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

FORM 10-Q

(Mark One)
☒ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended **September 30, 2019**

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 number: 001-37960

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

Delaware	**33-0479020**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
249 E. Gardena Blvd., Gardena, California 90248	**90248**
(Address of principal executive offices)	(Zip Code)

(310) 830-9153
(Registrant's telephone number, including area code)

Not Applicable
(Former name, former address and former fiscal year, if changed since last report)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, par value $0.0001 per share	POLA	The NASDAQ Stock Market, LLC

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes ☒ No ☐

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

Large Accelerated Filer ☐	Accelerated Filer ☐
Non-Accelerated Filer ☐	Smaller Reporting Company ☒
	Emerging Growth Company ☒

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☒

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

The number of shares outstanding of the Registrant's common stock, $0.0001 par value, as of November 14, 2019 was 10,143,158.

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SPECIAL NOTE REGARDING FORWARD LOOKING STATEMENTS

This Quarterly Report on Form 10-Q, including without limitation the sections entitled “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and “Risk Factors,” contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. In some cases you can identify these statements by forward-looking words such as “believe,” “may,” “will,” “might,” “estimate,” “continue,” “anticipate,” “intend,” “could,” “should,” “would,” “project,” “plan,” “outlook,” “target,” “expect,” or similar expressions, or the negative or plural of these words or expressions.

Such forward-looking statements are based on current expectations and assumptions that are subject to risks and uncertainties, which could cause our actual results to differ materially from those reflected in the forward-looking statements. These statements appear throughout this Quarterly Report on Form 10-Q and are statements regarding our intent, belief, or current expectations, primarily based on our current assumptions, expectations and projections about future events and trends that we may affect our business, financial conditions, operating results, cash flows or prospects, as well as related industry developments. You should not place undue reliance on these forward-looking statements, which apply only as of the date of this Quarterly Report on Form 10-Q. Our actual results could differ materially from those anticipated in these forward-looking statements for many reasons, including the risks faced by us and described in Part II, Item 1A, entitled “Risk Factors,” and in “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in Part I, Item 2 of this Quarterly Report on Form 10-Q. We undertake no obligation to update any forward-looking statements for any reason, or to conform these statements to actual results or to changes in our expectations.

PART I – FINANCIAL INFORMATION

ITEM 1. Condensed Financial Statements

POLAR POWER, INC.
CONDENSED BALANCE SHEETS

	September 30, 2019 (Unaudited)	December 31, 2018
ASSETS		
Current assets		
Cash and cash equivalents (including restricted cash of $1,002,683 at December 31, 2018)	$ 3,666,475	$ 5,640,078
Accounts receivable	5,038,302	7,726,919
Inventories, net	14,142,895	8,471,769
Prepaid expenses	1,174,216	468,666
Refundable income taxes	231,444	715,916
Total current assets	24,253,332	23,023,348
Operating lease right-of-use assets, net	2,339,353	—
Property and equipment, net	2,242,210	2,122,757
Deposits	94,001	94,001
Total assets	$ 28,928,896	$ 25,240,106
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable	$ 856,656	$ 1,066,415
Customer deposits	228,268	79,184
Accrued expenses and other current liabilities	942,292	504,559
Current portion of operating lease liabilities	589,696	—
Current portion of notes payable	329,490	283,388
Total current liabilities	2,946,402	1,933,546
Operating lease liabilities, net of current portion	1,818,927	—
Notes payable, net of current portion	858,983	924,539
Total liabilities	5,624,312	2,858,085
Commitments and Contingencies		
Stockholders' Equity		
Preferred stock, $0.0001 par value, 5,000,000 shares authorized, no shares issued and outstanding	—	—
Common stock, $0.0001 par value, 50,000,000 shares authorized, 10,143,158 shares issued and outstanding	1,014	1,014
Additional paid-in capital	19,815,258	19,578,426
Retained earnings	3,488,312	2,802,581
Total stockholders' equity	23,304,584	22,382,021
Total liabilities and stockholders' equity	$ 28,928,896	$ 25,240,106

See Accompanying Notes to the Condensed Financial Statements

POLAR POWER, INC.
CONDENSED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	**2018**	**2019**	**2018**
Net Sales	$ 6,939,318	$ 5,061,158	$ 23,922,651	$ 15,748,845
Cost of Sales	4,707,412	3,530,847	16,336,576	10,672,707
Gross Profit	2,231,906	1,530,311	7,586,075	5,076,138
Operating Expenses				
Sales and marketing	707,171	717,983	2,032,643	1,968,152
Research and development	546,144	571,300	1,649,794	1,371,981
General and administrative	935,352	1,004,984	3,209,596	2,589,018
Total operating expenses	2,188,667	2,294,267	6,892,033	5,929,151
Income (loss) from operations	43,239	(763,956)	694,042	(853,013)
Other (expenses) income				
Interest expense	(13,676)	(2,777)	(34,389)	(8,181)
Other income (expense)	18,678	9,616	26,078	8,716
Total other (expenses) income, net	5,002	6,839	(8,311)	535
Net income (loss)	$ 48,241	$ (757,117)	$ 685,731	$ (852,478)
Net income (loss) per share – basic and diluted	$ 0.00	$ (0.07)	$ 0.07	$ (0.08)
Weighted average shares outstanding, basic and diluted	10,143,158	10,143,158	10,143,158	10,143,158

See Accompanying Notes to the Condensed Financial Statements

POLAR POWER, INC.
CONDENSED STATEMENTS OF STOCKHOLDERS' EQUITY
(Unaudited)

Three months ended September 30, 2019 (Unaudited)

	Common Stock		Additional paid-in	Retained	Total Stockholders'
	Number	Amount	capital	Earnings	Equity
Balance, June 30, 2019 (unaudited)	10,143,158	$ 1,014	$ 19,736,314	$ 3,440,071	$ 23,177,399
Fair value of vested stock options	—	—	78,944	—	78,944
Net income	—	—	—	48,241	48,241
Balance, September 30, 2019 (unaudited)	10,143,158	$ 1,014	$ 19,815,258	$ 3,488,312	$ 23,304,584

Nine months ended September 30, 2019 (Unaudited)

	Common Stock		Additional paid-in	Retained	Total Stockholders'
	Number	Amount	capital	Earnings	Equity
Balance, December 31, 2018	10,143,158	$ 1,014	$ 19,578,426	$ 2,802,581	$ 22,382,021
Fair value of vested stock options	—	—	236,832	—	236,832
Net income	—	—	—	685,731	685,731
Balance, September 30, 2019 (unaudited)	10,143,158	$ 1,014	$ 19,815,258	$ 3,488,312	$ 23,304,584

Three months ended September 30, 2018 (Unaudited)

	Common Stock		Additional paid-in	Retained	Total Stockholders'
	Number	Amount	capital	Earnings	Equity
Balance, June 30, 2018 (unaudited)	10,143,158	$ 1,014	$ 19,379,338	$ 3,555,472	$ 22,935,824
Fair value of vested stock options	—	—	103,664	—	103,664
Net income	—	—	—	(757,117)	(757,117)
Balance, September 30, 2018 (unaudited)	10,143,158	$ 1,014	$ 19,483,002	$ 2,798,355	$ 22,282,371

Nine months ended September 30, 2018 (Unaudited)

	Common Stock		Additional paid-in	Retained	Total Stockholders'
	Number	Amount	capital	Earnings	Equity
Balance, December 31, 2017	10,143,158	$ 1,014	$ 19,250,955	$ 3,650,833	$ 22,902,802
Fair value of vested stock options	—	—	232,047	—	232,047
Net loss	—	—	—	(852,478)	(852,478)
Balance, September 30, 2018 (unaudited)	10,143,158	$ 1,014	$ 19,483,002	$ 2,798,355	$ 22,282,371

See Accompanying Notes to the Condensed Financial Statements

POLAR POWER, INC.
CONDENSED STATEMENTS OF CASH FLOW
(Unaudited)

	Nine Months Ended September 30,	
	2019	**2018**
Cash flows from operating activities:		
Net income (loss)	$ 685,731	$ (852,478)
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Fair value of vested stock options	236,832	232,047
Depreciation and amortization	459,110	269,726
Amortization of operating lease right-of-use asset	390,713	—
Changes in operating assets and liabilities		
Accounts receivable	2,688,617	(692,891)
Inventories	(5,671,126)	(1,926,562)
Prepaid expenses	(819,437)	(599,382)
Deposits	—	(24,205)
Refundable income taxes	484,472	—
Accounts payable	(209,759)	31,795
Customer deposits	149,084	162,285
Accrued expenses and other current liabilities	468,042	97,324
Decrease in lease liability	(351,752)	—
Net cash used in operating activities	(1,489,473)	(3,302,341)
Cash flows from investing activities:		
Acquisition of property and equipment	(311,369)	(208,998)
Net cash used in investing activities	(311,369)	(208,998)
Cash flows from financing activities:		
Repayment of notes	(172,761)	(82,369)
Net cash used in financing activities	(172,761)	(82,369)
Decrease in cash and cash equivalents	(1,973,603)	(3,593,708)
Cash and cash equivalents, beginning of period	5,640,078	14,201,163
Cash and cash equivalents, end of period	$ 3,666,475	$ 10,607,455
SUPPLEMENTAL NON-CASH INVESTING AND FINANCING ACTIVITIES:		
Assets acquired through issuance of notes payable	$ 153,307	$ 662,750
Initial recognition of operating lease right-of-use assets and operating lease obligations upon adoption of ASC Topic 842	$ 2,847,495	$ —
Reclassification of prepaid expenses to property and equipment	$ 113,887	$ —

See Accompanying Notes to the Condensed Financial Statements

POLAR POWER, INC.
NOTES TO CONDENSED FINANCIAL
STATEMENTS FOR THE THREE AND NINE MONTHS
ENDED SEPTEMBER 30, 2019 AND 2018
(UNAUDITED)

NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Company

Polar Power, Inc. was incorporated in the State of Washington as Polar Products, Inc. and in 1991 reincorporated in the State of California under the name Polar Power, Inc. In December 2016, Polar Power, Inc. reincorporated in the State of Delaware (the "Company"). The Company designs, manufactures and sells direct current, or DC, power systems to supply reliable and low-cost energy to off-grid, bad-grid and backup power applications. The Company's products integrate DC generator and proprietary automated controls, lithium batteries and solar systems to provide low operating cost and lower emissions alternative power needs in telecommunications, defense, automotive and industrial markets.

Basis of Presentation of Unaudited Financial Information

The unaudited condensed financial statements of the Company for the three and nine months ended September 30, 2019 and 2018 have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") for interim financial information and pursuant to the requirements for reporting on Form 10-Q and Regulation S-K for scaled disclosures for smaller reporting companies. Accordingly, they do not include all the information and footnotes required by GAAP for complete financial statements. However, such information reflects all adjustments (consisting solely of normal recurring adjustments), which are, in the opinion of management, necessary for the fair presentation of the Company's financial position and results of operations. Results shown for interim periods are not necessarily indicative of the results to be obtained for a full fiscal year. The balance sheet information as of December 31, 2018 was derived from the audited financial statements included in the Company's financial statements as of and for the years ended December 31, 2018 and 2017 contained in the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission ("SEC") on April 1, 2019. These financial statements should be read in conjunction with that report.

Estimates

The preparation of financial statements in conformity with GAAP 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 date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Material estimates relate to the assumptions made in determining reserves for uncollectible receivables, inventory reserves and returns, impairment analysis of long-term assets and deferred tax assets, income tax accruals, accruals for potential liabilities and assumptions made in valuing the fair market value of equity transactions. Actual results may differ from those estimates.

Revenue Recognition

The Company recognizes revenue in accordance with ASU 2014-09, Revenue from Contracts with Customers (Topic 606), (ASC 606). The underlying principle of ASC 606 is to recognize revenue to depict the transfer of goods or services to customers at the amount expected to be collected. ASC 606 creates a five-step model that requires entities to exercise judgment when considering the terms of contract(s), which includes (1) identifying the contract(s) or agreement(s) with a customer, (2) identifying our performance obligations in the contract or agreement, (3) determining the transaction price, (4) allocating the transaction price to the separate performance obligations, and (5) recognizing revenue as each performance obligation is satisfied. Under ASC 606, revenue is recognized when performance obligations under the terms of a contract are satisfied, which occurs for us upon shipment or delivery of products or services to our customers based on written sales terms, which is also when control is transferred. Revenue is measured as the amount of consideration we expect to receive in exchange for transferring the products or services to a customer.

We determine whether delivery has occurred based on when title transfers and the risks and rewards of ownership have transferred to the customer, which usually occurs when we place the product with the customer's carrier or deliver the product to a customer's location. We regularly review our customers' financial positions to ensure that collectability is reasonably assured.

We recognize revenues from rental equipment on a straight-line basis over the rental period. Our rental contracts are fixed price contracts for fixed durations of time and include freight and delivery charges. Our rental revenues have not been significant to date and accounted for less than one percent of our total revenues for the three and nine months ended September 30, 2019 and 2018.

Disaggregation of Net Sales

The following table shows the Company's disaggregated net sales by product type:

	Three months ended September 30,	
	2019 (Unaudited)	**2018 (Unaudited)**
DC power systems	$ 6,713,525	$ 4,958,670
Engineering & Tech Support Services	63,011	39,445
Accessories	162,782	63,043
Total net sales	$ 6,939,318	$ 5,061,158

	Nine months ended September 30,	
	2019 (Unaudited)	**2018 (Unaudited)**
DC power systems	$ 23,146,223	$ 15,288,835
Engineering & Tech Support Services	232,998	69,667
Accessories	543,430	390,343
Total net sales	$ 23,922,651	$ 15,748,845

The following table shows the Company's disaggregated net sales by customer type:

	Three months ended September 30,	
	2019 (Unaudited)	**2018 (Unaudited)**
Telecom	$ 6,753,226	$ 4,246,099
Government/Military	39,822	659,912
Marine	—	32,016
Other (backup DC power to various industries)	146,270	123,131
Total net sales	$ 6,939,318	$ 5,061,158

	Nine months ended September 30,	
	2019 (Unaudited)	**2018 (Unaudited)**
Telecom	$ 22,497,099	$ 14,054,886
Government/Military	588,482	1,257,292
Marine	60,642	87,010
Other (backup DC power to various industries)	776,428	349,657
Total net sales	$ 23,922,651	$ 15,748,845

Accounts Receivable

Trade receivables are recorded at net realizable value consisting of the carrying amount less an allowance for uncollectible accounts, as needed. The Company uses the allowance method to account for uncollectible trade receivable balances. Under the allowance method, if needed, an estimate of uncollectible customer balances is made based upon specific account balances that are considered uncollectible. Factors used to establish an allowance include the credit quality and payment history of the customer. The Company did not deem it necessary to provide an allowance for doubtful accounts as of September 30, 2019 and December 31, 2018.

Inventories

Inventories consist of raw materials and finished goods and are stated at the lower of cost or market. Cost is determined principally on a first-in-first-out average cost basis. Inventory quantities on hand are reviewed regularly and write-downs for obsolete inventory are recorded based on an estimated forecast of the inventory item demand in the near future. As of September 30, 2019 and December 31, 2018, the Company has established inventory reserves of $330,000 for obsolete and slow-moving inventory. As of September 30, 2019 and December 31, 2018, the components of inventories were as follows:

	September 30, 2019 (Unaudited)	December 31, 2018
Raw materials	$ 9,654,350	$ 6,060,448
Finished goods	4,818,545	2,741,321
	14,472,895	8,801,769
Less: Inventory reserve	(330,000)	(330,000)
Total Inventories, net	**$ 14,802,895**	**$ 8,471,769**

Leases

Prior to January 1, 2019, the Company accounted for leases under ASC 840,*Accounting for Leases*. Effective January 1, 2019, the Company adopted the guidance of ASC 842, *Leases,* which requires an entity to recognize a right-of-use asset and a lease liability for virtually all leases. The Company adopted ASC 842 using a modified retrospective approach. As a result, the comparative financial information has not been updated and the required disclosures prior to the date of adoption have not been updated and continue to be reported under the accounting standards in effect for those periods. The adoption of ASC 842 on January 1, 2019 resulted in the recognition of operating lease right-of-use assets and lease liabilities for operating leases of $2,847,495. There was no cumulative-effect adjustment to accumulated deficit. See Note 9 for further information regarding the adoption of ASC 842.

Product Warranties

The Company provides limited warranties for parts and labor at no cost to its customers within a specified time period after the sale. The warranty terms are typically from one to five years. The Company's warranties are of an assurance-type and come standard with all Company products to cover repair or replacement should product not perform as expected. Provisions for estimated expenses related to product warranties are made at the time products are sold. These estimates are established using historical information about the nature, frequency and average cost of warranty claim settlements as well as product manufacturing and recovery from suppliers. Management actively studies trends of warranty claims and takes action to improve product quality and minimize warranty costs. The Company estimates the actual historical warranty claims coupled with an analysis of unfulfilled claims to record a liability for specific warranty purposes. The Company's product warranty obligations are included in other accrued liabilities in the balance sheets. As of September 30, 2019 and December 31, 2018, the Company had accrued a liability for warranty reserve of $175,000 and $175,000, respectively. Management believes that the warranty accrual is appropriate; however, actual claims incurred could differ from original estimates, requiring adjustments to the accrual. The Company does not provide any service warranties to its customers that require to be accounted for as a separate performance obligation.

The following is a tabular reconciliation of the product warranty liability:

Changes in estimates for warranties	September 30, 2019 (Unaudited)	December 31, 2018
Balance at beginning of the period	$ 175,000	$ 175,000
Payments	(381,301)	(364,163)
Provision for warranties	381,301	364,163
Balance at end of the period	**$ 175,000**	**$ 175,000**

Income Taxes

The Company accounts for income taxes using the asset and liability method whereby deferred tax assets are recognized for deductible temporary differences, and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized before the Company is able to realize their benefits, or that future deductibility is uncertain. As of September 30, 2019, the Company has sufficient net operating loss carryforwards to offset any taxable income during the period.

Tax benefits from an uncertain tax position are recognized only if it more likely than not that the tax position will be sustained on examination by the taxing authorities based on technical merits of the position. The tax benefits recognized in the financial statements from such a position are measured based on the largest benefit that has greater than 50 percent likelihood of being realized upon ultimate resolution. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment.

Financial Assets and Liabilities Measured at Fair Value

The Company uses various inputs in determining the fair value of its investments and measures these assets on a recurring basis. Financial assets recorded at fair value in the balance sheets are categorized by the level of objectivity associated with the inputs used to measure their fair value.

Authoritative guidance provided by the Financial Accounting Standards Board defines the following levels directly related to the amount of subjectivity associated with the inputs to fair valuation of these financial assets:

Level 1 Quoted prices in active markets for identical assets or liabilities.

Level 2 Inputs, other than the quoted prices in active markets, that is observable either directly or indirectly.

Level 3 Unobservable inputs based on the Company’s assumptions.

The carrying amounts of financial assets and liabilities, such as cash and cash equivalents, accounts receivable and accounts payable, approximate their fair values because of the short maturity of these instruments. The carrying values of the line of credit, notes payable approximate their fair values due to the fact that the interest rates on these obligations are based on prevailing market interest rates.

Segments

The Company operates in one segment for the manufacture and distribution of its products. In accordance with the “Segment Reporting” Topic of the ASC, the Company’s chief operating decision maker has been identified as the Chief Executive Officer and President, who reviews operating results to make decisions about allocating resources and assessing performance for the entire Company. Existing guidance, which is based on a management approach to segment reporting, establishes requirements to report selected segment information quarterly and to report annually entity-wide disclosures about products and services, major customers, and the countries in which the entity holds material assets and reports revenue. All material operating units qualify for aggregation under “Segment Reporting” due to their similar customer base and similarities in: economic characteristics; nature of products and services; and procurement, manufacturing and distribution processes. Since the Company operates in one segment, all financial information required by “Segment Reporting” can be found in the accompanying financial statements.

Concentrations

Cash. The Company maintains cash balances at five banks, with the majority held at one bank located in the U.S. At times, the amount on deposit exceeds the federally insured limits. Management believes that the financial institutions that hold the Company’s cash are financially sound and, accordingly, minimal credit risk exists.

Cash denominated in Australian Dollars with a U.S. Dollar equivalent of $15,257 and $152,254 at September 30, 2019 and December 31, 2018, respectively, was held in an account at a financial institution located in Australia. Cash denominated in Romanian Leu with a U.S. Dollar equivalent of $5,120 and $9,368 at September 30, 2019 and December 31, 2018, respectively, was held in an account at a financial institution located in Romania

Revenues. For the three months ended September 30, 2019, 84% and 7.5% of revenues were generated from the Company's two largest customers, which are Tier-1 telecommunications wireless carriers. For the same period in 2018, 39% and 37% of revenues were generated from the Company's two largest customers, both Tier-1 telecommunications wireless carriers. For the three months ended September 30, 2019 and September 30, 2018, sales to telecommunications customers accounted for 97% and 84% of total revenues, respectively.

For the nine months ended September 30, 2019, sales to the Company's two largest customers, which are Tier-1 telecommunications wireless carriers, accounted for 68% and 19% of total revenues, respectively. For the same period in 2018, the Company's three largest customers, which are Tier-1 telecommunications wireless carriers, accounted for 61%, 13% and 12% of total revenues, respectively. For the nine months ended September 30, 2019 and September 30, 2018, sales to telecommunications customers accounted for 97% and 89% of total revenues, respectively.

Accounts receivable. At September 30, 2019, 78% and 6% of the Company's accounts receivable were from the Company's two largest customers. At December 31, 2018, 45% and 42% of the Company's accounts receivable were from the Company's two largest customers.

Accounts payable. At September 30, 2019, accounts payable to the Company's largest vendor represented 35% while the other two largest vendors represented 10% and 7%, respectively. At December 31, 2018, accounts payable to the Company's largest vendor represented 71% while the other two largest vendors represented 3% each.

Purchases. The Company has established relationships with third party engine suppliers and other key suppliers from which the Company sources components for its power systems. The Company is substantially dependent on two key engine suppliers, Yanmar Engines Company. Purchases from Yanmar represented 53% and 48% of the Company's total cost of sales for the three months ended September 30, 2019 and 2018, respectively, and 44% and 76% for the nine months ended September 30, 2019 and 2018, respectively.

Net Income (Loss) Per Share

Basic net income (loss) per share is computed by dividing net income (loss) by the weighted average number of common shares outstanding for the period. Diluted earnings per share is computed by dividing the net income applicable to common stockholders by the weighted average number of common shares outstanding plus the number of additional common shares that would have been outstanding if all dilutive potential common shares had been issued using the treasury stock method. Potential common shares are excluded from the computation when their effect is antidilutive. The dilutive effect of potentially dilutive securities is reflected in diluted net income per share if the exercise prices were lower than the average fair market value of common shares during the reporting period.

The following potentially dilutive shares were excluded from the shares used to calculate diluted earnings per share as their inclusion would be anti-dilutive:

	September 30, 2019 (Unaudited)	September 30, 2018 (Unaudited)
Options	360,000	360,000
Warrants	115,000	115,000
Total	475,000	475,000

Recent Accounting Pronouncements

The Company’s management does not believe that there are any recently issued, but not yet effective, authoritative guidance, if currently adopted, would have a material impact on the Company’s financial statement presentation or disclosures.

NOTE 2 – RESTRICTED CASH

As of December 31, 2018, the Company’s cash balance included restricted cash of $1,002,683. In March 2019, the Company closed the credit facility securing the restricted cash account, and as such, no cash balance was restricted as of September 30, 2019. The restricted cash served as a collateral for the line of credit (see Note 5) opened with a bank in March 2017 and closed in March 2019.

NOTE 3 – PROPERTY AND EQUIPMENT

Property and equipment consist of the following:

	September 30, 2019 (Unaudited)	December 31, 2018
Production tooling, jigs, fixtures	$ 70,749	$ 70,749
Shop equipment and machinery	3,237,191	2,808,928
Vehicles	188,597	188,597
Leasehold improvements	390,004	276,901
Office equipment	172,192	134,995
Software	102,690	102,690
Total property and equipment, cost	4,161,423	3,582,860
Less: accumulated depreciation and amortization	(1,919,213)	(1,460,103)
Property and equipment, net	$ 2,242,210	$ 2,122,757

Depreciation and amortization expense on property and equipment for the three months ended September 30, 2019 and September 30, 2018 was $163,889 and $114,779, respectively. During the three months ended September 30, 2019 and September 30, 2018, $152,757 and $105,882, respectively, of the depreciation expense was included in the balance of cost of sales.

Depreciation and amortization expense on property and equipment for the nine months ended September 30, 2019 and September 30, 2018 was $459,110 and $269,726, respectively. During the nine months ended September 30, 2019 and September 30, 2018, $428,290 and $243,285, respectively, of the depreciation expense was included in the balance of cost of sales.

NOTE 4 – NOTES PAYABLE

Notes payable consist of the following:

	September 30, 2019 (Unaudited)	December 31, 2018
Total Equipment Notes Payable	$ 1,188,473	$ 1,207,927
Less Current Portion	329,490	283,388
Notes Payable, long term	$ 858,983	$ 924,539

The Company has entered into several financing agreements for the purchase of equipment. The terms of these financing arrangements are for a term of 2 years to 5 years, with interest rates ranging from 1.9% to 6.9% per annum, secured by the purchased equipment. Aggregate monthly payments of principal and interest of approximately $29,000 are due through 2023.

NOTE 5 –FINANCING AGREEMENTS

Line of Credit

On March 21, 2017, the Company entered into a Credit Agreement and related documents with Citibank, N.A. for a revolving credit facility in the aggregate amount of up to $1,000,000. The credit facility was secured by a Certificate of Deposit (restricted cash) account opened by the Company with Citibank in the amount of $1,000,000 (see Note 2). On March 20, 2019, the Company terminated the credit facility and transferred the balance of the Certificate of Deposit that secured the credit facility to its liquid cash account. As of March 20, 2019, the Company had not borrowed any funds under the credit facility.

Supplier Agreement

Effective June 4, 2019, the Company executed a Supplier Agreement with Citibank, N.A. Under the terms of the Supplier Agreement, the Company may from time to time offer to sell to Citibank, without recourse, certain of the Company's accounts receivable relating to invoiced sales made to AT&T. Once AT&T approves the invoice, AT&T sends payment instructions to Citibank. The sale price is equal to the face amount of the receivable less the applicable discount charge calculated by multiplying the face amount of the receivable by (i) the annual discount rate (which is equal to the 90-day London Inter-bank Offered Rate plus 1.00%) and (ii) the discount acceptance period (which is equal the number of days in the payment terms less the number of days necessary to approve the invoice) divided by 360.

Citibank may change the pricing terms at any time in its sole discretion upon at least thirty days prior written notice to the Company. In addition, either party may terminate the Supplier Agreement upon thirty business days prior written notice to the other party, provided that either party may terminate the agreement upon five business days prior written notice if the other party is in breach of, or fails to perform any of its material obligations under the Supplier Agreement. For the three and nine months ended September 30, 2019, a total of $4,113,621 and $9,367,112, respectively, of accounts receivables were sold to Citibank by the Company, and the Company incurred fees of approximately $20,000 and $42,000, respectively, during the periods then ended.

NOTE 6 – STOCK OPTIONS

The following table summarizes stock option activity:

	Number of Options	Weighted Average Exercise Price
Outstanding, December 31, 2018	360,000	$ 5.28
Granted	—	—
Exercised	—	—
Outstanding, September 30, 2019 (unaudited)	360,000	$ 5.28
Exercisable, September 30, 2019 (unaudited)	140,000	$ 5.28

Effective July 8, 2016 the Company's board of directors approved the Polar Power 2016 Omnibus Incentive Plan (the "2016 Plan"), authorizing the issuance of up to 1,754,385 shares of common stock as incentives to employees and consultants to the Company with awards limited to a maximum of 350,877 shares in any calendar year.

During the nine months ended September 30, 2019, the Company expensed total stock-based compensation related to the vested options of $236,832, and the remaining unamortized cost of the outstanding options at September 30, 2019 was approximately $474,000. This cost will be amortized on a straight-line basis over the weighted average remaining vesting period of 2 years.

There was no intrinsic value of the outstanding and exercisable options at September 30, 2019.

NOTE 7 – WARRANTS

At September 30, 2019, warrant shares outstanding were as follows:

	Number of Warrants	Weighted Average Exercise Price
Outstanding September 30, 2018	115,000	$ 8.75
Issued	—	—
Exercised	—	—
Outstanding, September 30, 2019 (unaudited)	115,000	$ 8.75
Exercisable, September 30, 2019 (unaudited)	115,000	$ 8.75

In connection with the Company's underwritten initial public offering in December 2016, the Company issued warrants to the underwriters to purchase up to 115,000 shares of its common stock with an exercise price of $8.75 per share, which warrants expire five years from the date of issuance.

There was no intrinsic value of the outstanding and exercisable warrants at September 30, 2019.

NOTE 8 – DISTRIBUTION AGREEMENT WITH A RELATED ENTITY

On March 1, 2014, the Company entered into a subcontractor installer agreement with Smartgen Solutions, Inc. ("Smartgen"), a related entity that is engaged in business of equipment rental and provider of maintenance, repair and installation services to mobile telecommunications towers in California. Under the terms of the agreement, Smartgen has been appointed as a non-exclusive, authorized service provider for the installation, repair and service of the Company's products in Southern California. The agreement has a term of three years from the date of execution and automatically renews for additional one-year periods if not terminated.

During the three months ended September 30, 2019 and 2018, Smartgen performed $54,270 and $26,550 in field services, respectively. Smartgen performed $227,030 and $71,820 in field services for the nine months ended September 30, 2019 and 2018, respectively.

Smartgen had no purchases from the Company during the three months and the nine months ended September 30, 2019 and September 30, 2018, respectively.

NOTE 9 – LEASE OBLIGATIONS

The Company has operating lease agreements for two office spaces both with remaining lease terms of 4 years. The Company also has another storage facility on a twelve-month lease term. Leases with an initial term of 12 months or less are not recorded on the balance sheet. The Company accounts for the lease and non-lease components of its leases as a single lease component. Rent expense is recognized on a straight-line basis over the lease term.

Operating lease right-of-use ("ROU") assets and liabilities are recognized at commencement date based on the present value of lease payments over the lease term. ROU assets represent our right to use an underlying asset for the lease term and lease liabilities represent our obligation to make lease payments arising from the lease. Generally, the implicit rate of interest in arrangements is not readily determinable and the Company utilizes its incremental borrowing rate in determining the present value of lease payments. The Company's incremental borrowing rate is a hypothetical rate based on its understanding of what its credit rating would be. The operating lease ROU asset includes any lease payments made and excludes lease incentives.

The components of rent expense and supplemental cash flow information related to leases for the period are as follows:

		Nine Months Ended September 30, 2019
Lease Cost		
Operating lease cost (of which $446,674 is included in general and administration and $77,927 is included in cost of sales in the Company's unaudited condensed statement of operations)	$	524,601
Other Information		
Cash paid for amounts included in the measurement of lease liabilities for the first quarter 2019	$	—
Weighted average remaining lease term – operating leases (in years)		3.7
Average discount rate – operating leases		3.75%

The supplemental balance sheet information related to leases for the period is as follows:

		At September 30, 2019
Operating leases		
Long-term right-of-use assets	$	2,339,353
Short-term operating lease liabilities	$	589,696
Long-term operating lease liabilities		1,818,927
Total operating lease liabilities	$	2,408,623

Maturities of the Company's lease liabilities are as follows (in thousands):

Year Ending		Operating Leases
2019 (remaining 3 months)	$	153,765
2020		692,977
2021		720,922
2022		746,752
2023		272,057
Total lease payments		2,586,473
Less: Imputed interest/present value discount		(177,849)
Present value of lease liabilities	$	2,408,624

Rent expense for the three months ended September 30, 2019 and 2018 was $203,395 and $158,734, respectively (including short-term and other rentals). Rent expense for the nine months ended September 30, 2019 and 2018 was $601,772 and 414,317, respectively (including short-term and other rentals).

ITEM 2. Management's Discussion And Analysis Of Financial Condition And Results Of Operations

You should read the following discussion and analysis of our financial condition and results of operations together with our financial statements and the related notes and other financial information included elsewhere in this Quarterly Report on Form 10-Q. In addition to historical information, this discussion and analysis contains forward-looking statements that involve risks, uncertainties and assumptions. Our actual results may differ materially from those discussed below. Factors that could cause or contribute to such differences include, but are not limited to, those identified below, and those discussed in the section titled "Risk Factors" and elsewhere in this report. Our historical results are not necessarily indicative of the results to be expected for any future period, and results for any interim period are not necessarily indicative of the results to be expected for the full year.

Overview

We design, manufacture and sell direct current, or DC, power systems for applications primarily in the telecommunications market and, to a lesser extent, in other markets, including military, electric vehicle charging, cogeneration, distributed power and uninterruptable power supply. With the introduction of new LPG / propane and natural gas line of generators and solar hybrid power systems we will expand our markets to include residential and commercial. We plan to sell tier 1 and 2 telecom as direct accounts with residential and commercial being sold through distribution. Within the telecommunications market, our DC power systems provide reliable and low-cost Electrical power to service applications that do not have access to the utility grid (i.e., prime power applications) or have critical power needs and cannot be without power in the event of utility grid failure (i.e., back-up power applications). Within this market, we offer the following three configurations of our DC power systems, with output power ranging from 5 kW to 32 kW:

- ***DC base power systems***. These systems integrate a DC generator and automated controls with remote monitoring, which are typically contained within an environmentally regulated enclosure.

- ***DC hybrid power systems***. These systems incorporate lithium-ion batteries (or other advanced battery chemistries) with our proprietary battery management system into our standard DC power systems.

- ***DC solar hybrid power systems***. These systems incorporate photovoltaic and other sources of renewable energy into our DC hybrid power system.

Our DC power systems are available in diesel, natural gas, LPG / propane, and renewable fuel formats. Diesel, natural gas and propane gas being the predominant formats.

The current transition of telecommunications cellular network technology from 3G and 4G to 5G and to "edge computing at the cell tower" (i.e., allowing data produced by IoT devices to be processed closer to where the data is created rather than transmitting the data across long routes to the cloud or to data centers) requires an increase in power and reliability. In that regard, our telecommunications customers have expressed a desire for us to develop new products to addresses this need for increased power while reducing or keeping the same volume of space at the cell site. An increase in the size of our products would result in the need for more space at cell sites which, in turn, would result in many of our customers being subjected to increased rent and permitting costs. We feel that its the tight space requirements that gives Polar a competitive advantage over competition. Commencing in 2019, we began demonstrating higher-power DC generators to our Tier-1 telecommunications customers that are the same weight and footprint of our current DC generators. AC generators can be up to twice the size and weight of our DC generators, which are based on permanent magnet technology.

Our business from domestic Tier-1 telecommunications customers, which we believe are in the early stages of a multiyear expansion cycle, is driven primarily by the need for network reliability. The telecom industry's capital investment to upgrade existing telecom sites with backup power systems is competing with the capital needs associated with the expansion of 5G and cell site edge computing networks. We believe these rollouts will significantly expand the use of data and video streaming services including IoT uses, telemedicine, autonomous vehicles, and industrial internet, thereby requiring robust backup systems that eliminate the smallest data disruptions. We believe our higher capacity backup systems, which we believe are more dense in terms of storage and power than backup systems offered by our competitors, will satisfy the needs of next generation cell sites.

During the first nine months of 2019, we focused our R&D efforts on developing environmentally friendly solar hybrid power systems based combining solar with LPG and natural gas, this technology lowers CAPEX and OPEX and carbon emissions.

Recently, we successfully completed EPA emissions testing of our LPG and natural gas generators that range in output from 10kW to 15kW and which incorporate an 30,000 to 90,000 hour life engine with our proprietary control system. We plan to market these stationary generators within the telecom, commercial and residential markets. In addition, the recent fires in California which resulted in power shutdowns for both commercial and residential customers has led to an increase in market opportunities for lower emission backup generators. In addition, we displayed our LPG generator at the 2019 WLPG global conference in Amsterdam and have received significant follow-up interest in jointly addressing the power needs in emerging markets.

During the third quarter of 2019, we experienced a slowdown in backup generator product orders within the Tier-1 telecom markets we serve. We believe this slowdown is combination of factors including a temporary shift in budgets for mergers and acquisitions, 5 G roll outs, and a result of our Tier-1 customers' evaluating the impact of 5G on their future power requirements. Specifically, our Tier-1 telecommunications customers are attempting to define the correct power output for future 5G sites which, in turn, has lead to slowdown in orders. We offer a complete line of telecom backup generators, ranging in output from 6kW to 20 kW. We anticipate sales of our backup generator products will increase shortly after our Tier-1 telecommunications customers define their product mix requirements. We have also accelerated our market and geographic diversification strategy to counter the volatility within the domestic Tier-1 telecommunications market. The introduction of our LPG product line, development of indirect sales infrastructure and introduction of target market specific product configurations are some of the key cornerstones of our diversification strategy.

Critical Accounting Policies

Our financial statements have been prepared in accordance with GAAP. The preparation of these financial statements requires us to make estimates and judgments that may have a significant impact on the portrayal of our financial condition and results of operations. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis of making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results could differ materially from these estimates.

We believe that the following critical accounting policies, among others, affect our more significant judgment and estimates used in the preparation of our financial statements:

Revenue Recognition. The Company recognizes revenue in accordance with ASC 2014-09, Revenue from Contracts with Customers (Topic 606), (ASC 606). The underlying principle of ASC 606 is to recognize revenue to depict the transfer of goods or services to customers at the amount expected to be collected. ASC 606 creates a five-step model that requires entities to exercise judgment when considering the terms of contract(s), which includes (1) identifying the contract(s) or agreement(s) with a customer, (2) identifying our performance obligations in the contract or agreement, (3) determining the transaction price, (4) allocating the transaction price to the separate performance obligations, and (5) recognizing revenue as each performance obligation is satisfied. Under ASC 606, revenue is recognized when performance obligations under the terms of a contract are satisfied, which occurs for us upon shipment or delivery of products or services to our customers based on written sales terms, which is also when control is transferred. Revenue is measured as the amount of consideration we expect to receive in exchange for transferring the products or services to a customer.

We determine whether delivery has occurred based on when title transfers and the risks and rewards of ownership have transferred to the customer, which usually occurs when we place the product with the customer's carrier or deliver the product to a customer's location. We regularly review our customers' financial positions to ensure that collectability is reasonably assured.

Under ASC 606, revenue is recognized when performance obligations under the terms of a contract are satisfied, which occurs for the Company upon shipment or delivery of products or services to our customers based on written sales terms, which is also when control is transferred. Revenue is measured as the amount of consideration we expect to receive in exchange for transferring the products or services to a customer.

Warranty Costs. We provide limited warranties for parts and labor at no cost to our customers within a specified time period after the sale. The warranty terms are typically from one to five years. The Company's warranties are of an assurance-type and come standard with all Company product to cover repair or replacement should a product not perform as expected. The Company's warranties are not a separate performance obligation and no transaction price is allocated to it. Provisions for estimated expenses related to product warranties are made at the time products are sold. These estimates are established using historical information about the nature, frequency and average cost of warranty claim settlements as well as product manufacturing and recovery from suppliers. Management actively studies trends of warranty claims and takes action to improve product quality and minimize warranty costs. We estimate the actual historical warranty claims coupled with an analysis of unfulfilled claims to record a liability for specific warranty purposes. Our product warranty obligations are included in other accrued liabilities in the balance sheets. As of September 30, 2019, and December 31, 2018, we had accrued a liability for warranty reserve of $175,000 and $175,000, respectively. Management believes that the warranty accrual is appropriate; however, actual claims incurred could differ from original estimates, requiring adjustments to the accrual. The Company does not provide any service warranties to its customers that require to be accounted for as a separate performance obligation.

Effects of Inflation

The impact of inflation and changing prices has not been significant on the financial condition or results of operations of our company.

Impact of New Accounting Pronouncements

See "Note 1 – Organization and Summary of Significant Accounting Policies – Recent Accounting Pronouncements" of the Notes to our condensed financial statements commencing on page 5 of this Quarterly Report on Form 10-Q.

Jumpstart Our Business Startups Act of 2012

On April 5, 2012, the JOBS Act was enacted. Section 107 of the JOBS Act provides that an "emerging growth company" can take advantage of the extended transition period provided in Section 7(a)(2)(B) of the Securities Act for complying with new or revised accounting standards. In other words, an "emerging growth company" can delay the adoption of certain accounting standards until those standards would otherwise apply to private companies. We have irrevocably elected not to avail ourselves of this extended transition period and, as a result, we will adopt new or revised accounting standards on the relevant dates on which adoption of such standards is required for other public companies.

We are in the process of evaluating the benefits of relying on other exemptions and reduced reporting requirements provided by the JOBS Act. Subject to certain conditions set forth in the JOBS Act, if as an "emerging growth company" we choose to rely on such exemptions, we may not be required to, among other things, (i) provide an auditor's attestation report on our system of internal controls over financial reporting pursuant to Section 404, (ii) provide all of the compensation disclosure that may be required of non-emerging growth public companies under the Dodd-Frank Wall Street Reform and Consumer Protection Act, (iii) comply with any requirement that may be adopted by the Public Company Accounting Oversight Board regarding mandatory audit firm rotation or a supplement to the auditor's report providing additional information about the audit and the financial statements (auditor discussion and analysis), and (iv) disclose certain executive compensation-related items such as the correlation between executive compensation and performance and comparisons of the Chief Executive Officer's compensation to median employee compensation. These exemptions will apply until we no longer meet the requirements of being an "emerging growth company." We will remain an "emerging growth company" until the earliest of (i) the last day of the fiscal year in which we have total annual gross revenues of $1.07 billion or more; (ii) the last day of our fiscal year following the fifth anniversary of the date of the completion of this offering; (iii) the date on which we have issued more than $1 billion in nonconvertible debt during the previous three years; or (iv) the date on which we are deemed to be a large accelerated filer under the rules of the SEC.

Financial Performance Summary and Outlook

Our net sales for the three and nine months ended September 30, 2019 were $6,939,318 and $23,922,651, respectively. This represents a 37% and 52% increase, respectively, in net sales as compared to $5,061,158 and $15,748,845 for the three and nine months ended September 30, 2018, respectively. These increases are primarily a result of increased sales of our DC power systems to Tier-1 telecommunications customers in the U.S.

Our sales backlog as of September 30, 2019 was $3.0 million. We anticipate that approximately 90% of these orders will ship and be recognized as revenues during the next two quarters. We are experiencing short-term volatility with our Tier-1 telecom customers as they shifted their budgets for the second half of 2019 to favor 5G roll-out relative to back-up power. This movement negatively impacted our bookings for the quarter ended September 30, 2019. We believe these are short-term shifts and remain confident in our customers' forecasts for 2020.

During the nine months ending September 30, 2019, we invested in expanding our manufacturing capacity and stocking inventory of raw materials in order to improve our order fulfillment times and better serve our customers. We continue to focus our efforts on growing our customer base and diversifying our product line and markets we serve.

Results of Operations

The tables presented below, which compare our results of operations from one period to another, present the results for each period, the change in those results from one period to another in both dollars and percentage change, and the results for each period as a percentage of net revenues. The columns present the following:

- The first two data columns in each table show the absolute results for each period presented.

- The columns entitled "Dollar Variance" and "Percentage Variance" shows the change in results, both in dollars and percentages. These two columns show favorable changes as a positive and unfavorable changes as negative. For example, when our net revenues increase from one period to the next, that change is shown as a positive number in both columns. Conversely, when expenses increase from one period to the next, that change is shown as a negative in both columns.

- The last two columns in each table show the results for each period as a percentage of net revenues.

Three Months Ended September 30, 2019 Compared to the Three Months Ended September 30, 2018

	Three Months Ended September 30,		Dollar Variance	Percentage Variance	Results as a Percentage of Net Sales for the Period Ended September 30,	
	2019 (unaudited)	**2018 (unaudited)**	**Favorable (Unfavorable)**	**Favorable (Unfavorable)**	**2019**	**2018**
Net sales	$ 6,939,318	$ 5,061,158	$ 1,878,160	37%	100.0%	100.0%
Cost of sales	4,707,412	3,530,847	(1,176,565)	(33%)	67.8%	69.8%
Gross Profit	2,231,906	1,530,311	701,595	46%	32.2%	30.2%
Sales and marketing expenses	707,171	717,983	10,812	2%	10.2%	14.2%
Research and development expenses	546,144	571,300	25,156	4%	7.9%	11.3%
General and Administrative expenses	935,352	1,004,984	69,632	7%	13.5%	19.9%
Total operating expenses	2,188,667	2,294,267	105,600	5%	31.5%	45.3%
Income (loss) from operations	43,239	(763,956)	807,195	106%	0.6%	(15.1%)
Interest expenses	(13,676)	(2,777)	(10,899)	(392%)	(0.2%)	(0.1%)
Other income	18,678	9,616	9,062	94%	0.3%	0.2%
Net income (loss)	$ 48,241	$ (757,117)	$ 805,358	106%	0.7%	(15.0%)

Net Sales. Net sales increased $1,878,160, or 37%, to $6,939,318 for the three months ended September 30, 2019, as compared to $5,061,158 for the same period in 2018. The increase in net sales was primarily due to an increase in sales of our DC power systems to Tier-1 telecommunications customers in the U.S. Our two largest customers for the quarter ended September 30, 2019 were AT&T and Verizon Wireless accounted for 84% and 7.5% of our total net sales, respectively, as compared to AT&T and T-Mobile which accounted for 39% and 37%, respectively, of total net sales for the same period in 2018.

Cost of Sales. Cost of sales during the three months ended September 30, 2019 increased by $1,176,565, or 33%, to $4,707,412, as compared to $3,530,847 during the same period in 2018 as a result of an increase in shipments of our DC powers systems during the three months ended September 30, 2019, as compared to the same period in 2018. Cost of sales as a percentage of net sales during the three months ended September 30, 2019 decreased to 67.8% as compared to 69.8% in the same period in 2018 as a result of a decrease in material costs, an increase in labor efficiencies and improved absorption of manufacturing overhead.

Gross Profit. Gross profit during the three months ended September 30, 2019 increased by $701,595, or 46%, to $2,231,906, as compared to $1,530,311 during the same period in 2018. Our gross profit as a percentage of net sales was 32.2% for the quarter ended September 30, 2019, as compared to 30.2% in the same period in 2018. The increase in gross profit margin was attributable to an increase in manufacturing labor efficiencies and improved manufacturing plant capacity utilization.

Sales and Marketing Expenses. During the three months ended September 30, 2019, sales and marketing expenses decreased by $10,812, or 2%, to $707,171, as compared to $717,983 during the same period in 2018. Our sales and marketing expenses are expected to remain relatively constant for the remainder of 2019 as we continue to market and promote our DC power systems in the U.S. and international markets as part of our ongoing strategy to expand our customer base.

Research and Development Expenses. During the three months ended September 30, 2019, research and development expenses decreased by $25,156, or 4%, to $546,144, as compared to $571,300 during the same period in 2018 as a result of fewer projects under development during the most recent quarterly period.

General and Administrative Expenses. General and administrative expenses decreased by $69,632, or 7%, to $935,352 during the three months ended September 30, 2019, as compared to $1,004,984 during same period in 2018. The decrease in G&A was a result of a reduction in administration support services used to support the production ramp-up in the last twelve months. We anticipate our general and administrative costs to remain relatively constant during the remainder of 2019.

Interest Expense. Interest expense for the three months ended September 30, 2019 was $13,676, as compared to $2,777 during the same period in 2018, an increase of $10,899. Our interest expense during the three months ended September 30, 2019 is mainly attributable to financing costs related to the acquisition of new manufacturing equipment.

Income Tax. We had no income tax expense for the three months ended September 30, 2019, and for the same period in 2018.

Net Income. As a result of the factors identified above, we reported net income of $48,241, or $0.00 per basic and diluted share, for the three months ended September 30, 2019, as compared to a net loss of $757,117, or ($0.07) per basic and diluted share, for the same period in 2018.

Nine Months Ended September 30, 2019 Compared to the Nine Months Ended September 30, 2018

	Nine Months Ended September 30,		Dollar Variance	Percentage Variance	Results as a Percentage of Net Sales for the Period Ended September 30,	
	2019 (unaudited)	**2018 (unaudited)**	**Favorable (Unfavorable)**	**Favorable (Unfavorable)**	**2019**	**2018**
Net sales	$ 23,922,651	$ 15,748,845	$ 8,173,806	52%	100.0%	100.0%
Cost of sales	16,336,576	10,672,707	(5,663,869)	(53%)	68.3%	67.8%
Gross Profit	7,586,075	5,076,138	2,509,937	49%	31.7%	32.2%
Sales and marketing expenses	2,032,643	1,968,152	(64,491)	(3%)	8.5%	12.5%
Research and development expenses	1,649,794	1,371,981	(277,813)	(20%)	6.9%	8.7%
General and Administrative expenses	3,209,596	2,589,018	(620,578)	(24%)	13.4%	16.4%
Total operating expenses	6,892,033	5,929,151	(962,882)	(16%)	28.8%	37.6%
Income (loss) from operations	694,042	(853,013)	1,547,055	181%	2.9%	(5.4%)
Interest expenses	(34,389)	(8,181)	(26,208)	(320%)	(0.1%)	(0.1%)
Other income	26,078	8,716	17,362	199%	0.1%	0.1%
Net income (loss)	$ 685,731	$ (852,478)	$ 1,538,209	180%	2.9%	(5.4%)

Net Sales. Net sales increased $8,173,806, or 52%, to $23,922,651 for the nine months ended September 30, 2019, as compared to $15,748,845 for the same period in 2018. The increase in net sales was primarily due to an increase in sales of our DC power systems to Tier-1 telecommunications customers in the U.S. Sales to our two largest customers for the nine months ended September 30, 2019, AT&T and T-Mobile, accounted for 68% and 19% of our total net sales during the nine months ended September 30, 2019. Sales to our three largest customers as of September 30, 2018, AT&T, Verizon Wireless and T-Mobile, accounted for 61%, 13% and 12%, respectively, of total net sales.

Cost of Sales. Cost of sales during the nine months ended September 30, 2019 increased by $5,663,869, or 53%, to $16,336,576, as compared to $10,672,707 during the same period in 2018. The cost of sales increased as a result of an increase in shipped orders of our DC powers systems during the nine months ended September 30, 2019, as compared to the same period in 2018. Cost of sales as a percentage of net sales during the nine months ended September 30, 2019 increased to 68.3%, as compared to 67.8% in the same period in 2018 as a result of a slight increase in factory overhead absorption.

Gross Profit. Gross profit during the nine months ended September 30, 2019 increased by $2,509,937, or 49%, to $7,586,075, as compared to $5,076,138 during the same period in 2018. Our gross profit as a percentage of net sales was 31.7% for the nine months ended September 30, 2019, as compared to 32.2% in the same period in 2018. The decrease in gross profit margin was attributable to an increase in factory overhead absorption during the nine months ending September 30, 2019, as compared to the same period in 2018.

Sales and Marketing Expenses. During the nine months ended September 30, 2019, sales and marketing expenses increased by $64,491, or 3%, to $2,032,643, as compared to $1,968,152 during the same period in 2018. The increase in sales and marketing expenses was attributable to an increase tradeshows and similar promotional events to showcase our DC power systems.

Research and Development Expenses. During the nine months ended September 30, 2019, research and development expenses increased by $277,813, or 20%, to $1,649,794, as compared to $1,371,981 during the same period in 2018. The increase in research and development expenses was attributable to ongoing sales support to meet new customer requirements and new product development as part of our ongoing strategy to expand our product line and diversify our customer base.

General and Administrative Expenses. General and administrative expenses increased by $620,578, or 24%, to $3,209,596 during the nine months ended September 30, 2019, as compared to $2,589,018 during same period in 2018. The increase was due to a combination of increases in salaries as a result of additions of management staff, an increase in office rent related to our new facility, an increase in the cost of employee fringe benefits, and an increase in staff recruiting services.

Interest Expense. Interest expense for the nine months ended September 30, 2019 was $34,389, as compared to $8,181 during the same period in 2018, an increase of $23,208. Our interest expense during the nine months ended September 30, 2019 is mainly attributable to financing costs related to the acquisition of new manufacturing equipment.

Income Tax. We had no income tax expense for the nine months ended September 30, 2019, and for the same period in 2018.

Net Income/Loss. For the nine months ended September 30, 2019, we reported net income of $685,731, or $0.07 per basic and diluted share, as compared to a net loss of $852,478, or $(0.08) per basic and diluted share for the nine months ended September 30, 2018.

Liquidity and Capital Resources

Sources of Liquidity

During the nine months ended September 30, 2019, we funded our operations primarily from cash on hand and sales of receivables under our Supplier Agreement with Citibank. These funds were also used to make capital expenditures and to increase inventory to support a higher level of production. As of September 30, 2019, we had working capital of $21,306,930, as compared to working capital of $21,089,802 at December 31, 2018. This $217,128 increase in working capital is primarily attributable to our ability to collect on accounts receivable in a shorter period of time as a result of our Sup plier Agreement with Citibank, N.A. and using such funds to increase our inventory levels. During the nine months ended September 30, 2019, we sold $9,367,112 of receivables to Citibank under our Supplier Agreement, and incurred fees of approximately $42,000 in connection with such sales.

On September 30, 2019 and December 31, 2018, our net trade receivables totaled $5,038,302 and $7,726,919, respectively. On September 30, 2019, $3,927,171 (78%) represented customer account balances relating to our largest customer. On December 31, 2018, the customer account balances for our two largest customers were $3,457,433 (45%) and $3,220,907 (42%).

Our available capital resources on September 30, 2019 consisted primarily of $3,666,475 in cash and cash equivalents, as compared to $5,640,078 as of December 31, 2018.

Credit Facility

On March 21, 2017, we entered into a Credit Agreement and related documents with Citibank, N.A. for a revolving credit facility for an aggregate amount of up to $1,000,000.

On March 20, 2019, we terminated the credit facility and transferred the $1,000,000 secured by a Certificate of Deposit to our liquid cash account. As of March 20, 2019, we had not borrowed any funds under the credit facility.

Supplier Agreement

Effective June 4, 2019, we entered into a Supplier Agreement with Citibank, N.A. Under the terms of the Supplier Agreement, we may from time to time offer to sell to Citibank, without recourse, certain of our accounts receivable relating to invoiced sales made to AT&T. Once AT&T approves the invoice, AT&T sends payment instructions to Citibank. The sale price is equal to the face amount of the receivable less the applicable discount charge calculated by multiplying the face amount of the receivable by (i) the annual discount rate (which is equal to the 90-day London Inter-bank Offered Rate plus 1.00%) and (ii) the discount acceptance period (which is equal the number of days in the payment terms less the number of days necessary to approve the invoice) divided by 360.

Citibank may change the pricing terms at any time in its sole discretion upon at least thirty days prior written notice to us. In addition, either party may terminate the Supplier Agreement upon thirty business days prior written notice to the other party, provided that either party may terminate the agreement upon five business days prior written notice if the other party is in breach of, or fails to perform any of, its material obligations under the Supplier Agreement. During the nine months ended September 30, 2019, the Company sold receivables of $9,367,112 under the Supplier Agreement.

Future Capital Requirements

We believe that our current and future available capital resources, revenues from operations and other sources of liquidity will enable us to fund our operating expenses and capital expenditure requirements for at least the next twelve months.

Cash Flow

The following table sets forth the significant sources and uses of cash for the nine-month periods set forth below:

	September 30, 2019 (Unaudited)	**September 30, 2018 (Unaudited)**
Net Cash Used In:		
Operating Activities	$ (1,489,473)	$ (3,302,341)
Investing Activities	(311,369)	(208,998)
Financing Activities	(172,761)	(82,369)
Net decrease in cash	$ (1,973,603)	$ (3,593,708)

Operating Activities

Net cash used in operating activities for the nine months ended September 30, 2019 was $1,489,473, as compared to net cash used in operating activities of $3,302,341 for same period in 2018. This increase in net cash used in 2019 was primarily due to net income of $685,731, an increase in inventories of $5,671,126, an increase in prepaid expenses of $819,437, a decrease in accounts payable of $209,759, coupled with a decrease in accounts receivables of $2,688,617.

Investing Activities

Net cash used in investing activities for the nine months ended September 30, 2019 totaled $311,369, as compared to $208,998 for the same period in 2018, an increase of $102,371. This increase was primarily due to an increase in property and equipment acquisitions related to expansion of our production facility.

Financing Activities

Net cash used in financing activities totaled $172,761 for the nine months ended September 30, 2019, as compared to $82,369 for the same period in 2018. This increase was primarily due to increased equipment financing during the period.

Backlog

As of September 30, 2019, we had a backlog of $3.0 million. The amount of backlog represents revenue that we anticipate recognizing in the future, as evidenced by purchase orders and other purchase commitments received from customers, but on which work has not yet been initiated or with respect to which work is currently in progress. Over 99% of our backlog at September 30, 2019 was comprised of purchases of DC power systems by telecommunications customers. We believe that approximately 90% of our backlog will be shipped during the next two quarters. However, there can be no assurance that we will be successful in fulfilling such orders and commitments in a timely manner or that we will ultimately recognize as revenue the amounts reflected in our backlog.

We are experiencing short-term volatility with our Tier-1 telecom customers as they shifted their budgets for the second half of 2019 to favor 5G roll-out relative to back-up power. This movement negatively impacted our bookings for the quarter ended September 30, 2019. We believe these are short-term shifts and remain confident in our customers' forecasts for 2020.

ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

Not applicable.

ITEM 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our principal executive officer and our principal financial officer, evaluated, as of the end of the period covered by this Quarterly Report on Form 10-Q, the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, or the Exchange Act). Based on that evaluation, our principal executive officer and principal financial officer have concluded that as of September 30, 2019, our disclosure controls and procedures were effective at the reasonable assurance level. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and our management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

Management's Report on Internal Control Over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting as such term is defined in Rule 13a-15(f) under the Exchange Act. Internal control over financial reporting is a process designed under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Our internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of our assets; and (ii) provide reasonable assurance (a) transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, (b) our receipts and expenditures are being made only in accordance with authorizations of our management and directors, and (c) regarding the prevention or timely detection of the unauthorized acquisition, use or disposition of assets that could have a material effect on our financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

As of September 30, 2019, our management conducted an evaluation of the effectiveness of our internal control over financial reporting using the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in Internal Control - Integrated Framework (2013). Based on this evaluation, our management concluded that, as of September 30, 2019, our internal control over financial reporting was effective.

This Quarterly Report on Form 10-Q does not include an attestation report of our registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by our registered public accounting firm pursuant to rules of the SEC that permit us to provide only management's report in this Quarterly Report on Form 10-Q.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting identified in connection with the evaluation required by Rule 13a-15(d) and 15d-15(d) of the Exchange Act that occurred during the quarter or three months ended September 30, 2019 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION

ITEM 1. Legal Proceedings

From time to time, we may be involved in general commercial disputes arising in the ordinary course of our business. We are not currently involved in legal proceedings that could reasonably be expected to have material adverse effect on our business, prospects, financial condition or results of our operation.

ITEM 1A. Risk Factors

Before deciding to purchase, hold or sell our common stock, you should carefully consider the risks described below in addition to the other information contained in this Quarterly Report on Form 10-Q and in our other filings with the SEC, including subsequent reports on Forms 10-Q and 8-K. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties not presently known to us or that we currently deem immaterial may also affect our business. If any of these known or unknown risks or uncertainties actually occurs with material adverse effects on Polar Power, our business, financial condition, results of operations and/or liquidity could be seriously harmed. In that event, the market price for our common stock will likely decline, and you may lose all or part of your investment.

Risks Related to Our Business and Industry

We are dependent on, and derive substantially all of our revenue from, sales of our DC base power systems to three customers within the U.S. telecommunications market. Our efforts to expand our customer base, our product portfolio or markets within which we operate may not succeed and may reduce our revenue growth rate.

We derive substantially all our revenues from sales of our DC base power systems to three customers within the telecommunications market, AT&T, T-Mobile and Verizon Wireless. Any factor adversely affecting sales of these power systems to these three customers or to other customers within this market, including market acceptance, product competition, performance and reliability, reputation, price competition and economic and market conditions, could adversely affect our business and results of operations. In addition, any unfavorable change in our business relationship with our Tier-1 telecommunications wireless carrier customers, or delays in customer implementation and deployment of our products, could have a material adverse effect on our results of operation and financial condition. Our plan to invest in the development of higher capacity DC hybrid solar systems to address data centers and other applications within the telecommunications market may not result in an anticipated growth in sales and may reduce our revenue growth rate.

Many of our DC power systems involve long design and sales cycles, which could have an adverse impact on our results of operations and financial performance.

The design and sales cycle for our DC power systems, from initial contact with our potential customer to the shipments of our product, may be lengthy. Customers generally consider a wide range of factors before making a purchase decision. Prior to purchasing our products, our customers often require a significant technical review, tests and evaluations over long periods of time, assessments of competitive products and approval at a number of management levels within their organization. During the time our customers are evaluating our products, we may incur substantial sales and service, engineering and research and development expenses to customize our products to meet customer's application needs. We may also expend significant management efforts, increase manufacturing capacity, order long-lead-time components or purchase significant amounts of components and other inventory prior to receiving an order. Even after this evaluation process, a potential customer may not purchase our products.

The product development time before our customer agrees to purchase our DC power systems can be considerable. Our process for developing an integrated solution may require use of significant engineering resources, including design, prototyping, modeling, testing and application engineering. The length of this cycle is influenced by many factors, including the difficulty of the technical specification and complexity of the design and the customer's procurement processes. A significant period may elapse between our investment of time and resources in designing and developing a product for our customer and revenue from sales of that product. The length of this process combined with unanticipated delays in the development cycle could materially affect results of operations and financial conditions.

We do not have long-term commitments for significant revenues with most of our customers and may be unable to retain existing customers, attract new customers or replace departing customers with new customers that can provide comparable revenues and profits.

Because we generally do not obtain firm, long-term volume purchase commitments from our customers, most of our sales are derived from individual purchase orders. We remain dependent upon securing new purchase orders in the future in order to sustain and grow our revenues. Accordingly, there is no assurance that our revenues and business will grow in the future. Our failure to maintain and expand our customer relationships could materially and adversely affect our business and results of operations.

The high concentration of our sales within the telecommunications market could result in a significant reduction in sales and negatively affect our profitability if demand for our DC power systems declines within this market.

We expect to be predominately focused on the manufacturing, marketing and sales of DC power systems to telecommunications companies for the foreseeable future. We may be unable to shift our business focus away from these activities. Accordingly, the emergence of new competing DC power products or lower-cost alternative technologies may reduce the demand for our products. A downturn in the demand for our DC power systems within the telecommunications market would likely materially and adversely affect our sales and profitability.

Any failure by management to properly manage our expected growth could have a material adverse effect on our business, operating results and financial condition.

We anticipate that we will continue to grow in the near future. The growth of our business will require significant investments of capital and management's close attention. Our strategy envisions a period of growth that may impose a significant burden on our administrative, financial, and operational resources. If we experience difficulties in any of these areas, we may not be able to expand our business successfully or effectively manage our growth. Our ability to effectively manage our growth will require us to substantially expand the capabilities of our administrative and operational resources and to attract, train, manage and retain qualified management, engineers, and other personnel. We may be unable to do so. Further, our failure to properly manage our expected growth could have a material adverse effect on our ability to retain key personnel. In addition, our failure to successfully manage our growth could result in our sales not increasing commensurately with our capital investments. Any failure by management to manage growth and to respond to changes in our business could have a material adverse effect on our business, financial condition and results of operations.

The markets within which we compete are highly competitive. Many of our competitors have greater financial and other resources than we do and one or more of these competitors could use their greater financial and other resources to gain market share at our expense.

If our business continues to develop as expected, we anticipate that we will continue to grow in the near future. If, due to capital constraints or otherwise, we are unable to fulfill our existing backlog in a timely manner and/or procure and timely fulfill our anticipated future backlog, our customers and potential customers may decide to use competing DC power systems or continue the use of alternating current, or AC, power systems. If we are unable to fulfill the growing demand for products and services in a timely manner, our customers and potential customers may choose to purchase products from our competitors. Some of our larger competitors may be willing to reduce prices and accept lower margins in order to compete with us. In addition, we could face new competition from large international or domestic companies with established industrial brands and distribution networks that enter our end markets. Demand for our products may also be affected by our ability to respond to changes in design and functionality, to respond to downward pricing pressure, and to provide shorter lead times for our products than our competitors. If we are unable to respond successfully to these competitive pressures, we could lose market share, which could have an adverse impact on our results. We cannot assure that we will be able to compete successfully in our markets or compete effectively against current and new competitors as our industry continues to evolve.

Rapid technological changes may prevent us from remaining current with our technological resources and maintaining competitive product and service offerings.

The markets in which we and our customers operate are characterized by rapid technological change, especially within the telecommunications market. Significant technological changes could render our existing and potential new products, services and technology obsolete. Our future success will depend, in large part, upon our ability to:

- effectively identify and develop leading energy efficient technologies;
- continue to develop our technical expertise;
- enhance our current products and services with new, improved and competitive technology; and
- respond to technological changes in a cost-effective and timely manner.

If we are unable to successfully respond to technological change or if we do not respond to it in a cost-effective and timely manner, then our business will be materially and adversely affected. We cannot assure you that we will be successful in responding to changing technology. In addition, technologies developed by others may render our products, services and technology uncompetitive or obsolete. Even if we do successfully respond to technological advances, the integration of new technology may require substantial time and expense, and we cannot assure you that we will succeed in adapting our products, services and technology in a timely and cost-effective manner.

If we are unable to continue to develop new and enhanced products and services that achieve market acceptance in a timely manner, our competitive position and operating results could be harmed.

Our future success will depend on our ability to continue to develop new and enhanced DC power systems and related products and services that achieve market acceptance in a timely and cost-effective manner. The markets in which we and our customers operate are characterized by frequent introductions of new and enhanced products and services, evolving industry standards and regulatory requirements, government incentives and changes in customer needs. The successful development and market acceptance of our products and services depends on a number of factors, including:

- the changing requirements and preferences of the potential customers in our markets;
- the accurate prediction of market requirements, including regulatory issues;
- the timely completion and introduction of new products and services to avoid obsolescence;
- the quality, price and performance of new products and services;
- the availability, quality, price and performance of competing products and services;
- our customer service and support capabilities and responsiveness;
- the successful development of our relationships with existing and potential customers; and
- changes in industry standards.

We may experience financial or technical difficulties or limitations that could prevent us from introducing new or enhanced products or services. Furthermore, any of these new or enhanced products and services could contain problems that are discovered after they are introduced. We may need to significantly modify the design of these products and services to correct problems. Rapidly changing industry standards and customer preferences and requirements may impede market acceptance of our products and services.

Development and enhancement of our products and services will require significant additional investment and could strain our management, financial and operational resources. The lack of market acceptance of our products or services or our inability to generate sufficient revenues from this development or enhancement to offset their development costs could have a material adverse effect on our business. In addition, we may experience delays or other problems in releasing new products and services and enhancements, and any such delays or problems may cause customers to forego purchases of our products and services and to purchase those of our competitors.

We cannot provide assurance that products and services that we have recently developed or that we develop in the future will achieve market acceptance. If our new products and services fail to achieve market acceptance, or if we fail to develop new or enhanced products and services s that achieve market acceptance, our growth prospects, operating results and competitive position could be adversely affected.

We are dependent on relationships with our key material suppliers, and the partial or complete loss of one of these key suppliers, or the failure to find replacement suppliers or manufacturers in a timely manner, could adversely affect our business.

We have established relationships with third-party engine suppliers and other key suppliers from which we source components for our power systems. We purchase standard configurations of engines for our DC power systems and are substantially dependent on timely supply from two key engine suppliers, Yanmar Engines Company and Perkins Engines. Purchases from Yanmar and Perkins represented approximately 44% and 12% of our total cost of sales for the nine months ended September 30, 2019. We do not have any long-term contracts or commitments with Yanmar or Perkins. If these engine suppliers were to fail to provide emissions certified engines in a timely manner or fail to supply engines that meet our quality, quantity or cost requirements, or were to discontinue manufacturing any engines we source from them or discontinue providing any of these engines to us, and we were unable to obtain substitute sources in a timely manner or on terms acceptable to us, our ability to manufacture our products could be materially adversely affected.

Price increases in some of the key components in our DC power systems could materially and adversely affect our operating results and cash flows.

The prices of some of the key components of our DC power systems are subject to fluctuation due to market forces beyond our control, including changes in the costs of raw materials incorporated into these components. Such price increases occur from time to time due to spot shortages of commodities, increases in labor costs or longer-term shortages due to market forces. In particular, the prices of engines can fluctuate frequently and often significantly. We do not have any long-term contracts or commitments with our key engine supplier. Substantial increases in the prices of raw materials used in components which we source from our suppliers may result in increased prices charged by our suppliers. If we incur price increases from our suppliers for key components in our DC power systems, our production costs will increase. Given competitive market conditions, we may not be able to pass all or any of those cost increases on to our OEM customers in the form of higher sales prices. To the extent our competitors do not suffer comparable component cost increases, we may have even greater difficulty passing along price increases and our competitive position may be harmed. As a result, increases in costs of key components may adversely affect our margins and otherwise adversely affect our operating results and cash flows.

A portion of our key components are sourced in foreign countries, exposing us to additional risks that may not exist in the U.S.

A portion of our key components, such as engines, magnets and cooling systems, are purchased from suppliers located overseas, primarily in Asia. Our international sourcing subjects us to a number of potential risks in addition to the risks associated with third-party sourcing generally. These risks include:

- inflation or changes in political and economic conditions;
- unstable regulatory environments;
- changes in import and export duties;
- currency rate fluctuations;
- trade restrictions;
- labor unrest;
- logistical and communications challenges; and
- other restraints and burdensome taxes.

These factors may have an adverse effect on our ability to source our purchased components overseas. In particular, if the U.S. dollar were to depreciate significantly against the currencies in which we purchase raw materials from foreign suppliers, our cost of goods sold could increase materially, which would adversely affect our results of operations.

The unavailability or shortage, or increase in the cost, of raw materials and components could have an adverse effect on our sales and profitability.

Our operations require raw materials, such as aluminum, copper and permanent magnets. Commodities such as aluminum and copper are known to have significant price volatility based on global economic conditions. An increase in global economic outlook may result in significant price increases in the cost of our raw materials. In addition, we use Neodymium permanent magnets in our alternators, for which there are a limited number of global suppliers that can meet our standards. Increase in manufacturing of electric vehicles worldwide can have an adverse effect on the cost or supply of these magnets. At our current production volumes, we are unable to secure large quantities of these commodities at fixed prices; however, we do have multiple sources of supply for our raw materials to meet our near term forecasted needs.

Various factors could reduce the availability of raw materials and components and shortages may occur from time to time in the future. An increase in lead times for the supply of raw materials due to a global increase in demand for commodities outlined may significantly increase material costs of our products. If production was interrupted due to unavailability or shortage of raw materials and we were not able to find alternate third-party suppliers or re-engineer our products to accommodate different components or materials, we could experience disruptions in manufacturing and operations including product shortages, higher freight costs and re-engineering costs. If our supply of raw materials or components is disrupted or our lead times extended, our business, results of operations or financial condition could be materially adversely affected.

We manufacture and assemble a majority of our products at two facilities. Any prolonged disruption in the operations of these facilities would result in a decline in our sales and profitability.

We manufacture and assemble our DC power systems at our two facilities located in Gardena, California. Any prolonged disruption in the operations of our manufacturing and assembly facilities, whether due to equipment or information technology infrastructure failure, labor difficulties, destruction of or damage to either of these facilities as a result of an earthquake, fire, flood, other catastrophes, and other operational problems would result in a decline in our sales and profitability. In the event of a business interruption at our facilities, we may be unable to shift manufacturing and assembly capabilities to alternate locations, accept materials from suppliers or meet customer shipment needs, among other severe consequences. Such an event could have a material and adverse impact on our financial condition and results of our operations.

Our business operations are subject to substantial government regulation.

Our business operations are subject to certain federal, state, local and foreign laws and regulations. For example, our products, services and technologies are subject to regulations relating to building codes, public safety, electrical connections, security protocols, and local and state licensing requirements. The regulations to which we are subject may change, additional regulations may be imposed, or existing regulations may be applied in a manner that creates special requirements for the implementation and operation of our products or services that may significantly impact or even eliminate some of our revenues or markets. In addition, we may incur material costs or liabilities in complying with any such regulations. Furthermore, some of our customers must comply with numerous laws and regulations, which may affect their willingness and ability to purchase our products, services and technologies.

The modification of existing laws and regulations or interpretations thereof or the adoption of future laws and regulations could adversely affect our business, cause us to modify or alter our methods of operations and increase our costs and the price of our products, services and technology. In addition, we cannot provide any assurance that we will be able, for financial or other reasons, to comply with all applicable laws and regulations. If we fail to comply with these laws and regulations, we could become subject to substantial penalties or restrictions that could materially and adversely affect our business.

Certain of our products are used in critical communications networks which may subject us to significant liability claims.

Because certain of our products for customers in the telecommunications industry are used in critical communications networks, we may be subject to significant liability claims if our products do not work properly. We warrant to our current customers that our products will operate in accordance with our product specifications. If our products fail to conform to these specifications, our customers could require us to remedy the failure or could assert claims for damages. The provisions in our agreements with customers that are intended to limit our exposure to liability claims may not preclude all potential claims. In addition, any insurance policies we have may not adequately limit our exposure with respect to such claims. Liability claims could require us to spend significant time and money in litigation or to pay significant damages. Any such claims, whether or not successful, would be costly and time-consuming to defend, and could divert management’s attention and seriously damage our reputation and our business.

We could be adversely affected by our failure to comply with the laws applicable to our foreign activities, including the U.S. Foreign Corrupt Practices Act and other similar worldwide anti-bribery laws.

The U.S. Foreign Corrupt Practices Act, or the FCPA, and similar anti-bribery laws in other jurisdictions prohibit U.S.-based companies and their intermediaries from making improper payments to non-U.S. officials for the purpose of obtaining or retaining business. We may pursue opportunities in certain parts of the world that experience government corruption, and in certain circumstances, compliance with anti-bribery laws may conflict with local customs and practices. Our policies mandate compliance with all applicable anti-bribery laws. Further, we require our partners, subcontractors, agents and others who work for us or on our behalf to comply with the FCPA and other anti-bribery laws. Although we have policies and procedures, and have conducted training, designed to ensure that we, our employees, our agents and others who work with us in foreign countries comply with the FCPA and other anti-bribery laws, there is no assurance that such policies, procedures or training will protect us against liability under the FCPA or other laws for actions taken by our agents, employees and intermediaries. If we are found to be liable for FCPA violations (either due to our own acts or inadvertence, or due to the acts or inadvertence of others), we could suffer from severe criminal or civil penalties or other sanctions, which could have a material adverse effect on our reputation, business, results of operations or cash flows. In addition, detecting, investigating and resolving actual or alleged FCPA violations is expensive and could consume significant time and attention of our senior management.

We are exposed to risks related to our international sales, and the failure to manage these risks could harm our business. If we fail to expand our business into international markets, our revenues and results of operations may be adversely affected.

In addition to our sales to customers within the U.S., we plan to increase sales to customers outside the U.S. as we pursue expanding our business with current and potential customers worldwide. We have established full-time sales executives and support staff in Australia, Dubai, Singapore, Romania, Poland, Africa and the Dominican Republic. We expect that international sales will increase over time and that a significant portion of our future international sales will be from less developed or developing countries. As a result, the occurrence of any international, political, economic, or geographic event could result in a significant decline in revenue. There are significant risks associated with conducting operations internationally, requiring significant financial commitments to support such operations. These operations present a number of challenges including oversight of daily operating practices in each location, handling employee benefits and employee behavior. In addition, compliance with complex foreign and U.S. laws and regulations that apply to our international operations increases our cost of doing business in international jurisdictions. These numerous and sometimes conflicting laws and regulations include internal control and disclosure rules, data privacy and filtering requirements, anti-corruption laws, such as the FCPA, and other local laws prohibiting corrupt payments to governmental officials, and anti-competition regulations, among others. Violations of these laws and regulations could result in fines and penalties, criminal sanctions against us, our officers, or our employees, prohibitions on the conduct of our business and on our ability to offer our products and services in one or more countries, and could also materially affect our brand, our international expansion efforts, our ability to attract and retain employees, our business, and our operating results. Although we have implemented policies and procedures designed to ensure compliance with these laws and regulations, there can be no assurance that our employees, contractors, or agents will not violate our policies.

Some of the risks and challenges of doing business internationally include:

- requirements or preferences for domestic products or solutions, which could reduce demand for our products;
- unexpected changes in regulatory requirements;
- imposition of tariffs and other barriers and restrictions;
- restrictions on the import or export of critical technology;
- management communication and integration problems resulting from cultural and geographic dispersion;
- the burden of complying with a variety of laws and regulations in various countries;
- difficulties in enforcing contracts;
- the uncertainty of protection for intellectual property rights in some countries;
- application of the income tax laws and regulations of multiple jurisdictions, including relatively low-rate and relatively high-rate jurisdictions, to our sales and other transactions, which results in additional complexity and uncertainty;
- tariffs and trade barriers, export regulations and other regulatory and contractual limitations on our ability to sell products;
- greater risk of a failure of foreign employees to comply with both U.S. and foreign laws, including export and antitrust regulations, the FCPA and any trade regulations ensuring fair trade practices;
- heightened risk of unfair or corrupt business practices in certain geographies and of improper or fraudulent sales arrangements that may impact financial results and result in restatements of, or irregularities in, financial statements;
- potentially adverse tax consequences, including multiple and possibly overlapping tax structures;

- general economic and geopolitical conditions, including war and acts of terrorism;
- lack of the availability of qualified third-party financing; and
- currency exchange controls.

While these factors and the impacts of these factors are difficult to predict, any one or more of them could adversely affect our business, financial condition and results of operations in the future.

Failures or security breaches of our networks or information technology systems could have an adverse effect on our business.

We rely heavily on information technology, or IT, both in our products and services for customers and in our IT systems. Further, we collect and store sensitive information in our data centers and on our networks. Government agencies and security experts have warned about growing risks of hackers, cyber-criminals, malicious insiders and other actors targeting confidential information and all types of IT systems. These actors may engage in fraudulent activities, theft of confidential or proprietary information and sabotage.

Our IT systems and our confidential information may be vulnerable to damage or intrusion from a variety of attacks including computer viruses, worms or other malicious software programs. These attacks pose a risk to the security of the products, systems and networks of our customers, suppliers and third-party service providers, as well to the confidentiality of our information and the integrity and availability of our data. While we attempt to mitigate these risks through controls, due diligence, training, surveillance and other measures, we remain vulnerable to information security threats.

Despite the precautions we take, an intrusion or infection of our systems could result in the disruption of our business, loss of proprietary or confidential information, or injuries to people or property. Similarly, an attack on our IT systems could result in theft or disclosure of trade secrets or other intellectual property or a breach of confidential customer or employee information. Any such events could have an adverse impact on sales, harm our reputation and cause us to incur legal liability and increased costs to address such events and related security concerns. As the threats evolve and become more potent, we may incur additional costs to secure the products that we sell, as well as our data and infrastructure of networks and devices.

Risks Related to Our Intellectual Property

If we fail to adequately protect our intellectual property rights, we could lose important proprietary technology, which could materially and adversely affect our business.

Our success and ability to compete depends, in substantial part, upon our ability to develop and protect our proprietary technology and intellectual property rights to distinguish our products, services and technology from those of our competitors. The unauthorized use of our intellectual property rights and proprietary technology by others could materially harm our business.

Historically, we have relied primarily on a combination of trademark, copyright and trade secret laws, along with non-competition and confidentiality agreements, contractual provisions, licensing arrangements and proprietary software and manufacturing processes, to establish and protect our intellectual property rights. Although we hold several unregistered copyrights in our business, we believe that the success of our business depends more upon our proprietary technology, information, processes and know-how than on patents or trademark registrations. In addition, much of our proprietary information and technology may not be patentable; if we decided to apply for patents and/or trademarks in the future, we might not be successful in obtaining any such future patents or in registering any marks.

Despite our efforts to protect our intellectual property rights, existing laws afford only limited protection, and our actions may be inadequate to protect our rights or to prevent others from claiming violations of their proprietary rights. Unauthorized third parties may attempt to copy, reverse engineer or otherwise obtain, use or exploit aspects of our products and services, develop similar technology independently, or otherwise obtain and use information that we regard as proprietary. We cannot assure you that our competitors will not independently develop technology similar or superior to our technology or design around our intellectual property. In addition, the laws of some foreign countries may not protect our proprietary rights as fully or in the same manner as the laws of the U.S.

We may need to resort to litigation to enforce our intellectual property rights, to protect our trade secrets, and to determine the validity and scope of other companies' proprietary rights in the future. However, litigation could result in significant costs and in the diversion of management and financial resources. We cannot assure you that any such litigation will be successful or that we will prevail over counterclaims against us. Our failure to protect any of our important intellectual property rights or any litigation that we resort to in order to enforce those rights could materially and adversely affect our business.

If we face claims of intellectual property infringement by third parties, we could encounter expensive litigation, be liable for significant damages or incur restrictions on our ability to sell our products and services.

Although we are not aware of any present infringement of our products, services or technology on the intellectual property rights of others, we cannot be certain that our products, services and technologies do not or in the future will not infringe on the valid intellectual property rights held by third parties. In addition, we cannot assure you that third parties will not claim that we have infringed their intellectual property rights.

In recent years, there has been a significant amount of litigation in the U.S. involving patents and other intellectual property rights. In the future, we may be a party to litigation as a result of an alleged infringement of others' intellectual property. Successful infringement claims against us could result in substantial monetary liability, require us to enter into royalty or licensing arrangements, or otherwise materially disrupt the conduct of our business. In addition, even if we prevail on these claims, this litigation could be time-consuming and expensive to defend or settle and could result in the diversion of our time and attention and of operational resources, which could materially and adversely affect our business. Any potential intellectual property litigation also could force us to do one or more of the following:

- stop selling, incorporating or using our products and services that use the infringed intellectual property;
- obtain from the owner of the infringed intellectual property right a license to sell or use the relevant technology, which license may not be available on commercially reasonable terms, or at all; or
- redesign the products and services that use the technology.

If we are forced to take any of these actions, our business may be seriously harmed. Although we carry general liability insurance, our insurance may not cover potential claims of this type or may not be adequate to indemnify us for all liability that may be imposed.

Risks Related to Our Common Stock

Our operating results can fluctuate significantly from period to period, which makes our operating results difficult to predict and can cause our operating results in any particular period to be less than comparable periods and expectations from time to time.

Our operating results have fluctuated significantly from quarter-to-quarter, period-to-period and year-to-year during our operating history and are likely to continue to fluctuate in the future due to a variety of factors, many of which are outside of our control. Certain factors that may affect our operating results include, without limitation, those set forth under "Management's Discussion and Analysis of Financial Condition and Results of Operations — Critical Accounting Policies" in this Quarterly Report on Form 10-Q.

Because we have little or no control over many of these factors, our operating results are difficult to predict. Any adverse change in any of these factors could negatively affect our business and results of operations.

Our revenues, net income and other operating results are heavily dependent upon the size and timing of customer orders and projects, and the timing of the completion of those projects. The timing of our receipt of large individual orders, and of project completion, is difficult for us to predict. Because our operating expenses are based on anticipated revenues over the mid- and long-term and because a high percentage of our operating expenses are relatively fixed, a shortfall or delay in recognizing revenues can cause our operating results to vary significantly from quarter-to-quarter and can result in significant operating losses or declines in profit margins in any particular quarter. If our revenues fall below our expectations in any particular quarter, we may not be able, or it may not be prudent for us, to reduce our expenses rapidly in response to the revenue shortfall, which can result in us suffering significant operating losses or declines in profit margins in that quarter.

Due to these factors and the other risks discussed in this Quarterly Report on Form 10-Q, you should not rely on quarter-to-quarter, period-to-period or year-to-year comparisons of our results of operations as an indication of our future performance. Quarterly, period and annual comparisons of our operating results are not necessarily meaningful or indicative of future performance. As a result, it is likely that, from time to time, our results of operations or our revenue backlog could fall below historical levels or the expectations of public market analysts and investors, which could cause the trading price of our common stock to decline significantly.

Our Chairman, President and Chief Executive Officer owns a majority of our common stock and will exercise significant influence over matters requiring stockholder approval, regardless of the wishes of other stockholders.

Our Chairman, President, Chief Executive Officer and Secretary, Arthur D. Sams, beneficially owns approximately 55% of our outstanding shares of common stock. Mr. Sams therefore has significant influence over management and significant control over matters requiring stockholder approval, including the annual election of directors and significant corporate transactions, such as a merger or other sale of our company or our assets, for the foreseeable future. This concentrated control will limit stockholders' ability to influence corporate matters and, as a result, we may take actions that our stockholders do not view as beneficial. As a result, the market price of our common stock could be adversely affected.

We are a "controlled company" within the meaning of the Nasdaq Listing Rules. Although we do not currently intend to rely on the exemptions from certain corporate governance requirements afforded to a "controlled company" under Nasdaq Listing Rules, we could potentially seek to rely on such exemptions in the future.

Our Chairman, President, Chief Executive Officer and Secretary, Arthur D. Sams, controls a majority of our common stock. As a result, we are a "controlled company" within the meaning of the Nasdaq Listing Rules. Under these rules, a company of which more than 50% of the voting power for the election of directors is held by an individual, a group or another company is a "controlled company" and may elect not to comply with certain Nasdaq corporate governance requirements, including, without limitation (i) the requirement that a majority of the board of directors consist of independent directors, (ii) the requirement that the compensation of our officers be determined or recommended to our board of directors by a compensation committee that is comprised solely of independent directors, and (iii) the requirement that director nominees be selected or recommended to the board of directors by a majority of independent directors or a nominating committee comprised solely of independent directors. We do not currently intend to rely on those exemptions afforded to a "controlled company." Nonetheless, in the future, we could potentially seek to rely on certain of those exemptions afforded to a "controlled company," and in such case, you would not have the same protections afforded to stockholders of companies that are subject to all of the Nasdaq corporate governance requirements.

The price of our shares of common stock is volatile, and you could lose all or part of your investment.

The trading price of our shares of common stock is volatile and could be subject to wide fluctuations in response to various factors, some of which are beyond our control, including limited trading volume. In addition to the factors discussed in the "Risk Factors" section and elsewhere in this Quarterly Report on Form 10-Q, these factors include, without limitation:

- competition from existing technologies and products or new technologies and products that may emerge;
- the loss of significant customers, including AT&T, T-Mobile and Verizon Wireless;
- actual or anticipated variations in our quarterly operating results;

- failure to meet the estimates and projections of the investment community or that we may otherwise provide to the public;
- our cash position;
- announcement or expectation of additional financing efforts;
- issuances of debt or equity securities;
- our inability to successfully enter new markets or develop additional products;
- actual or anticipated fluctuations in our competitors' operating results or changes in their respective growth rates;
- sales of our shares of common stock by us, or our stockholders in the future;
- trading volume of our shares of common stock on the Nasdaq Capital Market;
- market conditions in our industry;
- overall performance of the equity markets and general political and economic conditions;
- introduction of new products or services by us or our competitors;
- additions or departures of key management, engineering or other personnel;
- publication of research reports about us or our industry or positive or negative recommendations or withdrawal of research coverage by securities or industry analysts;
- changes in the market valuation of similar companies;
- disputes or other developments related to intellectual property and other proprietary rights;
- changes in accounting practices;
- significant lawsuits, including stockholder litigation; and
- other events or factors, many of which are beyond our control.

Furthermore, the public equity markets have experienced extreme price and volume fluctuations that have affected and continue to affect the market prices of equity securities of many companies. These fluctuations often have been unrelated or disproportionate to the operating performance of those companies. These broad market and industry fluctuations, as well as general economic, political and market conditions such as recessions, interest rate changes or international currency fluctuations, may negatively impact the market price of our shares of common stock.

We do not anticipate paying cash dividends, and accordingly, stockholders must rely on stock appreciation for any return on their investment.

We have never declared or paid cash dividends on our capital stock. We intend to retain a significant portion of our future earnings, if any, to finance the operations, development and growth of our business. Any future determination to declare dividends will be made at the discretion of our board of directors, subject to applicable laws, and will depend on number of factors, including our financial condition, results of operations, capital requirements, contractual restrictions, general business conditions and other factors that our board of directors may deem relevant. As a result, only appreciation of the price of our common stock, which may never occur, will provide a return to stockholders.

If securities or industry analysts do not publish research or reports or publish inaccurate or unfavorable research or reports about our business, our share price and trading volume could decline.

The trading market for our shares of common stock depends, in part, on the research and reports that securities or industry analysts publish about us or our business. We do not have any control over these analysts. If no securities or industry analysts undertake coverage of our company, the trading price for our shares of common stock may be negatively impacted. If we obtain securities or industry analyst coverage and if one or more of the analysts who covers us downgrades our shares of common stock, changes their opinion of our shares or publishes inaccurate or unfavorable research about our business, our share price would likely decline. If one or more of these analysts ceases coverage of us or fails to publish reports on us regularly, demand for our shares of common stock could decrease and we could lose visibility in the financial markets, which could cause our share price and trading volume to decline.

We are not subject to the provisions of Section 203 of the Delaware General Corporation Law, which could negatively affect your investment.

We elected in our certificate of incorporation to not be subject to the provisions of Section 203 of the Delaware General Corporation Law, or Section 203. In general, Section 203 prohibits a publicly held Delaware corporation from engaging in a "business combination" with an "interested stockholder" for a period of three years after the date of the transaction in which the person became an interested stockholder, unless the business combination is approved in a prescribed manner. A "business combination" includes a merger, asset sale or other transaction resulting in a financial benefit to the interested stockholder. An "interested stockholder" is a person who, together with affiliates and associates, owns (or, in certain cases, within three years prior, did own) 15% or more of the corporation's voting stock. Our decision not to be subject to Section 203 will allow, for example, Arthur D. Sams, our Chairman, President, Chief Executive Officer and Secretary (who beneficially owns approximately 55% of our common stock) to transfer shares in excess of 15% of our voting stock to a third-party free of the restrictions imposed by Section 203. This may make us more vulnerable to takeovers that are completed without the approval of our board of directors and/or without giving us the ability to prohibit or delay such takeovers as effectively.

Some provisions of our charter documents and Delaware law may have anti-takeover effects that could discourage an acquisition of us by others, even if an acquisition would be beneficial to our stockholders, and may prevent attempts by our stockholders to replace or remove our current management.

Provisions in our certificate of incorporation and bylaws, as well as provisions of Delaware law, could make it more difficult for a third party to acquire us or increase the cost of acquiring us, even if doing so would benefit our stockholders. These provisions include:

- a requirement that special meetings of stockholders be called only by the board of directors, the president or the chief executive officer;
- advance notice requirements for stockholder proposals and nominations for election to our board of directors; and
- the authority of the board of directors to issue preferred stock on terms determined by the board of directors without stockholder approval and which preferred stock may include rights superior to the rights of the holders of common stock.

These anti-takeover provisions and other provisions in our certificate of incorporation and bylaws could make it more difficult for stockholders or potential acquirers to obtain control of our board of directors or initiate actions that are opposed by the then-current board of directors and could also delay or impede a merger, tender offer or proxy contest involving our Company. These provisions could also discourage proxy contests and make it more difficult for you and other stockholders to elect directors of your choosing or cause us to take other corporate actions you desire. Any delay or prevention of a change of control transaction or changes in our board of directors could cause the market price of our common stock to decline.

Our certificate of incorporation designates the Court of Chancery of the State of Delaware as the sole and exclusive forum for certain types of actions and proceedings that may be initiated by our stockholders, which could limit our stockholders' ability to obtain a favorable judicial forum for disputes with us or our directors, officers or other employees.

Our certificate of incorporation provides that, unless we consent in writing to the selection of an alternative forum, the Court of Chancery of the State of Delaware shall be the sole and exclusive forum for (i) any derivative action or proceeding brought on our behalf, (ii) any action asserting a claim of breach of a fiduciary duty owed by any of our directors, officers or other employees to us or our stockholders, (iii) any action asserting a claim arising pursuant to any provision of the Delaware General Corporation Law, our certificate of incorporation or our bylaws, or (iv) any action asserting a claim against us governed by the internal affairs doctrine. Any person or entity purchasing or otherwise acquiring any interest in shares of our capital stock shall be deemed to have notice of and consented to the provisions of certificate of incorporation described above. This choice of forum provision may limit a stockholder's ability to bring a claim in a judicial forum that it finds favorable for disputes with us or our directors, officers or other employees, which may discourage such lawsuits against us and our directors, officers and other employees. Alternatively, if a court were to find these provisions of our certificate of incorporation inapplicable to, or unenforceable in respect of, one or more of the specified types of actions or proceedings, we may incur additional costs associated with resolving such matters in other jurisdictions, which could adversely affect our business, financial condition or results of operations.

We are an "emerging growth company," and we cannot be certain if the reduced reporting requirements applicable to emerging growth companies will make our shares of common stock less attractive to investors.

We are an "emerging growth company," as defined in the JOBS Act. For as long as we continue to be an emerging growth company, we may take advantage of exemptions from various reporting requirements that are applicable to other public companies that are not emerging growth companies, including not being required to comply with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act of 2002, or the Sarbanes-Oxley Act, reduced disclosure obligations regarding executive compensation in this report, our periodic reports and proxy statements and exemptions from the requirements of holding a nonbinding advisory vote on executive compensation and stockholder approval of any golden parachute payments not previously approved. We could be an emerging growth company for up to five years, although circumstances could cause us to lose that status earlier, including if the market value of our shares of common stock held by non-affiliates exceeds $700 million as of any March 30 before that time or if we have total annual gross revenue of $1.0 billion or more during any fiscal year before that time, in which cases we would no longer be an emerging growth company as of the following December 31, or if we issue more than $1.0 billion in non-convertible debt during any three-year period before that time, in which case we would no longer be an emerging growth company immediately. We cannot predict if investors will find our shares of common stock less attractive because we may rely on these exemptions. If some investors find our shares of common stock less attractive as a result, there may be a less active trading market for our shares of common stock and our share price may be more volatile.

Under the JOBS Act, emerging growth companies also can delay adopting new or revised accounting standards until such time as those standards apply to private companies. We have irrevocably elected not to avail ourselves of this exemption from new or revised accounting standards and, therefore, will be subject to the same new or revised accounting standards as other public companies that are not emerging growth companies.

If we fail to maintain an effective system of internal control over financial reporting, we may not be able to accurately report our financial results or prevent fraud. As a result, stockholders could lose confidence in our financial and other public reporting, which would harm our business and the trading price of our common stock.

Effective internal controls over financial reporting are necessary for us to provide reliable financial reports and, together with adequate disclosure controls and procedures, are designed to prevent fraud. Any failure to implement required new or improved controls, or difficulties encountered in their implementation could cause us to fail to meet our reporting obligations. In addition, any testing by us conducted in connection with Section 404 of the Sarbanes-Oxley Act, or any subsequent testing by our independent registered public accounting firm, may reveal deficiencies in our internal controls over financial reporting that are deemed to be material weaknesses or that may require prospective or retroactive changes to our financial statements or identify other areas for further attention or improvement. Inferior internal controls could also cause investors to lose confidence in our reported financial information, which could have a negative effect on the trading price of our common stock.

We are required to disclose changes made in our internal controls and procedures on a quarterly basis and our management is required to assess the effectiveness of these controls annually. However, for as long as we are an "emerging growth company" under the JOBS Act, our independent registered public accounting firm will not be required to attest to the effectiveness of our internal controls over financial reporting pursuant to Section 404. We could be an "emerging growth company" for up to five years. An independent assessment of the effectiveness of our internal controls could detect problems that our management's assessment might not. Undetected material weaknesses in our internal controls could lead to financial statement restatements and require us to incur the expense of remediation.

We incur significant costs as a result of operating as a public company and our management expects to devote substantial time to public company compliance programs.

As a public company, we incur significant legal, accounting and other expenses due to our compliance with regulations and disclosure obligations applicable to us, including compliance with the Sarbanes-Oxley Act as well as rules implemented by the SEC and Nasdaq. The SEC and other regulators have continued to adopt new rules and regulations and make additional changes to existing regulations that require our compliance. In July 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act, or the Dodd-Frank Act, was enacted. There are significant corporate governance and executive compensation related provisions in the Dodd-Frank Act that have required the SEC to adopt additional rules and regulations in these areas. Stockholder activism, the current political environment, and the current high level of government intervention and regulatory reform may lead to substantial new regulations and disclosure obligations, which may lead to additional compliance costs and impact, in ways we cannot currently anticipate, the manner in which we operate our business. Our management and other personnel devote a substantial amount of time to these compliance programs and monitoring of public company reporting obligations and, as a result of the new corporate governance and executive compensation related rules, regulations, and guidelines prompted by the Dodd-Frank Act and further regulations and disclosure obligations expected in the future, we will likely need to devote additional time and costs to comply with such compliance programs and rules. These rules and regulations cause us to incur significant legal and financial compliance costs and make some activities more time-consuming and costly.

To comply with the requirements of being a public company, we may need to undertake various activities, including implementing new internal controls and procedures and hiring new accounting or internal audit staff. The Sarbanes-Oxley Act requires that we maintain effective disclosure controls and procedures and internal control over financial reporting. We are continuing to develop and refine our disclosure controls and other procedures that are designed to ensure that information required to be disclosed by us in the reports that we file with the SEC is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms, and that information required to be disclosed in reports under the Exchange Act, is accumulated and communicated to our principal executive and financial officers. Our current controls and any new controls that we develop may become inadequate and weaknesses in our internal control over financial reporting may be discovered in the future.

Any failure to develop or maintain effective controls could adversely affect the results of periodic management evaluations and annual independent registered public accounting firm attestation reports regarding the effectiveness of our internal control over financial reporting which we may be required to include in our periodic reports we will file with the SEC under Section 404 of the Sarbanes-Oxley Act, harm our operating results, cause us to fail to meet our reporting obligations, or result in a restatement of our prior period financial statements. In the event that we are not able to demonstrate compliance with the Sarbanes-Oxley Act, that our internal control over financial reporting is perceived as inadequate or that we are unable to produce timely or accurate financial statements, investors may lose confidence in our operating results and the price of our common stock could decline. In addition, if we are unable to continue to meet these requirements, we may not be able to remain listed on the Nasdaq Capital Market.

We are not currently required to comply with the SEC rules that implement Section 404 of the Sarbanes-Oxley Act, and are therefore not yet required to make a formal assessment of the effectiveness of our internal control over financial reporting for that purpose. However, we are required to comply with certain of these rules, which require management to certify financial and other information in our quarterly and annual reports and provide an annual management report on the effectiveness of our internal control over financial reporting commencing with our next annual report. This assessment will need to include the disclosure of any material weaknesses in our internal control over financial reporting identified by our management or our independent registered public accounting firm. We are just beginning the costly and challenging process of compiling the system and processing documentation needed to comply with such requirements. We may not be able to complete our evaluation, testing and any required remediation in a timely fashion. During the evaluation and testing process, if we identify one or more material weaknesses in our internal control over financial reporting, we will be unable to assert that our internal control over financial reporting is effective.

Raising additional capital, including through future sales and issuances of our common stock, the exercise of warrants or the exercise of rights to purchase common stock pursuant to our equity incentive plan could result in additional dilution of the percentage ownership of our stockholders, could cause our share price to fall and could restrict our operations.

We expect that significant additional capital will be needed in the future to continue our planned operations, including any potential acquisitions, purchasing of capital equipment, hiring new personnel, and continuing activities as an operating public company. To the extent we seek additional capital through a combination of public and private equity offerings and debt financings, our stockholders may experience substantial dilution. To the extent that we raise additional capital through the sale of equity or convertible debt securities, the ownership interest of our existing stockholders may be diluted, and the terms may include liquidation or other preferences that adversely affect the rights of our stockholders. Debt and receivables financings may be coupled with an equity component, such as warrants to purchase shares of our common stock, which could also result in dilution of our existing stockholders' ownership. The incurrence of indebtedness would result in increased fixed payment obligations and could also result in certain restrictive covenants, such as limitations on our ability to incur additional debt and other operating restrictions that could adversely impact our ability to conduct our business. A failure to obtain adequate funds may cause us to curtail certain operational activities, including sales and marketing, in order to reduce costs and sustain the business, and would have a material adverse effect on our business and financial condition.

Under our 2016 Plan, we may grant equity awards covering up to 1,754,385 shares of our common stock. As of the date of this Quarterly Report on Form 10-Q, we had granted options to purchase an aggregate of 360,000 shares of our common stock under the 2016 Plan. We have registered 1,754,385 shares of common stock available for issuance under our 2016 Plan. Sales of shares issued upon exercise of options or granted under our 2016 Plan may result in dilution to our existing stockholders, which could cause our share price to fall.

Our issuance of shares of preferred stock could adversely affect the market value of our common stock, dilute the voting power of common stockholders and delay or prevent a change of control.

Our board of directors has the authority to cause us to issue, without any further vote or action by the stockholders, up to 5,000,000 shares of preferred stock in one or more series, to designate the number of shares constituting any series, and to fix the rights, preferences, privileges and restrictions thereof, including dividend rights, voting rights, rights and terms of redemption, redemption price or prices and liquidation preferences of such series.

The issuance of shares of preferred stock with dividend or conversion rights, liquidation preferences or other economic terms favorable to the holders of preferred stock could adversely affect the market price for our common stock by making an investment in the common stock less attractive. For example, investors in the common stock may not wish to purchase common stock at a price above the conversion price of a series of convertible preferred stock because the holders of the preferred stock would effectively be entitled to purchase common stock at the lower conversion price causing economic dilution to the holders of common stock.

Further, the issuance of shares of preferred stock with voting rights may adversely affect the voting power of the holders of our other classes of voting stock either by diluting the voting power of our other classes of voting stock if they vote together as a single class, or by giving the holders of any such preferred stock the right to block an action on which they have a separate class vote even if the action were approved by the holders of our other classes of voting stock. The issuance of shares of preferred stock may also have the effect of delaying, deferring or preventing a change in control of our company without further action by the stockholders, even where stockholders are offered a premium for their shares.

Claims for indemnification by our directors and officers may reduce our available funds to satisfy successful third-party claims against us and may reduce the amount of money available to us.

Our certificate of incorporation and bylaws provide that we will indemnify our directors and officers, in each case to the fullest extent permitted by Delaware law. In addition, as permitted by Section 145 of the Delaware General Corporation Law, our bylaws and the indemnification agreements that we have entered into with our directors and officers provide that:

- We will indemnify our directors and officers for serving us in those capacities or for serving other business enterprises at our request, to the fullest extent permitted by Delaware law. Delaware law provides that a corporation may indemnify such person if such person acted in good faith and in a manner such person reasonably believed to be in or not opposed to the best interests of the registrant and, with respect to any criminal proceeding, had no reasonable cause to believe such person's conduct was unlawful.

- We may, in our discretion, indemnify employees and agents in those circumstances where indemnification is permitted by applicable law.

- We are required to advance expenses, as incurred, to our directors and officers in connection with defending a proceeding, except that such directors or officers shall undertake to repay such advances if it is ultimately determined that such person is not entitled to indemnification.

- We will not be obligated pursuant to our bylaws to indemnify a person with respect to proceedings initiated by that person against us or our other indemnitees, except with respect to proceedings authorized by our board of directors or brought to enforce a right to indemnification.

- The rights conferred in our bylaws are not exclusive, and we are authorized to enter into indemnification agreements with our directors, officers, employees and agents and to obtain insurance to indemnify such persons.

- We may not retroactively amend our bylaw provisions to reduce our indemnification obligations to directors, officers, employees and agents.

To the extent that a claim for indemnification is brought by any of our directors or officers, it would reduce the amount of funds available for use in our business.

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

None.

ITEM 3. Defaults Upon Senior Securities

Not applicable.

ITEM 4. Mine Safety Disclosure.

Not applicable.

ITEM 5. Other Information

None.

ITEM 6. Exhibits

Reference is made to the exhibits listed on the Index to Exhibits.

INDEX TO EXHIBITS

Exhibit Number	Description
31.1	Certification Required by Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification Required by Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema
101.CAL	XBRL Taxonomy Extension Calculation Linkbase
101.DEF	XBRL Taxonomy Extension Definition Linkbase
101.LAB	XBRL Taxonomy Extension Label Linkbase
101.PRE	XBRL Taxonomy Extension Presentation Linkbase

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, thereunto duly authorized.

Date: November 14, 2019

POLAR POWER, INC.

By: /s/ Arthur D. Sams
Arthur D. Sams
President, Chief Executive Officer and Secretary

Exhibit 31.1

CERTIFICATION

I, Arthur D. Sams, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Polar Power, Inc.;

2. Based on my knowledge, this 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 period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 14, 2019

/s/ Arthur D. Sams
Arthur D. Sams
President, Chief Executive Officer
and Secretary
(Principal Executive Officer)

Exhibit 31.2

CERTIFICATION

I, Luis Zavala, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Polar Power, Inc.;

2. Based on my knowledge, this 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 period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 14, 2019

/s/ Luis Zavala
Luis Zavala
Chief Financial Officer
(Principal Financial Officer)

Exhibit 32.1

CERTIFICATIONS OF CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER PURSUANT TO 18 U.S.C. SECTION 1350 AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report on Form 10-Q of Polar Power, Inc. (the "Company") for the quarterly period ended September 30, 2019, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned hereby certify in their capacities as the Chief Executive Officer and the Chief Financial Officer of the Company, respectively, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

2. the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: November 14, 2019

/s/ Arthur D. Sams	/s/ Luis Zavala
Arthur D. Sams	Luis Zavala
President and Chief Executive Officer	Chief Financial Officer
(Principal Executive Officer)	(Principal Financial Officer)

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signatures that appear in typed form within the electronic version of this written statement required by Section 906, has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.