POWER SOLUTIONS INTERNATIONAL, INC.
Form S-1
May 14, 2013
Table of Contents

As filed with the Securities and Exchange Commission on May 14, 2013

Registration No. 333-

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM S-1

REGISTRATION STATEMENT

Under

Securities Act of 1933

POWER SOLUTIONS INTERNATIONAL, INC.

(Exact name of registrant as specified in its charter)

Delaware	**3510**	**33-0963637**
(State or other jurisdiction of incorporation or organization)	**(Primary Standard Industrial Classification Code Number)**	**(I.R.S. Employer Identification No.)**

201 Mittel Drive

Wood Dale, IL 60191

(630) 350-9400

(Address, including zip code, and telephone number, including area code, of registrant s principal executive offices)

Gary S. Winemaster

Chief Executive Officer and President

Power Solutions International, Inc.

201 Mittel Drive

Wood Dale, IL 60191

(630) 350-9400

(Name, address, including zip code, and telephone number including area code, of agent for service)

Copies of all communications, including communications sent to agent for service, should be sent to:

Mark D. Wood, Esq.	**Catherine V. Andrews, Esq.**	**Thomas S. Levato, Esq.**
Katten Muchin Rosenman LLP	**Power Solutions International, Inc.**	**Goodwin Procter LLP**
525 W. Monroe Street	**General Counsel**	**The New York Times Building**
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Tel.: (312) 902-5200	**Wood Dale, IL 60191**	**New York, NY 10018**
	Tel.: (630) 350-9400	**Tel.: (212) 813-8800**

Approximate date of commencement of proposed sale to the public: As soon as practicable after the effective date of this registration statement.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933 check the following box. ¨

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

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 12b2 of the Exchange Act.

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

CALCULATION OF REGISTRATION FEE

Title of Securities to be Registered	Amount to be Registered	Proposed Maximum Offering Price Per Share	Proposed Maximum Aggregate Offering Price	Amount of Registration Fee
Common Stock, $0.001 par value per share	1,955,000(1)	$ 60,272,650(2)	$ 30.83(2)	$ 8,221

(1) Includes shares to be sold upon exercise of the underwriters option. See Underwriting.
(2) Estimated solely for the purpose of calculating the registration fee pursuant to Rule 457(c) based on the average of the high and low prices of the common stock reported on the OTC Bulletin Board on May 9, 2013, the date 3 business days prior to the date upon which this Registration Statement was originally filed.

The registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until this Registration Statement shall become effective on such date as the Commission, acting pursuant to said Section 8(a), may determine.

Table of Contents

The information in this preliminary prospectus is not complete and may be changed. We and the selling stockholders may not sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This preliminary prospectus is not an offer to sell these securities and is not soliciting an offer to buy these securities in any state or jurisdiction where the offer or sale is not permitted.

Subject to completion, dated May 14, 2013

POWER SOLUTIONS INTERNATIONAL, INC.

1,700,000 Shares of Common Stock

$ per share

We are offering 1,000,000 shares of our common stock, and the selling stockholders named in this prospectus are offering 700,000 shares of our common stock. We will not receive any proceeds from the sale of the shares by the selling stockholders.

Our common stock is quoted on the OTC Bulletin Board and the OTC Markets OTCQB tier under the symbol PSIX. On May 13, 2013, the last reported closing bid price of our common stock as reported on the OTC Bulletin Board was $31.80 per share. Prior to the completion of this offering, we intend to list our common stock on the NASDAQ Global Market.

The underwriters have an option to purchase a maximum of 255,000 additional shares of common stock from the selling stockholders to cover the over-allotment of shares.

Investing in the securities involves a high degree of risk. See *Risk Factors* beginning on page 12 of this prospectus to read about factors you should consider before buying shares of our common stock.

	Price to Public	Underwriting Discounts and Commissions	Proceeds to Company[1]	Proceeds to Selling Stockholders
Per Share.	$	$	$	$
Total	$	$	$	$

[1] See Underwriting for information relating to certain expenses of the underwriters to be reimbursed by us.

Delivery of the shares of common stock will be made on or about , 2013.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of the securities offered hereby or passed upon the adequacy or accuracy of this prospectus. Any representation to the contrary is a criminal offense.

Sole Book-Running Manager

Craig-Hallum Capital Group

Co-Lead Manager

Roth Capital Partners

The date of this prospectus is , 2013.

Table of Contents

Table of Contents

You should rely only on the information contained in this prospectus. Neither we, the selling stockholders nor the underwriters have authorized anyone to provide you with information that is different from that contained in this prospectus. We do not, and the selling stockholders and the underwriters do not, take any responsibility for, and can provide no assurances as to, the reliability of any information that others provide to you. We and the selling stockholders are offering to sell, and seeking offers to buy, shares of our common stock only in jurisdictions where offers and sales are permitted. The information contained in this prospectus is accurate only as of the date of this prospectus, regardless of the time of delivery of this prospectus or of any sale of our common stock.

No action is being taken in any jurisdiction outside the United States to permit a public offering of our securities or possession or distribution of this prospectus in that jurisdiction. Persons who come into possession of this prospectus in jurisdictions outside the United States are required to inform themselves about, and to observe, any restrictions as to the offering and the distribution of this prospectus applicable to those jurisdictions.

Table of Contents

Industry and Market Data

Certain market, industry and similar data included in this prospectus have been obtained from third-party sources that we believe to be reliable, including the Potential Gas Committee and Power Systems Research, Inc. We have not independently verified any market, industry or similar data presented in this prospectus. Such data involves risks and uncertainties and are subject to change based on various factors, including those discussed under the headings Cautionary Note Regarding Forward-Looking Statements and Risk Factors.

Table of Contents

Prospectus Summary

This summary highlights information contained elsewhere in this prospectus. It does not contain all of the information that you should consider before investing in our common stock. You should read this entire prospectus carefully, including the Risk Factors and the financial statements and related notes included herein. This prospectus includes forward-looking statements that involve risks and uncertainties. See Cautionary Note Regarding Forward-Looking Statements.

Except where the context otherwise requires or where otherwise indicated, references to we, us, our and our company refer to Power Solutions International, Inc. and its subsidiaries.

Our Company

Overview

We are a global producer and distributor of a broad range of high performance, certified low-emission, power systems that primarily run on alternative fuels such as natural gas and propane and are designed to meet emission standards of the Environmental Protection Agency (EPA) and the California Air Resources Board (CARB). Our customers include large, multinational original equipment manufacturers (OEMs) of off-highway industrial equipment, and we are a sole source provider of alternative fuel power systems for most of these customers. Our power systems are currently used by OEMs in a wide range of industries with a diversified set of applications, including, stationary electricity generators, oil and gas equipment, forklifts, aerial work platforms, industrial sweepers, arbor equipment, agricultural and turf equipment, aircraft ground support equipment, construction and irrigation equipment, and other industrial equipment. In addition to our primary focus on the industrial market, we are introducing a range of alternative fuel power systems designed for the on-road market.

Our power systems are highly engineered, comprehensive systems customized to meet specific industrial OEM application requirements and technical specifications, as well as requirements imposed by environmental regulatory bodies. Our power system configurations range from a basic engine block integrated with appropriate fuel system components to completely packaged power systems. We purchase engines from third party suppliers and have recently begun producing an internally-designed engine, both of which are then integrated into our power systems. We are also conducting research and development for the purpose of designing, developing and manufacturing other engines in-house. A substantial portion of the components we integrate into our power systems consist of internally designed components and components for which we coordinate significant design efforts with third party suppliers, with the remainder consisting largely of parts that we source off the shelf from third party suppliers. We are able to provide our customers with a comprehensive, emission-certified power system which can be incorporated, using a single part number, directly into a customer s specified application.

For industrial applications, our alternative fuel power systems meet or exceed emission standards of the EPA and CARB and represent a cleaner, and typically less expensive, alternative to diesel fuel power systems. While our power systems primarily run on alternative fuels, we also supply EPA and CARB emission-certified standard fuel power systems, and we are one of the largest suppliers of Perkins and Caterpillar diesel power systems under 275 horsepower. We expect that growth in domestic sales of our low-emission power systems will be driven by the substantial breadth of our emission-certified products, as well as increasing U.S. demand for alternative fuel power systems resulting from the adoption of increasingly stringent engine emission regulations. We are also experiencing increasing demand for our power systems from international industrial OEMs that manufacture industrial equipment for the U.S. import market.

Table of Contents

In addition to our emission-certified power systems, we also produce and distribute nonemission-certified power systems for industrial OEMs for particular applications in markets without emission standards (for example, oil and gas equipment used in Canada). Approximately 69% of our net sales for 2012 consisted of sales of emission-certified products, with approximately 57% of our 2012 net sales consisting of sales of emission certified products for which we hold the applicable regulatory certification and 12% of our 2012 net sales consisting of sales of diesel power systems for which the diesel engine supplier holds the applicable regulatory certification. Approximately 10% of our net sales in 2012 consisted of sales of aftermarket parts, and the remaining approximately 21% of our net sales in 2012 consisted of sales of our nonemission-certified power systems.

Recent Performance

We improved our operational and financial performance during our latest fiscal year ended December 31, 2012 and the most recent quarter ended March 31, 2013:

- Increased total revenue by 30.6% to $202.3 million for the fiscal year ended December 31, 2012 from $155.0 million for the fiscal year ended December 31, 2011;
- Increased adjusted diluted earnings per common share to $0.81 for the fiscal year ended December 31, 2012 from $0.48 for the fiscal year ended December 31, 2011;
- Increased total revenue by 9.4% to $52.6 million for the three months ended March 31, 2013 from $48.1 million for the three months ended March 31, 2012; and
- Increased adjusted diluted earnings per common share to $0.21 for the three months ended March 31, 2013 from $0.19 for the three months ended March 31, 2012.

Industry and Market Overview

Industrial OEM Market

The off-highway industrial OEM market represents a diversified set of applications and industry categories that include power generation, oil and gas, material handling, aerial work platforms, sweepers, arbor, welding, airport ground support, agricultural, turf, construction and irrigation. While the power system requirements for the industrial OEM market bear similarities to the requirements for power systems used in automotive

Table of Contents

applications, there are substantial application differences between automotive and industrial equipment applications. Torque, start, stop, low speed and, with respect to certain applications, indoor use requirements, make direct use of an automotive power system impractical for use in most industrial equipment applications. Recognizing these differences, the EPA and CARB have issued distinct emission standards and regulations for industrial applications, as compared to those for automotive applications. As a result, there is not a direct cross-over of available automotive power systems into the industrial OEM market. Power systems used in the industrial OEM market must satisfy these emission standards through a certification process with the EPA and CARB that includes durability testing of the engine emission system at zero and 5,000 hours, production line testing on a quarterly basis and field compliance audit testing. Given the level of engineering and financial resources that automotive engine manufacturers would need to dedicate to supply emission-certified product into the industrial OEM market, and that this market does not represent a core business for these manufacturers, it is generally impractical for automotive engine manufacturers to compete in the industrial OEM market.

Market Trends

The market for our power systems is continuing to grow globally as a result of several key drivers, including:

Increasingly Stringent Regulations and Growing Efforts to Reduce Emissions

Concerns regarding climate change and other environmental considerations have led to the implementation of laws and regulations that restrict, cap or tax emissions in the automotive industry and throughout other industries. In particular, EPA Tier 4 emission standards, CARB regulations, and recently implemented policies in Europe, generally referred to as Stage I, II, III and IV regulations, are requiring a significant reduction in the level of emissions and particulate matter produced by diesel power systems. These regulations are taking effect and are expected to increase both the cost (estimated by us to be between 30% and 100%) and size of emission-compliant diesel power products, primarily due to the need to incorporate additional combustion and after-treatment components. OEMs have experienced pressure to redesign their products to address these emission regulations, as products that are unable to meet emission standards may not be sold in the marketplace. However, we believe few suppliers to industrial OEMs have been capable of providing, or are willing to make the investments of time, financial, and other resources necessary to provide products that meet new emission regulations.

Increased Use of Alternative Fuels

A variety of market factors are contributing to the increased use of alternatives fuels and growth of alternative fuel technology, including economics, energy independence, environmental concerns, and the widespread availability of alternative fuels. The price of alternative fuels such as natural gas or propane is substantially less than diesel or gasoline, and alternative fuels produce lower amounts of toxic greenhouse gases. In the United States, significant domestic alternative fuel reserves have been identified, and it is believed these reserves could satisfy much of the energy needs of the U.S. for many years. According to a 2013 report published by the Potential Gas Committee (PGC), a nonprofit organization comprised of experts working in the natural gas field, the U.S. future natural gas supply at the end of 2012 was 2,688 trillion cubic feet (consisting of PGC s assessments of technically recoverable resources combined with the U.S. Department of Energy s latest determination of proved reserves), which represents an increase of 22.1% from 2010 levels as determined by PGC. The abundance of domestic natural gas resources is expected to increase U.S. energy independence by reducing oil imports from foreign countries. As a result of these market factors, we believe the use of alternative fuels will continue to grow and providers of equipment in industrial OEM categories, such as power generation, that rely significantly on coal, diesel fuel and gasoline, will face increasing pressure to use alternative fuel power systems.

Table of Contents

Industrial OEM Trend Toward Outsourcing

Industrial OEMs have been following the broader marketplace trend of outsourcing non-core functions. The dynamics of global sourcing and the need for cost competitiveness have led, and should continue to lead, industrial OEMs to assess what operations and system components are core to their business model and what they should outsource to their suppliers and partners. In particular, to comply with frequently changing environmental regulations while remaining competitive, industrial OEMs have been increasingly more reliant on outsourcing to third party suppliers and partners with specialized regulatory and design expertise. This is especially true for international OEMs seeking access to the U.S. market. By outsourcing power system design and production, OEMs are able to focus their resources on overall design and functionality of their products, rather than on developing the sophisticated technology associated with emission-certified power systems. We expect increasingly more industrial OEMs to outsource power systems, system components and subsystems to third party suppliers with the requisite experience and technology.

Our Competitive Strengths

We have a 27-year history and reputation as a proven supplier of cost-effective, technologically advanced products to the industrial OEM marketplace. We believe that our technological superiority and the comprehensive nature of our product offerings position us to capitalize on developing trends in the industrial OEM markets and drive significant future growth.

Broad Range of Alternative Fuel Power Systems

Our power systems represent a broad range of emission-certified, alternative fuel products for industrial applications. We are one of only a few providers of industrial OEM products that meet, and in many cases produce emissions at levels significantly lower than the emission standards of the EPA and CARB. Our alternative fuel engines range in size from under 1 liter to 22 liters and our power system configurations include any combination of cooling systems, electronic systems, air intake systems, fuel systems, housings, power takeoff systems, exhaust systems, hydraulic systems, enclosures, brackets, hoses, tubes and other assembled componentry. We provide standardized fuel system and component technology across our entire range of emission-certified power systems. As a result, our OEM customers are able to focus internal engineering and technical support resources, and train their personnel, on one standardized fuel system and one set of electronic controls employed throughout the range of power systems they acquire from us, and are able to reduce their product design and ongoing product support costs.

We believe our broad range of emission-certified, alternative fuel products strategically positions us to capitalize on the cost and packaging disadvantages associated with diesel power systems that are resulting from increased EPA and CARB emission regulations that are taking effect. Given the existing dominance of diesel power systems in the industrial OEM marketplace, even a minor shift in the marketplace from diesel to spark-ignited, alternative fuel power systems will represent a significant growth opportunity for us. Additionally, as international OEMs desire to supply industrial equipment products into the United States and must meet EPA and CARB emission requirements, we provide a fast, certain, cost-effective route for these foreign industrial OEMs to meet these emission requirements because we hold compliance certificates specific to our power systems. We have already secured commercial sales relationships with some of Asia s largest industrial OEMs, and have begun supplying EPA and CARB compliant power systems to these industrial OEM customers for incorporation into their product lineups.

Leverageable, OEM-Focused Business Model

We are able to take advantage of opportunities for component standardization across industry categories, while still providing each industrial OEM with the flexibility to customize as required for particular design and

Table of Contents

application specifications. We aggregate our product development efforts, and can amortize associated costs, over our large and diverse OEM customer base and across industry categories. Furthermore, we capitalize on volume, economies of scale and global supply opportunities when sourcing component products. We can, therefore, provide our OEM customers with lower cost structures than they would otherwise be able to achieve and help them reduce their part numbers and supply base by consolidating their procurement and assembly efforts down to a single part number product supplied by us. Our component sourcing relationships further enable our OEM customers to recognize resource reductions, inventory reductions and engineering support advantages.

Additionally, our relationships with international OEM customers that supply their industrial equipment into the United States generate opportunities for us to further supplement our business. We believe that once one of our emission-certified power systems is engineered into a foreign industrial OEM s product, that OEM is likely to also incorporate our power systems into its products that do not require emission-compliant power systems. This use by foreign industrial OEMs of our power systems for both their emission-certified and non-emission-compliant power system needs reduces ongoing engineering, aftermarket and field service support requirements, while supporting a product strategy that can easily be adjusted to any future worldwide changes in emission requirements. These relationships further provide us with growth opportunities beyond those dependent upon U.S. demand for emission regulated products, and solidify our supplier and partnership position with our foreign industrial OEM customers. Moreover, even if our relationship with an international OEM customer is limited to United States compliant power systems, we are in an opportune position to provide additional emission-compliant power systems in the future, as emission regulations for industrial equipment begin to emerge in other countries around the world.

Superior Technology

We are a recognized leader in providing industrial OEMs with highly engineered, technologically superior, emission-certified power systems that cover a wide range of possible fuel alternatives. Our power system development and manufacturing processes are supported by in-house design, prototyping, testing and engineering capabilities. We believe our customers are able to realize significant costs savings by leveraging our proven power system technology, our application engineering expertise, the broad range of our EPA and CARB emission-certified power systems and our industrial equipment testing and certification processes.

Table of Contents

Further, we are not captive to our own internal manufactured components and technology. Unlike some of our competitors that focus on developing and manufacturing most of their own product technology and components, we believe that superior technology is derived from having the flexibility to incorporate the best proven technology available in the marketplace. We focus on developing deep internal engineering and application expertise, more than on developing in-house components and technology. This affords us the flexibility to capitalize on current and emerging technology that best meets the requirements of any given application, as opposed to only using internally-developed technology that might not provide the best solution. Because we do not directly compete in the development of key technology, suppliers of underlying technology are interested in supplying their latest innovations to us. As a result, we believe we have access to the best proven technology in the marketplace. We believe this strategy puts us in a strong position to benefit from our significant OEM customer base and aggregation capabilities in order to provide the best available product and technology solutions for our OEM customers.

Dedicated Customer-Centric Product and Application Expertise

We have a customer-centric business focus, and we continually strive for customer satisfaction at all levels of customer interaction. We commit our attention and efforts to nurturing and expanding relationships with our customers by staying connected with them, being aware of challenges they face and understanding their evolving needs. From production personnel to our customer support staff, our entire team is highly experienced in both the products we sell and the OEM customer applications into which they are integrated. Through our extensive experience in the industrial OEM marketplace and our adaptive technology strategy that we use in developing our power systems, we are able to accept the specific requests of individual customers and provide tailored power systems to meet their needs. We assign a dedicated engineer to each OEM customer for application support and to provide a direct line of communication between the OEM s manufacturing line and our production operations. Our quality, field service support and service operations provide knowledgeable and responsive support to our OEM customers at every point of customer interface.

Growth Strategy

Our core strategy is to develop comprehensive power systems for the global industrial OEM marketplace. We believe that, with our competitive advantages, our continued pursuit of our core strategy will drive growth in our business. More specifically, we intend to seek future growth as follows:

Expand Products and Services Provided to Existing OEM Customers

We continually work to capitalize on organic growth opportunities and build upon our strong existing customer relationships, which in many cases are on a sole source basis. We plan to expand our business with existing customers by supporting their growth initiatives as they expand their produce lines, enter new markets, and adapt to changing emission standards. We also intend to develop and sell new products to our OEM customers as we broaden our range of emission-certified, alternative fuel power systems.

Establish New Industrial OEM Relationships

We expect to strengthen our OEM customer base by developing new relationships with industrial OEMs. We seek to acquire new clients and gain new business from OEMs that we do not presently serve by focusing our marketing efforts toward these potential customers and capitalizing on our strong reputation; the depth, breadth and technological sophistication of our power systems; our commitment to customer service; and the cost savings we can offer. Emphasizing our experience and reputation in market categories in which our power systems are already well-established, such as power generation, we are focused on establishing new industrial OEM relationships and capturing a greater portion of the market share. We are also targeting new OEM customers in high-growth market categories, such as material handling and oil and gas applications.

Table of Contents

Expand Into New Geographic Markets

We are focused on expanding our business internationally with OEM customers that require EPA and CARB compliant power systems to access the U.S. market and for non-compliant systems used in products sold outside the U.S. Furthermore, because we expect countries outside of the United States to implement emission regulations that are aligned with U.S. standards, we anticipate an opportunity to expand our relationships with industrial OEMs that supply emission-compliant products outside of the U.S. If such emission regulations are implemented consistent with our expectation, we anticipate being able to provide power systems to industrial OEMs that meet applicable foreign emission standards by leveraging our existing technology and experience in developing our EPA and CARB emission-certified products.

Develop New Products

By leveraging the deep industry experience of our engineering and new product development teams, we are working to broaden the range of our power system product offerings, including with respect to engine classes and the industrial OEM market categories into which we supply our products. We are also currently in the process of developing new 2.0 liter and 2.4 liter engines. We capitalize on our technologically sophisticated, in-house design, prototyping, testing and application engineering capabilities to further refine our superior spark-ignited power system technology. We plan to apply our experience and expertise in developing comprehensive, integrated green power systems to expand our spark-ignited alternative fuel offerings.

Expand Into On-Road Market

We have recently introduced a newly designed, state-of-the-art, 8.8-liter fuel flexible engine that we plan to sell to industrial, bus and truck OEMs which will be a fully-integrated drop-in solution. We expect this engine to be a solution in the industrial off-road and on-road markets and have a wide range of applications, including school buses, waste-hauling trucks and medium-duty delivery trucks. Furthermore, we have recently expanded our on-road product line by entering a multi-year supply agreement with General Motors for 4.8-liter and 6.0-liter alternative fuel engines. We believe we now have a comprehensive range of alternative fuel powertrains for vehicle OEMs in the Class 4 through Class 7 truck and bus market.

Selectively Pursue Complementary Strategic Transactions

We may enter into strategic transactions, such as acquisitions of, or joint ventures or partnerships with, companies that present complementary non-organic growth opportunities. Specifically, we will seek opportunities that extend or supplement our presence into new geographic markets or industrial OEM market categories, expand our customer base, add new products or service applications or provide significant operating synergies. We believe that there may be domestic or international strategic opportunities available to us as the sophistication of technology and amount of resources necessary to develop and supply power systems that meet increasingly stringent emission standards continue to increase.

Risk Factors

Our business is subject to a number of risks discussed under the heading Risk Factors and elsewhere in this prospectus. The principal risks facing our business include among others:

- the market for alternative fuel spark-ignited power systems may not develop according to our expectations;
- new products, including new engines we may develop, may not achieve widespread adoption;
- we may not succeed with the expansion of our product into the on-road market;

Table of Contents

changes in environmental and regulatory policies could hurt the market for our products;

we are dependent on relationships with our OEM customers and any change in our relationships with any of our key OEM customers could have a material adverse effect on our business and financial results; and

we are dependent on relationships with our material suppliers and the partial or complete loss of one of these key suppliers, or the failure to find replacement suppliers or manufacturers in a timely manner, could adversely affect our business.

There are also several risks relating to this offering and the ownership of our common stock. You should carefully consider these factors, as well as all of the other information set forth in this prospectus. See Risk Factors.

Corporate Information

We are a Delaware corporation founded in 1985 and we became publicly traded as a result of a reverse recapitalization transaction in 2011 (as further described below under Business Company History). Our principal executive offices are located at 201 Mittel Drive, Wood Dale, IL 60191 and our telephone number is (630) 350-9400. Our website address is www.psiengines.com. The information on, or that may be accessed through, our website is not incorporated by reference into this prospectus and should not be considered a part of this prospectus.

Table of Contents

The Offering

Common stock offered by us	1,000,000 shares
Common stock offered by the selling stockholders	700,000 shares
Common stock to be outstanding after the offering	10,216,621 shares
Over-allotment option	The underwriters have a 30-day option to purchase up to 255,000 additional shares of common stock from the selling stockholders.
Use of proceeds	We estimate that our net proceeds from the sale of shares of our common stock will be approximately $ million, based on an assumed public offering price of $ per share (the closing bid price of our common stock as reported on the OTC Bulletin Board on May , 2013), and after deducting underwriting discounts and commissions and estimated offering expenses payable by us. We currently intend to use a substantial portion of our net proceeds to pay down our outstanding borrowings under our revolving line of credit with BMO Harris Bank, N.A. We intend to use any remaining net proceeds (and the additional availability under our revolving line of credit resulting from the repayment of our outstanding borrowings thereunder with our proceeds from this offering) for working capital and other general corporate purposes.

We will not receive any proceeds from the sale of shares of common stock by the selling stockholders.

Unless otherwise indicated, the number of shares of our common stock that will be outstanding immediately after this offering is based on 9,216,621 shares of common stock outstanding as of May 10, 2013, and excludes, as of May 10, 2013:

- 597,918 shares of our common stock issuable upon the exercise of warrants at a weighted average exercise price of $13.00 per share;
- 543,872 shares of our common stock currently held in treasury that are underlying a stock appreciation right with a strike price of $22.07 issued pursuant to our 2012 Incentive Compensation Plan; and
- 287,053 shares of our common stock currently held in treasury and available for future awards pursuant to our 2012 Incentive Compensation Plan.

Except as otherwise noted, all information in this prospectus assumes:

- no exercise of the underwriters over-allotment option;

an assumed offering price of $ per share (the closing bid price of our common stock as reported on the OTC Bulletin Board on May , 2013); and

that no options, warrants, restricted shares, or stock appreciation rights were issued after May 10, 2013 and that no shares underlying the warrants and stock appreciation right outstanding as of May 10, 2013 were issued.

Table of Contents

Summary Historical Consolidated Financial and Operating Data

Set forth below is summary historical consolidated financial and operating data of the Company at the dates and for the periods indicated. The summary historical consolidated statement of operations data for the years ended December 31, 2010, December 31, 2011 and December 31, 2012 and the summary historical consolidated balance sheet data as of December 31, 2011 and December 31, 2012 have been derived from our audited consolidated financial statements included elsewhere in this prospectus. The summary historical consolidated balance sheet data as of December 31, 2010 has been derived from our audited consolidated financial statements that do not appear in this prospectus. The summary historical consolidated statement of operations data for the three months ended March 31, 2012 and March 31, 2013 and summary historical consolidated balance sheet data as of March 31, 2013 have been derived from our unaudited consolidated financial statements included elsewhere in this prospectus. The summary historical consolidated balance sheet data as of March 31, 2012 has been derived from our unaudited consolidated financial statements that do not appear in this prospectus. Our historical results are not necessarily indicative of the results that may be expected in any future period.

The summary historical consolidated financial and operating data set forth below should be read in conjunction with Use of Proceeds, Capitalization, Selected Historical Consolidated Financial and Operating Data, Management s Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements included elsewhere in this prospectus.

(Dollar amounts in thousands, except per share amounts)	Years Ended December 31, 2012	2011	2010	Three Months Ended March 31, 2013	2012
				(unaudited)	
Statement of Operations Data:					
Net sales	$ 202,342	$ 154,969	$ 100,521	$ 52,576	$ 48,072
Cost of sales	168,425	128,541	83,894	43,407	39,843
Gross profit	33,917	26,428	16,627	9,169	8,229
Operating expenses:					
Research & development and engineering	7,377	4,713	3,846	1,771	1,727
Selling and service	5,925	6,666	5,465	1,880	1,702
General and administrative	8,299	5,244	3,250	2,438	1,764
Total operating expenses	21,601	16,623	12,561	6,089	5,193
Operating income	12,316	9,805	4,066	3,080	3,036
Other (income) expense	1,471	2,971	2,131	5,040	855
Income before income taxes	10,845	6,834	1,935	(1,960)	2,181
Income tax provision	4,143	2,773	366	967	1,031
Net income (loss)	$ 6,702	$ 4,061	$ 1,569	$ (2,927)	$ 1,150
Undistributed earnings (loss)	$ 6,702	$ 4,061	$ 1,569	$ (2,927)	$ 1,150
Undistributed earnings allocable to Series A convertible preferred shares	$	$ 2,513	$ 1,510	$	$
Undistributed earnings allocable to common shares	$ 6,702	$ 1,548	$ 59	$ (2,927)	$ 1,150
Weighted-average common shares outstanding					
Basic	9,068,846	3,512,534	312,500	9,100,111	9,064,537
Diluted	9,068,846	3,512,534	312,500	9,100,111	9,064,537
Undistributed earnings (loss) per common share					
Basic	$ 0.74	$ 0.44	$ 0.19	$ (0.32)	$ 0.13
Diluted	$ 0.74	$ 0.44	$ 0.19	$ (0.32)	$ 0.13
Other Financial Data [(1)]:					

Adjusted net income	$ 7,455	$ 4,443	$ 1,569	$ 1,919	$ 1,743
Adjusted diluted earnings per common share	$ 0.81	$ 0.48	$ 0.19	$ 0.21	$ 0.19

Table of Contents

(Dollar amounts in thousands)	As of December 31, 2012	2011	2010	As of March 31, 2013	2012
				(unaudited)	
Balance Sheet Data:					
Current assets	$ 82,077	$ 66,021	$ 50,165	$ 82,272	$ 73,501
Property, plant & equipment, net	7,145	3,611	2,883	7,828	3,710
Total assets	90,765	71,083	55,353	91,473	79,215
Current liabilities	32,664	51,842	43,899	28,441	37,512
Total debt and capital leases (current and long-term portions)	30,942	19,730	29,535	31,945	20,809
Total liabilities	68,031	55,759	49,997	68,205	62,741
Stockholders equity	22,734	15,324	5,356	23,268	16,474

1) The Company believes supplementing its consolidated financial statements presented in accordance with GAAP with non-GAAP measures provides investors with useful information regarding the Company s short-term and long-term trends. Adjusted net income and adjusted diluted earnings per common share are derived from GAAP results by excluding the non-cash impact related to the change in the estimated fair value of the liability associated with the warrants issued in the Company s April 2011 private placement. The Company excludes this non-operating, non-cash impact, as the Company believes it is not indicative of its core operating results or future performance. The warrant revaluation results from facts and circumstances that fluctuate in impact and is excluded by management in its forecast and evaluation of the Company s operational performance. Adjusted net income and adjusted diluted earnings per common share also exclude costs incurred in connection with the Company s relocation of production, warehousing and administrative offices into new facilities. The Company excludes these costs as they, similar to the warrants, are not indicative of the Company s core operating results or future performance and are excluded by management in its forecast and evaluation of the Company s operational performance.

Adjusted net income, adjusted diluted earnings per common share and other non-GAAP financial measures used and presented by the Company may be calculated differently from, and therefore may not be comparable to, similarly titled measures used by other companies. Investors should consider non-GAAP measures in addition to, and not as a substitute for, or as superior to, financial performance measures prepared in accordance with GAAP. The following table presents reconciliations of net income to adjusted net income and diluted earnings per common share to adjusted diluted earnings per common share:

(Dollar amounts in thousands, except per share amounts)	Fiscal Year Ended 2012	2011	2010	Three Months Ended March 31, 2013	2012
				(unaudited)	
Reconciliation of net income (loss) to adjusted net income:					
Net income (loss)	$ 6,702	$ 4,061	$ 1,569	$ (2,927)	$ 1,150
Non-cash expense from warrant revaluation	448	382		4,846	593
Facility relocation costs, net of tax	305				
Adjusted net income	$ 7,455	$ 4,443	$ 1,569	$ 1,919	$ 1,743
Reconciliation of diluted EPS to adjusted diluted EPS:					
Diluted earnings (loss) per common share	$ 0.74	$ 0.44	$ 0.19	$ (0.32)	$ 0.13
Non-cash expense from warrant revaluation	0.04	0.04		0.53	0.06
Facility relocation costs	0.03				
Adjusted diluted earnings per common share	$ 0.81	$ 0.48	$ 0.19	$ 0.21	$ 0.19

Table of Contents

Risk Factors

Investing in our common stock involves a high degree of risk. You should consider carefully the risks, uncertainties and other factors described below, in addition to the other information set forth in this prospectus, before deciding whether to invest in shares of our common stock. Any of these risks, uncertainties and other factors could materially and adversely affect our business, financial condition, results of operations, cash flows or prospects. In that case, the market price of our common stock could decline, and you may lose all or part of your investment in our common stock. See also Cautionary Note Regarding Forward-Looking Statements.

Risks Related to our Business and our Industry

The market for alternative fuel spark-ignited power systems may not develop according to our expectations and, as a result, our business may not grow as planned and our business plan may be adversely affected.

Our future growth is dependent upon the market for efficient alternative fuel spark-ignited power systems (including natural gas and propane) expanding as a result of our customers and potential customers substituting alternative fuel power systems for diesel power systems. Part of our business plan is dependent on our market forecasts with respect to this expected substitution trend. However, there can be no assurance that we can accurately predict the potential impact of new diesel emission regulations, which we assume will help drive this trend by increasing the cost and product footprint of diesel power systems, nor can we assure that customers or potential customers would substitute natural gas and propane powered power systems for diesel power systems in response to these regulations. In addition, to the extent that diesel power system manufacturers develop the ability to design and produce emission-compliant diesel power systems that they can sell at a lower price and have smaller product footprints than we currently expect, diesel power systems will be more competitive with our alternative fuel power systems, and customers and potential customers may be less likely to substitute alternative fuel power systems for diesel power systems. Furthermore, even if alternative fuel power systems are substituted for diesel power systems, there can be no assurance that our power systems would capture any portion of this potential market size increase. If the industrial OEM market generally, or more specifically any of the industrial OEM categories which represent a significant portion of our business or in which we anticipate significant growth opportunities for our power systems, fails to develop or develops more slowly than we anticipate, the growth of our business and our business plan could be materially adversely affected.

New products, including new engines we develop, may not achieve widespread adoption.

Our growth may depend on our ability to develop and/or acquire new products, and/or refine our existing products and power system technology, to complement and enhance the breadth of our power system offering with respect to engine class and the industrial OEM market categories into which we supply our products. We are currently in the process of developing new 2.0 liter and 2.4 liter engines, and we offer, but have not had material sales of, connected asset services through our telematics tool, MasterTrak, to our OEM customers and other businesses to which we do not supply our power systems. We will generally seek to develop or acquire new products, or enhance our existing products and power system technology, if we believe they will provide significant additional revenues and favorable profit margins. However, we cannot know beforehand whether any new or enhanced products will successfully penetrate our target markets. There can be no assurance that newly developed or acquired products will perform as well as we expect, or that such products will gain widespread adoption among our customers.

Additionally, there are greater design and operational risks associated with new products. The inability of our suppliers to produce technologically sophisticated components for our new engines and power systems, the discovery of any product or process defects or failures associated with production of any new products and any related product returns could each have a material adverse effect on our business, financial condition and results of operations. If new products for which we expend significant resources to develop or acquire are not successful, our business could be adversely affected.

Table of Contents

Our new 8.8 liter engine block is the first engine block manufactured in-house by our company, and may not be successful.

We have introduced a newly designed 8.8 liter, fuel flexible engine block that we have internally developed to replace an engine that we previously purchased from a third party engine supplier. This is our first engine produced in-house by us. We may not be successful in obtaining acceptance of this product in the marketplace, particularly given that it is in part the replacement for an engine block produced by a well-known and long-time engine manufacturer. Even if this product is accepted in the marketplace, we do not have sufficient history with this engine to assess whether it will succeed without significant performance issues.

The discovery of any significant problems with the engine, or any of the engines we develop, could result in recall campaigns, increased warranty costs, potential product liability claims, reputational risk and brand risk. More specifically, sales of our own internally developed engine could lead to significantly higher warranty costs to service this engine if it does not perform to expectations, as we would be unable to rely on a warranty provided by a third-party engine manufacturer. Additionally, any performance issues with our internally developed engine could also result in increased product liability claims, and we would be unable to rely on any indemnification provided by a third-party engine manufacturer. Potential losses could also arise from other unforeseen issues associated with the internal production of our own base engine block. For additional detail regarding the risk of introducing a new product such as our 8.8 liter engine, see New products may not achieve widespread adoption. For additional detail regarding the risk of warranty costs and product liability claims, see We could suffer warranty claims and We could become subject to product liability claims.

We may not succeed with the expansion of our product into the on-road market

Our current products have historically been sold and used in the off-road industrial markets. We have announced our intention to expand our product line to on-road markets into which we have not previously sold. The costs and regulations involved with certifying an engine for on-road applications may be more than expected, which could affect our ability to successfully expand our product line into these markets. Additionally, the stresses and demands on engines and power systems used for on-road applications could result in unexpected issues. Not only are we attempting to expand into markets into which we have not previously sold, we are attempting to do so using our newly designed and internally developed 8.8 liter engine. This unproven engine for on-road applications (and other additional applications) may not gain acceptance as an alternative to proven engines already used in on-road applications, and our company may not generally gain acceptance as a supplier to on-road markets. For additional detail regarding the risks related to our newly developed 8.8 liter engine, see Our new 8.8 liter engine block is the first engine block manufactured in-house by our company, and may not be successful.

Even if we are able to gain on-road certification and sell into these markets, we may expose ourselves to additional costs associated with on-road engine failures. These costs could be significant, not only if the vehicle into which the engine is installed becomes damaged, but because of the increased potential for injuries or fatalities that could arise from a malfunction or manufacturing defect in an engine used for on-road applications. Finally, we may face significantly increased competition in the on-road markets from competitors with longer operating histories, greater name recognition and greater financial and marketing resources than our current competitors in the off-road markets. For additional detail regarding the competition faced by our company, see We currently face, and will continue to face, significant competition, which could result in a decrease in our revenue.

We have recently expanded our on-road product line by entering a multi-year supply agreement with General Motors for 4.8-liter and 6.0-liter alternative fuel engines. There is no guarantee that we will be successful in expanding our on-road product line which could have an effect on our on-road supply agreement with General Motors.

Table of Contents

Changes in environmental and regulatory policies could hurt the market for our products.

Our business is affected by government environmental policies, mandates and regulations around the world, most significantly with respect to emission standards in the United States. Examples of such regulations include those that (1) restrict the sale of power systems that do not meet emission standards, (2) impose penalties on sellers of non-compliant power systems, and (3) require the use of more expensive ultra-low sulfur diesel fuel. There can be no assurance that these policies, mandates and regulations will be continued or expanded as assumed in our growth strategy. Incumbent industry participants with a vested interest in gasoline and diesel, many of which have substantially greater resources than we do, may invest significant resources in an effort to influence environmental regulations in ways that delay or repeal requirements for more stringent carbon, particulate matter (a mixture of solid particles and liquid droplets found in the air that contain a variety of chemical components, such as dust, dirt, soot or smoke) and other emissions.

We generally must obtain product certification from both the EPA and CARB to sell our products in the United States. We may attempt to expand sales of our power systems to industrial OEMs that sell their products in Europe, which also has stringent emissions requirements. Accordingly, future sales of our product will depend upon their being certified to meet the existing and future air quality and energy standards imposed by the relevant regulatory agencies. While we incur significant research and developments costs to ensure that our products comply with emission standards and meet certification requirements in the regions where our products are sold, we cannot assure you that our products will continue to meet these standards. The failure to comply with certification requirements would not only adversely affect future sales but could result in the recall of our products or civil or criminal penalties.

The adoption of new, more stringent and burdensome government emission regulations, whether at the foreign, federal, state, or local level, in markets in which we supply our power systems, may require modification of our emission certification and other manufacturing processes for our power systems. Thus, we might incur unanticipated expenses in meeting future compliance requirements, and may be required to increase our research and product development expenditures. Increases in such costs and expenses could necessitate increases in the prices we charge our OEM customers for our power systems, which could adversely affect demand for them.

We currently face, and will continue to face, significant competition, which could result in a decrease in our revenue.

The market for our products and related services is intensely competitive, subject to rapid change and sensitive to new product and service introductions and changes in technical requirements. New developments in power system technology may negatively affect the development or sale of some or all of our power systems or make our power systems uncompetitive or obsolete. Other companies, some of which have longer operating histories, greater name recognition and greater financial and marketing resources than us, are currently engaged in the development of products and technologies that are similar to, or may be competitive with, certain of our products and power system technologies. If the markets for our products (including particular industrial OEM market categories) grow as we anticipate, competition may intensify, as existing and new competitors identify opportunities in such markets.

We face competition from companies that employ current power system technologies, and may face competition in the future from additional companies as new power system technologies are adopted. Among our competitors are fuel system providers such as Westport Innovations, Inc., Fuel System Solutions and Woodward Governor, Inc., which supply engines and engine system components to the industrial OEM marketplace. Additionally, we may face competition from companies developing technologies such as cleaner diesel engines, bio-diesel, fuel cells, advanced batteries and hybrid battery/internal combustion power systems. We may not be able to incorporate such technologies into our product offerings, or may be required to devote substantial resources to doing so. The success of our business depends in large part on our ability to provide single assembly, integrated, comprehensive, technologically sophisticated power systems to our customers. The development or enhancement by our competitors of similar capabilities could adversely affect our business.

Table of Contents

Our industrial OEM customers may not continue to outsource their power system needs.

The purchasers of our power systems are industrial OEMs that manufacture industrial equipment. As a result of the significant resources and expertise required to develop and manufacture emission-certified power systems, these customers have historically chosen to outsource production of power systems to us. Our business depends in significant part on our industrial OEMs continuing to outsource design and production of power systems, power system components and subsystems. However, there can be no assurance that our OEM customers will continue to outsource, or outsource as much of, their power system production in the future. Industrial OEMs that otherwise might use our power systems may instead seek to internalize the production of these power systems and related components. Increased levels of OEM vertical integration could result from a number of factors, such as shifts in our customers business strategies, acquisition by a customer of a power system manufacturer or the emergence of low-cost production opportunities in foreign countries.

We are dependent on certain products and industrial OEM market categories for a significant share of our revenues and profits.

During the three months ended March 31, 2013 and fiscal 2012, a significant portion of our revenues were derived from sales of our power systems to be incorporated into equipment used in the power generation and forklift market categories, and we anticipate that sales of power systems in these market categories will continue to represent a significant portion of our revenues for the foreseeable future. We further believe that our growth may depend in a significant part upon our ability to increase sales of our power systems in the material handling and oil and gas market categories, as well as certain other industrial OEM categories. There can be no assurance that the material handling and oil and gas market categories, or any other industrial market category into which we sell our power systems, will grow as quickly or as significantly as we expect (if at all), or that the current, or any future, demand for our power systems in any of these market categories will not decrease.

Failure to raise additional capital or to generate the significant capital necessary to continue our growth could reduce our ability to compete and could harm our business.

We may need to raise additional capital in the future, and we may not be able to obtain additional debt or equity financing on favorable terms, if at all. Our current credit facility contains covenants restricting our ability to enter into additional debt financing. See Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and capital resources Credit agreement for a description of our credit facility. If we raise additional equity financing, our stockholders may experience significant dilution of their ownership interests, and the per share value of our common stock could decline. Furthermore, if we engage in additional debt financing, the holders of debt would have priority over the holders of common stock, and we may be required to accept terms that restrict our ability to incur additional indebtedness, and take other actions that would otherwise be in the interests of our stockholders and force us to maintain specified liquidity or other ratios. If we need additional capital and cannot raise it on acceptable terms, we may not, among other things, be able to:

- continue to expand our research and product development operations and sales and marketing organization;
- expand operations both organically and through acquisitions; or
- respond to competitive pressures or unanticipated working capital requirements.

We are dependent on relationships with our OEM customers and any change in our relationships with any of our key OEM customers could have a material adverse effect on our business and financial results.

Our power systems are integrated into our OEM customers equipment for subsequent sales and distribution to end-users of off-highway industrial equipment. One of our customers represented more than 10% of our sales in each of the last three fiscal years. We do not currently have formal, written agreements with this customer or some of our other largest customers. There can be no assurance that our current material customers, or industrial OEMs in general, will continue manufacturing equipment that uses our power systems or, if they do manufacture

Table of Contents

such equipment, that the end-users of our OEM customers will choose to purchase products into which our power systems are incorporated. Any integration, design, manufacturing or marketing problems encountered by our OEM customers could adversely affect the demand for our power systems and the ability of our OEM customers to timely pay us amounts due for our products and services. Any change in our relationships with any of our key OEM customers, whether as a result of economic or competitive pressures or otherwise, including any decision by our OEM customers to reduce their commitments to purchase our power systems in favor of competing products, could have a material adverse effect on our business and financial results.

In addition, we may be subject to disputes arising from agreements and other arrangements with our OEM customers. Disputes with our OEM customers could lead to termination of arrangements with our OEM customers and delays in collaborative development or commercialization of power systems that we design for, and supply to, these customers. Moreover, disagreements may arise with our OEM customers over rights to proprietary technology and other intellectual property incorporated in our power systems and our customers products into which our power systems are integrated. Significant disagreements with our OEM customers could result in costly and time-consuming litigation. Any such conflicts with our OEM customers could negatively impact our relationships, reduce the number of power systems which we supply, and negatively impact our ability to obtain future business, in each case with these and other OEM customers.

We are dependent on relationships with our material suppliers, and the partial or complete loss of one of these key suppliers, or the failure to find replacement suppliers or manufacturers in a timely manner, could adversely affect our business.

We have established relationships with third party engine suppliers and other suppliers from which we source our components for our power systems. We are substantially dependent on our three key engine suppliers, General Motors, Perkins/Caterpillar and Doosan. Sales of our power systems incorporating engines from General Motors, Perkins/Caterpillar and Doosan represented approximately 51%, 12% and 19% of our total sales for the three months ended March 31, 2013, approximately 55%, 13% and 17% of our total sales for the three months ended March 31, 2012, respectively, approximately 57%, 13% and 15% of our total sales for fiscal 2012, respectively, and represented approximately 64%, 10% and 13% of our total sales for fiscal 2011, respectively. If any of these three engine suppliers were to fail to provide engines in a timely manner or to supply engines that meet our quality, quantity or cost requirements, or were to discontinue manufacturing any engines we source from them or providing any such engines to us, and we were unable to obtain substitute sources in a timely manner or on terms acceptable to us, our ability to manufacture our products could be materially adversely affected. In addition, we currently source other important components used in our power systems, such as catalysts, engine controllers, fuel mixers, wiring harnesses, engine sensors and intake manifolds, from a limited number of suppliers. Much of the technology incorporated into these components that we source from a limited number of suppliers is technologically sophisticated, and we do not believe that our competitors have access to some of this sophisticated technology. Our business could be harmed by adverse changes in our relationships with our non-engine component suppliers, or if our competitors gain access to the technology. Further, if our suppliers are unable to provide components to us in a timely manner, or are unable to meet our quality, quantity or cost requirements, we may not in all cases be able to promptly obtain substitute sources. Any extended delay in receiving engines or other critical components could impair our ability to deliver products to our OEM customers.

We do not have formal, written agreements with many of our component suppliers. Most of our non-engine component supply agreements do not extend past the end of 2013, and we do not believe that any of our non-engine component supply agreements constitutes a material agreement of our company. In any event, a component supplier may fail to provide components on a timely basis, or fail to meet our specifications or other requirements for a component, regardless of whether we have a written contract with such supplier.

Table of Contents

The quality and performance of our power systems are, in part, dependent on the quality of their component parts that we obtain from various suppliers, which makes us susceptible to performance issues that could materially and adversely affect our business, reputation and financial results.

Our power systems are sophisticated and complex, and the success of our power systems is dependent, in part, upon the quality and performance of key components, such as engines, fuel systems, generators, breakers, and complex electrical components and associated software. There can be no assurance that the power system parts and components will not have performance issues from time to time, and the warranties provided by our suppliers may not always cover the potential performance issues. We may face disputes with our suppliers with respect to those performance issues and their warranty obligations, and our customers could claim damages as a result of such performance issues.

If any of the component parts we obtain from our suppliers are defective, we may incur liabilities for warranty claims. The supplier in any such case may not fully compensate us for any such liabilities. We may also be responsible for obtaining replacement parts and incur liability related thereto.

We maintain a significant investment in inventory, and a decline in our customers purchases could lead to a decline in our sales and profitability and excess inventory.

We cannot always predict the timing, frequency or size of the future orders of our OEM customers. Our ability to accurately forecast our sales is further complicated by the continuing global economic uncertainty. We maintain significant inventories in an effort to ensure that our OEM customers have a reliable source of supply. If we fail to anticipate the changing needs of our customers and accurately forecast our customer demands, our customers may not continue to place orders with us, and we may accumulate significant inventories of products that we will be unable to sell or return to our suppliers. This may result in a significant decline in the value of our inventory and a decrease in our future gross profit.

Changes in our product mix could materially and adversely affect our business.

The margins on our revenues from some of our product and service offerings are higher than the margins on some of our other product and service offerings. In particular, the margins vary between sales of our power systems as compared to sales of our aftermarket parts and components. Our margins can also fluctuate based upon competition, alternative products and services, operating costs and contractual factors. In addition, we may not be able to accurately estimate the margins of some of our new and developing products and services due to our limited operating history with sales of these products. Our new products and services may have lower margins than our current products and services.

While margins differ across the range of our power systems, prices for our power systems generally vary based on the relative sizes in terms of horsepower of the power systems. For example, if a greater proportion of our revenues are generated from sales of our lower-power power systems, our total revenues and profits may be lower than what they would be if we sold a comparable number of larger power systems, even if margins on these smaller power systems are greater.

We derive a substantial majority of our revenues attributed to our diesel power systems business from our relationships with Perkins and Caterpillar.

We derive a significant portion of our diesel power systems business from our distributor agreement with Perkins, our packaging and distribution agreements with Caterpillar engine dealers and our association with Caterpillar. Our business with Perkins and Caterpillar represented approximately 16% and 16% for the three months ended March 31, 2013 and March 31, 2012, respectively and 16% and 14% of our revenues in fiscal 2012 and 2011, respectively. Any material change in our relationships with Perkins and Caterpillar, including the termination of our distribution agreement with Perkins, could have a material adverse effect on our business and financial results.

Table of Contents

Our financial position, results of operations and cash flows have been, and may in the future be, negatively impacted by challenging global economic conditions.

Challenging global economic conditions, which can have a particularly severe impact on industrial markets, have had, and may in the future have, a material adverse effect on our business. More specifically, such conditions resulted in significantly reduced demand in 2009 for our power systems and other products from our industrial OEM customers, as those customers faced sharp declines in market demand for their products into which our power systems are incorporated. Our net sales decreased 34% from 2008 to 2009, primarily due to lower power system shipment volumes and aftermarket parts sales resulting from this reduced demand. This sales decrease was reflected across our base of customers in all of the OEM categories in which our power systems are used. Difficult market conditions can also cause us to experience pricing pressure, negatively impacting our margins.

Future economic downturns may materially impact our OEM customers, as well as suppliers and other parties with which we do business. Economic conditions that adversely affect our customers may cause them to terminate existing supply agreements or to reduce the volume of power systems they purchase from us in the future. In the case of another economic downturn, we may have significant balances owing from customers that face liquidity issues. Failure to collect a significant portion of amounts due on those receivables could have a material adverse effect on our results of operations and financial condition. Similarly, with adverse market conditions, our key suppliers from which we source power system components may be unable to provide components to us. Furthermore, we may not be able to successfully anticipate, plan for and respond to changing economic conditions, and our business could be negatively affected.

Fuel price differentials are hard to predict and may have an adverse impact on the demand for our products in the future.

The prices of various fuel alternatives are subject to fluctuation, based upon many factors, including changes in resource bases, pipeline transportation capacity for natural gas, refining capacity for crude oil and government excise and fuel tax policies. The price differential among various fuel alternatives can impact OEMs and their decisions to buy power systems from us. For example, if fossil fuel prices increase significantly, OEMs may choose to seek power systems powered by electric motors instead of ones that use fossil fuels. Furthermore, if OEMs do decide to purchase power systems from us, relative fuel prices may affect which power systems they purchase from us. The margins on our sale of certain of our power systems are higher than the margins on other power systems that we sell to our OEM customers. See Changes in our product mix could materially and adversely affect our business.

Price increases in some of the key components in our power systems could materially and adversely affect our operating results and cash flows.

The prices of some of the key components of our power systems are subject to fluctuation due to market forces beyond our control, including changes in the costs of raw materials incorporated into these components. Such price increases occur from time to time due to spot shortages of commodities, increases in labor costs or longer-term shortages due to market forces. In particular, the prices of certain precious metals used in our emissions control systems fluctuate frequently and often significantly. Substantial increases in the prices of raw materials used in components which we source from our suppliers may result in increased prices charged by our suppliers. If we incur price increases from our suppliers for key components in our power systems, our production costs will increase. Given competitive market conditions, we may not be able to pass all or any of those cost increases on to our OEM customers in the form of higher sales prices. To the extent our competitors do not suffer comparable component cost increases, we may have even greater difficulty passing along price increases and our competitive position may be harmed. As a result, increases in costs of key components may adversely affect our margins and otherwise adversely affect our operating results and cash flows.

Table of Contents

Many of our power systems involve long and variable design and sales cycles, which could have a negative impact on our results of operations for any given quarter or year.

The design and sales cycle for our customized power systems, from initial contact with our potential OEM customer to the commencement of shipments of our power systems, may be lengthy. Customers generally consider a wide range of issues before making a decision to purchase our power systems. Before an industrial OEM commits to purchase our power systems, they often require a significant technical review, assessment of competitive products and approval at a number of management levels within their organization. During the time our customers are evaluating our products, we may incur substantial sales and marketing, engineering and research and development expenses to customize our power systems to the customer s needs. We may also expend significant management efforts, increase manufacturing capacity, order long-lead-time components or purchase significant amounts of power system components and other inventory prior to receiving an order. Even after this evaluation process, a potential customer may not purchase our products.

The product development time after an industrial OEM customer agrees to purchase our power systems can be considerable. Our process for establishing technical specifications and developing a customized, integrated power system requires use of significant engineering resources, including design, prototyping, modeling, testing and application engineering. The length of this cycle is influenced by many factors, including the difficulty of the technical specification, the novelty and complexity of the design and the customer s procurement processes.

Our design, development and sales cycle may vary based on the specific power system and the industrial OEM market category in which our customer s product will compete, and it is difficult to predict for any particular transaction. The length and variability of our sales cycle can make it difficult to predict whether particular sales commitments will be received in any given period. As a result, a significant period may elapse between our investment of time and resources in designing and developing a custom power system for an OEM customer and our revenue from sales of that power system.

The length of this process may increase the risk that an OEM customer will decide to cancel or change its plans related to its equipment into which our power system is integrated. Such a cancellation or change in plans by a customer could cause us to lose anticipated sales. In addition, our business, results of operations and financial condition could be materially adversely affected if a customer curtails, materially reduces or delays a significant order during our sales cycle, chooses not to release its equipment that contains our custom power system, or is not successful in the sale and marketing of its equipment that contains our custom power system.

The loss of one or more key members of our senior management, or our inability to attract and retain qualified personnel could harm our business.

Our success and future growth depends to a significant degree on the skills and continued services of our management team, in particular Gary Winemaster, our Chief Executive Officer and President, Eric Cohen, our Chief Operating Officer and Daniel Gorey, our Chief Financial Officer. The loss of any of our key members of management could inhibit our growth prospects. Our future success also depends in large part on our ability to attract, retain and motivate key management, engineering, manufacturing and operating personnel. As we develop additional capabilities, we may require more skilled personnel. Given the highly specialized nature of our power systems, these personnel must be highly skilled and have a sound understanding of our industry, business and our technology. The market for such personnel is highly competitive. As a result, we may not be able to continue to attract and retain the personnel needed to support our business.

Our existing debt or new debt that we incur could adversely affect our business and growth prospects.

At April 30, 2013, we had approximately $34.7 million in principal amount of outstanding debt under our credit line. Our total credit facility is $50.0 million. Our indebtedness, the cash flow needed to satisfy our debt and the covenants contained in current and potential future credit agreements have important consequences, including:

- limiting funds otherwise available for financing our capital expenditures by requiring us to dedicate a portion of our cash flows from operations to the repayment of debt and the interest on this debt;

Table of Contents

limiting our ability to incur additional indebtedness;

limiting our ability to capitalize on significant business opportunities;

placing us at a competitive disadvantage to those of our competitors that are less indebted than we are;

making us more vulnerable to rising interest rates; and

making us more vulnerable in the event of a downturn in our business.

More specifically, pursuant to our current loan and security agreement with our senior lender, we have agreed to certain financial covenants, including maintaining certain ratios between our adjusted EBITDA and our fixed charges. In addition, our current loan and security agreement places limitations on our ability to make capital expenditures and to make acquisitions of other companies. Any failure by us to comply with the financial covenants set forth in our current loan and security agreement in the future, if not cured or waived, could result in our senior lender accelerating the maturity of our indebtedness or preventing us from accessing availability under our credit facility. If the maturity of our indebtedness is accelerated, we may not have sufficient cash resources to satisfy our debt obligations and we may not be able to continue our operations as planned.

Furthermore, we may incur substantial additional indebtedness in the future. If new debt or other liabilities are added to our current debt levels, the related risks that we now face, as described above, could intensify.

Our quarterly operating results are subject to variability from quarter to quarter.

Our quarter-to-quarter and quarter-over-quarter operating results (including our sales, gross profit and net income) and cash flows have been, and in the future may be, impacted by a variety of internal and external events associated with our business operations, many of which are outside of our control. Examples of such events include (1) changes in regulatory emission requirements (which generally occur on January 1 of the year in which they become effective), (2) customer product phase-in/phase-out programs, (3) supplier product (i.e. a specific engine model) phase-in/phase-out programs, (4) changes in pricing by suppliers to us of engines, components and other parts (typically effective January 1 of any year), and (5) changes in our pricing to our customers (typically effective January 1 of any year), which may be related to changes in the pricing by suppliers to us.

In order to mitigate potential availability or pricing issues, customers may adjust their demand requirements from traditional patterns. We may also extend special programs to customers in advance of such events, and we are more likely to offer such programs in our fourth quarter of a year in anticipation of events expected to occur in the first quarter of the next year. The occurrence of any of the events discussed above may result in fluctuations in our operating results (including sales and profitability) and cash flows between and among reporting periods.

If we fail to adequately protect our intellectual property rights, we could lose important proprietary technology, which could materially and adversely affect our business.

We believe that the success of our business depends, in substantial part, upon our proprietary technology, information, processes and know-how. The unauthorized use of our intellectual property rights and proprietary technology by others could materially harm our business. We do not own any material patents and rely on a combination of trademark and trade secret laws, along with confidentiality agreements, contractual provisions and licensing arrangements, to establish and protect our intellectual property rights. Although certain of our employees have entered into confidentiality agreements with us to protect our proprietary technology and processes, not all of our employees have executed such agreements, nor can we ensure that employees who have executed such agreements will not violate them.

Table of Contents

Despite our efforts to protect our intellectual property rights, existing laws afford only limited protection, and our actions may be inadequate to protect our rights or to prevent others from claiming violations of their proprietary rights. Unauthorized third parties may attempt to copy, reverse engineer or otherwise obtain, use or exploit aspects of our products and services, develop similar technology independently, or otherwise obtain and use information that we regard as proprietary. We cannot assure you that our competitors will not independently develop technology similar or superior to our technology or design around our intellectual property.

In addition, the laws of some foreign countries may not protect our proprietary rights as fully or in the same manner as the laws of the United States. In particular, we sell our power systems to industrial OEM customers, and source certain components from suppliers, in China, where commercial laws are relatively underdeveloped compared to other geographic markets into which we sell our products. Protection of intellectual property is limited under Chinese law, and the sale of our products and the local sourcing of components may subject us to an increased risk of infringement or misappropriation of our intellectual property. As a result, we cannot be certain that we will be able to adequately protect our intellectual property rights in China.

We may need to resort to litigation to enforce our intellectual property rights to protect our trade secrets and to determine the validity and scope of other companies proprietary rights in the future. However, litigation could result in significant costs or in the diversion of financial resources and management s attention. We cannot assure you that any such litigation will be successful or that we will prevail over counterclaims against us.

In addition, many of the components we source from our suppliers and which are incorporated into our power systems use proprietary intellectual property of our suppliers. We also license or rely upon certain intellectual property from third parties, including the back office software and functionality for our telematics tool, MasterTrak. For a description of MasterTrak, our telematics tool, see Business Our Products and Industry Categories Connected Asset Services. Any of these third parties from which we source our power system components, from which we license intellectual property or on whose intellectual property we rely, may also supply these components (or other components that incorporate the same intellectual property) or license or provide such intellectual property, as applicable, to others, including our competitors, or terminate our access to such intellectual property.

If we face claims of intellectual property infringement by third parties, we could encounter expensive litigation, be liable for significant damages or incur restrictions on our ability to sell our products and services.

We cannot be certain that our products, services and power system technologies, including any intellectual property licensed from third parties for use therein or incorporated into components that we source from our suppliers, do not, or in the future will not, infringe or otherwise violate the intellectual property rights of third parties. We are not aware of all of the proprietary technology incorporated into, or used in developing, the components that we source and integrate into our power systems, nor are we familiar with all of the technology included in, or used in developing, products that are competitive with these components. Furthermore, the design, prototyping, testing and engineering capabilities we use to manufacture our power systems are technologically sophisticated, and we consider the processes by which we develop our power systems to be confidential and proprietary trade secrets. To compete in the industrial OEM market, our competitors likely also use proprietary development processes to manufacture their products. Given that neither we nor our competitors make information regarding such manufacturing and development processes available to the public, we cannot know the extent to which there may be any commonality between our respective processes and cannot be certain that we are not infringing on any intellectual property rights of others. In addition, for the above reasons, we cannot assure you that third parties will not claim that we have infringed their intellectual property rights.

A third party alleged, and asserted those allegations in proceedings against us (which proceedings were subsequently settled), that certain technology related to our telematics tool, MasterTrak, infringed upon the intellectual property rights of that party. As such, we may in the future be subject to similar infringement claims

Table of Contents

that may result in litigation. Successful infringement claims against us could result in substantial monetary liability, require us to enter into royalty or licensing arrangements, or otherwise materially disrupt the conduct of our business. In addition, even if we prevail in the defense of any such claims, any such litigation could be time-consuming and expensive to defend or settle, and could result in the diversion of the time and attention of management and of operational resources, which could materially and adversely affect our business. Any potential intellectual property litigation also could force us to do one or more of the following:

- stop selling and/or using the specific products and/or services incorporating the allegedly infringing technology and/or stop incorporating the allegedly infringing technology into such products and/or services;
- obtain from the owner of the infringed intellectual property right a license to sell and/or use the relevant technology, which license may not be available on commercially reasonable terms, or at all; or
- redesign the products and/or services that incorporate the allegedly infringing technology.

We could suffer warranty claims.

From time to time, we may incur liabilities for warranty claims as a result of defective products or components, including claims arising from defective products or components provided by our suppliers that are integrated into our power systems. Provisions we make for warranty accrual may not be sufficient, and we may recognize additional expenses as a result of warranty claims in excess of our current expectations. Such warranty claims may necessitate a redesign, re-specification, a change in manufacturing processes, and/or recall of our power systems, which could have an adverse impact on our finances and on existing or future sales of our power systems and other products. Even in the absence of any warranty claims, a product deficiency such as a manufacturing defect or a safety issue may necessitate a product recall, which could have an adverse impact on our finances and on existing or future sales.

We could become subject to product liability claims.

Our business exposes us to potential product liability claims that are inherent to natural gas, propane, gasoline and diesel, and products that use these fuels. Natural gas, propane and gasoline are flammable and are potentially dangerous products. Any accidents involving our power systems could materially impede widespread market acceptance and demand for our power systems. In addition, we may be subject to a claim by end-users of our OEM customers products or others alleging that they have suffered property damage, personal injury or death because our power systems or the products of our customers into which our power systems are integrated did not perform adequately. Such a claim could be made whether or not our power systems perform adequately under the circumstances. From time to time, we may be subject to product liability claims in the ordinary course of business, and we carry a limited amount of product liability insurance for this purpose. However, our current insurance policies may not provide sufficient or any coverage for such claims, and we cannot predict whether we will be able to maintain our insurance coverage on commercially acceptable terms.

Our telematics tool, MasterTrak, may not be successful.

Our telematics tool does not currently provide a material portion of our revenues. There can be no assurance that our telematics tool will gain widespread acceptance among customers or generate meaningful revenues or profits.

We are subject to various laws and regulations relating to our telematics tool. Among other things, wireless transceiver products are required to be certified by the Federal Communications Commission and comparable authorities in foreign countries where they are sold. If we fail to obtain product certifications for our telematics product, or otherwise fail to successfully comply with applicable regulations in this area, we may be required to make significant unanticipated expenditures to bring our telematics tool within compliance with such regulations,

Table of Contents

and future sales of our telematics tool may be adversely affected. Furthermore, through our telematics tool, we transmit and store information of customers, including equipment-specific information such as performance data. Equipment-specific information may also reveal customer-identifiable information. A growing body of laws designed to protect the privacy of personally-identifiable information, as well as to protect against its misuse, and the judicial interpretations of such laws, may adversely affect the growth of our telematics business. In particular, such laws could limit our ability to collect information related to users of our telematics tool, to store or process that information in what would otherwise be the most efficient manner, or to commercialize new telematics services based on emerging technologies. In addition, we could become subject to third party claims based upon allegations of loss or misuse of customer information.

See also If we face claims of intellectual property infringement by third parties, we could encounter expensive litigation, be liable for significant damages or incur restrictions on our ability to sell our products and services, for a discussion of a third party intellectual property infringement claim with respect to technology related to our telematics tool, which matter has been settled.

We may have difficulty managing the expansion of our operations.

Our organization and our facilities currently in place may not be adequate to support our future growth. In order to effectively manage our operations and any significant growth, including any significant growth in the sales of, and services related to, our power systems, we may need to:

- scale our internal infrastructure, including establishing additional facilities, while continuing to provide technologically sophisticated power systems on a timely basis;
- attract and retain sufficient numbers of talented personnel, including application engineers, customer support staff and production personnel;
- continue to enhance our compliance and quality assurance systems; and
- continue to improve our operational, financial and management controls and reporting systems and procedures.

Rapid expansion of our operations could place a significant strain on our senior management team, support teams, manufacturing lines, information technology platforms and other resources. In addition, we may be required to place more reliance on our strategic partners and suppliers, some of whom may not be capable of meeting our production demands in terms of timing, quantity, quality or cost. Difficulties in effectively managing the budgeting, forecasting and other process control issues presented by any rapid expansion could harm our business, prospects, results of operations or financial condition.

If we do not properly manage the sales of our products into foreign markets, our business could suffer.

A significant portion of our future revenues could be derived from sales outside of the United States, particularly in Asia. We have sales and distribution activities in Asia and Europe where we may lack sufficient expertise, knowledge of local customs or contacts. In Asia, we depend upon an independent sales and support organization to complement our OEM relationships and provide knowledge of local customs and requirements, while also providing immediate sales assistance and customer support. There can be no assurance that we will be able to maintain our current relationship with this independent sales and support organization, or that we will be able to develop effective, similar relationships in foreign markets into which we supply our products in the future.

Growing the market for our products in Asia and other markets outside of the United States may take longer and cost more to develop than we anticipate and is subject to inherent risks, including unexpected changes in government policies, trade barriers restricting our ability to sell our products in those countries, longer payment cycles, exposure to currency fluctuations, and foreign exchange controls that restrict or prohibit repatriation of funds. As a result, if we do not properly manage foreign sales, our business could suffer.

Table of Contents

In addition, our foreign sales subject us to numerous stringent U.S. and foreign laws, including the Foreign Corrupt Practices Act, or FCPA, and comparable foreign laws and regulations which prohibit improper payments or offers of payments to foreign governments and their officials and political parties by U.S. and other business entities for the purpose of obtaining or retaining business. Safeguards that we may implement to discourage these practices could prove to be ineffective, and violations of the FCPA and other laws may result in severe criminal or civil sanctions, or other liabilities or proceedings against us, including class action lawsuits and enforcement actions from the SEC, Department of Justice and overseas regulators. Any of these factors, or any other international factors, could impair our ability to effectively sell our power systems, or other products or services that we may develop, outside of the U.S.

If our production facilities become inoperable, our business, including our ability to manufacture our power systems, will be harmed.

We operate our business, including all of our production and manufacturing processes, out of facilities that are all located in Wood Dale, Illinois. If damaged, our facilities, our manufacturing lines, the equipment we use to perform our emission certification and other tests and our other business process systems would be costly to replace and could require substantial time to repair or replace. We are particularly subject to this risk because of our current geographic concentration of our facilities. During 2012, we completed the consolidation of our facilities that are all located in Wood Dale, Illinois. This consolidation further exacerbates this risk. Our facilities may be harmed or rendered inoperable by natural or man-made disasters, including earthquakes, wildfires, floods, acts of terrorism or other criminal activities, infectious disease outbreaks and power outages, which may render it difficult or impossible for us to efficiently operate our business for some period of time. In addition, such events may temporarily interrupt our ability to receive engines, fuel systems or other components for our power systems from our suppliers and to have access to our various production systems necessary to operate our business. Our insurance covering damage to our properties and the disruption of our business may not be sufficient to cover all of our potential losses and may not continue to be available to us on acceptable terms, or at all.

In the event our facilities are damaged or destroyed, we may need to find another facility into which we can move our operations. Finding a facility that meets the criteria necessary to operate our business would be time-consuming and costly and result in delays in our ability to provide our sophisticated power systems or to provide the same level of quality in our services as we currently provide.

We may be adversely impacted by work stoppages and other labor matters.

Our workforce consists of full-time and part-time employees, as well as, members of our production team whose services we obtain through an arrangement with a professional employer organization. While none of the members of our workforce are currently represented by a union or covered by a collective bargaining agreement, there have been unsuccessful efforts to unionize our manufacturing employees in the past, and there can be no assurance that members of our workforce will not in the future join a union. If our employees organize and join a union in the future, there can be no assurance that future issues with our workforce will be resolved favorably or that we will not encounter future strikes, work stoppages or other types of conflicts with labor unions or our employees. Any of these consequences may have an adverse effect on us or may limit our flexibility in dealing with our workforce.

In addition, many of our suppliers have unionized work forces. Work stoppages or slow-downs experienced by our material suppliers could result in slow-downs or closures at the manufacturing facilities of our suppliers from where our power system components are sourced. If one or more of our key suppliers experience a material work stoppage, it could have a material adverse effect on our operations.

Table of Contents

We could be adversely affected by risks associated with acquisitions and joint ventures.

From time to time, we may seek to expand our business through investments in, joint ventures with or acquisitions of, complementary businesses, technologies, services or products, subject to our business plans and management s ability to identify, acquire and develop suitable investments or acquisition targets in both new and existing industrial OEM market categories and geographic markets. In certain circumstances, acceptable investments or acquisition targets might not be available. Acquisitions involve a number of risks, including: (1) difficulty in integrating the operations, technologies, products and personnel of an acquired business, including consolidating redundant facilities and infrastructure; (2) potential disruption of our ongoing business and the distraction of management from our day-to-day operations; (3) difficulty entering markets in which we have limited or no prior experience and in which competitors have a stronger market position; (4) difficulty maintaining the quality of services that such acquired companies have historically provided; (5) potential legal and financial responsibility for liabilities of acquired businesses; (6) overpayment for the acquired company or assets; (7) increased expenses associated with completing an acquisition and amortizing any acquired intangible assets; and (8) challenges in implementing uniform standards, controls, procedures and policies throughout an acquired business. In addition, under the terms of our credit facility, we may be restricted from engaging in certain acquisition transactions. See Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and capital resources Credit agreement for a description of our credit facility.

If we were to pursue acquisition or investment opportunities, these potential risks could disrupt our ongoing business, result in the loss of key customers or personnel, increase expenses and otherwise have a material adverse effect on our business, results of operations and financial condition.

We could become liable for damages resulting from our manufacturing activities.

The nature of our manufacturing operations exposes us to potential claims and liability for environmental damage, personal injury, loss of life and damage to, or destruction of, property. Our manufacturing operations are subject to numerous laws and regulations that govern environmental protection and human health and safety. These laws and regulations have changed frequently in the past and it is reasonable to expect additional and more stringent changes in the future. Our manufacturing operations may not comply with future laws and regulations, and we may be required to make significant unanticipated capital and operating expenditures to bring our operations within compliance with such regulations. If we fail to comply with applicable environmental laws and regulations, manufacturing guidelines, and workplace safety requirements, governmental authorities may seek to impose fines and penalties on us or to revoke or deny the issuance or renewal of operating permits, and private parties may seek damages from us. Under such circumstances, we could be required to curtail or cease operations, conduct site remediation or other corrective action, or pay substantial damage claims for which we may not have sufficient or any insurance coverage for claims.

We may have unanticipated tax liabilities that could adversely impact our results of operations and financial condition.

We are subject to various types of taxes in the U.S., as well as foreign jurisdictions into which we supply our products. The determination of our provision for income taxes and other tax accruals involves various judgments, and therefore the ultimate tax determination is subject to uncertainty. In addition, changes in tax laws, regulations, or rules may adversely affect our future reported financial results, may impact the way in which we conduct our business, or may increase the risk of audit by the Internal Revenue Service or other tax authority. Although we are not subject to any audits currently, we may be in the future subject to an Internal Revenue Service audit or other audit by state, local and foreign tax authorities. The final determinations of any tax audits in the U.S. or abroad could be materially different from our historical income tax provisions and accruals. If any taxing authority disagrees with the positions taken by us on our tax returns, we could incur additional tax liabilities, including interest and penalties.

Table of Contents

Variability in self-insurance liability estimates could significantly impact our results of operations.

We self-insure for employee health insurance coverage up to a predetermined level, beyond which we maintain stop-loss insurance from a third-party insurer. Our aggregate exposure varies from year to year based upon the number of participants in this health insurance plan. We estimate our self-insurance liabilities using an analysis provided by our claims administrator and our historical claims experience. Our accruals for insurance reserves reflect these estimates and other management judgments, which are subject to a high degree of variability. Any significant variation in these estimates and judgments could cause a material change to our reserves for self-insurance liabilities, as well as our earnings.

Risks Related to the Shell Company

We may have contingent liabilities related to Format, Inc. s operations prior to the reverse recapitalization transaction of which we are not aware and for which we have not adequately provisioned.

Format, Inc. may be deemed to have been a shell company with nominal operations and assets prior to the reverse recapitalization transaction. Upon completion of the reverse recapitalization, we acquired all of the operations of The W Group and its subsidiaries. Immediately prior to the consummation of the reverse recapitalization, Format, Inc. was engaged, to a limited extent, in EDGARizing corporate documents for filing with the SEC, and providing limited commercial printing services. We cannot assure you that there are no material claims outstanding, or other circumstances of which we are not aware, that would give rise to a material liability relating to those prior operations, even though we do not record any provisions in our financial statements related to any such potential liability. If we are subject to past claims or material obligations relating to our operations prior to the consummation of the reverse recapitalization, such claims could materially adversely affect our business, financial condition and results of operations.

Risks Related to this Offering and Ownership of Our Common Stock

We incur significant costs and demands upon management and accounting and finance resources as a result of complying with the laws and regulations affecting public companies; any failure to establish and maintain adequate internal control over financial reporting or to recruit, train and retain necessary accounting and finance personnel could have an adverse effect on our ability to accurately and timely prepare our consolidated financial statements.

As a public operating company, we incur significant administrative, legal, accounting and other burdens and expenses beyond those of a private company, including those associated with corporate governance requirements and public company reporting obligations. In particular, we have needed to enhance and supplement our internal accounting resources with additional accounting and finance personnel with the requisite technical and public company experience and expertise, as well as refine our quarterly and annual financial statement closing process, to enable us to satisfy such reporting obligations.

Furthermore, we are required to comply with Section 404 of the Sarbanes-Oxley Act of 2002. In order to satisfy the requirements of Section 404 of the Sarbanes-Oxley Act of 2002, we are required to document and test our internal control procedures and prepare annual management assessments of the effectiveness of our internal control over financial reporting. These assessments must include disclosure of identified material weaknesses in our internal control over financial reporting. The existence of one or more material weaknesses could affect the accuracy and timing of our financial reporting. Testing and maintaining internal control over financial reporting involves significant costs and could divert management s attention from other matters that are important to our business. Additionally, we cannot provide any assurances that we will be successful in remediating any deficiencies that may be identified. If we are unable to remediate any such deficiencies or otherwise fail to establish and maintain adequate accounting systems and internal control over financial reporting, or we are unable to continue to recruit, train and retain necessary accounting and finance personnel, we may not be able to accurately and timely prepare our consolidated financial statements and otherwise satisfy our public reporting

Table of Contents

obligations. Any inaccuracies in our financial statements or other public disclosures (in particular if resulting in the need to restate previously filed financial statements), or delays in our making required SEC filings, could have a material adverse effect on the confidence in our financial reporting, our credibility in the marketplace and the trading price of our common stock.

We have identified material weaknesses in our internal controls, and we cannot provide assurances that these weaknesses will be effectively remediated or that additional material weaknesses will not occur in the future. Specifically, under the supervision of our Chief Executive Officer and Chief Financial Officer, our management conducted an assessment of the effectiveness of our internal control over financial reporting as of December 31, 2012, based on the framework in the Internal Control-Integrated Framework published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on this assessment, our management concluded that as of December 31, 2012, our internal control over financial reporting was not effective based on those criteria. Based on management s assessment, controls over the business system software used within our aftermarket parts group were not adequate. Our management has been engaged in developing and implementing a remediation plan to address the material weakness, but we cannot assure you that our internal control over financial reporting, as modified, will enable us to identify or avoid material weaknesses in the future.

As a smaller reporting company, we have been able to take advantage of an exemption from the auditor attestation requirements of Section 404(b) of the Sarbanes-Oxley Act. If we no longer qualify as a smaller reporting company, compliance with these auditor attestation requirements will require additional costs and significant time and resources from our management and finance and accounting personnel.

In addition, our management team must continue to adapt to other requirements of being a public company. We need to devote significant resources to address these public company-associated requirements, including compliance programs and investor relations, as well as our financial reporting obligations. We incur substantial legal and financial compliance costs as a result of complying with these rules and regulations promulgated by the SEC.

We are currently a smaller reporting company and are able to avail ourselves of reduced disclosure requirements applicable to smaller reporting companies, which could make our common stock less attractive to investors.

We are a smaller reporting company, as defined in the rules promulgated by the SEC under the Exchange Act. We have in this prospectus taken advantage of, and we plan in future filings with the SEC, for as long as we qualify as a smaller reporting company, to continue to take advantage of, certain exemptions from various reporting requirements that are applicable to public companies that are not smaller reporting companies, including reduced disclosure obligations regarding our business and executive compensation, as well as financial information. As a result, our stockholders may not have access to certain information they may deem important. We cannot predict if investors will find our common stock less attractive because we rely on these exemptions. If some investors find our common stock less attractive as a result, there may be a less active trading market for our common stock and our stock price may be more volatile.

Concentration of ownership among our existing executive officers may prevent new investors from influencing significant corporate decisions.

Following this offering, Gary Winemaster, our Chairman of the Board, Chief Executive Officer and President, and Kenneth Winemaster, our Senior Vice President and Secretary, will beneficially own in the aggregate approximately % of our outstanding shares of common stock (or % if the underwriters exercise their over-allotment option in full). On a fully-diluted basis, assuming the exercise of all outstanding warrants and outstanding stock appreciation rights, such individuals will beneficially own in the aggregate approximately % of our outstanding shares of common stock (or % if the underwriters exercise their

Table of Contents

over-allotment option in full). Following the offering, Gary Winemaster alone will beneficially own approximately % of our outstanding shares of common stock (or % if the underwriters exercise their over-allotment option in full). On a fully diluted basis, assuming the exercise of all outstanding warrants and outstanding stock appreciation rights, Gary Winemaster alone will beneficially own % of our outstanding shares of common stock (or % if the underwriters exercise their over-allotment option in full).

As a result of Gary Winemaster s and Kenneth Winemaster s beneficial ownership of a significant majority of our outstanding shares of common stock, these stockholders can exercise control over matters requiring stockholder approval, including the election of directors, amendment of our articles of incorporation and approval of significant corporate transactions. This control could have the effect of delaying or preventing a change of control of our company or changes in management and will make the approval of certain transactions impossible without the support of these stockholders.

A liquid and orderly trading market for our common stock may not develop, and the price of our stock may be volatile and may decline in value.

To date, there has not been a particularly liquid and orderly public trading market for our common stock. An active, liquid public trading market may not develop or may not be sustained. The lack of an active, liquid public trading market may impair your ability to sell your shares of common stock at the time you wish to sell them or at a price that you consider reasonable. The lack of an active, liquid public trading market for our common stock may also impair our ability to raise capital by selling shares of common stock and may impair our ability to acquire other companies or assets by using shares of our common stock as consideration.

The trading price of our common stock may be highly volatile and could be subject to wide fluctuations in response to various factors, some of which are beyond our control. The stock market in general has experienced extreme price and volume fluctuations that have often been unrelated or disproportionate to the operating performance of companies with securities traded in those markets. Broad market and industry factors may seriously affect the market price of companies stock, including ours, regardless of actual operating performance. In addition, in the past, following periods of volatility in the overall market and the market price of a particular company s securities, securities class action litigation has often been instituted against these companies. This litigation, if instituted against us, could result in substantial costs and a diversion of our management s attention and resources.

A significant number of shares of our common stock were registered for sale in 2011 and have become eligible for sale, which could depress the market price for our common stock. Future sales by us or our existing stockholders could similarly depress the market price of our common stock.

A significant number of shares of our common stock were registered for sale in 2011 and have become eligible for sale in the public market, which could cause the market price for our common stock to decline significantly. If we or our existing stockholders sell a large number of shares of our common stock, or if we sell additional securities that are convertible into common stock, in the future, the market price of our common stock similarly could decline. Further, even the perception in the public market that we or our existing stockholders might sell shares of common stock could depress the market price of our common stock.

We have broad discretion in the use the net proceeds that we will receive from this offering (or additional availability under our revolving line of credit resulting from the repayment of our outstanding borrowings thereunder with our proceeds from this offering) and may not use them in a manner in which our stockholders would consider appropriate.

Our management will have broad discretion in the application of the net proceeds that we will receive from this offering (or additional availability under our revolving line of credit resulting from the repayment of our outstanding borrowings thereunder with our proceeds from this offering). Our stockholders may not agree with the manner in which our management chooses to allocate and spend these funds. The failure by our management to apply these funds effectively could have a material adverse effect on our business.

Table of Contents

Anti-takeover provisions contained in our certificate of incorporation and bylaws, as well as provisions of Delaware law, could impair a takeover attempt.

In addition to the concentration of ownership described under Concentration of ownership among our existing executive officers and their affiliates may prevent new investors from influencing significant corporate decisions above, which will prevent any attempt to acquire control of our company not supported by these significant stockholders, our certificate of incorporation, bylaws and Delaware law contain provisions which could have the effect of rendering more difficult, delaying or preventing an acquisition deemed undesirable by our board of directors. Our organizational documents include provisions:

- authorizing blank check preferred stock, which may be issued by our board of directors without stockholder approval and may contain voting, liquidation, dividend and other rights superior to our common stock; and
- limiting the liability of, and providing indemnification to, our directors and officers.

These provisions, alone or together, could delay or prevent hostile takeovers and changes in control or changes in our management. Provisions of Delaware law may also have anti-takeover effects. Any provision of our certificate of incorporation or bylaws or Delaware law that has the effect of delaying or deterring a change in control could limit the opportunity for our stockholders to receive a premium for their shares of our common stock, and could also affect the price that some investors are willing to pay for our common stock.

Our stockholders may experience significant dilution if future equity offerings are used to fund operations or acquire complementary businesses.

If we engage in capital raising activities in the future, including issuances of common stock, to fund the growth of our business, our stockholders could experience significant dilution. In addition, securities issued in connection with future financing activities or potential acquisitions may have rights and preferences senior to the rights and preferences of our common stock. During 2012, we adopted the 2012 Incentive Compensation Plan, and this plan was approved by a majority of our stockholders. The adoption of this plan pursuant to which equity awards have been, and may continue to be, granted to eligible employees (including our executive officers), directors and consultants, and the related issuance of shares of our common stock upon the exercise of any such equity awards may result in dilution to our stockholders and adversely affect our earnings. In addition, in the near future, we may seek to increase the number of shares available for awards pursuant to this plan. See Executive Compensation 2012 Incentive Compensation Plan for a description of this plan.

If securities or industry analysts do not publish, or cease publishing, research or reports about us, our business or our market, or if they change their recommendations regarding our stock adversely, our stock price and trading volume could decline.

The trading market for our common stock will be influenced by the extent to which industry or securities analysts publish research and reports about us, our business, our market or our competitors and what they publish in those reports. Any analysts that do cover us may make adverse recommendations regarding our stock, adversely change their recommendations from time to time, and/or provide more favorable relative recommendations about our competitors. If any analyst who covers us were to cease coverage of our company or fail to regularly publish reports on us, or if analysts fail to cover us or publish reports about us at all, we could lose, or never gain, visibility in the financial markets, which in turn could cause our stock price or trading volume to decline.

We do not anticipate paying any dividends in the foreseeable future.

The payment of dividends is currently restricted by our credit agreement with BMO Harris Bank N.A. We intend to retain our future earnings to support operations and to finance expansion and, therefore, we do not

Table of Contents

anticipate paying any cash dividends to holders of our common stock in the foreseeable future. Because we do not anticipate paying dividends in the future, the only opportunity to realize the value of our common stock will likely be through an appreciation in value and a sale of those shares. There is no guarantee that shares of our common stock will appreciate in value or even maintain the price at which shares are sold in this offering.

A research report, which does not reflect our views, was published by one of our underwriters prior to the filing of our registration statement. No investor should rely on this research report when making an investment decision. We could be subject to liability as a result of the publication of this research report.

Prior to the filing of the registration statement of which this prospectus forms a part, a research report regarding our quarterly financial results was written and published by Craig-Hallum Capital Group LLC, one of our underwriters, which publishes and distributes research reports on our company in the regular course of its business.

We were not involved in any way in the preparation of this research report and had no knowledge of this research report until after it was released. Such report does not reflect our views, and we disclaim all responsibility for its contents. You should disregard the contents of this research report entirely when making any investment decision with respect to our common stock. Any decision to purchase our common stock in this offering should be based solely on the information contained in this prospectus.

The research report may be deemed a prospectus not meeting the requirements of the Securities Act, and the publication of the report could be found to be a violation of Section 5 of the Securities Act. If the publication of this research report were to be held by a court to be a violation by us of Section 5 of the Securities Act, we could be required to repurchase the shares sold to certain purchasers in this offering at the original purchase price, or, if such purchasers had already sold the securities, could be liable to them for damages. We could be subject to other claims for damages and costs as a result of the publication of the research report.

Cautionary Note Regarding Forward-Looking Statements

This prospectus includes forward-looking statements that reflect our expectations and projections about our future results, performance, prospects and opportunities. These statements can be identified by the fact that they do not relate strictly to historical or current facts. We have tried to identify forward-looking statements by using words such as anticipate, believe, could, estimate, expect, intend, may, plan, potential, should, will, will be, would and similar expressions, but this is not an exclusive way of identifying such statements. These forward-looking statements include, among others, statements relating to our future financial performance, our business prospects and strategy, anticipated financial position, liquidity and capital needs and other similar matters. These forward-looking statements are based on management s current expectations and assumptions about future events, which are inherently subject to uncertainties, risks and changes in circumstances that are difficult to predict. Our actual results, performance and achievements may differ materially from those expressed in, or implied by, the forward-looking statements contained in this prospectus as a result of various risks, uncertainties and other factors, including, among others, those described above under the heading Risk Factors and elsewhere in this prospectus. Accordingly, you should read this prospectus completely and with the understanding that our actual future results may be materially different from what we expect.

Forward-looking statements speak only as of the date of this prospectus. Except as expressly required under federal securities laws and the rules and regulations of the SEC, we do not undertake any obligation to update any forward-looking statements to reflect events or circumstances arising after the date of this prospectus, whether as a result of new information or future events or otherwise. You should not place undue reliance on the forward-looking statements included in this prospectus or that may be made elsewhere from time to time by us, or on our behalf. All forward-looking statements attributable to us are expressly qualified by these cautionary statements.

Table of Contents

Use of Proceeds

We estimate that our net proceeds from the sale of shares of our common stock will be approximately $ million, based on an assumed public offering price of $ per share (the closing bid price of our common stock as reported on the OTC Bulletin Board on May , 2013), and after deducting underwriting discounts and commissions and estimated offering expenses payable by us.

We currently intend to use a substantial portion of our net proceeds to pay down our outstanding borrowings under our revolving line of credit with BMO Harris Bank, N.A., which is scheduled to mature on March 20, 2017. Pursuant to the terms of our revolving line of credit, upon the issuance of any equity securities, we must repay our outstanding borrowings thereunder with 100% of the proceeds we receive in any such issuance. As of March 31, 2013, $6.9 million of the Company s outstanding borrowings under its revolving line of credit bore interest at the prime rate, which equated to 3.25% with the applicable margin included. The remaining outstanding balance of $25.0 million as of March 31, 2013, had been designated to bear interest at the LIBOR rate, plus an applicable margin, which equated to 1.95%. The unused and available revolving line of credit balance was $18.1 million at March 31, 2013. See Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources Credit Agreement below for additional information regarding our credit facility.

We intend to use any remaining net proceeds (and the additional availability under our revolving line of credit resulting from the repayment of our outstanding borrowings thereunder with our proceeds from this offering) for working capital and other general corporate purposes. Such purposes may include further expansion into on-road markets, development of new engines and product testing and certification. Additionally, we may use a portion of the remaining net proceeds (and the additional availability under our revolving line of credit) for the acquisition of, or investment in, companies, technologies or assets that complement our business and further our growth strategy; however, we have no present understandings, commitments or agreements to make any such material acquisitions or investments. We cannot specify with certainty the particular uses for our remaining net proceeds (or any additional availability under our revolving line of credit) and, at the date hereof, cannot accurately predict the amounts that we may spend for any particular purpose. Our management team will have broad discretion in determining the uses of our remaining net proceeds. The amounts of our actual expenditures will be influenced by a variety of factors, including the timing and extent of our expansion opportunities, the amount of cash used by our operations and the occurrence of unforeseen opportunities and events.

We will not receive any proceeds from the sale of shares of common stock by the selling stockholders.

Dividend Policy

We have not paid any cash dividends on our common stock to date. The payment of dividends is currently restricted by our Agreement with BMO Harris Bank, N.A. We intend to retain our future earnings to support operations and to finance expansion. See Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources Credit Agreement below for a further discussion regarding restrictions on the payment of dividends under our new credit facility.

Table of Contents

Price Range of Common Stock

Our common stock is traded on the OTC Bulletin Board and the OTC Markets OTCQB tier under the symbol PSIX. Prior to the completion of this offering, we intend to list our common stock on the NASDAQ Global Market. The table below sets forth the high and low bid prices per share of our common stock as quoted on the OTC Bulletin Board and the OTC Markets OTCQB tier for the periods indicated. Prior to April 29, 2011, the effective date of the reverse recapitalization, the common stock traded under the symbol FRMT. All over-the-counter market quotations for our common stock included below for periods prior to the effectiveness of the reverse split have been adjusted to give retroactive effect to the 1-for-32 reverse stock split of our common stock that was effected on August 26, 2011, pursuant to the migratory merger, and reflect inter-dealer prices, without retail mark-up, mark-down or commission and may not necessarily represent actual transactions.

Prior to the reverse recapitalization, there was limited or no trading activity in Format s common stock. Prior to the consummation of the reverse recapitalization transaction (and for a period thereafter) only one market maker posted quotations for our common stock on the OTC Bulletin Board or, to the extent there were multiple market makers, those market makers were posting unpriced quotations. Accordingly, there is limited information available about the market price of our common stock on the OTC Bulletin Board prior to the consummation of the reverse recapitalization transaction.

	High	Low
Fiscal Year Ended December 31, 2011		
First Quarter	$ 16.32	$ 6.40
Second Quarter	$ 16.32	$ 16.32
Third Quarter	$ 17.60	$ 6.40
Fourth Quarter	$ 13.50	$ 7.25
Fiscal Year Ended December 31, 2012		
First Quarter	$ 17.75	$ 10.00
Second Quarter	$ 20.95	$ 14.00
Third Quarter	$ 17.15	$ 15.10
Fourth Quarter	$ 18.00	$ 14.35
Fiscal Year Ending December 31, 2013		
First Quarter	$ 26.08	$ 16.18
Second Quarter (through May 13, 2013)	$ 31.85	$ 24.00

As of May 13, 2013, the closing bid price for our common stock on the OTC Bulletin Board was $31.80 per share.

Holders

As of May 10, 2013, there were approximately 23 holders of record of our common stock. The actual number of stockholders is significantly greater than this number of record holders and includes stockholders who are beneficial owners but whose shares are held in street name by brokers and other nominees. This number of holders of record also does not include stockholders whose shares may be held in trust by other entities.

Table of Contents

Capitalization

The following table sets forth our cash and our capitalization as of March 31, 2013:

On an actual basis; and

On a pro forma basis to give effect to (1) the sale of shares of our common stock by us in this offering at an assumed public offering price of $ per share (the closing bid price of our common stock as reported on the OTC Bulletin Board on May , 2013), after deducting the underwriters discounts and commissions and the estimated offering expenses payable by us and (2) the application of the estimated net proceeds to us from this offering as described under Use of Proceeds, as if the offering had occurred on March 31, 2013.

The information below is illustrative only and our cash and capitalization following the completion of this offering will be based on the actual public offering price and other terms of this offering determined at pricing. You should read this table together with Use of Proceeds, Management s Discussion and Analysis of Financial Condition and Results of Operations and our financial statements included elsewhere in this prospectus.

	March 31, 2013 (unaudited)	
	Actual	Pro Forma for this Offering(1)
	(in thousands, except share data)	
Cash	$ 295	$
Revolving line of credit	$ 31,945	
Stockholders equity:		
Common stock $0.001 par value per share. Authorized: 50,000,000 shares. Issued: 10,047,546 and 11,247,546 actual and pro forma, respectively. Outstanding: 9,216,621 and 10,216,621 actual and pro forma, respectively.	10	
Additional paid-in capital	14,323	
Retained earnings	13,185	
Treasury Stock, at cost, 830,925 shares actual and pro forma	(4,250)	
Total stockholders equity	23,268	
Total capitalization	$ 55,213	$

(1) Each $1.00 increase (decrease) in the assumed public offering price of $ per share of common stock (the closing bid price of our common stock as reported on the OTC Bulletin Board on May , 2013) would increase (decrease) the amount of cash, additional paid-in capital, total stockholders equity and total capitalization (pro forma for this Offering) by approximately $ million, assuming the number of shares offered by us, as set forth on the cover of this prospectus, remains the same and after deducting the estimated underwriting discounts and commissions and estimated offering expenses that we must pay.

Table of Contents

Selected Historical Consolidated Financial and Operating Data

Set forth below is selected historical consolidated financial and operating data of the Company at the dates and for the periods indicated. The selected historical consolidated statement of operations data for the years ended December 31, 2010, December 31, 2011 and December 31, 2012 and the selected historical consolidated balance sheet data as of December 31, 2011 and December 31, 2012 have been derived from our audited consolidated financial statements included elsewhere in this prospectus. The selected historical consolidated balance sheet data as of December 31, 2010 has been derived from our audited consolidated financial statements that do not appear in this prospectus. The selected historical consolidated statement of operations data for the three months ended March 31, 2012 and March 31, 2013 and selected historical consolidated balance sheet data as of March 31, 2013 have been derived from our unaudited consolidated financial statements included elsewhere in this prospectus. The summary historical consolidated balance sheet data as of March 31, 2012 has been derived from our unaudited consolidated financial statements that do not appear in this prospectus. Our historical results are not necessarily indicative of the results that may be expected in any future period.

The selected historical consolidated financial and operating data set forth below should be read in conjunction with Use of Proceeds, Capitalization, Management s Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements included elsewhere in this prospectus.

(Dollar amounts in thousands, except per share amounts)	Years Ended December 31, 2012	2011	2010	Three Months Ended March 31, 2013	2012
				(unaudited)	
Statement of Operations Data:					
Net sales	$ 202,342	$ 154,969	$ 100,521	$ 52,576	$ 48,072
Cost of sales	168,425	128,541	83,894	43,407	39,843
Gross profit	33,917	26,428	16,627	9,169	8,229
Operating expenses:					
Research & development and engineering	7,377	4,713	3,846	1,771	1,727
Selling and service	5,925	6,666	5,465	1,880	1,702
General and administrative	8,299	5,244	3,250	2,438	1,764
Total operating expenses	21,601	16,623	12,561	6,089	5,193
Operating income	12,316	9,805	4,066	3,080	3,036
Other (income) expense	1,471	2,971	2,131	5,040	855
Income before income taxes	10,845	6,834	1,935	(1,960)	2,181
Income tax provision	4,143	2,773	366	967	1,031
Net income (loss)	$ 6,702	$ 4,061	$ 1,569	$ (2,927)	$ 1,150
Undistributed earnings (loss)	$ 6,702	$ 4,061	$ 1,569	$ (2,927)	$ 1,150
Undistributed earnings allocable to Series A convertible preferred shares	$	$ 2,513	$ 1,510	$	$
Undistributed earnings allocable to common shares	$ 6,702	$ 1,548	$ 59	$ (2,927)	$ 1,150
Weighted-average common shares outstanding					
Basic	9,068,846	3,512,534	312,500	9,100,111	9,064,537
Diluted	9,068,846	3,512,534	312,500	9,100,111	9,064,537
Undistributed earnings (loss) per common share					
Basic	$ 0.74	$ 0.44	$ 0.19	$ (0.32)	$ 0.13
Diluted	$ 0.74	$ 0.44	$ 0.19	$ (0.32)	$ 0.13
Other Financial Data [1]:					

Adjusted net income	$ 7,455	$ 4,443	$ 1,569	$ 1,919	$ 1,743
Adjusted diluted earnings per common share	$ 0.81	$ 0.48	$ 0.19	$ 0.21	$ 0.19

Table of Contents

(Dollar amounts in thousands)	As of December 31, 2012	2011	2010	As of March 31, 2013	2012 (unaudited)
Balance Sheet Data:					
Current assets	$ 82,077	$ 66,021	$ 50,165	$ 82,272	$ 73,501
Property, plant & equipment, net	7,145	3,611	2,883	7,828	3,710
Total assets	90,765	71,083	55,353	91,473	79,215
Current liabilities	32,664	51,842	43,899	28,441	37,512
Total debt and capital leases (current and long-term portions)	30,942	19,730	29,535	31,945	20,809
Total liabilities	68,031	55,759	49,997	68,205	62,741
Stockholders equity	22,734	15,324	5,356	23,268	16,474

1) The Company believes supplementing its consolidated financial statements presented in accordance with GAAP with non-GAAP measures provides investors with useful information regarding the Company s short-term and long-term trends. Adjusted net income and adjusted diluted earnings per common share are derived from GAAP results by excluding the non-cash impact related to the change in the estimated fair value of the liability associated with the warrants issued in the Company s April 2011 private placement. The Company excludes this non-operating, non-cash impact, as the Company believes it is not indicative of its core operating results or future performance. The warrant revaluation results from facts and circumstances that fluctuate in impact and is excluded by management in its forecast and evaluation of the Company s operational performance. Adjusted net income and adjusted diluted earnings per common share also exclude costs incurred in connection with the Company s relocation of production, warehousing and administrative offices into new facilities. The Company excludes these costs as they, similar to the warrants, are not indicative of the Company s core operating results or future performance and are excluded by management in its forecast and evaluation of the Company s operational performance.

Adjusted net income, adjusted diluted earnings per common share and other non-GAAP financial measures used and presented by the Company may be calculated differently from, and therefore may not be comparable to, similarly titled measures used by other companies. Investors should consider non-GAAP measures in addition to, and not as a substitute for, or as superior to, financial performance measures prepared in accordance with GAAP. The following table presents reconciliations of net income to adjusted net income and diluted earnings per common share to adjusted diluted earnings per common share:

(Dollar amounts in thousands, except per share amounts)	Fiscal Year Ended 2012	2011	2010	Three Months Ended March 31, 2013	2012 (unaudited)
Reconciliation of net income (loss) to adjusted net income:					
Net income (loss)	$ 6,702	$ 4,061	$ 1,569	$ (2,927)	$ 1,150
Non-cash expense from warrant revaluation	448	382		4,846	593
Facility relocation costs, net of tax	305				
Adjusted net income	$ 7,455	$ 4,443	$ 1,569	$ 1,919	$ 1,743
Reconciliation of diluted EPS to adjusted diluted EPS:					
Diluted earnings (loss) per common share	$ 0.74	$ 0.44	$ 0.19	$ (0.32)	$ 0.13
Non-cash expense from warrant revaluation	0.04	0.04		0.53	0.06
Facility relocation costs	0.03				
Adjusted diluted earnings per common share	$ 0.81	$ 0.48	$ 0.19	$ 0.21	$ 0.19

Table of Contents

Management s Discussion and Analysis of

Financial Condition and Results of Operations

The following discussion includes forward-looking statements about our business, financial condition and results of operations, including discussions about management s expectations for our business. These statements represent projections, beliefs and expectations based on current circumstances and conditions and in light of recent events and trends, and you should not construe these statements either as assurances of performance or as promises of a given course of action. Instead, various known and unknown factors are likely to cause our actual performance and management s actions to vary, and the results of these variances may be both material and adverse. A description of material factors known to us that may cause our results to vary, or may cause management to deviate from its current plans and expectations, is set forth under Risk Factors. See Cautionary Note Regarding Forward-Looking Statements. The following discussion should also be read in conjunction with our financial statements, including the notes thereto.

Overview

Organization

We design, manufacture, distribute and support power systems for industrial OEMs across a broad range of industries including stationary electricity power generation, oil and gas, material handling, aerial work platforms, industrial sweepers, arbor, welding, airport ground support, turf, agricultural, construction and irrigation. Our engineering personnel design and test power system solutions and components supporting those solutions. Our major engine suppliers include Perkins/Caterpillar, General Motors and Doosan, and we source components from a variety of domestic and global suppliers. We operate as one business and geographic segment. Accordingly, the following discussion is based upon this presentation.

Net sales

We generate revenues and cash primarily from the sale of off-highway industrial power systems and aftermarket parts to industrial OEMs. Our products are sold globally, and we are a sole source power system provider of our products for many of our customers. Net sales are derived from gross sales less sales returns and or sales discounts.

Cost of sales

We manufacture all of our products at our facilities in Wood Dale, Illinois. The most significant component of our cost of sales is the engine cost. The remainder of our cost of sales primarily includes the cost of additional materials utilized in our finished goods, labor, freight, depreciation and other inventoriable costs such as allocated overhead.

Operating expenses

Operating expenses include research & development and engineering, selling and service and general and administrative expenses. Research & development and engineering expenses include both internal personnel costs and expenses associated with outsourced third party engineering relationships. Research & development and engineering activities are staff intensive; thus costs incurred primarily consist of wages and benefits for professional engineers and amounts paid to third parties under contractual engineering agreements. Research & development and engineering consist of a Product and Application Research and Development Engineering Group and a Customer Support Engineering Group. The primary focus of the Product and Application Research and Development Engineering Group is on current and future product design, prototyping, testing and application development activities. The Customer Support Engineering Group provides dedicated engineering and technical attention to customer production support, including a direct communication link with our internal operations.

Table of Contents

Selling and service expenses represent the costs of our OEM sales team, an aftermarket sales group and a customer support group for field service and warranty support of our products. We utilize a direct sales and marketing approach to maintain maximum customer interface and service support. Wages and benefits, together with expenses associated with travel, account for the majority of the costs in this category.

General and administrative expenses principally represent costs of our corporate office and personnel that provide management, accounting, finance, human resources, information systems and related costs which support the organization. In addition to wages and benefits, costs include professional services, insurance, banking fees and other general facility and administrative support costs.

Other expense

Other expense includes interest expense on our revolving line of credit and other obligations upon which we pay interest, changes in the valuation of the private placement warrants as well as other pre-tax transactions which require classification in other than operating results. The change in the valuation of our private placement warrants is subject to change based upon fluctuations in the market price of our common stock which can vary significantly from period to period.

2012 significant developments

Facility consolidation

During 2012, we exited two of our leased facilities. We consolidated our diesel engine production and a portion of our spark engine production with our primary component parts and aftermarket inventories into a newly leased 261,000 square foot facility. We moved our heavy duty power system production into a separately leased facility with our base engine block production. We converted our owned facility from production to a research and development facility. We capitalized approximately $2.0 million in leasehold improvements associated with the facilities consolidation. Leasehold improvements are amortized over the shorter of the assets useful economic life or the period from the date the assets are placed in service to the end of the lease term including renewal periods that are considered to be reasonably assured of being exercised. In addition, we incurred approximately $509,000 in moving and related costs during 2012 which have been classified as general and administrative expenses in our statement of operations.

Amendment to credit agreement

We completed two amendments to our credit agreement in 2012. On March 20, 2012, our credit agreement was amended to increase the total credit facility from $35.0 million to $50.0 million and to extend the maturity date to March 20, 2017. In addition, this amendment also resulted in a reduction of the LIBOR margin and unused line fee, and under certain circumstances, we are no longer required to report our fixed charge coverage ratio. On November 8, 2012, we amended our credit agreement to (i) increase our acquisition limit up to an aggregate value of $2.0 million; (ii) enter into joint ventures up to an aggregate value of $2.0 million, up from $500,000, and (iii) make annual capital expenditures up to an aggregate of $8.0 million, up from $4.0 million. These thresholds are subject to certain limitations as set forth in the November 8, 2012, amended agreement.

2011 significant developments

Reverse recapitalization, private placement and stock repurchase

On April 29, 2011, Format, Inc. (n/k/a Power Solutions International, Inc.) completed a reverse recapitalization transaction, in which PSI Merger Sub, Inc., a Delaware corporation that was newly-created as a wholly-owned subsidiary of Format, merged with and into The W Group, Inc. and The W Group remained as the surviving corporation of the merger. In that transaction, The W Group became a wholly-owned subsidiary of Power Solutions International, Inc. The reverse recapitalization transaction was consummated under Delaware

Table of Contents

corporate law pursuant to an agreement and plan of merger, dated as of April 29, 2011. Pursuant to this merger agreement, all of the outstanding shares of common stock of The W Group held by the three stockholders of The W Group at the closing of the reverse recapitalization converted into shares of our common stock and shares of preferred stock. In connection with the reverse recapitalization and Gary Winemaster and Thomas Somodi entering into a purchase and sale agreement, (1) The W Group and Mr. Somodi entered into a termination agreement, pursuant to which each of Mr. Somodi s employment agreement with The W Group (the term of which expired in April 2010) and the subscription agreement between The W Group and Mr. Somodi were terminated; and (2) Power Solutions International, Inc. entered into a new employment agreement with Mr. Somodi, which sets forth the terms of Mr. Somodi s employment with us. See Certain Relationships and Related Party Transactions Purchase and Sale Transaction below for a description of the purchase and sale agreement between Mr. Winemaster and Mr. Somodi, and see Executive Compensation Employment Agreements below for a description of the employment agreement with Mr. Somodi. Mr. Somodi subsequently retired from the company in January 2013.

The transaction was accounted for as a reverse recapitalization because, among other reasons: (1) the management of The W Group immediately prior to the reverse recapitalization dominated the management of Power Solutions International, Inc. immediately following the reverse recapitalization (i.e., the Chief Executive Officer, Chief Operating Officer and Chief Financial Officer and the Senior Vice President of Power Solutions International, Inc. were the same individuals who then held those titles with The W Group, Inc.) and (2) immediately prior to the consummation of the reverse recapitalization, Format, Inc. had nominal assets and operations.

Concurrently with the closing of the reverse recapitalization, on April 29, 2011, we completed a private placement of shares of our Series A Convertible Preferred Stock, together with warrants to purchase shares of our common stock, to 29 accredited investors, receiving total gross proceeds of $18.0 million. Each share of preferred stock was convertible into a number of shares of our common stock equal to $1,000 divided by the conversion price then in effect, subject to limitations on conversion set forth in the certificate of designation for the preferred stock. For every one share of our common stock issuable upon conversion of preferred stock purchased in the private placement, each investor in the private placement also received a warrant to purchase one-half of a share of our common stock, at an exercise price of $13.00 per share, as adjusted for the migratory merger and the reverse split, and subject to limitations on exercise and further adjustment as set forth in the warrants.

Concurrently with the closing of the reverse recapitalization, we issued to Roth Capital Partners, LLC, as compensation for its role as placement agent, a warrant. In accordance with its terms, on September 1, 2011, Roth Capital Partners cashlessly exercised in full this warrant. Prior to its exercise in full, this warrant represented the right to purchase an aggregate of 105,000 shares of our common stock, with an exercise price of $13.20 per share, as adjusted for the migratory merger and the reverse split and subject to further adjustment for non-cash dividends, distributions, stock splits or other reorganizations or reclassifications of our common stock. The warrant was not exercisable prior to the effectiveness of the reverse split, and was scheduled to expire on April 29, 2016.

In connection with the reverse recapitalization and the private placement, Format, Inc. entered into a stock repurchase and debt satisfaction agreement, dated as of April 29, 2011, with Ryan Neely, who was the sole director and executive officer of Format, Inc. immediately prior to the closing of the reverse recapitalization, and his wife, Michelle Neely. Pursuant to this agreement, at the time the reverse recapitalization was completed, (1) Format repurchased 93,750 shares (3,000,000 shares without giving effect to the reverse split) of Format common stock from Ryan and Michelle Neely, and (2) Ryan Neely and Michelle Neely terminated all of their interest in, and released Format from all obligations Format had with respect to, the loans made by Ryan Neely and Michelle Neely to Format, Inc. from time to time (which, as of the closing of the transactions contemplated by the stock repurchase and debt satisfaction agreement, were in an aggregate principal amount of $114,156), in exchange for aggregate consideration of $360,000. As part of the stock repurchase agreement, Ryan and Michelle

Table of Contents

Neely also released Format from any other obligations Format owed to them, which included the balance of accrued liabilities on Format s balance sheet of approximately $50,000. The remaining liabilities of Format, which consisted of accounts payable, were settled in connection with but prior to, the consummation of the recapitalization with the available cash on Format s balance sheet, and Format also transferred to Ryan Neely all of its rights and obligations under the real property lease relating to Format s sole office space. In addition, assets, consisting of prepaid expenses, office equipment and furniture, with a net book value of approximately $5,000, were written off.

As a result of the reverse recapitalization transaction, Power Solutions International, Inc. succeeded to the business of The W Group.

Replacement of prior credit agreement

On April 29, 2011, in connection with the closing of the reverse recapitalization, the repurchase of shares of our common stock from Ryan and Michelle Neely and the private placement, Power Solutions International, Inc. and The W Group entered into a loan and security agreement with Harris N.A. (now known as BMO Harris Bank, N.A.), and such loan and security agreement replaced the then existing loan and security agreement that The W Group had with its senior lender prior to the closing of the reverse recapitalization. Pursuant to the loan and security agreement with Harris N.A., among other things, Power Solutions International, Inc. became a party to the loan and security agreement, the maximum loan amount under the senior credit facility was reduced from the maximum loan amount under The W Group s prior credit facility to reflect The W Group s repayment in full of its two previously outstanding term loans under the prior credit facility and the financial covenants under the prior credit facility were replaced with a new fixed charge coverage ratio. See Liquidity and capital resources Credit agreement below for a discussion of our current credit facility and The W Group s prior credit facility, which was replaced by the current credit facility in connection with the reverse recapitalization.

Reverse split and migratory merger

In connection with, and prior to the consummation of, the reverse recapitalization, the board of directors of Format approved the reverse split and the migratory merger. On August 25, 2011, we held a special meeting of our stockholders at which our stockholders approved the reverse split, the migratory merger and related matters. On August 26, 2011, Power Solutions International, Inc., a Nevada corporation, merged with and into its wholly owned subsidiary, Power Solutions International, Inc., a Delaware corporation, pursuant to an agreement and plan of merger between Power Solutions International, Inc., a Delaware corporation, and Power Solutions International, Inc., a Nevada corporation. Power Solutions International, Inc., a Delaware corporation, continued as the surviving entity of the migratory merger. Pursuant to the migratory merger, we changed our state of incorporation from Nevada to Delaware and each 32 shares of our common stock converted into one share of common stock of the surviving entity in the migratory merger, thereby effecting a 1-for-32 reverse stock split of our common stock. Upon the consummation of the migratory merger (including the reverse split of our common stock effected thereby), the 113,960.90289 then-issued and outstanding shares of preferred stock automatically converted into an aggregate of 9,496,753 shares of our common stock. The consolidated financial statements included in this report have been restated to retroactively reflect the reverse split in accordance with SEC Staff Accounting Bulletin 4C *Equity Accounts Change in Capital Structure* and ASC 260 *Earnings Per Share* (ASC 260). The conversion of shares of preferred stock to common stock has been presented prospectively in our financial statements, effective with the reporting periods as of, and for the three and nine months ended, September 30, 2011, in accordance with ASC 260. See Note 13 to the Consolidated Financial Statements, Stockholders equity , for additional information regarding the financial statement impact of the reverse split and migratory merger.

Further, in connection with the private placement, each of our current stockholders who was a stockholder of The W Group and who received shares pursuant to the reverse recapitalization or received, as a gift, stock from the stockholders of The W Group, entered into a voting agreement, pursuant to which such person agreed to

Table of Contents

vote his shares of our common stock and preferred stock, as applicable, in favor of the reverse split and the migratory merger. The persons who entered into the voting agreements held, in the aggregate, a substantial majority of the voting securities of our company. Accordingly, approval of the reverse split and the migratory merger was probable. Pursuant to the terms of the voting agreements, at the special meeting of our stockholders held on August 25, 2011, each of the individuals subject to a voting agreement voted all of his shares of our common stock and preferred stock to approve the migratory merger and related matters.

Stock purchase agreement with management stockholder

The company and Gary S. Winemaster, the company s Chief Executive Officer and President, and a member of the Board of Directors of the company, entered into a Stock Purchase Agreement, pursuant to which, on October 31, 2011, we purchased from Mr. Winemaster 830,925 shares of company common stock for $4.25 million, or $5.11 per share. These shares were returned to our treasury as authorized and issued, but not outstanding, shares of common stock of the company. For additional detail regarding the stock purchase agreement between Mr. Winemaster and the company, see Certain Relationships and Related Party Transactions Purchase and Sale Transaction below.

Factors affecting comparability

We have set forth below selected factors that we believe have had, or can be expected to have, a significant effect on the comparability of recent or future results of operations:

Public company expenses

As a result of the reverse recapitalization, we are now a public company. As a result, our general and administrative expenses have increased as we pay our employees, legal counsel and accountants to assist us in, among other things, establishing and maintaining a more comprehensive compliance and board governance function, establishing and maintaining internal control over financial reporting in accordance with Section 404 of the Sarbanes-Oxley Act, and preparing and distributing periodic public reports under the federal securities laws. In addition, as a public company the cost of director and officer liability insurance has increased. We have also incurred additional costs associated with compensation of non-employee directors.

Private placement warrants

Our period comparisons can be impacted by our private placement warrant liability. The change in estimated fair value of the liability associated with the private placement warrants is primarily attributable to fluctuations in the value of our common stock during a period.

Stock-based and other executive compensation

Prior to 2012, we had not granted or issued any stock-based compensation. Accordingly, we had not recognized any stock-based compensation expense. During 2012, our Compensation Committee of the Board of Directors approved, and we granted a Stock Appreciation Rights Award Agreement. As a result, we have incurred non-cash, stock-based compensation expense in 2012 that did not occur in 2011. We may consider making additional awards to our directors, officers and other employees and possibly to consultants and, if we do, we will incur additional non-cash, stock-based compensation expenses in future periods.

Events affecting sales and profitability comparisons

Our profitability comparisons (including our sales, gross profit and net income) and cash flows can be impacted by a variety of internal and external events associated with our business operations. Examples of such events include (1) changes in regulatory emission requirements (which generally occur on January 1 of the year

Table of Contents

in which they become effective), (2) customer product phase-in/phase-out programs, (3) supplier product (e.g., a specific engine model) phase-in/phase-out programs, (4) changes in pricing by suppliers to us of engines, components and other parts (typically effective January 1 of any year), and (5) changes in our pricing to our customers (typically effective January 1 of any year), which may be related to changes in the pricing by suppliers to us. In order to mitigate potential availability or pricing issues, customers may adjust their demand requirements from traditional patterns. We may also extend special programs to customers in advance of such events, and we are more likely to offer such programs in our fourth quarter of a year in anticipation of events expected to occur in the first quarter of the next year. The occurrence of any of the events discussed above may result in fluctuations in our operating results (including sales and profitability) and cash flows between and among reporting periods.

Results of operations

Three months ended March 31, 2013 compared with the three months ended March 31, 2012

Net sales

Our net sales increased $4,504,000 (9.4%) to $52,576,000 for the three months ended March 31, 2013, compared to $48,072,000 in the three months ended March 31, 2012, of which an increase in sales volume (as opposed to price increases) accounted for approximately $3,789,000 of the year over year increase. Our power systems and related sales increased approximately $3,688,000 and parts sales accounted for the remaining $816,000 increase. The sales increase was primarily due to growth in power generation sales aided by increased demand for our larger power systems. Our sales in the three months ended March 31, 2013, also includes $284,000 arising from grant revenue recognized in connection with certain engine certification and engine application activities.

Gross profit

Our gross profit increased $940,000 (11.4%) to $9,169,000 for the three months ended March 31, 2013, from $8,229,000 in the three months ended March 31, 2012. Our gross profit increased primarily due to the previously discussed increase in sales. Gross margin was substantially unchanged at 17.4% for the three months ended March 31, 2013, compared to 17.1% for the same period in 2012.

Research & development and engineering

Research & development and engineering expense increased $44,000 (2.5%) to $1,771,000 for the three months ended March 31, 2013, as compared to $1,727,000 for the same period in 2012. Research & development and engineering activities are staff intensive, and we incur significant expenses connected with our professional engineers and amounts paid to third parties for contract services associated with our research and development activities. Compensation and benefits increased $179,000 in the three months ended March 31, 2013 as compared to the same period in 2012 as we added staff to support product development activities. Partially offsetting this increase were decreases in other expense categories, none of which was individually significant. As a percentage of net sales, research & development and engineering expenses decreased to 3.4% for the three months ended March 31, 2013, compared to 3.6% for the same period in 2012.

Selling and service expense

Selling and service expenses increased $178,000 (10.5%) to $1,880,000 for the three months ended March 31, 2013, from $1,702,000 in the three months ended March 31, 2012. Expenses increased across multiple categories, but the increase was generally due to additional promotional activities and an increase in wages and benefits As a percentage of net sales, selling and service expenses was substantially unchanged at 3.6% for the three months ended March 31, 2013 as compared to 3.5% for the same period in 2012.

Table of Contents

General and administrative expense

General and administrative expenses increased $674,000 (38.2%) to $2,438,000 for the three months ended March 31, 2013, from $1,764,000 for the three months ended March 31, 2012. Wages and benefits increased $460,000, which was primarily due to compensation expense associated with new senior staff to support public company requirements and other increases in our administrative headcount. The remaining net increase of $214,000 occurred across almost all other expense categories, none of which was individually significant. As a percentage of net sales, general and administrative expenses increased to 4.6% in the three months ended March 31, 2013, from 3.7% for the same period in 2012.

Other expense

Interest expense decreased $33,000 (14.5%) to $194,000 for the three months ended March 31, 2013, as compared to $227,000 for the same period in 2012. The decrease in interest expense was attributable to a decrease in the weighted average borrowing rate on our bank debt from 2.57% in 2012 to 2.17% in 2013 and a decrease in bank loan fees accounted for as interest expense year over year. Holding all other variables constant, we believe that for the full year of 2013 our effective interest will slightly decrease from 2012.

Other expense, net increased $4,218,000 to $4,846,000 for the three months ended March 31, 2013 as compared to $628,000 in the three months ended March 31, 2012. The increase was attributable to a change in the estimated fair value of our private placement warrants resulting in an expense of $4,846,000 in the three months ended March 31, 2013 as compared to $593,000 for the same period in 2012. The change in estimated fair value of the private placement warrants was primarily attributable to an increase in the trading price of our common stock during the period.

Income tax expense

Our income tax expense decreased $64,000 to $967,000 in the three months ended March 31, 2013, as compared to $1,031,000 for the same period in 2012. Our income tax expense for the three months ended March 31, 2013, included $100,000 for the benefit of the federal research tax credit expected to be realized for the year ended December 31, 2012. Such amount was recorded in the first quarter of 2013 and not during 2012 because the enactment of the legislation providing the federal research tax credits for 2012 was not signed into law until January 2, 2013, and generally accepted accounting principles prohibit retroactive application of tax law changes. We have estimated an interim effective income tax rate of 37% for 2013, excluding, (i) the 2012 federal research tax credit, and (ii) the impact of any change in the valuation of the private placement warrants. The change in the valuation of our private placement warrants is a non-taxable transaction. Given the subjectivity and volatility of the valuation of the private placement warrants, we are unable to estimate the annual impact of the change in the private placement warrants and the corresponding effect on our effective tax rate for the full year. Accordingly, we include the effect of the change in the valuation of the private placement warrants, when known, in the period in which it occurs. Due to the significance of the change in the valuation of the private placement warrants on income which resulted in a pre-tax loss for financial statement purposes and its exclusion from the computation of income taxes, the actual income tax rate for the three months ended March 31, 2013, is not a meaningful calculation.

Our income tax rate for the three months ended March 31, 2012 was 47.3% after taking into account the non-deductibility of the expense associated with the private placement warrants recognized in the three months ended March 31, 2012. Excluding the impact of the expense associated with the private placement warrants, our effective income tax rate was 36.2% in the three months ended March 31, 2012.

Year ended December 31, 2012 compared with the year ended December 31, 2011

Net sales

Our net sales increased $47,373,000 (30.6%) to $202,342,000 for the year ended December 31, 2012, compared to $154,969,000 for the year ended December 31, 2011, of which an increase in sales volume (as opposed to price increases) accounted for approximately $43.9 million of the year over year increase.

Table of Contents

Our power systems and related sales increased approximately $45.1 million and parts sales accounted for the remaining $2.3 million increase. The sales increase occurred across all power systems product categories. In addition, the sales increase also increased across a majority of our customer base.

Gross profit

Our gross profit increased $7,489,000 (28.3%) to $33,917,000 for the year ended December 31, 2012, from $26,428,000 in the year ended December 31, 2011. Our gross profit increased primarily due to the previously discussed increase in sales volume. As a percentage of net sales, gross margin was 16.8% for the year ended December 31, 2012, compared to 17.1% in 2011. The lower gross margin during 2012 was principally attributable to an increase in materials costs in excess of price increases.

Research & development and engineering

Research & development and engineering expense increased $2,664,000 (56.5%) to $7,377,000 for the year ended December 31, 2012, as compared to $4,713,000 in 2011, due to an increase in customer product support activities associated with the increase in sales and product development. Research & development and engineering activities are staff intensive; thus, costs incurred primarily consist of salary and benefits for professional engineers and amounts paid to third parties for contract services associated with our research and development activities. Compensation and benefits increased $1,170,000 as we increased headcount to support our production development and engineering applications with respect to new and existing products, including efforts to build proprietary engines. Materials used in connection with these activities also increased $1,289,000 from 2011. The remaining $205,000 increase was attributable to other research & development and engineering expenses, none of which was individually significant. As a percentage of net sales, research & development and engineering expenses increased to 3.6% for the year ended December 31, 2012, compared to 3.0% for 2011.

Selling and service expense

Selling and service expenses decreased $741,000 (11.1%) to $5,925,000 for the year ended December 31, 2012, from $6,666,000 in 2011. Warranty expense decreased $497,000 as we realized lower than expected claims for the covered periods. The remaining $244,000 decrease was attributable to various fluctuations in other expense categories, none of which was individually significant. As a percentage of net sales, selling and service expenses decreased to 2.9% in 2012 compared to 4.3% in 2011.

General and administrative expense

General and administrative expenses increased $3,055,000 (58.3%) to $8,299,000 for the year ended December 31, 2012, from $5,244,000 in 2011. Wages and benefits increased $1,462,000 and was primarily due to wages and benefits of our new Chief Operating Officer hired in 2012 and the transition of our prior Chief Operating Officer who subsequently retired in early 2013. We also incurred $509,000 of costs to consolidate our facilities to accommodate our sales growth. Public company and consulting expenses increased $544,000 principally due to a full year operating as a public company. Other general and administrative expenses increased $540,000, none of which was individually significant. As a percentage of net sales, general and administrative expenses increased to 4.1% in the twelve months ended December 31, 2012, from 3.4% in 2011.

Other (income) expense

Interest expense decreased $317,000 (23.7%) to $1,023,000 for the year ended December 31, 2012, as compared to $1,340,000 for the year ended December 31, 2011. The decrease in interest expense was attributable to a decrease in the weighted average borrowing rate on our bank debt from 4.11% in 2011 to 2.41% in 2012 and a decrease in bank loan fees accounted for as interest expense year over year. These decreases were partially offset by additional interest incurred due to a $5.0 million increase in average outstanding bank borrowings principally arising from an increase in working capital requirements in support of our higher level of sales activity in 2012 over 2011.

Table of Contents

We recognized a loss on debt extinguishment of $485,000 in the year ended December 31, 2011, due to the write off of unamortized loan fees associated with our prior credit facility. The remaining unamortized loan fees were required to be expensed when we refinanced our prior credit facility with a new lender and repaid the balances outstanding under our prior credit agreement. See *Liquidity and capital resources credit agreement* below for a further discussion regarding the refinancing of our prior credit facility.

Also, other expense, net was $448,000 for the year ended December 31, 2012, as compared to $1,146,000 for the same period in 2011. Other expense in 2012 consisted entirely of the change in the valuation of our private placement warrants. Other expense in 2011, included $762,000 of non-capitalizable transaction costs incurred in connection with the issuance of the warrants in the $18.0 million private placement. The expense also includes $382,000 related to the increase in the liability of the estimated value of private placement warrants for the year ended December 31, 2011. See *Reverse recapitalization, private placement and stock repurchase* for further discussion of these costs.

Income tax expense

Our income tax expense increased $1,370,000 to $4,143,000, as compared to $2,773,000 in 2011. Our effective income tax rate for the year ended December 31, 2012, was 38.2% as compared with 40.6% for the prior year. Our income tax expense for the year ended December 31, 2012, increased principally due to the higher taxable income realized in 2012 as compared with 2011. In addition, our income tax expense does not include the benefit of any federal research tax credits expected to be realized for the year ended December 31, 2012, because the enactment of the legislation providing the federal research tax credits for 2012 was not signed into law until January 2, 2013, and generally accepted accounting principles prohibit retroactive application of tax law changes. The federal research tax credit included in our 2011 federal income tax provision was $240,000.

Our income tax rate for the year ended December 31, 2012, decreased due to a lower effective state rate as compared to 2011, which was principally attributable to estimated state tax credits. In addition, the 2011, estimated tax rate was adversely impacted by non-deductible expenses associated with certain transaction costs incurred in connection with the reverse recapitalization. See *Reverse recapitalization, private placement and stock repurchase* for further discussion of these transactions.

Year ended December 31, 2011 compared with the year ended December 31, 2010

Net sales

Our net sales increased $54,448,000 (54.2%) to $154,969,000 for the year ended December 31, 2011, compared to $100,521,000 for the year ended December 31, 2010, of which an increase in sales volume (as opposed to price increases) accounted for approximately $49.2 million of the year over year increase.

Our alternative fuel power systems sales increased $47.3 million, and parts sales accounted for the remaining $7.1 million increase. The sales increase was driven by (i) a full year of power system sales to Asia-based customers, which accounted for $14.6 million of the increase in sales; (ii) a $6.4 million increase in sales of our alternative fuel large power systems introduced in late 2009 and (iii) sales to new customers and general increase in demand from existing customers.

Gross profit

Our gross profit increased $9,801,000 (58.9%) to $26,428,000 for the year ended December 31, 2011, from $16,627,000 in the year ended December 31, 2010. Our gross profit increased primarily due to the previously discussed increase in sales volume. As a percentage of net sales, gross margin was 17.1% for the year ended December 31, 2011, compared to 16.5% in 2010. The higher gross profit during the year 2011 was principally attributable to the broadened product mix and higher sales volume relative to production costs. Production costs

Table of Contents

were spread over higher volumes which favorably affected gross margin. In addition, the increase in sales, noted in *Net sales* above, occurred across the majority of our customer base, broadening our product mix, which also favorably impacted our gross margin.

Research & development and engineering

Research & development and engineering expense increased $867,000 (22.5%) to $4,713,000 for the year ended December 31, 2011, as compared to $3,846,000 in 2010 due to an increase in customer product support activities associated with the increase in sales and product development. Compensation and benefits increased $997,000, as we increased headcount to support the research & development and engineering of new power systems, including the design and development of an 8.8 liter engine to meet anticipated customer requirements. This increase was partially offset by a $184,000 decrease in emission certification fee expense. The remaining increase was attributable to other research & development and engineering expenses, none of which was individually significant. As a percentage of net sales, research & development and engineering expenses decreased to 3.0% for the year ended December 31, 2011, compared to 3.8% for 2010. The decrease in the research & development and engineering costs as a percentage of net sales was due to the leveraging of these costs against higher sales volumes.

Selling and service expense

Selling and service expenses increased $1,201,000 (22.0%) to $6,666,000 for the year ended December 31, 2011, from $5,465,000 in 2010. Compensation, benefits and commissions costs increased $308,000 and warranty costs increased $482,000, both as a result of our increased product sales for the year ended December 31, 2011, as compared to 2010. The remaining increase was attributable to increases in other expense categories, none of which was individually significant. As a percentage of net sales, selling and service expenses decreased to 4.3% in 2011, compared to 5.4% in 2010, as we effectively increased sales with our existing sales infrastructure.

General and administrative expense

General and administrative expenses increased $1,994,000 (61.4%) to $5,244,000 for the year ended December 31, 2011, from $3,250,000 in 2010. The increase was principally attributable to (i) a $942,000 increase in professional, consulting, and bank fees incurred in connection with our year end audit, reverse recapitalization and the refinancing of our credit facility in April 2011, (ii) $606,000 for the cost of additional staff positions to support both our higher sales volume and public company responsibilities, and (iii) $347,000 of public company costs. As a percentage of net sales, general and administrative expenses increased to 3.4% in the twelve months ended December 31, 2011, from 3.2% in 2010.

Other (income) expense

Interest expense decreased $791,000 (37.1%) to $1,340,000 for the year ended December 31, 2011, as compared to $2,131,000 for the year ended December 31, 2010. Our average outstanding bank borrowings were $6.8 million lower for the year ended December 31, 2011, compared to the year ended December 31, 2010. This decrease was attributable to the payoff of our bank term debt and a reduction in our outstanding revolving line of credit from the proceeds received in the private placement. In addition, the weighted average borrowing rate on our bank debt decreased from 5.82% during the year ended December 31, 2010 to 4.11% for the year ended December 31, 2011.

We recognized a loss on debt extinguishment of $485,000 in the year ended December 31, 2011, due to the write off of unamortized loan fees associated with our prior credit facility.

Also, other expense, net was $1,146,000 for the year ended December 31, 2011, with no similar balance in the same period in 2010. This amount included $762,000 of non-capitalizable transaction costs incurred in

Table of Contents

connection with the issuance of the warrants in the $18.0 million private placement. The expense also included $382,000 related to the increase in the liability of the estimated value of the private placement warrants for the year ended December 31, 2011. See *Reverse recapitalization, private placement and stock repurchase* for further discussion of these costs.

Income tax expense

Our income tax expense increased $2,407,000 to $2,773,000, as compared to $366,000 in 2010. Our effective tax rate for the year ended December 31, 2011, was 40.6% as compared with 18.9% for the prior year. Our income tax expense for the year ended December 31, 2011, reflected the impact of non-deductible expenses associated with certain transactions costs incurred in connection with the reverse recapitalization and issuance of the private placement warrants. See *Reverse recapitalization, private placement and stock repurchase* for further discussion of these transactions. The increase in our effective tax rate in 2011, as compared to 2010, was also impacted by the extent to which research tax credits offset our income tax provision. Our taxable income and corresponding provision for the year ended December 31, 2011, increased over 2010 by more than the increase in offsetting research tax credits, which resulted in an increase in our effective tax rate. In addition, the combined corporate state income and replacement tax for Illinois increased from 7.3% in 2010 to 9.5% in 2011, which also adversely impacted our effective tax rate.

Liquidity and capital resources

Our cash requirements are dependent upon a variety of factors, foremost of which is the execution of our strategic plan. We expect to continue to devote substantial capital resources to running our business. Our primary sources of liquidity are cash flows from operations, principally collections of customer accounts receivable and borrowing capacity under our credit facility. Prior to the amendment of our credit facility with BMO Harris Bank N.A. (formerly Harris N.A.) on March 20, 2012, our existing and historical financing arrangements required that cash received by us be applied against our revolving line of credit. Accordingly, we typically did not maintain cash or cash equivalents on our consolidated balance sheet. As a result of the amendment to our credit facility with BMO Harris Bank N.A., our cash balances are no longer automatically swept by BMO Harris Bank N.A. and, as a result, from time to time, we may carry cash balances on our consolidated balance sheet.

Based on our current forecasts and assumptions, we believe that our sources of cash, namely the sales of our power systems and aftermarket products and access to borrowings on our existing or future credit facilities will be sufficient to meet our anticipated cash needs for working capital and capital expenditures over at least the next twelve months. Although we believe our existing sources of liquidity will also be sufficient on a longer-term basis, that will depend on numerous factors, including the following: the continuation of our existing customer relationships and our development of new customer relationships; market acceptance of our existing and future products; the success of our product development and commercialization efforts and the costs associated with those efforts; and the costs associated with any future acquisitions, joint ventures or other strategic transactions. Accordingly, in the future we may pursue various financing alternatives, including a larger credit facility, other debt financing and/or equity financing.

As of March 31, 2013, we had working capital of $53,831,000 compared to $49,413,000 as of December 31, 2012. Our working capital increase of $4,418,000 was primarily attributable to a $4,472,000 reduction in our accounts payable balance since December 31, 2012, principally resulting from payments of trade obligations. We also realized fluctuations in other working capital accounts, the net changes of which were not significant. From December 31, 2012 to March 31, 2013, our inventories increased $1,578,000, but this increase was partially offset by a $793,000 decrease in our accounts receivable, net and a $342,000 decrease in prepaid expenses and other current assets. The decrease in accounts receivable, net was due principally to collections on accounts in excess of the increase in sales during the period. Our income taxes payable increased $914,000 from December 31, 2012, to March 31, 2013, primarily due to the timing of the payment of our income tax liability for the first quarter of 2013 which was not due until April 15, 2013. Changes in the remaining components of working capital totaled $417,000, none of which was individually significant.

Table of Contents

Our December 31, 2012 working capital of $49,413,000 represented an increase of $35,234,000 compared to $14,179,000 as of December 31, 2011. This increase of $35,234,000 was primarily attributable to the reclassification of our revolving line of credit to long-term obligations at December 31, 2012, from current liabilities as of December 31, 2011. This reclassification of our revolving line of credit accounted for $19,666,000 of the increase in working capital year over year. The reclassification of our revolving line of credit to long-term obligations resulted from an amendment to our revolving line of credit effective March 20, 2012 as further described below under Credit agreement. Increases in accounts receivable and inventories also contributed to the increase in our working capital from December 31, 2011 to December 31, 2012. Accounts receivable increased $7,957,000 from December 31, 2011, to December 31, 2012, due principally to an increase in sales. Specifically, our sales in 2012 were $47,373,000 higher as compared to December 31, 2011. Inventories increased $6,575,000 from December 31, 2011, to 2012 to support our higher sales volumes. Changes in the remaining components of working capital year over year totaled $1,036,000, none of which was individually significant.

A limited number of our customers have payment terms which may extend up to 150 days. As of March 31, 2013, December 31, 2012, and December 31, 2011, our trade receivables included $9.2 million, $7.3 million and $3.0 million, respectively, of trade receivables which represented aggregate customer account balances subject to these terms. Of these amounts, $5.4 million, $3.3 million and $0.7 million as of March 31, 2013, December 31, 2012, and December 31, 2011, respectively, represented the portion of the balance outstanding with these extended trade terms. Under our revolving line of credit which funds our working capital as needed, these receivables represent eligible collateral on the same basis as our other trade receivables and remain eligible as collateral upon which we may borrow up to their extended due date of 150 days.

Cash flows for the three months ended March 31, 2013

Operating activities

For the three months ended March 31, 2013, we used $2,381,000 to fund our operations. We had a net loss of $2,927,000 which was offset by non-cash adjustments totaling $5,401,000, resulting in cash generated of $2,474,000 before considering changes in our operating assets and liabilities. Our non-cash adjustments included an expense of $4,846,000 arising from a change in the valuation of our private placement warrants during the three months ended March 31, 2013. Other non-cash adjustments also included depreciation and amortization expense of $364,000, expenses associated with stock appreciation rights of $207,000 and a $16,000 decrease in our accounts receivable allowances.

Operating assets and liabilities used $4,855,000 in the three months ended March 31, 2013. We used $4,852,000 of cash to pay trade accounts payable during the three months ended March 31, 2013, and we also increased our inventory by $1,578,000 during this same period, as we built up our inventory to support current and future period sales. Partially offsetting the cash used was cash generated by an $809,000 decrease in our accounts receivable arising from collections in excess of our sales activity for the three months ended March 31, 2013. Our cash from operations also increased $914,000 arising from an increase in our income tax liability which was not yet paid as of March 31, 2013, as the obligation was not due until April 15, 2013. Changes in the other components of operating activities netted to cash used of $148,000, none of which was individually significant.

Investing activities

Net cash used in investing activities was $667,000 in the three months ended March 31, 2013, which was and related to the acquisition of property and equipment.

Table of Contents

Financing activities

We generated approximately $2,800,000 of cash from financing activities for the three months ended March 31, 2013. We generated $1,797,000 of cash from the exercise of private placement warrants by our investors. We also generated $1,003,000 of cash from net borrowings on our revolving line of credit.

Cash flows for the three months ended March 31, 2012

Operating activities

For the three months ended March 31, 2012, we generated $3.3 million from our operations. We generated cash flow from net income of $1.2 million including $0.6 million in non-cash adjustments, which primarily consisted of an increase in the liability associated with the valuation of private placement warrants and depreciation and amortization net of our deferred income tax benefit.

We generated cash from an $8.1 million increase in accounts payable arising from the timing of purchases from, and payments to, our vendors. We generated cash of $1.9 million from a decrease in our accounts receivable due to the receipt of cash from our customers in excess of our sales activity in the three months ended March 31, 2012, and we generated $1.2 million from an increase in our income tax liability for which payment was due subsequent to March 31, 2012. These increases to cash generated by operations were offset by an $8.8 million increase in our inventories as we elected to take significant positions in certain engines in connection with our sales activities, and we also increased our component purchases in support of our sales activities for 2012. We also had other net cash uses of $0.3 million, none of which were individually significant.

Investing activities

Net cash used in investing activities was $0.3 million for the three months ended March 31, 2012 related primarily to the acquisition of property and equipment.

Financing activities

We used $2.8 million for financing activities for the three months ended March 31, 2012. Our cash overdraft balance decreased $3.8 million from December 31, 2011 to March 31, 2012, which was principally attributable to the timing of payments to vendors. We also incurred $0.1 million in financing fees associated with an amendment to our existing credit facility, which is discussed below under Credit Agreement. These uses of cash were partially offset by a $1.1 million increase in net borrowings under our revolving line of credit from December 31, 2011 to March 31, 2012.

Cash flows for the year ended December 31, 2012

Operating activities

For the year ended December 31, 2012, we used $2,941,000 to fund our operations. We generated cash flow from net income of $6,702,000 plus $1,426,000 in net non-cash adjustments principally from depreciation and amortization, equity-based compensation expense, and an increase in the liability associated with the valuation of private placement warrants.

We generated cash from a $2,473,000 increase in accounts payable arising from the timing of payments to vendors and a $924,000 increase in accrued liabilities. These increases in cash were offset by a $7,957,000 increase in accounts receivable due to an increase in our sales volume for which we had not yet collected the cash and a $6,575,000 increase in inventories purchased to support the sales activity. We also had other net cash generated of $66,000, none of which was individually significant.

Table of Contents

Investing activities

Net cash used in investing activities of $3,898,000 for the year ended December 31, 2012, related primarily to the purchase of property, equipment and other assets.

Financing activities

We generated $7,382,000 of cash from financing activities for the year ended December 31, 2012. Of this net amount $11,276,000 was generated from an increase in borrowings on our revolving line of credit. This amount was partially offset by a $3,780,000 decrease in the cash overdraft balance. Prior to the amendment of our credit facility with BMO Harris Bank N.A. on March 20, 2012, our credit facility agreement required that our cash be applied against our revolving line of credit. As such, we did not maintain a cash balance, and we borrowed on the revolving line of credit to fund outstanding checks as they cleared our bank. Our cash overdrafts fluctuated based on the timing of checks issued which had not yet cleared our bank as of a given date. Other financing activities used cash of $114,000, none of which was individually significant.

Cash flows for the year ended December 31, 2011

Operating activities

For the year ended December 31, 2011, we used $973,000 to fund our operations. We generated cash flow from net income of $4,061,000 plus $574,000 in non-cash adjustments, principally depreciation, loss on debt extinguishment and an increase in the liability associated with the valuation of private placement warrants.

We also generated cash from a $7,365,000 increase in accounts payable arising from the timing of purchases from vendors and a $1,609,000 increase in accrued liabilities arising from incremental costs to support the higher level of sales activities. These increases in cash were offset by a $12,992,000 increase in accounts receivable due to an increase in our sales volume for which we had not yet collected the cash and a $1,225,000 increase in inventories purchased to support the sales activity. We also had other net cash uses of $365,000, none of which was individually significant.

Investing activities

Net cash used in investing activities of $1,570,000 for the year ended December 31, 2011, related primarily to the acquisition of property, equipment and other assets.

Financing activities

We generated $2,543,000 of cash from financing activities for the year ended December 31, 2011. In connection with the private placement for which we issued preferred stock and warrants to purchase our common stock, we generated gross proceeds of $18.0 million. In addition, in 2011 we refinanced our revolving line of credit with a new bank, Harris, N.A. (now known as BMO Harris Bank N.A.) under which our initial proceeds from borrowings were $18,338,000. The terms of the revolving line of credit with BMO Harris Bank N.A. are discussed below under *Credit agreement*. The proceeds from the private placement and revolving line of credit were used to pay off our existing term loans and our revolving line of credit with our prior lender, Fifth Third Bank. We used $21,633,000 in cash to payoff of the prior revolving line of credit and $7,880,000 in cash to pay off other scheduled debt payments. We used $4,654,000 million of cash to pay transaction and financing costs associated with the private placement and refinancing of our revolving line of credit.

We also had a $3,251,000 increase in our cash overdraft balance as of December 31, 2011, over December 31, 2010, which offset the cash used. In addition, $1,328,000 in cash was provided by net borrowings for the year ended December 31, 2011, under our current revolving line of credit. Offsetting these increases was $4.25 million used to repurchase shares of our common stock. Other financing activities generated $43,000 of cash, none of which was individually significant.

Table of Contents

Cash flows for the year ended December 31, 2010

Operating activities

For the year ended December 31, 2010, we generated cash flows from operations of $3,924,000, of which $2,644,000 arose from net income and other non-cash items of depreciation and receivable allowances, as compared to $3,289,000 in 2009.

We also realized a reduction in our working capital during the year, which contributed to the cash generated from operations, primarily arising from a $12,012,000 reduction in accounts receivable that was partially offset by a $9,255,000 reduction in accounts payable and a $1,001,000 increase in our inventories. The decrease in accounts receivable and accounts payable primarily arose from a high level of sales activity occurring in the fourth quarter of 2009, which resulted in both an increase in receivables from those sales and related payables from the purchase of inventories to support those sales. We collected the receivables and paid the corresponding payables in the first quarter of 2010. The $12,012,000 change in accounts receivable also includes an increase of $1.1 million due from customers with payment terms of up to 150 days to $2.7 million from $1.6 million as of December 31, 2009, due to an increase in shipments to these customers in 2010.

Investing activities

Net cash used in investing activities of $583,000 in the year ended December 31, 2010, related primarily to the acquisition of fixed assets. Fixed asset expenditures principally arose from the purchase of tooling and transportation equipment.

Financing activities

During 2010, our financing activities included scheduled payments of $2,226,000 of bank term debt, capital lease obligations and other notes payable. Our overall revolving line of credit decreased $776,000 principally arising from the cash flows generated from operations. We also used $314,000 of cash during the year for the payment of financing fees in connection with the reverse recapitalization and private placement. We also had $120,000 decrease in cash overdrafts. At December 31, 2010, we were not in compliance with certain of our bank covenants, including our senior debt leverage and our fixed charge coverage ratios. On January 20, 2011, we obtained a waiver from our bank for these events of non-compliance. Subsequent to December 31, 2010, we completed a reverse recapitalization and private placement offering on April 29, 2011, which resulted in the repayment in full of our remaining term debt, and we also refinanced our existing revolving line of credit with another bank.

Credit agreement

In connection with the consummation of the reverse recapitalization and the private placement, on April 29, 2011, we entered into a loan and security agreement with certain lenders and BMO Harris Bank N.A. (formerly known as Harris N.A.), as agent for the lenders, and such agreement has been amended since inception as discussed below. That credit agreement replaced the loan and security agreement with Fifth Third Bank, the terms of which are discussed below.

Prior to the amendment of our credit facility with BMO Harris Bank N.A., as discussed below, our credit agreement provided for borrowings of up to $35.0 million under a revolving line of credit, which revolving line of credit was scheduled to mature on April 29, 2014 and had a variable interest rate as described below. Borrowings under our credit agreement are collateralized by substantially all of our assets. Under our credit agreement, we are required to meet certain financial covenants, including a minimum monthly fixed charge coverage ratio of not less than 1.1 to 1.0 and a limitation on annual capital expenditures, the testing of which commenced on April 30, 2011.

Table of Contents

Our credit agreement also contains customary covenants and restrictions applicable to us, including agreements to provide financial information, comply with laws, pay taxes and maintain insurance, restrictions on the incurrence of certain indebtedness, guarantees and liens, restrictions on mergers, acquisitions and certain dispositions of assets, and restrictions on the payment of dividends and distributions. In addition, our credit agreement requires our cash accounts to be held with BMO Harris Bank N.A. Prior to the March 20, 2012 amendment of the credit facility, our cash deposits in the new revolving line of credit account were swept by BMO Harris Bank N.A. daily and applied against the outstanding balance on our new revolving line of credit. As a result, we maintained a zero cash balance in our bank deposit account, and we borrowed on the revolving line of credit on a daily basis to fund our cash disbursements.

Except as modified and discussed under the amended credit agreement with BMO Harris Bank N.A. below, under our credit agreement (in contrast to the prior credit agreement discussed below): (a) Power Solutions International, Inc. is a party to the new credit agreement and pledged the equity interests of The W Group to BMO Harris Bank N.A.; (b) there are no term loans; (c) the new revolving line of credit bears interest at BMO Harris Bank N.A. s prime rate (3.25% at March 31, 2013) plus an applicable margin ranging from 0% to 0.50% or, at our option, a portion of the new revolving line of credit can be designated to bear interest at LIBOR plus an applicable margin ranging from 2.00% to 2.50%; (d) there is a higher limit on annual capital expenditures; (e) there is no maximum quarterly senior debt leverage ratio; and (f) there is a fixed charge coverage ratio similar to the fixed charge coverage ratio in the prior credit agreement with Fifth Third Bank, except that the fixed charge coverage ratio under the new credit agreement excludes historical debt service on Term Loan A and Term Loan B (each as defined and discussed below) and certain other one-time expenses.

On March 20, 2012, the credit agreement with BMO Harris Bank N.A was amended to increase the total credit facility from $35.0 million to $50.0 million and is now scheduled to mature on March 20, 2017. Under the terms of the amended agreement (in contrast to the original BMO Harris Bank N.A. agreement): (a) the revolving line of credit bears interest at Harris prime rate plus an applicable margin ranging from 0% to 0.50%; or, at our option, all or a portion of the revolving line of credit can be designated to bear interest at LIBOR plus an applicable margin ranging from 1.75% to 2.25%; (b) the unused line fee has been reduced to 0.25%; and (c) we are only required to report our compliance with the fixed charge coverage ratio for any month when our excess availability, as defined in the amended agreement, is less than the liquidity threshold, as defined in the amended agreement and we must continue to report our compliance with the applicable bank covenants until we have exceeded the liquidity threshold for 60 consecutive days. In addition, our cash balances are no longer automatically swept by BMO Harris Bank N.A., and as a result, from time to time, we may carry cash balances on our consolidated balance sheet. The liquidity threshold is defined as the greater of (i) $7,500,000 or (ii) 12.5% of the total credit facility of $50.0 million as may be reduced from time to time pursuant to the terms of the amended agreement.

On November 8, 2012, the loan and security agreement with BMO Harris Bank was further amended to increase our thresholds for certain transactions, allowing us to: (i) make acquisitions up to an aggregate of $2.0 million (ii) enter into joint ventures up to an aggregate of $2.0 million, up from $500,000, and (iii) make annual capital expenditures up to $8.0 million, up from $4.0 million. These thresholds are subject to certain limitations as set forth in the November 8, 2012, amended agreement.

As of March 31, 2013, $6.9 million of our outstanding borrowings under our revolving line of credit bore interest at the prime rate, which equated to 3.25% with the applicable margin included. The remaining outstanding balance as of March 31, 2013, of $25.0 million had been designated to bear interest at the LIBOR rate, plus an applicable margin, which equated to an aggregate interest rate of 1.95%. The unused and available revolving line of credit balance was approximately $18.1 million at March 31, 2013.

As of December 31, 2012, $5.9 million of our outstanding borrowings under our revolving line of credit bore interest at the prime rate, which equates to 3.25% with the applicable margin included. The remaining outstanding balance as of December 31, 2012, of $25.0 million had been designated to bear interest at the LIBOR

Table of Contents

rate, plus an applicable margin, which equated to an aggregate interest rate of 1.96%. The unused and available revolving line of credit balance was $19.1 million at December 31, 2012.

We were in compliance with the financial covenants under our current credit facility as of March 31, 2013 and as of December 31, 2012.

On April 29, 2011, upon consummation of the reverse recapitalization and the other transactions referred to above under *2011 significant developments*, we used net proceeds from the private placement and proceeds from a draw on the new revolving line of credit to repay the prior loans (as discussed below) under the prior credit agreement with Fifth Third Bank in full. Upon consummation of the reverse recapitalization and immediately following the repayment of these prior loans on April 29, 2011, availability under the new revolving line of credit was approximately $12.7 million.

The prior credit agreement was entered into in 2008 among Fifth Third Bank and The W Group and its subsidiaries. The initial proceeds from the prior credit agreement were used to retire the revolving line of credit and term loans with our predecessor bank. The prior credit agreement provided for a revolving line of credit of up to $37.5 million, a term loan of $8.7 million (Term Loan A) and a term loan of $2.4 million (Term Loan B), which prior loans collectively were scheduled to mature on July 15, 2013 and had variable interest rates. Under the terms of the prior credit agreement with Fifth Third Bank, we had the ability to elect whether outstanding amounts under the prior loans accrued interest based on the prime rate plus a margin or LIBOR plus a margin. Prior to being repaid in full, the loans under our prior credit agreement were collateralized by substantially all of our assets. Under the prior credit agreement, we were required to maintain our cash accounts with Fifth Third Bank. We had our cash deposits in our prior revolving line of credit account swept by Fifth Third Bank daily and applied against the outstanding revolving line of credit balance. As a result, we maintained a zero cash balance in our prior revolving line of credit account, and we borrowed on our prior revolving line of credit on a daily basis to fund our cash disbursements. Outstanding borrowings under our prior revolving line of credit were $25.4 million at April 29, 2011 (immediately prior to the repayment of the prior revolving line of credit). Prior to its repayment in full in connection with the closing of the reverse recapitalization, principal payments of Term Loan A were payable in quarterly installments ranging from $0.2 million to $0.6 million over the life of the loan. Term Loan A had an outstanding balance of $5.1 million as of April 29, 2011 (immediately prior to the repayment of the loan balance). Prior to its repayment in full in connection with the closing of the reverse recapitalization, principal payments of Term Loan B were payable in quarterly installments of less than $0.1 million over the life of the loan plus a balloon payment at maturity. Term Loan B had an outstanding balance of $2.1 million as of April 29, 2011 (immediately prior to the repayment of the loan balance). In addition to scheduled quarterly payments, prior to its replacement, the prior credit agreement required an annual repayment equal to 60% of excess cash flow.

Our prior revolving line of credit was amended in August 2009, to reduce the maximum borrowings from $37.5 million to $29.0 million, bearing interest at Fifth Third Bank s prime rate (3.25% at December 31, 2009) plus an applicable margin ranging from 2.25% to 2.50%. At our option a portion of the prior revolving line of credit could be designated to bear interest at LIBOR, subject to a 2.00% floor, plus an applicable margin ranging from 3.25% to 3.50%.

Off-balance sheet arrangements

We do not have any material off-balance sheet arrangements (as defined in Item 303(a)(4) of Regulation S-K).

Critical accounting policies and estimates

The discussion and analysis of our financial condition and results of operations are based on our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States (GAAP). The preparation of these financial statements in accordance with GAAP

Table of Contents

requires us to make estimates, assumptions and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, we evaluate our estimates, assumptions and judgments, including those related to revenue recognition, bad debts, inventories, warranties, private placement warrants and income taxes. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities and our revenue recognition. Actual results may differ from these estimates under different assumptions or conditions.

Revenue recognition

We recognize revenue at the time title and risk of loss of inventory passes to the customer, which is typically upon shipment of goods. From time to time, we recognize revenue upon billing for goods which are not immediately shipped at the request and for the convenience of our customer, otherwise known as a bill and hold arrangement. In these cases, revenue is recognized under the same terms and conditions as any other sale, except that the products are held by us until the customer initiates the shipment of the product from our warehouses. Transfer of the title and risk of loss pass to the customer, and there are no future performance obligations, at the time the bill and hold sale is recognized. Any product that has been sold under a bill and hold arrangement is segregated from our owned inventory. As of December 31, 2010, we had $1,742,000 of undelivered product, of which $391,000 was unpaid, and such product was shipped and the unpaid balance collected during 2011. We did not enter into any bill and hold arrangements during 2011, 2012 or for the three months ended March 31, 2013.

We classify shipping and handling charges billed to customers as revenue. Shipping and handling costs paid to others are classified as a component of cost of sales when incurred.

Allowance for doubtful accounts

The carrying amount of accounts receivable is reduced by a valuation allowance that reflects our management s best estimate of the amounts that will not be collected. Our management specifically reviews all past due accounts receivable balances and, based on historical experience and an assessment of current creditworthiness, estimates the portion, if any, of the balance that will not be collected.

Inventories

Our inventories consist primarily of engines and parts. Engines are valued at the lower of cost plus estimated freight-in, as determined by specific serial number identification, or market value. Parts are valued at the lower of cost (first-in, first out) or market value.

We write down inventory for an estimated amount equal to the difference between the cost of the inventory and the estimated realizable value. Additionally, an inventory reserve is provided for based upon our estimation of future demand for the quantity of inventory on hand. In determining an estimate of future demand, multiple factors are taken into consideration including (i) customer purchase orders and customer forecasted demand; (ii) historical sales/usage for each inventory item; and (iii) utilization within a current or anticipated future power system. These factors are primarily based upon quantifiable information and therefore, we have not experienced significant differences in inventory valuation due to variances in our estimation of future demand. We estimate that at March 31, 2013 a 10% variance between the estimated net realizable value of our inventory and its recorded cost would have a less than $100,000 effect on the value of our inventory.

Warranty programs

We offer a standard limited warranty on the workmanship of our products that in most cases covers defects for a period of (i) one year from the date of shipment or (ii) six months from the date products are placed into

Table of Contents

service, whichever occurs first. Warranties for certified emission products are mandated by the EPA and/or the CARB and are longer than our standard warranty on certain emission related products. Our products also carry limited warranties from suppliers. Costs related to supplier warranty claims are borne by the supplier; our warranties apply only to the modifications we make to supplier base products. We estimate and record a liability, and related charge to income, for our warranty program at the time products are sold to customers. Our estimates are based on historical experience and reflect management s best estimates of expected costs at the time products are sold. We make adjustments to our estimates in the period in which it is determined that actual costs may differ from our initial or previous estimates. We estimate that at March 31, 2013 a 10% change in the amount of historical warranty expense would have a less than $100,000 impact on our warranty liability.

Private placement warrants

Our private placement warrants are accounted for as a liability, in accordance with ASC 480-10-25-14, *Distinguishing Liabilities from Equity*. ASC 480-10-25-14 states that, if an entity must or could settle an instrument by issuing a variable number of its own shares, and, as in this case, the obligation s monetary value is based solely or predominantly on variations in the fair value of the company s equity shares, but moves in the opposite direction, then the obligation to issue shares is to be recorded as a liability at the inception of the arrangement, and is adjusted with subsequent changes in the fair value of the underlying stock. Our private placement warrants were measured at fair value under ASC Topic 820, *Fair Value Measurements and Disclosures of the Accounting Standards Codification.* Our liability for the private placement warrants is measured at fair value based on unobservable inputs, and thus is considered a Level 3 financial instrument. At March 31, 2013, if all other assumptions were held constant, the recorded liability of the private placement warrants would increase or decrease by approximately $706,000 due to a 10% change in the value of our warrants based on the Black-Scholes option pricing model.

Equity-based compensation

Our equity-based compensation expense for awards granted to employees for service is accounted for over the service period based on the grant date fair value. Furthermore, the stock appreciation right granted is accounted for as equity, in accordance with ASC 718, *Compensation Stock Compensation*.

Income taxes

We account for income taxes under the asset and liability method, which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements. Under this method, deferred tax assets and liabilities are determined based on the differences between the financial statements and tax basis of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enactment date.

We record net deferred tax assets to the extent we believe the assets will more likely than not be realized. In making such a determination, we consider all available positive and negative evidence, including future reversals of existing taxable temporary differences, projected future taxable income, tax-planning strategies, and results of recent operations. As of March 31, 2013 and December 31, 2012 and 2011, we had not recorded a tax asset valuation allowance.

We record uncertain tax positions in accordance with ASC 740, *Income Taxes*, on the basis of a two-step process whereby (1) we determine whether it is more likely than not that the tax positions will be sustained based on the technical merits of the position and (2) for those tax positions that meet the more-likely-than-not recognition threshold, we recognize the largest amount of tax benefit that is greater than 50 percent likely to be realized upon ultimate settlement with the related tax authority. As of March 31, 2013 and December 31, 2012 and 2011, we had not recorded any tax benefit or tax liability for uncertain tax positions.

Table of Contents

Impact of recently issued accounting standards

We evaluate the pronouncements of authoritative accounting organizations, including the Financial Accounting Standards Board, to determine the impact of new pronouncements on GAAP and our consolidated financial statements. There are no new accounting pronouncements that have been issued or adopted as of March 31, 2013, that we expect will have a significant effect on our consolidated financial statements.

Table of Contents

Business

Company Overview

We are a global producer and distributor of a broad range of high performance, certified low-emission, power systems that primarily run on alternative fuels such as natural gas and propane and are designed to meet emission standards of the EPA and the CARB. Our customers include large, multinational OEMs of off-highway industrial equipment, and we are a sole source provider of alternative fuel power systems for most of these customers. Our power systems are currently used by OEMs in a wide range of industries with a diversified set of applications, including, stationary electricity generators, oil and gas equipment, forklifts, aerial work platforms, industrial sweepers, arbor equipment, agricultural and turf equipment, aircraft ground support equipment, construction and irrigation equipment, and other industrial equipment. In addition to our primary focus on the industrial market, we are introducing a range of alternative fuel power systems designed for the on-road market.

Our power systems are highly engineered, comprehensive systems customized to meet specific industrial OEM application requirements and technical specifications, as well as requirements imposed by environmental regulatory bodies. Our power system configurations range from a basic engine block integrated with appropriate fuel system components to completely packaged power systems. We purchase engines from third party suppliers and have recently begun producing an internally-designed engine, both of which are then integrated into our power systems. We are also conducting research and development for the purpose of designing, developing and manufacturing other engines in-house. A substantial portion of the components we integrate into our power systems consist of internally designed components and components for which we coordinate significant design efforts with third party suppliers, with the remainder consisting largely of parts that we source off the shelf from third party suppliers. We are able to provide our customers with a comprehensive, emission-certified power system which can be incorporated, using a single part number, directly into a customer s specified application.

For industrial applications, our alternative fuel power systems meet or exceed emission standards of the EPA and CARB and represent a cleaner, and typically less expensive, alternative to diesel fuel power systems. While our power systems primarily run on alternative fuels, we also supply EPA and CARB emission-certified standard fuel power systems, and we are one of the largest suppliers of Perkins and Caterpillar diesel power systems under 275 horsepower. We expect that growth in domestic sales of our low-emission power systems will be driven by the substantial breadth of our emission-certified products, as well as increasing U.S. demand for alternative fuel power systems resulting from the adoption of increasingly stringent engine emission regulations. We are also experiencing increasing demand for our power systems from international industrial OEMs that manufacture industrial equipment for the U.S. import market.

Table of Contents

In addition to our emission-certified power systems, we also produce and distribute nonemission-certified power systems for industrial OEMs for particular applications in markets without emission standards (for example, oil and gas equipment used in Canada). Approximately 69% of our net sales for 2012 consisted of sales of emission-certified products, with approximately 57% of our 2012 net sales consisting of sales of emission certified products for which we hold the applicable regulatory certification and 12% of our 2012 net sales consisting of sales of diesel power systems for which the diesel engine supplier holds the applicable regulatory certification. Approximately 10% of our net sales in 2012 consisted of sales of aftermarket parts, and the remaining approximately 21% of our net sales in 2012 consisted of sales of our nonemission-certified power systems.

Recent Performance

We improved our operational and financial performance during our latest fiscal year ended December 31, 2012 and the most recent quarter ended March 31, 2013:

- Increased total revenue by 30.6% to $202.3 million for the fiscal year ended December 31, 2012 from $155.0 million for the fiscal year ended December 31, 2011;
- Increased adjusted diluted earnings per common share to $0.81 for the fiscal year ended December 31, 2012 from $0.48 for the fiscal year ended December 31, 2011;
- Increased total revenue by 9.4% to $52.6 million for the three months ended March 31, 2013 from $48.1 million for the three months ended March 31, 2012; and
- Increased adjusted diluted earnings per common share to $0.21 for the three months ended March 31, 2013 from $0.19 for the three months ended March 31, 2012.

Industry and Market Overview

Industrial OEM Market

The off-highway industrial OEM market represents a diversified set of applications and industry categories that include power generation, oil and gas, material handling, aerial work platforms, sweepers, arbor, welding, airport ground support, agricultural, turf, construction and irrigation. While the power system requirements for the industrial OEM market bear similarities to the requirements for power systems used in automotive applications, there are substantial application differences between automotive and industrial equipment applications. Torque, start, stop, low speed and, with respect to certain applications, indoor use requirements, make direct use of an automotive power system impractical for use in most industrial equipment applications. Recognizing these differences, the EPA and CARB have issued distinct emission standards and regulations for industrial applications, as compared to those for automotive applications. As a result, there is not a direct cross-over of available automotive power systems into the industrial OEM market. Power systems used in the industrial OEM market must satisfy these emission standards through a certification process with the EPA and CARB that includes durability testing of the engine emission system at zero and 5,000 hours, production line testing on a quarterly basis and field compliance audit testing. Given the level of engineering and financial resources that automotive engine manufacturers would need to dedicate to supply emission-certified product into the industrial OEM market, and that this market does not represent a core business for these manufacturers, it is generally impractical for automotive engine manufacturers to compete in the industrial OEM market.

Industrial OEM power systems use internal combustion engines (both diesel and spark-ignited), as well as electric motors. Diesel engine systems, which use compression to initiate ignition to burn fuel, in contrast to spark-ignited engine systems which use a spark plug to initiate the combustion process, currently represent the dominant power systems, depending on the specific industrial application involved. For example, diesel powered equipment is generally used in outdoor industrial applications, while electric motors and alternative fuel, spark-ignited power systems are used for indoor industrial applications where carbon monoxide and air quality issues

57

Table of Contents

must be addressed. Both diesel power systems and electric motors have significant limitations. Diesel power systems present unique emission compliance challenges, while electric motors are often not feasible alternatives in industrial applications as a result of limitations on battery storage capacity. These challenges present opportunities to increase demand for spark-ignited power systems within the industrial OEM marketplace.

Market Trends

The market for our power systems is continuing to grow globally as a result of several key drivers.

Increasingly Stringent Regulations and Growing Efforts to Reduce Emissions

Concerns regarding climate change and other environmental considerations have led to the implementation of laws and regulations that restrict, cap or tax emissions in the automotive industry and throughout other industries. In particular, EPA Tier 4 emission standards, CARB regulations, and recently implemented policies in Europe, generally referred to as Stage I, II, III and IV regulations, are requiring a significant reduction in the level of emissions and particulate matter produced by diesel power systems. OEMs have experienced pressure to redesign their products to address these emission regulations, as products that are unable to meet emission standards may not be sold in the marketplace. However, we believe few suppliers to industrial OEMs have been capable of providing, or are willing to make the investments of time, financial, and other resources necessary to provide products that meet new emission regulations.

Increased EPA and CARB emission regulations associated with diesel power systems are taking effect and are expected to increase both the cost and product footprint (in other words, the size of the power system) of diesel power products. Internal combustion engines generally produce emissions of carbon monoxide, unburned hydrocarbons (organic compounds consisting entirely of hydrogen and carbon that can be emitted as a result of incomplete fuel combustion and fuel evaporation), and oxides of nitrogen (highly reactive gases formed when oxygen and nitrogen in the air react with each other during combustion), and diesel engines produce particularly high levels of these pollutants. In addition, diesel engines produce particulate matter, which is among the areas of focus of these emission regulations. In 2004, the EPA adopted rules introducing Tier 4 emission standards which significantly reduce permitted emissions of oxides of nitrogen and particulate matter, and restrict hydrocarbon emissions, for off-road diesel engines of various sizes. The most recent standards adopted were initially implemented in 2008 and will continue to be phased in through 2015. As an example of the increasingly stringent standards to which diesel engines are subject, in 2012 permitted levels of particulate matter for nonroad diesel engines were reduced by approximately 90% from 2009 permitted levels. As a result, manufacturers and suppliers of diesel power systems, in comparison to spark-ignited and hybrid power systems, face greater challenges in complying with the new emission regulations. A manufacturer of diesel power systems must expend significant resources to develop a compliant power system, often through incorporation of additional components into a power system to reduce levels of particulate and other emissions. This can be a lengthy and expensive process. Based upon our experience with customers and suppliers, and on additional information provided by Power Systems Research, Inc., industrial OEMs are experiencing cost increases of between 30% and 100% for a comprehensive diesel power system with combustion and aftertreatments incorporated to satisfy the new requirements. Furthermore, these emission regulations created not only a cost but also a footprint disadvantage for a diesel power system, when compared to a spark-ignited, emission-certified power system.

Additionally, countries outside of the United States have historically adopted emission regulations aligned with those of the U.S., and accordingly, it is anticipated that regulations comparable to current and future EPA and CARB emission regulations will be implemented internationally. For example, recently implemented policies in Europe, generally referred to as Stage I, II, III and IV regulations, regulate emissions of off-road mobile equipment. Similar to emission regulations in the U.S., these regulations in Europe call for reductions in emissions of hydrocarbons, oxides of nitrogen and particulate matter, to be phased in over a period of time. If foreign jurisdictions continue to adopt emission regulations consistent with those of the U.S., it is expected that

Table of Contents

the international industrial OEM market will experience similar pressures to use cost effective, emission-certified power systems.

Increased Use of Alternative Fuels

A variety of market factors are contributing to the increased use of alternatives fuels and growth of alternative fuel technology, including economics, energy independence, environmental concerns, and the widespread availability of alternative fuels. The price of alternative fuels such as natural gas or propane is substantially less than diesel or gasoline, and alternative fuels produce lower amounts of toxic greenhouse gases. In the United States, significant domestic alternative fuel reserves have been identified, and it is believed these reserves could satisfy much of the energy needs of the U.S. for many years. According to a 2013 report published by the Potential Gas Committee (PGC), a nonprofit organization comprised of experts working in the natural gas field, the U.S. future natural gas supply at the end of 2012 was 2,688 trillion cubic feet (consisting of PGC s assessments of technically recoverable resources combined with the U.S. Department of Energy s latest determination of proved reserves), which represents an increase of 22.1% from 2010 levels as determined by PGC. The abundance of domestic natural gas resources is expected to increase U.S. energy independence by reducing oil imports from foreign countries. As a result of these market factors, we believe the use of alternative fuels will continue to grow and providers of equipment in industrial OEM categories, such as power generation, that rely significantly on coal, diesel fuel and gasoline, will face increasing pressure to use alternative fuel power systems.

Additionally, the infrastructure supporting alternative fuel in the United States continues to expand. Further, the United States and some other countries have taken action to increase demand and support for alternative fuels, in an effort to reduce dependence on imported oil, capitalize on domestic natural gas reserves and reduce emissions from diesel engines. For example, the EPA has provided subsidies in the form of grants and other financing programs for the advancement of alternative fuel technologies (to date directed primarily towards on-road vehicles). Additionally, industry organizations, such as the Propane Education and Research Council, an organization authorized by the U.S. Congress with the passage of the Propane Education and Research Act, award grants to a wide variety of institutions, universities, and government organizations for the continued research, development, demonstration and commercialization of alternative fuel technologies.

Industrial OEM Trend Toward Outsourcing

Industrial OEMs have been following the broader marketplace trend of outsourcing non-core functions. The dynamics of global sourcing and the need for cost competitiveness have led, and should continue to lead, industrial OEMs to assess what operations and system components are core to their business model and what they should outsource to their suppliers and partners. In particular, to comply with frequently changing environmental regulations while remaining competitive, industrial OEMs have been increasingly more reliant on outsourcing to third party suppliers and partners with specialized regulatory and design expertise. This is especially true for international OEMs seeking access to the U.S. market. By outsourcing power system design and production, OEMs are able to focus their resources on overall design and functionality of their products, rather than on developing the sophisticated technology associated with emission-certified power systems. We expect increasingly more industrial OEMs to outsource power systems, system components and subsystems to third party suppliers with the requisite experience and technology.

Penetration by International Suppliers into Regulated Markets

The implementation of emission regulations domestically and in non-U.S. markets also impacts international suppliers of industrial equipment products outside these regulated markets. International industrial OEMs that supply into regulated industrial OEM markets, including those already doing so and those recognizing emerging opportunities to sell their products into these markets, must meet applicable emission requirements,

Table of Contents

like those imposed by the EPA and CARB in the U.S. For example, Chinese and other Asian suppliers have recognized that, in order to effectively penetrate and sell into emission regulated industrial OEM markets like North America and Western Europe, their products must be emission-certified. These international industrial OEMs generally lack the regulatory and design expertise necessary to develop their own emission-certified power systems. Furthermore, they recognize that, even if they had or could acquire the relevant expertise, it can be much less time consuming and much more cost-effective for them to acquire compliant power systems from third-party suppliers, rather than internally developing and manufacturing their own solutions. Accordingly, just as domestic industrial OEMs are outsourcing this function, so too are international industrial OEMs, and we expect this trend to continue.

Growing Demand for Sophisticated Electronic Technology and Automotive Grade Quality Standards

Demanding automotive grade quality, as well as on-time delivery, has become standard practice in the industrial OEM marketplace. Consistent with the trend in the automotive industry, the level of technology and sophistication, including electronic controls, associated with industrial OEM power systems has advanced significantly to meet the growing demand for improved quality, reliability and performance. This has led to an ongoing reduction in the number of suppliers capable of supporting such product requirements.

Our Competitive Strengths

We have a 27-year history and reputation as a proven supplier of cost-effective, technologically advanced products to the industrial OEM marketplace. We believe that our technological superiority and the comprehensive nature of our product offerings position us to capitalize on developing trends in the industrial OEM markets and drive significant future growth.

Broad Range of Alternative Fuel Power Systems

Our power systems represent a broad range of emission-certified, alternative fuel products for industrial applications. We are one of only a few providers of industrial OEM products that meet, and in many cases produce emissions at levels significantly lower than the emission standards of the EPA and CARB. Our alternative fuel engines range in size from under 1 liter to 22 liters and our power system configurations include any combination of cooling systems, electronic systems, air intake systems, fuel systems, housings, power takeoff systems, exhaust systems, hydraulic systems, enclosures, brackets, hoses, tubes and other assembled componentry. We provide standardized fuel system and component technology across our entire range of emission-certified power systems. As a result, our OEM customers are able to focus internal engineering and technical support resources, and train their personnel, on one standardized fuel system and one set of electronic controls employed throughout the range of power systems they acquire from us, and are able to reduce their product design and ongoing product support costs.

We believe our broad range of emission-certified, alternative fuel products strategically positions us to capitalize on the cost and packaging disadvantages associated with diesel power systems that are resulting from increased EPA and CARB emission regulations that are taking effect. Given the existing dominance of diesel power systems in the industrial OEM marketplace, even a minor shift in the marketplace from diesel to spark-ignited, alternative fuel power systems will represent a significant growth opportunity for us. Additionally, as international OEMs desire to supply industrial equipment products into the United States and must meet EPA and CARB emission requirements, we provide a fast, certain, cost-effective route for these foreign industrial OEMs to meet these emission requirements because we hold compliance certificates specific to our power systems. We have already secured commercial sales relationships with some of Asia s largest industrial OEMs, and have begun supplying EPA and CARB compliant power systems to these industrial OEM customers for incorporation into their product lineups.

Table of Contents

Leverageable, OEM-Focused Business Model

We are able to take advantage of opportunities for component standardization across industry categories, while still providing each industrial OEM with the flexibility to customize as required for particular design and application specifications. We aggregate our product development efforts, and can amortize associated costs, over our large and diverse OEM customer base and across industry categories. Furthermore, we capitalize on volume, economies of scale and global supply opportunities when sourcing component products. We can, therefore, provide our OEM customers with lower cost structures than they would otherwise be able to achieve and help them reduce their part numbers and supply base by consolidating their procurement and assembly efforts down to a single part number product supplied by us. Our component sourcing relationships further enable our OEM customers to recognize resource reductions, inventory reductions and engineering support advantages.

Additionally, our relationships with international OEM customers that supply their industrial equipment into the United States generate opportunities for us to further supplement our business. We believe that once one of our emission-certified power systems is engineered into a foreign industrial OEM s product, that OEM is likely to also incorporate our power systems into its products that do not require emission-compliant power systems. This use by foreign industrial OEMs of our power systems for both their emission-certified and non-emission-compliant power system needs reduces ongoing engineering, aftermarket and field service support requirements, while supporting a product strategy that can easily be adjusted to any future worldwide changes in emission requirements. These relationships further provide us with growth opportunities beyond those dependent upon U.S. demand for emission regulated products, and solidify our supplier and partnership position with our foreign industrial OEM customers. Moreover, even if our relationship with an international OEM customer is limited to United States compliant power systems, we are in an opportune position to provide additional emission-compliant power systems in the future as emission regulations for industrial equipment begin to emerge in other countries around the world.

Superior Technology

We are a recognized leader in providing industrial OEMs with highly engineered, technologically superior, emission-certified power systems that cover a wide range of possible fuel alternatives. Our power system development and manufacturing processes are supported by in-house design, prototyping, testing and engineering capabilities. We believe our customers are able to realize significant costs savings by leveraging our proven power system technology, our application engineering expertise, the broad range of our EPA and CARB emission-certified power systems and our industrial equipment testing and certification processes. They are also able to focus their efforts on the development of operations and system components core to their business, without having to expend considerable resources associated with the emission certification process, which requires potentially years to perform durability testing of the engine emission system at zero and 5,000 hours, production line testing on a quarterly basis and field compliance audit testing, each of which is mandated and regulated by the EPA and CARB.

Table of Contents

The level and range of our EPA and CARB emission-certified product offering further demonstrates the strength of our technology. Our emission-certified products meet all current existing emission standards of the EPA and CARB. We are able to maintain and enhance our position as a supplier of technologically sophisticated, emission-certified power systems through our experienced and technologically savvy team of application engineers. This team gives us the ability to support and integrate our power systems into a significant number of industrial OEM applications. We believe that our continued recruitment and development of talented personnel will augment our ability to stay ahead of emerging technologies in the industrial OEM marketplace.

Further, we are not captive to our own internal manufactured components and technology. Unlike some of our competitors that focus on developing and manufacturing most of their own product technology and components, we believe that superior technology is derived from having the flexibility to incorporate the best proven technology available in the marketplace. We focus on developing deep internal engineering and application expertise, more than on developing in-house components and technology. This affords us the flexibility to capitalize on current and emerging technology that best meets the requirements of any given application, as opposed to only using internally-developed technology that might not provide the best solution. Because we do not directly compete in the development of key technology, suppliers of underlying technology are interested in supplying their latest innovations to us. As a result, we believe we have access to the best proven technology in the marketplace. We believe this strategy puts us in a strong position to benefit from our significant OEM customer base and aggregation capabilities in order to provide the best available product and technology solutions for our OEM customers.

Dedicated Customer-Centric Product and Application Expertise

We have a customer-centric business focus, and we continually strive for customer satisfaction at all levels of customer interaction. We commit our attention and efforts to nurturing and expanding relationships with our customers by staying connected with them, being aware of challenges they face and understanding their evolving needs. From production personnel to our customer support staff, our entire team is highly experienced in both the products we sell and the OEM customer applications into which they are integrated. Through our extensive experience in the industrial OEM marketplace and our adaptive technology strategy that we use in developing our power systems, we are able to accept the specific requests of individual customers and provide tailored power systems to meet their needs. We assign a dedicated engineer to each OEM customer for application support and to provide a direct line of communication between the OEM s manufacturing line and our production operations. Our quality, field service support and service operations provide knowledgeable and responsive support to our OEM customers at every point of customer interface.

Growth Strategy

Our core strategy is to develop comprehensive power systems for the global industrial OEM marketplace. We believe that, with our competitive advantages, our continued pursuit of our core strategy will drive growth in our business. More specifically, we intend to seek future growth as follows:

Expand Products and Services Provided to Existing OEM Customers

We continually work to capitalize on organic growth opportunities and build upon our strong existing customer relationships, which in many cases are on a sole source basis. We plan to expand our business with existing customers by supporting their growth initiatives as they expand their produce lines, enter new markets, and adapt to changing emission standards. We also intend to develop and sell new products to our OEM customers as we broaden our range of emission-certified, alternative fuel power systems.

Table of Contents

Establish New Industrial OEM Relationships

We expect to strengthen our OEM customer base by developing new relationships with industrial OEMs. We seek to acquire new clients and gain new business from OEMs that we do not presently serve by focusing our marketing efforts toward these potential customers and capitalizing on our strong reputation; the depth, breadth and technological sophistication of our power systems; our commitment to customer service; and the cost savings we can offer. Emphasizing our experience and reputation in market categories in which our power systems are already well-established, such as power generation, we are focused on establishing new industrial OEM relationships and capturing a greater portion of the market share. We are also targeting new OEM customers in high-growth market categories, such as material handling and oil and gas applications, while maintaining and enhancing our penetration in market categories that are growing more slowly. As we gain traction in emerging industrial OEM categories that did not previously represent significant opportunities for our power systems, we plan to further focus our efforts on potential customers in those categories.

Expand Into New Geographic Markets

We are focused on expanding our business internationally with OEM customers that require EPA and CARB compliant power systems to access the U.S. market and for non-compliant systems used in products sold outside the U.S. Furthermore, because we expect countries outside of the United States to implement emission regulations that are aligned with U.S. standards, we anticipate an opportunity to expand our relationships with industrial OEMs that supply emission-compliant products outside of the U.S. If such emission regulations are implemented consistent with our expectation, we anticipate being able to provide power systems to industrial OEMs that meet applicable foreign emission standards by leveraging our existing technology and experience in developing our EPA and CARB emission-certified products.

Develop New Products

By leveraging the deep industry experience of our engineering and new product development teams, we are working to broaden the range of our power system product offerings, including with respect to engine classes and the industrial OEM market categories into which we supply our products. We are also currently in the process of developing new 2.0 liter and 2.4 liter engines. We capitalize on our technologically sophisticated, in-house design, prototyping, testing and application engineering capabilities to further refine our superior spark-ignited power system technology. We plan to apply our experience and expertise in developing comprehensive, integrated green power systems to expand our spark-ignited alternative fuel offerings.

Expand Into On-Road Market

We have recently introduced a newly designed, state-of-the-art, 8.8-liter fuel flexible engine that we plan to sell to industrial, bus and truck OEMs which will be a fully-integrated drop-in solution. We expect this engine to be a solution in the industrial off-road and on-road markets and have a wide range of applications, including school buses, waste-hauling trucks and medium-duty delivery trucks. Furthermore, we have recently expanded our on-road product line by entering a multi-year supply agreement with General Motors for 4.8-liter and 6.0-liter alternative fuel engines. We believe we now have a comprehensive range of alternative fuel powertrains for vehicle OEMs in the Class 4 through Class 7 truck and bus market.

Selectively Pursue Complementary Strategic Transactions

We may enter into strategic transactions, such as acquisitions of, or joint ventures or partnerships with, companies that present complementary non-organic growth opportunities. Specifically, we will seek opportunities that extend or supplement our presence into new geographic markets or industrial OEM market categories, expand our customer base, add new products or service applications or provide significant operating synergies. We believe that there may be domestic or international strategic opportunities available to us as the

Table of Contents

sophistication of technology and amount of resources necessary to develop and supply power systems that meet increasingly stringent emission standards continue to increase.

Company History

Founded in 1985, we sought to break the then-prevalent OEM focus on the diesel engine as a commodity by providing value-added engineering, procurement and packaging of products and services to the industrial OEM marketplace. Because of our expanded product and service offerings, we played a significant role in moving the industrial OEM marketplace from a simple, engine-centric model to a more comprehensive model. This comprehensive power system model includes engineering, procurement and packaging solutions for cooling, electronics, air intake, fuel systems, power takeoff, exhaust, hydraulics and packaging application requirements. Through implementation of our strategy, we grew our diesel power system sales and became one of the largest Perkins diesel power system distributors in the world, a position we still maintain today.

Our desire to expand our product and service offerings, coupled with the success of our strategy in the diesel marketplace, motivated us to move into the marketplace for spark-ignited power systems. From the mid-1990s going forward, we have applied our strategy to spark-ignited gasoline and alternative fuel products. In applying our extensive, prior experience developing power systems for our diesel power system OEM customers to the spark-ignited industrial OEM marketplace, and addressing the growing demand for diesel alternatives as a result of environmental and economic considerations, we have developed a comprehensive range of alternative fuel power systems. As a result, we have become a significant supplier of power systems to prominent OEM customers located throughout North America, with sales to OEM customers located (with location determined based upon the continent to which we ship a product) throughout North America representing approximately 91% of our net sales in 2012. We also sell our power systems to OEM customers located throughout Asia (approximately 8% of our net sales in 2012) and Europe (approximately 1% of our net sales in 2012), where we intend to increase our sales efforts.

On April 29, 2011, The W Group, Inc. completed a reverse acquisition transaction with Format, Inc. (which is now Power Solutions International, Inc.), in which PSI Merger Sub, Inc., a Delaware corporation that was newly-created as a wholly-owned subsidiary of Format, merged into The W Group, and The W Group remained as the surviving corporation of the merger. In that transaction, The W Group became a wholly-owned subsidiary of Power Solutions International, Inc.

Format was incorporated in the State of Nevada on March 21, 2001 for the purpose of providing EDGARizing services to various commercial and corporate entities. Immediately prior to the consummation of the reverse acquisition transaction, Format was engaged, to a limited extent, in EDGARizing corporate documents for filing with the SEC, and providing limited commercial printing services, and had assets that included cash, rights under a services agreement with Format s sole customer (which agreement was terminated in connection with the reverse recapitalization), a real property lease pursuant to which Format leased its sole office space (which lease was transferred to Ryan Neely, Format s sole director and executive officer immediately prior to the closing of the reverse recapitalization, in connection with the reverse recapitalization) and depreciated office equipment located in Format s transferred, leased office space. Due to the nominal operations and assets of Format immediately prior to the consummation of the reverse recapitalization and related transactions, this reverse acquisition transaction was accounted for as a recapitalization.

The reverse recapitalization transaction was consummated under Delaware corporate law pursuant to an agreement and plan of merger. Upon completion of the reverse recapitalization, Format changed its name to Power Solutions International, Inc. All of the outstanding shares of common stock of The W Group held by the three stockholders of The W Group at the closing of the reverse recapitalization converted into an aggregate of 10,000,000 shares of our common stock and 95,960.90289 shares of preferred stock. These shares represented a substantial majority of the shares of our common stock and shares of preferred stock outstanding immediately following the consummation of the reverse recapitalization transaction.

Table of Contents

In connection with the reverse recapitalization transaction, Format entered into a stock repurchase and debt satisfaction agreement with Ryan Neely and his wife, Michelle Neely. Pursuant to this agreement, at the time the reverse recapitalization transaction was completed, (1) Format repurchased 3,000,000 shares of Format common stock, representing approximately 79.57% of the shares of Format common stock outstanding immediately prior to the consummation of the reverse recapitalization transaction, from Ryan and Michelle Neely, and (2) Ryan Neely and Michelle Neely terminated all of their interest in, and released Format from all obligations it had with respect to, the loans made by Ryan Neely and Michelle Neely to Format from time to time, in exchange for aggregate consideration of $360,000. In addition, Ryan and Michelle Neely released Format from any obligations Format had to them in respect of any other amounts (including any accrued compensation) that may have been at any time owed from Format prior to the closing of the reverse recapitalization. In connection with, but prior to, the closing of the reverse recapitalization, Format used all of its available cash to settle remaining liabilities that Format had prior to the completion of the reverse recapitalization. These included amounts owed to Format s accountants, independent auditors and legal counsel; provided that Format s legal counsel agreed to release Format from its obligation to pay a portion of legal fees incurred by Format in connection with the reverse recapitalization and related transactions. Further, in connection with, but prior to, the closing of the reverse recapitalization, Format entered into a termination agreement, pursuant to which Format terminated its services agreement with its sole customer. In connection with, but prior to, the closing of the reverse recapitalization, Format also transferred to Ryan Neely all of its rights and obligations under the real property lease relating to Format s sole office space.

As a result of the reverse recapitalization, Power Solutions International, Inc. succeeded to the business of The W Group.

Pursuant to the terms of the private placement, we also agreed to consummate, and Format s board of directors approved, a migratory merger of our company into a Delaware corporation. On August 25, 2011, we held a special meeting of our stockholders at which our stockholders approved the reverse split, the migratory merger and related matters. On August 26, 2011, Power Solutions International, Inc., a Nevada corporation, merged into its wholly-owned subsidiary, Power Solutions International, Inc., a Delaware corporation. Power Solutions International, Inc., a Delaware corporation, continued as the surviving entity of the migratory merger. Pursuant to the migratory merger, we changed our state of incorporation from Nevada to Delaware and each 32 shares of common stock of Power Solutions International, Inc., a Nevada corporation, converted into one share of common stock of the surviving entity in the migratory merger, thereby effecting a 1-for-32 reverse stock split of our common stock. As a result of the migratory merger, (1) Power Solutions International, Inc., a Delaware corporation, acquired all of the rights, privileges and powers, and became subject to all restrictions and duties, of Power Solutions International, Inc., the previously existing Nevada corporation, (2) all liabilities and obligations of Power Solutions International, Inc., the previously existing Nevada corporation, became the liabilities and obligations of Power Solutions International, Inc., a Delaware corporation, as the surviving corporation of the migratory merger and (3) Power Solutions International, Inc., a Delaware corporation, succeeded to the business of Power Solutions International, Inc., the previously existing Nevada corporation.

Further, pursuant to the Certificate of Designation for the Series A Convertible Preferred Stock and the agreement and plan of merger for the migratory merger, and upon the effective date of the migratory merger, each share of preferred stock automatically converted into a number of shares of our common stock equal to $1,000 divided by $12.00, the conversion price then in effect as adjusted for the migratory merger and the reverse split. Any stockholder of our company that was otherwise entitled to a fraction of a share of our common stock (after aggregating all fractional shares of our common stock to be received by such holder) as a result of the migratory merger, received an additional share of our common stock (in other words, the aggregate number of shares of our common stock of a stockholder resulting from the migratory merger was rounded up to the nearest whole number). The authorized shares of our capital stock and the par value of our common stock immediately following the consummation of the migratory merger are identical to the authorized shares of capital stock of Power Solutions International, Inc., a Nevada corporation, and the par value of its common stock immediately prior to the consummation of the migratory merger.

Table of Contents

Our Products and Industry Categories

Power Systems for Off-Highway Industrial Equipment

Our power systems are customized to meet specific industrial OEM application requirements. Power system configurations range from a basic engine block integrated with appropriate fuel system components to completely packaged power systems that include any combination of cooling systems, electronic systems, air intake systems, fuel systems, housings, power takeoff systems, exhaust systems, hydraulic systems, enclosures, brackets, hoses, tubes and other assembled componentry.

Our power systems include (1) EPA and CARB emission-certified spark-ignited water-cooled internal combustion engines ranging from 0.97 liters to 22 liters, which use alternative fuels and gasoline, (2) non-certified spark-ignited water-cooled internal combustion engines ranging from 0.65 liters to 22 liters, which similarly use alternative fuels and gasoline, and (3) emission-certified Perkins engines ranging from 0.5 liters to 7.1 liters, which use diesel fuel. Our diesel and alternative fuel power systems use water-cooled (as opposed to air-cooled), multi-cylinder engines.

Our products are sold into a diversified set of markets within the industrial OEM industry, including power generation, oil and gas, material handling, aerial work platforms, sweepers, arbor, welding, airport ground support, agricultural, turf, construction and irrigation. Different types of power systems are used within different industry categories (from which we receive varying, unequal amounts of revenues).

Power Generation

We offer EPA and CARB emission-certified power systems, including 0.97 liter to 22 liter spark-ignited power systems that use alternative fuels, for stationary emergency and non-emergency power generation products. Emergency engines are stationary engines which operate solely in emergency situations and during required periodic testing and maintenance. Examples include engines used in generators to produce power for critical networks when electrical power from the local utility provider is interrupted, and stand-by engines that pump water in the event of a fire or flood. Non-emergency products include prime power generation products, which produce continuous generation of power for an extended period of time, and peak shaving products, which generate power at times of maximum power demand.

We currently supply our power systems to a substantial number of manufacturers of power generation products. We believe that our customers choose our power systems because of our broad range of emission-certified, spark-ignited power systems for this industry category. Additionally, by using a common fuel system and electronic controls across our range of power systems, we provide our customers with the opportunity to support and train their personnel on one standardized fuel system and one set of electronic controls employed throughout the range of products they acquire from us.

Material Handling Forklift Trucks

The material handling market category includes forklift trucks and other mobile products used for movement, handling and storage of materials within a facility or at a specific location. We provide spark-ignited power systems into the high volume 1.5, 3.5 and 5 ton capacity forklift markets, and may expand production in the future to support the 8 and 10 ton forklift markets in connection with anticipated increases in diesel prices resulting from regulations on diesel engines taking effect through 2015.

Demand is currently strong in the United States for our material handling power systems as a result of emission and OSHA regulations. Based upon data supplied by Power Systems Research, Inc., we believe that, in the United States, nearly 100% of the indoor forklift market uses spark-ignited liquid propane gas or electric powered units (with approximately equal market shares), in contrast to Asian and European forklift markets which currently use diesel in excess of 80% of all applications. In connection with the implementation of EPA

Table of Contents

Tier 4 and European Stage IV regulations, and the resulting price increases related to the compliance of diesel engines with these regulations, we expect foreign markets for spark-ignited liquid propane gas power systems to grow. We expect this growth to drive increased international demand for our power systems.

Oil and Gas

The oil and gas market category includes oil field pumps, progressing cavity pumps, and other components and machines used in drilling, evaluation, completion and production of oil and gas assets. Previously, OEMs competing in these markets were generally not concerned about fuel economy, cost of repair or efficiency of operation. Today, however, there is a growing focus in this market category on, and understanding of, the costs associated with down time, the value of fuel savings with more economical solutions and the benefits of using product portfolios with consistent fuel systems and aftermarket support. We believe that these factors will create significant opportunities for our power systems in this market category. Furthermore, we believe that recent discoveries of oil and gas reserves in North America will drive domestic demand for the products of oil and gas OEMs, enhancing our growth opportunities.

We are continuing to develop relationships with oil and gas companies for their well head jacks, compressors and power generators. We believe we are the only provider in this market that supplies pre-certified, as opposed to site-certified, power systems. Site certification is a tedious and costly process for oil and gas equipment OEMs that can take many hours to s