

ENERGYCONNECT GROUP INC

FORM 10-Q (Quarterly Report)

Filed 08/07/08 for the Period Ending 06/28/08

Address	5335 SW MEADOWS ROAD SUITE 325 LAKE OSWEGO, OR 97035
Telephone	8664887642
CIK	0000944947
Symbol	ECNG
SIC Code	1731 - Electrical Work
Industry	Computer Peripherals
Sector	Technology
Fiscal Year	01/02

U.S. Securities and Exchange Commission

Washington, D. C. 20549

Form 10-Q

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

For the quarterly period ended June 28, 2008

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

For the transition period from _____ to _____

Commission File Number : 0-26226

MICROFIELD GROUP, INC.

(Name of small business issuer in its charter)

Oregon

(State or other jurisdiction of incorporation or organization)

93-0935149

(I. R. S. Employer Identification No.)

111 SW Columbia Ave., Suite 480

Portland, Oregon 97201

(Address of principal executive offices and zip code)

(503) 419-3580

(Issuer's telephone number)

Securities registered under Section 12(b) of the Exchange Act: None

Securities registered under Section 12(g) of the Exchange Act:

Common Stock

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

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

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

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

The number of shares outstanding of the Registrant's Common Stock as of July 31, 2008 was 94,651,461 shares.

MICROFIELD GROUP, INC.

FORM 10-Q

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Item 1. Financial Statements

MICROFIELD GROUP, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

	June 28, 2008	December 29, 2007
Current assets:	(Unaudited)	
Cash and cash equivalents	\$ 1,360,855	\$ 758,299
Certificates of deposit	300,000	133,400
Accounts receivable	1,929,381	1,532,843
Other current assets	557,428	551,601
Discontinued operations	-	12,666,606
Total current assets	<u>4,147,664</u>	<u>15,642,749</u>
Property and equipment, net	260,329	202,487
Intangible assets, net (Note 5)	1,753,156	1,872,689
Goodwill	29,353,527	29,353,527
Other assets	75,740	43,175
Discontinued operations	-	971,017
	<u>\$ 35,590,416</u>	<u>\$ 48,085,644</u>
Current liabilities:		
Accounts payable	\$ 3,657,145	\$ 2,975,847
Bank line of credit (Note 4)	117,257	118,456
Other current liabilities	143,432	122,652
Discontinued operations	-	13,549,408
Total current liabilities	<u>3,917,834</u>	<u>16,766,363</u>
Long-term liabilities:		
Discontinued operations	-	61,327
Total long-term liabilities	<u>-</u>	<u>61,327</u>
Commitments and contingencies		
Shareholders' equity :		
Common stock, no par value, 225,000,000 shares authorized, 94,651,461 and 83,569,416 shares issued and outstanding, respectively (Note 2)	120,499,217	115,776,415
Common stock warrants (Note 3)	36,178,218	36,178,218
Accumulated deficit	(125,004,853)	(120,696,679)
Total shareholders' equity	<u>31,672,582</u>	<u>31,257,954</u>
	<u>\$ 35,590,416</u>	<u>\$ 48,085,644</u>

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

MICROFIELD GROUP, INC.

CONDENSED CONSOLIDATED STATEMENT OF OPERATIONS
(Unaudited)

	Three months ended		Six months ended	
	June 28, 2008	June 30, 2007	June 28, 2008	June 30, 2007
Sales	\$ 5,062,682	\$ 3,117,329	\$ 12,441,695	\$ 5,717,491
Cost of goods sold	<u>4,299,758</u>	<u>2,500,496</u>	<u>10,486,713</u>	<u>4,668,495</u>
Gross profit	762,924	616,833	1,954,982	1,048,996
Operating expenses				
Sales, general and administrative	<u>3,196,204</u>	<u>1,947,713</u>	<u>6,298,320</u>	<u>3,726,123</u>
Loss from operations	(2,433,280)	(1,330,880)	(4,343,338)	(2,677,127)
Other income (expense)				
Interest income, net	13,833	4,838	19,683	10,825
Other income, net	<u>26,763</u>	<u>2,246</u>	<u>26,763</u>	<u>2,246</u>
Loss before provision for income taxes	(2,392,684)	(1,323,796)	(4,296,892)	(2,664,056)
Provision for income taxes	-	-	-	-
Loss from continuing operations	(2,392,684)	(1,323,796)	(4,296,892)	(2,664,056)
Discontinued operations:				
Gain (loss) on discontinued operations	28,585	263,135	(146,057)	(369,031)
Gain on sale of discontinued operations	<u>134,775</u>		<u>134,775</u>	
Net loss	<u>\$ (2,229,324)</u>	<u>\$ (1,060,661)</u>	<u>\$ (4,308,174)</u>	<u>\$ (3,033,087)</u>
Net loss per share from continuing operations:				
Basic	<u>\$ (0.03)</u>	<u>\$ (0.02)</u>	<u>\$ (0.05)</u>	<u>\$ (0.03)</u>
Diluted	<u>\$ (0.03)</u>	<u>\$ (0.02)</u>	<u>\$ (0.05)</u>	<u>\$ (0.03)</u>
Net income (loss) per share from discontinued operations:				
Basic	<u>\$ 0.00</u>	<u>\$ 0.01</u>	<u>\$ (0.00)</u>	<u>\$ (0.01)</u>
Diluted	<u>\$ 0.00</u>	<u>\$ 0.01</u>	<u>\$ (0.00)</u>	<u>\$ (0.01)</u>
Net loss per share:				
Basic	<u>\$ (0.03)</u>	<u>\$ (0.01)</u>	<u>\$ (0.05)</u>	<u>\$ (0.04)</u>
Diluted	<u>\$ (0.03)</u>	<u>\$ (0.01)</u>	<u>\$ (0.05)</u>	<u>\$ (0.04)</u>
Shares used in per share calculations:				
Basic	<u>90,392,194</u>	<u>83,012,972</u>	<u>87,569,489</u>	<u>81,453,776</u>
Diluted	<u>90,392,194</u>	<u>83,012,972</u>	<u>87,569,489</u>	<u>81,453,776</u>

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements .

MICROFIELD GROUP, INC.

CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

(Unaudited)

	Six Months Ended	
	June 28, 2008	June 30, 2007
Cash Flows From Operating Activities:		
Net loss	\$ (4,308,174)	\$ (3,033,087)
Add (deduct):		
Loss on discontinued operations	11,282	369,031
Loss from continuing operations	(4,296,892)	(2,664,056)
Depreciation of equipment	52,354	145,570
Amortization of intangible assets	119,534	264,342
Option vesting valuation	471,567	483,999
Common stock issued for services	214,883	-
Changes in current assets and liabilities:		
Restricted cash	(166,600)	-
Accounts receivable	(396,538)	98,693
Other current assets	(383,147)	(149,523)
Other assets	(32,566)	(583)
Accounts payable	681,298	178,324
Other current liabilities	20,780	(101,860)
Net cash used by continuing operations	(3,715,327)	(1,745,094)
Net cash provided (used) by discontinued operations	379,320	(359,125)
Net cash used by operating activities	(3,336,007)	(2,104,219)
Cash flows from investing activities:		
Purchases of fixed assets	(110,196)	(39,196)
Net cash used by continuing investing activities	(110,196)	(39,196)
Net cash used by discontinued investing activities	(534,326)	(158,676)
Net cash used by investing activities	(644,522)	(197,872)
Cash flows from financing activities:		
Repayments on line of credit	(1,199)	(1,020)
Exercise of options and warrants	568,230	-
Proceeds from private placement, net of direct costs	3,476,891	-
Net cash provided (used) by continuing financing activities	4,043,922	(1,020)
Net cash provided by discontinued financing activities	539,163	1,805,744
Net cash provided by financing activities	4,583,085	1,804,724
Net increase (decrease) in cash and cash equivalents	602,556	(497,367)
Cash and cash equivalents, beginning of period	758,299	2,193,308
Cash and cash equivalents, end of period	\$ 1,360,855	\$ 1,695,941
Supplemental disclosures for cash flow information:		
Cash paid during the period for interest	\$ 5,893	\$ 171,967
Cash paid during the period for income taxes	\$ -	\$ -
Supplemental schedule of non-cash financing and investing activities:		
Conversion of preferred to common	\$ -	\$ 1,031,093

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

MICROFIELD GROUP, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
June 28, 2008
(Unaudited)

1. Description of the Business

General

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements.

In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Accordingly, the results from operations for the three and six-month periods ended June 28, 2008, are not necessarily indicative of the results that may be expected for the year ended January 3, 2009. The unaudited condensed consolidated financial statements should be read in conjunction with the consolidated December 29, 2007 financial statements and footnotes thereto included in the Company's Form 10-K.

Business and Basis of Presentation

Microfield Group, Inc. (the "Company," "Microfield," "we," "us," or "our") through its continuing subsidiary EnergyConnect, Inc. ("ECI") provides a full range of demand response services to the electric power industry. Our customers are the regional grid operators who pay us market rates for reductions in electrical demand during periods of high prices or peak demand and for being on stand by to reduce electric power demand on request at periods of capacity limitations or in response to grid emergencies. Our suppliers are large commercial and industrial consumers of electricity who we pay to shift their demand for electricity from high priced hours in the day to lower priced hours. We also pay these participating energy consumers to be on stand by to curtail electric demand on request.

Through proprietary technology and business processes we automate electric consumer demand response transactions and the associated measurement, verification, and support decisions. These capabilities make it possible and easy for electric consumers, particularly commercial and industrial facilities, to shift load from high priced hours to lower priced periods.

Our services provide market incentives to reduce electric demand during periods of peak demand or high prices. By shifting load from high demand periods to times of lower electrical demand our services improve the operating efficiency of the electrical grids and improve grid reliability. We also delay the need for construction of new electrical generating plants. Through higher efficiencies on the grid, lower cost of generation and improved reliability all consumers of electricity benefit from our demand response activities on the electrical grid. By providing consumers of electricity an effective means of responding to grid wholesale prices of electricity we complete the supply demand market place for electricity and provide offsetting market forces to electricity generators.

Our customers are regional electric grid operators such as PJM, the largest electric grid in the nation, and selected electric utilities who support and sponsor demand response. All of our current operations are in the United States with services provided in more than 25 states. Following a three year testing and pilot period, we began commercial operations in 2005 and have been growing steadily since then. Our revenues in 2007 were \$12.6 million. Our suppliers are commercial and industrial electric energy consumers who we pay to shift, curtail, bank, and in some cases produce electric energy.

ECI operates on a national footprint currently serving consumers and grid operators in more than 25 states. ECI delivers services to wholesale electric markets of regional electric grids. Selected needs of electric grid operators, including energy, capacity, and reserves have been formed into products that can be delivered through ECI systems to the grid. ECI technologies, processes, and services enable buildings and electric consumers to contribute to such wholesale services in direct competition with expensive peaking power plants.

In 2003 we acquired a part of Christenson Electric, Inc. ("CEI"), and in 2005, we acquired the remainder of CEI and the operations of ECI. This combined a 60 year old electrical contracting and technology business with a high growth demand response business. In 2007 we determined that ECI had grown to a self sustaining transition point and in November 2007 we agreed to sell the stock of CEI. Our objective is to leverage our unique and proprietary technologies, business processes, and resources and build a viable, profitable demand response business servicing North American wholesale power markets. Financial statements and accompanying notes included in this report include disclosure of the results of operations for CEI, for all periods presented, as discontinued operations. All significant inter-company accounts and transactions have been eliminated in consolidation.

The Company was incorporated in October 1986 as an Oregon Corporation, succeeding operations that began in October 1984. The Company's headquarters are located in Portland, Oregon.

Reclassification

Certain reclassifications have been made to conform to prior periods' data to the current presentation. These reclassifications had no effect on reported losses.

Fiscal Year

The Company's fiscal year is the 52- or 53-week period ending on the Saturday closest to the last day of December. The Company's current fiscal year is the 52-week period ending January 3, 2009. The Company's last fiscal year was the 52-week period ended December 29, 2007. The Company's second fiscal quarters in fiscal 2008 and 2007 were the 13-week periods ended June 28, 2008 and June 30, 2007, respectively.

Revenue Recognition

We produce revenue through agreements with both building owners and the power grid operators. Under our agreements with facilities owners, we use electrical and energy related products that help energy consumers control energy use in their buildings. In conjunction with this agreement we are members of the power grid operators and have agreed to provide the grids with energy, capacity, and related ancillary services during specified times and under specified conditions. These transactions are summarized at the end of each monthly period and submitted to the power grids for settlement and approval. While the power grids are our customers, they are primarily a conduit through which these electrical curtailment transactions are processed. The vast majority of our revenue in 2007 was processed through the PJM Interconnection. PJM serves as the market for electrical transactions in a specific region in the United States. Our agreement with PJM is an ongoing one as we are members of PJM. These transactions are initiated by building owners, who are our participants. These transactions form the basis for our revenue. We have little risk, if any, from the concentration of revenue through this power grid as it's a not-for-profit organization that exists to act as the market for electrical transactions.

In 2008, we have revised our accounting for reserves for collections of revenues. The revision in our reserve accounting is a result of improvements in our ability to accurately estimate collections, which is based upon historical trends and timely and accurate information. Previously the transactions were recorded as revenue on the settlement date, which may fall 45-70 days after the transaction date from which the revenue is derived, because management believed that without an established history for this source of revenue, and the potential for disputes, that the settlement date, on which both parties agree to the amount of revenue to recognize, was the most conservative and appropriate date to use. For periods beginning with the first quarter of 2008 and forward, revenue from these settlements will be accrued into the prior month instead of recognizing revenue as the settlement amounts were received. The record of these settlement amounts being realized over these prior two years has been extremely accurate so that management believes it is appropriate to accrue the settlement amounts into the prior month. This revision in our reserve accounting resulted in an extra month of revenue being recorded in the first quarter of 2008. This quarter contains the payment received in January of 2008 (which was not accrued into December) and the settlement amounts from the fifth business day in February, March and April of 2008, each of which was accrued into the prior months of January, February and March of 2008.

An additional source of our revenue is derived from agreements with the power grid operators whereby a monthly reserve fee is paid for our agreement to standby, ready to provide relief in the form of curtailment of energy usage, in times of high energy demand. We record these payments as revenue over the period during which we're required to perform under these programs. Under certain programs, our obligation to perform may not coincide with the period over which we receive payments under that program. In these cases we record revenue over the mandatory performance obligation period and record a receivable for the amount of payments that will be received after that period has been completed.

New Accounting Pronouncements

In April 2008, the FASB issued FSP No. 142-3, "Determination of the Useful Life of Intangible Assets" ("FSP 142-3"). FSP 142-3 amends the factors an entity should consider in developing renewal or extension assumptions used in determining the useful life of recognized intangible assets under FASB Statement No. 142, "Goodwill and Other Intangible Assets". This new guidance applies prospectively to intangible assets that are acquired individually or with a group of other assets in business combinations and asset acquisitions. FSP 142-3 is effective for financial statements issued for fiscal years and interim periods beginning after December 15, 2008. Early adoption is prohibited. We are currently evaluating the impact, if any, that FSP 142-3 will have on our consolidated financial statements.

In May 2008, the FASB issued SFAS No. 162, "The Hierarchy of Generally Accepted Accounting Principles" ("SFAS 162"). SFAS 162 identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements of nongovernmental entities that are presented in conformity with generally accepted accounting principles (the GAAP hierarchy). SFAS 162 will become effective 60 days following the SEC's approval of the Public Company Accounting Oversight Board amendments to AU Section 411, "The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles." We do not currently expect the adoption of SFAS 162 to have a material effect on our consolidated results of operations and financial condition.

In May 2008, the FASB issued FSP Accounting Principles Board ("APB") 14-1 "Accounting for Convertible Debt instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)" ("FSP APB 14-1"). FSP APB 14-1 requires the issuer of certain convertible debt instruments that may be settled in cash (or other assets) on conversion to separately account for the liability (debt) and equity (conversion option) components of the instrument in a manner that reflects the issuer's non-convertible debt borrowing rate. FSP APB 14-1 is effective for fiscal years beginning after December 15, 2008 on a retroactive basis. As we do not have convertible debt at this time, we currently believe the adoption of FSP APB 14-1 will have no effect on our consolidated results of operations and financial condition.

2. Capital Stock

The Company has authorized 10,000,000 shares of Preferred Stock, no par value. As of June 28, 2008 and December 29, 2007, the Company's Series 2, Series 3 and Series 4 preferred stock had been completely converted to common shares. The Company has authorized 225,000,000 shares of Common Stock, no par value. As of June 28, 2008 and December 29, 2007, the Company had 94,651,461 and 83,569,416 shares of common stock issued and outstanding, respectively. During the six month period ended June 28, 2008, the Company issued an aggregate of 11,082,046 shares of common stock, of which 9,051,310 were issued in a private placement, 355,438 were issued for services, 34,467 in exchange for warrants exercised, and 1,640,831 in exchange for common stock options exercised.

3. Stock Options and Warrants

Stock Incentive Plan

The Company has a Stock Incentive Plan (the "Plan"). At June 28, 2008 and June 30, 2007, 7,686,370 and 7,520,750 shares of common stock were reserved, respectively, for issuance to employees, officers, directors and outside advisors. Under the Plan, the options may be granted to purchase shares of the Company's common stock at fair market value, as determined by the Company's Board of Directors, at the date of grant. The options are exercisable over a period of up to ten years from the date of grant or such shorter term as provided for in the Plan. The options become exercisable over periods from zero to four years.

A total of 62,000 options to purchase shares of the Company's common stock were granted to employees of the Company, and 85,000 options granted to consultants during the six months ended June 28, 2008. There were 362,500 options granted to employees, directors and consultants during the six months ended June 30, 2007. The 62,000 options issued to employees during the six months ended June 28, 2008 are forfeited if not exercised within five years. All of these options granted during the six months ended June 28, 2008 have a 12 month waiting period during which no vesting occurs. At the end of this period, the options become 25% vested, and then vest ratably over the remaining thirty six-months of the vesting period. The weighted average per share value of these options was \$0.55.

The following table summarizes the changes in stock options outstanding and the related prices for the shares of the Company's common stock issued to employees, officers and directors of the Company under the Plan.

Exercise Prices	Options Outstanding			Options Exercisable		
	Number Outstanding	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price	
\$ 0.26 - \$0.94	7,409,981	3.77	\$ 0.69	4,283,950	\$ 0.59	
\$ 1.76 - \$2.70	276,389	2.93	\$ 2.13	170,138	\$ 2.20	
	<u>7,686,370</u>	<u>3.70</u>	<u>\$ 0.74</u>	<u>4,454,088</u>	<u>\$ 0.65</u>	

Transactions involving stock options issued are summarized as follows:

	Number of Shares	Weighted Average Price Per Share
Outstanding at December 31, 2005	<u>7,717,765</u>	<u>\$ 0.44</u>
Granted	1,625,000	1.02
Exercised	(265,188)	0.38
Cancelled or expired	(20,000)	1.25
Outstanding at December 30, 2006	<u>9,057,577</u>	<u>\$ 0.54</u>
Granted	2,707,500	0.55
Exercised	(1,829,507)	0.34
Cancelled or expired	(211,820)	0.32
Outstanding at December 29, 2007	<u>9,723,750</u>	<u>\$ 0.60</u>
Granted	147,000	0.46
Exercised	(1,640,831)	0.34
Cancelled or expired	(543,549)	0.97
Outstanding at June 28, 2008	<u>7,686,370</u>	<u>\$ 0.74</u>

The Company has computed the value of all options granted during fiscal 2008 and 2007 using the Black-Scholes pricing model as prescribed by SFAS No. 123(R). The following assumptions were used to calculate the value of options granted during the second quarters of 2008 and 2007:

	2008	2007
Risk-free interest rate	3.54%	4.64%
Expected dividend yield	-	-
Expected life	5 years	5 years
Expected volatility	122%	134%

Stock-based compensation expense recognized under SFAS 123(R) for the three and six months ended June 28, 2008 was \$274,143 and \$471,567, respectively. Stock-based compensation expense recognized under SFAS 123(R) for the three and six months ended June 30, 2007 was \$284,197 and \$483,999, respectively.

Common Stock Warrants

In connection with an April 2003 common stock private placement, we issued 111,308 warrants to purchase common stock. Each warrant is exercisable into one share of common stock at \$0.40 per share and will expire in 2008. Subsequent to this private placement, the Company exercised an option to convert \$1,400,000 of outstanding debt into preferred stock that is convertible into shares of common stock. This exercise, when aggregated with all other outstanding equity arrangements, resulted in the total number of common shares that could be required to be delivered to exceed the number of authorized common shares. In accordance with EITF 00-19, the fair value of the warrants issued in the private placement must be recorded as a liability in the financial statements using the Black-Scholes model, and any subsequent changes in the Company's stock price to be recorded in earnings. Accordingly, the fair value of these warrants at the date of issuance was determined to be \$19,832. At September 1, 2004, the Company's shareholder's voted to increase the authorized shares available for issuance or conversion, which cured the situation described above. Accordingly, the fair value of the warrants on September 1, 2004 was determined to be \$48,976. The warrant liability was reclassified to shareholders' equity and the increase from the initial warrant value was recorded in earnings in the fiscal year ended January 1, 2005. As of June 28, 2008, the warrant holders have exercised 101,308 warrants in exchange for 101,308 shares of our common stock and 10,000 warrants have expired.

In September 2003, in connection with a preferred stock private placement, we issued 333,334 warrants to purchase common stock. Each warrant is exercisable into one share of common stock at \$0.42 per share and will expire in 2008. In September 2003, in connection with a preferred stock private placement, the Company issued 333,334 warrants to purchase common stock. Each warrant is exercisable into one share of common stock at \$0.42 per share and will expire in 2008. Subsequent to this private placement, the Company exercised an option to convert \$1,400,000 of outstanding debt into preferred stock that is convertible into shares of common stock. This exercise, when aggregated with all other outstanding equity arrangements, resulted in the total number of common shares that could be required to be delivered to exceed the number of authorized common shares. In accordance with EITF 00-19, the fair value of the warrants issued in the private placement must be recorded as a liability in the financial statements using the Black-Scholes model, and any subsequent changes in the Company's stock price to be recorded in earnings. Accordingly, the fair value of these warrants at the date of issuance was determined to be \$64,902. At September 1, 2004, the Company's shareholder's voted to increase the authorized shares available for issuance or conversion, which cured the situation described above. Accordingly, the fair value of the warrants on September 1, 2004 was determined to be \$139,000. The warrant liability was reclassified to shareholders' equity and the increase from the initial warrant value was recorded in earnings in the fiscal year ended January 1, 2005. As of June 28, 2008, the warrant holders have exercised 217,800 warrants in exchange for 217,800 shares of our common stock and 115,534 warrants remain outstanding.

In connection with the August 24, 2004 debt issuance by Destination Capital, LLC, the Company is obligated to issue warrants to purchase the Company's common stock. According to the terms of the debt issuance, warrants in the amount of 12.5% of the loan balance, outstanding on the first day of each month, will be issued to the debt holders for each calendar month that the debt is outstanding. Each warrant is exercisable into one share of common stock at the lesser of \$0.38 per share or the price applicable to any shares, warrants or options issued (other than options issued to employees or directors) while the loan is outstanding, and will expire in 2009. Prior to this debt issuance, the Company exercised an option to convert \$1,400,000 of outstanding debt into preferred stock that is convertible into shares of common stock. This exercise, when aggregated with all other outstanding equity arrangements, resulted in the total number of common shares that could be required to be delivered to exceed the number of authorized common shares. In accordance with EITF 00-19, the fair value of the 37,500 warrants initially issued in connection with the debt issuance must be recorded as a liability for warrant settlement in the financial statements using the Black-Scholes model, and any subsequent changes in the Company's stock price to be recorded in earnings. Accordingly, the aggregate fair value of these warrants, issued prior to September 1, 2004, was determined to be \$17,513. At September 1, 2004, the Company's shareholder's voted to increase the authorized shares available for issuance or conversion, which cured the situation described above. Accordingly, the fair value of the warrants on September 1, 2004 was determined to be \$20,776. The warrant liability was reclassified to shareholders' equity and the increase from the initial warrant value was recorded in earnings in the fiscal year ended January 1, 2005. For the months from August 1, 2004 to July 2, 2005, according to the terms of the warrant provision of the August 24, 2004 debt agreement, the Company was obligated to issue 1,626,042 additional warrants. The value of these warrants of \$604,955 was added to shareholders' equity on the consolidated balance sheet, with a corresponding expense charged to interest expense in the consolidated statement of operations. As of June 28, 2008, the holders of these warrants exercised 1,309,616 warrants in exchange for 1,170,841 shares of the Company's common stock, and 316,426 warrants remain outstanding.

On October 13, 2005, the Company issued an aggregate of 19,695,432 warrants in connection with the acquisition of acquired EnergyConnect, Inc. The Company valued the warrants using the Black-Scholes option pricing model, applying a useful life of 5 years, a risk-free rate of 4.06%, an expected dividend yield of 0%, a volatility of 129% and a fair value of the common stock of \$2.17. Total value of the warrants issued amounted \$36,495,391, which was included in the purchase price of ECI. As of June 28, 2008, the warrant holders have not exercised any of these warrants.

On October 5, 2005, in conjunction with a private placement which resulted in gross proceeds of \$3,276,000, the Company sold 5,233,603 shares of common stock at \$0.70 per share, and issued warrants to purchase up to 2,944,693 shares of common stock. The warrants have a term of five years and an exercise price of \$0.90 per share. As of June 28, 2008, the warrant holders have exercised 192,370 warrants, for 180,409 shares of common stock, and 2,752,323 warrants remain outstanding.

On June 30, 2006, in conjunction with a private placement which resulted in gross proceeds of \$15,000,000, the Company sold 7,500,000 shares of common stock at \$2.00 per share, and issued warrants to purchase up to 5,625,000 shares of common stock. The warrants have a term of five years and an exercise price of \$3.00 per share. As of June 28, 2008, the warrant holders have not exercised any of these warrants.

On May 7, 2008, in conjunction with a private placement which resulted in gross proceeds of \$3,615,000, the Company sold 9,051,310 shares of common stock at \$0.40 per share, and issued warrants to purchase up to 4,525,655 shares of common stock. The warrants have a term of five years and an exercise price of \$0.60 per share. As of June 28, 2008, the warrant holders have not exercised any of these warrants.

Warrants for 34,467 common shares were exercised during the six months ended June 28, 2008.

4. Debt

Operating Line of Credit

The Company has a loan facility which is an unsecured \$120,000 line of credit at prime plus 3 ¾%, due on demand with interest payable monthly. As of June 28, 2008 and December 29, 2007, there was \$117,257 and \$118,456 outstanding, respectively, under this line. The Company was in compliance with the terms of this line of credit at June 28, 2008. The Company had no other term debt or loans outstanding at June 28, 2008.

5. Intangible Assets and Goodwill

As a result of our acquisition of ECI we recorded an intangible asset of \$2,390,667 at the date of acquisition representing developed technology that is currently used within ECI. The intangible asset acquired has an estimated useful life of ten years, and as such is being amortized monthly, over that period. Goodwill of \$106,544,871 represented the excess of the purchase price over the fair value of the net tangible and intangible assets acquired. At December 31, 2005, it was determined in an independent valuation that the goodwill generated in this transaction was impaired. The Company decided to write off approximately \$77,191,344 of this goodwill. The write-off of the goodwill, and the amortization of the intangible assets are included in operating expenses in the consolidated statement of operations. The following table presents details of the purchased intangible assets as of June 28, 2008 and December 29, 2007:

	<u>June 28, 2008</u>	<u>December 29, 2007</u>
Developed technology	2,390,667	2,390,667
Less accumulated amortization	(637,511)	(517,978)
	<u>\$ 1,753,156</u>	<u>\$ 1,872,689</u>

Amortization of intangible assets included as a charge to income was \$59,767 and \$ 119,533 for both of the three and six month periods ended June 28, 2008 and June 30, 2007 .

Based on the Company's current intangible assets, amortization expense for the five succeeding years will be as follows:

<u>Year</u>	<u>Amortization Expense</u>
Twelve months ended June 30, 2009	\$ 239,067
Twelve months ended June 30, 2010	239,067
Twelve months ended June 30, 2011	239,067
Twelve months ended June 30, 2012	239,067
Twelve months ended June 30, 2013	239,067
July 1, 2013 and beyond	557,821
Total	<u>\$ 1,753,156</u>

The Company does not amortize goodwill. There were no changes in the carrying amount of goodwill during the year ended December 29, 2007 and the quarter ended June 28, 2008.

6. Business Concentrations

Financial transactions and instruments that potentially subject us to concentrations of credit risk consist primarily of revenue generating transactions and the resultant accounts receivable. During the three months ended June 28, 2008, revenue from one major customer approximated \$4,809,000 or 95% of sales. This revenue is the result of multiple participating electric consumers who each executed myriad energy transactions that were aggregated and billed to the PJM Interconnection, or PJM. The revenue is dependent on actions taken by these third parties in conjunction with ECI, for which PJM, as our customer remits payment. These transactions form the basis for our revenue. We have little risk, if any, from the concentration of revenue through this power grid as it's a not-for-profit organization that exists to act as the market for electrical transactions. Of these participants, there were three whose transactions resulted in revenue that totaled 10% or more (21%, 17% and 12%) of our revenue in the three months ended June 28, 2008 and two whose transactions resulted in revenue that totaled 10% or more (46% and 18%) of our revenue in the three months ended June 30, 2007. For the six month period ended June 28, 2008 there were two participants whose transactions resulted in revenue that totaled 21% and 13% of our revenue. For the six month period ended June 30, 2007, there were two participants whose transactions resulted in revenue that totaled 50% and 17% of our revenue.



7. Sale of Discontinued Operations

Divestiture of Christenson Electric, Inc.

On July 20, 2005, the Company acquired Christenson Electric, Inc. (CEI) in exchange for 2,000,000 shares of the Company's common stock and the assumption of certain liabilities within CEI. CEI provides services to utilities and other energy related companies. On November 29, 2007, our board of directors signed an agreement to sell all of the shares of our wholly-owned subsidiary Christenson Electric, Inc. to a corporation formed by the management of CEI. The agreement was approved by our shareholders in a vote on March 10, 2008. The closing occurred on April 24, 2008.

The following summarizes the actual results of the disposition of the CEI business segment.

Debts assumed by buyer	\$ 12,653,197
Net assets disposed of	(12,149,018)
Expenses incurred in connection with the transaction	<u>(369,404)</u>
Net gain on disposal of CEI	<u>\$ 134,775</u>

8. Private Placement

On May 7, 2008 we closed a private placement in which we issued 9,051,310 shares of common stock resulting in aggregate gross proceeds of \$3,512,000 and elimination of accounts payable of \$103,000. In conjunction with this private placement, we also issued 4,525,655 five year warrants exercisable at \$0.60 per share. The proceeds of this financing will be used for general working capital purposes.

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

The following discussion of the financial condition and results of operations of Microfield Group, Inc. should be read in conjunction with the Management's Discussion and Analysis of Financial Condition and Results of Operations, and the Consolidated Financial Statements and the Notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 29, 2007.

Forward-Looking Statements

Certain statements contained in this Form 10-Q concerning expectations, beliefs, plans, objectives, goals, strategies, future events or performance and underlying assumptions and other statements which are other than statements of historical facts are "forward-looking statements" within the meaning of the federal securities laws. Although the Company believes that the expectations and assumptions reflected in these statements are reasonable, there can be no assurance that these expectations will prove to be correct. These forward-looking statements involve a number of risks and uncertainties, and actual results may differ materially from the results discussed in the forward-looking statements. Any such forward-looking statements should be considered in light of such important factors and in conjunction with other documents of the Company on file with the SEC.

New factors that could cause actual results to differ materially from those described in forward-looking statements emerge from time to time, and it is not possible for the Company to predict all of such factors, or the extent to which any such factor or combination of factors may cause actual results to differ from those contained in any forward-looking statement. Any forward-looking statement speaks only as of the date on which such statement is made, and the Company undertakes no obligations to update the information contained in such statement to reflect subsequent developments or information.

Overview

Microfield Group, Inc. (the "Company," "Microfield," "we," "us," or "our") through its subsidiary EnergyConnect, Inc. ("ECI") provides a full range of demand response services to the electric power industry. Our customers are the regional grid operators who pay us market rates for reductions in electrical demand during periods of high prices or peak demand and for being on stand by to reduce electric power demand on request at periods of capacity limitations or in response to grid emergencies. Our suppliers are large commercial and industrial consumers of electricity who we pay to shift their demand for electricity from high priced hours in the day to lower priced hours. We also pay these participating energy consumers to be on stand by to curtail electric demand on request.

Through proprietary technology and business processes we automate electric consumer demand response transactions and the associated measurement, verification, and support decisions. These capabilities make it possible and easy for electric consumers, particularly commercial and industrial facilities, to shift load from high priced hours to lower priced periods.

Our services provide market incentives to reduce electric demand during periods of peak demand or high prices. By shifting load from high demand periods to times of lower electrical demand our services improve the operating efficiency of the electrical grids and improve grid reliability. We also delay the need for construction of new electrical generating plants. Through higher efficiencies on the grid, lower cost of generation and improved reliability all consumers of electricity benefit from our demand response activities on the electrical grid. By providing consumers of electricity an effective means of responding to grid wholesale prices of electricity we complete the supply demand market place for electricity and provide offsetting market forces to electricity generators.

Our customers are regional electric grid operators such as PJM, the largest electric grid in the nation, and selected electric utilities who support and sponsor demand response. All of our current operations are in the United States with services provided in more than 25 states. Following a three year testing and pilot period, we began commercial operations in 2005 and have been growing steadily since then. Our revenues in 2007 were \$12.7 million. Our suppliers are commercial and industrial electric energy consumers who we pay to shift, curtail, bank, and in some cases produce electric energy.

ECI operates on a national footprint currently serving consumers and grid operators in more than 25 states. ECI delivers services to wholesale electric markets of regional electric grids. Selected needs of electric grid operators, including energy, capacity, and reserves have been formed into products that can be delivered through ECI systems to the grid. ECI technologies, processes, and services enable buildings and electric consumers to contribute to such wholesale services in direct competition with expensive peaking power plants.

In 2003 we acquired a part of Christenson Electric, Inc. (“CEI”), and in 2005, we acquired the remainder of CEI and the operations of ECI. This combined a 60 year old electrical contracting and technology business with a high growth demand response business. In 2007 we determined that ECI had grown to a self sustaining transition point and in November 2007 we agreed to sell the stock of CEI. Our objective is to leverage our unique and proprietary technologies, business processes, and resources and build a viable, profitable demand response business servicing North American wholesale power markets. Financial statements and accompanying notes included in this report include disclosure of the results of operations for CEI, for all periods presented, as discontinued operations. All significant inter-company accounts and transactions have been eliminated in consolidation.

The Company was incorporated in October 1986 as an Oregon Corporation, succeeding operations that began in October 1984. The Company’s headquarters are located in Portland, Oregon.

Critical Accounting Policies

The discussion and analysis of financial condition and results of operations is based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. We continuously evaluate, our estimates and judgments, including those related to revenue recognition, sales returns, bad debts, excess inventory, impairment of goodwill and intangible assets, income taxes, contingencies and litigation. Our estimates are based on historical experience and assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. We discuss the development and selection of the critical accounting estimates with the Audit Committee of our Board of Directors on a quarterly basis, and the Audit Committee has reviewed our related disclosure in this Form 10-Q.

We believe the following critical accounting policies, among others, affect our more significant judgments and estimates used in the preparation of our consolidated financial statements:

Revenue recognition

We produce revenue through agreements with both building owners and the power grid operators. Under our agreements with facilities owners, we use electrical and energy related products that help energy consumers control energy use in their buildings. In conjunction with this agreement we are members of the power grid operators and have agreed to provide the grids with energy, capacity, and related ancillary services during specified times and under specified conditions. These transactions are summarized at the end of each monthly period and submitted to the power grids for settlement and approval. While the power grids are our customers, they are primarily a conduit through which these electrical curtailment transactions are processed. The vast majority of our revenue in 2007 was processed through the PJM Interconnection. PJM serves as the market for electrical transactions in a specific region in the United States. Our agreement with PJM is an ongoing one as we are members of PJM. These transactions are initiated by building owners, who are our participants. The transactions form the basis for our revenue. We have little risk, if any, from the concentration of revenue through this power grid as it’s a not-for-profit organization that exists to act as the market for electrical transactions.

In 2008, we have revised our accounting for reserves for collections of revenues. The revision in our reserve accounting is a result of improvements in our ability to accurately estimate collections, which is based upon historical trends and timely and accurate information. Previously the transactions were recorded as revenue on the settlement date, which may fall 45-70 days after the transaction date from which the revenue is derived, because management believed that without an established history for this source of revenue, and the potential for disputes, that the settlement date, on which both parties agree to the amount of revenue to recognize, was the most conservative and appropriate date to use. For periods beginning with the first quarter of 2008 and forward, revenue from these settlements will be accrued into the prior month instead of recognizing revenue as the settlement amounts were received. The record of these settlement amounts being realized over these prior two years has been extremely accurate so that management believes it is appropriate to accrue the settlement amounts into the prior month. This revision in our reserve accounting resulted in an extra month of revenue being recorded in the first quarter of 2008. This quarter contains the payment received in January of 2008 (which was not accrued into December) and the settlement amounts from the fifth business day in February, March and April of 2008, each of which was accrued into the prior months of January, February and March of 2008.

An additional source of our revenue is derived from agreements with the power grid operators whereby a monthly reserve fee is paid for our agreement to standby, ready to provide relief in the form of curtailment of energy usage, in times of high energy demand. We record these payments as revenue over the period during which we're required to perform under these programs. Under certain programs, our obligation to perform may not coincide with the period over which we receive payments under that program. In these cases we record revenue over the mandatory performance obligation period and record a receivable for the amount of payments that will be received after that period has been completed.

Accruals for contingent liabilities

We make estimates of liabilities that arise from various contingencies for which values are not fully known at the date of the accrual. These contingencies may include accruals for reserves for costs and awards involving legal settlements, costs associated with vacating leased premises or abandoning leased equipment, and costs involved with the discontinuance of a segment of a business. Events may occur that are resolved over a period of time or on a specific future date. Management makes estimates of the potential cost of these occurrences, and charges them to expense in the appropriate periods. If the ultimate resolution of any event is different than management's estimate, compensating entries to earnings may be required.

Purchase price allocation and impairment of intangible and long-lived assets

Intangible and long-lived assets to be held and used are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amounts of such assets may not be recoverable. Determination of recoverability is based on an estimate of undiscounted future cash flows resulting from the use of the asset, and its eventual disposition. Measurement of an impairment loss for intangible and long-lived assets that management expects to hold and use is based on the fair value of the asset as estimated using a discounted cash flow model.

We measure the carrying value of goodwill recorded in connection with the acquisitions for potential impairment in accordance with SFAS No. 142, Goodwill and Other Intangible Assets." To apply SFAS 142, a company is divided into separate "reporting units," each representing groups of products that are separately managed. For this purpose, we have one reporting unit. To determine whether or not goodwill may be impaired, a test is required at least annually, and more often when there is a change in circumstances that could result in an impairment of goodwill. If the trading of our common stock is below book value for a sustained period, or if other negative trends occur in our results of operations, a goodwill impairment test will be performed by comparing book value to estimated market value. To the extent goodwill is determined to be impaired, an impairment charge is recorded in accordance with SFAS 142.

We tested our intangibles for impairment as of the end of fiscal years 2007, 2006, and 2005. Goodwill of \$106,544,871 was recorded upon the acquisition of ECI, and represents the excess of the purchase price over the fair value of the net tangible and intangible assets acquired. At December 31, 2005, it was determined in an independent valuation that the goodwill generated in this transaction was impaired. The Company decided to write off approximately \$77,191,344 of this goodwill. The write-off of the goodwill, and the amortization of the intangible assets are included in operating expenses in the consolidated statements of operations. There were no changes in the carrying value of goodwill at December 30, 2006 and December 29, 2007.

Stock-Based Compensation

On January 1, 2006, we adopted Statement of Financial Accounting Standards No. 123 (revised 2004), "Share-Based Payment," ("SFAS 123 (R)") which requires the measurement and recognition of compensation expense for all share-based payment awards made to employees and directors including employee stock options based on estimated fair values. SFAS 123(R) supersedes our previous accounting under Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25") for periods beginning in fiscal 2006. In March 2005, the Securities and Exchange Commission issued Staff Accounting Bulletin No. 107 ("SAB 107") relating to SFAS 123(R). The Company has applied the provisions of SAB 107 in its adoption of SFAS 123(R).

We adopted SFAS 123(R) using the modified prospective transition method, which requires the application of the accounting standard as of January 1, 2006, the first day of the Company's fiscal year 2006. Our Consolidated Financial Statements for three months ended June 28, 2008 and June 30, 2007 reflect the impact of SFAS 123(R). Stock-based compensation expense recognized under SFAS 123(R) for the three months ended June 28, 2008 and June 30, 2007 was \$274,000 and \$284,000, respectively.

SFAS 123(R) requires companies to estimate the fair value of share-based payment awards on the date of grant using an option-pricing model. The value of the portion of the award that is ultimately expected to vest is recognized as expense over the requisite service periods in our Consolidated Statement of Operations. Prior to the adoption of SFAS 123(R), we accounted for stock-based awards to employees and directors using the intrinsic value method in accordance with APB 25 as allowed under Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" ("SFAS 123"). Under the intrinsic value method, no stock-based compensation expense had been recognized in our Consolidated Statement of Operations because the exercise price of our stock options granted to employees and directors equaled the fair market value of the underlying stock at the date of grant.

Stock-based compensation expense recognized during the period is based on the value of the portion of share-based payment awards that is ultimately expected to vest during the period. Stock-based compensation expense recognized in our Consolidated Statements of Operations for the three months ended June 28, 2008 and June 30, 2007 included compensation expense for share-based payment awards granted prior to, but not yet vested as of December 31, 2005 based on the grant date fair value estimated in accordance with the pro forma provisions of SFAS 123 and compensation expense for the share-based payment awards granted subsequent to December 31, 2005 based on the grant date fair value estimated in accordance with the provisions of SFAS 123(R). SFAS 123(R) requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates.

Upon adoption of SFAS 123(R), we are using the Black-Scholes option-pricing model as its method of valuation for share-based awards granted beginning in fiscal 2006, which was also previously used for our pro forma information required under SFAS 123. Our determination of fair value of share-based payment awards on the date of grant using an option-pricing model is affected by our stock price as well as assumptions regarding a number of highly complex and subjective variables. These variables include, but are not limited to our expected stock price volatility over the term of the awards, and certain other market variables such as the risk free interest rate.

Computation of Net Income (Loss) per Share

Basic earnings (loss) per common share is computed using the weighted-average number of common shares outstanding during the period. Diluted earnings per common share is computed using the combination of dilutive common share equivalents, which include convertible preferred shares, options and warrants and the weighted-average number of common shares outstanding during the period. During the three and six months ended June 28, 2008 and June 30, 2007, common stock equivalents are not considered in the calculation of the weighted average number of common shares outstanding because they would be anti-dilutive, thereby decreasing the net loss per common share.

Concentrations

Financial transactions and instruments that potentially subject us to concentrations of credit risk consist primarily of revenue generating transactions and the resultant accounts receivable. During the three months ended June 28, 2008, revenue from one major customer approximated \$4,809,000 or 95% of sales. This revenue is the result of multiple participating electric consumers who each executed myriad energy transactions that were aggregated and billed to the PJM Interconnection, or PJM. The revenue is dependent on actions taken by these third parties in conjunction with ECI, for which PJM, as our customer remits payment. The transactions form the basis for our revenue. We have little risk, if any, from the concentration of revenue through this power grid as it's a not-for-profit organization that exists to act as the market for electrical transactions. Of these participants, there were three whose transactions resulted in revenue that totaled 10% or more (21%, 17% and 12%) of our revenue in the three months ended June 28, 2008 and two whose transactions resulted in revenue that totaled 10% or more (46% and 18%) of our revenue in the three months ended June 30, 2007. For the six month period ended June 28, 2008 there were two participants whose transactions resulted in revenue that totaled 21% and 13% of our revenue. For the six month period ended June 30, 2007, there were two participants whose transactions resulted in revenue that totaled 50% and 17% of our revenue.

At June 28, 2008 and December 29, 2007 there was one customer whose accounts receivable accounted for all of our outstanding trade accounts receivable. We have little risk, if any, from the concentration of receivables through this power grid as it's a not-for-profit organization that exists to act as the market for electrical transactions. We perform limited credit evaluations of our customers and do not require collateral on accounts receivable balances. We have not experienced material credit losses for the periods presented. The level of revenue resulting from any single participant's transactions may vary and the loss of any one of these participants, or a decrease in the level of revenue from transactions generated by any one of these participants, could have a material adverse impact on our financial condition and results of operations.

Recent Accounting Pronouncements

See Note 1 of the Condensed Consolidated Financial Statements for a full description of new accounting pronouncements, including the respective expected dates of adoption and effects on results of operations and financial condition.

Results of Operations

The financial information presented for the three and six months ended June 28, 2008 and June 30, 2007, represents activity in Microfield Group, Inc. and its wholly-owned subsidiaries, CEI and ECI.

Sales . Revenue for the three months ended June 28, 2008 was \$5,063,000 compared to \$3,117,000 for the three months ended June 30, 2007. This increase in year-over-year quarterly revenue in ECI represents both increased usage of services and growth of the participant base within ECI. Transactions during the quarter by three participants generated 21%, 17%, and 12% of the Company's total revenue for the three months ended June 28, 2008. Transactions by two participants generated 46% and 18% of the Company's total revenue for the three months ended June 30, 2007.

We produce revenue through agreements with both building owners and the power grid operators. Under our agreements with facilities owners, we use electrical and energy related products that help energy consumers control energy use in their buildings. In conjunction with this agreement we are members of the power grid operators and have agreed to provide the grids with energy, capacity, and related ancillary services during specified times and under specified conditions. These transactions are summarized at the end of each monthly period and submitted to the power grids for settlement and approval. While the power grids are our customers, they are primarily a conduit through which these electrical curtailment transactions are processed. The vast majority of our revenue in 2007 was processed through PJM. Our agreement with PJM is an ongoing one as we are members of PJM. These transactions are initiated by building owners, who are our participants. These transactions form the basis for our revenue.

Revenue for the six months ended June 28, 2008 was \$12,442,000 compared to \$5,717,000 for the six months ended June 30, 2007. Transactions by two participants generated 21% and 13% of the Company's total revenue for the six months ended June 28, 2008. Transactions by two participants generated 50% and 17% of the Company's total revenue for the six months ended June 30, 2007.

Cost of Sales . Cost of sales totaled \$4,300,000 (or 84.9% of sales) for the fiscal quarter ended June 28, 2008, compared to \$2,500,000 (or 80.2% of sales) for the same period in the prior year. This increase in costs coincides with the higher levels of sales in the current year quarter. Cost of sales for the six months ended June 28, 2008 was \$10,487,000 compared to \$4,668,000 for the six months ended June 30, 2007. Cost of sales includes the payments to our participants for transactions initiated by them, and various costs required to do business in the grids in which we operate.

Gross Profit. Gross profit for the three months ended June 28, 2008 was \$763,000 (or 15.1%) compared to \$617,000 (or 19.8%) for the same period in 2007. This decrease in gross margin of 4.7% of total sales is due primarily to increases in the percentages paid for transactions in our participant base combined with start up costs associated with entering new grid territories. Gross profit for the six months ended June 28, 2008 was \$1,955,000 (or 15.7%) compared to \$1,049,000 (or 18.3%) for the same period in 2007.

Future gross profit margins will depend on the Company's ability to sign contracts with participants for higher percentages for the duration of the contract term. The Company will record revenue from capacity programs in the third quarter of 2008 at a margin level that when combined with economic transaction revenue are anticipated to result in overall gross margins for the full year of approximately 20%.

Operating Expenses . Operating expenses were \$3,196,000 (63.1% of sales) for the three months ended June 28, 2008, compared to \$1,948,000 (62.5% of sales) for the three months ended June 30, 2007. This increase in expenses is primarily due to added personnel costs in ECI as we continue to invest in the sales force needed to build ECI's revenue base. Included in the current quarter's expense was \$274,000 in non-cash, stock-based compensation expense. Of this amount, \$94,000 of non-cash expense was due to accelerated vesting of incentive stock options for employees of CEI negotiated in the sale of the stock of CEI. Non-cash, stock based compensation expense totaled \$284,000 in the same quarter in 2007.

The percentage of operating expenses to sales for the current quarter was comparable with the prior year's percentage of operating expenses compared to total sales in that quarter. Operating expenses are comprised mainly of payroll costs, facilities rent, outside services, insurance, utilities and depreciation. Personnel costs, which include salary, payroll taxes, fringe benefits, recruiting and training totaled \$1,744,000 for the three months ended June 28, 2008 compared to \$836,000 in the three months ended June 30, 2007.

Operating expenses were \$6,298,000 (50.6% of sales) for the six months ended June 28, 2008, compared to \$3,726,000 (65.2% of sales) for the six months ended June 30, 2007. The increase is due to higher personnel costs associated with building the sales force in ECI. Operating costs were also affected by the non-cash charge for stock-based compensation, which was \$472,000 for the six months ended June 28, 2008, compared to \$484,000 in the six months ended June 30, 2007.

Interest Expense . Net interest income was \$14,000 for the three months ended June 28, 2008, compared to \$5,000 for the three months ended June 30, 2007. The Company's cash levels were higher in the second quarter of 2008 compared to the available cash in the second quarter of 2007. Net interest income was \$20,000 for the six months ended June 28, 2008 compared to \$11,000 for the six months ended June 30, 2007.

Gain / Loss From Discontinued Operations . Discontinued operations represents a loss from the operations of the Christenson Electric electrical construction business. On November 29, 2007, our board of directors signed an agreement to sell all of the shares of our wholly-owned subsidiary Christenson Electric, Inc. to a corporation formed by the management of CEI. The agreement was approved by our shareholders in a vote on March 10, 2008. The closing occurred on April 24, 2008. The Company recorded gains from discontinued operations of \$29,000 and \$263,000 for the three months ended June 28, 2008 and June 30, 2007, respectively. The Company recorded losses from discontinued operations of \$146,000 and \$369,000 for the six months ended June 28, 2008 and June 30, 2007, respectively. On April 24, 2008, the sale of discontinued operations was consummated and the Company recorded a gain on the sale of discontinued operations in the amount of \$135,000.

Income Taxes. There was a small provision for income taxes for the three and six months ended June 28, 2008 due to minimum income taxes due to various state tax agencies in those periods. No federal tax benefit from loss carryback was recorded in either year as there was no income tax paid in the open loss carryback periods. The Company has provided a full valuation allowance on its net deferred tax asset.

Liquidity and Capital Resources

Since inception, the Company has financed its operations and capital expenditures through public and private sales of equity securities, cash from operations, and borrowings under bank lines of credit. At June 28, 2008, the Company had positive working capital of approximately \$230,000 and its primary source of liquidity consisted of cash generated through its private placement and cash generated from operations.

On May 7, 2008 we closed a private placement in which we issued 9,051,310 shares of common stock resulting in aggregate cash proceeds of \$3,512,000 and elimination of accounts payable of \$103,000. In conjunction with this private placement, we also issued 4,525,655 five year warrants exercisable at \$0.60 per share. The proceeds of this financing will be used for general working capital purposes.

Accounts receivable increased to \$1,929,000 at June 28, 2008 from \$1,533,000 at December 29, 2007. The increase is due to the revision in our accounting for reserves for collections of revenues. These receivables were produced by wholesale electric market transactions initiated by electricity consumers with whom we've contracted. The receivables are not net of any allowance for doubtful accounts. Management expects these receivables to increase or decrease in accordance with the increases and decreases in revenue levels achieved in future quarters. To the extent that we expect to record significant revenue from the ILR capacity program in PJM in the third quarter, receivables will increase in accordance with the revenue recognized, but not yet received as of the end of the third quarter. The large majority of our revenue, and therefore cash and receivables, is generated through the PJM Interconnection. PJM serves as the market for electrical transactions in a specific region in the United States. We are members of PJM, and our relationship with this power grid is perpetual. We have little risk, if any, from the concentration of revenue through this power grid as it's a not-for-profit organization that exists to act as the market for electrical transactions.

Property and equipment, net of depreciation increased to \$260,000 at June 28, 2008, compared to \$202,000 at December 29, 2007. This increase was due primarily to the purchase of computer equipment less normal depreciation on fixed assets. The Company does not anticipate spending significant amounts to acquire fixed assets for the foreseeable future.

Accounts payable increased to \$3,657,000 at June 28, 2008 from \$2,976,000 at December 29, 2007. This increase is due to the revision in our accounting for reserves for collections of revenues which precipitated an accrual of participant payments based on the increase in accrued revenue. Payables consist primarily of the payments made to participants in our economic and capacity programs.

The Company had no commitments for capital expenditures in material amounts at June 28, 2008.

As a result of our history of losses and our experiencing difficulty in generating sufficient cash flow to meet our obligations and sustain our operations, our independent registered public accounting firm, in their report included in our December 29, 2007 Form 10-K, have expressed substantial doubt about our ability to continue as going concern.

In prior periods, we generated cash through our discontinued operating subsidiary, Christenson Electric, Inc. This subsidiary also held a \$10 million operating line of credit under which we borrowed funds against eligible accounts receivable. The funds generated from the discontinued operations and their debt facility will no longer be available to the continuing entity. All future cash will need to be generated from the operations of EnergyConnect, and from funds raised through future debt and equity financings should cash generated from operations prove insufficient.

The Company closed a private placement in which we issued 9,051,310 shares of common stock resulting in aggregate cash proceeds of \$3,512,000 and elimination of accounts payable of \$103,000. In conjunction with this private placement, we also issued 4,525,655 five year warrants exercisable at \$0.60 per share. The proceeds of this financing will be used for general working capital purposes.

By adjusting the Company's operations and development to the level of capitalization, management believes it has sufficient capital resources to meet projected cash flow deficits. However, if during that period or thereafter, the Company is not successful in generating sufficient liquidity from operations or in raising sufficient capital resources, on terms acceptable to them, this could have a material adverse effect on the Company's business, results of operations liquidity and financial condition. If operations and cash flows continue to improve through these efforts, management believes that the Company can continue to operate. However, no assurance can be given that management's actions will result in profitable operations or the resolution of its liquidity problems.

Inflation

In the opinion of management, inflation will not have an impact on the Company's financial condition and results of its operations.

Off-Balance Sheet Arrangements

The Company does not maintain off-balance sheet arrangements nor does it participate in any non-exchange traded contracts requiring fair value accounting treatment.

Item 3. Quantitative and Qualitative Disclosures About Market Risks.

The Company does not own or trade any financial instruments about which disclosure of quantitative and qualitative market risks are required to be disclosed.

Item 4. Controls and Procedures

Disclosure controls and procedures are controls and other procedures that are designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by us in the reports that we file under the Exchange Act is accumulated and communicated to our management, including our principal executive and financial officers, as appropriate to allow timely decisions regarding required disclosure.

Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this Quarterly Report, we carried out an evaluation, under the supervision and with the participation of our Chief Executive Officer (CEO) and Chief Financial Officer (CFO), of our disclosure controls and procedures (as defined in Rules 13a-15 (e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”). Based on that evaluation, our CEO and CFO concluded, as of the end of such period, our disclosure controls and procedures were effective in ensuring that the information required to be filed or submitted under the Exchange Act is recorded, processed, summarized and reported as specified in the Securities and Exchange Commission's rules and forms, and accumulated and communicated to our management, including our CEO and CFO, as appropriate to allow timely decisions regarding required disclosure.

The Company's independent auditors have issued an audit report on the effectiveness of the Company's internal control over financial reporting as of December 29, 2007.

Changes in Internal Control over Financial Reporting

Except as described below, there were no changes in internal controls over financial reporting that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially effect, our internal control over financial reporting.

Among the changes in internal controls that have been implemented in the past several periods are:

Revenue recognition

- Criteria and procedures established defining approved customer contracts
- Control function established to review and monitor compliance to new procedures
- Improved document control and file check out procedures
- Procedure established defining consistent percentage completion Gross Margin estimation process

Cash disbursements and liability recognition

- Document control system established and monitored for compliance
- Cut off procedures formalized and consistently applied
- Centralized departmental budgets and accountability established
- Purchasing procedures have been formalized and implementation has been completed
- Procedures instituted to provide for appropriate separation of duties

Other

- Procedures established and personnel assigned to reconcile key accounts on a timely basis
- Control function added to review reconciliations
- Control evidence records and procedures for each job function
- Timely and frequent project reviews
- Timely closing and review of books and records
- Deadlines imposed for period end closings

To correct the material weakness, checklists have been developed delineating tasks, preparation responsibilities, and review responsibilities targeting specific completion dates. The checklists provide evidentiary support of work performed and review. Specific checklists have been developed for non-quarter end months, quarter end months and the annual close. These checklists were developed in 2006 and 2007, and were implemented in the 2008 quarterly close processes and utilized in the preparation of this Quarterly Report.

Our officers have been working with the Board of Directors to address recommendations from our registered independent public accounting firm regarding deficiencies in the disclosure controls and procedures. Management expects that these new procedures will result in disclosure controls and procedures pursuant to Rule 13a-14 of the Exchange Act, which will timely alert the CEO to material information relating to our requirements to be included in our Exchange Act filings.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

The Company is subject to legal proceedings and claims, which arise in the ordinary course of its business. Although occasional adverse decisions or settlements may occur, the Company believes that the final disposition of such matters should not have a material adverse effect on its financial position, results of operations or liquidity.

Item 1A. Risk Factors

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Item 7 (Management's Discussion and Analysis of Financial Condition and Plan of Operation) of our Annual Report on Form 10-K for the year ended December 29, 2007 (the "Annual Report"), which could materially affect our business, financial condition or future results. There have been no material changes to the risk factors disclosed in the Annual Report.

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

On May 7, 2008 we closed a private placement in which we issued 9,051,310 shares of common stock resulting in aggregate cash proceeds of \$3,512,000 and elimination of accounts payable of \$103,000. In conjunction with this private placement, we also issued 4,525,655 five year warrants exercisable at \$0.60 per share. The proceeds of this financing will be used for general working capital purposes.

Item 3. Defaults Upon Senior Securities

None

Item 4. Submission of Matters to a Vote of Security Holders

There were no matters submitted to a vote of security holders during the quarter.

Item 5. Other Information

None

Item 6. Exhibits

(a) The exhibits filed as part of this report are listed below:

Exhibit No.

31.1 Certification of Chief Executive Officer pursuant to Section 302, of the Sarbanes-Oxley Act of 2002.

31.2 Certification of Chief Financial Officer 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.

SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Dated: August 7, 2008

MICROFIELD GROUP, INC.

By: /s/ Rodney M. Boucher
Rodney M. Boucher
Chief Executive Officer
(Principal Executive Officer)

I, Rodney M. Boucher, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Microfield Group, Inc.;
2. Based on my knowledge, this quarterly 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 quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly 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 quarterly report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
 - a) designed such disclosure controls and procedures 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 quarterly report is being prepared;
 - b) 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 period covered by this report based on such evaluation; and
 - c) 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;
5. I have disclosed, based on my most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
 - a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of my most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: August 7, 2008

/s/ Rodney M. Boucher
Rodney M. Boucher
Chief Executive Officer

I, Randall R. Reed, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Microfield Group, Inc.;
2. Based on my knowledge, this quarterly 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 quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly 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 quarterly report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
 - a) designed such disclosure controls and procedures 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 quarterly report is being prepared;
 - b) 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 period covered by this report based on such evaluation; and
 - c) 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;
5. I have disclosed, based on my most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
 - a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of my most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: August 7, 2008

/s/ Randall R. Reed
Randall R. Reed
Chief Financial Officer

**CERTIFICATION PURSUANT TO SECTION 906
OF
THE SARBANES-OXLEY ACT OF 2002**

In connection with the quarterly report on Form 10-Q of Microfield Group, Inc. (the "Company") for the period ended June 28, 2008, as filed with the Securities and Exchange Commission on the date hereof (the "Covered Report"), I, Rodney M. Boucher, the principal executive officer of the Company, pursuant to 18 U.S.C. § 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, hereby certify that:

The Covered Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

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

IN WITNESS WHEREOF, I have executed this certificate as of this 7th day of August 2008.

/s/ Rodney M. Boucher
Rodney M. Boucher
Chief Executive Officer

**CERTIFICATION PURSUANT TO SECTION 906
OF
THE SARBANES-OXLEY ACT OF 2002**

In connection with the quarterly report on Form 10-Q of Microfield Group, Inc. (the "Company") for the period ended June 28, 2008, as filed with the Securities and Exchange Commission on the date hereof (the "Covered Report"), I, Randall R. Reed, the principal financial officer of the Company, pursuant to 18 U.S.C. § 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, hereby certify that:

The Covered Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

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

IN WITNESS WHEREOF, I have executed this certificate as of this 7th day of August 2008.

/s/ Randall R. Reed
Randall R. Reed
Chief Financial Officer
