ENOVA SYSTEMS INC
Form 10-Q
May 20, 2014

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

FORM 10-Q

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ending March 31, 2014

or

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____________ to ______________

Commission file no. 1-33001

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

California (State or other jurisdiction of incorporation or organization)	95-3056150 (I.R.S. Employer Identification Number)

2945 Columbia Street, Torrance, California 90503
(Address of principal executive offices, including zip code)

(650) 346-4770
(Registrant's telephone number, including area code)

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 periods that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes [X] No [ ]

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

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

Large accelerated filer	[ ]	Accelerated filer	[ ]
Non-accelerated filer	[ ]	Smaller reporting company	[X]

(Do not check if a smaller reporting company)

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

As of April 30, 2014, there were 64,520,195 shares of common stock outstanding.

ENOVA SYSTEMS, INC.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

ENOVA SYSTEMS, INC.

BALANCE SHEETS

	March 31, 2014 (unaudited)	December 31, 2013
ASSETS		
Current assets:		
Cash and cash equivalents	$ 114,000	$ 1,000
Accounts receivable, net	-	-
Inventories and supplies, net	427,000	427,000
Prepaid expenses and other current assets	30,000	42,000
Total current assets	571,000	470,000
Long term accounts receivable	-	-
Property and equipment, net	69,000	80,000
Total assets	$ 640,000	$ 550,000
LIABILITIES AND STOCKHOLDERS' DEFICIT		
Current liabilities:		
Accounts payable	$ 546,000	$ 642,000
Loans from employees	68,000	36,000
Deferred revenues	213,000	213,000
Accrued payroll and related expenses	217,000	194,000
Accrued loss for litigation settlement	2,014,000	2,014,000
Other accrued liabilities	346,000	294,000
Current portion of notes payable	40,000	40,000
Total current liabilities	3,444,000	3,433,000
Accrued interest payable	1,420,000	1,401,000
Notes payable, net of current portion	1,238,000	1,238,000
Total liabilities	6,102,000	6,072,000
Stockholders' deficit:		
Series A convertible preferred stock — no par value, 30,000,000 shares authorized; 0 shares issued and outstanding; liquidating preference at $0.60 per share as of March 31, 2014 and December 31, 2013	-	-
Series B convertible preferred stock — no par value, 5,000,000 shares authorized; 546,000 shares issued and outstanding; liquidating preference at $2 per share as of March 31, 2014 and December 31, 2013	1,094,000	1,094,000
Common Stock to be issued	528,000	528,000
Common Stock — no par value, 750,000,000 shares authorized; 64,520,000 and 44,520,000 shares issued and outstanding as of March 31, 2014 and December 31, 2013, respectively	145,735,000	145,512,000
Additional paid-in capital	9,599,000	9,595,000
Accumulated deficit	(162,418,000)	(162,251,000)
Total stockholders' deficit	(5,462,000)	(5,522,000)
Total liabilities and stockholders' deficit	$ 640,000	$ 550,000

See accompanying condensed notes to these financial statements.

ENOVA SYSTEMS, INC.
STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended March 31	
	2014	2013
Revenues	$ -	$ 53,000
Cost of revenues	-	56,000
Gross income (loss)	-	(3,000)
Operating expenses		
Research and development	-	-
Selling, general & administrative	136,000	383,000
Total operating expenses	136,000	383,000
Operating loss	(136,000)	(386,000)
Other income and (expense)		
Interest and other income (expense)	(31,000)	(20,000)
Total other income and (expense)	(31,000)	(20,000)
Net loss	$ (167,000)	$ (406,000)
Basic and diluted loss per share	$ (0.00)	$ (0.01)
Weighted average number of common shares outstanding	46,742,000	44,520,000

See accompanying condensed notes to these financial statements.

ENOVA SYSTEMS, INC.
STATEMENTS OF CASH FLOWS
(Unaudited)

	Three Months Ended March 31	
Cash flows from operating activities:	2014	2013
Net loss	$ (167,000)	$ (406,000)
Adjustments to reconcile net loss to net cash used in operating activities:		
Inventory reserve	-	11,000
Inventory write-off	-	(11,000)
Depreciation and amortization	11,000	58,000
Loss on asset disposal	-	10,000
Stock option expense	4,000	2,000
(Increase) decrease in:		
Accounts receivable	-	123,000
Inventory and supplies	-	(29,000)
Prepaid expenses and other current assets	12,000	(49,000)
Long term receivables	-	25,000
Increase (decrease) in:		
Accounts payable	(96,000)	(96,000)
Deferred revenues	-	315,000
Accrued payroll and related expense	23,000	(23,000)
Other accrued liabilities	52,000	20,000
Accrued interest payable	19,000	21,000
Net cash used in operating activities	(142,000)	(29,000)
Cash flows from investing activities:		
Net cash used in investing activities	-	-
Cash flows from financing activities:		
Net proceeds from the issuance of common stock	223,000	-
Proceeds from related party loans	32,000	-
Payment on notes payable	-	(6,000)
Net cash provided by (used in) financing activities	255,000	(6,000)
Net decrease in cash and cash equivalents	113,000	(35,000)
Cash and cash equivalents, beginning of period	1,000	57,000
Cash and cash equivalents, end of period	$ 114,000	$ 22,000
Supplemental disclosure of cash flow information:		
Interest paid	$ -	$ 2,000

See accompanying condensed notes to these financial statements.

ENOVA SYSTEMS, INC.

CONDENSED NOTES TO FINANCIAL STATEMENTS
(Unaudited)

1. Description of the Company and its Business

Enova Systems, Inc., ("Enova", "We" or "the Company"), a California corporation, was incorporated in July 1976, and trades on the OTCQB under the trading symbol "ENVS" and on the London Stock Exchange under the symbol "ENV" or "ENVS". The Company believes it has been a globally recognized leader as a supplier of efficient, environmentally-friendly digital power components and systems products, in conjunction with associated engineering services. The Company's core competencies are focused on the commercialization of power management and conversion systems for mobile and stationary applications.

THE DISCUSSION SET FORTH BELOW AND ELSEWHERE IN THIS 10-Q IS QUALIFIED IN ITS ENTIRETY BY THE FOLLOWING: ENOVA REMAINS INSOLVENT AND OWES IN EXCESS OF $4.5 MILLION IN THE AGGREGATE TO ITS TWO PRINCIPAL CREDITORS, THE CREDIT MANAGERS ASSOCIATION AND ARENS CONTROLS COMPANY, L.L.C. ("ARENS"). WITHOUT IMMEDIATE ADDITIONAL FINANCING OR COLLECTION OF RECEIVABLES, THE COMPANY WILL NEED TO CEASE OPERATIONS. THE COMPANY CURRENTLY HAS NO VISIBILITY AS TO EITHER ADDITIONAL FINANCING OR THE COLLECTION OF RECEIVABLES. SPECIFICALLY, WITHOUT A MUTUALLY ACCEPTABLE SETTLEMENT OF THE ARENS JUDGMENT ARISING OUT OF ARENS CONTROLS COMPANY, L.L.C. v. ENOVA SYSTEMS, INC., CASE NO. 13-1102 (7TH CIRCUIT) IN THE AMOUNT OF $2.0 MILLION, THE COMPANY DOES NOT CURRENTLY BELIEVE IT HAS ANY ALTERNATIVE OTHER THAN TO CEASE OPERATIONS. THE COMPANY CURRENTLY EMPLOYS ONLY TWO PERSONNEL, JOHN MICEK, THE COMPANY'S CEO, CFO AND SECRETARY, AND ONE ADDITIONAL INDIVIDUAL IN THE FINANCE DEPARTMENT.

ON SEPTEMBER 24, 2013, THE COMPANY ENTERED INTO A SETTLEMENT AGREEMENT AND MUTUAL RELEASE WITH ARENS PROVIDING A PERIOD OF 120 DAYS TO SETTLE THE JUDGMENT FOR THE AMOUNT OF $300,000. THE COMPANY WAS NOT ABLE TO MAKE THE PAYMENT BY THE DUE DATE OF JANURY 22, 2014. THEREFORE, THE JUDGMENT AGAINST THE COMPANY CAN BE ENFORCED WITHOUT FURTHER NOTICE.

2. Summary of Significant Accounting Policies

Basis of Presentation — Interim Financial Statements

The financial information as of and for the three ended March 31, 2014 and 2013 is unaudited but includes all adjustments (consisting only of normal recurring adjustments) that the Company considers necessary for a fair statement of its financial position at such dates and the operating results and cash flows for those periods. The year-end balance sheet data was derived from audited financial statements, and certain information and note disclosures normally included in annual financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to SEC rules or regulations; however, the Company believes the disclosures made are adequate to make the information presented not misleading.

The preparation of financial statements in conformity with U.S. generally accepted accounting principles 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 revenues and expenses during the reporting period. Although management believes these estimates and assumptions are adequate, actual results could differ from the estimates and assumptions used.

The results of operations for the interim periods presented are not necessarily indicative of the results of operations to be expected for the year. These interim financial statements should be read in conjunction with the audited financial statements for the year ended December 31, 2013, which are included in the Company's Annual Report on Form 10-K for the year then ended.

Liquidity and Going Concern

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. However, historically the Company has experienced significant recurring net losses and operating cash flow deficits. The Company's ability to continue as a going concern is dependent on many factors, including among others, its ability to raise additional funding, and its ability to successfully restructure operations to lower manufacturing costs and reduce operating expenses.

To date, the Company has incurred recurring net losses and negative cash flows from operations. At March 31, 2014, the Company had an accumulated deficit of approximately $162.4 million, cash and cash equivalents of $114,000, working capital of approximately negative $2.9 million and shareholders' deficit of approximately $5.5 million. Until the Company can generate significant cash from its operations, the Company expects to continue to fund its operations with existing cash resources, proceeds from one or more private placement agreements, as well as potentially through debt financing or the sale of equity securities. However, the Company may not be successful in obtaining additional funding. In addition, the Company cannot be sure that its existing cash and investment resources will be adequate or that additional financing will be available when needed or that, if available, financing will be obtained on terms favorable to the Company or its stockholders.

Our operations will require us to make necessary investments in human and production resources, regulatory compliance, as well as sales and marketing efforts. We do not currently have adequate internal liquidity to meet these objectives in the long term. On June 21, 2012, we reported in a Form 8-K filing that, as part of cost cutting measures in response to our decrease in revenue amid continued delays in industry adoption of EV technology resulting from ongoing battery cost and reliability concerns, in excess of 80% of our workforce left our Company, including the resignation of members of our senior management. We continue to evaluate strategic partnering opportunities and other external sources of liquidity, including the public and private financial markets and strategic partners. As a result of having insufficient funds, the Company has delayed all of its product development. Failure to obtain adequate financing also will adversely affect the Company's ability to continue in business. If the Company raises additional funds by issuing equity securities, substantial dilution to existing stockholders would likely result. If the Company raises additional funds by incurring debt financing, the terms of the debt may involve significant cash payment obligations, as well as covenants and specific financial ratios that may restrict its ability to operate its business.

The Company continues to pursue other options to raise additional capital to fund its operations; however, there can be no assurance that we can successfully raise additional funds through the capital markets.

As of March 31, 2014, the Company had approximately $114,000 in cash and cash equivalents and does not anticipate that its anticipated receivables collections will be sufficient to meet its projected operating requirements through December 2014 to continue operations and market trading.

Significant Accounting Policies

The accounting and reporting policies of the Company conform to US GAAP. There have been no significant changes in the Company's significant accounting policies during the three months ended March 31, 2014 compared to what was previously disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2013.

Revenue Recognition

The Company manufactures proprietary products and other products based on design specifications provided by its customers. The Company recognizes revenue only when all of the following criteria have been met:

- Persuasive Evidence of an Arrangement — The Company documents all terms of an arrangement in a written contract signed by the customer prior to recognizing revenue.

- Delivery Has Occurred or Services Have Been Rendered — The Company performs all services or delivers all products prior to recognizing revenue. Professional consulting and engineering services are considered to be performed when the services are complete. Equipment is considered delivered upon delivery to a customer's designated location. In certain instances, the customer elects to take title upon shipment.

- The Fee for the Arrangement is Fixed or Determinable — Prior to recognizing revenue, a customer's fee is either fixed or determinable under the terms of the written contract. Fees for professional consulting services, engineering services and equipment sales are fixed under the terms of the written contract. The customer's fee is negotiated at the outset of the arrangement and is not subject to refund or adjustment during the initial term of the arrangement.

- Collectability is Reasonably Assured — The Company determines that collectability is reasonably assured prior to recognizing revenue. Collectability is assessed on a customer-by-customer basis based on criteria outlined by management. New customers are subject to a credit review process which evaluates the customer's financial position and ultimately its ability to pay. The Company does not enter into arrangements unless collectability is reasonably assured at the outset. Existing customers are subject to ongoing credit evaluations based on payment history and other factors. If it is determined during the arrangement that collectability is not reasonably assured, revenue is recognized on a cash basis. Amounts received upfront for engineering or development fees under multiple-element arrangements are deferred and recognized over the period of committed services or performance, if such arrangements require the Company to provide on-going services or performance. All amounts received under collaborative research agreements or research and development contracts are nonrefundable, regardless of the success of the underlying research.

The Company recognizes revenue from milestone payments over the remaining minimum period of performance obligations.

The Company also recognizes engineering and construction contract revenues using the percentage-of-completion method, based primarily on contract costs incurred to date compared with total estimated contract costs. Customer-furnished materials, labor, and equipment, and in certain cases subcontractor materials, labor, and equipment, are included in revenues and cost of revenues when management believes that the company is responsible for the ultimate acceptability of the project. Contracts are segmented between types of services, such as engineering and construction, and accordingly, revenue and gross margin related to each activity is recognized as those separate services are rendered.

Changes to total estimated contract costs or losses, if any, are recognized in the period in which they are determined. Claims against customers are recognized as revenue upon settlement. Revenues recognized in excess of amounts received are classified as current assets. Amounts billed to clients in excess of revenues recognized to date are classified as current liabilities on contracts.

Changes in project performance and conditions, estimated profitability, and final contract settlements may result in future revisions to engineering and development contract costs and revenue.

These accounting policies were applied consistently for all periods presented. Our operating results would be affected if other alternatives were used. Information about the impact on our operating results is included in the footnotes to our financial statements.

Several other factors related to the Company may have a significant impact on our operating results from year to year. For example, the accounting rules governing the timing of revenue recognition related to product contracts are complex and it can be difficult to estimate when we will recognize revenue generated by a given transaction. Factors such as acceptance of services provided, payment terms, creditworthiness of the customer, and timing of delivery or acceptance of our products often cause revenues related to sales generated in one period to be deferred and recognized in later periods. For arrangements in which services revenue is deferred, related direct and incremental costs may also be deferred.

Deferred Revenues

The Company recognizes revenues as earned. Amounts billed in advance of the period in which service is rendered are recorded as a liability under deferred revenues. When the Company enters into production and development contracts with customers, an evaluation is made to ascertain the specific revenue generating activities of each contract and establishes the units of accounting for each activity. Revenue on these units of accounting is not recognized until a) there is persuasive evidence of the existence of a contract, b) the service has been rendered and delivery has occurred, c) there is a fixed and determinable price, and d) collectability is reasonable assured.

Warranty Costs

The Company provides product warranties for specific product lines and accrues for estimated future warranty costs in the period in which revenue is recognized. Our products are generally warranted to be free of defects in materials and workmanship for a period of 12 to 24 months from the date of installation, subject to standard limitations for equipment that has been altered by other than Enova Systems personnel and equipment which has been subject to negligent use. Warranty provisions are based on past experience of product returns, number of units repaired and our historical warranty incidence over the past twenty-four month period. The warranty liability is evaluated on an ongoing basis for adequacy and may be adjusted as additional information regarding expected warranty costs becomes known.

Stock Based Compensation

We measure the compensation cost for stock-based awards classified as equity at their fair value on the date of grant and recognize compensation expense over the service period for awards expected to vest, net of estimated forfeitures.

Loss Per Share

Basic loss per share is computed by dividing loss available to common stockholders by the weighted-average number of common shares outstanding. Diluted loss per share is computed similar to basic loss per share except that the denominator is increased to include the number of additional common shares that would have been outstanding if the potential common shares had been issued and if the additional common shares were dilutive. Common equivalent shares are excluded from the computation if their effect is anti-dilutive. The Company’s common share equivalents consist of stock options, warrants and preferred stock.

The potential shares, which are excluded from the determination of basic and diluted net loss per share as their effect is anti-dilutive, are as follows:

	Three Months Ended March 31,	
	2014	2013
Options to purchase common stock	5,210,000	810,000
Warrants to purchase common stock	11,250,000	11,250,000
Series A and B preferred shares conversion	83,000	83,000
Potential equivalent shares excluded	16,543,000	12,143,000

Accounting Changes and Recent Accounting Pronouncements

Certain accounting standards that have been issued or proposed by the FASB or other standards-setting bodies are not expected to have a material impact on the Company’s financial position, results of operations and cash flows.

3. Inventory

Inventory, consisting of materials, labor and manufacturing overhead, is stated at the lower of cost (first-in, first-out) or market and consisted of the following at:

	March 31, 2014	December 31, 2013
Raw materials	$ 3,098,000	$ 3,098,000
Work-in-process	222,000	222,000
Finished goods	449,000	449,000

Reserve for obsolescence		(3,342,000)		(3,342,000)
	$	427,000	$	427,000

The Company did not have production operations in the three months ended March 31, 2014. Therefore, there was no change the balance of inventory between December 31, 2013 and March 31, 2014. Inventory valuation adjustments and other inventory write-offs amounted to $11,000 for the three months ended March 31, 2013.

4. Property and Equipment

Property and equipment consisted of the following at:

	March 31, 2014	December 31, 2013
Computers and software	$ 59,000	$ 59,000
Machinery and equipment	251,000	251,000
Furniture and office equipment	86,000	86,000
Demonstration vehicles and buses	127,000	127,000
	523,000	523,000
Less accumulated depreciation and amortization	(454,000)	(443,000)
Total	$ 69,000	$ 80,000

Depreciation and amortization expense was $11,000 and $58,000 for the three months ended March 31, 2014 and 2013, respectively, and within those total expenses, the amortization of leasehold improvements was $0 and $22,000 for the three months ended March 31, 2014 and 2013. The Company's headquarters lease expired on January 31, 2013 and the balance of leasehold improvements was decreased to $0. In addition, an evaluation of fixed assets as of March 31, 2013 identified $367,000 in obsolete fixed assets which were disposed of or abandoned and a loss on disposal of fixed assets of $10,000 was recorded in the three months ended March 31, 2013. There was no impairment charge recorded in the three months ended March 31, 2014.

5. Other Accrued Liabilities

Other accrued liabilities consisted of the following at:

	March 31, 2014	December 31, 2013
Accrued inventory received	$ 10,000	$ 10,000
Accrued professional services	219,000	161,000
Accrued warranty	74,000	74,000
Other	43,000	49,000
Total	$ 346,000	$ 294,000

Accrued warranty consisted of the following activities during the three months ended March 31:

	2014	2013
Balance at beginning of year	$ 74,000	$ 117,000
Accruals for warranties issued during the period	-	10,000
Warranty claims	-	(34,000)
Balance at end of quarter	$ 74,000	$ 93,000

6. Notes Payable, Long-Term Debt and Other Financing

Notes payable consisted of the following at:

	March 31, 2014	December 31, 2013
	$ 1,238,000	$ 1,238,000

Secured note payable to Credit Managers Association of California, bearing interest at prime plus 3% (6.25% as of March 31, 2014), and is adjusted annually in April through maturity. Principal and unpaid interest due in April 2016. A sinking fund escrow may be funded with 10% of future equity financing, as defined in the Agreement						
Secured note payable to Coca Cola Enterprises in the original amount of $40,000, bearing interest at 10% per annum. Principal and unpaid interest due on demand		40,000			40,000	
		1,278,000			1,278,000	
Less current portion of notes payable		(40,000	)		(40,000	)
Notes payable, net of current portion	$	1,238,000		$	1,238,000	

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As of March 31, 2014 and December 31, 2013, the balance of long term interest payable amounted to $1,420,000 and $1,401,000, respectively, of which the Credit Managers Association of California note amounted to $1,383,000 and $1,365,000, respectively. Interest expense on notes payable amounted to approximately $19,000 and $21,000 for the three months ended March 31, 2014 and 2013, respectively.

In June 2013, the vehicle that secured the note payable due March 10, 2016 was repossessed by the secured lender. The Company was invoiced by the lender for $8,000 for final settlement, which is included in accounts payable at March 31, 2014 and December 31, 2013, respectively. In the fourth quarter of 2013, three vehicles that secured notes due on February 19, 2014, August 25, 2014 and April 9, 2015 were repossessed by the secured lenders. The Company has accrued approximately $18,000 for final settlements for the three vehicles, which is included in other accrued liabilities at March 31, 2014 and December 31, 2013, respectively.

7. Deferred Revenues

The Company had deferred $213,000 in revenue related to a production contract at March 31, 2014 and December 31, 2013. The Company's management is attempting to obtain funding to complete the order in the second quarter of 2014.

8. Stockholders' Equity

On February 23, 2014, Enova Systems, Inc, entered into Subscription Agreements with various offshore investors to sell approximately GBP 150,000 (approximately US$249,000) in gross proceeds by a private subscription of 19,999,998 common shares to be newly issued on the Alternative Investment Market of the London Stock Exchange (the "AIM Exchange"). The common shares were issued at a price of 0.0075 pence (approximately US$0.01per share) to certain eligible offshore investors (the "Subscription"). In connection with the Subscription, Enova entered into an Agreement for the Provision of Receiving Agent Services (the "Agreement") with Daniel Stewart & Company PLC (UK) for receiving agent services. Daniel Stewart presently serves as the Nominated Adviser for the listing of Enova's common shares on the AIM Exchange. The newly issued common shares for the Subscription were issued in three tranches of approximately GBP 50,000 each.

Daniel Stewart received an introducing agent's fee of 10% of the aggregate funds raised pursuant to the subscription in addition to reimbursement of expenses. Factoring in the commission, legal and other expenses of the offering, Enova received approximately US$223,000 in net proceeds.

The offer and sale of the shares were made pursuant to Regulation S under the Securities Act of 1933, as amended (the "Securities Act"). Among other things, each investor purchasing shares of Enova's common stock in the offering represented that the investor is not a United States person as defined in Regulation S. In addition, neither Enova nor the receiving agent conducted any selling efforts directed at the United States in connection with the offering. All shares of common stock issued in the offering included a restrictive legend indicating that the shares were issued pursuant to Regulation S under the Securities Act and are deemed to be "restricted securities." As a result, the purchasers of such shares will not be able to resell the shares unless in accordance with Regulation S, pursuant to a registration statement, or upon reliance of an applicable exemption from registration under the Securities Act. The shares to be sold pursuant to the Subscription Agreements were not registered under the Securities Act, and there is no obligation on the part of Enova to so register such shares.

During the three months ended March 31, 2014 and 2013, the Company did not issue any shares of common stock to directors or employees as compensation.

9. Stock Options

Stock Option Program Description

As of March 31, 2014, the Company had two equity compensation plans, the 1996 Stock Option Plan (the “1996 Plan”) and the 2006 equity compensation plan (the “2006 Plan”). The 1996 Plan has expired for the purposes of issuing new grants. However, the 1996 Plan will continue to govern awards previously granted under that plan. The 2006 Plan has been approved by the Company’s shareholders. Equity compensation grants are designed to reward employees and executives for their long term contributions to the Company and to provide incentives for them to remain with the Company. The number and frequency of equity compensation grants are based on competitive practices, operating results of the company, and government regulations.

The maximum number of shares issuable over the term of the 1996 Plan was limited to 65 million shares (without giving effect to subsequent stock splits). Options granted under the 1996 Plan typically have an exercise price of 100% of the fair market value of the underlying stock on the grant date and expire no later than ten years from the grant date. On August 27, 2013, the Board of Directors of Enova Systems approved amendments to Enova's 2006 Equity Compensation Plan (a) to increase the number of shares authorized for issuance from 3,000,000 shares to 9,000,000 shares and (b) to increase the number of shares of common stock that may be issued to an individual in any calendar year from 500,000 shares to 5,000,000 shares. Of the 9,000,000 shares reserved for issuance under the amended 2006 Plan, none were granted in the three months ended March 31, 2014 and 2013 and 3,780,000 shares were available for grant as of March 31, 2014. Options granted under the 2006 Plan have terms of between three and ten years and generally vest and become fully exercisable from one to three years from the date of grant or vest according to the price performance of our shares.

Stock-based compensation expense related to stock options was $4,000 and $2,000 for the three months ended March 31, 2014 and 2013, respectively. As of March 31, 2014, the total compensation cost related to non-vested awards not yet recognized is $37,000. The remaining period over which the future compensation cost is expected to be recognized is 27 months.

The following table summarizes information about stock options outstanding and exercisable at March 31, 2014:

	Number of Share Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term in Years	Aggregate Intrinsic Value(1)
Outstanding at December 31, 2013	5,210,000	$ 0.12	2.72	$ —
Granted	—	$ —	—	$ —
Exercised	—	$ —	—	$ —
Forfeited or Cancelled	69,000	$ 1.26	—	$ —
Outstanding at March 31, 2014	5,141,000	$ 0.10	2.42	$ —
Exercisable at March 31, 2014	632,000	$ 0.67	2.65	$ —
Vested and expected to vest (2)	5,141,000	$ 0.10	2.42	$ —

(1) Aggregate intrinsic value represents the value of the closing price per share of our common stock on the last trading day of the fiscal period in excess of the exercise price multiplied by the number of options outstanding or exercisable, except for the "Exercised" line, which uses the closing price on the date exercised.
(2) Number of shares includes options vested and those expected to vest net of estimated forfeitures.

The exercise prices of the options outstanding at March 31, 2014 ranged from $0.07 to $4.35. The Company's policy is to issue shares from its authorized shares upon the exercise of stock options.

Unvested share activity for the three months ended March 31, 2014 is summarized below:

	Unvested Number of Options	Weighted Average Grant Date Fair Value
Unvested balance at December 31, 2013	4,535,000	$ 0.02

Granted	—	$	—
Vested	(25,000)	$	0.11
Forfeited	—	$	—
Unvested balance at March 31, 2014	4,510,000	$	0.02

The fair values of all stock options granted are estimated on the date of grant using the Black-Scholes option-pricing model. During the three months ended March 31, 2014 and 2013 no options were granted.

The estimated fair value of grants of stock options to nonemployees of the Company is charged to expense in the financial statements. These options vest in the same manner as the employee options granted under each of the option plans as described above.

10. Warrants

In December 2011, the Company completed a private equity placement of 11,250,000 shares of common stock for $1,245,000 together with warrants to purchase up to 11,250,000 shares of common stock to a group of 17 shareholders (the “Low-Beer Managed Accounts”). The warrants are exercisable for a period of five years and exercisable at a price of $0.22 per share. The warrants further provide that if, for a twenty consecutive trading day period, the average of the closing price quoted on the OTCQB market is greater than or equal to $0.44 per share, with at least an average of 10,000 shares traded per day, then, on the 10th calendar day following written notice from the Company, any outstanding warrants will be deemed automatically exercised pursuant to the cashless/net exercise provisions under the warrants.

The following is a summary of changes to outstanding warrants during the quarter ended March 31, 2014:

	Number of Share Options		Weighted Average Exercise Price	Weighted Average Remaining Contractual Life
Outstanding at December 31, 2013	111,250,000	$	0.22	2.75
Granted	—	$	—	—
Exercised	—	$	—	—
Forfeited or Cancelled	—	$	—	—
Outstanding at March 31, 2014	11,250,000	$	0.22	2.75
Exercisable at March 31, 2014	11,250,000	$	0.22	2.75

11. Concentrations

The Company's trade receivables are concentrated with a few customers. The Company performs credit evaluations on its customers’ financial condition and generally requires no collateral from its customers. Concentrations of credit risk, with respect to accounts receivable, exist to the extent of amounts presented in the financial statements. Two customers represented 62% and 38%, respectively, of gross accounts receivable at March 31, 2014 and December 31, 2013, respectively.

The Company's revenues are concentrated with a few customers. The Company did not have revenue for the three months ended March 31, 2014, and for the three months ended March 31, 2013, three customers represented 60%, 24% and 14% of gross revenues.

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

This Quarterly Report on Form 10-Q contains statements indicating expectations about future performance and other forward-looking statements that involve risks and uncertainties. We usually use words such as "may," "will," "should," "expect," "plan," "anticipate," "believe," "estimate," "predict," "future," "intend," "potential," or "continue" or the negative or similar expressions to identify forward-looking statements. These statements appear throughout this Quarterly Report on Form 10-Q and are statements regarding our current intent, belief or expectation, primarily with respect to our operations and related industry developments. Examples of these statements include, but are not limited to, statements regarding the following: our future operating expenses, our future losses, our future expenditures for research and development and the sufficiency of our cash resources. 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 our Annual Report on Form 10-K for the year ended December 31, 2013, as updated by the disclosure contained in Item 1A of Part II of this Form 10-Q.

The following discussion and analysis should be read in conjunction with the unaudited interim financial statements and notes thereto included in Part I, Item 1 of this Quarterly Report on Form 10-Q and with the financial statements and notes thereto and Management's Discussion and Analysis of Financial Condition and Results of Operations contained in our Annual Report on Form 10-K for the year ended December 31, 2013.

Enova believes it has been a leader in the development, design and production of proprietary, power train systems and related components for electric and hybrid electric buses and medium and heavy duty commercial vehicles. Electric drive systems are comprised of an electric motor, electronics control unit and a gear unit which power a vehicle. Hybrid electric systems, which are similar to pure electric drive systems, contain an internal combustion engine in addition to the electric motor, and may eliminate external recharging of the battery system. A hydrogen fuel cell based system is similar to a hybrid system, except that instead of an internal combustion engine, a fuel cell is utilized as the power source. A fuel cell is a system which combines hydrogen and oxygen in a chemical process to produce electricity.

A fundamental element of Enova's strategy has been to develop and produce advanced proprietary software and hardware for applications in these alternative power markets. Our focus has been on powertrain systems including digital power conversion, power management and system integration, focusing chiefly on vehicle power generation. Specifically, we have developed, designed and produce drive systems and related components for electric, hybrid electric and fuel cell powered vehicles in both the new and retrofit markets. We also perform internal research and development ("R&D") and funded third party R&D to augment our product development and support our customers.

Our product development strategy is to design and introduce to market successively advanced products, each based on our core technical competencies. In each of our product/market segments, we provide products and services to leverage our core competencies in digital power management, power conversion and system integration. We believe that the underlying technical requirements shared among the market segments will allow us to more quickly transition from one emerging market to the next, with the goal of capturing early market share.

Enova's primary market focus has been centered on aligning ourselves with key customers and integrating with original equipment manufacturers ("OEMs") in our target markets. We believe that alliances will result in the latest technology being implemented and customer requirements being met, with an optimized level of additional time and expense. Provided we generate necessary resources, we will continue to work refining both our market strategy and our product line to maintain our edge in power management and conversion systems for vehicle applications.

Our website, www.enovasystems.com, contains up-to-date information on our company, our products, programs and current events. Our website is a prime focal point for current and prospective customers, investors and other affiliated parties seeking additional information on our business.

Enova has incurred significant operating losses in the past. As of March 31, 2014, we had an accumulated deficit of approximately $162.4 million, working capital of approximately negative $2.9 million and shareholders' deficit of approximately $5.5 million. As reported in our Form 8-K filing on June 21, 2012, due to continued delays in industry adoption of EV technology, the Company's revenues continue to significantly decrease. As part of cost cutting measures, we implemented a reduction in our workforce whereby in excess of 80% of our employees left the Company. We continue to evaluate strategic opportunities to leverage resources and assist with operations. We expect to incur additional operating losses until we re-position the company in order to achieve a level of product sales sufficient to cover our operating and other expenses. As of March 31, 2014, the Company had approximately $114,000 in cash and cash equivalents and we do not anticipate that our anticipated receivables collections will be sufficient to meet projected operating requirements through the end of 2014 to continue operations and market trading.

Customer Highlights

FIRST AUTO WORKS (FAW) - Enova continued to supply drive systems to FAW for their hybrid buses in 2013. Since the 2008 Olympics in Beijing, Enova Systems and First Auto Works have deployed over 500 vehicles utilizing Enova's pre-transmission hybrid drive system components.

SMITH ELECTRIC VEHICLES (SEV) – Enova continued to supply drive system components to SEC in 2013. SEV is a leader in the all EV market in North America and Europe.

Technology Highlights

OMNI INVERTER. Power-source and motor design agnostic, Enova's new Omni-series inverter/vehicle controller offers increased flexibility and ease-of-integration. With plug-and-play connectivity, it is compatible with a wide range of vehicle drive systems and motors, and can be configured for HEV, PHEV and EV applications. The inverter is fully production validated.

OMNI CHARGER. Our Omni-series 10kW on-board battery charger for plug-in hybrid-electric and all-electric vehicles is a CAN control based unit that offers increased flexibility, ease-of-integration and compatibility with a wide range of vehicle platforms.

Enova has delayed further introduction of the Omni Inverter and Charger with customers due to the reduction in our workforce and current financial resource constraints. Provided additional resources are obtained, we anticipate continuing development and marketing of these two products, which we believe can gain broad market acceptance.

Critical Accounting Policies

In the ordinary course of business, the Company has made a number of estimates and assumptions relating to the reporting of results of operations and financial condition in the preparation of its financial statements in conformity with accounting principles generally accepted in the United States of America. The Company constantly re-evaluates these significant factors and makes adjustments where facts and circumstances dictate. Estimates and assumptions include, but are not limited to, customer receivables, inventories, equity investments, fixed asset lives, contingencies and litigation. There have been no material changes in estimates or assumptions compared to our most recent Annual Report for the fiscal year ended December 31, 2013.

The following represents a summary of our critical accounting policies, defined as those policies that we believe: (a) are the most important to the portrayal of our financial condition and results of operations and (b) involve inherently uncertain issues which require management's most difficult, subjective or complex judgments.

Cash and cash equivalents — Cash consists of currency held at reputable financial institutions.

Inventory — Inventories are priced at the lower of cost or market utilizing first-in, first-out (“FIFO”) cost flow assumption. We maintain a perpetual inventory system and continuously record the quantity on-hand and standard cost for each product, including purchased components, subassemblies and finished goods. We maintain the integrity of perpetual inventory records through periodic physical counts of quantities on hand. Finished goods are reported as inventories until the point of transfer to the customer. Generally, title transfer is documented in the terms of sale.

Inventory reserve — We maintain an allowance against inventory for the potential future obsolescence or excess inventory. A substantial decrease in expected demand for our products, or decreases in our selling prices could lead to excess or overvalued inventories and could require us to substantially increase our allowance for excess inventory. If future customer demand or market conditions are less favorable than our projections, additional inventory write-downs may be required, and would be reflected in cost of revenues in the period the revision is made.

Allowance for doubtful accounts — We maintain allowances for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. The assessment of the ultimate realization of accounts receivable including the current credit-worthiness of each customer is subject to a considerable degree to the judgment of our management. If the financial condition of the Company's customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required.

Stock-based Compensation — The Company measures and recognizes compensation expense for all share-based payment awards made to employees and directors, including employee stock options based on the estimated fair values at the date of grant. The compensation expense is recognized over the requisite service period.

Revenue recognition — Effective January 1, 2011, we adopted the provisions of Accounting Standards Update, or ASU, 2009-13, Multiple-Deliverable Revenue Arrangements, or ASU 2009-13, which is included within the Codification as Revenue Recognition-Multiple Element Arrangements, on a prospective basis. Under the provisions of ASU 2009-13, we no longer rely on objective and reliable evidence of the fair value of the elements in a revenue arrangement in order to separate a deliverable into a separate unit of accounting, and the use of the residual method has been eliminated. We instead use a selling price hierarchy for determining the selling price of a deliverable, which is used to determine the allocation of consideration to each unit of accounting under an arrangement. The selling price used for each deliverable will be based on vendor-specific objective evidence, if available, third-party evidence if vendor-specific objective evidence is not available or estimated selling price if neither vendor-specific objective evidence nor third-party evidence is available. As of March 31,. 2014, we had not applied the provisions of ASU 2009-13 to any of our revenue arrangements as we had not entered into any new revenue arrangements since our adoption of ASU 2009-13. Therefore, there was no material impact on our financial position or results of operations from adopting ASU 2009-13. However, the provisions of ASU 2009-13 could have a material impact on the revenue recognized from any collaboration agreements that we may enter into in future periods.

We generally recognize revenue at the time of shipment when title and risk of loss have passed to the customer, persuasive evidence of an arrangement exists, performance of our obligation is complete, our price to the buyer is fixed or determinable, and we are reasonably assured of collection. If a loss is anticipated on any contract, a provision for the entire loss is made immediately. Determination of these criteria, in some cases, requires management's judgment. Should changes in conditions cause management to determine that these criteria are not met for certain future transactions, revenue for any reporting period could be adversely affected.

The Company also recognizes engineering and construction contract revenues using the percentage-of-completion method, based primarily on contract costs incurred to date compared with total estimated contract costs. Customer-furnished materials, labor, and equipment, and in certain cases subcontractor materials, labor, and equipment, are included in revenues and cost of revenues when management believes that the company is responsible for the ultimate acceptability of the project. Contracts are segmented between types of services, such as engineering and construction, and accordingly, gross margin related to each activity is recognized as those separate services are rendered.

These accounting policies were applied consistently for all periods presented. Our operating results would be affected if other alternatives were used. Information about the impact on our operating results is included in the footnotes to our financial statements.

Several other factors related to the Company may have a significant impact on our operating results from year to year. For example, the accounting rules governing the timing of revenue recognition related to product contracts are complex and it can be difficult to estimate when we will recognize revenue generated by a given transaction. Factors such as acceptance of services provided, payment terms, creditworthiness of the customer, and timing of delivery or acceptance of our products often cause revenues related to sales generated in one period to be deferred and recognized in later periods. For arrangements in which services revenue is deferred, related direct and incremental costs may also be deferred.

RESULTS OF OPERATIONS

Three Months Ended March 31, 2014 compared to Three Months Ended March 31, 2013

First Quarter of Fiscal 2014 vs. First Quarter of Fiscal 2013

	Three Months Ended March 31,			As a % of Revenues March 31,	
	2014	2013	% Change	2014	2013
Revenues	$ -	$ 53,000	-100%	n/a	100%
Cost of revenues	-	56,000	-100%	n/a	106%
Gross loss	-	(3,000)	100%	n/a	-6%
Operating expenses					
Research and development	-	-	-	n/a	0%
Selling, general & administrative	136,000	383,000	64%	n/a	723%
Total operating expenses	136,000	383,000	64%	n/a	723%
Operating loss	(136,000)	(386,000)	57%	n/a	-728%
Other income (expense)					
Interest and other income (expense)	(31,000)	(20,000)	-55%	n/a	-38%
Total other income (expense)	(31,000)	(20,000)	-55%	n/a	-38%
Net loss	$ (167,000)	$ (406,000)	51%	n/a	-766%

The sum of the amounts and percentages may not equal the totals for the period due to the effects of rounding.

Computations of percentage change period over period are based upon our results, as rounded and presented herein.

Revenues. Revenues in the current year were negatively affected by uncertainty over the Company's ability to continue operations after our restructuring in June 2012, which reduced our capacity to pursue new business. The decrease in revenue for the three months ended March 31, 2014 compared to the same period in 2013 was mainly due to our inability to sustain production in 2014. Revenues in the first three months of 2013 were mainly attributed to shipments to First Auto Works in China and the Smith Electric Vehicles in the U.S. We will have fluctuations in revenue from quarter to quarter and there can be no assurance there will be continuing demand for our products and services.

Cost of Revenues. Cost of revenues consists of component and material costs, direct labor costs, integration costs and overhead related to manufacturing our products as well as inventory valuation reserve amounts. Cost of revenues for the three months ended March 31, 2014 decreased primarily due to the reduction in our operations.

Gross Loss. The decrease in gross loss for the three months ended March 31, 2014 compared to the same period in the prior year is primarily attributable to the decrease in operating expense in the three months ended March 31, 2014.

Research and Development (“R&D”). The Company halted R&D activities as our engineering staff was eliminated in June 2012 due to the Company’s lack of financial resources. As a result, the Company’s development of its next generation Omni-series motor control unit and 10kW charger was put on hold at the end of the second quarter of 2012.

Selling, General, and Administrative Expenses (“S, G & A”). S, G & A is comprised of activities in the executive, finance, marketing, field service and quality departments’ compensation as well as related payroll benefits, and non-cash charges for depreciation and options expense. The decrease in S, G & A for the three months ended March 31, 2014 compared to the same period in the prior year is attributable to the resignation of approximately 80% of the Company’s workforce from June 2012 and the maintenance of only minimal operations. We continually monitor S, G & A in light of our business outlook and take steps to control these costs.

Interest and Other Income (Expense). The interest and other income (expense) for the three months ended March 31, 2014 increased compared to the same period in the prior year primarily due to the timing of recording asset impairment charges.

Net Loss. The decrease in the net loss for the three months ended March 31, 2014 compared to the same period in the prior year was mainly due to the reduction in our workforce in the second quarter of 2012 which resulted in lower operating costs and the maintenance on only minimal operations.

Comparability of Quarterly Results. Our quarterly results have fluctuated in the past and we believe they will continue to do so in the future. Certain factors that could affect our quarterly operating results are described in Part I, Item 1A-Risk Factors contained in our Form 10-K for 2013. Due to these and other factors, we believe that quarter-to-quarter comparisons of our results of operations are not meaningful indicators of future performance.

LIQUIDITY AND CAPITAL RESOURCES

We have experienced losses primarily attributable to research, development, marketing and other costs associated with our strategic plan as an international developer and supplier of electric drive and power management systems and components. Historically cash flows from operations have not been sufficient to meet our obligations and we have had to raise funds through several financing transactions. At least until we reach breakeven volume in sales and develop and/or acquire the capability to manufacture and sell our products profitably, we will need to continue to rely on cash from external financing sources. Our operations during the three months ended March 31, 2014 were financed from working capital reserves and a capital raise in March 2014.

Net cash used in operating activities was $142,000 for the three months ended March 31, 2014, a decrease of $113,000 compared to net cash used in operating activities of $29,000 for the three months ended March 31, 2013. Operating cash used in the first three months of 2014 decreased compared to the prior year period primarily due to collections of accounts receivables and the receipt of customer deposits for production orders in the prior year. Non-cash items include expense for stock-based compensation, depreciation and amortization and other losses. These non-cash items decreased by $66,000 for the three months ended March 31, 2014 as compared to the same period in the prior year primarily due to lower depreciation expense in 2014 resulting from termination of our lease at our former headquarters in January 2013 and decrease in depreciation for other fixed assets that were impaired or disposed of. The decrease in net loss was primarily due to a decrease in administrative related to over 80% of our workforce leaving the Company in June 2012 and our restricting other administrative expenditures to conserve cash resources. As of March 31, 2014, the Company had $114,000 of cash and cash equivalents compared to $1,000 as of December 31, 2013.

Net cash used in investing activities was $0 for the three months ended March 31, 2014 and 2013, respectively. The Company halted capital expenditures after the reduction in work force in June 2012.

Net cash from financing activities was $255,000 for the three months ended March 31, 2014, an increase of $261,000 compared to net cash used in financing activities of $6,000 in 2013. The increase was primarily attributable to net proceeds of $223,000 from the issuance of Common Stock during first quarter of 2014 as explained in Note 8 –

Stockholders' Equity to the financial statements included in Item 1 of this Form 10-Q and the receipt of related party loans of $32,000 during the first quarter of 2014.

Net accounts receivable were $0 at March 31, 2014 and December 31, 2013, respectively. The Company wrote down the value of its receivables at the end of 2013 due to management's concern over the ability of the Company to continue as a going concern and collect receivables in the normal course of business.

Net inventory and supplies were unchanged at $427,000 as of March 31, 2014 and December 31, 2013, respectively. The Company's operations were halted in the first quarter of 2014 due to the Company's lack of resources to complete customer orders.

Prepaid expenses and other current assets decreased by $12,000, or 29%, to $30,000 at March 31, 2014, compared to a balance of $42,000 at December 31, 2013. The decrease was primarily due to a write down in a deposit to a vendor reflecting management's concern that the product can be utilized in future operations.

Long term accounts receivable were unchanged at $0 as of March 31, 2014 and December 31, 2013, respectively. The Company agreed to defer collection of certain accounts receivable as requested by a customer for the term of the Company's warranty guarantee. Due to its financial condition, the Company is not servicing warranty claims with the customer, which could delay collection of the receivable. Therefore, management has determined to fully reserve the long-term accounts receivables as of December 31, 2013.

Property and equipment, net of depreciation, decreased by $11,000, or 14%, to $69,000 at March 31, 2014 compared to a balance of $80,000 at December 31, 2013. The decrease is primarily due to depreciation expense of $11,000.

Accounts payable decreased by $96,000, or 15%, to $546,000 at March 31, 2014 compared to a balance of $642,000 at December 31, 2013. The decrease was primarily due to partial payment of legal and exchange fees from the proceeds of the equity issuance in March 2014.

Loans from employees increased by $32,000, or 89%, to $68,000 at March 31, 2014 compared to a balance of $36,000 at December 31, 2013. Due the financial condition of the company, employees loaned funds to the Company to pay for certain necessary administrative costs.

Deferred revenues were unchanged at $213,000 at March 31, 2014 and December 31, 2013, respectively. The Company's management is attempting to obtain funding in order to sub-contract out the completion of the orders in the second quarter of 2014.

Accrued payroll and related expenses increased by $23,000, or 12%, to $217,000 at March 31, 2014 compared to a balance of $194,000 at December 31, 2013. The increase was primarily due to an increase in unpaid compensation in the first quarter of 2014 resulting from the financial condition of the Company.

Accrued loss for litigation settlement was unchanged at March 31, 2014 compared to the balance at December 31, 2013. As disclosed under the heading "Judgment entered in Arens Controls Litigation" below, on December 12, 2012, a judgment was entered in favor of Arens Controls Company, L.L.C. by the United States District Court Northern District of Illinois in the amount of $2,014,169 in the case of Arens Controls Company, L.L.C. v. Enova Systems, Inc. See also Item 1 of Part II of this report on Form 10-Q.

Other accrued liabilities increased by $52,000, or 18%, to $346,000 at March 31, 2014 compared to a balance of $294,000 at December 31, 2013. The increase was primarily due to an increase in the accrual for professional services incurred in the first three months of 2014.

Accrued interest payable increased by $19,000, or 1%, to $1,420,000 at March 31, 2014 compared to a balance of $1,401,000 at December 31, 2013. The increase was due to interest related to our debt instruments, primarily the interest on the secured note payable in the amount of $1,344,000 to the Credit Managers Association of California.

Going concern

To date, the Company has incurred recurring net losses and negative cash flows from operations. At March 31, 2014, the Company had an accumulated deficit of approximately $162.4 million, working capital of approximately negative $2.9 million and shareholders' deficit of approximately $5.5 million. Until the Company can generate significant cash from its operations, the Company expects to continue to fund its operations with existing working capital, proceeds from one or more private placement agreements, as well as potentially through debt financing or the sale of equity securities. However, the Company may not be successful in obtaining additional funding. In addition, the Company cannot be sure that its existing cash and investment resources will be adequate or that additional financing will be available when needed or that, if available, financing will be obtained on terms favorable to the Company or its shareholders.

Our operations will require us to make necessary investments in human and production resources, regulatory compliance, as well as sales and marketing efforts. We do not currently have adequate internal liquidity to meet these objectives in the long term. On June 21, 2012, we reported in a Form 8-K filing that, as part of cost cutting measures in response to our decrease in revenue amid continued delays in industry adoption of EV technology resulting from ongoing battery cost and reliability concerns, in excess of 80% of our workforce left our Company, including the resignation of members of our senior management. We continue to evaluate strategic partnering opportunities and other external sources of liquidity, including the public and private financial markets and strategic partners. Having insufficient funds has required the Company to eliminate its product development, and may result in relinquishing rights to product candidates at an earlier stage of development or negotiate less favorable terms than it would otherwise choose. Failure to obtain adequate financing also will adversely affect the Company's ability to continue in business. If the Company raises additional funds by issuing equity securities, substantial dilution to existing stockholders would likely result. If the Company raises additional funds by incurring debt financing, the terms of the debt may involve significant cash payment obligations, as well as covenants and specific financial ratios that may restrict its ability to operate its business.

As of March 31, 2014, the Company had approximately $114,000 in cash and cash equivalents and we do not anticipate that our existing anticipated receivables collections will be sufficient to meet projected operating requirements through the end of 2014 to continue operations and market trading.

Judgment entered in Arens Controls Litigation

On December 12, 2012, a judgment was entered by the United States District Court Northern District of Illinois in favor of Arens Controls Company, L.L.C. in the amount of $2,014,169 regarding claims for two counts. In 2008, Arens Controls Company, L.L.C. ("Arens") filed claims against Enova with the United States District Court Northern District of Illinois. A Partial Settlement Agreement, as amended on January 14, 2011, resolved certain claims made by Arens. However, the claims were preserved under two remaining counts concerning i) anticipatory breach of contract by Enova for certain purchase orders that resulted in lost profit to Arens and ii) reimbursement for engineering and capital equipment costs incurred by Arens exclusively for the fulfillment of certain purchase orders received from Enova.

On September 24, 2013, Enova and Arens entered into a Settlement Agreement and Mutual Release (the "Settlement Agreement") to resolve the remaining issues between them. Under the terms of the Settlement Agreement, Enova filed on September 27, 2013 a motion to dismiss the pending appeal with prejudice and Arens agreed that, for a period of 120 calendar days from the date of the Settlement Agreement, Arens would not take any action to enforce the Judgment. Thereafter, Arens is entitled, without further notice, to enforce the Judgment against Enova or otherwise exercise all available procedures and remedies for collection of the full amount of the Judgment and Enova has agreed not to contest the validity of the Judgment. However, if Enova had paid to Arens $300,000 at any time during the 120 day period, then within 3 business days after Arens received confirmation of such payment, Arens agreed to file a satisfaction of judgment stating that the Judgment has been satisfied and completely release and forever discharge Enova from any and all claims for damages whatsoever that occurred prior to the date of the Settlement Agreement. In exchange for Arens's release, Enova agreed to completely release and forever discharge Arens from any and all claims for damages whatsoever that occurred prior to the date of the Settlement Agreement. The Company was not able to comply with the due date for such payment by January 22, 2014. Therefore, the judgment against the Company can be enforced without further notice.

Off-Balance Sheet Arrangements

The Company has no off-balance sheet arrangements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not applicable.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

The Company maintains disclosure controls and procedures which are designed to provide reasonable assurance that information required to be disclosed in the Company's periodic Securities and Exchange Commission ("SEC") reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to its principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure.

As required by SEC Rule 13a-15(b) under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Exchange Act) as of March 31, 2014. Based on that evaluation, our management, including the Chief Executive Officer and Chief Financial Officer, concluded that as of March 31, 2014, our disclosure controls and procedures were not effective to ensure the information required to be disclosed by an issuer in the reports it files or submits under the Securities Exchange Act of 1934, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms relating to us, and was accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, or persons performing similar functions, as appropriate, to allow timely decisions regarding required disclosure. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures, including the possibility of human error and the circumvention or overriding of the controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives.

Changes in Internal Control Over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in Rule 13a-15(f) and 15d-15(f) promulgated under the Exchange Act. We maintain internal control over financial reporting designed 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.

In June 2012, all but two of the Company's employees resigned, and such staff reduction resulted in our inability to complete documentation of proper accounting procedures and management review. Not all fully implemented fundamental elements of an effective control were present as of March 31, 2014, including formalized monitoring procedures. Based on this evaluation, management has concluded that the aforementioned factors constituted a material weakness in the Company's internal control over financial reporting as of March 31, 2014.

PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings

As reported in our Form 10-K for the fiscal year 2012, six of the eight counts in the litigation between Enova and Arens Controls Company, L.L.C. were settled. The two counts that were not settled remained outstanding. The two remaining counts concerned i) anticipatory breach of contract by Enova for certain purchase orders that resulted in lost profit to Arens and ii) reimbursement for engineering and capital equipment costs incurred by Arens exclusively for the fulfillment of certain purchase orders received from Enova.

On December 12, 2012, a judgment was entered under the two remaining counts by the United States District Court Northern District of Illinois in favor of Arens Controls Company, L.L.C. in the amount of $2,014,169.

On September 24, 2013, Enova and Arens entered into a Settlement Agreement and Mutual Release (the "Settlement Agreement") to resolve the remaining issues between them. Under the terms of the Settlement Agreement, Enova filed on September 27, 2013 a motion to dismiss the pending appeal with prejudice and Arens agreed that, for a period of 120 calendar days from the date of the Settlement Agreement, Arens would not take any action to enforce the Judgment. Thereafter, Arens is entitled, without further notice, to enforce the Judgment against Enova or otherwise exercise all available procedures and remedies for collection of the full amount of the Judgment and Enova has agreed not to contest the validity of the Judgment. However, if Enova had paid to Arens $300,000 at any time during the 120 day period, then within 3 business days after Arens received confirmation of such payment, Arens agreed to file a satisfaction of judgment stating that the Judgment has been satisfied and completely release and forever discharge Enova from any and all claims for damages whatsoever that occurred prior to the date of the Settlement Agreement. In exchange for Arens's release, Enova agreed to completely release and forever discharge Arens from any and all claims for damages whatsoever that occurred prior to the date of the Settlement Agreement. The Company was not able to comply with the due date for such payment by January 22, 2014. Therefore, the judgment against the Company can be enforced without further notice

From time to time, we are subject to legal proceedings arising out of the conduct of our business, including matters relating to commercial transactions. We recognize a liability for any contingency that is probable of occurrence and reasonably estimable. We continually assess the likelihood of adverse outcomes in these matters, as well as potential ranges of probable losses (taking into consideration any insurance recoveries), based on a careful analysis of each matter with the assistance of outside legal counsel and, if applicable, other experts.

Given the uncertainty inherent in litigation, we do not believe it is possible to develop estimates of the range of reasonably possible loss for these matters. Considering our past experience, we do not expect the outcome of these matters, either individually or in the aggregate, to have a material adverse effect on our consolidated financial position. Because most contingencies are resolved over long periods of time, potential liabilities are subject to change due to new developments, changes in settlement strategy or the impact of evidentiary requirements, which could cause us to pay damage awards or settlements (or become subject to equitable remedies) that could have a material adverse effect on our results of operations or operating cash flows in the periods recognized or paid.

ITEM 1A. Risk Factors

Our Annual Report on Form 10-K for the fiscal year ended December 31, 2013 lists risk factors for the Company. There have been no material changes from the risk factors as previously disclosed in such Annual Report on Form 10-K.

ITEM 2. Unregistered Sales of Equity and Use of Proceeds

On February 23, 2014, Enova Systems, Inc, entered into Subscription Agreements with various offshore investors to sell approximately GBP 150,000 (approximately US$249,000) in gross proceeds by a private subscription of 19,999,998 common shares to be newly issued on the Alternative Investment Market of the London Stock Exchange (the "AIM Exchange"). The common shares were issued at a price of 0.0075 pence (approximately US$0.01per share) to certain eligible offshore investors (the "Subscription"). In connection with the Subscription, Enova entered into an Agreement for the Provision of Receiving Agent Services (the "Agreement") with Daniel Stewart & Company PLC (UK) for receiving agent services. Daniel Stewart presently serves as the Nominated Adviser for the listing of Enova's common shares on the AIM Exchange. The newly issued common shares for the Subscription were issued in three tranches of approximately GBP 50,000 each.

Daniel Stewart received an introducing agent's fee of 10% of the aggregate funds raised pursuant to the subscription in addition to reimbursement of expenses. Factoring in the commission, legal and other expenses of the offering, Enova received approximately US$223,000 in net proceeds.

The offer and sale of the shares were made pursuant to Regulation S under the Securities Act of 1933, as amended (the "Securities Act"). Among other things, each investor purchasing shares of Enova's common stock in the offering represented that the investor is not a United States person as defined in Regulation S. In addition, neither Enova nor the receiving agent conducted any selling efforts directed at the United States in connection with the offering. All shares of common stock issued in the offering included a restrictive legend indicating that the shares were issued pursuant to Regulation S under the Securities Act and are deemed to be "restricted securities." As a result, the purchasers of such shares will not be able to resell the shares unless in accordance with Regulation S, pursuant to a registration statement, or upon reliance of an applicable exemption from registration under the Securities Act. The shares to be sold pursuant to the Subscription Agreements were not registered under the Securities Act, and there is no obligation on the part of Enova to so register such shares.

ITEM 3. Defaults upon Senior Securities

None.

ITEM 4. Mine Safety Disclosures

Not applicable.

ITEM 5. Other Information

None.

ITEM 6. Exhibits

10.1	Agreement for the Provision of Receiving Agent Services entered into February 23, 2014 with Daniel Stewart & Company PLC in connection to the issuance of 19,999,998 shares on the AIM Exchange.*
31.1	Certification of the Chief Executive Officer and Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act Of 2002.*
32.1	Certification Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.*
101. XML	XBRL Instance Document**
101.XSD	XBRL Taxonomy Extension Schema Document**
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document**
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document**
101.LAB	XBRL Taxonomy Extension Label Linkbase Document**
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document**

* Filed herewith

** In accordance with Regulation S-T, the XBRL-related information in Exhibit 101 to this Quarterly Report on Form 10-Q shall be deemed to be "furnished" and not "filed."

SIGNATURE

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: May 20, 2014

ENOVA SYSTEMS, INC. (Registrant)

By; /s/ John Micek
John Micek, Chief Executive Officer and Chief Financial Officer

Exhibit List:

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