

PIONEER POWER SOLUTIONS, INC.  
Form 10-K  
March 31, 2011

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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON D.C. 20549

FORM 10-K

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

For the fiscal year ended: December 31, 2010

OR

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

COMMISSION FILE NUMBER: 333-155375

PIONEER POWER SOLUTIONS, INC.  
(Exact name of Registrant as specified in its charter)

Delaware  
(State or other jurisdiction of incorporation)      27-1347616  
(I.R.S. Employer Identification Number)

One Parker Plaza  
400 Kelby Street, 9th Floor  
Fort Lee, New Jersey  
(Address of principal executive office)      07024  
(Zip Code)

Registrant's telephone number, including area code: (212) 867-0700

Securities registered pursuant to Section 12(b) of the Exchange Act: None

Securities registered pursuant to Section 12(g) of the Exchange Act: None

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Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.  
Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

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

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Indicate by check 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  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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.

Large accelerated filer <input type="checkbox"/>	Accelerated filer <input type="checkbox"/>
Non-accelerated filer <input type="checkbox"/> (Do not check if a smaller reporting company)	Smaller reporting company <input type="checkbox"/>

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

The aggregate market value of the voting and non-voting stock held by non-affiliates of the registrant as of the last business day of the registrant's most recently completed second fiscal quarter, based on the price at which the common equity was last sold on the OTC Bulletin Board on such date, was approximately \$16.5 million. For purposes of this computation only, all officers, directors and 10% or greater stockholders of the registrant are deemed to be affiliates.

Indicate the number of shares outstanding of each of the registrant's classes of common stock as of the latest practicable date.

Class	Outstanding at March 31, 2010
Common Stock, \$0.001 par value	29,536,275

Documents incorporated by reference:

None

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Form 10-K contains “forward-looking statements,” which include information relating to future events, future financial performance, strategies, expectations, competitive environment and regulation. Words such as “may,” “should,” “could,” “would,” “predicts,” “potential,” “continue,” “expects,” “anticipates,” “future,” “intends,” “plans,” “believes,” “estimates,” and “will” are intended to identify forward-looking statements. Forward-looking statements should not be read as a guarantee of future performance or results and will probably not be accurate indications of when such performance or results will be achieved. Forward-looking statements are based on information we have when those statements are made or our management’s good faith belief as of that time with respect to future events, and are subject to risks and uncertainties that could cause actual performance or results to differ materially from those expressed in or suggested by the forward-looking statements. Important factors that could cause such differences include, but are not limited to:

- General economic conditions and market conditions in the electrical equipment, power generation, commercial construction, industrial production, oil & gas, marine and infrastructure industries.
  - Market acceptance of existing and new products.
  - Successful integration of acquisitions and related restructuring.
- Operating margin risk due to competitive pricing and operating efficiencies, supply chain risk, material, labor or overhead cost increases, foreign currency risk, interest rate risk and commodity risk.
- The impact of geopolitical activity on the economy, changes in government regulations such as income taxes, climate control initiatives, the timing or strength of an economic recovery in our markets and our ability to access capital markets.
- We depend on Hydro-Quebec Utility Company and Siemens Industry, Inc. for a large portion of our business, and any change in the level of orders from Hydro-Quebec Utility Company or Siemens Industry, Inc., could have a significant impact on our results of operations.
- Unanticipated increases in raw material prices or disruptions in supply could increase production costs and adversely affect our profitability.
- A majority of our expenditures and revenue is spent or derived in Canada. However, we report our financial condition and results of operations in U.S. dollars. As a result, fluctuations between the U.S. dollar and the Canadian dollar will impact the amount of our revenues.
- Many of our competitors are better established and have significantly greater resources, and may subsidize their competitive offerings with other products and services, which may make it difficult for us to attract and retain customers.
- Restrictive loan covenants under our credit facilities could limit our future financing options and liquidity position and may limit our ability to grow our business.
- Our chairman controls a majority of our combined voting power, and may have, or may develop in the future, interests that may diverge from yours.
  - Future sales of large blocks of our common stock may adversely impact our stock price.

When used herein, unless the context requires otherwise, references to the “Company,” “Pioneer,” “we,” “our” and “us” periods prior to the closing of our share exchange on December 2, 2009 refer to Pioneer Transformers Ltd., a company incorporated under the Canada Business Corporations Act that is now our wholly-owned subsidiary, and its subsidiaries. For periods subsequent to the closing of the share exchange on December 2, 2009, references to the “Company,” “Pioneer,” “we,” “our” and “us” refer to Pioneer Power Solutions, Inc., a publicly traded company, and subsidiaries, including Pioneer Transformers Ltd., Jefferson Electric, Inc., and Pioneer Wind Energy Systems Inc.

## PART I

### ITEM 1. BUSINESS.

#### Overview

Pioneer Power Solutions, Inc., based in Fort Lee, New Jersey, is an owner and operator of specialty electrical equipment manufacturing and service businesses. Our subsidiaries provide a range of products and services to the electrical transmission and distribution industry and our focus is on the electric utility, industrial, commercial and wind energy market segments. We intend to grow our business by increasing our portfolio of highly-engineered solutions for specialty electrical applications, both through acquisitions and internal product development.

Our customers, which include a number of recognized electric utilities, are primarily located in North America. We presently have five locations in the U.S., Canada and Mexico for manufacturing, centralized distribution, engineering, sales and administration. In addition, we have a network of 21 independently-operated stocking locations in the United States, including two regional distribution centers.

#### Operating Structure

We operate in two business segments, electrical transformers and wind energy equipment and services.

#### Electrical Transformers

Our electrical transformers segment designs and manufactures a full line of custom and standard liquid-filled, encapsulated and ventilated electrical transformers used in the control and conditioning of electrical current for critical processes. Our operating companies, Pioneer Transformers Ltd. and Jefferson Electric, Inc., specialize in liquid-filled and dry-type transformers, respectively. Each business unit distinguishes itself by producing a wide range of engineered-to-order and standard equipment, sold either directly to end users, through engineering and construction firms, or through wholesale distributors. We serve customers in a variety of industries including electric utilities, industrial customers, commercial construction companies, original equipment manufacturers, brand label customers and renewable energy producers.

#### Wind Energy Equipment and Service Business

We are currently developing our wind energy business segment to provide project integration solutions, including equipment sales, procurement, after-sales services and financing to community wind and industrial customers seeking wind turbines with generation capacities of one to two megawatts (MW). Our wind energy operating company, Pioneer Wind Energy Systems Inc., was established through an acquisition in 2010. Its predecessors have a 10-year history of developing, manufacturing, commissioning and servicing our advanced wind turbine designs, principally the P-1650, which is a 1.65 MW wind turbine generator. Our portfolio of completed projects encompasses five units in the Northeast U.S., California and for the U.S. military, all commissioned between 2008 and 2010. We intend to rely on Pioneer Wind Energy Systems Inc.'s portfolio of licensed technologies and our expertise in engineering, procurement and field services to meet the specific challenges of each wind energy project. We also intend to advance growth in this segment of our business by offering customers creative financing arrangements with extended payment terms and revenue-sharing features.

#### Business Strategy

We believe we have developed a stable platform from which to develop and grow our business lines, revenues, earnings and shareholder value. We intend to expand rapidly over the next several years through a two-pronged strategy. First, we intend to pursue strategic acquisitions that provide us with complementary product and service offerings, new sales channels, end markets and scalable operations. Second, we are focused on internal growth through operating efficiencies, customer focus and our continued migration towards more highly-engineered products and specialized services.

## Acquisitions

We believe a disciplined acquisition program is a key component to accelerating our growth and we intend to pursue opportunities to acquire businesses that broaden the range of customer solutions we provide, increase our market share or expand our geographic reach. In addition to transformer manufacturers, we also intend to acquire producers of other technically-advanced, customized, ancillary or complementary products which address market segments where we seek penetration -- such as in power quality and conditioning. We operate in a highly fragmented industry that is served by a few global diversified electrical equipment manufacturers and numerous small manufacturing companies that provide niche products and services to various sub-segments of the power transmission and distribution market. We favor candidates that have competencies and business characteristics similar to our own, and those that we expect will benefit from some of the major trends affecting our industry.

## Internal Growth

We intend to build our revenue and earnings at rates exceeding industry norms primarily by continuing our sales and product mix movement towards more value-added products. We intend to accomplish this goal within our liquid-filled transformer business by emphasizing the sale of more power, network and subsurface transformers to new and existing utility customers, particularly in the U.S. In February 2011, we completed a plant expansion that added approximately 6,000 square feet to our Granby, Quebec facility which will allow us to increase our manufacturing capacity for these larger products. We believe our internal growth objectives for our dry-type transformer business will be achieved by expanding the geographic coverage and productivity of our national distribution network, as well as by continuing to expand our direct sales channel with original equipment manufacturers (OEMs) and brand label customers. Within our wind energy business, we intend to cross-sell equipment manufactured by our other business units, find innovative ways to make our products and services more accessible and better suited to community wind market customers, and establish new partnerships with major international wind turbine equipment manufacturers as appropriate.

## Products

### Electrical Transformers

We design, develop, manufacture and sell a wide range of liquid-filled and dry-type power, distribution and specialty electrical transformers. An electric transformer is used to reduce or increase the voltage of electricity traveling through a wire. This is accomplished by transferring electric energy from one coil or winding to another coil through electromagnetic induction. Electric power generating plants use generator transformers to “step-up,” or increase, voltage that is transferred through power lines in order to transmit the electricity more efficiently and over long distances. When the high voltage electricity nears its final destination, a “step-down” transformer reduces its voltage. A distribution transformer makes a final step-down in voltage by diminishing the force of the electricity to a level usable in homes and businesses.

Transformers are integral to every electrical transmission and distribution system. Electric utilities use transformers for the construction and maintenance of their power networks. Industrial firms use transformers to supply factories with electricity and to distribute power to production machinery. The renewable energy industry uses transformers to connect new sources of electricity generation to the power grid, as does the construction industry for the supply of electricity to new homes and buildings.

### Liquid-Filled Transformers



Our liquid-filled transformer products are manufactured by our wholly-owned subsidiary, Pioneer Transformers Ltd., in electrical power ranges from 25 kVA (kilovolt amperes) to 30 MVA (megavolt amperes) and at up to 69 kV (kilovolts) in voltage. In recent years, we have focused primarily on the small power market, generally considered to include transformers between 1 MVA and 10 MVA, as well as on specialty transformers such as network and other highly-customized models. We sell these products to electrical utilities, independent power providers, electrical co-ops, industrial companies, commercial users and electric equipment wholesalers. Our primary categories of liquid-filled transformers are as follows:

Transformer Type	Range of Sizes	Applications
Small and Medium Power	300 kVA to 30 MVA	Power conversion for the utility and industrial/commercial market, typically found in substations
Network	300 kVA to 3.75 MVA	Subway and vault-type transformers designed to withstand harsh environments and typically used by utilities and municipal power authorities to ensure reliability of service
Pad-Mount	75 kVA to 10 MVA	Distribution transformers commonly used in underground power or distribution systems
Unitized Pad-Mount	Up to 5 MVA	Combines pad-mounts with other equipment in a product that can be substituted for conventional unit substations at apartment complexes, shopping centers, hospitals and similar commercial facilities
Mini-Pad	25 kVA to 167 kVA	Single phase, low profile pad-mounted distribution transformers for residential and underground distribution
Platform-Mount	250 kVA to 2.5 MVA	Single phase units from 250 kVA to 1 MVA, also supplied for substation installation up to 2.5 MVA

### Dry-Type Transformers

Our dry-type transformer products are manufactured by our wholly-owned subsidiary, Jefferson Electric, Inc. Our focus is primarily on low voltage distribution transformers for commercial and industrial power applications, typically in the 15 kVA through 1 MVA size range and for indoor use. Our primary categories of dry-type transformers are as follows:

Transformer Type	Range of Sizes	Applications
Encapsulated Single & Three Phase	50 VA to 50 kVA 3 kVA to 75 kVA	General purpose encapsulated transformers for lighting, industrial and commercial applications. Suitable for indoor or outdoor use
Ventilated Single & Three Phase	25 kVA to 100 kVA 15 kVA to 1 MVA	Ventilated transformers designed for general loads, indoors or out, including for lighting, industrial and commercial applications
Floor Mount Encapsulated	30 kVA to 75 kVA	For all general loads in rugged environment areas including refineries, factories, chemical plants, marine duty, ship docks, and grain mills

Buck Boost Transformers	50 VA to 10 kVA	Single phase transformers for correcting voltage line drops, landscape lighting, low voltage lighting, international voltage adaptation and motor applications
Non-Linear Transformers	15 kVA to 300 kVA	Jefferson Plus™ line of non-linear transformers are designed to meet the load demands caused by computers and other electronic office equipment
Other Transformers	Various size ranges	Drive isolation, industrial control and custom designed transformers, lighting ballasts, reactors, filters and associated other parts

## Wind Energy Products & Services

Our P-1650 model wind turbine generator is a 1.65 MW, three-blade wind turbine equipped with full span pitch control and a transmission system with integrated main shaft and main bearings. Our P-1650 turbine is Germanischer Lloyd-certified and was developed by us through a technology license with AMSC Windtec GmbH, a subsidiary of American Superconductor. There is only one other company licensed to sell this wind turbine design in the U.S. The P-1650 unit is also available in a 1.5 MW power rating and can be delivered with a tower height ranging from 65 to 100 meters and a rotor diameter of 77 meters. This model uses a variable speed asynchronous generator and fixed speed gearbox. The combination of electrical torque control and variable pitch control allows the wind turbine to operate at wind speeds from 3.5 meters per second (m/s) and with a constant 1.65 MW energy production in wind speeds between 11 m/s and 20 m/s. In situations where the site characteristics and investment constraints of a project are not conducive to the deployment of our P-1650 unit, our strategy is to acquire and resell comparable units from other manufacturers that meet the project owner's requirements.

Our monitoring service provides real-time performance tracking and remote control of wind turbines in operation. We also provide operations and maintenance (O&M) services including scheduled maintenance, as well as unscheduled maintenance in situations where uncharacteristic weather conditions, network disturbances or other operating complications arise. As is standard in our industry, we offer a range of manufacturer warranties:

- electro-mechanical warranty (two years standard);
- power curve warranty (one year standard);
- sound level warranty (one year standard); and
- an availability warranty covering the duration of the O&M contract.

According to each customer's needs, we also offer extended warranties typically covering the three to five year period after installation.

Harnessing the power of wind requires knowledge of the grid, electrical equipment expertise and an understanding of the complexities of interconnection. In addition to wind turbine products, our wind energy business assists customers in the procurement of ancillary electrical equipment for the project balance of plant, including medium voltage switchgear and liquid-filled transformers such as those manufactured by Pioneer Transformers Ltd.

Community wind projects require a substantial investment. The cost of a single 1.65 MW wind turbine such as ours, including blades and the tower, typically will exceed \$2 million. In addition, the project owner must fund the costs of transportation, construction, the balance of plant and professional fees. In order to alleviate this obstacle for qualified projects, our wind energy business seeks to provide vendor financing for the wind turbine portion of the total project cost. We offer financing structures tailored to each project that reduce the amount of down payment required and establish a repayment schedule following delivery that includes interest charges. Our equipment financing terms are accompanied by customary credit protections and may require that the customer purchase a minimum scope of related services from us, such as an O&M contract.

## Our Industries

### Electrical Transmission & Distribution Equipment

Demand for our electrical power and distribution transformers results primarily from spending by electric utilities for replacement equipment, grid expansion and efficiency improvements. Demand is also sensitive to overall economic conditions, particularly with respect to the level of industrial production and investment in commercial and residential construction. Other market factors include voltage conversion, voltage unit upgrades, electrical equipment failures, higher energy costs, stricter environmental regulations and investment in sources of renewable energy generation.

According to IBISWorld Inc., a market research firm, the total value of U.S. electrical equipment industry shipments was approximately \$34.6 billion in 2010. Of this amount, 16.0%, or \$5.5 billion, was comprised of power, distribution and specialty transformers, compared with a 13.1% share of total shipments for transformers in 2002. Together with Canadian shipments of transformers, we believe that the North American market currently exceeds \$6.0 billion annually. IBISWorld expects U.S. electrical equipment industry revenue to increase in real terms on average by 4.3% annually in the five year period ending in 2015.

This prediction of industry growth is consistent with the need to modernize and upgrade the U.S. power grid and is supported by regulatory initiatives intended to improve system stability and promote growth in electric power generation by independent producers and in renewable energy sources such as wind power. For example, according to The Brattle Group, a consulting firm, 70% of all power transformers in the U.S. are currently over 25 years old. Moreover, The Brattle Group estimates \$1.5 trillion of capital investment will be required in the U.S. electrical infrastructure by 2030 in order to meet growing demand and targets for efficiency, emissions and renewable sources in light of the fact that numerous components of the U.S. power grid are operating at, close to or past their planned service lives. A majority of these expenditures, or approximately \$900 billion, is expected by The Brattle Group to be for transmission and distribution equipment, with the remainder being spent on increasing generation capacity.

The transformer market is very fragmented due to the range of sizes, voltages and technological standards required by different categories of end users. Many orders are custom-engineered and tend to be very time-sensitive since other critical work is frequently being coordinated around the customer's transformer installation. The vast majority of North American demand for transformers is satisfied by producers in the U.S. and Canada. According to the U.S. Census Bureau, there are over 250 transformer manufacturers in the U.S. and at least 50 that manufacture larger power and distribution transformers such as those produced by us.

### Wind Energy Equipment & Services

With rising energy demand, volatile carbon fuel prices and increasing awareness of the effects of climate change, the wind power market has expanded substantially in the U.S. over the past 5 years. As of January 2011, the American Wind Energy Association (AWEA) reported that total U.S. wind generation capacity stands at 40,180 MW, representing an average annual increase of 35% per annum since the year 2005. Due primarily to the effects of the economic downturn and financial crisis starting in 2008, the rate of U.S. wind generation capacity additions decreased significantly in 2010 versus 2009, but still grew 15% in 2010. The latest industry statistics from AWEA indicate that wind power projects accounted for 39% of all new generating capacity added in 2009 and 1.8% of all electricity provided to the U.S. electric grid.

Investment in wind generation capacity is heavily dependent on government incentives to promote commercial-scale development. The effectiveness of these incentives, principally federal programs like the production tax credit (PTC) and the investment tax credit (ITC), has been marred by frequent expirations and one-to-two-year extension periods. Historical uncertainty surrounding the continuation of such incentives has created a boom-and-bust cycle of wind

project development and hindered rational industry planning, investments in technology and efforts to reduce costs. In addition to federal-level tax incentives, wind project development is also driven by states that have instituted their own renewable portfolio standards (RPS) requiring electricity service providers to gradually increase the percentage of renewable sources used to meet their electricity demand by specified dates. RPS policies, which invoke financial penalties on service providers if targets are not met, currently exist in 28 U.S. states, but not at the national level.

The wind turbine equipment market is dominated by several large, multi-national manufacturers that are equipped for orders requiring dozens or even hundreds of units sold to utilities and other well-capitalized project developers. By contrast, the market segment addressed by our wind energy business, “community wind,” encompasses projects that are locally owned and employ utility-scale equipment, but are generally intended to have less than 20 MW in generation capacity, with many requiring as few as one wind turbine. Community wind projects are commonly owned by municipal or cooperative electric utilities, towns, universities, individual landowners and local businesses or factories. Although community wind represents only a small sub-sector of the entire U.S. wind market, it has several characteristics that we believe are favorable to our business:

- local ownership and support which tends to facilitate project approval and implementation; and
- the power generated is often for on-site consumption, rather than exclusively intended for resale and distribution into the broader grid.

These factors generally make the viability of community wind projects less susceptible to fluctuations in wholesale electricity prices and the availability of financing in the capital markets. At the same time, given the relatively small size of community wind projects, developers frequently have difficulty attracting major turbine manufacturers and traditional sources of financing, challenges that we feel represent an opportunity for our wind energy business.

#### Customers

Prior to 2010, we sold our products principally to Canadian customers, including many of Canada’s electrical utilities, municipal power systems, large industrial companies, engineering and construction firms and a number of electrical distributors. After giving effect to our acquisition of Jefferson Electric, Inc. on April 30, 2010, we expect annual sales in our electrical transformers segment to be more balanced between the U.S. and Canada, with Canadian customers still representing the majority. In our wind energy segment, Pioneer Wind Energy Systems Inc. is focused primarily on selling products and services to U.S. customers, and did not make any contribution to our revenue during 2010.

Approximately 36% and 40% of our sales in 2010 and 2009, respectively, were made to Hydro-Quebec Utility Company, a government-owned utility in the Province of Quebec, Canada. The majority of our sales to Hydro-Quebec Utility Company are made pursuant to a long-term contract for the supply of pad-mount transformers that expired and was replaced in 2010. In 2010, we were awarded an additional contract by Hydro-Quebec Utility Company for the supply of submersible transformers. Both contracts have initial terms expiring during the second quarter of 2012 and two one-year renewal options providing for a maximum term of four years. The contracts set forth the terms, conditions and rights of the parties with respect to the supply of the subject products including ordering and delivery procedures, required technical specifications, minimum performance standards, product pricing and price adjustment mechanisms, terms of payment and rights of termination. The contracts do not require Hydro-Quebec Utility Company to order any minimum quantity of products from us and do not grant us any form of supply exclusivity. Hydro-Quebec Utility Company has been a customer of ours and our predecessors for approximately 40 years, over which time we have been party to consecutive long-term contracts for an uninterrupted period spanning several decades. We believe the status of our business relationship with Hydro-Quebec Utility Company to be good. In 2010, no other customer accounted for 10% or more of our sales, although Siemens Industry, Inc., a significant customer of our Jefferson Electric, Inc. subsidiary, did represent 9%. Aside from Hydro-Quebec Utility Company and Siemens Industry, Inc., we do not believe that the loss of any specific customer would have a material adverse effect on our business.

#### Marketing, Sales and Distribution

A substantial portion of the transformers manufactured by us are sold to customers by our direct sales force of full-time sales personnel and executive management operating from our office locations in the U.S. and Canada. Our transformer products are also sold through a network of independent sales agents throughout North America that sell primarily to full-line electrical distributors and to maintenance, repair and overhaul organizations. Our direct sales force markets to end users and to third parties, such as original equipment manufacturers and engineering firms, that prescribe the specifications and parameters that control the applications of our products. Our wind energy products and services are marketed entirely on a direct basis to customers by our full-time business development personnel.



## Sales Backlog

Backlog reflects the amount of revenue we expect to realize upon the shipment of customer orders for our transformer products that are not yet complete or for which work has not yet begun. Our sales backlog as of December 31, 2010 was approximately \$18.7 million, as compared to \$16.5 million at December 31, 2009. We anticipate that substantially all of our current backlog will be delivered during 2011. Orders included in our sales backlog are represented by customer purchase orders and contracts that we believe to be firm. As of December 31, 2010, there was no backlog for our wind energy business.

## Competition

### Electrical Transformer Business

We experience competition from a large number of transformer manufacturers. The number and size of our competitors varies considerably by product line, with many of our competitors tending to be small, highly specialized or focused on a certain geographic market area or customer. However, several of our competitors have substantially greater financial and technical resources than us, including some of the world's largest electrical products companies. A representative list of our competitors includes ABB Ltd., Actuant Corporation, Carte International, Inc., Cooper Industries plc, General Electric Company, Groupe Schneider, Hammond Power Solutions Inc., Howard Industries, Inc. and Partner Technologies, Inc.

We believe that we compete primarily on the basis of product quality, product innovation, product availability, service and price. In our liquid-filled transformer business, we have established a niche in the manufacture and design of small power and distribution electrical transformers and, in particular, custom transformers for specialized and complex applications. As a result of our long-time presence in the industry, we possess a number of special transformer designs that we have engineered and developed specifically for our customers. We believe these designs give us a competitive advantage and that they are a major contributor to our frequency of repeat customer orders. Our customers order from us as their needs may require, and the level of their orders can change significantly from year-to-year based on the status of their individual construction projects and capital budgeting activities. Despite these variations we have a significant number of repeat customers. Approximately 40% to 50% of our customers in any given year were also customers in the prior year. In our dry-type transformer business, we believe that we compete primarily on the basis of product quality, price, availability, on-time shipment record, service and flexibility to provide custom-engineered solutions to satisfy customer needs.

### Wind Energy Business

The wind turbine equipment and services business is highly competitive and dominated by a few much larger corporations with significantly greater resources than us such as GE Energy, Vestas Wind Systems A/S, Siemens Wind Power A/S and Gamesa Corporation Tecnologica S.A. In future years we also expect increasing competition in the North American market from a number of low-cost manufacturers based in China. Our ability to grow in the face of this competition will depend on our ability to successfully provide customized, innovative solutions to community wind customers, a segment of the marketplace we currently believe to be underserved by our competition.

## Raw Materials and Suppliers

The principal raw materials purchased by us are core steel, copper wire, aluminum strip and insulating materials including transformer oil. We also purchase certain electrical components from a variety of suppliers including bushings, switches, fuses and protectors. These raw materials and components are available from and supplied by numerous sources at competitive prices, although there are more limited sources of supply for electrical core steel and transformer oil. Unanticipated increases in raw material prices or disruptions in supply could increase production costs and adversely affect our profitability. We attempt to minimize the effect on our profit margins of unanticipated changes in the prices of raw materials by including escalation clauses in our customer contracts that allow us to increase or reduce our fees if the costs of raw materials unexpectedly rise or decrease. Approximately 50% of our annual sales are made pursuant to contracts that contain such escalation clauses, which, subject to various formulae and limitations, permit us to adjust the final prices we charge. We anticipate no significant difficulty fulfilling our raw material purchase requirements and have not experienced any such difficulty in the past several years. Our largest suppliers include Aztek Technologies, S.A. De C.V, Cogent Power, Inc., Essex Group, Inc., Itochu Corporation, JFE Shoji Steel America, Inc. and Rea Magnet Wire Company.

Purchases of raw materials and components in our wind energy business were insignificant during the seven-month period in 2010 in which we were an industry participant. In the future, as order volume may dictate, we anticipate that the largest components of our purchases will consist of finished wind turbine nacelles, towers and rotor blades. The wind turbine equipment supply chain is a large and global industry with many participants and we do not anticipate significant difficulty in fulfilling our potential future purchasing requirements.

## Employees

At December 31, 2010, we had 203 employees consisting of 58 salaried staff and 145 hourly workers. We also had two part-time employees. Our hourly employees located at our plant in Granby, Quebec, Canada are covered by a collective bargaining agreement with the United Steel Workers of America Local 9414 that expires in May 2015. The hourly employees located at our manufacturing facility in Reynosa, Mexico are also covered by a collective bargaining agreement with a local labor union that has an indefinite term, subject to annual review and negotiation of key provisions. We consider our relationship with our employees to be good.

## Environmental

We are subject to numerous environmental laws and regulations concerning, among other areas, air emissions, discharges into waterways and the generation, handling, storing, transportation, treatment and disposal of waste materials. These laws and regulations are constantly changing and it is impossible to predict with accuracy the effect they may have on us in the future. Like many other industrial enterprises, our manufacturing operations entail the risk of noncompliance, which may result in fines, penalties and remediation costs, and there can be no assurance that such costs will be insignificant. To our knowledge, we are in substantial compliance with all federal, state, provincial and local environmental protection provisions, and believe that the future cost of fines, penalties and remediation protection provisions, if any, should not have a material adverse effect on our capital expenditures, earnings or competitive position. However, legal and regulatory requirements in these areas have been increasing and there can be no assurance that significant costs and liabilities will not be incurred in the future due to regulatory noncompliance.

## Corporate History

We were originally formed in the State of Nevada in 2008. On November 30, 2009, we merged with and into Pioneer Power Solutions, Inc., a Delaware corporation and our wholly-owned subsidiary, for the sole purpose of changing our state of incorporation from Nevada to Delaware and changing our name to "Pioneer Power Solutions, Inc." On

December 2, 2009, pursuant to a share exchange agreement, we acquired all of the issued and outstanding capital stock of Pioneer Transformers Ltd. and our officers and directors were replaced by designees of Pioneer Transformers Ltd. After the share exchange, we divested all of our pre-share exchange operating assets and succeeded to the business of Pioneer Transformers Ltd. as our sole line of business.

On April 30, 2010, we acquired Jefferson Electric, Inc. through a merger pursuant to which JEI Acquisition, Inc., a wholly-owned subsidiary of ours, merged with and into Jefferson Electric, Inc., with Jefferson Electric, Inc. continuing as the surviving corporation and becoming a wholly-owned subsidiary of ours.

On June 7, 2010, through our wholly-owned subsidiary Pioneer Wind Energy Systems Inc., we acquired substantially all the inventory, capital assets, intangible assets and intellectual property of AAER Inc., a manufacturer of wind turbines with generation capacities exceeding one MW based in Quebec, Canada. On August 13, 2010, through our wholly-owned subsidiary Pioneer Wind Energy Holdings, Inc., we purchased common shares representing 100% of the voting and economic interests of AAER Inc., including its residual assets and accumulated operating tax losses. On December 31, 2010, we completed a share exchange in which Pioneer Wind Energy Systems Inc. was merged with and into AAER Inc., the entity through which we conduct all our wind energy business activities. On March 18, 2011, we amended the articles of incorporation of AAER Inc. to change its name to Pioneer Wind Energy Systems Inc.

#### ITEM 1A.RISK FACTORS.

Investing in our common stock involves a high degree of risk. Before investing in our common stock you should carefully consider the following risks, together with the financial and other information contained in this Form 10-K. If any of the following risks actually occurs, our business, prospects, financial condition and results of operations could be adversely affected. In that case, the trading price of our common stock would likely decline and you may lose all or a part of your investment.

##### Risks Relating to Our Business

Our industry is highly competitive.

The electrical transformer industry is highly competitive. Principal competitors in our markets include ABB Ltd., Carte International, Inc., Cooper Industries plc, General Electric Company, Groupe Schneider, Hammond Power Solutions Inc., Howard Industries, Inc. and Partner Technologies, Inc. A number of these competitors are significantly larger and have substantially greater resources than we do and are able to achieve greater economies of scale and lower cost structures than us and may, therefore, be able to provide their products to customers at lower prices than we are able to. Moreover, we cannot be certain that our competitors will not develop the expertise, experience and resources to offer products that are superior in both price and quality to our products. Similarly, we cannot be certain that we will be able to maintain or enhance our competitive position within our industry, maintain our customer base at current levels or increase our customer base.

Because we currently derive a significant portion of our revenues from two customers, any decrease in orders from these customers could have an adverse effect on our business, financial condition and operating results.

We depend on Hydro-Quebec Utility Company for a large portion of our business, and any change in the level of orders from Hydro-Quebec Utility Company, has, in the past, had a significant impact on our results of operations. In particular, Hydro-Quebec Utility Company represented a substantial portion of our sales, approximately 36% and 40% of net sales in the years ended December 31, 2010 and 2009, respectively. In addition, Siemens Industry, Inc. accounted for 34% and 29% of Jefferson Electric, Inc.'s net sales in the years ended December 31, 2010 and 2009, respectively. If either of these customers was to significantly cancel, delay or reduce the amount of business it does with us, there could be a material adverse effect on our business, financial condition and operating results. Our long term supply agreements for the sale of our products to Hydro-Quebec Utility Company expire in 2012 and we therefore cannot assure you that Hydro-Quebec Utility Company will continue to purchase transformers from us in quantities consistent with the past or at all. Moreover, although Jefferson Electric, Inc. has an agreement for the sale

of its products to Siemens Industry, Inc., nothing in the agreement provides assurance that Siemens Industry, Inc. will continue to purchase transformers from Jefferson Electric, Inc. in quantities consistent with the past or at all. If either of these customers were to become insolvent or otherwise unable to pay or were to delay payment for services, our business, financial condition and operating results could also be materially adversely affected.

Fluctuations in the price and supply of raw materials used to manufacture our products may reduce our profits.

Our raw material costs represented approximately 63% and 64% of our revenues for the years ended December 31, 2010 and 2009, respectively. Although we anticipate that this percentage will be lower in the future due to our acquisition of Jefferson Electric, Inc., there is no guarantee that such result will be achieved. The principal raw materials purchased by us are core steel, copper wire, aluminum strip and insulating materials including transformer oil. We also purchase certain electrical components from a variety of suppliers including bushings, switches, fuses and protectors. These raw materials and components are available from and supplied by numerous sources at competitive prices, although there are more limited sources of supply for electrical core steel and transformer oil. Unanticipated increases in raw material prices or disruptions in supply could increase production costs and adversely affect our profitability. While we do not anticipate significant difficulty fulfilling our raw material purchase requirements and have not experienced any such difficulty in the past three years, we cannot provide any assurances that we will not experience such difficulties in the future.

We may not be able to fully realize the revenue value reported in our backlog.

We have a backlog of work to be completed on contracts. Orders included in our backlog are represented by customer purchase orders and contracts that we believe to be firm. Backlog develops as a result of new business taken, which represents the revenue value of new customer orders received by us during a given period. Backlog consists of customer orders that either (1) have not yet been started or (2) are in progress and are not yet completed. In the latter case, the revenue value reported in backlog is the remaining value associated with work that has not yet been completed. From time to time, customer orders are canceled that appeared to have a high certainty of going forward at the time they were recorded as new business taken. In the event of a customer order cancellation, we may be reimbursed for certain costs but typically have no contractual right to the total revenue reflected in our backlog. In addition to our being unable to recover certain direct costs, canceled customer orders may also result in additional unrecoverable costs due to the resulting underutilization of our assets.

We are subject to pricing pressure from our larger customers.

We face significant pricing pressures in all of our business segments from our larger customers, including Hydro-Quebec Utility Company. Because of their purchasing size, our larger customers can influence market participants to compete on price terms. Such customers also use their buying power to negotiate lower prices. If we are not able to offset pricing reductions resulting from these pressures by improved operating efficiencies and reduced expenditures, those price reductions may have an adverse impact on our financial results.

Deterioration in the credit quality of several major customers could have a material adverse effect on our operating results and financial condition.

A significant asset included in our working capital is accounts receivable from customers. If customers responsible for a significant amount of accounts receivable become insolvent or otherwise unable to pay for products and services, or become unwilling or unable to make payments in a timely manner, our operating results and financial condition could be adversely affected. A significant deterioration in the economy could have an adverse effect on the servicing of these accounts receivable, which could result in longer payment cycles, increased collection costs and defaults in excess of management's expectations. Deterioration in the credit quality of Hydro-Quebec Utility Company, Siemens Industry, Inc. or of any other major customers, could have a material adverse effect on our operating results and financial condition.



We may face impairment charges if economic environments in which our business operates and key economic and business assumptions substantially change.

Assessment of the potential impairment of property, plant and equipment, goodwill and other identifiable intangible assets is an integral part of our normal ongoing review of operations. Testing for potential impairment of long-lived assets is dependent on numerous assumptions and reflects our best estimates at a particular point in time, which may vary from testing date to testing date. The economic environments in which our businesses operate and key economic and business assumptions with respect to projected product selling prices and materials costs, market growth and inflation rates, can significantly affect the outcome of impairment tests. Estimates based on these assumptions may differ significantly from actual results. Changes in factors and assumptions used in assessing potential impairments can have a significant impact on both the existence and magnitude of impairments, as well as the time at which such impairments are recognized. Future changes in the economic environment and the economic outlook for the assets being evaluated could also result in additional impairment charges. Any significant asset impairments would adversely impact our financial results.

We are vulnerable to economic downturns in the commercial construction market, which may reduce the demand for some of our products and adversely affect our sales, earnings, cash flow or financial condition.

Portions of our business, in particular those of Jefferson Electric, Inc., involve sales in connection with commercial real estate construction. Our sales to this segment are affected by the levels of discretionary consumer and business spending. During economic downturns in these segments, the levels of consumer and business discretionary spending may decrease. This decrease in spending will likely reduce the demand for some of our products and may adversely affect our sales, earnings, cash flow or financial condition.

The commercial and industrial building and maintenance sectors began to experience a significant decline in 2008. The downturn in these segments contributed to a decline in the demand for some of Jefferson Electric, Inc.'s products and adversely affected Jefferson Electric, Inc.'s sales and earnings in prior periods. We cannot predict the duration or severity of the downturn in these segments. Continued downturn in these segments could continue to reduce the demand for some of our products and may adversely impact sales, earnings and cash flow.

Our operating results may vary significantly from quarter to quarter.

Our quarterly results may be materially and adversely affected by:

- the timing and volume of work under new agreements;
- general economic conditions;
- the spending patterns of customers;
- customer orders received;
- losses experienced in our operations not otherwise covered by insurance;
- a change in the demand or production of our products caused by severe weather conditions;
  - a change in the mix of our customers, contracts and business;
  - increases in design and manufacturing costs; and
- the ability of customers to pay their invoices owed to us and disagreements with customers related to product performance on delivery.

Accordingly, our operating results in any particular quarter may not be indicative of the results that you can expect for any other quarter or for an entire year.

We rely on third parties whose operations are outside our control.



We rely on arrangements with third-party shippers and carriers such as independent shipping companies for timely delivery of our products to our customers. As a result, we may be subject to carrier disruptions and increased costs due to factors that are beyond our control, including labor strikes, inclement weather, natural disasters and rapidly increasing fuel costs. If the services of any of these third parties become unsatisfactory, we may experience delays in meeting our customers' product demands and we may not be able to find a suitable replacement on a timely basis or on commercially reasonable terms. Any failure to deliver products to our customers in a timely and accurate manner may damage our reputation and could cause us to lose customers.

We also utilize third party distributors and manufacturer's representatives to sell, install and service certain of our products. While we are selective in whom we choose to represent us, it is difficult for us to ensure that our distributors and manufacturer's representatives consistently act in accordance with the standards we set for them. To the extent any of our end-customers have negative experiences with any of our distributors or manufacturer's representatives, it could reflect poorly on us and damage our reputation, thereby negatively impacting our financial results.

We plan to engage in acquisitions and joint ventures, and may encounter unexpected difficulties identifying, pricing or integrating those businesses.

We seek to grow, in part, through strategic acquisitions that are intended to complement or expand our business, and expect to continue to do so in the future. The success of this strategy will depend on our ability to identify, price, finance and complete these transactions or arrangements. Success will also depend on our ability to integrate the businesses acquired in these transactions. We may encounter unexpected difficulties in completing and integrating acquisitions with our existing operations, and in managing strategic investments. Furthermore, we may not realize the degree, or timing, of benefits we anticipated when we first entered into a transaction. Any of the foregoing could adversely affect our business and results of operations.

We may be unsuccessful at generating internal growth.

Our ability to generate internal growth will be affected by, among other factors, our ability to attract new customers, increase the number or size of orders received by existing customers, hire and retain employees and increase volume utilizing our existing facilities. In addition, our customers may reduce the number or size of their orders. Many of the factors affecting our ability to generate internal growth may be beyond our control, and we cannot be certain that our strategies will be successful or that we will be able to generate cash flow sufficient to fund our operations and to support internal growth. If we are unsuccessful, we may not be able to achieve internal growth, expand our operations or grow our business.

The departure of key personnel could disrupt our business.

We depend on the continued efforts of Nathan J. Mazurek, our principal executive officer, and other senior management. We cannot be certain that any of these individuals will continue in their capacities for any particular period of time. The loss of key personnel, or the inability to hire and retain qualified employees, could negatively impact our ability to manage our business.

Our business requires skilled labor, and we may be unable to attract and retain qualified employees.

Our ability to maintain our productivity and profitability will be limited by our ability to employ, train and retain skilled personnel necessary to meet our requirements. We may experience shortages of qualified personnel. We cannot be certain that we will be able to maintain an adequate skilled labor force necessary to operate efficiently and to support our growth strategy or that our labor expenses will not increase as a result of a shortage in the supply of skilled personnel. Labor shortages or increased labor costs could impair our ability to maintain our business or grow our revenues, and may adversely impact our profitability.

Our business operations are dependent upon our ability to engage in successful collective bargaining with our unionized workforce.

Approximately 75% of our workforce is unionized. Our current collective bargaining agreement with our unionized workforce in Canada expires in May 2015. We have a similar agreement our unionized workforce in Reynosa, Mexico that has an indefinite term, subject to annual review and negotiation of key provisions. If we are unable to renew our agreements regarding the terms of these collective bargaining agreements, or if additional segments of our workforce become unionized, we may be subject to work interruptions or stoppages. Strikes or labor disputes with our employees may adversely affect our ability to conduct our business.

We carry insurance against many potential liabilities, and our risk management activities may leave us exposed to unidentified or unanticipated risks.

Although we maintain insurance policies with respect to our related exposures, these policies contain deductibles and limits of coverage. We estimate our liabilities for known claims and unpaid claims and expenses based on information available as well as projections for claims incurred but not reported. However, insurance liabilities are difficult to estimate due to various factors. If any of our insurance policies or programs are not effective in mitigating our risks, we may incur losses that are not covered by our insurance policies or that exceed our accruals or that exceed our coverage limits and could adversely impact our consolidated results of operations, cash flows and financial position.

Unforeseen adverse regulatory, environmental, monetary and other governmental policies could have a material adverse effect on our profitability.

We are subject to international, federal, provincial, state and local laws and regulations governing environmental matters, including emissions to air, discharge to waters and the generation and handling of waste. We are also subject to laws relating to occupational health and safety. The operation of manufacturing plants involves a high level of susceptibility in these areas, and there is no assurance that we will not incur material environmental or occupational health and safety liabilities in the future. Moreover, expectations of remediation expenses could be affected by, and potentially significant expenditures could be required to comply with, environmental regulations and health and safety laws that may be adopted or imposed in the future. Future remediation technology advances could adversely impact expectations of remediation expenses.

Future litigation could impact our financial results and condition.

Our business, results of operations and financial condition could be affected by significant future litigation or claims adverse to us. Types of potential litigation cases include product liability, contract, employment-related, labor relations, personal injury or property damage, intellectual property, stockholder claims and claims arising from any injury or damage to persons, property or the environment from hazardous substances used, generated or disposed of in the conduct of our business.

Market disruptions caused by the worldwide financial crisis could affect our ability to meet our liquidity needs at reasonable cost and our ability to meet long-term commitments, which could adversely affect our financial condition and results of operations.

We rely on our credit facilities with our lenders, amongst other avenues, to satisfy our liquidity needs. Disruptions in the credit markets or deterioration of the banking industry's financial condition, may discourage or prevent our lenders and other lenders from meeting their existing lending commitments, extending the terms of such commitments or agreeing to new commitments. Market disruptions may also limit our ability to issue debt securities in the capital markets. We can provide no assurances that our lenders or any other lenders we may have will meet their existing

commitments or that we will be able to access the credit markets in the future on terms acceptable to us or at all.

Longer term disruptions in the capital and credit markets as a result of uncertainty, reduced financing alternatives or failures of significant financial institutions could adversely affect our access to the liquidity needed for our business. Any disruption could require us to take measures to conserve cash until the market stabilizes or until alternative financing can be arranged. Such measures could include deferring capital expenditures and reducing other discretionary expenditures.

Market disruptions could cause a broad economic downturn that may lead to increased incidence of customers' failure to pay for services delivered, which could adversely affect our financial condition, results of operations and cash flow.

Capital market disruptions could result in increased costs related to variable rate debt. As a result, continuation of market disruptions could increase our interest expense and adversely impact our results of operations.

Disruption in the capital markets and its actual or perceived effects on particular businesses and the greater economy also adversely affects the value of the investments held within our pension plans. Significant declines in the value of the investments held within our pension plans may require us to increase contributions to those plans in order to meet future funding requirements if the actual asset returns do not recover these declines in value in the foreseeable future. These trends may also adversely impact our results of operations, net cash flows and financial positions, including our stockholders' equity.

Pioneer Transformers Ltd. has credit facilities with restrictive loan covenants that may impact our ability to operate our business and to pursue our business strategies, and our failure to comply with these covenants could result in an acceleration of our indebtedness.

Our credit facilities with our lenders contain certain covenants that restrict our ability to, among other things:

- effect an amalgamation, merger or consolidation with any legal entity;
- cause our subsidiaries to wind up, liquidate or dissolve their affairs;
- change the nature of our core business; or
- alter our capital structure in a manner that would be materially adverse to our lenders, undergo a change of control and make investments or advancements to affiliated or related companies without our primary lender's prior written consent.

The majority of the liquidity derived from our credit facilities is based on availability determined by a borrowing base. Specifically, the availability of credit is dependent upon our eligible receivables, inventory and certain liens. We may not be able to maintain adequate levels of eligible assets to support our required liquidity.

In addition, our credit facilities require us to meet certain financial ratios, including maintenance of a minimum debt service coverage ratio, a minimum current ratio and a maximum total debt to tangible net worth ratio. Our ability to meet these financial provisions may be affected by events beyond our control. If, as or when required, we are unable to repay, refinance or restructure our indebtedness under, or amend the covenants contained in, our credit facilities, our lenders could institute foreclosure proceedings against the assets securing borrowings under those facilities for approximately \$10.0 million, which would harm our business, financial condition and results of operations.

Jefferson Electric, Inc. may be unable to service, repay or refinance its debt and remain in compliance with its debt covenants, which could have a material adverse effect on our business.

Jefferson Electric, Inc. is highly leveraged, and its ability to repay its debt, substantially all of which is due to be repaid in October 2011, will depend on its financial and operating performance and on our ability to successfully implement our business strategy with respect to Jefferson Electric, Inc. The financial and operational performance of

Jefferson Electric, Inc. will depend on numerous factors, many of which are beyond our control, such as economic conditions and governmental regulation. We cannot be certain that Jefferson Electric, Inc.'s earnings will be sufficient to allow it to pay the principal and interest on its debt and meet its other obligations. If Jefferson Electric, Inc. does not generate enough cash flow to service its debt, it may be unable to refinance all or part of the existing debt or sell assets on terms acceptable to us, if at all. Further, failing to comply with the financial and other restrictive covenants in its loan agreement could result in an event of default, which could result in acceleration of the payments due. Because Jefferson Electric, Inc.'s debt is secured by substantially all of Jefferson Electric, Inc.'s assets, if Jefferson Electric, Inc. is unable to service, repay or refinance its debt and remain in compliance with its debt covenants, we could lose all of our investment in Jefferson Electric, Inc.

Our revenue may be adversely affected by fluctuations in currency exchange rates.

A majority of our expenditures and revenue will be spent or derived in Canada. However, we report our financial condition and results of operations in U.S. dollars. As a result, fluctuations between the U.S. dollar and the Canadian dollar will impact the amount of our revenues. For example, if the Canadian dollar appreciates relative to the U.S. dollar, the fluctuation will result in a positive impact on the revenues that we report. However, if the Canadian dollar depreciates relative to the U.S. dollar, there will be a negative impact on the revenues we report due to such fluctuation. It is possible that the impact of currency fluctuations will result in a decrease in reported sales even though we have experienced an increase in sales when reported in the Canadian dollar. Conversely, the impact of currency fluctuations may result in an increase in reported sales despite declining sales when reported in the Canadian dollar. The exchange rate from the U.S. dollar to the Canadian dollar has fluctuated substantially and may continue to do so in the future. Though we may choose to hedge our exposure to foreign currency exchange rate changes in the future, there is no guarantee such hedging, if undertaken, will be successful.

#### Risks Related to Pioneer Wind Energy Systems Inc.

The wind turbine-related assets that we acquired from AAER Inc. were acquired pursuant to Canadian court proceedings in which AAER Inc. sought protection from its creditors after it failed to raise additional capital to fund losses from its wind turbine manufacturing and marketing business. As such, no assurance can be given that we will be able to operate AAER Inc.'s former business at a profit, or that we will continue to provide for the funding needs of Pioneer Wind Energy Systems Inc. if it does not perform to our expectations.

All of our wind turbine assets were acquired from AAER Inc. in connection with the failure of AAER Inc. to raise sufficient capital to continue funding its wind turbine manufacturing and marketing business. We are seeking a qualified third party to assemble our wind turbine model for us, but have so far been unable to establish such an arrangement. While we believe this operating model for our Pioneer Wind Energy Systems Inc. business would entail less inventory risk and require less working capital than AAER Inc.'s operations, no assurance can be given that we will be able to monetize the wind turbine assets we purchased, and related products sold in the future, at a profit and succeed where AAER Inc. was unable to. In particular, we have limited experience in working with wind turbines. Moreover, the wind turbine business is highly competitive and dominated by a few much larger corporations with greater resources such as GE Energy, Siemens Wind Power A/S, Vestas Wind Systems A/S and Gamesa Corporation Tecnologica S.A.

Our wind turbine business is highly dependent on our customers receiving regulatory incentives, subsidies and third party financing.

The wind energy industry is supported in many territories through a variety of financial incentives offered by government and regulatory bodies. If the availability of such incentives was reduced or removed it would likely have an adverse effect on our business. In the U.S. such an incentive, the production tax credit (the "PTC"), is due to expire on December 31, 2012. Without the PTC, the projected return on investment in an individual wind power facility may not be sufficient to attract investment capital in the amount necessary to fund the acquisition, development and construction of wind power projects in the U.S.

While the PTC has been in effect continuously since 1992 and most recently renewed in February 2009, there can be no assurance that the PTC will be renewed beyond its current expiration date of December 31, 2012. The absence of the PTC could have a significant adverse effect on our growth potential.





The PTC will only be available for qualifying facilities that are placed in service while the PTC is in effect or through a retrospective application of the PTC. The time required to identify potential wind power projects, and to then pursue them to completion and implementation, typically ranges from 18 to 36 months, although lesser periods are possible for smaller projects. If the PTC is not extended beyond 2012, U.S. projects under development by us at that time and not completed by December 31, 2012 would not be eligible for the PTC. Accordingly, our customers might have to reduce their project spending to offset the corresponding reduction in revenues from the sale of U.S. projects.

The wind energy industry in other jurisdictions in which we expect to have a market presence may also rely to some extent on financial incentives and/or penalties designed to support the wind energy industry in that jurisdiction. Changes to, or the removal of such measures may have a significant adverse affect on our ability to compete in such jurisdictions.

Finally, in addition to regulatory incentives, some of our customers will rely on third party financing in connection with the purchase of wind turbines from us. Starting during the economic downturn of 2008 such financing became very difficult to obtain for wind power projects and remains challenging to secure. The absence of easily obtainable third party financing for wind power projects could materially reduce demand for our wind turbines.

Our customers may have difficulty in locating suitable project development sites, resulting in less demand for our wind turbines.

The development of new wind power generating projects requires the identification, acquisition and permit for viable wind resource land assets. We believe that adequate wind resource land exists and can be acquired by our current and prospective customers on a reasonable cost basis. However, competition for wind resource sites is increasing and developers in some areas have bid up site costs to levels that result in marginal project economics. This trend may increase and spread to many wind regions, limiting demand for our wind turbines. In some locations, residents and others have objected to wind projects based on noise, visual aesthetics or avian concerns.

Our business strategy includes providing equipment financing assistance to our customers, a practice with which we have no experience to date.

Inherent in our strategy to provide financing in conjunction with sales of our wind turbine equipment is credit risk associated with our customers. We intend to provide customers extended payment terms from the time of wind turbine delivery and installation. If successful selling wind turbine equipment on this basis, we anticipate that each sale will create over \$1.0 million of accounts receivable plus interest per customer per project and will provide for a payment schedule of up to, or exceeding, one year. If customers responsible for a significant amount of accounts receivable become insolvent or otherwise unable to pay for our equipment and services, or become unwilling or unable to make payments in a timely manner, our operating results and financial condition could be adversely affected. The creditworthiness of each customer and the rate of delinquencies, repossessions and net losses on customer obligations will be directly impacted by several factors, including relevant industry and economic conditions, the availability of capital, the experience and expertise of the customer's management team, the sustained value of the underlying collateral and the overall performance of the customer's power project. In the event of delinquencies that might cause us to seek to take possession of our collateral, there can be no assurance that we will be able to sell such collateral at a price sufficient to recover our investment.

Changes in tax laws may adversely affect our wind turbine business.

When the U.S. Congress renewed the PTC in 2004, it amended certain provisions of the Internal Revenue Code in a manner that resulted in wind energy property no longer qualifying as five-year depreciation property. The American Wind Energy Association believed that disqualifying wind energy property from using the 5-year depreciation

provision was an unintended consequence caused by obscure cross-references in the Internal Revenue Code of which Congress was unaware, and Congress restored the availability of accelerated 5-year depreciation as part of the Energy Policy Act of 2005, which also extended the PTC. There can be no assurance, however, that future changes in U.S. tax laws will not require wind energy property to be depreciated over a longer period of time. Such changes could force us to modify our pricing and could lead to a material adverse effect on our business.

## Risks Relating to Our Common Stock

Our stock price may be volatile, which could result in substantial losses for investors.

The market price of our common stock is highly volatile and could fluctuate widely in response to various factors, many of which are beyond our control, including the following:

- technological innovations or new products and services by us or our competitors;
  - additions or departures of key personnel;
- sales of our common stock, including management shares;
- limited availability of freely-tradable “unrestricted” shares of our common stock to satisfy purchase orders and demand;
  - our ability to execute our business plan;
  - operating results that fall below expectations;
  - loss of any strategic relationship;
  - industry developments;
  - economic and other external factors; and
  - period-to-period fluctuations in our financial results.

In addition, the securities markets have from time to time experienced significant price and volume fluctuations that are unrelated to the operating performance of particular companies. These market fluctuations may also significantly affect the market price of our common stock.

There is, at present, only a limited market for our common stock and we cannot ensure investors that an active market for our common stock will ever develop or be sustained.

There is, at present, only a limited trading market for our common stock. The price at which our common stock may be sold is very unpredictable because there are very few trades in our common stock. Because our common stock is so thinly traded, a large block of shares traded can lead to a dramatic fluctuation in the share price. In addition, our common stock currently trades on the OTC Bulletin Board, which generally lacks the liquidity, research coverage and institutional investor following of a national stock exchange like the NYSE Amex Equities, the New York Stock Exchange or the Nasdaq Stock Market. While we intend to list our common stock on a national stock exchange once we satisfy the initial listing standards for such an exchange, we currently do not, and may not ever, satisfy such initial listing standards. Furthermore, in order for us to satisfy these initial listing standards, we may be required to effectuate a reverse stock split or potentially dilutive offering. Should we nonetheless fail to satisfy the initial listing standards for a national stock exchange or should our common stock be otherwise rejected for listing and remain on the OTC Bulletin Board or be suspended from the OTC Bulletin Board, the trading price of our common stock could suffer, the trading market for our common stock may be less liquid and our common stock price may be subject to increased volatility.

Substantial sales of our common stock, or the perception that such sales are likely to occur, could cause the price of our common stock to decline.

Sales of a significant number of shares of our common stock in the public market could harm the market price of our common stock and make it more difficult for us to raise funds through future offerings of common stock.

In addition, if our stockholders sell substantial amounts of our common stock in the public market, or upon the expiration of any statutory holding period under Rule 144, upon expiration of lock-up periods applicable to outstanding shares, or issued upon the exercise of outstanding options or warrants, it could create a circumstance

commonly referred to as an “overhang” and in anticipation of which the market price of our common stock could fall. The existence of an overhang, whether or not sales have occurred or are occurring, could also make it more difficult for us to raise additional financing through the sale of equity or equity-related securities in the future at a time and price that we deem reasonable or appropriate.

We do not expect to pay dividends in the future. As a result, any return on investment may be limited to the value of our common stock.

We do not anticipate paying cash dividends on our common stock in the foreseeable future. The payment of dividends on our common stock will depend on our earnings, financial condition and other business and economic factors as our board of directors may consider relevant. If we do not pay dividends, our common stock may be less valuable because a return on your investment will only occur if our stock price appreciates.

#### Risks Relating to Our Organization

Our certificate of incorporation authorizes our board to create new series of preferred stock without further approval by our stockholders, which could adversely affect the rights of the holders of our common stock.

Our board of directors has the authority to fix and determine the relative rights and preferences of preferred stock. Our board of directors also has the authority to issue preferred stock without further stockholder approval. As a result, our board of directors could authorize the issuance of a series of preferred stock that would grant to holders the preferred right to our assets upon liquidation, the right to receive dividend payments before dividends are distributed to the holders of common stock and the right to the redemption of the shares, together with a premium, prior to the redemption of our common stock. In addition, our board of directors could authorize the issuance of a series of preferred stock that has greater voting power than our common stock or that is convertible into our common stock, which could decrease the relative voting power of our common stock or result in dilution to our existing stockholders.

Your ability to influence corporate decisions may be limited because Provident Pioneer Partners, L.P. owns a controlling percentage of our common stock.

Provident Pioneer Partners, L.P., which is controlled by Nathan J. Mazurek, chief executive officer and chairman of the board of directors, beneficially owns approximately 78% of our outstanding common stock. As a result of this stock ownership, Provident Pioneer Partners, L.P. and Mr. Mazurek can control all matters submitted to our stockholders for approval, including the election of directors and approval of any merger, consolidation or sale of all or substantially all of our assets. This concentration of voting power could delay or prevent an acquisition of our company on terms that other stockholders may desire. In addition, as the interests of Provident Pioneer Partners, L.P. and our minority stockholders may not always be the same, this large concentration of voting power may lead to stockholder votes that are inconsistent with the best interests of our minority stockholders or the best interest of us as a whole.

We are subject to financial reporting and other requirements for which our accounting, internal audit and other management systems and resources may not be adequately prepared.

On December 2, 2009, we became subject to reporting and other obligations under the Securities Exchange Act of 1934, as amended, including the requirements of Section 404 of the Sarbanes-Oxley Act. Section 404 requires us to conduct an annual management assessment of the effectiveness of our internal controls over financial reporting. These reporting and other obligations place significant demands on our management, administrative, operational, internal audit and accounting resources. We anticipate that we may need to upgrade our systems; implement additional financial and management controls, reporting systems and procedures; implement an internal audit function; and hire additional accounting, internal audit and finance staff. If we are unable to accomplish these objectives in a timely and effective fashion, our ability to comply with our financial reporting requirements and other rules that apply to reporting companies could be impaired. Any failure to maintain effective internal controls could have a material adverse effect on our business, operating results and stock price.

Because we became public by means of a reverse merger, we may not be able to attract the attention of major brokerage firms.

There may be risks associated with us becoming public through a “reverse merger.” Securities analysts of major brokerage firms may not provide coverage of us since there is no incentive to brokerage firms to recommend the purchase of our common stock. No assurance can be given that brokerage firms will, in the future, want to conduct any secondary offerings on our behalf.

## ITEM 1B. UNRESOLVED STAFF COMMENTS.

Not applicable.

## ITEM 2. PROPERTIES.

We have two manufacturing facilities, one located in Granby, Quebec, Canada, and the other located in Reynosa, Mexico. Our Granby facility was built in 1962 and consists of approximately 44,000 square feet. The facility sits on approximately 25 acres in the town of Granby which is located approximately 40 miles east of Montreal. We own both the facility and the land through our wholly-owned subsidiary, Barnard Granby Realty, Inc. Our Reynosa facility consists of approximately 52,000 square feet of manufacturing and office space and is leased for approximately \$24,000 per month under a lease that expires in 2013. The lease includes an option to renew for an additional five years at the same lease rate. We also lease a 22,000 square foot centralized logistics facility in Pharr, Texas for approximately \$12,000 per month under a lease that expires in 2013.

We believe our manufacturing and distribution facilities are well maintained and in proper condition to operate at current levels. In order to increase the manufacturing capacity of our Granby facility, in February 2011 we completed a plan that expanded its size by approximately 6,000 square feet by building onto land that we already owned.

We lease office space for the engineering and marketing activities of our Pioneer Transformers Ltd. subsidiary in Mississauga near Toronto, Ontario, Canada. Our monthly rent is \$3,200 and the lease expires in 2016. Our Jefferson Electric, Inc. subsidiary leases office space for its management, sales, marketing, design engineering and administrative functions in Franklin, Wisconsin for a monthly rent of approximately \$4,300 under a lease that expires in December 2013. We also pay approximately \$3,400 per month to lease our executive management and sales office in Fort Lee, New Jersey.

## ITEM 3. LEGAL PROCEEDINGS.

We are not presently a party to any material legal proceedings nor are we aware of any such threatened or pending litigation.

## ITEM 4. REMOVED AND RESERVED.

## PART II

## ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.

Our common stock was originally approved for quotation on the OTC Bulletin Board on February 2, 2009 and since January 7, 2010, our common stock has been quoted under the trading symbol PPSI.OB. Prior to January 7, 2010, our common stock did not trade regularly. The following table sets forth the high and low bid prices for our common stock for the periods indicated, as reported by the OTC Bulletin Board. The quotations reflect inter-dealer prices, without retail mark-up, mark-down or commission, and may not represent actual transactions.

Fiscal Year 2010	High	Low
First Quarter	\$3.40	\$1.50
Second Quarter	\$3.09	\$2.65
Third Quarter	\$3.05	\$2.00
Fourth Quarter	\$3.00	\$2.65





The last reported sales price of our common stock on the OTC Bulletin Board on March 24, 2011, was \$2.40 per share. As of March 24, 2011, there were 24 holders of record of our common stock.

In the past, we have not declared or paid cash dividends on our common stock, and we do not intend to pay any cash dividends on our common stock. Rather, we intend to retain future earnings (if any) to fund the operation and expansion of our business and for general corporate purposes. Subject to legal and contractual limits, our board of directors will make any decision as to whether to pay dividends in the future. Notwithstanding the foregoing, Pioneer Transformers Ltd., our wholly-owned subsidiary, prior to our share exchange on December 2, 2009, paid cash dividends to Provident Pioneer Partners, L.P., its sole stockholder at the time, of \$2.7 million during 2009.

ITEM 6. SELECTED FINANCIAL DATA.

Not applicable.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

Overview and Recent Events

We are an owner and operator of electrical equipment and service businesses headquartered in Fort Lee, New Jersey. Our subsidiaries provide a range of products and services to the electrical transmission and distribution industry. Our focus is on the electric utility, industrial, commercial and wind energy market segments and our customers are primarily located in North America.

On December 2, 2009, we completed a share exchange pursuant to which we acquired all of the issued and outstanding capital stock of Pioneer Transformers Ltd. in exchange for a controlling interest in us and our officers and directors were replaced by designees of Pioneer Transformers Ltd.. In addition, following the share exchange, we discontinued development of our former business and succeeded to the business of Pioneer Transformers Ltd. As a result, the share exchange was accounted for as a reverse business combination in which Pioneer Transformers Ltd., rather than us, was deemed to be the accounting acquirer. Accordingly, the historical financial statements presented and the discussion of financial condition and results of operations herein are those of Pioneer Transformers Ltd. and do not include historical financial results of our former business.

On April 30, 2010, we completed the acquisition of Jefferson Electric, Inc., a Wisconsin-based manufacturer and supplier of dry-type transformers. In addition, through transactions completed in June and August 2010 we acquired substantially all the assets and the capital stock of AAER Inc. to form Pioneer Wind Energy Systems Inc., a manufacturer of wind turbines with generation capacities exceeding one MW based in Quebec, Canada.

Accounting for the Share Exchange

The share exchange on December 2, 2009 was accounted for as a recapitalization. Pioneer Transformers Ltd. was the acquirer for accounting purposes and we were the acquired company. Accordingly, the historical financial statements presented and the discussion of financial condition and results of operations herein are those of Pioneer Transformers Ltd., retroactively restated for, and giving effect to, the number of shares received in the share exchange, and do not include the historical financial results of our former business. The accumulated earnings of Pioneer Transformers Ltd. were also carried forward after the share exchange and earnings per share have been retroactively restated to give effect to the recapitalization for all periods presented. Therefore, results of operations reported for periods prior to the share exchange are those of Pioneer Transformers Ltd.

### Foreign Currency Exchange Rates

In connection with our share exchange with Pioneer Transformers Ltd. and the discontinuation of our former business, we elected to report our financial results in U.S. dollars. Accordingly, all comparative financial information contained in this discussion has been recast from Canadian dollars to U.S. dollars. We also elected to report our financial results in accordance with generally accepted accounting principles in the U.S. to improve the comparability of our financial information with our peer companies.

Although we have elected to report our results in accordance with generally accepted accounting principles in the U.S. and in U.S. dollars, our largest operating subsidiary, Pioneer Transformers Ltd., is a Canadian entity and its functional currency is the Canadian dollar. As such, the financial position, results of operations, cash flows and equity of Pioneer Transformers Ltd. are initially consolidated in Canadian dollars. The subsidiary's assets and liabilities are then translated from Canadian dollars to U.S. dollars by applying the foreign currency exchange rate in effect at the balance sheet date, while the results of its operations and cash flows are translated to U.S. dollars by applying the average foreign currency exchange rate in effect during the reporting period. The resulting translation adjustments are included in other comprehensive income or loss.

The financial position and operating results of Pioneer Transformers Ltd. have been translated to U.S. dollars by applying the following exchange rates, expressed as the number of Canadian dollars to one U.S. dollar for each period reported:

Quarter Ended	2010			2009		
	Consolidated Balance Sheet End of Period	Consolidated Statements of Earnings and Comprehensive Income		Consolidated Balance Sheet End of Period	Consolidated Statements of Earnings and Comprehensive Income	
		Period Average	Cumulative Average		Period Average	Cumulative Average
March 31	\$1.0158	\$1.0409	\$1.0409	\$1.2613	\$1.2453	\$1.2453
June 30	\$1.0646	\$1.0276	\$1.0343	\$1.1630	\$1.1672	\$1.2062
September 30	\$1.0290	\$1.0391	\$1.0359	\$1.0707	\$1.0974	\$1.1700
December 31	\$0.9946	\$1.0128	\$1.0301	\$1.0510	\$1.0563	\$1.1415

#### Critical Accounting Policies

**Use of Estimates.** The preparation of financial statements in accordance with generally accepted accounting principles in the U.S. requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The financial statements include estimates based on currently available information and our judgment as to the outcome of future conditions and circumstances. Significant estimates in these financial statements include pension expense, inventory provisions, useful lives and impairment of long-lived assets, determination of fair values of warrants and allowance for doubtful accounts. Changes in the status of certain facts or circumstances could result in material changes to the estimates used in the preparation of the financial statements and actual results could differ from the estimates and assumptions.

**Revenue Recognition Policies.** Revenue is recognized when (1) persuasive evidence of an arrangement exists, (2) delivery occurs, (3) the sales price is fixed or determinable, (4) collectability is reasonably assured and (5) customer acceptance criteria, if any, have been successfully demonstrated. Revenue is recognized on the sale of goods, when the significant risks and rewards of ownership have been transferred to the buyer upon delivery, provided that we maintain neither managerial involvement to the degree usually associated with ownership, nor effective control over the goods sold. There are no further obligations on our part subsequent to revenue recognition, except when customers have the right of return or when we warrant the product. We record a provision for future returns, based on historical experience at the time of shipment of products to customers. We warrant some of our products against defects in design, materials and workmanship for periods ranging from one to three years depending on the model. We record a provision for estimated future warranty costs based on the historical relationship of warranty claims to sales at the

time of shipment of products to customers. We periodically review the adequacy of our product warranties and adjust, if necessary, the warranty percentage and accrued warranty reserve for actual experience.

## Changes in Accounting Principles

No significant changes in accounting principles were adopted during 2009 and 2010, except for the following:

**Fair Value Measurements.** In January 2010, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2010-06, “Fair Value Measurements and Disclosures (Topic 820)” (“ASU 2010-06”). ASU 2010-06 requires reporting entities to make more robust disclosures about (1) the different classes of assets and liabilities measured at fair value, (2) the valuation techniques and inputs used, (3) the activity in Level 3 fair value measurements, including information on purchases, sales, issuances, and settlements on a gross basis, and (4) the transfers between Levels 1, 2, and 3. ASU 2010-06 is effective for fiscal years beginning on or after December 15, 2009, except for the disclosure regarding Level 3 activity, which is effective for fiscal years beginning after December 15, 2010. The adoption of ASU 2010-06 for Levels 1 and 2 did not have a material impact on our consolidated financial statements, and we do not expect the adoption of the standard for Level 3 to have a material impact on our consolidated financial statements.

## Results of Operations

### Year Ended December 31, 2010 Compared to the Year Ended December 31, 2009

**Revenue.** For the year ended December 31, 2010, consolidated revenues increased 16.3% to \$47.2 million, up from \$40.6 million during the year ended December 31, 2009. The acquisition of Jefferson Electric, Inc. on April 30, 2010 contributed approximately \$13.2 million to our revenue during 2010, versus no contribution in 2009. Revenue from Pioneer Transformers Ltd. decreased by approximately \$6.5 million, or 16.1%, during the year ended December 31, 2010, as compared to 2009. This decline was due to lower unit volume, attributed primarily to weakness in demand from industrial customers, as compared to the prior year. Our wind energy business, which was established in June 2010, made no contribution to our total revenue in 2010 and 2009.

**Gross Margin.** For the year ended December 31, 2010, our gross margin percentage decreased to 24.6% of revenues, compared to 29.2% during the year ended December 31, 2009. This decrease was attributable primarily to less favorable product mix and lower unit volume experienced by our Pioneer Transformers Ltd. business during the year ended December 31, 2010, as compared to the prior year. In addition, our new Jefferson Electric, Inc. subsidiary generally achieves a lower gross margin percentage as compared to Pioneer Transformers Ltd. On a consolidated basis, approximately 3.1% of the gross margin decline was attributable to Pioneer Transformers Ltd. and 1.5% to Jefferson Electric, Inc.

**Selling, General and Administrative Expense.** For the year ended December 31, 2010, selling, general and administrative expense increased by approximately \$3.8 million, or 90.7%, to approximately \$8.0 million, as compared to \$4.2 million during the year ended December 31, 2009. Approximately \$1.5 million of the increase was due to higher corporate expenses mostly incurred in connection with being a public company, including \$0.4 million for non-cash costs associated with the issuance of employee and director stock options and the issuance of stock and warrants to our investor relations firm. The remaining \$2.4 million net increase is attributable to the inclusion of Jefferson Electric, Inc. (\$2.4 million) and Pioneer Wind Energy Systems Inc. (\$0.4 million) in our consolidated results during the year ended December 31, 2010, offset by reduced selling, general and administrative expense at Pioneer Transformers Ltd. (\$0.5 million).

**Foreign Exchange (Gain) Loss.** Most of our consolidated operating revenues are denominated in Canadian dollars, principally via our Pioneer Transformers Ltd. operating subsidiary, and a material percentage of our expenses are denominated and disbursed in U.S. dollars. We have not historically engaged in currency hedging activities. Fluctuations in foreign currency exchange rates between the time we initiate and then settle transactions with our

customers and suppliers can have an impact on our operating results. For the year ended December 31, 2010, we recorded a gain of \$0.1 million due to currency fluctuations, compared to a gain of approximately \$0.3 million during the year ended December 31, 2009.

**Interest and Bank Charges.** For the year ended December 31, 2010, interest and bank charges were approximately \$0.2 million, as compared to \$0.3 million for the year ended December 31, 2009. The decrease in interest expense was due to the reversal of approximately \$0.1 million of interest accrued that was related to a tax liability previously recorded by Pioneer Transformers Ltd. In the fourth quarter of 2010, we agreed to a settlement with the Canadian tax authorities whereby no interest charges will be imposed and we are instead expecting to receive a significant refund. Without the effect of reversing this accrued interest, our interest expense would have been stable during 2010 as compared to 2009. We had higher average borrowings as a result of the assumption of our Jefferson Electric, Inc. subsidiary's debt in 2010. The resulting increase in interest expense was offset by a decrease at Pioneer Transformers Ltd. which had significantly lower average borrowings during 2010 as compared to 2009, primarily due to the repayment of approximately \$4.4 million of its bank indebtedness in December 2009.

**Other Expense (Income).** For the year ended December 31, 2010, our other expense of \$0.9 million consisted of professional fees and restructuring costs related to our acquisitions of Jefferson Electric, Inc., select assets from AAER Inc. and the acquisition of AAER Inc. Approximately 50% of these costs were transaction-related fees and expenses. The remainder of other expense (income) was incurred in connection with restructuring AAER Inc.'s business following the acquisition.

**Gain on Bargain Purchase.** On June 7, 2010, we acquired most of the inventory and substantially all of the capital assets, intangible assets and intellectual property of AAER Inc. for approximately \$0.4 million in cash. In connection with the transaction, the fair value of the inventory and capital assets acquired, net of deferred tax liabilities, was determined to be approximately \$1.5 million. In August 2010, we sold a portion of the AAER Inc. assets that were acquired in June at a price exceeding their initially recorded fair value, resulting in an additional gain on sale of approximately \$0.1 million. Accordingly, we recognized a gain on bargain purchase of approximately \$1.1 million, representing the excess of the fair value of net assets acquired over the consideration paid. In the fourth quarter of 2010, we determined that certain of the capital assets we acquired were impaired by an amount of \$0.4 million, resulting in a reduction to the previously recognized gain on bargain purchase to \$0.7 million.

**Provision for Income Taxes.** Our provision for income taxes reflects an effective tax rate on earnings before income taxes of 10.0% in 2010 compared to 32.7% in 2009. The decrease in the effective tax rate resulted primarily from a settlement we reached with the Canadian tax authority resulting in a \$0.9 million refund of taxes previously paid by us, to be received during 2011.

**Net Earnings.** We generated net earnings of \$2.9 million for the year ended December 31, 2010, down 42.4% from approximately \$5.1 million during the year ended December 31, 2009. Our net earnings benefited from the acquisition of Jefferson Electric, Inc. during 2010, but were negatively impacted by weaker sales and earnings from our Pioneer Transformers Ltd. subsidiary and significantly higher selling, general and administrative expenses during the year ended December 31, 2010, as compared to the year ended December 31, 2009. Earnings per basic and diluted share was \$0.10 for the year ended December 31, 2010, as compared to \$0.22 per basic and diluted share for the year ended December 31, 2009. There were 6.4 million additional weighted average diluted shares outstanding during the year ended December 31, 2010, as compared to the year ended December 31, 2009, an amount which reflects the completion of our share exchange and private placement transactions during the fourth quarter of 2009, as well as the issuance of our common shares in conjunction with the acquisition of Jefferson Electric, Inc.

**Backlog.** Our order backlog at December 31, 2010 was \$18.7 million, up 13.3% from \$16.5 million at December 31, 2009. The \$2.2 million increase in our backlog is evenly split between new orders received by Pioneer Transformers Ltd. and the inclusion of backlog from Jefferson Electric, Inc. in the 2010 period. Our backlog is based on orders expected to be delivered in the future, most of which is expected to occur during 2011. New orders placed during the year ended December 31, 2010 totaled \$47.7 million, an increase of 25.7% compared to new orders of \$38.0 million that were placed during the year ended December 31, 2009. The large percentage increase in orders on a

year-over-year basis is primarily due to the inclusion of Jefferson Electric, Inc. in our 2010 results.



## Liquidity and Capital Resources

General. At December 31, 2010, we had cash and cash equivalents of approximately \$0.5 million and total debt, including capital lease obligations, of \$6.1 million. We have historically met our cash needs through a combination of cash flows from operating activities and bank borrowings. Our cash requirements are generally for operating activities, debt repayment and capital improvements. We believe that working capital, borrowing capacity available under our credit facilities and funds generated from operations should be sufficient to finance our cash requirements for anticipated operating activities, capital improvements and principal repayments of debt through at least the next 12 months.

Our operating activities generated cash flow of approximately \$3.3 million during the year ended December 31, 2010, compared to cash flow from operating activities of \$4.3 million during the year ended December 31, 2009. The principal elements of cash flow from operating activities during 2010 were net earnings of \$2.9 million, offset by \$0.7 million of non-cash income related to the gain on bargain purchase associated with the AAER Inc. transaction. Cash flow from operating activities during 2010 also increased by approximately \$0.2 million from changes in our operating working capital and \$0.9 million from the effect of non-cash expenses included in our net earnings.

Cash used in investing activities during the year ended December 31, 2010 was approximately \$2.3 million, as compared to \$0.3 million during the year ended December 31, 2009. During the year ended December 31, 2010, we used approximately \$1.7 million for capital expenditures, principally for the expansion of our manufacturing facility located in Quebec, Canada. In 2010, we used another \$0.8 million for acquisitions. Offsetting our cash used in investing activities was \$0.2 million of net proceeds we received from the sale of certain capital assets we had previously purchased from AAER Inc. During the year ended December 31, 2009, our cash used in investing activities consisted entirely of additions to property and equipment at Pioneer Transformers Ltd.

Cash used by our financing activities was approximately \$2.0 million during the year ended December 31, 2010, compared to \$2.5 million during the year ended December 31, 2009. Our primary use of cash for financing activities during the year ended December 31, 2010 was for debt repayment of \$1.9 million, together with approximately \$0.1 million for equity financing transaction costs. During the year ended December 31, 2009, we raised gross proceeds of \$5.0 million from an issuance of common stock to investors. Our primary uses of cash for financing activities in 2009 consisted of \$4.5 million in debt repayments, \$2.7 million to make dividend payments to Provident Pioneer Partners, L.P., previously the sole stockholder of Pioneer Transformers Ltd., and \$0.2 million for equity financing transaction costs.

As of December 31, 2010, our current assets were 1.1 times our current liabilities. Current assets increased by \$2.1 million and current liabilities increased by \$9.0 million during the year ended December 31, 2010. These increases were primarily due to the acquisition of Jefferson Electric, Inc. during the year and the inclusion of its current maturities of debt and accounts payable and accrued liabilities. As a result, our net working capital balance decreased by \$6.9 million to \$2.0 million during the year ended December 31, 2010, as compared to \$9.0 million of net working capital as of December 31, 2009.

Credit Facilities. In October 2009, our Pioneer Transformers Ltd. subsidiary entered into a financing arrangement with a Canadian bank that replaced its previous credit facility. Expressed in approximate U.S. dollars, the \$10.0 million credit agreement consists of a \$7.7 million demand revolving credit facility, a \$1.8 million term loan facility and a \$0.5 million foreign exchange settlement risk facility. The credit facilities are secured by a first-ranking lien in the amount of approximately \$10.0 million on all of our assets, as well as a collateral mortgage of \$10.0 million on our land and buildings.

The credit facilities require Pioneer Transformers Ltd. to comply with various financial covenants, including maintaining a minimum debt service coverage ratio of 1.25, a minimum current ratio of 1.20 and a maximum total debt to tangible net worth ratio of 2.50. The credit facilities also restrict the ability of Pioneer Transformers Ltd. to make investments or advancements to affiliated or related companies without the lender's prior written consent. The demand revolving credit facility is subject to margin criteria and borrowings bear interest at the bank's prime rate plus 0.75% per annum on amounts borrowed in Canadian dollars, or the U.S. base rate plus 0.75% per annum on amounts borrowed in U.S. dollars. Borrowings under the term loan facility bear interest at the bank's prime rate plus 1.0% per annum. As of December 31, 2010, we had no borrowings outstanding under the credit facility and we were in compliance with its financial covenant requirements.

Our Jefferson Electric, Inc. subsidiary has a bank loan agreement with a U.S. bank that includes a revolving credit facility with a borrowing base of \$5.0 million and a term credit facility. Monthly payments of accrued interest must be made under the revolving credit facility and monthly payments of principal and accrued interest must be made under the term credit facility, with a final payment of all outstanding amounts due on October 31, 2011. Borrowings under the bank loan agreement are collateralized by substantially all the assets of Jefferson Electric, Inc. and are guaranteed by its Mexican subsidiary. In addition, an officer of Jefferson Electric, Inc. is a guarantor under the bank loan agreement and has provided additional collateral to the bank in the form of our common stock and a warrant to purchase our shares of common stock held by him.

The bank loan agreement requires Jefferson Electric, Inc. to comply with certain financial covenants, including a requirement to exceed minimum quarterly targets for tangible net worth, as defined, and maintain a minimum debt service coverage ratio. The bank loan agreement also restricts Jefferson Electric, Inc.'s ability to pay dividends or make distributions, advances or other transfers of assets. The interest rate under the revolving credit facility is equal to the greater of the bank's reference rate (currently 3.25% annually) or 6.5% annually. The interest rate under the term credit facility is 7.27% annually. As of December 31, 2010, our Jefferson Electric, Inc. subsidiary had approximately \$2.8 million outstanding under the revolving credit facility and approximately \$3.0 million outstanding under the term credit facility and was in compliance with its financial covenant requirements.

**Equipment Loans and Capital Lease Obligations.** As of December 31, 2010, we had equipment loans and capital lease obligations with an aggregate principal amount outstanding of approximately \$31,000, as compared to approximately \$134,000 outstanding as of December 31, 2009. These equipment loans and capital lease obligations bear interest at rates varying from 0.0% to 18.8% and are repayable in monthly installments. We anticipate that these equipment loans will be paid off by the end of December 2013.

**Loans from Stockholders.** Certain limited partners of Provident Pioneer Partners, L.P., our controlling stockholder, previously advanced to us an aggregate of \$150,000 at an interest rate of 12% per annum with no specific terms of repayment. During the year ended December 31, 2010, the aggregate principal amount of these advances were repaid in full.

**Capital Expenditures.** In September 2009, we commenced an expansion of our Pioneer Transformers Ltd. plant that increased our manufacturing facilities and office space by approximately 6,000 square feet. The capital budget for the project was approximately \$2.0 million, including machinery and equipment, and the project was substantially complete by December 2010. The cost of the project was funded through cash flow from operations. We have no major future capital projects planned, or significant replacement spending anticipated, during 2011.

### Factors That May Affect Future Operations

We believe that our future operating results will continue to be subject to quarterly variations based upon a wide variety of factors, including the cyclical nature of the electrical transformer and wind energy products industries and the markets for our products and services. Our operating results could also be impacted by a weakening of the Canadian dollar, changing customer requirements and exposure to fluctuations in prices of important raw supplies, such as copper, steel and aluminum. We attempt to minimize these increases through the inclusion of escalation clauses with respect to commodities in our customer contracts. In addition to these measures, we attempt to recover other cost increases through improvements to our manufacturing efficiency and through increases in prices where competitively feasible. Lastly, other economic conditions we cannot foresee may affect customer demand. We predominately sell to customers in the utility, industrial production and commercial construction markets. Accordingly, changes in the condition of any of our customers may have a greater impact than if our sales were more evenly distributed between different end markets.

### Off Balance Sheet Transactions and Related Matters

We have no off-balance sheet transactions, arrangements, obligations (including contingent obligations), or other relationships with unconsolidated entities or other persons that have, or may have, a material effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

### Recent Accounting Pronouncements

In December 2010, the FASB issued Update No. 2010-28, “Intangibles—Goodwill and Other (Topic 350): When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts” (“ASU 2010-28”). ASU 2010-28 affects all entities that have recognized goodwill and have one or more reporting units whose carrying amount for purposes of performing Step 1 of the goodwill impairment test is zero or negative. ASU 2010-28 modifies Step 1 so that for those reporting units, an entity is required to perform Step 2 of the goodwill impairment test if it is more likely than not that a goodwill impairment exists. In determining whether it is more likely than not that a goodwill impairment exists, an entity should consider whether there are any adverse qualitative factors indicating that an impairment may exist. The qualitative factors are consistent with existing guidance, which requires that goodwill of a reporting unit be tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. ASU 2010-28 is effective for fiscal years, and interim periods within those years, beginning after December 15, 2010. Early adoption is not permitted. We are currently evaluating the impact of ASU 2010-28 on our consolidated financial statements.

In December 2010, the FASB issued Update No. 2010-29, “Business Combinations (Topic 805): Disclosure of Supplementary Pro Forma Information for Business Combinations” (“ASU 2010-29”) The objective of ASU 2010-29 is to address diversity in practice about the interpretation of the pro forma revenue and earnings disclosure requirements for business combinations. ASU 2010-29 specifies that if a public entity presents comparative financial statements, the entity should disclose revenue and earnings of the combined entity as though the business combination(s) that occurred during the current year had occurred as of the beginning of the comparable prior annual reporting period only. The amendments also expand the supplemental pro forma disclosures to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination included in the reported pro forma revenue and earnings. The amendments affect any public entity as defined by Topic 805 that enters into business combinations that are material on an individual or aggregate basis. ASU 2010-29 is effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period on or after December 15, 2010. Early adoption is permitted. We are currently evaluating the impact

of ASU 2010-29 on our consolidated financial statements.

In April 2010, the FASB issued Update No. 2010-13, "Compensation—Stock Compensation (Topic 718): Effect of Denominating the Exercise Price of a Share-Based Payment Award in the Currency of the Market in Which the Underlying Equity Security Trades" ("ASU 2010-13"). This amendment clarifies that a share-based payment award with an exercise price denominated in the currency of a market in which a substantial portion of the entity's equity securities trades shall not be considered to contain a market, performance, or service condition. Therefore, such an award is not to be classified as a liability if it otherwise qualifies as equity classification. ASU 2010-13 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2010. Earlier application is permitted. We are currently evaluating the impact of ASU 2010-13 on our consolidated financial statements.

In April 2010, the FASB issued Update No. 2010-17, "Revenue Recognition—Milestone Method (Topic 605): Milestone Method of Revenue Recognition" ("ASU 2010-17"). ASU 2010-17 provides guidance on defining a milestone under Topic 605 and determining when it may be appropriate to apply the milestone method of revenue recognition for research or development transactions. Consideration that is contingent on achievement of a milestone in its entirety may be recognized as revenue in the period in which the milestone is achieved only if the milestone is judged to meet certain criteria to be considered substantive. Milestones should be considered substantive in their entirety and may not be bifurcated. An arrangement may contain both substantive and non-substantive milestones that should be evaluated individually. ASU 2010-17 is effective on a prospective basis for milestones achieved in fiscal years, and interim periods within those years, beginning on or after June 15, 2010. Early adoption is permitted. We are currently evaluating the impact of ASU 2010-17 on our consolidated financial statements.

In October 2009, the FASB issued Update No. 2009-13, "Revenue Recognition (Topic 605)—Multiple-Deliverable Revenue Arrangements a consensus of the FASB Emerging Issues Task Force" ("ASU 2009-13"). ASU 2009-13 provides amendments to the criteria in ASC 605-25 for separating consideration in multiple-deliverable arrangements. As a result of those amendments, multiple-deliverable arrangements will be separated in more circumstances than under existing U.S. GAAP. ASU 2009-13: (1) establishes a selling price hierarchy for determining the selling price of a deliverable, (2) eliminates the residual method of allocation and requires that arrangement consideration be allocated at the inception of the arrangement to all deliverables using the relative selling price method, (3) requires that a vendor determine its best estimate of selling price in a manner that is consistent with that used to determine the price to sell the deliverable on a standalone basis, and (4) significantly expands the disclosures related to a vendor's multiple-deliverable revenue arrangements. ASU 2009-13 is effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. We are currently evaluating the impact of ASU 2009-13 on our consolidated financial statements.

In October 2009, the FASB issued Update No. 2009-14, "Software (Topic 985) - Certain Revenue Arrangements That Include Software Elements a consensus of the FASB Emerging Issues Task Force" ("ASU 2009-14"). ASU 2009-14 changes the accounting model for revenue arrangements that include both tangible products and software elements and provides additional guidance on how to determine which software, if any, relating to tangible product would be excluded from the scope of the software revenue guidance. In addition, ASU 2009-14 provides guidance on how a vendor should allocate arrangement consideration to deliverables in an arrangement that includes both tangible products and software. ASU 2009-14 is effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. The adoption of ASU 2009-14 is not expected to have a material effect on our financial position or results of operations.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Not applicable.



ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

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Report of Independent Registered Public Accounting Firm

To the Shareholders and Board of Directors of  
Pioneer Power Solutions, Inc.

We have audited the accompanying consolidated balance sheets of Pioneer Power Solutions, Inc. as at December 31, 2010 and 2009 and the related consolidated statements of earnings, shareholders' equity and comprehensive income and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). These standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2010 and 2009 and the results of its operations, comprehensive income and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States.

Signed by RSM Richter Chamberland LLP

Chartered Accountants

Montréal, Québec  
March 31, 2011

1CA auditor permit no 13997



PIONEER POWER SOLUTIONS, INC.  
 Consolidated Balance Sheets  
 (In thousands)

	December 31,	
	2010	2009
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	\$516	\$1,560
Accounts receivable	5,358	5,492
Inventories	7,814	6,433
Income taxes receivable	1,191	-
Deferred income taxes	245	-
Prepaid expenses and other current assets	575	103
<b>Total current assets</b>	<b>15,699</b>	<b>13,588</b>
Property, plant and equipment	5,123	987
Noncurrent deferred income taxes	1,311	20
Intangible assets	4,436	-
Goodwill	5,534	-
<b>Total assets</b>	<b>\$32,103</b>	<b>\$14,595</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current liabilities		