Zagg INC
Form 10-Q
August 10, 2010

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

# FORM 10-Q

(Mark one)

[X] Quarterly Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended June 30, 2010, or

[ ] Transition Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from ______________ to _____________.

Commission File No. 000-52211
ZAGG INCORPORATED
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| Nevada<br>(State or other jurisdiction of incorporation or organization) | 20-2559624<br>(I.R.S. Employer Identification No.) |

3855 South 500 West, Suite J
Salt Lake City, Utah 84115
(Address of principal executive offices with zip code)

(801) 263-0699
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 229.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
Yes [ ] No [X]

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. [ ] Large accelerated filer [X] Accelerated filer [ ] Non-accelerated filer [ ] Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-25 of the Exchange Act).
Yes [ ] No [X]

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date: 22,489,231 common shares as of August 10, 2010.

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ZAGG INCORPORATED AND SUBSIDIARY
FORM 10-Q

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PART I - FINANCIAL INFORMATION

ZAGG INCORPORATED AND SUBSIDIARY
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

| | June 30, 2010 | December 31, 2009 |
|---|---|---|
| ASSETS | | |
| | | |
| Current assets | | |
| Cash | $ 6,401,597 | $ 4,970,756 |
| Accounts receivable, net | 9,220,818 | 5,450,722 |
| Inventories | 6,203,702 | 3,695,840 |
| Prepaid expenses and other current assets | 3,317,766 | 1,911,335 |
| Convertible bridge loan | 1,151,000 | 1,151,000 |
| Deferred income tax assets | 255,653 | 255,653 |
| | | |
| Total current assets | 26,550,536 | 17,435,306 |
| | | |
| Property and equipment, net | 938,984 | 887,705 |
| | | |
| Deferred income tax assets | 446,154 | 446,154 |
| | | |
| Deposits and other assets | 27,051 | 9,688 |
| | | |
| Intangible assets, net | 113,416 | 119,627 |
| | | |
| Total assets | $ 28,076,141 | $ 18,898,480 |
| | | |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| | | |
| Current liabilities | | |
| Accounts payable | $ 5,880,556 | $ 2,781,425 |
| Accrued liabilities | 2,702,259 | 1,252,461 |
| Accrued wages and wage related expenses | 205,464 | 164,495 |
| Deferred revenue | 313,860 | 262,937 |
| Sales returns liability | 923,447 | 550,201 |
| | | |
| Total current liabilities | 10,025,586 | 5,011,519 |
| | | |
| Total liabilities | 10,025,586 | 5,011,519 |
| | | |
| Stockholders' equity | | |
| Common stock, $0.001 par value; 50,000,000 shares authorized; | | |
| 22,340,564 and 21,711,862 shares issued and outstanding, respectively | 22,339 | 21,712 |
| Additional paid-in capital | 10,528,046 | 9,239,285 |

| | | | | |
|---|---|---|---|---|
| Cumulative translation adjustment | | 60,052 | | (112,039 ) |
| Retained earnings | | 7,440,118 | | 4,738,003 |
| Total stockholders' equity | | 18,050,555 | | 13,886,961 |
| Total liabilities and stockholders' equity | $ | 28,076,141 | $ | 18,898,480 |

See accompanying notes to condensed consolidated financial statements.

ZAGG INCORPORATED AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | June 30, 2010 | June 30, 2009 | June 30, 2010 | June 30, 2009 |
| Net sales | $15,058,783 | $9,214,971 | $23,822,402 | $17,290,146 |
| Cost of sales | 7,539,580 | 3,699,517 | 11,360,839 | 6,581,748 |
| Gross profit | 7,519,203 | 5,515,454 | 12,461,563 | 10,708,398 |
| Operating expenses: | | | | |
| Advertising and marketing | 1,016,660 | 1,393,194 | 2,077,623 | 2,846,248 |
| Selling, general and administrative | 3,278,265 | 2,259,150 | 5,827,870 | 4,395,148 |
| Total operating expenses | 4,294,925 | 3,652,344 | 7,905,493 | 7,241,396 |
| Income from operations | 3,224,278 | 1,863,110 | 4,556,070 | 3,467,002 |
| Other (expense) income: | | | | |
| Interest expense | (171,088) | (178) | (242,617) | (2,620) |
| Interest and other income | 6,853 | 50,226 | 13,563 | 92,274 |
| Total other (expense) income | (164,235) | 50,048 | (229,054) | 89,654 |
| Income before provision for income taxes | 3,060,043 | 1,913,158 | 4,327,016 | 3,556,656 |
| Income tax provision | (1,149,003) | (718,894) | (1,624,900) | (1,334,152) |
| Net income | $1,911,040 | $1,194,264 | $2,702,116 | $2,222,504 |
| Basic net income per common share | $0.09 | $0.06 | $0.12 | $0.11 |
| Diluted net income per common share | $0.08 | $0.05 | $0.11 | $0.10 |
| Weighted average number of shares outstanding - basic | 22,061,570 | 20,062,839 | 22,118,510 | 20,391,870 |
| Weighted average number of shares outstanding - diluted | 23,536,603 | 22,614,394 | 23,600,957 | 22,383,552 |

See accompanying notes to condensed consolidated financial statements.

ZAGG INCORPORATED AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

| ` | For the Six Months Ended June 30, 2010 | 2009 |
|---|---|---|
| Cash flows from operating activities | | |
| Net income | $ 2,702,116 | $ 2,222,504 |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities: | | |
| Non-cash expense related to stock-based compensation | 480,244 | 308,149 |
| Depreciation and amortization | 150,687 | 108,303 |
| Expense related to issuance of warrants | 30,548 | - |
| Bad debt expense | - | 60,421 |
| Foreign currency translation adjustment | 172,091 | (97,151) |
| Changes in assets and liabilities | | |
| Accounts receivable | (3,770,096) | (1,554,863) |
| Inventories | (2,507,862) | (2,265,961) |
| Prepaid expenses and other current assets | (1,406,431) | (594,164) |
| Other assets | (17,363) | - |
| Accounts payable | 3,099,130 | 690,862 |
| Accrued liabilities | 1,449,798 | (75,358) |
| Accrued wages and wage related expenses | 40,969 | 8,672 |
| Deferred revenues | 50,923 | (152,538) |
| Deferred tax liabilities | - | 1,329,765 |
| Sales return liability | 373,246 | 253,444 |
| Net cash provided by operating activities | 848,000 | 242,085 |
| Cash flows from investing activities | | |
| Payments for intangible assets | - | (32,921) |
| Purchase of property and equipment | (195,755) | (245,730) |
| Net cash used in investing activities | (195,755) | (278,651) |
| Cash flows from financing activities | | |
| Payments on debt | - | (10,024) |
| Proceeds from exercise of warrants and options | 778,596 | - |
| Proceeds from issuance of common stock and warrants | - | 2,315,096 |
| Net cash provided by financing activities | 778,596 | 2,305,072 |
| Net increase in cash and cash equivalents | 1,430,841 | 2,268,506 |
| Cash and cash equivalents at beginning of the period | 4,970,756 | 1,065,652 |

| | | | | |
|---|---|---|---|---|
| Cash and cash equivalents at end of the period | $ | 6,401,597 | $ | 3,334,158 |
| | | | | |
| Supplemental disclosure of cash flow information | | | | |
| Cash paid during the period for interest | $ | 242,617 | $ | 2,620 |
| Cash paid during the period for taxes | | 223,091 | | - |

See accompanying notes to condensed consolidated financial statements.

ZAGG INCORPORATED AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)
(Unaudited)

Supplemental schedule of noncash investing and financing activities

For the Six Months Ended June 30, 2010:

Issued 100,000 warrants.

For the Six Months Ended June 30, 2009:

None.

ZAGG INCORPORATED AND SUBSIDIARY
Notes to Condensed Consolidated Financial Statements
(Unaudited)

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation – The accompanying unaudited condensed consolidated financial statements of ZAGG Incorporated (collectively, the "Company" or "ZAGG") have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission (the "SEC"). Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations, although the Company believes that the following disclosures are adequate to make the information presented not misleading. The Company suggests that these condensed consolidated financial statements be read in conjunction with the consolidated financial statements and the notes thereto included in the Company's 2009 Annual Report on Form 10-K.

These condensed consolidated financial statements reflect all adjustments (consisting only of normal recurring adjustments) that, in the opinion of management, are necessary to present fairly the financial position and results of operations of the Company for the periods presented.

Operating results for the six months ended June 30, 2010, are not necessarily indicative of the results that may be expected for the year ending December 31, 2010.

Nature of Operations – The Company designs, manufactures and distributes protective coverings, audio accessories and power solutions for consumer electronic and hand-held devices under the brand names invisibleSHIELD™ and ZAGGaudio™.

Estimates – The discussion and analysis of the Company's financial condition and results of operations are based on the Company's financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States (U.S. GAAP). The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, the Company evaluates its estimates based on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. Significant estimates include the allowance for doubtful accounts, inventory valuation allowances, sales returns and warranty liability and the useful life of property and equipment.

Principles of Consolidation – The condensed consolidated financial statements include the accounts of ZAGG Incorporated, and its wholly owned subsidiary ZAGG Europe Ltd. All significant intercompany transactions have been eliminated in consolidation.

Revenue recognition – The Company records revenue when persuasive evidence of an arrangement exists or product delivery has occurred, the sales price to the customer is fixed or determinable, and collectability is reasonably assured. The Company's revenue is derived from sales of its products through its indirect channel including retailers and distributors and through its direct channel including ZAGG.com and its corporate owned mall kiosks, and from the fees derived from the sale of exclusive independent distributor licenses related to the kiosk program. For sales of product, the Company's standard shipping terms are FOB shipping point and the Company records revenue when the product is shipped, net of estimated returns and discounts. For some customers, the contractual shipping terms are FOB destination, for these shipments, the Company records revenue when the product is delivered, net of estimated returns and discounts.  For license fees, the Company recognizes revenue on a straight-line basis over the life of the license term.

Any incentives received from vendors are recognized as a reduction of the cost of products. Promotional products given to customers or potential customers are recognized as a cost of sales. Cash incentives provided to its customers are recognized as a reduction of the related sale price, and, therefore, are a reduction in sales.

ZAGG INCORPORATED AND SUBSIDIARY
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Reserve for Sales Returns and Warranty Liability – The Company's return policy generally allows its end users and retailers to return purchased products for refund or in exchange for new products within 45 days of end user purchase. The Company estimates a reserve for sales returns and records that reserve amount as a reduction of sales and as a sales return reserve liability. The sales return liability was $923,447 at June 30, 2010 and $550,201 at December 31, 2009.

The Company generally provides the ultimate consumer a warranty with each product and accrues warranty expense at the time of the sale based on the Company's prior claims history. Actual warranty costs incurred are charged against the accrual when paid. During the six months ended June 30, 2010 and 2009, warranty expense and the reserve for warranty liability, respectively, was not material.

Shipping and Handling Costs – Amounts invoiced to customers for shipping and handling are included in sales and were $762,307 and $753,708 for the six months ended June 30, 2010 and 2009, respectively. Actual shipping and handling costs to ship products to customers are included in cost of sales and were $3,230,777 and $2,393,243 for the six months ended June 30, 2010 and 2009, respectively.

Stock-based compensation – As required by generally accepted accounting principles, the Company recognizes the cost resulting from all stock-based payment transactions including shares issued under its stock option plans in the financial statements based upon the fair value of such equity instruments granted. For the six months ended June 30, 2010, the Company recognized stock-based compensation expense of $480,244, related to the issuance of common stock and options issued under its stock incentive plan.

Advertising – Advertising is expensed as incurred. Advertising expenses were $2,077,623 and $2,846,247 for the six months ended June 30, 2010 and 2009, respectively.

Foreign Currency Transactions – The condensed consolidated financial statements are presented in U.S. Dollars ("USD"). The Company's primary operations are at the parent level, which uses the USD as its functional currency.

Reclassifications – Certain amounts in the financial statements of the prior periods have been reclassified to conform to the current period presentation for comparative purposes.

Basic and Fully Diluted Net Income Per Common Share – Basic net income per share is computed by dividing net income by weighted average number of shares of common stock outstanding during each period. Diluted net income per share is computed by dividing net income by the weighted average number of shares of common stock, common stock equivalents and potentially dilutive securities outstanding during each period.

The following is a reconciliation of the numerator and denominator used to calculate Basic and Diluted EPS:

| | Net Income | Weighted Average Shares | Per Share Amount |
|---|---|---|---|
| Three months ended June 30, 2010: | | | |
| Basic EPS | $1,911,040 | 22,061,570 | $0.09 |
| Effect of common stock equivalents | — | 1,475,033 | |
| Diluted EPS | $1,911,040 | 23,536,603 | $0.08 |

| | | | |
|---|---|---|---|
| Three months ended June 30, 2009: | | | |
| Basic EPS | $1,194,264 | 20,062,839 | $0.06 |
| Effect of common stock equivalents | — | 2,551,555 | |
| Diluted EPS | $1,194,264 | 22,614,394 | $0.05 |

ZAGG INCORPORATED AND SUBSIDIARY
Notes to Condensed Consolidated Financial Statements
(Unaudited)

| | Net Income | Weighted Average Shares | Per Share Amount |
|---|---|---|---|
| Six months ended June 30, 2010: | | | |
| Basic EPS | $2,702,116 | 22,118,510 | $0.12 |
| Effect of common stock equivalents | — | 1,482,447 | |
| Diluted EPS | $2,702,116 | 23,600,957 | $0.11 |
| Six months ended June 30, 2009: | | | |
| Basic EPS | $2,222,504 | 20,391,870 | $0.11 |
| Effect of common stock equivalents | — | 1,991,682 | |
| Diluted EPS | $2,222,504 | 22,383,552 | $0.10 |

The calculation above for the three months ended June 30, 2010 excludes the exercise of 350,000 outstanding warrants and 1,023,833 outstanding stock options as the exercise of these warrants and stock options would have an anti-dilutive effect on earnings per share. The calculation for the six months ended June 30, 2010 excludes the exercise of 350,000 outstanding warrants and 1,048,833 outstanding stock options as the exercise of these warrants and stock options would have an anti-dilutive effect on earnings per share. The calculation above for the six months ended June 30, 2009 excludes the exercise of 3,000 outstanding stock options as the exercise of these stock options would have an anti-dilutive effect on earnings per share.

NOTE 2 – RECENT ACCOUNTING PRONOUNCEMENTS

Disclosures about Fair Value Measurements – In January 2010, the FASB issued guidance that requires an entity to disclose the following:

- Separately disclose the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and describe reasons for the transfers.

- Present separately information about purchases, sales, issuances and settlements, on a gross basis, rather than on one net number, in the reconciliation for fair value measurements using significant unobservable inputs (Level 3).

- Provide fair value measurement disclosures for each class of assets and liabilities.

- Provide disclosures about the valuation techniques and inputs used to measure fair value for both recurring and nonrecurring fair value measurements for fair value measurements that fall in either Level 2 or level 3.

This guidance is effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010. The Company is currently evaluating this guidance and does not expect the adoption of this guidance to have a material effect on the Company.

NOTE 3 – ACCOUNTS RECEIVABLE

Accounts receivable at June 30, 2010 and December 31, 2009 was as follows:

| | June 30, 2010 | December 31, 2009 |
|---|---|---|
| Accounts receivable | $9,905,973 | $6,135,877 |
| Less: Allowance for doubtful accounts | (685,155 ) | (685,155 ) |
| Accounts receivable, net | $9,220,818 | $5,450,722 |

ZAGG INCORPORATED AND SUBSIDIARY
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Bad debt expense for the six months ended June 30, 2010 and 2009 was $0 and $60,421, respectively.

On May 13, 2009, the Company entered into an accounts receivable financing agreement with Faunus Group International, Inc. ("FGI"). Under the agreement, the Company could offer to sell its accounts receivable to FGI each month during the term of the Agreement, up to a maximum amount outstanding at any time of $4,000,000. The Company could sell accounts receivable to FGI on either a credit approved or full recourse basis. Credit approved invoices were sold to FGI with no recourse, FGI accepted all credit default risk on invoices sold under the credit approved terms. The Company accounted for the sale of the credit approved invoices as a reduction to accounts receivable. Under the terms of the agreement, the Company was charged a monthly collateral management fee of 0.87% of the average monthly outstanding balance and interest at 7% per annum. The term of the agreement was for a period of four years, however, effective May 12, 2010, the Company terminated the receivable financing agreement with FGI. As a result of the early termination of the agreement, the Company paid a termination fee of $75,000 to FGI that was recorded as interest expense in the accompanying financial statements in full satisfaction of the Company's obligations under the agreement.

NOTE 4 – INVENTORIES

At June 30, 2010 and December 31, 2009 inventories consisted of the following:

| | June 30, 2010 | December 31, 2009 |
|---|---|---|
| Finished goods | $1,657,709 | $778,871 |
| Raw materials | 4,545,993 | 2,916,969 |
| Total inventory | $6,203,702 | $3,695,840 |

NOTE 5 – PROPERTY AND EQUIPMENT

At June 30, 2010 and December 31, 2009, property and equipment consisted of the following:

| | Useful Lives | June 30, 2010 | December 31, 2009 |
|---|---|---|---|
| Computer equipment and software | 3 to 5 years | $ 498,711 | $ 431,923 |
| Equipment | 3 to7 years | 560,372 | 452,473 |
| Furniture and fixtures | 7 years | 86,693 | 109,392 |
| Automobiles | 5 years | 93,002 | 93,002 |
| Leasehold improvements | 1 to 2.75 years | 361,946 | 318,180 |
| | | | |
| Total property and equipment | | 1,600,724 | 1,404,970 |
| Less: accumulated depreciation | | (661,740 ) | (517,265 ) |
| | | | |
| Total property and equipment, net | | $ 938,984 | $ 887,705 |

Depreciation expense was $144,476 and $105,834 for the six months ended June 30, 2010 and 2009, respectively.

NOTE 6 – INTANGIBLE ASSETS

At June 30, 2010, intangible assets consist of legal fees paid in connection with the Company’s patent application of $11,040 and amounts paid to secure the Company’s Internet addresses. The costs relating to the definite-lived intangible assets are amortized over their estimated useful lives using straight-line amortization. The useful life for Internet addresses is 10 years. As of June 30, 2010, the patent had not been granted. Accordingly, the Company has not begun to amortize the patent costs and will begin amortizing the patent over the legal life of the patent, when the patent is granted.

ZAGG INCORPORATED AND SUBSIDIARY
Notes to Condensed Consolidated Financial Statements
(Unaudited)

The Company has contractual rights customary in the industry to use its Internet addresses. However, the Company does not have and cannot acquire any property rights to the internet addresses. The Company does not expect to lose its rights to use the Internet addresses; however, there can be no assurance in this regard and such loss could have a material adverse effect on the Company's financial position and results of operations.

The Company's definite-lived intangible assets are summarized in the table below:

| June 30, 2010 | Gross Carrying Amount | Accumulated Amortization | Net Carrying Amount |
|---|---|---|---|
| Internet addresses | $124,234 | $ (21,858 ) | $102,376 |

For the six months ended June 30, 2010 and 2009, amortization expense was $6,212 and $2,248, respectively.

NOTE 7 – CONVERTIBLE BRIDGE LOAN

On September 28, 2009 the Company entered into a bridge loan agreement with HzO, ("HzO") for $1,151,000. HzO recently acquired the rights to the Golden Shellback technology developed by Northeast Maritime Institute, Inc. The technology is a molecular, vacuum deposited coating that is nonflammable, has low toxicity and has the ability to weatherproof electronic devices and other surfaces. The technology was renamed as the HzO Technology. The Company was granted the exclusive worldwide marketing rights for the HzO technology due to its efforts in assisting HzO in securing the HzO technology.

Under the terms of the bridge loan agreement, the Company has the option, but not the obligation, to convert the bridge loan into shares of Series A Preferred stock of HzO at a conversion price of $0.475 per share. The Company received a warrant of 300,000 shares of HzO Series A Preferred stock in lieu of interest payments for the loan. These warrants have not been assigned a value in the accompanying financial statements. The Company is a party to a guarantee agreement for an additional $2,000,000 payment to HzO, originally scheduled for payment on February 25, 2010 that has been indefinitely postponed, in the event that HzO, with its lead investor vSpring Capital, LLC, is unable to secure the necessary capitalization to abide by contractual terms.

NOTE 8 – PREPAID EXPENSES AND OTHER CURRENT ASSETS

Prepaid expenses and other current assets is summarized in the table below:

| | June 30, 2010 | December 31, 2009 |
|---|---|---|
| Interest and other receivables | $181,695 | $144,459 |
| Inventory deposits | 2,572,446 | 1,438,135 |
| Other | 563,625 | 328,741 |
| Total prepaid expenses and other current assets | $3,317,766 | $1,911,335 |

NOTE 9 – LINE OF CREDIT

Effective May 13, 2010, the Company entered into a Loan Agreement (the "Loan Agreement") with U.S. Bank National Association ("US Bank"). The Loan Agreement provides for revolving loans and other financial accommodations to or for the benefit of the Company of up to $5 million, to be used for working capital and other corporate purposes. The Company's obligations under the Loan Agreement and all related agreements are secured by all or substantially all of the Company's assets. The obligation of U.S. Bank to make advances under the Loan Agreement is subject to the conditions set forth in the Loan Agreement. The Loan Agreement and the credit facility mature on May 13, 2011.

ZAGG INCORPORATED AND SUBSIDIARY
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Advances under the Loan Agreement bear interest at LIBOR plus 2%. The default rate of interest is 3% per annum over the otherwise applicable interest rate. In addition to the accrual of interest at the default rate, in the event a payment is more than fifteen days past due, the Company shall pay a late fee equal to five percent of the missed payment.

At maturity, the entire outstanding principal balance, all remaining accrued and unpaid interest and all other amounts outstanding are be due and payable in full to U.S. Bank.

The Loan Agreement contains customary representations and warranties, certain affirmative and negative covenants as well as events that constitute events of default. The occurrence of an event of default could result in the acceleration of the obligations under the Loan Agreement. The Loan Agreement requires the Company to maintain a fixed charge coverage ratio of no less than 1.25 to 1.00 measured quarterly on a trailing twelve month basis and a leverage ratio of no greater than 2.0 to 1.0 measured quarterly on a trailing twelve month basis. The Loan Agreement's affirmative covenants require the Company to, among other things, deliver its financial statements, comply with applicable laws, and maintain its taxes and insurance. The Loan Agreement's negative covenants limit or restrict the Company's ability to, among other things, refund indebtedness or fund a distribution to equity holders, grant liens, or consummate mergers or the sale of assets. As of June 30, 2010, the Company was in compliance with all covenants under the Loan Agreement.

NOTE 10 – STOCKHOLDERS' EQUITY

During the six months ended June 30, 2010, the Company issued 20,000 shares of its common stock to employees valued at $42,200 and recorded as compensation expense in the accompanying condensed consolidated financial statements.

During the six months ended June 30, 2010 the Company granted employee stock options. These options vest equally over three years from the grant date and expire 5 years from the grant date. The Company values option grants using the Black-Scholes option pricing model and used the following assumptions:

| Options Granted | Exercise Price | Price at Grant Date | Expected Life | Volatility* | | Discount Rate | | Value |
|---|---|---|---|---|---|---|---|---|
| 771,500 | $2.53 | $2.53 | 2.5 years | 73 | % | 0.03 | % | $852,439 |
| 3,000 | $2.96 | $2.96 | 2.5 years | 72 | % | 0.15 | % | $3,843 |
| 3,000 | $3.04 | $3.04 | 2.5 years | 72 | % | 0.14 | % | $3,947 |
| 1,000 | $3.03 | $3.03 | 2.5 years | 72 | % | 0.14 | % | $1,311 |

* Volatility is calculated using historical volatility to provide an implied volatility as the Company's options do not trade

Based on vesting provisions, the Company expensed $438,044 relating to these new option grants and prior grants for the six months ended June 30, 2010.

During the six months ended June 30, 2010, the Company issued warrants for consulting services for 100,000 common shares exercisable at $2.58 per share. The warrants were valued at $30,548 using the Black-Scholes method with the following assumptions: stock price $2.58, expected life of .2 years; volatility of 66% (using historical volatility to provide an implied volatility as the Company's options do not trade) and a discount rate of 0.02%.

During the six months ended June 30, 2010, the Company issued 35,834 shares of its common stock in exercise of options to purchase 35,834 shares. The Company received proceeds of $33,867 related to the exercise of the options. The Company also issued 572,868 shares of its common stock in exercise of warrants to purchase 572,868 shares. The Company received proceeds of $744,728 related to the exercise of the warrants.

NOTE 11 – COMMITMENTS AND CONTINGENCIES

From time to time the Company may become subject to proceedings, lawsuits and other claims in the ordinary course of business, including proceedings related to environmental and other matters. Such matters are subject to many uncertainties, and outcomes are not predictable with assurance. As of June 30, 2010, the Company did not have any outstanding legal matters.

ZAGG INCORPORATED AND SUBSIDIARY
Notes to Condensed Consolidated Financial Statements
(Unaudited)

NOTE 12 – SUBSEQUENT EVENTS

Subsequent to June 30, 2010, the Company issued 115,000 shares of its common stock in exercise of warrants to purchase 115,000 shares of common stock and received proceeds of $149,500. The Company also issued 33,667 shares of common stock in exercise of employee options to purchase 33,667 shares of common stock and received proceeds of $29,811.

Management has evaluated subsequent events as of August 10, 2010, and has determined there are no further subsequent events to be reported.

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

Certain statements, other than purely historical information, including estimates, projections, statements relating to our business plans, objectives, and expected operating results, and the assumptions upon which those statements are based, are "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These forward-looking statements generally are identified by the words "believes," "project," "expects," "anticipates," "estimates," "intends," "strategy," "plan," "may," "will," "would," "will be," "will continue," "will likely result," and similar expressions. such forward-looking statements to be covered by the safe-harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995, and are including this statement for purposes of complying with those safe-harbor provisions. Forward-looking statements are based on current expectations and assumptions that are subject to risks and uncertainties which may cause actual results to differ materially from the forward-looking statements. Our ability to predict results or the actual effect of future plans or strategies is inherently uncertain. Factors which could have a material adverse affect on our operations and future prospects include, but are not limited to: changes in economic conditions, legislative/regulatory changes, availability of capital, interest rates, competition, and generally accepted accounting principles. These risks and uncertainties should also be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements. We undertake no obligation to update or revise publicly any forward-looking statements, whether as a result of new information, future events or otherwise. Further information concerning our business, including additional factors that could materially affect our financial results, is included herein and in our other filings with the SEC.

### Our Business

Headquartered in Salt Lake City, Utah, ZAGG Incorporated designs, manufactures and distributes protective coverings, audio accessories and power solutions for consumer electronic and hand-held devices under the brand names invisibleSHIELD™ and ZAGGaudio™. ZAGG has also introduced beta testing of AppSpace.com, an online destination for the fast-growing mobile app market, combined with the networking power of social media.

Our flagship product, invisibleSHIELD, is made from a protective, film covering that was developed originally to protect the leading edges of rotary blades of military helicopters. We determined that this same film product could be configured to fit onto the surface of electronic devices and marketed to consumers for use in protecting such devices from everyday wear and tear; including scratches, scrapes, debris and other surface blemishes. The film also permits touch sensitivity, meaning it can be used on devices that have a touch-screen interface. The invisibleSHIELD film material is highly reliable and durable since it was originally developed for use in a high friction, high velocity context within the aerospace industry. The film provides long lasting protection for the surface of electronic devices subject to normal wear and tear. The film is a form of polyurethane substance, akin to a very thin, pliable, flexible and durable clear plastic that adheres to the surface and shape of the object it is applied to.

The invisibleSHIELD is designed specifically for iPods®, laptops, cell phones, digital cameras, PDAs, watch faces, GPS systems, gaming devices, and other items. The product is "cut" to fit specific devices and packaged together with a moisture activating solution which makes the invisibleSHIELD adhere to the surface of the device, literally "like a second skin," and virtually invisible to the eye. The patent-pending invisibleSHIELD is the first scratch protection solution of its kind on the market. The invisibleSHIELD is not ornamental, but rather provides a long lasting barrier to preserve the brand new look of the surface of an electronic device. Currently, ZAGG offers over 4,000 precision pre-cut designs with a lifetime replacement warranty through online channels, big-box retailers, electronics specialty stores, resellers, college bookstores, Mac stores, and mall kiosks. We plan to increase our product lines to offer new electronic accessories to our tech-savvy customer base, as well as an expanded array of invisibleSHIELD products for other industries.

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The ZAGGaudio line of electronics accessories and products was released in late 2008, and focuses on innovation and superior value. The flagship product within ZAGGaudio is the award winning, Z.buds™. Other headphone, speaker and audio products have been released and we intend to release additional products in the ZAGGaudio line in the coming months and years.

We maintain our corporate offices and operational facility at 3855 South 500 West, Suites B, C, J, K, L and R, Salt Lake City, Utah, 84115. The telephone number of the Company is 801-263-0699. Our website address is www.ZAGG.com.

Estimates

The discussion and analysis of our financial condition and results of operations are based on our financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States (U.S. GAAP). 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 related disclosure of contingent assets and liabilities. On an on-going basis, we evaluate our estimates based on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. Significant estimates include the allowance for doubtful accounts, inventory valuation allowances, sales returns and warranty liability and the useful life of property and equipment.

Recent Accounting Pronouncements

Disclosures about Fair Value Measurements – In January 2010, the FASB issued guidance requires an entity to disclose the following:

- Separately disclose the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and describe reasons for the transfers.

- Present separately information about purchases, sales, issuances and settlements, on a gross basis, rather than on one net number, in the reconciliation for fair value measurements using significant unobservable inputs (Level 3).

- Provide fair value measurement disclosures for each class of assets and liabilities.

- Provide disclosures about the valuation techniques and inputs used to measure fair value for both recurring and nonrecurring fair value measurements for fair value measurements that fall in either Level 2 or level 3.

This guidance is effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010. We are currently evaluating this guidance and do not expect the adoption of this guidance to have a material effect on our financials.

Revenue recognition

We record revenue when persuasive evidence of an arrangement exists or product delivery has occurred, the sales price to the customer is fixed or determinable, and collectability is reasonably assured. Our revenue is derived from sales of our products through our indirect channel including retailers and distributors and through our direct channel including ZAGG.com and our corporate owned mall kiosk, and from the fees derived from the sale of exclusive independent distributor licenses related to the kiosk program.  For sales of product, our standard shipping terms are FOB shipping point and we record revenue when the product is shipped, net of estimated returns and discounts.  For some customers, the contractual shipping terms are FOB destination, for these shipments, we record revenue when the products are delivered, net of estimated returns and discounts.  For license fees, we recognize revenue on a straight-line basis over the life of the license term.

Any incentives received from vendors are recognized as a reduction of the cost of products. Promotional products given to customers or potential customers are recognized as a cost of sales. Cash incentives provided to our customers are recognized as a reduction of the related sale price, and, therefore, are a reduction in sales.

Factors Affecting Results of Operations

Our operating expenses consisted primarily of the following:

- Cost of sales, which consists primarily of raw materials, components and production of our products, including, maintenance, facilities and other operating costs associated with the production of our products;

- Selling, general and administrative expenses, which consist primarily of salaries, commissions and related benefits paid to our employees and related selling and administrative costs including professional fees and advertising expenses; and

- Depreciation and amortization expenses which result from the depreciation of our property and equipment, including amortization of our intangible assets.

Reserve for Sales Returns and Warranty Liability

Our return policy generally allows our end users and retailers to return purchased products for refund or in exchange for new products within 45 days of end user purchase. We estimate a reserve for sales returns and record that reserve amount as a reduction of sales and as a sales return reserve liability.

We generally provide the ultimate consumer a warranty with each product and accrue warranty expense at the time of the sale based on our prior claims history. Actual warranty costs incurred are charged against the accrual when paid.

Results of Operations

THREE MONTHS ENDED JUNE 30, 2010 AND 2009

Net sales

Net sales for the quarter ended June 30, 2010 were $15,058,783 as compared to net sales of $9,214,971 for the quarter ended June 30, 2009, an increase of $5,843,812 or 63%.

For the quarter ended June 30, 2010, our sales mix breakdown was 66% through indirect wholesale channels, 23% direct through our website to retail customers, 8% through our mall cart and kiosk programs and 3% from shipping and handling charges. Sales of our invisibleSHIELD product continue to represent the majority of our sales. We are continuing to see increased demand for our invisibleSHIELD product, particularly from our wholesale distribution channel partners including Best Buy and Radio Shack.

Cost of sales

Cost of sales includes raw materials, packing materials, shipping and fulfillment costs. For the quarter ended June 30, 2010, cost of sales amounted to $7,539,580 or approximately 50% of net sales as compared to cost of sales of $3,699,517 or approximately 40% of net sales for quarter ended June 30, 2009. The increase in cost of sales as a percentage of net revenues for the quarter ended June 30, 2010 as compared to the quarter ended June 30, 2009 is attributable to the overall sales mix shift to wholesale customers which have a lower average selling price than our internet sales and increased costs due to the need to pay expedited shipping costs related to some of our raw materials for our invisibleSHIELD product line.

Gross profit

Gross profit for the quarter ended June 30, 2010 was $7,519,203 or approximately 50% of net sales as compared to $5,515,454 or approximately 60% of net sales for the quarter ended June 30, 2009. The decrease in gross profit percentage was due to the sales mix shift from higher margin internet sales to wholesale customers which have a lower average selling price and a decrease in internet sales for the quarter ended June 30, 2010 as compared to the quarter ended June 30, 2009 and elevated costs of expediting raw materials in order to meet the rapid sales growth during the quarter ended June 30, 2010. There are no assurances that we will continue to recognize similar gross profit margins in the future.

Operating expenses

Total operating expenses for the quarter ended June 30, 2010 were $4,294,925, an increase of $642,581 from total operating expenses for the quarter ended June 30, 2009 of $3,652,344. The increases are primarily attributable to the following:

- For the quarter ended June 30, 2010, salaries and related taxes increased by $274,906 to $1,358,138 from $1,083,232 for the quarter ended June 30, 2009. The increase is due to the increase in our staff as we continue to build the people infrastructure to meet the demand for our product and continue to develop new products and offerings, and non-cash compensation expense related to our stock based compensation plan of $238,174.

    - For the quarter ended June 30, 2010, marketing, advertising and promotion expenses were $1,016,660, a decrease of $376,534 as compared to $1,393,194 for the quarter ended June 30, 2009. We continue to invest heavily in the development of the invisibleSHIELD and ZAGG brands through internet key word advertising and through traditional print media, television and radio advertising and through the use of coupons. We expect our marketing and advertising expenses to continue to be a significant expenditure as our revenues increase and expect to spend increased funds on advertising and promotion of our products as well as sales training. During the fiscal year 2010, we intend to continue to expand our marketing efforts related to our products.

- For the quarter ended June 30, 2010, other selling, general and administrative expenses, net of salaries and related taxes described above, were $1,920,127 as compared to $1,175,918 for the quarter ended June 30, 2009. The changes by category are summarized in the table below:

| | Three Months Ended June 30, 2010 | Three Months Ended June 30, 2009 |
|---|---|---|
| Professional fees | $272,391 | $134,933 |
| Rent | 189,205 | 124,635 |
| Credit card and bank fees | 120,047 | 172,215 |
| Commissions | 292,269 | 171,261 |
| Other | 1,046,215 | 572,874 |
| Total | $1,920,127 | $1,175,918 |

Income from operations

We reported income from operations of $3,224,278 for the quarter ended June 30, 2010 as compared to income from operations of $1,863,110 for the quarter ended June 30, 2009, an increase of $1,361,168. The increase in income from operations for the quarter ended June 30, 2010 as compared to the quarter ended June 30, 2009 is primarily attributable to our overall increase in net sales, partially offset by a decrease in gross profit with the sales mix shift from the direct channel to the indirect channel.

Other (expense) income

For the quarter ended June 30, 2010, total other expense was ($164,235) as compared to other income of $50,048 for the quarter ended June 30, 2009. The decrease is primarily attributed to interest expense associated with our terminated credit facility and decreased interest income related to short-term loans.

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Net income

As a result of these factors, we reported net income of $1,911,040 or $0.08 per share on a fully diluted basis for the quarter ended June 30, 2010 as compared to net income of $1,194,264 or $0.05 per share on a fully diluted basis for the quarter ended June 30, 2009.

SIX MONTHS ENDED JUNE 30, 2010 AND 2009

Net sales

Net sales for the six months ended June 30, 2010 were $23,822,402 as compared to net sales of $17,290,146 for the six months ended June 30, 2009, an increase of $6,532,256 or 38%.

For the six months ended June 30, 2010, our sales mix breakdown was 65% through indirect wholesale channels, 23% direct through our website to retail customers, 9% through our mall cart and kiosk programs and 3% from shipping and handling charges. Sales of our invisibleSHIELD product continue to represent the majority of our sales. We are continuing to see increased demand for our invisibleSHIELD product, particularly from our wholesale distribution channel partners including Best Buy and Radio Shack.

Cost of sales

Cost of sales includes raw materials, packing materials, shipping and fulfillment costs. For the six months ended June 30, 2010, cost of sales amounted to $11,360,839 or approximately 48% of net sales as compared to cost of sales of $6,581,748 or approximately 38% of net sales for six months ended June 30, 2009. The increase in cost of sales as a percentage of net revenues for the quarter ended June 30, 2010 as compared to the quarter ended June 30, 2009 is attributable to the overall sales mix shift to wholesale customers which have a lower average selling price than our internet sales and increased costs due to the need to pay expedited shipping costs related to some of our raw materials for our invisibleSHIELD product line.

Gross profit

Gross profit for the six months ended June 30, 2010 was $12,461,563 or approximately 52% of net sales as compared to $10,708,398 or approximately 62% of net sales for the six months ended June 30, 2009. The decrease in gross profit percentage was due to the sales mix shift from higher margin internet sales to wholesale customers which have a lower average selling price and a decrease in internet sales for the six months ended June 30, 2010 as compared to the six months ended June 30, 2009 and elevated costs of expediting raw materials in order to meet the rapid sales growth during the quarter ended June 30, 2010. There are no assurances that we will continue to recognize similar gross profit margins in the future.

Operating expenses

Total operating expenses for the six months ended June 30, 2010 were $7,905,493, an increase of $664,097 from total operating expenses for the six months ended June 30, 2009 of $7,241,396. The increases are primarily attributable to the following:

- For the six months ended June 30, 2010, salaries and related taxes increased by $807,133 to $2,727,967 from $1,920,834 for the six months ended June 30, 2009. The increase is due to the increase in our staff as we continue to build the people infrastructure to meet the demand for our product and continue to develop new products and offerings, and non-cash compensation expense related to our stock based compensation plan of $480,244.

- For the six months ended June 30, 2010, marketing, advertising and promotion expenses were $2,077,623, a decrease of $768,625 as compared to $2,846,248 for the six months ended June 30, 2009. We continue to invest heavily in the development of the invisibleSHIELD and ZAGG brands through internet key word advertising and through traditional print media, television and radio advertising and through the use of coupons. We expect our marketing and advertising expenses to continue to be a significant expenditure as our revenues increase and expect to spend increased funds on advertising and promotion of our products as well as sales training. During the fiscal year 2010, we intend to continue to expand our marketing efforts related to our products.

- For the six months ended June 30, 2010, other selling, general and administrative expenses, net of salaries and related taxes described above, were $3,099,903 as compared to $2,474,314 for the six months ended June 30, 2009. The changes by category are summarized in the table below:

| | Six Months Ended June 30, 2010 | Six Months Ended June 30, 2009 |
|---|---|---|
| Professional fees | $356,408 | $204,999 |
| Rent | 336,022 | 222,225 |
| Credit card and bank fees | 271,048 | 348,747 |
| Commissions | 500,664 | 421,437 |
| Other | 1,635,761 | 1,276,906 |
| Total | $3,099,903 | $2,474,314 |

Income from operations

We reported income from operations of $4,566,070 for the six months ended June 30, 2010 as compared to income from operations of $3,467,002 for the six months ended June 30, 2009, an increase of $1,099,068. The increase in income from operations for the six months ended June 30, 2010 as compared to the six months ended June 30, 2009 is primarily attributable to our overall increase in net sales, partially offset by a decrease in gross profit with the sales mix shift from the direct channel to the indirect channel.

Other (expense) income

For the six months ended June 30, 2010, total other expense was ($229,054) as compared to other income of $89,654 for the six months ended June 30, 2009. The decrease is primarily attributed to interest expense associated with our terminated credit facility and decreased interest income related to short-term loans.

Net income

As a result of these factors, we reported net income of $2,702,116 or $0.11 per share on a fully diluted basis for the six months ended June 30, 2010 as compared to net income of $2,222,504 or $0.10 per share on a fully diluted basis for the quarter ended June 30, 2009.

Liquidity and Capital Resources

Liquidity is the ability of a company to generate funds to support its current and future operations, satisfy its liabilities and otherwise operate on an ongoing basis.

At June 30, 2010, we had a cash balance of $6,401,597.

Our working capital position increased by $4,101,163 to working capital of $16,524,950 at June 30, 2010 from working capital of $12,423,787 at December 31, 2009. This increase in working capital is primarily attributable to the overall increase in current assets of $9,115,230 due to increased accounts receivable of $3,770,096, increased inventories of $2,507,862, increased prepaid expenses and other current assets of $1,406,431and increased cash of $1,430,841, partially offset by increased accounts payable of $3,099,130, increased accrued liabilities of $1,449,798, increased sales return liability of $373,246, increased deferred revenues of $50,923 and increased accrued wages of $40,969.

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Net cash provided by operating activities for the six months ended June 30, 2010 was $848,000 as compared to net cash provided by operating activities of $242,085 for the six months ended June 30, 2009. For the six months ended June 30, 2010, net cash provided by operating activities was attributable primarily to increased accounts payable of $3,099,130, increased accrued liabilities of $1,449,798, non-cash expense related to stock based compensation of $480,244, increased sales return liabilities of $373,246, foreign currency translation adjustment of $172,091, depreciation and amortization of $150,687, increased deferred revenues of $50,923, increased accrued wages and wage related expenses of $40,969, expenses related to the issuance of warrants of $30,548 partially offset by increased accounts receivable of $3,770,096, increased inventories of $2,507,862 and increased prepaid expenses and other current assets of $1,406,431

Net cash used in investing activities for the six months ended June 30, 2010 was ($195,755) attributable to the purchase of equipment.

Net cash provided by financing activities for the six months ended June 30, 2010 was $778,596 attributable to proceeds from the exercise of options and warrants.

We reported a net increase in cash for the six months ended June 30, 2010 of $1,430,841.

For the six months ended June 30, 2010 and 2009, we generated revenues of $23,822,402 and $17,290,146, respectively and reported net income of $2,702,116 and $2,222,504, respectively. For the six months ended June 30, 2010, we had cash flow from operating activities of $848,000 and $242,085, respectively. As of June 30, 2010, we had stockholders' equity of $18,050,555, retained earnings of $7,440,118, working capital of $16,524,950, accounts payable of $5,880,556, accrued liabilities of $2,702,259, sales returns liability of $923,447, deferred revenue of $313,860 and accrued wages and wage related expenses of $205,464. Management believes that existing cash, along with cash generated from the collection of accounts receivable and the sale of products will be sufficient to meet the Company's cash requirements during the next twelve months.

Off Balance Sheet Arrangements

As of June 30, 2010, there were no off balance sheet arrangements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

We are exposed to certain market risks in the ordinary course of our business. These risks result primarily from changes in foreign currency exchange rates and interest rates. In addition, our international operations are subject to risks related to differing economic conditions, changes in political climate, differing tax structures and other regulations and restrictions.

To date we have not utilized derivative financial instruments or derivative commodity instruments. We do not expect to employ these or other strategies to hedge market risk in the foreseeable future. We invest our cash in money market funds, which we believe are subject to minimal credit and market risk. We believe that the market risks associated with these financial instruments are immaterial.

Item 4T. Controls and Procedures

As of the date of this report, our Chief Executive Officer and Chief Financial Officer evaluated the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Rule 13a-15b under the Securities Exchange Act of 1934. Based on their review of our disclosure controls and procedures, they have concluded that our disclosure controls and procedures are effective in timely alerting them to material information relating to us that is required to be included in our periodic SEC filings. Further, there were no significant changes in the internal controls or in other factors that could significantly affect these disclosure controls after the evaluation date and the date of this report. Nor were there any significant deficiencies or material weaknesses in such disclosure controls and procedures requiring corrective actions. As a result, no corrective actions were taken. We have made no changes in our internal controls over financial reporting in the most recent quarterly reporting period that have materially affected, or are reasonably likely to affect, our internal controls over financial reporting.

Limitations on the Effectiveness of Internal Controls

Our management does not expect that our disclosure controls and procedures or our internal control over financial reporting will necessarily prevent all fraud and material error. An internal control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the internal control. The design of any system of controls also 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. Over time, control may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

We are not presently party to any legal proceedings.  We are not aware of any pending legal proceeding to which any of our officers, directors, or any beneficial holders of 5% or more of our voting securities are adverse to us or have a material interest adverse to us.

Item 1A. Risk Factors

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I. “Item 1A. Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2009 (the “2009 Form 10-K”), which could materially affect our business, financial condition or future results.  The following information updates certain of our risk factors and should be read in conjunction with the risk factors disclosed in the 2009 Form 10-K.  These risk factors should be read carefully in connection with evaluating our business and in connection with the forward-looking statements contained in this Quarterly Report on Form 10-Q.  Any of the risks described below or in the 2009 Form 10-K could materially adversely affect our business, financial condition or future results and the actual outcome of matters as to which forward-looking statements are made.  These are not the only risks we face.  Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results.

We depend on large purchases from a significant customer, Best Buy, and any loss, cancellation or delay in purchases by this customer could cause a shortfall in revenue, excess inventory and inventory holding or obsolescence charges.

For the three months ended June 30, 2010, Best Buy alone represented 39% of our revenue.  Best Buy does not have minimum purchase requirements and can stop purchasing our products at any time or with very short notice.  In addition, including Best Buy, most of our customer agreements are short term and non-exclusive and provide for purchases on a purchase order basis.  We expect that Best Buy will continue to represent a substantial percentage of our sales.  If Best Buy reduces, delays or cancels orders with us, and we are not able to sell our products to new customers at comparable levels, our revenue could decline significantly and could result in excess inventory and inventory holding or obsolescence charges.  In addition, any difficulty in collecting amounts due from Best Buy would negatively impact our result of operations.

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

During the six months ended June 30, 2010, we issued the following securities:

§ 20,000 shares of common stock to employees valued at $42,200;

§ 778,500 stock options as shown in the table below:

| Options Granted | Exercise Price | Price at Grant Date | Expected Life | Volatility* | Discount Rate | Value |
|---|---|---|---|---|---|---|
| 771,500 | $2.53 | $2.53 | 2.5 years | 73 % | 0.03 % | $852,439 |
| 3,000 | $2.96 | $2.96 | 2.5 years | 72 % | 0.15 % | $3,843 |
| 3,000 | $3.04 | $3.04 | 2.5 years | 72 % | 0.14 % | $3,947 |
| 1,000 | $3.03 | $3.03 | 2.5 years | 72 % | 0.14 % | $1,311 |

* Volatility is calculated using historical volatility to provide an implied volatility as the Company's options do not trade

§ warrants for consulting services for 100,000 common shares exercisable at $2.58 per share expiring in 5 years and vesting equally over 1 year. The warrants were valued at $30,548 using the Black-Scholes method with the following assumptions: stock price $2.58, expected life of .2 years; volatility of 67% (using historical volatility to provide an implied volatility as the Company's options do not trade) and a discount rate of 0.02%.

§ 35,834 shares of common stock in exercise of options to purchase 35,834 shares. We received proceeds of $33,867 related to the exercise of the options. We also issued 572,868 shares of common stock in exercise of warrants to purchase 572,868 shares. We received proceeds of $744,728 related to the exercise of the warrants.

Subsequent to June 30, 2010, we issued 115,000 shares of our common stock in exercise of warrants to purchase 115,000 shares of common stock and received proceeds of $149,500. We also issued 33,667 shares of common stock in exercise of employee options to purchase 33,667 shares of common stock and received proceeds of $29,811.

These securities were issued pursuant to Section 4(2) of the Securities Act of 1933, as amended , and /or Rule 506 of Regulation D promulgated thereunder.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Reserved

Item 5. Other Information

None.

Item 6. Exhibits

a. Exhibits: The following Exhibits are filed with this Form 10-Q pursuant to Item 601(a) of Regulation S-K:

| Exhibit No. | Description of Exhibit |
|---|---|
| 31.1 | Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant toSection 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2 | Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant toSection 302 of the Sarbanes-Oxley Act of 2002. |
| 32.1 | Certification of Chief Executive Officer pursuant to 18 U.S. C. Section 1350, as adopted pursuant toSection 906 of the Sarbanes-Oxley Act of 2002. |

| | |
|---|---|
| 32.2 | Certification of Chief Financial Officer pursuant to 18 U.S. C. Section 1350, as adopted pursuant toSection 906 of the Sarbanes-Oxley Act of 2002. |

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

ZAGG INCORPORATED

| | | |
|---|---|---|
| Date: August 10, 2010 | By: | /s/ROBERT G. PEDERSEN II<br>Robert G. Pedersen II,<br>President and Chief Executive Officer |
| Date: August 10, 2010 | By: | /s/ BRANDON T. O'BRIEN<br>Brandon T. O'Brien,<br>Chief Financial Officer<br>(Principal financial officer) |