UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

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

For the quarterly period ended June 30, 2014

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

For the transition period from to

Commission file number 001-16265

LIME ENERGY CO.

(Exact name of registrant as specified in its charter)

Delaware	**36-4197337**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

16810 Kenton Drive, Suite 240, Huntersville, NC 28078
(Address of principal executive offices, including zip code)

(704) 892-4442
(Registrant s telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer o	Accelerated Filer o
Non-Accelerated Filer o	Smaller reporting company x

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

3,760,267 shares of the registrant s common stock, $.0001 par value per share, were outstanding as of August 14, 2014.

Table of Contents

LIME ENERGY CO.

FORM 10-Q

For The Quarter Ended June 30, 2014

INDEX

Table of Contents

PART I - FINANCIAL INFORMATION

ITEM 1. Financial Statements

Lime Energy Co.

Condensed Consolidated Balance Sheets

(in thousands)

	June 30, 2014 (unaudited)	December 31, 2013 (1)
Assets		
Current Assets		
Cash and cash equivalents	$ 504	$ 6,940
Restricted cash	500	500
Accounts receivable, net of allowance for doubtful accounts of $1,991 and $1,824, respectively	9,035	9,151
Costs and estimated earnings in excess of billings on uncompleted contracts	6,283	6,625
Prepaid expenses and other	487	255
Current assets of discontinued operations	2,145	3,442
Total Current Assets	18,954	26,913
Net Property and Equipment	1,468	1,562
Long-Term Receivables	404	296
Goodwill	6,009	6,009
	$ 26,835	$ 34,780

Table of Contents

Lime Energy Co.

Condensed Consolidated Balance Sheets

(in thousands, except share data)

	June 30, 2014 (unaudited)	December 31, 2013 (1)
Liabilities and Stockholders Equity		
Current Liabilities		
Accounts payable	$ 13,463	$ 15,835
Accrued expenses	1,258	2,907
Billings in excess of costs and estimated earnings on uncompleted contracts	419	1,711
Customer deposits	151	72
Current liability to trade creditor	1,493	3,236
Current liabilities of discontinued operations	1,435	3,245
Total Current Liabilities	18,219	27,006
Total Liabilities	18,219	27,006
Stockholders Equity		
Series A Preferred stock, $0.01 par value; 2,000,000 authorized 1,016,982 and 957,624 issued and outstanding as of June 30, 2014 and December 31, 2013, respectively	10	9
Series B Preferred stock, $0.01 par value; 1,000,000 authorized 636,170 and 401,232 issued and outstanding as of June 30, 2014 and December 31, 2013, respectively	6	4
Common stock, $.0001 par value; 50,000,000 shares authorized 3,731,705 and 3,667,298 issued and outstanding as of June 30, 2014 and December 31, 2013, respectively		
Additional paid-in capital	207,669	205,489
Accumulated deficit	(199,069)	(197,728)
Total Stockholders Equity	8,616	7,774
	$ 26,835	$ 34,780

See accompanying notes to condensed consolidated financial statements

(1) Derived from audited financial statements in the Company s annual report on Form 10-K for the year ended December 31, 2013

Table of Contents

Lime Energy Co.

Unaudited Condensed Consolidated Statements of Operations

(in thousands, unaudited)

	Three Months Ended June 30, 2014	Three Months Ended June 30, 2013	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013
Revenue	$ 13,590	$ 12,943	$ 25,871	$ 24,159
Cost of sales	9,176	9,192	17,727	17,782
Gross Profit	4,414	3,751	8,144	6,377
Selling, general and administrative	4,666	5,416	9,576	11,444
Amortization of intangibles		4		10
Operating loss	(252)	(1,669)	(1,432)	(5,077)
Other Income (Expense)				
Interest income	23	12	39	26
Interest expense		(261)		(522)
Total other income (expense)	23	(249)	39	(496)
Loss from continuing operations	(229)	(1,918)	(1,393)	(5,573)
Discontinued Operations:				
Income (Loss) from operation of discontinued business	55	(128)	52	(3,176)
Net loss	$ (174)	$ (2,046)	$ (1,341)	$ (8,749)
Preferred stock dividends	(486)		(1,953)	
Net loss available to common stockholders	(660)	(2,046)	(3,294)	(8,749)
Basic and diluted (loss) earnings per common share from				
Continuing operations	$ (0.19)	$ (0.53)	$ (0.89)	$ (1.55)
Discontinued operations	0.01	(0.04)	0.01	(0.88)
Basic and Diluted Loss Per Common Share	$ (0.18)	$ (0.57)	$ (0.88)	$ (2.43)
Weighted Average Common Shares Outstanding	3,730	3,593	3,728	3,594

See accompanying notes to condensed consolidated financial statements

Table of Contents

Lime Energy Co.

Unaudited Condensed Consolidated Statement of Stockholders Equity

(in thousands, unaudited)

	Common Shares	Common Stock	Series A Preferred Shares	Series A Preferred Stock	Series B Preferred Shares	Series B Preferred Stock	Additional Paid-in Capital	Accumulated Deficit	Total Stockholders Equity
Balance, December 31, 2013	**3,667**	**$**	**958**	**$ 9**	**$ 401**	**$ 4**	**$ 205,489**	**$ (197,728)**	**$ 7,774**
Issuance of preferred stock					200	2	1,998		2,000
Issuance costs							(9)		(9)
Preferred stock dividends							(943)		(943)
Satisfaction of preferred stock dividends through the issuance of preferred stock			59	1	35		943		944
Shares issued for benefit plans	64								
Share based compensation							191		191
Net loss								(1,341)	(1,341)
Balance, June 30, 2014	**3,731**	**$**	**1,017**	**$ 10**	**636**	**$ 6**	**$ 207,669**	**$ (199,069)**	**$ 8,616**

See accompanying notes to condensed consolidated financial statements.

Table of Contents

Lime Energy Co.

Unaudited Condensed Consolidated Statements of Cash Flows

(in thousands, unaudited)

	Three Months Ended June 30, 2014	Three Months Ended June 30, 2013	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013
Cash Flows From Operating Activities				
Net Loss	$ (174)	$ (2,046)	$ (1,341)	$ (8,749)
Adjustments to reconcile net loss to net cash used in operating activities:				
Provision for bad debt	179	238	368	341
Share-based compensation	65	194	191	376
Depreciation and amortization	181	264	369	532
PIK notes issued for interest		384		384
Amortization of deferred financing costs		26		52
Amortization of original issue discount		66		132
Loss on disposition of property and equipment				13
Changes in assets and liabilities:				
Accounts receivable	83	(121)	(360)	264
Inventories		3		3
Costs and estimated earnings in excess of billings on uncompleted contracts	(1,438)	(1,150)	342	(1,724)
Prepaid expenses and other	(199)	(16)	(232)	(36)
Assets of discontinued operations	200	284	1,297	1,588
Accounts payable	1,789	3,524	(2,372)	4,542
Accrued expenses	(693)	(217)	(1,649)	248
Billings in excess of costs and estimated earnings on uncompleted contracts	12	(43)	(1,292)	309
Other current liabilities	(825)	(283)	(1,664)	(510)
Liabilities of discontinued operations	(391)	(1,264)	(1,810)	633
Net cash used in operating activities	(1,211)	(157)	(8,153)	(1,602)
Cash Flows From Investing Activities				
Proceeds from sale of ESCO business				1,860
Purchases of property and equipment	(182)	(100)	(274)	(287)
Net cash (used in) provided by investing activities	(182)	(100)	(274)	1,573
Cash Flows From Financing Activities				
Payments of long-term debt		(30)		(77)
Proceeds from the issuance of preferred stock			2,000	
Costs related to stock issuances	(1)		(9)	
Net cash (used in) provided by financing activities	(1)	(30)	1,991	(77)
Net Increase (Decrease) in Cash and Cash Equivalents	(1,394)	(287)	(6,436)	(106)
Cash and Cash Equivalents, at beginning of period	1,898	2,193	6,940	2,012

Cash and Cash Equivalents, at end of period	$	504	$	1,906	$	504	$	1,906

Table of Contents

	Three Months Ended June 30, 2014	Three Months Ended June 30, 2013	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013
Supplemental Disclosure of Cash Flow Information:				
Preferred dividends satisfied through issuance of preferred stock:	$ 486	$	$ 943	$
Cash paid during the period for interest:				
Continuing operations	$	$ 36	$	$ 86
Discontinued operations	$	$	$	$ 1

See accompanying notes to condensed consolidated financial statements

Table of Contents

Note 1 Basis of Presentation

The accompanying unaudited condensed consolidated financial statements (the Financial Statements) of Lime Energy Co. (Lime Energy and, together with its subsidiaries, the Company , we , us or our) have been prepared in accordance with Rule 10-01 of Regulation S-X promulgated b the Securities and Exchange Commission (the SEC) and, therefore, do not include all information and footnotes necessary for a fair presentation of financial position, results of operations and cash flows in conformity with accounting principles generally accepted in the United States of America (GAAP). In our opinion, however, the Financial Statements contain all adjustments, consisting only of normal recurring adjustments, necessary to present fairly our financial position, results of operations and cash flows as of and for the interim periods.

The results of operations for the three and six month periods ended June 30, 2014 and 2013 are not necessarily indicative of the results to be expected for the full year.

The Company has raised a significant amount of capital since its formation through the issuance of shares of its common and preferred stock, all of which have allowed the Company to continue to execute its business plan. The actual timing and amount of future funding requirements will depend on many factors, including the amount, timing and profitability of future revenues, working capital requirements, the level and amount of the Company s sales efforts, among other things. While it is possible that current cash balances will be sufficient to carry the Company until operations turn cash flow positive, it is also possible that the Company will need to raise additional capital sometime in the near future. If the Company determines it is necessary to raise additional capital, there is no assurance it will be able to do so, or, it may only be available on terms that are not favorable to the Company and/or existing stockholders.

The December 31, 2013 balance sheet data was derived from audited financial statements, but does not include all disclosures required by GAAP.

For further information, refer to the audited financial statements and the related footnotes included in the Lime Energy Co. Annual Report on Form 10-K for the year ended December 31, 2013.

Note 2 - Share-Based Compensation

A committee of the Board of Directors grants stock options and restricted stock under the Company s 2008 Long Term Incentive Plan, as amended (the Plan). All of the options have been granted at a price equal to or greater than the market price of the Company s stock on the date of grant. Substantially all stock option grants outstanding under the Plan vest ratably over three years and expire 10 years from the date of grant. In addition to the Plan, the Company gave employees the right to purchase shares at a discount to the market price under its employee stock purchase plan (ESPP). The ESPP expired on December 31, 2012, but at the Company s annual meeting held in December 2013, its stockholders approved a new ESPP for a one year period commencing January 1, 2014 (the 2014 ESPP). The new plan (2015 ESPP) was approved at the annual meeting held on June 25, 2014, which replaced the 2014 ESPP with a new ESPP that will run from July 1, 2014 through June 30, 2015, and will better correspond with the Company s annual meeting dates..

During the second quarter of 2010, the Company issued options to certain employees that vest upon achievement of certain financial objectives in combination with a minimum market price for its common stock during a five-year period (the Cliff Options). The Company assesses the probability of achieving these objectives at the end of each month and recognizes expense accordingly.

In addition to the Plan and the ESPPs, the Board of Directors grants restricted stock to non-employee directors under the Company s 2010 Non-Employee Director Stock Plan (the Directors Plan). Restricted stock granted to date under the Directors Plan vest 50% upon grant and 50% on the first anniversary of the grant date if the director is still serving on the Board of Directors on the vesting date.

The Company accounts for employee share-based awards in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 718. This pronouncement requires companies to measure the cost of employee service received in exchange for a share-based award

Table of Contents

based on the fair value of the award at the date of grant, with expense recognized over the requisite service period, which is generally equal to the vesting period of the grant.

The following table summarizes the Company s total share-based compensation expense for the three and six month periods ended June 30, 2014 and 2013 (in thousands):

	Three Months Ended June 30, 2014	Three Months Ended June 30, 2013	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013
Stock options	$ 6	$ 109	$ 13	$ 234
Restricted stock	54	85	166	142
Employee Stock Purchase Plan	5		12	
	$ 65	$ 194	$ 191	$ 376

The compensation expense to be recognized in future periods related to the Company s employee options and restricted stock is as follows (in thousands):

As of June 30, 2014	Unrecognized Compensation Expense	Weighted Average Remaining Life (in Months)
Stock options	$ 20	12.7
Restricted stock	$ 177	9.6

In addition, there was approximately $538 thousand of unrecognized expense related to the Cliff Options which may be recognized over the next 10 months, if vesting requirements are met.

Table of Contents

Note 3 Recent Accounting Pronouncements

In April 2014, the FASB issued Accounting Standards Update (ASU) 2014-08, Presentation of Financial Statements (Topic 205) and Property, Plant and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity. The amendments in ASU 2014-08 change the criteria for reporting a discontinued operation and require new disclosures of both discontinued operations and certain other disposals that do not meet the definition of a discontinued operation. Only disposals representing a strategic shift in operations should be presented as discontinued operations. This accounting standard update is effective for annual filings beginning on or after December 15, 2014. Early adoption is permitted. The impact of the adoption of ASU 2014-08 on the Company s results of operations, financial position, cash flows and disclosures will be based on the Company s future disposal activity.

In May 2014, the FASB issued ASU 2014-09, Revenue From Contracts With Customers. ASU 2014-09 supersedes nearly all existing revenue recognition under U.S. GAAP. The core principle of ASU 2014-09 is to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration the Company expects to be entitled to for those goods or services using a defined five step process. More judgment and estimates may be required to achieve this principle than under existing U.S. GAAP. ASU 2014-09 is effective for annual periods beginning after December 15, 2016, including interim periods therein, using either of the following transition methods: (i) a full retrospective approach reflecting the application of the standard in each prior reporting period with the option to elect certain practical expedients or (ii) a retrospective approach with the cumulative effect upon initial adoption recognized at the date of adoption which includes additional footnote disclosures. The Company is currently evaluating the impact of the adoption of ASU 2014-09 on the Company s consolidated financial statements and has not yet determined the method of adoption.

Note 4 Earnings Per Share

The Company computes income or loss per share under ACS 260 Earnings Per Share, which requires presentation of two amounts: basic and diluted loss per common share. Basic loss per common share is computed by dividing income or loss available to common stockholders by the number of weighted average common shares outstanding, and includes all common stock issued. Diluted earnings include all common stock equivalents. The Company has not included the outstanding options or warrants as common stock equivalents in the computation of diluted loss per share for the three and six months ended June 30, 2014 and 2013, because the effect would be anti-dilutive.

The following table sets forth the weighted average shares issuable upon exercise of outstanding options and warrants as of June 30, 2014:

Table of Contents

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Weighted average shares issuable upon exercise of outstanding options	363,423	468,454	354,411	471,650
Weighted average shares issuable upon exercise of outstanding warrants	1,798,384	697,200	1,745,283	697,200
Total	2,161,807	1,165,654	2,099,694	1,168,850

Note 5 GES-Port Charlotte (GESPC)

During 2010, the Company established Lime Energy Asset Development, LLC (LEAD), to develop, construct, operate and in certain situations own energy producing assets. On November 1, 2013, the Company sold GES-Port Charlotte to Green Gas Americas, Inc. (Green Gas or the Buyer). The sale was consummated pursuant to a Membership Interest Purchase Agreement (the Purchase Agreement), dated November 1, 2013, by and between LEAD, as the seller, and Green Gas, as the purchaser. The total purchase price paid for the membership interest was $3.3 million, less a $152,300 contribution on the part of the Seller toward the cost of wellfield improvements. The agreement also provides for a 5%, or $165,000, hold-back of the purchase price (the Hold-Back) to be held in escrow to cover the indemnification obligations of the seller and any additional pre-closing liabilities. The Hold-Back was reduced by $65,000 on February 2, 2014. After application by the Buyer to obligations of the Seller the balance at June 30, 2014 was $58,000 and included in Accounts Receivable. On August 6, 2014 the Hold-Back was reduced by $40,000 and the remaining $18,000 is scheduled for release on November 2, 2014. At June 30, 2014, the balance of the escrow of the Company provided typical indemnifications to the Buyer, including for breach of representations, third party claims, pre-closing liabilities, etc., all of which are capped at the total purchase price paid by the Buyer.

As part of the Purchase Agreement, Lime agreed to assume GESPC s obligation to Florida Power and Light (FP&L) for the cost of completing an interconnect between GESPC s facility and the FP&L s transmission system. This obligation totaled $400,000 as of November 1, 2013, and requires monthly payments of $50,000 to FP&L. The amount remaining under this obligation as of June 30, 2014 of $50,000 is included in accrued expenses on the consolidated balance sheets.

The Company recognized a $27,000 loss on the sale of GESPC. Upon the closing of the transaction, the Company repaid in full the term loan it used to fund the construction of the Zemel Road facility.

Note 6 Current Liability to Trade Creditor

In December 2012, one of the Company s major suppliers agreed to allow it to pay for approximately $5.3 million worth of purchases over a 23 month period. The balance of this liability was $1.5 million and $3.2 million as of June 30, 2014 and December 31, 2013, respectively.

Table of Contents

Note 7 Term Loan

On November 3, 2011, GES-Port Charlotte, LLC (GES), entered into a Loan Agreement with RBC Bank (USA) (RBC) (RBC was subsequently acquired by PNC Bank) under which GES borrowed $3.6 million (the Loan Agreement). The Loan Agreement was to mature on, and all outstanding balances were due and payable on, October 31, 2016. The Company sold GES on November 1, 2013, at which time it repaid the loan in full.

The Company had entered into an interest rate swap to fix the interest rate on $1.9 million of the principal amount of the term loan at 6.56% through October 2016. This interest rate swap was being carried at fair-market value on the Company s books, with changes in value included in interest expense. The swap was terminated on November 1, 2013, when the Company paid off the Term Loan.

Note 8 Conversion of Subordinated Debt and Sale of Series A Preferred Stock

On September 23, 2013, the Company entered into a Preferred Stock and Warrant Purchase Agreement (the Series A Purchase Agreement) with a group of investors including Mr. Richard Kiphart, the Company s Chairman and largest individual stockholder, and Mr. Christopher Capps, a member of its Board of Directors (collectively with the other investors, the Investors). Pursuant to the terms of the Series A Purchase Agreement, the Investors purchased 926,223 shares of the Company s Series A Preferred Stock (the Series A Preferred Shares) at a price per Preferred Share of $10.00. The purchase price was paid with (a) $2,500,000 in cash and (b) the exchange of $6,779,950 (principal amount and accrued interest) of the Company s Subordinated Secured Convertible Pay-In-Kind Note (the Notes), representing all of the outstanding Notes.

The Series A Preferred Shares are entitled to an accruing dividend of 12.5% per annum of their original issue price (subject to adjustment for stock splits, combinations and similar recapitalizations), payable semi-annually in arrears. Such dividends shall be paid in additional shares of Series A Preferred Stock at the original issue price (subject to adjustment for stock splits, combinations and similar recapitalizations) or, at the sole discretion of the Company s board of directors, in cash. The Company accrued dividends of $298 and $594 thousand on the Series A Preferred during the three and six month periods ended June 30, 2014, respectively. The accrued dividends were satisfied through the issuance of preferred stock on June 30, 2014.

The Series A Preferred Shares may be converted at the election of the holder of such shares, into shares of the Company s common stock at a conversion price which was initially equal to $3.78 per share (the Conversion Price). The Conversion Price is to be proportionately adjusted for stock splits, combinations and similar recapitalizations, and, subject to a floor of $3.50, shall be adjusted for future issuances of common stock (excluding certain issuances) at a price per share less than the Conversion Price on a broad based, weighted average basis. The Company can require conversion of the Series A Preferred Shares if the weighted average price for its common stock is at least two hundred percent (200%) of the Conversion Price for at least 20 trading days during a 30 trading day period ending within 5 trading days prior to the Company sending a notice of forced conversion to the holders of the Series A Preferred Shares. On December 30, 2013, as the result of the issuance of shares of series B convertible preferred stock, the Conversion Price of the Series A Preferred Shares was reduced to $3.58 per share. The Conversion Price was further reduced to $3.51 per share on February 4, 2014, when the Company issued additional shares of series B convertible preferred stock resulting in a $178 thousand non-cash deemed dividend. The deemed dividend was calculated as the increase in the value of the shares into which the Series A would be convertible resulting from the adjustment to the conversion price, based on

11

Table of Contents

the market price of our common stock on the date of the adjustment. This deemed dividend was recorded to dividend expense, with an offset to the accumulated paid in capital.

The Company may redeem all or a portion of the Series A Preferred Shares at its option at any time unless prohibited by Delaware law governing distributions to stockholders. The redemption price for each Series A Preferred Share shall be its original issue price (subject to adjustment for stock splits, combinations and similar recapitalizations) plus any accrued but unpaid dividends multiplied by a factor based on the date the notice of such redemption is sent to holders of the Series A Preferred Shares. If such notice is sent before the first anniversary of the issuance of the Series A Preferred Shares, the factor shall be 103%, if thereafter but before the second such anniversary, the factor shall be 102%, if thereafter but before the third such anniversary, the factor shall be 101% and thereafter, the factor shall be 100%.

The Company used the cash proceeds from the sale of the Series A Preferred Shares for general corporate purposes.

Note 9 Subordinated Convertible Term Notes

On October 22, 2012, the Company entered into a Convertible Note and Warrant Purchase Agreement (the Sub Debt Purchase Agreement) with a group of investors including Mr. Richard Kiphart, the Company s Chairman and largest individual stockholder, and Mr. Christopher Capps, a member of its Board of Directors (collectively with the other investors, the Holders). Pursuant to the terms of the Sub Debt Purchase Agreement, the Holders lent the Company $6,050,000 under a Subordinated Secured Convertible Pay-In-Kind Note (the Notes). The Notes had a term of five years, accrued interest at the rate of 12-1/2% per year, payable semi-annually at the Company s election in cash or additional Notes. On September 23, 2013, the Notes and all accrued interest were converted to shares of Series A Preferred Stock (see Note 8 for additional information regarding the Series A Preferred Stock).

In connection with the entry into the Sub Debt Purchase Agreement, the Company issued the Holders warrants to purchase 644,991 shares of its common stock at $4.69 per share (the Sub Debt Warrants). These warrants expire on the fifth anniversary of their issuance and contain a cashless exercise option. The Company determined the value of the Sub Debt Warrants to be $1.4 million using a trinomial option pricing model.

In recording the transaction, the Company allocated the value of the proceeds to the Notes and Sub Debt Warrants based on their relative fair values. In doing so, it determined that the Notes contained a beneficial conversion feature since the fair market value of the common stock issuable upon conversion of the Notes (determined on the Note issuance date) exceeded the value allocated to the Notes of $4,924,000. The Notes were convertible into 1,179,912 shares of common stock, which at the market price of $4.48 per share on date of issuance of the Notes was worth $5,286,000. The difference of $362,000 between the market value of the shares issuable upon conversion and the value allocated to the Notes was considered to be the value of the beneficial conversion feature.

The value of the beneficial conversion feature and the value of the warrants were recorded as a discount to the Notes, which was being amortized over the term of the Notes using the effective interest method. Amortization of the discount of $66 thousand was included in interest expense for the three-month period ended March 31, 2013. Upon the conversion of the Notes to preferred stock in September 2013, the remaining unamortized discount of $1.2 million was recorded to interest expense.

Table of Contents

The Company incurred costs of approximately $37,000 to issue the Notes. These costs were capitalized and were also being amortized over the term of the Notes using the effective interest method. Amortization of the deferred issuance costs of $3 thousand was included in interest expense for the six-month period ended June 30, 2013. Upon the conversion of the Notes to preferred stock in September 2013, the balance of the deferred issuance costs of $30,000 was recorded to interest expense.

The Company elected to pay the interest accrued through September 23, 2013, of $712,000 in additional Notes. The Notes issued in satisfaction of the accrued interest were also converted to shares of preferred stock on September 23, 2013 (see Note 8 for additional information regarding the Series A Preferred Stock).

Note 10   Sale of Series B Preferred Stock

On December 30, 2013, the Company entered into a Preferred Stock and Warrant Purchase Agreement (the   Series B Purchase Agreement   ) with a group of Series B Investors including Mr. Richard Kiphart, the Company   s Chairman and largest individual stockholder (collectively with the other investors, the   Series B Investors   ). Pursuant to the terms of the Series B Purchase Agreement, the Series B Investors purchased 400,000 shares of the Company   s Series B Preferred Stock (the   Series B Preferred Shares   ) at a price per Series B Preferred Share of $10.00.

On January 29, 2014, the Company entered into a Series B Purchase Agreement with Greener Capital Partners Fund II, L.P. (the   Greener Capital   ), pursuant to which Greener Capital has purchased an aggregate of 200,000 shares of the Company   s Series B Preferred Shares at a price per Preferred Share of $10.00. Greener Capital funded the purchase and the transaction closed on February 4, 2014.

The Series B Preferred Shares are entitled to an accruing dividend of 12.5% per annum of their original issue price (subject to adjustment for stock splits, combinations and similar recapitalizations), payable semi-annually in arrears. Such dividends shall be paid in additional shares of Series B Preferred Stock at the original issue price (subject to adjustment for stock splits, combinations and similar recapitalizations) or, at the sole discretion of the Company   s board of directors, in cash. The Company accrued dividends of $188 and $349 thousand on the Series B Preferred during the three and six month periods ended June 30, 2014, respectively. The accrued dividends were satisfied through the issuance of preferred stock on June 30, 2014.

The Series B Preferred Shares may be converted, at any time following the approval of such conversion by the Company   s stockholders, at the election of the holder of such shares, into shares of the Company   s common stock at a conversion price which was initially equal to $2.83 per share (the   Conversion Price   ). The Conversion Price shall be proportionately adjusted for stock splits, combinations and similar recapitalizations, and, subject to a floor of $2.50, shall be adjusted for future issuances of common stock (excluding certain issuances) at a price per share less than the Conversion Price on a broad based, weighted average basis. The Company can require conversion of the Series B Preferred Shares if the weighted average price for its common stock is at least two hundred percent (200%) of the Conversion Price for at least 20 trading days during a 30 trading day period ending within 5 trading days prior to the Company sending a notice of forced conversion to the holders of the Series B Preferred Shares.

The Company may redeem all or a portion of the Series B Preferred Shares at its option at any time, unless prohibited by Delaware law governing distributions to stockholders. The redemption price for each Series B Preferred Share shall be its original issue price (subject to adjustment for stock splits,

13

Table of Contents

combinations and similar recapitalizations) plus any accrued but unpaid dividends multiplied by a factor based on the date the notice of such redemption is sent to holders of the Series B Preferred Shares. If such notice is sent before the first anniversary of the issuance of the Series B Preferred Shares, the factor shall be 103%, if thereafter but before the second such anniversary, the factor shall be 102%, if thereafter but before the third such anniversary, the factor shall be 101% and thereafter, the factor shall be 100%.

In connection with the entry into the Series B Purchase Agreement, the Company issued the Series B Investors warrants to purchase 848,058 shares of its common stock at $2.83 per share (the Series B Warrants). These warrants expire on the fifth anniversary of their issuance and contain a cashless exercise option. The Warrants may not be exercised until the Company s common stockholders approve the exercise of the Warrants.

In recording the Series B transactions, the Company allocated the value of the proceeds to the Series B Preferred Shares and the Series B Warrants based on their relative fair values. In doing so, it determined that the Series B Preferred Shares contained a beneficial conversion feature. The value of the beneficial conversion feature, along with the value of the warrants, where both considered to be non-cash deemed dividends and were recorded to dividend expense, with an offsetting entry to additional paid in capital in the period in which the Series B Preferred was issued. Dividend expense for the six-month period ended June 30, 2014, contains $832 thousand of such deemed dividends.

The Series B Purchase Agreement requires that the Company seek stockholder approval of the conversion of the Series B Preferred Shares and the exercise of the Series B Warrants on or before July 31, 2014. The Company received such approval at its annual meeting of stockholders held on June 25, 2014.

The Company used the cash proceeds from the sale of the Series B Preferred Shares for general corporate purposes.

Note 11 Sale of ESCO Business

On February 28, 2013, the Company sold its ESCO business to Powersecure, Inc., a wholly-owned subsidiary of PowerSecure International, Inc. (Powersecure). The ESCO business, which represented the largest portion of the Company s public sector business, designed, installed and maintained energy conservation measures, primarily as a subcontractor to large energy service company providers (ESCOs), for the benefit of public sector, commercial, industrial and institutional customers as end users. The sale was structured as an asset sale. The total purchase price for the assets sold was $4.0 million in cash, subject to a working capital adjustment, and the assumption of approximately $9.8 million of liabilities, comprising certain other debts, liabilities and obligations relating to the acquired business and assumed contracts. After application of the working capital adjustment in accordance with the Purchase Agreement, the cash purchase price is approximately $1.9 million, subject to post-closing confirmation of the working capital adjustment, resulting in an effective purchase price, including the assumption of liabilities, of approximately $11.7 million. In connection with the acquisition of the ESCO business, PowerSecure assumed certain unfinished contracts and projects in the acquired business, along with the accounts receivables and accounts payables associated with those projects.

During the fourth quarter of 2012, utilizing the purchase price received for the sale of the ESCO business as an indication of its fair market value, the Company determined that its carrying value associated with the business exceeded the fair market value by approximately $3.2 million. Accordingly, it reduced the carrying value to the fair market value, recording a $3.2 million impairment loss in the process.

Table of Contents

After adjusting the carrying value of the assets during the fourth quarter of 2012, the net carrying value of the assets and liabilities of the ESCO business was equal to the proceeds received for the sale of the business on February 28, 2013, therefore there was no gain or loss resulting from the sale recorded during the first quarter of 2013. However, the Asset Purchase Agreement provided that within 90 days of the closing the seller provide the buyer a final calculation of the Closing Net Working Capital as of February 28, 2013. To the extent that this calculation showed an increase in the Closing Net Working Capital from the amount estimated on the closing date, the buyer would owe the seller an amount equal to the increase and to the extent the Closing Net Working Capital was less than the amount estimated on the closing date, the seller would owe the buyer an amount equal to the reduction. The calculation of the final Closing Net Working Capital was completed in August 2013 and it was determined that the buyer owed the seller an additional $128 thousand. This additional consideration was included in income from discontinued operations during the quarter ended September 30, 2013.

Note 12 Discontinued Operations

As discussed in Note 11, the Company sold the majority of its public sector business on February 28, 2013 to Powersecure. During the third quarter of 2013, the Company s board of directors authorized management to sell or dispose of GES-Port Charlotte, its contract with the Army Corp. of Engineers under the Federal Renewal and Renovation program (the FRR contract), and the regional service business located in Bethlehem, Pennsylvania. These businesses, along with the remaining public sector business, which the Company is in the process of exiting, and Asset Development business, which the Company shut down at the end of 2012, have all been reported as discontinued operations in the accompanying financial statements.

The revenue and operating profit (loss) related to discontinued operations were as follows (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	**2013**	**2014**	**2013**
Revenue	$ 43	$ 1,029	$ 183	$ 4,472
Operating profit (loss)	$ 55	$ (128)	$ 52	$ (3,176)

The assets and liabilities related to discontinued operations were as follows (in thousands):

Table of Contents

	June 30, 2014	December 31, 2013
Accounts receivable	$ 1,124	$ 2,423
Costs and estimated earnings in excess of billings on uncompleted contracts	1,021	1,019
Total current assets	2,145	3,442
Total Assets	$ 2,145	$ 3,442
Accounts payable	$ 807	$ 2,240
Accrued Expenses	227	504
Billings in excess of costs and estimated earnings on uncompleted contracts	360	460
Customer deposits	41	41
Total current liabilities	1,435	3,245
Total Liabilities	$ 1,435	$ 3,245

Note 13 Business Segment Information

With the sale of the public sector business and renewable energy business during 2013, all of the Company s remaining operations are focused on one business segment, its energy efficiency segment.

Note 14 Other Equity Issuances

During three and six months ended June 30, 2014, the Company granted 0 and 34,250 shares, respectively, of restricted stock to its outside directors pursuant to the 2010 Non-Employee Directors Stock Plan as compensation for their service on the Board. The shares granted under the 2010 Non-Employee Directors Stock Plan vest 50% upon grant and 50% on the first anniversary of the grant date if the director is still serving on the Company s board of directors on the vesting date. The Company also issued 25,157 shares of restricted stock to its Chief Executive Officer and 5,000 shares to its Chief Financial Officer pursuant to its 2008 Employee Long-term Incentive Plan. These shares vest one-third on each of December 31, 2014, 2015 and 2016, if the holder is still an employee of the Company on the vesting date.

Note 15 Letter of Credit Agreement

On December 7, 2012, the Company entered into a Letter of Credit Agreement (the Agreement) with Richard P. Kiphart, the Company s Chairman and largest individual stockholder. Pursuant to the Agreement, Mr. Kiphart agreed to cause the issuance of one or more Letters of Credit (collectively, the Letter of Credit) for the benefit of a surety at the Company s request, up to an aggregate amount of $1,000,000. The Letter of Credit is being used to support the issuance of performance bonds required by certain of the Company s contracts with Public Sector customers. Mr. Kiphart s obligation to cause the issuance of, or leave in place, the Letter of Credit was to terminate on December 7, 2013, however he has

16

Table of Contents

agreed to extend his support for outstanding Letters of Credit until the projects they are associated with are completed sometime in 2014.

The Company has agreed to indemnify Mr. Kiphart for any liability in connection with any payment or disbursement made under the Letter of Credit. The Company will also pay all of Mr. Kiphart s fees and out-of-pocket expenses incurred in connection with the Letter of Credit. All such indemnification, fees and expenses will be payable by the Company within ten business days of the Company s receipt of Mr. Kiphart s written demand.

Note 16 Commitments and Contingencies

The Company carries Directors and Officers insurance with an aggregate limit of $10 million, which it anticipates will cover the cost of defending an existing class action suit and derivative action and any related awards or settlements, up to the limit of the policy. At this point in the legal process, the Company estimates that its reasonably possible costs, over and above the amounts covered by insurance, of responding to these lawsuits, responding to the SEC investigation and completing its internal investigation and restatement will be between $6.5 million and $7.0 million, of which $6.0 million had been incurred through June 30, 2014. There are many factors that could cause the actual costs to exceed or be less than this estimate; therefore the Company has not accrued for these potential future costs.

Note 17 Legal Matters

Satterfield v. Lime Energy Co. et al., Case No. 12-cv-5704 (N.D. Ill.): This is a putative class action on behalf of purchasers of our securities between May 14, 2008 and December 27, 2012, inclusive. Following an announcement by us dated July 17, 2012, four separate putative class actions were filed alleging violations of the federal securities laws and naming as Defendants the Company and two of its officers, John O Rourke and Jeffrey Mistarz. The four cases were consolidated.

Pursuant to the Private Securities Litigation Reform Act of 1995 (the PSLRA), on October 26, 2012, the Court appointed Lead Plaintiffs. Lead Plaintiffs filed a Consolidated Amended Class Action Complaint on January 18, 2013, alleging that Defendants issued false and misleading statements concerning Lime Energy s revenues during the class period and thereby artificially inflated our stock price. On January 21, 2014, following several months of arm s length negotiations, the Lead Plaintiffs and Defendants entered into a stipulation of settlement under which this matter would be fully and finally settled. As part of the settlement, Defendants agreed to cause $2.5 million to be paid into a settlement fund, which $2.5 million has been provided by the Company s directors and officers liability insurers. On January 28, 2014, Judge Sara Ellis entered an order granting preliminary approval of the class action settlement and notice to the settlement class in the matter. On June 4, 2014, Judge Sara Ellis entered an order granting final approval of the class action settlement and notice to the settlement class in the matter *Satterfield v. Lime Energy Co. et al.*, Case No. 12-cv-05704.

Kuberski v. Lime Energy Co. et al., Case No. 12-cv-7993 (N.D. Ill.): This is a putative shareholder derivative action alleging that certain of our officers and directors breached their fiduciary duties to the Company from May 14, 2008 through the present by failing to maintain adequate internal controls and causing the Company to issue false and misleading statements concerning our revenues. An initial derivative complaint was filed on October 5, 2012. A second derivative action was filed on March 5, 2013. The two cases were consolidated and the Court appointed Lead Counsel for the Plaintiffs on April 9, 2013. On May 9, 2013, the Plaintiffs filed a Verified Consolidated Shareholder Derivative Complaint. On June 10, 2013, Defendants filed a motion to dismiss for failure to make a demand on the

Table of Contents

Board of Directors of the Company or to adequately plead why demand should be excused, as required by Rule 23.1 of the Federal Rules of Civil Procedure and Delaware law. Briefing on the motion to dismiss was completed as of July 22, 2013. On March 25, 2014, the Court granted Defendants motion to dismiss and dismissed the case with prejudice. On April 22, 2014, Plaintiffs filed a motion for reconsideration of the Court s ruling. On June 25, 2014 the Court denied the Plaintiffs motion for reconsideration.

SEC Investigation: The SEC is conducting an investigation of our revenue recognition practices and financial reporting. On September 11, 2012, the Commission issued a subpoena for documents. On July 25, 2014, the SEC asked for some additional documentation and asked to schedule three interviews. We are cooperating with the Commission s investigation.

In accordance with ASC 450, Contingencies, and related guidance, we record reserves for estimated losses relating to claims and lawsuits when available information indicates that a loss is probable and the amount of the loss, or range of loss, can be reasonably estimated. The Company expenses legal costs as they are incurred. We are not aware of pending claims or assessments, other than as described above, which may have a material adverse impact on our liquidity, financial position, results of operations, or cash flows.

Note 18 Subsequent Events

On July 29, 2014, the Company announced that it has been awarded a contract by Duke Energy Business Services (Duke Energy) for a small business energy saver program. As previously disclosed, the program targets small business customers in the Carolinas with an average electric demand of 100 kW or less. Pending regulatory approval, this new award would expand the program to a broader territory in North and South Carolina and would extend the program for five years. Among other things, the Company would perform energy usage and equipment assessments of small business facilities and would perform upgrades to those facilities through its network of contractors. The actual impact of this award on the Company s revenues would depend on the receipt of certain regulatory approvals and the Company s ability to sell sufficient program services.

On August 1, 2014, the Company entered into a Letter of Credit Agreement (the LOC Agreement) with Richard P. Kiphart, the Company s Chairman and largest individual stockholder. Pursuant to the LOC Agreement, Mr. Kiphart agreed to cause the issuance of one or more Letters of Credit (collectively, the Kiphart Letter of Credit) for the benefit of a surety at the Company s request, up to an aggregate amount of $1,300,000. The Kiphart Letter of Credit is being used to guarantee certain obligations of the Company in connection with its performance under the Company s contract with Duke Energy. Mr. Kiphart s obligation to cause the issuance of, or leave in place, the Kiphart Letter of Credit will terminate on December 31, 2019. The Company has agreed to indemnify Mr. Kiphart for any liability in connection with any payment or disbursement made under the Kiphart Letter of Credit. The Company will also pay all of Mr. Kiphart s fees and out-of-pocket expenses incurred in connection with the Kiphart Letter of Credit. All such indemnification, fees and expenses will be payable by the Company within ten business days of the Company s receipt of Mr. Kiphart s written demand.

Pursuant to the LOC Agreement, the Company issued to Mr. Kiphart a warrant (the LOC Warrant) to purchase 50,000 shares of the Company s common stock as consideration for his obligations under the LOC Agreement. The LOC Warrant will be issued between August 11, 2014 and August 13, 2014 at an exercise price of the closing bid price of our stock at the date of issuance. The LOC Warrant has a five year term and may be exercised on a cashless basis at Mr. Kiphart s election. In addition, the Company

18

has agreed to pay to Mr. Kiphart simple interest at six percent per annum on the aggregate amount of the Kiphart Letter of Credit.

On August 4, 2014, the Company entered into a Subscription Agreement (the Subscription Agreement) with a group of investors including Mr. Richard Kiphart (collectively with the other investors, the Note Holders). Pursuant to the terms of the Subscription Agreement, the Note Holders lent to the Company $1,000,000 under Subordinated Secured Convertible Pay-In-Kind Notes (the 2014 Notes). The 2014 Notes have a term of ten years and will accrue interest at the rate of 12-1/2% per year, payable semi-annually at the Company s election in cash or additional 2014 Notes.

The Note Holders are entitled to convert the 2014 Notes at any time, at their election, into shares of the Company s common stock at the Conversion Price (as such term is defined in the 2014 Notes). The Company can require conversion of the 2014 Notes if the weighted average price for the its common stock (i) during the period commencing on the issuance date and terminating on the first anniversary of the issuance date, is at least two hundred percent (200%) of the Conversion Price for at least 20 trading days during a 30-trading day period ending within five trading days prior to the Company sending a notice of forced conversion to the holders of the 2014 Notes, or (ii) during the period commencing on the day following the first anniversary of the issuance date and terminating on the maturity date, is at least one hundred seventy-five percent (175%) of the Conversion Price for at least 20 trading days during a 30-trading day period ending within five trading days prior to the Company sending a forced conversion notice to the holders of the 2014 Notes. The number of shares the Company shall be obligated to issue will be limited such at it would not violate any requirements of any exchange upon which it might be listed at the time of the conversion.

The Note Holders can require that the Company redeem all or any portion of the 2014 Notes upon the occurrence of a Trigger Event. Trigger Events include (i) failure to have sufficient authorized shares at any time following the 60th day after issuance, (ii) failure to pay any amount of principal, interest or other amounts when and as due under the 2014 Notes, (iii) if the Company voluntarily or involuntarily seeks protection under bankruptcy laws, or (iv) if the Company breaches any representation, warranty or covenant or other term or condition of any transaction document. The Company is required to redeem the 2014 Notes upon a Change of Control (as such term is defined in the 2014 Notes) at the Change of Control Premium. The Change of Control Premium is defined as (i) 130% from the issuance date through the second anniversary of the issuance date, (ii) 120% after the second anniversary of the issuance date through the fourth anniversary of the issuance date and (iii) 100% thereafter. Under the terms of the Subscription Notes, the Company covenants not to (i) redeem debt that is subordinated to the 2014 Notes, or (ii) redeem, repurchase or declare or pay a cash dividend or distribution on its capital stock. The 2014 Notes are subordinated to (i) all commercial loans or other credit facilities that are or will be secured by all or substantially all of the assets of the Company and that have been approved by the Company s Board of Directors as senior in rank to the 2014 Notes and (ii) any and all obligations to the issuers of surety bonds and performance bonds for which the Company or any of its subsidiaries is the principal obligor.

The Company intends to use the proceeds from the issuance of the 2014 Notes for general corporate purposes.

Table of Contents

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

You should read the following discussion regarding the Company along with our financial statements and related notes included in this quarterly report. This quarterly report, including the following discussion, contains forward-looking statements that are subject to risks, uncertainties and assumptions. Our actual results, performance and achievements in 2014 and beyond may differ materially from those expressed in, or implied by, these forward-looking statements. See Cautionary Note Regarding Forward-Looking Statements.

Overview

We are a leader in designing and implementing energy efficiency programs that enable our utility clients to reach their underserved markets and achieve their energy reduction goals. Utility-sponsored energy efficiency programs help reduce customer demand for electricity. Using less electricity when demand is high (like on a hot summer day) can mean fewer new power plants and a smaller electric distribution system, which saves money and benefits the environment. We offer utilities energy efficiency program delivery services targeted to their small and medium-sized business customers. Our programs help these businesses use less energy through the upgrade of existing equipment with new, more energy efficient equipment. This service allows the utility to delay investments in transmission and distribution upgrades and new power plants, while at the same time providing benefits to their clients in the form of lower energy bills, improved equipment reliability, reduced maintenance costs and a better overall operating environment.

Our eight energy efficiency programs operate exclusively within the utility sector and our clients include two of the five largest investor-owned utilities in the country. We focus on deploying direct install energy efficiency solutions for small and mid-size commercial and industrial business programs that improve energy efficiency, reduce energy-related expenditures and lessen the impact of energy use on the environment. Currently, these solutions include energy efficient lighting upgrades and energy efficient mechanical upgrades. We also have expertise in water conservation, building controls, refrigeration and facility weatherization. We are prepared to offer these measures should they become eligible within a utility program. Our small business direct install (SBDI) programs provide a cost-effective avenue for our utility clients to offer products and services to a hard-to-reach customer base, while satisfying aggressive state-mandated energy reduction goals. Our direct install model is a turnkey solution under which we contract with our utility clients to design and market their small and mid-size energy efficiency programs within a defined territory, perform the technical audits, sell the solution to the end-use customer and oversee the implementation of the energy efficiency measures. This model makes it easy and affordable for small businesses to upgrade to new, more energy efficient equipment.

Events Impacting Future Results

On July 29, 2014, the Company announced that it has been awarded a contract by Duke Energy for a small business energy saver program. As previously disclosed, the program targets small business

Table of Contents

customers in the Carolinas with an average electric demand of 100 kW or less. Pending regulatory approval, this new award would expand the program to a broader territory in North and South Carolina and would extend the program for five years. Among other things, the Company would perform energy usage and equipment assessments of small business facilities and would perform upgrades to those facilities through its network of contractors. The actual impact of this award on the Company s revenues would depend on the receipt of certain regulatory approvals and the Company s ability to sell sufficient program services.

Results of Operations

Revenue

We generate the majority of our revenue from the sale of our services and the products that we purchase and resell to our clients. We charge our clients based upon an agreed to rate schedule based on the item installed or the savings generated. A typical project for a small business utility client can take anywhere from a few hours to a few weeks to complete.

Gross Profit

Gross profit equals our revenue less costs of sales. The cost of sales for our business consists primarily of materials, our internal labor, including engineering, and the cost of subcontracted labor.

Gross profit is a key metric that we use to evaluate our performance. Gross profit depends in large part on the volume and mix of products and services that we sell during any given period.

Selling, General and Administrative Expenses

Selling, general and administrative expenses (SG&A) include the following components:

- direct labor and commission costs related to our employee sales force;
- costs of our non-production management, supervisory and staff salaries and employee benefits, including the costs of share-based compensation;

- costs related to insurance, travel and entertainment, office supplies and utilities;
- costs related to marketing and advertising our products;
- legal and accounting expenses; and
- costs related to administrative functions that serve to support our existing businesses, as well as to provide the infrastructure for future growth.

Amortization of Intangibles

When we acquire companies we allocate the purchase price to tangible assets (such as property, equipment, accounts receivable, etc.), and identifiable intangible assets (such as contract backlogs, customer lists, technology, trade name, etc.), with the balance recorded as goodwill. We amortize the value of certain intangible assets over their estimated useful lives as a non-cash expense.

Table of Contents

Interest Expense, Net

Net interest expense consists of interest expense net of interest income. Net interest expense represents the interest costs associated with our subordinated convertible term notes (including amortization of the related debt discount and issuance costs). Interest income includes earnings on our invested cash balances and amortization of the discount on our long-term receivables.

Three months Ended June 30, 2014 Compared to Three months Ended June 30, 2013