend the due date for the remaining \$150,000 unpaid interest to April 30, 2010, which date has been further extended to October 31, 2010.

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## 2007 Equity Incentive Plan

On February 1, 2010, the Company's Compensation Committee issued options and a restricted stock award pursuant to the Company's 2007 Equity Incentive Plan to certain employees, outside consultants and professionals who had provided services to the Company during 2008 and 2009, consistent with management's recommendations to the committee.

In total, options to purchase an aggregate 1,060,000 shares of the Company's common stock were issued, at an exercise price of \$0.575 per share, which price was \$0.075 more than the \$0.50 closing price of the Company's common stock on the date of grant. Of the options issued, 400,000 were issued to third party consultants for their respective roles within the Company and the remaining 660,000 options were issued to the Company's principal executive officer, principal financial officer, and named executive officers, as set forth in the following table:

Name	Position	Number of Shares Underlying Options
Dennis P. Calvert	President and Chief Executive Officer	200,000
Charles K. Dargan II	Chief Financial Officer	60,000
Kenneth R. Code	Chief Technology Officer	200,000
Joseph L. Provenzano	Secretary, VP of Operations	200,000
	Total	660,000

With one exception, the options issued expire ten years from the date of grant (the option issued to Mr. Code expires five years from the date of grant).

## Critical Accounting Policies

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

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

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

Company and/or services or products received for non-cash consideration of the Company's common stock. The value is based on the market price of the Company's common stock issued as consideration, at the date of the agreement of each transaction or when the service is rendered or product is received, as adjusted for applicable discounts.

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

#### Recent Accounting Pronouncements

Only July 1, 2009, the Financial Accounting Standards Board (FASB) launched the FASB Accounting Standards Codification as the single source of authoritative nongovernmental U.S. generally accepted accounting principles (GAAP). The Codification is effective for interim and annual periods ending after September 15, 2009. All existing accounting standards documents are superseded as described in FASB Statement No. 168, The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles. All other accounting literature not included in the Codification is nonauthoritative.

Other recent accounting pronouncements issued by Financial Accounting Standards Board (including its Emerging Issued Task Force), the American Institute of Certified Public Accountants and the SEC did not or are not believed by management to have a material impact on the Company's present or future consolidated financial statements.

#### Item 4. Controls and Procedures

##### (a) Evaluation of disclosure controls and procedures.

We conducted an evaluation, under the supervision and with the participation of management, including our chief executive officer and chief financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this Report.

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

Based on this evaluation, our chief executive officer and chief financial officer concluded that as of the evaluation date our disclosure controls and procedures are effective but need improvement. Additionally, due to limited personnel and the resulting competing demands on our senior officers, at times there have been delays in disseminating information internally to those parties responsible for processing such information for disclosure. We have implemented certain further steps that we believe are warranted and believe, subject to our continuing evaluation and review of these further steps, that yet additional steps may also be warranted. We have adopted disclosure controls and procedures guidelines, however, additional steps that we believe that we must undertake are to retain a consulting firm to, among other things, design and implement adequate systems of accounting and financial statement disclosure controls during the current fiscal year to comply with the requirements of the SEC. We believe that the ultimate success of our plan to improve further our internal controls over financial reporting and disclosure controls and procedures will require a combination of additional financial resources, outside consulting services, legal advice, additional personnel, further reallocation of responsibility among various persons, improved lines of communication internally and substantial additional training of those of our officers, personnel and others, including certain of our directors such as our committee chairs, who are charged with implementing and/or carrying out our plan.

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

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

## PART II

## OTHER INFORMATION

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

## Spring 2010 Offering

Pursuant to a private offering that commenced January 2010 (the “Spring 2010 Offering”) and continued through March 31, 2010, we sold \$229,000 of our 10% convertible notes (the “Spring 2010 Notes”), which are due and payable on April 15, 2013, to ten investors, convertible into an aggregate 398,266 shares of our common stock. The Spring 2010 Notes are convertible into shares of our common stock at an initial conversion price of \$0.575 per share. The Spring 2010 Notes can be converted voluntarily by the noteholders at any time prior to the maturity date. We can unilaterally convert the Spring 2010 Notes (i) on or after July 31, 2010, if we have received one or more written firm commitments, or have closed on one or more transactions, or a combination of the foregoing, of at least \$3 million gross proceeds of equity or debt; or (ii) on the maturity date. Accordingly, the Spring 2010 Notes may be repaid in cash or may be converted, at our sole option, into shares of our common stock, on or before the April 15, 2013 maturity date.

Each purchaser of the Spring 2010 Notes received, for no additional consideration, two stock purchase warrants, each of which entitle the holder to purchase the number of shares of our common stock into which the holder’s Spring 2010 Note is initially convertible. The first warrant (the “Spring 2010 Eighteen Month Warrant”) is exercisable at a price of \$0.75 per share and expires on July 15, 2011. The second warrant (the “Spring 2010 Thirty-Six Month Warrant”) is exercisable at a price of \$1.00 per share and expires on January 15, 2013. (See Note 8.)

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

## Item 6. Exhibits

The exhibits listed below are attached hereto and filed herewith:

Exhibit No.	Description
31.1	Certification of Chief Executive Officer of Quarterly Report Pursuant to Rule 13(a)-15(e) or Rule 15(d)-15(e).
31.2	Certification of Chief Financial Officer of Quarterly Report Pursuant to 18 U.S.C. Section 1350
32	Certification of Chief Executive Officer and Chief Financial Officer of Quarterly Report pursuant to Rule 13(a)-15(e) or Rule 15(d)-15(e).

SIGNATURES

In accordance with Section 13 or 15(d) of the Exchange Act, the Registrant has caused this report to be signed on its behalf by the undersigned, hereunto duly authorized.

BIOLARGO, INC.

Date: May 17, 2010

By: /s/ DENNIS P. CALVERT  
Dennis P. Calvert  
Chief Executive Officer

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EXHIBIT INDEX

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32	Certification of Chief Executive Officer and Chief Financial Officer of Quarterly Report pursuant to Rule 13(a)-15(e) or Rule 15(d)-15(e).