ENVIRONMENTAL POWER CORP
Form 8-K/A
August 14, 2001

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 8-KA

CURRENT REPORT

Pursuant to Section 13 or 15(d) of the Securities
Exchange Act of 1934

Date of Report (Date of earliest event reported): July 23, 2001

Environmental Power Corporation
(Exact name of registrant as specified in its charter)

Delaware	0-15472	04-2782065
(State of other jurisdiction of incorporation)	(Commission File Number)	(IRS Employer Identification No.)

500 Market Street, Suite 1-E, Portsmouth, New Hampshire 03801
(Address of principal executive offices)

(603) 431-1780
(Registrant's telephone number, including area code)

The undersigned Registrant hereby amends the following item of its Current Report on Form 8-K filed August 7, 2001, and files the further financial statements, as set forth below.

ITEM 7. FINANCIAL STATEMENTS, PRO FORMA FINANCIAL INFORMATION AND EXHIBITS

(A) FINANCIAL STATEMENTS FOR MICROGY

A. Audited Financial Statements
- (1) Report of Independent Auditors *
- (2) Balance Sheet as of June 30, 2000 *
- (3) Statements of Operations for the Year Ended June 30, 2000 and for the Period from March 25, 1999 (inception) through June 30, 2000 *
- (4) Statements of Changes in Stockholders' for the Period from March 25, 1999 (inception) through June 30, 2000 *
- (5) Statements of Cash Flows for the Year Ended June 30, 2000 and for the Period from March 25, 1999 (inception) through June 30, 2000 *
- (6) Notes to the Financial Statements *

B. Unaudited Interim Financial Statements
   (1) Balance Sheet as of March 31, 2001**
   (2) Statement of Operations for the Nine Months Ended March 31, 2001**
   (3) Statement of Operations for the Period from March 25, 1999 (inception) through March 31, 2001
   (4) Statement of Cash Flows for the Nine Months Ended March 31, 2001**
   (5) Statement of Cash Flows for the Period from March 25, 1999 (inception) through March 31, 2001
   (6) Notes to Condensed Financial Statements

(B) PRO FORMA FINANCIAL INFORMATION

1. Pro Forma Combined Condensed Financial Statements
   (1) Unaudited Pro Forma Combined Condensed Balance Sheet at March 31, 2001, as restated
   (2) Unaudited Pro Forma Combined Condensed Statements of Operations for the Three Months Ended March 31, 2001 and Year Ended December 31, 2000, as restated
   (3) Notes to Unaudited Pro Forma Combined Condensed Financial Statements, as restated

(C) EXHIBITS

3.02 Certificate of Designations related to the Company's newly designated, $.01 par value, Series B Convertible Preferred Stock. *

* Previously filed
** Refiled herewith for reader convenience

(C) EXHIBITS (CONTINUED)

10.03 Share Exchange Agreement dated June 20, 2001 among the Company, Microgy and the Principal Microgy Shareholders (incorporated by reference to Exhibit 2 to Amendment No. 7 to Schedule 13D filed by Joseph E. Cresci on August 2, 2001 (the "13D")).

10.04 Stockholders' Agreement dated July 23, 2001 among the Company, the Principal Microgy Shareholders, Joseph E. Cresci and Donald A. Livingston (incorporated by reference to Exhibit 4 to the 13D)

10.05 Registration Rights Agreement dated July 23, 2001 among the Company, the Principal Microgy Shareholders, Joseph E. Cresci, Donald A. Livingston and future exchanging Microgy security holders who become a party thereto (incorporated by reference to Exhibit 5 to the 13D).

10.06 Form of Joinder Agreement (incorporated by reference to Exhibit 6 to the 13D).

10.07 Form of Waiver Agreement dated July 23, 2001 executed by certain Microgy Shareholders (incorporated by reference to Exhibit 3 to the 13D).

10.08 Warrant Agreement dated July 23, 2001 between the Company and Daniel J. Eastman. (incorporated by reference to Exhibit 6 to the Schedule 13D filed by Daniel J. Eastman on August 2, 2001).

CAUTIONARY STATEMENT

The Private Securities Litigation Reform Act of 1995 (the "Act") provides a "safe harbor" for forward-looking statements. Certain statements contained in this report, such as statements concerning Microgy's intentions to develop, finance, own and operate project facilities, Microgy's intentions to develop and license from others proprietary technologies, anticipated business trends, changes to EPC's authorized capital, changes to EPC's Board of Directors, EPC's acquisition of the remaining Microgy securities, future registrations of EPC's securities and other statements contained herein regarding matters that are not historical facts, are forward looking statements as such term is defined in the Act. Because such statements involve risks and uncertainties, actual results may differ materially from those expressed or implied by such forward-looking statements. Factors that could cause actual results to differ materially include, but are not limited to, uncertainties involving development stage companies, financing requirements and uncertainties, difficulties involved in executing on a business plan, technological uncertainties, risks relating to managing and integrating acquired businesses, volatile and unpredictable developments (including plant outages and repair requirements), the difficulty of estimating construction, development, repair and maintenance costs and timeframes, the uncertainties involved in estimating insurance and implied warranty recoveries, if any, the inability to predict the course or outcome of any negotiations with parties involved with EPC's or Microgy's projects, uncertainties relating to general economic and industry conditions, the amount and rate of growth in expenses, uncertainties relating to government and regulatory policies, the legal environment, intellectual property issues, the competitive environment in which EPC and Microgy operate and other factors, including those described in the Company's filings with the Securities and Exchange Commission, including the section "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Certain Factors That May Impact Future Results" of EPC's Quarterly Report on Form 10-Q for the period ended March 31, 2001. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of their dates. EPC undertakes no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

SIGNATURES

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

ENVIRONMENTAL POWER CORPORATION

August 14, 2001

/s/ William D. Linehan

William D. Linehan
Treasurer and
Chief Financial Officer
(principal accounting officer
and authorized officer)

MICROGY COGENERATION SYSTEMS, INC.
(A DEVELOPMENT STAGE COMPANY)
UNAUDITED BALANCE SHEET
AS OF MARCH 31, 2001

ASSETS

Current Assets:	
Cash and Cash Equivalents	92,321.73
Due from Affiliate	66,074.45
Allowance for Doubtful Collections	(66,074.45)
Employee Travel Advances	1,500.00
Prepaid Expenses	4,187.00
Total Current Assets	98,008.73
Property and Equipment:	
Total Property and Equipment	41,267.36
Accumulated Depreciation	(5,579.00)
Net Property and Equipment	35,688.36
Other Assets:	
Refundable Deposits	110.00
Investment in Preferred Stock	83,407.32
Investment in Microgy Projects	100,693.50
Total Other Assets	184,210.82
Total Assets	317,907.91

LIABILITIES AND STOCKHOLDERS' EQUITY

Current Liabilities:	
Accounts Payable	151,101.04
Notes Payable - Shareholder	75,000.00
Payroll Due to Employees	80,381.55
Total Current Liabilities	306,482.59
Stockholders' Equity:	
Common Stock	18,149.28
Additional Paid-in Capital	1,476,703.58
Accumulated Deficit	(1,483,427.54)
Total Stockholders' Equity	11,425.32
Total Liabilities & Stockholders' Equity	317,907.91

MICROGY COGENERATION SYSTEMS, INC.
(A DEVELOPMENT STAGE COMPANY)
UNAUDITED STATEMENT OF OPERATIONS

	NINE MONTHS ENDED MARCH 31, 2001	INCEPTION TO MARCH 31, 2001
Revenues:		
Other Revenues	9,000.00	9,000.00
Interest Income	14,576.57	14,669.82
Total Revenues	23,576.57	23,669.82
Project Costs:		
Project Related Legal Costs	10,784.12	10,784.12
Other Project Related Corporate Costs	2,096.64	2,096.64
Total Project Costs	12,880.76	12,880.76
Gross Profit	10,695.81	10,789.06
Operating Expenses:		
Salaries and Benefits:		
Salaries	462,565.69	683,918.21
Issuance of Common Stock for Services	-	104,341.00
Payroll Taxes and Benefits	42,767.85	66,701.00
Total Salaries and Benefits	505,333.54	854,960.21
Marketing and Sales:		
Business Development	32,375.22	57,361.18
Trade Shows	400.00	400.00
Total Marketing and Sales	32,775.22	57,761.18
General and Administrative:		
Legal	35,588.36	78,788.00
Accounting	12,180.75	15,264.75
General Travel and Entertainment	31,353.65	31,353.65
Auto Expenses	9,433.27	16,488.46
Office Rents	36,003.00	56,660.00
Telephone	25,788.34	39,575.43
Office Supplies and Expenses	16,071.08	21,109.27
Couriers and Postage	4,484.15	5,369.57
Dues, Licenses, and Subscriptions	4,599.15	5,014.15
Computer System Expenses	15,599.12	16,748.62
Seminars and Training	772.50	772.50
Bad Debts	39,800.00	66,074.45
Miscellaneous Expense	1,521.18	2,774.86
Total General and Administrative	233,194.55	355,993.71
Other Expenses:		
Corporate Financing Costs	15,157.00	16,933.00
New Technology Licensing Fees	15,000.00	15,000.00
Consulting Fees	120,349.00	147,849.00
Purchased Opportunities	-	25,000.00
Directors Fees	11,250.00	12,500.00

Other Expenses	2,089.00	2,640.50
Total Other Expenses	163,845.00	219,922.50
Total Operating Expenses	935,148.31	1,488,637.60
Loss from Operations	(924,452.50)	(1,477,848.54)
Depreciation	5,533.00	5,579.00
Loss Before Income Taxes	(929,985.50)	(1,483,427.54)
Income Taxes	-	-
Net Loss	(929,985.50)	(1,483,427.54)

MICROGY COGENERATION SYSTEMS, INC.
(A DEVELOPMENT STAGE COMPANY)
UNAUDITED STATEMENT OF CASH FLOWS

	NINE MONTHS ENDED MARCH 31, 2001	INCEPTIO MARCH 31,
Operating Activities:		
Net Loss	$ (929,985.50)	$ (1,483,4
Adjustments to Reconcile Net Loss to Net Cash Used for Operating Activities		
Depreciation	5,533.00	5,5
Issuance of Common Stock for Services	-	104,3
Employee Travel Advances	(1,324.02)	(1,5
Prepaid Expenses	(751.00)	(4,2
Accounts Payable	81,003.26	151,1
Payroll and Taxes Payable	53,470.44	80,3
Net Cash Used for Operating Activities	(792,053.82)	(1,147,8
Investing Activities:		
Purchase of Equipment	(39,806.47)	(41,2
Investment in Affiliate	(83,407.32)	(83,4
Investment in Projects	(100,693.50)	(100,6
Net Cash Used for Investing Activities	(223,907.29)	(225,3
Financing Activities:		
Issuance of common stock	675,008.04	1,307,1
Note Payable - Stockholder	75,000.00	75,0
Issuance of Common Stock to affiliate	83,407.32	83,4

Net Cash Provided by Financing Activities	833,415.36	1,465,5
Net Change in Cash	(182,545.75)	92,3
Beginning Cash	274,867.48	
Ending Cash	$ 92,321.73	$ 92,3

MICROGY COGENERATION SYSTEMS, INC.
(A development stage company)

NOTES TO CONDENSED FINANCIAL STATEMENTS

March 31, 2001

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

ORGANIZATION AND DEVELOPMENT STAGE ACTIVITY

Microgy Cogeneration Systems, Inc. (the "Company") was incorporated in Colorado on March 25, 1999, and is in a development stage as of March 31, 2001. The Company is an alternative energy company developing renewable energy projects worldwide through proprietary technologies and systems. The initial projects are biopower facilities that process agricultural and organic wastes into renewable energy and fuels through Company systems using proprietary technologies.

CASH AND CASH EQUIVALENTS

Cash and cash equivalents include cash on hand at the balance sheet date.

PROPERTY AND EQUIPMENT

Property and equipment, consisting primarily of furniture, fixtures, and computer equipment, is stated at cost. Depreciation is computed over the estimated useful lives of the assets, which range from 5 to 7 years.

USE OF ESTIMATES

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

STOCK-BASED COMPENSATION

Pursuant to the provisions of Statement of Financial Accounting Standards No. 123, Accounting and Disclosure of Stock-Based Compensation (Statement No. 123), the Company accounts for its stock compensation arrangements under Accounting Principles Board No. 25, Accounting for Stock Issued to Employees (APB No. 25), and related pronouncements. Under the provisions of APB No. 25, no compensation expense is recognized when stock options are granted with exercise prices equal to or greater than market value on the date of the grant.

DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

On January 1, 2001, the Company adopted Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities (Statement No. 133), which established accounting and reporting standards for derivative instruments, derivative instruments embedded in other contracts, and hedging activities. Statement No. 133 requires that entities recognize all derivative instruments as either assets or liabilities in the statement of financial position and measure those instruments at fair value. The adoption of Statement No. 133 did not have a material impact on the Company's unaudited condensed financial statements.

NEW ACCOUNTING PRONOUNCEMENTS

In June 2001, the Financial Accounting Standards Board ("FASB") issued two new pronouncements: Statement of Financial Accounting Standards No. 141, Business Combinations (Statement No. 141), and Statement of Financial Accounting Standards No. 142, Goodwill and Other Intangible Assets (Statement No. 142). Statement No. 141 is effective as follows: a) use of the pooling-of-interest method is prohibited for business combinations initiated after June 30, 2001; and b) the provisions of Statement No. 141 also apply to all business combinations accounted for by the purchase method that are completed after June 30, 2001 (that is, the date of the acquisition is July 2001 or later). There are also transition provisions that apply to business combinations completed before July 1, 2001, that were accounted for by the purchase method. The most significant changes made by Statement No. 142 are: a) goodwill and indefinite-lived intangible assets will be tested for impairment at least annually; b) goodwill will no longer be amortized to income; and c) the amortization period of intangible assets with finite lives will no longer be limited to forty years. Statement No. 142 is effective for fiscal years beginning after December 15, 2001 to all goodwill and other intangible assets recognized in an entity's statement of financial position at that date, regardless of when those assets were initially recognized. The Company is currently evaluating the provisions of Statement No. 141 and Statement No. 142 and has not adopted such provisions in its March 31, 2001 unaudited condensed financial statements.

2. INCOME TAXES

The Company accounts for income taxes in conformity with Statement of Financial Accounting Standards No. 109, Accounting for Income Taxes (Statement No. 109). Under the provisions of Statement No. 109, a deferred tax liability or asset (net of a valuation allowance) is provided in the financial statements by applying the provisions of applicable tax laws to measure the deferred tax consequences of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. These temporary differences will result in net taxable or deductible amounts in future years as a result of events recognized in the financial statements in the current or preceding years.

The Tax Reform Act of 1986 contains provisions that limit the utilization of net operating loss and tax credit carryforwards if there has been a "change in ownership" as described in Section 382 of the Internal Revenue Code. Such a change of ownership may limit the Company's utilization of its net operating loss and tax credit carryforwards, and could be triggered by an initial public offering or by subsequent sales of securities by the Company or its stockholders.

Significant components of the Company's deferred tax liabilities and assets for March 31, 2001 are as follows:

Deferred tax assets:	
Net operating loss carryforward	$ 563,700
Allowance for uncollectible notes	25,100
Total deferred tax assets	588,800
Valuation allowance	(588,800)
Net deferred taxes	$ -

At March 31, 2001, the Company had net operating loss carryforwards for income tax purposes of approximately $1,417,000, which expire through 2020.

3. LEASES

Commencing on April 1, 2000, the Company entered into an operating lease for office space in Golden, Colorado for a period of one year. After expiration of the lease, the Company continues to lease the office space on a month-to-month basis.

On December 1, 2000, the Company entered into an operating lease for office space in Mequon, Wisconsin for a period of one year. The Company was released from this lease effective August 6, 2001. The Company's Wisconsin office currently is in Thiensville, Wisconsin and on a month-to-month rental basis.

Rental expense was approximately $36,000 for the nine months ended March 31, 2001.

4. COMMON STOCK ISSUANCES

In July 2000, pursuant to a share exchange agreement, the Company issued 154,458 shares of its common stock and warrants in exchange for 797,299 shares of preferred stock of a related party. This investment transaction was recorded at $83,407.

5. STOCK OPTIONS

In June 2000, the Company's Board of Directors and stockholders approved the 2000 Stock Option Plan (the 2000 Plan) pursuant to which a total of 5,000,000 shares of common stock have been reserved for issuance to eligible employees, consultants and directors of the Company. Awards under the 2000 Plan may consist of incentive stock options, which qualify under Section 422 of the Internal Revenue Code, or nonqualified stock options, which do not qualify under that provision. The 2000 Plan provides for an exercise period of up to six years with the price being equal to the fair market value at the time the option is granted. The 2000 Plan is administered by the Board of Directors, which has the authority to select the individuals to whom awards will be granted and to determine whether and to what extent stock options are to be granted, the numbers of shares of common stock to be covered by each award, the vesting schedule of stock options, and all other terms and conditions of each award. Incentive stock options totaling 290,000

shares have been issued to employees under the Plan. There were 4,710,000 shares of common stock still reserved for issuance under the 2000 Plan as of March 31, 2001.

6. PREFERRED STOCK

The Company is authorized to issue up to 25,000,000 shares of nonvoting preferred stock, $0.001 par value, with the shares to be issued in series by the Board of Directors. The shares of preferred stock may be issued in one or more series with such designations, rights, preferences and limitations as the Company's Board of Directors may determine without approval of its stockholders. As of March 31, 2001 there were no preferred shares issued or outstanding.

7. WARRANTS

In May 1999, the Company issued 885,000 warrants to stockholders of the Company. The shareholder warrants expire in May 2002. Each warrant is exercisable for one share of common stock at a price of $1.00 per share. The Company has the ability to call the warrants at a price of $1.20 per common share or greater.

In December 1999, an employee was issued a warrant to purchase 800,000 shares of common stock at an exercise price of $0.50 per share through March 2001 and $1.00 per share through September 2002. The warrant has been revised to extend the $0.50 per share exercise price through May 31, 2002 and $1.00 per share exercise price from June 1, 2002 through September 30, 2002.

8. RELATED PARTY TRANSACTIONS

As disclosed in Note 4, during July 2001, the Company acquired all of the preferred stock of a related party whose President and Vice President are also officers and stockholders of the Company.

Advances have also been made to that related party under a promissory note related to a secured advance line not to exceed $250,000. The Company had advanced $66,074 as of March 31, 2001. Due to the uncertainty of collection, this amount has been reserved in full. In addition, no interest income related to the note receivable has been recognized by the Company.

On March 30, 2001, the Company borrowed $75,000 from a Company officer and stockholder under a promissory note related to an unsecured advance line not to exceed $200,000. The note has an interest rate of 8%. The Company had borrowed $75,000 under this note as of March 31, 2001.

9. INVESTMENT IN PROJECTS

Investment in Projects as of March 31, 2001, consists primarily of the cost of engineering work related to the Company's future biopower generating projects. The Company may, if appropriate, recognize the cost of this engineering work in the future as a portion of its equity

contribution to these projects. The cost of this engineering work totaled $100,694 as of March 31, 2001.

10. POWER CONTRACTS

On December 18, 2000, the Company, through a wholly-owned LLC entity, entered into an agreement with a West Coast utility for up to 15 megawatts of green power at facilities in central California.

11. EUROPEAN TECHNOLOGY PROVIDER

On May 12, 2000, the Company entered into a revised licensing agreement with a European technology provider whereby the Company is granted a perpetual and exclusive license for use of certain proprietary technology in its cogeneration facilities. This agreement superseded an initial license agreement executed in

November 1999.

The European technology provider will own a 5% minority equity stake in any legal entity that owns any project developed by the Company using the European technology provider's enhanced anaerobic digester technology wherein the Company retains an equity position.

The agreement specifies a fixed payment amount per project to the European technology provider for engineering work and construction drawings. The agreement also specifies that a licensing fee as well as a monthly consulting fee will be paid to the European technology provider.

12. COLORADO TECHNOLOGY PROVIDER

On September 17, 1999, the Company entered into an agreement with a Colorado technology provider whereby the Company is granted an exclusive and perpetual worldwide license for use of the Colorado technology provider's proprietary microturbine in the Company's biogas or cogeneration projects. The agreement also gives the Company the right to manufacture the microturbine. The Company also has a nonexclusive and perpetual worldwide license for the manufacture and use of the proprietary microturbine in stand-alone or utility-connected systems.

13. ADEQUACY OF DISCLOSURE

The accompanying unaudited condensed financial statements of the Company have been prepared by management and may not include all of the information and footnotes required by generally accepted accounting principles for annual financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. The results of operations for the nine months ended March 31, 2001 are not necessarily indicative of results to be expected for the year ending June 30, 2001. For further information, refer to the financial statements and footnotes included in the Company's Audited Financial Statements for the Period from March 25, 1999 (inception) through June 30, 2000.

ENVIRONMENTAL POWER CORPORATION AND SUBSIDIARIES
UNAUDITED PRO FORMA COMBINED CONDENSED BALANCE SHEET (AS RESTATED)
AS OF MARCH 31, 2001

	EPC (PRIOR FILING)	MICROGY (STANDALONE)	PRO FORMA ADJUSTMENTS	NOTE
ASSETS				
CURRENT ASSETS:				
Cash and cash equivalents	$ 11,427	$ 92,322		
Restricted cash	798,979			
Receivable from utility	7,694,577			
Other current assets	1,355,034	5,687		
TOTAL CURRENT ASSETS	9,860,017	98,009	-	
PROPERTY, PLANT AND EQUIPMENT, NET	517,629	35,688		
DEFERRED INCOME TAX ASSET	724,193			
LEASE RIGHTS, NET	2,273,256			

ACCRUED POWER GENERATION REVENUES	58,053,351			
GOODWILL			6,186,827	(C)
OTHER ASSETS	451,328	184,211		
	$ 71,879,774	$ 317,908	$ 6,186,827	
LIABILITIES AND SHAREHOLDERS' (DEFICIT) EQUITY				
CURRENT LIABILITIES:				
Accounts payable and accrued expenses	$ 7,122,399	$ 231,483		
Other current liabilities	2,865,489	75,000		
TOTAL CURRENT LIABILITIES	9,987,888	306,483	-	
DEFERRED GAIN, NET	4,703,262			
SECURED PROMISSORY NOTES PAYABLE AND OTHER BORROWINGS	2,118,172			
ACCRUED LEASE EXPENSES	58,053,351			
TOTAL LIABILITIES	74,862,673	306,483	-	
MINORITY INTEREST			1,405	(E)
SHAREHOLDERS' (DEFICIT) EQUITY:				
Preferred Stock	100			
Common Stock	125,254	18,149	(18,149)	(E)
Additional Paid-in Capital		1,476,704	(1,476,704)	(E)
Accumulated deficit	(2,206,034)	(1,483,428)	1,483,428	(E)
	(2,080,680)	11,425	(11,425)	
Treasury stock	(456,271)			
Notes receivable from officers and board members	(445,948)			
TOTAL SHAREHOLDERS' (DEFICIT) EQUITY	(2,982,899)	11,425	(11,425)	
	$ 71,879,774	$ 317,908	$ (10,020)	

See Notes to Unaudited Pro Forma Combined Condensed Financial Statements

Environmental Power Corporation and Subsidiaries
Unaudited Pro Forma Combined Condensed Statement of Operations (As Restated)
Three Months Ended March 31, 2001

	EPC (prior filing)	Microgy (standalone)	Pro For Adjustme
POWER GENERATION REVENUES	$ 13,482,891	-	

COSTS AND EXPENSES:			
Operating expenses	4,957,240		
Lease expenses	6,015,022		
General and administrative expenses	685,729	286,979	
Depreciation and amortization	86,547	2,051	154
	11,744,538	289,030	154
OPERATING INCOME	1,738,353	(289,030)	(154
OTHER INCOME (EXPENSE):			
Interest income	18,784	996	
Interest expense	(69,303)		
Amortization of deferred gain	77,103		
	26,584	996	
INCOME BEFORE INCOME TAXES AND MINORITY INTEREST	1,764,937	(288,034)	(154
MINORITY INTEREST			35
INCOME TAX EXPENSE	(777,000)	-	100
NET INCOME	$ 987,937	$ (288,034)	$ (18
EARNINGS PER COMMON SHARE:			
Basic	$ 0.09		
Diluted	$ 0.09		

See Notes to Unaudited Pro Forma Combined Condensed Financial Statements

ENVIRONMENTAL POWER CORPORATION AND SUBSIDIARIES
UNAUDITED PRO FORMA COMBINED CONDENSED STATEMENT OF OPERATIONS (AS RESTATED)
YEAR ENDED DECEMBER 31, 2000

	EPC (PRIOR FILING)	MICROGY (STANDALONE)	PRO FORMA ADJUSTMENTS
POWER GENERATION REVENUES	$ 54,303,222	-	
COSTS AND EXPENSES:			
Operating expenses	22,291,069		
Lease expenses	26,415,897		
General and administrative expenses	3,602,960	1,052,344	
Depreciation and amortization	415,230	3,528	618,6
	52,725,156	1,055,872	618,6
OPERATING INCOME	1,578,066	(1,055,872)	(618,6
OTHER INCOME (EXPENSE):			
Interest income	736,867	13,611	
Interest expense	(320,641)		
Amortization of deferred gain	308,411		
Sale of NOx emission credits	1,156,338		

Other income	-	9,000	
	1,880,975	22,611	
INCOME BEFORE INCOME TAXES AND MINORITY INTEREST	3,459,041	(1,033,261)	(618,6
MINORITY INTEREST			127,0
INCOME TAX EXPENSE	(1,632,233)	-	361,6
NET INCOME	$ 1,826,808	$(1,033,261)	$ (129,9
EARNINGS PER COMMON SHARE:			
Basic	$ 0.16		
Diluted	$ 0.16		

See Notes to Unaudited Pro Forma Combined Condensed Financial Statements

NOTES TO UNAUDITED PRO FORMA COMBINED CONDENSED FINANCIAL STATEMENTS (AS RESTATED)

NOTE A -- BASIS OF PRESENTATION

On July 23, 2001, Environmental Power Corporation (individually "EPC" or consolidated "the Company") acquired approximately 87.7% of the outstanding common stock of Microgy Cogeneration Systems Inc. ("Microgy") in exchange for securities of the Company pursuant to a Share Exchange Agreement (the "Exchange Agreement") dated as of June 20, 2001 among the Company, Microgy and the Principal Microgy Shareholders, as defined therein. Under the terms of the Exchange Agreement, the Company issued an aggregate of 5,521,549 shares of the Company's common stock, $.01 par value ("Common Stock") and 197,760.7 shares of the Company's newly designated Series B Convertible Preferred Stock, $.01 par value (the "Preferred Stock"), to the Principal Microgy Shareholders in exchange for 15,919,147 shares of Microgy common stock. Each share of Preferred Stock, which votes with the Common Stock on an as converted basis, will automatically be converted into ten shares of Common Stock upon an increase in the authorized common stock to an amount sufficient to allow conversion of the Preferred Stock. The exchange ratio ("Exchange Ratio") used was 0.3468495 shares of Common Stock and 0.0124228 shares of Preferred Stock for each share of Microgy common stock. Under the terms of the Exchange Agreement, the Company agreed to offer the remaining shareholders of Microgy (who own an aggregate of 2,230,126 shares of Microgy common stock, warrants to purchase 885,000 shares of Microgy common stock and options to purchase 290,000 shares of Microgy common stock) an opportunity to exchange their Microgy securities for EPC securities based on the Exchange Ratio. On July 23, 2001, one of the Principal Microgy Shareholders also exchanged a warrant to purchase 800,000 shares of Microgy common stock for a warrant to purchase securities of the Company based on the Exchange Ratio. The exercise price for the warrant to purchase securities of the Company exceeded the estimated market value of the Company's common stock on the date of the exchange.

Solely for purposes of this presentation, these unaudited combined condensed financial statements have been prepared as if Microgy were combined with EPC and its other subsidiaries into one reporting entity. The purchase price paid by EPC for Microgy's net assets has been pushed down to the subsidiary. The portion of the purchase price not allocated to assets or liabilities has been recorded as goodwill (See Note C).

The accompanying unaudited pro forma combined condensed financial statements of the Company have been prepared in accordance with the instructions to Form 10-Q and Regulation S-X and do not include all of the information and footnotes required by generally accepted accounting principles for annual financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. For further information, refer to the consolidated financial statements and footnotes included in the Company's Annual Report on Form 10-K for the year ended December 31, 2000.

NOTE B - PURCHASE PRICE

For purposes of the unaudited pro forma combined condensed financial statements, the purchase price for approximately 87.7% of the outstanding common stock of Microgy was calculated as follows:

	Common	Preferred	Total Purchase Price
EPC shares issued as consideration	5,521,549	197,760.7	
Market price per share	$ 0.773	$ 7.73	
Fair Market Value of Stock Issued	$4,268,157	$1,528,690	$5,796,847
Estimated Direct Acquisition Costs			400,000
Total Purchase Price			$6,196,847

Market prices per share were based on the average closing market price of EPC's common stock from June 18, 2001 through June 27, 2001. Each preferred share is convertible to ten common shares and votes with common shares on an as converted basis. Therefore, the market price for each preferred share was estimated to be ten times the market price for each common share.

Direct acquisition costs were estimated at the time of making this report and will be revised in future reports when actual cost information is available.

NOTE C -- GOODWILL

For purposes of the unaudited pro forma combined condensed financial statements, the Company has allocated 100% of the purchase price which was not allocable to net tangible assets to goodwill. Goodwill, which is being amortized on a straight-line basis over ten years, was determined as follows:

Total Purchase Price of the 87.7% interest in Microgy	$6,196,847
Estimated fair value of the net tangible assets acquired:	
87.7% of the historical book value of Microgy as of March 31, 2001	(10,020)
Estimated Goodwill as of March 31, 2001	$6,186,827

The Company reported amortization of goodwill of $618,683 and $154,671 in its unaudited pro forma combined condensed statements of operations for the year ended December 31, 2000 and the three months ended March 31, 2001, respectively.

The Company is still in the process of evaluating its acquired intellectual property for the purpose of separately identifying, valuing and providing meaningful disclosures of each identifiable intangible asset. After such evaluation, the Company will provide further information about its intangible assets.

NOTE D - INCOME TAXES

Microgy is a development stage company which currently does not report income taxes on a standalone basis. For purposes of the unaudited pro forma combined condensed financial statements, the Company has reported an income tax benefit representing 35% of Microgy's loss before income taxes. This amount represents the Company's estimated savings of Federal and certain state income taxes from including Microgy's operations in a combined tax return.

NOTE E - MINORITY INTEREST

The Company has a 12.3% minority interest of Microgy shareholders who were not a party to the Exchange Agreement. For purposes of the unaudited pro forma combined condensed financial statements, the Company has made the following pro forma adjustments:

- The Company eliminated 100% of the Microgy equity and reported 12.3% of such equity as a minority interest on its Pro Forma Combined Condensed Balance Sheet as of March 31, 2001.

- The Company reported 12.3% of Microgy's loss before income taxes as a minority interest under the caption other income in its Pro Forma Combined Condensed Statements of Operations for the three months ended March 31, 2001 and the year ended December 31, 2000.

NOTE F -- EARNINGS PER COMMON SHARE

The Company computes its earnings per common share using the treasury stock method in accordance with SFAS No. 128, "Earnings per Share". The Company computes basic earnings per share by dividing net income for the period by the weighted average number of shares of common stock outstanding during the period. For purposes of calculating diluted earnings per share, the Company assumes the conversion of its Series B Convertible Preferred Stock and considers its shares issuable in connection with stock options to be dilutive common stock equivalents when the exercise price is less than the average market price of the Company's common stock for the period. The Company excludes antidilutive common stock equivalents from the calculation of diluted earnings per share. The following table outlines the calculation of basic earnings per share and diluted earnings per share for the three months ended March 31, 2001 and year ended December 31, 2000.

NOTE F -- EARNINGS PER COMMON SHARE (CONTINUED)

	Income (Numerator)	SHARES (DENOMINATOR)	PER AM
Three Months Ended March 31, 2001:			
Income attributable to shareholders	$681,472	16,928,332	
Effect of dividends to preferred stockholders	(1,250)		
Basic EPS - Income attributable to common shareholders	680,222	16,928,332	
Effect of dilutive securities:			
Assumed conversion of Series B Preferred Stock		1,977,607	
Assumed exercise of dilutive stock options		1,207	
Diluted EPS - Income attributable to common shareholders	$680,222	18,907,146	
YEAR ENDED DECEMBER 31, 2000:			
Income attributable to shareholders	$663,596	16,928,332	
Effect of dividends to preferred stockholders	(5,000)		
Basic EPS - Income attributable to common shareholders	658,596	16,928,332	
Effect of dilutive securities:			
Assumed conversion of Series B Preferred Stock		1,977,607	
Assumed exercise of dilutive stock options		2,026	
Diluted EPS - Income attributable to common shareholders	$658,596	18,907,965	

NOTE G - RESTATEMENT

The pro forma financial statements have been restated from those previously filed principally to increase the purchase price of Microgy to include estimated direct costs of the acquisition. This resulted in an increase to goodwill and an increase to amortization expense for the three months ended March 31, 2001 and the year ended December 31, 2001.