

PIONEER POWER SOLUTIONS, INC.

Form 10-Q

November 13, 2017

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-Q**

**(Mark One)**

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

**For the quarterly period ended September 30, 2017**

**OR**

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

**Commission file number: 001-35212**

**PIONEER POWER SOLUTIONS, INC.**

**(Exact name of registrant as specified in its charter)**

**Delaware**

**27-1347616**

(State of incorporation) (I.R.S. Employer Identification No.)

**400 Kelby Street, 12th Floor**

**Fort Lee, New Jersey 07024**

(Address of principal executive offices)

**(212) 867-0700**

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter 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 definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act (Check one):

Large accelerated filer	Accelerated filer
Non-accelerated filer	(Do not check if a smaller reporting company)
Smaller reporting company	Emerging growth company

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

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

The number of shares outstanding of the registrant's common stock, \$0.001 par value, as of November 13, 2017 was 8,726,045.

**PIONEER POWER SOLUTIONS, INC.**

**Form 10-Q**

**For the Quarter Ended September 30, 2017**

**TABLE OF CONTENTS**

**PART I. FINANCIAL INFORMATION**

	Page
<u>Item 1. Financial Statements</u>	1
<u>Unaudited Consolidated Statements of (Loss) Income for the Three and Nine Months Ended September 30, 2017 and 2016</u>	1
<u>Unaudited Consolidated Statements of Comprehensive (Loss) Income for the Three and Nine Months Ended September 30, 2017 and 2016</u>	2
<u>Consolidated Balance Sheets at September 30, 2017 (unaudited) and December 31, 2016</u>	3
<u>Unaudited Consolidated Statements of Cash Flows for the Nine Months Ended September 30, 2017 and 2016</u>	4
<u>Notes to Unaudited Consolidated Financial Statements</u>	5
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	16
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	26
<u>Item 4. Controls and Procedures</u>	26

**PART II. OTHER INFORMATION**

<u>Item 1. Legal Proceedings</u>	27
<u>Item 1A. Risk Factors</u>	27
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	27
<u>Item 3. Defaults Upon Senior Securities</u>	27
<u>Item 4. Mine Safety Disclosures</u>	27
<u>Item 5. Other Information</u>	27
<u>Item 6. Exhibits</u>	28
<u>Signatures</u>	29

**PART I – FINANCIAL INFORMATION****Item 1. FINANCIAL STATEMENTS****PIONEER POWER SOLUTIONS, INC.****Consolidated Statements of (Loss) Income****(In thousands, except per share data)****(Unaudited)**

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Revenues	\$ 29,794	\$ 29,389	\$ 87,953	\$ 85,889
Cost of goods sold				
Cost of goods sold	23,475	22,872	69,547	67,248
Restructuring and integration	873	—	873	—
Total cost of goods sold	24,348	22,872	70,420	67,248
Gross profit	5,446	6,517	17,533	18,641
Operating expenses				
Selling, general and administrative	5,041	5,338	14,455	14,894
Restructuring and integration	—	19	160	199
Foreign exchange gain	(194 )	(52 )	(465 )	(142 )
Total operating expenses	4,847	5,305	14,150	14,951
Operating Income	599	1,212	3,383	3,690
Interest expense	588	556	1,662	1,151
Other expense	245	264	647	554
(Loss) / income before taxes	(234 )	392	1,074	1,985
Income tax expense	530	70	396	900
Net (loss) / income	\$ (764 )	\$ 322	\$ 678	\$ 1,085
Net (loss) / income per common share:				
Basic	\$ (0.09 )	\$ 0.04	\$ 0.08	\$ 0.12
Diluted	\$ (0.09 )	\$ 0.04	\$ 0.08	\$ 0.12
Weighted average common shares outstanding:				
Basic	8,725	8,700	8,713	8,700
Diluted	8,725	8,708	8,727	8,708

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

**PIONEER POWER SOLUTIONS, INC.****Consolidated Statements of Comprehensive (Loss) Income****(In thousands)****(Unaudited)**

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Net (loss) / income	\$ (764 )	\$ 322	\$ 678	\$ 1,085
Other comprehensive (loss) / income				
Foreign currency translation adjustments	—	(147 )	68	445
Amortization of net prior service costs and net actuarial gains / (losses), net of tax	(42 )	32	(15 )	(109 )
Other comprehensive (loss) / income	(42 )	(115 )	53	336
Comprehensive (loss) / income	\$ (806 )	\$ 207	\$ 731	\$ 1,421

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

**PIONEER POWER SOLUTIONS, INC.****Consolidated Balance Sheets****(In thousands, except share data)**

	September 30, 2017 <b>(Unaudited)</b>	December 31, 2016
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	\$ 950	\$ 246
Accounts receivable, net	19,255	17,508
Inventories, net	28,324	26,147
Income taxes receivable	546	72
Prepaid expenses and other current assets	2,765	2,215
Total current assets	51,840	46,188
Property, plant and equipment, net	7,025	6,591
Deferred income taxes	5,913	5,659
Other assets	216	830
Intangible assets, net	6,783	8,168
Goodwill	9,972	9,972
Total assets	\$ 81,749	\$ 77,408
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities		
Bank overdrafts	\$ 1,386	\$ 1,200
Revolving credit facilities	20,197	17,689
Short term borrowings	5,339	3,973
Accounts payable and accrued liabilities	18,205	18,139
Current maturities of long-term debt	4,926	1,379
Income taxes payable	1,619	1,360
Total current liabilities	51,672	43,740
Long-term debt, net of current maturities	—	4,005
Pension deficit	173	172
Other long-term liabilities	582	892
Noncurrent deferred income taxes	1,954	2,400
Total liabilities	54,381	51,209
Stockholders' equity		
Preferred stock, \$0.001 par value, 5,000,000 shares authorized; none issued	—	—
Common stock, \$0.001 par value, 30,000,000 shares authorized; 8,726,045 shares issued and outstanding on September 30, 2017 and 8,699,712 shares issued and outstanding on December 31, 2016	9	9
Additional paid-in capital	23,653	23,215



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Accumulated other comprehensive loss	(5,810 )	(5,863 )
Retained earnings	9,516	8,838
Total stockholders' equity	27,368	26,199
Total liabilities and stockholders' equity	\$ 81,749	\$ 77,408

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

**PIONEER POWER SOLUTIONS, INC.****Consolidated Statements of Cash Flows****(In thousands)****(Unaudited)**

	Nine Months Ended September 30,	
	2017	2016
Operating activities		
Net income	\$ 678	\$ 1,085
Depreciation	956	1,006
Amortization of intangible assets	1,390	1,309
Amortization of debt issuance cost	185	153
Deferred income taxes	(689 )	206
Change in receivable reserves	53	250
Change in inventory reserves	38	(435 )
Accrued pension	(24 )	(68 )
Stock-based compensation	319	34
(Gain) / loss on disposition of fixed assets	(5 )	77
Foreign currency remeasurement (gain) / loss	(40 )	2
Changes in current operating assets and liabilities:		
Accounts receivable	(1,434 )	(4,188 )
Inventories	(1,678 )	(8,455 )
Prepaid expenses and other assets	76	(378 )
Income taxes	(289 )	890
Accounts payable and accrued liabilities	(9 )	(348 )
Net cash used in operating activities	(473 )	(8,860 )
Investing activities		
Additions to property, plant and equipment	(1,245 )	(476 )
Proceeds from sale of fixed assets	20	7
Net cash used in investing activities	(1,225 )	(469 )
Financing activities		
Increase / (decrease) in bank overdrafts	162	(922 )
Increase / (decrease) of short term borrowings	1,365	4,919
Borrowings under debt agreement	31,919	30,413
Repayment of debt	(30,465 )	(24,564 )
Payment of debt issuance costs	(157 )	(226 )
Proceeds from the exercise of options for common stock	120	—
Net cash provided by financing activities	2,944	9,620

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Increase in cash and cash equivalents	1,246	291
Effect of foreign exchange on cash and cash equivalents	(542 )	(102 )
Cash and cash equivalents		
Beginning of period	246	648
End of period	\$ 950	\$ 837

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

**PIONEER POWER SOLUTIONS, INC.**

**Notes to Consolidated Financial Statements**

**September 30, 2017 (unaudited)**

**1. BASIS OF PRESENTATION**

**Overview**

Pioneer Power Solutions, Inc. and its wholly-owned subsidiaries (referred to herein as the “Company,” “Pioneer,” “we,” “our” and “us”) manufacture, sell and service a broad range of specialty electrical transmission, distribution and on-site power generation equipment for applications in the utility, industrial, commercial and backup power markets. The Company is headquartered in Fort Lee, New Jersey and operates from thirteen additional locations in the U.S., Canada and Mexico for manufacturing, centralized distribution, engineering, sales and administration.

We have two reportable segments as defined in our Annual Report on Form 10-K for the year ended December 31, 2016, as filed with the Securities and Exchange Commission (the “SEC”) on March 29, 2017: Transmission and Distribution Solutions (“T&D Solutions”) and Critical Power Solutions (“Critical Power”).

**Presentation**

The accompanying unaudited consolidated financial statements of the Company have been prepared pursuant to the rules of the SEC and reflect the accounts of the Company as of September 30, 2017. Certain information and footnote disclosures, normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the United States (“U.S. GAAP”), have been condensed or omitted pursuant to those rules and regulations. We believe that the disclosures made are adequate to make the information presented not misleading to the reader. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, necessary to fairly state the financial position, results of operations and cash flows with respect to the interim consolidated financial statements have been included. The results of operations for the interim period are not necessarily indicative of the results for the entire fiscal year. The year-end balance sheet data was derived from audited financial statements, but does not include all disclosures required by U.S. GAAP for a year-end balance sheet.

All dollar amounts (except share and per share data) presented in the notes to our unaudited consolidated financial statements are stated in thousands of dollars, unless otherwise noted. Amounts may not foot due to rounding.

These unaudited consolidated financial statements include the accounts of Pioneer and its wholly-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation. As further described in the two paragraphs below, certain prior year amounts have been reclassified to conform to the current year presentation.

As the Company continues to implement the remediation plans discussed under the heading “Part I – Item 4. Controls and Procedures” of this Quarterly Report on Form 10-Q, the Company has determined that there were inconsistencies in classification of expenses between its business units in the reporting periods prior to December 31, 2016. As a result, the company reclassified certain expenses from operating expenses to cost of goods sold for the year ended December 31, 2016, as previously disclosed in the Annual Report on Form 10-K filed with the SEC on March 29, 2017, and for the three and nine months ended September 30, 2016, resulting in a decrease to gross profit of \$18, or negative 0.06% as a percentage of sales for the three months ended September 30, 2016 and, resulting in a decrease to gross profit of \$262, or negative 0.30% as a percentage of sales for the nine months ended September 30, 2016, respectively.

These unaudited consolidated financial statements should be read in conjunction with the risk factors and the audited consolidated financial statements and notes thereto of the Company and its subsidiaries included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2016.

## **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The Company’s significant accounting policies are described in Note 2 to the audited consolidated financial statements included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2016. There have been no significant changes in the Company’s accounting policies during the third quarter of 2017.

### **Recent Accounting Pronouncements**

*Revenue from Contracts with Customers.* In May 2014, the FASB issued Accounting Standards Update No. 2014-09 (“ASU 2014-09”), which supersedes nearly all existing revenue recognition guidance under U.S. GAAP. The core principle of ASU 2014-09 is to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration to which an entity expects to be entitled for those goods or services. ASU 2014-09 defines a five step process to achieve this core principle and, in doing so, more judgment and estimates may

be required within the revenue recognition process than are required under existing U.S. GAAP.

In July 2015, the FASB made a decision to defer the effective date of the new standard for one year and permit early adoption as of the original effective date. The Company is currently reviewing its various revenue streams from its two reportable segments: (i) T&D Solutions and (ii) Critical Power. Concurrently, through the use of various data gathering methods, we are categorizing the types of sales for our business units for the purpose of comparing how we currently recognize revenue and quantifying the impact, if any, that this new standard will have on our consolidated financial statements. The Company plans to elect to apply the modified retrospective approach upon adoption. Additionally, the new guidance requires enhanced disclosures about the nature, amount, timing, and uncertainty of revenue and cash flows arising from customer contracts, including revenue recognition policies to identify performance obligations, assets recognized from costs incurred to obtain and fulfill a contract, and significant judgments in measurement and recognition. The Company is determining the impact of adopting Topic 606 on its revenue recognition policies, procedures and control framework and the resulting impact on its consolidated financial position, results of operation and cash flows. The Company is in the process of reviewing revenue sources and evaluating the customer population to determine the appropriate distribution of customer accounts into populations with similar contract terms and performance obligations. We expect to complete this process before the filing of our Form 10-K for the year ended December 31, 2017.

*Simplifying the Measurement of Inventory.* In July 2015, the FASB issued ASU No. 2015-11, Inventory (Topic 330): Simplifying the Measurement of Inventory. This standard amends Topic 330, Inventory, which currently requires an entity to measure inventory at the lower of cost or market. Market could be replacement cost, net realizable value, or net realizable value less an approximately normal profit margin. When this standard is adopted, an entity should measure in scope inventory at the lower of cost and net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. The amendments are effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. The Company adopted ASU No. 2015-11 in 2017 and has reflected the impact in the current year's consolidated financial statements.

*Leases.* In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*, which requires, among other things, a lessee to recognize a liability representing future lease payments and a right-of-use asset representing its right to use the underlying asset for the lease term. For operating leases, a lessee will be required to recognize at inception a right-of-use asset and a lease liability equal to the net present value of the lease payments, with lease expense recognized over the lease term on a straight-line basis. For leases with a term of twelve months or less, ASU 2016-02 allows a reporting entity to make an accounting policy election to not recognize a right-of-use asset and a lease liability, and to recognize lease expense on a straight-line basis. ASU No. 2016-02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years, with early adoption permitted. Upon adoption, a reporting entity should apply the provisions of ASU 2016-02 at the beginning of the earliest period presented using a modified retrospective approach, which includes certain optional practical expedients that an entity may elect to apply. The Company is evaluating the potential impact of adopting ASU 2016-02 on its consolidated financial statements. It is expected that upon adoption we will show a significant increase in assets and corresponding liabilities.

*Share-Based Compensation.* In April 2016, the FASB issued ASU No. 2016-09, “Compensation-Stock Compensation (Topic 718), Improvements to Employee Share-Based Payment Accounting”. Under ASU No. 2016-09, companies will no longer record excess tax benefits and certain tax deficiencies in additional paid-in capital (“APIC”). Instead, they will record all excess tax benefits and tax deficiencies as income tax expense or benefit in the income statement and the APIC pools will be eliminated. In addition, ASU No. 2016-09 eliminates the requirement that excess tax benefits be realized before companies can recognize them. ASU No. 2016-09 also requires companies to present excess tax benefits as an operating activity on the statement of cash flows rather than as a financing activity. Furthermore, ASU No. 2016-09 will increase the amount an employer can withhold to cover income taxes on awards and still qualify for the exception to liability classification for shares used to satisfy the employer’s statutory income tax withholding obligation. An employer with a statutory income tax withholding obligation will now be allowed to withhold shares with a fair value up to the amount of taxes owed using the maximum statutory tax rate in the employee’s applicable jurisdiction(s). ASU No. 2016-09 requires a company to classify the cash paid to a tax authority when shares are withheld to satisfy its statutory income tax withholding obligation as a financing activity on the statement of cash flows. Under current GAAP, it was not specified how these cash flows should be classified. In addition, companies will now have to elect whether to account for forfeitures on share-based payments by (1) recognizing forfeitures of awards as they occur or (2) estimating the number of awards expected to be forfeited and adjusting the estimate when it is likely to change, as is currently required. The Amendments of this ASU are effective for reporting periods beginning after December 15, 2016, with early adoption permitted but all of the guidance must be adopted in the same period. The Company adopted ASU No. 2016-09 in 2017. The adoption of the new guidance did not materially affect the Company’s financial position, results of operations or cash flows.

*Statement of Cash Flows.* In August 2016, the FASB issued ASC Update No. 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*. The purpose of Update No. 2016-15 is to reduce the diversity in practice in presentation and classification of the following items within the statement of cash flows: debt prepayments or debt extinguishment costs, settlement of zero coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing, contingent consideration payments made after a business combination, proceeds from the settlement of insurance claims, proceeds from the settlement of corporate-owned life insurance policies, distributions received from equity method investments and beneficial interests in securitization transactions. It also addresses classification of transactions that have characteristics of more than one class of cash flows. Update No. 2016-15 is effective for annual periods beginning after December 15, 2017, and a retrospective transition method is required. We do not expect the adoption to have a material impact on our consolidated statements of cash flows for 2016 or 2017.



*Simplifying the Test for Goodwill Impairment.* In January 2017, the FASB issued ASU No. 2017-04, “Simplifying the Test for Goodwill Impairment.” This standard was established to simplify how an entity is required to test goodwill for impairment by eliminating Step 2 from the goodwill impairment test. Step 2 measures a goodwill impairment loss by comparing the implied fair value of a reporting unit’s goodwill with the carrying amount of that goodwill. Under the amendments in this Update, an entity should perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An entity should recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit’s fair value; however, the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. Additionally, an entity should consider income tax effects from any tax deductible goodwill on the carrying amount of the reporting unit when measuring the goodwill impairment loss, if applicable. The FASB also eliminated the requirements for any reporting unit with a zero or negative carrying amount to perform a qualitative assessment and, if it fails that qualitative test, to perform Step 2 of the goodwill impairment test. Therefore, the same impairment assessment applies to all reporting units. An entity is required to disclose the amount of goodwill allocated to each reporting unit with a zero or negative carrying amount of net assets. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary. The company will early adopt this standard during the fourth quarter of 2017 in conjunction with our goodwill impairment assessment.

### 3. OTHER EXPENSE

Other expense in the consolidated statements of income for the three and nine months ended September 30, 2017 and 2016, respectively, are as follows:

	Three Months Ended September 30,		Nine Months Ending September 30,	
	2017	2016	2017	2016
Payroll tax interest and penalties accrued	\$ 40	\$ 68	\$ 28	\$ 23
Other non-operating expenses	205	196	619	531
Other expense	\$ 245	\$ 264	\$ 647	\$ 554

The Company continues to record interest on past due and unpaid payroll tax obligations. During the nine months ended September 30, 2017 and 2016, the Company received waivers of certain interest and penalties on these obligations totaling \$0.1 million and \$0.4 million, respectively.

### 4. INVENTORIES

The components of inventories are summarized below:

	September 30, 2017 (Unaudited)	December 31, 2016
Raw materials	\$ 10,116	\$ 10,175
Work in process	7,453	6,535
Finished goods	11,152	9,826
Provision for excess and obsolete inventory	(397 )	(389 )
Total inventories	\$ 28,324	\$ 26,147

Included in raw materials and finished goods at September 30, 2017 and December 31, 2016 are goods in transit of approximately \$3.1 million.

At September 30, 2017 and December 31, 2016, raw materials not pledged to our secured creditor were used as collateral to secure short term borrowings under a product financing agreement amounting to \$5.3 million and \$4.0 million, respectively.

**5. PROPERTY, PLANT AND EQUIPMENT**

Property, plant and equipment are summarized below:

	September <b>2017</b> <b>(Unaudited)</b>	December 31, 2016
Land	\$ 50	\$ 46
Buildings	2,467	2,293
Machinery and equipment	10,656	9,421
Furniture and fixtures	476	466
Computer hardware and software	1,364	1,289
Leasehold improvements	715	534
Construction in progress	18	18
	15,746	14,067
Less: Accumulated depreciation	(8,721 )	(7,476 )
Total property, plant and equipment, net	\$ 7,025	\$ 6,591

Depreciation expense was \$1.0 million in the nine months ended September 30, 2017 and 2016.

**6. OTHER ASSETS**

In December 2011 and January 2012, the Company made two loans, each in the amount of \$0.3 million to a developer of a renewable energy project in the U.S. The promissory notes accrue interest at a rate of 4.5% per annum with a final payment of all unpaid principal and interest becoming fully due and payable upon the earlier to occur of (i) the four year anniversary of the issuance date of the promissory notes, or (ii) an event of default. As defined in the promissory notes, an event of default includes, but is not limited to, the following: any bankruptcy, reorganization or similar proceeding involving the borrower, a sale or transfer of substantially all the assets of the borrower, a default by the borrower relating to any indebtedness due to third parties, the incurrence of additional indebtedness by the borrower without the Company's written consent and failure of the borrower to perform its obligations pursuant to its other agreements with the Company, including its purchase order for pad mount transformers. The principal balance of the loan receivable is outstanding at September 30, 2017 and December 31, 2016. The Company expects to fully recover these amounts. At September 30, 2017, the Company has classified the principal of \$0.6 million to other current assets as the Company anticipates the settlement of both notes in the next twelve months based upon negotiations with the debtor.

Included in Other Assets at September 30, 2017 and December 31, 2016 is a customer note receivable of \$0.2 million.

## 7. GOODWILL AND OTHER INTANGIBLE ASSETS

There were no changes in the carrying values of goodwill for the nine months ended September 30, 2017.

	T&D Solutions Segment	Critical Power Solutions Segment	Total Goodwill
Gross Goodwill:			
Balance as of January 1, 2017	\$ 7,978	\$ 2,970	\$ 10,948
No activity	—	—	—
Balance as of September 30, 2017	\$ 7,978	\$ 2,970	\$ 10,948
Accumulated impairment losses:			
Balance as of January 1, 2017	\$ (976 )	\$ —	\$ (976 )
No activity	—	—	—
Balance as of September 30, 2017	\$ (976 )	\$ —	\$ (976 )
<b>Net Goodwill as of September 30, 2017</b>	<b>\$ 7,002</b>	<b>\$ 2,970</b>	<b>\$ 9,972</b>

Changes in the carrying values of intangible assets for the nine months ended September 30, 2017, were as follows:

	T&D Solutions Segment	Critical Power Solutions Segment	Total Intangible Assets
Balance as of January 1, 2017	5,565	2,603	8,168
Amortization	(312 )	(1,078 )	(1,390 )
Foreign currency translation	5	—	5
Balance as of September 30, 2017	\$ 5,258	\$ 1,525	\$ 6,783

The components of intangible assets as of September 30, 2017 are summarized below:

	Weighted Average Amortization Years	Gross Carrying Amount	Accumulated Amortization	Foreign Currency Translation	Net Book Value
Customer relationships	7	\$ 7,201	\$ (4,571 )	\$ —	\$ 2,630

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Non-compete agreements	6	705	(459 )	—	246
Trademarks	Indefinite	1,816	—	—	1,816
Distributor territory license	4	474	(474 )	—	—
Internally developed software	7	289	(114 )	—	175
Developed technology	10	492	(135 )	—	357
Technology-related industry accreditations	Indefinite	1,575	—	(16 )	1,559
Total intangible assets		\$ 12,552	\$ (5,753 )	\$ (16 )	\$ 6,783

The Company accelerated and fully amortized the distributor territory license intangible asset upon the termination of its distribution agreement with a supplier during the quarter ended September 30, 2017.

## 8. DEBT

### *Canadian Credit Facilities*

Our Canadian subsidiaries have maintained credit facilities with BMO since October 2009. In June 2011, our wholly owned subsidiary Pioneer Electrogrouop Canada Inc. entered into a letter loan agreement with BMO (the “Initial Canadian Facilities”) that replaced and superseded all of our businesses’ prior financing arrangements with the bank.

Our Initial Canadian Facilities originally provided for up to \$22.0 million Canadian dollars (“CAD”) (approximately \$15.9 million expressed in U.S. dollars) consisting of a \$10.0 million CAD demand revolving credit facility (“Facility A”) to finance ongoing operations, a \$2.0 million CAD term credit facility (“Facility B”) that financed a plant expansion, and a \$10.0 million CAD term credit facility (“Facility C”) that financed a business acquisition and the purchase and expansion of its manufacturing facilities.

The Initial Canadian Facilities required us to comply on a consolidated Canadian basis with various financial covenants, including maintaining a minimum fixed charge coverage ratio, a maximum funded debt to EBITDA ratio and a limitation on funded debt as a percent of capitalization.

Facility A was originally subject to margin criteria and borrowings bore interest at BMO’s prime rate plus 0.50% per annum on amounts borrowed in Canadian dollars, or its U.S. base rate plus 0.50% per annum or LIBOR plus 2.00% per annum on amounts borrowed in U.S. dollars.

Borrowings under Facility B originally bore interest at BMO’s prime rate plus 1.00% per annum with principal repayments becoming due on a five year amortization schedule.

Borrowings under Facility C were repayable according to a five year principal amortization schedule and bore interest at the following rates: if the funded debt to EBITDA ratio is equal to or greater than 2.00, BMO’s prime rate plus 1.25% per annum on amounts borrowed in Canadian dollars, or its U.S. base rate plus 1.25% per annum or LIBOR plus 2.50% per annum on amounts borrowed in U.S. dollars; or, if the funded debt to EBITDA ratio is less than 2.00, BMO’s prime rate plus 1.00% per annum on amounts borrowed in Canadian dollars, or its U.S. base rate plus 1.00% per annum or LIBOR plus 2.25% per annum on amounts borrowed in U.S. dollars. In addition, Facility C was subject to a standby fee which is calculated monthly using the unused portion of the facility at either 0.625% per annum if the funded debt to EBITDA ratio is equal to or greater than 2.00 or 0.5625% per annum if the funded debt to EBITDA

ratio is less than 2.00.

In the third quarter of 2015, in connection with an amendment to our United States credit facilities, we elected to prepay \$5.0 million Canadian dollars (approximately \$4.0 million expressed in U.S. dollars) of Facility C with cash available on hand.

In April 2016, our wholly owned subsidiary, Pioneer Electrogroupp Canada Inc. (“PECI”), entered into an Amended and Restated Credit Agreement (“CAD ARCA”) with BMO with respect to our existing Canadian credit facilities (as amended and restated, the “Canadian Facilities”) that replaced and superseded all of our businesses’ prior financing arrangements with the bank. This CAD ARCA extended the maturity date of our Canadian Facilities to July 31, 2017. Additionally, defaults relating to the breach of certain financial covenants under the prior financing arrangements with the bank were waived by BMO. On March 15, 2017, the CAD ARCA was further amended (the “2017 CAD ARCA Amendment”).

Our Canadian Facilities provided for up to \$8.2 million CAD (approximately \$6.3 million expressed in U.S. dollars) consisting of a revolving \$7.0 million CAD Facility A to finance ongoing operations, a \$0.5 million CAD Facility B that financed a plant expansion, and a \$0.7 million USD Facility C that financed a business acquisition and the purchase and expansion of its manufacturing facilities. The 2017 CAD ARCA Amendment increased the Facility A to \$8.0 million CAD, increasing the total amount of loans available under the Canadian Facilities to \$9.1 million CAD.

Facility A, as amended and restated, is subject to margin criteria and borrowings bear interest at BMO’s prime rate plus 0.75% per annum on amounts borrowed in Canadian dollars, or its U.S. base rate plus 0.75% per annum or LIBOR plus 2.25% per annum on amounts borrowed in U.S. dollars. Pursuant to the 2017 CAD ARCA Amendment, Facility A will mature on July 31, 2018.

Borrowings under Facility B, as amended and restated, bear interest at BMO’s prime rate plus 1.25% per annum with principal repayments becoming due on a five year amortization schedule. Pursuant to the CAD ARCA, quarterly principal repayments were reduced to \$47 CAD, with a balloon payment of \$141 CAD due on July 31, 2017. The 2017 CAD ARCA Amendment amended the payment schedules so that the quarterly principal payments of \$47 CAD will continue after July 31, 2017 until our borrowings under the facility is fully paid on April 30, 2018.



Borrowings under Facility C, as amended and restated, bear interest at BMO's prime rate plus 1.50% per annum on amounts borrowed in Canadian dollars, or its U.S. base rate plus 1.50% per annum or LIBOR plus 2.75% per annum on amounts borrowed in U.S. dollars. Pursuant to the CAD ARCA, a principal repayment of \$72 USD was due on June 30, 2016, and the reduced quarterly principal repayments of \$36 USD was to be made beginning on October 31, 2016, with a balloon payment of \$496 USD due on July 31, 2017. The 2017 CAD ARCA Amendment amended the payment schedules so that the quarterly payments of \$36 USD will continue until July 31, 2018, with a balloon payment of \$352 due on July 31, 2018.

The CAD ARCA modified financial covenant testing so that testing will be performed on our consolidated financial statements. The financial covenants were changed pursuant to the CAD 2017 Amendment to require certain minimum working capital ratios, minimum EBITDA levels and effective tangible net worth levels for each fiscal quarter, which were further modified by the 2017 CAD ARCA Amendment. On March 6, 2017, we received a waiver from BMO on a certain financial covenant as of December 31, 2016.

We are currently in the process of renegotiating the terms of our credit facilities with BMO. BMO has agreed to suspend testing of the current ratio covenant as of September 30, 2017, due to such ongoing negotiation. We are in compliance with all financial covenants not suspended and required to be tested at September 30, 2017. We anticipate renegotiating our credit facilities on terms that will allow the Company to meet its covenants prospectively.

As of September 30, 2017, we had approximately \$6.8 million in U.S. dollar equivalents outstanding under our Canadian Credit Facilities. Our borrowings consisted of approximately \$6.2 million outstanding under Facility A, \$0.1 million outstanding under Facility B and \$0.5 million outstanding under Facility C.

### *United States Credit Facilities*

On December 2, 2014, our existing U.S. credit facilities (the "U.S. Facilities") were amended in order to provide a \$5.0 million term loan facility that was used for the acquisition of Titan. The term loan facility had principal repayments becoming due on a five year amortization schedule.

The U.S. Facilities initially required us to comply with a two-step test of financial covenants. First, as measured on a consolidated basis, we were required to comply with a maximum funded debt to adjusted EBITDA ratio of (a) 3.15x for the quarter ended December 31, 2014 and the quarter ending March 31, 2015, (b) 3.25x for the quarter ending June 30, 2015, (c) 3.65x for the quarter ending September 30, 2015, and (d) 2.75x for the quarter ending December 31, 2015 and all testing periods thereafter. Secondly, if the funded debt to adjusted EBITDA tests above are met, and our fixed charge coverage ratio is at or above 1.10x for the quarter ended December 31, 2014, and at or above 1.25x for all

testing periods thereafter, then no further compliance tests were required.

Alternatively, we could comply with the financial covenant requirements of the U.S. Facilities if our U.S. operations maintained a maximum funded debt to capitalization ratio and various minimum fixed charge coverage ratios and maximum funded debt to adjusted EBITDA ratios which were set at different thresholds by time period.

Borrowings under the demand revolving credit facility (USD Facility A) bore interest, at our option, at the bank's prime rate plus 1.00% per annum on U.S. prime rate loans, or an adjusted LIBOR rate plus 2.25% per annum on Eurodollar loans. Borrowings under the term loan facility (USD Facility B) bore interest, at our option, at the bank's prime rate plus 1.25% per annum on U.S. prime rate loans, or an adjusted LIBOR rate plus 2.50% per annum on Eurodollar loans.

In April 2016, we entered into an Amended and Restated Credit Agreement ("US ARCA") with BMO with respect to our U.S. Facilities that replaced and superseded all of our businesses' prior financing arrangements with the bank. Additionally, defaults relating to the breach of certain financial covenants under the prior financing arrangements with the bank were waived by BMO. On March 15, 2017, the US ARCA was further amended (the "2017 US ARCA Amendment").

Our U.S. Facilities, as amended and restated, provided for up to \$19.1 million consisting of a \$14.0 million USD Facility A to finance ongoing operations, a \$5.0 million USD Facility B that financed the acquisition of Titan, and a new \$0.1 million revolving credit facility provided pursuant to a MasterCard is to be used to pay for and temporarily finance our day-to-day business expenses and for no other purpose. The 2017 US ARCA Amendment increased the USD Facility A to \$15.0 million, increasing the total amount of loans available under the U.S. Facilities to \$20.1 million USD.

USD Facility A continues to bear interest, at our option, at the bank's prime rate plus 1.00% per annum on U.S. prime rate loans, or an adjusted LIBOR rate plus 2.25% per annum on Eurodollar loans. USD Facility A had a maturity date of July 31, 2017, which was extended to July 31, 2018 pursuant to the 2017 US ARCA Amendment.

Borrowings under USD Facility B bear interest, at our option, at U.S. base rate plus 1.25% per annum on U.S. prime loans, or an adjusted LIBOR rate plus 2.50% per annum on Eurodollar loans. Pursuant to the US ARCA, our quarterly principal payments were reduced to \$31 USD for calendar year 2016, with the original amortization schedule continuing to apply to all quarterly principal payments made after December 31, 2016, and the final maturity date of December 2, 2019. The 2017 US ARCA Amendment reduced the scheduled quarterly principal payments to \$31 USD, commencing March 31, 2017, to continue until July 31, 2018, with a balloon payment of \$4,438 on July 31, 2018.

The US ARCA modified financial covenant testing so that testing will be performed on our consolidated financial statements. The financial covenants were changed pursuant to the US ARCA to require certain minimum working capital ratios, minimum EBITDA levels and effective tangible net worth levels for each fiscal quarter, which were further modified by the 2017 US ARCA Amendment. On March 6, 2017, we received a waiver from BMO on a certain financial covenant as of December 31, 2016.

We are currently in the process of renegotiating the terms of our credit facilities with BMO. BMO has agreed to suspend testing of the current ratio covenant as of September 30, 2017 due to such ongoing negotiation. We are in compliance with all financial covenants not suspended and required to be tested at September 30, 2017. We anticipate renegotiating our credit facilities on terms that will allow the Company to meet its covenants prospectively.

Our obligations under the U.S. Facilities are guaranteed by all our wholly-owned U.S. subsidiaries. In addition, we and our wholly-owned U.S. subsidiaries granted a security interest in substantially all of our assets, including 65% of the shares of Pioneer Electrogroupp Canada Inc. held by us, to secure our obligations for borrowed money under the U.S. Facilities. The U.S. Facilities also restrict our ability to incur indebtedness, create or incur liens, make investments, make distributions or dividends and enter into merger agreements for the sale of any or all our assets.

As of September 30, 2017, we had approximately \$18.5 million outstanding under our U.S. Credit Facilities. Our borrowings consisted of approximately \$14.0 million outstanding under USD Facility A, and \$4.5 million outstanding under USD Facility B.

### **Nexus Promissory Note**

On July 25, 2012, the Company's Mexican subsidiary, Nexus Magneticos de Mexico, S. de R.L. de C.V. ("Nexus"), entered into a \$1.7 million term loan agreement with GE CF Mexico, S.A. de C.V. ("GE Capital Mexico"). The term loan was payable in 60 consecutive monthly installments and bore interest, payable monthly, at a rate of 6.93% per annum. The obligations of Nexus under the term loan were secured by certain machinery and equipment located in

Mexico and by a corporate guaranty by the Company. As of September 30, 2017 the balance of the note has been fully repaid, while at December 31, 2016 there was approximately \$185 outstanding under the Nexus Promissory Note.

Long-term debt consists of the following:

	September 30, 2017 (Unaudited)	December 31, 2016
Term credit facilities, net (a)	\$ 4,923	\$ 5,194
Nexus promissory note	—	185
Capital lease obligations	3	5
Total debt	4,926	5,384
Less current portion	(4,926 )	(1,379 )
Total long-term debt	\$ —	\$ 4,005

(a) The balances as of September 30, 2017 and December 31, 2016 are net of debt issuance costs of \$218 and \$245, respectively.

## 9. PENSION PLAN

The Company's Canadian subsidiary sponsors a defined benefit pension plan at one of its locations in which a majority of its employees are members. The subsidiary funds 100% of all contributions to the plan. The benefits, or the rate per year of credit service, are established by the Company and updated at its discretion.

The components of the expense the Company incurred under the pension plan are as follows:

	Three Months		Nine Months	
	Ended		Ended	
	September 30,		September 30,	
	2017	2016	2017	2016
Current service cost, net of employee contributions	\$ 10	\$ 10	\$ 35	\$ 33
Interest cost on accrued benefit obligation	27	26	79	76
Expected return on plan assets	(44 )	(41 )	(128 )	(121 )
Amortization of transitional obligation	3	3	9	8
Amortization of past service costs	2	3	6	8
Amortization of net actuarial gain	12	10	36	28
Total cost of benefit	\$ 10	\$ 11	\$ 37	\$ 32

The Company's policy is to fund the pension plan at or above the minimum level required by law. The Company made \$56 and \$86 of contributions to its defined benefit pension plan during the nine months ended September 30, 2017 and 2016, respectively. Changes in the discount rate and actual investment returns that are lower than the long-term expected return on plan assets could result in the Company making additional contributions. There were no changes during the current period.

## 10. STOCKHOLDERS' EQUITY

### Common Stock

The Company had 8,726,045 and 8,699,712 shares of common stock, \$0.001 par value per share, outstanding as of September 30, 2017 and December 31, 2016, respectively.

### Warrants

As of September 30, 2017 and December 31, 2016, the Company had warrants outstanding to purchase 50,600 shares of common stock with a weighted average exercise price of \$7.00 per share. The warrants expire on September 18, 2018. No warrants were exercised during the nine months ended September 30, 2017.

**Stock-Based Compensation**

A summary of stock option activity under the 2011 Long-Term Incentive Plan as of September 30, 2017, and changes during the nine months ended September 30, 2017, are presented below:

	Stock Options	Weighted average exercise price	Weighted average remaining contractual term	Aggregate intrinsic value
Outstanding as of January 1, 2017	247,400	\$ 8.75		\$
Granted	262,000	7.30		
Exercised	(26,333 )	4.55		
Forfeited	(47,267 )	6.74		
Outstanding as of September 30, 2017	435,800	\$ 8.35	7.7	\$ 238,140
Exercisable as of September 30, 2017	173,800	9.94	5.0	138,580

As of September 30, 2017 there were 237,867 shares available for future grants under the Company's 2011 Long-Term Incentive Plan.

Stock-based compensation expense recorded for the three and nine months ended September 30, 2017 was approximately \$148 and \$319, respectively, as compared to the expense of \$28 and \$34, during the three and nine months ended September 30, 2016, respectively. At September 30, 2017, the Company had total stock-based compensation expense remaining to be recognized in the consolidated statements of income of approximately \$339.

## Foreign Currency Translation

Foreign assets and liabilities are translated using the exchange rate in effect at the balance sheet date, and results of operations are translated using an average rate for the period. Translation adjustments are accumulated and reported as a component of accumulated other comprehensive income (loss). The Company had foreign currency translation adjustments resulting in a nominal unrealized loss for the three months ended September 30, 2017 and \$147 for the three months ended September 30, 2016. For the nine months ended September 30, 2017 and 2016, the Company had foreign currency translation adjustments resulting in unrealized income of \$68 and \$445, respectively.

## 11. BASIC AND DILUTED (LOSS) INCOME PER COMMON SHARE

Basic and diluted income per common share is calculated based on the weighted average number of shares outstanding during the period. The Company's employee and director stock option awards, as well as incremental shares issuable upon exercise of warrants, are not considered in the calculations if the effect would be anti-dilutive. In periods where the company reported a net loss, diluted net loss per common share is the same as basic net loss per common share for those periods. The following table sets forth the computation of basic and diluted (loss) income per share (in thousands, except per share data):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Numerator:				
Net (loss) income	\$ (764 )	\$ 322	\$ 678	\$ 1,085
Denominator:				
Weighted average basic shares outstanding	8,725	8,700	8,713	8,700
Effect of dilutive securities - equity based compensation plans	—	8	14	8
Net dilutive effect of warrants outstanding	—	—	—	—
Denominator for diluted net (loss) income per common share	8,725	8,708	8,727	8,708
Net (loss) income per common share:				
Basic	\$ (0.09 )	\$ 0.04	\$ 0.08	\$ 0.12
Diluted	\$ (0.09 )	\$ 0.04	\$ 0.08	\$ 0.12
Anti-dilutive securities (excluded from per share calculation):				
Equity based compensation plans	397	173	383	173
Warrants	51	51	51	51

## **12. BUSINESS SEGMENT AND GEOGRAPHIC INFORMATION**

The Company follows ASC 280 - Segment Reporting in determining its reportable segments. The Company considered the way its management team, most notably its chief operating decision maker, makes operating decisions and assesses performance and considered which components of the Company's enterprise have discrete financial information available. As the Company makes decisions using a manufactured products vs. distributed products and services group focus, its analysis resulted in two reportable segments: T&D Solutions and Critical Power. The Critical Power reportable segment is comprised solely of the Company's Titan Energy Systems Inc. subsidiary. The T&D Solutions reportable segment is an aggregation of all other Company subsidiaries, together with sales and expenses attributable to the strategic sales group for its T&D Solutions marketing activities.

The T&D Solutions segment is involved in the design, manufacture and distribution of electrical transformers and switchgear used primarily by utilities, large industrial and commercial operations to manage their electrical power distribution needs. The Critical Power segment provides power generation equipment, and aftermarket field-services primarily to help customers ensure smooth, uninterrupted power to operations during times of emergency.



The following tables present information about segment income and loss:

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2017	2016	2017	2016
Revenues				
T&D Solutions				
Transformers	\$ 21,548	\$ 21,110	\$ 66,198	\$ 61,605
Switchgear	4,299	4,268	10,118	10,876
	25,847	25,378	76,316	72,481
Critical Power				
Equipment	1,261	1,741	4,490	7,598
Service	2,686	2,270	7,147	5,810
	3,947	4,011	11,637	13,408
Consolidated	\$ 29,794	\$ 29,389	\$ 87,953	\$ 85,889

	Three Months		Nine Months Ended	
	Ended		September 30,	
	September 30,	September 30,	2017	2016
	2017	2016	2017	2016
Depreciation and Amortization				
T&D Solutions	\$ 366	\$ 450	\$ 1,082	\$ 1,203
Critical Power	507	355	1,210	1,063
Unallocated Corporate Overhead Expenses	17	17	52	51
Consolidated	\$ 890	\$ 822	\$ 2,344	\$ 2,317

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2017	2016	2017	2016
Operating Income (Loss)				
T&D Solutions	\$ 1,442	\$ 2,002	\$ 6,207	\$ 6,083
Critical Power	72	(10 )	(277 )	(100 )
Unallocated Corporate Overhead Expenses	(915 )	(780 )	(2,547 )	(2,293 )
Consolidated	\$ 599	\$ 1,212	\$ 3,383	\$ 3,690

Revenues are attributable to countries based on the location of the Company's customers:

Three Months Ended		Nine Months Ended	
September 30		September 30,	
2017	2016	2017	2016

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United States	\$ 20,804	\$ 20,594	\$ 59,790	\$ 59,067
Canada	8,990	8,795	28,163	26,758
Others	—	—	—	64
Total	\$ 29,794	\$ 29,389	\$ 87,953	\$ 85,889

15

## **ITEM 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

*The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the accompanying consolidated interim financial statements and related notes included elsewhere in this Quarterly Report on Form 10-Q and with our Annual Report on Form 10-K for the year ended December 31, 2016, which was filed with the Securities and Exchange Commission on March 29, 2017.*

*Unless the context requires otherwise, references in this Form 10-Q to the “Company,” “Pioneer,” “we,” “our” and “us” refer to Pioneer Power Solutions, Inc. and its subsidiaries.*

### **Special Note Regarding Forward-Looking Statements**

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

General economic conditions and their effect on demand for electrical equipment, particularly in the commercial construction market, but also in the power generation, industrial production, data center, oil and gas, marine and infrastructure industries.

The effects of fluctuations in sales on our business, revenues, expenses, net income, income (loss) per share, margins and profitability.

Many of our competitors are better established and have significantly greater resources, and may subsidize their competitive offerings with other products and services, which may make it difficult for us to attract and retain customers.

We depend on Siemens Industry, Inc. (“Siemens”) for a large portion of our business, and any change in the level of orders from Siemens could have a significant impact on our results of operations.

The potential loss or departure of key personnel, including Nathan J. Mazurek, our chairman, president and chief executive officer.

Our ability to expand our business through strategic acquisitions.

Our ability to integrate acquisitions and related businesses.

Our ability to generate internal growth, maintain market acceptance of our existing products and gain acceptance for our new products.

Unanticipated increases in raw material prices or disruptions in supply could increase production costs and adversely affect our profitability.

Restrictive loan covenants and/or our ability to repay or refinance debt under our credit facilities could limit our future financing options and liquidity position and may limit our ability to grow our business.

Our ability to realize revenue reported in our backlog.

Operating margin risk due to competitive pricing and operating efficiencies, supply chain risk, material, labor or overhead cost increases, interest rate risk and commodity risk.

Strikes or labor disputes with our employees may adversely affect our ability to conduct our business.

A significant portion of our revenue and expenditures are derived or spent in Canadian dollars. However, we report our financial condition and results of operations in U.S. dollars. As a result, fluctuations between the U.S. dollar and the Canadian dollar will impact the amount of our revenues and net income (loss).

The impact of geopolitical activity on the economy, changes in government regulations such as income taxes, duties and tariffs on the importation of products we sell into the United States, climate control initiatives, the timing or strength of an economic recovery in our markets and our ability to access capital markets.

Our chairman controls a majority of our voting power, and may have, or may develop in the future, interests that may diverge from yours.

Material weaknesses in internal controls.

Future sales of large blocks of our common stock may adversely impact our stock price.

The liquidity and trading volume of our common stock.

The foregoing does not represent an exhaustive list of matters that may be covered by the forward-looking statements contained herein or risk factors that we are faced with that may cause our actual results to differ from those anticipated in our forward-looking statements. Moreover, new risks regularly emerge and it is not possible for us to predict or articulate all risks we face, nor can we assess the impact of all risks on our business or the extent to which any risk, or combination of risks, may cause actual results to differ from those contained in any forward-looking statements. Except to the extent required by applicable laws or rules, we undertake no obligation to publicly update or revise any forward-looking statement, whether as a result of new information, future events or otherwise. You should review carefully the risks and uncertainties described under the heading “Part II - Item 1A. Risk Factors” in this Quarterly Report on Form 10-Q and in our Annual Report on Form 10-K for the year ended December 31, 2016 for a discussion of the foregoing and other risks that relate to our business and investing in shares of our common stock.

## **Business Overview**

We manufacture, sell and service a broad range of specialty electrical transmission, distribution and on-site power generation equipment for applications in the utility, industrial, commercial and backup power markets. Our principal products and services include custom-engineered electrical transformers, switchgear and engine-generator sets and controls, complemented by a national field-service network to maintain and repair power generation assets. We are headquartered in Fort Lee, New Jersey and operate from 13 additional locations in the U.S., Canada and Mexico for manufacturing, service, centralized distribution, engineering, sales and administration.

## **Description of Business Segments**

We have two reportable segments: Transmission & Distribution Solutions (“T&D Solutions”) and Critical Power Solutions (“Critical Power”).

Our T&D Solutions business provides equipment solutions that help customers effectively and efficiently manage their electrical power distribution systems to desired specifications. The reporting segment is comprised of two primary product categories: electrical transformers and switchgear. These solutions are marketed principally through our Pioneer Transformers Ltd. (“PTL”), Jefferson Electric, Inc. (“Jefferson”), Bemag Transformers, Inc. (“Bemag”), Pioneer Critical Power, Inc. (“PCPI”) and Pioneer Custom Electric Products, Inc. (“PCEP”) brand names.

Our Critical Power business provides customers with sophisticated power generation equipment and an advanced data collection and monitoring platform, the combination of which is used to ensure smooth, uninterrupted power to operations during times of emergency. These solutions are marketed by our operations headquartered in Minnesota, currently doing business under the Titan Energy Systems Inc. (“Titan”), as well as the Pioneer Critical Power brand names.

## Foreign Currency Exchange Rates

Although we report our results in accordance with U.S. GAAP and in U.S. dollars, PTL and Bemag are Canadian operations whose functional currency is the Canadian dollar. As such, the financial position, results of operations, cash flows and equity of these operations are initially consolidated in Canadian dollars. Their assets and liabilities are then translated from Canadian dollars to U.S. dollars by applying the foreign currency exchange rate in effect at the balance sheet date, while the results of their operations and cash flows are translated to U.S. dollars by applying weighted average foreign currency exchange rates in effect during the reporting period. The resulting translation adjustments are included in other comprehensive income or loss.

The following table provides actual end of period exchange rates used to translate the financial position of our Canadian operations at the end of each period reported. The average exchange rates presented below, as provided by the Bank of Canada, are indicative of the weighted average rates we used to translate the revenues and expenses of our Canadian operations into U.S. dollars (rates expressed as the number of U.S. dollars to one Canadian dollar for each period reported):

	2017			2016		
	<b>Balance Sheet</b>	<b>Statements of Operations and Comprehensive Income</b>		<b>Balance Sheet</b>	<b>Statements of Operations and Comprehensive Income</b>	
Quarter Ended	End of Period	Period Average	Cumulative Average	End of Period	Period Average	Cumulative Average
March 31	\$ 0.7519	\$ 0.7559	\$ 0.7559	\$ 0.7700	\$ 0.7274	\$ 0.7274
June 30	\$ 0.7706	\$ 0.7436	\$ 0.7497	\$ 0.7742	\$ 0.7760	\$ 0.7509
September 30	\$ 0.8013	\$ 0.7983	\$ 0.7652	\$ 0.7624	\$ 0.7662	\$ 0.7560

## **Reclassifications**

As the Company continues to implement the remediation plans discussed under the heading “Part I – Item 4. Controls and Procedures” of this Quarterly Report on Form 10-Q, the Company has determined that there were inconsistencies in classification of expenses between its business units in the reporting periods prior to December 31, 2016. As a result, the Company reclassified certain expenses from operating expenses to cost of goods sold for the year ended December 31, 2016, as previously disclosed in the Annual Report on Form 10-K filed with the SEC on March 29, 2017, and for the three and nine months ended September 30, 2016, resulting in a decrease to gross profit of \$18, or negative 0.06% as a percentage of sales for the three months ended September 30, 2016 and, resulting in a decrease to gross profit of \$262, or negative 0.30% as a percentage of sales for the nine months ended September 30, 2016, respectively.

## **Critical Accounting Policies**

The Company’s significant accounting policies are described in Note 2 to the audited consolidated financial statements included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2016. There have been no material changes to our critical accounting policies as disclosed in our Annual Report on Form 10-K for the year ended December 31, 2016.

## **RESULTS OF OPERATIONS**

### ***Overview of Nine Month Results***

Selected financial and operating data for our reportable business segments for the most recent reporting period is summarized below. This information, as well as the selected financial data provided in Note 12 – Business Segment and Geographic Information and in our unaudited Consolidated Financial Statements and related notes included in this Quarterly Report on Form 10-Q, should be referred to when reading our discussion and analysis of results of operations below.

Our summary of operating results during the three and nine months ended September 30, 2017 and 2016 are as follows:

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	Three Months Ended September		Nine Months Ended September	
	30,		30,	
	2017	2016	2017	2016
Revenues				
T&D Solutions	\$ 25,847	\$ 25,378	\$ 76,316	\$ 72,481
Critical Power	3,947	4,011	11,637	13,408
Consolidated	29,794	29,389	87,953	85,889
Cost of sales				
T&D Solutions	21,425	19,682	61,327	55,909
Critical Power	2,923	3,190	9,093	11,339
Consolidated	24,348	22,872	70,420	67,248
Gross profit	5,446	6,517	17,533	18,641
Selling, general and administrative expenses	4,359	4,794	12,724	13,269
Depreciation and amortization expense	682	544	1,731	1,625
Restructuring and integration	—	19	160	199
Foreign exchange gain	(194 )	(52 )	(465 )	(142 )
Total operating expenses	4,847	5,305	14,150	14,951
Operating income	599	1,212	3,383	3,690
Interest expense	588	556	1,662	1,151
Other expense	245	264	647	554
(Loss) income before taxes	(234 )	392	1,074	1,985
Income tax expense	530	70	396	900
Net (loss) / income	\$ (764 )	\$ 322	\$ 678	\$ 1,085

**Backlog**

Our backlog is based on firm orders from our customers expected to be delivered in the future, most of which is expected to occur during the next twelve months. Backlog may vary significantly from reporting period to reporting period due to the timing of customer commitments. The time between receipt of an order and actual delivery, or completion, of our products and services varies from one or more days, in the case of inventoried standard products, to three to nine months, in the case of certain custom engineered equipment solutions, and up to one year or more under our service contracts.



The following table represents the progression of our backlog, by reporting segment, as of the end of the last five quarters:

	September 30, 2017	June 30, 2017	March 31, 2017	December 31, 2016	September 30, 2016
T&D Solutions	\$ 28,059	\$ 29,182	\$ 31,705	\$ 34,588	\$ 36,699
Critical Power	10,626	10,466	5,039	3,970	4,831
Total order backlog	\$ 38,685	\$ 39,648	\$ 36,744	\$ 38,558	\$ 41,530

### Revenue

The following table represents our revenues by reporting segment and major product category for the periods indicated:

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2017	2016	Variance	%	2017	2016	Variance	%
T&D Solutions								
Transformers	\$ 21,548	\$ 21,110	\$ 438	2.1	\$ 66,198	\$ 61,605	\$ 4,593	7.5
Switchgear	4,299	4,268	31	0.7	10,118	10,876	(758 )	(7.0 )
	25,847	25,378	469	1.8	76,316	72,481	3,835	5.3
Critical Power								
Equipment	1,261	1,741	(480 )	(27.6 )	4,490	7,598	(3,108 )	(40.9 )
Service	2,686	2,270	416	18.3	7,147	5,810	1,337	23.0
	3,947	4,011	(64 )	(1.6 )	11,637	13,408	(1,771 )	(13.2 )
Total revenue	\$ 29,794	\$ 29,389	\$ 405	1.4	\$ 87,953	\$ 85,889	\$ 2,064	2.4

For the three months ended September 30, 2017, our consolidated revenue increased by \$405, or 1.4%, to \$29.8 million, up from \$29.4 million during the three months ended September 30, 2016. For the nine months ended September 30, 2017, our consolidated revenue increased by \$2,064, or 2.4%, to \$88.0 million, up from \$85.9 million during the nine months ended September 30, 2016.

*T&D Solutions.* During the three and nine months ended September 30, 2017, revenue from our transformer product lines increased by \$438, or 2.1%, and \$4,593, or 7.5%, as compared to the three and nine months ended September 30, 2016. The increase was driven by our “dry-type” transformer product lines in the United States, which increased by \$1,147, or 10.0%, during the three months ended September 30, 2017 and \$3,650, or 10.9%, during the nine months

ended September 30, 2017 as compared to the three and nine months ended September 30, 2016.

Our sales of T&D switchgear increased by 0.7% to \$4.3 million, during the three months ended September 30, 2017, as compared to the same period of the prior year due to an increase in sales of automatic transfer switches. For the nine months ended September 30, 2017, our switchgear sales decreased by 7.0% to \$10.1 million when compared to the same period last year as a result of lower sales of our low voltage switchgear products.

*Critical Power.* Titan is the only business unit in the Critical Power segment. For the three months ended September 30, 2017, equipment sales decreased by \$480, or 27.6%, as compared to the same period in the prior year, resulting from a reduced focus on this revenue stream. For the nine months ended September 30, 2017, equipment sales were down by \$3,108, or 40.9%, compared to the same period in 2016.

For the three and nine months ended September 30, 2017, service revenue increased by \$416, or 18.3% and \$1,337, or 23.0%, respectively, as compared to the same periods in the prior year due to increase in our service business with our multi-location customers.

**Gross Profit and Gross Margin**

The following table represents our gross profit by reporting segment for the periods indicated:

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2017	2016	Variance	%	2017	2016	Variance	%
<b>T&amp;D Solutions</b>								
Gross profit	\$ 4,422	\$ 5,696	\$ (1,274 )	(22.4 )	\$ 14,989	\$ 16,572	\$ (1,583 )	(9.6 )
Gross margin %	17.1	22.4	(5.3 )		19.6	22.9	(3.3 )	
<b>Critical Power</b>								
Gross profit	1,024	821	203	24.7	2,544	2,069	475	23.0
Gross margin %	25.9	20.5	5.4		21.9	15.4	6.5	
<b>Consolidated</b>								
gross profit	\$ 5,446	\$ 6,517	\$ (1,071 )	(16.4 )	\$ 17,533	\$ 18,641	\$ (1,108 )	(5.9 )
Consolidated gross margin %	18.3	22.2	(3.9 )		19.9	21.7	(1.8 )	

For the three months ended September 30, 2017, our gross margin was 18.3% of revenues, compared to 22.2% during the three months ended September 30, 2016. For the nine months ended September 30, 2017, our gross margin was 19.9% of revenues, compared to 21.7% for the nine months ended September 30, 2016. The decrease in our consolidated gross margin percentage for the three and nine months ended September 30, 2017 is due to the decreased gross margin in our T&D Solutions segment as explained below.

*T&D Solutions.* During the three and nine months ended September 30, 2017 the decrease in our T&D Solutions gross margin of 5.3% and 3.3%, respectively, as compared to the same periods in 2016 resulted primarily from lower margins in our dry-type transformer due to the write off of raw material inventory not relocated from Canada. The raw material inventory was not relocated due to the review of allowable sourcing and suppliers of components for finished goods.

*Critical Power.* During the three and nine months ended September 30, 2017, the gross margin increased 5.4% and 6.5% respectively, when compared to the same periods in 2016. This increase is the result of revenue mix with a shift towards service sales, which provide a greater gross margin than equipment sales.

**Operating Expenses**

The following table represents our operating expenses by reportable segment for the periods indicated:

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2017	2016	Variance	%	2017	2016	Variance	%
T&D Solutions								
Selling, general and administrative expense	\$ 3,016	\$ 3,573	\$ (557 )	(15.6 )	\$ 8,618	\$ 9,976	\$ (1,358 )	(13.6 )
Depreciation and amortization expense	158	172	(14 )	(8.1 )	469	511	(42 )	(8.2 )
Restructuring and integration	—	—	—	—	160	143	17	11.9
Foreign exchange gain	(194 )	(52 )	(142 )	273.1	(465 )	(142 )	(323 )	227.5
Segment operating expense	\$ 2,980	\$ 3,693	\$ (713 )	(19.3 )	\$ 8,782	\$ 10,488	\$ (1,706 )	(16.3 )
Critical Power								
Selling, general and administrative expense	\$ 445	\$ 477	\$ (32 )	(6.7 )	\$ 1,611	\$ 1,107	\$ 504	45.5
Depreciation and amortization expense	507	355	152	42.8	1,210	1,063	147	13.8
Restructuring and integration	—	—	—	—	—	(1 )	1	(100.0 )
Segment operating expense	\$ 952	\$ 832	\$ 120	14.4	\$ 2,821	\$ 2,169	\$ 652	30.1
Unallocated Corporate Overhead Expenses								

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Selling, general and administrative expense	\$ 898	\$ 744	\$ 154	20.7	\$ 2,495	\$ 2,186	\$ 309	14.1
Depreciation expense	17	17	—	—	52	51	1	2.0
Restructuring and integration	—	19	(19 )	(100.0 )	—	57	(57 )	(100.0 )
Segment operating expense	\$ 915	\$ 780	\$ 135	17.3	\$ 2,547	\$ 2,294	\$ 253	11.0
Consolidated Selling, general and administrative expense	\$ 4,359	\$ 4,794	\$ (435 )	(9.1 )	\$ 12,724	\$ 13,269	\$ (545 )	(4.1 )
Depreciation and amortization expense	682	544	138	25.4	1,731	1,625	106	6.5
Restructuring and integration	—	19	(19 )	(100.0 )	160	199	(39 )	(19.6 )
Foreign exchange gain	(194 )	(52 )	(142 )	273.1	(465 )	(142 )	(323 )	227.5
Consolidated operating expense	\$ 5,720	\$ 5,305	\$ (458 )	(8.6 )	\$ 14,150	\$ 14,951	\$ (801 )	(5.4 )

*Selling, General and Administrative Expense.* For the three months ended September 30, 2017, consolidated selling, general and administrative expense, before depreciation and amortization, decreased by \$435, or 9.1%, to \$4.4 million, as compared to \$4.8 million during the three months ended September 30, 2016 primarily due to lower salary and benefits expenses. As a percentage of our consolidated revenue, selling, general and administrative expense before depreciation and amortization decreased to 14.5% in the 2017 period, as compared to 16.3% in 2016.

During the nine months ended September 30, 2017, consolidated selling, general and administrative expense, before depreciation and amortization, decreased by \$545 or 4.1%, to \$12.7 million, as compared to \$13.3 million during the nine months ended September 30, 2016 primarily due to lower salary and benefits expenses. As a percentage of our consolidated revenue, selling, general and administrative expense before depreciation and amortization decreased to 14.5% in the 2017 period, as compared to 15.5% in 2016.

*Depreciation and Amortization Expenses.* Depreciation and amortization expense consists primarily of amortization of definite-lived intangible assets and depreciation of fixed assets, and excludes amounts included in cost of sales. For the three months ended September 30, 2017, depreciation and amortization expense increased by \$138 or 25.4% when

compared to the same period in 2016. For the nine months ended September 30, 2017, depreciation and amortization expense increased by \$106 or 6.5% when compared to the same period in 2016. These increases are the result of the write-off of the distributor territory license upon termination of a distribution agreement in the Critical Power segment for the three months ended September 31, 2017.

*Restructuring and Integration Expenses.* For the three and nine months ended September 30, 2017, restructuring and integration expense decreased by approximately \$19 and \$39, respectively, compared to the same periods in 2016, primarily due to completion of the relocation of our dry-type transformers from Canada in second quarter of 2017.

*Foreign Exchange Gain.* During the three months ended September 30, 2017 and 2016, approximately 29% and 27% of our consolidated operating revenues were denominated in Canadian dollars. During the nine months ended September 30, 2017 and 2016, approximately 31% and 29%, respectively of our consolidated operating revenues were denominated in Canadian dollars. Most of our expenses were denominated and disbursed in U.S. dollars during the three and nine months ended September 30, 2017 and 2016. We have not historically engaged in currency hedging activities. Fluctuations in foreign currency exchange rates between the time we initiate and then settle transactions with our customers and suppliers can have an impact on our operating results. For the three months ended September 30, 2017 and 2016, we recorded a gain of \$194 and \$52 respectively, due to currency fluctuations. For the nine months ended September 30, 2017 and 2016, we recorded a gain of \$465 and \$142, respectively, due to currency fluctuations.

### ***Operating Income (Loss)***

The following table represents our operating income or loss by reportable segment for the periods indicated:

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2017	2016	Variance	%	2017	2016	Variance	%
T&D Solutions	\$ 1,442	\$ 2,002	\$ (560 )	(28.0 )	\$ 6,207	\$ 6,083	\$ 124	2.0
Critical Power	72	(10 )	82	(820.0 )	(277 )	(100 )	(177 )	177.0
Unallocated								
Corporate Overhead Expenses	(915 )	(780 )	(135 )	17.3	(2,547 )	(2,293 )	(254 )	11.1
Total operating income	\$ 599	\$ 1,212	\$ (613 )	(50.6 )	\$ 3,383	\$ 3,690	\$ (307 )	(8.3 )

*T&D Solutions.* During the three and nine months ended September 30, 2017, T&D segment operating income was \$1,442 and \$6,208 respectively, as compared to \$2,003 and \$6,083 during the same periods of 2016. The decrease in operating income for the three months ended September 30, 2016 as compared to the same period in the prior year is primarily due to the write off-of raw material inventory that was not relocated to Mexico during relocation of our dry-type reporting unit. The increase in operating income for the nine months ended September 30, 2017 as compared to the same period in 2016 is primarily due to higher revenues and lower selling, general and administrative expenses.

*Critical Power.* During the three and nine months ended September 30, 2017, our Critical Power segment generated an operating income of \$72 and an operating loss of \$277, respectively, as compared to an operating loss of \$11 and \$100 during the same periods of 2016.

*Unallocated Corporate Overhead Expenses.* Our corporate expenses consists primarily of executive management, corporate accounting and human resources personnel, office expenses, financing and corporate development activities, payroll and benefits administration, treasury, tax compliance, legal, stock-based compensation and public reporting costs, and costs not specifically allocated to reportable business segments. During the three and nine months period ended September 30, 2017, our Unallocated Corporate Overhead Expenses increased \$135 or 17.3% and \$254 or 11.1%, respectively, as compared to the same periods in 2016, primarily due to an increase in stock based compensation expense.

### *Non-Operating Expense*

*Interest Expense.* For the three and nine months ended September 30, 2017, interest expense was approximately \$588 and \$1,662, respectively, as compared to \$556 and \$1,151 during the three and nine months ended September 30, 2016, respectively. The increase in our interest expense was due to higher average borrowings outstanding under our credit facilities and the increased utilization of short term borrowings during the 2017 period as compared to 2016.

*Other Expense.* For the three and nine months ended September 30, 2017, other non-operating expense was \$245 and \$647, respectively, as compared to \$264 and \$554, during the same periods of 2016. The Company continues to record interest on past due and unpaid payroll tax obligations. Included in the nine months ended September 30, 2017 and 2016 are waivers of certain interest and penalties on payroll tax obligations totaling \$70 and \$362, respectively.

*Income Tax Expense (Benefit).* Our effective income tax rate was 226.5% for the three months ended September 30, 2017, compared to 17.9% during the same period in 2016. For the nine months ended September 30, 2017, our effective income tax rate was 36.9%, as compared to 45.3% during the same period in 2016, as set forth below (dollars in thousands):

	Three Months Ended September			Nine Months Ended September		
	30, 2017	2016	Variance	30, 2017	2016	Variance
(Loss) income before income taxes	\$ (234 )	\$ 392	\$ (626 )	\$ 1,074	\$ 1,985	\$ (911 )
Income tax expense	530	70	460	396	900	(504 )
Effective income tax rate %	226.5	17.9	208.6	36.9	45.3	(8.5 )



Our effective income tax rate increased by 208.6% for three months ended September 30, 2017, as compared to the same period in 2016 primarily due to additional expense for assessment by tax authorities in Canada, dividend income recorded offset by foreign tax credit, and provision to tax return true-ups. For the nine months ended September 30, 2017, our effective income tax rate decreased 8.5% as compared to the same period in 2016 primarily due to realized foreign exchange loss in Canada during the nine months ended September 30, 2017.

### *Net (Loss) Income*

We generated net loss of \$764 and net income of \$678 during the three and nine months ended September 30, 2017 respectively, as compared to a net income of \$322 and \$1,085 for the three and nine months ended September 30, 2016, respectively. Our net loss per basic and diluted share for the three months ended September 30, 2017 was \$0.09 and our net income per basic and diluted share for the nine months ended September 30, 2017 was \$0.08, as compared to net income per basic and diluted share of \$0.04 and \$0.12 for the three and nine months ended September 30, 2016, respectively. The decrease in our net income for the three months ended September 30, 2017 was driven by an increase in our restructuring and income tax expenses when compared to the same period in 2016 was driven primarily by lower gross profit due to the write off of inventory that had not relocated from Canada and higher income tax expense. The decrease in our net income for the nine months ended September 30, 2017 as compared to the same period in 2016 was driven primarily by lower gross profit due to the write off of inventory that had not relocated from Canada, partially offset by lower income tax expense.

## **LIQUIDITY AND CAPITAL RESOURCES**

*General.* At September 30, 2017, we had total debt of \$31,848 and \$950 of cash and cash equivalents on hand. We have historically met our cash needs through a combination of cash flows from operating activities and bank borrowings under our revolving credit facilities. Our cash requirements are generally for operating activities, debt repayment, capital improvements and acquisitions. We believe that working capital, the borrowing capacity available under our credit facilities and funds generated from operations should be sufficient to finance our cash requirements for anticipated operating activities, capital improvements and principal repayments of debt through at least the next twelve months.

*Cash Used in Operating Activities.* Cash used by our operating activities was \$473 and \$8,860 during the nine months ended September 30, 2017 and 2016, respectively, primarily due to the decrease in working capital as we reported the term credit facilities within our current liabilities in the nine months ended September 30, 2017.

*Cash Used in Investing Activities.* Cash used in investing activities during the nine months ended September 30, 2017 was \$1,225 as compared to \$469 during the nine months ended September 30, 2016. Additions to our property, plant and equipment were \$1,245 as compared to \$476 in the prior year comparable period.

*Cash Provided by Financing Activities.* Cash provided by our financing activities was \$2,944 and \$9,620 during the nine months ended September 30, 2017 and 2016, respectively. During the nine months ended September 30, 2017, our net cash provided by financing activities included \$31,919 of increased borrowings under our credit facilities, an increase in short term borrowings of \$1,365 as a result of a product financing arrangement and a \$162 increase in bank overdrafts, offset by debt payments of \$30,465 under our credit facilities.

*Working Capital.* As of September 30, 2017, we had working capital of \$168, including \$950 of cash and cash equivalents, compared to working capital of \$2,448, including \$246 of cash and cash equivalents at December 31, 2016. The decrease in working capital as of September 30, 2017, as compared to September 30, 2016, is primarily due to our reporting of the term credit facilities within our current liabilities. We are currently in the process of renegotiating the terms of our credit facilities with BMO. Our current assets were approximately 1.0 and 1.1 times our current liabilities at September 30, 2017 and December 31, 2016, respectively. At September 30, 2017 and December 31, 2016, we had \$1,214 and \$1,535, respectively, of available and unused borrowing capacity from our revolving credit facilities. However, the availability of this capacity under our revolving credit facilities is subject to restrictions on the use of proceeds and is dependent upon our ability to satisfy certain financial and operating covenants, including financial ratios.

## **Credit Facilities and Long-Term Debt**

### **Canadian Credit Facilities**

Our Canadian subsidiaries have maintained credit facilities with BMO since October 2009. In June 2011, our wholly owned subsidiary Pioneer Electrogroupp Canada Inc. entered into a letter loan agreement with BMO (the “Initial Canadian Facilities”) that replaced and superseded all of our businesses’ prior financing arrangements with the bank.

Our Initial Canadian Facilities originally provided for up to \$22.0 million Canadian dollars (“CAD”) (approximately \$15.9 million expressed in U.S. dollars) consisting of a \$10.0 million CAD demand revolving credit facility (“Facility A”) to finance ongoing operations, a \$2.0 million CAD term credit facility (“Facility B”) that financed a plant expansion, and a \$10.0 million CAD term credit facility (“Facility C”) that financed a business acquisition and the purchase and expansion of its manufacturing facilities.

The Initial Canadian Facilities required us to comply on a consolidated Canadian basis with various financial covenants, including maintaining a minimum fixed charge coverage ratio, a maximum funded debt to EBITDA ratio

and a limitation on funded debt as a percent of capitalization.

Facility A was originally subject to margin criteria and borrowings bore interest at BMO's prime rate plus 0.50% per annum on amounts borrowed in Canadian dollars, or its U.S. base rate plus 0.50% per annum or LIBOR plus 2.00% per annum on amounts borrowed in U.S. dollars.

Borrowings under Facility B originally bore interest at BMO's prime rate plus 1.00% per annum with principal repayments becoming due on a five year amortization schedule.

Borrowings under Facility C were repayable according to a five year principal amortization schedule and bore interest at the following rates: if the funded debt to EBITDA ratio is equal to or greater than 2.00, BMO's prime rate plus 1.25% per annum on amounts borrowed in Canadian dollars, or its U.S. base rate plus 1.25% per annum or LIBOR plus 2.50% per annum on amounts borrowed in U.S. dollars; or, if the funded debt to EBITDA ratio is less than 2.00, BMO's prime rate plus 1.00% per annum on amounts borrowed in Canadian dollars, or its U.S. base rate plus 1.00% per annum or LIBOR plus 2.25% per annum on amounts borrowed in U.S. dollars. In addition, Facility C was subject to a standby fee which is calculated monthly using the unused portion of the facility at either 0.625% per annum if the funded debt to EBITDA ratio is equal to or greater than 2.00 or 0.5625% per annum if the funded debt to EBITDA ratio is less than 2.00.

In the third quarter of 2015, in connection with an amendment to our United States credit facilities, we elected to prepay \$5.0 million Canadian dollars (approximately \$4.0 million expressed in U.S. dollars) of Facility C with cash available on hand.

In April 2016, our wholly owned subsidiary, Pioneer Electrogroupp Canada Inc. ("PECI"), entered into an Amended and Restated Credit Agreement ("CAD ARCA") with BMO with respect to our existing Canadian credit facilities (as amended and restated, the "Canadian Facilities") that replaced and superseded all of our businesses' prior financing arrangements with the bank. This CAD ARCA extended the maturity date of our Canadian Facilities to July 31, 2017. Additionally, defaults relating to the breach of certain financial covenants under the prior financing arrangements with the bank were waived by BMO. On March 15, 2017, the CAD ARCA was further amended (the "2017 CAD ARCA Amendment").

Our Canadian Facilities provided for up to \$8.2 million CAD (approximately \$6.3 million expressed in U.S. dollars) consisting of a revolving \$7.0 million CAD Facility A to finance ongoing operations, a \$0.5 million CAD Facility B that financed a plant expansion, and a \$0.7 million USD Facility C that financed a business acquisition and the purchase and expansion of its manufacturing facilities. The 2017 CAD ARCA Amendment increased the Facility A to \$8.0 million CAD, increasing the total amount of loans available under the Canadian Facilities to \$9.1 million CAD.

Facility A, as amended and restated, is subject to margin criteria and borrowings bear interest at BMO's prime rate plus 0.75% per annum on amounts borrowed in Canadian dollars, or its U.S. base rate plus 0.75% per annum or LIBOR plus 2.25% per annum on amounts borrowed in U.S. dollars. Pursuant to the 2017 CAD ARCA Amendment, Facility A will mature on July 31, 2018.

Borrowings under Facility B, as amended and restated, bear interest at BMO's prime rate plus 1.25% per annum with principal repayments becoming due on a five year amortization schedule. Pursuant to the CAD ARCA, quarterly principal repayments were reduced to \$47 CAD, with a balloon payment of \$141 CAD due on July 31, 2017. The 2017 CAD ARCA Amendment amended the payment schedules so that the quarterly principal payments of \$47 CAD will continue after July 31, 2017 until our borrowings under the facility is fully paid on April 30, 2018.

Borrowings under Facility C, as amended and restated, bear interest at BMO's prime rate plus 1.50% per annum on amounts borrowed in Canadian dollars, or its U.S. base rate plus 1.50% per annum or LIBOR plus 2.75% per annum on amounts borrowed in U.S. dollars. Pursuant to the CAD ARCA, a principal repayment of \$72 USD was due on June 30, 2016, and the reduced quarterly principal repayments of \$36 USD was to be made beginning on October 31, 2016, with a balloon payment of \$496 USD due on July 31, 2017. The 2017 CAD ARCA Amendment amended the payment schedules so that the quarterly payments of \$36 USD will continue until July 31, 2018, with a balloon payment of \$352 due on July 31, 2018.

The CAD ARCA modified financial covenant testing so that testing will be performed on our consolidated financial statements. The financial covenants were changed pursuant to the CAD 2017 Amendment to require certain minimum working capital ratios, minimum EBITDA levels and effective tangible net worth levels for each fiscal quarter, which were further modified by the 2017 CAD ARCA Amendment. On March 6, 2017, we received a waiver from BMO on a certain financial covenant as of December 31, 2016.

We are currently in the process of renegotiating the terms of our credit facilities with BMO. BMO has agreed to suspend testing of the current ratio covenant as of September 30, 2017 due to such ongoing negotiation. We are in compliance with all financial covenants not suspended and required to be tested at September 30, 2017. We anticipate renegotiating our credit facilities on terms that will allow the Company to meet its covenants prospectively.

As of September 30, 2017, we had approximately \$6.8 million in U.S. dollar equivalents outstanding under our Canadian Credit Facilities. Our borrowings consisted of approximately \$6.2 million outstanding under Facility A, \$0.1 million outstanding under Facility B and \$0.5 million outstanding under Facility C.

### *United States Credit Facilities*

On December 2, 2014, our existing U.S. credit facilities (the “U.S. Facilities”) were amended in order to provide a \$5.0 million term loan facility that was used for the acquisition of Titan. The term loan facility had principal repayments becoming due on a five year amortization schedule.

The U.S. Facilities initially required us to comply with a two-step test of financial covenants. First, as measured on a consolidated basis, we were required to comply with a maximum funded debt to adjusted EBITDA ratio of (a) 3.15x for the quarter ended December 31, 2014 and the quarter ending March 31, 2015, (b) 3.25x for the quarter ending June 30, 2015, (c) 3.65x for the quarter ending September 30, 2015, and (d) 2.75x for the quarter ending December 31, 2015 and all testing periods thereafter. Secondly, if the funded debt to adjusted EBITDA tests above are met, and our fixed charge coverage ratio is at or above 1.10x for the quarter ended December 31, 2014, and at or above 1.25x for all testing periods thereafter, then no further compliance tests were required.

Alternatively, we could comply with the financial covenant requirements of the U.S. Facilities if our U.S. operations maintained a maximum funded debt to capitalization ratio and various minimum fixed charge coverage ratios and maximum funded debt to adjusted EBITDA ratios which were set at different thresholds by time period.

Borrowings under the demand revolving credit facility (USD Facility A) bore interest, at our option, at the bank’s prime rate plus 1.00% per annum on U.S. prime rate loans, or an adjusted LIBOR rate plus 2.25% per annum on Eurodollar loans. Borrowings under the term loan facility (USD Facility B) bore interest, at our option, at the bank’s prime rate plus 1.25% per annum on U.S. prime rate loans, or an adjusted LIBOR rate plus 2.50% per annum on Eurodollar loans.

In April 2016, we entered into an Amended and Restated Credit Agreement (“US ARCA”) with BMO with respect to our U.S. Facilities that replaced and superseded all of our businesses’ prior financing arrangements with the bank. Additionally, defaults relating to the breach of certain financial covenants under the prior financing arrangements with the bank were waived by BMO. On March 15, 2017, the US ARCA was further amended (the “2017 US ARCA Amendment”).

Our U.S. Facilities, as amended and restated, provided for up to \$19.1 million consisting of a \$14.0 million USD Facility A to finance ongoing operations, a \$5.0 million USD Facility B that financed the acquisition of Titan, and a new \$0.1 million revolving credit facility provided pursuant to a MasterCard is to be used to pay for and temporarily finance our day-to-day business expenses and for no other purpose. The 2017 US ARCA Amendment increased the USD Facility A to \$15.0 million, increasing the total amount of loans available under the U.S. Facilities to \$20.1 million USD.

USD Facility A continues to bear interest, at our option, at the bank's prime rate plus 1.00% per annum on U.S. prime rate loans, or an adjusted LIBOR rate plus 2.25% per annum on Eurodollar loans. USD Facility A had a maturity date of July 31, 2017, which was extended to July 31, 2018 pursuant to the 2017 US ARCA Amendment.

Borrowings under USD Facility B bear interest, at our option, at U.S. base rate plus 1.25% per annum on U.S. prime loans, or an adjusted LIBOR rate plus 2.50% per annum on Eurodollar loans. Pursuant to the US ARCA, our quarterly principal payments were reduced to \$31 USD for calendar year 2016, with the original amortization schedule continuing to apply to all quarterly principal payments made after December 31, 2016, and the final maturity date of December 2, 2019. The 2017 US ARCA Amendment reduced the scheduled quarterly principal payments to \$31 USD, commencing March 31, 2017, to continue until July 31, 2018, with a balloon payment of \$4,438 on July 31, 2018.

The US ARCA modified financial covenant testing so that testing will be performed on our consolidated financial statements. The financial covenants were changed pursuant to the US ARCA to require certain minimum working capital ratios, minimum EBITDA levels and effective tangible net worth levels for each fiscal quarter, which were further modified by the 2017 US ARCA Amendment. On March 6, 2017, we received a waiver from BMO on a certain financial covenant as of December 31, 2016.

We are currently in the process of renegotiating the terms of our credit facilities with BMO. BMO has agreed to suspend testing of the current ratio covenant as of September 30, 2017 due to such ongoing negotiation. We are in compliance with all financial covenants not suspended and required to be tested at September 30, 2017. We anticipate renegotiating our credit facilities on terms that will allow the Company to meet its covenants prospectively.

Our obligations under the U.S. Facilities are guaranteed by all our wholly-owned U.S. subsidiaries. In addition, we and our wholly-owned U.S. subsidiaries granted a security interest in substantially all of our assets, including 65% of the shares of Pioneer Electrogroupp Canada Inc. held by us, to secure our obligations for borrowed money under the U.S. Facilities. The U.S. Facilities also restrict our ability to incur indebtedness, create or incur liens, make investments, make distributions or dividends and enter into merger agreements for the sale of any or all our assets.

As of September 30, 2017, we had approximately \$18.5 million outstanding under our U.S. Credit Facilities. Our borrowings consisted of approximately \$14.0 million outstanding under USD Facility A, and \$4.5 million outstanding under USD Facility B.

#### *Nexus Promissory Note*

On July 25, 2012, Nexus Magneticos de Mexico, S. de R.L. de C.V., a subsidiary of Jefferson Electric, Inc., entered into a \$1.7 million term loan agreement with GE CF Mexico, S.A. de C.V. The term loan from GE CF Mexico, S.A. de C.V. was payable in 60 consecutive monthly installments and bore interest, payable monthly, at a rate of 6.93% per annum. In December 2013, we elected to make a \$250 advance payment against the Nexus Promissory Note. We provided a guaranty to GE CF Mexico, S.A. de C.V. of all of Nexus Magneticos de Mexico, S. de R.L. de C.V.'s obligations under the term loan agreement. As of September 30, 2017 the balance of the note has been fully repaid, while at December 31, 2016 there was approximately \$185 outstanding under the Nexus Promissory Note.

#### **Capital Expenditures**

Our additions to property, plant and equipment were \$1,245 during the nine months ended September 30, 2017, as compared to \$476 during the nine months ended September 30, 2016. We have no major future capital projects planned, or significant replacement spending anticipated during 2017. We anticipate approximately \$1,000 of additions to property, plant and equipment in the next twelve months. We expect to finance our capital expenditures with available cash and cash provided under our credit facilities.

#### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.**

Not Applicable

#### **ITEM 4. CONTROLS AND PROCEDURES**

##### **Management's Conclusions Regarding Effectiveness of Disclosure Controls and Procedures**



A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis. The matters that management identified in our Annual Report on Form 10-K for the year ended December 31, 2016, filed with the SEC on March 29, 2017, continued to exist and were still considered material weaknesses in our internal control over financial reporting at September 30, 2017.

We conducted an evaluation of the effectiveness of our “disclosure controls and procedures” (“Disclosure Controls”), as defined by Rules 13a-15(e) and 15d-15(e) of the Exchange Act, as of December 31, 2016, the end of the period covered by this Annual Report on Form 10-K. The Disclosure Controls evaluation was done in conjunction with an independent consulting firm and under the supervision and with the participation of management, including our chief executive officer and chief financial officer. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures. As of September 30, 2017, based on the evaluation of these disclosure controls and procedures, and in light of the material weaknesses found in our internal controls over financial reporting, our chief executive officer and chief financial officer have concluded that our disclosure controls and procedures were not effective.

### **Remediation Plan**

As of September 30, 2017, there were control deficiencies which constituted a material weakness in our internal control over financial reporting. Management has taken, and is taking steps to strengthen our internal control over financial reporting. Specifically

We have executed a plan that provided for the recruitment of new senior personnel at our reporting unit locations, as well as additional training for existing accounting staff as it relates to our financial reporting requirements. Members of management and the accounting staff have received additional training related to policies, procedures and internal controls, including Pioneer’s policies regarding monthly reconciliations and supervisory review procedures for all significant accounts.

Our corporate accounting group, assisted by an independent consulting firm that has been engaged, has reviewed and assessed progress on the remediation plan noted above.

In addition, we have implemented a component part of our restructuring and integration plan, designed to reduce the number of our production facilities from six locations to three. As a result, the controls and procedures which were previously identified as ineffective at our Bemag and PCPI reporting units have become inapplicable, as performance of their relevant business activities has been transferred to other Pioneer locations having suitable entity-level controls and financial closing and reporting processes. While we have taken certain actions to address the material weaknesses identified, additional measures may be necessary as we work to improve the overall effectiveness of our internal controls over financial reporting. Until the remediation plan is fully implemented and operating for a sufficient period of time, we will not be able to conclude that the material weaknesses have been remediated. We will continue to monitor and assess our remediation activities to address the material weaknesses discussed above through remediation as soon as practicable.



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

Other than the changes discussed above in the Remediation Plan, there has been no change in our internal control over financial reporting during the third quarter ended September 30, 2017 that materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

## **PART II – OTHER INFORMATION**

### **ITEM 1. LEGAL PROCEEDINGS**

From time to time, we may become involved in lawsuits, investigations and claims that arise in the ordinary course of business.

On January 11, 2016, Myers Power Products, Inc., a specialty electrical products manufacturer, filed suit with the Superior Court of the State of California, County of Los Angeles, against us, PCEP and two PCEP's employees who are former employees of Myers Power Products, Inc., Geo Murickan, the president of PCEP ("Murickan"), and Brett DeChellis ("DeChellis"), alleging, among other things, that Murickan wrongly used and retained confidential business information of Myers Power Products, Inc. for the benefit of us and PCEP, in breach of their confidentiality agreement and/or employment agreement entered into with Myers Power Products, Inc., and that we and PCEP knowingly received and used such confidential business information. Myers Power Products, Inc. is seeking injunctive relief enjoining us, PCEP and our employees from using its confidential business information and compensatory damages of an unspecified unlimited (exceeding \$25,000) amount. On March 18, 2016, we filed an answer to the complaint, denying generally each and every allegation and relief sought by Myers Power Products, Inc. and seeking dismissal based on, among other things, failure to state facts sufficient to constitute a cause of action. We intend to contest the matter vigorously. Due to the uncertainties of litigation, however, we can give no assurance that we, PCEP and our employees will prevail on any claims made against us, PCEP and our employees in any such lawsuit. Also, we can give no assurance that any other lawsuits or claims brought in the future will not have an adverse effect on our financial condition, liquidity or operating results.

As of the date of this filing, we are not aware of any other material legal proceedings to which we or any of our subsidiaries is a party or to which any of our property is subject, nor are we aware of any such threatened or pending litigation or any such proceedings known to be contemplated by governmental authorities other than other than the foregoing suit filed by Myers Power Products, Inc.

We are not aware of any material proceedings in which any of our directors, officers or affiliates or any registered or beneficial shareholder of more than 5% of our common stock is an adverse party or has a material interest adverse to our interest.

**ITEM 1A. RISK FACTORS**

During the fiscal quarter ended September 30, 2017 there were no material changes from the risk factors disclosed in our Annual Report on Form 10-K for the year ended December 31, 2016.

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

None.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

None.

**ITEM 4. MINE SAFETY DISCLOSURES**

Not applicable.

**ITEM 5. OTHER INFORMATION**

None.

**ITEM 6. EXHIBITS**

See the Exhibit Index following the signature page to this Quarterly Report on Form 10-Q for a list of exhibits filed or furnished with this report, which Exhibit Index is incorporated herein by reference.

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) 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.

**PIONEER POWER SOLUTIONS, INC.**

Date: November 13, 2017 By: /s/ Nathan J. Mazurek  
Name: Nathan J. Mazurek  
Title: Chief Executive Officer

Date: November 13, 2017 /s/ Thomas Klink  
Name: Thomas Klink  
Title: Chief Financial Officer

(Principal Financial Officer duly authorized to sign on behalf of Registrant)

**EXHIBIT INDEX**

<b>Exhibit No.</b>	<b>Description</b>
<u>3.1</u>	Composite Certificate of Incorporation (Incorporated by reference to Exhibit 3.1 to Amendment No. 4 to the Registration Statement on Form S-1 of Pioneer Power Solutions, Inc. filed with the Securities and Exchange Commission on June 21, 2011).
<u>3.2</u>	Bylaws (Incorporated by reference to Exhibit 3.2 to the Current Report on Form 8-K of Pioneer Power Solutions, Inc. filed with the Securities and Exchange Commission on December 2, 2009).
<u>31.1*</u>	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
<u>31.2*</u>	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
<u>32.1*</u>	Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
<u>32.2*</u>	Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101*	The following materials from the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2017, formatted in XBRL (eXtensible Business Reporting Language), (i) Consolidated Statements of Operations, (ii) Consolidated Balance Sheets, (iii) Consolidated Statements of Comprehensive Income (Loss), (iv) Consolidated Statements of Cash Flows and (v) Notes to the Consolidated Financial Statements.

\* Filed herewith.