

**QUARTERLY REPORT**  
**PURSUANT TO**  
**PINK SHEETS GUIDELINES FOR PROVIDING ADEQUATE PUBLIC DISCLOSURE**

**COVERING PERIOD ENDING JUNE 30, 2009**

**PACIFIC ENTERTAINMENT CORPORATION**  
**A CALIFORNIA CORPORATION**

All information contained in this Information and Disclosure Statement has been compiled to fulfill the disclosure requirements of Rule 15c2-11(a)(5) promulgated under the Securities Act of 1934 as amended. The enumerated captions contained herein correspond to the sequential format as set forth in the Guidelines for Providing Adequate Current Public Information provided by PinkSheets, LLC.



INITIAL COMPANY INFORMATION AND DISCLOSURE STATEMENT

PART A GENERAL COMPANY INFORMATION

**Item I. Exact Name Of The Issuer And The Address Of Its Principal Executive Offices**

Pacific Entertainment Corporation (the "Company")  
5820 Oberlin Drive, Suite 203  
San Diego, California 92121  
Office – (858) 450-2900  
Fax - (858) 450-2907  
<http://www.pacificentcorp.com/>  
<http://babygenius.com/>

Investor relations for Pacific Entertainment Corporation will be handled by its Chief Executive Officer, Klaus Moeller, who may be contacted as follows:

5820 Oberlin Drive, Suite 203  
San Diego, California 92121  
Tele - (310) 858-7838  
E-mail - [klaus@pacificentcorp.com](mailto:klaus@pacificentcorp.com)

**Item II. Shares Outstanding.**

As of June 30, 2009, there were approximately 54,332,500 shares of common stock issued and outstanding. The Company's authorized common shares are 100,000,000 shares. The total number of shares that are free trading are 13,062,500 shares. The total number of beneficial shareholders is 80. The total number of shareholders of record is 85.

**Item III. Interim Financial Statements.**

Our financial report for the period ended June 30, 2009 are attached to the end of this Quarterly Report and are hereby incorporated by reference as follows:

Balance Sheets  
Statements of Operations  
Statements of Stockholder's Equity (Deficit)  
Statements of Cash Flows  
Notes to Financial Statements

The afore-mentioned financial statements can be found immediately following the certification of this Quarterly Report.

#### **Item IV. Management's Discussion And Analysis Or Plan Of Operation.**

The following management's discussion and analysis of financial condition and results of operations (MD&A) is intended to help the reader understand the results of operations and financial condition of Pacific Entertainment Corporation. The MD&A is provided as a supplement to, and should be read in conjunction with, our Financial Statements and the accompanying Notes to the Financial Statements in this report.

#### **Safe Harbor for Forward-Looking Statements**

When used in this statement, the words "may," "will," "expect," "anticipate," "continue," "estimate," "project," "intend," and similar expressions are intended to identify forward-looking statements within the meaning of Section 27a of the Securities Act of 1933 and Section 21e of the Securities Exchange Act of 1934 regarding events, conditions, and financial trends that may affect the Company's future plans of operations, business strategy, operating results, and financial position. Persons reviewing this report are cautioned that any forward-looking statements are not guarantees of future performance and are subject to risks and uncertainties and those actual results may differ materially from those included within the forward looking statements as a result of various factors. Such factors include, among other things, uncertainties relating to our success in judging consumer preferences, financing our operations, entering into strategic partnerships, engaging management, seasonal and period-to-period fluctuations in sales, failure to increase market share or sales, inability to service outstanding debt obligations, dependence on a limited number of customers, increased production costs or delays in production of new products, intense competition within the industry, inability to protect intellectual property in the international market for our products, changes in market condition and other matters disclosed by us in our public filings from time to time. Forward-looking statements speak only as to the date they are made. The Company does not undertake to update forward-looking statements to reflect circumstances or events that occur after the date the forward-looking statements are made.

#### **Our Business**

Pacific Entertainment Corporation commenced operations in January 2006, assuming all of the rights and obligations of its Chief Executive Officer, Klaus Moeller, under an Asset Purchase Agreement between the Company and Genius Products, Inc., in which we obtained all rights, copyrights, and trademarks to the brands "Baby Genius," "Little Genius," "Kid Genius," and "Wee Worship," and all then existing productions under those titles. We provide music-based products that are educational and entertaining for infants and young children, in both English and Spanish languages, sold globally through retailers, distributors, and through licensing of the brand.

We generate revenue from creating, manufacturing, and selling at wholesale DVD's and music CD's based on our brands. In addition, we license other brands that we feel we can market and sell through our distribution channel, such as "Guess How Much I Love You" and "The Snowman". We also license our brand internationally for others to manufacture and sell, and from which we derive royalty revenue.

#### **Results of Operations**

Please refer to the financial statements, which are attached immediately following this Quarterly Report and are incorporated herein by reference, for further information regarding the results of

operations of the Company. All references to notes in the financial statements are references to the financial statements attached to this Quarterly Report.

*Three- And Six-Month Period Ended June 30, 2009 Compared to December 31, 2008*

Our summary results are presented below:

	<b>Three Months</b>	<b>Six Months</b>	<b>Twelve Months</b>
	<b>Ending</b>	<b>Ending</b>	<b>Ending</b>
	<b>6/30/2009</b>	<b>6/30/2009</b>	<b>12/31/2008</b>
Revenues	\$ 452,791	\$ 1,449,506	\$ 2,126,589
Costs and expenses	(763,832)	(2,041,426)	(2,959,828)
Depreciation and Amortization	(151,893)	(303,200)	(600,628)
Loss from Operations	(462,934)	(895,120)	(1,433,867)
Other Income	32	495	2,559
Interest Expense	(76,681)	(158,671)	(346,239)
Gain on Settlement of Debt	0	0	42,261
Loss on Disposition of Assets	0	(2,775)	(9,028)
Total Other Income	(76,649)	(160,951)	(310,447)
Net Loss	\$ (539,583)	\$ (1,056,071)	\$ (1,744,314)
Net Loss per common share	\$ (0.01)	\$ (0.02)	\$ (0.04)
Weighted average shares outstanding	54,290,742	54,163,163	46,964,959

**Revenues.** Revenues by product segment and for the Company as a whole were as follows:

	<b>Three Months</b>	<b>Six Months</b>	<b>Twelve Months</b>
	<b>Ending</b>	<b>Ending</b>	<b>Ending</b>
	<b>6/30/2009</b>	<b>6/30/2009</b>	<b>12/31/2008</b>
Direct PEC Product Sales	\$ 376,890	\$ 1,345,091	\$ 890,132
Licensed Products	12,993	26,700	210,665
Licensing & Royalties	62,908	77,715	1,025,792
Total Revenue	\$ 452,791	\$ 1,449,506	\$ 2,126,589

Direct product sales represent items in which the Company holds the patents and/or copyrights to the characters and which are manufactured and sold by the Company directly at wholesale to retail stores and outlets. The increase of the six month period ending June 30, 2009 versus the twelve month period ending December 31, 2008, was due in part to sales of approximately \$623,000 in remainder inventory received from the various settlement agreements. Exclusive of these items, direct sales were approximately \$722,000. Included in this growth are retail outlets previously managed by Genius

Products, Inc. that have converted to direct sales subsequent to the termination of the distribution agreement as of December 31, 2008. Management believes that the Company is on target to meet the sales projection of \$3 million for 2009, although economic and retail conditions in the market could impact our future sales in a negative manner.

Licensing and royalty revenue is subject to reporting inconsistency from representative firms and are recorded as revenue when received. Management is working with the involved firms to improve the timeliness of the revenue recognition. There may be fluctuation in licensing revenue due to economic conditions in the sales territory. A significant factor in the reduction of royalty revenue versus 2008 is the result of the cancellation of the Genius Products, Inc. distribution agreement. Due to the terms of the agreement, revenue from sales of our products by Genius Products was booked net of all expenses as a royalty. Not all outlets have converted to direct distribution as yet, and there continue to be additional sales opportunities as a result, although it is possible that retailers will choose not to include our product line.

Our products compete in the pre-school music and DVD categories. We believe we compare favorably in the quality of our products, as well as competitive price point. In spite of the global economic decline we exhibited a significant growth in revenue both in the first two quarters of 2009 and the year 2008. We continue to aggressively market direct to retailers and are exploring new international licensing opportunities. We are investigating additional relevant external brands to license, adding to the diversity of our product line, while maintaining the integrity of our core mission of educating and entertaining children.

The Company's business is subject to the effects of seasonality, causing revenues to fluctuate with consumer purchasing behavior, competition, and the timing of holiday periods.

The 2009 economic outlook remains unclear, however, we anticipate continued sales growth through our actions to improve our existing products, maintaining highly competitive price points, and adding content to our product pallet.

**Costs.** Selling, General and Administrative (SG&A) expenses consist primarily of salaries, employee benefits and stock based compensation as well as other expenses associated with executive management, finance, legal, facilities, marketing, rent, and other professional services. Costs associated with these categories are detailed as follows:

	<b>Three Months</b>	<b>Six Months</b>	<b>Twelve Months</b>
	<b>Ending</b>	<b>Ending</b>	<b>Ending</b>
	<b>6/30/2009</b>	<b>6/30/2009</b>	<b>12/31/2008</b>
General and Administrative	\$ 491,101	\$ 1,153,648	\$ 1,837,917
Marketing and Sales	73,887	175,982	324,156
Product Development	8,637	9,176	34,008
Total Selling, General, and Administrative	<u>\$ 573,625</u>	<u>\$ 1,338,806</u>	<u>\$ 2,196,081</u>

General and administrative costs for the six months ending June 30, 2009 include \$243,270 in Stock Compensation Expense, \$163,260 for Accounting Services, \$45,272 for Legal Services and \$35,000 increases for Salaries. As the result of a voluntary salary reduction effective April 1, 2009, the employment agreements with officers of the Company were reduced by a combined \$70,000 per quarter until further notice, subject to return to the contractual levels upon notice from the officers. See Note 10:

Employment Agreements for additional information. Expenditures for SG&A are not generally seasonal and require consistent cash outflows.

The stock compensation expense, for options granted at 110% of current market price to officers of the Company with a two year vesting period, was valued using the Black-Scholes model as required by SFAS 123-R. In 2009, \$486,539 of stock compensation expense will be recorded in quarterly increments of \$121,635. There is no cash outflow associated with the granting of the options or recognition of the expense. A complete discussion of the subject can be found in Note 9: Stock Options in the notes to the financial statements.

Accounting services expenditures are primarily related to outside accounting firm fees for audits performed for the years 2007 and 2008 charged in 2009 (\$82,352) and 2008 (\$31,058). It is expected that the fees for future audits will be substantially less as the audits will be performed annually and improved processes have been implemented. The Company also engaged outside accounting services for support to the daily operational activities and special projects with an additional expenditure for these services of \$80,908 for the six month period ending June 30, 2009.

Legal services expenditures are primarily attributable to our Disclosure Statement filing with the Financial Investment Regulatory Agency (FINRA) to establish a secondary trading market on the Pink Sheets Electronic Market system and activities caused by the bankruptcy of a licensee and subsequent recapture of inventory.

Marketing and sales expenses include trade shows, public relations firms, and personal contact. Marketing expenses exhibit some fluctuation earlier in the year due to timing of trade shows, with a \$33,801 charge in the six month period ending June 30, 2009.

Product development charges are for routine and periodic alterations to existing products. All costs for new product development and significant improvements to existing products are capitalized in accordance with FASB #2, Accounting for Research and Development Costs.

**Interest Expense.** Interest expense resulted from related party loans and debentures. A full discussion of the related party notes payable and debentures issued can be located in Note 4: Notes Payable with the subsequent conversion of the full amount of the debentures to common stock disclosure in Note 5: Shareholders Equity. As part of the agreement for conversion of the debentures to common stock, interest expense continues to accrue on the full amount of the debentures, payable in common stock at a rate of 1 share per \$.40 of interest, until a secondary trading market is created. On June 2, 2009, the Company, through Glendale Securities, Inc. of Sherman Oaks, California as broker-dealer, filed a Disclosure Statement with the Financial Investment Regulatory Agency (FINRA) pursuant to Rule 15c2-11 of the Securities and Exchange Act of 1934, as amended, to establish a secondary trading market on the Pink Sheets Electronic OTC Markets system. The application was cleared for un-priced quotations on July 13, 2009 and the debenture interest was terminated on July 24, 2009.

## **Liquidity and Capital Resources**

### *Six Month Period Ended June 30, 2009 Compared to Fiscal Year Ended December 31, 2008*

Cash and cash equivalents totaled \$131,518 and \$547,724 at June 30, 2009 and December 31, 2008 respectively. The change in cash and cash equivalents is as follows:

	<b>Six Months</b>	<b>Twelve Months</b>	
	<b>Ending</b>	<b>Ending</b>	
	<b>6/30/2009</b>	<b>12/31/2008</b>	<b>Change</b>
Cash provided/(used) by operations	(24,565)	367,851	(392,416)
Cash provided/(used) in investing activities	(77,072)	(99,513)	22,441
Cash provided/(used) in financing activities	(314,569)	216,760	(531,329)
Increase/(decrease) in cash and cash equivalents	(416,206)	485,098	(901,304)

Our cash flow is very seasonal and a vast majority of our sales historically occur in the last two quarters of the year as retailers expand inventories for the holiday selling season. Cash provided by operations decreased \$24,565 primarily due to a longer Accounts Receivable collection cycle on remainder sales mitigated by accrued, unpaid officers' salaries, while a reduction in the cash used in investing activities was related to limited expenditures for new product development. Cash was used for financing activities as repayment was made on a portion of the related party notes payable, offset in part by sales of common stock to accredited investors prior to the suspension of the Private Placement Memorandum.

Management believes that its increasing sales and cash generated by operations, together with funds available from short-term related party advances, will be sufficient to fund planned operations for the next twelve months. However, there can be no assurance that operations and operating cash flows will continue at the current levels or improve in the near future. If the Company is unable to obtain profitable operations and positive operating cash flows sufficient to meet scheduled debt obligations, it may need to seek additional funding through equity and related party loans or be forced to scale back its development plans or to significantly reduce or terminate operations.

### **Critical Accounting Policies**

The Company's accounting policies are described in Note 1: The Company and Significant Accounting Policies of the notes to the Company's financial statements. Below is a summary of the critical accounting policies, among others, that management believes involve significant judgments and estimates used in the preparation of its financial statements.

*Revenue Recognition* – Revenues associated with the sale of branded CDs, DVDs and other products, are recorded when shipped to customers pursuant to approved customer purchase orders resulting in the transfer of title and risk of loss. Cost of sales, rebates and discounts are recorded at the time of revenue recognition or at each financial reporting date.

The Company's licensing and royalty revenue represent variable payments based on net sales from brand licensees for exclusive content distribution rights. These license agreements are held in conjunction with third parties that are responsible for collecting fees due and remitting to the Company its share after expenses.

*Other Estimates* – The Company estimates reserves for future returns of product based on an analysis that considers historical returns, changes in customer demand and current economic trends. The Company regularly reviews the outstanding Accounts Receivable balances for each account and monitors delinquent accounts for collectability. The Company reviews all intangible assets periodically to determine if the value has been impaired by recent financial transactions using the discounted cash flow analysis of revenue stream for the estimated life of the assets.

Management's Discussion and Analysis of financial Condition and Results of Operations discusses the Company's financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of the revenues and expenses during the reporting period. The Company continually evaluates the policies and estimates that it uses to prepare its financial statements. In general, management's estimates and assumptions are based on historical experience, known trends or events, information from third-party professionals and other factors that are believed to be reasonable under the circumstances, the results of which form the basis for making the judgments about carrying values of assets and liabilities. Actual results may differ from these estimates under different assumptions and conditions.

#### **Off Balance Sheet Arrangements**

The Company has no off balance sheet arrangements.

#### **Item V. Legal Proceedings.**

There are no current or past, pending or threatened legal proceedings or administrative actions either by or against the Company that could have a material effect on its business, financial condition or operations, and there are no current, past or pending suspensions by any securities regulator.

#### **Item VI. Defaults Upon Senior Securities.**

Not applicable.

#### **Item VII. Other Information.**

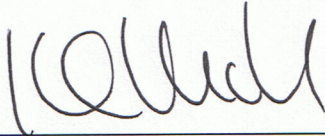
The change in the number of outstanding shares as of June 30, 2009 from March 31, 2009 were due to the late issuance of 100,000 shares which were sold pursuant to our private placement memorandum and previously authorized, but were not issued until May 8, 2009.

**Item IX. Certifications.**

I, Klaus Moeller, certify that:

1. I have reviewed this quarterly report of Pacific Entertainment Corporation;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the periods covered by this disclosure statement; and
3. Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this disclosure statement.

Date: August 17, 2009



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Klaus Moeller, Chief Executive Officer and  
Chief Financial Officer of Pacific Entertainment  
Corporation

**PACIFIC ENTERTAINMENT CORPORATION  
COMPARATIVE FINANCIAL STATEMENTS  
AS OF AND FOR THE PERIOD ENDING  
JUNE 30, 2009 (Unaudited)**

## TABLE OF CONTENTS

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	<u>Page No.</u>
FINANCIAL STATEMENTS	
Balance Sheets	3
Statements of Operations Period Ending, June 30	4
Statements of Stockholders' Equity (Deficit)	5
Statements of Cash Flows	6
Notes to Financial Statements	7

**Pacific Entertainment Corporation**  
**Balance Sheets**  
**June 30, 2009 (Unaudited) and December 31, 2008**

	<u>ASSETS</u>	<u>06/30/2009</u>	<u>12/31/2008</u>
Current Assets:			
Cash		\$ 131,518	\$ 547,724
Accounts Receivable, net		518,735	609,929
Inventory		214,987	311,005
Prepaid and Other Assets		132,851	31,941
Total Current Assets		998,091	1,500,599
Property and Equipment, net		38,131	31,916
Capitalized Product Development		61,973	243,238
Intangible Assets, net		1,273,640	1,327,494
<b>Total Assets</b>		<b>\$ 2,371,835</b>	<b>\$ 3,103,247</b>
<b><u>LIABILITIES AND STOCKHOLDERS'</u></b>			
<b><u>EQUITY (DEFICIT)</u></b>			
Current Liabilities:			
Accounts Payable		\$ 573,507	\$ 511,563
Accrued Expenses		131,563	100,135
Accrued Salaries and Wages		1,363,370	1,218,381
Accrued Stock Compensation			810,898
		-	
Accrued Interest - Debentures		80,552	15,552
Notes Payable – Related Party		729,450	1,106,185
Total Current Liabilities		2,878,442	3,762,714
<b>Total Liabilities</b>		<b>2,878,442</b>	<b>3,762,714</b>
Stockholders' Equity (Deficit)			
Common Stock, no par value, 100,000,000 shares authorized; 54,332,500 and 53,932,500 shares issued and outstanding, respectively		3,089,665	2,945,234
Additional Paid in Capital		1,684,181	619,681
Accumulated Deficit		(5,280,453)	(4,224,382)
Total Stockholders' Equity (Deficit)		(506,607)	(659,467)
<b>Total Liabilities &amp; Stockholders' Equity (Deficit)</b>		<b>\$ 2,371,835</b>	<b>\$ 3,103,247</b>

See accompanying notes to financial statements

**Pacific Entertainment Corporation**  
**Statements of Operations**  
**Periods Ending June 30, 2009 (Unaudited) and December 31, 2008**

	<b>Three Months Ending 06/30/2009</b>	<b>Six Months Ending 06/30/2009</b>	<b>Twelve Months Ending 12/31/2008</b>
Revenues:			
Product Sales	\$ 389,883	\$ 1,371,790	\$ 1,100,798
Licensing & Royalties	62,908	77,716	1,025,791
Total Revenues	452,791	1,449,506	2,126,589
Cost of Sales	189,408	701,020	428,048
Gross Profit	263,383	748,486	1,698,541
Operating Expenses:			
Product Development	8,637	9,176	34,008
Professional Services	83,107	238,685	152,428
Rent Expense	32,238	59,088	71,959
Marketing & Sales	59,745	153,689	324,156
Depreciation & Amortization	151,893	303,200	600,628
Salaries and Related Expenses	239,396	563,415	1,027,019
Stock Compensation Expense	121,635	243,269	810,898
General & Administrative	29,666	73,084	111,312
Total Operating Expenses	726,317	1,643,606	3,132,408
Loss from Operations	(462,934)	(895,120)	(1,433,867)
Other Income (Expense):			
Other Income	32	495	2,559
Interest Expense	(62,645)	(126,074)	(249,928)
Interest Expense – Related Parties	(14,036)	(32,597)	(96,311)
Gain on Settlement of Debt	-	-	42,261
Loss on Disposition of Intangible Assets	-	(2,775)	(9,028)
Net Other Income (Expense)	(76,649)	(160,951)	(310,447)
Loss before Income Taxes	(539,583)	(1,056,071)	(1,744,314)
Income Tax	-	-	-
Net Loss	\$ (539,583)	\$(1,056,071)	\$(1,744,314)
Net Loss per common share	\$ (0.01)	\$ (0.02)	\$ (0.04)
Weighted average shares outstanding	54,290,742	54,163,163	46,964,959

**See accompanying notes to financial statements**

**Pacific Entertainment Corporation**  
**Statements of Stockholders' Equity (Deficit)**  
**June 30, 2009 (Unaudited) and December 31, 2008**

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	<u>Common Stock</u>		Accumulated	Accumulated	Total
	Shares	Amount	Paid in Capital	Deficit	
Balance, December 31, 2008	53,932,500	2,945,234	619,681	(4,224,382)	(659,467)
Common Stock Issued for Cash	250,000	100,000			100,000
Common Stock Issued for Interest	150,000	60,000			60,000
Stock Offering Costs	-	(15,569)			(15,569)
Stock Compensation Expense	-	-	243,269		243,269
Stock Options Granted for Accrued Stock Compensation	-	-	810,898		810,898
Imputed Interest on Related Party Notes Payable	-	-	10,333		10,333
Net Loss	-	-	-	(1,056,071)	(1,056,071)
Balance, June 30, 2009	54,332,500	3,089,665	1,684,181	(5,280,453)	(506,607)

**See accompanying notes to financial statements**

**Pacific Entertainment Corporation**  
**Statements of Cash Flows**  
**Periods Ended and June 30, 2009 (Unaudited) and December 31, 2008**

	<b>Six Months Ending 06/30/2009</b>	<b>Twelve Months Ending 12/31/2008</b>
<b>Cash Flows from Operating Activities:</b>		
Net Loss	\$(1,056,071)	\$(1,744,314)
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation Expense	5,538	9,502
Amortization Expense	297,662	591,126
Loss on Disposal of Intangible Assets	2,775	9,028
Issuance of Common Stock for Interest	60,000	125,000
Capital Contribution Related Party Interest	10,333	21,963
Gain on Settlement of Debt	-	(42,261)
Stock Compensation Expense	243,269	-
Decrease (increase) in operating assets		
Accounts Receivable	(199,317)	(219,148)
Inventory	96,018	(302,724)
Prepaid Expenses & Other Assets	(29,210)	(16,469)
Other Receivable	218,811	194,425
Increase (decrease) in operating liabilities		
Accounts Payable	(17,910)	337,143
Accrued Salaries	144,466	542,678
Accrued Stock Compensation Expense	-	810,898
Accrued Interest	65,000	(50,568)
Accrued Interest – Related Party	22,265	41,322
Other Accrued Expenses	111,806	60,250
Net cash provided/(used) in operating activities	<u>(24,565)</u>	<u>367,851</u>
<b>Cash Flows from Investing Activities:</b>		
Investment in Product Masters	(65,318)	(96,414)
Purchase of Fixed Assets	(11,754)	(3,099)
Net cash provided/(used) by investing activities	<u>(77,072)</u>	<u>(99,513)</u>
<b>Cash Flows from Financing Activities:</b>		
Sale of Common Stock	100,000	223,000
Common Stock Offering Cost	(15,569)	(19,266)
Proceeds from Related Party Debt	1,000	590,000
Payments on Related Party Debt	(400,000)	(576,974)
Net cash provided/(used) by financing activities	<u>(314,569)</u>	<u>216,760</u>
Net increase/(decrease) in cash	(416,206)	485,098
Cash at December 31, 2008	547,724	62,626
Cash at June 30, 2009	<u>\$ 131,518</u>	<u>\$ 547,724</u>
Supplemental disclosures of cash flow information:		
Cash paid for interest	\$ -	\$ 207,254
Cash paid for income taxes	\$ -	\$ -
Schedule of non-cash financing activities:		
Conversion of Debentures to Common Stock	\$ -	\$ 2,500,000
Capital Contribution for extinguishment of related party debt	\$ -	\$ 597,718
Stock Options Granted for Accrued Stock Compensation	\$ 810,898	\$ -

**See accompanying notes to financial statements**

**Pacific Entertainment Corporation**  
**Notes to Financial Statements**  
**June 30, 2009 (Unaudited)**

**Note 1: The Company and Significant Accounting Policies**

*Organization and Nature of Business*

Pacific Entertainment Corporation (“we”, “us”, “our” or the “Company”) provides music-based products that are entertaining, educational and beneficial to the well-being of infants and young children. We create, market and sell children’s DVDs and CD music products in the United States by distribution at wholesale to retail stores and outlets. We license the use of our brands internationally to others to manufacture, market and sell the products, whereby we receive advances and royalties. The Company also licenses in select brands we feel we can market and sell through our distribution channels, such as “Guess How Much I Love You” and “The Snowman”. We recently added “Precious Moments” as a licensed product line and are creating three music CD’s with an estimated release in third quarter 2009.

The Company commenced operations on January 2, 2006. Through an Asset Purchase Agreement between our Chief Executive Officer, Klaus Moeller, and Genius Products, Inc., the rights and obligations of which was subsequently assumed by the Company, we obtained all rights, copyrights and trademarks to the brands “Baby Genius”, “Little Genius”, “Kid Genius” and “Wee Worship” (the “Brands”), and all then existing productions under those titles.

The Company’s Financial Statements are prepared in accordance with accounting principles generally accepted in the United States of America. These require the use of estimates and assumptions that affect the assets, liabilities, revenues and expenses reported in the financial statements, as well as amounts included in the notes thereto, including discussion and disclosure of contingent liabilities. Although the Company uses its best estimates and judgments, actual results could differ from these estimates as future confirming events occur.

*Interim Financial Statements*

The accompanying condensed financial statements of the Company have been prepared without audit or review. Certain information and disclosures required by accounting principles generally accepted in the United States have been condensed or omitted. These condensed financial statements reflect all adjustments that, in the opinion of management, are necessary to present fairly the results of operations of the Company for the periods presented. The results of operations for the three month and six month periods ended June 30, 2009, are not necessarily indicative of the results that may be expected for any future period or the fiscal year ending December 31, 2009.

The Company evaluated subsequent events through July 31, 2009. These financial statements should be read in conjunction with the financial statements included in the Company’s 2008 Annual Report.

*Liquidity*

Historically, the Company has incurred net losses and negative cash flows from operations. As of June 30, 2009, the Company had an accumulated deficit of \$5,280,453 and total stockholders’ deficit of \$506,607. At June 30, 2009, the Company had current assets of \$998,091, including cash and cash equivalents of \$131,518, and current liabilities of \$2,878,442, resulting in a working capital deficiency of \$1,880,351. The working capital deficiency includes \$1,675,958 in amounts due to the officers of the Company for accrued salaries and loans. These officers are also majority shareholders of the Company. For the three month period ending June 30, 2009, the Company reported a net loss of \$539,583, with a cumulative net loss of \$1,056,071 year to date through June 30, 2009. The Company had net cash used in operating activities of \$24,565. Management believes that its increasing sales and cash generated by operations, together with funds available from short-term related party advances, will be sufficient to fund planned operations for the next twelve months. However, there can be no assurance that operations and operating cash flows will continue at the current levels or improve in the near future. If the Company is unable to obtain profitable operations and positive operating cash flows sufficient to meet scheduled debt

**Pacific Entertainment Corporation**  
**Notes to Financial Statements**  
**June 30, 2009 (Unaudited)**

obligations, it may need to seek additional funding or be forced to scale back its development plans or to significantly reduce or terminate operations.

**Note 2: Plant, Property, and Equipment and Intangible Assets**

The Company has plant, property and equipment and other intangible assets used in the creation of revenue of the following as of June 30:

	<u>06/30/2009</u>	<u>12/31/2008</u>
Furniture and Equipment	\$ 61,196	\$ 49,443
Less Accumulated Depreciation	(23,065)	(17,527)
<b>Net Fixed Assets</b>	<b>\$ 38,131</b>	<b>\$ 31,916</b>
Trademarks	\$ 107,856	\$ 107,856
Website Development	17,000	-
Books	11,184	-
Product Masters	3,085,973	2,881,972
Other Intangible Assets	35,703	24,080
Less Accumulated Amortization	(1,984,076)	(1,686,414)
<b>Net Intangible Assets</b>	<b>\$ 1,273,640</b>	<b>\$ 1,327,494</b>

Pursuant to FASB 141, *Business Combinations*, FASB 142, *Goodwill and Other Intangible Assets*, and APB Opinion 29, *Accounting for Nonmonetary Transactions*, intangible asset(s) acquired either individually or with a group of other assets shall be initially recognized and measured based on fair value. In the acquisition of the assets from Genius Products, fair value was calculated using a discounted cash flow analysis of the revenue streams for the estimated life of the assets. As this resulted in a FMV in excess of the purchase price, the assets were recorded at \$2,489,082, the total purchase price discounted with the imputed interest rate of 10%. Further discussion of this transaction is found in Note 7: Related Party Transactions.

The Company reviews all intangible assets periodically to determine if the value has been impaired by recent financial transactions using the discounted cash flow analysis of revenue stream for the estimated life of the assets. At year end December 31, 2008, it was determined that no impairment exists.

The Company continues to develop new CDs and DVDs, in addition to adding content, improved animation and bonus songs/features to their existing CD and DVD collection. In accordance with Statement of Financial Accounting Standards #2, *Accounting for Research and Development Costs*, the costs of new product development and significant improvement to existing products are capitalized while routine and periodic alterations to existing products are expensed as incurred.

**Note 3: Accrued Liabilities**

Accrued but unpaid Salaries and Vacation benefits for the six month period ended June 30, 2009 total \$1,363,370 and \$1,218,381 for 2008, and include a reduction in the salary levels per agreement with the Officers effective April 1, 2009 (see Note 10: Employment Agreements). Debenture Interest accrued and unpaid for the original \$2.5 million principal balance is \$80,552 as of June 30, 2009 and \$15,552 in 2008. The increase was due to the suspension of stock share issuance during the application for listing on the Pink Sheet OTC. The shares were issued in July 2009 (see Note 11: Subsequent Events for additional information). Other accrued liabilities totaling \$131,563 as of June 30, 2009 and \$100,135 in 2008,

**Pacific Entertainment Corporation**  
**Notes to Financial Statements**  
**June 30, 2009 (Unaudited)**

include a reserve for product returns, music royalty payments and commissions to outside representatives on net sales. The reserve return was increased by \$56,000 due to prior returns notification of items sold in the current quarter. We anticipate that the product will be in recoupable condition and will be resold at full value once the product has been received and inspected. The remaining amounts are minor as royalties and commissions are generally paid when earned.

**Note 4: Notes Payable**

As of June 30, 2009 and December 31, 2008, the Company had the following notes payable balances outstanding:

	06/30/2009	12/31/2008
<b>Related Party Note to PEC</b>	\$ 346,829	\$ 333,361
<b>Officer Loans to PEC</b>	\$ 382,621	\$ 772,824

Notes were issued in favor of the Officers for loans to the Company at various times during 2009 and 2008. On February 13, 2009, the Officers agreed to an extension of the maturity date of all outstanding notes to December 31, 2009 at the stated interest rate of the original note. The term of the notes issued between September 2008 and January 2009 have a payment date of December 31, 2009 and a stated interest rate of 1.63%. The notes issued prior to September 2008 originally matured one year from the date of the note with a stated interest rate of 6%. The amounts stated include \$57,121 and \$48,324 in accrued but unpaid interest as of June 30, 2009 and December 31, 2008, respectively. In accordance with generally accepted accounting principles, stated interest rates on the related party notes were reviewed for compliance with APB 21, *Interest on Receivables & Payables*. As a result, imputed interest was calculated for a market rate of 7% in 2009 and 2008, resulting in Additional Paid in Capital contribution of \$32,292.

In 2006, the Company issued \$2.5 million in convertible debentures with a maturity date of December 31, 2010 to certain accredited investors. The debentures had a stated interest rate of 10% and a conversion rate of \$0.20 per share of common stock. Per review of EITF Abstract 98-5, Accounting for Convertible Securities with Beneficial Conversion Features or Contingently Adjustable Conversion Ratios, and EITF Abstract 00-27, Application of Issue No. 98-5 to Certain Convertible Instruments, the Company determined that the convertible debentures had no beneficial conversion option and intrinsic value because the conversion rate was set at the estimated fair market value of the Company's stock during 2006. In order to estimate the fair market value of the Company's common stock, the Company considered the following: During 2006 there was no public trading vehicle for the Company's common stock. During 2006 the company issued 40,000,000 founder shares to its four officers, for \$4,000 in cash or \$0.0001 per share. During 2006, the Company issued 562,500 shares of common stock for services valued at \$112,500, or \$0.20 per share. The fair market value of these shares issued for services were determined in accordance with EITF 00-19. The Company determined that the value of the services performed was the more readily determinable price for the shares, as there was not a current market for the common stock of Pacific Entertainment. The fair market value of these shares for services was determined to be \$0.20 per share. As the convertible debentures were issued with a \$0.20 per share conversion rate, which is the same price as determined for the shares issued for services, the Company concluded that there was no beneficial conversion option and no intrinsic value associated with the convertible debentures. On June 30, 2008, the entire \$2.5 million in convertible debentures were converted to common stock for a total of 12,500,000 shares, with a continued interest obligation payable in common stock of the Company until a secondary trading market is established. In 2007, these debentures constituted an unsecured, general obligation of the Company.

**Pacific Entertainment Corporation**  
**Notes to Financial Statements**  
**June 30, 2009 (Unaudited)**

On February 1, 2008, Isabel Moeller, sister of our Chief Executive Officer, Klaus Moeller, loaned \$310,000 to the Company at an interest rate equal to 8% per annum. The note originally provided that the Company was not obligated to pay any interest or principal on the note until all remaining amounts due to Genius under the Asset Purchase Agreement had been paid in full and, thereafter, required quarterly payments equal to 20% of net revenue until all principal and interest were paid. Since the amendment to the Distribution Agreement in August 2008, the note had been amended to require payment of all principal and accrued interest on June 30, 2009. An additional extension was executed on June 29, 2009 to require full payment on December 31, 2009. The funds were borrowed from Ms. Moeller in order to reduce outstanding obligations due to Genius at that time. The amount due to Ms. Moeller as of June 30, 2009 is \$346,829, including \$36,829 in accrued but unpaid interest due.

**Note 5: Stockholders' Equity**

As of June 30, 2009, 54,332,500 shares of common stock were outstanding out of the 100,000,000 shares of common authorized. During 2009, additional shares were sold subject to the Confidential Private Placement Memorandum offering of September 5, 2008, whereby the Company offered 25,000,000 shares of common stock to certain accredited investors. The shares were offered at a purchase price of \$0.40 per share. A total of 250,000 shares were sold for cash at a total investment of \$100,000. Offering costs were recognized and offset against the common stock account in the amount of \$15,569 for 2009.

The Company issued \$2.5 million in 10% debentures, which converted into shares of the Company's common stock at a conversion rate of one share for each \$.20 converted on June 30, 2008. The effect of this full conversion of the outstanding debentures was issuance of 12,500,000 shares. In addition, the terms of the conversion offering included the continued payment of interest in shares of stock at a rate of \$0.40 per share. However, due to our voluntary suspension of stock issuance pending the application to FINRA for inclusion in the Pink Sheets Electronic OTC Market system, the 150,000 shares, representing \$62,500 for interest due for the three months ended June 30, 2009, were not issued. The liability was recorded as accrued interest (see Note 3: Accrued Liabilities).

In addition, the officers were issued stock option grant notices on January 20, 2009 pursuant to the 2008 Stock Option plan and in accordance with the employment agreements entered into on January 1, 2008 of 8 million shares vesting over a period of two years. Additional information regarding this subject is found in Note 9: Stock Options.

**Note 6: Income Taxes**

The Financial Accounting Standards Board ("FASB") has issued Financial Interpretation No. 48, Accounting for Uncertainty in Income Taxes - An Interpretation of FASB Statement No.109 (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No. 109, Accounting for Income Taxes. FIN 48 requires a company to determine whether it is more likely than not that a tax position will be sustained upon examination based upon the technical merits of the position. If the more-likely-than-not threshold is met, a company must measure the tax position to determine the amount to recognize in the financial statements. As a result of the implementation of FIN 48, the Company performed a review of its material tax positions in accordance with recognition and measurement standards established by FIN 48.

At the adoption date of January 1, 2007, the Company had no unrecognized tax benefit which would affect the effective tax rate if recognized.

**Pacific Entertainment Corporation**  
**Notes to Financial Statements**  
**June 30, 2009 (Unaudited)**

The Company includes interest and penalties arising from the underpayment of income taxes in the statements of operations in the provision for income taxes. As of December 31, 2008, the Company had no accrued interest or penalties related to uncertain tax positions.

The Company files income tax returns in the U.S. federal jurisdiction and in the state of California. The Company is not subject to U.S. federal, state and local, or non-U.S. income tax examinations by tax authorities for years before 2006.

**Note 7: Related Party Transactions**

*Officer Loans*

Throughout 2009 and 2008, the Company borrowed \$1,000 and \$280,000 respectively from the Officers of the Company and issued promissory notes in favor of the Officers. Under the aforementioned notes, interest is due on the unpaid principal balance plus accrued but unpaid interest at an annual rate of one point sixty-three percent (1.63%) on the amounts added during the period September 2008 to January 2009, and six percent (6%) on notes prior to September 2008. The notes are payable on or before December 31, 2009. The proceeds from the notes were used to pay operating obligations of the Company. As of June 30, 2009 and December 31, 2008, an aggregate of \$382,621 and \$772,824, respectively, in principal and accrued interest expense were outstanding under the notes. See Note 4: Notes Payable for additional detail on these transactions.

*Genius Products Asset Purchase Agreement and Related Promissory Note*

On December 31, 2005, our Chief Executive Officer, Klaus Moeller, entered into an Asset Purchase Agreement with Genius Products, whereby he acquired all right, title and interest to the “Baby Genius”, “Kid Genius”, and “Wee Worship” brands, in addition to the titles “Child Genius” and “Little Genius” for a stated purchase price of \$3 million payable in installments of \$250,000 in cash at closing, \$750,000 by means of a full-recourse secured promissory note due and payable in full on January 30, 2006, bearing interest at 4.5% per annum, and \$2 million pursuant to a full-recourse secured promissory note due and payable in full, together with accrued interest, on the fifth anniversary of the date of closing with a stated interest rate of 4.5% per annum. The Company assumed all of the rights and obligations of the Asset Purchase Agreement through an amendment to the Agreement on January 6, 2006.

According to Generally Accepted Accounting Principles (GAAP), as required by FASB 57, *Related Party Disclosures* and APB 21, *Interest on Receivables & Payables*, it was determined and is hereby disclosed that this is a related party transaction based on Mr. Moeller’s prior tenure as an Officer and Board Member of Genius Products and his current position as an Officer, Board Member, and substantial shareholder of Pacific Entertainment. As such, a review of the 4.5% stated interest rate on the \$2 million promissory note was undertaken. As the Company also issued Debentures with a stated 10% interest rate at essentially the same time, the Company determined that 10% was a reasonable market rate available to the Company at the time of the purchase transaction. The fair market value of the note for accounting purposes was recorded on January 1, 2006 at \$1,489,082 based on the net present value of the \$2 million dollar face value due in 5 years, discounted at an imputed interest rate of 10%. As a result, the purchased value of the assets was recorded at \$2,489,082 on the Company’s books as of January 1, 2006. Related party interest expense was recorded related to this note in the amount of \$33,026 in 2008 and \$127,814 in 2007.

The payment of \$250,000 due on signing of the Agreement by Mr. Moeller and Genius Products was made by Mr. Moeller on December 31, 2005 and subsequently repaid by the Company in accordance with the terms of the Assumption Agreement. A payment of \$761,687, representing the principal due on January 30, 2006, along with any accrued interest then payable, was made on January 16, 2006 by the Company.

**Pacific Entertainment Corporation**  
**Notes to Financial Statements**  
**June 30, 2009 (Unaudited)**

The Company also entered into a Distribution Agreement with Genius Products for the sales, manufacture and distribution of our products which requires the Company pay a distribution fee of 20% of net sales made through Genius, plus a matching sum withheld and applied against the remaining balance of the second promissory note. Under the terms of the Distribution Agreement, Genius was retained as the Company's exclusive U.S. distributor of all sound and video recordings owned or controlled directly or indirectly by the Company at any time during the term of the distribution agreement. The Distribution Agreement had a term of 5 years but provided for earlier termination upon full payment of the purchase price under the Asset Purchase Agreement. During 2007, the payment amount applied to the Genius Products note payable balance was \$291,306 of which \$163,492 was applied to principal and the remaining \$127,814 of the payment was recorded as interest expense.

In June 2008 and December 2008, the Company negotiated settlements with Genius Products whereby the Note Payable from the Asset Purchase Agreement was deemed satisfied in full, inventory was transferred to the Company, and all amounts due to the Company from Genius Products and payable by the Company to Genius Products were relieved. In addition, the Distribution Agreement was terminated without penalty. The resultant income of \$835,190 from the transactions was recorded in 2008.

On February 1, 2008, Isabel Moeller, sister of our Chief Executive Officer, Klaus Moeller, loaned \$310,000 to the Company at an interest rate equal to 8% per annum. The note originally provided that the Company was not obligated to pay any interest or principal on the note until all remaining amounts due to Genius under the Asset Purchase Agreement had been paid in full and, thereafter, required quarterly payments equal to 20% of net revenue until all principal and interest were paid. Since the amendment to the Distribution Agreement in August 2008, the note had been amended to require payment of all principal and accrued interest on June 30, 2009. The maturity of the note was extended to December 31, 2009 by way of a second amendment dated June 29, 2009. The funds were borrowed from Ms. Moeller in order to reduce outstanding obligations due to Genius at that time.

**Note 8: Recent Accounting Pronouncements**

In June 2009, the FASB issued Statement of Financial Accounting Standards No. 166, *Accounting for Transfers of Financial Assets, an amendment to SFAS No. 140* (SFAS 166). SFAS 166 eliminates the concept of a qualifying special-purpose entity, changes the requirements for derecognizing financial assets including limiting the circumstances in which a company can derecognize a portion of a financial asset, and requires additional disclosures. SFAS 166 is effective for the Company's 2011 fiscal year. The Company does not believe that the adoption of SFAS 166 will have a material impact on its financial statements.

In June 2009, the FASB issued Statement of Financial Accounting Standards No. 167, *Amendments to FASB Interpretation No. 46(R)* (SFAS 167). SFAS 167 revises the approach to determining when an entity that is insufficiently capitalized or not controlled through voting rights (referred to as a variable interest entity or VIE) should be consolidated. The new consolidation model for VIEs considers whether the enterprise has the power to direct the activities that most significantly impact the VIE's economic performance and shares in the significant risks and rewards of the entity. SFAS 167 requires companies to continually reassess their involvement with VIEs to determine if consolidation is appropriate and provide additional disclosures about their involvement with them. SFAS 167 is effective for the Company's 2011 fiscal year. The Company does not believe that the adoption of SFAS 167 will have a material impact on its financial statements.

**Pacific Entertainment Corporation**  
**Notes to Financial Statements**  
**June 30, 2009 (Unaudited)**

**Note 9: Stock Options**

The Company has adopted the provisions of Statement of Financial Accounting Standards (“SFAS”) No. 123R, *Share Based Payments*, which requires companies to measure the cost of employee services received in exchange for equity instruments based on the grant date fair value of those awards and to recognize the compensation expense over the requisite service period during which the awards are expected to vest.

On May 6, 2007, the Company entered into a two-year employment agreement with its Vice President of Sales, Michael N. Ballard, pursuant to which Mr. Ballard was granted a non-statutory stock option which entitles him to purchase up to 400,000 shares of the Company’s common stock at an exercise price of \$0.01 per share. The option vests as to all 400,000 shares fifteen days following the end of the fiscal quarter in which the cumulative total of all revenue produced for the Company through direct sales by the V.P. of Sales equal \$10,000,000 or higher (the Revenue Threshold). The Revenue Threshold must be reached prior to May 6, 2009 in order for the option to vest. At the time of issuance, the Company and Mr. Ballard both believed that the stock options would never vest, and therefore the company did not record an expense associated with the grant, as the Company determined that the fair market value was of the 400,000 share options to be \$0.00. As of May 6, 2009, the agreement expired without renewal and the options have lapsed in their entirety.

In January of 2008, the Company entered into employment agreements with four of its officers. Pursuant to these agreements, the Company committed to issue options to purchase up to 8 million shares of the Company’s common stock. The options are to vest over a two-year period.

On December 29, 2008, the Company adopted the Pacific Entertainment Corporation 2008 Stock Plan (the “Plan”), which provides for the issuance of a variety of forms of equity awards, including stock options, restricted stock and stock appreciation rights to officers, directors, employees and other qualified persons. The Plan is administered by the Board of Directors of the Company or a committee appointed by the Board of Directors. The number of shares of the Company’s common stock initially reserved for issuance under the Plan is 11 million.

On January 20, 2009 the Company granted the 8 million stock options to its four officers as required by the employment agreements mentioned above. The options have a 5 year life, an exercise price of \$0.44, which in accordance with the 2008 Stock Option Plan is 10% above the current Fair Market value, and become fully vested at 12/31/2009. The Company used the Black-Scholes valuation model to estimate the grant date fair value of its stock options and warrants. The model requires various judgmental assumptions including estimated stock price volatility, forfeiture rates and expected life.

The Company’s calculations of the fair market value of each stock-based award that were granted, on January 20, 2009, used the following assumptions:

Risk-free interest rate	1.48%
Expected life in years	5
Dividend yield	0
Expected volatility	48.43%

Using the above assumptions the company calculated the fair market value of the 8,000,000 options on January 20, 2009 to be \$0.16 per option, or \$1,297,437 for all of the options granted. As the Company had the obligation to grant these stock options at the beginning of 2008 and the options were to vest partially during 2008 the Company accrued the Stock Compensation Expense of \$810,898 and recorded a liability to the four officers in the same amount as of December 31, 2008. This amount has been recognized as Additional Paid in Capital as of January 1, 2009. The remaining \$486,539 of stock

**Pacific Entertainment Corporation**  
**Notes to Financial Statements**  
**June 30, 2009 (Unaudited)**

compensation expense will be expensed in 2009 at a rate of \$121,635 on a quarterly basis, for a total of \$243,269 for the six months ended June 30, 2009.

**Note 10: Employment Agreements**

On January 1, 2008, the Company entered into Employment Agreements with the Officers of the Company for a term of five years, expiring on December 31, 2012. The agreements specify increasing annual salary amounts, car allowances, participation in benefit plans, vacations, and stock option plans, and severance benefits. The following is a schedule by year of the future minimum salary payments related to these employment agreements:

2008	\$ 685,600
2009	825,600
2010	885,600
2011	945,600
2012	1,025,600
Total	<u><u>\$4,368,000</u></u>

On June 30, 2009, the Board of Directors ratified and approved an offer by the Officers of a salary reduction to \$125,000 annually effective April 1, 2009 and continuing until further notice. The Officers can, at any time and effective on the date of notice, require that all future salary payments be returned to the level of the employment agreement in effect at that time.

**Note 11: Subsequent Events**

On June 2, 2009, the Company, through Glendale Securities, Inc. of Sherman Oaks, California as broker-dealer, filed a Disclosure Statement with the Financial Investment Regulatory Agency (FINRA) pursuant to Rule 15c2-11 of the Securities and Exchange Act of 1934, as amended, to establish a secondary trading market on the Pink Sheets Electronic OTC Markets system. Glendale Securities' request for un-priced quotation on the Pink Sheets was cleared by FINRA on July 13, 2009. The trading symbol is PENT.PK.

Pacific Entertainment entered into a licensing agreement with Precious Moments on July 10, 2009 granting the Company non-exclusive rights to use the Copyrights and Trademarks in connection with the manufacture, distribution, sale, and advertising of music CD's for children in exchange for royalty payments based on the net receipts from the licensed product. The term of the agreement is June 1, 2009 through December 31, 2012. The Company initially intends to produce three CD's for release in third quarter 2009.