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U.S. Securities and Exchange Commission

Washington, D. C. 20549

Form 1O-Q

(Mark One)

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

For the quarterly period ended April 2, 2011

OR

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

For the transition period from _____ to _____

Commission file number: 000-26226

ENERGYCONNECT GROUP, INC.

(Exact Name of Registrant as Specified in its Charter)

Oregon **(State or Other Jurisdiction of Incorporation or Organization)**	**93-0935149** **(I.R.S. Employer Identification No.)**
901 Campisi Way, Suite 260, Campbell, CA **(Address of Principal Executive Offices)**	**95008** **(Zip Code)**

(408) 370-3311
(Registrant's Telephone Number, Including Area Code)

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 has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☐ 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 definitions 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	☐ (Do not check if a smaller reporting company)	Smaller reporting company	☒

Indicate by check mark whether the 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 May 10, 2011 was 136,320,765 shares.

ENERGYCONNECT GROUP, INC.

FORM 10-Q

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Item 1. Financial Statements (Unaudited)

ENERGYCONNECT GROUP, INC. AND SUBSIDIARY

CONDENSED CONSOLIDATED BALANCE SHEETS
AS OF APRIL 2, 2011 AND JANUARY 1, 2011

	April 2, 2011 (Unaudited)	January 1, 2011
Current assets:		
Cash and cash equivalents	$ 1,871,749	$ 1,136,074
Accounts receivable, net of zero allowance	11,269,721	12,612,560
Other current assets	653,134	745,383
Total current assets	13,794,604	14,494,017

Property and equipment, net	285,413	188,696
Intangible assets, net (Note 5)	1,099,928	1,159,695
Other assets	77,508	77,508
Total assets	$ 15,257,453	$ 15,919,916
Current liabilities:		
Accounts payable	$ 9,421,076	$ 10,796,332
Line of credit	1,750,000	—
Other current liabilities	344,356	490,653
Total current liabilities	11,515,432	11,286,985
Long-term liabilities:		
Other liabilities	15,637	24,804
Commitments and contingencies (Note 10)		
Shareholders' equity :		
Preferred Stock, no par value, 10,000,000 shares authorized, none outstanding at April 2, 2011 or January 1, 2011	—	—
Common stock, no par value, 225,000,000 shares authorized, 136,320,765 and 135,735,879 shares issued and outstanding at April 2, 2011 and January 1, 2011, respectively (Note 2)	163,124,199	162,911,984
Accumulated deficit	(159,397,815)	(158,303,857)
Total shareholders' equity	3,726,384	4,608,127
Total liabilities and shareholders' equity	$ 15,257,453	$ 15,919,916

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

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ENERGYCONNECT GROUP, INC. AND SUBSIDIARY

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended April 2, 2011	Three Months Ended April 3, 2010
Revenue	$ 5,778,041	$ 7,023,833
Cost of revenue	2,622,369	2,454,591
Gross profit	3,155,672	4,569,242
Operating expenses	4,089,467	2,261,077
Income (loss) from operations	(933,795)	2,308,165
Interest expense, net and other	(136,049)	(226,339)
Net income (loss) before provision for income taxes	(1,069,844)	2,081,826
Provision for income taxes	24,114	—
Net income (loss)	$ (1,093,958)	$ 2,081,826
Net income (loss) per share:		
Basic	$ (0.01)	$ 0.02
Diluted	$ (0.01)	$ 0.02
Shares used in per share calculations:		
Basic	133,598,494	95,749,193
Diluted	133,598,494	133,936,604

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

ENERGYCONNECT GROUP, INC. AND SUBSIDIARY

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Three Months Ended	
	April 2, 2011	April 3, 2010
Cash flows from operating activities:		
Net income (loss)	$(1,093,958)	$ 2,081,826
Reconciling adjustments:		
Depreciation of equipment	30,800	33,483
Amortization of intangible assets	59,767	59,767
Stock-based compensation related to options	94,471	103,703
Stock-based compensation related to restricted stock	116,000	81,000
Amortization of debt discount including beneficial conversion feature	—	15,815
Changes in current assets and liabilities:		
Accounts receivable	1,342,839	(2,931,198)
Other current assets	92,249	(2,096)
Other assets	—	(13,360)
Accounts payable	(1,375,256)	(1,563,993)
Other current liabilities	(155,464)	(117,090)
Net cash used in operating activities	(888,552)	(2,252,143)
Cash flows from investing activities:		
Purchases of property and equipment	(127,517)	(40,294)
Net cash used in investing activities	(127,517)	(40,294)
Cash flows from financing activities:		
Net borrowings against line of credit	1,750,000	—
Proceeds from debt financing, net of repayments	—	1,368,818
Proceeds from exercise of options	1,744	9,167
Collection of notes receivable for exercise of stock options	—	2,850
Net cash provided by financing activities	1,751,744	1,380,835
Net increase (decrease) in cash and cash equivalents	735,675	(911,602)
Cash and cash equivalents, beginning of the period	1,136,074	1,062,306
Cash and cash equivalents, end of the period	$ 1,871,749	$ 150,704
Supplemental disclosures for cash flow information:		
Cash paid during the period for interest	$ 35,243	$ 173,953

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

ENERGYCONNECT GROUP, INC. AND SUBSIDIARY

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
April 2, 2011

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 entries considered necessary for a fair presentation have been included. The results from operations for the three months ended April 2, 2011 are not necessarily indicative of the results that may be expected for the year ending December 31, 2011. The unaudited condensed consolidated financial statements should be read in conjunction with the consolidated January 1, 2011 financial statements and footnotes thereto included in the Company's Form 10-K.

Business and Basis of Presentation

EnergyConnect Group, Inc. is a leading provider of demand response services to the electricity grid. Demand response programs provide grid operators with additional electricity generation capacity by encouraging consumers to curtail their electricity usage. Historically, to provide a reliable supply of electricity and to avoid service disruption, grid operators have increased power generation by building additional power plants and transmission infrastructure. However, an alternative approach to increasing the supply side of electricity is to use demand response programs to reduce overall peak demand or shift load from peak to off-peak times, thereby optimizing the balance of demand and supply and reducing the need for additional power generation capacity. Demand response programs fall into two main groups, programs made for participants to stand by and respond to a grid event initiated by the grid operator and programs that rely on participants curtailing their use of electricity based upon price signals.

Through our proprietary software as a service (SaaS) platform, we allow commercial and industrial consumers of electricity to access demand response programs that are offered by the grid and get paid by agreeing to stand by and curtail based upon a grid event or responding to a price signal. Our participants are commercial and industrial consumers of electricity with whom we contract to identify, develop and if necessary implement curtailment strategies. We enroll our participants in demand response programs operated by grid operators, who pay us for standing by or for reducing load by responding to a price signal. We in turn pass on a portion of these payments to our participants in accordance with their contract with us.

The Company was incorporated in August 1986 as an Oregon Corporation, succeeding operations that began in October 1984. In 2009 we moved our corporate headquarters from Lake Oswego, Oregon, to Campbell, California. The Company's financial statements represent activity in EnergyConnect Group, Inc. and its wholly-owned operating subsidiary, EnergyConnect, Inc (ECI).

Going Concern

The accompanying unaudited condensed consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. As shown in the consolidated financial statements for the year ended January 1, 2011, the Company incurred a net loss of $0.3 million and generated negative cash flow from operations in the amount of $1.1 million. Further, in the three months ended April 2, 2011, the Company incurred a net loss of $1.1 million and generated negative cash flow from operations in the amount of $0.9 million. These factors among others indicate that the Company may need additional funds to continue as a going concern for a reasonable period of time.

The Company's existence is dependent upon management's ability to develop profitable operations and resolve its liquidity problems. Management anticipates the Company will attain profitable status and improve its liquidity through continued growth, distribution and additional equity investment in the Company. The accompanying condensed consolidated financial statements do not include any adjustments that might result should the Company be unable to continue as a going concern.

In February 2009, and as amended in December 2009, the Company entered into a secured convertible debt facility to supplement the Company's cash needs for 2010 and beyond. The net balance outstanding on the facility on September 8, 2010 of $3,307,279 was converted into common stock, which eliminated all of our long term debt. The Company arranged for a new facility on November 5, 2010, which allows for borrowing of up to $4 million, of which $2.25 million was unused as at April 2, 2011.

We believe that revenues generated by operations, combined with our $4 million line of credit, will be adequate to fund our operations until September 2011. Thereafter, we may need to renew the credit facility or obtain alternative financing in order to attain cash flow break even from operations. Financing transactions may include the issuance of equity or debt securities, obtaining credit facilities, or other financing mechanisms. However, the trading price of our common stock, the downturn in the U.S. stock and debt markets and the first priority lien on all of our assets granted to our secured lender could make it more difficult to obtain financing through the issuance of equity or debt securities. Even if we are able to raise the funds required, it is possible that we could incur unexpected costs and expenses, fail to collect significant amounts owed to us, or experience unexpected cash requirements that would force us to seek alternative financing. Further, if we issue additional equity or debt securities, stockholders may experience additional dilution or the new equity securities may have rights, preferences or privileges senior to those of existing holders of our common stock. If additional financing is not available or is not available on acceptable terms, we may have to curtail our operations.

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 the Company is not successful in generating sufficient liquidity from operations or in raising sufficient capital resources on acceptable terms, or is no longer in compliance with the terms of its debt facility, 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.

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 December 31, 2011. The Company's last fiscal year was the 52-week period ended January 1, 2011. The Company's first fiscal quarters in fiscal 2011 and 2010 were the 13-week periods ended April 2, 2011 and April 3, 2010, respectively.

Revenue Recognition

We provide grid operators with products similar to those the grid operator purchases from electric power generators. Our products can be grouped into two main categories: "Capacity" and "Economic".

The Capacity programs are designed to curtail usage during times when an electrical grid approaches its capacity limits of electrical generation just before a blackout or brownout. Participants in the capacity program are generally paid a fee to be on standby to respond on several hours' notice to a request from the grid to reduce electrical usage for a specified period.

The Economic programs differ from the capacity programs as they allow commercial and industrial consumers of electricity to curtail usage at their discretion based on price signals from the grid. Participants in such programs are paid for their discretionary performance rather than being paid to standby and curtail based on a request from the grid.

Under the Capacity programs grid operators pay us an annual fee in weekly installments to stand by and provide demand response resources to the grid when the grid calls an event. We record these payments as revenue over the time when we are required to perform under these capacity programs. For some programs our obligation to perform does not match the period over which we are paid by the grid in which case we recognize revenues over the mandatory performance period.

Under the Economic programs we are paid by the grid for our commercial and industrial participants' ability to reduce electricity usage in response to a price signal from the grid. Through our software we summarize price responsive activity and submit to the grid for payment. At the end of each monthly period the power grid approves the payments, and we in turn recognize revenue based upon the grid approval.

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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 be available 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 are 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. An allowance for doubtful accounts is assessed based on a combination of historical experience, aging analysis and information on specific accounts.

New Accounting Pronouncements

In January 2010, the FASB issued ASC Update No. 2010-06, *Improving Disclosure about Fair Value Measurements* (ASU 2010-06). ASU 2010-06 requires additional disclosures regarding fair value measurements, amends disclosures about post-retirement benefit plan assets and provides clarification regarding the level of disaggregation of fair value disclosures by investment class. ASU 2010-06 is effective for interim and annual reporting periods beginning after December 15, 2009, except for certain Level 3 activity disclosure requirements that became effective for reporting periods beginning after December 15, 2010. We adopted the requirements of this standard related to certain Level 3 activity disclosures effective January 2, 2011, and its adoption did not have a material impact on our consolidated financial position or results of operations.

2. Capital Stock

The Company has authorized 10,000,000 shares of Preferred Stock, no par value. As of April 2, 2011 and January 1, 2011, there were no preferred shares outstanding. The Company has authorized 225,000,000 shares of Common Stock, no par value. The Company had 136,320,765 and 135,735,879 shares of common stock issued and outstanding as of April 2, 2011 and January 1, 2011, respectively. These both include 2,500,000 shares of unregistered restricted stock units issued to officers in November 2010, none of which was vested as of April 2, 2011 (see Note 3). During the three months ended April 2, 2011, the Company issued an aggregate of 550,000 shares of common stock to directors for their services on the Company's board and 34,886 shares of common stock due to the exercise of options (see Note 3). During the three months ended April 3, 2010, the Company issued an aggregate of 450,000 shares of common stock to directors for their services on the Company's board and 183,334 shares of common stock due to the exercise of options (see Note 3).

3. Stock Options and Warrants

Stock Incentive Plan

The Company presently grants awards under the 2004 Stock Incentive Plan, as amended (the "Plan"). The purpose of the Plan is to enable the Company to attract and retain the services of (1) selected employees, officers and directors of the Company or of any subsidiary of the Company and (2) selected nonemployee agents, consultants, advisors, persons involved in the sale or distribution of the Company's products and independent contractors of the Company or any subsidiary. The Plan is administered by the Compensation Committee of the Board of Directors, who may grant various awards, including Incentive Stock Options ("ISOs"), Non-Statutory Stock Options ("NSOs"), Stock Appreciation Rights and Restricted Shares.

The Company has issued both options and restricted stock under the Plan. Restricted stock grants afford the recipient the opportunity to receive shares of common stock, subject to certain terms, whereas options give them the right to purchase common stock at a set price. The Company's options generally have vesting restrictions that are eliminated over a four-year period, although vesting may be over a shorter period, or may occur on the grant date, depending on the terms of each individual award.

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A summary of stock option and restricted stock transactions under Stock Incentive Plans in the three months ended April 2, 2011 is as follows:

		Stock Options		Restricted Stock	
	Shares Available for Grant	Number of Options Outstanding	Weighted Average Exercise Price	Number of Shares Outstanding	Weighted Average Grant-Date Fair Value
Balance at January 1, 2011	2,163,985	12,770,251	$ 0.20	—	$ —
Granted	(180,000)	180,000	$ 0.14	—	$ —
Granted – restricted stock	(550,000)	—	$ —	550,000	$ 0.12
Exercised	—	(34,886)	$ 0.05	—	$ —
Vested – restricted stock	—	—	$ —	(550,000)	$ 0.12
Cancelled or expired	654,913	(654,913)	$ 0.32	—	$ —
Balance at April 2, 2011	2,088,898	12,260,452	$ 0.19	—	$ —

The Company received $1,744 for the 34,886 options exercised during the three months ended April 2, 2011, which had an intrinsic value of $2,791. The Company received $9,167 for the 183,334 options exercised during the three months ended April 3, 2010, which had an intrinsic value of $7,333.

The following table summarizes information concerning options outstanding and exercisable as of April 2, 2011, with the first line showing options that were in-the-money:

	Options Outstanding			Options Exercisable		
Range of Exercise Prices	Number Outstanding as of April 2, 2011	Weighted Average Remaining Contractual Life (in Years)	Weighted Average Exercise Price	Number Exercisable as of April 2, 2011	Weighted Average Remaining Contractual Life (in Years)	Weighted Average Exercise Price
$0.050 - $0.209	10,776,510	6.38	$ 0.10	4,819,786	5.68	$ 0.09
$0.210 - $1.830	1,483,942	1.24	$ 0.85	1,342,457	1.19	$ 0.84
	12,260,452	5.76	$ 0.19	6,162,243	4.70	$ 0.25

The aggregate intrinsic value of options outstanding and exercisable at April 2, 2011 was $1,136,522 and $574,049, respectively. Aggregate intrinsic value is the total pretax amount (i.e., the difference between the Company's stock price and the exercise price) that would have been received by the option holders had all their in-the-money options been exercised.

The fair value of stock options vested in the three months ended April 2, 2011 and April 3, 2010 was $99,008 and $259,297, respectively. The weighted average grant date fair value of all options granted in the three months ended April 2, 2011 and April 3, 2010 was $0.09 and $0.12, respectively, computed using the Black-Scholes pricing model and the following assumptions:

	2011	2010
Risk-free interest rate	2.04%	2.60%
Expected dividend yield	0%	0%
Expected term	5 years	5 years
Expected volatility	82.02%	83.52%

The amounts expensed for stock-based compensation related to options totaled $94,471 and $103,703 for the three months ended April 2, 2011 and April 3, 2010, respectively. Amounts expensed for stock-based compensation related to restricted stock awards totaled $116,000 and $81,000 for the three months ended April 2, 2011 and April 3, 2010, respectively. $50,000 of the expense in the three months ended April 2, 2011 relates to awards totaling 2,500,000 unregistered shares to five officers of the Company on November 10, 2010, which will vest 25% after six months, then 12.5% at the end of each three month period, assuming continuous

employment, so these shares will be fully vested after two years. The remaining expense of $66,000 in the three months ended April 2, 2011, and all of the $81,000 expense for the three months ended April 3, 2010, relates to awards to independent directors of the Company in connection with their services as directors. These awards granted five directors a total of 550,000 shares in the three months ended April 2, 2011, and four directors a total of 450,000 shares of the Company's common stock in the three months ended April 3, 2010 (see Note 2). These shares are fully vested on the award date, but are restricted from transfer, except as permitted for estate planning purposes, until January 15 of the year following the award.

At April 2, 2011, the total stock-based compensation cost not yet recognized was $917,592. This cost is expected to be recognized over an estimated weighted average amortization period of 1.99 years. No amounts related to stock-based compensation costs have been capitalized. The tax benefit and the resulting effect on cash flows from operating and financing activities related to stock-based compensation costs were not recognized as the Company currently provides a full valuation allowance for all of its deferred taxes.

Common Stock Warrants

The Company has various warrants to purchase shares of its common stock outstanding, which were issued in conjunction with private placements, acquisitions and debt issuance, or in exchange for services received. All warrants contain standard anti-dilution clauses in the event of recapitalization, stock splits or combinations, merger or reorganization, dividends or distributions and similar equity adjustments, but none of the warrants presently outstanding contain anti-dilution provisions that would prevent them from being considered indexed to the Company's own stock, so they are all accounted for within Stockholders' Equity.

A summary of changes in the number of outstanding common stock warrants in the three months ended April 2, 2011 is as follows:

Balance on January 1, 2011	During the Three Months Ended April 2, 2011			Balance on April 2, 2011	Exercise Price	Expiration Date
	Granted	Exercised	Forfeited			
3,750,000	—	—	—	3,750,000	$ 0.15	November 2017
100,000	—	—	—	100,000	$ 0.40	May 2013
4,565,874	—	—	—	4,565,874	$ 0.60	May 2013
5,625,000	—	—	—	5,625,000	$ 3.00	June 2011
14,040,874	—	—	—	14,040,874		

The 3,750,000 warrants with an exercise price of $0.15, expiring in November 2017, were issued in conjunction with obtaining a line of credit in 2010 (see Note 4).

4. Debt

Bank Line of Credit

On November 5, 2010, we entered into a $4,000,000 revolving line of credit with Silicon Valley Bank and Partners For Growth III, L.P. (collectively "SVB"). Borrowings under the agreement are at an interest rate of 12.5%. The facility matures on September 30, 2011. We granted the lender a first priority security interest in all of our assets. We issued a total of 3.75 million warrants to SVB in connection with the agreement, to which we allocated a total fair value of $365,625. This sum was recorded within current assets, and is being amortized as interest expense on a straight line basis over the term of the credit line.

As at April 2, 2011, the Company had borrowed $1,750,000 against the line. As at January 1, 2011, the Company had not yet borrowed against the line. The Company is in compliance with all covenants under this facility.

Debt Facility

On February 26, 2009, the Company entered into a $5 million loan agreement with Aequitas Commercial Finance, LLC (“Aequitas”, see also Note 9). On December 23, 2009, the Company entered into an amendment of the convertible debt agreement. This loan agreement, as amended, provided us with a debt facility that enabled us to borrow money in a maximum principal amount not to exceed $5 million. The interest rate for funds borrowed by us in the first 12 month term was 23% payable monthly in arrears, with an additional 7% deferred interest per annum. For the balance of the term, and for all amounts borrowed under the

amendment, the interest rate was 22% payable monthly in arrears, with an additional 3% deferred interest per annum. The accrued deferred interest at 7% was added to the current principal balance of the loan at the end of the first twelve-month term. The accrued deferred interest at 3% was added to the current principal balance of the loan prior to conversion. The lender was granted a first priority security interest in all of our assets, and had the right to convert up to 100% of unpaid principal and interest into shares of our common stock at an exercise price of $0.0906 per share, either on the planned maturity date of February 24, 2012, or to the extent the Company gave notice of its intent to pay down the principal balance outstanding.

On September 8, 2010, following notice that the Company intended to repay the balance of the facility, the lender opted to convert all but $1 of the remaining principal plus accrued interest, totaling $3,307,280, into 36,504,180 shares of common stock. The Company repaid the remaining $1 on September 24, 2010. We remained current with our obligations under this agreement, and were in compliance with all covenants, up to the date of conversion.

Interest paid to Aequitas totaled $173,953 for the three months ended April 3, 2010, and a further $25,309 was expensed as deferred interest. In addition, the Company paid Aequitas fees of $3,000 per month in this period. We also recorded non-cash interest expense in the amount of $15,815 for amortization of the convertible note debt discount attributed to the beneficial conversion feature and in the three months ended April 3, 2010.

5. Intangible Assets

Intangible assets currently consist of the following:

	April 2, 2011	January 1, 2011
Developed technology	$ 2,394,873	$ 2,394,873
Less: accumulated amortization	(1,294,945)	(1,235,178)
Net Intangible Assets	$ 1,099,928	$ 1,159,695

Amortization of intangible assets included as a charge to income was $59,767 for each of the three month periods ended April 2, 2011 and April 3, 2010**.**

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

Year	Amortization Expense
Twelve months ended March 2012	$ 239,067
Twelve months ended March 2013	239,067
Twelve months ended March 2014	239,067
Twelve months ended March 2015	239,067
Twelve months ended March 2016 and beyond	143,660
Total	$1,099,928

6. Business Concentrations

We record revenue and therefore accounts receivable 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 revenues each year are processed through PJM, which 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. Transactions are initiated by building owners, who are our participants. These transactions form the basis for our revenue.

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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 April 2, 2011, and April 3, 2010, sales to one customer, PJM, accounted for $5,648,000, or 98% of revenue, and $6,831,000, or 97% of revenue, respectively. PJM pays us to provide electrical capacity, which we provide either by selling our obligation at auction, or via a number of transactions with participants using our software. Substantially all of our revenue in the three months ended April 2, 2011, and April 3, 2010, was derived from the sale of our obligations at auction. PJM accounted for 98.4% and 98.0% of accounts receivable at April 2, 2011, and January 1, 2011, respectively.

7. Net Income (loss) per Share

The following table presents the calculation of basic and diluted net income (loss) per share:

	Three Months Ended	
	April 2, 2011	April 3, 2010
Net income (loss)	$ (1,093,958)	$ 2,081,826
Interest charges applicable to convertible debt	—	213,378
Net income (loss) used for net income per share—diluted calculation	$ (1,093,958)	$ 2,295,204
Weighted-average shares—basic	133,598,494	95,749,193
Common share equivalents from exercise of stock options	—	2,443,968
Potential common shares from conversion of debt	—	35,743,443
Weighted-average shares—diluted	133,598,494	133,936,604
Net income per share—basic	$ (0.01)	$ 0.02
Net income per share—diluted	$ (0.01)	$ 0.02

Interest charges applicable to convertible debt and the weighted average shares that would have been issued on conversion were reflected in the calculation of diluted earnings per share (EPS) in the three months ended April 3, 2010, as the effect was dilutive. The common share equivalents that would have been issued on conversion of in-the-money options were also reflected in the calculation of diluted EPS in the three months ended April 3, 2010, as the effect was dilutive. The common share equivalents that would have been issued on the vesting of restricted stock units and conversion of in-the-money options and warrants were excluded from the calculation of diluted EPS in the three months ended April 2, 2011, as the effect was anti-dilutive due to the net loss.

The following potential common shares arising from unvested restricted stock, stock options and warrants were excluded from the computation of diluted net loss per share attributable to holders of common stock as they had antidilutive effects for the periods indicated:

	Three Months Ended	
	April 2, 2011	April 3, 2010
Shares issuable upon vesting of restricted stock units	2,500,000	—
Shares issuable upon exercise of outstanding options	13,263,762	7,391,612
Shares issuable upon exercise of outstanding warrants	14,040,874	33,055,055
Total common share equivalents excluded from denominator for diluted EPS computation	29,804,636	40,446,667

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Options, unvested shares, warrants and similar equity instruments granted by the Company, as well as convertible debt, are treated as potential common shares outstanding in computing diluted earnings per share. Diluted shares outstanding include the dilutive effect of in-the-money options and warrants, which are calculated based on the average share price for each fiscal period using the treasury stock method. Under the treasury stock method, the amount the employee must pay for exercising stock options, the amount of compensation cost for future service that the Company has not yet recognized, and the amount of tax benefits that would be recorded in additional paid-in capital when the award becomes deductible are assumed to be used to repurchase shares.

8. Fair Value Measurement

Fair value measurements are determined under a three-level hierarchy for fair value measurements that prioritizes the inputs to valuation techniques used to measure fair value, distinguishing between market participant assumptions developed based on market data obtained from sources independent of the reporting entity ("observable inputs") and the reporting entity's own assumptions about market participant assumptions developed based on the best information available in the circumstances ("unobservable inputs").

Fair value is the price that would be received to sell an asset or would be paid to transfer a liability (i.e., the "exit price") in an orderly transaction between market participants at the measurement date. In determining fair value, we primarily use prices and other relevant information generated by market transactions involving identical or comparable assets ("market approach"). We also consider the impact of a significant decrease in volume and level of activity for an asset or liability when compared with normal activity to identify transactions that are not orderly.

The highest priority is given to unadjusted quoted prices in active markets for identical assets (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). Securities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

The three hierarchy levels are defined as follows:

Level 1 inputs are observable inputs and use quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date and are deemed to be most reliable measure of fair value.

Level 2 inputs are observable inputs and reflect assumptions that market participants would use in pricing the asset or liability developed based on market data obtained from sources independent of the reporting entity. Level 2 inputs include 1) quoted prices for similar assets or liabilities in active markets, 2) quoted prices for identical or similar assets or liabilities in markets that are not active, 3) observable inputs such as interest rates and yield curves observable at commonly quoted intervals, volatilities, prepayment speeds, credit risks, default rates, and 4) market-corroborated inputs.

Level 3 inputs are unobservable inputs and reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability based on the best information available under the circumstances.

The carrying value of the Company's cash and cash equivalents, accounts receivable, accounts payable and other current assets and liabilities approximate fair value because of their short-term maturity. The carrying value of the Company's long term debt approximates fair value.

9. Related party and related party transactions

The Company had a convertible debt facility with Aequitas Commercial Finance LLC, an affiliate of Aequitas Management LLC (Aequitas) which, with its associates, had beneficial ownership of approximately 30% of the Company as of April 2, 2011, following conversion of principal outstanding on the debt facility into 36,504,180 shares of our common stock. As at April 3, 2010, Aequitas affiliates owned approximately 10% of the Company's stock. One of the Company's directors (until his resignation, effective September 17, 2010), William McCormick, is also an advisor of Aequitas. Interest paid to Aequitas totaled $173,953 for the three months ended April 3, 2010. These interest payments exclude $168,818 in deferred interest charges that were added to the principal balance of the note in February 2010 and thus paid in common stock as part of the conversion on September 8, 2010. In addition, the Company paid Aequitas fees of $3,000 per month in this period. See also Note 4 above.

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10. Contingencies

On March 2, 2011, we entered into an Agreement and Plan of Merger with Johnson Controls Holding Company, Inc., a Delaware corporation, ("JCI"), and Eureka, Inc., an Oregon corporation and wholly owned subsidiary of JCI ("Merger Sub"), pursuant to which Merger Sub will merge with and into us, with us being the surviving corporation and a wholly owned subsidiary of JCI (the "Merger"). We currently anticipate the Merger to close some time during the third quarter of 2011.

EnergyConnect, its board of directors, JCI Holding, and Merger Sub are named as defendants in four putative class action lawsuits brought by alleged EnergyConnect shareholders challenging EnergyConnect's proposed merger with JCI Holding. A stipulation was entered causing the lawsuits to be consolidated, and an amended complaint was filed alleging, among other things, that each member of the EnergyConnect board of directors breached their fiduciary duties to EnergyConnect shareholders by authorizing the sale of EnergyConnect to JCI Holding for consideration that does not maximize value to EnergyConnect shareholders, engineering the transaction to benefit themselves without regard to EnergyConnect's shareholders, and issuing a preliminary proxy statement that fails to disclose material information sufficient for EnergyConnect shareholders to analyze the fairness of the proposed merger. The amended complaint also alleges that EnergyConnect, JCI Holding and Merger Sub aided and abetted the breaches of fiduciary duty purportedly committed by members of the EnergyConnect board of directors. The shareholder action seeks equitable relief, including an injunction against consummating the merger on the agreed-upon terms.

On May 2, 2011, counsel for the parties in the consolidated action entered into a memorandum of understanding in which they agreed on the terms of a settlement, which would include the dismissal with prejudice of all claims against all defendants. The proposed settlement is conditioned upon, among other things, the execution of an appropriate stipulation of settlement and final approval of the proposed settlement by the court. In connection with the settlement and as provided in the memorandum of understanding, the parties contemplate that plaintiffs' counsel will seek an award of attorneys' fees and expenses as part of the settlement. There can be no assurance that the parties will ultimately enter into a stipulation of settlement or that the court will approve the settlement even if the parties were to enter into such stipulation. In such event, the proposed settlement as contemplated by the memorandum of understanding may be terminated. The settlement will not affect the amount of the merger consideration that EnergyConnect stockholders are entitled to receive in the merger. The company denies and continues to deny all liability with respect to the facts and claims alleged in the lawsuits.

As of April 2, 2011, the Company has accrued its own legal costs, including an amount equal to its deductible under its applicable D&O insurance policy.

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 EnergyConnect 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 January 2, 2010.

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 Securities and Exchange Commission.

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

EnergyConnect Group, Inc. is a leading provider of demand response services to the electricity grid. Demand response programs provide grid operators with additional electricity generation capacity by encouraging consumers to curtail their electricity usage. Historically, to provide a reliable supply of electricity and to avoid service disruption, grid operators have increased power generation by building additional power plants and transmission infrastructure. However, an alternative approach to increasing the supply side of electricity is to use demand response programs to reduce overall peak demand or shift load from peak to off-peak times, thereby optimizing the balance of demand and supply and reducing the need for additional power generation capacity. Demand response programs fall into two main groups: programs made for participants to stand by and respond to a grid event initiated by the grid operator, and programs that rely on participants curtailing their use of electricity based upon price signals.

Through our proprietary software as a service (SaaS) platform, we allow commercial and industrial consumers of electricity to access demand response programs that are offered by the grid and get paid for agreeing to stand by and curtail based upon a grid event or responding to a price signal. Our participants are commercial and industrial consumers of electricity with whom we contract to identify, develop and if necessary implement curtailment strategies. We enroll our participants in demand response programs operated by grid operators, who pay us for standing by or for reducing load by responding to a price signal. We make payments to our participants based on the terms and conditions of their contract with us.

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

Description of Market

In a wholesale electricity market, such as the energy market operated by Pennsylvania, New Jersey, Maryland Interconnection, LLC ("PJM"), the market operator is responsible for buying, selling and delivering wholesale electricity thereby balancing the needs of suppliers, wholesale customers and other market participants. These markets operate like a stock exchange, with the price of electricity resulting from matching supply, for example power supplied by the generators, with demand, consisting of the retail, industrial and commercial consumers of electricity. The PJM market uses locational marginal pricing ("LMP") that reflects the value of electricity at a specific time and location. If the lowest-priced electricity can reach all locations, prices are the same across the entire grid. If there is congestion and energy cannot flow to all locations, more expensive electricity is ordered to meet that

demand. As a result, the LMP is higher in those locations of constraint. Wholesale electricity prices fluctuate based on five-minute intervals across the grid, however most consumers of electricity pay rates that are based on an average price of electricity that includes a hedge premium. This means that most consumers do not see wholesale prices and have no way of reacting to them. We have developed and deployed a software solution that allows our participants to transact in the wholesale market.

The energy market consists of Day-Ahead and Real-Time, or Day-Of, markets. The Day-Ahead market is a forward market in which hourly LMPs are calculated for the next operating day based on generation offers, demand bids and scheduled bilateral transactions. The Real-Time market is a spot market in which LMPs are calculated at five-minute intervals based on actual grid operating conditions.

Real-Time Response

Our participants reduce their usage of electricity based on a pre-determined curtailment strategy they have developed and estimated prices for wholesale electricity that we provide. EnergyConnect is paid for the actual measured reduction in electricity usage expressed either in kilowatts per hour (KWh) or megawatts per hour (MWh) at the actual LMP less the participant's retail rate. We in turn pay our participants a percentage of the payment we receive based upon our individual contracts with them.

Real-Time Dispatch

Our participants reduce their usage of electricity in response to requests by the grid operator. The grid operator notifies us of an emergency event, we in turn notify our participants of their need to reduce demand. EnergyConnect is paid for our participants standing by to respond to the grid operator's request to curtail. We in turn pay our participants a percentage of the payment we receive based upon our individual contracts with them.

Day-Ahead

Some grid operators establish Day-Ahead economic markets with forward hourly electricity prices. The price certainty of the Day-Ahead market provides a known return for a specific curtailment strategy, for example, by pre-cooling buildings in early morning hours to create subsequent reductions of energy use in the peak afternoon hours. We provide our participants with all the information and support required to participate in the Day-Ahead electrical energy market. EnergyConnect is paid for the reduction in usage. Reductions in excess of the amount committed to the Day-Ahead market are generally paid at the prevailing Real-Time rate. Under-delivery generally must be made up by our participants buying energy at the Real-Time rate.

Critical Accounting Policies

The discussion and analysis of financial condition and results of operations is based upon our condensed 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 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 disclosures 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 provide grid operators with products similar to those the grid operator purchases from electric power generators. Our products can be grouped into two main categories: "Capacity" and "Economic".

The Capacity programs are designed to curtail usage during times when an electrical grid approaches its capacity limits of electrical generation just before a blackout or brownout. Participants in the capacity program are generally paid a fee to be on standby to respond on several hours' notice to a request from the grid to reduce electrical usage for a specified period.

The Economic programs differ from the capacity programs as they allow commercial and industrial consumers of electricity to curtail usage at their discretion based on price signals from the grid. Participants in such programs are paid for their discretionary performance rather than being paid to standby and curtail based on a request from the grid.

Under the Capacity programs grid operators pay us an annual fee in weekly installments to stand by and provide demand response resources to the grid when the grid calls an event. We record these payments as revenue over the time when we are required to perform under these capacity programs. For some programs our obligation to perform does not match the period over which we are paid by the grid in which case we recognize revenues over the mandatory performance period.

Under the Economic programs we are paid by the grid for our commercial and industrial participants' ability to reduce electricity usage in response to a price signal from the grid. Through our software we summarize price responsive activity and submit to the grid for payment. At the end of each monthly period the power grid approves the payments, and, we in turn recognize revenue based upon the grid approval.

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 be available 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 are 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. An allowance for doubtful accounts is assessed based on a combination of historical experience, aging analysis and information on specific accounts.

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.

Impairment of Intangible and Long-Lived Assets

In accordance with ASC 360, *Accounting for the Impairment or Disposal of Long-Lived Assets*, we assess the impairment of long-lived assets whenever events or changes in circumstances indicate that their carrying value may not be recoverable from the estimated future cash flows expected to result from their use and eventual disposition. Our long-lived assets subject to this evaluation include property and equipment and amortizable intangible assets. If our estimate of future undiscounted net cash flows is insufficient to recover the carrying value of the assets, we will record an impairment loss in the amount by which the carrying value of the assets exceeds the fair value. If assets are determined to be recoverable but the useful lives are shorter than originally estimated, we depreciate or amortize the net book value of the asset over the newly determined remaining useful lives.

Stock-Based Compensation

We account for stock-based compensation under the provisions of ASC 718-10 and ASC 505-50, "Stock Compensation and Equity Based

Payments to Non-Employees”. ASC 718 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.

The weighted average grant date fair value of all options granted in the three months ended April 2, 2011 and April 3, 2010 was $0.09 and $0.12, respectively, computed using the Black-Scholes pricing model and the following assumptions:

	2011	2010
Risk-free interest rate	2.04%	2.60%
Expected dividend yield	0%	0%
Expected term	5 years	5 years
Expected volatility	82.02%	83.52%

The amounts expensed for stock-based compensation related to options totaled $94,471 and $103,703 for the three months ended April 2, 2011 and April 3, 2010, respectively.

Results of Operations

The financial information presented for the three months ended April 2, 2011 and April 3, 2010 represents activity in EnergyConnect Group, Inc. and its wholly-owned operating subsidiary, EnergyConnect, Inc (ECI).

Revenue. The Company generates revenue mainly from demand response transactions regulated by a Federal Energy Regulatory Commission (FERC) tariff. These transactions include economic or price-based programs and capacity programs. Economic or price-based programs entail voluntary, daily opportunities to enter into transactions in the energy markets based on our participants’ responses to fluctuations in hourly energy prices.

Capacity programs allow for payments to partners such as ECI based on energy availability and curtailment when required by an electric grid to stabilize the supply and demand of electricity on the grid. Also included in the FERC tariff are rules under which we recognize revenue in capacity-based energy programs.

The FERC tariff also allows for other revenue opportunities in helping to meet various needs of electric grids. We recognize revenue from these programs ratably over the months during which our response is required.

Revenue for the three months ended April 2, 2011 was $5,778,000 compared to $7,024,000 for the three months ended April 3, 2010, a decrease of 17.7%. This decrease in year-over-year quarterly revenue in ECI is due primarily to a decrease in PJM capacity transaction revenues from $6,578,000 to $5,449,000, a decrease of 17.2%.

We have contracted with PJM sufficient MWs to support growth in our capacity offerings for the next two years. These commitments are positions that we have entered in at auctions PJM holds. We also have contracts with our participants which are multi-year agreements for their participation in capacity markets where both the pricing and the participant’s commitment are known.

Gross Profit. Gross profit for the three months ended April 2, 2011 was $3,156,000 (or 54.6% of revenue) compared to $4,569,000 (or 65.0% of revenue) for the same period in 2010, a decrease of 30.9%. This decrease in gross profit is due to the reduction in revenue from capacity transactions from $6,578,000 to $5,449,000, and a decline in the gross margin from these transactions from 70.7% to 56.9%.

Gross profit comprises revenue, less the related amounts due to our participants for capacity commitments made by them, and for transactions initiated by them, and various costs required to do business in the grids in which we operate. Future gross profit margins will depend on the Company’s ability to sign contracts with participants for appropriate percentages for the duration of the contract term.

Operating Expenses. Operating expenses were $4,090,000 (70.8% of revenue) for the three months ended April 2, 2011, compared to $2,261,000 (32.2% of revenue) for the three months ended April 3, 2010, an increase of 80.9%. This increase in expenses is primarily due to increases of $991,000 in legal and professional fees, and $787,000 in personnel costs, including salaries and non-cash stock-based compensation. The increase in these costs is due to expenses directly related to the proposed merger with Johnson Controls (see Note 10 to the Condensed Consolidated Financial Statements in Part I, Item 1).

Interest expense, net and other. Net interest expense was $136,000 for the three months ended April 2, 2011, compared to $226,000 for the three months ended April 3, 2010. Net interest expense for the three months ended April 2, 2011, comprised mainly interest on borrowings against the Company’s line of credit, plus a non-cash charge of approximately $34,000 per month relating to amortization of the expense attributed to warrants issued to obtain this line through September 30, 2011. Net interest expense for the three months ended April 3, 2010, comprised mainly interest expense incurred under the Company's debt facility and amortization of debt discount associated with the beneficial conversion feature of the debt facility. Net interest expense decreased in 2011 due to lower average aggregate borrowings at a lower interest rate and the absence of debt discount amortization, offset by the warrant expense amortization.

Taxation. We have recorded an income tax charge of $24,000 for the three months ended April 2, 2011, all relating to state tax charges, by applying our estimated tax rate for the full year to the loss recorded year-to-date. We have provided a full valuation allowance on our net deferred tax asset.

Liquidity and Capital Resources

Since inception, we have financed our operations and capital expenditures through public and private sales of equity securities, cash from operations, and borrowings under operating and revolving lines of credit.

At April 2, 2011, the Company had positive working capital of approximately $2,280,000, compared to approximately $3,207,000 at January 1, 2011. The decrease is primarily due to borrowings against the line of credit, which is renewable on September 30, 2011, and thus classified as a current liability. The Company derived significant liquidity in the year ended January 1, 2011, as the balance on its convertible note was repaid in common stock. At April 2, 2011, $2,250,000 of the total available on our line of credit remained unused.

Accounts receivable decreased to $11,270,000 at April 2, 2011, from $12,613,000 at January 1, 2011. The decrease was primarily due to the receipt of funds relating to the 2010-2011 PJM annual capacity program, offset by billings for the capacity transactions in the first quarter of 2011. We receive funds from the PJM annual capacity program on a weekly basis starting each June. Our remaining receivables will increase and decrease in accordance with the revenue recognized in each quarter. The large majority of our revenue, and therefore cash and receivables, is generated through PJM, which 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 do have a concentration of receivables from PJM, however, we do not believe there is a significant risk arising from this concentration.

Property and equipment, net of depreciation increased to $285,000 at April 2, 2011, compared to $189,000 at January 1, 2011. This increase was due to approximately $127,000 in additions to fixed assets offset by normal depreciation charges of $31,000 during the period. We may capitalize purchased software in the coming quarters, but do not anticipate spending significant amounts to acquire other fixed assets for the foreseeable future.

Accounts payable decreased to $9,421,000 at April 2, 2011, from $10,796,000 at January 1, 2011. The decrease was primarily due to the payment of funds relating to the 2010-2011 PJM annual capacity program, offset by sums payable participants for the capacity transactions in the first quarter of 2011. At April 2, 2011 and January 1, 2011, other than normal obligations to vendors for operating expenses, accounts payable consists primarily of payment obligations to participants in our capacity programs, not currently due, and to normal monthly obligations in our economic programs.

The Company had no commitments for capital expenditures in material amounts at April 2, 2011.

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 its report dated April 1, 2011, included in our January 1, 2011 Form 10-K, referred to substantial doubt about our ability to continue as going concern.

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We believe that revenues generated by operations, combined with our $4 million line of credit, will be adequate to fund our operations until September 2011. Thereafter, we may need to renew the credit facility or obtain alternative financing in order to attain cash flow break even from operations. Financing transactions may include the issuance of equity or debt securities, obtaining credit facilities, or other financing mechanisms. However, the trading price of our common stock, the downturn in the U.S. stock and debt markets and the first priority lien on all of our assets granted to our secured lender could make it more difficult to obtain financing through the issuance of equity or debt securities. Even if we are able to raise the funds required, it is possible that we could incur unexpected costs and expenses, fail to collect significant amounts owed to us, or experience unexpected cash requirements that would force us to seek alternative financing. Further, if we issue additional equity or debt securities, stockholders may experience additional dilution or the new equity securities may have rights, preferences or privileges senior to those of existing holders of our common stock. If additional financing is not available or is not available on acceptable terms, we may have to curtail our operations.

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 the Company is not successful in generating sufficient liquidity from operations or in raising sufficient capital resources on acceptable terms, or is no longer in compliance with the terms of its debt facility, 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.

Recent regulatory developments may require us to post letters of credit or security deposits in order to participate in key demand response programs. Given our limited access to capital, we may not have sufficient funds to meet these credit requirements that may in turn preclude us from participating in these markets, adversely affecting our ability to create shareholder value as a standalone company.

Concentrations

We record revenue and therefore accounts receivable 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 revenues each year are processed through PJM, which 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.

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 April 2, 2011, and April 3, 2010, sales to one customer, PJM, accounted for $5,648,000, or 98% of revenue, and $6,831,000, or 97% of revenue, respectively. PJM pays us to provide electrical capacity, which we provide either by selling our obligation at auction, or via a number of transactions with participants using our software. Substantially all of our revenue in the three months ended April 2, 2011, and April 3, 2010, was derived from the sale of our obligations at auction. PJM accounted for 98.4% and 98.0% of accounts receivable at April 2, 2011, and January 1, 2011, respectively.

Recent Accounting Pronouncements

See the "New Accounting Pronouncements" in Note 1 to the Condensed Consolidated Financial Statements in Part I, Item 1 for a full description of new accounting standards, including the respective expected dates of adoption, none of which have had, or are expected to have, a material impact on our results of operations or financial condition.

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 Securities Exchange Act of 1934, as amended (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 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.

Changes in Internal Control over Financial Reporting

There were no changes in internal controls over financial reporting that occurred during the period covered by this report that have affected, or are reasonably likely to affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

From time to time, we may become involved in various lawsuits and legal proceedings which arise in the ordinary course of business. Litigation is subject to inherent uncertainties, and an adverse result in these or other matters may arise from time to time that may harm our business.

EnergyConnect, its board of directors, JCI Holding, and Merger Sub are named as defendants in four putative class action lawsuits brought by alleged EnergyConnect shareholders challenging EnergyConnect's proposed merger with JCI Holding. The shareholder actions were filed in the Superior Court of California, Santa Clara County. The actions are called Jeff Putney v. EnergyConnect Group, Inc., et al., filed March 9, 2011, Case No. 111-CV196058, Wanda A. Huber v. EnergyConnect Group, Inc., et al., filed March 14, 2011, Case No. 111-CV196265, David Pierce v. Energy Connect Group, Inc., et al., filed March 25, 2011, Case No. 111-CV197445, and Bruce B. Barber v. EnergyConnect Group, Inc., et al., filed April 14, 2011, Case No. 111-CV198920. A stipulation was entered causing the lawsuits to be consolidated. On April 12, 2011, a consolidated amended complaint was filed, alleging, among other things, that each member of the EnergyConnect board of directors breached his or her fiduciary duties to EnergyConnect shareholders by authorizing the sale of EnergyConnect to JCI Holding for consideration that does not maximize value to EnergyConnect shareholders, engineering the transaction to benefit themselves without regard to EnergyConnect's shareholders, and issuing a preliminary proxy statement that fails to disclose material information sufficient for EnergyConnect shareholders to analyze the fairness of the proposed merger. The amended complaint also alleges that EnergyConnect, JCI Holding and Merger Sub aided and abetted the breaches of fiduciary duty allegedly committed by the members of the EnergyConnect board of directors. The shareholder action seeks equitable relief, including an injunction against consummating the merger on the agreed-upon terms.

On May 2, 2011, counsel for the parties in the consolidated action entered into a memorandum of understanding in which they agreed on the terms of a settlement, which would include the dismissal with prejudice of all claims against all defendants. The proposed settlement is conditioned upon, among other things, the execution of an appropriate stipulation of settlement and final approval of the proposed settlement by the court. In connection with the settlement and as provided in the memorandum of understanding, the parties contemplate that plaintiffs' counsel will seek an award of attorneys' fees and expenses as part of the settlement. There can be no assurance that the parties will ultimately enter into a stipulation of settlement or that the court will approve the settlement even if the parties were to enter into such stipulation. In such event, the proposed settlement as contemplated by the memorandum of understanding may be terminated. The settlement will not affect the amount of the merger consideration that EnergyConnect stockholders are entitled to receive in the merger. The company denies and continues to deny all liability with respect to the facts and claims alleged in the lawsuits.

As of April 2, 2011, the Company has accrued its own legal costs, including an amount equal to its deductible under its applicable D&O insurance policy.

Item 1A. Risk Factors

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, Item 1A "Risk Factors" in our Annual Report on Form 10-K for the year ended January 1, 2011 (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

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Reserved.

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: May 12, 2011

ENERGYCONNECT GROUP, INC.

By: /s/ Kevin R. Evans
Kevin R. Evans
Chief Executive Officer
(Principal Executive Officer)

By: /s/ Amir Ameri
Amir Ameri
Chief Financial Officer
(Principal Financial and Accounting Officer)

EXHIBIT INDEX

Exhibit No.	Description
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