

# LARGE FILING SEPARATOR SHEET

CASE NUMBER: 06-1363-GA-AGG

FILE DATE: November 20, 2014

SECTION: 4 of 5

NUMBER OF PAGES: 200

DESCRIPTION OF DOCUMENT:

Renewal Application

# WORLD ENERGY SOLUTIONS, INC.

## FORM 10-Q (Quarterly Report)

Filed 05/08/14 for the Period Ending 03/31/14

|             |  |
|-------------|--|
| Address     | 100 FRONT STREET<br>WORCESTER, MA 01608            |
| Telephone   | 508-459-8100                                       |
| CIK         | 0001371781   |
| Symbol      | XWES   |
| SIC Code    | 7389 - Business Services, Not Elsewhere Classified |
| Industry    | Investment Services                                |
| Sector      | Financial  |
| Fiscal Year | 12/31  |

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

**FORM 10-Q**

- ☒ Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 For the quarterly period ended March 31, 2014; or
- ☐ Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number: 001-34289

**World Energy Solutions, Inc.**

(Exact name of registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of incorporation or organization)

**04-3474959**

(I.R.S. Employer Identification Number)

**100 Front Street**

**Worcester, Massachusetts 01608**

(Address of principal executive offices)

**508-459-8100**

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically 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 (§232.405 of this chapter) 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 whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☐

Accelerated filer ☐

Non-accelerated filer ☐

Smaller reporting company ☒

(Do not check if a smaller reporting company)

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

As of May 2, 2014, the registrant had 12,630,250 shares of common stock outstanding.

## TABLE OF CONTENTS

|  | <u>Page</u> |
|--|-------------|
| <b>PART I. Financial Information</b>   |             |
| Item 1. Financial Statements (Unaudited)   | 2           |
| Condensed Consolidated Balance Sheets as of March 31, 2014 and December 31, 2013                   | 2           |
| Condensed Consolidated Statements of Operations for the Three Months Ended March 31, 2014 and 2013 | 3           |
| Condensed Consolidated Statements of Cash Flows for the Three Months Ended March 31, 2014 and 2013 | 4           |
| Notes to Condensed Consolidated Financial Statements   | 5           |
| Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations      | 12          |
| Item 3. Quantitative and Qualitative Disclosure about Market Risk                                  | 19          |
| Item 4. Controls and Procedures  | 19          |
| <b>PART II. Other Information</b>  |             |
| Item 1. Legal Proceedings  | 21          |
| Item 1A. Risk Factors  | 21          |
| Item 2. Unregistered Sales of Equity Securities and Use of Proceeds                                | 21          |
| Item 3. Defaults Upon Senior Securities  | 22          |
| Item 4. Mine Safety Disclosures (Not applicable)   | 22          |
| Item 5. Other Information  | 22          |
| Item 6. Exhibits   | 22          |

---



**PART I  
FINANCIAL INFORMATION**

**Item 1. Financial Statements**

**WORLD ENERGY SOLUTIONS, INC.  
CONDENSED CONSOLIDATED BALANCE SHEETS**

|   | March 31,<br>2014<br>(Unaudited) | December 31,<br>2013 |
|---|----------------------------------|----------------------|
| <b>ASSETS</b>   |                                  |                      |
| Current assets:   |                                  |                      |
| Cash and cash equivalents   | \$ 2,578,970                     | \$ 1,725,136         |
| Trade accounts receivable, net  | 7,439,892                        | 7,738,141            |
| Inventory   | 365,197                          | 415,770              |
| Current portion of deferred tax asset   | 895,350                          | 901,350              |
| Prepaid expenses and other current assets   | 589,829                          | 477,406              |
| Total current assets  | 11,869,238                       | 11,257,803           |
| Property and equipment, net   | 558,052                          | 573,778              |
| Intangible assets, net  | 14,267,320                       | 15,193,965           |
| Goodwill  | 16,167,834                       | 16,167,834           |
| Deferred tax asset, net of current portion  | 7,147,984                        | 7,198,984            |
| Other assets, net   | 753,569                          | 687,098              |
| Total assets  | <u>\$ 50,763,997</u>             | <u>\$ 51,079,462</u> |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>   |                                  |                      |
| Current liabilities:  |                                  |                      |
| Accounts payable  | \$ 1,421,918                     | \$ 1,697,798         |
| Accrued commissions   | 1,597,493                        | 1,567,839            |
| Accrued compensation  | 1,545,965                        | 2,119,784            |
| Accrued contingent consideration  | 928,000                          | 1,000,000            |
| Accrued expenses and other current liabilities  | 1,318,482                        | 1,242,274            |
| Deferred revenue and customer advances  | 4,438,499                        | 3,546,380            |
| Related party subordinated notes payable  | 500,000                          | 500,000              |
| Current portion of long-term debt   | 755,165                          | 477,712              |
| Total current liabilities   | 12,505,522                       | 12,151,787           |
| Long-term debt, net of current portion  | 5,244,835                        | 5,522,288            |
| Subordinated note payable   | 4,000,000                        | 4,000,000            |
| Deferred revenue and customer advances, net of current portion  | 3,714,029                        | 3,910,035            |
| Other liabilities   | 13,764                           | 14,768               |
| Total liabilities   | 25,478,150                       | 25,598,878           |
| Commitments and contingencies   |                                  |                      |
| Stockholders' equity:   |                                  |                      |
| Preferred stock, \$0.0001 par value; 5,000,000 shares authorized, no shares issued or outstanding   |                                  |                      |
| Common stock, \$0.0001 par value; 30,000,000 shares authorized; 12,222,566 shares issued and 12,164,500 shares outstanding at March 31, 2014, and 12,178,366 shares issued and 12,120,338 shares outstanding at December 31, 2013 | 1,216                            | 1,212                |
| Additional paid-in capital  | 45,198,189                       | 44,894,961           |
| Accumulated deficit   | (19,654,025)                     | (19,156,245)         |
| Treasury stock, at cost; 58,066 shares at March 31, 2014 and 58,028 shares at December 31, 2013   | (259,533)                        | (259,344)            |
| Total stockholders' equity  | 25,285,847                       | 25,480,584           |
| Total liabilities and stockholders' equity  | <u>\$ 50,763,997</u>             | <u>\$ 51,079,462</u> |

See accompanying notes to condensed consolidated financial statements.

**WORLD ENERGY SOLUTIONS, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
(Unaudited)

|   | Three Months Ended March 31, |              |
|---|------------------------------|--------------|
|   | 2014                         | 2013         |
| Revenue:  |                              |              |
| Brokerage commissions, transaction fees and efficiency projects | \$ 9,338,164                 | \$ 8,470,959 |
| Management fees   | 182,189                      | 186,523      |
| Total revenue   | 9,520,353                    | 8,657,482    |
| Cost of revenue   | 2,312,313                    | 2,233,151    |
| Gross profit  | 7,208,040                    | 6,424,331    |
| Operating expenses:   |                              |              |
| Sales and marketing   | 4,761,991                    | 4,978,081    |
| General and administrative                                      | 2,684,475                    | 2,061,673    |
| Total operating expenses  | 7,446,466                    | 7,039,754    |
| Operating loss  | (238,426)                    | (615,423)    |
| Interest expense, net   | (200,397)                    | (202,737)    |
| Other income (expense)  | 4,043                        | (7,420)      |
| Loss before income taxes  | (434,780)                    | (825,580)    |
| Income tax expense  | 63,000                       | 131,305      |
| Net loss  | \$ (497,780)                 | \$ (956,885) |
| Net loss per common share — basic and diluted                   | \$ (0.04)                    | \$ (0.08)    |
| Weighted average shares outstanding — basic and diluted         | 12,133,752                   | 11,966,108   |

See accompanying notes to condensed consolidated financial statements.

**WORLD ENERGY SOLUTIONS, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(Unaudited)

|   | <b>Three Months Ended March 31,</b> |                     |
|---|-------------------------------------|---------------------|
|   | <b>2014</b>                         | <b>2013</b>         |
| <b>Cash flows from operating activities:</b>                                    |                                     |                     |
| Net loss  | \$ (497,780)                        | \$ (956,885)        |
| Adjustments to reconcile net loss to net cash provided by operating activities: |                                     |                     |
| Depreciation and amortization   | 993,121                             | 1,038,934           |
| Deferred income taxes   | 57,000                              | 108,805             |
| Stock-based compensation  | 161,903                             | 145,986             |
| Loss on disposal of property and equipment                                      | 4,273                               | 10,377              |
| Non-cash interest expense on warrants related to debt discount                  | -                                   | 9,968               |
| Interest on accrued contingent consideration                                    | -                                   | 9,863               |
| Changes in operating assets and liabilities:                                    |                                     |                     |
| Trade accounts receivable, net  | 298,249                             | (3,754)             |
| Inventory   | 50,573                              | (277,374)           |
| Prepaid expenses and other current assets                                       | (55,748)                            | (70,949)            |
| Accounts payable  | (275,880)                           | 500,275             |
| Accrued commissions   | 29,654                              | 301,742             |
| Accrued compensation  | (573,819)                           | (531,422)           |
| Accrued contingent consideration  | (72,000)                            |                     |
| Accrued expenses and other current liabilities                                  | 76,113                              | (621,659)           |
| Deferred revenue and customer advances  | 696,113                             | 1,001,490           |
| Net cash provided by operating activities                                       | <u>891,772</u>                      | <u>665,397</u>      |
| <b>Cash flows from investing activities:</b>                                    |                                     |                     |
| (Increase) decrease in other assets   | (80,036)                            | 13,075              |
| Purchases of property and equipment, net of disposals                           | (41,458)                            | (9,216)             |
| Net cash (used in) provided by investing activities                             | <u>(121,494)</u>                    | <u>3,859</u>        |
| <b>Cash flows from financing activities:</b>                                    |                                     |                     |
| Proceeds from exercise of stock options   | 84,654                              | 66,900              |
| Purchase of treasury stock  | (189)                               | (41)                |
| Principal payments on long term debt  | -                                   | (500,000)           |
| Payments of contingent consideration  | -                                   | (1,435,548)         |
| Principal payments on capital lease obligations                                 | (909)                               | (5,143)             |
| Net cash provided by (used in) financing activities                             | <u>83,556</u>                       | <u>(1,873,832)</u>  |
| Net increase (decrease) in cash and cash equivalents                            | 853,834                             | (1,204,576)         |
| Cash and cash equivalents, beginning of period                                  | 1,725,136                           | 3,307,822           |
| Cash and cash equivalents, end of period  | <u>\$ 2,578,970</u>                 | <u>\$ 2,103,246</u> |
| <b>Supplemental Disclosure of Cash Flow Information:</b>                        |                                     |                     |
| Net cash paid for interest  | \$ 195,800                          | \$ 233,420          |
| Net cash paid for income taxes  | \$ 1,300                            | \$ 30,550           |
| <b>Non-cash activities:</b>   |                                     |                     |
| Equipment acquired under capital leases   | <u>\$ -</u>                         | <u>\$ 21,416</u>    |

See accompanying notes to condensed consolidated financial statements.

**WORLD ENERGY SOLUTIONS, INC.**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(Unaudited)**

**March 31, 2014**

**1. Nature of Business and Basis of Presentation**

World Energy Solutions, Inc. ("World Energy" or the "Company") offers a range of energy management solutions to commercial and industrial businesses, institutions, utilities, and governments to reduce their overall energy costs. The Company comes to market with a holistic approach to energy management helping customers a) contract for a competitive price for energy, b) engage in energy efficiency projects to minimize quantity used and c) pursue available rebate and incentive programs. The Company made its mark on the industry with an innovative approach to procurement via its online auction platform, the World Energy Exchange<sup>®</sup>. With recent investments and acquisitions, World Energy is building out its energy efficiency practice engaging new customers while also pursuing more cross-selling opportunities for its procurement services.

**2. Interim Financial Statements**

The December 31, 2013 condensed consolidated balance sheet has been derived from audited consolidated financial statements and the accompanying March 31, 2014 unaudited interim condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC") regarding interim reporting. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America ("GAAP") for complete financial statements and should be read in conjunction with the audited consolidated financial statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2013, as filed with the SEC on March 31, 2014.

In the opinion of the Company's management, the unaudited interim condensed consolidated financial statements have been prepared on the same basis as the audited consolidated financial statements and include all adjustments consisting of normal recurring adjustments and accruals necessary for the fair presentation of the Company's financial position as of March 31, 2014 and the results of its operations and cash flows for the three months ended March 31, 2014 and 2013, respectively. The results of operations for the three months ended March 31, 2014 are not necessarily indicative of the results to be expected for the fiscal year ending December 31, 2014.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Accordingly, actual results could differ from these estimates.

The Company's most judgmental estimates affecting its condensed consolidated financial statements are those relating to revenue recognition and the estimate of actual energy delivered from the bidder to the lister of such energy; stock-based compensation; the valuation of intangible assets and goodwill; the valuation of contingent consideration; impairment of long-lived assets; and estimates of future taxable income as it relates to the realization of our net deferred tax assets. The Company regularly evaluates its estimates and assumptions based upon historical experience and various other factors that the Company believes to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. To the extent actual results differ from those estimates, future results of operations may be affected.

**3. Loss Per Share**

As of March 31, 2014 and 2013, the Company only had one issued and outstanding class of stock – common stock. As a result, the basic loss per share for the three months ended March 31, 2014 and 2013 is computed by dividing net loss by the weighted average number of common shares outstanding for the period.

The following table provides a reconciliation of the denominators of the Company's reported basic and diluted earnings per share computation for the three months ended March 31, 2014 and 2013, respectively:

|  | For the Three Months Ended March 31, |            |
|--|--------------------------------------|------------|
|  | 2014                                 | 2013       |
| Weighted number of common shares - basic                         | 12,133,752                           | 11,966,108 |
| Common stock equivalents   | —                                    | —          |
| Weighted number of common and common equivalent shares - diluted | 12,133,752                           | 11,966,108 |

The computed loss per share does not assume conversion, exercise, or contingent exercise of securities that would have an antidilutive effect on loss per share. As the Company was in a net loss position for the three months ended March 31, 2014 and 2013, all common stock equivalents in those periods were anti-dilutive.

For the three months ended March 31, 2014, 722,429, 49,545 and 265,750 shares issuable relative to common stock options, common stock warrants and restricted stock, respectively, were excluded from net loss per share since the inclusion of such shares would be anti-dilutive. For the three months ended March 31, 2013, 755,506, 49,545 and 145,000 shares issuable relative to common stock options, common stock warrants and restricted stock, respectively, were excluded from net loss per share since the inclusion of such shares would be anti-dilutive. The Company did not declare or pay any dividends in 2014 or 2013.

#### 4. Concentration of Credit Risk and Off-Balance Sheet Risk

Financial instruments that potentially expose the Company to concentrations of credit risk consist principally of cash and cash equivalents and trade accounts receivable. The Company has no material off-balance sheet risk such as foreign exchange contracts, option contracts, or other foreign hedging arrangements. The Company places its cash and cash equivalents with two institutions, which management believes are of high credit quality. As of March 31, 2014, all of the Company's cash and cash equivalents are held in interest bearing accounts.

The Company provides credit in the form of invoiced and unbilled accounts receivable in the normal course of business. Collateral is not required for trade accounts receivable, but ongoing credit evaluations are performed. While the majority of the Company's revenue is generated from retail energy transactions where the winning bidder pays a commission to the Company, commission payments for certain auctions can be paid by the lister, bidder or a combination of both.

The following represents revenue and trade accounts receivable from bidders exceeding 10% of the total in each category:

| Bidder | Revenue for the three months ended March 31, |      | Trade accounts receivable as of March 31, |      |
|--------|--|------|---|------|
|        | 2014   | 2013 | 2014                                      | 2013 |
| A      | 19%  | 17%  | 21%                                       | 16%  |
| B      | 9%   | 10%  | 11%                                       | 12%  |
| C      | 7%   | 10%  | 11%                                       | 12%  |

Two bidders merged at the end of 2013 and have been combined for presentation purposes above. In addition to its direct relationship with bidders, the Company also has direct contractual relationships with listers for the online procurement of certain of their energy, demand response or environmental needs. These listers are primarily large businesses and government organizations and do not have a direct creditor relationship with the Company. For the three months ended March 31, 2014 and 2013, no lister represented more than 10% individually of the Company's aggregate revenue.

#### 5. Trade Accounts Receivable, Net

The Company does not invoice bidders for the commissions earned on retail electricity, certain natural gas and demand response transactions and, therefore, reports a significant portion of its receivables as "unbilled." Unbilled accounts receivable represent management's best estimate of energy provided by the energy suppliers to the energy consumers for a specific completed time period at contracted commission rates.

The Company generally invoices bidders for commissions earned on wholesale and a substantial portion of retail natural gas transactions as well as energy efficiency customers, which are reflected as billed accounts receivable. For natural gas and wholesale transactions, the total commission earned on these transactions is recognized upon completion of the procurement event and are generally due within 30 days of invoice date. For efficiency projects, revenue is recognized and invoiced upon project installation and acceptance, as required, and are generally due within 30 days of invoice date. In addition, the Company invoices the bidder, lister or combination of both for certain auctions performed for environmental commodity product transactions. These transactions are earned and invoiced either upon lister acceptance of the auction results or, in some cases, upon delivery of the credits or cash settlement of the transaction. Management provides for an allowance for doubtful accounts on a specifically identified basis, as well as through historical experience applied to an aging of accounts, if necessary. Trade accounts receivable are written off when deemed uncollectible. To date, write-offs have not been material. Trade accounts receivable, net consists of the following:

|                                 | March 31, 2014 | December 31, 2013 |
|---------------------------------|----------------|-------------------|
| Unbilled accounts receivable    | \$ 6,606,411   | \$ 6,070,227      |
| Billed accounts receivable      | 1,208,660      | 1,993,093         |
|                                 | 7,815,071      | 8,063,320         |
| Allowance for doubtful accounts | (375,179)      | (325,179)         |
| Trade accounts receivable, net  | \$ 7,439,892   | \$ 7,738,141      |

## 6. Inventory

Inventory is maintained in the Company's Energy efficiency services segment and consists of prepaid expendables and project materials. Prepaid expendables represents consumable components that are used in project installations and are stated at the lower of cost or market, with cost being determined on a first-in, first-out (FIFO) basis. Historical inventory usage and current trends are considered in estimating both excess and obsolete inventory. To date, there have been no material write-downs of inventory and therefore no allowance for excess or obsolete inventory was recorded at March 31, 2014 or December 31, 2013. Project materials represent direct costs incurred on projects-in-process as of each reporting period. Inventory consists of the following:

|                     | March 31, 2014 | December 31, 2013 |
|---------------------|----------------|-------------------|
| Prepaid expendables | \$ 63,109      | \$ 55,563         |
| Project materials   | 302,088        | 360,207           |
| Total inventory     | \$ 365,197     | \$ 415,770        |

## 7. Intangibles, Net

Intangibles, net with finite lives are summarized as follows as of March 31, 2014 and December 31, 2013:

|                        | Estimated Useful Life | March 31, 2014  |                          |              | December 31, 2013 |                          |              |
|------------------------|-----------------------|-----------------|--------------------------|--------------|-------------------|--------------------------|--------------|
|                        |                       | Carrying Amount | Accumulated Amortization | Net          | Carrying Amount   | Accumulated Amortization | Net          |
| Customer contracts     | 1 - 4 years           | \$ 5,276,000    | \$ 3,393,000             | \$ 1,883,000 | \$ 5,276,000      | \$ 3,017,000             | \$ 2,259,000 |
| Customer relationships | 7 - 10 years          | 13,792,000      | 5,166,000                | 8,626,000    | 13,792,000        | 4,812,000                | 8,980,000    |
| Non-compete agreements | 5 years               | 2,585,000       | 1,091,000                | 1,494,000    | 2,585,000         | 962,000                  | 1,623,000    |
| Trade names            | 4 years               | 1,090,000       | 562,000                  | 528,000      | 1,090,000         | 494,000                  | 596,000      |
| Total                  |                       | \$22,743,000    | \$ 10,212,000            | \$12,531,000 | \$22,743,000      | \$ 9,285,000             | \$13,458,000 |

The Company also recorded acquisition related intangible assets with indefinite lives in the amount of \$1,736,000 pertaining to customer relationships, which is not reflected in the above tables.

Amortization expense was approximately \$927,000 and \$975,000 for the three months ended March 31, 2014 and 2013, respectively. The approximate future amortization expense of intangible assets is as follows:

|                     |                      |
|---------------------|----------------------|
| Remainder of 2014   | \$ 2,443,000         |
| 2015                | 2,801,000            |
| 2016                | 2,416,000            |
| 2017                | 1,273,000            |
| 2018                | 915,000              |
| 2019 and thereafter | 2,683,000            |
|                     | <u>\$ 12,531,000</u> |

#### 8. Deferred Revenue and Customer Advances

Deferred revenue and customer advances arise when energy suppliers pay the Company a commission prior to the Company meeting all the requirements necessary to recognize revenue. In addition, deferred revenue and customer advances includes cash received for Energy efficiency services projects that have not been completed. Deferred revenue and customer advances expected to be recognized as revenue by year are approximately as follows:

|  | Amount              |
|--|---------------------|
| Remainder of 2014                            | \$ 3,703,000        |
| 2015   | 2,668,000           |
| 2016   | 1,256,000           |
| 2017   | 325,000             |
| 2018 and thereafter                          | 201,000             |
| Total deferred revenue and customer advances | <u>\$ 8,153,000</u> |

The following table provides a rollforward of deferred revenue and customer advances:

|                            | Amount              |
|----------------------------|---------------------|
| Balance at January 1, 2014 | \$ 7,456,000        |
| Cash received              | 1,920,000           |
| Revenue recognized         | <u>(1,223,000)</u>  |
| Balance at March 31, 2014  | <u>\$ 8,153,000</u> |

#### 9. Segment Reporting

The Company operates its business based on two industry segments: Energy procurement and Energy efficiency services. The Company delivers its Energy procurement services to four markets: retail energy, wholesale energy, demand response and environmental commodity. The Energy procurement process is substantially the same regardless of the market being serviced and is supported by the same operations personnel utilizing the same basic technology and back office support. There is no discrete financial information for these product lines nor are there segment managers who have operating responsibility for each product line. Energy efficiency services focuses on turn-key electrical, mechanical and lighting energy efficiency measures servicing commercial, industrial and institutional customers.

Segment operating income represents income from operations, including share-based compensation, amortization of intangible assets and depreciation. The following tables present certain continuing operating division information in accordance with the provisions of Accounting Standards Codification ("ASC") 280, "Segment Reporting".

**Consolidated revenue from external customers:**

Energy procurement

Energy efficiency services

Consolidated total revenue

**Consolidated loss before income taxes:**

Energy procurement

Energy efficiency services

Consolidated loss before income taxes

**Three Months Ended March 31,****2014****2013**

\$ 7,969,644

\$ 1,550,709

\$ 9,520,353

\$ (160,425)

\$ (274,355)

\$ (434,780)

\$ 7,421,159

\$ 1,236,323

\$ 8,657,482

\$ (625,539)

\$ (200,041)

\$ (825,580)

**Energy Procurement:**

Amortization

Depreciation

Interest expense, net

**Energy Efficiency Services:**

Amortization

Depreciation

Interest expense, net

**Three Months Ended March 31,****2014****2013**

\$ 900,921

\$ 46,059

\$ 200,397

\$ 39,289

\$ 6,852

\$ -

\$ 943,976

\$ 48,564

\$ 202,737

\$ 39,289

\$ 7,105

\$ -

**March 31, 2014****December 31, 2013****Consolidated total assets:**

Energy procurement

Energy efficiency services

Consolidated total assets

\$ 45,341,888

\$ 5,422,109

\$ 50,763,997

\$ 44,898,931

\$ 6,180,531

\$ 51,079,462

**10. Fair Value Measurement and Fair Value of Financial Instruments**

The Company follows ASC 820, "Fair Value Measurements and Disclosures" ("ASC 820") for fair value measurements. ASC 820 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. The standard provides a consistent definition of fair value, which focuses on an exit price, which is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The standard also prioritizes, within the measurement of fair value, the use of market-based information over entity specific information and establishes a three-level hierarchy for fair value measurements based on the nature of inputs used in the valuation of an asset or liability as of the measurement date.

The hierarchy established under ASC 820 gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3).

Level 1 - Pricing inputs are quoted prices available in active markets for identical investments as of the reporting date. As required by ASC 820, the Company does not adjust the quoted price for these investments, even in situations where the Company holds a large position and a sale could reasonably impact the quoted price.

Level 2 - Pricing inputs are quoted prices for similar investments, or inputs that are observable, either directly or indirectly, for substantially the full term through corroboration with observable market data. Level 2 includes investments valued at quoted prices adjusted for legal or contractual restrictions specific to these investments.

Level 3 - Pricing inputs are unobservable for the investment, that is, inputs that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability. Level 3 includes investments that are supported by little or no market activity.



Assets and liabilities of the Company measured at fair values on a recurring basis as of March 31, 2014 and December 31, 2013 are summarized as follows:

|                          | March 31, 2014    | Level 1     | Level 2     | Level 3           |
|--------------------------|-------------------|-------------|-------------|-------------------|
| <b>Liabilities</b>       |                   |             |             |                   |
| Contingent consideration | \$ 928,000        | \$ —        | \$ —        | \$ 928,000        |
| <b>Total Liabilities</b> | <b>\$ 928,000</b> | <b>\$ —</b> | <b>\$ —</b> | <b>\$ 928,000</b> |

  

|                          | December 31, 2013   | Level 1     | Level 2     | Level 3             |
|--------------------------|---------------------|-------------|-------------|---------------------|
| <b>Liabilities</b>       |                     |             |             |                     |
| Contingent consideration | \$ 1,000,000        | \$ —        | \$ —        | \$ 1,000,000        |
| <b>Total Liabilities</b> | <b>\$ 1,000,000</b> | <b>\$ —</b> | <b>\$ —</b> | <b>\$ 1,000,000</b> |

The Company determines the fair value of acquisition-related contingent consideration based on assessment of the probability that the Company would be required to make such future payment. Changes to the fair value of contingent consideration are recorded in general and administrative expense. The Company settled its contingent consideration obligations subsequent to quarter end. As part of the settlement, the Company issued 200,000 shares of common stock to GSE Consulting, L.P. ("GSE") that had a fair value of \$928,000 on the date of issuance.

The following table provides a rollforward of the fair value, as determined by Level 3 inputs, of the contingent consideration.

|   | Three Months Ended<br>March 31, 2014 |
|---|--------------------------------------|
| Beginning balance                         | \$ 1,000,000                         |
| Additions                                 | —                                    |
| Payments                                  | —                                    |
| Change in fair value included in earnings | (72,000)                             |
| Accrued interest                          | —                                    |
| Ending balance                            | <b>\$ 928,000</b>                    |

The carrying amounts and fair values of the Company's debt obligations are as follows:

|  | March 31, 2014       |                      | December 31, 2013    |                      |
|--|----------------------|----------------------|----------------------|----------------------|
|  | Carrying Value       | Fair Value           | Carrying Value       | Fair Value           |
| Long-term debt                           | \$ 6,000,000         | \$ 6,000,000         | \$ 6,000,000         | \$ 6,000,000         |
| Subordinated notes payable               | 4,000,000            | 4,000,000            | 4,000,000            | 4,000,000            |
| Related party subordinated notes payable | 500,000              | 500,000              | 500,000              | 500,000              |
| <b>Total debt obligations</b>            | <b>\$ 10,500,000</b> | <b>\$ 10,500,000</b> | <b>\$ 10,500,000</b> | <b>\$ 10,500,000</b> |

The carrying amount for fixed rate long-term debt and variable rate long-term debt approximate fair value because the underlying instruments are primarily at current market rates available to the Company for similar borrowings. The interest rate on the Commerce Bank and Trust Company ("Commerce") debt is tied to the prime rate and will fluctuate with changes in that rate. Related party notes payable are classified as short-term on the Company's accompanying condensed consolidated balance sheets.

## 11. Credit Arrangements

### Credit Facility

The Company has a \$8.5 million credit facility with Commerce consisting of a revolving credit facility of up to \$2.5 million (the "Revolver") that matures on December 30, 2016 and a 60-month term loan of \$6.0 million (the "Term Loan").

The Revolver bears interest at the prime rate plus 1.75% (totaling 5% at March 31, 2014) and is adjusted every six months for any change in the prime rate. In addition to changes in the Prime Rate, the rate can be reduced by up to .50% based on certain EBITDA achievement levels. Under the Revolver, the Company may borrow, repay and re-borrow an amount not to exceed the lesser of \$2,500,000 or the total of 80% of eligible billed and unbilled accounts receivable (less the aggregate outstanding on any letters of

credit). There have been no borrowings under the Revolver. The Term Loan bears interest for the first 6 months at the prime rate plus 2.75% (totaling 6% at March 31, 2014), and is adjusted every six months for any change in the prime rate. In addition to changes in the prime rate, the rate can be reduced by up to .50% based on certain EBITDA achievement levels. The Term Loan is interest only for six months followed by 54 principal and interest payments commencing on July 30, 2014 with a balloon payment for any remaining principal balance at maturity.

### **Subordinated Notes**

On October 3, 2012, the Company entered into a Note Purchase Agreement with Massachusetts Capital Resource Company ("MCRC"), in which the Company entered into an 8-year, \$4 million Subordinated Note due 2020 with MCRC (the "MCRC Note"). The MCRC Note bears interest at 10.5% and is interest only for the first four years followed by 48 equal principal payments commencing October 31, 2016. The Company must pay a premium of 3% if it prepays the MCRC Note before October 1, 2014 and a 1% premium if it prepays the MCRC Note before October 1, 2015. The MCRC Note is subordinated to the Company's credit facility with Commerce and contains a Minimum Fixed Charge Ratio covenant that the Company is in compliance with at March 31, 2014.

## **12. Commitments and Contingencies**

### **Litigation**

Two former employees/consultants of GSE have filed two separate complaints in Texas County Court alleging, among other things, claims related to breach of contract, quantum meruit, promissory estoppel, and tortious interference. Each plaintiff claims that GSE and/or the Company failed to pay commissions due for services that they provided prior to the date of the Company's purchase of certain GSE assets, based on their respective employment or independent contractor agreements with GSE. Each plaintiff has also asserted claims for recovery of their attorneys' fees. The Company denies the allegations and has filed counterclaims for damages, asserting claims for conversion, unjust enrichment, misappropriation of confidential information, and violation of the Texas Theft Liability Act against each of the plaintiffs. The Company has also filed a counterclaim against one of the plaintiffs for her breach of a non-competition and non-solicitation agreement, based on her working for a competitor of the Company's during her one-year restrictive period and her improper solicitation of former GSE customers on behalf of the competitor. The plaintiffs have also asserted claims against the GSE affiliates and their individual principals. The court has assigned a trial date of September 29, 2014 for one of the cases. The remaining case is awaiting assignment of a trial date. The Company's motion for summary judgment seeking dismissal of all claims against one of the two plaintiffs has been denied. The Company's motion for summary judgment against the other plaintiff has been filed and is awaiting oral argument.

The Company has estimated the potential commissions allegedly due to the two plaintiffs to be approximately \$0.3 million. The Company has not recorded any accrual for contingent liabilities associated with these legal proceedings based on its belief that any potential losses, while reasonably possible, is not probable. The Company intends to continue to defend these actions vigorously and is currently unable to estimate a range of payments, if any, it may be required to pay, with respect to these claims. Further, the Company believes that the resolution of these matters will not result in a material effect to its condensed consolidated financial statements. However, due to uncertainties that accompany litigation of this nature, there could be no assurance that the Company will be successful, and the resolution of the lawsuits could have a material effect on its accompanying condensed consolidated financial statements.

In addition, the Company had filed cross claims against GSE for indemnification under the Asset Purchase Agreement in each of the plaintiffs' cases. The GSE affiliates and principals had also asserted cross claims against the Company seeking indemnification under the Asset Purchase Agreement. In December 2013, GSE had amended its cross claims in one of the matters to include claims asserting breach of the earnout provisions in the Asset Purchase Agreement. Subsequent to quarter end, the Company and GSE settled all claims against each other related to these lawsuits and the earnout provisions and filed with the court agreed motions to dismiss all claims against one another. The settlement calls for the Company to issue 200,000 shares of common stock to GSE and its affiliates that had a fair value of \$0.9 million on the date issued. This amount is reflected as a current liability in accrued contingent consideration as of March 31, 2014.

From time to time, the Company may be subject to legal proceedings and claims arising from the conduct of its business operations, including litigation related to employment matters. While it is impossible to ascertain the ultimate legal and financial liability with respect to contingent liabilities, including lawsuits, management believes that the aggregate amount of such liabilities, if any, will not have a material adverse effect on its condensed consolidated financial position and/or results of operations. It is possible, however, that future financial position or results of operations for any particular period could be materially affected by changes in the Company's assumptions or strategies related to those contingencies or changes out of its control.

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

*This quarterly report on Form 10-Q including this Item 2, contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, which involve risks and uncertainties. Readers can identify these statements by forward-looking words such as "may," "could," "should," "would," "intend," "will," "expect," "anticipate," "believe," "estimate," "continue" or similar words. Our actual results and the timing of certain events may differ significantly from the results and timing discussed in the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those discussed or referred to in this report and in the "Risk Factors" section of our Annual Report on Form 10-K and any later publicly available filing with the Securities and Exchange Commission ("SEC"). The following discussion and analysis of our financial condition and results of operations should be read in light of those factors and in conjunction with our accompanying condensed consolidated financial statements and notes thereto.*

### Overview

World Energy offers a range of energy management solutions to commercial and industrial businesses, institutions, utilities, and governments to reduce their overall energy costs. We come to market with a holistic approach to energy management helping customers a) contract for a competitive price for energy, b) engage in energy efficiency projects to minimize quantity used and c) pursue available rebate and incentive programs. We made our mark on the industry with an innovative approach to procurement via our online auction platform, the World Energy Exchange<sup>®</sup>. With recent investments and acquisitions, we are building out our energy efficiency practice by engaging new customers while also pursuing more cross-selling opportunities for our procurement services.

We provide energy management services utilizing state-of-the-art technology and the experience of a seasoned management team to bring lower energy costs to its customers. We use a simple equation

$$E = P \cdot Q - i$$

to help customers to understand the holistic nature of the energy management problem. Total energy cost (E) is a function of Energy Price (P) times the Quantity of Energy Consumed (Q), minus any rebates or incentives (i) the customer can earn. This approach not only makes energy management more approachable for customers, simplifying what has become an increasingly dynamic and complex problem, it also highlights the inter-related nature of the energy management challenge. We assert that point solution vendors may optimize one of the three elements, but we believe it takes looking at the problem holistically to unlock the most savings.

Acquisitions are an important component of our business strategy. Our focus is on both our core procurement business as well as new product lines within the energy management services industry such as energy efficiency services.

During the fourth quarter of 2012, we acquired substantially all of the assets and assumed certain obligations of Northeast Energy Partners, LLC ("NEP") pursuant to an Asset Purchase Agreement (the "Asset Purchase Agreement") between us, NEP, and its members. NEP was a Connecticut based energy management and procurement company. During the third and fourth quarters of 2011 we acquired the energy procurement business of Co-eXprise, Inc. ("Co-eXprise"), Northeast Energy Solutions, LLC ("NES") and GSE Consulting, LP ("GSE"). These acquisitions expanded our capabilities in the Energy efficiency services segment, enabled us to enter the growing small- and medium-sized customer Energy procurement marketplaces, and consolidate the large commercial, industrial and government auction space. With the acquisition of NES, we are managing the business as two business segments: Energy procurement and Energy efficiency services.

Our business model is heavily dependent on our people. We have significantly grown our employee base from 20 at the time of our initial public offering in November 2006 to 127 at March 31, 2014. This planned investment in staffing has been, and will continue to be, a key component of our strategic initiatives and revenue growth. These infrastructure investments will result in increased operating costs in the short-term, but in the long-term we expect them to generate cash flow and profitability as we build incremental revenue. To date we have funded our acquisitions and strategic investments primarily with cash on-hand, notes payable, cash from operations and long-term debt. We have also deferred portions of the purchase prices through the use of earnouts that are tied to the ongoing performance of the acquired entity. Through the utilization of seller notes and earnouts, we have been able to finance a portion of the cost of the acquisitions over time with the targets' ongoing cash flow. These acquisition activities will increase our operating costs both in the short and long-term and may require us to borrow against our current credit facility and/or raise funds through additional capital raises.

## Operations

### Revenue

#### Retail Electricity Transactions

We earn a monthly commission on energy sales contracted through our online auction platform from each bidder or energy supplier based on the energy usage transacted between the bidder and the energy consumer. Our commissions are not based on the retail price for electricity; rather on the amount of energy consumed. Commissions are calculated based on the volume of energy usage transacted between the energy supplier and energy consumer multiplied by our contractual commission rate. Our contractual commission rate is negotiated with the energy consumer on a procurement-by-procurement basis based on energy consumer specific circumstances, including the size of auction, the effort required to organize and run the respective auction and competitive factors, among others. Once the contractual commission is agreed to with the energy consumer, all energy suppliers participating in the auction agree to that rate. That commission rate remains fixed for the duration of the contractual term regardless of energy usage. Energy consumers provide us with a letter of authorization to request their usage history from the local utility. We then use this data to compile a usage profile for that energy consumer that will become the basis for the auction. This data may also be used to estimate revenue on a going forward basis, as noted below.

Historically, our revenue and operating results have varied from quarter-to-quarter and are expected to continue to fluctuate in the future. These fluctuations are primarily due to the buying patterns of our wholesale and natural gas customers, which tend to have large, seasonal purchases during the fourth and first quarters and electricity usage having higher demand in our second and third quarters. In addition, the activity levels on the World Energy Exchange® can fluctuate due to a number of factors, including market prices, weather conditions, energy consumers' credit ratings, the ability of suppliers to obtain financing in credit markets, and economic and geopolitical events. To the extent these factors affect the purchasing decisions of energy consumers, our future results of operations may be affected. Contracts between energy suppliers and energy consumers are signed for a variety of term lengths, with a one to two year contract term being typical for commercial and industrial energy consumers, and government contracts typically having two to three year terms.

We do not invoice our electricity energy suppliers for monthly commissions earned and, therefore, we report a substantial portion of our receivables as "unbilled." Unbilled accounts receivable is based on management's best estimate of energy provided by the energy suppliers to the energy consumers for a specific completed time period at contracted commission rates and is made up of two components. The first component represents energy usage for which we have received actual data from the supplier and/or the utility, but for which payment has not been received at the balance sheet date. The majority of our contractual relationships with energy suppliers require them to supply actual usage data to us on a monthly basis and remit payment to us based on that usage. The second component represents energy usage for which we have not received actual data, but for which we have estimated usage. Commissions paid in advance by certain bidders are recorded as deferred revenue and amortized to commission revenue on a monthly basis on the energy exchanged that month.

#### Retail Natural Gas Transactions

There are two primary fee components to our retail natural gas services: transaction fees and management fees. Transaction fees are billed to and paid by the energy supplier awarded business on the platform. These fees are established prior to award and are the same for each supplier. For the majority of our natural gas transactions, we bill the supplier upon the conclusion of the transaction based on the estimated energy volume transacted for the entire award term multiplied by the transaction fee. Management fees are paid by our energy consumers and are generally billed on a monthly basis for services rendered based on terms and conditions included in contractual arrangements. While substantially all of our retail natural gas transactions are accounted for in accordance with this policy, a significant percentage is accounted for as the natural gas is consumed by the energy consumer and recognized as revenue in accordance with the retail electricity transaction revenue recognition methodology described above.

### Mid-Market Transactions

We earn a monthly commission on energy sales from each energy supplier based on the energy usage transacted between the energy supplier and energy consumer. The commissions are not based on the retail price for electricity but rather on the amount of energy consumed. Commissions are calculated based on the energy usage transacted between the energy supplier and energy consumer multiplied by our contractual commission rate. Revenue from commissions is recognized as earned over the life of each contract as energy is consumed, provided there is persuasive evidence of an arrangement, the sales price is fixed or determinable, collection of the fee is reasonably assured, and customer acceptance criteria, if any, has been successfully demonstrated. We generally recognize revenue on these transactions when we have received verification from the electricity supplier of the end-users power usage and electricity supplier's subsequent collection of the fees billed to the end user. The verification is generally accompanied with payment of the agreed upon fee to us, at which time the revenue is recognized. Commissions paid in advance are recorded as customer advances and are recognized monthly as commission revenue based on the energy exchanged that month. To the extent we do not receive verification of actual energy usage or we cannot reliably estimate what actual energy usage was for a given period, revenue is deferred until usage and collection data is received from the energy supplier. To the extent that we do not receive actual usage data from the energy supplier, we will recognize revenue at the end of the contract flow date.

### Demand Response Transactions

Demand response transaction fees are recognized when we have received confirmation from the demand response provider ("DRP") that the energy consumer has performed under the applicable Regional Transmission Organization ("RTO") or Independent System Operator ("ISO") program requirements. The energy consumer is either called to perform during an actual curtailment event or is required to demonstrate its ability to perform in a test event during the performance period. For the PJM Interconnection ("PJM"), an RTO that coordinates the movement of wholesale electricity in all or parts of 13 states and the District of Columbia, the performance period is June through September in a calendar year. Test results are submitted to the PJM by the DRPs and we receive confirmation of the energy consumer's performance in the fourth quarter. DRPs typically pay us ratably on a quarterly basis throughout the demand response fiscal (June to May) year. As a result, a portion of the revenue we recognize is reflected as unbilled accounts receivable.

### Wholesale and Environmental Commodity Transactions

Wholesale transaction fees are invoiced upon the conclusion of the auction based on a fixed fee. These revenues are not tied to future energy usage and are recognized upon the completion of the online auction. For reverse auctions where our customers bid for a consumer's business, the fees are paid by the bidder. For forward auctions where a lister is selling energy products, the fees are typically paid by the lister.

Environmental commodity transaction fees are accounted for utilizing two primary methods. For regulated allowance programs like Regional Greenhouse Gas Initiative, Inc. ("RGGI"), fees are paid by the lister and are recognized quarterly as revenue as auctions are completed and approved. For most other environmental commodity transactions both the lister and the bidder pay the transaction fee and revenue is recognized upon the consummation of the underlying transaction as credits are delivered by the lister and payment is made by the bidder.

### Energy Efficiency Services

Our Energy efficiency services segment is primarily project driven where we identify efficiency measures that energy consumers can implement to reduce their energy usage. We present retrofit opportunities to customers, get approval from them to proceed and submit the proposal to the local utility for cost reimbursement. Once the utility approves funding for the project, we install the equipment, typically new heating, ventilation or air conditioning equipment, or replace lighting fixtures to more efficient models. We recognize revenue for Energy efficiency services when persuasive evidence of an arrangement exists, delivery has occurred, the price is fixed or determinable and collectability is reasonably assured. Due to the short-term nature of projects (typically two to three weeks), we utilize the completed-contract method. We also assess multiple contracts entered into by the same customer in close proximity to determine if the contracts should be combined for revenue recognition purposes. Revenues are recognized based upon factors such as passage of title, installation, payments and customer acceptance.

### *Cost of revenue*

Cost of revenue consists primarily of:

- salaries, bonus and commissions, employee benefits and share-based compensation associated with our auction management and efficiency services, which are directly related to the development and production of the online auction and maintenance of market-related data on our auction platform and monthly management fees (our supply desk function);
- project costs including direct labor equipment and materials directly associated with efficiency projects; and

- rent, depreciation and other related overhead and facility-related costs.

#### ***Sales and marketing***

Sales and marketing expenses consist primarily of:

- salaries, bonus and commissions, employee benefits and share-based compensation related to sales and marketing personnel;
- third party commission expenses to our channel partners;
- travel and related expenses;
- amortization related to customer relationships and contracts;
- rent, depreciation and other related overhead and facility-related costs; and
- general marketing costs such as trade shows, marketing materials and outsourced services.

#### ***General and administrative***

General and administrative expenses consist primarily of:

- salaries, bonus and commissions, employee benefits and share-based compensation related to general and administrative personnel;
- accounting, legal, investor relations, information technology, insurance and other professional fees; and
- rent, depreciation and other related overhead and facility-related costs.

#### ***Interest expense, net***

Interest expense, net consists primarily of:

- interest income earned on cash held in the bank; and
- interest expense related to bank term loans, notes payable and contingent consideration.

#### ***Income tax expense***

Income tax expense reflects the release of our deferred tax assets to apply to projected annualized taxable income, federal alternative minimum tax liability and state income taxes.

#### **Results of Operations**

The following table sets forth certain items as a percent of revenue for the periods presented:

|                            | <b>For the Three Months Ended March 31,</b> |             |
|----------------------------|---|-------------|
|                            | <b>2014</b>                                 | <b>2013</b> |
| Revenue                    | 100%  | 100%        |
| Cost of revenue            | 24  | 26          |
| Gross profit               | 76  | 74          |
| Operating expenses:        |   |             |
| Sales and marketing        | 50  | 57          |
| General and administrative | 29  | 24          |
| Operating loss             | (3)   | (7)         |
| Other expense, net         | (2)   | (2)         |
| Income tax expense         | 0   | (2)         |
| Net loss                   | (5%)  | (11%)       |

# Comparison of the Three Months Ended March 31, 2014 and 2013

## Revenue

|                            | For the Three Months Ended<br>March 31, |                     | Increase          |     |
|----------------------------|---|---------------------|-------------------|-----|
|                            | 2014                                    | 2013                |                   |     |
| Energy procurement         | \$ 7,969,644                            | \$ 7,421,159        | \$ 548,485        | 7%  |
| Energy efficiency services | 1,550,709                               | 1,236,323           | 314,386           | 25  |
| Total revenue              | <u>\$ 9,520,353</u>                     | <u>\$ 8,657,482</u> | <u>\$ 862,871</u> | 10% |

Revenue increased 10 % for the three months ended March 31, 2014 as revenue from both segments increased as compared to the same period in 2013. Energy procurement segment revenue increased 7% due to increased revenue in our retail product line from both our auction and mid-market customers. These increases were partially offset by decreases in wholesale and gas transaction activity in the first quarter of 2014 as increased commodity prices during the quarter resulted in delayed contracting decisions by listers. Energy efficiency services segment revenue increased 25% as the reorganization of the Massachusetts sales team in 2013 resulted in increased revenue in the NSTAR territory in Massachusetts in the first quarter of 2014.

## Cost of revenue

|                            | For the Three Months Ended March 31, |              |                     |              | Increase (Decrease) |       |
|----------------------------|--------------------------------------|--------------|---------------------|--------------|---------------------|-------|
|                            | 2014                                 | 2013         |                     |              |                     |       |
|                            | \$                                   | % of Revenue | \$                  | % of Revenue |                     |       |
| Energy procurement         | \$ 1,045,371                         | 13%          | \$ 1,248,503        | 17%          | \$ (203,132)        | (16%) |
| Energy efficiency services | 1,266,942                            | 82           | 984,648             | 80           | 282,294             | 29    |
| Total cost of revenue      | <u>\$ 2,312,313</u>                  | 24%          | <u>\$ 2,233,151</u> | 26%          | <u>\$ 79,162</u>    | 4%    |

Cost of revenue increased 4 % for the three months ended March 31, 2014 as compared to the same period in 2013 primarily due to increases in equipment, material and labor costs associated with projects completed by our Energy efficiency services segment. Cost of revenue for our Energy procurement segment decreased 16% due to decreases in payroll reflecting our integration, automation and reorganization efforts. Cost of revenue associated with our Energy procurement segment as a percent of revenue decreased by 4% primarily due to the cost decreases described above and, to a lesser extent, the 7% increase in Energy procurement revenue. Cost of revenue associated with our Energy efficiency services segment increased 29% primarily due to an increase in project costs associated with the 25% increase in revenue. Cost of revenue associated with our Energy efficiency services segment as a percent of revenue increased by 2% primarily due to slightly lower contribution margins on projects completed in the first quarter of 2014.

## Operating expenses

|                            | For the Three Months Ended March 31, |              |                    |              | Increase (Decrease) |      |
|----------------------------|--------------------------------------|--------------|--------------------|--------------|---------------------|------|
|                            | 2014                                 | 2013         |                    |              |                     |      |
|                            | \$                                   | % of Revenue | \$                 | % of Revenue |                     |      |
| Sales and marketing        | \$4,761,991                          | 50%          | \$4,978,081        | 57%          | \$ (216,090)        | (4%) |
| General and administrative | 2,684,475                            | 29           | 2,061,673          | 24           | 622,802             | 30   |
| Total operating expenses   | <u>\$7,446,466</u>                   | 79%          | <u>\$7,039,754</u> | 81%          | <u>\$ 406,712</u>   | 6%   |

Sales and marketing expenses decreased 4% for the three months ended March 31, 2014 as compared to the same period in 2013 primarily due to decreases in internal commissions and amortization of intangible assets. Internal commissions decreased due to the change in commission policy for our mid-market group we implemented in the second quarter of 2013. Under the revised policy, we continued to pay commissions based on cash received from mid-market transactions that are deferred for revenue purposes and provided for a bookings bonus to offset the impact of the change in our policy. We converted the bookings bonus to a draw program in 2014, eliminating that component of commission expense. Amortization expense related to intangible assets decreased as certain intangible assets related to our acquisitions became fully amortized in 2014. Sales and marketing expense as a percentage of revenue decreased 7% due to the decrease in costs described above, and the 10% increase in total revenue.

The 30 % increase in general and administrative expenses for the three months ended March 31, 2014 as compared to the same period in 2013 was primarily due to increased legal and consulting costs of approximately \$0.4 million primarily related to a shareholder action during the first quarter of 2014. In addition, payroll costs increased due to investments in our product development

team. General and administrative expenses as a percent of revenue increased 5% primarily due to the cost increases described above, partially offset by the 10% increase in total revenue.

#### *Other income (expense), net*

Net interest expense was approximately \$0.2 million for the three months ended March 31, 2014 and March 31, 2013, respectively, as our outstanding indebtedness and interest rates were relatively the same for both periods.

#### *Income tax expense*

We recorded income tax expense of approximately \$0.1 million for the three months ended March 31, 2014 and March 31, 2013, respectively. In the first quarter of both periods income tax expense reflects a deferred tax provision, federal alternative minimum tax liability and state income taxes.

#### *Net loss*

We reported a net loss of approximately \$0.5 million for the three months ended March 31, 2014 and a net loss of approximately \$1.0 million for the three months ended March 31, 2013. The net loss decreased \$0.5 million primarily due to the increase in revenue, improved gross margin and the decrease in sales and marketing expenses. These reductions in net loss were partially offset by the increase in general and administrative expense.

### **Liquidity and Capital Resources**

At March 31, 2014, we had no commitments for material capital expenditures. We have identified and executed against a number of strategic initiatives that we believe are key components of our future growth, including: making strategic acquisitions; entering into other energy-related markets including energy efficiency; expanding our community of listers, bidders and channel partners on our exchanges; strengthening and extending our long-term relationships with government agencies; and growing our direct and inside sales force. As of March 31, 2014 our workforce numbered 127, an increase of one from the number that we employed at December 31, 2013. At March 31, 2014, we had 59 professionals in our sales and marketing and account management groups, 41 in our supply desk group and 27 in our general and administrative group.

We paid \$10.4 million to acquire three businesses in 2011 through the use of cash on hand, cash flow from ongoing operations as well as cash flow generated by the acquisitions. In addition, we have paid \$6.7 million in seller notes and contingent consideration bringing the total cash paid for the 2011 acquisitions to \$17.1 million. We borrowed \$8.0 million in long-term bank debt to acquire NEP in October 2012 and entered into a \$2.0 million seller note with NEP. While the expansion/addition of these debt instruments significantly increased our commitments, we believe we have the resources to meet both our short- and long-term obligations under these arrangements based on cash on-hand, operating cash flows from our base business and cash expected to be generated from all of our acquired businesses. During 2013, we paid an additional \$1.3 million in cash related to NEP contingent consideration and \$1.5 million against the NEP seller note. As of March 31, 2014 we have substantially retired all of our obligations related to these acquisitions. We have \$0.9 million of accrued contingent consideration recorded within current liabilities related to the GSE acquisition and \$0.5 million remaining on the NEP Seller note that was due April 1, 2014. Subsequent to quarter end we repaid the remaining \$0.5 million NEP Seller note and settled all outstanding earnout claims with GSE by issuing 200,000 shares of common stock, which had a fair value of approximately \$0.9 million. During the first three months of 2014 we generated cash flow from operations of \$0.9 million and ended the quarter with \$2.6 million in cash and cash equivalents.

#### **Comparison of March 31, 2014 to December 31, 2013**

|                                | March 31,<br>2014 | December 31,<br>2013 | Increase (Decrease) |     |
|--------------------------------|-------------------|----------------------|---------------------|-----|
| Cash and cash equivalents      | \$ 2,578,970      | \$ 1,725,136         | \$ 853,834          | 49% |
| Trade accounts receivable, net | 7,439,892         | 7,738,141            | (298,249)           | (4) |
| Days sales outstanding         | 70                | 76                   | (6)                 | (8) |
| Working capital (deficit)      | (636,284)         | (893,984)            | 257,700             | 29  |
| Stockholders' equity           | 25,285,847        | 25,480,584           | (194,737)           | (1) |

Cash and cash equivalents increased 49% primarily due to cash flows from operations of approximately \$0.9 million. Deferred revenue and customer advances increased due to advance payments related to our Energy efficiency services segment. Accrued compensation decreased due to the payment of year-end bonuses for 2013. Trade accounts receivable at March 31, 2014 decreased 4% as compared to the fourth quarter of 2013 as days sales outstanding decreased 8%. Days sales outstanding (representing accounts receivable outstanding at March 31, 2014 divided by the average sales per day during the current quarter, as adjusted) decreased 8% due to the timing of in-period revenue recognized and cash receipts within the first quarter of 2014 as compared to the fourth quarter



of 2013. Revenue from bidders representing 10% or more of our revenue decreased to 19% from one bidder during the three months ended March 31, 2014, from an aggregate 37% for three different bidders in the same period of the previous year. Two bidders merged at the end of 2013 and have been combined to determine the percentages above.

The working capital balance at March 31, 2014 (consisting of current assets less current liabilities) improved \$0.3 million from December 31, 2013 primarily due to an increase in cash and cash equivalents. Stockholders' equity decreased 1% for the three months ended March 31, 2014 due to a \$0.5 million net loss, partially offset by share-based compensation and proceeds from the exercise of stock options.

Cash provided by operating activities for the three months ended March 31, 2014 was approximately \$0.9 million compared to \$0.7 million for the three months ended March 31, 2013. The 2014 increase was primarily due to an increase of approximately \$0.4 million in EBITDA. Cash used in investing activities for the three months ended March 31, 2014 was approximately \$0.1 million which was substantially offset by cash provided by financing activities of approximately \$0.1 million. Cash used in financing activities for the three months ended March 31, 2013 was \$1.9 million, primarily resulting from a \$1.4 million payment of contingent consideration and \$0.5 million of principal payments on long term debt.

EBITDA, representing net loss before interest, income taxes, depreciation and amortization for the three months ended March 31, 2014 was \$0.8 million as compared to \$0.4 million for the same period in the prior year. Please refer to the section below discussing non-GAAP financial measures for a reconciliation of non-GAAP measures to the most directly comparable measure calculated and presented in accordance with accounting principles generally accepted in the United States of America ("GAAP").

In this Quarterly Report on Form 10-Q, we provide certain "non-GAAP financial measures". A non-GAAP financial measure refers to a numerical financial measure that excludes (or includes) amounts that are included in (or excluded from) the most directly comparable financial measure calculated and presented in accordance with GAAP in our financial statements. In this Quarterly Report on Form 10-Q, we provide EBITDA and adjusted EBITDA as additional information relating to our operating results. These non-GAAP measures exclude expenses related to share-based compensation, depreciation related to our fixed assets, amortization expense related to acquisition-related assets and other assets, interest expense on bank borrowings, notes payable to sellers and contingent consideration, interest income on invested funds, and income taxes. Management uses these non-GAAP measures for internal reporting and bank reporting purposes. We have provided these non-GAAP financial measures in addition to GAAP financial results because we believe that these non-GAAP financial measures provide useful information to certain investors and financial analysts in assessing our operating performance due to the following factors:

- We believe that the presentation of a non-GAAP measure that adjusts for the impact of share-based compensation expenses, depreciation of fixed assets, amortization expense related to acquisition-related assets and other assets, interest expense on bank borrowings, seller notes and contingent consideration, interest income on invested funds, and income taxes, provides investors and financial analysts with a consistent basis for comparison across accounting periods and, therefore, is useful to investors and financial analysts in helping them to better understand our operating results and underlying operational trends;
- Although share-based compensation is an important aspect of the compensation of our employees and executives, share-based compensation expense is generally fixed at the time of grant, then amortized over a period of several years after the grant of the share-based instrument, and generally cannot be changed or influenced by management after the grant;
- We do not acquire intangible assets on a predictable cycle. Our intangible assets relate solely to business acquisitions. Amortization costs are fixed at the time of an acquisition, are then amortized over a period of several years after the acquisition and generally cannot be changed or influenced by management after the acquisition;
- We do not regularly incur capitalized software and website costs. Our capitalized software costs relate primarily to the build-out of our exchanges. Amortization costs are fixed at the time the costs are incurred and are then amortized over a period of several years and generally cannot be changed or influenced by management after the initial costs are incurred;
- We do not regularly invest in fixed assets. Our fixed assets relate primarily to computer and office equipment and furniture and fixtures. Depreciation costs are fixed at the time of purchase and are then depreciated over several years and generally cannot be changed or influenced by management after the purchase;
- We do not regularly enter into bank debt, seller notes and/or pay interest on contingent consideration. Our seller notes and contingent consideration relate to acquisition activities. Interest expense is fixed at the time of purchase and recorded over the life of the lease and generally cannot be changed or influenced by management after the purchase;
- We do not regularly earn interest on our cash accounts. Our cash is invested in U.S. Treasury funds and has not yielded material returns to date and these returns generally cannot be changed or influenced by management; and

- We do not regularly pay federal or state income taxes due to our net operating loss carryforwards. Our income tax expense reflects the release of our deferred tax assets to apply to projected annualized taxable income, and an anticipated alternative minimum tax liability based on statutory rates that generally cannot be changed or influenced by management.

Pursuant to the requirements of the SEC, we have provided below a reconciliation of the non-GAAP financial measures used to the most directly comparable financial measures prepared in accordance with GAAP. These non-GAAP financial measures are not prepared in accordance with GAAP. These measures may differ from the GAAP information, even where similarly titled used by other companies, and therefore should not be used to compare our performance to that of other companies. The presentation of this additional information is not meant to be considered in isolation or as a substitute for net income prepared in accordance with GAAP.

|                                   | Three Months Ended March 31, |              |
|-----------------------------------|------------------------------|--------------|
|                                   | 2014                         | 2013         |
| GAAP net loss                     | \$ (497,780)                 | \$ (956,885) |
| Add: Interest expense, net        | 200,397                      | 202,737      |
| Add: Income taxes                 | 63,000                       | 131,305      |
| Add: Amortization of intangibles  | 926,645                      | 974,758      |
| Add: Amortization of other assets | 13,565                       | 8,507        |
| Add: Depreciation                 | 52,911                       | 55,669       |
| Non-GAAP EBITDA                   | \$ 758,738                   | \$ 416,091   |
| Add: Stock-based compensation     | 161,903                      | 145,986      |
| Non-GAAP adjusted EBITDA          | \$ 920,641                   | \$ 562,077   |

#### **Critical Accounting Policies**

The preparation of financial statements in conformity with GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Accordingly, actual results could differ from these estimates.

The most judgmental estimates affecting our consolidated financial statements are those relating to revenue recognition and the estimate of actual energy delivered from the bidder to the lister of such energy; stock-based compensation; the valuation of intangible assets and goodwill; the valuation of contingent consideration; impairment of long-lived assets; and estimates of future taxable income as it relates to the realization of our net deferred tax assets. We regularly evaluate our estimates and assumptions based upon historical experience and various other factors that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. To the extent actual results differ from those estimates; future results of operations may be affected. We believe the following critical accounting policies affect our more significant judgments and estimates used in the preparation of our accompanying consolidated financial statements. Refer to Note 2 of our consolidated financial statements within our Annual Report on Form 10-K as filed with the SEC on March 31, 2014 for a description of our accounting policies.

#### **Off-Balance Sheet Arrangements**

We currently have no off-balance sheet arrangements that have or are reasonably likely to have a current or future material effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

#### **Item 3. Quantitative and Qualitative Disclosure about Market Risk**

As a smaller reporting company as defined by Rule 12b-2 of the Exchange Act and in Item 10(f)(1) of Regulation S-K, we are electing scaled disclosure reporting obligations and therefore are not required to provide the information requested by this Item.

#### **Item 4. Controls and Procedures**

##### **Evaluation of Disclosure Controls and Procedures**

As required by Rule 13a-15 under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), the Company carried out an evaluation under the supervision and with the participation of the Company's management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the Company's disclosure controls and procedures as of December 31, 2013. In designing and evaluating the Company's disclosure controls and procedures, the Company and its management recognize

that there are inherent limitations to the effectiveness of any system of disclosure controls and procedures, including the possibility of human error and the circumvention or overriding of the controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their desired control objectives. Additionally, in evaluating and implementing possible controls and procedures, the Company's management was required to apply its reasonable judgment. Based upon the required evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that as of March 31, 2014, the Company's disclosure controls and procedures were effective at the reasonable assurance level to ensure that information required to be disclosed by the Company in the reports it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and procedures also were effective in ensuring that information required to be disclosed by the Company in the reports it files or submits under the Exchange Act is accumulated and communicated to its management, including the Company's Chief Executive Officer and Chief Financial Officer as appropriate, to allow timely decisions regarding required disclosure.

#### Changes in Internal Control Over Financial Reporting

There was no change in the Company's internal control over financial reporting that occurred during the three months ended March 31, 2014 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

## PART II OTHER INFORMATION

### Item 1. Legal Proceedings

Two former employees/consultants of GSE have filed two separate complaints in Texas County Court alleging, among other things, claims related to breach of contract, quantum meruit, promissory estoppel, and tortious interference. Each plaintiff claims that GSE and/or we failed to pay commissions due for services that they provided prior to the date of our purchase of certain GSE assets, based on their respective employment or independent contractor agreements with GSE. Each plaintiff has also asserted claims for recovery of their attorneys' fees. We deny the allegations and have filed counterclaims for damages, asserting claims for conversion, unjust enrichment, misappropriation of confidential information, and violation of the Texas Theft Liability Act against each of the plaintiffs. We have also filed a counterclaim against one of the plaintiffs for her breach of a non-competition and non-solicitation agreement, based on her working for a competitor of ours during her one-year restrictive period and her improper solicitation of former GSE customers on behalf of the competitor. The plaintiffs have also asserted claims against the GSE affiliates and their individual principals. The court has assigned a trial date of September 29, 2014 for one of the cases. The remaining case is awaiting assignment of a trial date. Our motion for summary judgment seeking dismissal of all claims against one of the two plaintiffs has been denied. Our motion for summary judgment against the other plaintiff has been filed and is awaiting oral argument.

We have estimated the potential commissions allegedly due to the two plaintiffs to be approximately \$0.3 million. We have not recorded any accrual for contingent liabilities associated with these legal proceedings based on its belief that any potential loss, while reasonably possible, is not probable. We intend to continue to defend these actions vigorously and are currently unable to estimate a range of payments, if any, we may be required to pay, with respect to these claims. Further, we believe that the resolution of these matters will not result in a material effect to our condensed consolidated financial statements. However, due to uncertainties that accompany litigation of this nature, there could be no assurance that we will be successful, and the resolution of the lawsuits could have a material effect on our accompanying condensed consolidated financial statements.

In addition, we had filed cross claims against GSE for indemnification under the Asset Purchase Agreement in each of the plaintiffs' cases. The GSE affiliates and principals had also asserted cross claims against us seeking indemnification under the Asset Purchase Agreement. In December 2013, GSE had amended its cross claims in one of the matters to include claims asserting breach of the earnout provisions in the Asset Purchase Agreement. Subsequent to quarter end, GSE and we settled all claims against each other related to these lawsuits and the earnout provisions and filed with the court agreed motions to dismiss all claims against one another. The settlement calls for us to issue 200,000 shares of common stock to GSE and its affiliates that had a fair value of \$0.9 million on the date issued. This amount is reflected as a current liability in accrued contingent consideration as of March 31, 2014.

From time to time, we may be subject to legal proceedings and claims arising from the conduct of its business operations, including litigation related to employment matters. While it is impossible to ascertain the ultimate legal and financial liability with respect to contingent liabilities, including lawsuits, we believe that the aggregate amount of such liabilities, if any, will not have a material adverse effect on our condensed consolidated financial position and/or results of operations. It is possible, however, that future financial position or results of operations for any particular period could be materially affected by changes in our assumptions or strategies related to those contingencies or changes out of our control.

### Item 1A. Risk Factors

There have been no material changes from risk factors previously disclosed in our annual report on Form 10-K for the fiscal year ended December 31, 2013, as filed with the Securities and Exchange Commission on March 31, 2014.

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

#### Recent Sales of Unregistered Securities; Use of Proceeds from Registered Securities

During the quarter ended March 31, 2014, we did not sell any unregistered equity securities.

#### Purchases of Equity Securities by the Issuer and Affiliated Purchasers

In connection with the vesting of restricted stock granted to employees, we withheld certain shares with value equivalent to employees' minimum statutory obligations for the applicable income and other employment taxes.

A summary of the shares withheld to satisfy employee tax withholding obligations for the three months ended March 31, 2014 is as follows:

| Period              | Total Number<br>of<br>Shares<br>Purchased | Average Price<br>Paid<br>Per Share | Total Number<br>of<br>Shares<br>Purchased<br>As Part of<br>Publicly<br>Announced<br>Plans or<br>Programs | Maximum<br>Number<br>of Shares That<br>May<br>Yet Be<br>Purchased<br>Under The Plan |
|---------------------|---|------------------------------------|--|---|
| 01/01/14 - 01/31/14 | —   | \$ —                               | —  | —   |
| 02/01/14 - 02/28/14 | —   | \$ —                               | —  | —   |
| 03/01/14 - 03/31/14 | 38  | \$ 4.96                            | —  | —   |
| Total               | 38  | \$ 4.96                            | —  | —   |

### Item 3. Defaults Upon Senior Securities

None.

### Item 4. Mine Safety Disclosures (not applicable)

None.

### Item 5. Other Information

None.

### Item 6. Exhibits

- 31.1 Certification of the Chief Executive Officer pursuant to §302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of the Chief Financial Officer pursuant to §302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of the Chief Executive Officer pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of the Chief Financial Officer pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002.
- 101 The following materials from World Energy Solutions, Inc.'s Quarterly Report on Form 10-Q for the three months ended March 31, 2014, formatted in Extensible Business Reporting Language: (i) the condensed consolidated balance sheets; (ii) the condensed consolidated statements of operations; (iii) the condensed consolidated statements of cash flows; and (iv) notes to the condensed consolidated financial statements.

## SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

World Energy Solutions, Inc.

Dated: May 8, 2014

By: /s/ Philip Adams  
Philip Adams  
Chief Executive Officer

Dated: May 8, 2014

By: /s/ James Parslow  
James Parslow  
Chief Financial Officer

**CERTIFICATION OF THE CHIEF EXECUTIVE OFFICER PURSUANT TO  
§302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Philip Adams, certify that:

1. I have reviewed this quarterly report on Form 10-Q of World Energy Solutions, Inc. (the "Registrant");

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

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

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

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

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

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

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

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

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

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

Dated: May 8, 2014

By: /s/ Philip Adams  
Philip Adams  
Chief Executive Officer

**CERTIFICATION OF THE CHIEF FINANCIAL OFFICER PURSUANT TO  
§302 OF THE SARBANES-OXLEY ACT OF 2002**

I, James Parslow, certify that:

1. I have reviewed this quarterly report on Form 10-Q of World Energy Solutions, Inc. (the "Registrant");
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this report;
4. The Registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the Registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the Registrant's internal control over financial reporting that occurred during the Registrant's most recent fiscal quarter (the Registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the Registrant's internal control over financial reporting;
5. The Registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant's auditors and the audit committee of the Registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant's internal control over financial reporting.

Dated: May 8, 2014

By: /s/ James Parslow

James Parslow  
Chief Financial Officer



**CERTIFICATION PURSUANT TO 18 U.S.C. §1350, AS ADOPTED  
PURSUANT TO §906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the filing of this quarterly report of World Energy Solutions, Inc. (the "Company") on Form 10-Q (the "Report") for the period ended March 31, 2014 as filed with the Securities and Exchange Commission on the date hereof, I, Philip Adams, Chief Executive Officer of the Company, certify, to the best of my knowledge, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: May 8, 2014

By: /s/ Philip Adams  
Philip Adams  
Chief Executive Officer

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

**CERTIFICATION PURSUANT TO 18 U.S.C. §1350, AS ADOPTED  
PURSUANT TO §906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the filing of this quarterly report of World Energy Solutions, Inc. (the "Company") on Form 10-Q (the "Report") for the period ended March 31, 2014 as filed with the Securities and Exchange Commission on the date hereof, I, James Parslow, Chief Financial Officer of the Company, certify that, to the best of my knowledge, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: May 8, 2014

By: /s/ James Parslow

James Parslow  
Chief Financial Officer

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

# WORLD ENERGY SOLUTIONS, INC.

## FORM 10-Q (Quarterly Report)

Filed 08/08/14 for the Period Ending 06/30/14

|             |  |
|-------------|--|
| Address     | 100 FRONT STREET<br>WORCESTER, MA 01608            |
| Telephone   | 508-459-8100                                       |
| CIK         | 0001371781   |
| Symbol      | XWES   |
| SIC Code    | 7389 - Business Services, Not Elsewhere Classified |
| Industry    | Investment Services                                |
| Sector      | Financial  |
| Fiscal Year | 12/31  |

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

**FORM 10-Q**

- ☒ Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 For the quarterly period ended June 30, 2014; or
- ☐ Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number: 001-34289

**World Energy Solutions, Inc.**

(Exact name of registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of incorporation or organization)

**04-3474959**

(I.R.S. Employer Identification Number)

**100 Front Street**

**Worcester, Massachusetts 01608**

(Address of principal executive offices)

**508-459-8100**

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically 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 (§232.405 of this chapter) 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 whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☐

Accelerated filer ☐

Non-accelerated filer ☐

Smaller reporting company ☒

(Do not check if a smaller reporting company)

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

As of August 1, 2014, the registrant had 12,740,139 shares of common stock outstanding.

## TABLE OF CONTENTS

|   | <u>Page</u> |
|---|-------------|
| <b>PART I. Financial Information</b>  |             |
| Item 1. Financial Statements (Unaudited)  | 2           |
| Condensed Consolidated Balance Sheets as of June 30, 2014 and December 31, 2013                           | 2           |
| Condensed Consolidated Statements of Operations for the Three and Six Months Ended June 30, 2014 and 2013 | 3           |
| Condensed Consolidated Statements of Cash Flows for the Six Months Ended June 30, 2014 and 2013           | 4           |
| Notes to Condensed Consolidated Financial Statements  | 5           |
| Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations             | 13          |
| Item 3. Quantitative and Qualitative Disclosure about Market Risk   | 23          |
| Item 4. Controls and Procedures   | 23          |
| <br><b>PART II. Other Information</b>   |             |
| Item 1. Legal Proceedings   | 24          |
| Item 1A. Risk Factors   | 24          |
| Item 2. Unregistered Sales of Equity Securities and Use of Proceeds                                       | 24          |
| Item 3. Defaults Upon Senior Securities   | 25          |
| Item 4. Mine Safety Disclosures   | 25          |
| Item 5. Other Information   | 25          |
| Item 6. Exhibits  | 25          |

---

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

**Item 1. Financial Statements**

**WORLD ENERGY SOLUTIONS, INC.**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**

|  | June 30,<br>2014     | December 31,<br>2013 |
|--|----------------------|----------------------|
|  | (Unaudited)          |                      |
| <b>ASSETS</b>  |                      |                      |
| Current assets:  |                      |                      |
| Cash and cash equivalents  | \$ 2,290,370         | \$ 1,725,136         |
| Trade accounts receivable, net   | 7,205,500            | 7,738,141            |
| Inventory  | 666,051              | 415,770              |
| Current portion of deferred tax asset  | 906,350              | 901,350              |
| Prepaid expenses and other current assets  | 636,744              | 477,406              |
| Total current assets   | 11,705,015           | 11,257,803           |
| Property and equipment, net  | 516,094              | 573,778              |
| Intangible assets, net   | 13,422,620           | 15,193,965           |
| Goodwill   | 16,167,834           | 16,167,834           |
| Deferred tax asset, net of current portion   | 7,230,984            | 7,198,984            |
| Other assets, net  | 842,355              | 687,098              |
| Total assets   | <u>\$ 49,884,902</u> | <u>\$ 51,079,462</u> |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>  |                      |                      |
| Current liabilities:   |                      |                      |
| Accounts payable   | \$ 1,174,136         | \$ 1,697,798         |
| Accrued commissions  | 1,673,685            | 1,567,839            |
| Accrued compensation   | 1,963,304            | 2,119,784            |
| Accrued contingent consideration   | —                    | 1,000,000            |
| Accrued expenses and other current liabilities   | 783,302              | 1,242,274            |
| Deferred revenue and customer advances   | 3,997,901            | 3,546,380            |
| Related party subordinated notes payable   | —                    | 500,000              |
| Current portion of long-term debt  | 1,035,939            | 477,712              |
| Total current liabilities  | 10,628,267           | 12,151,787           |
| Long-term debt, net of current portion   | 4,964,061            | 5,522,288            |
| Subordinated note payable  | 4,000,000            | 4,000,000            |
| Deferred revenue and customer advances, net of current portion   | 3,521,338            | 3,910,035            |
| Other liabilities  | 12,734               | 14,768               |
| Total liabilities  | 23,126,400           | 25,598,878           |
| Commitments and contingencies (Note 12)  |                      |                      |
| Stockholders' equity:  |                      |                      |
| Preferred stock, \$0.0001 par value; 5,000,000 shares authorized, no shares issued or outstanding  | —                    | —                    |
| Common stock, \$0.0001 par value; 30,000,000 shares authorized; 12,473,960 shares issued and 12,411,163 shares outstanding at June 30, 2014, and 12,178,366 shares issued and 12,120,338 shares outstanding at December 31, 2013 | 1,241                | 1,212                |
| Additional paid-in capital   | 46,384,524           | 44,894,961           |
| Accumulated deficit  | (19,348,420)         | (19,156,245)         |
| Treasury stock, at cost; 62,797 shares at June 30, 2014 and 58,028 shares at December 31, 2013   | (278,843)            | (259,344)            |
| Total stockholders' equity   | 26,758,502           | 25,480,584           |
| Total liabilities and stockholders' equity   | <u>\$ 49,884,902</u> | <u>\$ 51,079,462</u> |

See accompanying notes to condensed consolidated financial statements.

**WORLD ENERGY SOLUTIONS, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
(Unaudited)

|   | Three Months Ended June 30, |                | Six Months Ended June 30, |                |
|---|-----------------------------|----------------|---------------------------|----------------|
|   | 2014                        | 2013           | 2014                      | 2013           |
| <b>Revenue</b>  |                             |                |                           |                |
| Brokerage commissions, transaction fees and efficiency projects | \$ 9,214,613                | \$ 7,744,234   | \$ 18,552,778             | \$ 16,215,193  |
| Management fees   | 178,423                     | 191,423        | 360,612                   | 377,946        |
| Total revenue   | 9,393,036                   | 7,935,657      | 18,913,390                | 16,593,139     |
| <b>Cost of revenue</b>  | 2,119,806                   | 2,144,455      | 4,432,119                 | 4,377,606      |
| Gross profit  | 7,273,230                   | 5,791,202      | 14,481,271                | 12,215,533     |
| <b>Operating expenses</b>                                       |                             |                |                           |                |
| Sales and marketing   | 4,633,760                   | 4,890,347      | 9,395,751                 | 9,868,428      |
| General and administrative                                      | 2,228,641                   | 2,167,021      | 4,913,114                 | 4,228,694      |
| Total operating expenses  | 6,862,401                   | 7,057,368      | 14,308,865                | 14,097,122     |
| Operating income (loss)   | 410,829                     | (1,266,166)    | 172,406                   | (1,881,589)    |
| Interest expense, net   | (197,899)                   | (277,397)      | (398,296)                 | (480,134)      |
| Other income  | 4,672                       | 20,713         | 8,715                     | 13,293         |
| Income (loss) before income taxes                               | 217,602                     | (1,522,850)    | (217,175)                 | (2,348,430)    |
| Income tax benefit (expense)                                    | 88,000                      | (131,305)      | 25,000                    | (262,610)      |
| Net income (loss)   | \$ 305,602                  | \$ (1,654,155) | \$ (192,175)              | \$ (2,611,040) |
| Net income (loss) per common share — basic                      | \$ 0.02                     | \$ (0.14)      | \$ (0.02)                 | \$ (0.22)      |
| Net income (loss) per common share — diluted                    | \$ 0.02                     | \$ (0.14)      | \$ (0.02)                 | \$ (0.22)      |
| Weighted average shares outstanding — basic                     | 12,369,034                  | 11,982,656     | 12,252,044                | 11,974,428     |
| Weighted average shares outstanding — diluted                   | 12,518,390                  | 11,982,656     | 12,252,044                | 11,974,428     |

See accompanying notes to condensed consolidated financial statements.

**WORLD ENERGY SOLUTIONS, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(Unaudited)

|  | <b>Six Months Ended June 30,</b> |                     |
|--|----------------------------------|---------------------|
|  | <b>2014</b>                      | <b>2013</b>         |
| <b>Cash flows from operating activities:</b>   |                                  |                     |
| Net loss   | \$ (192,175)                     | \$ (2,611,040)      |
| <b>Adjustments to reconcile net loss to net cash provided by operating activities:</b> |                                  |                     |
| Depreciation and amortization  | 1,902,353                        | 2,077,268           |
| Deferred income taxes  | (37,000)                         | 220,610             |
| Stock-based compensation   | 352,664                          | 292,309             |
| Loss on disposal of property and equipment   | 4,698                            | 11,177              |
| Non-cash interest expense on warrants related to debt discount                         | —                                | 19,937              |
| Interest on accrued contingent consideration   | —                                | 19,836              |
| <b>Changes in operating assets and liabilities:</b>                                    |                                  |                     |
| Trade accounts receivable, net   | 532,641                          | 237,001             |
| Inventory  | (250,281)                        | (300,358)           |
| Prepaid expenses and other current assets  | (102,664)                        | (320,987)           |
| Accounts payable   | (523,662)                        | 659,647             |
| Accrued commissions  | 105,846                          | 390,330             |
| Accrued compensation   | (156,480)                        | (249,428)           |
| Accrued contingent consideration   | (72,000)                         | (188,000)           |
| Accrued expenses and other current liabilities   | (458,972)                        | (687,756)           |
| Deferred revenue and customer advances   | 62,824                           | 1,676,579           |
| <b>Net cash provided by operating activities</b>                                       | <b>1,167,792</b>                 | <b>1,247,125</b>    |
| <b>Cash flows from investing activities:</b>   |                                  |                     |
| (Increase) decrease in other assets  | (181,269)                        | 72,699              |
| Purchases of property and equipment, net of disposals                                  | (52,010)                         | (65,489)            |
| <b>Net cash (used in) provided by investing activities</b>                             | <b>(233,279)</b>                 | <b>7,210</b>        |
| <b>Cash flows from financing activities:</b>   |                                  |                     |
| Proceeds from exercise of stock options  | 152,254                          | 107,814             |
| Purchase of treasury stock   | (19,499)                         | (34,575)            |
| Principal payments on long-term debt   | —                                | (1,000,000)         |
| Principal payments on notes payable  | (500,000)                        | —                   |
| Payments of contingent consideration   | —                                | (1,435,548)         |
| Principal payments on capital lease obligations  | (2,034)                          | (8,370)             |
| <b>Net cash used in financing activities</b>   | <b>(369,279)</b>                 | <b>(2,370,679)</b>  |
| <b>Net increase (decrease) in cash and cash equivalents</b>                            | <b>565,234</b>                   | <b>(1,116,344)</b>  |
| Cash and cash equivalents, beginning of period   | 1,725,136                        | 3,307,822           |
| <b>Cash and cash equivalents, end of period</b>  | <b>\$ 2,290,370</b>              | <b>\$ 2,191,478</b> |
| <b>Supplemental Disclosure of Cash Flow Information:</b>                               |                                  |                     |
| Net cash paid for interest   | \$ 424,561                       | \$ 480,623          |
| Net cash paid for income taxes   | \$ 15,190                        | \$ 98,050           |
| <b>Non-cash activities:</b>  |                                  |                     |
| Contingent consideration settled with common stock                                     | \$ 928,000                       | \$ —                |
| Equipment acquired under capital leases  | \$ —                             | \$ 21,416           |

See accompanying notes to condensed consolidated financial statements.



**WORLD ENERGY SOLUTIONS, INC.**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(Unaudited)**

**June 30, 2014**

**1. Nature of Business and Basis of Presentation**

World Energy Solutions, Inc. ("World Energy" or the "Company") offers a range of energy management solutions to commercial and industrial businesses, institutions, utilities, and governments to reduce their overall energy costs. The Company comes to market with a holistic approach to energy management helping customers a) contract for a competitive price for energy, b) engage in energy efficiency projects to minimize quantity used and c) pursue available rebate and incentive programs. The Company made its mark on the industry with an innovative approach to procurement via its online auction platform, the World Energy Exchange<sup>®</sup>. With recent investments and acquisitions, World Energy is building out its energy efficiency practice engaging new customers while also pursuing more cross-selling opportunities for its procurement services.

**2. Interim Financial Statements**

The December 31, 2013 condensed consolidated balance sheet has been derived from audited consolidated financial statements and the accompanying June 30, 2014 unaudited interim condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC") regarding interim reporting. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America ("GAAP") for complete financial statements and should be read in conjunction with the audited consolidated financial statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2013, as filed with the SEC on March 31, 2014.

In the opinion of the Company's management, the unaudited interim condensed consolidated financial statements have been prepared on the same basis as the audited consolidated financial statements and include all adjustments consisting of normal recurring adjustments and accruals necessary for the fair presentation of the Company's financial position as of June 30, 2014, the results of its operations for the three and six months ended June 30, 2014 and 2013 and the results of its cash flows for the six months ended June 30, 2014 and 2013, respectively.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Accordingly, actual results could differ from these estimates.

The Company's most judgmental estimates affecting its condensed consolidated financial statements are those relating to revenue recognition and the estimate of actual energy delivered from the bidder to the lister of such energy; stock-based compensation; the valuation of intangible assets and goodwill; the valuation of contingent consideration; impairment of long-lived assets; and estimates of future taxable income as it relates to the realization of our net deferred tax assets. The Company regularly evaluates its estimates and assumptions based upon historical experience and various other factors that the Company believes to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. To the extent actual results differ from those estimates, future results of operations may be affected.

**3. Income (Loss) Per Share**

As of June 30, 2014 and 2013, the Company only had one issued and outstanding class of stock – common stock. The basic income (loss) per share for the three and six months ended June 30, 2014 and 2013 is computed by dividing net income (loss) by the weighted average number of shares outstanding for the period. The diluted income (loss) per share for the three and six months ended June 30, 2014 and 2013 is calculated by dividing the net income (loss) by the weighted average number of common shares outstanding for the period plus the amounts representing the dilutive effect of common stock options, common stock warrants and restricted stock that would be issuable upon conversion, exercise, or contingent exercise.

The following table provides a reconciliation of the denominators of the Company's reported basic and diluted earnings per share computation for the three and six months ended June 30, 2014 and 2013, respectively:

|  | For the three months ended<br>June 30, |            | For the six months ended<br>June 30, |            |
|--|--|------------|--------------------------------------|------------|
|  | 2014                                   | 2013       | 2014                                 | 2013       |
| Weighted number of common shares - basic                         | 12,369,034                             | 11,982,656 | 12,252,044                           | 11,974,428 |
| Common stock equivalents   | 149,356                                | —          | —                                    | —          |
| Weighted number of common and common equivalent shares - diluted | 12,518,390                             | 11,982,656 | 12,252,044                           | 11,974,428 |

As the Company was in a net loss position for the three months ended June 30, 2013 and the six months ended June 30, 2014 and 2013, the computed diluted loss per share does not assume conversion, exercise, or contingent exercise of securities as that would have an anti-dilutive effect on the loss per share in those periods.

For the three months ended June 30, 2014, 373,000 and 45,045 shares issuable relative to common stock options and common stock warrants, respectively, were excluded from net income (loss) per share since the inclusion of such shares would be anti-dilutive. For the six months ended June 30, 2014, 674,867, 49,545 and 251,750 shares issuable relative to common stock options, common stock warrants and restricted stock, respectively, were excluded from net loss per share since the inclusion of such shares would be anti-dilutive. For the three and six months ended June 30, 2013, 770,714, 49,545, and 122,000 shares issuable relative to common stock options, common stock warrants and restricted stock, respectively, were excluded from net loss per share since the inclusion of such shares would be anti-dilutive. The Company did not declare or pay any dividends in 2014 or 2013.

#### 4. Concentration of Credit Risk and Off-Balance Sheet Risk

Financial instruments that potentially expose the Company to concentrations of credit risk consist principally of cash and cash equivalents and trade accounts receivable. The Company has no material off-balance sheet risk such as foreign exchange contracts, option contracts, or other foreign hedging arrangements. The Company places its cash and cash equivalents with two institutions, which management believes are of high credit quality. As of June 30, 2014, all of the Company's cash and cash equivalents are held in interest bearing accounts.

The Company provides credit in the form of invoiced and unbilled accounts receivable in the normal course of business. Collateral is not required for trade accounts receivable, but ongoing credit evaluations are performed. While the majority of the Company's revenue is generated from retail energy transactions where the winning bidder pays a commission to the Company, commission payments for certain auctions can be paid by the lister, bidder or a combination of both.

The following represents revenue and trade accounts receivable from bidders exceeding 10% of the total in each category:

| Bidder | Revenue for the three<br>months ended June 30, |      | Revenue for the six<br>months ended June 30, |      | Trade Accounts<br>Receivable as of June 30, |      |
|--------|--|------|--|------|---|------|
|        | 2014   | 2013 | 2014   | 2013 | 2014  | 2013 |
| A      | 12%  | 18%  | 15%  | 17%  | 21%   | 17%  |
| B      | 13%  | 12%  | 11%  | 11%  | 13%   | 13%  |
| C      | 7%   | 9%   | 7%   | 9%   | 11%   | 10%  |

Two bidders merged at the end of 2013 and have been combined for presentation purposes above. In addition to its direct relationship with bidders, the Company also has direct contractual relationships with listers for the online procurement of certain of their energy, demand response or environmental needs. These listers are primarily large businesses and government organizations and do not have a direct creditor relationship with the Company. For the three and six months ended June 30, 2014 and 2013, no lister represented more than 10% individually of the Company's aggregate revenue.

## 5. Trade Accounts Receivable, Net

The Company does not invoice bidders for the commissions earned on retail electricity, certain natural gas and demand response transactions and, therefore, reports a significant portion of its receivables as "unbilled." Unbilled accounts receivable represent management's best estimate of energy provided by the energy suppliers to the energy consumers for a specific completed time period at contracted commission rates.

The Company does invoice bidders for commissions earned on wholesale, a substantial portion of retail natural gas and energy efficiency transactions, which are reflected as billed accounts receivable. For natural gas and wholesale transactions, the total commission earned on these transactions is recognized upon completion of the procurement event and are generally due within 30 days of invoice date. For efficiency projects, revenue is recognized and invoiced upon project installation and acceptance, as required, and are generally due within 30 days of invoice date. In addition, the Company invoices the bidder, lister or combination of both for certain auctions performed for environmental commodity product transactions. These transactions are earned and invoiced either upon lister acceptance of the auction results or, in some cases, upon delivery of the credits or cash settlement of the transaction. Management provides for an allowance for doubtful accounts on a specifically identified basis, as well as through historical experience applied to an aging of accounts, if necessary. Trade accounts receivable are written off when deemed uncollectible. To date, write-offs have not been material. Trade accounts receivable, net consists of the following:

|                                 | June 30, 2014       | December 31, 2013   |
|---------------------------------|---------------------|---------------------|
| Unbilled accounts receivable    | \$ 6,517,791        | \$ 6,070,227        |
| Billed accounts receivable      | 1,187,888           | 1,993,093           |
|                                 | <u>7,705,679</u>    | <u>8,063,320</u>    |
| Allowance for doubtful accounts | (500,179)           | (325,179)           |
| Trade accounts receivable, net  | <u>\$ 7,205,500</u> | <u>\$ 7,738,141</u> |

## 6. Inventory

Inventory is maintained in the Company's Energy efficiency services segment and consists of prepaid expendables and project materials. Prepaid expendables represents consumable components that are used in project installations and are stated at the lower of cost or market, with cost being determined on a first-in, first-out (FIFO) basis. Historical inventory usage and current trends are considered in estimating both excess and obsolete inventory. To date, there have been no material write-downs of inventory and therefore no allowance for excess or obsolete inventory was recorded at June 30, 2014 or December 31, 2013. Project materials represent direct costs incurred on projects-in-process as of each reporting period. Inventory consists of the following:

|                     | June 30, 2014     | December 31, 2013 |
|---------------------|-------------------|-------------------|
| Prepaid expendables | \$ 46,556         | \$ 55,563         |
| Project materials   | 619,495           | 360,207           |
| Total inventory     | <u>\$ 666,051</u> | <u>\$ 415,770</u> |

## 7. Intangible Assets, Net

Intangibles, net with finite lives are summarized as follows as of June 30, 2014 and December 31, 2013:

|                        | Estimated Useful Life | June 30, 2014        |                          |                      | December 31, 2013    |                          |                      |
|------------------------|-----------------------|----------------------|--------------------------|----------------------|----------------------|--------------------------|----------------------|
|                        |                       | Carrying Amount      | Accumulated Amortization | Net                  | Carrying Amount      | Accumulated Amortization | Net                  |
| Customer contracts     | 1 - 4 years           | \$ 5,276,000         | \$ 3,687,000             | \$ 1,589,000         | \$ 5,276,000         | \$ 3,017,000             | \$ 2,259,000         |
| Customer relationships | 7 - 10 years          | 13,792,000           | 5,519,000                | 8,273,000            | 13,792,000           | 4,812,000                | 8,980,000            |
| Non-compete agreements | 5 years               | 2,585,000            | 1,220,000                | 1,365,000            | 2,585,000            | 962,000                  | 1,623,000            |
| Trade names            | 4 years               | 1,090,000            | 630,000                  | 460,000              | 1,090,000            | 494,000                  | 596,000              |
| Total                  |                       | <u>\$ 22,743,000</u> | <u>\$ 11,056,000</u>     | <u>\$ 11,687,000</u> | <u>\$ 22,743,000</u> | <u>\$ 9,285,000</u>      | <u>\$ 13,458,000</u> |

The Company also recorded acquisition related intangible assets with indefinite lives in the amount of \$1,736,000 pertaining to customer relationships, which is not reflected in the above tables.

Amortization expense was approximately \$1.8 million and \$2.0 million for the six months ended June 30, 2014 and 2013, respectively. The approximate future amortization expense of intangible assets is as follows:

|                     |                      |
|---------------------|----------------------|
| Remainder of 2014   | \$ 1,599,000         |
| 2015                | 2,801,000            |
| 2016                | 2,416,000            |
| 2017                | 1,273,000            |
| 2018                | 915,000              |
| 2019 and thereafter | 2,683,000            |
|                     | <u>\$ 11,687,000</u> |

#### 8. Deferred Revenue and Customer Advances

Deferred revenue and customer advances arise when energy suppliers pay the Company a commission prior to the Company meeting all the requirements necessary to recognize revenue. In addition, deferred revenue and customer advances includes cash received for Energy efficiency services projects that have not been completed. Deferred revenue and customer advances expected to be recognized as revenue by year are approximately as follows:

|  | Amount              |
|--|---------------------|
| Remainder of 2014                            | \$ 2,233,000        |
| 2015   | 3,432,000           |
| 2016   | 1,308,000           |
| 2017   | 334,000             |
| 2018 and thereafter                          | 212,000             |
| Total deferred revenue and customer advances | <u>\$ 7,519,000</u> |

The following table provides a rollforward of deferred revenue and customer advances:

|                            | Amount              |
|----------------------------|---------------------|
| Balance at January 1, 2014 | \$ 7,456,000        |
| Cash received              | 2,925,000           |
| Revenue recognized         | (2,862,000)         |
| Balance at June 30, 2014   | <u>\$ 7,519,000</u> |

#### 9. Segment Reporting

The Company operates its business based on two industry segments: Energy procurement and Energy efficiency services. The Company delivers its Energy procurement services to four markets: retail energy, wholesale energy, demand response and environmental commodity. The Energy procurement process is substantially the same regardless of the market being serviced and is supported by the same operations personnel utilizing the same basic technology and back office support. There is no discrete financial information for these product lines nor are there segment managers who have operating responsibility for each product line. Energy efficiency services focuses on turn-key electrical, mechanical and lighting energy efficiency measures servicing commercial, industrial and institutional customers.

Segment operating income represents income from operations, including share-based compensation, amortization of intangible assets and depreciation. The following tables present certain continuing operating division information in accordance with the provisions of Accounting Standards Codification ("ASC") 280, "Segment Reporting".

|  | For the three months ended June 30, |                       | For the six months ended June 30, |                       |
|--|-------------------------------------|-----------------------|-----------------------------------|-----------------------|
|  | 2014                                | 2013                  | 2014                              | 2013                  |
| <b>Consolidated revenue from external customers:</b>   |                                     |                       |                                   |                       |
| Energy procurement                                     | \$ 7,954,352                        | \$ 6,956,838          | \$ 15,923,997                     | \$ 14,377,997         |
| Energy efficiency services                             | 1,438,684                           | 978,819               | 2,989,393                         | 2,215,142             |
| Consolidated total revenue                             | <u>\$ 9,393,036</u>                 | <u>\$ 7,935,657</u>   | <u>\$ 18,913,390</u>              | <u>\$ 16,593,139</u>  |
| <b>Consolidated income (loss) before income taxes:</b> |                                     |                       |                                   |                       |
| Energy procurement                                     | \$ 452,621                          | \$ (1,173,962)        | \$ 297,240                        | \$ (1,799,501)        |
| Energy efficiency services                             | (235,019)                           | (348,888)             | (514,415)                         | (548,929)             |
| Consolidated income (loss) before income taxes         | <u>\$ 217,602</u>                   | <u>\$ (1,522,850)</u> | <u>\$ (217,175)</u>               | <u>\$ (2,348,430)</u> |

|                                    | For the three months ended June 30, |            | For the six months ended June 30, |              |
|------------------------------------|-------------------------------------|------------|-----------------------------------|--------------|
|                                    | 2014                                | 2013       | 2014                              | 2013         |
| <b>Energy Procurement:</b>         |                                     |            |                                   |              |
| Amortization                       | \$ 817,857                          | \$ 943,974 | \$ 1,718,778                      | \$ 1,887,950 |
| Depreciation                       | 45,314                              | 49,263     | 91,373                            | 97,827       |
| Interest expense, net              | 197,899                             | 1,277,397  | 439,826                           | 2,480,134    |
| <b>Energy Efficiency Services:</b> |                                     |            |                                   |              |
| Amortization                       | \$ 39,290                           | \$ 39,290  | \$ 78,579                         | \$ 78,579    |
| Depreciation                       | 6,771                               | 5,807      | 13,623                            | 12,912       |
| Interest expense, net              |                                     |            |                                   |              |

|                                   | June 30, 2014        | December 31, 2013    |
|-----------------------------------|----------------------|----------------------|
| <b>Consolidated total assets:</b> |                      |                      |
| Energy procurement                | \$ 44,317,053        | \$ 44,898,931        |
| Energy efficiency services        | 5,567,849            | 6,180,531            |
| Consolidated total assets         | <u>\$ 49,884,902</u> | <u>\$ 51,079,462</u> |

## 10. Income Taxes

In accordance with ASC 740, *Income Taxes*, each interim period is considered integral to the annual period and the tax benefit (expense) is measured using an estimated annual effective tax rate. An entity is required to record income tax provision each quarter based on its best estimate of the annual effective tax rate for the full fiscal year and use that rate to provide for income taxes on a current year-to-date basis, as adjusted for discrete taxable events that occur during the interim period. If, however, the entity is unable to reliably estimate its annual effective tax rate, then the actual effective tax rate for the year-to-date period may be the best annual effective tax rate estimate. For the six months ended June 30, 2014, the Company determined that it was unable to make a reliable estimate of the annual effective tax rate as relatively small changes in its projected income or loss produce significant variances in its annual effective tax rate. Therefore, the Company recorded a tax benefit in the amount of \$88,000 and \$25,000 for the three and six months ended June 30, 2014, respectively, based on the actual effective rate for the six months ended June 30, 2014. The effective tax rate for the three and six months ended June 30, 2013 was calculated based on an estimated annual effective tax rate resulting in an income tax expense of \$131,000 and \$263,000, respectively.

## 11. Fair Value Measurement and Fair Value of Financial Instruments

The Company follows ASC 820, "Fair Value Measurements and Disclosures" ("ASC 820") for fair value measurements. ASC 820 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. The standard provides a consistent definition of fair value, which focuses on an exit price, which is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The standard also prioritizes, within the measurement of fair value, the use of market-based information over entity specific information and establishes a three-level hierarchy for fair value measurements based on the nature of inputs used in the valuation of an asset or liability as of the measurement date.

The hierarchy established under ASC 820 gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3).

Level 1 - Pricing inputs are quoted prices available in active markets for identical investments as of the reporting date. As required by ASC 820, the Company does not adjust the quoted price for these investments, even in situations where the Company holds a large position and a sale could reasonably impact the quoted price.

Level 2 - Pricing inputs are quoted prices for similar investments, or inputs that are observable, either directly or indirectly, for substantially the full term through corroboration with observable market data. Level 2 includes investments valued at quoted prices adjusted for legal or contractual restrictions specific to these investments.

Level 3 - Pricing inputs are unobservable for the investment, that is, inputs that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability. Level 3 includes investments that are supported by little or no market activity.

As of June 30, 2014, the Company did not have any assets and liabilities measured at fair values on a recurring basis.

Assets and liabilities of the Company measured at fair values on a recurring basis as of December 31, 2013 are summarized as follows:

|                          | December 31,<br>2013 | Level 1     | Level 2     | Level 3             |
|--------------------------|----------------------|-------------|-------------|---------------------|
| <b>Liabilities</b>       |                      |             |             |                     |
| Contingent consideration | \$ 1,000,000         | \$ —        | \$ —        | \$ 1,000,000        |
| <b>Total liabilities</b> | <b>\$ 1,000,000</b>  | <b>\$ —</b> | <b>\$ —</b> | <b>\$ 1,000,000</b> |

The Company determines the fair value of acquisition-related contingent consideration based on assessment of the probability that the Company would be required to make such future payment. Changes to the fair value of contingent consideration are recorded in general and administrative expense. During the three months ended June 30, 2014, the Company settled its contingent consideration obligations. As part of the settlement, the Company issued 200,000 shares of common stock to GSE Consulting, L.P. ("GSE") that had a fair value of \$928,000 on the date of issuance.

The following table provides a rollforward of the fair value, as determined by Level 3 inputs, of the contingent consideration.

|   | For The Six Months<br>Ended June 30, 2014 |
|---|---|
| <b>Beginning balance</b>                  | <b>\$ 1,000,000</b>                       |
| Additions                                 | —   |
| Settlement                                | (928,000)                                 |
| Change in fair value included in earnings | (72,000)                                  |
| Accrued interest                          | —   |
| <b>Ending balance</b>                     | <b>\$ —</b>                               |

The carrying amounts and fair values of the Company's debt obligations are as follows

|  | June 30, 2014  |               | December 31, 2013 |               |
|--|----------------|---------------|-------------------|---------------|
|  | Carrying Value | Fair Value    | Carrying Value    | Fair Value    |
| Term loan                                | \$ 6,000,000   | \$ 6,000,000  | \$ 6,000,000      | \$ 6,000,000  |
| Subordinated notes payable               | 4,000,000      | 4,000,000     | 4,000,000         | 4,000,000     |
| Related party subordinated notes payable |                |               | 500,000           | 500,000       |
| Total debt obligations                   | \$ 10,000,000  | \$ 10,000,000 | \$ 10,500,000     | \$ 10,500,000 |

The carrying amount for fixed rate long-term debt and variable rate long-term debt approximate fair value because the underlying instruments are primarily at current market rates available to the Company for similar borrowings. The interest rate on the Commerce Bank and Trust Company ("Commerce") debt is tied to the prime rate and will fluctuate with changes in that rate. Related party notes payable are classified as short-term on the Company's accompanying condensed consolidated balance sheets.

## 12. Credit Arrangements

### Credit Facility

The Company has a \$8.5 million credit facility with Commerce consisting of a revolving credit facility of up to \$2.5 million (the "Revolver") that matures on December 30, 2016 and a 60-month term loan of \$6.0 million (the "Term Loan").

The Revolver bears interest at the prime rate plus 1.75% (totaling 5% at June 30, 2014) and is adjusted every six months for any change in the prime rate. In addition to changes in the Prime Rate, the rate can be reduced by up to .50% based on certain EBITDA achievement levels. Under the Revolver, the Company may borrow, repay and re-borrow an amount not to exceed the lesser of \$2.5 million or the total of 80% of eligible billed and unbilled accounts receivable (less the aggregate outstanding on any letters of credit). There have been no borrowings under the Revolver. The Term Loan bears interest for the first 6 months at the prime rate plus 2.75% (totaling 6% at June 30, 2014), and is adjusted every six months for any change in the prime rate. In addition to changes in the prime rate, the rate can be reduced by up to .50% based on certain EBITDA achievement levels. The Term Loan is interest only for six months followed by 54 monthly principal and interest payments commencing on July 30, 2014 with a balloon payment for any remaining principal balance at maturity.

### Subordinated Notes

On October 3, 2012, the Company entered into a Note Purchase Agreement with Massachusetts Capital Resource Company ("MCRC"), in which the Company entered into an 8-year, \$4.0 million Subordinated Note due September 30, 2020 with MCRC (the "MCRC Note"). The MCRC Note bears interest at 10.5% and is interest only for the first four years followed by 48 equal principal payments commencing October 31, 2016. The Company must pay a premium of 3% if it prepays the MCRC Note before October 1, 2014 and a 1% premium if it prepays the MCRC Note before October 1, 2015. The MCRC Note is subordinated to the Company's credit facility with Commerce and contains a Minimum Fixed Charge Ratio covenant that the Company is in compliance with at June 30, 2014.

### 13 . Commitments and Contingencies

#### Litigation

Two former employees/consultants of GSE have filed two separate complaints in the District Courts of Dallas County and Tarrant County Texas alleging, among other things, claims related to breach of contract, quantum meruit, promissory estoppel, tortious interference, and civil conspiracy. Each plaintiff claims that GSE and/or the Company failed to pay commissions due for services that they provided prior to the date of the Company's purchase of certain GSE assets, based on their respective employment or independent contractor agreements with GSE. Each plaintiff has also asserted claims for recovery of their attorneys' fees. The Company denies the allegations and has filed counterclaims for damages, asserting claims for conversion, unjust enrichment, misappropriation of confidential information, and violation of the Texas Theft Liability Act against each of the plaintiffs. The Company has also filed a counterclaim against one of the plaintiffs for her breach of a non-competition and non-solicitation agreement, based on her working for a competitor of the Company's during her one-year restrictive period and her improper solicitation of former GSE customers on behalf of the competitor. The plaintiffs have also asserted claims against the GSE affiliates and their individual principals. The Company's motions for summary judgment seeking dismissal of all of the plaintiff's claims was denied in its entirety in one of the cases. In the other case, the Company's motion for summary judgment was partially granted, dismissing the plaintiff's civil conspiracy claim. The courts have assigned trial dates of September 29, 2014 and November 17, 2014.

The Company has estimated the potential commissions allegedly due to the two plaintiffs to be approximately \$0.3 million. The Company has not recorded any accrual for contingent liabilities associated with these legal proceedings based on its belief that any potential loss, while reasonably possible, is not probable. The Company intends to continue to defend these actions vigorously and is currently unable to estimate a range of payments, if any, it may be required to pay, with respect to these claims. Further, the Company believes that the resolution of these matters will not result in a material effect to its condensed consolidated financial statements. However, due to uncertainties that accompany litigation of this nature, there could be no assurance that the Company will be successful, and the resolution of the lawsuits could have a material effect on its accompanying condensed consolidated financial statements.

In addition, the Company had filed cross claims against GSE for indemnification under the Asset Purchase Agreement in each of the plaintiffs' cases. The GSE affiliates and principals had also asserted cross claims against the Company seeking indemnification under the Asset Purchase Agreement. In December 2013, GSE had amended its cross claims in one of the matters to include claims asserting breach of the earnout provisions in the Asset Purchase Agreement. During the three months ended June 30, 2014, the Company and GSE settled all claims against each other related to these lawsuits and the earnout provisions. The Company and GSE filed with the court agreed motions to dismiss all claims against one another, which were allowed by the court. The settlement called for the Company to issue 200,000 shares of common stock to GSE and its affiliates that had a fair value of \$0.9 million on the date issued.

From time to time, the Company may be subject to legal proceedings and claims arising from the conduct of its business operations, including litigation related to employment matters. While it is impossible to ascertain the ultimate legal and financial liability with respect to contingent liabilities, including lawsuits, management believes that the aggregate amount of such liabilities, if any, will not have a material adverse effect on its condensed consolidated financial position and/or results of operations. It is possible, however, that future financial position or results of operations for any particular period could be materially affected by changes in the Company's assumptions or strategies related to those contingencies or changes out of its control.



## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

*This quarterly report on Form 10-Q including this Item 2, contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, which involve risks and uncertainties. Readers can identify these statements by forward-looking words such as "may," "could," "should," "would," "intend," "will," "expect," "anticipate," "believe," "estimate," "continue" or similar words. Our actual results and the timing of certain events may differ significantly from the results and timing discussed in the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those discussed or referred to in this report and in the "Risk Factors" section of our Annual Report on Form 10-K and any later publicly available filing with the Securities and Exchange Commission ("SEC"). The following discussion and analysis of our financial condition and results of operations should be read in light of those factors and in conjunction with our accompanying condensed consolidated financial statements and notes thereto.*

### Overview

World Energy offers a range of energy management solutions to commercial and industrial businesses, institutions, utilities, and governments to reduce their overall energy costs. We come to market with a holistic approach to energy management helping customers a) contract for a competitive price for energy, b) engage in energy efficiency projects to minimize quantity used and c) pursue available rebate and incentive programs. We made our mark on the industry with an innovative approach to procurement via our online auction platform, the World Energy Exchange®. With recent investments and acquisitions, we are building out our energy efficiency practice by engaging new customers while also pursuing more cross-selling opportunities for our procurement services.

We provide energy management services utilizing state-of-the-art technology and the experience of a seasoned management team to bring lower energy costs to its customers. We use a simple equation

$$E = P \cdot Q - i$$

to help customers to understand the holistic nature of the energy management problem. Total energy cost (E) is a function of Energy Price (P) times the Quantity of Energy Consumed (Q), minus any rebates or incentives (i) the customer can earn. This approach not only makes energy management more approachable for customers, simplifying what has become an increasingly dynamic and complex problem, it also highlights the inter-related nature of the energy management challenge. We assert that point solution vendors may optimize one of the three elements, but we believe it takes looking at the problem holistically to unlock the most savings.

Acquisitions are an important component of our business strategy. Our focus is on both our core procurement business as well as new product lines within the energy management services industry such as energy efficiency services.

During the fourth quarter of 2012, we acquired substantially all of the assets and assumed certain obligations of Northeast Energy Partners, LLC ("NEP") pursuant to an Asset Purchase Agreement (the "Asset Purchase Agreement") between us, NEP, and its members. NEP was a Connecticut based energy management and procurement company. During the third and fourth quarters of 2011 we acquired the energy procurement business of Co-eXprise, Inc. ("Co-eXprise"), Northeast Energy Solutions, LLC ("NES") and GSE Consulting, LP ("GSE"). These acquisitions expanded our capabilities in the Energy efficiency services segment, enabled us to enter the growing small- and medium-sized customer Energy procurement marketplaces, and consolidate the large commercial, industrial and government auction space. With the acquisition of NES, we are managing the business as two business segments: Energy procurement and Energy efficiency services.

Our business model is heavily dependent on our people. We have significantly grown our employee base from 20 at the time of our initial public offering in November 2006 to 127 at June 30, 2014. This planned investment in staffing has been, and will continue to be, a key component of our strategic initiatives and revenue growth. These infrastructure investments will result in increased operating costs in the short-term, but in the long-term we expect them to generate cash flow and profitability as we build incremental revenue. To date we have funded our acquisitions and strategic investments primarily with cash on-hand, notes payable, cash from operations and long-term debt. We have also deferred portions of the purchase prices through the use of earnouts that are tied to the ongoing performance of the acquired entity. Through the utilization of seller notes and earnouts, we have been able to finance a portion of the cost of the acquisitions over time with the targets' ongoing cash flow. These acquisition activities will increase our operating costs both in the short and long-term and may require us to borrow against our current credit facility and/or raise funds through additional capital raises.

## Operations

### Revenue

#### Retail Electricity Transactions

We earn a monthly commission on energy sales contracted through our online auction platform from each bidder or energy supplier based on the energy usage transacted between the bidder and lister or energy consumer. Our commissions are not based on the retail price for electricity; rather on the amount of energy consumed. Commissions are calculated based on the volume of energy usage transacted between the energy supplier and energy consumer multiplied by our contractual commission rate. Our contractual commission rate is negotiated with the energy consumer on a procurement-by-procurement basis based on energy consumer specific circumstances, including the size of auction, the effort required to organize and run the respective auction and competitive factors, among others. Once the contractual commission is agreed to with the energy consumer, all energy suppliers participating in the auction agree to that rate. That commission rate remains fixed for the duration of the contractual term regardless of energy usage. Energy consumers provide us with a letter of authorization to request their usage history from the local utility. We then use this data to compile a usage profile for that energy consumer that will become the basis for the auction. This data may also be used to estimate revenue on a going forward basis, as noted below.

Historically, our revenue and operating results have varied from quarter-to-quarter and are expected to continue to fluctuate in the future. These fluctuations are primarily due to the buying patterns of our wholesale and natural gas customers, which tend to have large, seasonal purchases during the fourth and first quarters and electricity usage having higher demand in our second and third quarters. In addition, the activity levels on the World Energy Exchange<sup>®</sup> can fluctuate due to a number of factors, including market prices, weather conditions, energy consumers' credit ratings, the ability of suppliers to obtain financing in credit markets, and economic and geopolitical events. To the extent these factors affect the purchasing decisions of energy consumers, our future results of operations may be affected. Contracts between energy suppliers and energy consumers are signed for a variety of term lengths, with a one to two year contract term being typical for commercial and industrial energy consumers, and government contracts typically having two to three year terms.

We do not invoice our electricity energy suppliers for monthly commissions earned and, therefore, we report a substantial portion of our receivables as "unbilled." Unbilled accounts receivable is based on management's best estimate of energy provided by the energy suppliers to the energy consumers for a specific completed time period at contracted commission rates and is made up of two components. The first component represents energy usage for which we have received actual data from the supplier and/or the utility, but for which payment has not been received at the balance sheet date. The majority of our contractual relationships with energy suppliers require them to supply actual usage data to us on a monthly basis and remit payment to us based on that usage. The second component represents energy usage for which we have not received actual data, but for which we have estimated usage. Commissions paid in advance by certain bidders are recorded as deferred revenue and amortized to commission revenue on a monthly basis on the energy exchanged that month.

#### Retail Natural Gas Transactions

There are two primary fee components to our retail natural gas services: transaction fees and management fees. Transaction fees are billed to and paid by the energy supplier awarded business on the platform. These fees are established prior to award and are the same for each supplier. For the majority of our natural gas transactions, we bill the supplier upon the conclusion of the transaction based on the estimated energy volume transacted for the entire award term multiplied by the transaction fee. Management fees are paid by our energy consumers and are generally billed on a monthly basis for services rendered based on terms and conditions included in contractual arrangements. While substantially all of our retail natural gas transactions are accounted for in accordance with this policy, a significant percentage is accounted for as the natural gas is consumed by the energy consumer and recognized as revenue in accordance with the retail electricity transaction revenue recognition methodology described above.

### Mid-Market Transactions

We earn a monthly commission on energy sales from each energy supplier based on the energy usage transacted between the energy supplier and energy consumer. The commissions are not based on the retail price for electricity but rather on the amount of energy consumed. Commissions are calculated based on the energy usage transacted between the energy supplier and energy consumer multiplied by our contractual commission rate. Revenue from commissions is recognized as earned over the life of each contract as energy is consumed, provided there is persuasive evidence of an arrangement, the sales price is fixed or determinable, collection of the fee is reasonably assured, and customer acceptance criteria, if any, has been successfully demonstrated. We generally recognize revenue on these transactions when we have received verification from the energy supplier of the end-users energy usage and energy supplier's subsequent collection of the fees billed to the end user. The verification is generally accompanied with payment of the agreed upon fee to us, at which time the revenue is recognized. Commissions paid in advance are recorded as customer advances and are recognized monthly as commission revenue based on the energy exchanged that month. To the extent we do not receive verification of actual energy usage or we cannot reliably estimate what actual energy usage was for a given period, revenue is deferred until usage and collection data is received from the energy supplier. To the extent that we do not receive actual usage data from the energy supplier, we will recognize revenue at the end of the contract flow date.

### Demand Response Transactions

Demand response transaction fees are recognized when we have received confirmation from the demand response provider ("DRP") that the energy consumer has performed under the applicable Regional Transmission Organization ("RTO") or Independent System Operator ("ISO") program requirements. The energy consumer is either called to perform during an actual curtailment event or is required to demonstrate its ability to perform in a test event during the performance period. For the PJM Interconnection ("PJM"), an RTO that coordinates the movement of wholesale electricity in all or parts of 13 states and the District of Columbia, the performance period is June through September in a calendar year. Test results are submitted to the PJM by the DRPs and we receive confirmation of the energy consumer's performance in the fourth quarter. DRPs typically pay us ratably on a quarterly basis throughout the demand response fiscal (June to May) year. As a result, a portion of the revenue we recognize is reflected as unbilled accounts receivable.

### Wholesale and Environmental Commodity Transactions

Wholesale transaction fees are invoiced upon the conclusion of the auction based on a fixed fee. These revenues are not tied to future energy usage and are recognized upon the completion of the online auction. For reverse auctions where our customers bid for a consumer's business, the fees are paid by the bidder. For forward auctions where a lister is selling energy products, the fees are typically paid by the lister.

Environmental commodity transaction fees are accounted for utilizing two primary methods. For regulated allowance programs like Regional Greenhouse Gas Initiative, Inc. ("RGGI"), fees are paid by the lister and are recognized quarterly as revenue as auctions are completed and approved. For most other environmental commodity transactions both the lister and the bidder pay the transaction fee and revenue is recognized upon the consummation of the underlying transaction as credits are delivered by the lister and payment is made by the bidder.

### Energy Efficiency Services

Our Energy efficiency services segment is primarily project driven where we identify efficiency measures that energy consumers can implement to reduce their energy usage. We present retrofit opportunities to customers, get approval from them to proceed and submit the proposal to the local utility for cost reimbursement. Once the utility approves funding for the project, we install the equipment, typically new heating, ventilation or air conditioning equipment, or replace lighting fixtures to more efficient models. We recognize revenue for Energy efficiency services when persuasive evidence of an arrangement exists, delivery has occurred, the price is fixed or determinable and collectability is reasonably assured. Due to the short-term nature of projects (typically two to three weeks), we utilize the completed-contract method. We also assess multiple contracts entered into by the same customer in close proximity to determine if the contracts should be combined for revenue recognition purposes. Revenues are recognized based upon factors such as passage of title, installation, payments and customer acceptance.

### ***Cost of revenue***

Cost of revenue consists primarily of:

- salaries, bonus and commissions, employee benefits and share-based compensation associated with our auction management and efficiency services, which are directly related to the development and production of the online auction and maintenance of market-related data on our auction platform and monthly management fees (our supply desk function);
- project costs including direct labor equipment and materials directly associated with efficiency projects; and
- rent, depreciation and other related overhead and facility-related costs.

### ***Sales and marketing***

Sales and marketing expenses consist primarily of:

- salaries, bonus and commissions, employee benefits and share-based compensation related to sales and marketing personnel;
- third party commission expenses to our channel partners;
- travel and related expenses;
- amortization related to customer relationships and contracts;
- rent, depreciation and other related overhead and facility-related costs; and
- general marketing costs such as trade shows, marketing materials and outsourced services.

### ***General and administrative***

General and administrative expenses consist primarily of:

- salaries, bonus and commissions, employee benefits and share-based compensation related to general and administrative personnel;
- accounting, legal, investor relations, information technology, insurance and other professional fees; and
- rent, depreciation and other related overhead and facility-related costs.

### ***Interest expense, net***

Interest expense, net consists primarily of:

- interest income earned on cash held in the bank; and
- interest expense related to bank term loans, notes payable and contingent consideration.

### ***Income tax benefit (expense)***

Income tax benefit (expense) is based on projected annualized taxable income or loss when this can be reliably estimated. In the event that we cannot reliably estimate due to the fact that a relatively small change in projected annualized taxable income or loss produces a significant variance in our annual effective tax rate then we utilize the actual effective rate for the year to date period. Under both scenarios, the benefit (expense) also reflects our deferred tax provision, federal alternative minimum liability and state income taxes.

|                              | For the Three Months Ended June 30, |       | For the Six Months Ended June 30, |       |
|------------------------------|-------------------------------------|-------|-----------------------------------|-------|
|                              | 2014                                | 2013  | 2014                              | 2013  |
| Revenue                      | 100%                                | 100%  | 100%                              | 100%  |
| Cost of revenue              | 23                                  | 27    | 23                                | 26    |
| Gross profit                 | 77                                  | 73    | 77                                | 74    |
| Operating expenses:          |                                     |       |                                   |       |
| Sales and marketing          | 49                                  | 62    | 50                                | 59    |
| General and administrative   | 24                                  | 27    | 26                                | 26    |
| Operating income (loss)      | 4                                   | (16)  | 1                                 | (11)  |
| Other expense, net           | (2)                                 | (3)   | (2)                               | (3)   |
| Income tax benefit (expense) | 1                                   | (2)   | 0                                 | (2)   |
| Net income (loss)            | 3%                                  | (21%) | (1%)                              | (16%) |

## Results of Operations

The following table sets forth certain items as a percent of revenue for the periods presented:

### Comparison of the Three Months Ended June 30, 2014 and 2013

#### Revenue

|                            | For the Three Months Ended June 30, |              | Increase     |     |
|----------------------------|-------------------------------------|--------------|--------------|-----|
|                            | 2014                                | 2013         |              |     |
| Energy procurement         | \$ 7,954,352                        | \$ 6,956,838 | \$ 997,514   | 14% |
| Energy efficiency services | 1,438,684                           | 978,819      | 459,865      | 47  |
| Total revenue              | \$ 9,393,036                        | \$ 7,935,657 | \$ 1,457,379 | 18% |

Revenue increased 18% for the three months ended June 30, 2014 as revenue from both segments increased as compared to the same period in 2013. Energy procurement segment revenue increased 14% due to increased transaction activity from our auction and mid-market customers as well as increased revenue recognized from previously deferred items. Energy efficiency services segment revenue increased 47% as the rebuilt Massachusetts sales team gained traction in the market and delivered an increase in the number of projects as well as an increase in the average project size compared to the second quarter of 2013.

#### Cost of revenue

|                            | For the Three Months Ended June 30, |                 |              |                 |                     |
|----------------------------|-------------------------------------|-----------------|--------------|-----------------|---------------------|
|                            | 2014                                |                 | 2013         |                 |                     |
|                            | \$                                  | %<br>of Revenue | \$           | %<br>of Revenue | Increase (Decrease) |
| Energy procurement         | \$ 2,977,082                        | 12%             | \$ 1,249,181 | 18%             | \$ (2,720,991)      |
| Energy efficiency services | 1,142,724                           | 79              | 895,274      | 91              | 247,450             |
| Total cost of revenue      | \$2,119,806                         | 23%             | \$2,144,455  | 27%             | \$ (24,649)         |

Cost of revenue decreased 1% for the three months ended June 30, 2014 as compared to the same period in 2013. Cost of revenue for our Energy procurement segment decreased 22% due to decreases in payroll reflecting our integration, automation and reorganization efforts. Cost of revenue associated with our Energy procurement segment as a percent of revenue decreased by 6% primarily due to the cost decreases described above and, to a lesser extent, the 14% increase in Energy procurement revenue. Cost of revenue associated with our Energy efficiency services segment increased 28% primarily due to an increase in project costs associated with the 47% increase in revenue. Cost of revenue associated with our Energy efficiency services segment as a percent of revenue decreased by 12% primarily due to improved contribution margins on projects completed in the second quarter of 2014 as compared to the second quarter of 2013.

## Operating expenses

|                            | For the Three Months Ended June 30, |              |             |              |                     |      |
|----------------------------|-------------------------------------|--------------|-------------|--------------|---------------------|------|
|                            | 2014                                |              | 2013        |              |                     |      |
|                            | \$                                  | % of Revenue | \$          | % of Revenue | Increase (Decrease) |      |
| Sales and marketing        | \$4,633,760                         | 49%          | \$4,890,347 | 62%          | \$(256,587)         | (5%) |
| General and administrative | 2,228,641                           | 24           | 2,167,021   | 27           | 61,620              | 3    |
| Total operating expenses   | \$6,862,401                         | 73%          | \$7,057,368 | 89%          | \$(194,967)         | (3%) |

Sales and marketing expenses decreased 5% for the three months ended June 30, 2014 as compared to the same period in 2013 primarily due to decreases in internal commissions and amortization of intangible assets. Internal commissions decreased due to the change in commission policy for our mid-market group that we implemented in the second quarter of 2013. Under the revised policy, we continued to pay commissions based on cash received from mid-market transactions that were deferred for revenue purposes and provided for a bookings bonus to offset the impact of the change in our policy. We converted the bookings bonus to a draw program in 2014, eliminating that component of commission expense. Amortization expense related to intangible assets decreased as certain intangible assets related to our acquisitions became fully amortized in 2014. These decreases were partially offset by an increase in third party commission expense as we continue to expand our channel partner network. Sales and marketing expense as a percentage of revenue decreased 13% due to the decrease in costs described above, and the 18% increase in total revenue.

The 3% increase in general and administrative expenses for the three months ended June 30, 2014 as compared to the same period in 2013 was primarily due to an increase in bad debt expense and payroll costs. The increases were partially offset by a reduction in legal costs. Payroll costs increased due to investments in our product development team. General and administrative expenses as a percent of revenue decreased 3% primarily due to the cost increases described above, offset by the 18% increase in total revenue.

### Other income (expense), net

We recorded net interest expense of approximately \$0.2 million for the three months ended June 30, 2014 compared to net interest expense of approximately \$0.3 for the three months ended June 30, 2013. The decrease in net interest expense in 2014 was primarily due to a reduction in the interest charged on our long-term debt resulting from the replacement of our credit facility in the fourth quarter of 2013.

### Income tax benefit (expense)

We recorded an income tax benefit of approximately \$0.1 million for the three months ended June 30, 2014 and an income tax expense of approximately \$0.1 million for the three months ended June 30, 2013. For the three months ended June 30, 2014, we were unable to make a reliable estimate of our annual effective tax rate as relatively small changes in our projected income or loss could produce a significant variance in our annual effective tax rate and as a result we utilized the actual effective tax rate as the basis for the income tax benefit. For the three months ended June 30, 2013, the effective tax rate was based on our estimated annual effective tax rate. Both periods reflect a deferred tax provision, federal alternative minimum tax liability and state income taxes.

### Net income (loss)

We reported net income of approximately \$0.3 million for the three months ended June 30, 2014 and a net loss of approximately \$1.7 million for the three months ended June 30, 2013. The \$2.0 million increase was primarily due to the increase in revenue, improved gross margin and the decrease in sales and marketing expenses.

## Comparison of the Six Months Ended June 30, 2014 and 2013

### Revenue

|                            | For the Six Months Ended June 30, |               |              |     |
|----------------------------|-----------------------------------|---------------|--------------|-----|
|                            | 2014                              | 2013          | Increase     |     |
| Energy procurement         | \$ 15,923,997                     | \$ 14,377,997 | \$ 1,546,000 | 11% |
| Energy efficiency services | 2,989,393                         | 2,215,142     | 774,251      | 35  |
| Total revenue              | \$ 18,913,390                     | \$ 16,593,139 | \$ 2,320,251 | 14% |

Revenue increased 14% for the six months ended June 30, 2014 as revenue from both segments increased as compared to the same period in 2013. Energy procurement segment revenue increased 11% due to increased transaction activity from our auction and mid-market customers as well as increased revenue recognized from previously deferred items. These increases were partially offset by decreases in wholesale and gas transaction activity in the six months ended June 30, 2014 as increased commodity prices during the first quarter resulted in delayed contracting decisions by listers. Energy efficiency services segment revenue increased 35% as the rebuilt Massachusetts sales team delivered increased revenue in the NSTAR territory in Massachusetts during the six months ended June 30, 2014 as compared to the six months ended June 30, 2013.

#### *Cost of revenue*

|                            | For the Six Months Ended June 30, |            |  |             |            |                     |
|----------------------------|-----------------------------------|------------|--|-------------|------------|---------------------|
|                            | 2014                              |            |  | 2013        |            |                     |
|                            | \$                                | %          |  | \$          | %          |                     |
|                            |                                   | of Revenue |  |             | of Revenue | Increase (Decrease) |
| Energy procurement         | \$2,019,933                       | 13%        |  | \$2,497,684 | 17%        | \$ (477,751) (19%)  |
| Energy efficiency services | 2,412,186                         | 81         |  | 1,879,922   | 85         | 532,264 28          |
| Total cost of revenue      | \$4,432,119                       | 23%        |  | \$4,377,606 | 26%        | \$ 54,513 1%        |

Cost of revenue increased 1% for the six months ended June 30, 2014 as compared to the same period in 2013. Cost of revenue for our Energy procurement segment decreased 19% due to decreases in payroll reflecting our integration, automation and reorganization efforts. Cost of revenue associated with our Energy procurement segment as a percent of revenue decreased by 4% primarily due to the cost decreases described above and, to a lesser extent, the 11% increase in Energy procurement revenue. Cost of revenue associated with our Energy efficiency services segment increased 28% primarily due to an increase in project costs associated with the 35% increase in revenue. Cost of revenue associated with our Energy efficiency services segment as a percent of revenue decreased by 4% primarily due to improved contribution margins on projects completed in the six months ended June 30, 2014 as compared to the six months ended June 30, 2013.

#### *Operating expenses*

|                            | For the Six Months Ended June 30, |            |  |              |            |                     |
|----------------------------|-----------------------------------|------------|--|--------------|------------|---------------------|
|                            | 2014                              |            |  | 2013         |            |                     |
|                            | \$                                | %          |  | \$           | %          |                     |
|                            |                                   | of Revenue |  |              | of Revenue | Increase (Decrease) |
| Sales and marketing        | \$9,395,751                       | 50%        |  | \$9,868,428  | 59%        | \$ (472,677) (5%)   |
| General and administrative | 4,913,114                         | 26         |  | 4,228,694    | 26         | 684,420 16          |
| Total operating expenses   | \$14,308,865                      | 76%        |  | \$14,097,122 | 85%        | \$ 211,743 2%       |

Sales and marketing expenses decreased 5% for the six months ended June 30, 2014 as compared to the same period in 2013 primarily due to decreases in internal commissions and amortization of intangible assets. Internal commissions decreased due to lower quota attainment in 2014 compared to 2013 and due to the change in commission policy for our mid-market group that we implemented in the second quarter of 2013. Under the revised policy, we continued to pay commissions based on cash received from mid-market transactions that were deferred for revenue purposes and provided for a bookings bonus to offset the impact of the change in our policy. We converted the bookings bonus to a draw program in 2014, eliminating that component of commission expense. Amortization expense related to intangible assets decreased as certain intangible assets related to our acquisitions became fully amortized in 2014. These decreases were partially offset by an increase in third party commission expense as we continued to expand our channel partner network. Sales and marketing expense as a percentage of revenue decreased 9% due to the decrease in costs described above the 14% increase in revenue.

The 16% increase in general and administrative expenses for the six months ended June 30, 2014 as compared to the same period in 2013 was due to increased legal and consulting costs of approximately \$0.4 million primarily related to a shareholder action during the first quarter of 2014. In addition, payroll costs increased due to investments in our product development team. General and administrative expenses as a percent of revenue was substantially consistent with the prior year period as the 14% increase in revenue offset the above noted cost increases.

### *Other income (expense), net*

We recorded net interest expense of approximately \$0.4 million for the six months ended June 30, 2014 compared to net interest expense of approximately \$0.5 million for the six months ended June 30, 2013. The decrease in net interest expense in 2014 was primarily due to a reduction in the interest charged on our long-term debt resulting from the replacement of our credit facility in the fourth quarter of 2013.

### *Income tax benefit (expense)*

We recorded an income tax benefit of approximately \$25,000 for the six months ended June 30, 2014 and an income tax expense of approximately \$0.3 million for the six months ended June 30, 2013. For the six months ended June 30, 2014, we were unable to make a reliable estimate of our annual effective tax rate as relatively small changes in our projected income or loss could produce a significant variance in our annual effective tax rate and as a result we utilized the actual effective tax rate as the basis for the income tax benefit. For the three months ended June 30, 2013, the effective tax rate was based on our estimated annual effective tax rate. Both periods reflect a deferred tax provision, federal alternative minimum tax liability and state income taxes.

### *Net income (loss)*

Net loss decreased approximately \$2.4 million for the six months ended June 30, 2014 compared to the same period in 2013, primarily due the increase in revenue, improved gross margin and the decrease in sales and marketing expenses. These decreases in net loss were partially offset by the increase in general and administrative expense.

### **Liquidity and Capital Resources**

At June 30, 2014, we had no commitments for material capital expenditures. We have identified and executed against a number of strategic initiatives that we believe are key components of our future growth, including: making strategic acquisitions; entering into other energy-related markets including energy efficiency; expanding our community of listers, bidders and channel partners on our exchanges; strengthening and extending our long-term relationships with government agencies; and growing our direct and inside sales force. As of June 30, 2014 our workforce numbered 127, an increase of one from the number that we employed at December 31, 2013. At June 30, 2014, we had 61 professionals in our sales and marketing and account management groups, 40 in our supply desk group and 26 in our general and administrative group.

We paid \$10.4 million to acquire three businesses in 2011 through the use of cash on hand, cash flow from ongoing operations as well as cash flow generated by the acquisitions. In addition, we have paid \$6.7 million in seller notes and contingent consideration bringing the total cash paid for the 2011 acquisitions to \$17.1 million. In October 2012, we borrowed \$8.0 million in long-term bank debt and entered into a \$2.0 million seller note to acquire NEP. While the expansion/addition of these debt instruments significantly increased our commitments, we believe we have the resources to meet both our short- and long-term obligations under these arrangements based on cash on-hand, operating cash flows from our base business and cash expected to be generated from all of our acquired businesses. During 2013, we paid an additional \$1.3 million in cash related to NEP contingent consideration and retired \$1.5 million against the NEP seller note. During 2014, we repaid the remaining \$0.5 million NEP Seller note and settled all outstanding earnout claims with GSE by issuing 200,000 shares of common stock, which had a fair value of approximately \$0.9 million. As of June 30, 2014 we have retired all of our seller-note and earnout obligations related to these acquisitions. During the six months ended June 30, 2014 we generated cash flow from operations of \$1.2 million and ended the quarter with \$2.3 million in cash and cash equivalents.

### **Comparison of June 30, 2014 to December 31, 2013**

|                                | June 30,<br>2014 | December 31,<br>2013 | Increase (Decrease) |     |
|--------------------------------|------------------|----------------------|---------------------|-----|
| Cash and cash equivalents      | \$ 2,290,370     | \$ 1,725,186         | \$ 565,234          | 33% |
| Trade accounts receivable, net | 7,205,500        | 7,738,141            | (532,641)           | (7) |
| Days sales outstanding         | 69               | 76                   | (7)                 | (9) |
| Working capital (deficit)      | 1,076,748        | (893,984)            | 1,970,732           | 220 |
| Stockholders' equity           | 26,758,502       | 25,480,584           | 1,277,918           | 5   |



Cash and cash equivalents increased 33% primarily due to cash flows from operations of approximately \$1.2 million. Trade accounts receivable at June 30, 2014 decreased 7% as compared to the fourth quarter of 2013 as days sales outstanding (representing accounts receivable outstanding at June 30, 2014 divided by the average sales per day during the three months ended June 30, 2014, as adjusted) decreased 9%. Days sales outstanding decreased 9% due to the timing of in-period revenue recognized and cash receipts within the six months ended June 30, 2014 as compared to the same period in 2013. Revenue from bidders representing 10% or more of our revenue decreased to 26% from two bidders during the six months ended June 30, 2014, from an aggregate 28% for two bidders in the same period of the previous year. Two bidders merged at the end of 2013 and have been combined to determine the percentages above in both periods.

The working capital balance at June 30, 2014 (consisting of current assets less current liabilities) improved \$2.0 million from December 31, 2013. Current assets increased \$0.4 million primarily due to the increase in cash and cash equivalents. Current liabilities decreased \$1.5 million due to the settlement of our contingent consideration obligations and the \$0.5 million payment against the short-term related party note. Stockholders' equity increased 5% for the six months ended June 30, 2014 primarily due to the issuance of shares under the GSE settlement and share-based compensation, both partially offset by the \$0.2 million net loss.

Cash provided by operating activities for the six months ended June 30, 2014 and 2013 was approximately \$1.2 million for both periods. Cash used in investing activities for the six months ended June 30, 2014 was approximately \$0.2 million primarily due to capitalized software cost and capital expenditures. Cash used in financing activities for the six months ended June 30, 2014 and 2013 was approximately \$0.4 million and \$2.4 million, respectively. Cash used in financing activities for the six months ended June 30, 2014 primarily resulted from the final payment of the NEP seller note, partially offset by proceeds from the exercise of stock options. Cash used in financing activities for the six months ended June 30, 2013 was \$2.4 million, primarily resulting from a \$1.4 million payment of contingent consideration and \$1.0 million of principal payments on long term debt.

EBITDA, representing net income (loss) before interest, income taxes, depreciation and amortization for the six months ended June 30, 2014 was \$2.1 million as compared to \$0.2 million for the same period in the prior year. Please refer to the section below discussing non-GAAP financial measures for a reconciliation of non-GAAP measures to the most directly comparable measure calculated and presented in accordance with accounting principles generally accepted in the United States of America ("GAAP").

In this Quarterly Report on Form 10-Q, we provide certain "non-GAAP financial measures". A non-GAAP financial measure refers to a numerical financial measure that excludes (or includes) amounts that are included in (or excluded from) the most directly comparable financial measure calculated and presented in accordance with GAAP in our financial statements. In this Quarterly Report on Form 10-Q, we provide EBITDA and adjusted EBITDA as additional information relating to our operating results. These non-GAAP measures exclude expenses related to share-based compensation, depreciation related to our fixed assets, amortization expense related to acquisition-related assets and other assets, interest expense on bank borrowings, notes payable to sellers and contingent consideration, interest income on invested funds, and income taxes. Management uses these non-GAAP measures for internal reporting and bank reporting purposes. We have provided these non-GAAP financial measures in addition to GAAP financial results because we believe that these non-GAAP financial measures provide useful information to certain investors and financial analysts in assessing our operating performance due to the following factors:

- We believe that the presentation of a non-GAAP measure that adjusts for the impact of share-based compensation expenses, depreciation of fixed assets, amortization expense related to acquisition-related assets and other assets, interest expense on bank borrowings, seller notes and contingent consideration, interest income on invested funds, and income taxes, provides investors and financial analysts with a consistent basis for comparison across accounting periods and, therefore, is useful to investors and financial analysts in helping them to better understand our operating results and underlying operational trends;
- Although share-based compensation is an important aspect of the compensation of our employees and executives, share-based compensation expense is generally fixed at the time of grant, then amortized over a period of several years after the grant of the share-based instrument, and generally cannot be changed or influenced by management after the grant;
- We do not acquire intangible assets on a predictable cycle. Our intangible assets relate solely to business acquisitions. Amortization costs are fixed at the time of an acquisition, are then amortized over a period of several years after the acquisition and generally cannot be changed or influenced by management after the acquisition;
- We do not regularly incur capitalized software and website costs. Our capitalized software costs relate primarily to the build-out of our exchanges. Amortization costs are fixed at the time the costs are incurred and are then amortized over a period of several years and generally cannot be changed or influenced by management after the initial costs are incurred;

- We do not regularly invest in fixed assets. Our fixed assets relate primarily to computer and office equipment and furniture and fixtures. Depreciation costs are fixed at the time of purchase and are then depreciated over several years and generally cannot be changed or influenced by management after the purchase;
- We do not regularly enter into bank debt, seller notes and/or pay interest on contingent consideration. Our seller notes and contingent consideration relate to acquisition activities. Interest expense is fixed at the time of purchase and recorded over the life of the lease and generally cannot be changed or influenced by management after the purchase;
- We do not regularly earn interest on our cash accounts. Our cash has not yielded material returns to date and these returns generally cannot be changed or influenced by management; and
- We do not regularly pay federal or state income taxes due to our net operating loss carryforwards. Our income tax expense reflects the release of our deferred tax assets to apply to projected annualized taxable income, and an anticipated alternative minimum tax liability based on statutory rates that generally cannot be changed or influenced by management.

Pursuant to the requirements of the SEC, we have provided below a reconciliation of the non-GAAP financial measures used to the most directly comparable financial measures prepared in accordance with GAAP. These non-GAAP financial measures are not prepared in accordance with GAAP. These measures may differ from the GAAP information, even where similarly titled used by other companies, and therefore should not be used to compare our performance to that of other companies. The presentation of this additional information is not meant to be considered in isolation or as a substitute for net income (loss) prepared in accordance with GAAP.

|                                   | Three Months Ended June 30, |              | Six Months Ended June 30, |                |
|-----------------------------------|-----------------------------|--------------|---------------------------|----------------|
|                                   | 2014                        | 2013         | 2014                      | 2013           |
| GAAP net income (loss)            | \$ 305,602                  | \$ (165,155) | \$ (192,175)              | \$ (2,611,040) |
| Add: Interest expense, net        | 197,899                     | 277,397      | 398,296                   | 480,134        |
| Add: Income taxes                 | (88,000)                    | (131,305)    | (25,000)                  | 262,610        |
| Add: Amortization of intangibles  | 844,700                     | 974,758      | 1,771,345                 | 1,949,516      |
| Add: Amortization of other assets | 12,447                      | 8,506        | 26,012                    | 17,013         |
| Add: Depreciation                 | 52,085                      | 55,070       | 104,996                   | 110,739        |
| Non-GAAP EBITDA                   | \$ 1,324,733                | \$ (207,119) | \$ 2,083,474              | \$ (208,972)   |
| Add: Stock-based compensation     | 190,761                     | 146,323      | 352,664                   | 292,309        |
| Non-GAAP adjusted EBITDA          | \$ 1,515,494                | \$ (60,796)  | \$ 2,436,138              | \$ 81,337      |

#### Critical Accounting Policies

The preparation of financial statements in conformity with GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Accordingly, actual results could differ from these estimates.

The most judgmental estimates affecting our consolidated financial statements are those relating to revenue recognition and the estimate of actual energy delivered from the bidder to the lister of such energy; stock-based compensation; the valuation of intangible assets and goodwill; the valuation of contingent consideration; impairment of long-lived assets; and estimates of future taxable income as it relates to the realization of our net deferred tax assets. We regularly evaluate our estimates and assumptions based upon historical experience and various other factors that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. To the extent actual results differ from those estimates; future results of operations may be affected. Refer to Note 2 of our consolidated financial statements within our Annual Report on Form 10-K as filed with the SEC on March 31, 2014 for a description of our accounting policies.

#### Off-Balance Sheet Arrangements

We currently have no off-balance sheet arrangements that have or are reasonably likely to have a current or future material effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

### **Item 3. Quantitative and Qualitative Disclosure about Market Risk**

As a smaller reporting company as defined by Rule 12b-2 of the Exchange Act and in Item 10(f)(1) of Regulation S-K, we are electing scaled disclosure reporting obligations and therefore are not required to provide the information requested by this Item.

### **Item 4. Controls and Procedures**

#### **Evaluation of Disclosure Controls and Procedures**

As required by Rule 13a-15 under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), the Company carried out an evaluation under the supervision and with the participation of the Company's management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the Company's disclosure controls and procedures as of December 31, 2013. In designing and evaluating the Company's disclosure controls and procedures, the Company and its management recognize that there are inherent limitations to the effectiveness of any system of disclosure controls and procedures, including the possibility of human error and the circumvention or overriding of the controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their desired control objectives. Additionally, in evaluating and implementing possible controls and procedures, the Company's management was required to apply its reasonable judgment. Based upon the required evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that as of June 30, 2014, the Company's disclosure controls and procedures were effective at the reasonable assurance level to ensure that information required to be disclosed by the Company in the reports it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and procedures also were effective in ensuring that information required to be disclosed by the Company in the reports it files or submits under the Exchange Act is accumulated and communicated to its management, including the Company's Chief Executive Officer and Chief Financial Officer as appropriate, to allow timely decisions regarding required disclosure.

#### **Changes in Internal Control Over Financial Reporting**

There was no change in the Company's internal control over financial reporting that occurred during the three months ended June 30, 2014 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

## PART II OTHER INFORMATION

### Item 1. Legal Proceedings

Two former employees/consultants of GSE have filed two separate complaints in the District Courts of Dallas County and Tarrant County Texas alleging, among other things, claims related to breach of contract, quantum meruit, promissory estoppel, tortious interference, and civil conspiracy. Each plaintiff claims that GSE and/or we failed to pay commissions due for services that they provided prior to the date of our purchase of certain GSE assets, based on their respective employment or independent contractor agreements with GSE. Each plaintiff has also asserted claims for recovery of their attorneys' fees. We deny the allegations and have filed counterclaims for damages, asserting claims for conversion, unjust enrichment, misappropriation of confidential information, and violation of the Texas Theft Liability Act against each of the plaintiffs. We have also filed a counterclaim against one of the plaintiffs for her breach of a non-competition and non-solicitation agreement, based on her working for a competitor of ours during her one-year restrictive period and her improper solicitation of former GSE customers on behalf of the competitor. The plaintiffs have also asserted claims against the GSE affiliates and their individual principals. Our motions for summary judgment seeking dismissal of all of the plaintiff's claims was denied in its entirety in one of the cases. In the other case, our motion for summary judgment was partially granted, dismissing the plaintiff's civil conspiracy claim. The courts have assigned trial dates of September 29, 2014 and November 17, 2014.

We have estimated the potential commissions allegedly due to the two plaintiffs to be approximately \$0.3 million. We have not recorded any accrual for contingent liabilities associated with these legal proceedings based on its belief that any potential loss, while reasonably possible, is not probable. We intend to continue to defend these actions vigorously and are currently unable to estimate a range of payments, if any, we may be required to pay, with respect to these claims. Further, we believe that the resolution of these matters will not result in a material effect to our condensed consolidated financial statements. However, due to uncertainties that accompany litigation of this nature, there could be no assurance that we will be successful, and the resolution of the lawsuits could have a material effect on our accompanying condensed consolidated financial statements.

In addition, we had filed cross claims against GSE for indemnification under the Asset Purchase Agreement in each of the plaintiffs' cases. The GSE affiliates and principals had also asserted cross claims against us seeking indemnification under the Asset Purchase Agreement. In December 2013, GSE had amended its cross claims in one of the matters to include claims asserting breach of the earnout provisions in the Asset Purchase Agreement. During the three months ended June 30, 2014, GSE and we settled all claims against each other related to these lawsuits and the earnout provisions. We and GSE filed with the court agreed motions to dismiss all claims against one another, which were allowed by the court. The settlement called for us to issue 200,000 shares of common stock to GSE and its affiliates that had a fair value of \$0.9 million on the date issued.

From time to time, we may be subject to legal proceedings and claims arising from the conduct of its business operations, including litigation related to employment matters. While it is impossible to ascertain the ultimate legal and financial liability with respect to contingent liabilities, including lawsuits, we believe that the aggregate amount of such liabilities, if any, will not have a material adverse effect on our condensed consolidated financial position and/or results of operations. It is possible, however, that future financial position or results of operations for any particular period could be materially affected by changes in our assumptions or strategies related to those contingencies or changes out of our control.

### Item 1A. Risk Factors

*There have been no material changes from risk factors previously disclosed in our annual report on Form 10-K for the fiscal year ended December 31, 2013, as filed with the Securities and Exchange Commission on March 31, 2014.*

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

#### Recent Sales of Unregistered Securities; Use of Proceeds from Registered Securities

During the quarter ended June 30, 2014, The Company issued 200,000 shares of common stock to Bruner & Bruner PC, GSE Consulting, LP, Great Lakes Energy, LP, Brian Dafferner, Glenwood Energy Partners, LTD, and Gulf States Energy, Inc. as part of an agreement between the Company and GSE Consulting, LP and related entities and affiliates to settle litigation and claims related to contingent consideration between the parties. The shares were issued on April 4, 2014 under an exemption from registration pursuant to Rule 506 of Regulation D under the Securities Act of 1933, and the shares were subsequently registered for resale on Form S-3 effective on June 19, 2014.

Purchases of Equity Securities by the Issuer and Affiliated Purchasers

In connection with the vesting of restricted stock granted to employees, we withheld certain shares with value equivalent to employees' minimum statutory obligations for the applicable income and other employment taxes.

A summary of the shares withheld to satisfy employee tax withholding obligations for the three months ended June 30, 2014 is as follows:

| Period                         | Total Number<br>of<br>Shares<br>Purchased | Average Price<br>Paid<br>Per Share | Total Number<br>of<br>Shares<br>Purchased<br>As Part of<br>Publicly<br>Announced<br>Plans or<br>Programs | Maximum<br>Number<br>of Shares That<br>May<br>Yet Be<br>Purchased<br>Under The Plan |
|--------------------------------|---|------------------------------------|--|---|
| <del>04/01/14 - 04/30/14</del> | <del>—</del>                              | <del>\$ —</del>                    | <del>—</del>   | <del>—</del>  |
| 05/01/14 - 05/31/14            | 39  | \$ 4.31                            | —  | —   |
| <del>06/01/14 - 06/30/14</del> | <del>4,692</del>                          | <del>\$ 4.08</del>                 | <del>—</del>   | <del>—</del>  |
| Total                          | 4,731                                     | \$ 4.08                            | —  | —   |

**Item 3. Defaults Upon Senior Securities**

None.

**Item 4. Mine Safety Disclosures**

None.

**Item 5. Other Information**

None.

**Item 6. Exhibits**

- 31.1 Certification of the Chief Executive Officer pursuant to §302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of the Chief Financial Officer pursuant to §302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of the Chief Executive Officer pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of the Chief Financial Officer pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002.
- 101 The following materials from World Energy Solutions, Inc.'s Quarterly Report on Form 10-Q for the three and six months ended June 30, 2014, formatted in Extensible Business Reporting Language: (i) the condensed consolidated balance sheets; (ii) the condensed consolidated statements of operations; (iii) the condensed consolidated statements of cash flows; and (iv) notes to the condensed consolidated financial statements.

## SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

*World Energy Solutions, Inc.*

Dated: August 8, 2014

By: /s/ Philip Adams

Philip Adams

Chief Executive Officer

Dated: August 8, 2014

By: /s/ James Parslow

James Parslow

Chief Financial Officer

**CERTIFICATION OF THE CHIEF EXECUTIVE OFFICER PURSUANT TO  
§302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Philip Adams, certify that:

1. I have reviewed this quarterly report on Form 10-Q of World Energy Solutions, Inc. (the "Registrant");
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this report;
4. The Registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the Registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the Registrant's internal control over financial reporting that occurred during the Registrant's most recent fiscal quarter (the Registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the Registrant's internal control over financial reporting;
5. The Registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant's auditors and the audit committee of the Registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant's internal control over financial reporting.

Dated: August 8, 2014

By: /s/ Philip Adams  
Philip Adams  
Chief Executive Officer

**CERTIFICATION OF THE CHIEF FINANCIAL OFFICER PURSUANT TO  
§302 OF THE SARBANES-OXLEY ACT OF 2002**

I, James Parslow, certify that:

1. I have reviewed this quarterly report on Form 10-Q of World Energy Solutions, Inc. (the "Registrant");

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

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

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

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

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

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

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

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

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

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

Dated: August 8, 2014

By: /s/ James Parslow

James Parslow  
Chief Financial Officer



**CERTIFICATION PURSUANT TO 18 U.S.C. §1350, AS ADOPTED  
PURSUANT TO §906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the filing of this quarterly report of World Energy Solutions, Inc. (the "Company") on Form 10-Q (the "Report") for the period ended June 30, 2014 as filed with the Securities and Exchange Commission on the date hereof, I, Philip Adams, Chief Executive Officer of the Company, certify, to the best of my knowledge, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: August 8, 2014

By: /s/ Philip Adams

Philip Adams  
Chief Executive Officer

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

**CERTIFICATION PURSUANT TO 18 U.S.C. §1350, AS ADOPTED  
PURSUANT TO §906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the filing of this quarterly report of World Energy Solutions, Inc. (the "Company") on Form 10-Q (the "Report") for the period ended June 30, 2014 as filed with the Securities and Exchange Commission on the date hereof, I, James Parslow, Chief Financial Officer of the Company, certify that, to the best of my knowledge, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: August 8, 2014

By: /s/ James Parslow

James Parslow  
Chief Financial Officer

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

# WORLD ENERGY SOLUTIONS, INC.

## FORM 8-K (Current report filing)

Filed 07/30/14 for the Period Ending 07/24/14

|             |  |
|-------------|--|
| Address     | 100 FRONT STREET<br>WORCESTER, MA 01608            |
| Telephone   | 508-459-8100                                       |
| CIK         | 0001371781   |
| Symbol      | XWES   |
| SIC Code    | 7389 - Business Services, Not Elsewhere Classified |
| Industry    | Investment Services                                |
| Sector      | Financial  |
| Fiscal Year | 12/31  |

---

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

---

**FORM 8-K**

---

**CURRENT REPORT**  
Pursuant to Section 13 or 15(d)  
of the Securities Exchange Act of 1934

**Date of Report (Date of earliest event reported): July 24, 2014**

---

**World Energy Solutions, Inc.**  
(Exact Name of Registrant as Specified in Charter)

---

**Delaware**  
(State or Other Jurisdiction  
of Incorporation)

**001-34289**  
(Commission  
File Number)

**04-3474959**  
(IRS Employer  
Identification No.)

**100 Front Street**  
**Worcester, Massachusetts**  
(Address of Principal Executive Offices)

**01608**  
(Zip Code)

**Registrant's telephone number, including area code: (508) 459-8100**

**n/a**  
(Former Name or Former Address, if Changed Since Last Report)

---

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions ( see General Instruction A.2. below):

- ☐ Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)
  - ☐ Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)
  - ☐ Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))
  - ☐ Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))
-

**Item 5.02 Departure of Directors or Certain Officers; Election of Directors; Appointment of Certain Officers; Compensatory Arrangements of Certain Officers.**

(e) On July 24, 2014, the Board of Directors revised the Bonus Compensation Plan for executive officers for fiscal year ended December 31, 2014. Under the revised bonus plan the Company's annual cash incentive bonus for executive officers is intended to compensate for performance related to the Company's operational and financial goals. No executive bonus may be awarded unless the Company has achieved net income at fiscal year-end. The net income shall be split, with 50% retained by the Company, and 50% forming the bonus pool up to an aggregate total executive bonus pool cap of \$340,000 and any additional net income shall be retained by the Company. Further, any amount in the bonus pool that is not awarded shall be retained by the Company.

The bonuses will be awarded based on the following business performance criteria and percentages, as set forth below: (1) net income; (2) new bookings and renewals achievement; and (3) year-end cash balance. The CEO and COO will receive 50% of their bonus upon achievement of the net income target, 25% upon the new bookings target, and 25% upon the renewals achievement target. The CFO will receive 50% of his bonus upon achievement of the net income target, 12.5% upon the new bookings target, 12.5% upon the renewals achievement, and 25% upon achievement of the year-end cash balance target, including collections against accounts receivable.

The Compensation Committee works with the CEO to develop the business performance criteria over the next year. The Compensation Committee anticipates that this model will evolve as the Company grows.

Cash incentive bonus participants are eligible for bonus payments ranging from 0% to 100% of their caps. For fiscal year 2014, bonus cap parameters for the Company's executive team were defined as follows:

| <u>2014 Executive Bonus Caps</u>       | <u>CEO</u>       | <u>COO</u>       | <u>CFO</u>      |
|--|------------------|------------------|-----------------|
| <u>Attainment of Net Income Goals</u>  | <u>\$ 75,000</u> | <u>\$ 50,000</u> | <u>\$45,000</u> |
| <u>Attainment of New Bookings</u>      | <u>37,500</u>    | <u>25,000</u>    | <u>11,250</u>   |
| <u>Achievement of Renewal Bookings</u> | <u>37,500</u>    | <u>25,000</u>    | <u>11,250</u>   |
| <u>Year-End Cash Balance</u>           | <u>—</u>         | <u>—</u>         | <u>22,500</u>   |
| <u>Total Annual Bonus Caps</u>         | <u>\$150,000</u> | <u>\$100,000</u> | <u>\$90,000</u> |

---

**SIGNATURE**

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

**WORLD ENERGY SOLUTIONS, INC.**

Date: July 30, 2014

By: /s/ Philip V. Adams

Philip V. Adams

President and Chief Executive Officer

# **WORLD ENERGY SOLUTIONS, INC.**

## **FORM 10-Q** (Quarterly Report)

**Filed 11/10/14 for the Period Ending 09/30/14**

|             |  |
|-------------|--|
| Address     | 100 FRONT STREET<br>WORCESTER, MA 01608            |
| Telephone   | 508-459-8100                                       |
| CIK         | 0001371781   |
| Symbol      | XWES   |
| SIC Code    | 7389 - Business Services, Not Elsewhere Classified |
| Industry    | Investment Services                                |
| Sector      | Financial  |
| Fiscal Year | 12/31  |

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

**FORM 10-Q**

- ☒ Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 For the quarterly period ended September 30, 2014; or
- ☐ Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number: 001-34289

**World Energy Solutions, Inc.**

(Exact name of registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of incorporation or organization)

**04-3474959**

(I.R.S. Employer Identification Number)

**100 Front Street**

**Worcester, Massachusetts 01608**

(Address of principal executive offices)

**508-459-8100**

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically 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 (§232.405 of this chapter) 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 whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☐

Accelerated filer ☐

Non-accelerated filer ☐

Smaller reporting company ☒

(Do not check if a smaller reporting company)

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

As of October 31, 2014, the registrant had 12,713,158 shares of common stock outstanding.



## TABLE OF CONTENTS

|  | <u>Page</u> |
|--|-------------|
| <b>PART I. Financial Information</b>   |             |
| Item 1. <u>Financial Statements (Unaudited)</u>  | 2           |
| <u>Condensed Consolidated Balance Sheets as of September 30, 2014 and December 31, 2013</u>                            | 2           |
| <u>Condensed Consolidated Statements of Operations for the Three and Nine Months Ended September 30, 2014 and 2013</u> | 3           |
| <u>Condensed Consolidated Statements of Cash Flows for the Nine Months Ended September 30, 2014 and 2013</u>           | 4           |
| <u>Notes to Condensed Consolidated Financial Statements</u>  | 5           |
| Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>                   | 14          |
| Item 3. <u>Quantitative and Qualitative Disclosure about Market Risk</u>   | 24          |
| Item 4. <u>Controls and Procedures</u>   | 24          |
| <br><b>PART II. Other Information</b>  |             |
| Item 1. <u>Legal Proceedings</u>   | 25          |
| Item 1A. <u>Risk Factors</u>   | 25          |
| Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>   | 25          |
| Item 3. <u>Defaults Upon Senior Securities</u>   | 26          |
| Item 4. <u>Mine Safety Disclosures</u>   | 26          |
| Item 5. <u>Other Information</u>   | 26          |
| Item 6. <u>Exhibits</u>  | 26          |

---

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

**Item 1. Financial Statements**

**WORLD ENERGY SOLUTIONS, INC.**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**

|   | September 30,<br>2014<br>(Unaudited) | December 31,<br>2013 |
|---|--------------------------------------|----------------------|
| <b>ASSETS</b>   |                                      |                      |
| Current assets:   |                                      |                      |
| Cash and cash equivalents   | \$ 2,756,332                         | \$ 1,725,136         |
| Trade accounts receivable, net  | 7,995,230                            | 7,738,141            |
| Inventory   | 759,558                              | 415,770              |
| Current portion of deferred tax asset   | 907,093                              | 901,350              |
| Prepaid expenses and other current assets   | 579,902                              | 477,406              |
| Total current assets  | 12,998,115                           | 11,257,803           |
| Property and equipment, net   | 479,496                              | 573,778              |
| Intangible assets, net  | 12,577,919                           | 15,193,965           |
| Goodwill  | 16,167,834                           | 16,167,834           |
| Deferred tax asset, net of current portion  | 7,236,903                            | 7,198,984            |
| Other assets, net   | 986,047                              | 687,098              |
| Total assets  | <u>\$ 50,446,314</u>                 | <u>\$ 51,079,462</u> |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>   |                                      |                      |
| Current liabilities:  |                                      |                      |
| Accounts payable  | \$ 1,460,509                         | \$ 1,697,798         |
| Accrued commissions   | 1,666,733                            | 1,567,839            |
| Accrued compensation  | 2,322,224                            | 2,119,784            |
| Accrued contingent consideration  | —                                    | 1,000,000            |
| Accrued expenses and other current liabilities  | 1,329,233                            | 1,242,274            |
| Deferred revenue and customer advances  | 4,678,249                            | 3,546,380            |
| Related party subordinated notes payable  | —                                    | 500,000              |
| Current portion of long-term debt   | 1,117,904                            | 477,712              |
| Total current liabilities   | 12,574,852                           | 12,151,787           |
| Long-term debt, net of current portion  | 4,613,790                            | 5,522,288            |
| Subordinated note payable   | 4,000,000                            | 4,000,000            |
| Deferred revenue and customer advances, net of current portion  | 2,331,918                            | 3,910,035            |
| Other liabilities   | 11,679                               | 14,768               |
| Total liabilities   | 23,532,239                           | 25,598,878           |
| Commitments and contingencies (Note 13)   |                                      |                      |
| Stockholders' equity:   |                                      |                      |
| Preferred stock, \$0.0001 par value; 5,000,000 shares authorized, no shares issued or outstanding   | —                                    | —                    |
| Common stock, \$0.0001 par value; 30,000,000 shares authorized; 12,505,087 shares issued and 12,442,253 shares outstanding at September 30, 2014, and 12,178,366 shares issued and 12,120,338 shares outstanding at December 31, 2013 | 1,244                                | 1,212                |
| Additional paid-in capital  | 46,689,588                           | 44,894,961           |
| Accumulated deficit   | (19,497,759)                         | (19,156,245)         |
| Treasury stock, at cost: 62,834 shares at September 30, 2014 and 58,028 shares at December 31, 2013   | (278,998)                            | (259,344)            |
| Total stockholders' equity  | 26,914,075                           | 25,480,584           |
| Total liabilities and stockholders' equity  | <u>\$ 50,446,314</u>                 | <u>\$ 51,079,462</u> |

See accompanying notes to condensed consolidated financial statements.

**WORLD ENERGY SOLUTIONS, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
(Unaudited)

|   | Three Months Ended<br>September 30, |              | Nine Months Ended<br>September 30, |                |
|---|-------------------------------------|--------------|------------------------------------|----------------|
|   | 2014                                | 2013         | 2014                               | 2013           |
| <b>Revenue:</b>   |                                     |              |                                    |                |
| Brokerage commissions, transaction fees and efficiency projects | \$ 9,761,927                        | \$ 8,552,381 | \$ 28,314,705                      | \$ 24,767,574  |
| Management fees   | 155,712                             | 186,176      | 516,324                            | 564,122        |
| Total revenue   | 9,917,639                           | 8,738,557    | 28,831,029                         | 25,331,696     |
| <b>Cost of revenue</b>  | 2,669,066                           | 2,243,875    | 7,101,185                          | 6,621,481      |
| Gross profit  | 7,248,573                           | 6,494,682    | 21,729,844                         | 18,710,215     |
| <b>Operating expenses:</b>                                      |                                     |              |                                    |                |
| Sales and marketing   | 4,767,475                           | 4,875,985    | 14,163,226                         | 14,744,413     |
| General and administrative                                      | 2,399,892                           | 1,817,996    | 7,313,006                          | 6,046,690      |
| Total operating expenses  | 7,167,367                           | 6,693,981    | 21,476,232                         | 20,791,103     |
| Operating income (loss)   | 81,206                              | (199,299)    | 253,612                            | (2,080,888)    |
| Interest expense, net   | (196,010)                           | (253,822)    | (594,306)                          | (733,956)      |
| Other income  | 2,309                               | 3,378        | 11,024                             | 16,671         |
| Loss before income taxes  | (112,495)                           | (449,743)    | (329,670)                          | (2,798,173)    |
| <b>Income tax expense</b>                                       | (36,844)                            | (142,555)    | (11,844)                           | (405,165)      |
| Net loss  | \$ (149,339)                        | \$ (592,298) | \$ (341,514)                       | \$ (3,203,338) |
| <b>Net loss per common share — basic and diluted</b>            | \$ (0.01)                           | \$ (0.05)    | \$ (0.03)                          | \$ (0.27)      |
| Weighted average shares outstanding — basic and diluted         | 12,421,143                          | 12,007,667   | 12,309,029                         | 11,985,629     |

See accompanying notes to condensed consolidated financial statements.

**WORLD ENERGY SOLUTIONS, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(Unaudited)

|   | <u>Nine Months Ended September 30,</u> |                     |
|---|--|---------------------|
|   | <u>2014</u>                            | <u>2013</u>         |
| <b>Cash flows from operating activities:</b>                                    |  |                     |
| Net loss  | \$ (341,514)                           | \$ (3,203,338)      |
| Adjustments to reconcile net loss to net cash provided by operating activities: |  |                     |
| Depreciation and amortization   | 2,807,928                              | 3,116,907           |
| Deferred income taxes   | (43,662)                               | 326,415             |
| Stock-based compensation  | 662,624                                | 435,234             |
| Loss on disposal of property and equipment                                      | 4,698                                  | 11,177              |
| Non-cash interest expense on warrants related to debt discount                  | —                                      | 29,905              |
| Interest on accrued contingent consideration                                    | —                                      | 23,124              |
| Changes in operating assets and liabilities:                                    |  |                     |
| Trade accounts receivable, net  | (257,089)                              | 134,592             |
| Inventory   | (343,788)                              | (346,780)           |
| Prepaid expenses and other current assets                                       | (102,496)                              | (77,908)            |
| Accounts payable  | (237,289)                              | 576,980             |
| Accrued commissions   | 98,894                                 | 439,761             |
| Accrued compensation  | 202,440                                | (242,671)           |
| Accrued contingent consideration  | (72,000)                               | (478,099)           |
| Accrued expenses and other current liabilities                                  | 86,959                                 | (675,034)           |
| Deferred revenue and customer advances  | (446,248)                              | 2,095,996           |
| Net cash provided by operating activities                                       | <u>2,019,457</u>                       | <u>2,166,261</u>    |
| <b>Cash flows from investing activities:</b>                                    |  |                     |
| (Increase) decrease in other assets   | (336,908)                              | 34,078              |
| Purchases of property and equipment, net of disposals                           | (64,339)                               | (120,217)           |
| Net cash used in investing activities   | <u>(401,247)</u>                       | <u>(86,139)</u>     |
| <b>Cash flows from financing activities:</b>                                    |  |                     |
| Proceeds from exercise of stock options   | 204,035                                | 113,815             |
| Purchase of treasury stock  | (19,654)                               | (34,838)            |
| Principal payments on long-term debt  | (268,306)                              | (1,500,000)         |
| Principal payments on notes payable   | (500,000)                              | —                   |
| Payments of contingent consideration  | —                                      | (1,435,548)         |
| Principal payments on capital lease obligations                                 | (3,089)                                | (12,996)            |
| Net cash used in financing activities   | <u>(587,014)</u>                       | <u>(2,869,567)</u>  |
| Net increase (decrease) in cash and cash equivalents                            | 1,031,196                              | (789,445)           |
| Cash and cash equivalents, beginning of period                                  | 1,725,136                              | 3,307,822           |
| Cash and cash equivalents, end of period  | <u>\$ 2,756,332</u>                    | <u>\$ 2,518,377</u> |
| <b>Supplemental Disclosure of Cash Flow Information:</b>                        |  |                     |
| Net cash paid for interest  | <u>\$ 621,348</u>                      | <u>\$ 724,033</u>   |
| Net cash paid for income taxes  | <u>\$ 23,535</u>                       | <u>\$ 123,587</u>   |
| <b>Non-cash activities:</b>   |  |                     |
| Contingent consideration settled with common stock                              | <u>\$ 928,000</u>                      | <u>\$ —</u>         |
| Equipment acquired under capital leases   | <u>\$ —</u>                            | <u>\$ 21,416</u>    |

See accompanying notes to condensed consolidated financial statements.

**WORLD ENERGY SOLUTIONS, INC.**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(Unaudited)**

**September 30, 2014**

**1. Nature of Business and Basis of Presentation**

World Energy Solutions, Inc. ("World Energy" or the "Company") offers a range of energy management solutions to commercial and industrial businesses, institutions, utilities, and governments to reduce their overall energy costs. The Company comes to market with a holistic approach to energy management helping customers a) contract for a competitive price for energy, b) engage in energy efficiency projects to minimize quantity used and c) pursue available rebate and incentive programs. The Company made its mark on the industry with an innovative approach to procurement via its online auction platform, the World Energy Exchange®. With recent investments and acquisitions, World Energy is building out its energy efficiency practice engaging new customers while also pursuing more cross-selling opportunities for its procurement services.

**2. Interim Financial Statements**

The December 31, 2013 condensed consolidated balance sheet has been derived from audited consolidated financial statements and the accompanying September 30, 2014 unaudited interim condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC") regarding interim reporting. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America ("GAAP") for complete financial statements and should be read in conjunction with the audited consolidated financial statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2013, as filed with the SEC on March 31, 2014.

In the opinion of the Company's management, the unaudited interim condensed consolidated financial statements have been prepared on the same basis as the audited consolidated financial statements and include all adjustments consisting of normal recurring adjustments and accruals necessary for the fair presentation of the Company's financial position as of September 30, 2014, the results of its operations for the three and nine months ended September 30, 2014 and 2013 and the results of its cash flows for the nine months ended September 30, 2014 and 2013, respectively.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Accordingly, actual results could differ from these estimates.

The Company's most judgmental estimates affecting its condensed consolidated financial statements are those relating to revenue recognition and the estimate of actual energy delivered from the bidder to the lister of such energy; stock-based compensation; the valuation of intangible assets and goodwill; the valuation of contingent consideration; impairment of long-lived assets; and estimates of future taxable income as it relates to the realization of our net deferred tax assets. The Company regularly evaluates its estimates and assumptions based upon historical experience and various other factors that the Company believes to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. To the extent actual results differ from those estimates, future results of operations may be affected.

**3. Loss Per Share**

As of September 30, 2014 and 2013, the Company only had one issued and outstanding class of stock – common stock. The basic and diluted loss per share for the three and nine months ended September 30, 2014 and 2013 is computed by dividing net loss by the weighted average number of shares outstanding for the period.

The following table provides a reconciliation of the denominators of the Company's reported basic and diluted earnings per share computation for the three and nine months ended September 30, 2014 and 2013, respectively:

|  | For the three months ended<br>September 30, |            | For the nine months ended<br>September 30, |            |
|--|---|------------|--|------------|
|  | 2014  | 2013       | 2014                                       | 2013       |
| Weighted number of common shares - basic                         | 12,421,143                                  | 12,007,667 | 12,309,029                                 | 11,985,629 |
| Common stock equivalents   | —   | —          | —  | —          |
| Weighted number of common and common equivalent shares - diluted | 12,421,143                                  | 12,007,667 | 12,309,029                                 | 11,985,629 |

As the Company was in a net loss position for the three and nine months ended September 30, 2013, the computed diluted loss per share does not assume conversion, exercise, or contingent exercise of securities as that would have an anti-dilutive effect on the loss per share in those periods.

For the three and nine months ended September 30, 2014, 658,210, 49,545, and 251,750 shares issuable relative to common stock options, common stock warrants and restricted stock, respectively, were excluded from net loss per share since the inclusion of such shares would be anti-dilutive. For the three and nine months ended September 30, 2013, 787,106, 49,545 and 202,000 shares issuable relative to common stock options, common stock warrants and restricted stock, respectively, were excluded from net loss per share since the inclusion of such shares would be anti-dilutive. The Company did not declare or pay any dividends in 2014 or 2013.

#### 4. Concentration of Credit Risk and Off-Balance Sheet Risk

Financial instruments that potentially expose the Company to concentrations of credit risk consist principally of cash and cash equivalents and trade accounts receivable. The Company has no material off-balance sheet risk such as foreign exchange contracts, option contracts, or other foreign hedging arrangements. The Company places its cash and cash equivalents with two institutions, which management believes are of high credit quality. As of September 30, 2014, all of the Company's cash and cash equivalents are held in interest bearing accounts.

The Company provides credit in the form of invoiced and unbilled accounts receivable in the normal course of business. Collateral is not required for trade accounts receivable, but ongoing credit evaluations are performed. While the majority of the Company's revenue is generated from retail energy transactions where the winning bidder pays a commission to the Company, commission payments for certain auctions can be paid by the lister, bidder or a combination of both.

|        | Revenue for the three<br>months ended<br>September 30, |      | Revenue for the nine<br>months ended<br>September 30, |      | Trade Accounts<br>Receivable as of<br>September 30, |      |
|--------|--|------|---|------|---|------|
|        | 2014   | 2013 | 2014  | 2013 | 2014  | 2013 |
| Bidder |  |      |   |      |   |      |
| A      | 16%  | 14%  | 16%   | 16%  | 17%   | 17%  |
| B      | 8%   | 13%  | 10%   | 12%  | 12%   | 14%  |
| C      | 8%   | 8%   | 7%  | 8%   | 11%   | 10%  |

Two bidders merged at the end of 2013 and have been combined for presentation purposes above. In addition to its direct relationship with bidders, the Company also has direct contractual relationships with listers for the online procurement of certain of their energy, demand response or environmental needs. These listers are primarily large businesses and government organizations and do not have a direct creditor relationship with the Company. For the three and nine months ended September 30, 2014 and 2013, no lister represented more than 10% individually of the Company's aggregate revenue.

#### 5. Trade Accounts Receivable, Net

The Company does not invoice bidders for the commissions earned on retail electricity, certain natural gas and demand response transactions and, therefore, reports a significant portion of its receivables as "unbilled." Unbilled accounts receivable represent management's best estimate of energy provided by the energy suppliers to the energy consumers for a specific completed time period at contracted commission rates.

The Company does invoice bidders for commissions earned on wholesale and certain retail natural gas and energy efficiency transactions, which are reflected as billed accounts receivable. For natural gas and wholesale transactions, the total commission earned on these transactions is recognized upon completion of the procurement event and are generally due within 30 days of invoice date. For efficiency projects, revenue is recognized and invoiced upon project installation and acceptance, as required, and are generally due within 30 days of invoice date. In addition, the Company invoices the bidder, lister or combination of both for certain auctions performed for environmental commodity product transactions. These transactions are earned and invoiced either upon lister acceptance of the auction results or, in some cases, upon delivery of the credits or cash settlement of the transaction. Management provides for an allowance for doubtful accounts on a specifically identified basis, as well as through historical experience applied to an aging of accounts, if necessary. Trade accounts receivable are written off when deemed uncollectible. To date, write-offs have not been material. Trade accounts receivable, net consists of the following:

|                                 | September 30, 2014 | December 31, 2013 |
|---------------------------------|--------------------|-------------------|
| Unbilled accounts receivable    | \$ 6,716,918       | \$ 6,070,227      |
| Billed accounts receivable      | 1,823,491          | 1,993,093         |
|                                 | 8,540,409          | 8,063,320         |
| Allowance for doubtful accounts | (545,179)          | (325,179)         |
| Trade accounts receivable, net  | \$ 7,995,230       | \$ 7,738,141      |

## 6. Inventory

Inventory is maintained in the Company's Energy efficiency services segment and consists of prepaid expendables and project materials. Prepaid expendables represents consumable components that are used in project installations and are stated at the lower of cost or market, with cost being determined on a first-in, first-out (FIFO) basis. Historical inventory usage and current trends are considered in estimating both excess and obsolete inventory. To date, there have been no material write-downs of inventory and therefore no allowance for excess or obsolete inventory was recorded at September 30, 2014 or December 31, 2013. Project materials represent direct costs incurred on projects-in-process as of each reporting period. Inventory consists of the following:

|                     | September 30, 2014 | December 31, 2013 |
|---------------------|--------------------|-------------------|
| Prepaid expendables | \$ 53,957          | \$ 55,563         |
| Project materials   | 705,601            | 360,207           |
| Total inventory     | \$ 759,558         | \$ 415,770        |

## 7. Intangible Assets, Net

Intangibles, net with finite lives are summarized as follows as of September 30, 2014 and December 31, 2013:

|                        | Estimated Useful Life | September 30, 2014 |                          |              | December 31, 2013 |                          |              |
|------------------------|-----------------------|--------------------|--------------------------|--------------|-------------------|--------------------------|--------------|
|                        |                       | Carrying Amount    | Accumulated Amortization | Net          | Carrying Amount   | Accumulated Amortization | Net          |
| Customer contracts     | 1 - 4 years           | \$ 5,276,000       | \$ 3,980,000             | \$ 1,296,000 | \$ 5,276,000      | \$ 3,017,000             | \$ 2,259,000 |
| Customer relationships | 7 - 10 years          | 13,792,000         | 5,872,000                | 7,920,000    | 13,792,000        | 4,812,000                | 8,980,000    |
| Non-compete agreements | 5 years               | 2,585,000          | 1,350,000                | 1,235,000    | 2,585,000         | 962,000                  | 1,623,000    |
| Trade names            | 4 years               | 1,090,000          | 699,000                  | 391,000      | 1,090,000         | 494,000                  | 596,000      |
| Total                  |                       | \$22,743,000       | \$ 11,901,000            | \$10,842,000 | \$22,743,000      | \$ 9,285,000             | \$13,458,000 |

The Company also recorded acquisition related intangible assets with indefinite lives in the amount of \$1,736,000 pertaining to customer relationships, which is not reflected in the above tables.

Amortization expense was approximately \$2.6 million and \$2.9 million for the nine months ended September 30, 2014 and 2013, respectively. The approximate future amortization expense of intangible assets is as follows:

|                     |                      |
|---------------------|----------------------|
| Remainder of 2014   | \$ 754,000           |
| 2015                | 2,801,000            |
| 2016                | 2,416,000            |
| 2017                | 1,273,000            |
| 2018                | 915,000              |
| 2019 and thereafter | 2,683,000            |
|                     | <u>\$ 10,842,000</u> |

#### 8. Deferred Revenue and Customer Advances

Deferred revenue and customer advances arise when energy suppliers pay the Company a commission prior to the Company meeting all the requirements necessary to recognize revenue. In addition, deferred revenue and customer advances includes cash received for Energy efficiency services projects that have not been completed. Deferred revenue and customer advances expected to be recognized as revenue by year are approximately as follows:

|  | Amount              |
|--|---------------------|
| Remainder of 2014                            | \$ 789,000          |
| 2015   | 4,260,000           |
| 2016   | 1,386,000           |
| 2017   | 365,000             |
| 2018 and thereafter                          | 210,000             |
| Total deferred revenue and customer advances | <u>\$ 7,010,000</u> |

The following table provides a rollforward of deferred revenue and customer advances:

|                               | Amount              |
|-------------------------------|---------------------|
| Balance at January 1, 2014    | \$ 7,456,000        |
| Cash received                 | 3,724,000           |
| Revenue recognized            | (4,170,000)         |
| Balance at September 30, 2014 | <u>\$ 7,010,000</u> |

#### 9. Segment Reporting

The Company operates its business based on two industry segments: Energy procurement and Energy efficiency services. The Company delivers its Energy procurement services to four markets: retail energy, wholesale energy, demand response and environmental commodity. The Energy procurement process is substantially the same regardless of the market being serviced and is supported by the same operations personnel utilizing the same basic technology and back office support. There is no discrete financial information for these product lines nor are there segment managers who have operating responsibility for each product line. Energy efficiency services focuses on turn-key electrical, mechanical and lighting energy efficiency measures servicing commercial, industrial and institutional customers.

Segment operating income represents income from operations, including share-based compensation, amortization of intangible assets and depreciation. The following tables present certain continuing operating division information in accordance with the provisions of Accounting Standards Codification ("ASC") 280, "Segment Reporting".



|  | For the three months ended<br>September 30, |                     | For the nine months ended<br>September 30, |                       |
|--|---|---------------------|--|-----------------------|
|  | 2014  | 2013                | 2014                                       | 2013                  |
| <b>Consolidated revenue from external customers:</b>   |   |                     |  |                       |
| Energy procurement                                     | \$ 7,762,852                                | \$ 7,295,276        | \$ 23,686,849                              | \$ 21,673,273         |
| Energy efficiency services                             | 2,154,787                                   | 1,443,281           | 5,144,180                                  | 3,658,423             |
| Consolidated total revenue                             | <u>\$ 9,917,639</u>                         | <u>\$ 8,738,557</u> | <u>\$ 28,831,029</u>                       | <u>\$ 25,331,696</u>  |
| <b>Consolidated income (loss) before income taxes:</b> |   |                     |  |                       |
| Energy procurement                                     | \$ 33,901                                   | \$ (332,233)        | \$ 331,141                                 | \$ (2,131,734)        |
| Energy efficiency services                             | (146,396)                                   | (117,510)           | (660,811)                                  | (666,439)             |
| Consolidated loss before income taxes                  | <u>\$ (112,495)</u>                         | <u>\$ (449,743)</u> | <u>\$ (329,670)</u>                        | <u>\$ (2,798,173)</u> |

|                                    | For the three months ended<br>September 30, |                   | For the nine months ended<br>September 30, |                   |
|------------------------------------|---|-------------------|--|-------------------|
|                                    | 2014  | 2013              | 2014                                       | 2013              |
| <b>Energy Procurement:</b>         |   |                   |  |                   |
| Amortization                       | \$ 817,359                                  | \$ 943,977        | \$ 2,536,137                               | \$ 2,831,927      |
| Depreciation                       | \$ 42,566                                   | \$ 50,482         | \$ 133,939                                 | \$ 148,309        |
| Interest expense, net              | <u>\$ 196,010</u>                           | <u>\$ 253,822</u> | <u>\$ 594,306</u>                          | <u>\$ 733,956</u> |
| <b>Energy Efficiency Services:</b> |   |                   |  |                   |
| Amortization                       | \$ 39,289                                   | \$ 39,289         | \$ 117,868                                 | \$ 117,868        |
| Depreciation                       | \$ 6,361                                    | \$ 5,891          | \$ 19,984                                  | \$ 18,803         |
| Interest expense, net              | <u>\$ —</u>                                 | <u>\$ —</u>       | <u>\$ —</u>                                | <u>\$ —</u>       |

|                                   | September 30, 2014   | December 31, 2013    |
|-----------------------------------|----------------------|----------------------|
| <b>Consolidated total assets:</b> |                      |                      |
| Energy procurement                | \$ 44,086,032        | \$ 44,898,931        |
| Energy efficiency services        | 6,360,282            | 6,180,531            |
| Consolidated total assets         | <u>\$ 50,446,314</u> | <u>\$ 51,079,462</u> |

## 10. Income Taxes

In accordance with ASC 740, *Income Taxes*, each interim period is considered integral to the annual period and the tax benefit (expense) is measured using an estimated annual effective tax rate. An entity is required to record an income tax provision each quarter based on its best estimate of the annual effective tax rate for the full fiscal year and use that rate to provide for income taxes on a current year-to-date basis, as adjusted for discrete taxable events that occur during the interim period. If, however, the entity is unable to reliably estimate its annual effective tax rate, then the actual effective tax rate for the year-to-date period may be the best annual effective tax rate estimate. For the nine months ended September 30, 2014, the Company determined that it was unable to make a reliable estimate of the annual effective tax rate as relatively small changes in its projected income or loss produce significant variances in its annual effective tax rate. Therefore, the Company recorded a tax expense in the amount of \$37,000 and \$12,000 for the three and nine months ended September 30, 2014, respectively, based on the actual effective rate for the nine months ended September 30, 2014. The effective tax rate for the three and nine months ended September 30, 2013 was calculated based on an estimated annual effective tax rate resulting in an income tax expense of \$143,000 and \$405,000, respectively.

## 11. Fair Value Measurement and Fair Value of Financial Instruments

The Company follows ASC 820, "Fair Value Measurements and Disclosures" ("ASC 820") for fair value measurements. ASC 820 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. The standard provides a consistent definition of fair value, which focuses on an exit price, which is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The standard also prioritizes, within the measurement of fair value, the use of market-based information over entity specific information and establishes a three-level hierarchy for fair value measurements based on the nature of inputs used in the valuation of an asset or liability as of the measurement date.

The hierarchy established under ASC 820 gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3).

Level 1 - Pricing inputs are quoted prices available in active markets for identical investments as of the reporting date. As required by ASC 820, the Company does not adjust the quoted price for these investments, even in situations where the Company holds a large position and a sale could reasonably impact the quoted price.

Level 2 - Pricing inputs are quoted prices for similar investments, or inputs that are observable, either directly or indirectly, for substantially the full term through corroboration with observable market data. Level 2 includes investments valued at quoted prices adjusted for legal or contractual restrictions specific to these investments.

Level 3 - Pricing inputs are unobservable for the investment, that is, inputs that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability. Level 3 includes investments that are supported by little or no market activity.

As of September 30, 2014, the Company did not have any assets and liabilities measured at fair values on a recurring basis.

Assets and liabilities of the Company measured at fair values on a recurring basis as of December 31, 2013 are summarized as follows:

|                          | December 31,<br>2013 | Level 1     | Level 2     | Level 3             |
|--------------------------|----------------------|-------------|-------------|---------------------|
| <b>Liabilities</b>       |                      |             |             |                     |
| Contingent consideration | \$ 1,000,000         | \$ —        | \$ —        | \$ 1,000,000        |
| <b>Total liabilities</b> | <b>\$ 1,000,000</b>  | <b>\$ —</b> | <b>\$ —</b> | <b>\$ 1,000,000</b> |

The Company determines the fair value of acquisition-related contingent consideration based on assessment of the probability that the Company would be required to make such future payment. Changes to the fair value of contingent consideration are recorded in general and administrative expense. During the nine months ended September 30, 2014, the Company settled its contingent consideration obligations. As part of the settlement, the Company issued 200,000 shares of common stock to GSE Consulting, L.P. ("GSE") that had a fair value of \$928,000 on the date of issuance.

The following table provides a rollforward of the fair value, as determined by Level 3 inputs, of the contingent consideration.

|   | For the nine months<br>ended September 30,<br>2014 |
|---|--|
| <b>Beginning balance</b>                  | \$ 1,000,000                                       |
| Additions                                 | —  |
| <b>Settlement</b>                         | (928,000)  |
| Change in fair value included in earnings | (72,000)   |
| <b>Accrued interest</b>                   | —  |
| <b>Ending balance</b>                     | <b>\$ —</b>  |

The carrying amounts and fair values of the Company's debt obligations are as follows:

|  | September 30, 2014 |              | December 31, 2013 |               |
|--|--------------------|--------------|-------------------|---------------|
|  | Carrying Value     | Fair Value   | Carrying Value    | Fair Value    |
| <u>Term loan</u>                         | \$ 5,731,694       | \$ 5,731,694 | \$ 6,000,000      | \$ 6,000,000  |
| Subordinated notes payable               | 4,000,000          | 4,000,000    | 4,000,000         | 4,000,000     |
| Related party subordinated notes payable | —                  | —            | 500,000           | 500,000       |
| Total debt obligations                   | \$ 9,731,694       | \$ 9,731,694 | \$ 10,500,000     | \$ 10,500,000 |

The carrying amount for fixed rate long-term debt and variable rate long-term debt approximate fair value because the underlying instruments are primarily at current market rates available to the Company for similar borrowings. The interest rate on the Commerce Bank and Trust Company ("Commerce") debt is tied to the prime rate and will fluctuate with changes in that rate. Related party notes payable are classified as short-term on the Company's accompanying condensed consolidated balance sheets.

## 12. Credit Arrangements

### Credit Facility

The Company has a \$8.5 million credit facility with Commerce consisting of a revolving credit facility of up to \$2.5 million (the "Revolver") that matures on December 30, 2016 and a 60-month term loan of \$6.0 million (the "Term Loan").

The Revolver bears interest at the prime rate plus 1.75% (totaling 5% at September 30, 2014) and is adjusted every six months for any change in the prime rate. In addition to changes in the Prime Rate, the rate can be reduced by up to .50% based on certain EBITDA achievement levels. Under the Revolver, the Company may borrow, repay and re-borrow an amount not to exceed the lesser of \$2.5 million or the total of 80% of eligible billed and unbilled accounts receivable (less the aggregate outstanding on any letters of credit). There have been no borrowings under the Revolver.

The Term Loan bears interest for the first 6 months at the prime rate plus 2.75% (totaling 6% at September 30, 2014), and is adjusted every six months for any change in the prime rate. In addition to changes in the prime rate, the rate can be reduced by up to .50% based on certain EBITDA achievement levels. The Term Loan was interest only for six months followed by 54 monthly principal and interest payments which commenced on July 30, 2014 with a balloon payment for any remaining principal balance at maturity.

### Subordinated Notes

On October 3, 2012, the Company entered into a Note Purchase Agreement with Massachusetts Capital Resource Company ("MCRC"), in which the Company entered into an 8-year, \$4.0 million Subordinated Note due September 30, 2020 with MCRC (the "MCRC Note"). The MCRC Note bears interest at 10.5% and is interest only for the first four years followed by 48 equal principal payments commencing October 31, 2016. The Company must pay a premium of 3% if it prepays the MCRC Note before October 1, 2014 and a 1% premium if it prepays the MCRC Note before October 1, 2015. The MCRC Note is subordinated to the Company's credit facility with Commerce and contains a Minimum Fixed Charge Ratio covenant that the Company is in compliance with at September 30, 2014.

## 13. Commitments and Contingencies

### Litigation

Two former employees/consultants of GSE have filed two separate complaints in the District Courts of Dallas County and Tarrant County Texas against World Energy and GSE Consulting, LP alleging, among other things, claims related to breach of contract, quantum meruit, unjust enrichment, promissory estoppel, tortious interference, fraud, assumed liability, and civil conspiracy. One of the plaintiffs has filed a claim against a GSE principal for intentional infliction of emotional distress. Each plaintiff claims that GSE and/or the Company failed to pay commissions due for services that they provided prior to the date of the Company's purchase of certain GSE assets, based on their respective employment or independent contractor agreements with GSE. Each plaintiff has also asserted claims for recovery of their attorneys' fees. The Company denies the allegations and has filed counterclaims for damages, asserting claims for conversion, unjust enrichment, misappropriation of confidential information, and violation of the Texas Theft

Liability Act against each of the plaintiffs. The Company has also filed a counterclaim against one of the plaintiffs for her breach of a non-competition and non-solicitation agreement, based on her working for a competitor of the Company's during her one-year restrictive period and her improper solicitation of former GSE customers on behalf of the competitor. The Company also filed a counterclaim against the other plaintiff for breach of contract based on the exclusivity obligation set forth in her independent contractor agreement. This counterclaim will only apply if the jury finds that World Energy assumed the plaintiff's independent contractor agreement. The Company's motions for summary judgment seeking dismissal of all of the plaintiff's claims was denied in its entirety in one of the cases. In the other case, the Company's motion for summary judgment was partially granted, dismissing the plaintiff's civil conspiracy claim. One of the plaintiffs successfully moved for summary judgment on all counterclaims except the breach of contract based on the exclusivity obligation. The courts have assigned trial dates of November 17, 2014 and January 26, 2015. The court recently granted a continuance of the November 17<sup>th</sup> trial to a time and date to be determined in February / March 2015.

The Company has estimated the potential commissions allegedly due to the two plaintiffs to be approximately \$0.3 million. The Company has not recorded any accrual for contingent liabilities associated with these legal proceedings based on its belief that any potential loss, while reasonably possible, is not probable. The Company intends to continue to defend these actions vigorously and is currently unable to estimate a range of payments, if any, it may be required to pay, with respect to these claims. Further, the Company believes that the resolution of these matters will not result in a material effect to its condensed consolidated financial statements. However, due to uncertainties that accompany litigation of this nature, there could be no assurance that the Company will be successful, and the resolution of the lawsuits could have a material effect on its accompanying condensed consolidated financial statements.

In addition, the Company had filed cross claims against GSE for indemnification under the Asset Purchase Agreement in each of the plaintiffs' cases. The GSE affiliates and principals had also asserted cross claims against the Company seeking indemnification under the Asset Purchase Agreement. In December 2013, GSE had amended its cross claims in one of the matters to include claims asserting breach of the earnout provisions in the Asset Purchase Agreement. In April 2014, the Company and GSE settled all claims against each other related to these lawsuits and the earnout provisions. The Company and GSE filed with the court agreed motions to dismiss all claims against one another, which were allowed by the court. The settlement called for the Company to issue 200,000 shares of common stock to GSE and its affiliates that had a fair value of \$0.9 million on the date issued.

From time to time, the Company may be subject to legal proceedings and claims arising from the conduct of its business operations, including litigation related to employment matters. While it is impossible to ascertain the ultimate legal and financial liability with respect to contingent liabilities, including lawsuits, management believes that the aggregate amount of such liabilities, if any, will not have a material adverse effect on its condensed consolidated financial position and/or results of operations. It is possible, however, that future financial position or results of operations for any particular period could be materially affected by changes in the Company's assumptions or strategies related to those contingencies or changes out of its control.

#### **14. Subsequent Event**

On November 4, 2014, the Company entered into an Agreement and Plan of Merger (the "Merger Agreement") with EnerNOC, Inc. ("Parent") and Wolf Merger Sub Corporation, a wholly owned subsidiary of Parent ("Merger Sub"), pursuant to which Parent and Merger Sub will commence an offer (the "Offer") to acquire all of the outstanding shares of the Company's common stock (the "Shares"), at a price of \$5.50 per share in cash (the "Offer Price"). The Merger Sub is required to commence the Offer no later than 10 business days after the date of the Merger Agreement. If the Offer is consummated, Shares not tendered will be acquired by Merger Sub in a second step merger (the "Merger") for the Offer Price.

Completion of the Offer is subject to a number of conditions, including (i) that a majority of the Shares outstanding be validly tendered and not validly withdrawn prior to the expiration of the Offer; (ii) completion of a 55-day "go-shop" period during which time the Company will solicit alternative proposals to the Offer and Merger and (iii) certain other customary conditions. The Offer and the Merger are not subject to any financing conditions. The Board has approved the Merger Agreement and unanimously recommends that stockholders of the Company tender their Shares in the Offer. The Company will file a Schedule 14D-9 with the SEC containing the recommendation of the Board on the same day that the Offer is commenced.

Parent and the Company have made customary representations, warranties and covenants in the Merger Agreement, including covenants (i) to promptly make all filings required by the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and other applicable laws with respect to the Offer and the Merger; and (ii) to use their reasonable best efforts to take all appropriate action to consummate and effectuate the Offer, the Merger and the other transactions contemplated by the Merger Agreement. Additionally, prior to consummation of the Merger, the Company has agreed to conduct its business in all material respects in the ordinary and usual course and to comply with certain other operating covenants through the consummation of the Merger.

Prior to the closing of the Offer, the Board may, subject to compliance with certain obligations, (i) terminate the Merger Agreement to enter into a definitive agreement with respect to a Takeover Proposal; or (ii) change its recommendation to the Company's stockholders regarding tendering into the Offer and approving the Merger and related transactions and the Board determines in good faith, after consultation with its legal advisors, that failure to take such action would be inconsistent with the directors' fiduciary duties under applicable law. Upon termination of the Merger Agreement under specified circumstances, the Company and the Parent will be required to pay termination and reverse termination fees, respectively.

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

*This quarterly report on Form 10-Q including this Item 2, contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, which involve risks and uncertainties. Readers can identify these statements by forward-looking words such as "may," "could," "should," "would," "intend," "will," "expect," "anticipate," "believe," "estimate," "continue" or similar words. Our actual results and the timing of certain events may differ significantly from the results and timing discussed in the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those discussed or referred to in this report and in the "Risk Factors" section of our Annual Report on Form 10-K and any later publicly available filing with the Securities and Exchange Commission ("SEC"). The following discussion and analysis of our financial condition and results of operations should be read in light of those factors and in conjunction with our accompanying condensed consolidated financial statements and notes thereto.*

### Overview

World Energy (the "Company") offers a range of energy management solutions to commercial and industrial businesses, institutions, utilities, and governments to reduce their overall energy costs. We come to market with a holistic approach to energy management helping customers a) contract for a competitive price for energy, b) engage in energy efficiency projects to minimize quantity used and c) pursue available rebate and incentive programs. We made our mark on the industry with an innovative approach to procurement via our online auction platform, the World Energy Exchange®. With recent investments and acquisitions, we are building out our energy efficiency practice by engaging new customers while also pursuing more cross-selling opportunities for our procurement services.

We provide energy management services utilizing state-of-the-art technology and the experience of a seasoned management team to bring lower energy costs to its customers. We use a simple equation

$$E = P \cdot Q - i$$

to help customers to understand the holistic nature of the energy management problem. Total energy cost (E) is a function of Energy Price (P) times the Quantity of Energy Consumed (Q), minus any rebates or incentives (i) the customer can earn. This approach not only makes energy management more approachable for customers, simplifying what has become an increasingly dynamic and complex problem, it also highlights the inter-related nature of the energy management challenge. We assert that point solution vendors may optimize one of the three elements, but we believe it takes looking at the problem holistically to unlock the most savings.

Acquisitions are an important component of our business strategy. Our focus is on both our core procurement business as well as new product lines within the energy management services industry such as energy efficiency services.

During the fourth quarter of 2012, we acquired substantially all of the assets and assumed certain obligations of Northeast Energy Partners, LLC ("NEP") pursuant to an Asset Purchase Agreement (the "Asset Purchase Agreement") between us, NEP, and its members. NEP was a Connecticut based energy management and procurement company. During the third and fourth quarters of 2011 we acquired the energy procurement business of Co-eXprise, Inc. ("Co-eXprise"), Northeast Energy Solutions, LLC ("NES") and GSE Consulting, LP ("GSE"). These acquisitions expanded our capabilities in the Energy efficiency services segment, enabled us to enter the growing small- and medium-sized customer Energy procurement marketplaces, and consolidate the large commercial, industrial and government auction space. With the acquisition of NES, we are managing the business as two business segments: Energy procurement and Energy efficiency services.

On November 4, 2014, we entered into an Agreement and Plan of Merger (the "Merger Agreement") with EnerNOC, Inc. ("Parent") and Wolf Merger Sub Corporation, a wholly owned subsidiary of Parent ("Merger Sub"), pursuant to which Parent and Merger Sub will commence an offer (the "Offer") to acquire all of the outstanding shares of our common stock (the "Shares"), at a price of \$5.50 per share in cash (the "Offer Price"). The Merger Sub is required to commence the Offer no later than 10 business days after the date of the Merger Agreement. If the Offer is consummated, Shares not tendered will be acquired by Merger Sub in a second step merger (the "Merger") for the Offer Price.

Completion of the Offer is subject to a number of conditions, including (i) that a majority of the Shares outstanding be validly tendered and not validly withdrawn prior to the expiration of the Offer; (ii) completion of a 55-day "go-shop" period during which time we will solicit alternative proposals to the Offer and Merger and (iii) certain other customary conditions. The Offer and the Merger are not subject to any financing conditions. The Board has approved the Merger Agreement and unanimously recommends that our stockholders tender their Shares in the Offer. We will file a Schedule 14D-9 with the SEC containing the recommendation of the Board on the same day that the Offer is commenced.

Parent and the Company have made customary representations, warranties and covenants in the Merger Agreement, including covenants (i) to promptly make all filings required by the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and other applicable laws with respect to the Offer and the Merger; and (ii) to use their reasonable best efforts to take all appropriate action to consummate and effectuate the Offer, the Merger and the other transactions contemplated by the Merger Agreement. Additionally, prior to consummation of the Merger, we have agreed to conduct our business in all material respects in the ordinary and usual course and to comply with certain other operating covenants through the consummation of the Merger.

Prior to the closing of the Offer, the Board may, subject to compliance with certain obligations, (i) terminate the Merger Agreement to enter into a definitive agreement with respect to a Takeover Proposal; or (ii) change its recommendation to our stockholders regarding tendering into the Offer and approving the Merger and related transactions and the Board determines in good faith, after consultation with its legal advisors, that failure to take such action would be inconsistent with the directors' fiduciary duties under applicable law. Upon termination of the Merger Agreement under specified circumstances, the Company and the Parent will be required to pay termination and reverse termination fees, respectively.

Our business model is heavily dependent on our people. We have significantly grown our employee base from 20 at the time of our initial public offering in November 2006 to 130 at September 30, 2014. This planned investment in staffing has been, and will continue to be, a key component of our strategic initiatives and revenue growth. These infrastructure investments will result in increased operating costs in the short-term, but in the long-term we expect them to generate cash flow and profitability as we build incremental revenue. To date we have funded our acquisitions and strategic investments primarily with cash on-hand, notes payable, cash from operations and long-term debt. We have also deferred portions of the purchase prices through the use of earnouts that are tied to the ongoing performance of the acquired entity. Through the utilization of seller notes and earnouts, we have been able to finance a portion of the cost of the acquisitions over time with the targets' ongoing cash flow. These acquisition activities will increase our operating costs both in the short and long-term and may require us to borrow against our current credit facility and/or raise funds through additional capital raises.

## **Operations**

### **Revenue**

#### **Retail Electricity Transactions**

We earn a monthly commission on energy sales contracted through our online auction platform from each bidder or energy supplier based on the energy usage transacted between the bidder and lister or energy consumer. Our commissions are not based on the retail price for electricity; rather on the amount of energy consumed. Commissions are calculated based on the volume of energy usage transacted between the energy supplier and energy consumer multiplied by our contractual commission rate. Our contractual commission rate is negotiated with the energy consumer on a procurement-by-procurement basis based on energy consumer specific circumstances, including the size of auction, the effort required to organize and run the respective auction and competitive factors, among others. Once the contractual commission is agreed to with the energy consumer, all energy suppliers participating in the auction agree to that rate. That commission rate remains fixed for the duration of the contractual term regardless of energy usage. Energy consumers provide us with a letter of authorization to request their usage history from the local utility. We then use this data to compile a usage profile for that energy consumer that will become the basis for the auction. This data may also be used to estimate revenue on a going forward basis, as noted below.

Historically, our revenue and operating results have varied from quarter-to-quarter and are expected to continue to fluctuate in the future. These fluctuations are primarily due to the buying patterns of our wholesale and natural gas customers, which tend to have large, seasonal purchases during the fourth and first quarters and electricity usage having higher demand in our second and third quarters. In addition, the activity levels on the World Energy Exchange<sup>®</sup> can fluctuate due to a number of factors, including market prices, weather conditions, energy consumers' credit ratings, the ability of suppliers to obtain financing in credit markets, and economic and geopolitical events. To the extent these factors affect the purchasing decisions of energy consumers, our future results of operations may be affected. Contracts between energy suppliers and energy consumers are signed for a variety of term lengths, with a one to two year contract term being typical for commercial and industrial energy consumers, and government contracts typically having two to three year terms.

We do not invoice our electricity energy suppliers for monthly commissions earned and, therefore, we report a substantial portion of our receivables as "unbilled." Unbilled accounts receivable is based on management's best estimate of energy provided by the energy suppliers to the energy consumers for a specific completed time period at contracted commission rates and is made up of two components. The first component represents energy usage for which we have received actual data from the supplier and/or the utility, but for which payment has not been received at the balance sheet date. The majority of our contractual relationships with energy suppliers require them to supply actual usage data to us on a monthly basis and remit payment to us based on that usage. The second component represents energy usage for which we have not received actual data, but for which we have estimated usage.

Commissions paid in advance by certain bidders are recorded as deferred revenue and amortized to commission revenue on a monthly basis on the energy exchanged that month.

#### Retail Natural Gas Transactions

There are two primary fee components to our retail natural gas services: transaction fees and management fees. Transaction fees are billed to and paid by the energy supplier awarded business on the platform. These fees are established prior to award and are the same for each supplier. For the majority of our natural gas transactions, we bill the supplier upon the conclusion of the transaction based on the estimated energy volume transacted for the entire award term multiplied by the transaction fee. Management fees are paid by our energy consumers and are generally billed on a monthly basis for services rendered based on terms and conditions included in contractual arrangements. While substantially all of our retail natural gas transactions are accounted for in accordance with this policy, a significant percentage is accounted for as the natural gas is consumed by the energy consumer and recognized as revenue in accordance with the retail electricity transaction revenue recognition methodology described above.

#### Mid-Market Transactions

We earn a monthly commission on energy sales from each energy supplier based on the energy usage transacted between the energy supplier and energy consumer. The commissions are not based on the retail price for electricity but rather on the amount of energy consumed. Commissions are calculated based on the energy usage transacted between the energy supplier and energy consumer multiplied by our contractual commission rate. Revenue from commissions is recognized as earned over the life of each contract as energy is consumed, provided there is persuasive evidence of an arrangement, the sales price is fixed or determinable, collection of the fee is reasonably assured, and customer acceptance criteria, if any, has been successfully demonstrated. We generally recognize revenue on these transactions when we have received verification from the energy supplier of the end-users energy usage and energy supplier's subsequent collection of the fees billed to the end user. The verification is generally accompanied with payment of the agreed upon fee to us, at which time the revenue is recognized. Commissions paid in advance are recorded as customer advances and are recognized monthly as commission revenue based on the energy exchanged that month. To the extent we do not receive verification of actual energy usage or we cannot reliably estimate what actual energy usage was for a given period, revenue is deferred until usage and collection data is received from the energy supplier. To the extent that we do not receive actual usage data from the energy supplier, we will recognize revenue at the end of the contract flow date.

#### Demand Response Transactions

Demand response transaction fees are recognized when we have received confirmation from the demand response provider ("DRP") that the energy consumer has performed under the applicable Regional Transmission Organization ("RTO") or Independent System Operator ("ISO") program requirements. The energy consumer is either called to perform during an actual curtailment event or is required to demonstrate its ability to perform in a test event during the performance period. For the PJM Interconnection ("PJM"), an RTO that coordinates the movement of wholesale electricity in all or parts of 13 states and the District of Columbia, the performance period is June through September in a calendar year. Test results are submitted to the PJM by the DRPs and we receive confirmation of the energy consumer's performance in the fourth quarter. DRPs typically pay us ratably on a quarterly basis throughout the demand response fiscal (June to May) year. As a result, a portion of the revenue we recognize is reflected as unbilled accounts receivable.

#### Wholesale and Environmental Commodity Transactions

Wholesale transaction fees are invoiced upon the conclusion of the auction based on a fixed fee. These revenues are not tied to future energy usage and are recognized upon the completion of the online auction. For reverse auctions where our customers bid for a consumer's business, the fees are paid by the bidder. For forward auctions where a lister is selling energy products, the fees are typically paid by the lister.

Environmental commodity transaction fees are accounted for utilizing two primary methods. For regulated allowance programs like Regional Greenhouse Gas Initiative, Inc. ("RGGI"), fees are paid by the lister and are recognized quarterly as revenue as auctions are completed and approved. For most other environmental commodity transactions both the lister and the bidder pay the transaction fee and revenue is recognized upon the consummation of the underlying transaction as credits are delivered by the lister and payment is made by the bidder.

#### Energy Efficiency Services

Our Energy efficiency services segment is primarily project driven where we identify efficiency measures that energy consumers can implement to reduce their energy usage. We present retrofit opportunities to customers, get approval from them to proceed and submit the proposal to the local utility for cost reimbursement. Once the utility approves funding for the project, we



install the equipment, typically new heating, ventilation or air conditioning equipment, or replace lighting fixtures to more efficient models. We recognize revenue for Energy efficiency services when persuasive evidence of an arrangement exists, delivery has occurred, the price is fixed or determinable and collectability is reasonably assured. Due to the short-term nature of projects (typically two to three weeks), we utilize the completed-contract method. We also assess multiple contracts entered into by the same customer in close proximity to determine if the contracts should be combined for revenue recognition purposes. Revenues are recognized based upon factors such as passage of title, installation, payments and customer acceptance.

#### ***Cost of revenue***

Cost of revenue consists primarily of:

- salaries, bonus and commissions, employee benefits and share-based compensation associated with our auction management and efficiency services, which are directly related to the development and production of the online auction and maintenance of market-related data on our auction platform and monthly management fees (our supply desk function);
- project costs including direct labor equipment and materials directly associated with efficiency projects; and
- rent, depreciation and other related overhead and facility-related costs.

#### ***Sales and marketing***

Sales and marketing expenses consist primarily of:

- salaries, bonus and commissions, employee benefits and share-based compensation related to sales and marketing personnel;
- third party commission expenses to our channel partners;
- travel and related expenses;
- amortization related to customer relationships and contracts;
- rent, depreciation and other related overhead and facility-related costs; and
- general marketing costs such as trade shows, marketing materials and outsourced services.

#### ***General and administrative***

General and administrative expenses consist primarily of:

- salaries, bonus and commissions, employee benefits and share-based compensation related to general and administrative personnel;
- accounting, legal, investor relations, information technology, insurance and other professional fees; and
- rent, depreciation and other related overhead and facility-related costs.

#### ***Interest expense, net***

Interest expense, net consists primarily of:

- interest income earned on cash held in the bank; and
- interest expense related to bank term loans, notes payable and contingent consideration.

#### ***Income tax benefit (expense)***

Income tax benefit (expense) is based on projected annualized taxable income or loss when this can be reliably estimated. In the event that we cannot reliably estimate due to the fact that a relatively small change in projected annualized taxable income or loss produces a significant variance in our annual effective tax rate then we utilize the actual effective rate for the year to date period.

Under both scenarios, the benefit (expense) also reflects our deferred tax provision, federal alternative minimum liability, if applicable, and state income taxes.

|                              | For the Three Months Ended<br>September 30, |      | For the Nine Months Ended<br>September 30, |       |
|------------------------------|---|------|--|-------|
|                              | 2014  | 2013 | 2014                                       | 2013  |
| Revenue                      | 100%  | 100% | 100%                                       | 100%  |
| Cost of revenue              | 27  | 26   | 25   | 26    |
| Gross profit                 | 73  | 74   | 75   | 74    |
| Operating expenses:          |   |      |  |       |
| Sales and marketing          | 48  | 56   | 49   | 58    |
| General and administrative   | 24  | 20   | 25   | 24    |
| Operating income (loss)      | 1   | (2)  | 1  | (8)   |
| Other expense, net           | (2)   | (3)  | (2)  | (3)   |
| Income tax benefit (expense) | 0   | (2)  | 0  | (2)   |
| Net income (loss)            | (1%)  | (7%) | (1%)                                       | (13%) |

### Results of Operations

The following table sets forth certain items as a percent of revenue for the periods presented:

#### Comparison of the Three Months Ended September 30, 2014 and 2013

##### Revenue

|                            | For the Three Months Ended<br>September 30, |              |              |     |
|----------------------------|---|--------------|--------------|-----|
|                            | 2014  | 2013         | Increase     |     |
| Energy procurement         | \$ 7,762,852                                | \$ 7,295,276 | \$ 467,576   | 6%  |
| Energy efficiency services | 2,154,787                                   | 1,443,281    | 711,506      | 49  |
| Total revenue              | \$ 9,917,639                                | \$ 8,738,557 | \$ 1,179,082 | 13% |

Revenue increased 13% for the three months ended September 30, 2014 as revenue from both segments increased as compared to the same period in 2013. Energy procurement segment revenue increased 6% due to increased transaction activity from our auction, mid-market and wholesale customers as well as increased revenue recognized from previously deferred items. These increases were partially offset by a decrease of in-period natural gas transaction activity. Energy efficiency services segment revenue increased 49% as the rebuilt Massachusetts sales team continued to deliver an increase in the number of projects as well as an increase in the average project size compared to the third quarter of 2013.

##### Cost of revenue

|                            | For the Three Months Ended September 30, |              |              |              |                     |       |
|----------------------------|--|--------------|--------------|--------------|---------------------|-------|
|                            | 2014                                     |              | 2013         |              |                     |       |
|                            | \$                                       | % of Revenue | \$           | % of Revenue | Increase (Decrease) |       |
| Energy procurement         | \$ 959,069                               | 12%          | \$ 1,141,432 | 16%          | \$ (182,363)        | (16%) |
| Energy efficiency services | 1,709,997                                | 79           | 1,102,443    | 76           | 607,554             | 55    |
| Total cost of revenue      | \$ 2,669,066                             | 27%          | \$ 2,243,875 | 26%          | \$ 425,191          | 19%   |

Cost of revenue increased 19% for the three months ended September 30, 2014 as compared to the same period in 2013. Cost of revenue for our Energy procurement segment decreased 16% due to decreases in payroll reflecting our integration, automation and reorganization efforts. Cost of revenue associated with our Energy procurement segment as a percent of revenue decreased by 4% primarily due to the cost decreases described above and, to a lesser extent, the 6% increase in Energy procurement revenue. Cost of revenue associated with our Energy efficiency services segment increased 55% primarily due to an increase in project costs associated with the 49% increase in revenue. Cost of revenue associated with our Energy efficiency services segment as a percent of revenue increased by 3% primarily due to a lower contribution margin on one large project completed in the third quarter of 2014.

## Operating expenses

|                            | For the Three Months Ended September 30, |                 |                    |                 |                     |      |
|----------------------------|--|-----------------|--------------------|-----------------|---------------------|------|
|                            | 2014                                     |                 | 2013               |                 |                     |      |
|                            | \$                                       | %<br>of Revenue | \$                 | %<br>of Revenue | Increase (Decrease) |      |
| Sales and marketing        | \$4,767,475                              | 48%             | \$4,875,985        | 56%             | \$ (108,510)        | (2%) |
| General and administrative | 2,399,892                                | 24              | 1,817,996          | 20              | 581,896             | 32   |
| Total operating expenses   | <u>\$7,167,367</u>                       | 72%             | <u>\$6,693,981</u> | 76%             | <u>\$ 473,386</u>   | 7%   |

Sales and marketing expenses decreased 2% for the three months ended September 30, 2014 as compared to the same period in 2013 primarily due to decreases in internal commissions, marketing expenses and amortization of intangible assets. Internal commissions decreased due to the change in commission policy for our mid-market group that we implemented in the second quarter of 2013. Under the revised policy, we continued to pay commissions based on cash received from mid-market transactions that were deferred for revenue purposes and also provided for a bookings bonus to offset the impact of the change in our policy. We converted the bookings bonus to a draw program in 2014, eliminating that component of commission expense. The decrease resulting from this change in policy was substantially offset by increases in efficiency and energy procurement commissions. Amortization expense related to intangible assets decreased as certain intangible assets related to our acquisitions became fully amortized in 2014. These decreases were partially offset by an increase in share-based compensation and third party commission expense. Sales and marketing expense as a percentage of revenue decreased 8% primarily due to the 13% increase in total revenue.

The 32% increase in general and administrative expenses for the three months ended September 30, 2014 as compared to the same period in 2013 was primarily due to merger related costs associated with the proposed sale of the Company to EnerNOC as well as an increase in payroll costs. In addition, the third quarter of last year benefitted from a decrease in contingent consideration. Payroll costs increased primarily due to investments in our product development team. General and administrative expenses as a percent of revenue increased 4% due to the transaction costs described above.

### Other income (expense), net

We recorded net interest expense of approximately \$0.2 million for the three months ended September 30, 2014 compared to net interest expense of approximately \$0.3 for the three months ended September 30, 2013. The decrease in net interest expense in 2014 was primarily due to a reduction in the interest rate charged on our long-term debt resulting from the replacement of our credit facility in the fourth quarter of 2013.

### Income tax benefit (expense)

We recorded an income tax expense of approximately \$37,000 for the three months ended September 30, 2014 and an income tax expense of approximately \$0.1 million for the three months ended September 30, 2013. For the three months ended September 30, 2014, we utilized our actual effective tax rate as the basis for the income tax expense as we were unable to make a reliable estimate of our annual effective tax rate. For the three months ended September 30, 2013, the effective tax rate was based on our estimated annual effective tax rate. The income tax expense for the three months ended September 30, 2014 reflects a deferred tax benefit and state income taxes. The income tax expense for the three months ended September 30, 2013 reflects a deferred tax provision, federal alternative minimum tax liability and state income taxes.

### Net loss

We reported a net loss of approximately \$0.1 million for the three months ended September 30, 2014 and approximately \$0.6 million for the three months ended September 30, 2013. The \$0.5 million decrease in net loss was primarily due to the increase in revenue, improved gross margin and the decrease in sales and marketing expenses. These increases were partially offset by an increase in general and administrative costs associated with our proposed merger with EnerNOC.

**Comparison of the Nine Months Ended September 30, 2014 and 2013**

**Revenue**

|                            | For the Nine Months Ended September 30, |                      |                     |            |
|----------------------------|---|----------------------|---------------------|------------|
|                            | 2014                                    | 2013                 | Increase            |            |
| Energy procurement         | \$ 23,686,849                           | \$ 21,673,273        | \$ 2,013,576        | 9%         |
| Energy efficiency services | 5,144,180                               | 3,658,423            | 1,485,757           | 41         |
| <b>Total revenue</b>       | <b>\$ 28,831,029</b>                    | <b>\$ 25,331,696</b> | <b>\$ 3,499,333</b> | <b>14%</b> |

Revenue increased 14% for the nine months ended September 30, 2014 as revenue from both segments increased as compared to the same period in 2013. Energy procurement segment revenue increased 9% due to increased transaction activity from our auction and mid-market customers as well as increased revenue recognized from previously deferred items. These increases were partially offset by a decrease in gas transaction activity in the nine months ended September 30, 2014 as increased commodity prices during the first quarter resulted in delayed contracting decisions by listers. Energy efficiency services segment revenue increased 41% as the rebuilt Massachusetts sales team continued to deliver increased revenue in the NSTAR territory in Massachusetts during the nine months ended September 30, 2014 as compared to the nine months ended September 30, 2013.

**Cost of revenue**

|                              | For the Nine Months Ended September 30, |              |                    |              |                     |           |
|------------------------------|---|--------------|--------------------|--------------|---------------------|-----------|
|                              | 2014                                    |              | 2013               |              | Increase (Decrease) |           |
|                              | \$                                      | % of Revenue | \$                 | % of Revenue |                     |           |
| Energy procurement           | \$2,979,002                             | 13%          | \$3,639,116        | 17%          | \$ (660,114)        | (18%)     |
| Energy efficiency services   | 4,122,183                               | 80           | 2,982,365          | 82           | 1,139,818           | 38        |
| <b>Total cost of revenue</b> | <b>\$7,101,185</b>                      | <b>25%</b>   | <b>\$6,621,481</b> | <b>26%</b>   | <b>\$ 479,704</b>   | <b>7%</b> |

Cost of revenue increased 7% for the nine months ended September 30, 2014 as compared to the same period in 2013. Cost of revenue for our Energy procurement segment decreased 18% due to decreases in payroll reflecting our integration, automation and reorganization efforts. Cost of revenue associated with our Energy procurement segment as a percent of revenue decreased by 4% primarily due to the cost decreases described above and, to a lesser extent, the 9% increase in Energy procurement revenue. Cost of revenue associated with our Energy efficiency services segment increased 38% primarily due to an increase in project costs associated with the 41% increase in revenue. Cost of revenue associated with our Energy efficiency services segment as a percent of revenue decreased by 2% primarily due to improved contribution margins on projects completed in the nine months ended September 30, 2014 as compared to the nine months ended September 30, 2013.

**Operating expenses**

|                                 | For the Nine Months Ended September 30, |              |                     |              |                     |           |
|---------------------------------|---|--------------|---------------------|--------------|---------------------|-----------|
|                                 | 2014                                    |              | 2013                |              | Increase (Decrease) |           |
|                                 | \$                                      | % of Revenue | \$                  | % of Revenue |                     |           |
| Sales and marketing             | \$14,163,226                            | 49%          | \$14,744,413        | 58%          | \$ (581,187)        | (4%)      |
| General and administrative      | 7,313,006                               | 25           | 6,046,690           | 24           | 1,266,316           | 21        |
| <b>Total operating expenses</b> | <b>\$21,476,232</b>                     | <b>75%</b>   | <b>\$20,791,103</b> | <b>82%</b>   | <b>\$ 685,129</b>   | <b>3%</b> |

Sales and marketing expenses decreased 4% for the nine months ended September 30, 2014 as compared to the same period in 2013 primarily due to decreases in internal commissions and amortization of intangible assets. Internal commissions decreased due to the change in commission policy for our mid-market group that we implemented in the second quarter of 2013. Under the revised policy, we continued to pay commissions based on cash received from mid-market transactions that were deferred for revenue purposes and provided for a bookings bonus to offset the impact of the change in our policy. We converted the bookings bonus to a draw program in 2014, eliminating that component of commission expense. This decrease in mid-market commissions was offset by increased commission expense for our auction and efficiency groups. Amortization expense related to intangible assets decreased as certain intangible assets related to our acquisitions became fully amortized in 2014. These decreases were partially offset by an increase in third party commission expense as we continued to expand our channel partner network. Sales and marketing expense as a percentage of revenue decreased 9% primarily due to the 14% increase in revenue.

The 21% increase in general and administrative expenses for the nine months ended September 30, 2014 as compared to the same period in 2013 was due to an increase in legal, transaction, and payroll costs. Legal and transaction costs increased primarily due to a shareholder action during the first quarter of 2014 and the proposed sale of the Company to EnerNOC. Payroll costs increased due to investments in our product development team. In addition, 2013 benefitted from a decrease in contingent consideration. General and administrative expenses as a percent of revenue was substantially consistent with the prior year period as the 14% increase in revenue offset the above noted cost increases.

*Other income (expense), net*

We recorded net interest expense of approximately \$0.6 million for the nine months ended September 30, 2014 compared to net interest expense of approximately \$0.7 million for the nine months ended September 30, 2013. The decrease in net interest expense in 2014 was primarily due to a reduction in the interest rate charged on our long-term debt resulting from the replacement of our credit facility in the fourth quarter of 2013.

*Income tax benefit (expense)*

We recorded an income tax expense of approximately \$12,000 for the nine months ended September 30, 2014 and an income tax expense of approximately \$0.4 million for the nine months ended September 30, 2013. For the nine months ended September 30, 2014, we utilized our actual year-to-date effective tax rate as the basis for the income tax expense as we were unable to rely on our annual effective tax rate. For the nine months ended September 30, 2013, the effective tax rate was based on our estimated annual effective tax rate. The income tax expense for the nine months ended September 30, 2014 reflects a deferred tax benefit and state income taxes. The income tax expense for the nine months ended September 30, 2013 reflects a deferred tax provision, federal alternative minimum tax liability and state income taxes.

*Net loss*

Net loss improved approximately \$2.9 million for the nine months ended September 30, 2014 compared to the same period in 2013, primarily due the increase in revenue, improved gross margin and the decrease in sales and marketing expenses. These decreases in net loss were partially offset by the increase in general and administrative expenses.

**Liquidity and Capital Resources**

At September 30, 2014, we had no commitments for material capital expenditures. We have identified and executed against a number of strategic initiatives that we believe are key components of our future growth, including: making strategic acquisitions; entering into other energy-related markets including energy efficiency; expanding our community of listers, bidders and channel partners on our exchanges; strengthening and extending our long-term relationships with government agencies; and growing our direct and inside sales force. As of September 30, 2014 our workforce numbered 130, an increase of four from the number that we employed at December 31, 2013. At September 30, 2014, we had 62 professionals in our sales and marketing and account management groups, 41 in our supply desk group and 27 in our general and administrative group.

We paid \$10.4 million to acquire three businesses in 2011 through the use of cash on hand, cash flow from ongoing operations as well as cash flow generated by the acquisitions. In addition, we have paid \$6.7 million in seller notes and contingent consideration bringing the total cash paid for the 2011 acquisitions to \$17.1 million. In October 2012, we acquired NEP for \$11.3 million. We funded this acquisition through the issuance of \$8.0 million in long-term bank debt, a \$2.0 million seller note and \$1.3 million in contingent consideration. While the expansion/addition of these debt instruments significantly increased our commitments, we believe we have the resources to meet both our short- and long-term obligations under these arrangements based on cash on-hand, operating cash flows from our base business and cash expected to be generated from all of our acquired businesses. We subsequently retired the seller note and contingent consideration payments and commenced repayment of the long-term bank debt. In addition, in 2014 we settled all outstanding earnout claims with GSE by issuing 200,000 shares of common stock, which had a fair value of approximately \$0.9 million. As of September 30, 2014 we have retired all of our seller-note and earnout obligations related to all of our acquisitions. During the nine months ended September 30, 2014 we generated cash flow from operations of \$2.0 million and ended the quarter with \$2.8 million in cash and cash equivalents.

**Comparison of September 30, 2014 to December 31, 2013**

|                                | September 30,<br>2014 | December 31,<br>2013 | Increase (Decrease) |     |
|--------------------------------|-----------------------|----------------------|---------------------|-----|
| Cash and cash equivalents      | \$ 2,756,332          | \$ 1,725,136         | \$ 1,031,196        | 60% |
| Trade accounts receivable, net | 7,995,230             | 7,738,141            | 257,089             | 3   |
| Days sales outstanding         | 74                    | 76                   | (2)                 | (3) |
| Working capital (deficit)      | 423,263               | (893,984)            | 1,317,247           | 147 |
| Stockholders' equity           | 26,914,075            | 25,480,584           | 1,433,491           | 6   |

Cash and cash equivalents increased 60% primarily due to cash flows from operations of approximately \$2.0 million. Trade accounts receivable at September 30, 2014 increased 3% as compared to the fourth quarter of 2013 as days sales outstanding (representing accounts receivable outstanding at September 30, 2014 divided by the average sales per day during the three months ended September 30, 2014, as adjusted) decreased 3%. Days sales outstanding decreased 3% due to the timing of in-period revenue recognized and cash receipts within the nine months ended September 30, 2014 as compared to the same period in 2013. Revenue from bidders representing 10% or more of our revenue decreased to 26% from two bidders during the nine months ended September 30, 2014, from an aggregate 28% for two bidders in the same period of the previous year. Two bidders merged at the end of 2013 and have been combined to determine the percentages above in both periods.

The working capital balance at September 30, 2014 (consisting of current assets less current liabilities) improved \$1.3 million from December 31, 2013. Current assets increased \$1.7 million primarily due to the increase in cash and cash equivalents. Current liabilities increased \$0.4 million due to increases in short-term deferred revenue and long-term debt. These increases were partially offset by the settlement of our contingent consideration obligations and the \$0.5 million payment against the short-term related party note. Stockholders' equity increased 6% for the nine months ended September 30, 2014 primarily due to the issuance of shares under the GSE settlement and share-based compensation.

Cash provided by operating activities for the nine months ended September 30, 2014 and 2013 was approximately \$2.0 million and \$2.2 million, respectively. Cash used in investing activities for the nine months ended September 30, 2014 was approximately \$0.4 million primarily due to capitalized software cost. Cash used in financing activities for the nine months ended September 30, 2014 and 2013 was approximately \$0.6 million and \$2.9 million, respectively. Cash used in financing activities for the nine months ended September 30, 2014 primarily resulted from the final \$0.5 million payment of the NEP seller note and repayment of long-term debt, both partially offset by proceeds from the exercise of stock options. Cash used in financing activities for the nine months ended September 30, 2013 was primarily due to a contingent consideration payment of \$1.4 million and \$1.5 million of principal payments on long term debt.

Adjusted EBITDA, representing net loss adjusted for non-recurring transaction costs before interest, income taxes, depreciation and amortization for the nine months ended September 30, 2014 was \$3.6 million as compared to \$1.1 million for the same period in the prior year. Please refer to the section below discussing non-GAAP financial measures for a reconciliation of non-GAAP measures to the most directly comparable measure calculated and presented in accordance with accounting principles generally accepted in the United States of America ("GAAP").

In this Quarterly Report on Form 10-Q, we provide certain "non-GAAP financial measures". A non-GAAP financial measure refers to a numerical financial measure that excludes (or includes) amounts that are included in (or excluded from) the most directly comparable financial measure calculated and presented in accordance with GAAP in our financial statements. In this Quarterly Report on Form 10-Q, we provide Non-GAAP adjusted net income (loss) and adjusted EBITDA as additional information relating to our operating results. These non-GAAP measures exclude expenses related to the proposed sale of the Company to EnerNOC, depreciation related to our fixed assets, amortization expense related to acquisition-related assets and other assets, interest expense on bank borrowings, notes payable to sellers and contingent consideration, interest income on invested funds, and income taxes. Management uses these non-GAAP measures for internal reporting and bank reporting purposes. We have provided these non-GAAP financial measures in addition to GAAP financial results because we believe that these non-GAAP financial measures provide useful information to certain investors and financial analysts in assessing our operating performance due to the following factors:

- We believe that the presentation of a non-GAAP measure that adjusts for depreciation of fixed assets, amortization expense related to acquisition-related assets and other assets, interest expense on bank borrowings, seller notes and contingent consideration, interest income on invested funds, and income taxes, provides investors and financial analysts with a consistent basis for comparison across accounting periods and, therefore, is useful to investors and financial analysts in helping them to better understand our operating results and underlying operational trends;

- We do not regularly incur costs relating to an evaluation of strategic alternatives and costs associated with entering into an Agreement and Plan of Merger. We identify these costs as non-recurring and, once incurred, generally cannot be changed or influenced by management;
- We do not acquire intangible assets on a predictable cycle. Our intangible assets relate solely to business acquisitions. Amortization costs are fixed at the time of an acquisition, are then amortized over a period of several years after the acquisition and generally cannot be changed or influenced by management after the acquisition;
- We do not regularly incur capitalized software and website costs. Our capitalized software costs relate primarily to the build-out of our exchanges. Amortization costs are fixed at the time the costs are incurred and are then amortized over a period of several years and generally cannot be changed or influenced by management after the initial costs are incurred;
- We do not regularly invest in fixed assets. Our fixed assets relate primarily to computer and office equipment and furniture and fixtures. Depreciation costs are fixed at the time of purchase and are then depreciated over several years and generally cannot be changed or influenced by management after the purchase;
- We do not regularly enter into bank debt, seller notes and/or pay interest on contingent consideration. Our seller notes and contingent consideration relate to acquisition activities. Interest expense is fixed at the time of purchase and recorded over the life of the lease and generally cannot be changed or influenced by management after the purchase;
- We do not regularly earn interest on our cash accounts. Our cash has not yielded material returns to date and these returns generally cannot be changed or influenced by management; and
- We do not regularly pay federal or state income taxes due to our net operating loss carryforwards. Our income tax expense reflects the release of our deferred tax assets to apply to projected annualized taxable income, and an anticipated alternative minimum tax liability based on statutory rates that generally cannot be changed or influenced by management.

Pursuant to the requirements of the SEC, we have provided below a reconciliation of the non-GAAP financial measures used to the most directly comparable financial measures prepared in accordance with GAAP. These non-GAAP financial measures are not prepared in accordance with GAAP. These measures may differ from the GAAP information, even where similarly titled used by other companies, and therefore should not be used to compare our performance to that of other companies. The presentation of this additional information is not meant to be considered in isolation or as a substitute for net income (loss) prepared in accordance with GAAP.

|                                      | Three Months Ended September 30, |              | Nine Months Ended September 30, |                |
|--------------------------------------|----------------------------------|--------------|---------------------------------|----------------|
|                                      | 2014                             | 2013         | 2014                            | 2013           |
| GAAP net loss                        | \$ (149,339)                     | \$ (592,298) | \$ (341,514)                    | \$ (3,203,338) |
| Add: Non-recurring transaction costs | 405,807                          | —            | 488,807                         | —              |
| Non-GAAP adjusted net income (loss)  | \$ 256,468                       | \$ (592,298) | \$ 147,293                      | \$ (3,203,338) |
| Add: Interest expense, net           | 196,010                          | 253,822      | 594,306                         | 733,956        |
| Add: Income taxes                    | 36,844                           | 142,555      | 11,844                          | 405,165        |
| Add: Amortization of intangibles     | 844,701                          | 974,759      | 2,616,046                       | 2,924,275      |
| Add: Amortization of other assets    | 11,947                           | 8,507        | 37,959                          | 25,520         |
| Add: Depreciation                    | 48,927                           | 56,373       | 153,923                         | 167,112        |
| Non-GAAP adjusted EBITDA             | \$ 1,394,897                     | \$ 843,718   | \$ 3,561,371                    | \$ 1,052,690   |

#### **Critical Accounting Policies**

The preparation of financial statements in conformity with GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Accordingly, actual results could differ from these estimates.

The most judgmental estimates affecting our consolidated financial statements are those relating to revenue recognition and the estimate of actual energy delivered from the bidder to the lister of such energy; stock-based compensation; the valuation of intangible assets and goodwill; the valuation of contingent consideration; impairment of long-lived assets; and estimates of future taxable income as it relates to the realization of our net deferred tax assets. We regularly evaluate our estimates and assumptions based upon historical

experience and various other factors that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. To the extent actual results differ from those estimates; future results of operations may be affected. Refer to Note 2 of our consolidated financial statements within our Annual Report on Form 10-K as filed with the SEC on March 31, 2014 for a description of our accounting policies.

#### **Off-Balance Sheet Arrangements**

We currently have no off-balance sheet arrangements that have or are reasonably likely to have a current or future material effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

#### **Item 3. Quantitative and Qualitative Disclosure about Market Risk**

As a smaller reporting company as defined by Rule 12b-2 of the Exchange Act and in Item 10(f)(1) of Regulation S-K, we are electing scaled disclosure reporting obligations and therefore are not required to provide the information requested by this Item.

#### **Item 4. Controls and Procedures**

##### **Evaluation of Disclosure Controls and Procedures**

As required by Rule 13a-15 under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), the Company carried out an evaluation under the supervision and with the participation of the Company's management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the Company's disclosure controls and procedures as of December 31, 2013. In designing and evaluating the Company's disclosure controls and procedures, the Company and its management recognize that there are inherent limitations to the effectiveness of any system of disclosure controls and procedures, including the possibility of human error and the circumvention or overriding of the controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their desired control objectives. Additionally, in evaluating and implementing possible controls and procedures, the Company's management was required to apply its reasonable judgment. Based upon the required evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that as of September 30, 2014, the Company's disclosure controls and procedures were effective at the reasonable assurance level to ensure that information required to be disclosed by the Company in the reports it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and procedures also were effective in ensuring that information required to be disclosed by the Company in the reports it files or submits under the Exchange Act is accumulated and communicated to its management, including the Company's Chief Executive Officer and Chief Financial Officer as appropriate, to allow timely decisions regarding required disclosure.

##### **Changes in Internal Control Over Financial Reporting**

There was no change in the Company's internal control over financial reporting that occurred during the three months ended September 30, 2014 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.



## PART II OTHER INFORMATION

### Item 1. Legal Proceedings

Two former employees/consultants of GSE have filed two separate complaints in the District Courts of Dallas County and Tarrant County Texas against GSE Consulting, LP and us alleging, among other things, claims related to breach of contract, quantum meruit, unjust enrichment, promissory estoppel, tortious interference, fraud, assumed liability, and civil conspiracy. One of the plaintiffs has filed a claim against a GSE principal for intentional infliction of emotional distress. Each plaintiff claims that GSE and/or we failed to pay commissions due for services that they provided prior to the date of the Company's purchase of certain GSE assets, based on their respective employment or independent contractor agreements with GSE. Each plaintiff has also asserted claims for recovery of their attorneys' fees. We deny the allegations and have filed counterclaims for damages, asserting claims for conversion, unjust enrichment, misappropriation of confidential information, and violation of the Texas Theft Liability Act against each of the plaintiffs. We have also filed a counterclaim against one of the plaintiffs for her breach of a non-competition and non-solicitation agreement, based on her working for a competitor of ours during her one-year restrictive period and her improper solicitation of former GSE customers on behalf of the competitor. We have also filed a counterclaim against the other plaintiff for breach of contract based on the exclusivity obligation set forth in her independent contractor agreement. This counterclaim will only apply if the jury finds that we assumed the plaintiff's independent contractor agreement. Our motions for summary judgment seeking dismissal of all of the plaintiff's claims was denied in its entirety in one of the cases. In the other case, our motion for summary judgment was partially granted, dismissing the plaintiff's civil conspiracy claim. One of the plaintiffs successfully moved for summary judgment on all counterclaims except the breach of contract based on the exclusivity obligation. The courts have assigned trial dates of November 17, 2014 and January 26, 2015. The court recently granted a continuance of the November 17<sup>th</sup> trial to a time and date to be determined in February / March 2015.

We have estimated the potential commissions allegedly due to the two plaintiffs to be approximately \$0.3 million. We have not recorded any accrual for contingent liabilities associated with these legal proceedings based on its belief that any potential loss, while reasonably possible, is not probable. We intend to continue to defend these actions vigorously and are currently unable to estimate a range of payments, if any, we may be required to pay, with respect to these claims. Further, we believe that the resolution of these matters will not result in a material effect to our condensed consolidated financial statements. However, due to uncertainties that accompany litigation of this nature, there could be no assurance that we will be successful, and the resolution of the lawsuits could have a material effect on our accompanying condensed consolidated financial statements.

In addition, we had filed cross claims against GSE for indemnification under the Asset Purchase Agreement in each of the plaintiffs' cases. The GSE affiliates and principals had also asserted cross claims against us seeking indemnification under the Asset Purchase Agreement. In December 2013, GSE had amended its cross claims in one of the matters to include claims asserting breach of the earnout provisions in the Asset Purchase Agreement. In April 2014, GSE and we settled all claims against each other related to these lawsuits and the earnout provisions. We and GSE filed with the court agreed motions to dismiss all claims against one another, which were allowed by the court. The settlement called for us to issue 200,000 shares of common stock to GSE and its affiliates that had a fair value of \$0.9 million on the date issued.

From time to time, we may be subject to legal proceedings and claims arising from the conduct of its business operations, including litigation related to employment matters. While it is impossible to ascertain the ultimate legal and financial liability with respect to contingent liabilities, including lawsuits, we believe that the aggregate amount of such liabilities, if any, will not have a material adverse effect on our condensed consolidated financial position and/or results of operations. It is possible, however, that future financial position or results of operations for any particular period could be materially affected by changes in our assumptions or strategies related to those contingencies or changes out of our control.

### Item 1A. Risk Factors

There have been no material changes from risk factors previously disclosed in our annual report on Form 10-K for the fiscal year ended December 31, 2013, as filed with the Securities and Exchange Commission on March 31, 2014.

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

#### Recent Sales of Unregistered Securities; Use of Proceeds from Registered Securities

During the quarter ended September 30, 2014, we did not sell any unregistered equity securities.

### Purchases of Equity Securities by the Issuer and Affiliated Purchasers

In connection with the vesting of restricted stock granted to employees, we withheld certain shares with value equivalent to employees' minimum statutory obligations for the applicable income and other employment taxes.

A summary of the shares withheld to satisfy employee tax withholding obligations for the three months ended September 30, 2014 is as follows:

| Period              | Total Number<br>of<br>Shares<br>Purchased | Average Price<br>Paid<br>Per Share | Total Number<br>of<br>Shares<br>Purchased<br>As Part of<br>Publicly<br>Announced<br>Plans or<br>Programs | Maximum<br>Number<br>of Shares That<br>May<br>Yet Be<br>Purchased<br>Under The Plan |
|---------------------|---|------------------------------------|--|---|
| 07/01/14 – 07/31/14 | —   | \$ —                               | —  | —   |
| 08/01/14 – 08/31/14 | 37  | \$ 4.20                            | —  | —   |
| 09/01/14 – 09/30/14 | —   | \$ —                               | —  | —   |
| Total               | 37  | \$ 4.20                            | —  | —   |

### **Item 3. Defaults Upon Senior Securities**

None.

### **Item 4. Mine Safety Disclosures**

None.

### **Item 5. Other Information**

None.

### **Item 6. Exhibits**

- 2.1 Agreement and Plan of Merger by and among World Energy Solutions, Inc., EnerNOC, Inc., and Wolf Merger Sub Corporation, dated November 4, 2014 (incorporated by reference to Exhibit 2.2 to our report on Form 8-K filed November 5, 2014).
- 3.1 Amended and Restated By-Laws effective November 3, 2014 (incorporated by reference to Exhibit 2.2 to our report on Form 8-K filed November 5, 2014).
- 31.1 Certification of the Chief Executive Officer pursuant to §302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of the Chief Financial Officer pursuant to §302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of the Chief Executive Officer pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of the Chief Financial Officer pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002.
- 101 The following materials from World Energy Solutions, Inc.'s Quarterly Report on Form 10-Q for the three and nine months ended September 30, 2014, formatted in Extensible Business Reporting Language: (i) the condensed consolidated balance sheets; (ii) the condensed consolidated statements of operations; (iii) the condensed consolidated statements of cash flows; and (iv) notes to the condensed consolidated financial statements.

## SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

World Energy Solutions, Inc.

Dated: November 10, 2014

By: /s/ Philip Adams  
Philip Adams  
Chief Executive Officer

Dated: November 10, 2014

By: /s/ James Parslow  
James Parslow  
Chief Financial Officer

**CERTIFICATION OF THE CHIEF EXECUTIVE OFFICER PURSUANT TO  
§302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Philip Adams, certify that:

1. I have reviewed this quarterly report on Form 10-Q of World Energy Solutions, Inc. (the "Registrant");

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

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

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

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

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

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

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

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

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

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

Dated: November 10, 2014

By: /s/ Philip Adams

Philip Adams  
Chief Executive Officer

**CERTIFICATION OF THE CHIEF FINANCIAL OFFICER PURSUANT TO  
§302 OF THE SARBANES-OXLEY ACT OF 2002**

I, James Parslow, certify that:

1. I have reviewed this quarterly report on Form 10-Q of World Energy Solutions, Inc. (the "Registrant");
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this report;
4. The Registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the Registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the Registrant's internal control over financial reporting that occurred during the Registrant's most recent fiscal quarter (the Registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the Registrant's internal control over financial reporting;
5. The Registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant's auditors and the audit committee of the Registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant's internal control over financial reporting.

Dated: November 10, 2014

By: /s/ James Parslow  
James Parslow  
Chief Financial Officer

**CERTIFICATION PURSUANT TO 18 U.S.C. §1350, AS ADOPTED  
PURSUANT TO §906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the filing of this quarterly report of World Energy Solutions, Inc. (the "Company") on Form 10-Q (the "Report") for the period ended September 30, 2014 as filed with the Securities and Exchange Commission on the date hereof, I, Philip Adams, Chief Executive Officer of the Company, certify, to the best of my knowledge, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: November 10, 2014

By: /s/ Philip Adams  
Philip Adams  
Chief Executive Officer

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

**CERTIFICATION PURSUANT TO 18 U.S.C. §1350, AS ADOPTED  
PURSUANT TO §906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the filing of this quarterly report of World Energy Solutions, Inc. (the "Company") on Form 10-Q (the "Report") for the period ended September 30, 2014 as filed with the Securities and Exchange Commission on the date hereof, I, James Parslow, Chief Financial Officer of the Company, certify that, to the best of my knowledge, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: November 10, 2014

By: /s/ James Parslow

James Parslow  
Chief Financial Officer

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



#### **Exhibit C-4 "Financial Arrangements"**

World Energy Solutions, Inc. is an online auction provider and energy broker. World Energy Solutions, Inc. does not take title to the electricity. However, World Energy Solutions, Inc. does have bank financing agreements through Commerce Bank & Trust Company and Massachusetts Capital Resource Company. Copies of those bank financing agreements can be found in the attached 8K filings dated January 6, 2014 and October 4, 2012 respectively.



# WORLD ENERGY SOLUTIONS, INC.

## FORM 8-K (Current report filing)

Filed 01/06/14 for the Period Ending 12/30/13

|             |  |
|-------------|--|
| Address     | 100 FRONT STREET<br>WORCESTER, MA 01608            |
| Telephone   | 508-459-8100                                       |
| CIK         | 0001371781   |
| Symbol      | XWES   |
| SIC Code    | 7389 - Business Services, Not Elsewhere Classified |
| Industry    | Investment Services                                |
| Sector      | Financial  |
| Fiscal Year | 12/31  |

---

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

---

**FORM 8-K**

---

**CURRENT REPORT**  
**Pursuant to Section 13 or 15(d)**  
**of the Securities Exchange Act of 1934**

**Date of Report (Date of earliest event reported): December 30, 2013**

---

**World Energy Solutions, Inc.**  
(Exact Name of Registrant as Specified in Charter)

---

**Delaware**  
(State or Other Jurisdiction  
of Incorporation)

**001-34289**  
(Commission  
File Number)

**04-3474959**  
(IRS Employer  
Identification No.)

**100 Front Street**  
**Worcester, Massachusetts**  
(Address of Principal Executive Offices)

**01608**  
(Zip Code)

**Registrant's telephone number, including area code: (508) 459-8100**

**n/a**  
(Former Name or Former Address, if Changed Since Last Report)

---

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions ( *see* General Instruction A.2. below):

- ☐ Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)
  - ☐ Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)
  - ☐ Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))
  - ☐ Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))
-

---

**Item 2.03. Creation of a Direct Financial Obligation or an Obligation under an Off-Balance Sheet Arrangement of a Registrant.**

On December 30, 2013, World Energy Solutions, Inc. (the "Company") entered into a Loan and Security Agreement (the "Agreement") with Commerce Bank & Trust Company ("Commerce Bank"). Under the Agreement, Commerce Bank has committed to a 3-year revolving credit facility of up to \$2,500,000 and a 60-month term loan of \$6,000,000. The Commerce Bank credit facility replaces the Company's prior \$9,000,000 credit facility with Silicon Valley Bank.

The \$2,500,000, 3-year revolving credit facility bears interest at the Prime Rate plus 1.75% (5% at December 30, 2013), and is adjusted every 6-months for any change in the Prime Rate. In addition to changes in the Prime Rate, the rate can be reduced by up to .50% based on certain EBITDA achievement levels. The Company may borrow, repay and re-borrow an amount not to exceed the lesser of \$2,500,000 or the total of 80% of eligible billed and unbilled accounts receivable (less the aggregate outstanding on any letters of credit). The Company has not borrowed against this revolving credit facility.

The 60-month term loan of \$6,000,000 bears interest for the first 6 months at the Prime Rate plus 2.75% (6% at December 30, 2013), and is adjusted every 6-months for any change in the Prime Rate. In addition to changes in the Prime Rate, the rate can be reduced by up to .50% based on certain EBITDA achievement levels. The term loan is interest only for six months followed by 54 principal and interest payments commencing on July 30, 2014 with a balloon payment for any remaining principal balance at maturity.

The loans may be prepaid without penalty. The current indebtedness to Massachusetts Capital Resource Company is subordinated to the Commerce Bank loans. The Company intends to use the credit facility as working capital and to pay off its existing facility with Silicon Valley Bank. The Silicon Valley Bank facility was paid off in full as of December 31, 2013.

The credit facility is secured by a first priority perfected security interest in substantially all of the Company's assets and all of the assets of World Energy Securities Corp.

The Loan and Security Agreement contains certain affirmative and negative covenants including a minimum Debt Service Coverage Ratio and financial reporting requirements. Any failure by the Company to comply with these covenants and any other obligations under the Agreement could result in an event of default which could lead to acceleration of the amounts owed and other remedies.

The foregoing description of the loan facility with Commerce Bank does not purport to be complete and is qualified in its entirety by reference to the full text of the Loan and Security Agreement, the \$2,500,000 Revolving Credit Note, the \$6,000,000 Term Note, and the Subordination Agreement, all of which are attached to this Current Report as Exhibit 10.1, 10.2, 10.3 and 10.4, respectively, and incorporated herein by reference. A Press Release announcing the new loan facility is also attached to this Current Report as Exhibit 99.1.

**Item 9.01. Financial Statements and Exhibits.****(d) Exhibits**

See Exhibit Index attached hereto.

---

**SIGNATURE**

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

WORLD ENERGY SOLUTIONS, INC.

Date: January 6, 2014

By: /s/ James Parslow

James Parslow

Chief Financial Officer

---

## EXHIBIT INDEX

| <u>Exhibit</u> | <u>Description</u>   |
|----------------|--|
| 10.1           | Loan and Security Agreement by and between World Energy Solutions, Inc. and Commerce Bank & Trust Company dated December 30, 2013. |
| 10.2           | \$2,500,000 Revolving Credit Note for the benefit of Commerce Bank & Trust Company dated December 30, 2013.                        |
| 10.3           | \$6,000,000 Term Note for the benefit of Commerce Bank & Trust Company dated December 30, 2013.                                    |
| 10.4           | Subordination Agreement between Commerce Bank & Trust Company and Massachusetts Capital Resource Company dated December 30, 2013.  |
| 99.1           | Press Release dated January 6, 2014.   |

## LOAN AND SECURITY AGREEMENT

THIS LOAN AND SECURITY AGREEMENT dated as of December 30, 2013 is by and between **WORLD ENERGY SOLUTIONS, INC.**, a Delaware corporation with its principal place of business at 100 Front Street, 20<sup>th</sup> Floor, Worcester, Massachusetts 01608 (the "Borrower") and **COMMERCE BANK & TRUST COMPANY**, a Massachusetts banking corporation with an office at 386 Main Street, Worcester, Massachusetts 01608 (the "Lender").

### WITNESSETH:

**BACKGROUND.** The Borrower has requested the Lender to lend it up to the sum of \$2,500,000.00 on a revolving loan basis (the "Revolving Credit") and the sum of \$6,000,000.00 on a term loan basis (the "Term Loan") (the Revolving Credit and the Term Loan hereinafter together referred to as the "Loans"), and the Lender is willing to do so upon the terms and conditions hereinafter set forth.

NOW, THEREFORE, in consideration of the premises herein contained, and each intending to be legally bound hereby, the parties agree as follows:

### ARTICLE 1.0 DEFINITIONS

1.01 As used herein:

"Accounts", "Chattel Paper", "Collateral", "Commercial Tort Claims", "Contracts", "Deposit Accounts", "Documents", "Electronic Chattel Paper", "Equipment", "Financial Assets", "Fixtures", "General Intangibles", "Goods", "Instruments", "Inventory", "Investment Property", "Letter-of-Credit-Rights", "Payment Intangibles", "Promissory Notes", "Supporting Obligations" and "Tangible Chattel Paper" shall have the same respective meanings as are given to those terms in the Uniform Commercial Code as in effect from time to time in The Commonwealth of Massachusetts, if not otherwise defined in this Agreement.

"Actual EBITDA" shall mean the Borrower's EBITDA tested on a rolling basis for the prior six (6) month period.

"Affiliate" means, as to any Person, each other Person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or under common control with, such Person.

"Agreement" means this Loan and Security Agreement (together with any and all schedules and exhibits attached from time to time hereto), as the same may from time to time be amended, modified or supplemented.

"Borrowing Base" means, at any time, the amount computed on the Borrowing Base Certificate most recently delivered to, and accepted by, the Lender in accordance with this Agreement and equal to the lesser of:

(A) \$2,500,000.00; or

(B) The aggregate of (1) eighty percent (80%) of the billed Eligible Accounts of the Borrower, plus (2) eighty percent (80%) of the Eligible Unbilled Accounts, minus (3) any reductions attributable to the aggregate face amount of outstanding Letters of Credit as required by Section 2.04(B) herein.

"Borrowing Base Certificate" means a fully completed certificate in the form of Exhibit 1.01(A) to this Agreement, and to include the worksheets, supporting documentation and schedules as required by the Lender, certified by the chief financial officer of the Borrower to be correct and delivered to, and accepted by, the Lender pursuant to Section 2.02 or Section 6.01(B)(5).

"Business Day" means a day other than a Saturday, a Sunday, and a day on which commercial banks in Worcester, Massachusetts are authorized to close.

"Change of Control" means (A) a change in ownership, through purchase or otherwise (including the agreement to act in concert without anything more), by any Person or group of Persons acting in concert, directly or indirectly, in one or more transactions, of all or substantially all of the assets of the Borrower, except to a Subsidiary of the Borrower or (B) the failure of the Borrower to maintain beneficial ownership, directly or indirectly, of at least 100% of the Equity Interest in each Guarantor. For purposes of this definition, the terms "Person" and "group" shall include the meanings for such terms as used for purposes of Sections 13(d) and 14(d) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), whether or not applicable, and "beneficial ownership" shall include the meaning of "beneficial owner" as that term is used in Rules 13d 3 and 13d 5 under the Exchange Act, whether or not applicable, and a Person shall be deemed to have "beneficial ownership" of all Equity Interests that such Person has the right to acquire (whether such right is exercisable immediately or with the passage of time or the occurrence of a contingency).

"Closing" has the meaning given to such term in Section 3.01.

"Collateral" has the meaning given to such term in Section 4.01.

"Current Assets" means, at any time, all assets that, in accordance with GAAP, should be classified as current assets on a consolidated balance sheet of the Borrower and its Subsidiaries.

"Debt Service Coverage Ratio" means, during the applicable period, that quotient equal to (a) the aggregate of (A) (1) Operating Free Cash Flow, minus (2) unfunded capital expenditures, minus (3) dividends, divided by (B) the total of all scheduled payments of principal and interest on all indebtedness on the Loans, all Subordinated Indebtedness and capital equipment leases.

"Disbursement Authorization Letter" means a duly authorized and executed disbursement authorization letter from the Borrower to the Lender in the form of Exhibit 1.01(B) attached hereto and made a part hereof.

"EBITDA" means net income (loss) plus income tax expense, interest expense, depreciation and amortization expense plus non-cash or non-recurring items as approved by the Lender.

"Eligible Account" means, at any time, an Account that the Lender in its reasonable discretion, determines is eligible for inclusion in the Borrowing Base and that conforms and continues to conform to each of the following conditions:

(A) The Account arose from a bona fide outright sale of Goods by the Borrower or from services performed by the Borrower, and such Goods have been shipped to the appropriate account debtors or their designees (or the sale has otherwise been consummated), or the services have been performed for the appropriate account debtors;

(B) The Account is based upon an enforceable order or contract, written or oral, for Goods shipped or held or for services performed, and the same were shipped, held, or performed in accordance with such order or contract;

(C) The title of the Borrower to the Account and, except as to the account debtor, to any Goods is absolute and is not subject to any prior assignment, claim, lien, or security interest, except Permitted Liens;

(D) The amount shown on the books of the Borrower and on any invoice or statement delivered to the Lender is owing to the Borrower, less any partial payment that has been made thereon by anyone;

(E) The Account is not subject to any claim of reduction, counterclaim, set-off, recoupment, or any claim for credits, allowances, or adjustments by the account debtor because of returned, inferior, or damaged Goods or unsatisfactory services, or for any other reason, except for customary discounts not to exceed two percent (2%) allowed for prompt payment;

(F) The account debtor has not returned or refused to retain, or otherwise notified the Borrower of any dispute concerning, or claimed nonconformity of, any of the Goods or services from the sale of which the Account arose;

(G) INTENTIONALLY OMITTED;

(H) The Account is not more than sixty (60) days past due nor outstanding more than ninety (90) days from the date of the invoice therefor;

(I) The Account does not arise out of a contract with, or order from, an account debtor that, by its terms, forbids or makes void or unenforceable the assignment by the Borrower to the Lender of the Account arising with respect thereto;

(J) The Borrower has not received any note, trade acceptance, draft, or other Instrument with respect to, or in payment of, the Account, nor any Chattel Paper with respect to the Goods giving rise to the Account, unless, if any such Instrument or Chattel Paper has been received, the Borrower promptly notifies the Lender and, at the latter's request, endorses or assigns and delivers the same to the Lender and the Lender accepts same;

(K) The Borrower has not received any notice of the death of the account debtor or a partner thereof; nor of the dissolution, termination of existence, insolvency, business failure, appointment of a receiver for any part of the property of, assignment for the benefit of creditors



by, or the filing of a petition in bankruptcy or the commencement of any proceeding under any bankruptcy or insolvency laws by or against, the account debtor. Upon the receipt by the Borrower of any such notice, it will promptly give the Lender written advice thereof;

(L) The account debtor is not an officer, agent, employee, shareholder, director, Subsidiary or other Affiliate of, or a sales representative for, the Borrower; and

(M) The Lender has not deemed such Account ineligible because of uncertainty about the creditworthiness of the account debtor or because the Lender determines, in its reasonable discretion, otherwise reasonably considers the collateral value thereof to the Lender to be impaired or its ability to realize such value to be insecure.

In addition to the foregoing, Eligible Account shall mean any amount receivable by the Borrower under any insurance policy covering Goods which have, within the preceding forty-five (45) days, been damaged or destroyed by fire or other direct casualty loss, provided that a claim therefor has been made in compliance with such insurance policy, to the extent that such claim has not been in any way denied or contested by the insurer and provided that such insurer, if such insurer were an account debtor of the Borrower, would be a qualified account debtor under this Section.

The enumeration of the aforementioned conditions shall not in any way alter the right of the Lender, in its reasonable discretion, to exclude any Account from being an Eligible Account for any purposes hereunder.

In the event of any dispute under the foregoing criteria as to whether an Account is or has ceased to be an Eligible Account, the decision of the Lender shall control.

"Eligible Unbilled Account" means, at any time, an Account that satisfies all of the conditions necessary to be an Eligible Account hereunder, with the single exception that the Borrower has recognized the revenue with respect to such Account on its books in accordance with GAAP but has not billed the Account to the account debtor, and, for purposes of condition (H) of the definition of Eligible Account, the phrase "date revenue is recognized" shall be substituted for "date of invoice".

"Equity Interest" means, with respect to the Borrower and the Guarantor, shares authorized, issued and outstanding as of the date of this Agreement and so long as any Obligations remain outstanding.

"Event of Default" has the meaning provided in Section 7.01.

"Financial Statements" means those financial statements presented to the Lender by the Borrower and the Guarantor in connection with the underwriting of the Loans as more particularly described in Exhibit 1.01(C) attached hereto.

"Financing Statements" means those certain Uniform Commercial Code Financing Statements duly authorized and authenticated by the Borrower and the Guarantor, and duly recorded or filed for the benefit of the Lender, as from time to time supplemented or amended.

"Fixed Assets" means, at any time, all assets (other than Current Assets) that should, in accordance with GAAP, be classified as assets on a consolidated balance sheet of the Borrower and its Subsidiaries.

"GAAP" means generally accepted accounting principles applied consistently, with such changes or modifications thereto as may be approved in writing by the Lender.

"Guarantor" means World Energy Securities Corp., a Massachusetts corporation with its principal place of business at 100 Front Street, Worcester, Massachusetts 01608, and the sole Subsidiary of the Borrower.

"Guarantor Security Agreement" means with respect to the Guarantor, a duly authorized and executed Security Agreement dated of even date herewith in the form of Exhibit 1.01(D) to this Agreement.

"Guaranty" means with respect to the Guarantor, a duly authorized and executed Unlimited Guaranty dated of even date herewith in the form of Exhibit 1.01(E) to this Agreement.

"Indebtedness" means, as to the Borrower or the Subsidiary, all items of indebtedness, obligation or liability whether joint or several, matured or unmatured, liquidated or unliquidated, direct or contingent, including without limitation:

(A) All indebtedness guaranteed, directly or indirectly, in any manner, or endorsed (other than for collection or deposit in the ordinary course of business) or discounted with recourse;

(B) All indebtedness in effect guaranteed, directly or indirectly, through agreements, contingent or otherwise: (1) to purchase such indebtedness; or (2) to purchase, sell, or lease (as lessee or lessor) property, products, materials, or supplies or to purchase or sell services, primarily for the purpose of enabling the debtor to make payment of such indebtedness or to insure the owner of the indebtedness against loss; or (3) to supply funds to, or in any other manner invest in, the debtor;

(C) All indebtedness secured by (or for which the holder of such indebtedness has a right, contingent or otherwise, to be secured by) any mortgage, deed of trust, pledge, lien, security interest, or other charge or encumbrance upon property owned or acquired subject thereto, whether or not the liabilities secured thereby have been assumed; and

(D) All indebtedness incurred as the lessee of goods or services under leases that, in accordance with GAAP, should be reflected on the lessee's balance sheet.

"Intellectual Property" means trademarks, service marks, trade names, trade styles, logos, goodwill, trade secrets, patents, applications, and licenses acquired under any statutory, common law or registration process in any state or nation at any time, or under any agreement executed with any person or entity at any time. The term "license" refers not only to rights granted by agreement from the owner of patents, trademarks, service marks and the like, but also to rights granted by a franchisor under a franchise or similar agreement. The foregoing enumeration is not intended as a limitation of the meaning of the word "license".

"IP Security Agreement" means a duly authorized and executed Intellectual Property Security Agreement by and between the Borrower and the Lender in the form of Exhibit 1.0(F) attached hereto and made a part hereof, and the Financing Statements to be authenticated by each Borrower and duly filed for the benefit of the Lender, as from time to time supplemented or amended.

"Landlord's Waiver" means the Landlord's Consent and Waiver duly authorized and executed by each of the Borrower, the Lender and the landlord with respect to the premises at 100 Front Street, Worcester, Massachusetts, in the form of Exhibit 1.01(G) attached hereto and made a part hereof, as from time to time supplemented or amended.

"Laws" means all ordinances, statutes, rules, regulations, orders, injunctions, writs, or decrees of any government or political subdivision or agency thereof, or of any court or similar entity established by any thereof.

"Letters of Credit" means any and all commercial or standby letters of credit or bank guarantees which may be issued by the Lender from time to time to third parties for the benefit of the Borrower pursuant to Section 2.04 of this Agreement.

"Loan Documents" includes this Agreement, the Notes, the IP Security Agreement, the Guaranty, the Guarantor Security Agreement, the Landlord's Waiver, the Disbursement Authorization, the Subordination Agreement(s) and the documents, whether deliverable at or after the Closing, required pursuant to Articles 3.0 and 4.0, as from time to time modified, extended, supplemented or amended.

"Maturity Date" means, with respect to the Term Note, December 30, 2018 or such later date as is agreed to by the Lender in a written instrument executed by a duly authorized officer of the Lender.

"Notes" means each and both of the Revolving Credit Note and the Term Note.

"Obligations" is intended to be used in its most comprehensive sense and means the obligation of the Borrower or, as the context requires, the Guarantor to the Lender of whatever kind and description, whether direct or indirect, absolute or contingent, primary or secondary, joint or several, due or to become due, or held or to be held by, the Lender for its own account or as agent for another or others, whether created directly or acquired by assignment or otherwise and howsoever evidenced, whether now existing or hereafter incurred or acquired and whether by way of loan, guaranty, discount, letter of credit, lease or otherwise, including without limitation, the following obligations:

(A) To pay the principal of, and interest on, the Notes in accordance with the terms thereof and to satisfy all other liabilities to the Lender, whether hereunder or otherwise, whether now existing or hereafter incurred, matured or unmatured, direct or contingent, joint or several, including any extensions, modifications, renewals thereof and substitutions therefor.

(B) To repay to the Lender all amounts advanced by the Lender hereunder or otherwise on behalf of the Borrower or the Guarantor, including, but without limitation, advances for principal or interest payments to prior secured parties, mortgagees, or lienors, or for taxes, levies, insurance, rent, or repairs to, or maintenance or storage of, any of the Collateral;

(C) All obligations to reimburse the Lender in accordance with the terms of any and all agreements between the Lender and the Borrower with respect to any Letters of Credit and foreign exchange contracts for the amounts required to be paid on account of any and all such Letters of Credit and foreign exchange contracts issued by or executed by the Lender for the benefit of the Borrower.

(D) To perform and observe all covenants, agreements and undertakings of the Borrower or the Guarantor pursuant to the terms and conditions of this Agreement, the Notes, the other Loan Documents or any other agreement or instrument now or hereafter delivered to the Lender by the Borrower or the Guarantor;

(E) All obligations under any interest rate swap agreement, any cap, floor or hedging agreement or other similar agreement, or other financial agreement or arrangement designed to protect the Borrower against fluctuations in any interest rate charged by the Lender under the Notes or otherwise, including any obligations of the Borrower arising out of or in connection with any Automated Clearing House ("ACH") Agreement relating to the processing of ACH transactions, together with all fees, expenses, charges and other amounts owing by or chargeable to the Borrower under any ACH Agreement;

(F) All obligations to reimburse the Lender, on demand, in connection with overdrafts and other amounts due to the Lender under any existing or future agreements relating to cash management services; and

(G) All obligations to reimburse the Lender, on demand, for all of the Lender's expenses and costs, including without limitation the reasonable fees and expenses of its counsel, in connection with the preparation, administration, amendment, modification, or enforcement of this Agreement and the documents required hereunder or related hereto, including, without limitation, any proceeding brought, or threatened, to enforce payment of any of the obligations referred to in the foregoing Paragraphs (A) through (F).

"Operating Free Cash Flow" shall mean net income (loss) plus interest plus depreciation and amortization plus share based compensation plus deferred income taxes plus any other non-cash items plus change in operating assets and operating liabilities plus deferred revenue plus net capital expenditures.

"Origination Fee" means a fee of \$20,000.00 to be paid to the Lender by the Borrower at Closing.

"Perfection Certificate(s)" means a duly authorized and executed Perfection Certificate from each of the Borrower and the Guarantor in the form of Exhibit 1.01(H) to this Agreement.

"Permitted Investments" means: (a) direct obligations of, or obligations the principal of and interest on which are unconditionally guaranteed by, the United States of America (or by any agency thereof to the extent such obligations are backed by the full faith and credit of the United States of America), in each case maturing within one year from the date of acquisition thereof;

(b) without limiting the provisions of paragraph (d) below, investments in commercial paper maturing within one year from the date of acquisition thereof and having, at such date of acquisition, a rating of at least "A-2" or the equivalent thereof from Standard & Poor's Corporation or of at least "P-2" or the equivalent thereof from Moody's Investors Service, Inc.; (c) investments in certificates of deposit, bankers' acceptances and time deposits (including Eurodollar time deposits) maturing within one year from the date of acquisition thereof issued or guaranteed by or placed with (i) the Lender (ii) any domestic office of any other commercial bank of recognized standing organized under the laws of the United States of America or any State thereof that has a combined capital and surplus and undivided profits of not less than \$1,000,000,000 and is the principal banking Subsidiary of a bank holding company having a long-term unsecured debt rating of at least "A-2" or the equivalent thereof from Standard & Poor's Corporation or at least "P-2" or the equivalent thereof from Moody's Investors Service, Inc.; (d) investments in commercial paper maturing within one year from the date of acquisition thereof and issued by (i) the holding company of the Lender or (ii) the holding company of any other commercial bank of recognized standing organized under the laws of the United States of America or any State thereof that has (A) a combined capital and surplus in excess of \$1,000,000,000 and (B) commercial paper rated at least "A-2" or the equivalent thereof from Standard & Poor's Corporation or of at least "P-2" or the equivalent thereof from Moody's Investors Service, Inc.; (e) investments in repurchase obligations with a term of not more than seven days for underlying securities of the types described in clause (a) above entered into with any office of a bank or trust company meeting the qualifications specified in clause (c) above; (f) investments in money markets funds substantially all the assets of which are comprised of securities of the types described in clauses (a) through (e) above.

"Permitted Liens" means:

(A) Liens for taxes, assessments, or similar charges, incurred in the ordinary course of business, that are not yet due and payable;

(B) Pledges or deposits made in the ordinary course of business to secure payment of worker's compensation, or to participate in any fund in connection with worker's compensation, unemployment insurance, old-age pensions, or other social security programs;

(C) Liens of mechanics, materialmen, warehousemen, carriers, or other like liens, securing obligations incurred in the ordinary course of business that are not yet due and payable;

(D) Good faith pledges or deposits made in the ordinary course of business to secure performance of bids, tenders, contracts (other than for the repayment of borrowed money) or leases, not in excess of ten percent (10%) of the aggregate amount due thereunder, or to secure statutory obligations, or surety, appeal, indemnity, performance, or other similar bonds required in the ordinary course of business;

(E) Encumbrances consisting of zoning restrictions, easements, or other restrictions on the use of real property, none of which materially impairs the use of such property by the Borrower in the operation of its business, and none of which is violated in any material respect by existing or proposed structures or land use;

(F) Liens in favor of the Lender;

(G) Existing liens set forth or described on Exhibit 1.01(I) attached hereto and made a part hereof;

(H) Purchase money security interests granted to secure not more than seventy-five percent (75%) of the purchase price of assets, the purchase of which does not violate this Agreement or any instrument required hereunder; and

(I) The following, if the validity or amount thereof is being contested in good faith by appropriate and lawful proceedings, so long as levy and execution thereon have been stayed and continue to be stayed and they do not, in the aggregate, materially detract from the value of the property of the Borrower or any Subsidiary, or materially impair the use thereof in the operation of its business:

(1) Claims or liens for taxes, assessments, or charges due and payable and subject to interest or penalty;

(2) Claims, liens and encumbrances upon, and defects of title to, real or personal property, including any attachment of personal or real property or other legal process prior to adjudication of a dispute on the merits;

(3) Claims or liens of mechanics, materialmen, warehousemen, carriers, or other like liens; and

(4) Adverse judgments on appeal.

"Person" means any individual, corporation, limited liability company, partnership, association, joint-stock company, trust, unincorporated organization, joint venture, court, or government or political subdivision or agency thereof.

"Prime Rate" means that rate of interest published from time to time in The Wall Street Journal (Eastern Edition) as the "Prime Rate" of interest.

"Projected EBITDA" shall mean the Borrower's projected EBITDA, as approved by the Borrower's Board of Directors and provided to the Lender no later than March 15 of the applicable fiscal year, and reviewed and approved by the Lender, tested on a rolling basis for the prior six (6) month period.

"Records" means correspondence, memoranda, tapes, discs, papers, books and other documents, or transcribed information of any type, whether expressed in ordinary or machine readable language.

"Revolving Credit Note" means the promissory note referred to in Section 2.03(A).

"Revolving Credit Termination Date" means, with respect to the Revolving Credit Note, December 30, 2016, or such later date as is agreed to by the Lender in a written instrument executed by a duly authorized officer of the Lender.

"Subordinated Creditors" means the parties set forth on Exhibit 1.01(J) as the currently existing Subordinated Creditors.

"Subordinated Indebtedness" means all Indebtedness incurred at any time by the Borrower or any Subsidiary, the repayment of which is subordinated to the Loans in form and manner satisfactory to the Lender. All currently existing Subordinated Indebtedness is so specified in Exhibit 1.01(K).

"Subordination Agreement" means a duly authorized and executed Subordination Agreement with respect to any Subordinated Indebtedness, in the form attached hereto as Exhibit 1.01(L) and containing such provisions as are acceptable to the Lender.

"Subsidiary" means any Affiliate that is directly, or indirectly through one or more intermediaries, controlled by the Borrower or not less than 50% of the voting interest of which is owned, directly or through one or more intermediaries, by the Borrower and includes the Guarantor.

"Term Note" means the promissory note referred to in Section 2.03(B).

#### 1.02 Accounting.

(A) Generally. All accounting terms not specifically or completely defined herein shall be construed in conformity with, and all financial data (including financial ratios and other financial calculations) required to be submitted pursuant to this Agreement shall be prepared in conformity with, GAAP applied on a consistent basis, as in effect from time to time, except as otherwise specifically prescribed herein. To the extent any defined term states that it is determined "on a consolidated basis", such consolidation shall be in accordance with GAAP applied on a consistent basis. Notwithstanding the foregoing, for purposes of determining compliance with any covenant (including the computation of any financial covenant) contained herein, Indebtedness of the Borrower and its Subsidiaries shall be deemed to be carried at 100% of the outstanding principal amount thereof, and the effects of FASB ASC 820 on financial liabilities shall be disregarded.

(B) Changes in GAAP. If at any time any change in GAAP would affect the computation of any financial ratio or requirement set forth in this Agreement or any other Loan Document, and either the Borrower or the Lender shall so request, the Lender and the Borrower shall negotiate in good faith to amend such ratio or requirement to preserve the original intent thereof in light of such change in GAAP; provided that, until so amended, (i) such ratio or requirement shall continue to be computed in accordance with GAAP prior to such change therein and (ii) the Borrower shall provide to the Lender financial statements and other documents required under this Agreement or as reasonably requested hereunder setting forth a reconciliation between calculations of such ratio or requirement made before and after giving effect to such change in GAAP.

## ARTICLE 2.0 THE LOANS

### 2.01 Disbursement of the Loans.

The Lender will credit the proceeds of the Revolving Credit from time to time, at the request of the Borrower and in accordance with the provisions of Section 2.02 of this Agreement to the Borrower's deposit account with the Lender.

The Lender will disburse the Term Loan in accordance with the Disbursement Authorization Letter.

### 2.02 General Terms -- the Revolving Credit.

Subject to the terms hereof, the Lender will lend the Borrower, or issue letters of credit for the account of the Borrower in, from time to time until the Revolving Credit Termination Date, such sums as the Borrower may request by reasonable same day notice to the Lender, received by the Lender not later than 11:00 A.M. of such day, but which shall not exceed, in the aggregate principal amount at any one time outstanding, the then existing Borrowing Base (the "Revolving Credit Commitment"). The Borrower shall provide the Lender with a duly executed Borrowing Base Certificate as of a date not less than two (2) Business Days prior to its first request for an advance on the Revolving Credit Note. The Borrower may borrow, repay without penalty or premium and reborrow hereunder, from the date of this Agreement until the Revolving Credit Termination Date, the lesser of the then existing Borrowing Base or the Revolving Credit Commitment in integral multiples of \$50,000.00. It is the intention of the parties that the aggregate of amounts outstanding pursuant to the Revolving Credit and aggregate face amount of all Letters of Credit from time to time outstanding shall at no time exceed the amount of the then existing Borrowing Base, and if, at any time, an excess shall for any reason exist, the full amount of such excess, together with accrued and unpaid interest thereon as herein provided, shall be immediately due and payable in full.

### 2.03 The Notes.

(A) The Revolving Credit Commitment shall be evidenced by the Revolving Credit Note fully due and payable on the Revolving Credit Termination Date, in the form attached hereto as Exhibit 2.03(A).

(B) The Term Loan shall be evidenced by the Term Note fully due and payable on the Maturity Date, in the form attached hereto as Exhibit 2.03(B).

### 2.04 Letters of Credit.

(A) From time to time prior to the Revolving Credit Termination Date, the Lender shall issue Letters of Credit under the Revolving Credit, on account of the Borrower, subject to the following conditions:

- (1) No beneficiary shall be an Affiliate;
- (2) With respect to each Letter of Credit, the Borrower shall pay to the Lender a Letter of Credit fee per annum payable quarterly in advance, upon the maximum amount available under each outstanding Letter of Credit, at the initial rate of 1.75% per annum and, beginning as of June 30, 2014, at a rate to be determined semi-annually in accordance with the ratio of Actual EBITDA to Projected EBITDA in effect as set forth on the following grid:

| <u>Ratio of Actual EBITDA to Projected EBITDA</u> | <u>Letter of Credit Fee</u> |
|---|-----------------------------|
| >1.50:1.00  | 1.25%                       |
| >1.25:1.00 but < 1.50:1.00                        | 1.50%                       |
| <1.25:1.00  | 1.75%                       |



- (3) In addition to the Letter of Credit Fee, the Borrower shall pay to the Lender a Letter of Credit Issuance Fee equal to 0.25% per annum, payable quarterly, on the aggregate face amount of such Letters of Credit, together with such other customary administrative fees and charges;
- (4) No such Letter of Credit shall have an expiration date which is later than the Revolving Credit Termination Date, unless otherwise agreed to by the Bank in its reasonable discretion, and in such case, the expiration date shall not exceed twelve (12) months beyond the Revolving Credit Termination Date;
- (5) Each such Letter of Credit shall be issued pursuant to such agreements and upon such terms and conditions as shall be required by the Bank;
- (6) No Event of Default shall have occurred and be continuing hereunder at the time of issuance of such Letter of Credit; and
- (7) The aggregate face amount of all Letters of Credit at any time outstanding shall not exceed \$250,000.00.

(B) The Borrowing Base available from time to time shall be reduced by the aggregate face amount of all Letters of Credit at any time outstanding.

#### 2.05 Interest Rate and Payments of Interest.

(A) Interest shall be paid as follows:

(1) Except as otherwise provided under Section 2.05(B), interest on the principal balance of each of the Loans from time to time outstanding will be payable at the rates of interest and in the manner set forth in each of the Notes.

(2) Interest shall be calculated on the basis of a 360-day year, counting the actual number of days elapsed, and shall be payable monthly in arrears on the first day of each month and at maturity, whether by acceleration or otherwise.

(B) All agreements between or among the Borrower, the Guarantor and the Lender are hereby expressly limited so that in no contingency or event whatsoever, whether by reason of acceleration of maturity of the indebtedness evidenced by the Notes, this Agreement, or otherwise, shall the amount paid or agreed to be paid to the Lender for the use or the forbearance of the indebtedness evidenced by the Notes, this Agreement, or otherwise, exceed the maximum permissible under applicable law. As used herein, the term "applicable law" shall mean the law in effect as of the date hereof provided, however that in the event there is a change in the law which results in a higher permissible rate of interest, then the Notes shall be governed by such new law as of its effective date. In this regard, it is expressly agreed that it is the intent of the Borrower and the Lender in the execution, delivery and acceptance of the Notes and this Agreement to contract in strict compliance with the laws of The Commonwealth of Massachusetts from time to time in effect. If, under or from any circumstances whatsoever, fulfillment of any provision hereof or of the Notes or any of the other Loan Documents or other financing instruments executed in connection herewith at the time of performance of such provision shall be due, shall involve transcending the limit of such validity prescribed by applicable law, then the obligation to be fulfilled shall automatically be reduced to the limits of such validity, and if under or from circumstances whatsoever the Lender should ever receive as interest an amount which would exceed the highest lawful rate, such amount which would be excessive interest shall be applied to the reduction of the principal balances evidenced by the Notes and not to the payment of interest. This provision shall control every other provision of all agreements between or among the Borrower, the Guarantor and the Lender.

## 2.06 Payment to the Lender.

The Lender shall send the Borrower statements of all amounts due hereunder, which statements shall be considered correct and conclusively binding on the Borrower absent manifest error unless the Borrower notifies the Lender to the contrary within thirty (30) days of its receipt of any statement that it deems to be incorrect. Alternatively, at its reasonable discretion, the Lender may charge against any deposit account of the Borrower all or any part of any amount due hereunder.

## ARTICLE 3.0 CONDITIONS PRECEDENT

The obligation of the Lender to make the Loans and issue any Letter of Credit is subject to the following conditions precedent:

### 3.01 Documents Required for the Closing.

The Borrower shall have delivered to the Lender, prior to the initial disbursement of the Loans (the "Closing"), the following:

- (A) This Agreement duly executed by the Borrower;
- (B) Each of the Notes duly executed by the Borrower;
- (C) The IP Security Agreement duly executed by the Borrower;
- (D) The Guaranty duly executed by the Guarantor;

- 
- (E) The Guarantor Security Agreement duly executed by the Guarantor;
- (F) The Disbursement Authorization Letter duly executed by the Borrower;
- (G) The Landlord's Waiver duly executed by each of the Borrower, the Lender and the Borrower's landlord;
- (H) Subordination Agreements duly executed by each of the Borrower, the Lender and the Subordinated Creditors;
- (I) Perfection Certificates duly executed by each of the Borrower and the Guarantor;
- (J) The Financing Statements and other instruments required by Article 4.0;
- (K) Satisfactory review of the field examination by the Lender;
- (L) A copy, certified as of the date of the Closing, of resolutions of the board of directors of the Borrower, authorizing the execution, delivery, and performance of this Agreement, the Notes, the other Loan Documents, and each other document to be delivered pursuant hereto;
- (M) A copy, certified as of the date of the Closing, of the bylaws of the Borrower;
- (N) A certificate (dated the date of the Closing) of the corporate secretary or assistant secretary of the Borrower as to the incumbency and signatures of the officers of the Borrower signing this Agreement, the Notes, the other Loan Documents, and each other document to be delivered pursuant hereto;
- (O) A copy, certified as of the most recent date practicable by the Secretary of the State of Delaware, of the Certificate of Incorporation of the Borrower, and all amendments thereto, together with a certificate (dated the date of the Closing) of the corporate secretary or assistant secretary of the Borrower to the effect that such Certificate of Incorporation have not been further amended since the date of the aforesaid certification of the Secretary of the State of Delaware;
- (P) A copy, certified as of the most recent date practicable by the Secretary of The Commonwealth of Massachusetts, of the Foreign Corporation Certificate of the Borrower, and all amendments thereto, together with a certificate (dated the date of the Closing) of the corporate secretary or assistant secretary of the Borrower to the effect that such Foreign Corporation Certificate have not been further amended since the date of the aforesaid certification of the Secretary of The Commonwealth of Massachusetts;
- (Q) Certificate of tax and corporate good standing dated as of the most recent date practicable, issued by the Secretary of State of the State of Delaware as to the tax good standing and the legal existence and good legal standing of the Borrower;

(R) Certificates, as of the most recent dates practicable, of the Secretary of The Commonwealth of Massachusetts and of the secretary of state of each other state in which the Borrower is qualified as a foreign corporation;

(S) A written opinion of the law firm of Mirick, O'Connell, DeMallie & Lougee, LLP, legal counsel for the Borrower and the Guarantor, dated the date of the Closing and addressed to the Lender, in form satisfactory to the Lender and its counsel;

(T) A certificate, dated the date of the Closing, signed by the chief executive officer or chief financial officer of the Borrower and to the effect that:

(1) The representations and warranties set forth in Section 5.01 are true as of the date of the Closing; and

(2) No Event of Default hereunder, and no event which, with the giving of notice or passage of time or both, would become such an Event of Default, has occurred as of such date;

(U) Copies of all documents evidencing the terms and conditions of any debt specified as Subordinated Indebtedness on Exhibit 1.01(K);

(V) Payment of the Origination Fee by the Borrower; and

(W) Any and all documents required to be executed in connection with any Letters of Credit being issued as of the Closing.

### 3.02 Documents Required for Subsequent Disbursements or issuance of Letters of Credit.

At the time of, and as a condition to, any disbursement of any part of the Loans or issuance of any Letter of Credit to be made by the Lender subsequent to the Closing, the Lender may require the Borrower to deliver to the Lender a certificate, dated the date on which any such disbursement is to be made, signed by the chief executive officer or chief financial officer of the Borrower, and to the effect that:

(A) As of the date thereof, no Event of Default has occurred and is continuing, and no event has occurred and is continuing that, but for the giving of notice or passage of time or both, would be an Event of Default;

(B) No material adverse change has occurred in the financial condition, or results of operations of the Borrower or any Subsidiary since the date of the Financial Statements; and

(C) Each of the representations and warranties contained in Section 5.01 is true and correct in all material respects as if made on and as of the date of such disbursement (except for such representations and warranties made as of a particular date).

### 3.03 Certain Events.

At the time of, and as a condition to, the Closing and each disbursement of any part of the Loans or issuance of a Letter of Credit to be made by the Lender at or subsequent to the Closing:

(A) No Event of Default shall have occurred and be continuing, and no event shall have occurred and be continuing that, with the giving of notice or passage of time or both, would be an Event of Default;

(B) No material adverse change shall have occurred in the financial condition, or results of operations of the Borrower or any Subsidiary since the dates of the Financial Statements; and

(C) All of the Loan Documents shall have remained in full force and effect.

### 3.04 Legal Matters.

At the time of the Closing and at the discretion of the Lender, at the time of each subsequent disbursement, all legal matters incidental thereto shall be satisfactory to Bowditch & Dewey, LLP, legal counsel to the Lender.

## ARTICLE 4.0 COLLATERAL SECURITY

### 4.01 Composition of the Collateral.

The property in which a security interest is granted pursuant to the provisions of Sections 4.02 and 4.03 and pursuant to the Loan Documents is herein collectively called the "Collateral". The Collateral, together with all other property of the Borrower of any kind held by the Lender, shall stand as one general, continuing collateral security for all Obligations and may be retained by the Lender until all Obligations have been satisfied in full.

### 4.02 Rights in Property Held by the Lender.

As security for the prompt satisfaction of all Obligations, the Borrower hereby assigns, transfers, and sets over to the Lender all of its right, title, and interest in and to, and grants the Lender a lien on and a security interest in, all amounts that may be owing, from time to time, by the Lender to the Borrower in any capacity, including, but without limitation, any balance or share belonging to the Borrower, or any deposit or other account with the Lender, which lien and security interest shall be independent of, and in addition to, any right of set-off that the Lender has under Section 8.06 or otherwise.

### 4.03 Rights in Property Held Either by the Borrower or by the Lender.

As further security for the prompt satisfaction of all of the Obligations, the Borrower hereby assigns to the Lender all of its right, title and interest in and to, and grants the Lender a lien upon and a continuing security interest in all assets of every type and description, wherever located, whether now owned or hereafter acquired, together with all substitutions and replacements therefor, accessions thereto, and proceeds (including, but without limitation, insurance proceeds) and products thereof, including, without limitation, the following:

(A) All Inventory;

(B) All Accounts, Deposit Accounts, Contracts, accounts receivable, contract rights, and Chattel Paper, regardless whether they constitute proceeds of other Collateral;

(C) All Investment Property, securities entitlements and Financial Assets, and all General Intangibles (including Payment Intangibles), regardless whether they constitute proceeds of other Collateral, including, without limitation, all the Borrower's rights (which the Lender may exercise or not as it in its reasonable discretion may determine) to acquire or obtain Goods and/or services with respect to the manufacture, processing, storage, sale, shipment, delivery or installation of any of the Borrower's Inventory or other Collateral; all Payment Intangibles; and including any and all right, title and interest of the Borrower in, to or under any and all licenses, franchises, permits and approvals obtained or required in connection with Borrower's business operations;

(D) All rights to payment of any insurance proceeds or awards for damages in connection with any condemnations or takings of any interest in and to any real or personal property, wherever located, or any conveyance in lieu thereof;

(E) All products of and accessions to any of the Collateral;

(F) All liens, guaranties, securities, rights, remedies and privileges pertaining to any of the Collateral, including the right of stoppage in transit;

(G) All obligations owing to the Borrower of every kind and nature, and all choses in action, all Commercial Tort Claims, all Letter-of-Credit Rights and all Supporting Obligations;

(H) All tax refunds of every kind and nature to which the Borrower is now or hereafter may become entitled no matter however arising, including, without limitation, loss carry back refunds;

(I) All Intellectual Property, goodwill, trade secrets, computer programs, source codes, licenses, customer lists, trade names, copyrights, trademarks and patents, all domain names, internet web sites and other rights;

(J) All Chattel Paper (including Electronic Chattel Paper and Tangible Chattel Paper), Documents and Instruments, including Promissory Notes (whether negotiable or non-negotiable, and regardless of their being attached to Chattel Paper) and all money, cash and coins;

(K) All Equipment, including without limitation machinery, furniture, motor vehicles, Fixtures and all other goods used in the conduct of the business of the Borrower;

(L) All insurance policies and all proceeds of Collateral of every kind and nature and in whatever form, including without limitation both cash and non-cash proceeds resulting or arising from the rendering of services by the Borrower or the sale or other disposition by the Borrower of the Inventory or other Collateral and including all insurance proceeds;

(M) All books and records, magnetic tapes, electronic data, computer records and discs relating to the conduct of the Borrower's business including, without in any way limiting the generality of the foregoing, those relating to its Accounts;

(N) All Deposit Accounts maintained by the Borrower with any bank, trust company, credit union, investment firm or fund, or any similar institution or organization; and

(O) All property of the Borrower in the possession of the Lender.

#### 4.04 Priority of Liens.

The foregoing liens shall be first and prior liens except for Permitted Liens.

#### 4.05 Financing Statements and Certificates of Title.

(A) The Borrower will:

(1) Execute or authenticate and deliver to the Lender any writings and do all things necessary, effectual or requested by the Lender to carry into effect the provisions and intent of this Agreement, or to vest more fully in or assure to the Lender (including without limitation, all steps to create and perfect) the security interest in the Collateral granted to the Lender by this Agreement or to comply with applicable statute or law and to facilitate the collection of the Collateral, including the furnishing at the Borrower's cost and expense, at such intervals as the Lender may establish from time to time, of reports, financial data and analyses satisfactory to the Lender. A carbon, photographic or other reproduction of this Agreement or any financing statement prepared pursuant to the terms hereof shall be sufficient as a financing statement for the purpose of filing with the appropriate authorities, and the Borrower hereby appoints the Lender as its attorney-in-fact (without requiring the Lender to act as such) to perform all other acts that the Lender deems appropriate to protect and preserve, the Collateral;

(2) Pay, or reimburse the Lender for paying, all costs and taxes of filing or recording the same in all offices and registries in which it is necessary to file or record such financing statements so as to perfect the Lender's security interest in and lien on all Collateral; and

(3) Take such other steps as the Lender, from time to time, may direct, including the noting of the Lender's lien on the Collateral and on any Certificates of Title therefor, all too perfect to the satisfaction of the Lender the Lender's interest in the Collateral.

(B) In addition to the foregoing, and not in limitation thereof, to the extent lawful, the Borrower hereby appoints the Lender as its attorney-in-fact (without requiring the Lender to act as such) (i) to execute, authenticate, amend, file, correct, record and/or register any financing statement in the name of the Borrower, and to perform all other acts that the Lender, in its reasonable discretion, deems appropriate to perfect and continue its security interest in and lien on, and to protect or preserve, the Collateral; (ii) to enter into a control agreement or other agreement for the purpose of perfecting or maintaining the perfection of the security interests in and liens upon the Collateral; and (iii) to take any other action deemed necessary or prudent by

the Lender, in the reasonable exercise of its discretion, to effect, perfect, continue or maintain the security interests in and liens upon any Collateral as contemplated by this Agreement or the other Loan Documents.

#### 4.06 Mortgagees', Landlords', and Warehousemen's Waivers.

The Borrower will, within twenty (20) days after any request of the Lender, cause any mortgagee of real estate owned by the Borrower, any landlord of premises leased by the Borrower, and any warehouseman or other bailee on whose premises any of the Collateral may be located to execute and deliver to the Lender instruments, in form and substance satisfactory to the Lender, by which such mortgagee, landlord or warehouseman or other bailee waives its rights, if any, in and to all Goods composing a part of the Collateral.

### ARTICLE 5.0 REPRESENTATIONS AND WARRANTIES

#### 5.01 Original.

To induce the Lender to enter into this Agreement, the Borrower represents and warrants to the Lender as follows:

(A) The Borrower is a corporation duly organized, validly existing, and in good standing under the Laws of the State of Delaware; the Borrower has no Subsidiaries other than the Subsidiaries named in Exhibit 5.01(A); each Subsidiary is a corporation duly organized, validly existing, and in good standing under the Laws of its state of incorporation, all as set forth in Exhibit 5.01(A); the Borrower and Subsidiaries have the lawful power to own their properties and to engage in the businesses they conduct, and each is duly qualified and in good standing as a foreign corporation in the jurisdictions wherein the nature of the business transacted by it or property owned by it makes such qualification necessary; the states in which the Borrower and each Subsidiary are qualified to do business are set forth in Exhibit 5.01(A) or otherwise disclosed to the Lender in writing; the percentage of the Borrower's ownership of the outstanding stock of each Subsidiary is as listed in Exhibit 5.01(A); the addresses of all places of business of the Borrower and its Subsidiaries are as set forth in Exhibit 5.01(A) or otherwise disclosed to the Lender in writing; neither the Borrower nor any Subsidiary has changed its name, been the surviving corporation in a merger, acquired any business, or changed its principal executive office within five (5) years and one (1) month prior to the date hereof except as set forth in Exhibit 5.01(A); and all of the authorized, issued, and outstanding shares of capital stock of each Subsidiary are owned by the Borrower;

(B) Neither the Borrower nor any Subsidiary is directly or indirectly controlled by, or acting on behalf of, any Person which is an "Investment Company", within the meaning of the Investment Company Act of 1940, as amended;

(C) Neither the Borrower nor any Subsidiary is in default with respect to any of its existing Indebtedness, and the making and performance of this Agreement, the Notes, and the other Loan Documents will not (promptly or with the passage of time, the giving of notice, or both):

(1) Violate the Certificate of Incorporation or by-laws of the Borrower or any Subsidiary, or violate any Laws or result in a default under any contract, agreement, or instrument to which the Borrower or any Subsidiary is a party or by which the Borrower or any Subsidiary or its property is bound; or

(2) Result in the creation or imposition of any security interest in, or lien or encumbrance upon, any of the assets of the Borrower or any Subsidiary except in favor of the Lender;



(D) The Borrower and the Guarantor, to the extent applicable to it, has the power and authority to enter into and perform this Agreement, the Notes, and the other Loan Documents, and to incur the obligations herein and therein provided for, and has taken all actions necessary to authorize the execution, delivery, and performance of this Agreement, the Notes, and the other Loan Documents;

(E) This Agreement, the Notes, and the other Loan Documents are, or when delivered will be, valid, binding, and enforceable in accordance with their respective terms;

(F) Except as disclosed in Exhibit 5.01(F) hereto, there is no pending order, notice, claim, litigation, proceeding, or investigation against or affecting the Borrower or any Subsidiary, whether or not covered by insurance, that would in the aggregate involve the payment of \$100,000.00 or more or would otherwise materially or adversely affect the financial condition or business prospects of the Borrower or any Subsidiary if adversely determined;

(G) The Borrower and its Subsidiaries have good and marketable title to all of their assets, none of which is subject to any security interest, encumbrance or lien, or claim of any third Person except for Permitted Liens;

(H) The Financial Statements, including any schedules and notes pertaining thereto, have been prepared in accordance with GAAP, and fully and fairly present the financial condition of the Borrower and its Subsidiaries at the dates thereof and the results of operations for the periods covered thereby, and there have been no material adverse changes in the consolidated financial condition or business of the Borrower and its Subsidiaries from September 30, 2013, to the date hereof;

(I) As of the date hereof, the Borrower and its Subsidiaries have no material Indebtedness of any nature, including, but without limitation, liabilities for taxes and any interest or penalties relating thereto except to the extent reflected (in a footnote or otherwise) and reserved against in the consolidated balance sheet dated December 31, 2012 included in the Financial Statements or as disclosed in, or permitted by, this Agreement; and the Borrower does not know or have reasonable ground to know of any basis for the assertion against it or any Subsidiary of any such claim or litigation based upon such Indebtedness as of the date of the Closing except as disclosed on Exhibit 5.01(F) or otherwise disclosed to the Lender in writing;

(J) Except as otherwise permitted herein, the Borrower has filed all federal, state, and local tax returns and other reports required by any applicable Laws to have been filed prior to the date hereof, has paid or caused to be paid all taxes, assessments, and other governmental charges that are due and payable prior to the date hereof, and has made adequate provision for the

payment of such taxes, assessments, or other charges accruing but not yet payable; the Borrower has no knowledge of any deficiency or additional assessment in a materially important amount in connection with any taxes, assessments, or charges not provided for on its books;

(K) Except to the extent that the failure to comply would not materially interfere with the conduct of the business of the Borrower or any Subsidiary, the Borrower and its Subsidiaries have each complied with all applicable Laws with respect to (1) any restrictions, specifications, or other requirements pertaining to products that it manufactures or sells or to the services it performs; (2) the conduct of its business; and (3) the use, maintenance, and operation of the real and personal properties owned or leased by it in the conduct of its business;

(L) No representation or warranty by or with respect to the Borrower or any Subsidiary contained herein or in any certificate or other document furnished by the Borrower or any Subsidiary pursuant hereto contains any untrue statement of a material fact or omits to state a material fact necessary to make such representation or warranty not misleading in light of the circumstances under which it was made;

(M) Each consent, approval or authorization of, or filing, registration or qualification with, any Person required to be obtained or effected by the Borrower, any Subsidiary or the Guarantor in connection with the execution and delivery of this Agreement, the Notes, and the other Loan Documents or the undertaking or performance of any obligation hereunder or thereunder has been duly obtained or effected;

(N) All existing Indebtedness of the Borrower or any Subsidiary: (1) for money borrowed, or (2) under any security agreement, mortgage or agreement covering the lease by the Borrower or any Subsidiary as lessee of real or personal property is described in Exhibit 5.01(N);

(O) Except as entered into in the ordinary course of business, reflected in the Financial Statements or otherwise described in Exhibit 5.01 (O), attached hereto, or otherwise disclosed to the Lender in writing, (a) neither the Borrower nor any Subsidiary has any material leases, contracts, or commitments of any kind (including, without limitation, potential "earn-out" payments; employment agreements; collective bargaining agreements; powers of attorney; distribution arrangements; licenses, patents or license agreements; contracts for future purchase or delivery of goods or rendering of services; bonuses, pension, and retirement plans; or accrued vacation pay, insurance, and welfare agreements); (b) to the best of Borrower's knowledge, all parties to all such material leases, contracts, and other commitments to which the Borrower or any Subsidiary is a party have complied with the provisions of such leases, contracts, and other commitments; and (c) to the best of Borrower's knowledge, no party is in default under any thereof and no event has occurred which, but for the giving of notice or the passage of time, or both, would constitute a default;

(P) All registered patents, trademarks and copyrights of the Borrower, the Guarantor or any other Subsidiary, all pending applications of the Borrower, the Guarantor or any other Subsidiary for registration of any patents, trademarks or copyrights, and all licenses or agreements in connection with any Intellectual Property of the Borrower, the Guarantor or any other Subsidiary are described in Exhibit 5.01(P) attached hereto;

(Q) The Borrower has not made any agreement or taken any action which may cause anyone to become entitled to a commission or finder's fee as a result of or in connection with the making of the Loans;

(R) The Borrower's consolidated federal tax returns for all years of operation, including the year ended December 31, 2012, have been filed with the Internal Revenue Service and have not been challenged;

(S) Any Employee Pension Benefit Plans, as defined in the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), of the Borrower and each Subsidiary meet, as of the date hereof, the minimum funding standards of 29 U.S.C.A. 1082 (Section 302 of ERISA), and no Reportable Event or Prohibited Transaction, as defined in ERISA, has occurred with respect to any Employee Benefit Plans, as defined in ERISA, of the Borrower or any Subsidiary;

(T) The liens and security interests created pursuant to Sections 4.02 and 4.03 are in all cases first and prior liens except for Permitted Liens; and

(U) Neither the Borrower nor any Subsidiary, to the best knowledge of the Borrower, owns occupies or operates, or, to the best of their knowledge has ever owned, occupied or operated a site or vessel on which has been stored any hazardous material or oil, without compliance with all statutes, regulations, ordinances, directives, and orders of every federal, state, municipal and other governmental authority which has or claims jurisdiction relative thereto (the terms "site," "vessel" and "hazardous material," respectively, as used herein include the definitions of those terms in Massachusetts General Laws, Ch. 21E); neither the Borrower nor any Subsidiary, to the best knowledge of the Borrower, has ever disposed of, transported or arranged for the transport of any hazardous material or oil without compliance with all such statutes, regulations, ordinances, directives and orders in all material respects.

#### 5.02 Survival.

All of the representations and warranties set forth in Section 5.01 shall survive until all Obligations are satisfied in full and there remain no outstanding commitments hereunder.

### ARTICLE 6.0 COVENANTS OF THE BORROWER

#### 6.01 Affirmative Covenants.

The Borrower does hereby covenant and agree with the Lender that, so long as any of the Obligations remain unsatisfied or any commitments hereunder remain outstanding, it will comply, or if appropriate cause its Subsidiaries to comply, at all times with the following affirmative covenants:

(A) The Borrower will use the proceeds of the Loans only for the purposes set forth in Exhibit 6.01(A), and will furnish the Lender such evidence as it may reasonably require with respect to such use;

(B) The Borrower will furnish the Lender:

(1) As soon as available, but in any event within one hundred five (105) days after the close of each fiscal year: (a) a consolidated statement of stockholders' equity and a consolidated statement of operations of the Borrower and its Subsidiaries for such fiscal year; (b) consolidated cash flows of the Borrower and its Subsidiaries for such fiscal year; and (c) consolidated balance sheets of the Borrower and its Subsidiaries as of the end of such fiscal year-all such statements to be in reasonable detail, including all supporting schedules, comments, footnotes and related management letters; the consolidated statements and balance sheets to be audited by an independent certified public accountant selected by Borrower and acceptable to the Lender, and certified by such accountants to have been prepared in accordance with GAAP and to present fairly the consolidated financial position and results of operations of the Borrower and its Subsidiaries and to contain such accountants' unqualified opinion; the Lender shall have the right, from time to time to discuss the affairs of the Borrower directly with such independent certified public accountants and the Borrower shall have the opportunity, at its option, to be represented at any such discussions.

(2) Promptly after the sending or making available or filing of the same and in no event later than five (5) days after filing, copies of all reports, proxy statements, and financial statements, including without limitation Forms 10K, 10Q and 8K, that the Borrower sends or makes available to its stockholders and all registration statements and reports that the Borrower or the Guarantor files with the Securities and Exchange Commission or any successor Person;

(3) Contemporaneously with each year-end financial report or filing of financial statements with the Securities and Exchange Commission, required by the foregoing paragraphs (1) and (2), or at such other times as the Lender requests, a Compliance Certificate in the form attached hereto as Exhibit 6.01(B)(3), of the chief executive officer or chief financial officer of the Borrower stating that he has individually reviewed the provisions of this Agreement and that a review of the activities of the Borrower during the applicable period, has been made by him or under his supervision, with a view to determining whether the Borrower has fulfilled all its obligations under this Agreement, and that, to the best of his knowledge, the Borrower has observed and performed each undertaking contained in this Agreement and is not in default in the observance or performance of any of the provisions hereof or, if the Borrower shall be so in default, specifying all such defaults and events of which he may have knowledge;

(4) Whenever there are borrowings outstanding with respect to the Revolving Credit, within twenty (20) days after the end of each calendar month, in such form and detail as shall be satisfactory to the Lender, an aging, as of the end of such month, of (a) the then Eligible Accounts and Eligible Unbilled Accounts, (b) all other Accounts of the Borrower certified by the chief executive officer or chief financial officer of the Borrower to be complete and correct;

(5) Whenever there are borrowings outstanding with respect to the Revolving Credit, within twenty (20) days after the end of each calendar month (and at any additional time in the discretion of the Lender or if any material deterioration in the Borrowing Base would be disclosed thereby) a Borrowing Base Certificate as of the end of such month, and a certificate of the chief executive officer or chief financial officer of the Borrower stating that he has individually reviewed the provisions of this Agreement and that a review of the

activities of the Borrower during such period, has been made by him or under his supervision, with a view to determining whether the Borrower has fulfilled all its obligations under this Agreement, and that, to the best of his knowledge, the Borrower has observed and performed each undertaking contained in this Agreement and is not in default in the observance or performance of any of the provisions hereof or, if the Borrower shall be so in default, specifying all such defaults and events of which he may have knowledge. Each Borrowing Base Certificate shall be effective only as accepted by the Lender (and with such revisions, if any, as the Lender may require as a condition to such acceptance), such acceptance to be presumed after receipt of such Borrowing Base Certificate unless the Lender otherwise notifies the Borrower, whether thereafter, theretofore, or contemporaneously therewith;

(6) Within twenty (20) days after the end of each fiscal quarter of the Borrower, a written retail backlog report;

(7) As soon as available, but in any event on or before March 15 of each year, Board-approved projections for the next fiscal year, prepared in reasonable detail and containing such revenue projections and pro forma financial information and in such form as is satisfactory to the Lender, together with, upon request by the Lender, internally generated updates to Board-approved projections if available and at reasonable intervals; and

(8) Upon the Lender's request, from time to time, copies of any or all agreements, contracts, or commitments referred to in Section 5.01(O) hereof;

(C) The Borrower will maintain its Inventory, Equipment, real estate, and other properties in good condition and repair (normal wear and tear excepted), and will pay and discharge or cause to be paid and discharged, when due, the cost of repairs to, or maintenance of, the same, and will pay or cause to be paid in a timely manner all rental or mortgage payments due on such real estate. The Borrower hereby agrees that, in the event it fails to pay or cause to be paid any such payment, it will promptly notify the Lender thereof, and the Lender may, in its discretion, do so and on demand be reimbursed therefor by the Borrower;

(D) The Borrower and its Subsidiaries will maintain, or cause to be maintained, public liability insurance (subject to such deductibles for each entity as are acceptable to the Lender in its discretion) and fire and extended coverage insurance on all assets that are of a character usually insured by businesses engaged in the same or similar operations, all in form and amount sufficient to indemnify the Borrower or Subsidiary for 100% of the appraised value of any such asset lost or damaged (subject to any deductible customary in the Borrower's or Subsidiary's industry) or in an amount consistent with the amount of insurance generally carried on comparable assets within the industry and with such insurers as may be satisfactory to the Lender. The Borrower and its Subsidiaries will cause all such insurance policies to contain a standard mortgage clause and to be payable to the Lender as its interest may appear, to cause the Lender to be named as an additional insured on all such liability policies, to deliver the policies of insurance to the Lender, and, in the case of all policies of insurance carried for the benefit of the Borrower or any Subsidiary by any lessee, sublessee, subtenant, or other party having rights to occupy or use the mortgaged property or any part thereof or interest therein under any lease, sublease, or other agreement (whether oral, written, or otherwise evidenced), to cause all such policies to be payable to the Lender as its interest may appear. Such policies shall contain a

provision whereby they cannot be cancelled except after twenty (20) days' written notice to the Lender. The Borrower will furnish to the Lender such evidence of insurance as the Lender may require. The Borrower hereby agrees that, in the event it or any Subsidiary fails to pay or cause to be paid the premium on any such insurance when due, the Lender, in its discretion, may do so and be reimbursed by the Borrower therefor. The Borrower and each Subsidiary hereby assign to the Lender any returned or unearned premiums that may be due the Borrower or any Subsidiary upon cancellation by the insurer of any such policy for any reason whatsoever and direct any such insurer to pay the Lender any amounts so due, provided, however, that the Lender will pay to the Borrower or the appropriate Subsidiary any such returned or unearned premiums within five (5) days after the receipt thereof if there has not occurred and be continuing an Event of Default hereunder. The Lender is hereby appointed the attorney-in-fact of the Borrower and each Subsidiary (without requiring the Lender to act as such) to endorse any check which may be payable to the Borrower or any Subsidiary to collect any premiums or the proceeds of such insurance (other than proceeds of public liability insurance), and any amount so collected may be applied by the Lender toward satisfaction of the Loans and any other Obligations. If the Lender receives any proceeds from insurance in the absence of an Event of Default, it shall remit such proceeds to the Borrower or such Subsidiary within three (3) Business Days after the Lender's receipt of such proceeds, provided that immediately prior to any such remittance the Lender is provided with a Borrowing Base Certificate reflecting a current Borrowing Base not less than the amount of the Revolving Credit then outstanding;

(E) The Borrower and its Subsidiaries will each pay or cause to be paid when due, all taxes, assessments, and charges or levies imposed upon it or on any of its property or which it is required to withhold and pay except where contested in good faith by appropriate proceedings with adequate reserves therefor having been set aside on its books; provided, however, that the Borrower and each Subsidiary shall pay or cause to be paid all such taxes, assessments, charges or levies forthwith whenever foreclosure on any lien that may have attached (or security therefor) appears imminent;

(F) The Borrower will maintain:

(1) A Debt Service Coverage Ratio at all times equal to or greater than 1.20:1.0, tested as of the end of each fiscal year of the Borrower, beginning with the fiscal year ending December 31, 2014, and

(2) A Borrowing Base such that the amount of the Borrower's outstanding Revolving Credit will not, at any time, exceed its Borrowing Base;

(G) The Borrower and its Subsidiaries will each, when requested to do so, make available for inspection by duly authorized representatives of the Lender any of its books and records and will furnish the Lender any information regarding its business affairs and financial condition within a reasonable time after written request therefor;

(H) The Borrower and its Subsidiaries will each take all necessary steps to preserve its corporate existence and franchises and comply with all present and future Laws applicable to it in the operation of its business, and all material agreements to which it is subject;

(I) The Borrower and its Subsidiaries will each collect its Accounts and sell its Inventory only in the ordinary course of business;

(J) The Borrower and its Subsidiaries will each keep accurate and complete Records of its Accounts, Inventory, and Equipment consistent with sound business practices;

(K) The Borrower and its Subsidiaries will each give immediate notice to the Lender of (1) any litigation or proceeding in which it is a party if an adverse decision therein would require it to pay more than \$100,000.00 or deliver assets the value of which exceeds such sum (except where the claim is covered by insurance and the insurer has acknowledged coverage); and (2) the institution of any other suit or proceeding involving it that might materially and adversely affect its operations, financial condition, property, or business prospects;

(L) At the request of the Lender, the Borrower will furnish the Lender with true, correct and complete copies of federal income tax returns filed by the Borrower, together with all schedules thereto;

(M) The Borrower and its Subsidiaries will each (1) pay immediately from the proceeds of the initial disbursement of the Loans at the Closing, all of its outstanding Indebtedness (other than Subordinated Indebtedness and Indebtedness listed on Exhibit 5.01(N) to the extent shown on such Exhibit 5.01(N) to be permitted to exist after the Closing) and cause all security therefor or in respect thereof to be assigned to the Lender, and (2) pay when due (or within applicable grace periods) all of its other Indebtedness due third Persons except when the amount thereof is being contested in good faith by appropriate proceedings and with adequate reserves therefor being set aside on its books; provided, however, that no payment shall be made in respect to Subordinated Indebtedness except in strict compliance with all of the terms of subordination thereof theretofore approved in writing by the Lender. If default be made by the Borrower or any Subsidiary in the payment of any principal (or installment thereof) of, or interest on, any such Indebtedness, the Lender shall have the right, in its discretion, to pay such interest or principal for the account of the Borrower or such Subsidiary and be reimbursed by the Borrower or such Subsidiary therefor;

(N) The Borrower and its Subsidiaries will each notify the Lender promptly if it becomes aware of the occurrence of any Event of Default or of any fact, condition, or event that only with the giving of notice or passage of time or both, could become an Event of Default or if it becomes aware of any material adverse change in the financial condition (including, without limitation, proceedings in bankruptcy, insolvency, reorganization, or the appointment of a receiver or trustee), or results of operations of the Borrower, any Subsidiary, or the Guarantor or of the failure of the Borrower or any Subsidiary to observe any of their respective undertakings hereunder or under the Loan Documents;

(O) The Borrower and its Subsidiaries will each notify the Lender thirty (30) days in advance of any change in the location of any of its places of business or of the establishment of any new, or the discontinuance of any existing, place of business (it being agreed that a sales office is not a "place of business" for purposes of this Section 6.01(O));

(P) The Borrower and its Subsidiaries will each (1) fund any of its Employee Pension Benefit Plans in accordance with no less than the minimum funding standards of 29 U.S.C.A. 1082 (Section 302 of ERISA); (2) furnish the Lender, promptly after the filing of the same, with copies of any reports or other statements filed with the United States Department of Labor or the Internal Revenue Service with respect to any such Plan; and (3) promptly advise the Lender of the occurrence of any Reportable Event or Prohibited Transaction with respect to any Employee Benefit Plan;

(Q) The Borrower shall provide written notice to the Lender promptly upon becoming aware of the existence of any Commercial Tort Claims to which the Borrower is a party;

(R) The Borrower will permit the Lender to conduct field audits periodically at reasonable times on any premises occupied by the Borrower or on which any Collateral is located and shall pay to the Lender the Lender's reasonable costs and expenses related to each once per each twelve (12) month period, provided, however, that when an Event of Default has occurred and is continuing, the Borrower shall pay to the Lender the Lender's reasonable costs and expenses related to a field examination conducted during such period;

(S) Within thirty (30) days of Closing, the Borrower will use its reasonable best efforts to transfer to the Lender all of its deposit accounts and cash management services and shall in any event complete such transfer within ninety (90) days after Closing, except, if necessary, the Borrower may maintain an account at its existing depository institution with instructions for such depository institution to sweep any amount in such account into the Borrower's account maintained with the Lender; and

(T) The Borrower will maintain all of its deposit accounts and cash management services with the Lender while any Obligations to the Lender are outstanding.

#### 6.02 Negative Covenants.

The Borrower does hereby covenant and agree with the Lender that, so long as any of the Obligations remain unsatisfied or any commitments hereunder remain outstanding, it will comply, or if appropriate cause any Subsidiary to comply, at all times with the following negative covenants, unless the Lender shall otherwise have agreed in writing:

(A) Neither the Borrower nor any Subsidiary will enter into any merger, consolidation, reorganization or recapitalization, reclassify its capital stock, or allow any changes in its key management personnel, nor change its name without first providing the Lender with ninety (90) days advance written notice of the name change (for purposes of this Section 6.02(A), "key management" shall mean the President, Chief Executive Officer and Chief Financial Officer of the Borrower);

(B) Neither the Borrower nor any Subsidiary will allow any Change of Control;

(C) Neither the Borrower nor any Subsidiary sell, transfer, lease, or otherwise dispose of all or (except in the ordinary course of business) any material part of its assets;



(D) Neither the Borrower nor any Subsidiary will sell, lease, transfer, assign, or otherwise dispose of any of the Collateral except in the ordinary course of business, or disposition of obsolete or worn out Equipment;

(E) Neither the Borrower nor any Subsidiary will sell or otherwise dispose of, or for any reason cease operating, any of its divisions, franchises, or lines of business, except for disposition of divisions, franchises and lines of business generating less than \$250,000.00 of revenue in the aggregate, upon advance written notice to the Lender;

(F) Neither the Borrower nor any Subsidiary will mortgage, pledge, grant, or permit to exist a security interest in, or a lien upon, any of its assets of any kind, now owned or hereafter acquired, except for Permitted Liens, liens of the Loan Documents, and existing liens listed on Exhibit 1.01(I) to the extent shown on such Exhibit 1.01(I) to be permitted to exist after the Closing;

(G) Neither the Borrower nor any Subsidiary will become liable, directly or indirectly, as guarantor or otherwise for any obligation of any other Person, except for the endorsement of commercial paper for deposit or collection in the ordinary course of business;

(H) Neither the Borrower nor any Subsidiary will incur, create, assume, or permit to exist any Indebtedness except: (1) the Loans; (2) existing Indebtedness listed on Exhibit 5.01(N) to the extent shown on such Exhibit 5.01(N) to be permitted to exist after the Closing; (3) trade indebtedness incurred in the ordinary course of business (provided, however, that neither the Borrower nor any Subsidiary may acquire inventory other than for cash or on open account except as expressly approved in writing and in advance by the Lender); (4) contingent Indebtedness permitted by Section 6.02(F); (5) lease obligations permitted by Section 6.02(L); (6) Indebtedness secured by Permitted Liens; (7) Subordinated Indebtedness; and (8) up to an aggregate maximum of \$250,000.00 for loans to purchase equipment, relocate an office or other similar expenses incurred in the ordinary course of business;

(I) Neither the Borrower nor any Subsidiary (other than a wholly owned Subsidiary of the Borrower) (1) directly or indirectly make any investment other than Permitted Investments; (2) pay any dividends or make any distribution or payment or redeem, retire or purchase any capital stock, provided that (a) the Borrower may convert any of its convertible securities into other securities pursuant to the terms of such convertible securities or otherwise in exchange thereof, (b) the Borrower may pay dividends solely in common stock, and (c) the Borrower may repurchase the stock of existing and former employees or consultants pursuant to Board-approved stock repurchase agreements, so long as (X) an Event of Default does not exist at the time of such repurchase and would not exist after giving effect to such repurchase and (Y) such repurchase does not exceed \$250,000.00 in the aggregate in any fiscal year;

(J) Neither the Borrower nor any Subsidiary will form any subsidiary, make any investment in (including any assignment of Inventory or other property), or make any loan in the nature of an investment to, any Person, other than investments of the Borrower in the Subsidiaries listed on Exhibit 5.01(A);

(K) Neither the Borrower nor any Subsidiary will make any loan or advance to any officer, shareholder, director, or employee of the Borrower or any Subsidiary except for advances to employees for sales commissions, travel expenses and the like incurred in the ordinary course of business aggregating no more than \$600,000.00 outstanding at any time;

(L) Neither the Borrower nor any Subsidiary will make payments on account of the purchase or lease of Fixed Assets that, in the aggregate, in any fiscal year (commencing with the current fiscal year) will exceed the greater of (i) \$250,000.00 or (ii) depreciation taken or to be taken with respect to Fixed Assets during such year; as used in this paragraph, the term "lease" means a lease reflected on a consolidated balance sheet of the Borrower and its Subsidiaries or a lease that should be so reflected under GAAP;

(M) Neither the Borrower nor any Subsidiary will pay or commit to pay, in an aggregate amount for any fiscal quarter (commencing with the current fiscal quarter), in excess of \$75,000.00 with respect to lease obligations not existing as of the date of this Agreement, as used in this paragraph, the term "lease" means a lease that is not capitalized in a consolidated balance sheet of the Borrower and should not be so capitalized under GAAP;

(N) Neither the Borrower nor any Subsidiary will purchase or otherwise invest in or hold securities, nonoperating real estate, or other nonoperating assets except: (1) Permitted Investments; (2) the present investment in any such assets held as of September 30, 2013 and reflected in the Financial Statements; and (3) operating assets that hereafter become nonoperating assets;

(O) Neither the Borrower nor any Subsidiary will, except as permitted in accordance with Section 6.02(I) hereof, redeem, purchase, or retire any of its voting interest or purchase or retire for any consideration, any warrant, right, or option pertaining thereto or other security convertible into any of the foregoing, or permit any redemption or retirement of the outstanding voting interest of the Borrower or of any Subsidiary;

(P) Neither the Borrower nor any Subsidiary will prepay any Subordinated Indebtedness, Indebtedness for borrowed money except the Obligations, or Indebtedness secured by any of its assets (except the Obligations), or enter into or modify any agreement as a result of which the terms of payment of any of the foregoing Indebtedness are waived or modified;

(Q) Neither the Borrower nor any Subsidiary will enter into any sale-leaseback transaction;

(R) Neither the Borrower nor any Subsidiary will acquire or agree to acquire any stock in, or all or substantially all of the assets of, any Person;

(S) Neither the Borrower nor any Subsidiary will furnish the Lender any certificate or other document that will contain any untrue statement of material fact or that will omit to state a material fact necessary to make it not misleading in light of the circumstances under which it was furnished; and

(T) Neither the Borrower nor any Subsidiary will directly or indirectly apply any part of the proceeds of the Loans to the purchasing or carrying of any "margin stock" within the meaning of Regulation U of the Board of Governors of the Federal Reserve System, or any regulations, interpretations, or rulings thereunder.

## ARTICLE 7.0 DEFAULT

### 7.01 Events of Default.

The occurrence of any one or more of the following events shall constitute an Event of Default hereunder:

(A) The Borrower or the Guarantor shall fail to pay when due any Obligations to the Lender;

(B) The Borrower or the Guarantor or any other Subsidiary shall fail to observe or perform any other obligation to be observed or performed by it hereunder or under any of the Loan Documents, and such failure shall continue for thirty (30) days after (1) notice of such failure from the Lender; or (2) the Lender is notified of such failure or should have been so notified pursuant to the provisions of Section 6.01 (N), whichever is earlier;

(C) The Borrower or any Subsidiary shall fail to pay any Indebtedness due any third Persons in excess of \$10,000.00 in the aggregate, and such failure shall continue beyond any applicable grace period, or the Borrower or any Subsidiary shall suffer to exist any other event of default under any agreement binding the Borrower or any Subsidiary with the exception of failures to pay or defaults being contested in good faith in appropriate proceedings diligently conducted and for which adequate reserves have been set aside in accordance with GAAP;

(D) Any financial statement, representation, warranty, or certificate made or furnished by or with respect to the Borrower or the Guarantor or any other Subsidiary to the Lender in connection with this Agreement, or as inducement to the Lender to enter into this Agreement, or in any separate statement or document to be delivered to the Lender hereunder, shall be materially false, incorrect, or incomplete when made;

(E) The Borrower or the Guarantor or any other Subsidiary shall admit its inability to pay its debts as they mature or shall make an assignment for the benefit of itself or any of its creditors;

(F) Proceedings in bankruptcy, or for reorganization of the Borrower, the Guarantor or any other Subsidiary, or for the readjustment of any of their respective debts under the Bankruptcy Code, as amended, or any part thereof, or under any other Laws, whether state or federal, for the relief of debtors, now or hereafter existing, shall be commenced against or by the Borrower or the Guarantor or any other Subsidiary and, except with respect to any such proceedings instituted by the Borrower, the Guarantor or any other Subsidiary, shall not be discharged within ninety (90) days of their commencement;

(G) A receiver or trustee shall be appointed for the Borrower or the Guarantor or for any substantial part of their respective assets, or any proceedings shall be instituted for the dissolution or the full or partial liquidation of the Borrower or the Guarantor, and except with respect to any such appointments requested or instituted by the Borrower or the Guarantor, such

receiver or trustee shall not be discharged within ninety (90) days of his appointment, and except with respect to any such proceedings instituted by the Borrower or the Guarantor, such proceedings shall not be discharged within ninety (90) days of their commencement, or the Borrower or the Guarantor shall discontinue business or materially change the nature of its business, or the Collateral becomes, in the reasonable judgment of the Lender, insufficient in value to satisfy the Obligations, or the Lender otherwise reasonably finds itself insecure as to the prompt and punctual payment and discharge of the Obligations;

(H) The Borrower or the Guarantor shall suffer final judgments (which are not covered by insurance where the insurer has acknowledged coverage) for payment of money aggregating in excess of \$100,000.00 and shall not discharge the same within a period of thirty (30) days unless, pending further proceedings, execution has not been commenced or, if commenced, has been effectively stayed;

(I) A judgment creditor of the Borrower or the Guarantor shall obtain possession of any of the Collateral by any means, including (without implied limitation) levy, distraint, replevin, or self-help;

(J) Loss by fire or other casualty to any security for the Loans which is not insured exceeding \$250,000.00 as determined by a public adjuster acceptable to the Lender;

(K) Any obligee of Subordinated Indebtedness shall fail to comply with the subordination provisions of the instruments evidencing such Subordinated Indebtedness; or

(L) The Guarantor shall fail to comply fully with the requirements of the Guaranty, or give notice of or assert the termination, discontinuance, invalidity or unenforceability of any Guaranty;

(M) There occurs a Change of Control of the Borrower; or

(N) The Borrower shall fail to transfer to the Lender and maintain with the Lender its deposit accounts and cash management services in accordance with Section 6.01(S) of this Agreement.

#### 7.02 Acceleration.

At its option, and at any time, whether immediately or otherwise, the Lender may, upon the occurrence and during the continuance of any Event of Default, declare all Obligations immediately due and payable without further action of any kind including without limitation, notice, demand or presentment.

### ARTICLE 8.0 THE LENDER'S RIGHTS AND REMEDIES

#### 8.01 Account Debtors

Upon the occurrence and during the continuance of an Event of Default and at any time thereafter, the Lender, without presentment, demand, notice, protest or advertisement of any kind, may notify account debtors, at the Borrower's expense, that the Collateral has been

assigned to the Lender and that payments shall be made directly to the Lender. Upon request of the Lender, the Borrower will notify such account debtors that their accounts must be paid to the Lender. Upon the occurrence and during the continuance of an Event of Default and at all times thereafter, the Borrower will hold all checks, drafts, cash and other remittances in trust for the Lender and deliver them in kind to the Lender. The Lender shall have full power to collect, compromise, endorse, sell or otherwise deal with the Collateral or proceeds thereof in its own name or in the name of the Borrower.

#### 8.02 Possession and Foreclosure of Collateral

Upon the occurrence and during the continuance of an Event of Default and at any time thereafter, to the extent that the Borrower could legally do so, the Lender, without presentment, demand, notice, protest or advertisement of any kind, may enter onto, occupy and use any premises owned by the Borrower or in which the Borrower has any interest. The Lender may take possession of all Collateral. In the Lender's reasonable discretion, the Lender may operate and use the Borrower's equipment, complete work in process and sell inventory without being liable to the Borrower on account of any losses, damage or depreciation that may occur as a result thereof (so long as the Lender acts in good faith). The Lender may lease or license the Collateral to any Person for such purposes. In any event, the Lender may sell, lease, assign and deliver the whole or any part of the Collateral, at public or private sale, for cash, upon credit or for future delivery, at such prices and upon such terms as the Lender deems advisable. The Lender may sell or lease Collateral alone or in conjunction with other property, real or personal, and allocate the sale proceeds or leases among the items of Collateral sold without the necessity of the Collateral being present at any such sale, or in view of prospective purchasers thereof. If notice of sale is legally required, the Borrower agrees that five (5) days written notice shall be deemed reasonable. Upon such sale, the Lender may become the purchaser of the whole or any part of the Collateral sold, discharged from all claims and free from any right of redemption. In case of any such sale by the Lender of all or any of the Collateral on credit, or for future delivery, such Collateral so sold may be retained by the Lender until the selling price is paid by the purchaser. The Lender shall incur no liability in case of the failure of the purchaser to take possession and pay for the Collateral so sold. In case of any such failure, the said Collateral may be resold. Any Collateral remaining unsold after being offered at public auction may be abandoned or disposed of for no consideration in such manner as the Lender deems appropriate.

In any event, at any time and from time to time the Lender may abandon the Collateral or any part thereof. The Borrower agrees promptly upon demand to take possession of any and all abandoned Collateral and to remove it from any location in the possession of or under the control of the Lender.

#### 8.03 Use of Intellectual Property

Upon the occurrence and during the continuance of an Event of Default and at any time thereafter, the Lender, without presentment, demand, notice, protest or advertisement of any kind, may use all or any part of the Borrower's Intellectual Property which the Borrower now has or may hereafter acquire. The Lender may license such Intellectual Property to third parties, seek registration of such Intellectual Property in any state or nation or prosecute pending applications for patent, trademark, or service marks in the Borrower's name in any state or nation.

---

#### 8.04 Notification of Default to Third Parties

The Lender may notify account debtors of the Borrower to pay over to the Lender for application against the Obligations any sums due from such account debtors to the Borrower. In addition, upon the occurrence and during the continuance of an Event of Default and at any time thereafter, the Lender, without presentment, demand, notice, protest or advertisement of any kind, may notify the Borrower's suppliers and other third parties of the default and of any and all decisions made and actions taken by the Lender with respect to this Agreement, the Obligations or the Collateral, without liability of any kind.

#### 8.05 Assembly of Collateral

Upon the occurrence and during the continuance of an Event of Default and at any time thereafter, the Lender, without presentment, demand, notice, protest or advertisement of any kind, may require the Borrower to assemble the Collateral in a single location at a place to be designated by the Lender and make the Collateral at all times secure and available to the Lender.

#### 8.06 Right of Set-Off.

The Lender may, and is hereby authorized by the Borrower, at any time and from time to time, upon the occurrence and during the continuance of an Event of Default, to the fullest extent permitted by applicable Laws, without advance notice to the Borrower (any such notice being expressly waived by the Borrower), set-off and apply any and all deposits (general or special, time or demand, provisional or final) at any time held and any other indebtedness at any time owing by the Lender to, or for the credit or the account of, the Borrower against any or all of the Obligations of the Borrower or the Guarantor, now or hereafter existing, whether or not such Obligations have matured and irrespective of whether the Lender has exercised any other rights that it has or may have with respect to such Obligations, including without limitation any acceleration rights. The Lender agrees promptly to notify the Borrower after any such set-off and application, provided that the failure to give such notice shall not affect the validity of such set-off and application. The rights of the Lender under this Section 8.06 are in addition to the other rights and remedies (including, without limitation, other rights of set-off) which the Lender may have.

#### 8.07 Exercise of Other Remedies

Upon the occurrence and during the continuance of any Event of Default and at any time thereafter, the Lender, without presentment, demand, notice, protest or advertisement of any kind, may exercise the remedies of a secured party afforded by the Uniform Commercial Code and other applicable law or by the terms of any agreement between the Borrower and the Lender.

## 8.08 Cumulative Rights and Remedies

All rights and remedies of the Lender, whether provided for herein or in other agreements, instruments or documents or conferred by law, are cumulative and may be exercised alone or simultaneously.

## 8.09 Additional Rights and Remedies

(A) Upon the occurrence and during the continuance of an Event of Default, all obligations on the part of the Lender to make advances on the Revolving Credit Note, if the Lender so elects, shall cease and terminate, and, at the option of the Lender, each of the Notes shall become immediately due and payable, and the Lender shall thereupon be authorized and empowered to exercise any rights of foreclosure or as otherwise provided for the realization of any security for the Notes covered by any of the Loan Documents; but the Lender may, at its reasonable discretion, make any advances or portions of advances, after demand or the occurrence of any such Event of Default, without thereby waiving its right to demand payment of the Borrower's indebtedness evidenced by the Notes and secured by the Loan Documents, and without becoming liable to make any other or further advances as hereinabove contemplated by this Agreement.

(B) Upon the occurrence and during the continuance of any Event of Default, the rights, powers, and privileges provided in this Section 8.09 and all other remedies available to the Lender under this Agreement or at law or in equity may be exercised by the Lender at any time and from time to time, whether or not the indebtedness evidenced and secured by the Notes and the other Loan Documents shall be due and payable, and whether or not the Lender shall have instituted any foreclosure proceedings or other action for the enforcement of its rights under the Notes or any of the other Loan Documents.

## ARTICLE 9.0 ATTORNEY-IN-FACT

### 9.01 Attorney-In-Fact

Upon the occurrence and during the continuance of an Event of Default and at all times thereafter, the Borrower hereby irrevocably appoints the Lender, or its designee, as the Borrower's true and lawful attorney-in-fact, with full power as follows: (A) to endorse the name of the Borrower on any assignments, notes, checks, drafts, money orders, or other instruments of payment for Collateral; (B) to sign or endorse the name of the Borrower on any negotiable instrument, invoice, freight or express bill, bill of lading, storage or warehouse receipts, drafts, assignments, verifications and notices in connection with accounts; (C) to obtain, adjust, settle and cancel, in the Borrower's name, insurance policies as required by Section 6.01(D) and to sign the Borrower's name on settlement checks or drafts; (D) in the Borrower's name, to do any act which this Agreement requires Borrower to do, and, (E) to give notice to the United States Post Office to effect changes of address so that mail addressed to the Borrower may be delivered directly to the Lender. In exercising this power-of-attorney, the Lender shall not be liable to the extent that it acts in good faith.

## ARTICLE 10.0 MISCELLANEOUS

### 10.01 Construction.

The provisions of this Agreement shall be in addition to those of any guaranty, pledge or security agreement, note, or other evidence of liability now or hereafter held by the Lender, all of which shall be construed as complementary to each other. Nothing herein contained shall prevent the Lender from enforcing any or all other guaranty, pledge or security agreements, notes, or other evidences of liability in accordance with their respective terms.

### 10.02 Further Assurance.

From time to time, the Borrower will execute and deliver to the Lender such additional documents and will provide such additional information as the Lender may reasonably require to carry out the terms of this Agreement and be informed of the status and affairs of the Borrower.

### 10.03 Enforcement and Waiver by the Lender.

The Lender shall have the right at all times to enforce the provisions of this Agreement and the other Loan Documents in strict accordance with the terms hereof and thereof, notwithstanding any conduct or custom on the part of the Lender in refraining from so doing at any time or times. The failure of the Lender at any time or times to enforce its rights under such provisions, strictly in accordance with the same, shall not be construed as having created a custom in any way or manner contrary to specific provisions of this Agreement or as having in any way or manner modified or waived the same. All rights and remedies of the Lender are cumulative and concurrent and the exercise of one right or remedy shall not be deemed a waiver or release of any other right or remedy.

### 10.04 Expenses of the Lender.

The Borrower will, on demand, reimburse the Lender for all expenses, including the reasonable fees and expenses of legal counsel for the Lender, incurred by the Lender in connection with the preparation, administration, amendment, modification, or enforcement of this Agreement and the other Loan Documents and the collection or attempted collection of any of the Obligations including without limitation by reason of enumeration, all reasonable expenses and fees of legal counsel for the Lender incurred in connection with any bankruptcy or insolvency action of the Borrower, the Guarantor or any other Subsidiary.

### 10.05 Notices.

Any notices or consents required or permitted by this Agreement shall be in writing and shall be deemed delivered if delivered in person or by a nationally recognized overnight courier, or if sent by certified mail, postage prepaid, return receipt requested, facsimile transmission, as follows, unless such address is changed by written notice hereunder:

|                         |   |
|-------------------------|---|
| (A) If to the Borrower: | WORLD ENERGY SOLUTIONS, INC.<br>100 Front Street, 20 <sup>th</sup> Floor<br>Worcester, MA 01608<br>Attention: James F. Parslow,<br>Chief Financial Officer<br>Facsimile: 508-459-8101 |
|-------------------------|---|



With a copy to:

Paul J. D'Onfro, Esquire  
Michael A. Refolo, Esquire  
Mirick, O'Connell, DeMallie & Lougee, LLP  
100 Front Street  
Worcester, MA 01608  
Facsimile: 508-983-6249

(B) If to the Lender

COMMERCE BANK & TRUST COMPANY  
386 Main Street  
Worcester, MA 01608  
Attention: Senior Commercial Loan Officer  
Facsimile: 508-797-6933

With a copy to:

George W. Tetler III, Esquire  
Bowditch & Dewey, LLP  
311 Main Street  
P.O. Box 15156  
Worcester, MA 01615-0156  
Facsimile: 508-929-3052

Any party may change the address to which notices are to be sent to it by giving written notice of such change of address to the other party in the manner herein provided for giving notice. Any such notice, demand, request, or other communication shall be deemed given when mailed as aforesaid.

#### 10.06 Waiver and Indemnification by the Borrower.

To the maximum extent permitted by applicable Laws, the Borrower:

(A) Waives (1) protest of all commercial paper at any time held by the Lender on which the Borrower is in any way liable; (2) except as the same may herein be specifically granted, notice of acceleration and of intention to accelerate; and (3) notice and opportunity to be heard, after acceleration in the manner provided in Section 7.02, before exercise by the Lender of the remedies of self-help, set-off, or of other summary procedures permitted by any applicable Laws or by any agreement with the Borrower, and, except where required hereby or by any applicable Laws, notice of any other action taken by the Lender; and

(B) Defends, indemnifies and holds harmless the Lender and its officers, attorneys, agents, and employees from all claims for loss or damage caused by any act or omission on the

part of any of them in connection with the transactions contemplated by this Agreement or related to the banking relationship between or among the Borrower, the Guarantor and the Lender, excepting only the Lender's willful misconduct or gross negligence.

#### 10.07 Participation/Pledge.

Notwithstanding any other provision of this Agreement, the Borrower understands that the Lender may at any time enter into participation agreements with one or more participating banks whereby the Lender will allocate certain percentages of its commitment to them. The Borrower acknowledges that, for the convenience of all parties, this Agreement is being entered into with the Lender only and that its obligations under this Agreement are undertaken for the benefit of, and as an inducement to, any such participating bank as well as the Lender, and the Borrower hereby grants to each such participating bank, to the extent of its participation in the Loans, the right to set off deposit accounts maintained by the Borrower with such bank. Notwithstanding the foregoing provisions of this Section, any Lender may at any time pledge or assign all or any portion of such Lender's rights under this Agreement, the Notes, and the other Loan Documents to a Federal Reserve bank; provided, however, that no such pledge or assignment shall release such Lender from such Lender's obligations hereunder or under the Notes or any of the other Loan Documents.

#### 10.08 WAIVER OF JURY TRIAL.

**EACH OF THE LENDER AND THE BORROWER WAIVES ITS RIGHTS TO A TRIAL BY JURY WITH RESPECT TO ANY SUIT, ACTION OR PROCEEDING, WHETHER CLAIM OR COUNTERCLAIM, BROUGHT OR INSTITUTED BY ANY PARTY TO THIS AGREEMENT OR ANY OF THEIR SUCCESSORS AND ASSIGNS, WHICH RELATES DIRECTLY OR INDIRECTLY TO THIS AGREEMENT, THE LOANS, THE OTHER LOAN DOCUMENTS OR THE RELATIONSHIP BETWEEN THE LENDER AND THE BORROWER.**

#### 10.09 Applicable Law.

This Agreement is entered into and performable in The Commonwealth of Massachusetts and shall be subject to and construed and enforced in accordance with the laws of The Commonwealth of Massachusetts.

#### 10.10 Binding Effect, Assignment, and Entire Agreement.

This Agreement shall inure to the benefit of, and shall be binding upon, the respective successors and permitted assigns of the parties hereto. The Borrower has no right to assign any of its rights or obligations hereunder without the prior written consent of the Lender. This Agreement, including the Exhibits hereto, all of which are hereby incorporated herein by reference, and the documents executed and delivered pursuant hereto, constitute the entire agreement between the parties and may be amended only by a writing signed on behalf of each party.

10.11 Severability.

If any provision of this Agreement shall be held invalid under any applicable Laws, such invalidity shall not affect any other provision of this Agreement that can be given effect without the invalid provision, and, to this end, the provisions hereof are severable.

10.12 Counterparts.

This Agreement may be executed in any number of counterparts, each of which shall be deemed to be an original, but all of which together shall constitute but one and the same instrument.

10.13 Integration Clause

This Agreement is intended by the parties as the final, complete and exclusive statement of the transactions evidenced by this Agreement. All prior or contemporaneous promises, agreements and understandings, whether oral or written, are deemed to be superceded by this Agreement, and no party is relying on any promise, agreement or understanding not set forth in this Agreement. This Agreement may not be amended or modified except by written instrument describing such amendment or modification executed by the Borrower and the Lender.

10.14 Governing Law; Consent to Jurisdiction.

THIS AGREEMENT IS INTENDED TO TAKE EFFECT AS A SEALED INSTRUMENT AND SHALL BE GOVERNED BY, AND CONSTRUED IN ACCORDANCE WITH, THE LAWS OF THE COMMONWEALTH OF MASSACHUSETTS. The Borrower agrees that any suit for the enforcement of this Agreement may be brought in the courts of The Commonwealth of Massachusetts or any federal court sitting therein and consents to the non-exclusive jurisdiction of such court and to service of process in any such suit being made upon the Borrower by mail at the address identified with its signature below (unless the Borrower has by five (5) days written notice specified another address). The Borrower hereby waives any objection that it may now or hereafter have to the venue of any such suit or any such court or that such suit is brought in an inconvenient court.

*THIS SPACE INTENTIONALLY LEFT BLANK;  
SIGNATURES APPEAR ON THE FOLLOWING PAGE*

IN WITNESS WHEREOF, the parties hereto have duly executed this Agreement as a sealed instrument as of the day and year first above written.

**WORLD ENERGY SOLUTIONS, INC.**

/s/ \_\_\_\_\_  
Witness

By: /s/ James Parslow \_\_\_\_\_  
Name: James Parslow  
Title: Chief Financial Officer and Treasurer

**COMMERCE BANK & TRUST COMPANY**

/s/ \_\_\_\_\_  
Witness

By: /s/ Thomas Moschos \_\_\_\_\_  
Name: Thomas Moschos  
Title: Commercial Loan Officer

EXHIBIT 6.01(A)

USE OF LOAN PROCEEDS

The proceeds of the Term Loan shall be used to refinance all of the Borrower's outstanding indebtedness to Silicon Valley Bank and for working capital purposes.

The proceeds of the Revolving Credit shall be used for working capital of the Borrower.

**REVOLVING CREDIT NOTE**

\$2,500,000.00

Worcester, Massachusetts  
December 30, 2013

**FOR VALUE RECEIVED**, the undersigned, **WORLD ENERGY SOLUTIONS, INC.**, a Delaware corporation with its principal place of business at 100 Front Street, 20th Floor, Worcester, Massachusetts 01608 (the "**Borrower**"), hereby promises to pay to

**COMMERCE BANK & TRUST COMPANY,**

a Massachusetts banking corporation (the "**Lender**"), OR ORDER, at its office at 386 Main Street, Worcester, Massachusetts 01608, or such other place as the Lender may from time to time specify in writing, the principal sum of

**TWO MILLION FIVE HUNDRED THOUSAND AND NO/100 DOLLARS (\$2,500,000.00)**

(or so much as may be outstanding from time to time) with interest on the unpaid principal until paid at the rate and in the manner hereinafter provided in lawful money of the United States of America in immediately available funds, without counterclaim or setoff and free and clear of, and without any deduction or withholding for, any taxes or other payments.

This Revolving Credit Note is issued in conjunction with and secured as set forth in a Loan and Security Agreement dated as of even date herewith by and between the Borrower and the Lender (as may be amended from time to time, the "**Agreement**"), all the terms and conditions of which are incorporated herein by reference. No reference to the Agreement or to any provision thereof shall affect or impair the absolute and unconditional obligation of the Borrower to pay the principal of and interest on this Revolving Credit Note as herein provided. An Event of Default under the Agreement or, under any of the Loan Documents shall also constitute an Event of Default hereunder. The occurrence of an Event of Default shall constitute a default (beyond any applicable grace or cure periods) under each other obligation of the Borrower to the Lender.

Capitalized terms used and not otherwise defined herein shall have the meanings ascribed to such terms in the Agreement.

Interest shall be calculated on the daily unpaid principal balance of the indebtedness evidenced by this Revolving Credit Note computed on the basis of the actual number of days elapsed over a year assumed to have three hundred sixty (360) days, provided that interest shall be due for the actual number of days elapsed during each period for which interest is being charged.

The unpaid principal of this Revolving Credit Note from time to time outstanding shall bear interest at the applicable rate per annum (the "Note Rate"), in accordance with the provisions of this Revolving Credit Note, as follows:

(a) From the date of this Revolving Credit Note through and including June 30, 2014, at a fluctuating rate per annum equal to the aggregate of (i) the Prime Rate plus (ii) one and three-quarters percent (1.75%); and

(b) Commencing July 1, 2014 through and including the Revolving Credit Termination Date hereinafter defined, at a fluctuating rate per annum equal to the aggregate of (i) the Prime Rate plus (ii) the Applicable Margin (calculated as set forth below).

The "Applicable Margin" shall mean that percentage determined by calculation of the Lender to be the ratio of Actual EBITDA to Projected EBITDA as of each semi-annual fiscal period commencing with the semi-annual period ending on June 30, 2014, as follows:

| <u>Ratio of Actual EBITDA to Projected EBITDA</u>               | <u>Applicable Margin -</u> |
|---|----------------------------|
| <del>greater than 1.5 to 1.0</del>                              | <del>1.25%</del>           |
| equal to or greater than 1.25 to 1.0, but less than 1.50 to 1.0 | 1.50%                      |
| <del>less than 1.25 to 1.0</del>                                | <del>1.75%</del>           |

Interest hereunder shall be payable monthly in arrears commencing one (1) month from the date of this Revolving Credit Note and continuing to be due and payable on the same day of each succeeding month. All principal, interest and other indebtedness due hereunder if not sooner paid, shall be due and payable on December 30, 2016 (the "Revolving Credit Termination Date").

Until the earlier of (a) the Revolving Credit Termination Date or (b) the occurrence of an Event of Default, the Borrower may borrow, repay and reborrow hereunder from time to time as more particularly described herein and in the Agreement.

If the entire amount of any required principal and/or interest is not paid in full within fifteen (15) days after the same is due, the Borrower shall pay to the Lender a late fee equal to five percent (5.00%) of the required payment. Such late charge payments are made for the purpose of compensating the Lender for its administrative, costs and expenses in handling late payments and losses in connection therewith. This provision is not intended to provide a grace period for any payment otherwise due and payable and shall not constitute a waiver by the Lender to insist upon the strict performance of any of the Borrower's covenants or agreements with, or obligations to, the Lender or to declare an Event of Default for any payment not made when it was due and payable.

All payments shall be applied first to the payment of all fees, expenses and other amounts due to the Lender (excluding principal and interest), then to accrued interest, and the balance on account of outstanding principal; provided, however, that during the continuance of an Event of Default, payments will be applied to the obligations of the Borrower to the Lender as the Lender shall determine in its sole discretion.

Upon the occurrence and during the continuance of an Event of Default (whether or not the Lender has accelerated payment of this Revolving Credit Note), or after the Revolving Credit Termination Date or after judgment has been rendered on this Revolving Credit Note, the unpaid principal of this Revolving Credit Note, including interest, fees or costs which are not paid when due, will, at the option of the Lender, bear interest at a rate which is five percent (5.00%) per annum greater than the Note Rate (the "Default Rate"). This may result in compounding of interest. This will not constitute a waiver of any Event of Default.

At its option, and at any time, whether immediately or otherwise, upon the occurrence and during the continuance of an Event of Default, the Lender may declare this Revolving Credit Note immediately due and payable without further action of any kind including notice, further demand or presentment.

The Borrower and any guarantor hereby grant to the Lender a continuing lien, security interest and right of setoff as security for all liabilities and obligations to the Lender, whether now existing or hereafter arising, upon and against all deposits, credits, collateral and property, now or hereafter in the possession, custody, safekeeping or control of the Lender or any entity under the control of the Lender and its successors and assigns, or in transit to any of them. At any time, without demand or notice (any such notice being expressly waived by the Borrower), the Lender may set off the same or any part thereof and apply the same to any liability or obligation of the Borrower and any guarantor even though unmatured and regardless of the adequacy of any other collateral securing this Revolving Credit Note. ANY AND ALL RIGHTS TO REQUIRE THE LENDER TO EXERCISE ITS RIGHTS OR REMEDIES WITH RESPECT TO ANY OTHER COLLATERAL WHICH SECURES THIS REVOLVING CREDIT NOTE, PRIOR TO EXERCISING ITS RIGHT OF SETOFF WITH RESPECT TO SUCH DEPOSITS, CREDITS OR OTHER PROPERTY OF THE BORROWER AND ANY GUARANTOR, ARE HEREBY KNOWINGLY, VOLUNTARILY AND IRREVOCABLY WAIVED.

The Borrower shall pay on demand all reasonable expenses of the Lender in connection with the preparation, administration, default, collection, waiver or amendment of loan terms, or in connection with the Lender's exercise, preservation or enforcement of any of its rights, remedies or options hereunder, including, without limitation, reasonable fees of outside legal counsel or other similar professional fees or expenses, and any fees or expenses associated with travel or other costs relating to any appraisals or examinations conducted in connection with this Revolving Credit Note or any collateral therefor, and the amount of all such expenses, if not paid within thirty (30) days, shall, until paid, bear interest at the rate applicable to principal hereunder (including any Default Rate) and be an obligation secured by any collateral.

The Borrower and each guarantor, endorser or other person now or hereafter liable for the payment of any of the indebtedness evidenced by this Revolving Credit Note severally agree, by making, guaranteeing or endorsing this Revolving Credit Note or by making any agreement to pay any of the indebtedness evidenced by this Revolving Credit Note, to waive presentment for payment, protest and demand, notice of protest, demand and of dishonor and non-payment of this



Revolving Credit Note, and consent without notice or further assent (a) to the substitution, exchange, or release of the collateral securing this Revolving Credit Note or any part thereof at any time; (b) to the acceptance by the holder or holders at any time of any additional collateral or security or other guarantors of this Revolving Credit Note, (c) to the modification or amendment at any time, and from time to time, of this Revolving Credit Note, the Agreement and any other instrument securing this Revolving Credit Note, at the request of any person liable hereon; (d) to the granting by the holder hereof of any extension of the time for payment of this Revolving Credit Note or for the performance of the agreements, covenants, and conditions contained in this Revolving Credit Note, the Agreement or any instrument securing this Revolving Credit Note, at the request of any other person liable hereon; and (e) to any and all forbearances and indulgences whatsoever; and such consent shall not alter or diminish the liability of any person.

This Revolving Credit Note shall be governed by, and construed in accordance with, the laws of The Commonwealth of Massachusetts. The Borrower agrees that any suit for the enforcement of this Revolving Credit Note may be brought in the courts of The Commonwealth of Massachusetts or any Federal Court sitting therein and consents to the non-exclusive jurisdiction of such court and to service of process in any such suit being made upon the Borrower by mail at the address specified herein. The Borrower hereby waives any objection that it may now or hereafter have to the venue of any such suit or any such court or that such suit was brought in an inconvenient court.

**THE BORROWER AND THE LENDER (BY ACCEPTANCE OF THIS REVOLVING CREDIT NOTE) MUTUALLY HEREBY KNOWINGLY, VOLUNTARILY AND INTENTIONALLY WAIVE THE RIGHT TO A TRIAL BY JURY IN RESPECT OF ANY CLAIM BASED HEREON, ARISING OUT OF, UNDER OR IN CONNECTION WITH THIS REVOLVING CREDIT NOTE, THE AGREEMENT, THE LOAN DOCUMENTS OR ANY OTHER FINANCING INSTRUMENTS EXECUTED OR CONTEMPLATED TO BE EXECUTED IN CONNECTION HERewith OR WITH THE AGREEMENT OR ANY COURSE OF CONDUCT, COURSE OF DEALINGS, STATEMENTS (WHETHER VERBAL OR WRITTEN) OR ACTIONS OF ANY PARTY RELATED HERETO, INCLUDING, WITHOUT LIMITATION, ANY COURSE OF CONDUCT, COURSE OF DEALINGS, STATEMENTS OR ACTIONS OF THE LENDER RELATING TO THE ADMINISTRATION OF THE LOANS EVIDENCED BY THIS REVOLVING CREDIT NOTE OR ENFORCEMENT OF THE AGREEMENT, THE LOAN DOCUMENTS OR ANY SUCH FINANCING INSTRUMENTS, AND AGREE THAT NO PARTY WILL SEEK TO CONSOLIDATE ANY SUCH ACTION WITH ANY OTHER ACTION IN WHICH A JURY TRIAL CANNOT BE OR HAS NOT BEEN WAIVED. EXCEPT AS PROHIBITED BY LAW, THE BORROWER HEREBY WAIVES ANY RIGHT IT MAY HAVE TO CLAIM OR RECOVER IN ANY LITIGATION ANY SPECIAL, EXEMPLARY, PUNITIVE OR CONSEQUENTIAL DAMAGES OR ANY DAMAGES OTHER THAN, OR IN ADDITION TO, ACTUAL DAMAGES. THE BORROWER CERTIFIES THAT NO REPRESENTATIVE, AGENT OR ATTORNEY OF THE LENDER HAS REPRESENTED, EXPRESSLY OR OTHERWISE, THAT THE LENDER WOULD NOT, IN THE EVENT OF LITIGATION, SEEK TO ENFORCE THE FOREGOING WAIVER. THIS WAIVER CONSTITUTES A MATERIAL**

**INDUCEMENT FOR THE LENDER TO ACCEPT THIS REVOLVING CREDIT NOTE AND MAKE THE LOANS EVIDENCED BY THIS REVOLVING CREDIT NOTE AND THE AGREEMENT.**

This Revolving Credit Note shall be the joint and several obligation of the Borrower and all sureties, guarantors and endorsers, and shall be binding upon them and their respective successors and assigns and each or any of them.

This Revolving Credit Note and the rights and obligations of the parties hereunder shall be construed and interpreted in accordance with the laws of The Commonwealth of Massachusetts (excluding the laws applicable to conflicts or choice of law).

This Revolving Credit Note, the Agreement and the Loan Documents are intended by the parties as the final, complete and exclusive statement of the transactions evidenced by this Revolving Credit Note. All prior or contemporaneous promises, agreements and understandings, whether oral or written, are deemed to be superceded by this Revolving Credit Note, the Agreement and the Loan Documents and no party is relying on any promise, agreement or understanding not set forth in this Revolving Credit Note, the Agreement and the Loan Documents. This Revolving Credit Note may not be amended or modified except by a written instrument describing such amendment or modification executed by the Borrower and the Lender.

No portion of the proceeds of this Revolving Credit Note shall be used, in whole or in part, for the purpose of purchasing or carrying any "margin stock" as such term is defined in Regulation U of the Board of Governors of the Federal Reserve System.

Upon receipt of an affidavit of an officer of the Lender as to the loss, theft, destruction or mutilation of this Revolving Credit Note or any other security document which is not of public record, and, in the case of any such loss, theft, destruction or mutilation, upon cancellation of this Revolving Credit Note or other security document, the Borrower will issue, in lieu thereof, a replacement Revolving Credit Note or other security document in the same principal amount thereof and otherwise of like tenor.

IN WITNESS WHEREOF, the Borrower has caused this Revolving Credit Note to be executed by its duly authorized officer as an instrument under seal as of the day and year first above written.

**WORLD ENERGY SOLUTIONS, INC.**

By: /s/ James Parslow

Name: James Parslow

Title: Chief Financial Officer and Treasurer

/s/

Witness

**TERM NOTE**

\$6,000,000.00

Worcester, Massachusetts  
December 30, 2013

**FOR VALUE RECEIVED**, the undersigned, **WORLD ENERGY SOLUTIONS, INC.**, a Delaware corporation with its principal place of business at 100 Front Street, 20th Floor, Worcester, Massachusetts 01608 (the "Borrower"), hereby promises to pay to

**COMMERCE BANK & TRUST COMPANY,**

a Massachusetts banking corporation (the "Lender"), OR ORDER, at its office at 386 Main Street, Worcester, Massachusetts 01608, or such other place as the Lender may from time to time specify in writing, the principal sum of

**SIX MILLION AND NO/100 DOLLARS (\$6,000,000.00)**

with interest on the unpaid principal until paid at the rate and in the manner hereinafter provided in lawful money of the United States of America in immediately available funds, without counterclaim or setoff and free and clear of, and without any deduction or withholding for, any taxes or other payments.

This Term Note is issued in conjunction with and secured as set forth in a Loan and Security Agreement dated as of even date herewith by and between the Borrower and the Bank (as may be amended from time to time, the "Agreement"), all the terms and conditions of which are incorporated herein by reference. No reference to the Agreement or to any provision thereof shall affect or impair the absolute and unconditional obligation of the Borrower to pay the principal of and interest on this Term Note as herein provided. An Event of Default under the Agreement or under any of the Loan Documents shall also constitute an Event of Default hereunder. The occurrence of an Event of Default shall constitute a default (beyond any applicable grace or cure periods) under each other obligation of the Borrower to the Bank. Capitalized terms used and not otherwise defined herein shall have the meanings ascribed to such terms in the Agreement.

Interest shall be calculated on the daily unpaid principal balance of the indebtedness evidenced by this Term Note computed on the basis of the actual number of days elapsed over a year assumed to have three hundred sixty (360) days, provided that interest shall be due for the actual number of days elapsed during each period for which interest is being charged.

The unpaid principal of this Term Note from time to time outstanding shall bear interest at the applicable rate per annum (the "Note Rate"), in accordance with the provisions of this Term Note, as follows:

(a) From the date of this Term Note through and including June 30, 2014, at a fluctuating rate per annum equal to the aggregate of (i) the Prime Rate plus (ii) two and three-quarters percent (2.75%); and

(b) Commencing July 1, 2014 through and including the Maturity Date hereinafter defined, at a fluctuating rate per annum equal to the aggregate of (i) the Prime Rate plus (ii) the Applicable Margin (calculated as set forth below).

The "Applicable Margin" shall mean that percentage determined by calculation of the Lender to be the ratio of Actual EBITDA to Projected EBITDA as of each semi-annual fiscal period commencing on the semi-annual period ending on June 30, 2014, as follows:

| <u>Ratio of Actual EBITDA to Projected EBITDA</u>               | <u>Applicable Margin -</u> |
|---|----------------------------|
| greater than 1.5 to 1.0   | 2.25%                      |
| equal to or greater than 1.25 to 1.0, but less than 1.50 to 1.0 | 2.50%                      |
| less than 1.25 to 1.0   | 2.75%                      |

Interest hereunder shall be payable monthly in arrears commencing one (1) month from the date of this Term Note and continuing to be due and payable on the same day of each succeeding month. Commencing seven (7) months from the date hereof and continuing on the same day of each succeeding month through the Maturity Date hereinafter defined, principal and interest at the Note Rate shall be payable in monthly amounts set forth on an amortization schedule prepared by the Lender to reflect any adjustment in the Note Rate and providing for repayment of the indebtedness due on this Term Note at the then current Note Rate over a sixty (60) month term commencing as of July 1, 2014.

Such monthly payments shall continue until the entire indebtedness evidenced by this Term Note is fully paid; provided, however, if not sooner paid, the entire indebtedness hereunder shall be due and payable five (5) years from the date hereof (the "Maturity Date") without notice or demand of any kind.

The Borrower shall have the privilege of prepaying all or any part of the unpaid principal balance of this Term Note at any time without premium.

If the entire amount of any required principal and/or interest is not paid in full within fifteen (15) days after the same is due, the Borrower shall pay to the Lender a late fee equal to five percent (5.00%) of the required payment. Such late charge payments are made for the purpose of compensating the Lender for its administrative, costs and expenses in handling late payments and losses in connection therewith. This provision is not intended to provide a grace period for any payment otherwise due and payable and shall not constitute a waiver by the Lender to insist upon the strict performance of any of the Borrower's covenants or agreements with, or obligations to, the Lender or to declare an Event of Default for any payment not made when it was due and payable.

All payments shall be applied first to the payment of all fees, expenses and other amounts due to the Lender (excluding principal and interest), then to accrued interest, and the balance on account of outstanding principal; provided, however, that during the continuance of an Event of Default, payments will be applied to the obligations of the Borrower to the Lender as the Lender shall determine in its sole discretion.

Upon the occurrence and during the continuance of an Event of Default (whether or not the Lender has accelerated payment of this Term Note), or after the Maturity Date or after judgment has been rendered on this Term Note, the unpaid principal of this Term Note, including interest, fees or costs which are not paid when due, will, at the option of the Lender, bear interest at a rate which is five percent (5.00%) per annum greater than the Note Rate (the "Default Rate"). This may result in compounding of interest. This will not constitute a waiver of any Event of Default.

At its option, and at any time, whether immediately or otherwise, upon the occurrence and during the continuance of an Event of Default, the Lender may declare this Term Note immediately due and payable without further action of any kind including notice, further demand or presentment.

The Borrower and any guarantor hereby grant to the Lender a continuing lien, security interest and right of setoff as security for all liabilities and obligations to the Lender, whether now existing or hereafter arising, upon and against all deposits, credits, collateral and property, now or hereafter in the possession, custody, safekeeping or control of the Lender or any entity under the control of the Lender and its successors and assigns, or in transit to any of them. At any time, without demand or notice (any such notice being expressly waived by the Borrower), the Lender may set off the same or any part thereof and apply the same to any liability or obligation of the Borrower and any guarantor even though unmatured and regardless of the adequacy of any other collateral securing this Term Note. ANY AND ALL RIGHTS TO REQUIRE THE LENDER TO EXERCISE ITS RIGHTS OR REMEDIES WITH RESPECT TO ANY OTHER COLLATERAL WHICH SECURES THIS TERM NOTE, PRIOR TO EXERCISING ITS RIGHT OF SETOFF WITH RESPECT TO SUCH DEPOSITS, CREDITS OR OTHER PROPERTY OF THE BORROWER AND ANY GUARANTOR, ARE HEREBY KNOWINGLY, VOLUNTARILY AND IRREVOCABLY WAIVED.

The Borrower shall pay on demand all reasonable expenses of the Lender in connection with the preparation, administration, default, collection, waiver or amendment of loan terms, or in connection with the Lender's exercise, preservation or enforcement of any of its rights, remedies or options hereunder, including, without limitation, reasonable fees of outside legal counsel or other similar professional fees or expenses, and any fees or expenses associated with travel or other costs relating to any appraisals or examinations conducted in connection with this Term Note or any collateral therefor, and the amount of all such expenses, if not paid within thirty (30) days, shall, until paid, bear interest at the rate applicable to principal hereunder (including any Default Rate) and be an obligation secured by any collateral.

The Borrower and each guarantor, endorser or other person now or hereafter liable for the payment of any of the indebtedness evidenced by this Term Note severally agree, by making, guaranteeing or endorsing this Term Note or by making any agreement to pay any of the indebtedness evidenced by this Term Note, to waive presentment for payment, protest and demand, notice of protest, demand and of dishonor and non-payment of this Term Note, and consent without notice or further assent (a) to the substitution, exchange, or release of the collateral securing this Term Note or any part thereof at any time; (b) to the acceptance by the holder or holders at any time of any additional collateral or security or other guarantors of this Term Note, (c) to the modification or amendment at any time, and from time to time, of this Term Note, the Agreement and any other instrument securing this Term Note, at the request of any person liable hereon; (d) to the granting by the holder hereof of any extension of the time for payment of this Term Note or for the performance of the agreements, covenants, and conditions contained in this Term Note, the Agreement or any instrument securing this Term Note, at the request of any other person liable hereon; and (e) to any and all forbearances and indulgences whatsoever; and such consent shall not alter or diminish the liability of any person.

This Term Note shall be governed by, and construed in accordance with, the laws of The Commonwealth of Massachusetts. The Borrower agrees that any suit for the enforcement of this Term Note may be brought in the courts of The Commonwealth of Massachusetts or any Federal Court sitting therein and consents to the non-exclusive jurisdiction of such court and to service of process in any such suit being made upon the Borrower by mail at the address specified herein. The Borrower hereby waives any objection that it may now or hereafter have to the venue of any such suit or any such court or that such suit was brought in an inconvenient court.

THE BORROWER AND THE LENDER (BY ACCEPTANCE OF THIS TERM NOTE) MUTUALLY HEREBY KNOWINGLY, VOLUNTARILY AND INTENTIONALLY WAIVE THE RIGHT TO A TRIAL BY JURY IN RESPECT OF ANY CLAIM BASED HEREON, ARISING OUT OF, UNDER OR IN CONNECTION WITH THIS TERM NOTE, THE AGREEMENT, THE LOAN DOCUMENTS OR ANY OTHER FINANCING INSTRUMENTS EXECUTED OR CONTEMPLATED TO BE EXECUTED IN CONNECTION HERewith OR WITH THE AGREEMENT OR ANY COURSE OF CONDUCT, COURSE OF DEALINGS, STATEMENTS (WHETHER VERBAL OR WRITTEN) OR ACTIONS OF ANY PARTY RELATED HERETO, INCLUDING, WITHOUT LIMITATION, ANY COURSE OF CONDUCT, COURSE OF DEALINGS, STATEMENTS OR ACTIONS OF THE LENDER RELATING TO THE ADMINISTRATION OF THE LOANS EVIDENCED BY THIS TERM NOTE OR ENFORCEMENT OF THE AGREEMENT, THE LOAN DOCUMENTS OR ANY SUCH FINANCING INSTRUMENTS, AND AGREE THAT NO PARTY WILL SEEK TO CONSOLIDATE ANY SUCH ACTION WITH ANY OTHER ACTION IN WHICH A JURY TRIAL CANNOT BE OR HAS NOT BEEN WAIVED. EXCEPT AS PROHIBITED BY LAW, THE BORROWER HEREBY WAIVES ANY RIGHT IT MAY HAVE TO CLAIM OR RECOVER IN ANY LITIGATION ANY SPECIAL, EXEMPLARY, PUNITIVE OR CONSEQUENTIAL DAMAGES OR ANY DAMAGES OTHER THAN, OR IN ADDITION

TO, ACTUAL DAMAGES. THE BORROWER CERTIFIES THAT NO REPRESENTATIVE, AGENT OR ATTORNEY OF THE LENDER HAS REPRESENTED, EXPRESSLY OR OTHERWISE, THAT THE LENDER WOULD NOT, IN THE EVENT OF LITIGATION, SEEK TO ENFORCE THE FOREGOING WAIVER. THIS WAIVER CONSTITUTES A MATERIAL INDUCEMENT FOR THE LENDER TO ACCEPT THIS TERM NOTE AND MAKE THE LOANS EVIDENCED BY THIS TERM NOTE AND THE AGREEMENT.

This Term Note shall be the joint and several obligation of the Borrower and all sureties, guarantors and endorsers, and shall be binding upon them and their respective successors and assigns and each or any of them.

This Term Note and the rights and obligations of the parties hereunder shall be construed and interpreted in accordance with the laws of The Commonwealth of Massachusetts (excluding the laws applicable to conflicts or choice of law).

This Term Note, the Agreement and the Loan Documents are intended by the parties as the final, complete and exclusive statement of the transactions evidenced by this Term Note. All prior or contemporaneous promises, agreements and understandings, whether oral or written, are deemed to be superceded by this Term Note, the Agreement and the Loan Documents and no party is relying on any promise, agreement or understanding not set forth in this Term Note, the Agreement and the Loan Documents. This Term Note may not be amended or modified except by a written instrument describing such amendment or modification executed by the Borrower and the Lender.

No portion of the proceeds of this Term Note shall be used, in whole or in part, for the purpose of purchasing or carrying any "margin stock" as such term is defined in Regulation U of the Board of Governors of the Federal Reserve System.

Upon receipt of an affidavit of an officer of the Lender as to the loss, theft, destruction or mutilation of this Term Note or any other security document which is not of public record, and, in the case of any such loss, theft, destruction or mutilation, upon cancellation of this Term Note or other security document, the Borrower will issue, in lieu thereof, a replacement Term Note or other security document in the same principal amount thereof and otherwise of like tenor.

IN WITNESS WHEREOF, the Borrower has caused this Term Note to be executed by its duly authorized officer as an instrument under seal as of the day and year first above written.

**WORLD ENERGY SOLUTIONS, INC.**

\_\_\_\_\_  
/s/  
Witness

By: \_\_\_\_\_  
Name: James Parslow  
Title: Chief Financial Officer and Treasurer

**SUBORDINATION AGREEMENT**

**Borrower: WORLD ENERGY SOLUTIONS, INC.**

100 Front Street, 20<sup>th</sup> Floor  
Worcester, Massachusetts 01608

**Creditor: MASSACHUSETTS CAPITAL RESOURCE COMPANY**

420 Boylston Street  
Boston, Massachusetts 02116

**Lender: COMMERCE BANK & TRUST COMPANY**

386 Main Street  
Worcester, Massachusetts 01608

**THIS SUBORDINATION AGREEMENT** is entered into among **WORLD ENERGY SOLUTIONS, INC.**, a Delaware corporation, ("**Borrower**"), whose address is 446 Main Street, Worcester, Massachusetts 01608; Commerce Bank & Trust Company ("**Lender**"), a Massachusetts banking corporation whose address is 386 Main Street, Worcester, Massachusetts 01608; and Massachusetts Capital Resource Company ("**Creditor**"), whose address is 420 Boylston Street, Boston, Massachusetts 02116. As of the date of this Agreement, Borrower is or will be indebted to Creditor and Lender. Borrower and Creditor each want Lender to provide financial accommodations to Borrower in the form of (a) new credit or loan advances, (b) an extension of time to pay or other compromises regarding all or part of Borrower's present indebtedness to Lender, or (c) other benefits to Borrower. Borrower and Creditor each represent and acknowledge to Lender that Creditor will benefit as a result of these financial accommodations from Lender to Borrower, and Creditor acknowledge receipt of valuable consideration for entering into this Agreement. Based on the representations and acknowledgments contained in this Agreement, Creditor and Borrower agree with Lender as follows:

**1. Definitions.** The following words shall have the following meanings when used in this Agreement. Terms not otherwise defined in this Agreement shall have the meanings attributed to such terms in the Uniform Commercial Code. All references to dollar amounts shall mean amounts in lawful money of the United States of America.

**Agreement.** The word "**Agreement**" means this Subordination Agreement together with all exhibits and schedules attached to this Subordination Agreement from time to time, if any, and as amended from time to time.

**Borrower.** The word "**Borrower**" means World Energy Solutions, Inc.

**Creditor.** The word "**Creditor**" means Massachusetts Capital Resource Company.

**Lender.** The word "**Lender**" means Commerce Bank & Trust Company.



**Security Interest.** The words "**Security Interest**" mean and include without limitation any type of collateral security, whether in the form of a lien, charge, mortgage, deed of trust, assignment, pledge, chattel mortgage, chattel trust, factor's lien, equipment trust, conditional sale, trust receipt, lien or title retention contract, lease or consignment intended as a security device, or any other security or lien interest whatsoever, whether created by law, contract or otherwise.

**Subordinated Indebtedness.** The words "**Subordinated Indebtedness**" mean and include without limitation all present and future indebtedness, obligations, liabilities, claims, rights and demands of any kind which may be now or hereafter owing from Borrower to Creditor. The term "Subordinated Indebtedness" is used in its broadest sense and includes without limitation all principal, all interest, all costs and attorneys' fees, all sums paid for the purpose of protecting the rights of a holder of security (such as a secured party paying for insurance on collateral if the owner fails to do so), all contingent obligations of Borrower (such as a guaranty), and all other obligations, secured or unsecured, of any nature whatsoever.

**Superior Indebtedness.** The words "**Superior Indebtedness**" mean and include without limitation all present and future indebtedness, obligations, liabilities, claims, rights and demands of any kind which may be now or hereafter owing from Borrower to Lender. The term "Superior Indebtedness" is used in its broadest sense and includes without limitation all principal, all interest, all obligations under letters of credit issued by the Lender for the benefit of the Borrower, all costs and attorneys' fees, all sums paid for the purpose of protecting Lender's rights in security (such as paying for insurance on collateral if the owner fails to do so), all contingent obligations of Borrower (such as a guaranty), all obligations arising by reason of Borrower's accounts with Lender (such as an overdraft on a checking account), and all others obligations of Borrower to Lender, secured or unsecured, of any nature whatsoever.

**2. Subordination.** All Subordinated Indebtedness of Borrower to Creditor is and shall be subordinated in all respects to all Superior Indebtedness of Borrower to Lender as provided for in this Agreement. If the Creditor holds one or more Security Interests, whether now existing or hereafter acquired, in any of Borrower's real property or personal property, the Creditor also subordinates all its Security Interests to all such Security Interests held by Lender, whether the Lender's Security Interest or interests exist now or are acquired later.

**3. Payments to Creditor.** Except as provided below, Borrower will not make and Creditor will not accept, at any time while any Superior Indebtedness is owing to Lender or Lender has a commitment with Borrower to advance any Superior Indebtedness, (a) any payment upon any Subordinated Indebtedness, (b) any advance, transfer or assignment of assets to Creditor in any form whatsoever that would reduce at any time or in any way the amount of Subordinated Indebtedness, or (c) any transfer of any assets as security for the Subordinated Indebtedness, in each case except upon Lender's prior written consent. Notwithstanding the foregoing, Borrower may make regularly scheduled payments of interest and principal to Creditor as long as Borrower is not prohibited from doing so pursuant to Section 1.09(b) of that certain Note Purchase Agreement, dated as of October 3, 2012, between Borrower and Creditor.

In the event of any distribution, division or application, whether partial or complete, voluntary or involuntary, by operation of law or otherwise, of all or any part of Borrower's assets, or the

proceeds of Borrower's assets, in whatever form, to Creditor of Borrower or upon any indebtedness of Borrower, whether by reason of liquidation, dissolution or other winding-up of Borrower, or by reason of any execution sale, receivership, insolvency, or bankruptcy proceeding, assignment for the benefit of Creditor, proceedings for reorganization, or readjustment of Borrower or Borrower's properties, then and in such event, (a) the Superior Indebtedness shall be paid in full before any payment is made upon the Subordinated Indebtedness, and (b) all payments and distributions, of any kind or character and whether in cash, property, or securities, which shall be payable or deliverable upon or in respect of the Subordinated Indebtedness shall be paid or delivered directly to Lender for application in payment of the amounts then due on the Superior Indebtedness until the Superior Indebtedness shall have been paid in full. For purposes of this Agreement, "payment in full" of the Superior Indebtedness shall mean payment in full in cash or cash equivalents.

In order that Lender may establish its right to prove claims and recover for its own account dividends based on the Subordinated Indebtedness, the Creditor does hereby assign all its right, title and interest in such claims to Lender. The Creditor further agrees to supply such information and evidence, provide access to and copies of such of Creditor's records as may pertain to the Subordinated Indebtedness. For such purposes, the Creditor hereby irrevocably authorize Lender in its discretion to make and present for or on behalf of the Creditor such proofs of claims on account of the Subordinated Indebtedness as Lender may deem expedient and proper and to receive and collect any and all dividends, payments or other disbursements made thereon in whatever form the same may be paid or issued and to apply the same on account of the Superior Indebtedness.

Should any payment, distribution, security, or proceeds thereof be received by the Creditor at any time on the Subordinated Indebtedness contrary to the terms of this Agreement, the Creditor immediately will deliver the same to Lender in precisely the form received (except for the endorsement or assignment of the Creditor where necessary), for application on or to secure the Superior Indebtedness, whether it is due or not due, and until so delivered the same shall be held in trust by the Creditor as property of Lender. In the event the Creditor fails to make any such endorsements or assignment, Lender, or any of its officers on behalf of Lender, is hereby irrevocably authorized by the Creditor to make the same.

**4. Creditor's Notes.** The Creditor agrees not to sell, assign, pledge or otherwise transfer, in whole or in part, any of its Subordinated Notes or any other document or instrument evidencing its Subordinated Indebtedness, or any interest therein, to any other person or entity unless such transferee expressly acknowledges to the Lender in writing the subordination provided for herein and agrees to be bound by all of the terms hereof.

**5. Creditor's Representations and Warranties.** The Creditor represents and warrants to Lender that:

(a) no representations or agreements of any kind have been made to the Creditor which would limit or qualify in any way the terms of this Agreement;

(b) this Agreement is executed at Borrower's request and not at the request of Lender;

(c) Lender has made no representation to the Creditor as to the creditworthiness of Borrower; and

(d) The Creditor has established adequate means of obtaining from Borrower on a continuing basis information regarding Borrower's financial condition. The Creditor agrees to keep adequately informed from such means of any facts, events, or circumstances which might in any way affect the Creditor's risks under this Agreement and the Creditor further agrees that Lender shall have no obligation to disclose to the Creditor information or material acquired by Lender in the course of its relationship with Borrower.

**6. Creditor's Waivers.** The Creditor waives any right to require Lender:

(a) to make, extend, renew, or modify any loan to Borrower or to grant any other financial accommodations to Borrower whatsoever;

(b) to make any presentment, protest, demand, or notice of any kind, including notice of any nonpayment of the Superior Indebtedness or of any nonpayment related to any Security Interests, or notice of any action or nonaction on the part of Borrower, Lender, any surety, endorser, or other guarantor in connection with the Superior Indebtedness, or in connection with the creation of new or additional Superior Indebtedness;

(c) to resort for payment or to proceed directly or at once against any person, including Borrower;

(d) to proceed directly against or exhaust any Security Interests held by Lender from Borrower, any other guarantor, or any other person;

(e) to give notice of the terms, time, and place of any public or private sale of personal property security held by Lender from Borrower or to comply with any other applicable provisions of the Uniform Commercial Code;

(f) to pursue any other remedy within Lender's power; or

(g) to commit any act or omission of any kind, at any time, with respect to any matter whatsoever.

**7. Lender's Rights.** Lender may take or omit any and all actions with respect to the Superior Indebtedness or any Security Interests for the Superior Indebtedness without affecting whatsoever any of Lender's rights under this Agreement. In particular, without limitation, Lender may, without notice of any kind to Creditor:

(a) make one or more additional secured or unsecured loans to Borrower;

(b) repeatedly alter, compromise, renew, extend, accelerate, or otherwise change the time for payment or other terms of the Superior Indebtedness or any part thereof, including increases and decreases of the rate of interest on the Superior Indebtedness; extensions may be repeated and may be for longer than the original loan term;

(c) take and hold Security Interests for the payment of the Superior Indebtedness, and exchange, enforce, waive, and release any such Security Interests, with or without the substitution of new collateral;

(d) release, substitute, agree not to sue, or deal with any one or more of Borrower's sureties, endorsers, or guarantors on any terms or manner Lender chooses;

(e) determine how, when and what application of payments and credits shall be made on the Superior Indebtedness;

(f) apply such security and direct the order or manner of sale thereof, as Lender in its discretion may determine; and

(g) assign this Agreement in whole or in part.

**8. Default by Borrower**. If Borrower becomes insolvent or bankrupt, this Agreement shall remain in full force and effect. In the event of a corporate reorganization or corporate arrangement of Borrower under the provisions of the Bankruptcy Code, as amended, this Agreement shall remain in full force and effect and the court having jurisdiction over the reorganization or arrangement is hereby authorized to preserve such priority and subordination in approving any such plan of reorganization or arrangement. Any payment default under the terms of the Subordinated Indebtedness or any other event of default which could result in an acceleration of the Subordinated Indebtedness also shall be a default under the terms of the Superior Indebtedness to Lender.

**9. Duration and Termination**. This Agreement will take effect when received by Lender, without the necessity of any acceptance by Lender, in writing or otherwise, and will remain in full force and effect until Creditor shall notify Lender in writing by facsimile transmission (with confirmation of complete delivery), reputable overnight courier or by first-class mail, postage prepaid, at the address shown above (or such other address as Lender shall notify Creditor of by the same method) to the contrary, which notice shall be effective upon receipt by Lender. Any such notice shall not affect the Superior Indebtedness owed Lender by Borrower at the time of such notice, nor shall such notice affect Superior Indebtedness thereafter granted in compliance with a commitment made by Lender to Borrower prior to receipt of such notice, nor shall such notice affect any renewals or substitutions for any of the foregoing. Such notice shall affect only indebtedness of Borrower to Lender arising after receipt of such notice and not arising from financial assistance granted by Lender to Borrower in compliance with Lender's obligations under a commitment.

**10. Miscellaneous Provisions**. The following miscellaneous provisions are a part of this Agreement:

No provision contained in this Agreement shall be construed:

(a) as requiring Lender to grant to Borrower or to Creditor any financial assistance or other accommodations, or

(b) as limiting or precluding Lender from the exercise of Lender's own judgment and discretion about amounts and times of payment in making loans or extending accommodations to Borrower including, without limitation, the exercise of Lender's judgment and discretion as to whether or not to permit Borrower to incur additional Subordinated Indebtedness.

**Amendments.** This Agreement constitutes the entire understanding and agreement of the parties as to the matters set forth in this Agreement. No alteration of or amendment to this Agreement shall be effective unless made in writing and signed by Lender, Borrower, and Creditor.

**Attorneys' Fees; Expenses.** Borrower agrees to pay upon demand all of Lender's costs and expenses, including attorneys' fees and legal expenses, incurred in connection with enforcement of this Agreement. Lender may pay someone else to help enforce this Agreement, and Borrower shall pay the costs and expenses of such enforcement. Costs and expenses include Lender's attorneys' fees and legal expenses whether or not there is a lawsuit, including attorneys' fees and legal expenses for bankruptcy proceedings (and including efforts to modify or vacate any automatic stay or injunction), appeals, and any anticipated post-judgment collection services. Borrower also shall pay all court costs and such additional fees as may be directed by the court.

**Successors.** This Agreement shall extend to and bind the respective successors and assigns of the parties to this Agreement, and the covenants of Borrower and Creditor respecting subordination of the Subordinated Indebtedness in favor of Lender shall extend to, include, and be enforceable by any transferee or endorsee to whom Lender may transfer any or all of the Superior Indebtedness.

**Counterparts.** This Agreement may be executed in any number of counterparts, all of which together shall constitute one and the same instruments, and each of the parties hereby may execute this Agreement by signing any such counterpart.

**Waiver.** Lender shall not be deemed to have waived any rights under this Agreement unless such waiver is given in writing and signed by Lender. No delay or omission on the part of Lender in exercising any right shall operate as a waiver of such right or any other right. A waiver by Lender of a provision of this Agreement shall not prejudice or constitute a waiver of Lender's right otherwise to demand strict compliance with that provision or any other provision of this Agreement. No prior waiver by Lender, nor any course of dealing between Lender and Creditor, shall constitute a waiver of any of Lender's rights or of the Creditor's obligations as to any further transactions. Whenever the consent of Lender is required under this Agreement, the granting of such consent by Lender in any instance shall not constitute continuing consent to subsequent instances where such consent is required and in all cases such consent may be granted or withheld in the sole discretion of Lender.

**BORROWER AND CREDITOR ACKNOWLEDGE HAVING READ ALL OF THE PROVISIONS OF THIS SUBORDINATION AGREEMENT, AND BORROWER AND CREDITOR AGREE TO ITS TERMS. THIS AGREEMENT IS DATED AS OF DECEMBER 30, 2013. THIS AGREEMENT IS EXECUTED UNDER SEAL.**

**BORROWER:**

**WORLD ENERGY SOLUTIONS, INC.**

By: /s/ James Parslow  
James Parslow, Chief Financial Officer and Treasurer

**CREDITOR:**

**MASSACHUSETTS CAPITAL RESOURCE COMPANY**

By: /s/ Paul Bolger  
Paul Bolger, President

**LENDER:**

**COMMERCE BANK & TRUST COMPANY**

By: /s/ Thomas Moschos  
Thomas Moschos, Commercial Loan Officer

# WorldEnergy

**For Immediate Release**

## **World Energy Solutions Enters into New Strategic Banking Relationship with Commerce Bank**

### ***Signs New Term Loan and Line-of-Credit Agreement at Favorable Terms***

**WORCESTER, MA – January 6, 2014** – World Energy Solutions, Inc. (NASDAQ: XWES), a leading energy management services firm, today announced it has established a new strategic banking relationship with Commerce Bank, a Worcester-based financial institution.

Under a new \$8.5 million credit facility, World Energy has entered into a \$6 million, 60-month term loan and \$2.5 million line-of-credit effective December 30, 2013. This facility replaces the Company's prior \$9 million facility with Silicon Valley Bank (SVB). The new term loan bears interest at 6% (prime + 2.75%) and is interest only for the first six months. The line-of-credit bears interest at 5% (prime + 1.75%) and is a three-year committed facility. The rates for both the new term loan and line-of-credit can be further reduced by up to 0.5% if certain EBITDA performance criteria are met on a six-month rolling average.

"We are pleased to be entering into a strategic banking relationship with Commerce Bank, a well-regarded local institution," said Jim Parslow, Chief Financial Officer of World Energy Solutions. "Our line-of-credit was up for renewal in early 2014, and we took the opportunity to talk with several banks that expressed interest in our business. Commerce Bank came through with a very competitive offer, giving us substantially better terms, expanding our financial flexibility and reducing our interest rate on the term note by 1.75%."

Added Phil Adams, CEO: "World Energy is proud to be a Worcester company. We were founded here and have deepened our commitment to the City and region over the last decade by reliably serving its businesses and institutions, hiring locally, dedicating our charitable efforts to area causes, and signing a 10-year lease for our 100 Front Street headquarters. Teaming with Commerce Bank, a local institution that has been a fixture of the Worcester landscape since 1955, is a great move for us, and we are looking forward to working with them as we continue to execute our growth strategy."

### **About Commerce Bank**

Commerce Bank is a full-service, FDIC-insured, state-chartered financial institution. Founded in 1955 and headquartered in Worcester, Massachusetts, the Bank offers a comprehensive array of innovative financial solutions including commercial and consumer loans as well as deposit, savings and retirement accounts. These services are available through the Bank's 16 convenient offices located throughout Central Massachusetts and in Boston. As of December 31, 2012, Commerce Bank had \$1.7 billion in assets. For more information, visit [www.BankAtCommerce.com](http://www.BankAtCommerce.com).

---

## About World Energy Solutions, Inc.

World Energy Solutions, Inc. (NASDAQ: XWES) is an energy management services firm that brings together the passion, processes and technologies to take the complexity out of energy management and turn it into bottom-line impact for the businesses, institutions and governments we serve. To date, the Company has transacted more than \$40 billion in energy, demand response and environmental commodities on behalf of its customers, creating more than \$2 billion in value for them. World Energy is also a leader in the global carbon market, where its World Energy Exchange® supports the Regional Greenhouse Gas Initiative (RGGI), the first mandatory market-based regulatory program in the U.S. to reduce greenhouse gas emissions. For more information, please visit [www.worldenergy.com](http://www.worldenergy.com).

*This press release contains forward-looking statements. The words "anticipates," "believes," "estimates," "expects," "intends," "may," "plans," "projects," "will," "would" and similar expressions are intended to identify forward-looking statements, although not all forward-looking statements contain these identifying words. The Company has based these forward-looking statements on its current expectations and projections about future events, including without limitation, its expectations of backlog and energy prices. Although the Company believes that the expectations underlying any of its forward-looking statements are reasonable, these expectations may prove to be incorrect and all of these statements are subject to risks and uncertainties. Should one or more of these risks and uncertainties materialize, or should underlying assumptions, projections or expectations prove incorrect, actual results, performance or financial condition may vary materially and adversely from those anticipated, estimated or expected. Such risks and uncertainties include, but are not limited to the following: the Company's revenue and backlog are dependent on actual future energy purchases pursuant to completed procurements; the demand for the Company's services is affected by changes in regulated prices or cyclical volatility in competitive market prices for energy; the potential impact on the Company's historical and prospective financial results of a change in accounting policy may negatively impact its stock price; and other factors outside the Company's control that affect transaction volume in the electricity market. Additional risk factors are identified in the Company's Annual Report on Form 10-K for the year ended December 31, 2012 and subsequent reports filed with the Securities and Exchange Commission. The forward-looking statements made in this press release are made as at the date hereof. The Company undertakes no obligation to update any forward-looking statement to reflect events or circumstances after the date on which the statement is made or to reflect the occurrence of unanticipated events, other than as required by securities laws.*

For additional information, contact:

Jim Parslow  
World Energy Solutions  
508-459-8100  
[jparslow@worldenergy.com](mailto:jparslow@worldenergy.com)

Dan Mees  
World Energy Solutions  
508-459-8156  
[dmees@worldenergy.com](mailto:dmees@worldenergy.com)



# WORLD ENERGY SOLUTIONS, INC.

## FORM 8-K (Current report filing)

Filed 10/04/12 for the Period Ending 10/03/12

|             |  |
|-------------|--|
| Address     | 446 MAIN STREET<br>WORCESTER, MA 01608             |
| Telephone   | 508-459-8100                                       |
| CIK         | 0001371781   |
| Symbol      | XWES   |
| SIC Code    | 7389 - Business Services, Not Elsewhere Classified |
| Industry    | Investment Services                                |
| Sector      | Financial  |
| Fiscal Year | 12/31  |

---

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

---

**FORM 8-K**

---

**CURRENT REPORT**

---

Pursuant to Section 13 or 15(d) of the  
Securities Exchange Act of 1934

Date of Report (Date of earliest event reported): October 3, 2012

---

**World Energy Solutions, Inc.**

(Exact name of registrant as specified in its charter)

---

**Delaware**  
(State or other Jurisdiction  
of Incorporation)

**001-34289**  
(Commission  
File Number)

**04-3474959**  
(IRS Employer  
Identification No.)

**100 Front Street**  
**Worcester, Massachusetts**  
(Address of Principal Executive Offices)

**01608**  
(Zip Code)

Registrant's telephone number, including area code: (508) 459-8100

**N/A**  
(Former name or former address if changed since last report.)

---

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions:

- ☐ Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)
  - ☐ Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)
  - ☐ Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))
  - ☐ Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))
-

---

**Item 1.01. Entry into a Material Definitive Agreement.**

On October 3, 2012, World Energy Solutions, Inc. (the "Company") acquired substantially all of the assets and certain obligations of Northeast Energy Partners, LLC ("NEP") pursuant to an Asset Purchase Agreement (the "Asset Purchase Agreement") between the Company, NEP, and its members. NEP is a Connecticut based energy management and procurement company. The purchase price is approximately \$7.9 million in cash and a \$2.0 million Promissory Note with NEP (the "NEP Note"). The NEP Note bears interest at 4% with \$1.5 million of principal plus interest due on October 1, 2013 and the remaining \$500,000 of principal plus interest due April 1, 2014. NEP may also earn up to an additional \$3,180,000 in cash and shares, with up to \$2.5 million in cash, and 153,153 in shares based on achieving certain 12-month revenue and earnings before interest, taxes, depreciation and amortization (EBITDA) targets, as defined. The NEP Note is unsecured and subordinated to financing with Silicon Valley Bank ("SVB"). A press release describing the acquisition is attached as Exhibit 99.1.

On October 3, 2012, the Company, together with its wholly-owned subsidiary, World Energy Securities Corp., entered into a Fourth Loan Modification Agreement (the "Fourth Modification Agreement") with SVB, which modifies a Loan and Security Agreement between the Company and SVB dated September 8, 2008. SVB has increased the Company's borrowing capability to \$9 million, including a \$6.5 million term loan (the "Term Loan"), bearing interest at prime plus 2.75% (currently 6%), that replaces the Company's prior \$2.5 million term loan. The Term Loan is interest only for the first three months followed by 39 equal principal payments commencing on January 1, 2013. In addition, the Company will continue to maintain a \$2.5 million line of credit with SVB, which has been extended to March 14, 2014. No borrowings have been made under the line-of-credit to date. Terms of the loan modification are substantially the same as under the previous facility.

On October 3, 2012, the Company entered into a Note Purchase Agreement with Massachusetts Capital Resource Company ("MCRC"), in which the Company entered into an 8-year, \$4 million Subordinated Note due 2020 with MCRC (the "MCRC Note"). The MCRC Note bears interest at 10.5% and is interest only for the first four years followed by 48 equal principal payments commencing October 31, 2016. The Company must pay a premium of 5% of the total principal outstanding if it prepays the MCRC Note before October 1, 2013, a 3% premium if it prepays the MCRC Note before October 1, 2014, and a 1% premium if it prepays the MCRC Note before October 1, 2015.

The foregoing description of the Asset Purchase Agreement, the NEP Note, the Subordination Agreement, the Fourth Loan Modification Agreement, the Note Purchase Agreement and the MCRC Note does not purport to be complete and is qualified in its entirety by reference to the full text of such documents attached to this Form 8-K as Exhibits 2.1, 4.1, 10.3, 10.1, 10.2 and 4.3 respectively, and incorporated herein by reference.

---

**Item 2.01. Completion of Acquisition or Disposition of Assets**

The Company refers to Item 1.01 above, "Entry into a Material Definitive Agreement," and incorporates the contents of that section herein, as if fully set forth under this Section 2.01.

**Item 2.03. Creation of a Direct Financial Obligation or an Obligation under an Off-Balance Sheet Arrangement of a Registrant.**

The Company's discussion under Item 1.01 of this Current Report is hereby incorporated by this reference.

**Item 3.02. Unregistered Sales of Equity Securities**

The Company refers to Item 1.01 above, "Entry into a Material Definitive Agreement," and incorporates the contents of that section herein, as if fully set forth under this Section 3.02. Pursuant to the Asset Purchase Agreement, NEP may be paid an earn-out which includes up to 153,153 in shares, which, if earned in full, would equal less than 1% of the current issued and outstanding shares of common stock of the Company.

Pursuant to the Fourth Loan Modification with SVB, the Company granted to SVB a 7-year Warrant for the purchase of 45,045 shares of common stock of the Company, with a conversion price of \$4.44 per share (the "Warrant"), which, if converted immediately would equal approximately 1% of the current issued and outstanding shares of common stock of the Company.

The issuances of the equity securities described herein was exempt from registration pursuant to the exemption contained in Section 4(2) of the Securities Act of 1933, as amended, and Rule 506 of Regulation D, inasmuch as it was not a public offering since no general solicitation or advertising of any kind was used in connection with the issuances and there was only limited accredited investors.

The foregoing description of the Asset Purchase Agreement and the Warrant do not purport to be complete and is qualified in its entirety by reference to the full text of such documents attached to this Form 8-K as Exhibits 2.1 and 4.1 respectively, and incorporated herein by reference.

**Item 9.01. Financial Statements and Exhibits.****(a) Financial Statements of Business Acquired.**

The financial statements required to be filed by Item 9.01(a) of Form 8-K will be filed by amendment no later than 71 calendar days after the date this Current Report on Form 8-K is required to be filed.

---

**(b) Financial Statements of Business Acquired.**

The financial statements required to be filed by Item 9.01(b) of Form 8-K will be filed by amendment no later than 71 calendar days after the date this Current Report on Form 8-K is required to be filed.

**(d) Exhibits**

See Exhibit Index attached hereto.

---

**SIGNATURE**

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

WORLD ENERGY SOLUTIONS, INC.

Date: October 4, 2012

By: /s/ James Parslow  
Chief Financial Officer

---

## EXHIBIT INDEX

| <u>Exhibit</u> | <u>Description</u>  |
|----------------|---|
| 2.1            | Asset Purchase Agreement by and among World Energy Solutions, Inc., Northeast Energy Partners, LLC, and its Members dated October 3, 2012 |
| 4.1            | Promissory Note dated October 3, 2012 by World Energy Solutions, Inc. for the benefit of Northeast Energy Partners, LLC                   |
| 4.2            | Warrant to Purchase Stock between World Energy Solutions, Inc. and Silicon Valley Bank  |
| 4.3            | Subordinated Note Due 2020 by World Energy Solutions, Inc. for the benefit of Massachusetts Capital Resource Company                      |
| 10.1           | Fourth Loan Modification Agreement, dated October 3, 2012 to Loan and Security Agreement with Silicon Valley Bank                         |
| 10.2           | Note Purchase Agreement dated October 3, 2012 between World Energy Solutions, Inc. and Massachusetts Capital Resource Company             |
| 10.3           | Subordination Agreement with Northeast Energy Partners, LLC and Silicon Valley Bank dated October 3, 2012                                 |
| 99.1           | Press Release dated October 4, 2012   |

**ASSET PURCHASE AGREEMENT**

**Dated October 3, 2012**

**by and between**

**World Energy Solutions, Inc.**

**and**

***Northeast Energy Partners, LLC and its Members***



## ASSET PURCHASE AGREEMENT

This Asset Purchase Agreement ("Agreement") is entered into as of October 3, 2012 by and among World Energy Solutions, Inc., a Delaware corporation (the "Buyer"), and Northeast Energy Partners, LLC, a Connecticut limited liability company (the "Seller") and John Hardy, Thomas Lockwood and Lora Monroe, being all of the members of the Seller (the "Members"), jointly and only with respect to certain sections of this Agreement. This Agreement contemplates a transaction in which the Buyer will purchase substantially all of the assets and assume none of the liabilities of Seller except as described in this Agreement.

Capitalized terms used in this Agreement and not otherwise defined herein shall have the meanings ascribed to them in Article VIII.

In consideration of the representations, warranties and covenants herein contained, the Parties agree as follows.

### ARTICLE I

#### THE ASSET PURCHASE

##### 1.1 Purchase and Sale of Assets.

(a) Upon and subject to the terms and conditions of this Agreement, the Buyer agrees to purchase from the Seller, and the Seller agrees to sell, transfer, convey, assign and deliver to the Buyer, for the consideration specified below in this Article I, all right, title and interest in, to and under the Acquired Assets.

(b) Notwithstanding the provisions of Section 1.1(a), the Acquired Assets shall not include the Excluded Assets.

##### 1.2 Assumption of Liabilities.

(a) Upon and subject to the terms and conditions of this Agreement, the Buyer shall assume and become responsible for, from and after the date hereof, only the Assumed Liabilities.

(b) Notwithstanding the terms of Section 1.2(a) or any other provision of this Agreement to the contrary, the Buyer shall not assume or become responsible for, and the Seller shall remain liable for, the Retained Liabilities.

1.3 Purchase Price. The Purchase Price to be paid by the Buyer in accordance with Section 1.4 for the Acquired Assets shall be up to \$13,090,959 and shall consist of:

(a) \$7,910,959 in cash (the "Cash Portion") in accordance with Section 1.5(b) below;

(b) \$2,000,000 shall be paid by a promissory note of the Buyer in the form attached here to as Exhibit A ("Seller Note"); and

(c) up to an additional \$3,180,000 in cash and Shares (the "Earnout") will be paid to Seller in accordance with the terms of Section 1.7 below.

1.4 Left Intentionally Blank.

1.5 The Closing.

(a) The Closing shall take place remotely upon the execution and delivery of this Agreement by all of the parties hereto. All transactions at the Closing shall be deemed to take place simultaneously, and no transaction shall be deemed to have been completed and no documents or certificates shall be deemed to have been delivered until all other transactions are completed and all other documents and certificates are delivered.

(b) At the Closing:

(i) the Seller shall execute and deliver to the Buyer a bill of sale in substantially the form attached hereto as Exhibit B (the "Bill of Sale") in order to effect the sale, transfer, conveyance and assignment to the Buyer of valid ownership of the Acquired Assets;

(ii) each of Buyer and Seller shall execute and deliver to the other Party an instrument of assignment and assumption agreement in substantially the form attached hereto as Exhibit C with respect to all Assigned Contracts in order to effect the assumption by the Buyer of the Assumed Liabilities arising out of any Assigned Contracts (the "Assignment and Assumption Agreement");

(iii) the Buyer shall pay to the Seller, payable by wire transfer or other delivery of immediately available funds to an account designated by the Seller the Cash Portion;

(iv) the Seller shall deliver to the Buyer the \$2,000,000 Seller Note.

(vi) the Seller shall deliver to the Buyer the various certificates, instruments and documents referred to in Section 4.1 and/or as otherwise provided for in this Agreement;

(vii) the Buyer shall deliver to the Seller the various certificates, instruments and documents referred to in Section 4.2 and/or as otherwise provided for in this Agreement;

(viii) the Buyer and the Seller shall execute and deliver to each other a cross-receipt evidencing the transactions referred to above and each shall execute such other documents required by this Agreement including, without limitation, such instruments required to assign Seller's interest in the Acquired Assets to Buyer.

1.6 Allocation. The Buyer and the Seller agree to allocate the Purchase Price (and all other capitalizable costs) among the Acquired Assets and the non-solicitation and non-competition covenants set forth in Sections 5.2 and 5.3 for all purposes (including financial accounting and tax purposes) in accordance with the allocation schedule attached hereto as

Schedule 1.6. Buyer and Seller agree to use the allocations determined pursuant to this Section 1.6 for all tax purposes, including without limitation, those matters subject to Section 1060 of the Code, and the Treasury regulations promulgated thereunder. Buyer and Seller shall prepare and submit to the other for review their IRS Forms 8594 within ninety (90) days after the Closing. Each party shall have thirty (30) days to complete its review.

1.7 Earnout. The Earnout will be paid to Seller by Buyer based on the following:

| <u>Achievement of EBITDA Target</u>                           | <u>Earnout Paid in Cash</u> | <u>Earnout Paid in Shares</u> |
|---|-----------------------------|-------------------------------|
| \$0 to \$1,999,999  | \$ 0                        | \$ 0                          |
| \$2,000,000 to \$2,149,999                                    | \$ 625,000                  | \$ 170,000                    |
| <del>\$2,150,000 to \$2,299,999</del>                         | <del>\$ 625,000</del>       | <del>\$ 170,000</del>         |
| \$2,300,000 to 2,449,999                                      | \$ 625,000                  | \$ 170,000                    |
| <del>\$2,450,000+</del>                                       | <del>\$ 125,000</del>       | <del>\$ 45,000</del>          |
| \$2,450,000+ AND Achievement of Revenue Target of \$5,200,00+ | \$ 500,000                  | \$ 125,000                    |

Each tier of the Earnout is cumulative. By way of example, if Seller achieves an EBITDA Target of \$2,301,000, the Earnout payment shall be \$1,875,000 in cash and \$510,000 in Shares.

The measurement period for the determination of achievement of the EBITDA Target and for the Revenue Target in the last tier above for the purpose of determining any Earnout payment shall be from October 1, 2012 through and including September 30, 2013 (the "Earnout Period"), and the Earnout payment shall be made on or before December 31, 2013.

The number of Shares shall be determined by the dollar amount of the Earnout payable in Shares divided by the Conversion Price. The Conversion Price shall be the greater of (1) the NASDAQ Price; or (2) the volume weighted average price of XWES common stock on the NASDAQ Capital Market for the ten (10) consecutive trading days immediately preceding the Closing Date; provided that in no event shall the Conversion Price be less than \$1.00.

Payment of the Earnout shall be subject to the Buyer's setoff rights under Section 6.5(b) of this Agreement.

For purposes of this Section 1.7:

(a) Russ Monroe ("Monroe"), as the former president of the Seller and in his capacity as an employee of the Buyer, will continue to maintain books and records to measure EBITDA of the Seller's ongoing business during the Earnout Period and will provide Buyer with an EBITDA calculation within thirty (30) days of each quarter end.

It is the intention of the Parties that EBITDA will be calculated consistent with the historical financial results of the Seller and will include all normal and customary charges

associated with running the business. The Parties agree that revenue will be measured on a cash receipt basis from October 1, 2012 through September 30, 2013 consistent with how the Seller has historically accounted for revenue. Expenses will be recorded on a cash basis consistent with how the Seller has historically recorded such expenses. However, the Parties agree that certain items that are costs during the Earnout Period but not paid until after the Earnout Period will be reflected as part of the Earnout calculation. Monroe will not exclude certain incurred expenses by holding off payment to the respective vendor and/or employee. For example, Buyer intends to continue the Seller's commission plan through December 31, 2013. Bonuses may not be paid until December 31, 2013. As a result, Monroe's calculation of expenses will include an accrual of the respective bonus amount attributable for the Earnout Period. It is the intention of the Parties that EBITDA will reflect twelve (12) months of revenue and twelve (12) months of expenses attributable to the Seller's ongoing business. To the extent certain costs change (e.g. compensation, commission, bonus, benefits) as result of Buyer's acquisition of Seller's assets, such costs shall be properly reflected in the calculation of EBITDA.

It is understood that Buyer will account for Seller's operating results on a GAAP basis which will vary from Monroe's calculation of EBITDA. In no event shall Buyer's accounting affect Monroe's calculation of EBITDA. In addition, any revenues derived from Curb Energy, LLC or Rate Droppers, LLC or any efficiency projects conducted by Buyer post-acquisition will not be included in the EBITDA calculation. Similarly, no expenses attributable to Curb Energy, LLC or Rate Droppers, LLC will be reflected as part of the Earnout calculation. The parties agree that expenses related to the Seller's ongoing business will not be arbitrarily allocated to Curb Energy, LLC or Rate Droppers, LLC.

It is understood that the Buyer is purchasing the business for the long-term growth and profit prospects of the Seller. To that end, Monroe will continue to operate the business consistent with historical practices and as a going concern focused on the long-term growth and profitability of the business. At all times prior to the expiration of the applicable EBITDA measurement period for the Earnout, Buyer shall: (i) maintain the staffing levels, marketing, billing, invoicing, collection, incurring of expenses and employ methods of generating revenue and making expenditures and maintaining relationship management procedures and otherwise conduct Buyer's operation from the Leased Premises as were conducted by Seller in the Ordinary Course of Business immediately prior to the Closing Date, (ii) not unreasonably delay any marketing initiatives, execution of new Supplier Agreements and/or Assigned Contracts, and/or otherwise take any action which has the result of reducing revenue and/or increasing expenses with respect to Buyer's operation of the Division, as hereinafter defined, from the Leased Premises; (iii) not divert any new or current customers or suppliers to any Subsidiary and/or Affiliate of Buyer or any third party to provide the services currently provided by Seller, (iv) at a minimum, maintain and operate the business operations of Buyer to be conducted from the Leased Premises generated in part from the Acquired Assets so purchased by Buyer (the "Division") from the Leased Premises from the Closing Date through and including the Earnout measurement period; and (v) not take any other act for the purposes, directly or indirectly, of precluding Seller from receiving the full benefit of the Earnout. The Buyer will not make operating decisions for the sole purpose of attaining the Earnout criteria to the detriment of the long-term health of the Buyer. It is also understood that Buyer will integrate Seller into its retail group as part of its mid-market offering. For example, Monroe shall not terminate any employee other than for

performance simply to benefit from short-term cost savings. In addition, Monroe shall not postpone hiring decisions or any other programs that have historically been in place or were planned during the Earnout Period prior to the acquisition. It is also understood that the Seller will benefit from cost synergies as a result of the acquisition. For example, Monroe will no longer have to keep separate business insurance, incur professional fees for audit and tax reasons, and pay business taxes. In addition, Monroe will realize cost reductions for several operational expenses within human resources, accounting, information technology and marketing functions that will be handled by the Buyer post-acquisition. These are synergies attributable to the Buyer resulting from the acquisition. Seller agrees that Buyer will request Monroe to perform certain duties and incur certain costs as a component of the Buyer's operation. For example, Buyer may appoint Monroe to handle all administrative duties related to its mid-market group. This may require hiring additional personnel, incurring additional travel costs and other costs. Monroe may not unreasonably deny to perform any of these duties that are deemed to benefit the Buyer for the long-term. It is not the intention of the Buyer to burden Monroe with costs incremental to what it has historically incurred. However, the Buyer anticipates utilizing the cost synergies attributable to the acquisition to invest in the future growth of the Seller for the Buyer's ongoing business. These cost synergies are not to the benefit of Monroe alone for the purpose of achieving its Earnout targets.

(b) For purposes of calculating the Earnout, in the event of a breach by Buyer of its obligations under subparagraph (a) of this Section 1.7 which precludes Seller from receiving the full benefit of the Earnout, Seller shall be deemed to have achieved the Earnout as set forth in this Section 1.7. Additionally, upon a Change of Control Transaction, which results in a breach of Buyer's obligations under this Section 1.7 and precludes Seller from receiving the full benefit of the Earnout, Seller shall be deemed to have achieved the Earnout; and

(c) As promptly as possible, but in no event later than November 30, 2013, the Buyer shall deliver to Seller a written statement setting forth Buyer's calculation of the Earnout, together with reasonable documentation supporting the calculation thereof (the "Earnout Statement"). Within thirty (30) days after receipt of such Earnout Statement (the "Earnout Objection Period"), Seller must notify Buyer of any objections to Buyer's determinations of the applicable Earnout payment, providing in reasonable detail the basis for such objections. In the event that Seller does not timely or properly notify Buyer within the Earnout Objection Period that Seller has any objections to such statements or Buyer's calculation of the applicable Earnout payment shall be final and binding hereunder. In the event that Seller does notify Buyer, within the Earnout Objection Period, that Seller has any such objection, then Buyer and Seller shall attempt to resolve such disputed items. In the event Seller and Buyer are unable to resolve the disputed items within thirty (30) days after receipt by Buyer of Seller's notice of dispute, the Parties' respectively engaged independent certified public accountants shall attempt to resolve the disputed items. In the event that such accounting firms are unable to resolve such disputed items within sixty (60) days of Seller's notice of dispute, such disputed items shall be referred to such independent accounting firm as mutually agreed upon by Buyer and Seller or, in the absence of such agreement such independent accounting firm as Seller and Buyer's respective accounting firms jointly appoint to finally resolve such disputed items (provided that such firm has not within the preceding thirty-six (36) months had a, and does not have a current or prospective, business relationship with Buyer or Seller, or any of their respective Subsidiary

and/or Affiliates). The determination of such accounting firm shall be made as promptly as possible and shall be final and binding upon the parties absent demonstrable error. Seller and Buyer each shall be permitted to submit such data and information to such accounting firm as such party deems appropriate. The parties shall share responsibility for the out-of-pocket expenses and fees incurred in connection with resolving such disputed items as follows: (A) if the accounting firm's determination results in additional amounts payable to Seller as Earnout, Buyer will be responsible for all of the fees and expenses of the accounting firm so chosen by Seller's and Buyer's accounting firms; and (B) if the accounting firm's determination does not result in additional amounts payable to Seller as Earnout payment, Seller will be responsible for all of the fees and expenses of the accounting firm so chosen by Seller's and Buyer's respective accounting firms.

Any additional amounts payable to Seller as an Earnout payment determined by this Section 1.7 shall be made within three (3) business days after the applicable Earnout Payment has been finally determined in accordance with this Section 1.7 by wire transfer or other delivery of immediately available funds to an account designated by the Seller.

**1.8 Further Assurances.** At any time and from time to time after the Closing, at the reasonable request of a Party and without further consideration, the other Party shall execute and deliver such other instruments of sale, transfer, conveyance and assignment and take such actions as the other Party may reasonably request to more effectively effectuate the intent of this Agreement.

## ARTICLE II

### REPRESENTATIONS AND WARRANTIES OF THE SELLER

The Seller represents and warrants to the Buyer that, except as set forth in the Disclosure Schedule, the statements contained in this Article II are true and correct as of the date of this Agreement, except to the extent such representations and warranties are specifically made as of a particular date (in which case such representations and warranties will be true and correct as of such date). The Disclosure Schedule shall be arranged in sections and subsections corresponding to the numbered and lettered sections and subsections contained in this Article II. With respect to each such disclosure of the Disclosure Schedule, notwithstanding any reference to a specific section, all such information shall be deemed to qualify all other sections, where applicable, and not just such section.

**2.1 Organization, Qualification and Corporate Power.** The Seller is a limited liability company duly organized, validly existing and in good standing under the laws of the State of Connecticut. The Seller is duly qualified to conduct business and is in good standing under the laws of each jurisdiction listed in Section 2.1 of the Disclosure Schedule, which jurisdictions constitute the only jurisdictions in which the nature of the Seller's businesses as is presently conducted or the ownership or leasing of its properties as presently owned or leased requires such qualification. The Seller has all requisite power and authority to carry on the businesses in which it is engaged and to own and use the properties owned and used by it. The Seller has furnished to the Buyer complete and accurate copies of its Articles of Organization and its current Operating Agreement and Seller is not in default under or in violation of any provision of such documents and agreements. The Operating Agreement provided to the Buyer is the only

instrument setting forth (i) the rights, preferences and privileges of the Members (including all holders of equity or profits interests) of the Seller with respect to the Seller and/or among such Members, and (ii) matters relating to the operation and governance of the Seller.

**2.2 Members and Membership Interests.** The Members constitute all of the members of the Seller and Section 2.2 of the Disclosure Schedule sets forth their respective membership interests in the Seller. There are no options, warrants or other instruments giving any party the right to acquire any interest in the Seller. There are no outstanding agreements or commitments to which the Seller is a party or which are binding upon the Seller providing for the redemption of any of its membership interests.

**2.3 Authorization of Transaction.**

(a) The Seller has all requisite power and authority to execute and deliver this Agreement and the Ancillary Agreements and to perform its obligations hereunder and thereunder. The execution and delivery by the Seller of this Agreement and the Ancillary Agreements, the performance by the Seller of this Agreement and the Ancillary Agreements and the consummation by the Seller of the transactions contemplated hereby and thereby have been duly and validly authorized by all necessary action on the part of the Seller and its Members.

(b) Except as set forth in Schedule 2.3 of the Disclosure Schedule, this Agreement has been duly and validly executed and delivered by the Seller and constitutes, and each of the Ancillary Agreements, upon its execution and delivery by the Seller will constitute, a valid and binding obligation of the Seller, enforceable against the Seller in accordance with its terms subject to applicable bankruptcy, insolvency, reorganization, moratorium and similar laws affecting creditors' rights and remedies generally, and subject, as to enforceability, to general principles of equity, including principles of commercial reasonableness, good faith and fair dealing (regardless of whether enforcement is sought in a proceeding at law or in equity).

**2.4 Noncontravention.** Except as set forth in Section 2.4 of the Disclosure Schedule, neither the execution and delivery by the Seller of this Agreement or the Ancillary Agreements to which they are party, nor the consummation by the Seller of the transactions contemplated hereby or thereby, will (a) conflict with or violate any provision of the organizational and operational documents and agreement of the Seller (including without limitation its Operating Agreement, (b) require on the part of the Seller any notice to or filing with, or any permit, authorization, consent or approval of, any Governmental Entity, (c) to the Knowledge of Seller, conflict with, result in a breach of, constitute (with or without due notice or lapse of time or both) a default under, result in the acceleration of obligations under, create in any party the right to terminate, modify or cancel, or require any notice, consent or waiver under, any contract or instrument to which the Seller is a party or by which the Seller is bound or to which any of its assets is subject, (d) result in the imposition of any Security Interest upon any assets of the Seller or (e) to the Knowledge of Seller, violate any order, writ, injunction, decree, statute, rule or regulation applicable to the Seller or any of its properties or assets.

2.5 Subsidiaries. Seller has no Subsidiaries. The Seller does not control directly or indirectly or have any direct or indirect equity participation or similar interest in any corporation, partnership, limited liability company, joint venture, trust or other business association or entity.

2.6 Financial Statements.

(a) The Seller has provided to the Buyer the Financial Statements set forth in Section 2.6 to the Disclosure Schedule and to the Knowledge of Seller, the Financial Statements (i) comply as to form in all respects with applicable accounting requirements, (ii) to the Knowledge of Seller, were prepared in accordance with the income tax basis of accounting applied on a consistent basis throughout the periods covered thereby (except as may be indicated in the notes to such financial statements) and to the Knowledge of Seller, fairly present the financial position of the Seller as of the dates thereof and the results of its operations and cash flows for the periods indicated, consistent with the books and records of the Seller, except that the unaudited interim financial statements, if any, are subject to normal and recurring year-end adjustments which will not be material in amount or effect and do not include footnotes. Except as set forth in the Financial Statements, the Seller has no liabilities or obligations, contingent or otherwise, other than (i) liabilities incurred in the ordinary course of business subsequent to July 31, 2012, (ii) obligations under contracts and commitments incurred in the Ordinary Course of Business; and (iii) any other liabilities and obligations of a type or nature, which, in all such cases, individually and in the aggregate would not have a Seller Material Adverse Effect.

2.7 Absence of Certain Changes. Except as set forth in Section 2.7 to the Disclosure Schedule, since July 31, 2012, there has occurred no event or development which, individually or in the aggregate, has had, or could reasonably be expected to have in the future, a Seller Material Adverse Effect.

2.8 Left Intentionally Blank.

2.9 Tax Matters.

(a) Seller has properly filed on a timely basis all material Tax Returns that it is and was required to file, and all such Tax Returns were true, correct and complete in all material respects. The Seller has properly paid on a timely basis all material Taxes, required by law to pay that were due and payable. All material Taxes that the Seller is or was required by law to withhold or collect have been withheld or collected and, to the extent required, have been properly paid on a timely basis to the appropriate Governmental Entity. The Seller has complied with all information reporting and back-up withholding requirements in all material respects, including maintenance of the required records with respect thereto, in connection with amounts paid to any employee, independent contractor, creditor or other third party.

(b) The unpaid Taxes of the Seller for periods through the date of the Most Recent Balance Sheet Date do not materially exceed the accruals and reserves for Taxes (excluding accruals and reserves for deferred Taxes established to reflect timing differences between book and Tax income) set forth on the Most Recent Balance Sheet. All Taxes attributable to the period from and after the Most Recent Balance Sheet Date and continuing through the Closing Date are, or will be, attributable to the conduct by the Seller of its operations in the Ordinary Course of Business.



(c) No examination or audit of any Tax Return of the Seller by any Governmental Entity is currently in progress or, to the Knowledge of the Seller, threatened or contemplated. Section 2.9(c) of the Disclosure Schedule sets forth each jurisdiction (other than United States federal) in which the Seller files, or is required to file or has been required to file a material Tax Return or is or has been liable for material Taxes on a "nexus" basis. The Seller has not been informed by any jurisdiction that the jurisdiction believes that the Seller was required to file any Tax Return that was not filed.

(d) The Seller is, and has been since its inception, a limited liability company validly classified and treated as a partnership for federal income tax purposes and has been validly treated in a similar manner for purposes of the income Tax laws of all states in which it has been subject to taxation.

(e) Except as set forth in Section 2.9(e) of the Disclosure Schedules, the Seller has delivered or made available to the Buyer (i) complete and correct copies of all Tax Returns of the Seller relating to Taxes for all Taxable periods for which the applicable statute of limitations has not yet expired and (ii) complete and correct copies of all private letter rulings, revenue agent reports, information document requests, notices of assessment, notices of proposed deficiencies, deficiency notices, protests, petitions, closing agreements, settlement agreements, pending ruling requests and any similar documents submitted by, received by or agreed to by or on behalf of the Seller relating to Taxes for all taxable periods for which the applicable statute of limitations has not yet expired.

(f) The Seller has not (i) waived any statute of limitations with respect to Taxes or agreed to extend the period for assessment or collection of any Taxes, (ii) requested any extension of time within which to file any Tax Return, which Tax Return has not yet been filed, or (iii) executed or filed any power of attorney relating to Taxes with any Governmental Entity.

(g) The Seller is not a party to any litigation regarding Taxes.

(h) There are no Security Interests with respect to Taxes upon any of the Acquired Assets, other than with respect to Taxes not yet due and payable. To the Knowledge of Seller, there is no basis for the assertion of any claim relating or attributable to Taxes.

(i) The Seller is not bound by any tax indemnity, tax sharing or tax allocation agreement.

(j) The Seller is not a "foreign person" within the meaning of Section 1445 of the Code.

#### 2.10 Ownership and Condition of Assets .

(a) The Seller is the true and lawful owner, and has good title to, all of the Acquired Assets, free and clear of all Security Interests, except as set forth in Section 2.10(a) of the Disclosure Schedule. Upon the Closing, the Buyer will become the true and lawful owner of, and will receive good title to, the Acquired Assets, free and clear of all Security Interests.

(b) Except as set forth in Section 2.10(b) of the Disclosure Schedule, each tangible Acquired Asset is free from material defects, has been maintained in accordance with normal industry practice and to the Knowledge of Seller, is in good operating condition and repair (subject to normal wear and tear) and is suitable for the purposes for which it presently is used.

(c) Section 2.10(c) of the Disclosure Schedule lists individually (i) all Acquired Assets which are fixed assets (within the meaning of GAAP), indicating the cost, accumulated book depreciation (if any) and the net book value of each such fixed asset as of the Most Recent Balance Sheet Date, and (ii) all other Acquired Assets of a tangible nature (other than inventories) whose book value exceeds \$10,000.00.

(d) Each Acquired Asset constituting an item of equipment or other asset that the Seller has possession of pursuant to a lease agreement or other contractual arrangement is in such condition that, upon its return to its lessor or owner under the applicable lease or contract, the obligations of the Seller to such lessor or owner will have been discharged in full.

2.11 Owned Real Property. The Seller does not own and has never owned any real property.

2.12 Real Property Leases. Except as set forth in Section 2.12 of the Disclosure Schedule, Seller is not a party to any real property Lease as of the Closing Date.

2.13 Intellectual Property.

(a) There are no Seller Registrations.

(b) Seller has no Patent Rights.

(c) *Protection Measures*. The Seller has taken reasonable measures to protect the proprietary nature of each item of Seller Owned Intellectual Property, if any, and to maintain in confidence all trade secrets and confidential information comprising a part thereof. To the Knowledge of Seller, Seller has complied with all applicable contractual and legal requirements pertaining to information privacy and security. No complaint relating to an improper use or disclosure of, or a breach in the security of, any such information has been made or, to the Knowledge of the Seller, is threatened against the Seller. To the Knowledge of the Seller, there has been no: (i) unauthorized disclosure of any third party proprietary or confidential information in the possession, custody or control of the Seller or (ii) breach of the Seller's security procedures wherein confidential information has been disclosed to a third person.

(d) *Inbound IP Agreements*. Section 2.13(d) of the Disclosure Schedule identifies (i) each item of Seller Licensed Intellectual Property and the license or agreement pursuant to which the Seller Exploits it (excluding currently-available, off the shelf software programs that are part of the Internal Systems and are licensed by the Seller pursuant to "shrink wrap" licenses, the total fees associated with which are less than \$2,500) and (ii) each agreement,

contract, assignment or other instrument pursuant to which the Seller has obtained any joint or sole ownership interest in or to each item of Seller Owned Intellectual Property. To the Knowledge of Seller, no third party inventions, methods, services, materials, processes or Software are included in or required to Exploit the Customer Offerings or Internal Systems. None of the Customer Offerings or Internal Systems includes "shareware," "freeware" or other Software or other material that was obtained by the Seller from third parties other than pursuant to the license agreements listed in Section 2.13(d) of the Disclosure Schedule.

(e) *Employee and Contractor Assignments*. Each employee and each independent contractor of the Seller has executed a valid and binding written agreement expressly assigning to the Seller all right, title and interest in any inventions and works of authorship, whether or not patentable, invented, created, developed, conceived and/or reduced to practice during the term of such employee's employment or such independent contractor's work for the Seller, and all Intellectual Property rights therein, and has waived all moral rights therein to the extent legally permissible.

(f) *Infringement by Seller*. To the Knowledge of Seller, none of the Customer Offerings, or the Exploitation thereof by the Seller or by any reseller, distributor, customer or user thereof, or any other activity of the Seller, infringes or violates, or constitutes a misappropriation of, any Intellectual Property rights of any third party. To the Knowledge of Seller, none of the Internal Systems, or the Seller's past, current or currently contemplated Exploitation thereof, or any other activity undertaken by them in connection with the Business, infringes or violates, or constitutes a misappropriation of, any Intellectual Property rights of any third party. Section 2.13(f) of the Disclosure Schedule lists any complaint, claim or notice, or threat of any of the foregoing (including any notification that a license under any patent is or may be required), received by the Seller alleging any such infringement, violation or misappropriation and any request or demand for indemnification or defense received by the Seller from any reseller, distributor, customer, user or any other third party; and the Seller has provided to the Buyer copies of all such complaints, claims, notices, requests, demands or threats, as well as any legal opinions, studies, market surveys and analyses relating to any alleged or potential infringement, violation or misappropriation.

#### 2.14 Contracts.

(a) Section 2.14 of the Disclosure Schedule lists the following agreements (written or oral) to which the Seller is a party as of the date of this Agreement:

(i) any agreement (or group of related agreements) for the lease of personal property from or to third parties providing for lease payments in excess of \$10,000.00 per annum or having a remaining term longer than three months;

(ii) any agreement (or group of related agreements) for the purchase or sale of products or for the furnishing or receipt of services (A) which calls for performance over a period of more than one year, (B) which involves more than the sum of \$10,000.00, or (C) in which the Seller has granted manufacturing rights, "most favored nation" pricing provisions or marketing or distribution rights relating to any products or territory or has agreed to purchase a minimum quantity of goods or services or has agreed to purchase goods or services exclusively from a certain party;

(iii) any agreement concerning the establishment or operation of a partnership, joint venture or limited liability company;

(iv) any agreement (or group of related agreements) under which it has created, incurred, assumed or guaranteed (or may create, incur, assume or guarantee) indebtedness (including capitalized lease obligations) involving more than \$10,000 or under which it has imposed (or may impose) a Security Interest on any of its assets, tangible or intangible;

(v) any agreement for the disposition of any significant portion of the assets or business of the Seller (other than sales of products in the Ordinary Course of Business) or any agreement for the acquisition of the assets or business of any other entity (other than purchases of inventory or components in the Ordinary Course of Business);

(vi) any agreement concerning exclusivity or confidentiality;

(vii) any employment or consulting agreement;

(viii) any agreement involving any current or former officer, manager or member of the Seller;

(ix) any agreement which contains any provisions requiring the Seller to indemnify any other party (excluding indemnities contained in agreements for the purchase, sale or license of products entered into in the Ordinary Course of Business);

(x) any agreement under which the Seller is restricted from selling, licensing or otherwise distributing any of its technology or products, or providing services to, customers or potential customers or any class of customers, in any geographic area, during any period of time or any segment of the market or line of business;

(xi) any agreement which would entitle any third party to receive a license or any other right to intellectual property of the Buyer or any of the Buyer's Affiliates following the Closing; and

(xii) any other agreement (or group of related agreements) either involving more than \$10,000.00 or not entered into in the Ordinary Course of Business.

(b) The Seller has delivered to the Buyer a complete and accurate copy of each agreement listed in Section 2.13 or Section 2.14 of the Disclosure Schedule. Except as otherwise provided in this Agreement, with respect to each agreement so listed: (i) the agreement is legal, valid, binding and enforceable and in full force and effect subject to applicable bankruptcy, insolvency, reorganization, moratorium and similar laws affecting creditors' rights and remedies generally, and subject, as to enforceability, to general principles of equity, including principles of commercial reasonableness, good faith and fair dealing (regardless of whether enforcement is sought in a proceeding at law or in equity); and (ii) neither the Seller nor, to the

Knowledge of the Seller, any other party, is in breach or violation of, or default under, any such agreement, and no event has occurred, is pending or, to the Knowledge of the Seller, is threatened, which, after the giving of notice, with lapse of time, or otherwise, would constitute a breach or default by the Seller or, to the Knowledge of the Seller, any other party under such agreement.

2.15 Backlog. To the Knowledge of Seller, all Backlog of the Seller are valid receivables and the Seller is not aware of any setoffs or counterclaims. A complete and accurate list of the Backlog was provided to Buyer by Russ Monroe on September 6, 2012 and a summary by supplier of the Backlog is included in Schedule 2.15 of the Disclosure Schedule. The Seller has not received any written notice from an account debtor stating that any Backlog is subject to any contest, claim or setoff by such account debtor.

2.16 Insurance. Section 2.16 of the Disclosure Schedule lists each insurance policy (including fire, theft, casualty, comprehensive general liability, workers compensation, business interruption, environmental, product liability, errors and omissions, professional liability and automobile insurance policies and bond and surety arrangements) to which the Seller is a party, all of which are in full force and effect. There is no material claim pending under any such policy as to which coverage has been questioned, denied or disputed by the underwriter of such policy. All premiums due and payable under all such policies have been paid, neither the Seller nor the Buyer will be liable for retroactive premiums or similar payments, and the Seller is otherwise in compliance in all material respects with the terms of such policies. To the Knowledge of the Seller there is no threatened termination of, or premium increase with respect to, any such policy. To the Knowledge of Seller, Seller's insurance is adequate in terms of scope and coverage to pay all claims arising or made prior to the Closing.

2.17 Litigation. Except as set forth in Section 2.17 of the Disclosure Schedule, there is no Legal Proceeding which is pending or has been threatened in writing against the Seller which (a) seeks either damages or equitable relief in any way relating to the Seller or its business or (b) in any manner challenges or seeks to prevent, enjoin, alter or delay the transactions contemplated by this Agreement. There are no judgments, orders or decrees outstanding against the Seller.

2.18 Warranties. No product or service manufactured, sold, leased, licensed or delivered by the Seller is subject to any guaranty, warranty, right of return, right of credit or other indemnity other than third-party manufacturers' warranties for which the Seller has no liability.

2.19 Employees.

(a) Section 2.19 of the Disclosure Schedule contains a list of all employees of the Seller, along with the position and the annual rate of compensation of each such person. Each current or past employee of the Seller has entered into a confidentiality and assignment of inventions agreement with the Seller, a copy or form of which has previously been delivered to the Buyer. Section 2.19 of the Disclosure Schedule contains a list of all employees of the Seller who are a party to a non-competition agreement with the Seller; copies of such agreements have previously been delivered to the Buyer. Section 2.19 of the Disclosure Schedule contains a list of all employees of the Seller who are not citizens of the United States. To the Knowledge of Seller,

no key employee or group of employees has any plans to terminate employment with the Seller (other than for the purpose of accepting employment with the Buyer following the Closing) or not to accept employment with the Buyer. Seller is in compliance with all applicable laws relating to the hiring and employment of employees.

(b) The Seller is not a party to or bound by any collective bargaining agreement, nor has it experienced any strikes, grievances, claims of unfair labor practices or other collective bargaining disputes. To the Knowledge of Seller, there is no organizational effort made or threatened, either currently or within the past two years, by or on behalf of any labor union with respect to employees of the Seller.

#### 2.20 Employee Benefits.

(a) Section 2.20(a) of the Disclosure Schedule contains a complete and accurate list of all Seller Plans. Complete and accurate copies of (i) all Seller Plans which have been reduced to writing, (ii) written summaries of all unwritten Seller Plans, (iii) all related trust agreements, insurance contracts and summary plan descriptions, and (iv) all annual reports filed on IRS Form 5500, 5500C or 5500R and (for all funded plans) all plan financial statements for the last five plan years for Seller Plan, have been delivered to the Buyer.

(b) Each Seller Plan has been administered in all material respects in accordance with its terms and Seller and the ERISA Affiliates has in all material respects met its obligations with respect to each Seller Plan and has made all required contributions thereto. The Seller, each ERISA Affiliate and each Seller Plan are in compliance in all material respects with the currently applicable provisions of ERISA and the Code and the regulations thereunder (including Section 4980 B of the Code, Subtitle K, Chapter 100 of the Code and Sections 601 through 608 and Section 701 et seq. of ERISA). All filings and reports as to each Seller Plan required to have been submitted to the Internal Revenue Service or to the United States Department of Labor have been duly submitted. No Seller Plan has assets that include securities issued by the Seller or any ERISA Affiliate.

(c) There are no Legal Proceedings (except claims for benefits payable in the normal operation of the Seller Plans and proceedings with respect to qualified domestic relations orders) against or involving any Seller Plan or asserting any rights or claims to benefits under any Seller Plan that could give rise to any material liability.

(d) All the Seller Plans that are intended to be qualified under Section 401(a) of the Code have received determination letters from the Internal Revenue Service to the effect that such Seller Plans are qualified and the plans and the trusts related thereto are exempt from federal income taxes under Sections 401(a) and 501(a), respectively, of the Code, no such determination letter has been revoked and revocation has not been threatened, and no such Seller Plan has been amended since the date of its most recent determination letter or application therefor in any respect, and no act or omission has occurred, that would adversely affect its qualification or materially increase its cost. Each Seller Plan which is required to satisfy Section 401(k)(3) or Section 401(m)(2) of the Code has been tested for compliance with, and satisfies the requirements of Section 401(k)(3) and Section 401(m)(2) of the Code for each plan year ending prior to the Closing Date.

(e) Neither the Seller nor any ERISA Affiliate has ever maintained an Employee Benefit Plan subject to Section 412 of the Code or Title IV of ERISA.

(f) At no time has the Seller or any ERISA Affiliate been obligated to contribute to any "multiemployer plan" (as defined in Section 4001(a)(3) of ERISA).

(g) There are no unfunded obligations under any Seller Plan providing benefits after termination of employment to any employee of the Seller (or to any beneficiary of any such employee), including but not limited to retiree health coverage and deferred compensation, but excluding continuation of health coverage required to be continued under Section 4980B of the Code or other applicable law and insurance conversion privileges under state law. The assets of each Seller Plan which is funded are reported at their fair market value on the books and records of such Seller Plan.

(h) No act or omission has occurred and no condition exists with respect to any Seller Plan that would subject the Seller or any ERISA Affiliate to (i) any material fine, penalty, tax or liability of any kind imposed under ERISA or the Code or (ii) any contractual indemnification or contribution obligation protecting any fiduciary, insurer or service provider with respect to any Seller Plan.

(i) Each Seller Plan is funded by, associated with or related to a "voluntary employee's beneficiary association" within the meaning of Section 501(c)(9) of the Code.

(j) No Seller Plan is amendable and terminable unilaterally by the Seller at any time without liability or expense to the Seller or such Seller Plan as a result thereof (other than for benefits accrued through the date of termination or amendment and reasonable administrative expenses related thereto) and, no Seller Plan, plan documentation or agreement, summary plan description or other written communication distributed generally to employees by its terms prohibits the Seller from amending or terminating any such Seller Plan.

(k) Section 2.20(k) of the Disclosure Schedule discloses each: (i) agreement with any member, director, executive officer or other key employee of the Seller (A) the benefits of which are contingent, or the terms of which are altered, upon the occurrence of a transaction involving the Seller of the nature of any of the transactions contemplated by this Agreement, (B) providing any term of employment or compensation guarantee or (C) providing severance benefits or other benefits after the termination of employment of such director, executive officer or key employee; (ii) agreement, plan or arrangement under which any person may receive payments from the Seller that may be subject to the tax imposed by Section 4999 of the Code or included in the determination of such person's "parachute payment" under Section 280G of the Code; and (iii) agreement or plan binding the Seller, including any stock option plan, stock appreciation right plan, restricted stock plan, stock purchase plan, severance benefit plan or Seller Plan, any of the benefits of which will be increased, or the vesting of the benefits of which will be accelerated, by the occurrence of any of the transactions contemplated by this Agreement or the value of any of the benefits of which will be calculated on the basis of any of the transactions contemplated by this Agreement.

(l) Section 2.20(l) of the Disclosure Schedule sets forth the policy of the Seller with respect to accrued vacation, accrued sick time and earned time off and the amount of such liabilities as of the date hereof.

(m) Each Seller Plan that is a "nonqualified deferred compensation plan" (as defined in Code Section 409A(d)(1)) has been operated since January 1, 2005 in good faith compliance with Code Section 409A and IRS Notice 2005-1. No Seller Plan that is a "nonqualified deferred compensation plan" has been materially modified (as determined under Notice 2005-1) after October 3, 2004. No event has occurred that would be treated by Code Section 409A(b) as a transfer of property for purposes of Code Section 83. No stock option or equity unit option granted under any Seller Plan has an exercise price that has been or may be less than the fair market value of the underlying stock or equity units (as the case may be) as of the date such option was granted or has any feature for the deferral of compensation other than the deferral of recognition of income until the later of exercise or disposition of such option.

#### 2.21 Environmental Matters.

(a) The Seller has complied with all applicable Environmental Laws. There is no pending nor, to the Knowledge of Seller, threatened civil or criminal litigation, written notice of violation, formal administrative proceeding, or investigation, inquiry or information request by any Governmental Entity, relating to any Environmental Law involving the Seller.

(b) To the Knowledge of Seller, the Seller has no liabilities or obligations arising from the release of any Materials of Environmental Concern into the environment.

(c) The Seller is not a party to or bound by any court order, administrative order, consent order or other agreement with any Governmental Entity entered into in connection with any legal obligation or liability arising under any Environmental Law.

2.22 Legal Compliance. The Seller has, at all times, conducted its business in compliance with each applicable law (including rules and regulations thereunder) of any federal, state, local or foreign government, or any Governmental Entity except where such non-compliance would not reasonably be expected to have a Seller Material Adverse Effect. The Seller has not received any notice or communication from any Governmental Entity alleging noncompliance with any applicable law, rule or regulation except where such non-compliance would not reasonably be expected to have a Seller Material Adverse Effect.

2.23 Customers and Suppliers. Section 2.23 of the Disclosure Schedule sets forth a list of (a) each customer that accounted for more than 1% of the consolidated revenues of the Seller during the last full fiscal year or the interim period through the Most Recent Balance Sheet Date and the amount of revenues accounted for by such customer during each such period and (b) each supplier that is the sole supplier of any significant product or service to the Seller. No such customer or supplier has indicated within the past year that it will stop, or decrease the rate of, buying products or supplying products, as applicable, to the Seller.

2.24 Permits. Section 2.24 of the Disclosure Schedule sets forth a list of all Permits issued to or held by the Seller. To the Knowledge of Seller, each such Permit is in full force and effect; the Seller is in compliance with the terms of each such Permit except where such non-compliance



would not reasonably be expected to have a Seller Material Adverse Effect and, to the Knowledge of Seller, no suspension or cancellation of such Permit is threatened and there is no basis for believing that such Permit will not be renewable upon expiration.

2.25 Certain Business Relationships With Affiliates. Seller has no Affiliates.

2.26 Brokers' Fees. The Seller has no liability or obligation to pay any fees or commissions to any broker, finder or agent with respect to the transactions contemplated by this Agreement.

2.27 Books and Records. The books and records of the Seller accurately reflect the assets, liabilities, business, financial condition and results of operations of the Seller and have been maintained in accordance with reasonable business and bookkeeping practices. Section 2.27 of the Disclosure Schedule contains a list of all bank accounts and safe deposit boxes of the Seller and the names of persons having signature authority with respect thereto or access thereto.

2.28 Left Intentionally Blank.

2.29 Controls and Procedures. The Seller maintains accurate books and records reflecting its assets and liabilities and maintains proper and adequate internal control over financial reporting which provide assurance that (i) transactions are executed with management's authorization, (ii) transactions are recorded as necessary to permit preparation of the consolidated financial statements of the Seller and to maintain accountability for the Seller's consolidated assets, (iii) access to assets of the Seller is permitted only in accordance with management's authorization, (iv) the reporting of assets of the Seller is compared with existing assets at regular intervals and (v) accounts, notes and other receivables and inventory were recorded accurately, and proper and adequate procedures are implemented to effect the collection thereof on a current and timely basis.

2.30 Government Contracts. The Seller has not been suspended or debarred from bidding on contracts or subcontracts with any Governmental Entity; to the Knowledge of Seller, no such suspension or debarment has been threatened or initiated; and to the Knowledge of Seller, the consummation of the transactions contemplated by this Agreement will not result in any such suspension or debarment of the Seller or the Buyer (assuming that no such suspension or debarment will result solely from the identity of the Buyer). The Seller has not been or is now being audited or investigated by the United States Government Accounting Office, the United States Department of Defense or any of its agencies, the Defense Contract Audit Agency, the contracting or auditing function of any Governmental Entity with which it is contracting, the United States Department of Justice, the Inspector General of the United States Governmental Entity, or any prime contractor with a Governmental Entity; nor, to the Knowledge of Seller, has any such audit or investigation been threatened. To the Knowledge of Seller, there is no valid basis for (i) the suspension or debarment of the Seller from bidding on contracts or subcontracts with any Governmental Entity or (ii) any claim (including any claim for return of funds to the Government) pursuant to an audit or investigation by any of the entities named in the foregoing sentence. The Seller has no agreements, contracts or commitments which require it to obtain or maintain a security clearance with any Governmental Entity.

### 2.31 Securities Laws.

(a) The Seller and the Members have been furnished all of the materials relating to the Buyer, and its payment of the Purchase Price, that have been requested and each of them has been afforded an opportunity to ask questions of, and receive answers from, management of the Buyer in connection with the payment of the Purchase Price. The Seller and the Members have not been furnished with any oral or written representation in connection with the payment of the Purchase Price by or on behalf of the Buyer that it has relied on that is not contained in this Agreement.

(b) Each of the Seller and the Members: (i) is an "accredited investor" as defined in Rule 501 of Regulation D under the Securities Act of 1933, as amended; (ii) has obtained, in its judgment, sufficient information to evaluate the merits and risks of the payment of the Earnout with securities of the Buyer; (iii) has sufficient knowledge and experience in financial and business matters to evaluate the merits and risks associated with such payment of the Earnout with securities of the Buyer and to make an informed investment decision with respect thereto, and (iv) has consulted with his or its own advisors with respect to the receipt of securities as part of the Earnout.

(c) The securities being acquired hereunder are being acquired for each of the Seller and the Members' own account for investment and not for the benefit or account of any other person and not with a view to, or in connection with, any unlawful resale or distribution thereof. Each of the Seller and the Members fully understands and agrees that it must bear the economic risk of the investment in securities received hereunder for an indefinite period of time because, among other reasons, such securities received hereunder have not been registered under the Securities Act of 1933, as amended or under the securities laws of any states, and, therefore, the securities are "restricted securities" and cannot be resold, pledged, assigned or otherwise disposed of unless they are subsequently registered under the Securities Act of 1933, amended and under the applicable securities laws of such states or an exemption from such registration is otherwise available. Each of the Seller and the Members understands that the Buyer is not under any obligation to register such securities on the Seller and the Members' behalf or to assist such Seller and the Members in complying with any exemption from registration under the Securities Act or applicable state securities laws.

(d) Each of the Seller and the Members intends that the applicable state securities law will apply to its receipt of the securities hereunder. Each of the Seller and the Members meets all suitability standards imposed by the state securities laws relating to the receipt of the securities as part of the Earnout hereunder without registering any of the Buyer's securities under the securities laws of such state.

(e) Buyer shall assist Seller with an opinion of counsel with respect to any transfer of the shares if there is no material question as to the availability of Rule 144 promulgated under the Securities Act of 1933, as amended.

## ARTICLE III

### REPRESENTATIONS AND WARRANTIES OF THE BUYER

The Buyer represents and warrants to the Seller that the statements contained in this Article III are true and correct as of the date of this Agreement.

3.1 Organization and Corporate Power. The Buyer is a corporation duly organized, validly existing and in good standing under the laws of the State of Delaware. The Buyer has all requisite corporate power and authority to carry on the businesses in which it is engaged and to own and use the properties owned and used by it.

3.2 Authorization of the Transaction. The Buyer has all requisite power and authority to execute and deliver this Agreement and the Ancillary Agreements and to perform its obligations hereunder and thereunder and all other agreements contemplated by this Agreement. The execution and delivery by the Buyer of this Agreement and the Ancillary Agreements and the consummation by the Buyer of the transactions contemplated hereby and thereby have been duly and validly authorized by all necessary corporate action on the part of the Buyer. This Agreement has been duly and validly executed and delivered by the Buyer and constitutes a valid and binding obligation of the Buyer, enforceable against it in accordance with its terms.

3.3 Noncontravention. Neither the execution and delivery by the Buyer of this Agreement or the Ancillary Agreements, nor the consummation by the Buyer of the transactions contemplated hereby or thereby, will (a) conflict with or violate any provision of the Certificate of Incorporation or by-laws of the Buyer, (b) require on the part of the Buyer any filing with, or permit, authorization, consent or approval of, any Governmental Entity, (c) conflict with, result in breach of, constitute (with or without due notice or lapse of time or both) a default under, result in the acceleration of obligations under, create in any party any right to terminate, modify or cancel, or require any notice, consent or waiver under, any contract or instrument to which the Buyer is a party or by which it is bound or to which any of its assets is subject, or (d) violate any order, writ, injunction, decree, statute, rule or regulation applicable to the Buyer or any of its properties or assets except, in each case of (a) through (d), where such breach or violation would not reasonably be expected to have a Buyer Material Adverse Effect.

3.4 Equity Consideration. The Shares which may be issued to Seller under this Agreement are and/or will be duly and validly authorized by the Buyer when and if issued to Seller and the potential issuance of any such Shares to Buyer do not and will not violate at the time of the issuance to Seller any applicable rule or regulation applicable to Buyer or by which Buyer is subject.

#### 3.5 Buyer SEC Documents; No Undisclosed Liabilities.

(a) Buyer has filed all reports, schedules, forms, statements and other documents (including exhibits and other information incorporated therein) with the SEC required to be filed by Buyer since January 1, 2011 (such documents, the "Buyer SEC Documents"). As of their respective dates, the Buyer SEC Documents complied in all material respects with the requirements of the Securities Act or the Securities and Exchange Act of 1934, as amended, as

the case may be, and the rules and regulations of the SEC promulgated thereunder applicable to such Buyer SEC Documents, and, as of their respective dates, none of the Buyer SEC Documents contained any untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary in order to make the statements therein, in light of the circumstances under which they were made, not misleading. The financial statements of Buyer included in the Buyer SEC Documents complied as to form in all material respects with applicable accounting requirements and the published rules and regulations of the SEC with respect thereto as of their respective dates, were prepared in accordance with GAAP (except, in the case of unaudited statements, as permitted by Form 10-Q of the SEC) applied on a consistent basis during the periods involved (except as may be indicated in the notes thereto) and fairly presented in all material respects the financial position of Buyer and its consolidated Subsidiaries as of the dates thereof and the consolidated results of their operations and cash flows for the periods then ended (subject, in the case of unaudited statements, to normal year-end audit adjustments).

(b) Except as set forth in the most recent financial statements included in the Buyer SEC Documents filed by Buyer and publicly available prior to the date of this Agreement or for liabilities incurred in connection with this Agreement or in the ordinary course of business since the date of the most recent financial statements included in the Buyer SEC Documents, Buyer has no liabilities or obligations of any nature (whether accrued, absolute, contingent or otherwise) that would be required by GAAP to be reflected in, or reserved against or otherwise described in the consolidated balance sheet of Buyer (including the notes thereto) which, individually or in the aggregate, have had or would reasonably be expected to have a Buyer Material Adverse Effect.

#### ARTICLE IV

##### CONDITIONS PRECEDENT

4.1 Conditions to Obligations of the Buyer. The obligation of the Buyer to consummate the transactions contemplated by this Agreement to be consummated at the Closing is subject to the satisfaction of the following additional conditions:

(a) the Seller shall have obtained at its own expense (and shall have provided copies thereof to the Buyer) all of the waivers, permits, consents, approvals or other authorizations, and effected all registrations, filings and notices, which are required on the part of the Seller except with respect to the tax clearance letter issued by the Connecticut Department of Revenue Services;

(b) the representations and warranties of the Seller set forth in Sections 2.1 (first sentence), 2.2 and 2.3 and any representations and warranties of the Seller set forth in this Agreement that are qualified as to materiality shall be true and correct in all respects, and all other representations and warranties of the Seller set forth in this Agreement shall be true and correct in all material respects, in each case as of the date of this Agreement and as of the Closing as though made as of the Closing, except to the extent such representations and warranties are specifically made as of a particular date (in which case such representations and warranties shall be true and correct as of such date);

(c) the Seller shall have performed or complied with its agreements and covenants required to be performed or complied with under this Agreement as of or prior to the Closing;

(d) no Legal Proceeding shall be pending or threatened; and no judgment, order, decree, stipulation or injunction shall be pending, threatened, or in effect which would (i) prevent consummation of the transactions contemplated by this Agreement, (ii) cause the transactions contemplated by this Agreement to be rescinded following consummation, or (iii) affect adversely the right of the Buyer to own, operate or control any of the Acquired Assets, or to conduct the business of the Seller as currently conducted, following the Closing;

(e) the Seller shall have delivered to the Buyer the Seller Certificate;

(f) the Seller shall have delivered to the Buyer documents evidencing the release or termination of all Security Interests on the Acquired Assets, and copies of filed UCC termination statements with respect to all UCC financing statements evidencing Security Interests or written statements from the lien holders evidencing repayment in full of all outstanding principal loan amounts and interest with respect to any such loans evidencing such Security Interests;

(g) the Buyer shall have secured financing for the transactions contemplated herein on terms acceptable to the Buyer;

(h) the Buyer shall have entered into a lease of the premises at 174 South Road, Enfield, Connecticut on terms acceptable to Buyer;

(i) Russ Monroe has entered into an employment agreement with the Buyer on terms satisfactory to each party to such agreement;  
and

(j) the Buyer shall have received such other certificates and instruments (including certificates of good standing of the Seller in its jurisdiction of organization and the various foreign jurisdictions in which it is qualified, certified organizational and operational documents, certificates as to the incumbency of officers and the adoption of authorizing resolutions) as it shall reasonably request in connection with the Closing.

4.2 Conditions to Obligations of the Seller. The obligation of the Seller to consummate the transactions contemplated by this Agreement to be consummated at the Closing is subject to the satisfaction of the following additional conditions:

(a) the representations and warranties of the Buyer set forth in the first sentence of Section 3.1 and in Section 3.2 and any representations and warranties of the Buyer set forth in this Agreement that are qualified as to materiality shall be true and correct in all respects, and all other representations and warranties of the Buyer set forth in this Agreement shall be true

and correct in all material respects, in each case as of the date of this Agreement and as of the Closing as though made as of the Closing, except to the extent such representations and warranties are specifically made as of a particular date (in which case such representations and warranties shall be true and correct as of such date);

(b) the Buyer shall have performed or complied with in all material respects its agreements and covenants required to be performed or complied with under this Agreement as of or prior to the Closing;

(c) no Legal Proceeding shall be pending or threatened wherein an unfavorable judgment, order, decree, stipulation or injunction would (i) prevent consummation of the transactions contemplated by this Agreement or (ii) cause the transactions contemplated by this Agreement to be rescinded following consummation, and no such judgment, order, decree, stipulation or injunction shall be in effect;

(d) the Buyer shall have delivered to the Seller the Buyer Certificate;

(e) the Seller shall have received such other certificates and instruments (including certificates of good standing of the Buyer in its jurisdiction of organization, certificates as to the incumbency of officers and the adoption of authorizing resolutions) as it shall reasonably request in connection with the Closing;

(f) Russ Monroe has entered into an employment agreement with the Buyer on terms satisfactory to each party to each such employment agreement; and

## ARTICLE V

### POST-CLOSING COVENANTS

5.1 Proprietary Information. From and after the Closing, Seller, unless required by legal process, shall not disclose or make use of (except to pursue its rights under this Agreement or the Ancillary Agreements and with respect to providing any information under this Agreement to its attorneys, accountants and other professionals), any knowledge, information or documents of a confidential nature or not generally known to the public with respect to Acquired Assets, the Seller's business or the Buyer or its business (including the financial information, technical information or data relating to the Seller's products and names of customers of the Seller), except to the extent that such knowledge, information or documents shall have become public knowledge other than through improper disclosure by the Seller and except to the extent such information (a) is known to the public and did not become so known through any violation of legal obligation on the part of any of the Seller; (b) is required to be disclosed under the provisions of any applicable law, or by any stock exchange or similar body; or (c) is required to be disclosed by a rule or order of any court of competent jurisdiction. Notwithstanding the foregoing, Buyer acknowledges and agrees that the Seller, and its owners, have developed relationships with the customers of the business of Seller, and their owners may maintain such relationships for purposes of commercial activities that do not violate Section 5.3.

5.2 Solicitation and Hiring. For a period of five (5) years after the Closing Date, Seller and each of the Members shall not, either directly or indirectly (including through an

Affiliate), (a) solicit or attempt to induce any Restricted Employee to terminate his or her employment with the Buyer or any subsidiary of the Buyer or (b) hire or attempt to hire any Restricted Employee; provided, that this clause (b) shall not apply to any individual whose employment with the Buyer or a subsidiary of the Buyer has been terminated for a period of six months or longer.

### 5.3 Non-Competition.

(a) For a period of five (5) years after the Closing Date, Seller and each of the Members shall not, either directly or indirectly as an owner, partner, officer, employee, director, investor, lender, consultant, independent contractor or otherwise, (i) design, develop, manufacture, market, sell or license any product or provide any service anywhere in the United States which is competitive with any product designed, developed (or under development), manufactured, sold or licensed or any service provided by the Seller within the three-year period prior to the Closing Date or (ii) engage anywhere in the United States in any business competitive with the business of the Seller as conducted as of the Closing Date or during the three-year period prior to the Closing Date. Notwithstanding anything contained in this Agreement to the contrary, in no event shall the Seller or any Member (i) have any obligation to ensure compliance by any other party with respect to this Section 5.3 or (ii) have any liability whatsoever for the breach of this Section 5.3 by any other party.

(b) Seller and each of the Members agree that the duration and geographic scope of the non-competition provision set forth in this Section 5.3 are reasonable. In the event that any court determines that the duration or the geographic scope, or both, are unreasonable and that such provision is to that extent unenforceable, the Parties agree that the provision shall remain in full force and effect for the greatest time period and in the greatest area that would not render it unenforceable. The Parties intend that this non-competition provision shall be deemed to be a series of separate covenants, one for each and every county of each and every state of the United States of America and each and every political subdivision of each and every country outside the United States of America where this provision is intended to be effective.

### 5.4 Tax Matters.

(a) All transfer taxes, deed excise stamps and similar charges related to the sale of the Acquired Assets contemplated by this Agreement shall be paid by the Seller.

(b) The Seller shall be responsible for all Tax liabilities attributable to its business prior to and including the Closing Date.

(c) The Buyer shall be responsible for all Taxes attributable to the conduct of its business after the Closing Date.

(d) The Buyer shall make available to the Seller and its representatives all records and materials reasonably required by the Seller to prepare, pursue or contest any Tax matters related to taxable periods (or portions thereof) ending on or before the Closing Date and shall provide reasonable cooperation to the Seller in such case. The Seller shall make available to the Buyer and its representatives all records and materials reasonably required by the Buyer to prepare, pursue or contest any Tax matters arising after the Closing which have factual reference to the pre-closing tax period and shall provide reasonable cooperation to the Buyer in such case.

---

### 5.5 Sharing of Data.

(a) The Seller shall have the right for a period of seven years following the Closing Date to have reasonable access to such books, records and accounts, including financial and tax information, correspondence, production records, employment records and other records that are transferred to the Buyer pursuant to the terms of this Agreement for the limited purposes of concluding its involvement in the business conducted by the Seller prior to the Closing Date and for complying with its obligations under applicable securities, tax, environmental, employment or other laws and regulations. The Buyer shall have the right for a period of seven years following the Closing Date to have reasonable access to those books, records and accounts, including financial and accounting records (and to the extent available, the work papers of the Seller's independent accountants), tax records, correspondence, production records, employment records and other records that are retained by the Seller pursuant to the terms of this Agreement to the extent that any of the foregoing is needed by the Buyer for the purpose of conducting the business of the Seller after the Closing and complying with its obligations under applicable securities, tax, environmental, employment or other laws and regulations. Neither the Buyer nor the Seller shall destroy any such books, records or accounts retained by it without first providing the other Party with the opportunity to obtain or copy such books, records, or accounts at such other Party's expense.

(b) Seller will cooperate with the Buyer's auditors and Seller's auditors to produce the financial information and statements necessary so that Buyer may comply with its federal, state and regulatory reporting requirements. Seller will respond to any reasonable requests made by the Buyer, the Buyer's auditors or the Seller's auditors promptly. Promptly upon request by the Buyer, the Seller shall authorize the release to the Buyer of all files pertaining to the Seller, the Acquired Assets or the business or operations of the Seller held by any federal, state, county or local authorities, agencies or instrumentalities. Seller understands that Buyer will suffer harm if it does not meet regulatory requirements regarding reporting of this transaction.

5.6 Use of Name. Seller shall not use the name Northeast Energy Partners or any name reasonably similar thereto after the Closing Date. Within 10 days following the Closing, the Seller shall amend its organizational documents and state filings, where appropriate, and other corporate records, if necessary, to comply with this provision.

5.7 Cooperation in Litigation. From and after the Closing Date, each Party shall fully cooperate with the other in the defense or prosecution of any litigation or proceeding already instituted or which may be instituted hereafter against or by such other Party relating to or arising out of the conduct of the business of the Seller or the Buyer prior to or after the Closing Date and related to the transaction contemplated by this Agreement (other than litigation among the Parties and/or their Affiliates arising out of the transactions contemplated by this Agreement). The Party requesting such cooperation shall pay the reasonable out-of-pocket expenses incurred in providing such cooperation (including legal fees and disbursements) by the Party providing such cooperation and by its officers, directors, employees and agents.



#### 5.8 Assignment of Supplier Agreements.

(a) Notwithstanding anything to the contrary herein, only those Supplier Agreements that may be assigned or transferred without the consent of a third party are being assigned to the Buyer as of the Closing Date. Instead, the Seller will use its Commercially Reasonable Efforts to collect any and all amounts due to the Seller pursuant to the Supplier Agreements. The Seller will direct all suppliers making payments pursuant to the Supplier Agreements to remit payment directly to a lockbox that will be established with Silicon Valley Bank pursuant to a lockbox agreement (the "Supplier Agreement Lockbox"). The Seller agrees that it shall forward promptly to the Buyer any monies, checks or instruments received by the Seller after the Closing Date (a) pursuant to Supplier Agreements and (b) related to items earned, invoiced or to be invoiced after October 1, 2012. The Seller shall provide to the Buyer such reasonable assistance as the Buyer may request with respect to the collection of any such accounts receivable, provided the Buyer pays the reasonable out-of-pocket expenses of the Seller and its officers, directors and employees incurred in providing such assistance. Effective as of the Closing, the Seller hereby grants to the Buyer a power of attorney for the sole purpose of endorsing and cashing any checks or instruments payable or endorsed to the Seller or its order which are received by the Buyer and which relate to accounts receivable purchased by the Buyer from the Seller.

(b) If and to the extent that after the Closing Date, Buyer collects revenue pursuant to Any Supplier Agreement that relates to an invoice generated prior to October 1, 2012, Buyer shall remit such amounts to Seller within thirty (30) days after the end of the calendar month in which such amounts were received along with such schedules it has prepared to support the determination of such amount. Seller shall have the right at its expense to examine those financial records of Buyer as may be reasonably necessary to confirm the accuracy of the schedules provided to Seller and any calculations or payments made by Buyer hereunder. The Buyer will afford Seller access to the records during normal business hours, upon reasonable advance notice given by the Seller, and subject to such reasonable limitations as the Buyer may impose to delete competitively sensitive or privileged information.

5.9 Employees. Effective as of the Closing, the Seller shall terminate the employment of each of its employees. The Buyer shall be permitted to offer employment to each such employee, terminable at the will of the Buyer. The Seller hereby consents to the hiring of any such employees by the Buyer and waives, with respect to the employment by the Buyer of such employees, any claims or rights the Seller may have against the Buyer or any such employee under any non-competition, confidentiality or employment agreement.

#### 5.10 Third-Party Notices and Consents.

(a) The Seller shall use its Reasonable Best Efforts to obtain, at its expense, all such waivers, consents or approvals from third parties, and to give all such notices to third parties, as listed or are required to be listed in the Disclosure Schedule.

(b) If (i) any of the Assigned Contracts or other assets or rights constituting Acquired Assets may not be assigned and transferred by the Seller to the Buyer (as a result of either the provisions thereof or applicable law) without the consent or approval of a third party, (ii) the Seller, after using its Reasonable Best Efforts, is unable to obtain such consent or approval

prior to the Closing and (iii) the Closing occurs nevertheless, then (A) such Assigned Contracts and/or other assets or rights shall not be assigned and transferred by the Seller to the Buyer at the Closing and the Buyer shall not assume the Seller's liabilities with respect thereto at the Closing, (B) the Seller shall continue to use its Reasonable Best Efforts to obtain the necessary consent or approval as soon as practicable after the Closing, and (C) upon the obtaining of such consent or approval, the Buyer and the Seller shall execute such further instruments of conveyance (in substantially the form executed at the Closing) as may be necessary to assign and transfer such Assigned Contracts and/or other assets or rights (and the associated liabilities and obligations of the Seller) to the Buyer.

#### 5.11 Curb Energy and Rate Droppers Asset Purchase Agreement

The Buyer and Curb Energy, LLC and Rate Droppers, LLC shall negotiate in good faith to enter into an asset purchase agreement acceptable to Buyer, Seller and Curb Energy, LLC and Rate Droppers, LLC within thirty (30) days of the Closing Date on mutually agreeable terms.

#### 5.12 Insurance Coverage

Seller shall obtain, at Seller's expense, within thirty (30) days of the Closing Date a policy for tail coverage for its existing employee practices insurance policy for a period of twelve (12) months from the Closing Date.

#### 5.13 Connecticut Light and Power

Seller will continue to pay the electricity invoice from Connecticut Light and Power for the Leased Premises, and Buyer will reimburse Buyer for such amounts within ten (10) days of receipt of an invoice from Seller.

### **ARTICLE VI**

#### **INDEMNIFICATION**

**6.1 Indemnification by the Seller.** The Seller and its Members shall jointly and severally indemnify Buyer (and its officers, directors and affiliates) in respect of, and hold the Buyer (and its officers, directors and affiliates) harmless against, Damages incurred or suffered by the Buyer or any Affiliate thereof resulting from, relating to or constituting:

(a) any breach, as of the date of this Agreement, of any representation or warranty of any Seller contained in this Agreement, any Ancillary Agreement or any other agreement or instrument furnished by Seller to the Buyer pursuant to this Agreement;

(b) any failure to perform any covenant or agreement of Seller contained in this Agreement, any Ancillary Agreement or any agreement or instrument furnished by Seller to the Buyer pursuant to this Agreement;

(c) any Retained Liabilities; and/or

(d) the operation of its business or the Acquired Assets prior to the Closing Date.

6.2 Indemnification by the Buyer. The Buyer shall indemnify the Seller in respect of, and hold it harmless against, any and all Damages incurred or suffered by the Seller resulting from, relating to or constituting:

(a) any breach, as of the date of this Agreement, of any representation or warranty of the Buyer contained in this Agreement, any Ancillary Agreement or any other agreement or instrument furnished by the Buyer to the Seller pursuant to this Agreement;

(b) any failure to perform any covenant or agreement of the Buyer contained in this Agreement, any Ancillary Agreement or any other agreement or instrument furnished by the Buyer to the Seller pursuant to this Agreement;

(c) any Assumed Liabilities; and/or

(d) operation of its business or the Acquired Assets after the Closing Date.

6.3 Indemnification Procedure.

(a) In the event that any Legal Proceedings shall be instituted or that any claim or demand (" Claim ") shall be asserted by any Person in respect of which payment may be sought under Section 6.1 and 6.2 hereof (regardless of the limitations set forth in Section 6.4 ), the Indemnified Party shall reasonably and promptly cause written notice of the assertion of any Claim of which it has knowledge which is covered by this indemnity to be forwarded to the Indemnifying Party. The Indemnifying Party shall have the right, at its sole option and expense, to be represented by counsel of its choice, which must be reasonably satisfactory to the Indemnified Party, and to defend against, negotiate, settle or otherwise deal with any Claim which relates to any Damages indemnified against hereunder. If the Indemnifying Party elects to defend against, negotiate, settle or otherwise deal with any Claim which relates to any Damages indemnified against hereunder, it shall within thirty (30) days (or sooner, if the nature of the Claim so requires) notify the Indemnified Party of its intent to do so. If the Indemnifying Party elects not to defend against, negotiate, settle or otherwise deal with any Claim which relates to any Damages indemnified against hereunder, the Indemnified Party may defend against, negotiate, settle or otherwise deal with such Claim. If the Indemnifying Party shall assume the defense of any Claim, the Indemnified Party may participate, at his or its own expense, in the defense of such Claim. The parties hereto agree to cooperate fully with each other in connection with the defense, negotiation or settlement of any such Claim. Notwithstanding anything in this Section 6.3 to the contrary, neither the Indemnifying Party nor the Indemnified Party shall, without the written consent of the other party, settle or compromise any indemnifiable Claim or permit a default or consent to entry of any judgment unless the claimant and such party provide to such other party an unqualified release from all liability in respect of the indemnifiable Claim. Notwithstanding the foregoing, if a settlement offer is made by the applicable third party claimant, and the Indemnifying Party notifies the Indemnified Party in writing of the Indemnifying Party's willingness to accept the settlement offer and, subject to the applicable limitations of Section 6.4 , pay the amount called for by such offer, and the Indemnified Party

declines to accept such offer, the Indemnified Party may continue to contest such indemnifiable Claim, free of any participation by the Indemnifying Party, and the amount of any ultimate liability with respect to such Indemnifiable Claim that the Indemnifying Party has an obligation to pay hereunder shall be limited to the amount of the settlement offer.

(b) After any final judgment or award shall have been rendered by a Governmental Body of competent jurisdiction and the expiration of the time in which to appeal therefrom, or a settlement shall have been consummated, or the Indemnified Party and the Indemnifying Party shall have arrived at a mutually binding agreement with respect to a Claim hereunder, the Indemnified Party shall forward to the Indemnifying Party notice of any sums due and owing by the Indemnifying Party pursuant to this Agreement with respect to such matter.

**6.4 Survival of Representations and Warranties.** The representations and warranties of the Parties shall (a) survive Closing and (b) shall expire eighteen (18) months after the Closing Date, except that (i) the representations and warranties set forth in Sections 2.1 and 2.2 shall survive the Closing without limitation, and (ii) the representations and warranties set forth in Section 2.9, 2.10(a), 2.20 and 2.21 shall survive until 30 days following the expiration of the statute of limitations applicable to the matters referred to within each such section. If an Indemnified Party delivers to an Indemnifying Party, before expiration of a representation or warranty, a notice of a Claim based upon a breach of such representation or warranty, then the applicable representation or warranty shall survive until, but only for purposes of, the resolution of any claims arising from or related to the matter covered by such notice. The rights to indemnification set forth in this Article VI shall not be affected by (i) any investigation conducted by or on behalf of an Indemnified Party or any knowledge acquired (or capable of being acquired) by an Indemnified Party, whether before or after the date of this Agreement, with respect to the inaccuracy or noncompliance with any representation, warranty, covenant or obligation which is the subject of indemnification hereunder or (ii) any waiver by an Indemnified Party of any closing condition relating to the accuracy of any representations and warranties or the performance of or compliance with agreements and covenants.

**6.5 Exclusive Remedy and Set-Off.**

(a) Except with respect to claims based on fraud, after the Closing, the rights of the Indemnified Parties under this Article VI shall be the exclusive remedy of the Indemnified Parties with respect to claims resulting from or relating to any misrepresentation, breach of warranty or failure to perform any covenant or agreement contained in this Agreement.

(b) The Seller and the Buyer hereby agree that should the Buyer be entitled to indemnification under Section 6.1 of this Agreement, the Buyer shall first set off the outstanding indebtedness evidenced by the Seller Note and the Earnout against any and all obligations of the Seller and the Members arising under Section 6.1 of this Agreement. The Buyer shall not attempt to collect any Damages directly from the Seller and/or any of the Members unless and until it has exhausted all set off rights with respect to the Seller Note and the Earnout.

**6.6. Certain Limitations on Indemnification.**

(a) Notwithstanding the provisions of this Article VI, neither Seller nor Buyer shall have any indemnification obligations for Damages pursuant to Section 6.1 or 6.2, unless the aggregate amount of all such Damages finally determined for which such party would be liable, but for this paragraph (a) exceeds \$50,000 (the "Basket"), and in such event, the Indemnifying Party shall then be required to pay the total amount of such Damages in excess of the Basket, and subject to the Cap, provided that such limitation shall not apply to Seller's breach of Section 2.9.

(b) None of the Seller Parties or the Buyer shall be required to indemnify any Person for Damages pursuant to Section 6.1 or 6.2 for an aggregate amount of all such Damages exceeding \$2,500,000.00 provided that such limitation shall not apply to claims based on fraud. (the "Cap").

6.7 Treatment of Indemnity Payments. Any payments made to an Indemnified Party pursuant to this Article VI shall be treated as an adjustment to the Purchase Price for tax purposes.

## ARTICLE VIII

### DEFINITIONS

For purposes of this Agreement, each of the following terms shall have the meaning set forth below.

"Acquired Assets" shall mean all of the assets, properties and rights of the Seller existing as of the Closing, except to the extent included in the definition of Excluded Assets and to the extent assignable, including:

(a) all trade and other accounts receivable that are payable to the Seller, and all rights to unbilled amounts for products delivered or services provided, together with any security held by the Seller for the payment thereof;

(b) all computers, machinery, equipment, tools and tooling, furniture, fixtures, supplies, leasehold improvements, and other tangible personal property;

(c) all Intellectual Property, if any;

(d) all rights under Assigned Contracts to the extent assignable;

(e) all claims, prepayments, deposits, refunds, causes of action, choses in action, rights of recovery, rights of setoff and rights of recoupment;

(f) all Permits to the extent assignable;

(g) all books, records, accounts, ledgers, files, documents, correspondence, lists (including customer and prospect lists), employment records, manufacturing and procedural manuals, Intellectual Property records, sales and promotional materials, studies, reports and other printed or written materials;