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

FORM 10-Q

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

For the quarterly period ended September 30, 2015

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

For the transition period from ___________ to __________

Commission file number: 333-173040

ENER-CORE, INC.
(Exact name of registrant as specified in its charter)

Delaware	3511	46-0525350
(State or other jurisdiction of Incorporation or organization)	Primary Standard Industrial Classification Code Number	(IRS Employer Identification No.)

9400 Toledo Way
Irvine, California 92618
(Address of principal executive offices
And zip code)

(949) 616-3300
(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 the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

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

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

As of September 30, 2015 there were 2,464,160 shares of the issuer's common stock outstanding.

ENER-CORE, INC.
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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

FINANCIAL STATEMENTS

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Ener-Core, Inc.
Condensed Consolidated Balance Sheets

	September 30, 2015 (unaudited)	December 31, 2014
Assets		
Current assets:		
Cash and cash equivalents	$ 1,197,000	$ 2,176,000
Restricted cash	325,000	50,000
Accounts receivable, net	305,000	107,000
Inventory	133,000	53,000
Prepaid expenses and other current assets	474,000	91,000
Total current assets	2,434,000	2,477,000
Property and equipment, net	2,324,000	755,000
Intangibles, net	29,000	34,000
Deposits	27,000	27,000
Total assets	$ 4,814,000	$ 3,293,000
Liabilities and Stockholders' Equity (deficit)		
Current liabilities:		
Accounts payable	864,000	612,000
Accrued expenses	751,000	456,000
Deferred revenues and customer advances	1,009,000	—
Accrued warranty expense	30,000	242,000
Derivative liabilities	440,000	402,000
Convertible secured notes payable, net of discounts – short term	2,324,000	—
Capital leases payable—short term	26,000	19,000
Total current liabilities	5,444,000	1,731,000
Long term liabilities:		
Deposits	19,000	23,000
Capital lease payable—long term	20,000	30,000
Convertible secured notes payable, net of discounts—long term	1,544,000	—
Total liabilities	7,027,000	1,784,000
Commitments and contingencies (Note 14)		
Stockholders' equity (deficit):		
Preferred stock, $0.0001 par value; authorized 50,000,000 shares; no shares issued and outstanding at September 30, 2015 and December 31, 2014	—	—
Common stock, $0.0001 par value; authorized 200,000,000 shares; 2,464,160 and 2,282,120 shares issued and outstanding at September 30, 2015 and December 31, 2014, respectively	—	—
Additional paid-in capital	24,425,000	19,548,000
Accumulated deficit	(26,638,000)	(18,039,000)
Total stockholders' equity (deficit)	(2,213,000)	1,509,000
Total liabilities and stockholders' equity (deficit)	$ 4,814,000	$ 3,293,000

See accompanying notes to condensed consolidated financial statements.

Ener-Core, Inc.
Condensed Consolidated Statements of Operations
(unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	**2014**	**2015**	**2014**
Revenues	$ —	$ 58,000	$ —	$ 868,000
Cost of goods sold:	—	44,000	—	847,000
Gross Profit	—	14,000	—	21,000
Operating expenses:				
Selling, general, and administrative	1,165,000	1,226,000	3,475,000	4,017,000
Research and development	928,000	514,000	2,636,000	2,259,000
Total operating expenses	2,093,000	1,740,000	6,111,000	6,276,000
Operating loss	(2,093,000)	(1,726,000)	(6,111,000)	(6,255,000)
Other income (expenses):				
Interest expense, net	(150,000)	(21,000)	(257,000)	(28,000)
Amortization of debt discount and deferred financing costs	(1,117,000)	(2,694,000)	(1,921,000)	(3,234,000)
Loss on exchange of warrants	—	—	(279,000)	—
Gain (Loss) on valuation of derivative liabilities	50,000	1,618,000	(33,000)	1,748,000
Total other income (expenses), net	(1,217,000)	(1,097,000)	(2,490,000)	(1,514,000)
Loss before provision for income taxes	(3,310,000)	(2,823,000)	(8,601,000)	(7,769,000)
Provision for income taxes	—	—	—	1,000
Net loss	$ (3,310,000)	$ (2,823,000)	$ (8,601,000)	$ (7,770,000)
Loss per share—basic and diluted	$ (1.34)	$ (1.72)	$ (3.61)	$ (5.13)
Weighted average common shares—basic and diluted	2,464,100	1,642,600	2,385,500	1,515,000

See accompanying notes to condensed consolidated financial statements.

Ener-Core, Inc.
Condensed Consolidated Statements of Cash Flows
(unaudited)

	Nine Months Ended September 30,	
	2015	2014
Cash flows used in operating activities:		
Net loss	$ (8,601,000)	$ (7,770,000)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	276,000	176,000
Amortization of debt discount and deferred financing costs	1,921,000	3,234,000
Fair value of derivative liability	33,000	(1,748,000)
Stock-based compensation	1,113,000	2,813,000
Loss on exchange of warrants for common stock	279,000	—
Warrants issued for services	—	72,000
Changes in assets and liabilities:		
Accounts and other receivables	3,000	(97,000)
Payments on contract loss	—	(64,000)
Restricted cash	(275,000)	—
Prepaid expenses and other current assets	(36,000)	(12,000)
Inventory	(80,000)	—
Deferred revenue	808,000	(701,000)
Accounts payable	281,000	383,000
Accrued expenses and other liabilities	(318,000)	(9,000)
Accrued interest expense	50,000	19,000
Costs in excess of billings of uncompleted contracts	—	801,000
Net cash used in operating activities	(4,546,000)	(2,903,000)
Cash flows used in investing activities:		
Purchases of property and equipment	(1,830,000)	(27,000)
Net cash used in investing activities	(1,830,000)	(27,000)
Cash flows from financing activities:		
Proceeds from issuance of common stock, net	741,000	3,895,000
Proceeds from note payable, net	4,669,000	3,757,000
Payments on convertible notes payable	—	(1,883,000)
Repayment of capital leases payable	(13,000)	(9,000)
Net cash provided by financing activities	5,397,000	5,760,000
Net increase (decrease) in cash and cash equivalents	(979,000)	2,830,000
Cash and cash equivalents at beginning of period	2,176,000	1,201,000
Cash and cash equivalents at end of period	$ 1,197,000	$ 4,031,000

See accompanying notes to condensed consolidated financial statements.

Ener-Core, Inc.
Condensed Consolidated Statements of Cash Flows (continued)
(unaudited)

	Nine Months Ended September 30,	
	2015	**2014**
Supplemental disclosure of cash flow information:		
Cash paid during the period for:		
Income taxes	$ —	$ 1,000
Interest	$ 205,000	$ 4,000
Supplemental disclosure of non-cash activities:		
Capital leases for purchase of equipment	$ 10,000	$ 29,000
Debt discount and derivative liabilities recorded upon issuance of warrants and convertible secured notes	$ 2,750,000	$ 2,078,000
Common stock issued in exchange for warrant cancellation	$ 885,000	$ —
Original issue discount of convertible secured note issued	$ —	$ 572,000
Debt discount and accrued broker fees upon issuance of convertible secured note	$ —	186,000
Debt discount for warrants issued for broker fee in convertible secured note	$ —	$ 154,000
Warranty liability recorded for product commissioned	$ —	$ 22,000
Conversion of convertible notes and accrued interest into common stock	$ —	$ 2,711,000
Issuance of warrants for services	$ —	$ 72,000
Issuance of common stock for placement fees	$ —	$ 150,000
Issuance of warrants for placement fees	$ —	$ 101,000

See accompanying notes to condensed consolidated financial statements.

Ener-Core, Inc.
Notes to Condensed Consolidated Financial Statements
(unaudited)

Note 1—Description of Business

Organization

Ener-Core, Inc. (the “Company”, “we”, “us”, “our”), a Delaware corporation, was formed on April 29, 2010 as Inventtech, Inc. On July 1, 2013, we acquired our wholly owned subsidiary, Ener-Core Power, Inc., (formerly Flex Power Generation, Inc.), a Delaware corporation. The stockholders of Ener-Core Power, Inc. are now our stockholders and the management of Ener-Core Power, Inc. is now our management. The acquisition was treated as a “reverse merger” and our financial statements are those of Ener-Core Power, Inc. All equity amounts presented have been retroactively restated to reflect the reverse merger as if it had occurred on November 12, 2012.

Effective as of September 3, 2015, we changed our state of incorporation from the State of Nevada to the State of Delaware (the “Reincorporation”), pursuant to a plan of conversion dated September 2, 2015, following approval by our stockholders of the Reincorporation at our 2015 Annual Meeting of Stockholders held on August 28, 2015. As a Delaware corporation following the Reincorporation, we are deemed to be the same continuing entity as the Nevada corporation prior to the Reincorporation, and as such continue to possess all of the rights, privileges and powers and all of the debts, liabilities and obligations of the prior Nevada corporation. Upon effectiveness of the Reincorporation, all of the issued and outstanding shares of common stock of the Nevada corporation automatically converted into issued and outstanding shares of common stock of the Delaware corporation without any action on the part of our stockholders. Concurrent with the Reincorporation, on September 3, 2015 our authorized shares increased to 250,000,000 shares of stock consisting of 200,000,000 authorized shares of common stock and 50,000,000 authorized shares of preferred stock.

Reverse Merger

We entered into an Agreement and Plan of Merger (the “Merger Agreement”) with Ener-Core Power, Inc. and Flex Merger Acquisition Sub, Inc., a Delaware corporation and our wholly owned subsidiary (“Merger Sub”), pursuant to which the Merger Sub merged with and into Ener-Core Power, Inc., with Ener-Core Power, Inc. as the surviving entity (the “Merger”). Prior to the Merger, we were a public reporting “shell company,” as defined in Rule 12b-2 of the Securities Exchange Act of 1934, as amended. The Merger Agreement was approved by the boards of directors of each of the parties to the Merger Agreement. In April 2013, the pre-merger public shell company effected a 30-for-1 forward split of its common stock. All share amounts have been retroactively restated to reflect the effect of the stock split.

As provided in the Contribution Agreement dated November 12, 2012 (the “Contribution Agreement”) by and among FlexEnergy, Inc. (“FlexEnergy”), FlexEnergy Energy Systems, Inc. (“FEES”), and Ener-Core Power, Inc., Ener-Core Power, Inc. was spun-off from FlexEnergy as a separate corporation. As a part of that transaction, Ener-Core Power, Inc. received all assets (including intellectual property) and certain liabilities pertaining to the Power Oxidizer business carved out of FlexEnergy. The owners of FlexEnergy did not distribute ownership of Ener-Core Power, Inc. pro rata. The assets and liabilities were transferred to us and recorded at their historical carrying amounts since the transaction was a transfer of net assets between entities under common control.

On July 1, 2013, Ener-Core Power, Inc. completed the Merger with us. Upon completion of the Merger, we, immediately became a public company. The Merger was accounted for as a “reverse merger” and recapitalization. As part of the Merger, 2,410,400 shares of outstanding common stock of the pre-merger public shell company were cancelled. This cancellation has been retroactively accounted for as of the inception of Ener-Core Power, Inc. on November 12, 2012. Accordingly, Ener-Core Power, Inc. was deemed to be the accounting acquirer in the transaction and, consequently, the transaction was treated as a recapitalization of Ener-Core Power, Inc. Accordingly, the assets and liabilities and the historical operations that are reflected in the financial statements are those of Ener-Core Power, Inc. and are recorded at the historical cost basis of Ener-Core Power, Inc. Our assets, liabilities and results of operations were de minimis at the time of the Merger.

Reverse Stock Split

The board of directors of the Company approved a reverse stock split of the Company’s authorized, issued and outstanding shares of common stock, par value $0.0001 per share, as well as the Company’s authorized shares of preferred stock, par value $0.0001 per share, of which no shares are issued and outstanding (together, the “Stock”), at a ratio of 1-for-50 (the “Reverse Stock Split”). The Reverse Stock Split became effective on July 8, 2015 (the “Effective Date”). As a result of the Reverse Stock Split, the authorized preferred stock decreased to 1,000,000 shares and the authorized common stock decreased to 4,000,000 shares. Both the preferred stock and common stock par value remained at $0.0001 per share.

On the Effective Date, the total number of shares of common stock held by each stockholder of the Company were converted automatically into the number of shares of common stock equal to: (i) the number of issued and outstanding shares of common stock held by each such stockholder immediately prior to the Reverse Stock Split divided by (ii) 50. The Company issued one whole share of the post-Reverse Stock Split common stock to any stockholder who otherwise would have received a fractional share as a result of the Reverse Stock Split, determined at the beneficial owner level by share certificate. As a result, no fractional shares were issued in connection with the Reverse Stock Split and no cash or other consideration will be paid in connection with any fractional shares that would otherwise have resulted from the Reverse Stock Split. The Reverse Stock Split also affected all outstanding options and warrants by dividing each option or warrant outstanding by 50, rounded up to the nearest option or warrant, and multiplying the exercise price by 50 for each option or warrant outstanding.

Description of the Business

We design, develop, and manufacture products based on proprietary technologies that aim to expand the operating range of gaseous fuel while improving emissions, which technologies we refer to collectively as “Power Oxidation” or “Power Oxidizer” (previously called “Gradual Oxidation” and “Gradual Oxidizer,” respectively, in our prior public disclosures). Our products aim to expand power generation into previously uneconomical markets while, at the same time, reduce gaseous emissions from industrial processes that contribute to air pollution and climate change. The Power Oxidizer integrates with a gas turbine and generator to create a power station.

Our product, the FP250, is a complete system consisting of our designed and patented Power Oxidizer, integrated with a gas turbine and generator. The FP250 has been designed to operate on fuels from 100% combustible gas down to concentrations of 5% or less combustible gas content. The FP250 has applications in landfill, oil production, coal mining, and other operations, and offers our customers two distinct value propositions: the destruction of low quality waste gases with no harmful emissions and the generation of energy from a renewable fuel source.

We are currently developing our second commercial product, the Ener-Core Powerstation KG2-3G/GO (“KG2”), which will combine our Power Oxidizer with a two megawatt gas turbine developed by Dresser-Rand a.s., a subsidiary of Dresser-Rand Group Inc. (“Dresser-Rand”). We have completed system layout and analytic models integrating our Power Oxidizer with the turbine and have initiated design and development of the KG2. We expect to field test units in 2015, with initial commercial shipments shortly thereafter.

We sell our products directly and through distributors in two countries, the United States and Netherlands.

Going Concern

Our consolidated financial statements are prepared using the accrual method of accounting in accordance with accounting principles generally accepted in the United States of America (“GAAP”) and have been prepared on a going concern basis, which contemplates the realization of assets and settlement of liabilities in the normal course of business. Since our inception, we have made a substantial investment in research and development to develop the Power Oxidizer, have successfully deployed an EC250 field test unit at the U.S. Army base at Fort Benning, Georgia, and installed and commissioned our first commercial unit in the Netherlands in the second quarter of 2014. In November 2014 we signed a Commercial License Agreement with Dresser-Rand (the “D-R Agreement”) to incorporate our Power Oxidizer into Dresser-Rand’s 1.75MW turbine. In August 2015, the D-R Agreement became a mutually binding agreement due to the satisfaction of certain binding conditions contained in the D-R Agreement.

We have sustained recurring net losses and negative cash flows since inception and have not yet established an ongoing source of revenues sufficient to cover our operating costs and allow us to continue as a going concern. Despite a capital raise of approximately $4.0 million in September 2014 and further capital raises of $5.8 million in April and May 2015, we expect to require additional sources of capital to support the Company’s growth initiatives. We must secure additional funding to continue as a going concern and execute our business plan.

Management’s plan is to obtain capital sufficient to meet our operating expenses by seeking additional equity and/or debt financing, including through a proposed registered offering for which we filed a registration statement on July 29, 2015. The cash and cash equivalents balance (excluding restricted cash) on December 31, 2014 and September 30, 2015, was approximately $2.2 million and $1.2 million, respectively.

We raised a total of $5.8 million of debt and equity capital in April and May 2015, as described in Notes 9 and 12 below, and we expect that the $1.2 million of cash as of September 30, 2015, receipts on customer billings, and the anticipated net proceeds from the proposed registered offering will continue to fund our working capital needs, general corporate purposes, and related obligations into 2016 at our current spending levels. However, we expect to require significantly more cash for working capital and as financial security to support our growth initiatives.

We will pursue raising additional equity and/or debt financing to fund our operations and product development. If future funds are raised through issuance of stock or debt, these securities could have rights, privileges, or preferences senior to those of our common stock and debt covenants that could impose restrictions on our operations. Any equity or convertible debt financing will likely result in additional dilution to our current stockholders. We cannot make any assurances that any additional financing, including the proposed registered offering, will be completed on a timely basis, on acceptable terms or at all. Our inability to successfully raise capital in a timely manner will adversely impact our ability to continue as a going concern. If our business fails or we are unable to raise capital on a timely basis, our investors may face a complete loss of their investment.

The accompanying consolidated financial statements do not give effect to any adjustments that might be necessary if we were unable to meet our obligations or continue operations as a going concern.

Note 2—Summary of Significant Accounting Policies

Basis of Presentation

The accompanying consolidated financial statements include our accounts and our wholly-owned subsidiary, Ener-Core Power, Inc. All significant intercompany transactions and accounts have been eliminated in consolidation. All monetary amounts are rounded to the nearest $000, except certain per share amounts.

The accompanying financial statements have been prepared in accordance with GAAP.

Reclassifications

Certain amounts in the 2014 consolidated financial statements have been reclassified to conform to the current year presentation. These reclassifications have no effect on previously reported net loss.

Segments

We operate in one segment. Except for one consultant operating in Europe, all of our operations are located domestically.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of expenses during the reporting period. Significant items subject to such estimates and assumptions include but are not limited to: collectability of receivables; the valuation of certain assets, useful lives, and carrying amounts of property and equipment, equity instruments and share-based compensation; provision for contract losses; valuation allowances for deferred income tax assets; valuation of derivative liabilities; and exposure to warranty and other contingent liabilities. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

Foreign Currency Adjustments

Our functional currency for all operations worldwide is the U.S. dollar. Nonmonetary assets and liabilities are translated at historical rates and monetary assets and liabilities are translated at exchange rates in effect at the end of the year. Income statement accounts are translated at average rates for the year. At September 30, 2015 and December 31, 2014, we did not hold any foreign currency asset or liability amounts. Gains and losses resulting from foreign currency transactions are reported as other income in the period they occurred.

Concentrations of Credit Risk

Cash and Cash Equivalents

We maintain our non-interest bearing transactional cash accounts at financial institutions for which the Federal Deposit Insurance Corporation ("FDIC") provides insurance coverage of up to $250,000. For interest bearing cash accounts, from time to time, balances exceed the amount insured by the FDIC. We have not experienced any losses in such accounts and believe we are not exposed to any significant credit risk related to these deposits. At September 30, 2015, we had $1,044,000 in excess of the FDIC limit.

We consider all highly liquid investments available for current use with an initial maturity of three months or less and are not restricted to be cash equivalents. We invest our cash in short-term money market accounts.

Restricted Cash

Collateral Account

Under a credit card processing agreement with a financial institution that was entered in 2013, we are required to maintain funds on deposit with the financial institution as collateral. The amount of the deposit, which is at the discretion of the financial institution, was $50,000 on September 30, 2015 and December 31, 2014.

Dresser-Rand Escrow Account

Under our Commercial License Agreement with Dresser-Rand Corporation, a Siemens Company ("Dresser-Rand"), as amended, prepaid license fee payments of $400,000 per quarter are to be paid by Dresser-Rand into an escrow account with a financial institution beginning August, 2015. Dresser-Rand is allowed to withdraw up to $125,000 per quarter from this escrow account for qualified engineering expenses incurred by Dresser-Rand under the terms and conditions of the Dresser-Rand Commercial License Agreement. Dresser-Rand funded $400,000 in August 2015 and withdrew $125,000 in August 2015. The balance in the escrow account was $275,000 and $0 on September 30, 2015 and December 31, 2014. The Company is allowed to withdraw funds from the escrow account after completion of additional technical milestones, expected to be completed in the first half of 2016. See also Note 8 – Deferred Revenues and Customer Advances.

Accounts Receivable

Our accounts receivable are typically from credit worthy customers or, for international customers are supported by guarantees or letters of credit. For those customers to whom we extend credit, we perform periodic evaluations of them and maintain allowances for potential credit losses as deemed necessary. We generally do not require collateral to secure accounts receivable. We have a policy of reserving for uncollectible accounts based on our best estimate of the amount of probable credit losses in existing accounts receivable. We periodically review our accounts receivable to determine whether an allowance is necessary based on an analysis of past due accounts and other factors that may indicate that the realization of an account may be in doubt. Account balances deemed to be uncollectible are charged to the allowance after all means of collection have been exhausted and the potential for recovery is considered remote.

As of September 30, 2015 and December 31, 2014, two customers and one customer, respectively, accounted for 100% of net accounts receivable.

Accounts Payable

As of September 30, 2015 and December 31, 2014, two and six vendors, respectively, collectively accounted for approximately 25% and 54% of our total accounts payable.

Inventory

Inventory, which consists of raw materials, is stated at the lower of cost or net realizable value, with cost being determined by the average-cost method, which approximates the first-in, first-out method. At each balance sheet date, we evaluate our ending inventory for excess quantities and obsolescence. This evaluation primarily includes an analysis of forecasted demand in relation to the inventory on hand, among consideration of other factors. Based upon the evaluation, provisions are made to reduce excess or obsolete inventories to their estimated net realizable values. Once established, write-downs are considered permanent adjustments to the cost basis of the respective inventories. At September 30, 2015 and December 31, 2014, we did not have a reserve for slow-moving or obsolete inventory.

Property and Equipment

Property and equipment are stated at cost, and are being depreciated using the straight-line method over the estimated useful lives of the related assets, ranging from three to ten years. Maintenance and repairs that do not improve or extend the lives of the respective assets are expensed. At the time property and equipment are retired or otherwise disposed of, the cost and related accumulated depreciation accounts are relieved of the applicable amounts. Gains or losses from retirements or sales are reflected in the consolidated statements of operations.

Deposits

Deposits primarily consist of amounts incurred or paid in advance of the receipt of fixed assets or are deposits for rent and insurance.

Accrued Warranties

Accrued warranties represent the estimated costs that will be incurred during the warranty period of our products. We make an estimate of expected costs that will be incurred by us during the warranty period and charge that expense to the consolidated statement of operations at the date of sale. We also reevaluate the estimate at each balance sheet date and if the estimate is changed, the effect is reflected in the consolidated statement of operations. We made our initial commercial sale to Efficient Energy Conversion TurboMachinery, B.V. ("EECT") in the second quarter of 2014 with a six month warranty and later extended that warranty at our discretion. There was no warranty for the unit shipped to the Fort Benning site. We expect our future warranty period to be between nine months and one year depending on the warranties provided and the products sold. Accrued warranties for expected expenditures within the next year are classified as current liabilities and as non-current liabilities for expected expenditures for time periods beyond one year.

Deferred Rent

We record deferred rent expense, which represents the temporary differences between the reporting of rental expense on the financial statements and the actual amounts remitted to the landlord. The deferred rent portion of lease agreements are leasing inducements provided by the landlord. Also, tenant improvement allowances provided are recorded as a deferred rent liability and recognized ratably as a reduction to rent expense over the lease term.

Intangible Assets

Our intangible assets represent intellectual property acquired during the reverse merger. We amortize our intangible assets with finite lives over their estimated useful lives.

Impairment of Long-Lived Assets

We account for our long-lived assets in accordance with the accounting standards which require that long-lived assets be reviewed for impairment whenever events or changes in circumstances indicate that the historical carrying value of an asset may no longer be appropriate. We consider the carrying value of assets may not be recoverable based upon our review of the following events or changes in circumstances: the asset's ability to continue to generate income from operations and positive cash flow in future periods; loss of legal ownership or title to the assets; significant changes in our strategic business objectives and utilization of the asset; or significant negative industry or economic trends. An impairment loss would be recognized when estimated future cash flows expected to result from the use of the asset are less than its carrying amount. As of September 30, 2015 and December 31, 2014, we do not believe there have been any impairments of our long-lived assets. There can be no assurance, however, that market conditions will not change or demand for our products will continue, which could result in impairment of long-lived assets in the future.

Fair Value of Financial Instruments

Our financial instruments consist primarily of cash and cash equivalents, restricted cash, accounts receivable, accounts payable, derivative liabilities, secured notes payable and related debt discounts and capital lease liabilities. Fair value estimates discussed herein are based upon certain market assumptions and pertinent information available to management as of September 30, 2015 and December 31, 2014. The carrying amounts of short-term financial instruments are reasonable estimates of their fair values due to their short-term nature or proximity to market rates for similar items.

We determine the fair value of our financial instruments based on a three-level hierarchy established for fair value measurements under which these assets and liabilities must be grouped, based on significant levels of observable or unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect management's market assumptions. This hierarchy requires the use of observable market data when available. These two types of inputs have created the following fair-value hierarchy:

- Level 1: Valuations based on unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities. Currently, we classify our cash and cash equivalents as Level 1 financial instruments.

- Level 2: Valuations based on observable inputs (other than Level 1 prices), such as quoted prices for similar assets at the measurement date quoted prices in markets that are not active, or inputs which are observable, either directly or indirectly, for substantially the full term of the asset or liability. We do not currently have any accounts under Level 2.

- Level 3: Valuations based on inputs that require inputs that are both significant to the fair value measurement and unobservable and involve management judgment (i.e., supported by little or no market activity). Currently, we classify our warrants and conversion options accounted for as derivative liabilities as Level 3 financial instruments.

If the inputs used to measure fair value fall in different levels of the fair value hierarchy, a financial security's hierarchy level is based upon the lowest level of input that is significant to the fair value measurement.

Derivative Financial Instruments

The Company issues derivative financial instruments in conjunction with its debt and equity offerings and to provide additional incentive to investors and placement agents. The Company uses derivative financial instruments in order to obtain the lowest cash cost-source of funds. Derivative liabilities are recognized in the consolidated balance sheets at fair value based on the criteria specified in Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") topic 815-40 "*Derivatives and Hedging—Contracts in Entity's own Equity*." The estimated fair value of the derivative liabilities is calculated using either the Black-Scholes-Merton or Monte Carlo simulation model method.

The Company issued detachable common stock warrants and convertible secured notes payable with conversion features in April 2014 and issued detachable common stock warrants and secured debt with a partial conversion feature in April and May 2015. These embedded derivatives and detachable warrants were evaluated under ASC topic 815-40. We determined that the warrants and embedded conversion feature for the April 2014 issuance and the conversion feature for the 2015 issuances should be accounted for as derivative liabilities. We determined that the detachable warrants associated with the 2015 issuance should not be accounted for as derivative liabilities. Warrants and the debt conversion features determined to be derivative liabilities were bifurcated from the debt host and are classified as liabilities on the consolidated balance sheet. Warrants not determined to be derivative liabilities were recorded to debt discount and paid in capital. The Company records the warrants and embedded derivative liabilities at fair value and adjusts the carrying value of the common stock warrants and embedded derivatives to their estimated fair value at each reporting date with the increases or decreases in the fair value of such warrants and derivatives at each reporting date, recorded as a gain or (loss) in the consolidated statements of operations. The 2015 detachable warrants determined not to be derivative liabilities were recorded to debt discount with a corresponding entry to paid-in capital.

Revenue Recognition

We generate revenue from the sale of our clean power energy systems and from consulting services. Revenue is recognized when there is persuasive evidence of an arrangement, product delivery and acceptance have occurred, the sales price is fixed or determinable and collectability of the resulting receivable is reasonably assured. Amounts billed to clients for shipping and handling are classified as sales of product with related costs incurred included in cost of sales.

Provisions for discounts and rebates to customers, estimated returns and allowances, and other adjustments are provided for in the same period the related revenue is recorded. We defer any revenue for which the services have not been performed or are subject to refund until such time that we and our customer jointly determine that the services have been performed or no refund will be required.

Revenues under long-term construction contracts are generally recognized using the completed-contract method of accounting. Long-term construction-type contracts for which reasonably dependable estimates cannot be made or for which inherent hazards make estimates difficult are accounted for under the completed-contract method. Revenues under the completed-contract method are recognized upon substantial completion—that is acceptance by the customer, compliance with performance specifications demonstrated in a factory acceptance test or similar event. Accordingly, during the period of contract performance, billings and costs are accumulated on the balance sheet, but no profit or income is recorded before completion or substantial completion of the work. Anticipated losses on contracts are recognized in full in the period in which losses become probable and estimable. Changes in estimate of profit or loss on contracts are included in earnings on a cumulative basis in the period the estimate is changed. As of September 30, 2015 and December 31, 2014, we had no provision for contract losses.

Research and Development Costs

Research and development costs are expensed as incurred. Research and development costs were $928,000 and $514,000 for the three months ended September 30, 2015 and 2014, respectively and were $2,636,000 and $2,259,000 for the nine months ended September 30, 2015 and 2014 respectively.

Share-Based Compensation

We maintain an equity incentive plan and record expenses attributable to the awards granted under the equity incentive plan. We amortize share-based compensation from the date of grant on a weighted average basis over the requisite service (vesting) period for the entire award.

We account for equity instruments issued to consultants and vendors in exchange for goods and services at fair value. The measurement date for the fair value of the equity instruments issued is determined at the earlier of (i) the date at which a commitment for performance by the consultant or vendor is reached or (ii) the date at which the consultant's or vendor's performance is complete. In the case of equity instruments issued to consultants, the fair value of the equity instrument is recognized over the term of the consulting agreement.

In accordance with the accounting standards, an asset acquired in exchange for the issuance of fully vested, non-forfeitable equity instruments should not be presented or classified as an offset to equity on the grantor's balance sheet once the equity instrument is granted for accounting purposes. Accordingly, we record the fair value of the fully vested, non-forfeitable common stock issued for future consulting services as prepaid expense in our consolidated balance sheets.

Income Taxes

We account for income taxes under FASB ASC 740 "Income Taxes." Under the asset and liability method of FASB ASC 740, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statements carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Under FASB ASC 740, the effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period the enactment occurs. A valuation allowance is provided for certain deferred tax assets if it is more likely than not that we will not realize tax assets through future operations.

Earnings (Loss) per Share

Basic loss per share is computed by dividing net loss attributable to common stockholders by the weighted average number of common shares assumed to be outstanding during the period of computation. Diluted loss per share is computed similar to basic loss per share except that the denominator is increased to include the number of additional common shares that would have been outstanding if the potential shares had been issued and if the additional common shares were dilutive. Approximately 648,000 and 433,000 shares of common stock issuable upon full exercise of all options and warrants at September 30, 2015 and 2014, respectively and all shares potentially issuable in the future under the terms of the Secured Notes Payable were excluded from the computation of diluted loss per share due to the anti-dilutive effect on the net loss per share.

All share and per share amounts in the table below have been adjusted to reflect the 30-for-1 forward split of our issued and outstanding shares of common stock by way of a stock dividend on May 6, 2013 and the 1-for-50 reverse split of our issued and outstanding common stock on July 8, 2015, retroactively.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	**2014**	**2015**	**2014**
Net loss	$ (3,310,000)	$ (2,823,000)	$ (8,601,000)	$ (7,770,000)
Weighted average number of common shares outstanding:				
Basic and diluted	2,464,100	1,642,600	2,385,500	1,515,000
Net loss attributable to common stockholders per share:				
Basic and diluted	$ (1.34)	$ (1.72)	$ (3.61)	$ (5.13)

Comprehensive Income (Loss)

We have no items of other comprehensive income (loss) in any period presented. Therefore, net loss as presented in our Condensed Consolidated Statements of Operations equals comprehensive loss.

Recently Issued Accounting Pronouncements

In May, 2014, the FASB issued Accounting Standards Update ("ASU") 2014-09, Revenue from Contracts with Customers (Topic 606) ("ASU 2014-09"). ASU 2014-09 provides a framework for addressing revenue recognition issues and, upon its effective date, replaces almost all existing revenue recognition guidance, including industry-specific guidance, in current U.S. generally accepted accounting principles. ASU 2014-09 is effective beginning with the calendar year ended December 31, 2017. The Company has not yet assessed the impact ASU 2014-09 will have upon adoption on its financial position, results of operations or cash flows.

In August 2014, the FASB issued ASU 2014-15, Presentation of Financial Statements—Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern. ASU 2014-15 requires that an entity's management evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the entity's ability to continue as a going concern within one year after the date that the financial statements are issued. Substantial doubt about an entity's ability to continue as a going concern exists when relevant conditions and events, considered in the aggregate, indicate that it is probable that the entity will be unable to meet its obligations as they become due within one year after the date that the financial statements are issued. Certain disclosures are necessary in the footnotes to the financial statements in the event that conditions or events raise substantial doubt about an entity's ability to continue as a going concern. ASU 2014-15 is effective for the annual period ending after December 15, 2016, and for annual periods and interim periods thereafter and early application is permitted. The Company has not yet assessed the impact ASU 2014-15 will have upon adoption.

In November 2014, the FASB issued ASU 2014-16—Derivatives and Hedging: Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share is More Akin to Debt or to Equity. ASU 2014-16 clarifies how current GAAP should be interpreted in evaluating the economic characteristics and risks of a host contract in a hybrid financial instrument that is issued in the form of a share. ASU 2014-16 is effected for the interim and annual periods beginning after December 15, 2015. The Company has not yet assessed the impact ASU 2014-16 will have upon adoption.

In April 2015, the FASB issued ASU 2015-03, Interest—Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs. ASU 2015-03 simplifies the presentation of debt issuance costs by requiring that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs are not affected by the amendments in this update. ASU 2015-03 is effective for public business entities for financial statements issued for fiscal years beginning after December 15, 2015 and interim periods within those fiscal years and early application is permitted. The Company has elected to adopt ASU 2015-03 beginning with the interim period ending June 30, 2015. There were no impacts to any prior periods presented as a result of adopting ASU 2015-03.

In July 2015, the FASB issued ASU 2015-11, Inventory (Topic 330): Simplifying the Measurement of Inventory. ASU 2015-11 requires that entities measure inventory at the lower of cost and net realizable value. ASU 2015-11 is effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years and early application is permitted. The Company has not yet assessed the impact ASU 2015-11 will have upon adoption.

Note 3—Inventory

Inventory consists of Power Oxidizer parts used interchangeably as raw materials and as spare parts for the EC250 units installed to date. Inventory totaled $133,000 and $53,000 as of September 30, 2015 and December 31, 2014, respectively, and consisted of raw materials. The Company had no inventory reserve during 2015 or 2014.

Note 4—Prepaid expenses and other current assets

Prepaid expenses and other current assets consisted of the following:

	September 30, 2015 (unaudited)	December 31, 2014
Prepaid rent	$ 27,000	$ 27,000
Prepaid insurance	37,000	31,000
Prepaid offering costs	351,000	—
Prepaid fees	5,000	5,000
Prepaid deposit	32,000	8,000
Prepaid legal fees	22,000	20,000
Total	$ 474,000	$ 91,000

Note 5—Property and Equipment, Net

Property and equipment, net consisted of the following:

	September 30, 2015 (unaudited)	December 31, 2014
Machinery and equipment	$ 2,154,000	$ 849,000
Office furniture and fixtures	217,000	198,000
Computer equipment and software	166,000	149,000
Construction in progress	664,000	164,000
Total cost	3,201,000	1,360,000
Less accumulated depreciation	(877,000)	(605,000)
Net	$ 2,324,000	$ 755,000

During the nine months ended September 30, 2015 the Company spent approximately $1.3 million on a multi-fuel test facility located at our headquarters in Irvine, California. We placed this self-constructed asset in service in the second quarter of 2015.

Assets recorded under capital leases and included in property and equipment in our balance sheets consist of the following:

	September 30, 2015 (unaudited)	December 31, 2014
Machinery and equipment	$ 27,000	$ 27,000
Computer equipment and software	61,000	46,000
Total assets under capital lease	88,000	73,000
Less accumulated depreciation	(42,000)	(21,000)
Net assets under capital lease	$ 46,000	$ 52,000

Depreciation expense consisted of the following:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Research and development	$ 90,000	$ 26,000	$ 189,000	$ 77,000
General and administrative	29,000	26,000	87,000	77,000
	$ 119,000	$ 52,000	$ 276,000	$ 154,000

Amortization of assets under capital lease was $6,000 and $5,000 for the three months ended September 30, 2015 and 2014, respectively, and $13,000 and $10,000 for the nine months ended September 30, 2015 and 2014, respectively.

Note 6—Intangibles, Net

Intangibles, net consisted of the following:

	September 30, 2015	December 31, 2014
	(unaudited)	
Patents	$ 80,000	$ 80,000
Less accumulated amortization	(51,000)	(46,000)
Net	$ 29,000	$ 34,000

This intangible asset is amortized over its remaining life. Amortization expense related to this intangible asset was $1,000 and $3,000 for the three and nine months ended September 30, 2015 and 2014, respectively.

Amortization expense on intangible assets for the year ended December 31, 2015 and for each of the three succeeding years is $6,000 per year and a total of $7,000 thereafter.

The value capitalized for intangible assets represents the acquisition cost for purchased patents. We continue to invest in our intellectually property portfolio and are actively filing for patent protection for our technology in both the United States and abroad. The costs for these filings, including legal, associated with compiling and filing patent applications are expensed in selling, general and administrative expenses as incurred.

Note 7—Accrued Expenses

Accrued expenses consisted of the following:

	September 30, 2015	December 31, 2014
	(unaudited)	
Accrued professional fees	$ 348,000	$ 280,000
Accrued vacation	139,000	92,000
Accrued bonuses	150,000	—
Accrued other	64,000	49,000
Accrued interest	50,000	—
Accrued liabilities owed by Parent—reimbursable under Contribution Agreement	—	35,000
Total accrued expenses	$ 751,000	$ 456,000

Note 8—Deferred revenues and customer advances

Deferred revenues and customer advances consist of balances billed on existing customer contracts for which the revenue cycle is not complete. Customer advances on equipment sales represent down payments and progress payments under the terms and conditions of equipment sales of our Power Oxidizer and Power Station units. Prepaid license fees represent payments of license fees by Dresser-Rand into an escrow account. Deferred revenues and customer advances consisted of the following:

	September 30, 2015 (unaudited)	December 31, 2014
Customer advances on equipment sales	609,000	—
Prepaid license fees	400,000	—
Total Deferred revenues and customer advances	$ 1,009,000	$ —

Note 9—Secured Notes Payable

Secured Notes

During the nine months ended September 30, 2015, the Company sold senior secured promissory notes with an aggregate principal amount of $5.0 million (the "Notes") in two separate tranches. Other than the issuance date and the term of the respective notes and warrants issued, the notes and warrants were identical for both tranches. On April 23, 2015, the Company closed the first tranche representing $3.1 million in aggregate principal amount of Notes issued in a private placement to seven institutional investors and on May 7, 2015 the Company closed the second tranche, representing $1.9 million in aggregate principal amount of Notes to four institutional investors. The Company received total gross proceeds of $5.0 million, less transaction expenses of $0.3 million consisting of legal costs and placement agent fees. The Company agreed to pay the placement agent 5% of the aggregate principal amount of the Notes, which was paid at the closing date of the second tranche. The Company plans to continue to use the proceeds from the Notes offering for general corporate purposes.

The Notes bear interest at a rate of 12% per year, payable monthly, and are set to mature on the two year anniversary of the issuance dates of the Secured Notes on April 23, 2017 and May 7, 2017 for the first and second tranches, respectively. The Notes have a limited conversion feature. At the discretion of each investor, up to 50% of the principal balance of the Notes may be exchanged for shares of the Company's common stock if the Company consummates a registered underwritten public offering of equity securities with aggregate gross offering proceeds of at least $10 million (the "Qualified Public Offering"). The conversion period begins on the date of the consummation of the Qualified Public Offering and ends thirty days after the consummation of the Qualified Public Offering (the "Conversion Period"). The conversion price is the price per share of common stock sold in the Qualified Public Offering. The Notes may be repaid by the Company at any time except during a Conversion Period and unless the Notes are in default.

The Notes are secured by substantially all assets of the Company and provides for specified events of default, including: i) failure to pay principal and interest when due, and ii) failure to effectuate a reverse stock split on or prior to the three month anniversary of the first tranche of Notes. In addition, the Company must consummate a Qualified Public Offering on or prior to the six month anniversary of the first tranche of Notes. Any event of default may be waived by the holders of at least a majority of the aggregate principal amount of Notes, which must include a specified holder under specified circumstances. Upon the occurrence of an event of default, the interest rate immediately increases to 18% per annum and the Notes become convertible at a price per share equal to 85% of the average of the five lowest volume weighted average prices of the Company's common stock during a 15 consecutive trading day period immediately prior to the applicable conversion date.

Effective as of October 22, 2015, we executed a Second Amendment to Securities Purchase Agreement dated April 22, 2015, and a First Amendment to Securities Purchase Agreement dated May 7, 2015 (collectively, the "October Amendments"), each with certain investors holding the requisite number of conversion shares and warrant shares underlying the Notes and warrants issued in April 2015 and May 2015 pursuant to the referenced purchase agreements. The October Amendments extend the deadline to November 30, 2015 for the Company's consummation of a firm commitment underwritten public offering registered under the Securities Act of 1933, as amended, with aggregate gross proceeds to the Company equal to or in excess of $10,000,000, and related listing of its common stock on a national securities exchange.

The Notes were issued with detachable warrants to purchase 219,785 shares of the Company's common stock, exercisable for five years with an exercise price of $12.50 per share. The Company valued the warrants issued using the Black-Scholes option model at a combined $2,139,000 using an exercise price of $12.50 per share, a grant date fair value of $11.00–$11.25 per share, a risk free rate of 0.87%–1.02%, a five year life, and a volatility of 78%–83% for the April 23, 2015 and May 7, 2015 warrant valuations. The Company evaluated the accounting of the detachable warrants and determined that the warrants should not be accounted for as derivative liabilities.

The Company valued the embedded conversion feature using the Black Scholes option model at a combined $611,000 representing an option to convert $2,500,000 of debt at market prices until 30 days following the deadline of the Qualified Public Offering covenant using an exercise price and grant date fair value of $11.00–$11.25 per share, a risk free rate of 0.23%–0.25%, a seven month life, and a volatility of 138%–148%. The Company evaluated the accounting of the embedded conversion feature and determined that they should be accounted for as derivative liabilities.

Each holder may require us to redeem the Notes at a price equal to 115% of the sum of portion of the principal to be redeemed plus accrued and unpaid interest thereon and any accrued and unpaid late charges, if any, with respect to such principal and interest.(the "Conversion Amount") being redeemed (a) upon our default under the Notes, or (b) if we enter into a merger or consolidation, or sell or assign all or substantially all of our assets. In addition, at any time from and after the date that is the eighteen month anniversary of the original issuance date of the Notes, each holder shall have the right, in its sole and absolute discretion, at any time or times, to require that we redeem all or any portion of the Conversion Amount of its Note then outstanding at a price equal to 100% of the Conversion Amount of the portion of the Note being redeemed.

At any time after the issuance of the Notes, other than (i) at any time during which an event of default has occurred and is continuing or (ii) from the time we publicly announce a Qualified Public Offering through and including the date that is thirty days immediately following the consummation of such Qualified Public Offering, we have the right to redeem all or any portion of the Conversion Amount then remaining under the Notes, or a Company Optional Redemption; provided, that the aggregate Conversion Amount under Notes being redeemed shall be at least $500,000, or such lesser amount that is then outstanding under the Notes. The conversion price for such Company Optional Redemption shall be a price equal to 100% of the Conversion Amount of the Notes being redeemed.

The Notes were initially recorded net of a discount of $2,750,000, reflecting the fair value of the warrants and embedded conversion feature derivatives within the Notes on the issuance date and $303,000 of offering costs, representing cash placement fees and legal expenses. Both the $2,750,000 debt discount and the $303,000 of offering costs will be amortized through interest expense on the condensed consolidated statements of operations, using the effective interest method, over the expected term of the Notes.

Notes payable consisted of the following as of September 30, 2015:

	Notes	Debt Discount	Offering Costs	Net Total
Original Value	$ 5,000,000	$ (2,750,000)	(303,000)	$ 1,947,000
Amortization of debt discount and deferred financing costs	—	1,752,000	169,000	1,921,000
Ending balance—September 30, 2015	5,000,000	(998,000)	(134,000)	3,868,000
Less: Current Portion	(2,500,000)	159,000	17,000	(2,324,000)
Long Term Portion	$ 2,500,000	$ (839,000)	(117,000)	$ 1,544,000

Derivative Liabilities

We evaluate any freestanding financial instruments or embedded features that have the characteristics of a derivative, and to any freestanding financial instruments that are potentially settled in an entity's own common stock to determine if they are indexed to an entity's own stock.

Derivative liabilities consisted of the following:

	Warrants Liability	Embedded Note Conversion Feature	Total
Value as of December 31, 2014	$ 402,000	$ —	$ 402,000
Adjustment to fair value—warrants	277,000	—	277,000
Exchange of warrants for common stock—April 2, 2015	$ (679,000)	$ —	$ (679,000)
Issuance of Notes	—	611,000	611,000
Adjustment to fair value—conversion feature	—	(171,000)	(171,000)
Ending balance—September 30, 2015	$ —	$ 440,000	$ 440,000

Warrant Liability:

We issued warrants for the purchase of up to 81,942 shares of our common stock in conjunction with our April 2014 convertible notes offering. During 2014, the convertible notes were either redeemed or converted into common stock of the Company. The warrants that were issued with the April 2014 convertible notes were not issued with the intent of effectively hedging any future cash flow, fair value of any asset, liability or any net investment in a foreign operation. The warrants do not qualify for hedge accounting, and as such, all future changes in the fair value of these warrants will be recognized currently in earnings until such time as the warrants are exercised or expire. These warrants do not trade in an active securities market, and as such, we estimate the fair value of these warrants and embedded conversion features using the Binomial pricing model using the following assumptions:

	2015
Annual dividend yield	—
Expected life (years)	4.04
Risk-free interest rate	0.99%
Expected volatility	134%

Expected volatility is based primarily on historical volatility of us and our peer group. Historical volatility was computed using weekly pricing observations for us and daily pricing observations for our peer group for recent periods that correspond to the expected term. We believe this method produces an estimate that is representative of our expectations of future volatility over the expected term of these warrants.

We currently have no reason to believe future volatility over the expected remaining life of these warrants is likely to differ materially from historical volatility. The expected life is based on the remaining term of the warrants. The risk-free interest rate is based on one-year to five-year U.S. Treasury securities consistent with the remaining term of the warrants.

On April 2, 2015, we entered into a warrant exchange agreement with five institutional investors as describe in Notes 11 and 12 below. As a result of this exchange, we marked the warrants to market on April 2, 2015 and exchanged 81,942 warrants for 73,747 shares of common stock. The shares of common stock were issued to the investors on April 17, 2015. We incurred a loss of $279,000 as a result of the exchange, recorded in other expense in the condensed, consolidated statement of operations.

Embedded conversion feature liability:

The Notes were issued with a feature that allows for up to 50% of the principal to be converted into our common stock. We determined that this embedded conversion feature should be accounted for as a derivative. The grant date fair value of the embedded derivatives, which requires bifurcation from the Notes described above, were recorded within short-term liabilities on the condensed consolidated balance sheet. The embedded derivatives relate to the conversion option, redemption in the case of an event of default and redemption in the case of a change in control features of the convertible secured note. The embedded derivatives will be marked to market quarterly, with any change recorded as an adjustment to the carrying value of these liabilities and the gain or (loss) on warrants and derivatives liabilities recorded in the consolidated statements of operations. The fair value of the warrants and embedded derivatives from the issuance date to September 30, 2015 declined $0.2 million. Accordingly, this amount was recorded as a gain on derivative liabilities in the condensed consolidated statements of operations. The embedded derivatives were valued using Black-Scholes option pricing model where the exercise price was equal to the market price on the valuation date and the following assumptions:

	2015
Annual dividend yield	—
Expected life (years)	0.1-0.6 years
Risk-free interest rate	0.22-0.38%
Expected volatility	118–148%

Expected volatility is based primarily on historical volatility of us and our peer group. Historical volatility was computed using weekly pricing observations for us and daily pricing observations for our peer group for recent periods that correspond to the expected term. We believe this method produces an estimate that is representative of our expectations of future volatility over the expected term of these warrants.

We currently have no reason to believe future volatility over the expected remaining life of these embedded derivatives is likely to differ materially from historical volatility. The expected life is based on the remaining term of the conversion option. The risk-free interest rate is based on the U.S. Treasury securities consistent with the remaining term of the embedded derivatives.

Note 10—Fair Value Measurements and Disclosures

Fair value is defined as the price that would be received upon sale of an asset or paid upon transfer of a liability in an orderly transaction between market participants at the measurement date and in the principal or most advantageous market for that asset or liability. The fair value should be calculated based on assumptions that market participants would use in pricing the asset or liability, not on assumptions specific to the entity. In addition, the fair value of liabilities should include consideration of non-performance risk, including the Company's own credit risk.

Inputs used in measuring fair value are prioritized into a three-level hierarchy based on whether the inputs to those measurements are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's market assumptions. The fair-value hierarchy requires the use of observable market data when available and consists of the following levels:

- Level 1—Quoted prices for identical instruments in active markets;
- Level 2—Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations in which all significant inputs are observable in active markets; and
- Level 3—Valuations derived from valuation techniques in which one or more significant inputs are unobservable.

The following tables present information on the Company's financial instruments:

	Fair Value	Level 1	Level 2	Level 3
Derivative liabilities				
Cash and cash equivalents, including restricted cash	$ 1,522,000	$ 1,522,000	$ —	$ —
Embedded note conversion feature	$ 440,000	$ —	$ —	$ 440,000

Note 11—Capital Leases Payable

Capital Leases Payable

Capital leases payable consisted of the following:

	September 30, 2015 (unaudited)	December 31, 2014
Capital lease payable to De Lange Landon secured by forklift, 10.0% interest, due on October 1, 2018, monthly payment of $452.	$ 14,000	$ 17,000
Capital lease payable to Dell Computers secured by computer equipment, 15.09% interest, due on November 16, 2016, monthly payment of $592.	8,000	12,000
Capital lease payable to Dell Computers secured by computer equipment, 15.09% interest, due on December 15, 2016, monthly payment of $590.	8,000	12,000
Capital lease payable to Dell Computers secured by computer equipment, 15.09% interest, due on January 3, 2017, monthly payment of $405.	6,000	8,000
Capital lease payable to Dell Computers secured by computer equipment, 15.09% interest, due on January 3, 2017, monthly payment of $394.	10,000	—
Total capital leases	46,000	49,000
Less: current portion	(26,000)	(19,000)
Long-term portion of capital leases	$ 20,000	$ 30,000

The future minimum lease payments required under the capital leases and the present value of the net minimum lease payments as of September 30, 2015, are as follows:

	Year Ending December 31	Amount
	2015	$ 7,000
	2016	29,000
	2017	10,000
	2018	5,000
Net minimum lease payments		51,000
Less: Amount representing interest		(4,000)
Less: Taxes		(1,000)
Present value of net minimum lease payments		46,000
Less: Current maturities of capital lease payables		(26,000)
Long-term capital lease payables		$ 20,000

Note 12—Equity

On April 2, 2015, the Company entered into exchange agreements with the holders of all of the warrants issued in connection with the convertible notes offering in April 2014. As of March 31, 2015, the warrants were carried as derivative liabilities. On April 16, 2015, the exchange transaction was completed, with the Company issuing 73,747 shares of common stock (the "Exchange Shares") in exchange for the return and cancellation of all of the warrants exercisable for up to an aggregate 81,942 shares of the common stock. The Exchange Shares were subject to a lock-up agreement that prohibited any sale or transfer (subject to certain limited exceptions) of the Exchange Shares until the earlier of June 1, 2015 or the first date that the weighted average price of the common stock equaled or exceeded $0.30 (as adjusted for any stock split, stock dividend, stock combination, reclassification or similar transaction occurring after the closing of the exchange transaction) for each of ten (10) consecutive trading days. The value of the Exchange Shares issued on the date of the exchange was $885,000. Prior to the exchange, we marked the warrants to market and recorded an additional loss on adjustment of derivative liabilities to reflect the market value of the warrants as of the date of the exchange. The $278,000 difference between the market value of the shares issued, valued at the closing market price on April 2, 2015, and the value of the warrants was recorded as a loss on exchange of warrants, represented in other expense on the condensed, consolidated statement of operations.

In May 2015, we issued 108,000 shares of common stock to 30 accredited investors and received gross proceeds of $810,000 in cash. We paid placement fees and legal costs of $70,000 in cash, and we issued warrants to purchase 5,514 shares of the Company at an exercise price of $12.50 per share to the placement agent. The warrants expire in May 2020.

Reverse Stock Split

The board of directors of the Company approved the Reverse Stock Split, at a ratio of 1-for-50, effective as of the Effective Date. As a result of the Reverse Stock Split, the authorized preferred stock decreased to 1,000,000 shares and the authorized common stock decreased to 4,000,000 shares. Both the preferred stock and the common stock par value remained at $0.0001 per share. On September 3, 2015, as a result of the Company's adoption of a new certificate of incorporation in conjunction with its conversion to a Delaware corporation, the authorized preferred shares increased to 50,000,000 shares and the authorized common shares increased to 200,000,000 shares.

On the Effective Date, the total number of shares of common stock held by each stockholder of the Company were converted automatically into the number of shares of common stock equal to: (i) the number of issued and outstanding shares of common stock held by each such stockholder immediately prior to the Reverse Stock Split divided by (ii) 50. The Company issued one whole share of the post-Reverse Stock Split common stock to any stockholder who otherwise would have received a fractional share as a result of the Reverse Stock Split, determined at the beneficial owner level by share certificate. As a result, no fractional shares were issued in connection with the Reverse Stock Split and no cash or other consideration will be paid in connection with any fractional shares that would otherwise have resulted from the Reverse Stock Split. The Reverse Stock Split also affected all outstanding options and warrants by dividing each option or warrant outstanding by 50, rounded up to the nearest option or warrant, and multiplying the exercise price by 50 for each option or warrant outstanding.

The number of shares of common stock outstanding immediately prior to the Reverse Stock Split was 123,193,755, and on the Effective Date, there were 2,463,919 shares of common stock outstanding. On July 15, 2015, the Company issued 241 additional shares of common stock to reflect the rounding up of fractional shares outstanding on the Effective Date. The number of shares underlying outstanding warrants and options immediately prior to the Reverse Stock Split was 16,951,674 and 15,423,051, respectively, and the number of shares underlying outstanding warrants and options after the Reverse Stock Split was 339,043 and 308,464, respectively. As a result of the Reverse Stock Split, the weighted average exercise price of the outstanding warrants increased from $0.36 per share to $17.81 per share and the weighted average exercise price of the outstanding options increased from $0.27 per share to $13.61 per share.

Note 13—Stock Options and Warrants

Stock options

On July 1, 2013, our board of directors adopted and approved the 2013 Equity Incentive Plan (the "2013 Plan") and amended the 2013 Plan on March 24, 2015 to increase the number of shares available for issuance. The 2013 Plan authorizes us to grant non-qualified stock options and restricted stock purchase rights to purchase up to 420,000 shares of our common stock with vesting to employees (including officers) and other service providers. With the approval of the 2015 Plan described below, as of September 30, 2015, no shares of our common stock were available for issuance under the 2013 Plan.

On July 15, 2015, our board of directors approved the 2015 Omnibus Incentive Plan (the "2015 Plan"), which was approved by our stockholders on August 28, 2015. The 2015 Plan authorizes us to grant up to 300,000 shares of our common stock and is intended to replace the 2013 Equity Incentive Plan. If the 2015 Plan is approved by our stockholders, no additional grants will be made under the 2013 Plan.

The 2015 Plan permits the granting of any or all of the following types of awards: incentive stock options, non-qualified stock options, stock appreciation rights, restricted stock, restricted stock units, other stock-based awards, and performance awards payable in a combination of cash and company shares. There were no awards granted under the 2015 through September 30, 2015.

The 2015 Plan has the following limitations:

- *Limitation on terms of stock options and stock appreciation rights*. The maximum term of each stock option and stock appreciation right (SAR) is 10 years.

- *No repricing or grant of discounted stock options*. The 2015 Plan does not permit the repricing of options or SARs either by amending an existing award or by substituting a new award at a lower price without stockholder approval. The 2015 Plan prohibits the granting of stock options or SARs with an exercise price less than the fair market value of our common stock on the date of grant.

- *Clawback*. Awards granted under the 2015 Plan are subject to any then current compensation recovery or clawback policy of the Company that applies to awards under the 2015 Plan and all applicable laws requiring the clawback of compensation.

- *Double-trigger acceleration.* Acceleration of the vesting of awards that are assumed or replaced by the resulting entity after a change in control is not permitted unless an employee's employment is also terminated by the Company without cause or by the employee with good reason within two years of the change in control.

- *Code Section 162(m) Eligibility*. The 2015 Plan provides flexibility to grant awards that qualify as "performance-based" compensation under Internal Revenue Code Section 162(m).

- *Dividends*. Dividends or dividend equivalents on stock options, SARs or unearned performance shares under the 2015 Plan will not be paid.

At September 30, 2015, total unrecognized deferred stock compensation expected to be recognized over the remaining weighted-average vesting periods of 1.1 years for outstanding grants was $3.0 million.

The fair value of option awards is estimated on the grant date using the Black-Scholes option valuation model.

Estimates of fair value are not intended to predict actual future events or the value ultimately realized by employees who receive equity awards, and subsequent events are not indicative of the reasonableness of the original estimates of fair value made by us. The following table presents the weighted-average grant date assumptions used to estimate the fair value of options and stock appreciation rights granted.

	September 30, 2015
Expected volatility	100-150%
Dividend yield	0.00%
Risk-free interest rate	1.10–2.15%
Expected life (in years)	3.0-6.8

Expected volatility represents the estimated volatility of the shares over the expected life of the options. We have estimated the expected volatility based on the weighted-average historical volatilities of a pool of public companies that are comparable to Ener-Core.

We use an expected dividend yield of zero since no dividends are expected to be paid. The risk-free interest rate for periods within the expected life of the option is derived from the U.S. treasury interest rates in effect at the date of grant. The expected option life represents the period of time the option is expected to be outstanding. The simplified method is used to estimate the term since we do not have sufficient exercise history to calculate the expected life of the options.

Stock-based compensation expense is recorded only for those awards expected to vest. Currently, the forfeiture rate is zero. The rate is adjusted if actual forfeitures differ from the estimates in order to recognize compensation cost only for those awards that actually vest. If factors change and different assumptions are employed in future periods, the share-based compensation expense may differ from that recognized in previous periods.

Stock-based award activity was as follows:

Options	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Life	Aggregate Intrinsic Value
Balance, December 31, 2014	267,257	$ 15.00	6.51	$ 47,000
Forfeited during 2015	(21,033)	17.00	—	—
Granted during 2015	62,240	8.30	—	—
Balance, September 30, 2015	308,464	$ 13.61	6.32	$ —
Exercisable on September 30, 2015	129,240	$ 15.72	5.50	$ —

The options granted have a contract term ranging between three and ten years. Options granted typically vest over a four year period, with 25% vesting after one year and the remainder ratably over the remaining three years.

The following table summarizes information about stock options outstanding and exercisable at September 30, 2015:

	Options Outstanding					Options Exercisable		
Exercise Prices	Number of Shares		Weighted-Average Remaining Contractual Life (In years)		Weighted-Average Exercise Price	Number of Shares		Weighted-Average Exercise Price
$0–$10.00	118,840	$	8.02	$	7.74	31,912	$	7.70
$10.01–$15.00	34,888		8.12	$	12.50	6,254	$	12.50
$15.01–$20.00	132,178		4.51	$	17.50	72,775	$	17.50
$20.01–$25.00	22,558		5.22	$	23.47	18,299	$	23.71
	308,464	$	6.32	$	13.61	129,240	$	15.72

Restricted stock represents stock purchased by employees prior to July 1, 2013 for which the Company has a right to repurchase. The repurchase rights lapse over time until December 31, 2015 at which time all restricted shares are vested. Restricted stock activity for the nine months ended September 30, 2015 was as follows:

	Shares		Weighted-Average Grant Price
Unvested Balance, December 31, 2014	15,720	$	0.05
Repurchase of unvested restricted shares	—		—
Vested	(11,554)	$	0.05
Unvested Balance, September 30, 2015	4,166	$	0.05

Stock based compensation expense consisted of the following:

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2015		2014		2015		2014	
Research and development	$	148,000	$	184,000	$	443,000	$	1,178,000
General and administrative		224,000		260,000		670,000		1,635,000
	$	372,000	$	444,000	$	1,113,000	$	2,813,000

Warrants

From time to time, we issue warrants to purchase shares of our common stock to investors, note holders and to non-employees for services rendered or to be rendered in the future. The following table represents the activity for warrants outstanding, exchanged, and issued for the nine months ending September 30, 2015.

Balance outstanding at December 31, 2014	195,681	$	26.94
Exchanged for Common Stock	(81,942)		5.50
Issued for Senior Notes and Services	225,304		12.50
Balance outstanding at September 30, 2015	339,043	$	17.81

For the outstanding warrants exercisable for 339,043 shares of our common stock at September 30, 2015, the weighted average exercise price per share was $17.81 and the weighted average remaining life was 4.25 years. The warrants outstanding as of September 30, 2015 had no intrinsic value.

Warrants outstanding as of September 30, 2015 consist of:

	Issue Date	Expiry Date	Number of Warrants	Exercise Price per Share
2013 Services Warrants—July	Jul-13	Jul-18	9,494	$ 37.50
2013 Services Warrants—August	Aug-13	Aug-18	729	37.50
2013 Services Warrants—November	Nov-13	Nov-18	2,400	50.00
2014 Services Warrants—April(1)	Apr-14	Apr-19	13,657	39.00
2014 Services Warrants—September(2)	Aug-14	Aug-19	16,000	25.00
2014 PIPE Warrants—September(3)	Sept-14	Sept-18	26,500	25.00
2014 Services Warrants—November(4)	Nov-14	Nov-18	6,500	25.00
2014 Settlement Warrants—December(5)	Dec-14	Dec-19	38,464	25.00
2015 Senior Notes Warrants(6)	Apr/May-15	Apr/May-20	219,785	12.50
2015 Services Warrants – May	May-15	May-15	5,514	12.50
Balance outstanding at September 30, 2015			339,043	$ 17.81
Warrants exercisable at September 30, 2015			339,043	$ 17.81

(1) The 2014 Services Warrants—April were issued for fees incurred in conjunction with the issuance of convertible notes in 2014. The warrants were valued on the issuance date at $11.50 per share in conjunction with the valuation approach used for the initial valuation of the warrants issued in connection with the convertible notes issued in 2014.

(2) The 2014 Services Warrants—September were issued to a consultant in exchange for advisory services with no readily available fair value. The warrants were originally issued at $39.00 per share and had a one-time price reset provision to the exercise price of the warrants issued to investors in the convertible notes offering in April 2014 if the exercise price of such convertible notes warrants changed prior to the September 30, 2014. On September 22, 2014, the exercise price was changed to $25.00 per share. There are no further exercise price changes for this warrant series. The warrants were valued using the Black-Scholes option pricing model at $131,000 on the issuance date with an additional $6,000 recorded to expense on September 22, 2014 to reflect the change in fair value resulting from the exercise price change.

(3) On September 22, 2014 the Company issued 26,500 warrants with an exercise price of $25.00 per share in conjunction with placement agent services for the Company's September 2014 private equity placement. The warrants were valued using the Black-Scholes option pricing model at $296,000 on the issuance date.

(4) On November 26, 2014, the Company issued 6,500 warrants with an exercise price of $25.00 per share for compensation for investor relations services provided. The warrants were valued using the Black-Scholes option pricing model at $43,000 on the issuance date.

(5) On December 1, 2014, the Company issued 19,232 warrants with an exercise price of $39.00 per share and on December 15, 2014 issued 19,232 warrants with an exercise price of $25.00 per share to settle potential legal disputes resulting from claims made by the investors in the November 2013 private equity placement. The warrants issued on December 1, 2014 were issued concurrent with the issuance of 8,462 shares of the Company's common stock in partial settlement of the potential legal disputes arising from claims by two investors. The Company settled all remaining potential legal disputes with all of the remaining investors in the November 2013 private placement on December 15, 2014 by issuing the second tranche of warrants and setting the exercise price of each warrant series issued at $25.00 with no further reset provisions. The combined issuance of the warrants and expense resulting from any price changes were valued using the Black-Scholes option pricing model at $246,000 and expensed to general and administrative expense.

(6) On April 23, 2015 the Company issued warrants exercisable for up to 136,267 shares of our common stock and on May 7, 2015 the Company issued warrants exercisable for 83,518 shares of our common stock, each with an exercise price of $12.50 per share in conjunction with the Senior Notes described in Note 9. The warrants were valued using the Black-Scholes option pricing model at $2,139,000 on the issuance date.

(7) On May 7, 2015 the Company issued warrants exercisable for 5,514 shares of our common stock with an exercise price of $12.50 per share in conjunction with placement agent services for the Company's May 2015 private equity placement. The warrants were valued using the Black-Scholes option pricing model at $56,000 on the issuance date.

Note 14—Commitments and Contingencies

We may become a party to litigation in the normal course of business. We accrue for open claims based on our historical experience and available insurance coverage. In the opinion of management, there are no legal matters involving us that would have a material adverse effect upon our financial condition, results of operations or cash flows.

Warranties

Our warranty policy generally provides coverage for components of the Power Oxidizer that we produce. Typically, the coverage period is one calendar year from the date of commissioning. Provisions for estimated expenses related to product warranties are made at the time products are commissioned. These estimates are established using available information on the nature, frequency, and average cost of claims. Revision to the reserves for estimated product warranties is made when necessary, based on changes in these factors. Management actively studies trends of claims and takes action to improve product quality and minimize claims.

The following table presents the changes in the product warranty accrual included in accrued expenses in the accompanying condensed consolidated balance sheets for the nine months ended September 30, 2015:

		2015
Beginning balance, January 1, 2015	$	242,000
Charged to cost of revenues		—
Usage		(212,000)
Ending balance, September 30, 2015	$	30,000

Product Liability

With respect to product liability claims involving our products, we believe that any judgment against us for actual damages will be adequately covered by our recorded accruals and, where applicable, excess liability insurance coverage.

Lease

We lease our office facility, research and development facility and certain equipment under operating leases, which for the most part, are renewable. Certain leases also provide that we pay insurance and taxes.

Future minimum rental payments under operating leases that have initial noncancellable lease terms in excess of one year as of September 30, 2015 are as follows:

Three Months ending December 31, 2015		79,000
Year Ending December 31, 2016		315,000
	$	394,000

Minimum rent payments under operating leases are recognized on a straight-line basis over the term of the lease. Rent expense, net of sublease income, was $73,000 and $166,000 for three and nine months ended September 30, 2014, respectively, and $79,000 and $233,000 for the three and nine months ended September 30, 2015, respectively.

Our current headquarters is located at 9400 Toledo Way, Irvine, California 92618. The property consists of a mixed use commercial office, production, and warehouse facility of 32,649 square feet. Effective August 1, 2014, we assumed this lease. The lease has a remaining term of 18 months and expires December 31, 2016. The monthly base rent is $26,044 and increases on an annual basis.

In addition, we lease space from the Regents of the University of California, Irvine, for the installation and demonstration of the EC250 equipment. The lease expired on January 1, 2015 and reverted to a month-to-month lease with a monthly payment of $7,780.

Note 15—Subsequent Events

Effective as of October 22, 2015, we executed a Second Amendment to Securities Purchase Agreement dated April 22, 2015, and a First Amendment to Securities Purchase Agreement dated May 7, 2015 (collectively, the "October Amendments"), each with certain investors holding the requisite number of conversion shares and warrant shares underlying the notes and warrants issued in April 2015 and May 2015 pursuant to the referenced purchase agreements. The October Amendments extend the deadline to November 30, 2015 for the Company's consummation of a firm commitment underwritten public offering registered under the Securities Act of 1933, as amended, with aggregate gross proceeds to the Company equal to or in excess of $10,000,000, and related listing of its common stock on a national securities exchange.

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

Unless otherwise indicated, the following discussion and analysis of our financial condition is as of September 30, 2015. Our results of operations should be read in conjunction with our unaudited condensed consolidated financial statements and notes thereto included elsewhere in this quarterly report on Form 10-Q and the audited consolidated financial statements and the notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2014.

Forward-Looking Statements

Forward-looking statements contained in this quarterly report on Form 10-Q are made under the Safe Harbor Provision of the Private Securities Litigation Reform Act of 1995. These forward-looking statements involve risks, uncertainties, assumptions, and other factors, which, if they do not materialize or prove correct, could cause our results to differ materially from historical results, or those expressed or implied by such forward-looking statements. All statements, other than statements of historical fact, are statements that could be deemed forward-looking statements, including statements containing the words "can," "may," "scheduled, "planned," "expects," "believes," "strategy," "opportunity," "anticipates," and similar words. These statements may include, among others, plans, strategies, and objectives of management for future operations; any statements regarding proposed new products, services, or developments; any statements regarding future economic conditions or performance; statements of belief; and any statements of assumptions underlying any of the foregoing. The information contained in this quarterly report on Form 10-Q is as of the date of this report. Except as otherwise expressly referenced herein, we assume no obligation to update forward-looking statements.

Overview

We design, develop, manufacture and have commercially deployed products based on proprietary technologies that generate base-load, clean power from polluting waste gases that are otherwise typically destroyed or vented into the atmosphere by a variety of industries. We consider "power" to consist of industrial grade heat that can be used to (i) generate electricity by coupling our technology with a variety of modified gas turbines, (ii) produce industrial-grade steam by coupling our technology with a variety of modified steam boilers, or (iii) provide on-site heat at industrial facilities through heat exchanger applications. We also design our technologies to provide power generation solutions with a significantly reduced air emissions profile compared to traditional industrial power generation systems powered by fossil fuels. Whether our technology is applied to generate electricity, steam or heat, we refer to our technology as "Power Oxidation," and refer to our products as "Power Oxidizers" (previously called "Gradual Oxidation" and "Gradual Oxidizer," respectively, in our prior public disclosures). Our patented Power Oxidizer turns one of the world's most potent sources of air pollution into a profitable source of base-load clean energy, while simultaneously reducing gaseous emissions from industrial facilities that contribute to air pollution and climate change.

Our technology offers an alternative to traditional methods of destroying gaseous pollution, by simultaneously enabling industrial facilities (i.e., the sources of the gaseous emissions) to reduce their energy costs through the generation of on-site power from their waste gases and eliminating or reducing their air pollution. In addition, our technology provides an innovative alternative method that a wide range of industrial facilities could deploy in order to comply with or exceed environmental air quality regulations, which currently represent a significant operating cost for these industries. We currently partner with established manufacturers of gas turbines and work with the engineering teams of these manufacturers to integrate our Power Oxidizer with their gas turbines. These partnerships benefit us through improved brand awareness and facilitation of the commercialization of our Power Oxidizer technology. The coupling or integration of our technology with gas turbines allows our partners to market their modified gas turbines into new markets and sales opportunities that otherwise are not technically feasible with traditional power generation technologies. We also plan to partner with manufacturers of steam boilers in a similar manner, thereby enabling the steam boilers to create valuable industrial-grade steam from low-quality waste gases as a monetarily "free" input fuel. We do not yet have any agreements with such manufacturers, but we expect to negotiate and enter into additional partnerships for the larger turbines and steam products within the next 18 months.

Power Oxidation allows for the extraction of heat energy from previously unusable, low-quality industrial waste gases, while significantly reducing the emission of harmful greenhouse gases and pollutants into the atmosphere and enabling the production of useful, on-site energy products such as electricity and steam. Power Oxidation can potentially unlock a new, global source of clean power generation (electricity, steam and/or heat energy) by productively using a wide range of low-quality waste gases that are typically destroyed or vented to the atmosphere by a multitude of industries, and which currently contribute to approximately 32% of global greenhouse gas emissions. Our goal is to enable industrial process facilities to generate clean energy from their existing waste gases, thereby reducing the amount of energy that they purchase from their regional utilities, and simultaneously reducing the cost of compliance with local, state, and federal air quality regulations by avoiding the chemicals, catalysts, and complex permitting required by existing pollution abatement systems.

We have developed a 250/333 kilowatt, or kW, Power Oxidizer that we integrate with a 250 kW and a 333 kW gas turbine to produce 250 kW and 333 kW "Powerstations," respectively. We have two Powerstations currently in operation at a landfill site in the Netherlands and at the Irvine campus of the University of California, Irvine, or UCI, and one additional Powerstation currently in the production phase expected to be installed at a landfill in southern California. We are in the process of scaling up our Power Oxidizer systems to a significantly larger size of 2 megawatt, or MW, which has six times more power capacity than the 333 kW system, as well as working with engineers from Dresser-Rand a.s., a subsidiary of Dresser-Rand Group Inc., or Dresser-Rand, to integrate this larger Power Oxidizer with Dresser-Rand's "KG2" 2 MW gas turbine. We believe this scaled-up version of our Power Oxidizer, combined with the KG2 turbine, will result in a Powerstation product that is better aligned with the scale of emissions (and energy requirements) observed at the industrial facilities that we believe stand to benefit most from this technology. As with the existing, smaller Powerstation, the larger Powerstations will be designed to provide an alternative to typical combustion-based power generation and enable industries to utilize their own waste gases to generate power. We also expect to integrate our Power Oxidizer technology with traditional steam boilers, thereby enabling the commercialization and deployment of systems that will convert low-quality waste gases to steam (with no electrical power required) for customers that value industrial steam more than electrical power within their operations.

Our first commercial products, or the EC Series, the Ener-Core Powerstation EC250, or EC250, previously called "FP250," and EC333, or EC333, are products that combine our Power Oxidizer with a 250 kW and a 333 kW gas turbine, respectively. The gas turbines were initially developed by Ingersoll-Rand, plc, or Ingersoll-Rand, and subsequently enhanced by our predecessor, FlexEnergy, Inc., or FlexEnergy. The substitution of the Power Oxidizer for the combustor within a traditional turbine allows for the resulting, modified turbine to utilize low density waste gases as a fuel, in place of commercially purchased gases. The low energy density gases that the EC Series products can use as a fuel do not have an alternative commercial market as traditional combustion-based turbines require uncontaminated high energy fuels and thus cannot run on low energy density gases, and therefore such low energy density gases have no market value. The use of these waste gases results in a lower fuel cost to operate, in addition to providing a significant reduction in industrial air emissions.

We are currently scaling up our Power Oxidizer and working with Dresser-Rand to combine it with Dresser-Rand's KG2-3GEF turbine. The resulting product is currently being marketed and sold by Dresser-Rand's international teams under the Dresser-Rand brand and is called the KG2-3GEF/PO (or KG2 with Power Oxidizer, or KG2/PO). When fully integrated, the KG2/PO will combine our Power Oxidizer with a 2 MW gas turbine. We began the scale up and integration of our Power Oxidizer with Dresser-Rand's KG2 turbine in late 2014 and expect to continue to invest in engineering resources to support the integration of this unit throughout 2015. Dresser-Rand has already sold these scaled up units, and we expect the first commercial deployments of KG2 units to begin in 2016, assuming we are able to secure the funds we will require for such deployments.

Reverse Merger

Prior to the reverse merger discussed below, pursuant to a contribution agreement dated November 12, 2012 by and among FlexEnergy, Inc., FlexEnergy Energy Systems, Inc., and Ener-Core Power, Inc., Ener-Core Power, Inc. (formerly Flex Power Generation, Inc.) was spun-off from FlexEnergy, Inc. as a separate corporation. As part of that transaction, Ener-Core Power, Inc. received all of the assets (including intellectual property) and liabilities pertaining to the Power Oxidizer business, which was the business carved out of FlexEnergy, Inc.

We were originally incorporated on April 29, 2010 in Nevada under the name Inventtech, Inc. On April 16, 2013, we entered into a merger agreement with Ener-Core Power, Inc. and a wholly-owned merger sub, pursuant to which the merger sub merged with and into Ener-Core Power, Inc., with Ener-Core Power, Inc. as the surviving entity. Prior to the merger, we were a public reporting "shell company," as defined in Rule 12b-2 under the Exchange Act. On May 6, 2013, the pre-merger public shell company effected a 30-for-1 forward split of its common stock. All share amounts have been retroactively restated to reflect the effect of that stock split.

On July 1, 2013, we completed the reverse merger with Ener-Core Power, Inc., which remains our operating subsidiary. The merger was accounted for as a “reverse merger” and recapitalization. As part of the reverse merger, 120,520,000 shares of outstanding common stock of the pre-merger public shell company were cancelled (unadjusted for our July 8, 2015 reverse stock split). This cancellation has been retroactively accounted for as of the inception of Ener-Core Power, Inc. on November 12, 2012. Accordingly, Ener-Core Power, Inc. was deemed to be the accounting acquirer in the transaction and, consequently, the transaction was treated as a recapitalization of Ener-Core Power, Inc. Accordingly, the assets and liabilities and the historical operations that are reflected in the consolidated financial statements are those of Ener-Core Power, Inc. and are recorded at the historical cost basis of Ener-Core Power, Inc. Our assets, liabilities and results of operations were de minimis at the time of the reverse merger.

Reverse Stock Split

Our board of directors approved a reverse stock split of our authorized, issued and outstanding shares of common stock, as well as our authorized shares of preferred stock, par value $0.0001 per share, of which no shares are issued and outstanding, at a ratio of 1-for-50, or our Reverse Stock Split. On July 8, 2015, the Reverse Stock Split became effective and the total number of shares of common stock held by each stockholder of the Company converted automatically into the number of shares of common stock equal to: (i) the number of issued and outstanding shares of common stock held by each such stockholder immediately prior to the Reverse Stock Split divided by (ii) 50. We issued one whole share of the post-Reverse Stock Split common stock to any stockholder who otherwise would have received a fractional share as a result of the Reverse Stock Split, determined at the beneficial owner level by share certificate. As a result, no fractional shares were issued in connection with the Reverse Stock Split and no cash or other consideration was paid in connection with any fractional shares that would otherwise have resulted from the Reverse Stock Split.

Also on the effective date, all of our options, warrants and other convertible securities outstanding immediately prior to the Reverse Stock Split were adjusted by dividing the number of shares of common stock into which the options, warrants and other convertible securities are exercisable or convertible by 50 and multiplying the exercise or conversion price thereof by 50, all in accordance with the terms of the plans, agreements or arrangements governing such options, warrants and other convertible securities and subject to rounding to the nearest whole share. Such proportional adjustments were also made to the number of shares and restricted stock units issued and issuable under our equity compensation plans. The consolidated financial statements and notes to the condensed consolidated financial statements included elsewhere in this prospectus give retroactive effect to the Reverse Stock Split for all periods presented.

After giving effect to the Reverse Stock Split, on July 8, 2015, we had 2,463,919 shares of common stock, options to purchase up to 308,464 shares of common stock and warrants to purchase up to 339,043 shares of common stock outstanding.

Reincorporation

Effective as of September 3, 2015, we changed our state of incorporation from the State of Nevada to the State of Delaware, or the Reincorporation, pursuant to a plan of conversion dated September 2, 2015, following approval by our stockholders of the Reincorporation at our 2015 Annual Meeting of Stockholders held on August 28, 2015. In connection with the Reincorporation, we filed articles of conversion with the State of Nevada and a certificate of conversion with the State of Delaware. Upon effectiveness of the Reincorporation, the rights of our stockholders became governed by the Delaware General Corporation Law, the certificate of incorporation filed in Delaware and newly adopted bylaws. As a Delaware corporation following the Reincorporation, which we refer to as Ener-Core Delaware, we are deemed to be the same continuing entity as the Nevada corporation prior to the Reincorporation, which we refer to as Ener-Core Nevada. As such, Ener-Core Delaware continues to possess all of the rights, privileges and powers of Ener-Core Nevada, all of the properties of Ener-Core Nevada and all of the debts, liabilities and obligations of Ener-Core Nevada, including all contractual obligations, and continues with the same name, business, assets, liabilities, headquarters, officers and directors as immediately prior to the Reincorporation. Upon effectiveness of the Reincorporation, all of the issued and outstanding shares of common stock of Ener-Core Nevada automatically converted into issued and outstanding shares of common stock of Ener-Core Delaware without any action on the part of our stockholders.

Dresser-Rand 2 MW Integration

Throughout the nine months ended September 30, 2015, a significant portion of our resources, including nearly all of our engineering staff and additional consultants, was allocated to the scale up of our Power Oxidizer and the integration of our Power Oxidizer with the Dresser-Rand KG2-3GEF turbine.

On November 14, 2014, we entered into a global licensing agreement with the Dresser-Rand Company, which we refer to as the D-R Agreement, which grants Dresser-Rand the right to market and sell the Dresser-Rand KG2-3GEF 2 MW gas turbine coupled with the Ener-Core Power Oxidizer. The D-R Agreement grants Dresser-Rand exclusive rights to commercialize the Ener-Core Power Oxidizer, within ranges of 1–4 MW of power capacity, bundled with the Dresser-Rand KG2 gas-turbine product line. As part of the D-R Agreement, Dresser-Rand agreed to pay a $1.6 million initial license fee, which is currently in escrow, under the condition that we were able to successfully scale up the technology from the current size of 250 kW to a size of 2 MW. Dresser-Rand also agreed to achieve annual sales thresholds agreed to by both companies in order to retain the exclusivity of the commercial license. Upon payment of the initial license fee in full, Dresser-Rand shall have an exclusive license to sell the Ener-Core Power Oxidizer within ranges of 1–4 MW of power capacity, bundled with a gas-turbine to generate electricity. Beginning in November 2019, so long as Dresser-Rand continues to sell the agreed minimum quantity of units every year, or pays a “top up” license payment if the agreed minimum sales quantities are not achieved during any individual year, Dresser-Rand shall retain an exclusive license in the aforementioned 1–4 MW range of power capacity.

The D-R Agreement calls for a series of technical milestones. The first technical milestone involves the completion of a “Sub-Scale Acceptance Test,” or SSAT, which we successfully completed in July 2015. During the nine months ended September 30, 2015, we spent approximately $1.1 million to purchase the parts necessary to construct a “Multi-Fuel Test Facility,” or MFTF, and completed the assembly of the MFTF in April 2015. The MFTF was used initially for the SSAT testing. After the conclusion of the SSAT, we expect to utilize the

MFTF for additional Dresser-Rand related tests as well as for sales and marketing efforts for our other customers. Between April 2015 and July 2015, the MFTF was used to complete a comprehensive series of heat output and other oxidation tests for a Power Oxidizer. The SSAT was designed to be an interim in field test designed to be conducted without an integrated turbine and was intended to be a low-risk verification of the heat output required for the full integration. We completed and submitted the SSAT test results to Dresser-Rand in July 2015, and Dresser-Rand notified us on August 3, 2015 that we had successfully passed the SSAT.

The second technical milestone will be the "Full-Scale Acceptance Test," or FSAT, on which we started to commit resources in April 2015 for certain long lead time items and expect to commit additional resources beginning in the third quarter of fiscal 2015. The FSAT includes a multitude of tests using a full, working prototype of a combined Power Oxidizer and a Dresser-Rand KG2. The FSAT procedures are expected to be completed in early 2016. Both technical milestones are required prior to the delivery of the first commercial 1.75 MW units. We currently expect to ship the first two commercial KG2/PO units in 2016 to Dresser-Rand's customer, Pacific Ethanol, as announced by Pacific Ethanol in January 2015.

The D-R Agreement also requires the satisfaction of certain binding conditions in order for Dresser-Rand to be obligated to perform its covenants under the D-R Agreement, which covenants include the payment of license fees into escrow, the acceptance of binding purchase orders from its customers for KG2/PO units, the issuance of binding purchase orders to us for Power Oxidizer units and the performance of additional engineering services required for the FSAT. The binding conditions consist of: (i) Ener-Core providing evidence reasonably satisfactory to Dresser-Rand that there are no liens on specified intellectual property of Ener-Core and that Ener-Core owns and has recorded specified patents; (ii) the posting of a $1.6 million bond or letter of credit by Ener-Core on behalf of Dresser-Rand for security on the license fee payments; (iii) evidence reasonably satisfactory to Dresser-Rand that Ener-Core has sufficient operating capital for twelve months; and (iv) Dresser-Rand providing a written acknowledgement of an initial binding customer purchase order for a KG2-3GEF/PO unit.

In March 2015, the D-R Agreement was amended to revise the second binding condition. The revised binding condition eliminates the need for a bond but requires the $400,000 quarterly cash payments due from Dresser-Rand to be paid into a cash escrow account. Funds may be released from the cash escrow as follows: (i) to Dresser-Rand for up to $500,000 to reimburse Dresser-Rand for certain engineering costs; (ii) to Dresser-Rand in the event of termination of the D-R Agreement as a result of a failed acceptance test; or (iii) to Ener-Core upon the satisfaction of the FSAT. Ener-Core expects to complete the FSAT within the first quarter of fiscal 2016. Ener-Core expects that Dresser-Rand will be paid $125,000 per quarter from the escrowed cash for each of the next four quarters for Dresser-Rand engineering services related to the integration under the D-R Agreement. Upon satisfaction of the FSAT, Ener-Core will receive $1.1 million that is currently in escrow, which does not include the $500,000 that Dresser-Rand is to receive for reimbursement for certain engineering costs. If the FSAT condition is not satisfied, then Dresser-Rand shall receive the $1.1 million that is currently in escrow.

In August 2015, Dresser-Rand notified us that we had successfully passed all four binding conditions and the D-R Agreement was therefore a binding agreement. Dresser-Rand made the initial $400,000 license fee payment to the escrow account and we remitted $125,000 from the escrow account to Dresser-Rand's engineering division in August 2015.

Commercial Sales Efforts

Our commercial sales and marketing focus during 2015 is to build from our first commercial success in 2014 and add to our sales team as we begin to roll out our technology. Shortly after signing the D-R Agreement with Dresser-Rand in November 2014, our existing sales team began to work with the international sales and marketing teams from Dresser-Rand to develop a go-to-market strategy. In parallel, our existing internal sales team has continued to advance commercial opportunities from 2014 and enter new industrial markets with our EC250 and EC333 products.

During the first quarter of 2015, we began to focus our sales resources and efforts toward the improved commercialization of our technology, and we increased our sales efforts through the hiring of two key sales and marketing executives with experience in the oil and gas, waste remediation and pollution control industries. In January 2015, we engaged the services of John Millard as Director of the Europe/Middle East Region. Mr. Millard is based out of Zurich, Switzerland and has been tasked with marketing our Power Oxidizer technology into Europe and the Middle East, both of which are markets that we believe have demonstrated a willingness and a desire to be early adopters of our technology. In March 2015, we hired Mark Owen as Director of Sales in North America. Mr. Owen brings years of industry experience including recent experience selling pollution control systems throughout North America, along with experience rolling out new technology solutions and building sales teams and processes.

During the first quarter of 2015, one of our international distributors, Holland Renewable Energy Technologies, added an additional distribution partner to its commercial agreements. This new distributor, Hofstetter B.V, will begin to distribute our Power Oxidizer solutions in 2015 in the European market. Hofstetter is a world leader in flaring technology systems and has installed over 1,600 flaring systems worldwide. We believe this partnership will result in increased market awareness in Europe, a market that we believe is increasingly receptive of our technology solutions. We believe that Hofstetter provides an immediate and established market presence in Europe.

Dresser-Rand

In January 2015, the first sale of the new KG2-3GEF/PO unit was announced by Pacific Ethanol, which placed a two unit order with Dresser-Rand. Pursuant to the terms of the D-R Agreement, we began working on the initial phase of these two systems immediately after the announcement of the order received by Dresser-Rand from Pacific Ethanol. After receipt of formal acceptance of the successful completion of the SSAT, in August 2015, we received a binding purchase order from Dresser-Rand for two 1.75MW Power Oxidizer units for a total purchase price of $2.1 million. The purchase order calls for an initial payment of 50% of the order value, or $1,050,000 payable to us with additional progress payments made over time under the purchase order until delivery of the Power Oxidizer units. The purchase order also requires the Company to create a $2.1 million performance security, with an expected termination date of June 2017 by September 17, 2015, which date was extended until November 15, 2015. We have entered into a non-binding memorandum of understanding with an investor who will assist us in obtaining a letter of credit for the $2.1 million performance security interest. Upon satisfaction of the FSAT, we expect to receive $1.6 million of license fees, as reduced by $500,000 that Dresser-Rand is to receive for reimbursement for certain engineering costs, for a net amount due of $1.1 million. Under the D-R Agreement, the license fees are payable into escrow quarterly in equal installments. A total of $275,000 was in escrow on September 30, 2015 consisting of $400,000 for one quarterly installments, as reduced by $125,000 for engineering cost reimbursements paid to Dresser-Rand. If the FSAT condition is not satisfied, then Dresser-Rand shall receive all remaining amounts in escrow.

With the completion and acceptance of the SSAT and the verification by Dresser-Rand of the satisfaction of the four binding conditions, since July 2015, we have seen increased sales activity through proposals, customer visits and preliminary analyses requested by prospective customers. The SSAT was a key milestone contained in the D-R Agreement that had both technical and commercial ramifications. We believe that the SSAT provided Dresser-Rand management with a significant level of assurance over the commercial viability of the Power Oxidizer technology and that the acceptance of the SSAT results reduced the technology risk to the point where Dresser-Rand was willing to provide a $2.1 million binding purchase order. Moving forward, we believe that the successful SSAT should enable Dresser-Rand to advance from preliminary commercial discussions with prospective customers to allow them to provide binding quotes and proposals and, ultimately, begin accepting additional binding purchase orders from customers that are interested in purchasing Dresser-Rand's KG2-3GEF/PO Powerstations.

Landfill opportunities

According to data from the Landfill Methane Outreach Program of the U.S. Environmental Protection Agency, at least 50 percent of the landfills in the U.S. are already at full capacity and hence "closed," meaning no new landfill material is provided. When landfills close, they typically continue to emit harmful greenhouse gases for as long as 50 to 70 years after closure. Although an active landfill may generate electricity from methane production using combustion-based gas turbines or engines, the methane production at a closed landfill often falls below the 35% methane concentration level required for use of such technologies. The Santiago Canyon installation will be the first installation of an Ener-Core Powerstation at a "closed" landfill site in California and our first sale into a landfill managed by a small municipality. We believe that there are other significant opportunities available with other local governments or municipalities that often run local landfills. We believe that our technology can extend, or as in the case of Santiago Canyon, restart the power production of older closed landfills, which would otherwise be forced to stop electricity production and either vent or flare the residual gases produced. Instead of flaring the gas, our Power Oxidizer allows a gas turbine to run on a level of methane as low as a 5% concentration level. We intend to use this project to prove the ability to extend the power generation life of a "closed" landfill well beyond the ability of existing landfill gas generation capabilities and as a viable solution to extend the life of landfill power generation.

In May 2015, we received an award for our second commercial EC250 to be installed at the closed Santiago Canyon Landfill in Orange County, California. The Santiago Canyon landfill was closed in 1996 and as is typical for a closed landfill, the gas quality has degraded to a level that is insufficient for traditional power generation technology. Due to environmental regulations, the site is required to flare the waste gas emitted from the landfill. Installation of our EC250 Powerstation will enable the closed landfill to generate revenue by producing clean electricity from a declining waste gas source, while improving the landfill's air pollution profile. The installation, expected to be completed in 2017, is part of a renewable energy project made possible by the California Energy Commission's award of $1.5 million to the University of California, Irvine's Advanced Power & Energy Program in January 2015. We received a formal purchase order of approximately $900,000 in the third quarter of 2015. Once the system is fully operational, the municipality anticipates cost savings of $240,000 per year of avoided power purchases and gas flaring costs.

Revenue, Order-to-Cash Cycle and Customer Order Cash Flows

Our order-to-cash cycle is lengthy and requires multiple steps to complete. As such, we utilize and evaluate certain metrics such as bookings, backlog, and billed backlog. The initial commercial phase involves our sales team identifying a suitable project and evaluating each site to determine whether our value proposition fits the potential customer's needs. We evaluate potential industrial sites based on the amount, density and quality of the waste gas produced, the impacts of air quality penalties and required pollution abatement, and the expected cost savings or sales value of on-site power production. We also evaluate with the potential customer whether there are other financial considerations that could further strengthen the economic payback to the potential customer (which could include revenue increases that may result from pollution abatement benefits or carbon/emission credits or tax avoidance). As part of this evaluation, we work with potential customers to produce financial models, which seek to capture and quantify all of the various benefits of the potential project to determine the overall economic payback to the potential customer. If the potential customer determines to proceed after this evaluation, we enter into an agreement with the customer, which typically includes purchase order arrangements.

Customer orders, which are defined as firm commitments to purchase with fixed and determinable prices and contracted delivery terms, are considered bookings and are included as backlog. From the date of booking until the projected shipping date, we follow the standard practices that are typically followed by other power equipment producers, which include payment terms that involve customer advance payments designed to mirror our cash inventory outlays for sourcing parts and materials necessary to assemble the power plants to achieve a neutral customer order cash flow until delivery. All customer advance payments are recorded as billings, are reported as billed backlog and are represented on our balance sheet as deferred revenue or customer advances. As the Power Oxidizer plant assets are built, the costs are capitalized as inventory.

Powerstations are shipped to the customer locations and assembled on site. We supervise the assembly and commissioning of the Powerstations, which can take several months to complete. Once commissioning of the fully installed Powerstation(s) is(are) concluded and title passes to the customer, we issue the final billings and recognize revenues and costs of revenues by decrementing deferred revenues and inventory respectively.

We also charge customers for commissioning services, post-sale support, and post-warranty service and maintenance on our Power Oxidizer units. We provide a standard warranty, which typically ends between six months and one year after commissioning.

Commercial Activity

During the quarter ended September 30, 2015 we closed orders for two KG2 Oxidizer systems and one EC 250 Powerstation system for a total unit backlog of $3.0 million. With our $1.6 million in license fees due from Dresser-Rand under the terms of the commercial license agreement, we consider our backlog at September 30, 2015 to be $4.6 million. We expect to collect the license fees and ship the three units in 2016.

During the quarter ended September 30, 2015 we began to bill and collect customer deposits on our existing $4.6 million backlog consisting of $0.6 million billed for sales of our Power Oxidizers and Powerstations systems and $0.4 million billed for our license fee arrangement with Dresser Rand. Of the combined $1.0 million billed, we collected $0.4 million in cash prior to September 30, 2015, $0.4 million was collected into a restricted escrow account as described below, and $0.2 million is expected to be collected in the fourth quarter of 2015.

In October 2015 we entered into an non-binding memorandum of understanding pursuant to which an investor shall provide the Company with financial and other assistance (including the provision of sufficient and adequate collateral) as necessary in order for the Company to obtain a $2.1 million letter of credit acceptable to Dresser-Rand as the backstop security required in support of the purchase order for the first two KG2 Power Oxidizer units. Under the terms of the Dresser-Rand purchase order, the backstop security enables us to collect 50% of the order value in cash immediately with additional payments over time as we purchase materials for the Power Oxidizer units. If the investor is required to make any payments on the letter of credit, the Company shall reimburse the investor the full amount of any such payment. We expect to complete a definitive agreement for this memorandum of understanding prior to the November 15, 2015 due date for the Dresser-Rand backstop security.

Financing Activities

April 2015 Warrant Exchange

On April 2, 2015, we entered into warrant exchange agreements, or the Exchange Agreements, with five accredited investors, or the April 2014 Investors, that held warrants for the purchase of up to an aggregate of 81,941 shares of our common stock that were issued on April 16, 2014, or the April 2014 Warrants, in connection with our April 2014 senior secured convertible notes and warrants financing transaction, or the April 2014 Financing. Pursuant to the Exchange Agreements, the April 2014 Investors agreed to surrender for cancellation all of their April 2014 Warrants in exchange for shares of our common stock, which in the aggregate totaled 73,747 shares of our common stock, or the Exchange Shares. Under the Exchange Agreements, we granted the April 2014 Investors a right of first refusal to participate in any future sale of our equity or equity equivalent securities on a pro rata basis up to 50% of the securities offered in such sale, from the closing of the exchange transaction until April 16, 2016, except for a registered underwritten public offering. In the event that we engage in a registered underwritten public offering of our common stock and the offering price per share in such registered offering is more than 85% of the closing sale price of our common stock on the date of pricing of such offering, then the participation right shall be 20% of the securities offered in such registered offering. The April 2014 Investors have waived such right of participation with respect to the proposed registered offering contemplated by our currently pending registration statement. The Exchange Shares are subject to a separate lock-up agreement that prohibits any sale or transfer (subject to certain limited exceptions) of the Exchange Shares until the earlier of June 1, 2015 or the first date that the weighted average price of our common stock equals or exceeds $15.00 (as adjusted for any stock split, stock dividend, stock combination, reclassification or similar transaction occurring after the closing of the exchange transaction) for each of ten consecutive trading days.

May 2015 Equity Financing

On May 1, 2015, we sold 108,000 shares of our common stock at a purchase price of $7.50 per share and received gross proceeds of approximately $810,000 from the sale of such shares.

April 2015 and May 2015 Senior Secured Promissory Notes and Warrants Financing

On April 23, 2015, we sold senior secured promissory notes with an aggregate principal amount of $3.1 million, or the April 2015 Notes, and warrants for the purchase of up to 136,264 shares of our common stock, or the April 2015 Warrants. The investors in the offering paid $1,000 for each $1,000 of principal amount of April 2015 Notes and April 2015 Warrants. In connection with the offering, we agreed to effect a reverse stock split of our common stock initially yielding a post-split stock price of at least $4.00 per share of common stock within three months following the closing of the offering, to secure the listing of our common stock on a national securities exchange no later than six months following the closing of the offering, and to complete a firm commitment underwritten public offering registered under the Securities Act with aggregate gross proceeds to the Company equaling or exceeding $10,000,000 no later than six months following the closing of the offering.

On May 7, 2015, we sold senior secured promissory notes with an aggregate principal amount of $1.9 million, or the May 2015 Notes, and warrants for the purchase of up to 83,517 shares of our common stock, or the May 2015 Warrants. The investors in the offering paid $1,000 for each $1,000 of principal amount of May 2015 Notes and May 2015 Warrants. In connection with the offering, we agreed to covenants substantially identical to those described above relating to the April 2015 financing.

The April 2015 Notes mature on April 23, 2017, and the May 2015 Notes mature on May 7, 2017. The April 2015 Notes and the May 2015 Notes, which we collectively refer to as the 2015 Notes, each bear an interest rate of 12.00% per annum (which increases to 18% in the event of default) payable monthly in cash. The 2015 Notes are secured by a guaranty by Ener-Core Power, Inc. as well as current and future assets of the Company and Ener-Core Power, Inc. (excluding certain intellectual property assets described more fully below) pursuant to the pledge and security agreement entered into in connection with the 2015 Notes financings. The 2015 Notes contain the following provisions:

- The 2015 Notes are convertible under limited circumstances consisting solely of any time following an event of default under the terms of the 2015 Note, or an Event of Default Conversion Period, or during the period from the consummation of a Qualified Public Offering (as defined) and continuing for thirty days thereafter, or a QPO Conversion Period. During an Event of Default Conversion Period (as defined), each holder is entitled to convert any portion of the outstanding principal on its 2015 Note, plus any accrued and unpaid interest and applicable late payment charges with respect to such principal, which we collectively refer to as a Conversion Amount, into shares of our common stock. During a QPO Conversion Period, each holder is entitled to convert up to 50% of its outstanding principal, and accrued and unpaid interest into our common stock. The conversion rate shall be determined by dividing (1) the Conversion Amount by (2) a conversion price which shall be: (A) during an Event of Default Conversion Period, a price per share equal to 85% of the arithmetic average of the five (5) lowest weighted average prices of our common stock during the fifteen consecutive trading day period ending on the trading day immediately preceding the applicable conversion date, (B) as of any conversion date occurring during a QPO Conversion Period, a price per share equal to the offering price to the public of our common stock offered for sale by the Company in such Qualified Public Offering and (C) as to any conversion date occurring during a Conversion Period that is both an Event of Default Conversion Period and a QPO Conversion Period, the lower of (x) the price set forth in clause (A) and (y) the price set forth in clause (B). In addition, during a QPO Conversion Period, if we issue any securities directly or indirectly convertible, exchangeable or exercisable into our common stock in connection with a Qualified Public Offering, or QPO Derivative Securities, each holder, automatically and without having to pay any additional consideration to the Company, shall receive the same number of QPO Derivative Securities per share of our common stock receivable upon such conversion as was received by the holders in the applicable Qualified Public Offering. However, in any case, we are not permitted to effect any conversion if, following such conversion, a holder would beneficially own more than 9.99% of the shares of our common stock after giving effect to such conversion.

- Each holder may require us to redeem the 2015 Notes at a price equal to 115% of the Conversion Amount being redeemed (a) upon our default under the 2015 Notes, or (b) if we enter into a merger or consolidation, or sell or assign all or substantially all of our assets. In addition, at any time from and after the date that is the eighteen month anniversary of the original issuance date of the 2015 Notes, each holder shall have the right, in its sole and absolute discretion, at any time or times, to require that we redeem all or any portion of the Conversion Amount of its 2015 Note then outstanding at a price equal to 100% of the Conversion Amount of the portion of the 2015 Note being redeemed.

At any time after the issuance of the 2015 Notes, other than (i) at any time during which an event of default has occurred and is continuing or (ii) from the time we publicly announce a Qualified Public Offering through and including the date that is thirty days immediately following the consummation of such Qualified Public Offering, we have the right to redeem all or any portion of the Conversion Amount then remaining under the 2015 Notes, or a Company Optional Redemption; provided, that the aggregate Conversion Amount under 2015 Notes being redeemed shall be at least $500,000, or such lesser amount that is then outstanding under the 2015 Notes. The conversion price for such Company Optional Redemption shall be a price equal to 100% of the Conversion Amount of the 2015 Notes being redeemed.

Effective as of October 22, 2015, we executed a Second Amendment to Securities Purchase Agreement dated April 22, 2015, and a First Amendment to Securities Purchase Agreement dated May 7, 2015 (collectively, the “October Amendments”), each with certain investors holding the requisite number of conversion shares and warrant shares underlying the notes and warrants issued in April 2015 and May 2015 pursuant to the referenced purchase agreements. The October Amendments extend the deadline to November 30, 2015 for the Company’s consummation of a firm commitment underwritten public offering registered under the Securities Act of 1933, as amended, with aggregate gross proceeds to the Company equal to or in excess of $10,000,000, and related listing of its common stock on a national securities exchange.

The April 2015 Warrants and the May 2015 Warrants, which we collectively refer to as the 2015 Warrants, entitle their holders to purchase shares of our common stock at an exercise price of $12.50 per share and will expire on the 60-month anniversary of their issuance date. The 2015 Warrants may be exercised at any time and may be exercised on a “cashless” basis if a registration statement covering the resale of the shares underlying the 2015 Warrants is not then available; provided, however, that we shall not effect any exercise if, following such exercise, a holder would beneficially own more than 4.99% of the shares of our common stock outstanding immediately after giving effect to such exercise.

Going Concern

Going Concern

Our consolidated financial statements are prepared using the accrual method of accounting in accordance with accounting principles generally accepted in the United States of America ("GAAP") and have been prepared on a going concern basis, which contemplates the realization of assets and settlement of liabilities in the normal course of business. Since our inception, we have made a substantial investment in research and development to develop the Power Oxidizer, have successfully deployed an EC250 field test unit at the U.S. Army base at Fort Benning, Georgia, and installed and commissioned our first commercial unit in the Netherlands in the second quarter of 2014. In November 2014 we signed a Commercial License Agreement with Dresser-Rand (the "D-R Agreement") to incorporate our Power Oxidizer into Dresser-Rand's 1.75MW turbine. In August 2015, the D-R Agreement became a mutually binding agreement due to the satisfaction of certain binding conditions contained in the D-R Agreement.

We have sustained recurring net losses and negative cash flows since inception and have not yet established an ongoing source of revenues sufficient to cover our operating costs and allow us to continue as a going concern. Despite a capital raise of approximately $4.0 million in September 2014 and further capital raises of $5.8 million in April and May 2015, we expect to require additional sources of capital to support the Company's growth initiatives. We must secure additional funding to continue as a going concern and execute our business plan.

Management's plan is to obtain capital sufficient to meet our operating expenses by seeking additional equity and/or debt financing, including through a proposed registered offering for which we filed a registration statement on July 29, 2015. The cash and cash equivalents balance (excluding restricted cash) on December 31, 2014 and September 30, 2015, was approximately $2.2 million and $1.2 million, respectively.

We raised a total of $5.8 million of debt and equity capital in April and May 2015, as described in Notes 9 and 12 below, and we expect that the $1.2 million of cash as of September 30, 2015, receipts on customer billings, and the anticipated net proceeds from the proposed registered offering will continue to fund our working capital needs, general corporate purposes, and related obligations into 2016 at our current spending levels. However, we expect to require significantly more cash for working capital and as financial security to support our growth initiatives.

We will pursue raising additional equity and/or debt financing to fund our operations and product development. If future funds are raised through issuance of stock or debt, these securities could have rights, privileges, or preferences senior to those of our common stock and debt covenants that could impose restrictions on our operations. Any equity or convertible debt financing will likely result in additional dilution to our current stockholders. We cannot make any assurances that any additional financing, including the proposed registered offering, will be completed on a timely basis, on acceptable terms or at all. Our inability to successfully raise capital in a timely manner will adversely impact our ability to continue as a going concern. If our business fails or we are unable to raise capital on a timely basis, our investors may face a complete loss of their investment.

The accompanying consolidated financial statements do not give effect to any adjustments that might be necessary if we were unable to meet our obligations or continue operations as a going concern.

Critical Accounting Policies and Estimates

Our management's discussion and analysis of our financial condition and results of operations is based on our financial statements, which we have prepared in accordance with GAAP. The preparation of our financial statements requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of our financial statements, as well as the reported revenues and expenses during the reported periods. We evaluate these estimates and judgments on an ongoing basis. We base our estimates on historical experience and on various other factors that we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

While our significant accounting policies are more fully described in Note 2 to our unaudited condensed consolidated financial statements included elsewhere in this report, we believe that the following accounting policies are the most critical to aid you in fully understanding and evaluating this management discussion and analysis.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of expenses during the reporting period. Significant items subject to such estimates and assumptions include but are not limited to: collectability of receivables; the valuation of certain assets, useful lives, and carrying amounts of property and equipment, equity instruments and share-based compensation; provision for contract losses; valuation allowances for deferred income tax assets; valuation of derivative liabilities; and exposure to warranty and other contingent liabilities. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

Concentrations of Credit Risk

Cash and Cash Equivalents

We maintain our non-interest bearing transactional cash accounts at financial institutions for which the Federal Deposit Insurance Corporation ("FDIC") provides insurance coverage of up to $250,000. For interest bearing cash accounts, from time to time, balances exceed the amount insured by the FDIC. We have not experienced any losses in such accounts and believe we are not exposed to any significant credit risk related to these deposits. At September 30, 2015, we had $1,044,000 in excess of the FDIC limit.

We consider all highly liquid investments available for current use with an initial maturity of three months or less and are not restricted to be cash equivalents. We invest our cash in short-term money market accounts.

Restricted Cash

Collateral Account

Under a credit card processing agreement with a financial institution that was entered in 2013, we are required to maintain funds on deposit with the financial institution as collateral. The amount of the deposit, which is at the discretion of the financial institution, was $50,000 on September 30, 2015 and December 31, 2014.

Dresser-Rand Escrow Account

Under our Commercial License Agreement with Dresser-Rand, as amended, prepaid license fee payments of $400,000 per quarter are to be paid by Dresser-Rand into an escrow account with a financial institution beginning August, 2015. Dresser-Rand is allowed to withdraw up to $125,000 per quarter from this escrow account for qualified engineering expenses incurred by Dresser-Rand under the terms and conditions of the Dresser-Rand Commercial License Agreement. Dresser Rand funded $400,000 in August 2015 and withdrew $125,000 in August 2015. The balance in the escrow account was $275,000 and $0 on September 30, 2015 and December 31, 2014 respectively. We are allowed to withdraw funds from the escrow account after completion of additional technical milestones, expected to be completed in the first half of 2016. See also Note 8 – Deferred Revenues and Customer Advances.

Accounts Receivable

Our accounts receivable are typically from credit worthy customers or, for international customers are supported by guarantees or letters of credit. For those customers to whom we extend credit, we perform periodic evaluations of such customers and maintain allowances for potential credit losses as deemed necessary. We generally do not require collateral to secure accounts receivable. We have a policy of reserving for uncollectible accounts based on our best estimate of the amount of probable credit losses in existing accounts receivable. We periodically review our accounts receivable to determine whether an allowance is necessary based on an analysis of past due accounts and other factors that may indicate that the realization of an account may be in doubt. Account balances deemed to be uncollectible are charged to the allowance after all means of collection have been exhausted and the potential for recovery is considered remote.

At September 30, 2015 and December 31, 2014, we did not have any allowance for doubtful accounts. Although we expect to collect amounts due, actual collections may differ from the recorded amounts.

As of September 30, 2015 and December 31, 2014, two customers and one customer, respectively, accounted for 100% of net accounts receivable.

Accounts Payable

As of September 30, 2015 and December 31, 2014, two and six vendors, respectively, collectively accounted for approximately 25% and 54% of our total accounts payable.

Inventory

Inventory, which consists of raw materials, is stated at the lower of cost or net realizable value, with cost being determined by the average-cost method, which approximates the first-in, first-out method. At each balance sheet date, we evaluate our ending inventory for excess quantities and obsolescence. This evaluation primarily includes an analysis of forecasted demand in relation to the inventory on hand, among consideration of other factors. Based upon the evaluation, provisions are made to reduce excess or obsolete inventories to their estimated net realizable values. Once established, write-downs are considered permanent adjustments to the cost basis of the respective inventories. At September 30, 2015 and December 31, 2014, we did not have a reserve for slow-moving or obsolete inventory.

Property and Equipment

Property and equipment are stated at cost, and are being depreciated using the straight-line method over the estimated useful lives of the related assets, ranging from three to ten years. Maintenance and repairs that do not improve or extend the lives of the respective assets are expensed. At the time property and equipment are retired or otherwise disposed of, the cost and related accumulated depreciation accounts are relieved of the applicable amounts. Gains or losses from retirements or sales are reflected in the consolidated statements of operations.

Fair Value of Financial Instruments

Our financial instruments consist primarily of cash and cash equivalents, restricted cash, accounts receivable, accounts payable, derivative liabilities, secured notes payable and related debt discounts and capital lease liabilities. Fair value estimates discussed herein are based upon certain market assumptions and pertinent information available to management as of September 30, 2015 and December 31, 2014. The carrying amounts of short-term financial instruments are reasonable estimates of their fair values due to their short-term nature or proximity to market rates for similar items.

We determine the fair value of our financial instruments based on a three-level hierarchy established for fair value measurements under which these assets and liabilities must be grouped, based on significant levels of observable or unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect management's market assumptions. This hierarchy requires the use of observable market data when available. These two types of inputs have created the following fair-value hierarchy:

- Level 1: Valuations based on unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities. Currently, we classify our cash and cash equivalents as Level 1 financial instruments.

- Level 2: Valuations based on observable inputs (other than Level 1 prices), such as quoted prices for similar assets at the measurement date quoted prices in markets that are not active, or inputs which are observable, either directly or indirectly, for substantially the full term of the asset or liability. We do not currently have any accounts under Level 2.

- Level 3: Valuations based on inputs that require inputs that are both significant to the fair value measurement and unobservable and involve management judgment (i.e., supported by little or no market activity). Currently, we classify our warrants and conversion options accounted for as derivative liabilities as Level 3 financial instruments.

If the inputs used to measure fair value fall in different levels of the fair value hierarchy, a financial security's hierarchy level is based upon the lowest level of input that is significant to the fair value measurement.

Accrued Warranties

Accrued warranties represent the estimated costs that will be incurred during the warranty period of our products. We make an estimate of expected costs that will be incurred by us during the warranty period and charge that expense to the consolidated statement of operations at the date of sale. We also reevaluate the estimate at each balance sheet date and if the estimate is changed, the effect is reflected in the consolidated statement of operations. We made our initial commercial sale to Efficient Energy Conversion TurboMachinery, B.V. ("EECT") in the second quarter of 2014 with a six month warranty and later extended that warranty at our discretion. There was no warranty for the unit shipped to the Fort Benning site. We expect our future warranty period to be between nine months and one year depending on the warranties provided and the products sold. Accrued warranties for expected expenditures within the next year are classified as current liabilities and as non-current liabilities for expected expenditures for time periods beyond one year.

Derivative Financial Instruments

The Company issues derivative financial instruments in conjunction with its debt and equity offerings and to provide additional incentive to investors and placement agents. The Company uses derivative financial instruments in order to obtain the lowest cash cost-source of funds. Derivative liabilities are recognized in the consolidated balance sheets at fair value based on the criteria specified in Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") topic 815-40 "*Derivatives and Hedging—Contracts in Entity's own Equity*." The estimated fair value of the derivative liabilities is calculated using either the Black-Scholes-Merton or Monte Carlo simulation model method.

The Company issued detachable common stock warrants and convertible secured notes payable with conversion features in April 2014 and issued detachable common stock warrants and secured debt with a partial conversion feature in April and May 2015. These embedded derivatives and detachable warrants were evaluated under ASC topic 815-40. We determined that the warrants and embedded conversion feature for the April 2014 issuance and the conversion feature for the 2015 issuances should be accounted for as derivative liabilities. We determined that the detachable warrants associated with the 2015 issuance should not be accounted for as derivative liabilities. Warrants and the debt conversion features determined to be derivative liabilities were bifurcated from the debt host and are classified as liabilities on the consolidated balance sheet. Warrants not determined to be derivative liabilities were recorded to debt discount and paid in capital. The Company records the warrants and embedded derivative liabilities at fair value and adjusts the carrying value of the common stock warrants and embedded derivatives to their estimated fair value at each reporting date with the increases or decreases in the fair value of such warrants and derivatives at each reporting date, recorded as a gain or (loss) in the consolidated statements of operations. The 2015 detachable warrants determined not to be derivative liabilities were recorded to debt discount with a corresponding entry to paid-in capital.

Revenue Recognition

We generate revenue from the sale of our clean power energy systems and from consulting services. Revenue is recognized when there is persuasive evidence of an arrangement, product delivery and acceptance have occurred, the sales price is fixed or determinable and collectability of the resulting receivable is reasonably assured. Amounts billed to clients for shipping and handling are classified as sales of product with related costs incurred included in cost of sales.

Provisions for discounts and rebates to customers, estimated returns and allowances, and other adjustments are provided for in the same period the related revenue is recorded. We defer any revenue for which the services have not been performed or are subject to refund until such time that we and our customer jointly determine that the services have been performed or no refund will be required.

Revenues under long-term construction contracts are generally recognized using the completed-contract method of accounting. Long-term construction-type contracts for which reasonably dependable estimates cannot be made or for which inherent hazards make estimates difficult are accounted for under the completed-contract method. Revenues under the completed-contract method are recognized upon substantial completion—that is acceptance by the customer, compliance with performance specifications demonstrated in a factory acceptance test or similar event. Accordingly, during the period of contract performance, billings and costs are accumulated on the balance sheet, but no profit or income is recorded before completion or substantial completion of the work. Anticipated losses on contracts are recognized in full in the period in which losses become probable and estimable. Changes in estimate of profit or loss on contracts are included in earnings on a cumulative basis in the period the estimate is changed. As of September 30, 2015 and December 31, 2014, we had no provision for contract losses.

Research and Development Costs

Research and development costs are expensed as incurred. Research and development costs were $928,000 and $514,000 for the three months ended September 30, 2015 and 2014, respectively and were $2,636,000 and $2,259,000 for the nine months ended September 30, 2015 and 2014 respectively.

Share-Based Compensation

We maintain an equity incentive plan and record expenses attributable to the awards granted under the equity incentive plan. We amortize share-based compensation from the date of grant on a weighted average basis over the requisite service (vesting) period for the entire award.

We account for equity instruments issued to consultants and vendors in exchange for goods and services at fair value. The measurement date for the fair value of the equity instruments issued is determined at the earlier of (i) the date at which a commitment for performance by the consultant or vendor is reached or (ii) the date at which the consultant's or vendor's performance is complete. In the case of equity instruments issued to consultants, the fair value of the equity instrument is recognized over the term of the consulting agreement.

In accordance with the accounting standards, an asset acquired in exchange for the issuance of fully vested, non-forfeitable equity instruments should not be presented or classified as an offset to equity on the grantor's balance sheet once the equity instrument is granted for accounting purposes. Accordingly, we record the fair value of the fully vested, non-forfeitable common stock issued for future consulting services as prepaid expense in our consolidated balance sheets.

Earnings (Loss) per Share

Basic loss per share is computed by dividing net loss attributable to common stockholders by the weighted average number of common shares assumed to be outstanding during the period of computation. Diluted loss per share is computed similar to basic loss per share except that the denominator is increased to include the number of additional common shares that would have been outstanding if the potential shares had been issued and if the additional common shares were dilutive. Approximately 648,000 and 433,000 shares of common stock issuable upon full exercise of all options and warrants at September 30, 2015 and 2014, respectively and all shares potentially issuable in the future under the terms of the secured notes payable were excluded from the computation of diluted loss per share due to the anti-dilutive effect on the net loss per share.

All share and per share amounts in the table below have been adjusted to reflect the 30-for-1 forward split of our issued and outstanding shares of common stock by way of a stock dividend on May 6, 2013 and the 1-for-50 reverse split of our issued and outstanding common stock on July 8, 2015, retroactively.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	**2014**	**2015**	**2014**
Net loss	$ (3,310,000)	$ (2,823,000)	$ (8,601,000)	$ (7,770,000)
Weighted average number of common shares outstanding:				
Basic and diluted	2,464,100	1,642,600	2,385,500	1,515,000
Net loss attributable to common stockholders per share:				
Basic and diluted	$ (1.34)	$ (1.72)	$ (3.61)	$ (5.13)

Comprehensive Income (Loss)

We have no items of other comprehensive income (loss) in any period presented. Therefore, net loss as presented in our Condensed Consolidated Statements of Operations equals comprehensive loss.

Recently Issued Accounting Pronouncements

In May, 2014, the FASB issued Accounting Standards Update ("ASU") 2014-09, Revenue from Contracts with Customers (Topic 606) ("ASU 2014-09"). ASU 2014-09 provides a framework for addressing revenue recognition issues and, upon its effective date, replaces almost all existing revenue recognition guidance, including industry-specific guidance, in current U.S. generally accepted accounting principles. ASU 2014-09 is effective beginning with the calendar year ended December 31, 2017. The Company has not yet assessed the impact ASU 2014-09 will have upon adoption on its financial position, results of operations or cash flows.

In August 2014, the FASB issued ASU 2014-15, Presentation of Financial Statements—Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern. ASU 2014-15 requires that an entity's management evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the entity's ability to continue as a going concern within one year after the date that the financial statements are issued. Substantial doubt about an entity's ability to continue as a going concern exists when relevant conditions and events, considered in the aggregate, indicate that it is probable that the entity will be unable to meet its obligations as they become due within one year after the date that the financial statements are issued. Certain disclosures are necessary in the footnotes to the financial statements in the event that conditions or events raise substantial doubt about an entity's ability to continue as a going concern. ASU 2014-15 is effective for the annual period ending after December 15, 2016, and for annual periods and interim periods thereafter and early application is permitted. The Company has not yet assessed the impact ASU 2014-15 will have upon adoption.

In November 2014, the FASB issued ASU 2014-16—Derivatives and Hedging: Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share is More Akin to Debt or to Equity. ASU 2014-16 clarifies how current GAAP should be interpreted in evaluating the economic characteristics and risks of a host contract in a hybrid financial instrument that is issued in the form of a share. ASU 2014-16 is effected for the interim and annual periods beginning after December 15, 2015. The Company has not yet assessed the impact ASU 2014-16 will have upon adoption.

In April 2015, the FASB issued ASU 2015-03, Interest—Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs. ASU 2015-03 simplifies the presentation of debt issuance costs by requiring that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs are not affected by the amendments in this update. ASU 2015-03 is effective for public business entities for financial statements issued for fiscal years beginning after December 15, 2015 and interim periods within those fiscal years and early application is permitted. The Company has elected to adopt ASU 2015-03 beginning with the interim period ending June 30, 2015. There were no impacts to any prior periods presented as a result of adopting ASU 2015-03.

In July 2015, the FASB issued ASU 2015-11, Inventory (Topic 330): Simplifying the Measurement of Inventory. ASU 2015-11 requires that entities measure inventory at the lower of cost and net realizable value. ASU 2015-11 is effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years and early application is permitted. The Company has not yet assessed the impact ASU 2015-11 will have upon adoption.

RESULTS OF OPERATIONS FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2015, AS COMPARED TO THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2014

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	**2014**	**2015**	**2014**
Revenues	$ —	$ 58,000	$ —	$ 868,000
Cost of goods sold:	—	44,000	—	847,000
Gross Profit	—	14,000	—	21,000
Operating expenses:				
Selling, general, and administrative	1,165,000	1,226,000	3,475,000	4,017,000
Research and development	928,000	514,000	2,636,000	2,259,000
Total operating expenses	2,093,000	1,740,000	6,111,000	6,276,000
Operating loss	(2,093,000)	(1,726,000)	(6,111,000)	(6,255,000)
Other income (expenses):				
Interest expense, net	(150,000)	(21,000)	(257,000)	(28,000)
Amortization of debt discount and deferred financing costs	(1,117,000)	(2,694,000)	(1,921,000)	(3,234,000)
Loss on exchange of warrants	—	—	(279,000)	—
Gain (Loss) on valuation of derivative liabilities	50,000	1,618,000	(33,000)	1,748,000
Total other income (expenses), net	(1,217,000)	(1,097,000)	(2,490,000)	(1,514,000)
Loss before provision for income taxes	(3,310,000)	(2,823,000)	(8,601,000)	(7,769,000)
Provision for income taxes	—	—	—	1,000
Net loss	$ (3,310,000)	$ (2,823,000)	$ (8,601,000)	$ (7,770,000)
Loss per share—basic and diluted	$ (1.34)	$ (1.72)	$ (3.61)	$ (5.13)
Weighted average common shares—basic and diluted	2,464,100	1,642,600	2,385,500	1,515,000

Revenue

Our revenue primarily consists of Power Oxidizer sales as well as engineering services. For the three and nine months ended September 30, 2015, we had no product sales, as compared to $58,000 and $868,000 for the same periods of the prior year where we had $58,000 of waste gas testing consulting services for the three months ending September 30, 2014 and sold one unit to Attero in the Netherlands in the first half of 2014.

Cost of Goods Sold

For the three and nine months ended September 30, 2015, we had no product sales and thus had no cost of goods sold. Cost of goods sold for the 2014 periods primarily consisted of the costs to build our Power Oxidizer unit shipped to Attero, including materials, labor, overhead costs and warranty costs, and materials costs related to the consulting services.

Selling, General and Administrative Expenses

Selling, general and administrative expenses include officer compensation, salaries and benefits, stock-based compensation expense, consulting fees, legal expenses, intellectual property costs, accounting and auditing fees, investor relations costs, insurance, public company reporting costs and listing fees, and corporate overhead related costs. Total selling, general and administrative expenses for the three months ended September 30, 2015 decreased $61,000 or 5.0% to $1,165,000 from $1,226,000 for the same period of the prior year. Total selling, general and administrative expenses for the nine months ended September 30, 2015 decreased $542,000 or 13.5% to $3,475,000 from $4,017,000 for the same period of the prior year.

The decrease for the three months ended September 30, 2015 compared to the same period in the prior year is primarily due to the net effect of a decrease in stock-based compensation expense of $76,000, a decrease from a non-recurring fiscal 2014 settlement charge of $72,000 paid in warrants , and offset by a net increase in cash expenses of $87,000 consisting of increased employee headcount related costs for additional sales and marketing staff and increased legal, accounting, and board fees in the 2015 quarter relating to our corporate reorganization and stockholder meeting costs.

The decrease for the nine months ended September 30, 2015 compared to the same period in the prior year is due to the net effect of a decrease in stock-based compensation expense of $970,000, a decrease for the $72,000 settlement charge paid in warrants and an increase of expenses payable in cash of $500,000 primarily consisting of increased headcount related costs for additional sales and marketing staff and additional professional fees for additional patent related expenses, and public company related costs for insurance, board fees, and corporate reorganization costs.

Research and Development Expenses

Research and development costs include development expenses for the Power Oxidizer and integration expenses related to our Power Oxidizer products with partners such as Dresser-Rand and include salaries and benefits, consultant fees, cost of supplies and materials for samples and prototypes, depreciation, as well as outside services costs. Research and development expense for the three months ended September 30, 2015 increased $414,000 or 80.5% to $928,000 from $514,000 for the same period of the prior year. Research and development expense for the nine months ended September 30, 2015 increased $377,000, or 16.7%, to $2,636,000 from $2,259,000 for the same period of the prior year.

The increase for the three months ended September 30, 2015 compared to the same period in the prior year is due to the net effect of a decrease in stock-based compensation expense of $35,000 and an increase of $449,000 of expenses payable in cash. The decrease for the nine months ended September 30, 2015 compared to the same period in the prior year is due to the net effect of a decrease in stock-based compensation expense of $735,000 offset by an increase of expenses payable in cash of $1,112,000.

The increase in expenses payable in cash for both the three and nine months ended September 30, 2015 is due to increased costs related to higher engineering headcount for employees hired in late 2014, consultants working on the Dresser-Rand integration, and expensed materials and supplies to support the integration of our Power Oxidizer with the Dresser-Rand KG2/PO 2 megawatt unit.

Other Expenses

Other expenses consisted primarily of interest payable in cash, amortization of debt discount, and the change in the market value of warrants and debt conversion features accounted for as derivative liabilities and which were issued in conjunction with our 2015 Notes for fiscal 2015 and the April 2014 Convertible Debentures for fiscal 2014.

Other income and (expenses) for the three and nine months ended September 30, 2015 of ($1,217,000) and ($2,490,000) respectively consists primarily of combined interest expense and amortization of debt discount of ($1,267,000) and (3,262,000), respectively, related to our 2015 Notes offset by a gain (loss) on the fair value adjustment of our derivative liabilities of $50,000 and ($33,000), respectively. The nine month period ending September 30, 2015 was also impacted by a loss on exchange of warrants of ($279,000).

Other income and (expenses) for the three and nine months ended September 30, 2014 of ($1,097,000) and ($1,514,000) respectively consists primarily of combined interest expense and amortization of debt discount of ($2,715,000) and (3,262,000), respectively, offset by a gain on the fair value adjustment of our derivative liabilities of $1,618,000 and $1,748,000, respectively, which were both associated with the convertible debt offering which was entered into in April 2014 and settled in August 2014.

Net Loss

For the three months ended September 30, 2015, our net loss was approximately $3.3 million, primarily from operating expenses of $2.1 million, including stock-based compensation expenses of $0.4 million and increased research and development costs for the Dresser-Rand integration incurred in 2015 of $0.4 million; and $1.2 million of other expenses including interest expense of $1.3 million offset by a gain of $0.1 million for revaluation of derivative liabilities. For the three months ended September 30, 2014, our net loss of $2.8 million consisted of $1.7 million of operating expenses, including $0.4 million of stock compensation and $1.1 million of other expenses consisting of $2.7 million of interest expense, offset by a $1.6 million gain on derivative liability valuation.

For the nine months ended September 30, 2015, our net loss was $8.6 million, primarily from operating expenses of $6.1 million, including stock compensation expense of $1.1 million and increased research and development costs for the Dresser-Rand integration under the terms of the D-R Agreement of $1.1 million, and $2.5 million of other expenses consisting of $2.2 million of interest expense and $0.3 million in losses related to the warrant exchange. For the nine months ended September 30, 2014, our net loss of $7.8 million consisted of $6.3 million of operating expenses, including $2.8 million of stock compensation and $1.5 million of other expenses consisting of $3.3 million of interest expense related to the April 2014 convertible debt, offset by a $1.7 million gain on derivative liability valuation.

Other Income (Expenses):

For the three and nine months ended September 30, 2013, other income (expense) was for interest expense on a related party note payable.

Net Loss

For the three and nine months ended September 30, 2014, our net loss was approximately $2.8 million and $7.8 million, respectively, primarily from selling, general and administrative expenses, including stock-based compensation expenses and ongoing research and development costs for our products and other expenses. For the three and nine months ended September 30, 2013, our net loss was approximately $2.0 million and $4.6 million, respectively. The increases from the 2013 periods to the 2014 periods was due to increases of $1.1 million and $1.5 million in other expenses related to the April 2014 Secured Notes which did not exist in 2013 and for the decrease of $0.3 million for the three month period and an increase of $1.6 million for the nine month period ended September 30, 2014 As described in greater detail above, the changes were due to higher stock compensation expenses, including the additional expense incurred as a result of repricing options in April 2014, higher non-recurring consulting expenses in the September, 2014 quarter, and an overall reduction of employee headcount and overhead due to reduced R&D activity and cost savings measures.

Earnings (Loss) Per Share

Earnings (Loss) per share, basic and diluted were ($1.34) and ($1.72) for the three months ended September 30, 2015 and 2014, respectively and ($3.61) and ($5.13) for the nine months ended September 30, 2015 and 2014, respectively. All Earnings (Losses) per share have been adjusted to reflect the 1-for-50 reverse stock split implemented July 8, 2015.

Liquidity

Cash Flows used in Operating Activities

Our cash used in operating activities were approximately $4.5 million and $2.9 million for the nine months ended September 30, 2015 and 2014, respectively. Cash used in operating activities for the nine months ended September 30, 2015 resulted from a net loss of approximately $8.6 million, reduced by non-cash charges of $3.6 million for stock-based compensation, losses on revaluation of derivative securities, non-cash interest expense due to amortization of debt discount and deferred financing charges, and depreciation, and a change of $0.4 million of working capital, primarily due to a $0.2 million increase in customer advances, net of restricted cash and $0.2 million for an increase in accounts payable. Cash used in operating activities for the nine months ended September 30, 2014 resulted from a net loss of approximately $7.8 million reduced by $2.9 million of stock compensation expense, $2.5 million due to the accelerated amortization of debt discount on the August 2014 debt conversion, $0.7 million of debt amortization to interest expense, $0.2 million in depreciation and $0.2 million in working capital, offset by a $1.7 million gain on the reduction in fair value of derivative liabilities associated with the April 2014 Convertible Debt offering and which was exchanged for common stock in August 2014.

Cash Flows from Investing Activities

Cash used in investing activities of $1.8 million for the nine months ended September 30, 2015 was attributable to the purchase of property and equipment consisting primarily of the multi-fuel test facility which was used to satisfy the initial sub scale acceptance test for the D-R Agreement and payments made to construct the full KG2 prototype to be used in the KG2 integration for the full scale acceptance test.

Cash Flows from Financing Activities

Cash provided by financing activities of $5.4 million for the nine months ended September 30, 2015 was attributable the $0.8 million equity offering in May 2015 and the $5.0 million Senior Notes sold in April and May 2015, net of offering costs and fees. Cash provided by financing activities of $3.8 million for the nine months ended September 30, 2014 was attributable to cash received from the placement of the convertible securities issued in April 2014.

Capital Resources

Our principal capital requirements are to fund our working capital requirements, invest in research and development and capital equipment and fund the continued costs of public company compliance requirements. We have historically funded our operations through debt and equity financings.

From our inception, we have incurred losses from operations. For the nine months ended September 30, 2015, we have incurred losses from operations and have an accumulated deficit of approximately $26.6 million and a net loss of approximately $8.6 million. For the nine months ended September 30, 2015, we used cash in operations of approximately $4.5 million, which raises substantial doubt about our ability to continue as a going concern.

We expect to continue to incur substantial additional operating losses from costs related to the continuation of product and technology development and administrative activities. Our cash on hand at September 30, 2015 was approximately $1.5 million (including restricted cash of $325,000). On April 23, 2015, we sold senior secured promissory notes with an aggregate principal amount of $3.1 million and warrants for the purchase of up to 136,264 shares of our common stock. On May 1, 2015, we sold 108,000 shares of our common stock at a purchase price of $7.50 per share and received gross proceeds of approximately $810,000 from the sale of such shares. On May 7, 2015, we sold senior secured promissory notes with an aggregate principal amount of $1.9 million and warrants for the purchase of up to 83,517 shares of our common stock. We paid $0.4 million in costs and fees associated with these equity and debt financings.

Our sales cycle can exceed 24 months and we do not expect to generate sufficient revenue in the next twelve months to cover our operating costs. We anticipate that we will pursue raising additional debt or equity financing to fund new product development and execute on the commercialization of our product plans. On July 29, 2015, we filed a registration statement with the Securities and Exchange Commission for a proposed registered offering and filed amendments to this registration statement on September 18, 2015 and October 16, 2015. We cannot make any assurances that our strategies will be effective or that any additional financing will be completed on a timely basis, on acceptable terms or at all. Our inability to successfully implement our strategies or to complete any other financing will adversely impact our ability to continue as a going concern.

Until we achieve our product commercialization plans and are able to generate sales to realize the benefits of the strategy and sufficiently increase cash flow from operations, we will require additional capital to meet our working capital requirements, research and development, capital requirements and compliance requirements and will continue to pursue raising additional equity and/or debt financing.

Our principal sources of liquidity are cash and receivables. As of September 30, 2015, cash and cash equivalents (including restricted cash) were $1.5 million or 32.2% of total assets compared to $2.2 million, or 67.6% at December 31, 2014. The decrease in cash and cash equivalents was primarily attributable to cash used in operating activities of $4.5 million and $1.8 million of spending on fixed assets, primarily on the multi-fuel test facility and the prototype to be used for the full scale acceptance test, offset by $5.4 million of cash received from debt and equity financings.

We have not yet achieved profitable operations and have yet to establish an ongoing source of revenue to cover operating costs and meet our ongoing obligations. Our cash needs for the next 12 months are projected to be in excess of $10 million which includes the following:

- Employee, occupancy and related costs: $3.8 million
- Professional fees and business development costs: $1.2 million
- Research and development programs: $1.5 million
- Corporate filings: $0.5 million
- Working capital: $3.5 million

During the quarter ended September 30, 2015 we began to bill and collect customer deposits on our existing $4.6 million backlog consisting of $0.6 million billed for sales of our Power Oxidizers and Power Stations and $0.4 million billed for our license fee arrangement with Dresser Rand. Of the $1.0 million billed, we collected $0.4 million in cash, $0.4 million was placed into a restricted escrow account as described below, and $0.2 million is expected to be collected in the fourth quarter of 2015.

In October, 2015 we entered into an agreement with an investor to provide a collateral guaranty which enabled us to provide a backstop security to Dresser-Rand for our $2 million order for the first two KG2 Power Oxidizer units. Under the terms of the Dresser-Rand purchase order, the backstop security enables us to collect 50% of the order value in cash immediately with additional payments over time as we purchase materials for the Power Oxidizer units.

Dresser Rand Restricted Cash Escrow Account: As of September 30, 2015 we had $275,000 in restricted cash held in an escrow account under the terms and conditions of the Dresser Rand Commercial License Agreement (“CLA”). The escrowed funds represent 25% of the total $1,600,000 license fees due under the CLA, reduced by $125,000 of reimbursable engineering costs payable to Dresser Rand. We expect to receive additional cash payments of $400,000 per quarter which will be placed into escrow until a gross total of $1,600,000 is placed into the escrow account. Dresser Rand is allowed to draw up to $125,000 per quarter from the escrow account up to a maximum draw of $500,000. The remaining $1,100,000 will be released to us upon the satisfaction of the full scale acceptance tests identified in the CLA. We expect the full scale acceptance test requirements to be completed in the second quarter of 2016.

Off-Balance Sheet Arrangements

We have not entered into any other financial guarantees or other commitments to guarantee the payment obligations of any third parties. We have not entered into any derivative contracts that are indexed to our shares and classified as stockholders’ equity that are not reflected in our financial statements. Furthermore, we do not have any retained or contingent interest in assets transferred to an unconsolidated entity that serves as credit, liquidity or market risk support to such entity. We do not have any variable interest in any unconsolidated entity that provides financing, liquidity, market risk or credit support to us or engages in leasing, hedging or research and development services with us.

Inflation

We believe that inflation has not had a material effect on our operations to date.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Pursuant to Item 305(e) of Regulation S-K, we are not required to provide the information required by this Item 3.

Item 4. Controls and Procedures.

Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the Commission’s rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

As of September 30, 2015, the end of the quarterly period covered by this report, our management, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, has performed an evaluation of the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended).

Based on the evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as of September 30, 2015, our disclosure controls and procedures were ineffective at the reasonable assurance level. Such conclusion is due to the presence of material weaknesses in internal control over financial reporting. Management anticipates that our disclosure controls and procedures will remain ineffective until such material weaknesses are remediated.

Changes in Internal Control over Financial Reporting

Remediation of Material Weaknesses

To address our material weaknesses, management performed additional analyses and other procedures to ensure that the financial statements included herein fairly present, in all material respects, our financial position, results of operations and cash flows for the periods presented.

We are attempting to remediate the material weaknesses in our disclosure controls and procedures and internal controls over financial reporting identified above by refining our internal procedures (see below). During the nine months ended September 30, 2015, we initiated the following corrective actions, which management believes are reasonably likely to materially affect our financial reporting, as they are designed to remediate the material weaknesses as described above:

- We are in the process of further enhancing our internal finance and accounting organizational structure, which includes hiring additional resources.

- We are in the process of further enhancing the supervisory procedures to include additional levels of analysis and quality control reviews within the accounting and financial reporting functions.

- We are in the process of strengthening our internal policies and enhancing our processes for ensuring consistent treatment and recording of reserve estimates and that validation of our conclusions regarding significant accounting policies and their application to our business transactions are carried out by personnel with an appropriate level of accounting knowledge, experience and training.

- We are developing and implementing inventory control procedures.

- We have added additional independent directors to our board of directors.

- We have appointed additional independent directors to our board committees, including the addition of two directors to our compensation committee, two directors to our nominating and corporate governance committee, and two additional directors, for a total of three directors, to our audit committee.

We do not expect to have fully remediated these material weaknesses until management has tested those internal controls and found them to have been remediated. We expect to complete this process during our annual testing for fiscal 2015.

Limitations on Controls

Management does not expect that our disclosure controls and procedures or internal control over financial reporting will prevent or detect all errors and fraud. Any control system, no matter how well designed and operated, is based upon certain assumptions and can provide only reasonable, not absolute, assurance that its objectives will be met. Further, no evaluation of controls can provide absolute assurance that misstatements due to error or fraud will not occur or that all control issues and instances of fraud, if any, within the Company have been detected.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings.

We know of no material, existing or pending legal proceedings against our Company, nor are we involved as a plaintiff in any material proceeding or pending litigation. There are no proceedings in which any of our directors, officers or affiliates, or any registered or beneficial stockholder, is an adverse party or has a material interest adverse to our interest.

Item 1A. Risk Factors.

As a smaller reporting company, we are not required to provide the information required by this Item 1A.

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

No sales that were not previously reported on a Current Report on Form 8-K.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Item 6. Exhibits.

Exhibit No.		Description
2.1	(9)	Plan of Conversion, dated September 2, 2015
3.1	(1)	Amended and Restated Articles of Incorporation
3.2	(2)	Certificate of Merger, as filed with the Secretary of State of the State of Delaware on June 28, 2013
3.3	(7)	Certificate of Change, dated July 6, 2015
3.4	(9)	Articles of Conversion, as filed with the Nevada Secretary of State on September 2, 2015 and effective September 3, 2015.
3.5	(9)	Certificate of Conversion, as filed with the Delaware Secretary of State on September 2, 2015 and effective September 3, 2015.
3.6	(9)	Certificate of Incorporation, as filed with the Delaware Secretary of State on September 2, 2015 and effective September 3, 2015.
3.7	(1)	Amended and Restated Bylaws of Ener-Core, Inc., a Nevada corporation
3.9	(9)	Bylaws, as currently in effect
4.1	(4)	Form of the Notes dated April 23, 2015
4.2	(4)	Form of the Warrants dated April 23, 2015
4.3	(6)	Form of the Notes dated May 7, 2015
4.4	(6)	Form of the Warrants dated May 7, 2015
10.1	(3)	Form of Exchange Agreement
10.2	(3)	Form of Lock-Up Agreement
10.3	(4)	Securities Purchase Agreement dated April 22, 2015
10.4	(4)	Pledge and Security Agreement dated April 23, 2015
10.5	(5)	Securities Purchase Agreement dated May 1, 2015
10.6	(5)	Registration Rights Agreement dated May 1, 2015
10.7	(6)	Securities Purchase Agreement dated May 7, 2015
10.8	(6)	First Amendment to the Securities Purchase Agreement dated April 22, 2015, effective as of May 7, 2015
10.9	(6)	First Amendment to the Pledge and Security Agreement dated April 22, 2015, effective as of May 7, 2015
10.10	(10)	Second Amendment to Securities Purchase Agreement dated April 22, 2015, effective as of October 22, 2015
10.11	(10)	First Amendment to Securities Purchase Agreement dated May 7, 2015, effective as of October 22, 2015
10.12	(8)	Ener-Core, Inc. 2015 Omnibus Incentive Plan

Exhibit No.	Description
31.1*	Certification of Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1*	Certification of Principal Executive Officer and Principal Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS*	XBRL Instance Document
101.SCH*	XBRL Taxonomy Extension Schema
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase
101.DEF*	XBRL Taxonomy Extension Definition Linkbase
101.LAB*	XBRL Taxonomy Extension Label Linkbase
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase

* Filed herewith.

(1) Incorporated by reference to the Registrant’s Form 8-K filed on April 24, 2013.
(2) Incorporated by reference to the Registrant’s Form 8-K filed on July 10, 2013
(3) Incorporated by reference to the Registrant’s Form 8-K filed on April 7, 2015.
(4) Incorporated by reference to the Registrant’s Form 8-K filed on April 23, 2015.
(5) Incorporated by reference to the Registrant’s Form 8-K filed on May 1, 2015.
(6) Incorporated by reference to the Registrant’s Form 8-K filed on May 7, 2015.
(7) Incorporated by reference to the Registrant’s Form 8-K filed on July 8, 2015.
(8) Incorporated by reference to the Registrant’s Definitive Proxy Statement filed on July 15, 2015.
(9) Incorporated by reference to the Registrant’s Form 8-K filed on September 3, 2015.
(10) Incorporated by reference to the Registrant’s Form 8-K filed on October 23, 2015.

SIGNATURES

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

ENER-CORE, INC.
(Registrant)

Date: October 29, 2015

By: */s/ Alain Castro*
Alain Castro
Chief Executive Officer

Date: October 29, 2015

By: */s/ Domonic J. Carney*
Domonic J. Carney
Chief Financial Officer

EXHIBIT 31.1

OFFICER'S CERTIFICATE PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Alain Castro, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Ener-Core, Inc.;

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

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

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

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

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

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

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

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

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

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

Date: October 29, 2015

/s/ Alain Castro
Alain Castro
Chief Executive Officer

EXHIBIT 31.2

**OFFICER'S CERTIFICATE PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Domonic Carney, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Ener-Core, Inc.;

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

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

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

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

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

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

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

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

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

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

Date: October 29, 2015

/s/ Domonic Carney
Domonic Carney
Chief Financial Officer

EXHIBIT 32.1

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

In connection with the Quarterly Report of Ener-Core, Inc. (the "Company") on Form 10-Q for the period ended June 30, 2015, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Alain Castro, Chief Executive Officer, and I, Domonic Carney, Chief Financial Officer, on the date indicated below, hereby certify pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to the best of my knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operation of the Company.

Date: October 29, 2015

By: */s/ Alain Castro*
Alain Castro
Chief Executive Officer

Date: October 29, 2015

By: */s/ Domonic Carney*
Domonic Carney
Chief Financial Officer