ENOVA SYSTEMS INC
Form 10-Q
August 11, 2010

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

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

For the quarterly period ending June 30, 2010

or

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

1560 West 190th Street, Torrance, California 90501

(Address of principal executive offices, including zip code)

(310) 527-2800

(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 þ No o

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 o No o

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 o	Accelerated filer o	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company þ

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

As of July 31, 2010, there were 31,428,232 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

	June 30, 2010 (unaudited)	December 31, 2009
ASSETS		
Current assets:		
Cash and cash equivalents	$ 10,203,000	$ 13,078,000
Short term investments	200,000	200,000
Accounts receivable, net of allowance for doubtful accounts of $31,000 as of June 30, 2010 and December 31, 2009	1,660,000	1,442,000
Inventories and supplies, net	4,910,000	5,605,000
Prepaid expenses and other current assets	436,000	263,000
Total current assets	17,409,000	20,588,000
Long term accounts receivable	215,000	
Property and equipment, net	1,306,000	1,363,000
Intangible assets, net	58,000	60,000
Total assets	$ 18,988,000	$ 22,011,000
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 636,000	$ 415,000
Deferred revenues	98,000	357,000
Accrued payroll and related expenses	543,000	277,000
Other accrued liabilities	988,000	1,287,000
Current portion of notes payable	69,000	68,000
Total current liabilities	2,334,000	2,404,000
Accrued interest payable	1,115,000	1,074,000
Notes payable, net of current portion	1,296,000	1,286,000
Total liabilities	4,745,000	4,764,000
Stockholders equity:		
Series A convertible preferred stock no par value, 30,000,000 shares authorized; 2,652,000 shares issued and outstanding; liquidating preference at $0.60 per share as of June 30, 2010 and December 31, 2009	530,000	530,000
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 June 30, 2010 and December 31, 2009	1,094,000	1,094,000
Common Stock no par value, 750,000,000 shares authorized; 31,428,000 and 31,404,000 shares issued and outstanding as of June 30, 2010 and December 31, 2009, respectively	144,049,000	143,995,000
Additional paid-in capital	8,621,000	8,336,000

Accumulated deficit		(140,051,000)		(136,708,000)
Total stockholders equity		14,243,000		17,247,000
Total liabilities and stockholders equity	$	18,988,000	$	22,011,000

The accompanying notes are an integral part of these financial statements.

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ENOVA SYSTEMS, INC.
STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended June 30, 2010	Three Months Ended June 30, 2009	Six Months Ended June 30, 2010	Six Months Ended June 30, 2009
Revenues	$ 2,054,000	$ 576,000	$ 2,983,000	$ 1,264,000
Cost of revenues	1,764,000	613,000	2,610,000	1,192,000
Gross income (loss)	290,000	(37,000)	373,000	72,000
Operating expenses				
Research and development	361,000	335,000	683,000	589,000
Selling, general & administrative	1,551,000	1,570,000	3,028,000	3,065,000
Total operating expenses	1,912,000	1,905,000	3,711,000	3,654,000
Operating loss	(1,622,000)	(1,942,000)	(3,338,000)	(3,582,000)
Other income and (expense)				
Interest and other income (expense)	(2,000)	(98,000)	(5,000)	(104,000)
Gain (loss) from non-consolidated joint venture		6,000		(4,000)
Total other income (expense)	(2,000)	(92,000)	(5,000)	(108,000)
Net loss	$ (1,624,000)	$ (2,034,000)	$ (3,343,000)	$ (3,690,000)
Basic and diluted loss per share	$ (0.05)	$ (0.10)	$ (0.11)	$ (0.18)
Weighted average number of shares outstanding	31,416,000	20,896,000	31,410,000	20,871,000

The accompanying notes are an integral part of these financial statements.

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

	For the Six Months Ended June 30, 2010	2009
Cash flows from operating activities:		
Net loss	$ (3,343,000)	$ (3,690,000)
Adjustments to reconcile net loss to net cash used in operating activities:		
Inventory reserve	103,000	240,000
Depreciation and amortization	273,000	318,000
Loss on asset disposal		3,000
Equity in losses of non-consolidated joint venture		10,000
Gain from dissolution of non-consolidated joint venture		(6,000)
Issuance of common stock for director services		90,000
Issuance of common stock for employee services	48,000	124,000
Stock option expense	285,000	230,000
(Increase) decrease in:		
Accounts receivable	(218,000)	380,000
Inventory and supplies	592,000	469,000
Prepaid expenses and other current assets	(173,000)	(24,000)
Long term accounts receivable	(215,000)	
Increase (decrease) in:		
Accounts payable	221,000	334,000
Deferred revenues	(259,000)	670,000
Accrued payroll and related expenses	266,000	(69,000)
Other accrued liabilities	(299,000)	(805,000)
Accrued interest payable	41,000	41,000
Net cash used in operating activities	(2,678,000)	(1,685,000)
Cash flows from investing activities:		
Purchases of short-term investments		(200,000)
Maturities of short-term investments		2,000,000
Proceeds from the dissolution of non-consolidated joint venture		137,000
Purchases of property and equipment	(188,000)	(100,000)
Net cash provided by (used in) investing activities	(188,000)	1,837,000
Cash flows from financing activities:		
Payments on notes payable	(15,000)	(33,000)
Proceeds from the exercise of stock options	6,000	
Net cash used in financing activities	(9,000)	(33,000)
Net increase (decrease) in cash and cash equivalents	(2,875,000)	119,000
Cash and cash equivalents, beginning of period	13,078,000	5,324,000

Cash and cash equivalents, end of period	$ 10,203,000	$ 5,443,000
Supplemental disclosure of cash flow information:		
Interest paid	$ 3,000	$ 4,000
Assets acquired through financing arrangements	$ 26,000	$ 38,000
Net assets acquired in exchange for Enova s interest in joint venture:		
Inventory	$	$ 1,075,000
Prepaid expenses and other current assets	$	$ 104,000
Reduction of related party payable, net of receivable	$	$ 32,000

The accompanying notes are an integral part of these financial statements.

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ENOVA SYSTEMS, INC.
NOTES TO FINANCIAL STATEMENTS
(Unaudited)
Three and six months ended June 30, 2010 and 2009

1. Description of the Company and its Business

Enova Systems, Inc. (Enova We or the Company) changed its name in July 2000. The Company was previously known as U.S. Electricar, Inc., a California corporation, which was incorporated on July 30, 1976. The Company is 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.

2. Summary of Significant Accounting Policies

Basis of Presentation Interim Financial Statements

The financial information as of June 30, 2010 and for the three and six months ended June 30, 2010 and 2009 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 fiscal year. These interim financial statements should be read in conjunction with the audited financial statements for the year ended December 31, 2009, which are included in the Company s Annual Report on Form 10-K for the year then ended.

Fair Value of Financial Instruments

The carrying amount of financial instruments, including cash and cash equivalents, short-term investments, accounts receivable, accounts payable and accrued liabilities, approximate fair value due to the short maturity of these instruments. Short-term investments consist of certificates of deposits. The carrying value of all other financial instruments is representative of their fair values. The recorded values of notes payable and long-term debt approximate their fair values as interest rates approximate market rates.

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.

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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.

Collectibility is Reasonably Assured The Company determines that collectibility is reasonably assured prior to recognizing revenue. Collectibility 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 collectibility 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 collectibility 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.

We recognize 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, 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.

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.

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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.

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. The Company has entered into several production and development contracts with customers. The Company has evaluated these contracts, ascertained the specific revenue generating activities of each contract, and established 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 eighteen months from the date of delivery, subject to standard limitations for equipment that has been altered by other than Enova 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 eighteen month period. The warranty liability is evaluated on an ongoing basis for adequacy and may be adjusted as additional information regarding expected warranty costs become 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.

See Note 10 S*tock Options* for further information on stock-based compensation expense.

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:

	June 30, 2010	**December 31, 2009**
Raw Materials	$ 5,639,000	$ 6,341,000
Work In Progress	237,000	132,000
Finished Goods	115,000	111,000
Reserve for Obsolescence	(1,081,000)	(979,000)
Total	$ 4,910,000	$ 5,605,000

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4. Property and Equipment

Property and equipment consisted of the following at:

	June 30, 2010	December 31, 2009
Computers and software	$ 577,000	$ 556,000
Machinery and equipment	853,000	795,000
Furniture and office equipment	98,000	98,000
Demonstration vehicles and buses	650,000	507,000
Leasehold improvements	1,348,000	1,348,000
Construction in process		8,000
	3,526,000	3,312,000
Less accumulated depreciation and amortization	(2,220,000)	(1,949,000)
Total	$ 1,306,000	$ 1,363,000

Depreciation and amortization expense was $271,000 and $316,000 for the six months ended June 30, 2010 and 2009, respectively, and within those total expenses, the amortization of leasehold improvements was $134,000 and $135,000 for the six months ended June 30, 2010 and 2009, respectively. Depreciation and amortization expense was $134,000 and $159,000 for the three months ended June 30, 2010 and 2009, respectively, and within those total expenses, the amortization of leasehold improvements was $67,000 for each of the three months ended June 30, 2010 and 2009.

5. Other Accrued Liabilities

Other accrued liabilities consisted of the following at:

	June 30, 2010	December 31, 2009
Accrued Inventory Received	$ 183,000	$ 334,000
Accrued Professional Services	312,000	395,000
Accrued Warranty	493,000	558,000
Total	$ 988,000	$ 1,287,000

Accrued warranty consisted of the following activities during the six months ended June 30:

	2010	2009
Balance at beginning of year	$ 558,000	$ 545,000
Accruals for warranties issued during the period	207,000	71,000
Warranty claims	(272,000)	(86,000)
Balance at end of quarter	$ 493,000	$ 530,000

Accrued warranty consisted of the following activities during the three months ended June 30:

	2010	2009
Balance at beginning of quarter	$ 492,000	$ 538,000
Accruals for warranties issued during the period	169,000	29,000
Warranty claims	(168,000)	(37,000)

Balance at end of quarter	$ 493,000	$ 530,000

6. Intangible Assets

Intangible assets consist of legal fees directly associated with patent licensing. The Company has been granted three patents. These patents have been capitalized and are being amortized on a straight-line basis over a period of 20 years.

Intangible assets consisted of the following at:

	June 30, 2010	December 31, 2009
Patents	$ 93,000	$ 93,000
Less accumulated amortization	(35,000)	(33,000)
Total	$ 58,000	$ 60,000

Amortization expense charged to operations was $2,000 for the six months ended June 30, 2010 and 2009.

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

Notes payable consisted of the following at:

	June 30, 2010	December 31, 2009
Secured note payable to Credit Managers Association of California, bearing interest at prime plus 3% (6.25% as of June 30, 2010), 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	$ 1,238,000	$ 1,238,000
Secured note payable to a financial institution in the original amount of $23,000, bearing interest at 11.70%, payable in 36 equal monthly installments of principal and interest through October 1, 2010	3,000	8,000
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
Secured note payable to a financial institution in the original amount of $39,000, bearing interest at 4.99% per annum, payable in 48 equal monthly installments of principal and interest through September 1, 2011	13,000	18,000
Secured note payable to a financial institution in the original amount of $38,000, bearing interest at 8.25% per annum, payable in 60 equal monthly installments of principal and interest through February 19, 2014	29,000	32,000
Secured note payable to a financial institution in the original amount of $19,000 bearing interest at 10.50% per annum, payable in 60 equal monthly installments of principal and interest through August 25, 2014	17,000	18,000
Secured note payable to a financial institution in the original amount of $26,000 bearing interest at 7.91% per annum, payable in 60 equal monthly installments of principal and interest through April 9, 2015	25,000	
	1,365,000	1,354,000
Less current portion	(69,000)	(68,000)
Long-term portion	$ 1,296,000	$ 1,286,000

As of June 30, 2010 and December 31, 2009, the balance of long term interest payable with respect to the Credit Managers Association of California note amounted to $1,093,000 and $1,054,000, respectively. Interest expense on notes payable amounted to approximately $44,000 and $46,000 during the six months ended June 30, 2010 and 2009, respectively. Interest expense on notes payable amounted to approximately $22,000 during each of the three months ended June 30, 2010 and 2009.

8. Revolving Credit Agreement

The Company entered into a secured revolving credit facility with a financial institution (the Credit Agreement) for $200,000, which is secured by a $200,000 certificate of deposit. The facility expired on June 30, 2010 and was renewed for a period of 3 years and 6 months with the same terms on July 1, 2010 with an expiration of December 31, 2013. The interest rate on a drawdown from the facility is the certificate of deposit rate plus 1.25% with interest payable monthly and the principal due at maturity. The financial institution also renewed the $200,000 irrevocable letter of credit for the full amount of the credit facility in favor of the Company s landlord, Sunshine Distribution LP, with respect to the lease of the Company s corporate headquarters at 1560 West 190th Street, Torrance, California.

9. Stockholders Equity

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During the six months ended June 30, 2010 and 2009, the Company issued shares of common stock valued at $48,000 and $214,000, respectively, to directors and employees as compensation based upon the trading value of the common stock on the date of issuance. During the three months ended June 30, 2010 and 2009, the Company issued shares of common stock valued at $25,000 and $69,000, respectively, to directors and employees as compensation based upon the trading value of the common stock on the date of issuance.

10. Stock Options

Stock Option Program Description

As of June 30, 2010, 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, executives and directors 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 2006 Plan has a total of 3,000,000 shares reserved for issuance, of which 1,680,000 shares were available for grant as of June 30, 2010. All stock options have terms of between five and ten years and generally vest and become fully exercisable from one to three years from the date of grant. As of June 30, 2010, the Company had 1,348,000 options outstanding which were comprised of issuances under the 1996 Plan and the 2006 Plan of 74,000 and 1,274,000, respectively.

As of June 30, 2010, the total compensation cost related to non-vested awards not yet recognized is $614,000. The weighted average period over which the future compensation cost is expected to be recognized is 18 months. The aggregate intrinsic value represents the total pretax intrinsic value, which is the difference between the Company s closing stock price on the last trading day of the second quarter of fiscal 2010 of $0.92 and the exercise price times the number of shares that would have been received by the option holders if they had exercised their options on June 30, 2010. This amount will change based on the fair market value of the Company s stock. The intrinsic value of in-the-money stock options outstanding was $112,000 and $74,000 at June 30, 2010 and 2009, respectively. The aggregate intrinsic value of exercisable stock options was $61,000 and $18,000 at June 30, 2010 and 2009, respectively.

The following table summarizes information about stock options outstanding and exercisable at June 30, 2010:

	Number of Share Options	**Weighted Average Exercise Price**	**Weighted Average Remaining Contractual Term in Years**	**Aggregate Intrinsic Value**
Outstanding at December 31, 2009	1,410,000	$ 2.10	7.65	
Granted		$		
Exercised	(23,000)	$ 0.27		
Forfeited or Cancelled	(39,000)	$ 3.42		
Outstanding at June 30, 2010	1,348,000	$ 2.09	7.24	$ 112,000
Exercisable at June 30, 2010	749,000	$ 2.64	6.66	$ 61,000

The exercise prices of the options outstanding at June 30, 2010 ranged from $0.21 to $4.35. The weighted average grant-date fair value of options granted during the six months ended June 30, 2009 was $0.58. There were no new options granted during the six months ended June 30, 2010. The Company s policy is to issue shares from its authorized shares upon the exercise of stock options.

The fair values of all stock options granted during the six months ended June 30, 2009 were estimated on the date of grant using the Black-Scholes option-pricing model with the following range of assumptions:

	For the six months ended		For the three months ended	
	June 30, 2010	June 30, 2009	June 30, 2010	June 30, 2009
Expected life (in years)		4		4
Average risk-free interest rate		2%		2%
Expected volatility		194%		194%
Expected dividend yield		0%		0%
Forfeiture rate		3%		3%

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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.

11. Concentrations

The Company s trade receivables are concentrated with few customers. The Company performs credit evaluations on their customers financial condition. Concentrations of credit risk, with respect to accounts receivable, exist to the extent of amounts presented in the financial statements. Three customers represented 32%, 31% and 27%, respectively, of total gross accounts receivable at June 30, 2010, and two customers represented 77% and 11%, respectively, of total gross accounts receivable at December 31, 2009.

The Company s revenues are concentrated with few customers. For the three and six months ended June 30, 2010, three customers represented 31%, 31% and 24% of gross revenues and three customers represented 43%, 21% and 18% of gross revenues, respectively. For the three and six months ended June 30, 2009, three customers represented 65%, 15% and 14% of gross revenues and four customers represented 42%, 21%, 20% and 11% of gross revenues, respectively.

12. Recent Accounting Pronouncements

There have been no recent accounting pronouncements issued applicable to Enova Systems, Inc. other than those disclosed in the Company s Annual Report on Form 10-K for the year ended December 31, 2009.

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 ne 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, 2009.

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, 2009.

Overview

Enova believes it is a leader in the development and production of proprietary, commercial digital power management systems for transportation vehicles and stationary power generation systems. Power management systems control and monitor electric power in an automotive or commercial application such as an automobile or a stand-alone power generator. Electric drive systems are comprised of an electric motor, an electronics control unit, a gear unit and batteries which power an electric vehicle. Hybrid systems, which are similar to pure electric drive systems, contain an internal combustion engine in addition to the electric motor, eliminating external recharging of the battery system. Our hybrid systems can alternatively utilize a hydrogen fuel cell as a power source to recharge the battery system. Stationary power systems utilize similar components to those which are in a mobile drive system in addition to other elements.

A fundamental element of Enova s strategy is to develop and produce advanced proprietary software, firmware and hardware for applications in these alternative power markets. Our focus is digital power conversion, power management, and system integration, focusing chiefly on vehicle power generation.

Specifically, we develop, design and produce drive systems and related components for electric, hybrid-electric and fuel cell vehicles. We also develop, design and produce power management and power conversion components for stationary distributed power generation systems. Additionally, we perform research and development (R&D) to augment and support others and our own related product development efforts.

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 centers on both electric series and parallel hybrid medium and heavy-duty drive systems for multiple vehicle and marine applications. A series hybrid system is one where only the electric motor connects to the drive shaft; a parallel hybrid system is one where both the internal combustion engine and the electric motor are connected to the drive shaft. We believe series-hybrid and parallel-hybrid medium and heavy-duty drive system sales offer Enova the greatest return on investment in both the short and long term. We believe the medium and heavy-duty hybrid market s best chances of significant growth lie in identifying and pooling the largest possible numbers of early adopters in high-volume applications. By aligning ourselves with key customers 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 or expense. As we penetrate more market areas, we are continually refining both our market strategy and our product line to maintain our leading edge in power management and conversion systems for mobile 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 data on our business.

Recent Developments

In February 2010, Enova was awarded an exclusive supplier contract with the U.S. General Services Administration (GSA), which provides vehicles for government agencies and armed forces. Under that contract, Enova will supply our Zero Emissions (Ze) all-electric walk-in step vans to the GSA under the Cargo Vans category. Enova has partnered with Freightliner Custom Chassis Corporation (Freightliner), a subsidiary of Daimler Trucks North America LLC, to integrate and deploy the Ze technology with their MT-45 walk-in van chassis. Most recently, Enova was notified by GSA of its intent to extend the all-electric step van contract for another year.

Also in February 2010, Enova lauded Smith Electric Vehicles (Smith) recent GSA announcement of the Smith Newton product offering in the Medium and Heavy Duty Vans category with a gross vehicle weight rating (GVWR) of 25,500 lbs. The Smith Newton is an exclusive, all-electric medium and heavy duty truck offering on the GSA product menu. This was augmented by Navistar s continued leadership in the American school bus market with its exclusive GSA contract to supply hybrid school buses.

In March 2010, Smith was selected to receive an additional $22 million in grant funding from the Department of Energy (DOE), bringing the total DOE grant funding available to Smith to $32 million toward the production of all-electric, zero emissions commercial trucks. Smith has selected Enova as the exclusive drive system supplier for its flagship Newton route delivery vehicles, which incorporates Enova s 120kW drive system controller. The DOE grant will be used to help offset Smith s future vehicle development cost and to incentivize its customers to participate in a commercial electric vehicle demonstration program. Most recently and in response the aforementioned government funding, President Barack Obama visited Smith s new Kansas City manufacturing facility to speak on the creation of clean vehicle jobs.

In April 2010, Enova expanded its all electric Ze drive system offerings to include a Ford F-150 utility truck and Chevrolet Express cargo van. The Ford F-150 is the highest sales volume pick-up truck in the United States and has been integrated with a 90kW all-electric Ze drive system. The Chevy Express cargo van is one of the top selling domestic fleet vans in its vehicle classification and has been integrated with a 120kW all-electric Ze drive system. The all-electric Ford F-150 is currently being evaluated for a series of 3rd party testing at a nationally recognized clean vehicle testing center that started in June. Testing will include a range of dynamometer and on-road testing programs.

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In June 2010, the California Air Resources Board (CARB) continued the Hybrid Voucher Incentive Program (HVIP) by approving the State of California s AB 118 Air Quality Improvement Program Funding Plan for Fiscal Year 2010-11 for $25 million. The HVIP was designed to stimulate the purchase of both hybrid and zero-emission commercial trucks and buses by offsetting a portion of the incremental cost for these commercial vehicles through rebates. Currently, Navistar s Hybrid School Buses with Enova s Charge Depleting systems are eligible for rebates of between $20,000 and $30,000 depending on the weight class. The Smith Newton, which is powered by Enova s Ze all-electric drive system, is also eligible for a $20,000 rebate.

Also in June 2010, Enova partnered with Remy International, Inc. (Remy) to develop a new electric drive system based on the new Enova Omni Controller and the patented Remy High Voltage Hairpin (HVH) motor. The Omni Controller is Enova s next-generation 200kVA-capable power inverter for hybrid-electric and all-electric medium and heavy-duty commercial vehicles. The Remy HVH Permanent Magnet Motor maximizes fuel efficiency and offers class leading torque and power density. Together, the Remy/Enova electric drive system aims to increase the value proposition with more alternative propulsion energy and thus more miles on the road.

Enova has incurred significant operating losses in the past. As of June 30, 2010, we had an accumulated deficit of approximately $140.1 million. We expect to incur additional operating losses until we achieve a level of product sales sufficient to cover our operating and other expenses. However, the Company believes that its business outlook will improve, especially in light of government policies being implemented in the United States, China and the United Kingdom regarding the curbing of green house gas emissions in the future as well as intentions to provide government incentives that may induce consumption of our products and services.

We continue to receive greater recognition from both governmental and private industry with regards to both commercial and military application of our hybrid drive systems and fuel cell power management technologies. Although we believe that current negotiations with above named parties may result in additional production contracts during 2010 and beyond, there are no assurances that such additional agreements will be realized.

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, 2009.

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.

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Stock-based Compensation The Company calculates stock-based compensation expense in accordance with FASB ASC 718, Share-Based Payment (FASB ASC 718). This pronouncement requires the measurement and recognition of compensation expense for all share-based payment awards made to employees and directors, including employee stock options to be based on estimated fair values.

Revenue recognition The Company is required to make judgments based on historical experience and future expectations, as to the reliability of shipments made to its customers. These judgments are required to assess the propriety of the recognition of revenue based on ASC 605 and related guidance. The Company makes these assessments based on the following factors: i) customer-specific information, ii) return policies, and iii) historical experience for issues not yet identified.

The Company manufactures proprietary products and other products based on design specifications provided by its customers. Revenue from sales of products are generally recognized at the time title to the goods and the benefits and risks of ownership passes to the customer which is typically when products are shipped based on the terms of the customer purchase agreement. Revenue relating to long-term fixed price contracts is recognized using the percentage of completion method. Under the percentage of completion method, contract revenues and related costs are recognized based on the percentage that costs incurred to date bear to total estimated costs. Changes in job performance, estimated profitability and final contract settlements may result in revisions to cost and revenue, and are recognized in the period in which the revisions are determined. Contract costs include all direct materials, subcontract and labor costs and other indirect costs. General and administrative costs are charged to expense as incurred. At the time a loss on a contract becomes known, the entire amount of the estimated loss is accrued. The aggregate of costs incurred and estimated earnings recognized on uncompleted contracts in excess of related billings is shown as a current asset, and billings on uncompleted contracts in excess of costs incurred and estimated earnings is shown as a current liability.

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 and Six Months Ended June 30, 2010 compared to Three and Six Months Ended June 30, 2009

Second Quarter of Fiscal 2010 vs. Second Quarter of Fiscal 2009

	Three Months Ended June 30,			As a % of Revenues June 30,	
	2010	2009	% Change	2010	2009
Revenues	$ 2,054,000	$ 576,000	257%	100%	100%
Cost of revenues	1,764,000	613,000	188%	86%	106%
Gross profit (loss)	290,000	(37,000)	884%	14%	-6%
Operating expenses					
Research and development	361,000	335,000	8%	18%	58%
Selling, general & administrative	1,551,000	1,570,000	-1%	76%	273%
Total operating expenses	1,912,000	1,905,000	0%	93%	331%
Operating loss	(1,622,000)	(1,942,000)	-16%	-79%	-337%
Other income and (expense)					
Interest and other income (expense)	(2,000)	(98,000)	-98%	0%	-17%
Gain (loss) from non-consolidated joint venture		6,000	-100%	0%	1%
Total other income (expense)	(2,000)	(92,000)	-98%	0%	-16%
Net loss	$ (1,624,000)	$ (2,034,000)	-20%	-79%	-353%

First Six Months of Fiscal 2010 vs. First Six Months of Fiscal 2009

	Six Months Ended June 30,			As a % of Revenues June 30,	
	2010	2009	% Change	2010	2009
Revenues	$ 2,983,000	$ 1,264,000	136%	100%	100%
Cost of revenues	2,610,000	1,192,000	119%	87%	94%
Gross profit (loss)	373,000	72,000	418%	13%	6%
Operating expenses					
Research and development	683,000	589,000	16%	23%	47%
Selling, general & administrative	3,028,000	3,065,000	-1%	102%	242%
Total operating expenses	3,711,000	3,654,000	2%	124%	289%
Operating loss	(3,338,000)	(3,582,000)	-7%	-112%	-283%
Other income and (expense)					
Interest and other income (expense)	(5,000)	(104,000)	-95%	0%	-8%

Gain (loss) from non-consolidated joint venture		(4,000)	-100%	0%	0%
Total other income (expense)	(5,000)	(108,000)	-95%	0%	-9%
Net loss	$ (3,343,000)	$ (3,690,000)	-9%	-112%	-292%

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 benefited from U.S. government grant programs, resulting in increased sales for fulfillment of initial orders from Smith Electric Vehicles, the North American subsidiary of Tanfield Group Plc, as well as Navistar Inc. The increase in revenue for the six months ended June 30, 2010 compared to 2009 was mainly due to the delivery of fifty electric drive systems to Smith Electric Vehicles and continued shipments of our hybrid drive systems to Navistar and First Auto Works (FAW). Although we have seen indications for future production growth, 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 increased primarily due to the increase in revenue. The improvement in the cost of revenue percentage is primarily attributable to our continuing focus on manufacturing and inventory processes that resulted in tighter control over production costs.

Gross Profit (Loss). The change in gross margin is primarily attributable to efficiencies gained from higher production volumes and increased sales of higher margin spare parts in the first half of 2010 and our recording an increased inventory charge in 2009. We continue to focus on key customer production contracts, maturity of our supply chain, and efficiencies gained through increased in-house manufacturing and inventory processes that have resulted in tighter controls over production costs. As we make deliveries on higher volume production contracts in the second half of 2010, we expect to achieve continued benefit from these initiatives, although we may continue to experience variability in our gross margin.

Research and Development (R&D). R&D costs were higher as we devoted increased engineering personnel resources to the development of our next generation motor control unit and charger, continued testing of our EV vehicles, new battery technologies and electric motors, as well as engine off capability for our post transmission parallel hybrid drive system. We also continued to allocate necessary resources to the development and testing of upgraded proprietary control software, DC-DC converters and digital inverters as well as other power management firmware.

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, and non-cash charges for depreciation and options expense. The Company s cost savings measures in response to last year s dire economic conditions have fully matured and become an integral part of the new sales environment in 2010. This also spurred a selective focus of key strategic marketing and customer service initiatives in 2010. The Company constantly evaluates contemporary or fully matured cost measures in the event of potential or future growth changes.

Interest and Other Income (Expense). Interest and other income increased as a result of the Company having a larger average investable cash balance after our equity raise in December 2009 and a non-recurring cost of $88,000 to settle a vendor dispute was recorded in the first half of 2009.

Gain (loss) from Non-Consolidated Joint Venture. A gain of $6,000 and a loss of $4,000 were recorded in the three and six month period ended June 30, 2009, respectively, reflecting the pro-rata share of gains/losses attributable to the dissolution of the joint venture and the forty percent investment interest in the Hyundai-Enova Innovative Technology Center (ITC). The joint venture partners, Hyundai Heavy Industries, Enova and ITC, mutually agreed to the dissolution of ITC, which was completed on April 6, 2009. No such gains or losses were realized in the first or second quarter of 2010.

Net Loss. The decrease in the net loss was mainly due to increase in gross profit resulting from higher sales.

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 2009. 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 cash flow shortages due to operating losses primarily attributable to research and development, marketing and other general and administrative costs associated with our strategic plan as an international developer and supplier of electric drive and power management systems and components. Cash flows from operations have not been sufficient to meet our obligations. Therefore, we have had to raise funds through several financing transactions. The extent of our capital needs will phase out once we reach a breakeven volume in sales or develop and/or acquire the capability to manufacture and sell our products profitably. Our operations during the six months ended June 30, 2010 were financed by product sales as well as from working capital reserves.

The Company has a secured revolving credit facility with a financial institution (the Credit Agreement) for $200,000 which expired on June 30, 2010 and was renewed on July 1, 2010 for a term of 3 years and 6 months for the same amount and credit terms. The Credit Agreement is secured by a $200,000 certificate of deposit (CD). The interest rate is the certificate of deposit rate plus 1.25% with interest payable monthly and the principal due at maturity. As of June 30, 2010, the renewed Credit Agreement was fully drawn as the financial institution has issued a $200,000 irrevocable letter of credit in favor of our landlord, Sunshine Distribution LP, with respect to the lease of the Company s new corporate headquarters at 1560 West 190th Street, Torrance, California.

Net cash used in operating activities was $2,678,000 for the six months ended June 30, 2010, an increase of $993,000 compared to $1,685,000 for the six months ended June 30, 2009. The increase in 2010 was primarily due to an increase in customer receivables from increased sales and a realization of revenue associated with the deferred revenue liability. Non-cash items include expense for stock-based compensation, depreciation and amortization, and issuance of common stock for employee services. Stock compensation to our directors was changed effective in 2010 from the issuance of common stock to the issuance of stock options. This resulted in a decrease in the issuance of common stock for director services from $90,000 to $0 and an increase in stock options expense from $230,000 to $285,000 in the first six months of 2010 compared to the first six months of 2009. We continued to conserve cash resources by maintaining our reduced employee headcount and restrictions on administration and operating expenditures. As of June 30, 2010, the Company had $10,203,000 of cash and cash equivalents.

Net cash used in investing activities for capital expenditures was $188,000 for the first six months of 2010 compared to net cash provided of $1,837,000 for the first six months of 2009. In 2009, in conjunction with the reduction of our credit facility, we redeemed a certificate of deposit for $2,000,000 for use in operating activities and renewed the certificate of deposit at a reduced amount of $200,000.

Net cash used in financing activities totaled $9,000 for the first six months of 2010, compared to net cash used in financing activities of $33,000 for the first six months of 2009. This decrease was attributed to proceeds from the exercise of stock options and lower payments on notes payable in the first six months of 2010 compared to the same period in 2009.

As of June 30, 2010, net accounts receivable was $1,660,000, a 15% increase from the balance at December 31, 2009 of $1,442,000. The increase in the receivable balance was due to sales on orders for Smith, Navistar and FAW shipped during the second quarter of 2010.

Inventory decreased by $695,000 when comparing the balances at June 30, 2010 and December 31, 2009, which represents a 12% decrease in the inventory balance between the two dates. The decrease resulted from net inventory activity including receipts totaling approximately $1,299,000 and normal consumption of approximately $1,891,000 due to sales and research activities during the first six months of 2010.

Prepaid expenses and other current assets increased by a net $173,000, or 66%, to $436,000 at June 30, 2010 from the December 31, 2009 balance of $263,000. The increase was due to a deposit of $179,000 made on a purchase order to Hyundai Heavy Industries for electric motors to be delivered in the third quarter of 2010.

Long term accounts receivable increased to $215,000 at June 30, 2010 compared to $0 at December 31, 2009. The Company agreed to defer collection of accounts receivable as requested by a customer for the term of the Company s warranty guarantee. The Company has remedied all past and current warranty claims and anticipates full collection of the receivable.

Property and equipment decreased by $57,000, net of depreciation, at June 30, 2010, when compared to the December 31, 2009 balance of $1,363,000. In the first six months of 2010, the Company recognized depreciation expense of $271,000 and recorded additions to fixed assets totaling $188,000.

Accounts payable increased in the first six months of 2010 by $221,000 to $636,000 from $415,000 at December 31, 2009. The increase is due to purchases of inventory, mainly batteries, for customer sales in the second and third quarters of 2010.

Deferred revenues decreased by $259,000 to a balance of $98,000 at June 30, 2010 compared to a $357,000 balance at December 31, 2009. This balance is anticipated to be realized into revenue in the third quarter of 2010 and is associated with prepayment on purchase orders from several different customers.

Accrued payroll and related expenses increased by $266,000, or 96%, to $543,000 at June 30, 2010 compared to a balance of $277,000 at December 31, 2009. The change is primarily due to the accrual of a management estimate of 2010 employee incentive bonuses.

Other accrued liabilities decreased by $299,000, or 23%, to $988,000 at June 30, 2010 from the balance of $1,287,000 at December 31, 2009, primarily due to payments for accrued professional services and inventory, as well as a net decrease in the accrued warranty balance as costs for warranty repairs were greater than warranty accruals for sales during the first half of the year.

Accrued interest payable was $1,115,000 at June 30, 2010, an increase of 4% from the balance of $1,074,000 at December 31, 2009. The increase is due to interest related to our debt instruments, primarily the secured note payable in the amount of $1,238,000 to the Credit Managers Association of California.

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Our ongoing operations and anticipated growth will require us to make necessary investments in human and production resources, regulatory compliance, as well as sales and marketing efforts. We anticipate that our current cash balance and projected cash inflow as mentioned in the Recent Development section above regarding our capital raise will be adequate to meet our working capital and capital expenditure needs for at least the next 12 months. If we require additional capital resources to grow our Company, we may seek to sell more equity securities. The sale of equity securities could result in dilution to our stockholders. We may not be able to obtain financing arrangements in amounts or on terms acceptable to us in the future. In the event we are unable to obtain additional financing when needed, we may be compelled to delay or curtail our plans to develop our business, which could have a material adverse effect on our operations, market position and competitiveness.

Off-Balance Sheet Arrangements

The Company has no off-balance sheet arrangements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

None.

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 Rule 13a-15(b) under the Securities and Exchange Act of 1934, as amended, 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 for the period covered by this report. Based on that evaluation, the Company s Chief Executive Officer and Chief Financial Officer have concluded that the Company s internal control over disclosure controls and procedures was effective as of June 30, 2010.

Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the quarter ended June 30, 2010 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

We are subject to a number of lawsuits, investigations and disputes (some of which involve substantial amounts claimed) 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 in excess of current accruals for these matters. Considering our past experience and existing accruals, 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

There have been no other material changes from the risk factors as previously disclosed in our Annual Report on Form 10-K for the fiscal year ended December 31, 2009.

ITEM 2. Unregistered Sales of Equity and Use of Proceeds

None.

ITEM 3. Defaults upon Senior Securities

None.

ITEM 4. Removed and Reserved

Not applicable.

ITEM 5. Other Information

None.

ITEM 6. Exhibits

a) Exhibits

31.1	Certification of the Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act Of 2002.*
31.2	Certification of the 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.*

* - Filed herewith

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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: August 11, 2010

ENOVA SYSTEMS, INC. (Registrant)

/s/ Jarett Fenton

By: Jarett Fenton, Chief Financial Officer

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EXHIBIT INDEX

31.1 Certification of the Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act Of 2002.

31.2 Certification of the 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.