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 September 30, 2019

or

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

For the transition period from ________to________
Commission file number 001-35944

POWER SOLUTIONS INTERNATIONAL, INC.
(Exact Name of Registrant as Specified in its Charter)

Delaware	**33-0963637**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
201 Mittel Drive, Wood Dale, IL	**60191**
(Address of Principal Executive Offices)	(Zip Code)

(630) 350-9400
(Registrant's Telephone Number, Including Area Code)

Securities Registered Pursuant to Section 12(b) of the Act:

Title of Each Class	Trading Symbol(s)	Name of Each Exchange on Which Registered
None	___	___

Securities Registered Pursuant to Section 12(g) of the Act:
Common Stock, par value $0.001 per share

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). YES x NO ☐

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

Large accelerated filer	☐	Accelerated filer	☐
Non-accelerated filer	x	Smaller reporting company	x
		Emerging growth company	☐

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

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

As of April 22, 2020, there were 22,857,602 outstanding shares of the Common Stock of the registrant.

TABLE OF CONTENTS

FORWARD-LOOKING STATEMENTS

Certain statements contained in this Quarterly Report on Form 10-Q ("Quarterly Report") that are not historical facts are intended to constitute "forward-looking statements" entitled to the safe-harbor provisions of Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). These statements may involve risks and uncertainties. These statements often include words such as "anticipate," "believe," "budgeted," "contemplate," "estimate," "expect," "forecast," "guidance," "may," "outlook," "plan," "projection," "should," "target," "will," "would" or similar expressions, but these words are not the exclusive means for identifying such statements. These forward-looking statements include statements regarding Power Solutions International, Inc.'s, a Delaware corporation, ("Power Solutions," "PSI," or the "Company") projected sales and potential profitability, strategic initiatives, future business strategies, warranty mitigation efforts and market opportunities, improvements in its business, remediation of internal controls, improvement of product margins, and product market conditions and trends. These statements are not guarantees of performance or results, and they involve risks, uncertainties and assumptions. Although the Company believes that these forward-looking statements are based on reasonable assumptions, there are many factors that could affect the Company's results of operations and could cause actual results, performance or achievements to differ materially from those expressed in, or implied by, the Company's forward-looking statements.

The Company cautions that the risks, uncertainties and other factors that could cause its actual results to differ materially from those expressed in, or implied by, the forward-looking statements include, without limitation, the factors discussed in the Company's Annual Report on Form 10-K for the year ended December 31, 2018, and from time to time in the Company's subsequent filings with the United States Securities and Exchange Commission (the "SEC"); management's ability to successfully implement the Audit Committee's remedial recommendations; the timing of completion of steps to address, and the inability to address and remedy, material weaknesses; the identification of additional material weaknesses or significant deficiencies; variances in non-recurring expenses; risks relating to the substantial costs and diversion of personnel's attention and resources deployed to address the financial reporting and internal control matters; the ability of the Company to accurately budget for and forecast sales, and the extent to which sales result in recorded revenues; changes in customer demand for the Company's products; volatility in oil and gas prices, the impact of U.S. tariffs on imports from China on the Company's supply chain to source products; the impact of the investigations being conducted by the SEC, and the criminal division of the United States Attorney's Office for the Northern District of Illinois (the "USAO") and any related or additional governmental investigative or enforcement proceedings; any delays and challenges in recruiting key employees consistent with the Company's plans; the impact the recent outbreak of a new strain of coronavirus ("COVID-19 outbreak") could have on the Company's business and financial results; any negative impacts from delisting of the Company's common stock par value $0.001 (the "Common Stock") from the NASDAQ Stock Market ("NASDAQ") and any delays and challenges in obtaining a re-listing on a stock exchange.

The Company's forward-looking statements are presented as of the date hereof. Except as required by law, the Company expressly disclaims any intention or obligation to revise or update any forward-looking statements, whether as a result of new information, future events or otherwise.

AVAILABLE INFORMATION

The Company is subject to the reporting and information requirements of the Exchange Act, and as a result, it is obligated to file annual, quarterly and current reports, proxy statements and other information with the SEC. The Company makes these filings available free of charge on its website (http://www.psiengines.com) as soon as reasonably practicable after it electronically files them with, or furnishes them to, the SEC. Information on the Company's website does not constitute part of this Quarterly Report on Form 10-Q. In addition, the SEC maintains a website (http://www.sec.gov) that contains the annual, quarterly and current reports, proxy and information statements, and other information the Company electronically files with, or furnishes to, the SEC.

PART I – FINANCIAL INFORMATION

Item 1. Financial Statements.

POWER SOLUTIONS INTERNATIONAL, INC.
CONSOLIDATED BALANCE SHEETS
(UNAUDITED)

(in thousands, except par values)	As of September 30, 2019	As of December 31, 2018
ASSETS		
Current assets:		
Cash and cash equivalents	$ 1	$ 54
Accounts receivable, net of allowances of $3,796 and $2,596 as of September 30, 2019 and December 31, 2018, respectively	77,209	86,471
Income tax receivable	973	973
Inventories, net	114,675	105,614
Prepaid expenses and other current assets	17,685	22,917
Total current assets	210,543	216,029
Property, plant and equipment, net	23,468	24,266
Intangible assets, net	14,281	17,010
Goodwill	29,835	29,835
Other noncurrent assets	25,242	2,742
TOTAL ASSETS	$ 303,369	$ 289,882
LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)		
Current liabilities:		
Accounts payable	$ 86,305	$ 85,218
Current maturities of long-term debt	186	80
Revolving line of credit	36,756	54,613
Warrant liability	—	35,100
Other accrued liabilities	57,802	45,700
Total current liabilities	181,049	220,711
Deferred income taxes	617	647
Long-term debt, net of current maturities	55,704	55,088
Noncurrent contract liabilities	12,622	14,611
Other noncurrent liabilities	33,100	17,403
TOTAL LIABILITIES	$ 283,092	$ 308,460
STOCKHOLDERS' EQUITY (DEFICIT)		
Preferred stock – $0.001 par value. Shares authorized: 5,000. No shares issued and outstanding at all dates.	$ —	$ —
Common stock – $0.001 par value; 50,000 shares authorized; 23,117 and 19,067 shares issued; 22,856 and 18,638 shares outstanding at September 30, 2019 and December 31, 2018, respectively	23	19
Additional paid-in capital	165,380	126,412
Accumulated deficit	(134,988)	(135,160)
Treasury stock, at cost, 261 and 429 shares at September 30, 2019 and December 31, 2018, respectively	(10,138)	(9,849)
TOTAL STOCKHOLDERS' EQUITY (DEFICIT)	20,277	(18,578)
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)	$ 303,369	$ 289,882

See Notes to Consolidated Financial Statements

POWER SOLUTIONS INTERNATIONAL, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

(UNAUDITED)

(in thousands, except per share amounts)	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2019	**2018**	**2019**	**2018**
Net sales	$ 138,512	$ 136,318	$ 392,983	$ 357,804
Cost of sales	111,640	117,510	322,793	311,056
Gross profit	26,872	18,808	70,190	46,748
Operating expenses:				
Research, development and engineering expenses	6,366	7,708	18,695	20,691
Selling, general and administrative expenses	11,461	16,374	41,476	42,904
Amortization of intangible assets	910	1,321	2,729	3,687
Total operating expenses	18,737	25,403	62,900	67,282
Operating income (loss)	8,135	(6,595)	7,290	(20,534)
Other expense:				
Interest expense	1,921	1,974	6,156	5,425
Loss from change in value and exercise of warrants	—	10,200	1,352	19,200
Other income, net	(25)	(68)	(526)	(257)
Total other expense	1,896	12,106	6,982	24,368
Income (loss) before income taxes	6,239	(18,701)	308	(44,902)
Income tax expense (benefit)	483	118	136	(74)
Net income (loss)	$ 5,756	$ (18,819)	$ 172	$ (44,828)
Weighted-average common shares outstanding:				
Basic	22,849	18,625	21,064	18,567
Diluted	22,876	18,625	21,088	18,567
Earnings (loss) per common share:				
Basic	$ 0.25	$ (1.01)	$ 0.01	$ (2.41)
Diluted	$ 0.25	$ (1.01)	$ 0.01	$ (2.41)

See Notes to Consolidated Financial Statements

POWER SOLUTIONS INTERNATIONAL, INC.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(UNAUDITED)

(in thousands)	For the Three Months Ended				
	Common Stock	**Additional Paid-in Capital**	**Accumulated Deficit**	**Treasury Stock**	**Total Stockholders' Equity**
Balance at June 30, 2019	$ 23	$ 165,437	$ (140,744)	$ (10,325)	$ 14,391
Net income	—	—	5,756	—	5,756
Stock-based compensation expense	—	(14)	—	187	173
Payment of withholding taxes for net settlement of stock-based awards	—	(43)	—	—	(43)
Balance at September 30, 2019	$ 23	$ 165,380	$ (134,988)	$ (10,138)	$ 20,277
Balance at June 30, 2018	$ 19	$ 125,272	$ (106,443)	$ (9,923)	$ 8,925
Net loss	—	—	(18,819)	—	(18,819)
Stock-based compensation expense	—	586	—	(41)	545
Payment of withholding taxes for net settlement of stock-based awards	—	80	—	—	80
Balance at September 30, 2018	$ 19	$ 125,938	$ (125,262)	$ (9,964)	$ (9,269)

(in thousands)	For the Nine Months Ended				
	Common Stock	**Additional Paid-in Capital**	**Accumulated Deficit**	**Treasury Stock**	**Total Stockholders' Equity**
Balance at December 31, 2018	$ 19	$ 126,412	$ (135,160)	$ (9,849)	$ (18,578)
Net income	—	—	172	—	172
Stock-based compensation expense	—	1,390	—	(289)	1,101
Payment of withholding taxes for net settlement of stock-based awards	—	(486)	—	—	(486)
Exercise of Weichai Warrant	4	38,064	—	—	38,068
Balance at September 30, 2019	$ 23	$ 165,380	$ (134,988)	$ (10,138)	$ 20,277
Balance at December 31, 2017	$ 19	$ 123,838	$ (82,147)	$ (9,538)	$ 32,172
Net loss	—	—	(44,828)	—	(44,828)
Stock-based compensation expense	—	2,389	—	(426)	1,963
Payment of withholding taxes for net settlement of stock-based awards	—	(289)	—	—	(289)
Cumulative effect of adoption of ASC 606	—	—	1,713	—	1,713
Balance at September 30, 2018	$ 19	$ 125,938	$ (125,262)	$ (9,964)	$ (9,269)

See Notes to Consolidated Financial Statements

POWER SOLUTIONS INTERNATIONAL, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

(in thousands)	For the Nine Months Ended September 30,	
	2019	**2018**
Cash provided by (used in) operating activities		
Net income (loss)	$ 172	$ (44,828)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Amortization of intangible assets	2,729	3,687
Depreciation	3,875	3,849
Change in value and exercise of warrants	1,352	19,200
Stock-based compensation expense	1,101	1,963
Amortization of financing fees	545	947
Deferred income taxes	(30)	(87)
Other non-cash adjustments, net	193	1,661
Changes in operating assets and liabilities:		
Accounts receivable, net	9,213	(3,058)
Inventory, net	(9,613)	(32,657)
Prepaid expenses and other assets	6,897	(5,387)
Accounts payable	379	37,355
Accrued expenses	6,262	10,773
Other noncurrent liabilities	(3,953)	2,908
Net cash provided by (used in) operating activities	19,122	(3,674)
Cash used in investing activities		
Capital expenditures	(2,048)	(2,321)
Asset acquisitions	—	(6,595)
Other investing activities, net	13	—
Net cash used in investing activities	(2,035)	(8,916)
Cash (used in) provided by financing activities		
Proceeds from revolving line of credit	394,631	372,557
Repayments of revolving line of credit	(412,488)	(357,121)
Proceeds from Weichai Warrant exercise	1,616	—
Other financing activities, net	(899)	(832)
Net cash (used in) provided by financing activities	(17,140)	14,604
Net (decrease) increase in cash and restricted cash	(53)	2,014
Cash at beginning of the period	54	—
Cash at end of the period	$ 1	$ 2,014

See Notes to Consolidated Financial Statements

Note 1. Summary of Significant Accounting Policies and Other Information

Nature of Business Operations

Power Solutions International, Inc. ("Power Solutions," "PSI" or "the Company"), a Delaware corporation, is a global producer and distributor of a broad range of high-performance, certified, low-emission power systems, including alternative-fueled power systems for original equipment manufacturers ("OEMs") of off-highway industrial equipment and certain on-road vehicles and large custom-engineered integrated electrical power generation systems.

The Company's customers include large, industry-leading and multinational organizations. The Company's products and services are sold predominantly to customers throughout North America as well as to customers located throughout the Pacific Rim and Europe. The Company's power systems are highly engineered, comprehensive systems which, through the Company's technologically sophisticated development and manufacturing processes, including its in-house design, prototyping, testing and engineering capabilities and its analysis and determination of the specific components to be integrated into a given power system (driven in large part by emission standards and cost considerations), allow the Company to provide its customers with power systems customized to meet specific OEM application requirements, other technical customers' specifications and requirements imposed by environmental regulatory bodies.

The Company's power system configurations range from a basic engine 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. The Company also designs and manufactures large, custom-engineered integrated electrical power generation systems for both standby and prime power applications. The Company purchases engines from third-party suppliers and produces internally designed engines, all of which are then integrated into its power systems.

Of the other components that the Company integrates into its power systems, a substantial portion consist of internally designed components and components for which it coordinates significant design efforts with third-party suppliers, with the remainder consisting largely of parts that are sourced off-the-shelf from third-party suppliers. Some of the key components (including purchased engines) embody proprietary intellectual property of the Company's suppliers. As a result of its design and manufacturing capabilities, the Company is able to provide its customers with a power system that can be incorporated into a customer's specified application. In addition to the certified products described above, the Company sells diesel, gasoline and non-certified power systems and aftermarket components.

Stock Ownership and Control

In March 2017, the Company executed a share purchase agreement (the "SPA") with Weichai America Corp., a wholly owned subsidiary of Weichai Power Co., Ltd. (HK2338, SZ000338) (herein collectively referred to as "Weichai"). Under the terms of the SPA, Weichai invested $60.0 million in the Company purchasing a combination of newly issued Common and Preferred Stock as well as a stock purchase warrant (the "Weichai Warrant").

With the exercise of the Weichai Warrant in April 2019, Weichai owns a majority of the outstanding shares of the Company's Common Stock. As a result, Weichai is able to exercise control over matters requiring stockholders' approval, including the election of the directors, amendment of the Company's Charter and approval of significant corporate transactions. This control could have the effect of delaying or preventing a change of control of the Company or changes in management and will make the approval of certain transactions impractical without the support of Weichai.

Weichai also entered into an Investor Rights Agreement (the "Rights Agreement") with the Company upon execution of the SPA. The Rights Agreement provides Weichai with representation on the Company's Board of Directors (the "Board") and management representation rights. Weichai currently has three representatives on the Board. According to the Rights Agreement, once Weichai exercised the Weichai Warrant and became the majority owner of the Company's outstanding shares of Common Stock calculated on a fully diluted as-converted basis (excluding certain excepted issuances), the Company became required to appoint to the Board an additional individual designated by Weichai, or such additional numbers of individuals so that Weichai designees shall constitute the majority of the directors serving on the Board. As of the date of this filing, Weichai has not designated an additional representative to the Board. According to the Rights Agreement, during any period when the Company is a "controlled company" within the meaning of the NASDAQ Stock Market ("NASDAQ") Listing Rules, it will take such measures as to avail itself of the "controlled company" exemptions available under Rule 5615 of the NASDAQ Listing Rules of Rules 5605(b), (d) and (e).

Going Concern Considerations

On April 2, 2020, the Company closed on its new senior secured revolving credit facility pursuant to that certain credit agreement, dated as of March 27, 2020, between the Company and Standard Chartered Bank ("Standard Chartered"), as administrative agent (the “Credit Agreement”). The Credit Agreement, which allows the Company to borrow up to $130.0 million, matures on March 26, 2021 with an optional 60-day extension subject to certain conditions and payment of a 0.25% extension fee.

Significant uncertainties exist about the Company’s ability to refinance, extend, or repay its outstanding indebtedness, maintain sufficient liquidity to fund its business activities, and maintain compliance with the covenants and other requirements under the Credit Agreement. Based on the Company’s current forecasts, without additional financing, the Company anticipates that it will not have sufficient cash and cash equivalents to repay the Credit Agreement by March 26, 2021. Management plans to seek additional liquidity from its current or other lenders before March 26, 2021. There can be no assurance that the Company’s management will be able to successfully complete a financing on acceptable terms or repay this outstanding indebtedness, when required or if at all. The consolidated financial statements included in this Form 10-K do not include any adjustments that might result from the outcome of the Company’s efforts to address these issues.

Furthermore, if the Company cannot raise capital on acceptable terms, it may not, among other things, be able to do the following:

- continue to expand the Company’s research and product investments and sales and marketing organization;
- expand operations both organically and through acquisitions; and
- respond to competitive pressures or unanticipated working capital requirements.

Additionally, as discussed in Note 14. *Subsequent Events*, in January 2020, the World Health Organization (“WHO”) announced a global health emergency because of a new strain of coronavirus (the “COVID-19 outbreak”) and the risks to the international community as the virus spreads globally. In March 2020, the WHO classified the COVID-19 outbreak as a global pandemic (the “COVID-19 pandemic”), based on the rapid increase in exposure globally. The potential impact of future disruptions, continued economic uncertainty, and continued depressed crude oil prices and declining rig count levels may have a material adverse impact on the results of operations, financial position, and liquidity of the Company.

The Company’s management has concluded that, due to uncertainties surrounding the Company’s future ability to refinance, extend, or repay its outstanding indebtedness, maintain sufficient liquidity to fund its business activities, and maintain compliance with the covenants and other requirements under the Credit Agreement, substantial doubt exists as to its ability to continue as a going concern within one year after the date that these financial statements are issued. The Company’s plans to alleviate the substantial doubt about its ability to continue as a going concern may not be successful, and it may be forced to limit its business activities or be unable to continue as a going concern, which would have a material adverse effect on its results of operations and financial condition.

The consolidated financial statements included herein have been prepared assuming that the Company will continue as a going concern and contemplating the realization of assets and the satisfaction of liabilities and commitments in the normal course of business. The Company’s ability to continue as a going concern is dependent on generating profitable operating results, having sufficient liquidity, maintaining compliance with the covenants and other requirements under the Credit Agreement and refinancing or repaying the indebtedness outstanding under this agreement.

Basis of Presentation and Consolidation

The Company is filing this Form 10-Q for the three and nine months ended September 30, 2019, which contains unaudited consolidated financial statements as of and for the three and nine months ended September 30, 2019 and 2018.

The consolidated financial statements include the accounts of Power Solutions International, Inc. and its wholly owned subsidiaries and majority-owned subsidiaries in which the Company exercises control. The foregoing financial information was prepared in accordance with generally accepted accounting principles in the United States (“U.S. GAAP”) and rules and regulations of the U.S. Securities and Exchange Commission (“SEC”) for interim financial reporting. All intercompany balances and transactions have been eliminated in consolidation.

Certain information and note disclosures normally included in the Company’s annual financial statements prepared in accordance with U.S. GAAP have been condensed or omitted. The accompanying consolidated financial statements have been prepared in accordance with accounting policies described in the Company’s Annual Report on Form 10-K for the year ended December 31, 2018 ("the 2018 Annual Report"), which should be read in conjunction with the disclosures therein. The Company’s significant accounting policies are described in the aforementioned 2018 Annual Report. Included below are certain updates to those policies. The accompanying interim financial information is unaudited; however, the Company believes the financial information reflects all adjustments (consisting of items of a normal recurring nature) necessary for a fair presentation of financial position, results of operations and cash flows in conformity with U.S. GAAP. Operating results for interim periods are not necessarily indicative of annual operating results.

The Company operates as one business and geographic operating segment. Operating segments are defined as components of a business that can earn revenues and incur expenses for which discrete financial information is available that is evaluated on a regular basis by the chief operating decision maker (“CODM”). The Company’s CODM is its principal executive officer, who decides how to allocate resources and assess performance. A single management team reports to the CODM, who manages the entire business. The Company's CODM reviews consolidated statements of operations to make decisions, allocate resources and assess performance, and the CODM does not evaluate the profit or loss from any separate geography or product line.

Reclassifications

Certain amounts recorded in the prior-period consolidated financial statements presented have been reclassified to conform to the current-period financial statement presentation. These reclassifications had no effect on previously reported results of operations.

Concentrations

The following table presents customers individually accounting for more than 10% of the Company's net sales:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2019	2018	2019	2018
Customer A	11%	15%	15%	16%
Customer B	11%	**	**	10%
Customer C	15%	13%	12%	**
Customer D	11%	**	**	**

The following table presents customers individually accounting for more than 10% of the Company's accounts receivable:

	As of September 30, 2019	As of December 31, 2018
Customer A	18%	25%
Customer B	**	15%

The following table presents suppliers individually accounting for more than 10% of the Company's purchases:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2019	2018	2019	2018
Supplier A	29%	19%	20%	18%
Supplier B	12%	15%	12%	15%

** Less than 10% of the total

Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. GAAP requires that management make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Significant estimates and assumptions include the valuation of allowances for uncollectible receivables, inventory reserves, warranty reserves, stock-based compensation, evaluation of goodwill, other intangibles, plant and equipment for impairment, and determination of useful lives of long-lived assets. Actual results could materially differ from those estimates.

Research and Development

Research and development ("R&D") expenses are expensed when incurred. R&D expenses consist primarily of wages, materials, testing and consulting related to the development of new engines, parts and applications. These costs were $5.9 million and $7.3 million for the three months ended September 30, 2019 and 2018, respectively. These costs were $17.4 million and $19.4 million for the nine months ended September 30, 2019 and 2018, respectively.

Insurance Recoveries

The Company records insurance recoveries related to amounts recorded as estimated losses on events covered by the Company's insurance policies when management determines that the recovery is probable and the amount can be reasonably determined. As of September 30, 2019 and December 31, 2018, the Company had recorded assets related to insurance recoveries of $9.9 million and $16.0 million, respectively, primarily related to litigation reserves and related legal costs.

Inventories

The Company's inventories consist primarily of engines and parts. Engines are valued at the lower of cost plus estimated freight-in or net realizable value. Parts are valued at the lower of cost or net realizable value. Net realizable value approximates replacement cost. Cost is principally determined using the first-in, first-out method and includes material, labor and manufacturing overhead. It is the Company's policy to review inventories on a continuing basis for obsolete, excess and slow-moving items and to record valuation adjustments for such items in order to eliminate non-recoverable costs from inventory. Valuation adjustments are recorded in an inventory reserve account and reduce the cost basis of the inventory in the period in which the reduced valuation is determined. Inventory reserves are established based on quantities on hand, usage and sales history, customer orders, projected demand and utilization within a current or future power system. Specific analysis of individual items or groups of items is performed based on these same criteria, as well as on changes in market conditions or any other identified conditions.

Inventories consist of the following:

(in thousands)	As of September 30,	As of December 31,
Inventories	**2019**	**2018**
Raw materials	$ 94,739	$ 90,877
Work in process	3,079	2,390
Finished goods	21,120	18,077
Total inventories	118,938	111,344
Inventory allowance	(4,263)	(5,730)
Inventories, net	$ 114,675	$ 105,614

Activity in the Company's inventory allowance was as follows:

(in thousands)	For the Nine Months Ended September 30,	
Inventory Allowance	**2019**	**2018**
Balance at beginning of period	$ 5,730	$ 6,227
Charged to expense	560	1,830
Write-offs	(2,027)	(1,934)
Balance at end of period	$ 4,263	$ 6,123

Other Accrued Liabilities

Other accrued liabilities consisted of the following:

(in thousands)	As of September 30,	As of December 31,
Other Accrued Liabilities	**2019**	**2018**
Accrued product warranty	$ 14,677	$ 9,767
Litigation reserves *	7,695	16,139
Contract liabilities	15,959	4,897
Accrued compensation and benefits	6,670	4,520
Operating lease liabilities	3,860	—
Accrued interest expense	1,937	1,175
Other	7,004	9,202
Total	$ 57,802	$ 45,700

***** As of September 30, 2019, litigation reserves primarily consisted of reserves related to ongoing government investigations and for the settlement of the Federal Derivative Litigation and the Cohen matter. As of December 31, 2018, litigation reserves primarily consisted of accruals for the settlement of the Securities Litigation, Federal Derivative Litigation, and the Cohen matter. The Company concluded that insurance recovery was probable related to $4.9 million and $14.0 million of the litigation reserves at September 30, 2019 and December 31, 2018, respectively, and recognized full recovery of the settlement amounts in *Prepaid expenses and other current assets*. See Note 9. *Commitments and Contingencies* for additional information.

Warranty Costs

The Company offers a standard limited warranty on the workmanship of its products that in most cases covers defects for a defined period. Warranties for certified emission products are mandated by the U.S. Environmental Protection Agency (the "EPA") and/or the California Air Resources Board (the "CARB") and are longer than the Company's standard warranty on certain emission related products. The Company's products also carry limited warranties from suppliers. The Company's warranties generally apply to engines fully manufactured by the Company and to the modifications the Company makes to supplier base products. Costs related to supplier warranty claims are generally borne by the supplier and passed through to the end customer.

Warranty estimates are based on historical experience and represent the projected cost associated with the product. A liability and related expense are recognized at the time products are sold. The Company adjusts estimates when it is determined that actual costs may differ from initial or previous estimates.

Accrued product warranty activities are presented below:

(in thousands)	For the Nine Months Ended September 30,	
Accrued Product Warranty	**2019**	**2018**
Balance at beginning of period	$ 23,102	$ 12,628
Current year provision	7,706	9,385
Changes in estimates for preexisting warranties *	2,730	3,842
Payments made during the period	(7,244)	(5,940)
Balance at end of period	26,294	19,915
Less: current portion	14,677	10,589
Balance at end of period	$ 11,617	$ 9,326

* Change in estimates for preexisting warranties reflect changes in the Company's estimate of warranty costs for products sold in prior periods. Such adjustments typically occur when claims experience deviates from historic and expected trends. The Company's warranty liability is generally affected by failure rates, repair costs and the timing of failures. Future events and circumstances related to these factors could materially change the estimates and require adjustments to the warranty liability. In addition, new product launches require a greater use of judgment in developing estimates until historical experience becomes available. In the first quarter of 2019, the Company recorded a charge for changes in estimates of preexisting warranties of $2.7 million or $0.13 per diluted share.

Recently Issued Accounting Pronouncements – Adopted

In February 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2016-02, *Leases*, which created Accounting Standards Codification ("ASC") Topic 842, *Leases*, and superseded the existing guidance in ASC 840, *Leases.* See Note 7. *Leases*, for the required disclosures related to the adoption of ASC 842.

Recently Issued Accounting Pronouncements – Not Yet Adopted

In August 2018, the FASB issued ASU 2018-15, *Intangibles – Goodwill and Other – Internal Use Software: Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract*. This guidance requires the use of existing accounting guidance applicable to software developed for internal use to be applied to cloud computing service contracts' implementation costs. The costs capitalized would be amortized over the life of the agreement, including renewal option periods likely to be used. This guidance is effective for fiscal 2020, with early adoption permitted. The Company will adopt the standard effective January 1, 2020 on a prospective basis and does not anticipate that this guidance will have a material impact on its Consolidated Balance Sheet and Consolidated Statement of Operations.

In August 2018, the FASB issued ASU 2018-13, *Fair Value Measurement: Disclosure Framework – Changes to the Disclosure Requirements for Fair Value Measurement*, which both reduces and expands selected disclosure requirements. The principal changes expected to impact the Company's disclosure are requirements to disclose the range and weighted average of each of the significant unobservable items and the way the weighted average of a range is calculated for items in the "table of significant unobservable inputs." The guidance also requires disclosure of changes in unrealized gains and losses in other comprehensive income and removes requirements regarding, among other items, disclosure of the valuation process for Level 3 measurements. This guidance is effective for fiscal 2020. The Company plans to implement the guidance when it becomes effective and does not currently anticipate that this guidance will have a material impact on its Consolidated Balance Sheet and Consolidated Statement of Operations.

In January 2017, the FASB issued ASU 2017-04, *Intangibles – Goodwill and Other: Simplifying the Test for Goodwill Impairment*, which eliminated the requirement to calculate the implied fair value of goodwill to measure a goodwill impairment charge. Instead, entities will record an impairment charge based on the excess of a reporting unit's carrying amount over its fair value. The ASU is effective for annual and interim impairment tests performed in periods beginning after December 15, 2019; early adoption is permitted for annual and interim goodwill impairment testing dates after January 1, 2017. The amendments in this ASU are to be applied on a prospective basis. The Company currently plans on adopting the guidance on January 1, 2020 when it becomes effective and does not expect the guidance to have a material impact on its financial statements.

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments – Credit Losses: Measurement of Credit Losses on Financial Instruments*, which applies primarily to the Company's accounts receivable impairment loss allowances. The guidance provides a revised model whereby the current expected credit losses are used to compute impairment of financial instruments. The new model requires evaluation of historical experience and various current and expected factors, which may affect the estimated amount of losses and requires determination of whether the affected financial instruments should be grouped in units of account. The guidance, as originally issued, was effective for fiscal years beginning after December 15, 2019. In November 2019, the FASB issued ASU 2019-10, *Financial Instruments – Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842) Effective Dates*, which deferred the effective dates of these standards for certain entities. Based on the guidance, the effective date of ASU 2016-13 is deferred for the Company until fiscal year 2023. The Company currently plans to adopt the guidance on January 1, 2023 when it becomes effective. The Company is continuing to assess the impact of the standard on its financial statements.

Note 2. Revenue

Disaggregation of Revenue

The following table summarizes net sales by end market:

(in thousands)	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
End Market	**2019**	**2018**	**2019**	**2018**
Energy	$ 64,331	$ 48,481	$ 162,224	$ 139,062
Industrial	37,020	52,367	142,267	146,137
Transportation	37,161	35,470	88,492	72,605
Total	$ 138,512	$ 136,318	$ 392,983	$ 357,804

The following table summarizes net sales by geographic area:

(in thousands)	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
Geographic Area	**2019**	**2018**	**2019**	**2018**
North America	$ 125,971	$ 120,955	$ 343,593	$ 312,346
Pacific Rim	6,744	10,913	30,173	32,768
Europe	4,329	3,012	12,712	9,948
Other	1,468	1,438	6,505	2,742
Total	$ 138,512	$ 136,318	$ 392,983	$ 357,804

Contract Balances

Most of the Company's contracts are for a period of less than one year; however, certain long-term manufacturing and extended warranty contracts extend beyond one year. The timing of revenue recognition may differ from the time of invoicing to customers and these timing differences result in contract assets, or contract liabilities on the Company's Consolidated Balance Sheet. Contract assets include amounts related to the contractual right to consideration for completed performance when the right to consideration is conditional. The Company records contract liabilities when cash payments are received or due in advance of performance. Contract assets and contract liabilities are recognized at the contract level.

(in thousands)	As of	
	September 30, 2019	**December 31, 2018**
Short-term contract assets (included in *Prepaid expenses and other current assets*)	$ 4,038	$ 2,926
Short-term contract liabilities (included in *Other accrued liabilities*)	(15,959)	(4,897)
Long-term contract liabilities (included in *Noncurrent contract liabilities*)	(12,622)	(14,611)
Net contract liabilities	$ (24,543)	$ (16,582)

During the nine months ended September 30, 2019, the Company recognized $4.1 million of revenue upon satisfaction of performance obligations related to amounts that were included in the net contract liabilities balance as of December 31, 2018. The increase in the contract liabilities from December 31, 2018 to September 30, 2019 is primarily related to the prepayment for certain engines by a customer under a long-term supply agreement.

Remaining Performance Obligations

For performance obligations that extend beyond one year, the Company had $27.7 million of remaining performance obligations as of September 30, 2019. The Company expects to recognize revenue related to these remaining performance obligations of approximately $5.8 million in the remainder of 2019, $16.9 million in 2020, $2.9 million in 2021, $0.7 million in 2022, $0.6 million in 2023 and $0.8 million in 2024 and beyond.

Note 3. Weichai Transactions

Weichai Warrant

In September 2018, the Weichai Warrant was amended under the terms of a second amended and restated warrant ("Amended and Restated Warrant") to defer its exercise date to a 90-day period commencing April 1, 2019, to adjust the exercise price to a price per share of the Company's Common Stock equal to the lesser of (i) 50% of the Volume-Weighted Average Price ("VWAP") during the 20 consecutive trading day period preceding October 1, 2018 and (ii) 50% of the VWAP during the 20 consecutive trading day period preceding the date of exercise, subject to an adjustment that could reduce the exercise price by up to $15.0 million. In the event that the adjustment exceeded the exercise price, the excess would be due to the warrant holder.

On April 23, 2019, Weichai exercised the Weichai Warrant resulting in the Company issuing 4,049,759 shares of the Company's Common Stock and Weichai becoming the owner of 51.5% of the outstanding shares of the Company's Common Stock, as of such date. The exercise proceeds for the warrants of $1.6 million were based on 50% of the VWAP during the 20 consecutive trading day period preceding April 23, 2019 and the $15.0 million reduction in the exercise price described above.

The Weichai Warrant was a freestanding derivative financial instrument that was not indexed solely to the Company's Common Stock due to the Weichai Warrant's exercise terms. Therefore, the Weichai Warrant was presented at fair value in the Company's Consolidated Balance Sheet in *Warrant liability* for $35.1 million at December 31, 2018. Changes in value and the impact of exercise of the Weichai Warrant resulted in a net loss of $1.4 million reported in *Loss from change in value and exercise of warrants* in the Company's Consolidated Statements of Operations for the nine months ended September 30, 2019. Changes in value of the Weichai Warrant resulted in a net loss of $10.2 million and $19.2 million for the three and nine months ended September 30, 2018, respectively. See Note 8. *Fair Value of Financial Instruments* for additional details and assumptions used in valuing the Weichai Warrant, as well as adjustments for the nine months ended September 30, 2019 and 2018.

Related Party Transactions

The Company purchased $0.6 million and $1.5 million of inventory from Weichai during the three and nine months ended September 30, 2019, respectively. Purchases of inventory from Weichai were $1.0 million and $1.2 million material during the three and nine months ended September 30, 2018. Company sales to Weichai during the three and nine months ended September 30, 2019 and 2018 were insignificant.

Note 4. Property, Plant and Equipment

Property, plant and equipment by type were as follows:

(in thousands) **Property, Plant and Equipment**	**As of September 30, 2019**	**As of December 31, 2018**
Leasehold improvements	$ 6,524	$ 6,405
Machinery and equipment	40,829	38,454
Construction in progress	1,324	1,241
Total property, plant and equipment, at cost	48,677	46,100
Accumulated depreciation	(25,209)	(21,834)
Property, plant and equipment, net	$ 23,468	$ 24,266

In April 2018, the Company finalized the purchase of emissions testing assets and the sublease of an emissions testing facility from Ricardo, Inc., a subsidiary of the strategic engineering and environmental consultancy, Ricardo Plc., for $5.6 million in cash. The Company accounted for the acquisition as an asset acquisition and recorded property, plant and equipment of $6.9 million, included within machinery and equipment in the table above, and an asset retirement obligation of $1.3 million as a result of the transaction. The fair value of the asset retirement obligation was estimated using Level 3 inputs. The asset retirement obligation is recorded in *Other noncurrent liabilities* in the Company's Consolidated Balance Sheets.

Note 5. Goodwill and Other Intangibles

Goodwill

The carrying amount of goodwill at both September 30, 2019 and December 31, 2018 was $29.8 million. Accumulated impairment losses at both September 30, 2019 and December 31, 2018 were $11.6 million.

Other Intangible Assets

In March 2018, the Company acquired intellectual property ("IP") from AGA Systems, LLC ("AGA") for the conversion of certain gasoline engines to alternative fuel engines. The Company paid cash of $1.5 million ($1.0 million in 2018 and $0.5 million in 2017) to acquire the IP assets and provided a minimum guaranteed payment of an additional $1.2 million to be paid over a three-year period from the date of acquisition. If certain milestones related to future sales are met, the Company could pay up to an additional $3.3 million to AGA. The acquisition was accounted for as an asset acquisition because the gross assets acquired were concentrated within a group of similar identifiable assets. The Company recorded developed technology of $2.7 million related to the acquired IP and a liability of $1.2 million related to the guaranteed payment. The sales-based milestone payments are recorded as they are earned and the milestones are probable of being achieved. The developed technology was being depreciated over an estimated useful life of approximately three years. In the fourth quarter of 2018, based on uncertainty of the market for the conversion of certain gasoline engines to alternative fuel engines, the Company concluded that the forecasted future cash flows were not sufficient to recover the carrying value of the assets. As a result, the Company recorded an impairment charge of $2.2 million to write off the remaining book value of the intangible assets.

Components of intangible assets are as follows:

(in thousands)	As of September 30, 2019		
	Gross Carrying Value	**Accumulated Amortization**	**Net Book Value**
Customer relationships	$ 34,940	$ (21,381)	$ 13,559
Developed technology	700	(588)	112
Trade names and trademarks	1,700	(1,090)	610
Total	$ 37,340	$ (23,059)	$ 14,281

(in thousands)	As of December 31, 2018		
	Gross Carrying Value	**Accumulated Amortization**	**Net Book Value**
Customer relationships	$ 34,940	$ (18,816)	$ 16,124
Developed technology	700	(537)	163
Trade names and trademarks	1,700	(977)	723
Total	$ 37,340	$ (20,330)	$ 17,010

Note 6. Debt

The Company's outstanding debt consisted of the following:

(in thousands)	**As of September 30, 2019**	**As of December 31, 2018**
Short-term financing:		
Wells Fargo revolving credit facility	$ 36,756	$ 54,613
Long-term debt:		
Unsecured senior notes	$ 55,000	$ 55,000
Finance leases and other debt	965	456
Unamortized debt issuance costs *	(75)	(288)
Total long-term debt and finance leases	55,890	55,168
Less: Current maturities of long-term debt and finance leases	186	80
Long-term debt	$ 55,704	$ 55,088

* Unamortized financing costs and deferred fees on the Wells Fargo Bank, N.A. ("Wells Fargo") Revolving Credit Facility are not presented in the above table as they are classified as *Prepaid expenses and other current assets* on the Consolidated Balance Sheets.

Certain events of default (including delinquent filing of annual and periodic reports with the SEC and material weaknesses in the control environment) occurred with respect to the Company's credit agreements. While waivers were obtained, or debt was renegotiated with the respective lenders, absent such waivers the debt would have been in breach of covenants. The Company pledged substantially all of its tangible and intangible assets, including inventory, receivables and fixed assets, as collateral under the Wells Fargo Credit Agreement.

Wells Fargo Credit Agreement

In June 2013, the Company entered into a credit agreement with Wells Fargo Bank, N.A. ("Wells Fargo"), which has been amended and restated from time to time (the "Wells Fargo Credit Agreement"). The Wells Fargo Credit Agreement enabled the Company to borrow under a revolving credit facility secured by substantially all of the Company's tangible and intangible assets, including inventory, receivables and fixed assets. The Wells Fargo Credit Agreement has been amended several times since June 28, 2013.

Significant changes to the Wells Fargo Credit Agreement since December 31, 2018 are summarized in the table below:

Amendment Date and Title	Reason for Amendment	Significant Changes/Notes Regarding Amendment to the Wells Fargo Credit Agreement
May 16, 2019. Waiver to the June 28, 2016 Agreement	To consider implications of various events of default	• Waived any defaults that would arise from the failure to timely deliver annual audited financial statements for the fiscal year ended December 31, 2018 and the associated compliance certificate and the information required with it; provided that the financial statements and compliance certificate were delivered on or before December 31, 2019.

Unsecured Senior Notes

In April 2015, the Company entered into an agreement with certain institutional investors for a private sale of its unsecured senior notes for the aggregate amount of $55.0 million with an interest rate of 5.50% per annum (the "Unsecured Senior Notes"). Concurrently, in connection with the issuance of the Unsecured Senior Notes, the Company entered into an indenture agreement ("Indenture"), by and among the Company and its subsidiaries as guarantors and the Bank of New York Mellon, as Trustee. The Unsecured Senior Notes are unsecured debt of the Company and are effectively subordinated to its existing and future secured debt, including the debt in connection with the Wells Fargo Credit Agreement.

Significant amendments to the Unsecured Senior Notes since December 31, 2018 are included in the table below:

Amendment Date and Title	Reason for Amendment	Significant Changes/Notes Regarding Amendment to the Unsecured Senior Notes
October 30, 2019. Fifth Supplemental Indenture	To extend the maturity date	• Extended maturity date to June 30, 2020 (which also extended the maturity date of the Wells Fargo Credit Agreement to May 1, 2020). • The Company paid a fee of $0.3 million.

The interest rate on the Unsecured Senior Notes decreased to 7.50% per annum upon filing the Form 10-K for the fiscal year ended December 31, 2017 with the SEC in May 2019.

Credit Agreement

On April 2, 2020, the Company closed on its new senior secured revolving credit facility pursuant to the Credit Agreement with Standard Chartered. The Credit Agreement allows the Company to borrow up to $130.0 million and matures on March 26, 2021 with an optional 60-day extension subject to certain conditions and payment of a 0.25% extension fee. Borrowings under the Credit Agreement bear interest at either the base rate as defined in the Credit Agreement or London Interbank Offered Rate ("LIBOR") plus 2.00% per annum, and the Company is required to pay a 0.25% commitment fee on the average daily unused portion of the revolving credit facility under the Credit Agreement. The Credit Agreement is secured by substantially all of the Company's assets and includes certain financial covenants as well as a change of control provision. On April 2, 2020, the Company borrowed $95.0 million under the Credit Agreement and utilized the funds (i) to repay the outstanding balance of $16.8 million on the Wells Fargo Credit Agreement, (ii) to fully redeem and discharge $55.0 million in aggregate outstanding principal amount of the Unsecured Senior Notes and pay related interest, and (iii) for general corporate purposes. The Wells Fargo Credit Agreement was terminated in connection with repayment of the outstanding balance. The Company will recognize a loss on the extinguishment of the Wells Fargo Credit Agreement and the Unsecured Senior Notes of $0.1 million related to unamortized debt issuance costs and will defer additional debt issuance costs related to the closing of the Credit Agreement of $2.0 million.

Note 7. Leases

On January 1, 2019, the date of initial application, the Company adopted ASC 842 using the modified retrospective transition method whereby prior comparative periods have not been restated and continue to be reported under the accounting standards in effect for the prior period. The Company elected the package of practical expedients permitted under the transition guidance for all leases, which allowed the Company to adopt ASC 842 without reassessing whether arrangements contain leases, the lease classification, and the determination of initial direct costs.

Upon adoption on January 1, 2019, the Company recognized right-of-use ("ROU") assets inclusive of finance leases, net of prepaids, incentives, and impairments, of $24.6 million and lease liabilities of $25.1 million in the Consolidated Balance Sheet. At adoption, there was no impact to the Consolidated Statement of Operations, Consolidated Statement of Cash Flows or Consolidated Statement of Stockholders' Equity (Deficit).

Lease Policies

The Company determines if an arrangement contains a lease in whole or in part at the inception of the contract. ROU assets represent the right to use an underlying asset for the lease term while lease liabilities represent the obligation to make lease payments arising from the lease. All leases with an expected term greater than 12 months result in the recognition of a ROU asset and a liability at the lease commencement date based on the present value of the lease payments over the lease term. The Company uses its incremental borrowing rate based on the information available at the lease commencement date to determine the present value of the lease payments unless the implicit rate in the lease is readily determinable. The incremental borrowing rate is determined considering factors such as the lease term, the Company's credit standing and the economic environment of the location of the lease.

The lease term includes all non-cancellable periods and may include options to extend (or to not terminate) the lease when it is reasonably certain that the Company will exercise the option. Leases that have a term of 12 months or less at the commencement date are expensed on a straight-line basis over the lease term and do not result in the recognition of a ROU asset or lease liability.

The Company classifies leases as finance leases when (i) there is a transfer of ownership of the underlying asset by the end of the lease term, (ii) the lease contains an option to purchase the asset that the Company is reasonably certain will be exercised, (iii) the lease term is for the majority of the remaining economic life of the asset, or (iv) the present value of the lease payments and any residual value guarantee equals or substantially exceeds the fair value of the asset.

Lease expense for operating leases is recognized on a straight-line basis over the lease term. Lease expense for finance leases is generally front-loaded as the finance lease ROU asset is depreciated on a straight-line basis, but interest expense on the lease liability is recognized using the interest method which results in more expense during the early years of the lease. Variable lease payments are expensed in the period in which the obligation for those payments is incurred. The Company has elected to combine lease and non-lease components, such as fixed maintenance costs, as a single lease component in calculating ROU assets and lease liabilities for all classes of leased assets.

Leases

The Company has obligations under lease arrangements primarily for facilities, equipment and vehicles. These leases have original lease periods expiring between March 2020 and August 2039. For the three and nine months ended September 30, 2019, the Company recorded lease expense of $1.6 million and $5.2 million within *Cost of sales*, $0.3 million and $0.5 million within *Research, development and engineering and expenses*, $0.1 million and $0.2 million within *Selling, general and administrative* and less than $0.1 million within *Interest expense* in the Consolidated Statement of Operations, respectively.

The following table summarizes the components of lease expense:

(in thousands)	For the Three Months Ended September 30, 2019	For the Nine Months Ended September 30, 2019
Operating lease cost	$ 1,386	$ 4,193
Finance lease cost		
Amortization of ROU asset	50	119
Interest expense	14	35
Short-term lease cost	177	453
Variable lease cost	390	1,156
Total lease cost	$ 2,017	$ 5,956

For the three and nine months ended September 30, 2018, rent expense related to operating leases under previous accounting guidance was $1.3 million and $3.8 million, respectively.

The following table presents supplemental cash flow information related to leases:

(in thousands)	For the Nine Months Ended September 30, 2019	
Cash paid for amounts included in the measurement of lease liabilities		
Operating cash flows paid for operating leases	$	3,816
Operating cash flows paid for interest portion of finance leases		36
Financing cash flows paid for principal portion of finance leases		106
Right-of-use assets obtained in exchange for lease obligations		
Operating leases		280
Finance leases		517

As of September 30, 2019, the weighted-average remaining lease term was 6.9 years for operating leases and 4.8 years for finance leases. The weighted-average discount rate was 7.2% for operating leases and 6.8% for finance leases. The following table presents supplemental balance sheet information related to leases as of September 30, 2019:

(in thousands)	Operating Leases		Finance Leases	
ROU assets, net [1]	$	21,644	$	809
Lease liabilities, current [2]		3,860		186
Lease liabilities, non-current [3]		18,573		654
Total lease liabilities	$	22,433	$	840

1. Included in *Other noncurrent assets* for operating leases and *Property, plant and equipment, net* for finance leases on the Consolidated Balance Sheet.
2. Included in *Other accrued liabilities* for operating leases and *Current maturities of long-term debt* for finance leases on the Consolidated Balance Sheet.
3. Included in *Other noncurrent liabilities* for operating leases and *Long-term debt, net of current maturities* for finance leases on the Consolidated Balance Sheet.

The following table presents maturity analysis of lease liabilities as of September 30, 2019:

(in thousands)	Operating Leases		Finance Leases	
Three months ending December 31, 2019	$	1,365	$	59
Year ending December 31, 2020		5,210		236
Year ending December 31, 2021		4,827		236
Year ending December 31, 2022		4,668		169
Year ending December 31, 2023		3,247		101
Thereafter		9,202		178
Total undiscounted lease payments		28,519		979
Less: imputed interest		6,086		139
Total lease liabilities	$	22,433	$	840

Minimum lease commitments as of December 31, 2018 and accounted for under previous lease guidance were as follows:

(in thousands)	Operating		Capital	
2019	$	5,071	$	80
2020		5,175		63
2021		4,724		67
2022		4,681		50
2023		3,104		13
2024 and beyond		3,694		—
Total	$	26,449	$	273

Note 8. Fair Value of Financial Instruments

For assets and liabilities measured at fair value on a recurring and nonrecurring basis, a three-level hierarchy of measurements based upon observable and unobservable inputs is used to arrive at fair value. Observable inputs are developed based on market data obtained from independent sources, while unobservable inputs reflect the Company's assumptions about valuation based on the best information available in the circumstances. Depending on the inputs, the Company classifies each fair-value measurement as follows:

- Level 1 – based on quoted prices in active markets for identical assets or liabilities;
- Level 2 – based on other significant observable inputs for the assets or liabilities through corroborations with market data at the measurement date; and
- Level 3 – based on significant unobservable inputs that reflect management's best estimate of what market participants would use to price the assets or liabilities at the measurement date.

Financial Instruments Measured at Carrying Value

Current Assets

Cash and cash equivalents are measured at carrying value, which approximates fair value because of the short-term maturities of these instruments.

Debt

The Company measures the Wells Fargo Credit Agreement and the Unsecured Senior Notes at original carrying value including accrued interest, net of unamortized deferred financing costs and fees. The fair value of the revolving credit facility approximates carrying value, as it consists of short-term variable rate loans.

The fair value measurement of the Unsecured Senior Notes is defined as Level 3 in the three-level fair value hierarchy, as the inputs to their valuation are not all market observable.

(in thousands)	As of September 30, 2019			
		Fair Value		
	Carrying Value	Level 1	Level 2	Level 3
Wells Fargo Credit Agreement	$ 36,756	$ —	$ 36,756	$ —
Unsecured Senior Notes	54,925	—	—	54,600

(in thousands)	As of December 31, 2018			
		Fair Value		
	Carrying Value	Level 1	Level 2	Level 3
Wells Fargo Credit Agreement	$ 54,613	$ —	$ 54,613	$ —
Unsecured Senior Notes	54,712	—	—	52,700

Other Financial Assets and Liabilities

In addition to the methods and assumptions used for the financial instruments discussed above, accounts receivable, income tax receivable, accounts payable and certain accrued expenses are measured at carrying value, which approximates fair value because of the short-term maturities of these instruments.

Financial Instruments Measured at Fair Value

The Company's warrant liability was measured at fair value based on unobservable inputs and was, thus, considered a Level 3 financial instrument in the three-level valuation hierarchy.

(in thousands)	As of December 31, 2018			
		Fair Value		
	Carrying Value	Level 1	Level 2	Level 3
Warrant liability	$ 35,100	$ —	$ —	$ 35,100

Warrants

The following table summarizes changes in the estimated fair value of the Company’s warrant liability:

(in thousands)	For the Nine Months Ended September 30,	
	2019	2018
Balance at beginning of period	$ 35,100	$ 24,700
Issuance of warrants	1,352	19,200
Change in value of warrants *	(36,452)	—
Balance at end of period	$ —	$ 43,900

* The change in value of the warrant liability for each period is presented as *Loss (gain) from change in value and exercise of warrants* in the Company’s Consolidated Statements of Operations.

Weichai Warrant Liability

The Company estimated the fair value of the Weichai Warrant financial instrument using a publicly traded stock pricing approach with a Black-Scholes option pricing model and a Monte Carlo simulation. Given the unobservable nature of the inputs to the pricing models, the Weichai Warrant was classified as a Level 3 instrument.

The inputs of the Black-Scholes option pricing model were as follows:

Assumptions	As of December 31, 2018
Market value of the Common Stock	$9.25
Exercise price	varies
Risk-free interest rate	2.6%
Estimated price volatility	55%
Contractual term	0.5 years

The estimated price volatility represents the upper end of the range of implied volatility of publicly traded call options of benchmark companies.

Note 9. Commitments and Contingencies

Legal Contingencies

The legal matters discussed below and others could result in losses, including damages, fines, civil penalties and criminal charges, which could be substantial. The Company records accruals for these contingencies to the extent the Company concludes that a loss is both probable and reasonably estimable. Regarding the matters disclosed below, unless otherwise disclosed, the Company has determined that liabilities associated with these legal matters are reasonably possible; however, unless otherwise stated, the possible loss or range of possible loss cannot be reasonably estimated. Given the nature of the litigation and investigations and the complexities involved, the Company is unable to reasonably estimate a possible loss for all such matters until the Company knows, among other factors, the following:

- what claims, if any, will survive dispositive motion practice;
- the extent of the claims, particularly when damages are not specified or are indeterminate;
- how the discovery process will affect the litigation;
- the settlement posture of the other parties to the litigation; and
- any other factors that may have a material effect on the litigation or investigation.

However, the Company could incur judgments, enter into settlements or revise its expectations regarding the outcome of certain matters, and such developments could have a material adverse effect on the Company’s results of operations in the period in which the amounts are accrued and/or liquidity in the period in which the amounts are paid.

Securities and Exchange Commission and United States Attorney’s Office for the Northern District of Illinois Investigations

In August 2016, the Chicago Regional Office of the SEC commenced an investigation focused on, among other things, the Company’s financial reporting, misapplication of U.S. GAAP, revenue recognition practices and related conduct, which resulted in the accounting errors giving rise to the financial restatements reported in prior SEC filings. In 2016, the United States Attorney's Office for the Northern District of Illinois (the “USAO”) began conducting a parallel investigation regarding these matters. The Company is fully cooperating with the SEC and the USAO in their investigations. The Company is engaged in ongoing discussions with the SEC and the USAO regarding resolutions of these matters. If the SEC or the USAO determines that the Company violated federal securities or other laws and institutes civil enforcement or criminal proceedings, the Company may become subject to civil or criminal sanctions, including, but not limited to, criminal or civil charges, fines, other monetary penalties, injunctive relief and compliance conditions imposed by a court or agreement, which may have a material adverse effect on the financial condition, results of operations or cash flows of the Company.

Securities Litigation

In August 2016, Sumit Gupta filed a putative stockholder class-action complaint against the Company, Gary S. Winemaster, Michael P. Lewis and Daniel P. Gorey in the U.S. District Court for the Northern District of Illinois (the "*Gupta* Action"). The complaint alleged violations of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, as amended (the "Exchange Act") arising from public filings made between May 2015 and August 2016. In October 2016, Peter Stout initiated a second suit, asserting similar claims against the same defendants (the "*Stout* Action").

In January 2017, the court consolidated the *Gupta* Action and the *Stout* Action and appointed Richard Giunta as lead plaintiff. The consolidated case is captioned *Giunta v. Power Solutions International, Inc.*, No. 1:16-cv-09599 (N.D. Ill.) (the "*Giunta* Action"). The plaintiffs then filed an Amended Class Action Complaint (the "Amended Complaint") against the Company and certain current and former officers and directors. The Amended Complaint alleges violations of Sections 10(b) and 20(a) of the Exchange Act arising from public filings, press releases and conference calls between February 2014 and February 2017. In January 2019, the parties executed a Stipulation and Agreement of Settlement (the "Settlement") to resolve the *Giunta* Action. Under the terms of the Settlement, a payment of $8.5 million would be made by the Company and/or its insurers in exchange for the release of claims against the defendants and other released parties by the lead plaintiff and all settlement class members and for the dismissal of the Giunta Action with prejudice. The payment of the $8.5 million was placed into escrow by the Company's insurers in February 2019. In May 2019, the court granted final approval of the settlement. The Company accrued for the settlement in *Other accrued liabilities* and for the full insurance recovery of the settlement amount in *Prepaid expenses and other current assets* as of December 31, 2018. See Note 1. *Summary of Significant Accounting Policies and Other Information* for additional information related to the Company's insurance proceeds receivable and litigation reserves. No further action or impact to the Company's results of operations, financial condition or cash flows is expected.

Federal Derivative Litigation

In February 2017, Travis Dorvit filed a putative stockholder derivative action in the U.S. District Court for the Northern District of Illinois, captioned *Dorvit v. Winemaster, et al.*, No. 1:17-cv-01097 (N.D. Ill.) (the "*Dorvit* Action"), against certain of the Company's current and former officers and directors. The complaint asserted claims for breach of fiduciary duty and unjust enrichment arising from the same matters at issue in the *Giunta* Action. In April 2018, Michael Martin filed a second putative stockholder derivative action, captioned *Martin v. Winemaster, et al.*, No. 18-CV-2386 (N.D. Ill.) (the "*Martin* Action"), in the same court against certain of the Company's current and former officers and directors. In July 2018, the court consolidated the *Martin* Action and the *Dorvit* Action.

In July 2018, the plaintiffs in the consolidated *Dorvit* and *Martin* Actions filed an amended consolidated complaint (the "Second Amended Complaint") against certain of the Company's current and former officers and directors, who are indemnified by the Company as to their legal fees and defense costs. The Second Amended Complaint asserts claims for breach of fiduciary duty, unjust enrichment, corporate waste and failure to hold an annual stockholders' meeting, and it seeks an unspecified amount of damages, an order compelling the Company to hold an annual stockholders' meeting and an award of costs, including reasonable attorneys' fees and expenses. In April 2019, the parties reached an agreement in principle to settle the litigation for approximately $1.9 million ("Settlement Amount"), half of which will be used to pay certain defense costs on behalf of the Company, and the remaining half of which the plaintiffs sought as an award of their attorneys' fees and expenses in connection with the benefit conferred by the settlement. The settlement was approved by the court in August 2019 over two objections, including from the plaintiffs in the *McClenney* Action (defined below). Plaintiffs in the *McClenney* Action appealed the court's order approving the settlement. On February 28, 2020, the U.S. Court of Appeals for the Seventh Circuit affirmed the district court's approval of the settlement. Absent an extension, the plaintiffs in the *McClenney* Action have until July 27, 2020 to seek further review in the U.S. Supreme Court. The Company's insurers made a payment of half of the Settlement Amount in September 2019 toward the fulfillment of the plaintiff's award of attorneys' fees and expenses, and the insurers have allocated the remaining half of the Settlement Amount toward the payment of certain defense costs consistent with the terms of the settlement. The Company had accrued for the settlement in *Other accrued liabilities* and for the full insurance recovery of the Settlement Amount in *Prepaid expenses and other current assets* as of December 31, 2018. The settlement would not have a material impact on the Company's results of operations, financial condition or cash flows.

State Derivative Litigation

In May 2017, Lewis McClenney filed a putative stockholder derivative action in the Chancery Division of the Circuit Court of Cook County, Illinois, captioned *McClenney v. Winemaster, et al.*, No. 2017-CH-06481 (the "*McClenney* Action"), against certain of the Company's current and former officers and directors. The *McClenney* Action asserted claims for breach of fiduciary duty, unjust enrichment, abuse of control, gross mismanagement and corporate waste arising from the same matters at issue in the *Giunta*

Action. On the same day that the *McClenney* Action was filed, Sara Rebscher also filed a putative stockholder derivative action in the same court, captioned *Rebscher v. Winemaster, et al.*, No. 2017-CH-06517 (the "*Rebscher* Action"). The *Rebscher* Action asserts claims for breach of fiduciary duty and unjust enrichment against certain of the Company's current and former officers and directors, arising from the same matters at issue in the *Giunta* Action. Additionally, the complaint in the *Rebscher* Action asserts a claim for professional negligence and accounting malpractice against the Company's former auditor, RSM U.S. LLP ("RSM"). In July 2017, the court consolidated the *McClenney* Action and the *Rebscher* Action. Subsequently, the court appointed Rebscher as lead plaintiff and designated the *Rebscher* Action as the operative complaint. In November 2018, the court granted the Company's motion to dismiss the consolidated case with prejudice on the grounds that it is duplicative of the *Dorvit* and *Martin* Actions. Plaintiffs moved for reconsideration of the court's decision, which the court denied in January 2019. In February 2019, plaintiffs filed a notice of appeal from the court's order dismissing the case. In December 2019, the Illinois Appellate Court affirmed the dismissal of the *McClenney* Action. Plaintiffs did not seek rehearing in the Illinois Appellate Court and did not petition for leave to appeal to the Illinois Supreme Court.

Jerome Treadwell v. the Company

In October 2018, a putative class-action complaint was filed against the Company and NOVAtime Technology, Inc. ("NOVAtime") in the Circuit Court of Cook County, Illinois. In December 2018, NOVAtime removed the case to the U.S. District Court for the Northern District of Illinois, Eastern Division under the Class Action Fairness Act. Plaintiff has since voluntarily dismissed NOVAtime from the lawsuit without prejudice and filed an amended complaint in April 2019. The operative, amended complaint asserts violations of the Illinois Biometric Information Privacy Act ("BIPA") in connection with employees' use of the time clock to clock in and clock out using a finger scan and seeks statutory damages, attorneys' fees, and injunctive and equitable relief. An aggrieved party under BIPA may recover (i) $1,000 per violation if the Company is found to have negligently violated BIPA or (ii) $5,000 per violation if the Company is found to have intentionally or recklessly violated BIPA plus reasonable attorneys' fees. In May 2019, the Company filed its motion to dismiss the plaintiff's amended complaint. In December 2019, the court denied the Company's motion to dismiss. In January 2020, the Company moved for reconsideration of the court's order denying the motion to dismiss, or in the alternative, to stay the case pending the Illinois Appellate Court's ruling in *McDonald v. Symphony Healthcare* on a legal question that would be potentially dispositive in this matter. In February 2020, the court denied the Company's motion for reconsideration, but required the parties to submit additional briefing on the Company's motion to stay. On April 1, 2020, the Court granted the Company's motion to stay and stayed the case pending the Illinois Appellate Court's ruling in *McDonald v. Symphony Healthcare*. The Company intends to vigorously defend against this action. At this time, the Company is unable to predict the outcome of this matter or meaningfully quantify how the final resolution of this matter may impact its results of operations, financial condition or cash flows.

Don Wilkins v. the Company

In April 2017, Don Wilkins, former VP of Advanced Product Development for the Company, filed a two-count complaint alleging breach of contract by the Company and violation of the Illinois Wage Payment and Collections Act ("IWPCA") by the Company and its former CEO, Gary Winemaster (the "Wilkins Complaint"). The Wilkins Complaint claims the Company did not have cause to terminate Mr. Wilkins' Employment and Confidentiality Agreement ("Agreement"), executed January 6, 2012, and that the Company and Mr. Winemaster violated the IWPCA by failing to pay him accrued but unpaid vacation and earned commissions. The Wilkins Complaint seeks damages including a $2.0 million bonus entitlement in his Agreement, guaranteed annual salary to increase at 1.5 times Consumer Price Index per year from the termination date to the end-date of the Agreement, December 31, 2020, and 20,000 shares of restricted stock granted to him in 2013 with a vesting schedule through 2020. In June 2017, the Company and Mr. Winemaster answered the complaint and asserted numerous defenses. The Company also asserted counterclaims against Wilkins including violation of the Illinois Trade Secrets Act, breach of the Agreement, breach of fiduciary duty, and spoliation. In January 2019, Wilkins voluntarily dismissed with prejudice his claims for unpaid commissions and vacation against the Company and Mr. Winemaster, subject to the parties' confidential settlement agreement of those claims. Discovery is ongoing and no trial date has been set. In February 2020, the Company filed a motion for protective order or to stay the litigation, which the Court denied on April 7, 2020. The Company intends to vigorously defend against this action. On April 22, 2020, the parties reached an agreement in principle to settle all remaining claims for a $1.1 million payment ("Wilkins Settlement Amount") to Mr. Wilkins. The Company will contribute $0.9 million of the Wilkins Settlement Amount which was reserved during the first quarter of 2019. The parties are working on the final settlement documents. The parties will stipulate to the dismissal of the litigation with prejudice within 7 days after payment of the Wilkins Settlement Amount.

Other Commitments

At September 30, 2019, the Company had six outstanding letters of credit totaling $2.5 million. The letters of credit primarily serve as collateral for the Company for certain facility leases and insurance policies.

The Company has arrangements with certain suppliers that require it to purchase minimum volumes or be subject to monetary penalties. At September 30, 2019, if the Company were to stop purchasing from each of these suppliers, the aggregate amount of the penalty would be approximately $1 million. Most of these arrangements enable the Company to secure supplies of critical components. The Company does not currently anticipate any penalties under these contracts; however, given the significant declines in oil prices in early 2020, the Company is evaluating the impact of potential future purchase volume reductions.

In October 2019, the Company entered into an addendum (the "Addendum") to a supply agreement (the "Supply Agreement"), dated December 11, 2007, with a key supplier. The Addendum extends the Supply Agreement to December 31, 2023 with automatic annual extensions thereafter unless notice of termination is provided. The Addendum extends the Company's exclusivity for the prescribed territory, but carves out of the restriction the competing engine products supplied by General Motors Company and Weichai. The Company committed to maximize sales and service opportunities on both the key supplier and Weichai engine products, recognizing their different value proposition and target markets. The Addendum also updates the minimum product purchase commitments for the period 2019 through 2023 to $40.0 million per year, subject to reductions based on market declines in oil prices and defined prescribed payments to the key supplier triggered by shortfalls in purchases made by the Company during each annual calendar period.

Note 10. Income Taxes

On a quarterly basis, the Company computes an estimated annual effective tax rate considering ordinary income and related income tax expense. Ordinary income refers to income (loss) before income tax expense excluding significant, unusual or infrequently occurring items. The tax effect of an unusual or infrequently occurring item is recorded in the interim period in which it occurs.

The Company has assessed the need to maintain a valuation allowance for deferred tax assets based on an assessment of whether it is more likely than not that deferred tax benefits will be realized through the generation of future taxable income. Appropriate consideration is given to all available evidence, both positive and negative, in assessing the need for a valuation allowance. In assessing the realizability of the Company's deferred tax assets, the Company considered whether it is more likely than not that some or all of the deferred tax assets will be realized through the generation of future taxable income. In making this determination, the Company assessed all of the evidence available at the time, including recent earnings, forecasted income projections and historical performance. The Company determined that the negative evidence outweighed the objectively verifiable positive evidence and continues to maintain a full valuation allowance against deferred tax assets.

The effective tax rate for the three and nine months ended September 30, 2019 was 7.7% and 44.2%, respectively, compared to an effective tax rate for the three and nine months ended September 30, 2018 of (0.6)% and 0.2%, respectively. The effective tax rates for all periods were lower than the applicable U.S. statutory tax rate primarily due to the Company's full valuation allowance and the losses related to the Weichai Warrant (except the three months ended September 30, 2019 which was not impacted by the Weichai Warrant due to the April 2019 exercise). The effective rate in both periods was also impacted by the increase in the deferred tax liability related to indefinite-lived assets which cannot serve as a source of income for the realization of deferred tax assets and states that base tax on gross margin and not pretax income.

Coronavirus Aid, Relief, and Economic Security Act

On March 27, 2020, President Trump signed into law the *Coronavirus Aid, Relief, and Economic Security Act* (the "CARES Act"). Among the changes to the U.S. federal income tax rules, the CARES Act modified net operating loss carryback rules that were eliminated by the 2017 *Tax Cuts and Jobs Act*, restored 100% bonus depreciation for qualified improvement property, increased the limit on the deduction for net interest expense and accelerated the time frame for refunds of alternative minimum tax credits. The Company's ability to carryback the net operating losses to earlier years is expected to result in a tax benefit of $0.8 million. There is no net impact to the Company's deferred tax assets due to the full valuation allowance. The Company will continue to evaluate the effects of the CARES Act as additional legislative guidance becomes available.

Note 11. Stockholders' Equity

Common and Treasury Stock

The changes in shares of Common and Treasury Stock are as follows:

(in thousands)	Common Shares Issued	Treasury Stock Shares	Common Shares Outstanding
Balance as of January 1, 2019	19,067	429	18,638
Net shares issued for Stock awards	—	(168)	168
Shares issued to Weichai *	4,050	—	4,050
Balance as of September 30, 2019	23,117	261	22,856

* See Note 3. *Weichai Transactions* for additional information.

Weichai Warrant

On April 23, 2019, Weichai exercised the Weichai Warrant resulting in the Company issuing 4,049,759 shares of the Company's Common Stock and Weichai becoming the owner of 51.5% of the outstanding shares of the Company's Common Stock, as of such date. See Note 3. *Weichai Transactions* for additional information.

Note 12. Earnings (Loss) Per Share

The Company computes basic earnings (loss) per share by dividing net income (loss) by the weighted-average common shares outstanding during the period. Diluted earnings (loss) per share is calculated to give effect to all potentially dilutive common shares that were outstanding during the period. Weighted-average diluted common shares outstanding primarily reflect the additional shares that would be issued upon the assumed exercise of stock options and the assumed vesting of unvested share awards. The treasury stock method has been used to compute diluted earnings (loss) per share for the three and nine months ended September 30, 2019 and 2018.

The Company issued warrants that represent the right to purchase shares of Common Stock, Stock Appreciation Rights ("SARs") and Restricted Stock Awards ("RSAs"), all of which have been evaluated for their potentially dilutive effect under the treasury stock method. See Note 3. *Weichai Transactions* herein for additional information on the Weichai Warrants and Note 12. *Stock-Based Compensation* in the Company's 2018 Annual Report for additional information on the SARs and the RSAs.

The computations of basic and diluted earnings (loss) per share are as follows:

(in thousands, except per share basis)	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2019	**2018**	**2019**	**2018**
Numerator:				
Net income (loss)	$ 5,756	$ (18,819)	$ 172	$ (44,828)
Denominator:				
Shares used in computing net income (loss) per share:				
Weighted-average basic shares outstanding	22,849	18,625	21,064	18,567
Effect of dilutive securities	27	—	24	—
Weighted-average common shares outstanding – diluted	22,876	18,625	21,088	18,567
Earnings (loss) per common share:				
Earnings (loss) per share of common stock – basic	$ 0.25	$ (1.01)	$ 0.01	$ (2.41)
Earnings (loss) per share of common stock – diluted	$ 0.25	$ (1.01)	$ 0.01	$ (2.41)

The aggregate number of shares excluded from the diluted earnings (loss) per share calculations, because they would have been anti-dilutive, were 0.2 million and 1.8 million shares during the three and nine months ended September 30, 2019, respectively and 3.6 million and 3.9 million shares during the three and nine months ended September 30, 2018, respectively.

Note 13. Related Party Transactions

Weichai Transactions

See Note 3. *Weichai Transactions* for information regarding transactions with Weichai.

Transactions with Joint Ventures

Doosan-PSI, LLC

In 2015, the Company and Doosan Infracore Co., Ltd. ("Doosan"), a subsidiary of Doosan Group, entered into an agreement to form Doosan-PSI, LLC. The Company invested $1.0 million to acquire 50% of the venture, which was formed to operate in the field of developing, designing, testing, manufacturing, assembling, branding, marketing, selling, distributing and providing support for industrial gas engines and all components and materials required for assembly of the gas engines to the global power generation market outside of North America and South Korea. In the fourth quarter of 2019, Doosan and the Company agreed to wind down and dissolve the joint venture. This is expected to be completed in the second quarter of 2020.

Joint Venture Operating Results

The Company's Consolidated Statements of Operations included income of less than $0.1 million and $0.5 million from this investment during each of the three and nine months ended September 30, 2019, respectively. During each of the three and nine months ended September 30, 2018, the income from these investments was $0.1 million and $0.3 million, respectively. The joint venture operating results are presented in *Other income, net* in the Company's Consolidated Statements of Operations.

Note 14. Subsequent Events

As a result of the COVID-19 pandemic, the global economy has experienced substantial turmoil including impacts from the world financial markets which have experienced a period of significant volatility and overall declines. In addition, as of the date of this 2019 Annual Report, due to unprecedented decreases in demand, an oil price war, and economic uncertainty resulting from the COVID-19 pandemic, crude oil prices declined precipitously. A significant portion of the Company's sales and profitability is derived from the sale of products that are used within the oil and gas industry. While the Company has yet to experience significant supply chain interruptions or material cancellations of orders, the potential impact of future disruptions, continued economic uncertainty, and continued depressed crude oil prices and declining rig count levels may have a significant adverse impact on the results of future operations, financial position, and liquidity of the Company. Further, it is reasonably possible that these potential adverse impacts may result in the recognition of material impairments or other related charges.

The Company is aggressively beginning the execution of contingency actions as a result of the expected significant negative impacts of these factors. The Company is reviewing operating expenses as part of the contingency planning process, including prioritizing certain R&D investments in support of the Company's long-term growth objectives. As of the date of this Quarterly Report, the Company has implemented the following temporary cost reduction measures designed to mitigate the operating and financial impacts of the COVID-19 pandemic on its business:

- reduced the hours of operations of the Company's production facilities;
- reduced the work week for all office employees;
- reduced pay for salaried employees by between 10% and 30%, depending on the employee's position;
- suspended the Company's 401(k) plan match;
- deferred spending on certain R&D programs;
- implemented a hiring freeze;
- restricted all non-essential travel; and
- minimized discretionary expenses and consulting services.

On March 27, 2020, President Trump signed into law the CARES Act. The CARES Act, among other things, includes provisions relating to refundable payroll tax credits, deferment of employer side social security payments and income taxes. The income tax implications are discussed within Note 10. *Income Taxes*.

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

The following discussion and analysis includes forward-looking statements about the Company's business and consolidated results of operations for the three and nine months ended September 30, 2019 and 2018, including discussions about management's expectations for the Company's business. These statements represent projections, beliefs and expectations based on current circumstances and conditions and in light of recent events and trends, and these statements should not be construed either as assurances of performance or as promises of a given course of action. Instead, various known and unknown factors are likely to cause the Company's actual performance and management's actions to vary, and the results of these variances may be both material and adverse. See "Forward-Looking Statements." The following discussion should also be read in conjunction with the Company's unaudited consolidated financial statements and the related Notes included in this report.

Executive Overview

The Company designs, engineers, manufactures, markets and sells a broad range of advanced, emission-certified engines and power systems that run on a wide variety of fuels, including natural gas, propane, gasoline, diesel and biofuels, within the energy, industrial and transportation end markets with primary manufacturing, assembly, engineering, research and development ("R&D"), sales and distribution facilities located in suburban Chicago, Illinois, and Darien, Wisconsin. The Company provides highly engineered, comprehensive solutions designed to meet specific customer application requirements and technical specifications, including those imposed by environmental regulatory bodies, such as the U.S. Environmental Protection Agency ("EPA"), the California Air Resources Board ("CARB") and the People's Republic of China's Ministry of Ecology and Environment ("MEE," formerly the Ministry of Environmental Protection).

The Company's products are primarily used by global original equipment manufacturers ("OEMs") and end-user customers across a wide range of applications and equipment that includes standby and prime power generation, demand response, microgrid, combined heat and power, arbor care, material handling (including forklifts), agricultural and turf, construction, pumps and irrigation, compressors, utility vehicles, light- and medium-duty vocational trucks, school and transit buses, and utility power. The Company manages the business as a single reporting segment.

For the three months ended September 30, 2019, the Company's net sales increased $2.2 million, or 2%, from the three months ended September 30, 2018, as a result of increased sales of $15.9 million and $1.6 million in the energy and transportation end markets, respectively, partly offset by a decline of $15.3 million in the industrial end market. Gross margin for the three months ended September 30, 2019 was 19.4%, a strong improvement versus 13.8% in the comparable 2018 period. Gross profit improved by $8.1 million for the three months ended September 30, 2019, while operating expenses decreased by $6.7 million, as compared to the same period in 2018. Additionally, in the 2019 period, the Company recorded no impact from the change in value of the Weichai Warrant, an improvement of $10.2 million versus the comparable 2018 period due to the exercise of the Weichai Warrant in April 2019. Collectively, these factors contributed to a $24.6 million improvement in net income, which was $5.8 million in the 2019 period compared to a net loss of $18.8 million in the same period of 2018. Diluted earnings per share was $0.25 in the 2019 period compared to a diluted loss per share of $1.01 in the comparable 2018 period. Adjusted net income, which excludes certain items described below that the Company believes are not indicative of its ongoing operating performance, was $8.1 million in the 2019 period, an increase of $8.9 million, compared to an Adjusted net loss of $0.7 million in 2018. Adjusted earnings per share was $0.35 in 2019 compared to an Adjusted loss per share of $0.04 in 2018. Adjusted earnings before interest expense, income taxes, depreciation and amortization ("EBITDA") was $12.7 million in 2019 compared to $4.0 million in 2018.

For the nine months ended September 30, 2019, the Company's net sales increased $35.2 million, or 10%, from the nine months ended September 30, 2018, as a result of increased sales of $23.2 million and $15.9 million within the energy and transportation end markets, respectively, partly offset by a sales decline of $3.9 million in the industrial end market. Gross margin for the nine months ended September 30, 2019 was 17.9%, a strong improvement versus 13.1% in the comparable 2018 period. Gross profit improved by $23.4 million for the nine months ended September 30, 2019, while operating expenses decreased by $4.4 million, as compared to the same period in 2018. Additionally, in the 2019 period, the loss from the change in value and exercise of the Weichai Warrant declined by $17.8 million versus the comparable 2018 period. Collectively, these factors contributed to a $45.0 million improvement in net income, which was net income of $0.2 million in the 2019 period compared to a net loss of $44.8 million in the same period of 2018. Diluted earnings per share was $0.01 in the 2019 period compared to a diluted loss per share of $2.41 in the comparable 2018 period. Adjusted net income, which excludes certain items described below that the Company believes are not indicative of its ongoing operating performance, was $16.5 million in the 2019 period, an increase of $22.2 million, compared to an Adjusted net loss of $5.7 million in 2018. Adjusted earnings per share was $0.78 in 2019 compared to an Adjusted loss per share of $0.31 in 2018. Adjusted EBITDA was $29.4 million in 2019 compared to $7.2 million in 2018. Adjusted net income (loss), Adjusted earnings (loss) per share and Adjusted EBITDA are non-GAAP financial measures. For a reconciliation of each of these measures to the nearest applicable GAAP financial measure, as well as additional information about these non-GAAP measures, see the section entitled *Non-GAAP Financial Measures* in this Item 2.

Net sales by geographic area and by end market for the three and nine months ended September 30, 2019 and 2018 are presented below:

(in thousands)	For the Three Months Ended September 30,				For the Nine Months Ended September 30,			
	2019		2018		2019		2018	
Geographic Area		% of Total		% of Total		% of Total		% of Total
North America	$ 125,971	91%	$ 120,955	89%	$ 343,593	87%	$ 312,346	87%
Pacific Rim	6,744	5%	10,913	8%	30,173	8%	32,768	9%
Europe	4,329	3%	3,012	2%	12,712	3%	9,948	3%
Other	1,468	1%	1,438	1%	6,505	2%	2,742	1%
Total	$ 138,512	100%	$ 136,318	100%	$ 392,983	100%	$ 357,804	100%

(in thousands)	For the Three Months Ended September 30,				For the Nine Months Ended September 30,			
	2019		2018		2019		2018	
End Market		% of Total		% of Total		% of Total		% of Total
Energy	$ 64,331	46%	$ 48,481	36%	$ 162,224	41%	$ 139,062	39%
Industrial	37,020	27%	52,367	38%	142,267	36%	146,137	41%
Transportation	37,161	27%	35,470	26%	88,492	23%	72,605	20%
Total	$ 138,512	100%	$ 136,318	100%	$ 392,983	100%	$ 357,804	100%

Recent Trends and Business Outlook

Recent COVID-19 Outbreak and Oil and Gas Market Price Volatility

In January 2020, the World Health Organization ("WHO") announced a global health emergency because of a new strain of coronavirus (the "COVID-19 outbreak") and the risks to the international community as the virus spreads globally. In March 2020, the WHO classified the COVID-19 outbreak as a pandemic (the "COVID-19 pandemic"), based on the rapid increase in exposure globally. The COVID-19 pandemic has resulted in the implementation of significant governmental measures to control the spread of the virus, including quarantines, travel restrictions, business shutdowns, and restrictions on the movement of people in the United States and abroad. These factors, in turn, may not only impact the Company's operations, financial condition, and demand for its goods and services, but its overall ability to react timely to mitigate the impact of the COVID-19 pandemic. The Company is aggressively beginning the execution of contingency actions as a result of the expected significant negative impacts of these factors. The Company is reviewing operating expenses as part of the contingency planning process, including prioritizing certain R&D investments in support of the Company's long-term growth objectives. As of the date of this Quarterly Report, the Company has implemented the following temporary cost reduction measures designed to mitigate the operating and financial impacts of the COVID-19 pandemic on its business:

- reduced the hours of operations of the Company's production facilities;
- reduced the work week for all office employees;
- reduced pay for salaried employees by between 10% and 30%, depending on the employee's position;
- suspended the Company's 401(k) plan match;
- deferred spending on certain R&D programs;
- implemented a hiring freeze;
- restricted all non-essential travel; and
- minimized discretionary expenses and consulting services.

The full impact of the COVID-19 pandemic continues to evolve as of the date of this Quarterly Report.

The global economy has experienced substantial turmoil including impacts from the world financial markets which have experienced a period of significant volatility and overall declines. In addition, as of the date of this Quarterly Report, due to significant decreases on demand and economic uncertainty resulting from the COVID-19 pandemic, crude oil prices declined significantly. A significant portion of the Company's sales and profitability is derived from the sale of products used within the oil and gas industry. While the Company has yet to experience significant supply chain interruptions or material cancellations of orders, the potential impact of future disruptions, continued economic uncertainty, and continued depressed crude oil prices and declining rig count levels may have a significant adverse impact that may result in the recognition of material impairments or other related charges.

Results of Operations

Results of operations for the three and nine months ended September 30, 2019 and 2018:

(in thousands, except per share amounts)	For the Three Months Ended September 30, 2019	For the Three Months Ended September 30, 2018	Change	% Change	For the Nine Months Ended September 30, 2019	For the Nine Months Ended September 30, 2018	Change	% Change
Net sales	$ 138,512	$ 136,318	$ 2,194	2 %	$ 392,983	$ 357,804	$ 35,179	10 %
Cost of sales	111,640	117,510	(5,870)	(5)%	322,793	311,056	11,737	4 %
Gross profit	26,872	18,808	8,064	43 %	70,190	46,748	23,442	50 %
Gross margin %	*19.4%*	*13.8%*	*5.6 %*		*17.9%*	*13.1%*	*4.8 %*	
Operating expenses:								
Research, development and engineering expenses	6,366	7,708	(1,342)	(17)%	18,695	20,691	(1,996)	(10)%
Research, development and engineering expenses as a % of sales	*4.6%*	*5.7%*	*(1.1)%*		*4.8%*	*5.8%*	*(1.0)%*	
Selling, general and administrative expenses	11,461	16,374	(4,913)	(30)%	41,476	42,904	(1,428)	(3)%
Selling, general and administrative expenses as a % of sales	*8.3%*	*12.0%*	*(3.7)%*		*10.6%*	*12.0%*	*(1.4)%*	
Amortization of intangible assets	910	1,321	(411)	(31)%	2,729	3,687	(958)	(26)%
Total operating expenses	18,737	25,403	(6,666)	(26)%	62,900	67,282	(4,382)	(7)%
Operating income (loss)	8,135	(6,595)	14,730	NM	7,290	(20,534)	27,824	(136)%
Other expense:								
Interest expense	1,921	1,974	(53)	(3)%	6,156	5,425	731	13 %
Loss from change in value and exercise of warrants	—	10,200	(10,200)	(100)%	1,352	19,200	(17,848)	(93)%
Other income, net	(25)	(68)	43	(63)%	(526)	(257)	(269)	105 %
Total other expense	1,896	12,106	(10,210)	(84)%	6,982	24,368	(17,386)	(71)%
Income (loss) before income taxes	6,239	(18,701)	24,940	(133)%	308	(44,902)	45,210	(101)%
Income tax expense (benefit)	483	118	365	NM	136	(74)	210	NM
Net income (loss)	$ 5,756	$ (18,819)	$ 24,575	(131)%	$ 172	$ (44,828)	$ 45,000	(100)%
Earnings (loss) per common share:								
Basic	$ 0.25	$ (1.01)	$ 1.26	(125)%	$ 0.01	$ (2.41)	$ 2.42	(100)%
Diluted	$ 0.25	$ (1.01)	$ 1.26	(125)%	$ 0.01	$ (2.41)	$ 2.42	(100)%
Non-GAAP Financial Measures:								
Adjusted net income (loss) *	$ 8,147	$ (722)	$ 8,869	NM	$ 16,502	$ (5,701)	$ 22,203	NM
Adjusted earnings (loss) per share *	$ 0.35	$ (0.04)	$ 0.39	NM	$ 0.78	$ (0.31)	$ 1.09	NM
EBITDA *	$ 10,340	$ (14,081)	$ 24,421	(173)%	$ 13,068	$ (31,941)	$ 45,009	(141)%
Adjusted EBITDA *	$ 12,731	$ 4,016	$ 8,715	NM	$ 29,398	$ 7,186	$ 22,212	NM

NM Not meaningful
* See reconciliation of non-GAAP financial measures to GAAP results below

Net Sales

Net sales increased $2.2 million, or 2%, during the three months ended September 30, 2019 compared to the three months ended September 30, 2018, as a result of increased sales of $15.9 million and $1.6 million in the energy and transportation end markets, respectively, partly offset by a decline of $15.3 million in the industrial end market. The sales increase within the energy end market is primarily attributable to increased demand for power generation products, including those used within the oil and gas industry, and for demand response products. The increase within the transportation end market primarily reflects higher demand for products used in the medium-duty truck market. The decrease within the industrial end market primarily reflects lower demand for products used in the material handling/forklift and arbor care markets.

Net sales increased $35.2 million, or 10%, during the nine months ended September 30, 2019 compared to the nine months ended September 30, 2018, as a result of increased sales of $23.2 million and $15.9 million within the energy and transportation end markets, respectively, partly offset by a sales decline of $3.9 million in the industrial end market. The increase in the energy end market is primarily attributable to higher demand for power generation products, including those used within the oil and gas industry, partly offset by lower sales of demand response products. The increase in the transportation end market is primarily attributable to higher demand for products used in the medium-duty truck and school bus markets. The industrial end market decline is primarily due to lower demand for products used in the material handling/forklift and arbor care markets.

Gross Profit

Gross margin was 19.4% and 13.8% during the three months ended September 30, 2019 and 2018, respectively. Gross profit increased during the three months ended September 30, 2019 by $8.1 million, or 43%, compared to the three months ended September 30, 2018, primarily due to higher sales, favorable product mix, strategic price increases, lower warranty costs and operational productivity improvements. For the three months ended September 30, 2019, warranty costs were $3.0 million (net of supplier recoveries of $0.1 million), a decline of $0.8 million as compared to warranty costs of $3.8 million (net of supplier recoveries of $0.7 million) for the three months ended September 30, 2018. Warranty costs for the three months ended September 30, 2019 included $1.2 million of charges related to specific engine supplier quality issues, for which the Company is actively seeking cost reimbursement.

Gross margin was 17.9% and 13.1% during the nine months ended September 30, 2019 and 2018, respectively. Gross profit increased during the nine months ended September 30, 2019 by $23.4 million, or 50%, compared to the nine months ended September 30, 2018, primarily due to higher sales, favorable product mix, lower warranty costs, strategic price increases and operational productivity improvements. For the nine months ended September 30, 2019, warranty costs were $7.4 million (net of supplier and insurance recoveries of $3.0 million), including $2.7 million of charges for adjustments to preexisting warranties, a decline of $4.8 million as compared to warranty costs of $12.2 million (net of supplier recoveries of $0.9 million) for the nine months ended September 30, 2018, including $3.8 million of charges for adjustments to preexisting warranties. Warranty costs for the nine months ended September 30, 2019 included $4.1 million of charges related to specific engine supplier quality issues, for which the Company is actively seeking cost reimbursement.

Research, Development and Engineering Expenses

Research, development and engineering expenses during the three months ended September 30, 2019 were $6.4 million, a decrease of $1.3 million, or 17%, from the three months ended September 30, 2018 levels, primarily as a result of the timing of spending related to projects.

Research, development and engineering expenses during the nine months ended September 30, 2019 were $18.7 million, a decrease of $2.0 million, or 10%, from the nine months ended September 30, 2018 levels, primarily as a result of the timing of spending related to projects.

Selling, General and Administrative Expenses

Selling, general and administrative (“SG&A”) expenses decreased during the three months ended September 30, 2019 by $4.9 million, or 30%, compared to the three months ended September 30, 2018. The decrease in SG&A expenses are largely attributable to a $5.2 million reduction in incremental financial reporting and government investigation expenses and a $0.5 million reduction in key employee retention program costs, partly offset by higher wages, benefits and incentive compensation expense and a $0.3 million increase in severance costs.

Selling, general and administrative expenses decreased during the nine months ended September 30, 2019 by $1.4 million, or 3%, compared to the nine months ended September 30, 2018. The decrease in SG&A expenses are largely attributable to a $5.3 million reduction in incremental financial reporting and government investigation expenses and a $1.5 million reduction in key employee retention program costs, partly offset by higher wages, benefits and incentive compensation expense, a $1.9 million increase in severance expense and a $0.1 million increase in stock-based compensation expense.

Interest Expense

Interest expense decreased $0.1 million to $1.9 million for the three months ended September 30, 2019 compared to the three months ended September 30, 2018.

Interest expense increased $0.7 million to $6.2 million for the nine months ended September 30, 2019 compared to the nine months ended September 30, 2018, in part due to higher outstanding debt levels and a higher interest rate related to the Unsecured Senior Notes in the 2019 period.

Loss from Change in Value and Exercise of Warrants

For the three month period ended September 30, 2019, there was no impact from a change in value of the Weichai Warrants due to the exercise of the Weichai Warrants in April 2019. The Company recognized a loss of $10.2 million related to the change in value of the Weichai Warrants during the three month period ended September 30, 2018.

The Company recognized a loss of $1.4 million and $19.2 million for the nine months ended September 30, 2019 and 2018, respectively, from the change in the value and exercise of the Weichai Warrants. The loss recorded for the nine months ended September 30, 2019 includes the impact of the exercise of the Weichai Warrants in April 2019.

See Note 3. Weichai Transactions and Note 8. *Fair Value of Financial Instruments*, included in Part 1, Item 1. *Financial Statements*, for additional information.

Other Income, Net

Other income, net was nominal for each of the three month periods ended September 30, 2019 and 2018 resulting in an immaterial change period-over-period.

Other income, net increased by $0.3 million during each of the nine month periods ended September 30, 2019 compared to the nine months ended September 30, 2018 principally as a result of higher income earned from the Company's joint venture with Doosan.

See Note 13. *Related Party Transactions*, included in Part 1, Item 1. *Financial Statements*, for additional information.

Income Tax Expense

The Company recorded income tax expense of $0.5 million for the three months ended September 30, 2019, as compared to income tax expense of $0.1 million for the three months ended September 30, 2018. The Company's pretax income was $6.2 million for the three months ended September 30, 2019, compared to a pretax loss of $18.7 million for the three months ended September 30, 2018. There was no significant change in the Company's tax provision as the Company continues to record a full valuation allowance against deferred tax assets.

The Company recorded income tax expense of $0.1 million for the nine months ended September 30, 2019, as compared to an income tax benefit of $0.1 million for the nine months ended September 30, 2018. The Company's pretax income was $0.3 million for the nine months ended September 30, 2019, compared to a pretax loss of $44.9 million for the nine months ended September 30, 2018. There was no significant change in the Company's tax provision as the Company continues to record a full valuation allowance against deferred tax assets.

See Note 10. *Income Taxes*, included in Part 1, Item 1. *Financial Statements*, for additional information related to the Company's income tax provision.

Non-GAAP Financial Measures

In addition to the results provided in accordance with U.S. GAAP above, this report also includes non-GAAP (adjusted) financial measures. Non-GAAP financial measures provide insight into selected financial information and should be evaluated in the context in which they are presented. These non-GAAP financial measures have limitations as analytical tools and should not be considered in isolation from, or as a substitute for, financial information presented in compliance with U.S. GAAP, and non-GAAP financial measures as reported by the Company may not be comparable to similarly titled amounts reported by other companies. The non-GAAP financial measures should be considered in conjunction with the consolidated financial statements, including the related notes, and *Management's Discussion and Analysis of Financial Condition and Results of Operations* included in this report. Management does not use these non-GAAP financial measures for any purpose other than the reasons stated below.

Non-GAAP Financial Measure	Comparable GAAP Financial Measure
Adjusted net income (loss)	Net income (loss)
Adjusted earnings (loss) per share	Earnings (loss) per common share – diluted
EBITDA	Net income (loss)
Adjusted EBITDA	Net income (loss)

The Company believes that Adjusted net income (loss), Adjusted earnings (loss) per share, EBITDA, and Adjusted EBITDA provide relevant and useful information, which is widely used by analysts, investors and competitors in its industry as well as by the Company's management in assessing the performance of the Company. Adjusted net income (loss) is defined as net income as adjusted for certain items that the Company believes are not indicative of its ongoing operating performance. Adjusted earnings (loss) per share is a measure of the Company's diluted net earnings (loss) per share adjusted for the impact of special items. EBITDA provides the Company with an understanding of earnings before the impact of investing and financing charges and income taxes. Adjusted EBITDA further excludes the effects of other non-cash and certain other items that do not reflect the ordinary earnings of the Company's operations.

Adjusted net income (loss), Adjusted earnings (loss) per share, EBITDA, and Adjusted EBITDA are used by management for various purposes, including as a measure of performance of the Company's operations and as a basis for strategic planning and forecasting. Adjusted net income (loss), Adjusted earnings (loss) per share, and Adjusted EBITDA may be useful to an investor because these measures are widely used to evaluate companies' operating performance without regard to items excluded from the calculation of such measures, which can vary substantially from company to company depending on the accounting methods, the book value of assets, the capital structure and the method by which the assets were acquired, among other factors. They are not, however, intended as alternative measures of operating results or cash flow from operations as determined in accordance with U.S. GAAP.

The following table presents a reconciliation from Net income (loss) to Adjusted net income (loss) for the three and nine months ended September 30, 2019 and 2018:

(in thousands)	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2019	2018	2019	2018
Net income (loss)	$ 5,756	$ (18,819)	$ 172	$ (44,828)
Changes in value of warrants [1]	—	10,200	1,352	19,200
Stock-based compensation [2]	173	215	841	783
Key employee retention program [3]	10	551	492	2,030
Strategic alternatives and strategic review expenses [4]	—	—	—	24
Severance [5]	267	—	1,865	—
Incremental financial reporting and government investigation expenses [6]	1,941	7,131	11,780	17,090
Adjusted net income (loss)	$ 8,147	$ (722)	$ 16,502	$ (5,701)

The following table presents a reconciliation from Earnings (loss) per common share – diluted to Adjusted earnings (loss) per share for the three and nine months ended September 30, 2019 and 2018:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2019	2018	2019	2018
Earnings (loss) per common share – diluted	$ 0.25	$ (1.01)	$ 0.01	$ (2.41)
Changes in value of warrants [1]	—	0.55	0.06	1.03
Stock-based compensation [2]	0.01	0.01	0.04	0.04
Key employee retention program [3]	—	0.03	0.02	0.11
Strategic alternatives and strategic review expenses [5]	—	—	—	—
Severance [5]	0.01	—	0.09	—
Incremental financial reporting and government investigation expenses [6]	0.08	0.38	0.56	0.92
Adjusted earnings (loss) per share – diluted	$ 0.35	$ (0.04)	$ 0.78	$ (0.31)
Diluted Shares (in thousands)	22,876	18,625	21,088	18,567

The following table presents a reconciliation from Net income (loss) to EBITDA and Adjusted EBITDA for the three and nine months ended September 30, 2019 and 2018:

(in thousands)	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2019	2018	2019	2018
Net income (loss)	$ 5,756	$ (18,819)	$ 172	$ (44,828)
Interest expense	1,921	1,974	6,156	5,425
Income tax expense	483	118	136	(74)
Depreciation	1,270	1,325	3,875	3,849
Amortization of intangible assets	910	1,321	2,729	3,687
EBITDA	10,340	(14,081)	13,068	(31,941)
Change in value of warrants [1]	—	10,200	1,352	19,200
Stock-based compensation [2]	173	215	841	783
Key employee retention program [3]	10	551	492	2,030
Strategic alternatives and strategic review expenses [4]	—	—	—	24
Severance [5]	267	—	1,865	—
Incremental financial reporting and government investigation expenses [6]	1,941	7,131	11,780	17,090
Adjusted EBITDA	$ 12,731	$ 4,016	$ 29,398	$ 7,186

1. Amounts consist of changes in the value, including the impact of the exercise in April 2019, of the Weichai Warrant.
2. Amounts reflect non-cash stock-based compensation expense (amounts excludes nil and $0.3 million for the three months ended September 30, 2019 and 2018 and $0.3 million and $1.2 million for the nine months ended September 30, 2019 and 2018, respectively, associated with the retention programs (see note 3 below)).
3. Amounts represent incremental compensation costs (including nil and $0.3 million for the three months ended September 30, 2019 and 2018 and $0.3 million and $1.2 million for the nine months ended September 30, 2019 and 2018, respectively, of stock-based compensation) incurred to provide retention benefits to certain employees.
4. Represents professional services expenses incurred in connection with the evaluation of strategic alternatives and financing options.
5. Amounts represent severance and other post-employment costs for certain former employees of the Company.
6. Amounts represent professional services fees related to the Company's efforts to restate prior period financial statements, prepare, audit and file delinquent financial statements, and remediate internal control material weaknesses as well as fees and reserves related to the SEC and USAO investigations. The amounts exclude $0.1 million and $1.1 million for the three and nine months ended September 30, 2019, respectively, and $0.3 million and $1.3 million for the three and nine months ended September 30, 2018, respectively, of professional services fees related to the audit of the Company's financial statements and ongoing internal control remediation.

Cash Flows

Cash was impacted as follows:

(in thousands)	For the Nine Months Ended September 30,			
	2019	2018	Change	% Change
Net cash provided by (used in) operating activities	$ 19,122	$ (3,674)	$ 22,796	NM
Net cash used in investing activities	(2,035)	(8,916)	6,881	NM
Net cash (used in) provided by financing activities	(17,140)	14,604	(31,744)	NM
Net (decrease) increase in cash and restricted cash	$ (53)	$ 2,014	$ (2,067)	NM
Capital expenditures	$ (2,048)	$ (2,321)	$ 273	NM

Cash Flows for the Nine Months Ended September 30, 2019

Cash Flow from Operating Activities

Net cash provided by operating activities was $19.1 million in the nine months ended September 30, 2019 compared to net cash used in operating activities of $3.7 million in the nine months ended September 30, 2018, resulting in an increase of $22.8 million in cash provided by operating activities year over year. This was primarily due to an increase in net income of $45.0 million, partially offset by a decrease in non-cash adjustments of $21.4 million primarily related to the change in value of the Weichai Warrant and intangible amortization, and a decrease in cash provided by working capital accounts of $0.7 million.

Cash Flow from Investing Activities

Net cash used in investing activities was $2.0 million in the nine months ended September 30, 2019 compared to net cash used in investing activities of $8.9 million in the nine months ended September 30, 2018 resulting in a decrease of $6.9 million of net cash used in investing activities year-over-year. Cash flows from investing activities in the nine months ended September 30, 2019 primarily consisted of capital expenditures on materials and equipment. During the nine months ended September 30, 2018, the Company purchased intellectual property ("IP") from AGA Systems, LLC ("AGA") and emissions testing equipment from Ricardo, Inc. The Company paid $6.6 million in cash related to these asset acquisitions during the nine months ended September 30, 2018. Similar transactions did not occur during the nine months ended September 30, 2018, resulting in the decline in net cash used in investing activities.

Cash Flow from Financing Activities

The Company used $17.1 million in cash for financing activities in the nine months ended September 30, 2019 compared to $14.6 million in cash generated by financing activities in the nine months ended September 30, 2018. The cash used in financing activities for the nine months ended September 30, 2019 was primarily attributable to net cash payments on the Wells Fargo Credit Agreement compared to net cash advances during the nine months ended September 30, 2018.

Liquidity and Capital Resources

On April 2, 2020, the Company closed on its new senior secured revolving credit facility pursuant to that certain credit agreement dated March 27, 2020, between the Company and Standard Chartered Bank ("Standard Chartered"), as administrative agent (the "Credit Agreement"). The Credit Agreement, which allows the Company to borrow up to $130.0 million, matures on March 26, 2021 with an optional 60-day extension subject to certain conditions and payment of a 0.25% extension fee. The Credit Agreement bears interest at either the alternate base rate or LIBOR plus 2.00%, and the Company is required to pay a 0.25% commitment fee on the average daily unused portion of the revolving credit facility under the Credit Agreement. The Credit Agreement is secured by substantially all of the Company's assets and includes certain financial covenants as well as a change of control provision. On April 2, 2020, the Company borrowed $95.0 million under the Credit Agreement and utilized the funds (i) to repay the outstanding balance of $16.8 million under the credit agreement between the Company and Wells Fargo Bank, N.A. ("Wells Fargo"), as administrative agent (the "Wells Fargo Credit Agreement"), (ii) to fully redeem and discharge $55.0 million in aggregate principal amount of the unsecured 5.50% senior notes, due June 2020 (the "Unsecured Senior Notes") and (iii) for general corporate purposes. The Wells Fargo Credit Agreement was terminated in connection with the repayment of the outstanding balance. On April 29, 2020, the Company borrowed an additional $35.0 million under the Credit Agreement, which is the remaining portion of availability, providing the Company with greater financial flexibility. As of April 29, 2020, the Company had borrowings outstanding of $130.0 million under the Credit Agreement and a cash balance in excess of $45 million. These amounts reflect a net positive cash impact from customer prepayments of $11.8 million.

Significant uncertainties exist about the Company's ability to refinance, extend, or repay its outstanding indebtedness, maintain sufficient liquidity to fund its business activities, and maintain compliance with the covenants and other requirements under the Credit Agreement. Based on the Company's current forecasts, without additional financing, the Company anticipates that it will not have sufficient cash and cash equivalents to repay the Credit Agreement by the March 26, 2021 maturity date. Management currently plans to seek additional liquidity from its current or other lenders before March 26, 2021. There can be no assurance that the Company will be able to successfully complete a refinancing on acceptable terms or repay this outstanding indebtedness when required or if at all.

Additionally, in early 2020, the global economy has experienced substantial turmoil including impacts from the world financial markets which have experienced a period of significant volatility and overall declines. In addition, in early March 2020, due to unprecedented decreases in demand, an oil price war, and economic uncertainty resulting from the COVID-19 pandemic, crude oil prices have declined precipitously. A significant portion of the Company's sales and profitability is derived from the sale of products that are used within the oil and gas industry. While the Company has yet to experience supply chain interruptions or material cancellations of orders, the potential impact of future disruptions, continued economic uncertainty, and continued depressed crude oil prices and declining rig count levels may have a significant adverse impact that may result in the recognition of material impairments or other related charges. Moreover, the full impact of the COVID-19 pandemic on the Company's operations and liquidity continues to evolve.

Due to uncertainties surrounding the Company's ability to refinance, extend, or repay its outstanding indebtedness, maintain sufficient liquidity to fund its business activities, and maintain compliance with the covenants and other requirements under the Credit Agreement, substantial doubt exists as to its ability to continue as a going concern within one year after the date that these financial statements are issued. If the Company does not have sufficient liquidity to fund its business activities, it may be forced to limit its business activities or be unable to continue as a going concern, which would have a material adverse effect on its results of operations and financial condition.

As of September 30, 2019, the Company's total debt obligations under the Wells Fargo Credit Agreement and the Unsecured Senior Notes were $91.7 million in the aggregate, with available borrowing capacity of $19.5 million under the Wells Fargo Credit Agreement. In relation to last-time buys of GM 6.0L engines, the Company had a net positive impact from customer prepayments of approximately $10.8 million as of September 30, 2019.

The Wells Fargo Credit Agreement contained certain covenants for which a failure to satisfy could have resulted in a default under the Wells Fargo Credit Agreement. See Item 8. *Financial Statements and Supplementary Data* Note 6. *Debt* for additional information related to a waiver obtained from Wells Fargo on May 16, 2019 that waived the failure to satisfy financial information covenants through December 31, 2019.

Off-Balance Sheet Arrangements

At September 30, 2019, the Company had six outstanding letters of credit totaling $2.5 million. See Item 1. Note 9. *Commitments and Contingencies* for additional information related to the Company's off-balance sheet arrangements and the outstanding letters of credit.

Critical Accounting Policies and Estimates

The Company's consolidated financial statements are prepared in accordance with U.S GAAP. Preparation of these financial statements requires the Company 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. The Company's most critical accounting policies and estimates are those most important to the portrayal of its financial condition and results of operations and which require the Company to make its most difficult and subjective judgments, often as a result of the need to make estimates regarding matters that are inherently uncertain. The Company has identified the following as its most critical accounting policies and judgments. Although management believes that its estimates and assumptions are reasonable, they are based on information available when they are made and, therefore, may differ from estimates made under different assumptions or conditions.

The Company's significant accounting policies are consistent with those discussed in Note 1. *Summary of Significant Accounting Policies and Other Information*, to the consolidated financial statements and the MD&A section of the 2018 Annual Report. During the nine months ended September 30, 2019, there were no significant changes in the application of critical accounting policies.

The Company has identified the following accounting policies as its most critical because they require the Company to make difficult, subjective, and complex judgments:

- Revenue Recognition
- Allowance for Doubtful Accounts
- Inventories
- Goodwill and Other Intangibles
- Impairment of Long-Lived Assets
- Warranty
- Weichai Warrants
- Deferred Tax Asset Valuation Allowance
- Uncertain Tax Positions

Impact of New Accounting Standards

For information about recently issued accounting pronouncements, see Note 1. *Summary of Significant Accounting Policies and Other Information*, included in Part 1, Item 1.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

The Company is a smaller reporting company as defined by Rule 12b-2 of the Exchange Act and is not required to provide the information under this item.

Item 4. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures

The term “disclosure controls and procedures” is defined in Rule 13a-15(e) of the Exchange Act as “controls and other procedures of an issuer that are designed to ensure that information required to be disclosed by the issuer in the reports that it files or submits under the Act are recorded, processed, summarized and reported, within the time periods specified in the SEC rules and forms.” The Company’s disclosure controls and procedures are designed to ensure that material information relating to the Company and its consolidated subsidiaries is accumulated and communicated to its management, including its Chief Executive Officer and its Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosures.

The Company’s management, with the participation of its Chief Executive Officer and Chief Financial Officer, conducted an evaluation of the effectiveness of the Company’s disclosure controls and procedures as of September 30, 2019 (the end of the period covered by this Quarterly Report on Form 10-Q). Based upon that evaluation, the Company’s Chief Executive Officer and Chief Financial Officer have concluded that the Company’s disclosure controls and procedures were not effective as of September 30, 2019, because of the previously reported material weaknesses in internal control over financial reporting, as described below.

Ongoing Remediation of Material Weaknesses in Internal Control over Financial Reporting

As previously disclosed under “Item 9A – Controls and Procedures” in the 2018 Annual Report, the Company’s management concluded that its internal control over financial reporting was not effective based on the material weaknesses identified. Management is committed to the continued implementation of remediation efforts to address the material weaknesses. The remediation efforts summarized below, which have been or will be implemented, are intended both to address the identified material weaknesses and to enhance the Company’s overall internal control environment.

Control Environment, Risk Assessment, Information and Communication, and Monitoring

Control Environment:

Since 2017, the Company has either replaced or appointed new Board and Audit Committee members, a Chief Executive Officer, a Chief Financial Officer and a Vice President, Internal Audit. These changes, along with the actions of these individuals and other senior management, have collectively improved the tone of integrity, transparency and support of the Company’s updated Code of Business Conduct and Ethics.

The Company has updated its Code of Business Conduct and Ethics and has initiated an ongoing training program to help ensure employees understand and comply with the Code. The Company continues to enhance the program to provide extensive communications and training to employees across the entire organization regarding the importance of integrity and accountability.

The Company has established a process to identify and address internal control weaknesses through the internal control function.

Skillset and Competency:

The Company continues to assess the level of and technical skills in the information technology (“IT”) function to support the design and implementation of IT general controls (“ITGCs”). The IT function has been reorganized under the leadership of the Chief Financial Officer, and the Company is actively recruiting for a Chief Information Officer as well as certain technical IT positions.

Policies and Procedures:

- The Company has drafted a revised delegation of authority policy that appoints tiered approvers based upon risk and materiality of the transaction.
- The Company has identified a central repository to maintain all the Company’s policies, is providing training to users and is developing a framework to establish responsibility and accountability for executing and monitoring policies and procedures.
- The Company has drafted and is in the process of finalizing critical accounting, IT and record retention policies.
- The Company continues to create a culture of continuous improvement and design a framework for management to proactively and openly self-identify, document, reassess, report and remediate policies, procedures and control issues.

Segregation of Duties:

- The Company is establishing standards governing the segregation of incompatible duties across the organization.
- The Company is designing various accounting processes and application and system controls to adequately segregate job responsibilities and system access throughout the organization and to implement applicable mitigating internal controls.
- The Company is in the process of a technical upgrade to its Enterprise Resource Planning System ("ERP System") and is redesigning system access roles across the Company to improve the segregation of incompatible duties.

Control Activities

As part of the overall remediation plan, the Company is designing and implementing review and approval controls over data utilized in various accounting processes. These controls will address the accuracy, timely recording and completeness of data used in the determination of significant accounting estimates, reserves and valuations as well as impacted presentation and disclosures in accordance with U.S. GAAP.

Revenue Accounting:

- The Company is designing and implementing policies and procedures to ensure that critical inputs affecting the accuracy and timeliness of revenue recognition and related reserves and sales allowances are communicated to the accounting department on a timely basis.
- The Company has established and has begun implementing improved review and approval controls across the Company to ensure that revenue, including that of nonroutine revenue transactions, is recognized consistently in accordance with U.S. GAAP.
- The Company has developed sales transaction review procedures to review certain key transaction attributes.

Capitalization:

The Company is designing and implementing policies, procedures and controls over capitalization, including, but not limited to, the capitalization of costs incurred on capital asset projects and accounting treatment for research and development activities.

Complex and Nonroutine Transactions:

The Company is designing and implementing policies, procedures and controls over the evaluation, review and approval of complex and nonroutine transactions, including, but not limited to, identification of reporting units and triggering events that could impact the assessment of potential impairments of property, plant and equipment, intangibles and goodwill, accounting for debt transactions, purchase accounting for business combinations and lease classification.

Reserves and Accruals:

The Company is designing and implementing policies, procedures and controls over the review and approval of key reserves and accruals, including, but not limited to, excess and obsolete inventory and warranty reserves.

Period End Close/Accounting Documentation:

- The Company is designing and implementing policies, procedures and controls over the period-end close process and related documentation including, but not limited to, period-end checklists, review and approval of journal entries, taxes, inventory in-transit, account roll forwards and reconciliations, general-ledger account maintenance and financial statement analysis/thresholds.
- The Company has implemented a formal Section 302 disclosure and certification program that requires management to complete representation letters and disclosure sub-certification questionnaires in connection with SEC filings.

Information Technology:

- The Company has reconstructed its ITGC framework to focus on controls that mitigate key financial reporting risks.
- The Company has designed and is implementing controls over access, change management and IT operations to ensure that access rights are restricted to appropriate individuals, and that data integrity is maintained via effective change controls over system updates and over the flow of data between systems.
- The Company is planning both a technical upgrade as well as a re-implementation of its ERP System to further improve and automate ITGCs as well as other business process controls.

Data Maintenance:

- The Company is designing and implementing procedures and controls to appropriately identify and assess changes made to data repositories that could significantly impact data integrity and the internal control framework, including, but not limited to, (i) creating centralized, complete and accurate data repositories, (ii) maintaining customer and vendor master files, employee data files, perpetual inventory records, inventory cycle counts, stock compensation agreements and debt arrangements and (iii) communicating an enterprise data management policy and record retention policy.

- The Company is developing procedures to review and validate underlying data supporting the internal controls. When fully implemented and operational, the Company believes the measures described above will remediate the control deficiencies that have led to the material weaknesses it has identified and will strengthen its internal control over financial reporting. The Company is committed to continuing to improve its internal control processes and it will continue to review its financial reporting controls and procedures. As the Company continues to evaluate and work to improve its internal control over financial reporting, it may determine that a need exists to take additional measures to address control deficiencies or modify certain remediation measures described above.

Changes in Internal Control over Financial Reporting

Other than the ongoing remediation efforts described above, there have been no changes in the Company’s internal control over financial reporting during the quarter ended September 30, 2019 that have materially affected, or are reasonably likely to materially affect, its internal control over financial reporting.

PART II – OTHER INFORMATION

Item 1. Legal Proceedings.

See Note 9. *Commitments and Contingencies*, included in Part I, Item 1. *Financial Statements*, for a discussion of legal proceedings, which are incorporated herein by reference.

Item 1A. Risk Factors.

The Company is a smaller reporting company as defined by Rule 12b-2 of the Exchange Act and is not required to provide the information under this item.

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

None.

Item 3. Defaults upon Senior Securities.

None.

Item 4. Mine Safety Disclosures.

Not applicable.

Item 5. Other Information.

Not applicable.

Item 6. Exhibits.

EXHIBIT INDEX

The following documents listed below that have been previously filed with the SEC (1934 Act File No. 001-35944) are incorporated herein by reference:

			Incorporated by Reference Herein			
Exhibit No.		**Exhibit Description**	**Form**	**Exhibit**	**Filing Date**	**File No.**
10.1	* ††	Confidential Consulting Agreement.				
31.1		Certification of Chief Executive Officer, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.				
31.2		Certification of Chief Financial Officer, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.				
32.1	**	Certification of Chief Executive Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes Oxley Act of 2002.				
32.2	**	Certification of Chief Financial Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes Oxley Act of 2002.				
101.INS	*	XBRL Instance Document.				
101.SCH		XBRL Taxonomy Extension Schema Document.				
101.CAL		XBRL Taxonomy Extension Calculation Linkbase Document.				
101.LAB		XBRL Taxonomy Extension Labels Linkbase Document.				
101.PRE		XBRL Taxonomy Extension Presentation Linkbase Document.				
101.DEF	*	XBRL Taxonomy Definition Linkbase Document.				

* Filed with this Report.

** This exhibit shall not be deemed “filed” for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that Section. Such exhibit shall not be deemed incorporated into any filing under the Securities Act of 1933, as amended, or the Exchange Act.

†† Management contract or compensatory plan or arrangement.

SIGNATURES

Pursuant to the requirements of the Exchange Act, the registrant has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized, on the 4th day of May, 2020.

POWER SOLUTIONS INTERNATIONAL, INC.

By: /s/ Charles F. Avery, Jr.

Name: **Charles F. Avery, Jr.**

Title: Chief Financial Officer (Principal Financial Officer)

<u>CONFIDENTENTIAL CONSULTING AGREEMENT AND RELEASE</u>

This Confidential Consulting Agreement and Release (the “Agreement”) is entered into between William Buzogany (“Buzogany”) and Power Solutions International, Inc. (the “Company”) (collectively, the “Parties”). This Agreement will be effective upon expiration of the revocation period provided in Section 11 of this Agreement (the “Effective Date”).

RECITALS

WHEREAS, Buzogany currently serves as the Company’s Vice President of Human Resources and General Counsel and has been employed with the Company since February 15, 2014;

WHEREAS, Buzogany and the Company entered into an Employment Agreement (the “Employment Agreement”) dated and effective on September 15, 2017;

WHEREAS, the Parties have mutually agreed that it is in the best interests of the Parties to terminate the Employment Agreement and move Buzogany into a consulting role with the Company (the “Consultancy”) under the terms and conditions stated herein;

WHEREAS, Buzogany and PSI desire to enter into this Agreement to (a) provide Buzogany with the benefits described below in recognition of his contribution and service to the Company, (b) provide for Buzogany’s cooperation as needed with respect to the transition of his current responsibilities, and (c) avoid any disputes between them relating to or arising from Buzogany’s employment by the Company or his termination of employment.

NOW, THEREFORE, in consideration of the promises and mutual agreements set forth in this Agreement, the receipt and sufficiency of which are hereby acknowledged, the Parties agree as follows:

AGREEMENT

1. **Resignation of Employment.** Buzogany agrees to resign his employment with Company, effective July 17, 2019 (the “Effective Date”). Buzogany’s resignation will be announced in a statement prepared by the Company as mutually agreed with Buzogany over its content; however, the Company will apply the requirements of Regulation S-K in its reasonable judgment, as applicable. The Company will continue to employ Buzogany and will continue to provide Buzogany with all compensation and benefits set forth in Section 4 of his Employment Agreement effective September 15, 2017 (“Employment Agreement”) through the Effective Date. On or before the next regularly scheduled pay period following the Effective Date, Buzogany will receive payment for any unpaid final wages for time worked through and including the Effective Date. As of the Effective Date, all unvested stock awards, if any, will be cancelled. Except as set forth herein, all compensation and employee benefits will terminate on the Effective Date. Except as specifically provided in this Section 1 and with respect to Termination Benefits in Section 2, Buzogany acknowledges and agrees he is not entitled to any other payment, benefits, or consideration arising from his employment with the Company.

2. **Separation Benefits.**

A. The Company will pay Buzogany severance pay in the total amount of $189,000 less applicable withholdings in 12 equal monthly installments of $15,750 payable on the first day of each month beginning on July 17, 2019. The payment will not be considered compensation for retirement or other compensation plan purposes.

B. If Buzogany timely elects COBRA health insurance continuation coverage, the Company will pay a proportional share of the premiums owed by Buzogany as if Buzogany were still employed by the Company for a period of 12 months. Buzogany will be responsible for submitting all notices and forms required to elect COBRA.

C. The Company will take necessary steps to transfer the cell phone number currently assigned to Buzogany from the Company's account to Buzogany's account, and Buzogany shall assume responsibility for charges incurred through use of that number.

Buzogany acknowledges and agrees that he is responsible for all tax liability, if any, arising from the Separation Benefits provided in Section 2.

3. **Indemnification.** The Company agrees that the Indemnification Agreement between Buzogany and the Company dated October 26, 2016 and any duly executed amendments thereto ("Indemnification Agreement") remains in full force and effect. A true and accurate copy of the Indemnification Agreement is attached hereto as Exhibit A and is fully incorporated by reference.

4. **Expenses.** Buzogany agrees to disclose any amounts PSI paid for airline tickets or credits that remain unused no later than July 1, 2019. Buzogany shall submit documentation for any outstanding Business Expenses incurred under Section 4(e) of the Employment Agreement no later than July 12, 2019. For the avoidance of doubt, nothing in this Section 7 is intended to interfere with or affect the Parties' respective rights and obligations under the Indemnification Agreement.

5. **Release.** In exchange for the consideration specified in this Agreement, except for claims specifically exempted from the terms of this Release under the Agreement, Buzogany, on behalf of himself and his heirs, legatees, personal representatives and assigns, releases and discharges the Company, the Company affilliates, and each of their respective officers, directors, members, managers, partners and shareholders from any and all claims and causes of action, whether known or unknown, that Buzogany has, had or may have against them, related in any way to his employment with the Company or separation of employment, including any and all claims under the Employment Agreement. This Release specifically includes, but is in no way limited to, (i) all claims arising from or relating in any way to Buzogany's employment with the Company or his termination of employment with the Company; (ii) all claims under Title VII of the Civil Rights Act of 1964, as amended by the Civil Rights Act of 1991, 42 U.S.C. §§ 2000e *et seq.*; the Civil Rights Acts of 1866 and 1871 as amended, 42 U.S.C. § 1981; the Age Discrimination in Employment Act of 1967 as amended, 29 U.S.C. §§ 621 *et. seq.*; the Americans With Disabilities Act of 1990, 42 U.S.C. §§ 12101 *et seq.*, as amended; the Equal Pay Act, 29 U.S.C. § 29 U.S.C. § 206(d); the Family and Medical Leave Act of 1993, 29 U.S.C. §§ 2601 *et seq.*, as amended; the Employee Retirement Income Security Act of 1973 as amended, 29 U.S.C. §§ 1001 *et seq*.; the Occupational Safety and Health Act of 1970 as amended, 29 U.S.C. §§ 651 *et seq*.; the Illinois Human Rights Act, 765 ILCS 5/1-101 *et seq.*, the Illinois Whistleblower Act, 740 ILCS 174/1 *et seq.*, or any provision of Chapter 820 of the Illinois Compiled Statutes; and (iv) any other claims or causes of action that Buzogany has, had, or may have had under any federal, state, or local statute, regulation, ordinance, or the common law. Buzogany waives any right to receive any monetary or other benefit because of any charge, claim, lawsuit, or administrative proceeding based upon any claim released in this Agreement. This Release does not apply to claims for workers' compensation benefits or other claims that cannot be released under applicable law. For avoidance of doubt, this Release shall not act to preclude Buzogany from asserting any rights or claims as a Shareholder of the Company and shall not release any claims or modify any rights available to Buzogany under the Indemnification Agreement. Nothing in this Agreement limits Buzogany's ability to file a charge or complaint with the Equal Employment Opportunity Commission, the National Labor Relations Board, the Occupational Safety and Health Administration, the Securities and Exchange Commission or any other federal, state, or local government agency or commission ("Government Agencies"), but Buzogany waives his right to recover damages from PSI should any agency or other third party pursue

a claim on his behalf; provided, however, that nothing in this Section 5 or Agreement limits Buzogany's right to receive or fully retain a monetary award from a government administered whistleblower award program for providing information directly to a Government Agency. Buzogany further understands that this Agreement does not limit his ability to communicate with any Government Agencies or otherwise participate in any investigation or proceeding that may be conducted by any Government Agency. Nothing in this Agreement is intended to prevent, impede, or interfere with Buzogany providing testimony and information during an investigation authorized by law and conducted by any Government Agencies.

6. **Consultancy.** The Consultancy shall begin on the Effective Date and last until terminated ("Consulting Period") under the terms set forth in this Section 6:

A. Consulting Services. During the Consulting Period, Buzogany will provide services to the Company as a consultant to assist in the transition of his current responsibilities with the Company or as reasonably directed with regard to legal and human resources matters (the "Consulting Services"). Buzogany's duties and responsibilities as a consultant will be defined and communicated to Buzogany by the Company's CEO and will be consistent with Buzogany's duties and responsibilities in his current roles.

B. Termination of Consulting Period.

(1) Either party may terminate the Consulting Period for any reason at any time by giving 30 calendar days prior written notice of such termination to the other party.

(2) The Consulting Period shall terminate immediately if the Company determines, in its sole and reasonable discretion, that Buzogany is unable to perform Consulting Services due to death or physical or mental incapacity, and Buzogany shall not be entitled to any consulting fee, severance, reimbursements, or other benefits except for pro rata amounts earned or accrued prior to his last day providing Consulting Services.

(3) If the Company elects to terminate the Consulting Period, except due to Buzogany's death or disability under Section 6.B.2., the Company shall pay Buzogany 6 equal monthly installments of $27,250 payable on the first day of each month beginning after the Company's termination of such Consultancy (the "Severance Period") so long as he first executes and returns to the Company a general release agreement in a form mutually agreed between the Parties.

C. Consulting Fee and Benefits.

(1) In consideration for Buzogany's Consulting Services under this Agreement, the Company will pay Buzogany a consulting fee of $27,250 per month paid on the first day of the first month following the Effective Date and ending upon the termination of the Consulting Period. This monthly consulting fee assumes that Buzogany dedicates his work efforts on a full-time basis to the Company, consistent with past practices. To the extent that Buzogany dedicates his work efforts on less than a full-time basis, Buzogany and the Company agree to mutually determine a reasonable pro rata monthly fee amount to account for such less-than full-time schedule. As an independent contractor, Buzogany acknowledges and agrees that he is responsible for all withholding taxes, insurance, and compliance reporting to Government Agencies for compensation paid to Buzogany.

(2) Buzogany agrees to use best efforts to spend any amounts PSI paid for airline tickets or credits that remain unused prior to the Effective Date toward performing work for the Consultancy. The Company will reimburse Buzogany for reasonable expenses incurred by him in the course of performing his duties and responsibilities during the Consulting Period, consistent with the Company policies in effect from time to time with respect to travel, entertainment and other business expenses, subject to the Company's reasonable requirements, including submission of an expense report on a monthly basis, with respect to reporting and documentation of such expenses.

(3) The Company will make office space available for Buzogany to work on-site at PSI as necessary during the Consulting Period, along with necessary administrative support services, business systems, telephone use, email and other accommodations.

D. Return of Company Materials. Upon termination of the Consulting Period, Buzogany will cease acting as a consultant for the Company and will cooperate with the Company regarding the return of any Company property and confidential records and information.

E. Independent Contractor. In providing Consulting Services to the Company, Buzogany will act as an independent contractor and not an employee, agent, servant, joint venture, or partner of the Company. Buzogany shall not be entitled to any of the benefits available to the employees of the Company, except as set forth in this Agreement. Payments and benefits paid to Buzogany under this Agreement during the Consulting Period and Severance Period shall not be subject to federal, state, or local income or employment tax withholding by the Company and will be reported by the Company on Internal Revenue Service Form 1099. Buzogany will be responsible for reporting income and paying all applicable income and self-employment taxes relative to any payment or benefit under this Agreement. Any liability insurance purchased or held by the Company shall also cover Buzogany in his capacity as an independent contractor.

F. Cooperation. During the Severance Period and at any time after the Consulting Period terminates, Buzogany agrees, in his sole discretion, to continue to make himself reasonably available to assist with pending or future legal matters with which he may have knowledge as requested by the CEO. The Company agrees to reimburse him for time incurred on such assistance at the rate of $250 per hour plus reasonable expenses incurred by him in the course of performing his duties and responsibilities. Buzogany agrees that he will be responsible for any and all tax liability, if any, arising from the payments received under this Section 6.F. The scope and timing of such assistance, if any, shall be mutually agreed upon in advance by Buzogany and the Company to the extent practicable. This provision is intended to modify Section 8(b) of the Employment Agreement to remove the 18-month time limitation and to specify the per diem rate to be paid Buzogany. For the avoidance of doubt, this Agreement (i) shall not infringe or prevent Buzogany in any way from asserting his rights under the Fifth Amendment to the Constitution of the United States and (ii) shall not require Buzogany to cooperate in a manner adverse to his own interests in any governmental investigation. To the extent that the Company seeks Buzogany’s cooperation relating to a matter in which Buzogany is represented by counsel, the Company shall work directly with Buzogany’s counsel regarding the Company’s request for Buzogany’s assistance. The Company agrees to provide reasonable assistance and cooperation with Buzogany’s requests for information in connection with any legal proceeding, audit, or governmental investigation relating to matters within the scope of Buzogany’s employment by the Company. Buzogany understands that nothing in this Agreement prevents or is intended to prevent or discourage him from speaking to or cooperating with the government in any ongoing or future investigations.

7. **Post-Employment Covenants.** In exchange for the payments provided in Section 2, Buzogany agrees that the non-compete agreement set forth in Section 6(b) of the Employment Agreement will be enforceable until the two (2) year anniversary of the Effective Date. The Company agrees that it will not enforce the non-compete described in the previous sentence to preclude Buzogany from becoming employed with or providing consulting services to Weichai America. Except as explicitly set forth in Sections 5, 6, 7, and 8 of this Agreement, Buzogany agrees that the provisions of Sections 6, 7, and 8 of his Employment Agreement remain enforceable and are not superseded by this Agreement. Nothing in this Section 7 or Agreement (or the Employment Agreement) is intended to restrict Buzogany in the practice of law following the Effective Date and all post-employment covenants are intended to be construed and enforced in accordance with the Illinois Supreme Court Rules of Professional Conduct.

8. **Confidentiality.** The Company and Buzogany will keep the fact and terms of this Agreement confidential and will not discuss or disclose these matters with or to any third person other than the Parties’ attorneys and tax or financial advisors, except as required by law, including Regulation S-K, in the Company’s

reasonable judgment. Buzogany and the Company will advise any such person to whom such information is disclosed that the information is confidential and may not be disclosed except as provided herein. This Section does not preclude the Company or Buzogany from disclosing information about this Agreement (i) to any government agencies conducting the ongoing investigations, in a manner consistent with the confidential document productions to the agencies, or (ii) to a court or government agency as part of a legal proceeding or investigation, provided that any such disclosure, submission, or filing under part (ii) of this sentence is made under seal and on a confidential basis to the maximum extent allowed by law.

9. **Non-Disparagement.** Except as provided in the next sentence, Buzogany and the Company each agree that they will not make any statement at any time, in the present or future, to any person or entity which is disparaging of the individual, business, reputation, competence or good character of the other party or which, if publicized, would cause the other party humiliation or embarrassment, or would cause the public to question the other party's integrity, competence or good character. For the avoidance of doubt, nothing in this Agreement in any way precludes or interferes with, or is intended to preclude or interfere with, Buzogany or the Company or their agents from providing truthful testimony or information as part of a legal proceeding or investigation, or making any truthful statements to any government enforcement or regulatory agency.

10. **Knowing and Voluntary Waiver of Age Claims.** Buzogany acknowledges that:

A. He has been given a period of at least 21 days after being presented with this Agreement in which to consider whether to sign it, and has an adequate opportunity to review this Agreement and obtain any legal advice necessary to fully understand its terms;

B. The consideration he will receive under this Agreement is in addition to anything of value to which he is otherwise entitled to receive from the Company under applicable law;

C. He has read and understands this Agreement;

D. He is waiving any and all claims against the Company under the Age Discrimination in Employment Act arising up to the date on which he signs this Agreement; and

E. He has been advised that he may consult with an attorney of his choice before executing this Agreement.

11. **Revocation.** Buzogany may revoke this Agreement within 7 calendar days after signing it. The revocation will be effective only if written notice is received by the Company before the 8th calendar day after Buzogany signs this Agreement. The Company's obligations under this Agreement will not take effect until the time for Buzogany to revoke this Agreement has expired and Buzogany has not revoked the Agreement.

12. **Notice.** Any notice provided for in this Agreement must be in writing and sent to the recipients at the address indicated below:

If to Buzogany: William Buzogany
At the address on file with the Company

If to the Company: Power Solutions International, Inc.
201 Mittel Drive
Wood Dale, Il 60191
Attn: John Miller
JMiller@psiengines.com

or such other address or to the attention of such other person as the recipient party shall have specified by prior written notice to the sending party. Any notice under this Agreement shall be deemed to have been duly given or made as follows: (a) if sent by registered or certified mail in the United States, return receipt requested, upon actual receipt; (b) if sent by reputable overnight air courier (such as DHL or Federal Express), two business days after being so sent; or (c) if by electronic mail or otherwise actually personally delivered, when so delivered.

13. **Taxes and Deductions.** All payments provided for in this Agreement will be subject to payroll tax withholding and deductions to the extent required by law. Each party will report, as may be required by law for income tax purposes, its respective payment and receipt of the payments provided for in this Agreement and will bear its respective tax liabilities, if any, arising from this Agreement.

14. **No Admission of Wrongdoing.** Nothing in this Agreement constitutes an implication or admission of wrongdoing by Buzogany or the Company.

15. **Section 409A.**

A. The intent of the Parties is that payments and benefits under this Agreement comply with Internal Revenue Code Section 409A and the regulations and guidance promulgated thereunder (collectively "Section 409A") including the exceptions thereto and, accordingly, to the maximum extent permitted, this Agreement shall be interpreted to be in compliance therewith, and any payments hereunder shall be made upon an event and in a manner that complies with Section 409A or an applicable exemption. Any payments under this Agreement that may be excluded from Section 409A either as termination pay due to an involuntary termination from service or as a short-term deferral shall be excluded from Section 409A to the maximum extent possible. For purposes of Section 409A, each installment payment provided under this Agreement shall be treated as a separate payment. Any payments to be made under this Agreement in connection with a termination of employment shall only be made if such termination of employment constitutes a "separation from service" under Section 409A. The Company shall be entitled to amend this Agreement to comply and/or clarify a payment's compliance with Section 409A (or an exemption therefrom), provided, however, to the extent that any provision hereof is modified, such modification shall be made in good faith and shall, to the maximum extent reasonably possible, maintain the original intent and economic benefit to the Executive and the Company of the applicable provision without violating the provisions of Section 409A. Notwithstanding anything in the Agreement to the contrary, in no event whatsoever shall the Company be liable for any tax, interest or penalty that may be imposed on Buzogany under Section 409A or any damages for failing to comply with Section 409A.

B. Notwithstanding anything in this Agreement to the contrary, if any payment or benefit provided to Buzogany in connection with his retirement and termination of employment is determined to constitute "nonqualified deferred compensation" within the meaning of Section 409A and Buzogany is determined to be a "specified employee" as defined in Section 409A(a)(2)(b)(i), then such payment or benefit shall not be paid until the first payroll date to occur following the six-month anniversary of the Effective Date or, if earlier, on Buzogany's death (the "Specified Employee Payment Date"). The aggregate of any payments that would otherwise have been paid before the Specified Employee Payment Date shall be paid (without interest) to Buzogany in a lump sum on the Specified Employee Payment Date and thereafter, any remaining payments shall be paid without delay in accordance with their original schedule.

C. To the extent required by Section 409A, each reimbursement or in-kind benefit provided under this Agreement shall be provided in accordance with the following: (i) the amount of expenses eligible for reimbursement, or in-kind benefits provided, during each calendar year cannot affect the expenses eligible for reimbursement, or in-kind benefits to be provided, in any other calendar year; (ii) any reimbursement of an eligible expense shall be paid to Buzogany on or before the last day of the calendar year following the calendar year in which the expense was incurred; and (iii) any right to reimbursements or in-kind benefits under this Agreement shall not be subject to liquidation or exchange for another benefit.

16. **Entire Agreement.** This Agreement sets forth the entire agreement of the Parties and supersedes all prior and contemporaneous agreements and understandings between the Parties, including but not limited to the Employment Agreement, except as otherwise explicitly stated herein.

17. **Choice of Law.** This Agreement is to be construed in accordance with the laws of the State of Illinois, without regard to conflict of law principles.

18. **Modification of this Agreement.** This Agreement may not be amended or modified except in a writing signed by the Party against whom the amendment or modification is to be enforced.

19. **Execution in Counterparts.** This Agreement may be signed in counterparts, which together will form the original.

Severability. Nothing in this Agreement is to be construed as waiving rights that cannot be waived under applicable law, or as barring either Party from providing information or truthful testimony when required to do so under applicable law. Should any portion of this Agreement be ruled unenforceable by a court of competent jurisdiction, the remainder of this Agreement and the releases and covenant not to sue contained herein will remain in full force and effect as to any and all other claims.

Accepted and Agreed To By:

William Buzogany

/s/ William Buzogany

Date: July 10,2019

POWER SOLUTIONS INTERNATIONAL, INC.

By: /s/ John A. Miller

Title: Chief Executive Officer

Date: July 10, 2019

Exhibit 31.1

CERTIFICATION PURSUANT TO 17 CFR 240.13a-14 PROMULGATED UNDER SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, John P. Miller, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Power Solutions International, Inc.;

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

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

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

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

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

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

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

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

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

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

Date: May 4, 2020	By:	/s/ John P. Miller
	Name:	**John P. Miller**
	Title:	Chief Executive Officer and President

Exhibit 31.2

CERTIFICATION PURSUANT TO 17 CFR 240.13a-14 PROMULGATED UNDER SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Charles F. Avery, Jr., certify that:

1. I have reviewed this quarterly report on Form 10-Q of Power Solutions International, Inc.;

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

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

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

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

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

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

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

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

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

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

Date: May 4, 2020	By:	/s/ Charles F. Avery, Jr.
	Name:	**Charles F. Avery, Jr.**
	Title:	Chief Financial Officer

Exhibit 32.1

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

In connection with the Quarterly Report of Power Solutions International, Inc. (the “Company”) on Form 10-Q for the quarter ended September 30, 2019, as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, John P. Miller, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. 1350, as adopted pursuant to 906 of the Sarbanes-Oxley Act of 2002, that:

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

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

Date: May 4, 2020	By:	/s/ John P. Miller
	Name:	**John P. Miller**
	Title:	Chief Executive Officer and President

This certification accompanies each Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not, except to the extent required by the Sarbanes-Oxley Act of 2002, be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended.

A signed original of this written statement required by Section 906 has been provided by the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

Exhibit 32.2

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

In connection with the Quarterly Report of Power Solutions International, Inc. (the “Company”) on Form 10-Q for the fiscal quarter ended September 30, 2019, as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Charles F. Avery, Jr., Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. 1350, as adopted pursuant to 906 of the Sarbanes-Oxley Act of 2002, that:

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

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

Date: May 4, 2020	By:	/s/ Charles F. Avery, Jr.
	Name:	**Charles F. Avery, Jr.**
	Title:	Chief Financial Officer

This certification accompanies each Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not, except to the extent required by the Sarbanes-Oxley Act of 2002, be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended.

A signed original of this written statement required by Section 906 has been provided by the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.