

POWER EFFICIENCY CORP  
Form 10-Q  
May 15, 2008

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

**FORM 10-Q**

(Mark One)

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

**For the Quarterly Period Ended: March 31, 2008**

**OR**

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

**For the Transition Period from to  
Commission File No. 0-31805**

**POWER EFFICIENCY CORPORATION**

(Exact Name of Small Business Issuer as Specified in Its Charter)

Delaware  
(State or Other Jurisdiction of  
Incorporation or Organization)

22-3337365  
(I.R.S. Employer  
Identification No.)

3960 Howard Hughes Pkwy, Suite 460  
Las Vegas, NV 89169  
(Address of Principal Executive Offices)

(702) 697-0377  
(Issuer's Telephone Number,  
Including Area Code)

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

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

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

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

The number of shares of common stock outstanding as of May 13, 2008 was 40,411,858.

Transitional Small Business Disclosure Format (check one): Yes  No

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**PART I**  
**FINANCIAL INFORMATION**

**Item 1. Financial Statements**

**POWER EFFICIENCY CORPORATION**

**CONDENSED BALANCE SHEET**  
**Unaudited**

	March 31, 2008
<b>ASSETS</b>	
Current Assets:	
Cash	\$4,510,548
Accounts receivable, net	129,032
Inventory	133,441
Prepaid expenses and other current assets	113,777
Total Current Assets	4,886,798
Property and Equipment, Net	133,271
Other Assets:	
Patents, net	52,159
Deposits	80,833
Goodwill	1,929,963
Total Other Assets	2,062,955
Total Assets	\$7,083,024
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>	
Current Liabilities:	
Accounts payable and accrued expenses	\$451,507
Accrued salaries and payroll taxes	47,970
Total Current Liabilities	499,477
Long Term Liabilities	
Deferred Rent	12,063
Total Liabilities	511,540
Stockholders Equity:	
Series B Convertible Preferred Stock, \$.001 par value, 10,000,000 shares authorized, 140,000 issued or outstanding	140
Common stock, \$.001 par value, 140,000,000 shares authorized, 40,411,858 issued and outstanding	40,412
Additional paid-in capital	34,228,852
Accumulated deficit	(27,697,920)
Total Stockholders Equity	6,571,484
Total Liabilities and Stockholders Equity	\$7,083,024

*Accompanying notes are an integral part of the financial statements.*

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**POWER EFFICIENCY CORPORATION**

**CONDENSED STATEMENTS OF OPERATIONS**

**Unaudited**

	For the Three Months Ended March 31,	
	2008	2007
Revenues	\$ 133,695	\$ 36,615
Cost of Sales	98,163	34,639
Gross Profit	35,532	1,976
Costs and Expenses:		
Research and development	161,398	94,712
Selling, general and administrative	789,573	675,455
Depreciation and amortization	14,847	8,975
Total Costs and Expenses	965,818	779,142
Loss from Operations	(930,286 )	(777,166 )
Other Income (Expense):		
Interest income	42,130	12,320
Interest expense		(156,897 )
Total Other Income, net	42,130	(144,577 )
Net Loss	\$(888,156 )	\$(921,743 )
Basic and Fully Diluted Loss per Common Share	\$(0.02 )	\$(0.03 )
Weighted Average Common Shares Outstanding	40,393,007	36,765,138

*Accompanying notes are an integral part of the financial statements.*

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**POWER EFFICIENCY CORPORATION**

**CONDENSED STATEMENTS OF CASH FLOWS**

**Unaudited**

	For the Three Months Ended March 31,	
	2008	2007
Cash Flows from Operating Activities:		
Net loss	\$(888,156 )	\$(921,743 )
Adjustments to reconcile net loss to net cash used for operating activities:		
Depreciation and amortization	14,847	8,975
Amortization on capitalized manufacturing costs	1,377	
Debt discount related to issuance of debt securities		79,555
Warrants and options issued to employees and consultants	207,000	179,030
Amortization of deferred financing costs		3,368
Changes in assets and liabilities:		

Accounts receivable, trade	(19,780 )	(3,047 )
Inventory	(1,679 )	2,798
Prepaid expenses and other current assets	(73,858 )	(36,032 )
Deposits	41,430	
Accounts payable and accrued expenses	(86,981 )	(68,875 )
Customer Deposits	(1,605 )	
Net Cash Used for Operating Activities	(807,405 )	(755,971 )
Cash Flows from Investing Activities		
Costs related to patent applications	(12,661 )	
Purchase of property and equipment	(35,764 )	(36,780 )
Net Cash Used for Investing Activities	(48,425 )	(36,780 )
Cash Flows from Financing Activities:		
Proceeds from issuance of equity securities	280,000	1,025,000
Payments on notes payable		(8,332 )
Net Cash Provided by Financing Activities	280,000	1,016,668
(Decrease) Increase in cash	(575,830 )	223,917
Cash at beginning of period	5,086,378	1,693,584
Cash at end of period	\$4,510,548	\$1,917,510

*Accompanying notes are an integral part of the financial statements.*

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## POWER EFFICIENCY CORPORATION

# NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### Note 1 Basis of Presentation

The accompanying financial statements have been prepared by the Company, without an audit. In the opinion of management, all adjustments have been made, which include normal recurring adjustments necessary to present fairly the condensed financial statements. Operating results for the three months ended March 31, 2008 are not necessarily indicative of the operating results for the full year. 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. The Company believes that the disclosures provided are adequate to make the information presented not misleading. These unaudited condensed financial statements should be read in conjunction with the audited financial statements and related notes included in the Company's Annual Report for the year ended December 31, 2007 on Form 10-K and Form S-1.

The preparation of condensed financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

## **Note 2 Going Concern**

The accompanying financial statements have been prepared assuming the Company is a going concern, which assumption contemplates the realization of assets and satisfaction of liabilities in the normal course of business. The Company suffered recurring losses from operations, a recurring deficiency of cash from operations, including a cash deficiency of approximately \$807,000 from operations for the three months ended March 31, 2008. While the Company appears to have adequate liquidity at December 31, 2007, there can be no assurances that such liquidity will remain sufficient.

These factors raise substantial doubt about the Company's ability to continue as a going concern. The financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or the amount of liabilities that might be necessary should the Company be unable to continue in existence. Continuation of the Company as a going concern is dependent upon achieving profitable operations in the long-term and raising additional capital to support existing operations for at least the next twelve months. Management's plans to achieve profitability include developing new products, obtaining new customers and increasing sales to existing customers.

## **Note 3 Material Agreements**

On January 7, 2008, the Company entered into a consulting agreement with a European sales and marketing consultant. The agreement calls for the consultant to assist the Company in the business planning, and ultimately commercial development and marketing of the Company's Motor Efficiency Controller ( MEC ) line of products in Europe. For his services, the Company has agreed to pay the consultant 64,920 ICE per year, which is approximately equivalent to \$100,000 per year. In addition, the Company will reimburse all reasonable and necessary expenses incurred by the consultant. The initial term of this agreement is for 5 years, and can be terminated by either party upon 90 days written notice.

On January 23, 2008, the Company signed an efficiency aggregation contract with San Diego Gas & Electric Company ( SDG&E ). Under the terms of this contract, SDG&E will pay the Company \$0.14 per kWh of energy saved in the first year of operation of the MEC, for new installations of the MEC in SDG&E's service area. Payment to the Company is subject to certain inspections, approvals and time restrictions. The term of this contract is for 5 years, and either party may terminate this contract upon written notice.

## **Note 4 Issuance of Series B Convertible Preferred Stock**

On January 21, 2008, the Company issued and sold 5,600 units (the Units ), each Unit consisting of one share of the Company's Series B Preferred Stock, par value \$.001 per share ( Series B Preferred Stock ),

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## **POWER EFFICIENCY CORPORATION**

# **NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

## **Note 4 Issuance of Series B Convertible Preferred Stock (continued)**

and a warrant to purchase 50 shares of the Company's common stock, resulting in the sale and issuance of an aggregate of 5,600 shares of Series B Preferred Stock and warrants to purchase, initially, up to 280,000 shares of the Company's common stock (the Warrants), in a private offering for \$280,000 in cash.

In connection with the offering, the Company agreed to use its reasonable best efforts to file a registration statement (the Registration Statement) to register the common stock issuable upon conversion of the Series B Preferred Stock issued, as well as the common stock issuable upon exercise of the Warrants, not later than 60 days from the termination date of the Offering (the Termination Date), and must use its reasonable best efforts to have the Registration Statement declared effective not later than 120 days from the Termination Date.

Each share of Series B Preferred Stock is initially convertible into 100 shares of the Company's common stock, subject to adjustment under certain circumstances. The Series B Preferred Stock is convertible at the option of the holder at any time. The Series B Preferred Stock is also subject to mandatory conversion in the event the average closing price of the Company's common stock for any ten day period equals or exceeds \$1.00 per share, such conversion to be effective on the trading day immediately following such ten day period. The Series B Preferred Stock has an 8% dividend, payable annually in cash or stock, at the discretion of the Company's board of directors. As such, none is accredited in these financial statements.

The offering was conducted pursuant to an exemption from the registration requirements of the Securities Act of 1933, as amended, pursuant to Regulation D, Section 4(2) and Rule 506 thereunder. No placement agent or underwriter was used in connection with the Offering and there is no commission, finder's fee or other compensation due or owing to any party.

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## **Item 2. Management's Discussion and Analysis or Plan of Operation Overview**

The Company generates revenues from a single business segment: the design, development, marketing and sale of proprietary solid state electrical components designed to reduce energy consumption in alternating current induction motors.

The Company began generating revenues from sales of its patented MEC line of motor controllers in late 1995. As of March 31, 2008, the Company had total stockholders' equity of \$6,571,484 primarily due to (i) the Company's sale of 140,000 shares of Series B Convertible Preferred Stock in a private offering from October of 2007 through January of 2008, (ii) the Company's sale of 12,950,016 shares of common stock in a private stock offering from November of 2006 through March of 2007, (iii) the Company's sale of 14,500,000 shares of common stock in a private stock offering in July and August of 2005, (iv) the Company's sale of 2,346,233 shares of Series A-1 Convertible Preferred stock to Summit Energy Ventures, LLC in June of 2002 and (v) the conversion of notes payable of approximately \$1,047,000 into 982,504 shares of Series A-1 Convertible Preferred Stock in October of 2003.

## **Results of Operations for the Three Months Ended March 31, 2008 and 2007.**

### **Revenues**

Total revenues for the three months ended March 31, 2008 were approximately \$134,000 compared to \$37,000 for the three months ended March 31, 2007, an increase of \$97,000 or 262%. This increase is mainly attributable to an increase in sales in the elevator and escalator market segment. Specifically, sales in the first quarter of 2008 included approximately \$59,000 to major transit facilities and approximately \$10,000 to retail facilities. No such sales occurred during the first quarter of 2007.

### **Cost of Sales**

Total cost of sales, which includes material and direct labor and overhead for the three months ended March 31, 2008 were approximately \$98,000 compared to approximately \$35,000 for the three months ended March 31, 2007, an increase of \$63,000 or 180%. This increase in cost of sales is due to a higher volume of sales during the first quarter of 2008. As a percentage of sales, total cost of sales decreased to approximately 73% for the three months ended March 31, 2008 compared to approximately 95% for the three months ended March 31, 2007. The decrease in the costs as a percentage of sales was primarily due to the Company bringing the majority of its manufacturing in-house, which resulted in lower per unit production costs.

### **Gross Profit**

Gross profit for the three months ended March 31, 2008 was approximately \$36,000 compared to approximately \$2,000 for the three months ended March 31, 2007, an increase of \$34,000 or 1,700%. This increase was primarily due to a higher volume of sales during the first three months of 2008 and lower per unit production costs due to the Company bringing the majority of its manufacturing in-house.

### **Operating Expenses**

#### **Research and Development Expenses**

Research and development expenses were approximately \$161,000 for the three months ended March 31, 2008, as compared to approximately \$95,000 for the three months ended March 31, 2007, a \$66,000 or a 69% increase. This increase is mainly attributable to the Company's continued research and development efforts on its digital controller for both its single-phase and three-phase products, including additional personnel in the Company's research and development department, which resulted in higher salaries and related payroll costs, and the opening of a research and development center.

#### **Selling, General and Administrative Expenses**

Selling, general and administrative expenses were approximately \$790,000 for the three months ended March 31, 2008, as compared to \$675,000 for the three months ended March 31, 2007, an increase of \$115,000 or 17%. The increase in selling, general and administrative expenses compared to the prior year was primarily due to an increase in payroll, payroll related costs, and other cost related to SFAS 123R. These increases in expenses were due to the growth of the Company's sales force.

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**Financial Condition, Liquidity, and Capital Resources**

Since inception, the Company has financed its operations primarily through the sale of its equity securities, debt securities and using available bank lines of credit. As of March 31, 2008, the Company had cash of \$4,510,548.

Cash used for operating activities for the three months ended March 31, 2008 was \$807,405, which consisted of a net loss of \$888,156; less depreciation and amortization of \$14,847, amortization of capitalized manufacturing costs of \$1,377, warrants and options issued to employees and consultants of \$207,000 and a decrease in deposits of \$41,430, offset by increases in accounts receivable of \$19,780, inventory of \$1,679, prepaid expenses and other current assets of \$73,858, and decreases in accounts payable and accrued expenses of \$86,981 and customer deposits of \$1,605.

Cash used for operating activities for the three months ended March 31, 2007 was \$755,971, which consisted of: a net loss of \$921,743; less depreciation and amortization of \$8,975, debt discount related to the issuance of debt securities of \$79,555, warrants and options issued to employees and consultants of \$179,030, amortization of deferred financing costs of \$3,368, and a decrease in inventory of \$2,798; offset by increases in accounts receivable of \$3,047, and prepaid expenses and other current assets of \$36,032, and a decrease in accounts payable and accrued expenses of \$68,875.

Net cash used for investing activities for the three months ended March 31, 2008 was \$48,425, compared to \$36,780 for the three months ended March 31, 2007. The amount for the first quarter of 2008 consisted of the purchase of fixed assets of \$35,764, and capitalized costs related to patent applications of \$12,661. The total amount for the first quarter of 2007 consisted of the purchase of fixed assets.

Net cash provided by financing activities for the three months ended March 31, 2008 was \$280,000, which solely consisted of proceeds from the issuance equity securities. Net cash provided by financing activities for the three months ended March 31, 2007 was \$1,016,668, which consisted of the proceeds from the issuance of equity securities of \$1,025,000, offset by repayments of notes payable of \$8,332.

The Company expects to experience growth in its operating expenses, particularly in research and development and selling, general and administrative expenses, for the foreseeable future in order to execute its business strategy. As a result, the Company anticipates that operating expenses will constitute a material use of any cash resources.

Although we currently have over 12 months of working capital, management may need to sell additional equity or debt securities in order to continue to finance the Company's operations. The Company believes it can raise additional funds through private placements of equity or debt. However, there are no assurances that sufficient capital can be raised.

**Cash Requirements and Need for Additional Funds**

The Company anticipates a substantial need for cash to fund its working capital requirements. In accordance with the Company's prepared expansion plan, it is the opinion of management that approximately \$3.0 - \$3.6 million will be required to cover operating expenses, including, but not limited to, the development of the Company's next generation products, marketing, sales and operations during the next twelve months.

**Item 3. Quantitative and Qualitative Disclosures about Market Risk.**

The information in this Item is not being disclosed by Smaller Reporting Companies pursuant to Regulation S-K.

## Item 4T. Controls and Procedures

*(a) Evaluation of Disclosure Controls and Procedures.* Under the supervision and with the participation of its Chief Executive Officer and Chief Financial Officer, management has evaluated the effectiveness of the Company's disclosure controls and procedures as of the end of the period covered by this report pursuant to Rule 13a-15(b) under the Securities Exchange Act of 1934 (the Exchange Act). Based on that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures are effective in ensuring that information required to be disclosed in the Company's Exchange Act reports is (1) recorded, processed,

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summarized and reported in a timely manner, and (2) accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

*(b) Changes in Internal Controls.* There were no significant changes in the Company's internal controls or in other factors that could significantly affect these controls subsequent to the date of their evaluation, nor were there any significant deficiencies or material weaknesses in the Company's internal controls. Accordingly, no corrective actions were required or undertaken.

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## PART II OTHER INFORMATION

### Item 1. Legal Proceedings

None.

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

None.

### Item 3. Defaults Upon Senior Securities

None.

## Item 4. Submission of Matters to a Vote of Security Holders

None.

## Item 5. Other Information

None.

## Item 6. Exhibits

- 31.1 Certification by the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification by the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification by the Chief Executive Officer pursuant to Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002).
- 32.2 Certification by the Chief Financial Officer pursuant to Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002).

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## **SIGNATURES**

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

### **POWER EFFICIENCY CORPORATION (Company)**

By:

Date: May 15, 2008

/s/ Steven Strasser

Chief Executive Officer

By:

Date: May 15, 2008

/s/ John Lackland

Chief Financial Officer

(Principal Financial and Accounting Officer)

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