

LPL Investment Holdings Inc.
Form S-1/A
August 10, 2010

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As filed with the Securities and Exchange Commission on August 10, 2010

Registration No. 333-167325

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Amendment No. 3

to

Form S-1

REGISTRATION STATEMENT

UNDER

THE SECURITIES ACT OF 1933

LPL Investment Holdings Inc.

(Exact name of registrant as specified in its charter)

Delaware

*(State or other jurisdiction of
incorporation or organization)*

6200

*(Primary Standard Industrial
Classification Code Number)*

20-3717839

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

One Beacon Street, Boston, MA 02108

(617) 423-3644

(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

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Approximate date of commencement of proposed sale to public: As soon as practicable after this Registration Statement becomes effective.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, as amended (the Securities Act), check the following box.

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

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 <input type="checkbox"/>	Accelerated filer <input type="checkbox"/>	Non-accelerated filer <input type="checkbox"/>	Smaller reporting company <input type="checkbox"/>
-----------------------------------------------------	--------------------------------------------	------------------------------------------------	-------------------------------------------------------

(Do not check if a smaller reporting company)

The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933, as amended, or until the Registration Statement shall become effective on such date as the Securities and Exchange Commission, acting pursuant to said Section 8(a), may determine.

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The information in this preliminary prospectus is not complete and may be changed. These securities may not be sold until the registration statement filed with the Securities and Exchange Commission is effective. This preliminary prospectus is not an offer to sell these securities and it is not soliciting an offer to buy these securities in any jurisdiction where the offer or sale is not permitted.

Subject to Completion. Dated August 10, 2010.

Shares

Common Stock

This is an initial public offering of common stock of LPL Investment Holdings Inc.

The selling stockholders identified in this prospectus are offering _____ shares to be sold in the offering. LPL Investment Holdings Inc. will not receive any of the proceeds from the sale of the shares being sold by the selling stockholders.

Prior to this offering, there has been no public market for the common stock. It is currently estimated that the initial public offering price per share will be between \$ _____ and \$ _____. LPL Investment Holdings Inc. intends to list the common stock on the NASDAQ Global Select Market under the symbol LPLA.

See Risk Factors on page 14 to read about factors you should consider before buying shares of the common stock.

Neither the Securities and Exchange Commission nor any other regulatory body has approved or disapproved of these securities or passed upon the accuracy or adequacy of this prospectus. Any representation to the contrary is a criminal offense.

	Per Share	Total
Initial public offering price	\$ _____	\$ _____
Underwriting discount	\$ _____	\$ _____
Proceeds, before expenses, to the selling stockholders	\$ _____	\$ _____

To the extent the underwriters sell more than _____ shares of common stock, the underwriters have the option to purchase up to an additional _____ shares from LPL Investment Holdings Inc. and one of our stockholders at the initial public offering price less the underwriting discount.

The underwriters expect to deliver the shares against payment in New York, New York on _____, 2010.

Goldman, Sachs & Co.

Morgan Stanley

BofA Merrill Lynch

J.P. Morgan

Sanford C. Bernstein

William Blair & Company

Citi

Keefe, Bruyette & Woods

Lazard Capital Markets

Macquarie Capital

Sandler O'Neill + Partners, L.P.

UBS Investment Bank

Prospectus dated _____, 2010.

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We have not authorized anyone to provide any information or to make any representations other than those contained in or incorporated by reference into this prospectus or in any free writing prospectuses we have prepared. We take no responsibility for, and can provide no assurance as to the reliability of, any other information that others may give you. This prospectus is an offer to sell only the shares offered hereby, but only under circumstances and in jurisdictions where it is lawful to do so. The information contained in this prospectus is current only as of its date.

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MARKET, RANKING AND OTHER INDUSTRY DATA

The data included in this prospectus regarding markets and ranking, including the size of certain markets and our position and the position of our competitors within these markets, are based on reports of government agencies or published industry sources and estimates based on our management's knowledge and experience in the markets in which we operate. These estimates have been based on information obtained from our trade and business organizations and other contacts in the markets in which we operate. We believe these estimates to be accurate as of the date of this prospectus. However, this information may prove to be inaccurate because of the method by which we obtained some of the data for the estimates or because this information cannot always be verified with complete certainty due to the limits on the availability and reliability of raw data, the voluntary nature of the data gathering process and other limitations and uncertainties. As a result, you should be aware that market, ranking and other similar industry data included in this prospectus, and estimates and beliefs based on that data, may not be reliable.

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PROSPECTUS SUMMARY

This summary highlights information contained elsewhere or incorporated by reference in this prospectus. This summary does not contain all of the information you should consider before investing in our common stock. You should read this entire prospectus carefully, especially the Risk Factors section of this prospectus and our consolidated financial statements and related notes appearing at the end of this prospectus, before making an investment decision. This summary contains forward-looking statements that involve risks and uncertainties. Our actual results may differ significantly from the results discussed in the forward-looking statements as a result of certain factors, including those set forth in Risk Factors and Special Note Regarding Forward-Looking Statements.

We refer to Adjusted EBITDA, Adjusted Net Income and Adjusted Net Income per share in this prospectus summary and elsewhere in this prospectus. For the definitions of Adjusted EBITDA, Adjusted Net Income and Adjusted Net Income per share, an explanation of why we present these metrics and a description of the limitations of these non-GAAP measures, as well as a reconciliation to net income, see Management's Discussion and Analysis of Financial Condition and Results of Operations How We Evaluate Growth.

When we use the terms we, us, our, LPL or the company, we mean LPL Investment Holdings Inc., a Delaware corporation, and its consolidated subsidiaries, including LPL Financial Corporation (LPL Financial), taken as a whole, as well as the predecessor entity LPL Holdings, Inc. (predecessor), unless the context otherwise indicates.

Overview

We provide an integrated platform of proprietary technology, brokerage and investment advisory services to over 12,000 independent financial advisors and financial advisors at financial institutions (our advisors) across the country, enabling them to successfully service their retail investors with unbiased, conflict-free financial advice. In addition, we support over 4,000 financial advisors with customized clearing, advisory platforms and technology solutions. Our singular focus is to support our advisors with the front, middle and back-office support they need to serve the large and growing market for independent investment advice, particularly in the mass affluent market (which we define as investors with \$100,000-\$1,000,000 in investable assets). We believe we are the only company that offers advisors the unique combination of an integrated technology platform, comprehensive self-clearing services and full open architecture access to leading financial products, all delivered in an environment unencumbered by conflicts from product manufacturing, underwriting or market making.

For over 20 years we have served the independent advisor market. We currently support the largest independent advisor base and the fifth largest overall advisor base in the United States. Through our advisors, we are also one of the largest distributors of financial products in the United States. Our scale is a substantial competitive advantage and enables us to more effectively attract and retain advisors. Our unique model allows us to invest more resources in our advisors, increasing their revenues and creating a virtuous cycle of growth. We are headquartered in Boston and currently have over 2,500 employees in our Boston, Charlotte and San Diego locations.

Market Opportunity and Industry Background

The market our advisors serve is significant and expanding. According to the Federal Reserve, U.S. household and non-profit organization financial assets totaled \$45.1 trillion as of December 31, 2009, up from \$41.7 trillion at December 31, 2008 and \$38.9 trillion at December 31, 2004. In addition, according to Cerulli Associates, a research and consulting firm specializing in the financial services industry, \$8.5 trillion of retail assets were professionally managed as of December 31, 2008, up from \$6.8 trillion as of December 31, 2003. Finally, 58% of all

U.S. households utilized a financial advisor in 2008.

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Cerulli Associates divides the retail advisor market into six broad channels: the two independent channels that we serve (independent and registered investment advisors (RIAs)) and four employee model or captive channels (insurance, wirehouse, regional and bank). During the period from 2004 to 2009, the independent channels experienced substantial growth on both an absolute and relative basis, taking market share from the captive channels. According to Cerulli Associates, the independent channels market share by number of advisors increased from 37% in 2004 to 40% in 2009. In 2009, over 132,000 independent financial advisors managed \$3.5 trillion in client assets, representing 33% of total retail advisor client assets.

Cerulli Associates forecasts that total U.S. assets under management will grow 29% from 2008 to 2012 due to factors such as the retirement of the baby boomer generation as well as the continued growth of individual retirement account rollovers. Cerulli Associates estimates that from 2009 to 2012, the independent channels market share by number of advisors will grow by four percentage points to 44%, and market share by client assets will grow four percentage points to 37%.

We believe there are several key factors driving the growth of the independent channels. Investors in the mass affluent market, and increasingly in the high net worth market, are seeking unbiased, conflict-free advice. The number of advisors electing to leave the large financial institutions to become independent financial advisors has accelerated over the last several years in part because of the ongoing consolidation among the captive platforms, particularly among the wirehouses. Finally, many advisors have entrepreneurial aspirations and are attracted to the flexibility, control and compelling economics inherent in the independent financial advisor model.

Our Business

With our focus and scale, we are not only a beneficiary of the secular shift among advisors toward independence, but an active catalyst of this trend. Between 2004 and 2009, our number of advisors increased at a compound annual growth rate (CAGR) of 15%, while according to Cerulli Associates, the total number of advisors across all channels remained relatively flat. We enable our advisors to provide their clients with high quality independent financial advice and investment solutions, and support our advisors in managing the complexity of their businesses by providing a comprehensive integrated platform of technology and clearing services. We provide these services through an open architecture product platform with no proprietary manufactured products, which enables an unbiased, conflict-free environment. Our historical advisor growth rate does not guarantee that we will attract advisors at comparable rates in the future. For example, when comparing our number of advisors as of June 30, 2010 to June 30, 2009, we had a net decrease in advisors, and as of December 31, 2009 to December 31, 2008, we had relatively no change in our number of advisors, in both cases due to the attrition of advisors in connection with the consolidation of the operations of certain of our previously acquired subsidiaries. See Management s Discussion and Analysis of Financial Condition and Results of Operations How We Evaluate Growth.

Our Financial Advisors

For more than 20 years our Commitment Creed has been ingrained in our culture and reflects our singular focus on the advisors we serve. The size and growth of our business has benefited from this focus. Our advisor base has grown from 3,596 advisors in 2000 to 12,066 as of June 30, 2010, representing a CAGR of 13.6%. Our historical advisor growth rate does not guarantee that we will attract advisors at comparable rates in the future.

Our advisor base includes independent financial advisors, RIAs and advisors at small and mid-sized financial institutions. Advisors that join us average over 15 years of industry experience. This substantial industry experience allows us to focus on enhancing our advisors businesses without the need for basic training or subsidizing advisors that are new to the industry. We are also rigorous in both our initial advisor screening and diligence as well as our

ongoing monitoring through our internal risk management and compliance functions.

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Our independent advisors join us from a broad range of firms including wirehouses, regional and insurance broker-dealers, banks and other independent firms. Our flexible business platform allows our advisors to choose the most appropriate business model to support their clients, whether they conduct brokerage business, offer brokerage and fee-based services on our corporate RIA platforms or provide fee-based services through their own RIAs.

Among our 12,000 advisors, we support over 2,400 advisors at over 750 banks and credit unions. We believe these financial institutions are drawn to our outsourcing solutions because we provide the broad array of services advisors at these institutions need to be successful, allowing these institutions to focus their energy and capital on their core businesses.

We also provide support to over 4,000 additional financial advisors who are affiliated and licensed with insurance companies. These outsourcing arrangements provide customized clearing, advisory platforms and technology solutions that enable financial advisors at these insurance companies to efficiently provide a breadth of services to their client base.

Our Service Value Proposition

The core of our business is dedicated to meeting the evolving needs of our advisors and providing the platform and tools to grow and enhance the profitability of their businesses. We support our advisors by providing front, middle and back-office solutions through the four pillars of our distinct value proposition:

Enabling Technology. We provide our technology and service to advisors through BranchNet, our proprietary, integrated technology platform that is server-based and web-accessed. Using the BranchNet workstation, our advisors effectively manage all critical aspects of their businesses while remaining highly efficient and responsive to their clients' needs.

Comprehensive Clearing and Compliance Services. We custody and clear the majority of our advisors transactions, providing an enhanced advisor experience and expedited processing capabilities. Our self-clearing platform also enables us to serve a wider variety of advisors, including RIAs and dually-registered advisors (hybrid RIAs). We have made sizeable investments in our compliance offering to fully integrate these tools into our technology platform. Since 2000, our commitment of resources and focus on compliance have enabled us to maintain one of the best regulatory compliance records, based upon the number of regulatory events reported in FINRA's BrokerCheck Reports, among the five largest U.S. broker-dealers, ranked by number of advisors.

Practice Management Programs and Training. Our practice management programs help our advisors enhance and grow their businesses. Because of our scale, we are able to dedicate a large and experienced group of professionals that work with our advisors to build and better manage their business and client relationships through one-on-one consulting. In addition, we hold 140 conferences and group training events annually for the benefit of our advisors.

Independent Research. Our research team consists of over 25 professionals with an average of 12 years of industry experience, dedicated to providing unbiased, conflict-free advice. We provide our advisors with integrated access to comprehensive proprietary and third-party independent research on mutual funds, separate accounts, insurance and annuities, asset allocation strategies, financial markets and the economy, among other areas.

Our Economic Value Proposition

We offer a compelling economic value proposition that is a key factor in our ability to attract and retain advisors. The independent channels pay advisors a greater share of brokerage commissions and advisory fees than the captive channels generally 80-90% compared to 30-50%. Because of our scale and efficient operating model, we offer our advisors the highest average payout ratios

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among the five largest U.S. broker-dealers, ranked by number of advisors, which we believe provides us with an important competitive advantage. Throughout this prospectus, we use *payout ratio* to refer to the portion of advisor-generated revenues, consisting of commissions and advisory fees, that we collect from advisors' clients and pay to advisors.

We believe our superior technology and service platforms enable our advisors to operate their practices at a lower cost than other independent advisors. As a result, we believe owners of practices associated with us earn meaningfully more pre-tax profit than owners of practices affiliated with other independent brokerage firms. We attribute this difference in profitability, in part, to lower fixed costs driven by the need for fewer staff at our associated practices. Finally, as business owners, independent advisors, unlike captive advisors, also have the opportunity to build equity in their own businesses.

Our Product Access

We do not manufacture any financial products. Instead, we provide our advisors open architecture access to a large variety of commission, fee-based, cash and money market products and services. Our platform provides access to over 8,500 financial products, which are manufactured by over 400 product sponsors. Our product diligence group pre-screens all new products.

As of June 30, 2010, advisory and brokerage assets totaled \$277 billion, of which \$79 billion was in advisory assets. In 2009, brokerage sales were over \$28 billion, including over \$10 billion in mutual funds and \$14 billion in annuities. Advisory sales were \$23 billion, which consisted primarily of mutual funds. As a result of this scale and significant distribution capabilities, we can offer leading products and services with attractive economics to our advisors.

Our Financial Model

We have a proven track record of strong financial performance. We have increased our annual Adjusted EBITDA for the past five consecutive years with only one decline in annual revenue in 2009 in conjunction with the major market downturn. Our net income over the same period has declined two times, in 2006 and 2008. We have experienced greater variability in our net income primarily due to amortization of purchased assets and interest expense from our senior secured credit facilities and subordinated notes, both a result of our merger transaction in 2005 with the investment funds affiliated with Hellman & Friedman LLC and TPG Capital (collectively the *Majority Holders*), as well as expenses associated with our acquisition integration and restructuring initiatives.

Since 2005, we have grown our net revenues at an 18% CAGR, our net income at a 2% CAGR, our Adjusted EBITDA at a 17% CAGR and our Adjusted Net Income at a 13% CAGR. See *Selected Consolidated Financial Data*. Our historical growth rates do not guarantee future results, levels of activity, performance or achievements. See *Special Note Regarding Forward-Looking Statements*. As we demonstrated during the financial crisis of 2008 and 2009, our financial model has inherent resilience, and our overall financial performance is a function of the following favorable characteristics:

Diverse and Recurring Revenue. Our revenue stems from diverse and recurring sources, including commission and advisory fees, asset based fees, fees from product manufacturers, recordkeeping and cash sweep balances. Our recurring revenue is associated with asset balances and is not based on transaction volumes or other activity-based fees. Therefore, although the level of our revenue sources can be impacted by external market conditions such as the economic downturn experienced in 2008 and 2009, their recurring nature provides a level of predictability. This is demonstrated by our recurring revenues in 2009, 2008 and 2007, which were 57.3%, 58.5% and 57.1%, respectively, of our net revenues.

Variable Expenses. Our expenses are predominantly variable. They consist primarily of payouts to advisors, which are determined as a percentage of advisor-generated revenue. This percentage payout generally varies with advisor productivity, which is correlated to market

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performance. Our general and administrative expenses can be actively managed, as evidenced during the recent financial crisis.

Low Capital Requirements. We do not manufacture products, make markets, provide underwriting or engage in mortgage lending. As a result, our cash flow is not encumbered by capital intensive activities. In addition, we can reinvest the substantial free cash flows that we generate in our business.

Our Competitive Strengths

Significant Scale and Market Leadership Position. We are the established leader in the independent advisor market, which is our core business focus. Our scale enables us to benefit from the following dynamics:

We actively reinvest in our comprehensive technology platform and practice support, which further improves the productivity of our advisors.

As one of the largest distributors of financial products in the United States, we are able to obtain attractive economics from product manufacturers.

Among the five largest U.S. broker-dealers by number of advisors, we offer the highest average payout ratios to our advisors.

The combination of our ability to reinvest in the business and maintain highly competitive payout ratios allows us to attract and retain advisors successfully. This, in turn, drives our growth and leads to a virtuous cycle that reinforces our established scale advantage.

Unique Value Proposition for Independent Advisors. We believe we are the only company that offers a conflict-free, open architecture and scalable platform, which leads to greater economics for our advisors and allows them to build equity in their businesses. This generates a significant opportunity to attract and retain highly qualified advisors who are seeking independence.

Unique Value Proposition for Institutions. We provide solutions to financial institutions, such as regional banks, credit unions and insurers, who would otherwise find the technology, infrastructure and regulatory requirements associated with delivering financial advice to be cost-prohibitive.

Ability to Profitably Serve the Mass Affluent Market. We have designed and integrated all aspects of our platforms and services to profitably meet the needs of advisors who serve the mass affluent market. We believe there is an attractive opportunity in this market, in part because wirehouses have not historically focused on the mass affluent market. We believe our scale will sustain and strengthen our competitive advantage in the mass affluent market.

Ability to Serve a Broad Range of Advisor Models. As a result of our integrated technology platform and the resulting flexibility, we are able to attract and retain advisors from multiple channels, including wirehouses, regional broker-dealers and other independent broker-dealers. In addition, although we have grown through our focus on the mass affluent market, the breadth of our platform has facilitated growing penetration of the high net worth market. As of June 30, 2010, our advisors supported accounts with more than \$1 million in assets that in the aggregate represented \$38.5 billion in advisory and brokerage assets, or 14% of our total.

Experienced and Committed Senior Management Team. We have an experienced and committed senior management team that provides stable and long-standing leadership for our business. The management team

is aligned with stockholders and holds significant equity ownership in the company.

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Risks That We Face

Our business is subject to a number of risks of which you should be aware before making an investment decision. These risks are discussed more fully in the Risk Factors section of this prospectus immediately following this prospectus summary. These risks include the following:

We depend on our ability to attract and retain experienced and productive advisors. We derive a large portion of our revenues from commissions and fees generated by our advisors. If we fail to attract new advisors or to retain and motivate our current advisors, our business may suffer.

Our financial condition and results of operations may be adversely affected by market fluctuations and other economic factors. General economic and market factors can affect our commission and fee revenue. Significant downturns and volatility in equity and other financial markets have had and could continue to have an adverse effect on our financial condition and results of operations.

Regulatory developments and our failure to comply with regulations could adversely affect our business by increasing our costs and exposure to litigation, affecting our reputation and making our business less profitable. Our business is subject to extensive U.S. regulation and supervision, including securities and investment advisory services. The recently enacted Dodd-Frank Wall Street Reform and Consumer Protection Act is likely to generate a number of new rules and regulations. Our ability to conduct business depends on our compliance with these laws, rules and regulations, which is largely dependent on our establishment and maintenance of compliance systems and procedures.

We operate in an intensely competitive industry, which could cause us to lose advisors and their assets, thereby reducing our revenues and net income. We are subject to competition in all aspects of our business, including competition for our advisors and clients. If we fail to continue to attract highly qualified advisors or advisors licensed with us leave us to pursue other opportunities, or if current or potential clients of our advisors decide to use one of our competitors, we could face a significant decline in market share, commission and fee revenues and net income.

We rely on technology in our business, and technology and execution failures could subject us to losses, litigation and regulatory actions. Our business relies extensively on electronic data processing and communications systems. Failure of our systems, which could result from events beyond our control, or an inability to effectively upgrade those systems or implement new technology-driven products or services, could result in financial losses, liability to clients and damage to our reputation.

Our indebtedness could adversely affect our financial health and may limit our ability to use debt to fund future capital needs. Our level of indebtedness could increase our vulnerability to general adverse economic and industry conditions, require us to dedicate a substantial portion of our cash flow from operation to payments on our indebtedness and may limit our flexibility in planning for changes in our business and the industry in which we operate.

The Majority Holders will have the ability to control the outcome of matters submitted for stockholder approval and may have interests that differ from those of our other stockholders. Due to their ownership of a majority of our capital stock, the Majority Holders have significant influence over corporate transactions and are able to effectively control our decisions, regardless of whether or not other stockholders believe that the transaction is in their own best interests.

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Our Sources of Growth

We expect to increase our revenue and profitability by benefiting from favorable industry trends and by executing strategies to accelerate our growth beyond that of the broader markets in which we operate.

Favorable Industry Trends

Growth in Investable Assets. According to Cerulli Associates, total U.S. assets under management in the United States are anticipated to grow at 7% per year over the next four years and retirement assets are expected to grow 8% from 2008 to 2014 (in part due to the retirement of the baby boomer generation and the resulting assets which are projected to flow out of retirement plans and into individual retirement accounts). In addition, individual retirement account rollovers are projected to almost double, growing from \$3.6 trillion as of 2008 to \$6.8 trillion by 2014.

Increasing Demand for Independent Financial Advice. Retail investors, particularly in the mass affluent market, are increasingly seeking financial advice from independent sources.

Advisor Migration to Independence. Independent channels are gaining market share from captive channels. We believe that we are not just a beneficiary of this secular shift, but an active catalyst in the movement to independence.

Macroeconomic Trends. As the macroeconomic environment continues to stabilize, we anticipate an appreciation in asset prices and a rise in interest rates from current, historically low levels. We expect that our business will benefit from growth in advisory and brokerage assets as well as increasing asset-based and cash sweep fees.

LPL-Specific Growth Opportunities

Attracting New Advisors to our Platform. We have only 3.6% market share of the approximately 334,000 financial advisors in the United States, according to Cerulli Associates, which provides us with significant opportunity to attract new advisors.

Ramp-up of Newly-Attracted Advisors. We predominately attract experienced advisors who have established practices. In our experience, it takes an average of three years for new advisors to re-establish their practices and associated revenues. This seasoning process creates accelerated growth of revenue from our new advisors.

Increasing Productivity of Existing Advisor Base. The productivity of our advisors increases over time as we enable them to add new clients, gain shares of their clients' investable assets, and expand their existing practices with additional advisors. We facilitate these productivity improvements by helping our advisors better manage their practices in an increasingly complex environment.

Our Business Model has Inherent Economies of Scale. The largely fixed costs necessary to support our advisors deliver higher marginal profitability as our advisors' client assets and our revenues grow. Historically, this dynamic has been demonstrated through the growth in our operating margins.

Opportunistic Pursuit of Acquisitions. We have a proven history of expanding our business through opportunistic acquisitions. In the past six years, we have successfully completed four transactions. Our scalable business model and operating platform make us an attractive acquirer in a fragmented market.

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Recent Developments

Acquisition of National Retirement Partners

On July 14, 2010, we announced a definitive agreement to acquire certain assets from National Retirement Partners, Inc. (NRP). NRP s advisors offer products and services to retirement plan sponsors and participants and comprehensive financial services to high net worth individuals. Through this asset purchase, NRP s independent advisors will have the opportunity to join LPL Financial. This transaction will further enhance our capabilities and presence in group retirement plans, while providing benefits for both NRP advisors who join LPL Financial as well as for our existing advisors.

The consideration for the transaction consists of a payment on the closing date of \$27.0 million, subject to an escrow for specified matters, and a contingent payment to be made on the third anniversary of closing of approximately 25%-30% of the amount by which the gross trailing twelve-month commission and fee revenues relating to the business exceed an agreed upon performance target. Upon completion of this transaction, certain NRP employees will join LPL Financial. NRP has agreed to indemnify us for breaches of representations and warranties and covenants, as well as pre-closing actions or omissions. The transaction is expected to close in the fourth quarter of 2010, subject to customary closing conditions including regulatory approvals.

Our Corporate Structure

LPL Investment Holdings Inc. is the parent company of our collective businesses. Our address is One Beacon Street, Boston, Massachusetts 02108. Our telephone number is (617) 423-3644. Our website address is www.lpl.com. Information contained in, and that can be accessed through, our website is not incorporated into and does not form a part of this prospectus.

On December 28, 2005, LPL Holdings, Inc., the predecessor, and its subsidiaries were acquired through a merger transaction by funds affiliated with the Majority Holders. Any activities shown or described for periods prior to December 28, 2005 are those of the predecessor.

be determined by the board of directors; (b) a change in control of the company or (c) death or disability of the holder;

3,197,146 additional shares of common stock as of June 30, 2010 reserved for future grants under our equity incentive plans currently in effect and

12,055,945 additional shares of common stock reserved for future equity incentive plans to be effective upon the occurrence of this offering.

Unless otherwise indicated, all information in this prospectus:

assumes the adoption of our amended and restated certificate of incorporation (certificate of incorporation) and our second amended and restated bylaws (bylaws), to be effective upon the closing of this offering and

assumes no exercise by the underwriters of their option to purchase up to additional shares of our common stock in this offering.

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The following tables present a summary of our historical financial information and operating data. You should read the following summary in conjunction with Selected Consolidated Financial Data, Management's Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and related notes, all included elsewhere in this prospectus.

Historical dividends per share are presented as declared by the predecessor under its capital structure at that time. Shares of common stock of our predecessor are not equal to shares of common stock under our current capital structure and are not necessarily indicative of amounts that would have been received per share of common stock under our current capital structure.

For the Six Months Ended June 30,		For the Year Ended December 31,				Predecessor(2)
2010(1)	2009(1)	2009(1)	2008(1)	2007(1)	2006	2005
(unaudited)						

(In thousands, except per share data)

Consolidated statements of income data:

Net revenues \$ 1,533,567 \$ 1,312,295 \$ 2,749,505 \$ 3,116,349 \$ 2,716,574 \$ 1,739,635 \$ 1,406,320

After effecting the PIPE Transaction and the Parke and Kapadia acquisitions, we have the following:

Cash of approximately \$7 million (as of September 30, 2006);

No debt, except for the mortgage on our headquarters in the amount of \$532,000, a \$150,000 demand note owed to one of our stockholders, and various auto loans and capitalized leases totaling approximately \$53,000 (all balances as of September 30, 2006);

One class of outstanding equity (common stock), with no outstanding preferred stock or convertible debt;

Approximately 78 employees;

Eight sales offices located in New York, Chicago, Salt Lake City, San Diego, Glendora, California, Danville, California, Carmel, California and Ventura, California;

Proprietary technology that controls and reduces energy consumed in commercial lighting and HVAC applications;

A business that designs, engineers and installs energy efficient lighting upgrades for commercial and industrial users; and

A largely revamped board of directors (4 of the 7 directors have joined the board since October 2005) and senior management team (our CEO and our President are both new to the Company in 2006).

We believe that as a result of these recently implemented changes we will be better positioned to take advantage of the growth in demand for energy efficiency products and services, hopefully leading to improved profitability and cash flow. We also believe that there are opportunities for future acquisitions that could broaden our product line, increase our geographic reach and lead us to new markets for our products, all of which we hope would also

contribute to increased sales and to profitability.

RISK FACTORS

The following disclosure of risk factors includes all material risks known to us at this time. Additional risks we are not presently aware of or that we currently believe are immaterial may prove to impair our business and financial performance. Our business could be harmed by any of these risks, whether stated or unstated. We operate in a continually changing business environment and may as a result enter into new businesses and product lines. We cannot predict new risk factors that may arise in the future, and we cannot assess the impact, if any, of these new risk factors on our businesses or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those projected in any forward-looking statements. Accordingly, you should not rely on forward-looking statements as a prediction of actual results. In addition, our estimates of future operating results are based on our current complement of businesses, which is subject to change as we continue to assess and refine our business strategy. If any of the following risks actually occur, our business, results of operations, and financial condition could be adversely affected in a material manner and could negatively affect the value of your investment.

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Risks Related to Our Business

We have a limited operating history upon which to evaluate our potential for future success.

We were formed in December 1997. To date, we have generated limited revenues from the sale of our products and do not expect to generate significant revenues until we sell a significantly greater amount of our products and services. Accordingly, we have only a limited operating history upon which you can base an evaluation of our business and prospects. Moreover, we have acquired five businesses over the past six years and subsequently sold two of them because of changes in our overall strategy. The likelihood of our success must be considered in light of the risks and uncertainties frequently encountered by early stage companies like ours in an evolving market. If we are unsuccessful in addressing these risks and uncertainties, our business will be materially harmed or in the worst case, could fail.

We have incurred significant operating losses since inception and may not achieve or sustain profitability in the future.

We have experienced operating losses and negative cash flow from operations since our inception and we currently have an accumulated deficit. These factors raise substantial doubt about our ability to continue as a going concern. Our ability to continue as a going concern is ultimately dependent on our ability to increase sales to a level that will allow us to operate profitably and sustain positive operating cash flows. Although we are continuing our efforts to improve profitability through expansion of our business in both current and new markets, we must overcome significant manufacturing hurdles, including gearing up to produce large quantities of product or arranging to outsource the production of our products, and marketing hurdles, including gaining market acceptance, in order to sell large quantities of our products and services. In addition, we may be required to reduce the prices of our products or services in order to increase sales. If we reduce prices, we may not be able to reduce costs sufficiently to achieve acceptable profit margins. As we strive to grow our business, we have spent and expect to continue to spend significant funds (1) for general corporate purposes, including working capital, marketing, recruiting and hiring additional personnel; and (2) for research and development. To the extent that our revenues do not increase as quickly as these costs and expenditures, our results of operations and liquidity will be materially adversely affected. If we experience slower than anticipated revenue growth or if our operating expenses exceed our expectations, we may not achieve profitability. Even if we achieve profitability in the future, we may not be able to sustain it.

Our auditors have modified their opinion to our audited financial statements for the year ended December 31, 2005 to include an emphasis paragraph, stating that our continuing losses and negative cash flow from operations raise substantial doubt about our ability to continue as a going concern. We have recently raised gross proceeds of \$17,875,000 through the issuance of shares of our common stock, which has improved our current liquidity. We have also recently sold a subsidiary and acquired Parke P.A.N.D.A. Corporation (now named Parke Industries, LLC) and Kapadia Consulting, Inc. (now named Kapadia Energy Services, Inc.) and we are in the process of making other changes to our business which we hope will lead to an improvement in our cash flow in future periods. Whether these changes will lead to us becoming cash flow positive remains to be seen.

Our independent registered public accountants have issued a going concern opinion raising doubt about our financial viability.

As a result of our continuing losses and negative cash flows, our independent registered public accounting firm, BDO Seidman, LLP, issued a going concern opinion in connection with their audit of our financial statements for the year ended December 31, 2005. This opinion expressed substantial doubt as to our ability to continue as a going concern. The going concern opinion could have an adverse impact on our ability to execute our business plan, result in the reluctance on the part of certain suppliers to do business with us, result in the inability to obtain new business due to potential customers' concern about our ability to deliver products or services, or adversely affect our ability to raise additional debt or equity capital.

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Failure to replace a significant customer could materially and adversely affect our results of operations and financial condition.

We have historically derived a significant portion of our annual revenue from a limited number of customers. Seldom has any one customer represented 10% or more of our revenues for more than one year in a row. This requires that we continually replace major customers, whose needs we have satisfied, with one or more new customers. The failure to replace a major customer could have a significant negative effect on our results of operations and financial condition.

A decrease in electric retail rates could lessen demand for our products.

Our principal products, our EnergySaver and eMAC products and our lighting retro-fit services and energy engineering services, have the greatest profit potential in areas where commercial electric rates are relatively high. However, retail electric rates for commercial establishments in the United States may not remain at their current levels. Due to a potential overbuilding of power generating stations in certain regions of the United States, wholesale power prices may decrease in the future. Because the price of commercial retail electric power is largely attributed to the wholesale cost of power, it is reasonable to expect that commercial retail rates may decrease as well. In addition, much of the wholesale cost of power is directly related to the price of certain fuels, such as natural gas, oil and coal. If the prices of those fuels decrease, the prices of the wholesale cost of power may also decrease. This could result in lower electric retail rates and reduced demand for our energy saving products and services.

We have a license to use certain patents and our ability to sell our products may be adversely impacted if the license expires or is terminated.

We have entered into a license agreement with Messrs. Giorgio Reverberi and Joseph Marino with regard to the core technology used in our EnergySaver product. Mr. Reverberi holds a U.S. patent and has applied for several patents in other countries. Pursuant to the terms of the license, we have been granted the exclusive right to manufacture and sell products containing the load reduction technology claimed under Mr. Reverberi's U.S. patent or any other related patent held by him in the U.S., the remainder of North America, parts of South America and parts of Africa. However, the exclusive rights that we received may not have any value in territories where Mr. Reverberi does not have or does not obtain protectable rights. The term of the license expires when the last of these patents expires. We expect that these patents will expire around November 2017. The license agreement may be terminated if we materially breach its terms and fail to cure the breach within 180 days after we are notified of the breach. If our license is terminated it could impact our ability to manufacture, sell or otherwise commercialize EnergySaver products in those countries where Mr. Reverberi holds valid patents relating to our products, including the United States.

If we are not able to protect our intellectual property rights against infringement, or if others obtain intellectual property rights relating to energy management technology, we could lose our competitive advantage in the energy management market.

We regard our intellectual property rights, such as patents, licenses of patents, trademarks, copyrights and trade secrets, as important to our success. Although we have entered into confidentiality and rights to inventions agreements with our employees and consultants, the steps we have taken to protect our intellectual property rights may not be adequate. Third parties may infringe or misappropriate our intellectual property rights or we may not be able to detect unauthorized use and take appropriate steps to enforce our rights. Failure to take appropriate protective steps could materially adversely affect any competitive advantage we may have in the energy management market. Furthermore, our patents and our license to use Mr. Reverberi's patents may have little or no value to us if our patents or Mr. Reverberi's patents are not valid. In addition, patents held by third parties may limit our ability to manufacture, sell or otherwise commercialize products and could result in the assertion of claims of patent infringement against us. If that were to happen, we could try to modify our products to be non-infringing, but we might not be

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successful or such modifications might not avoid infringing on the intellectual property rights of third parties.

Claims of patent infringement against us, regardless of merit, could result in the expenditure of significant financial and managerial resources by us. We could be forced to seek to enter into license agreements with third parties (other than Mr. Reverberi) to resolve claims of infringement by our products of the intellectual property rights of third parties. Such licenses may not be available on acceptable terms or at all. The failure to obtain such licenses on acceptable terms could have a negative effect on our business.

David Asplund, our new Chief Executive Officer has limited experience operating a company such as ours and no direct industry experience.

Mr. Asplund, who has been on our board since June 2002, has a degree in mechanical engineering and has had a successful career in the financial industry. Mr. Asplund founded an investment banking firm in 1999 and operated the firm as its president for six years, but Mr. Asplund has not operated a manufacturing company and he has limited industry experience. His past experience does not assure that he will be successful in his new role as CEO of Lime Energy.

If we are unable to achieve or manage our growth, it will adversely affect our business, the quality of our products and services, and our ability to attract and retain key personnel.

If we succeed in growing our sales as we need to do, we will be subject to the risks inherent in the expansion and growth of a business enterprise. Growth in our business will place a strain on our operational and administrative resources and increase the level of responsibility for our existing and new management personnel. To manage our growth effectively, we will need to:

 further develop and improve our operating, information, accounting, financial and other internal systems and controls on a timely basis;

 improve our business development, marketing and sales capabilities; and

 expand, train, motivate and manage our employee base.

Our systems currently in place may not be adequate if we grow and may need to be modified and enhanced. The skills of management currently in place may not be adequate if we experience significant growth.

If our management fails to properly identify companies to acquire and to effectively negotiate the terms of these acquisition transactions, our growth may be impaired.

As part of our growth strategy, we have recently acquired Parke Industries and Kapadia Energy Services and intend to seek to acquire other companies with complementary technologies, products and/or services. Our management, including our board of directors, will have discretion in identifying and selecting companies to be acquired by us and in structuring and negotiating these acquisitions. In general, our common stockholders may not have the opportunity to approve these acquisitions. In addition, in making acquisition decisions, we will rely, in part, on financial projections developed by our management and the management of potential target companies. These projections will be based on assumptions and subjective judgments. The actual operating results of any acquired company or the combination of us and an acquired company may fall significantly short of projections.

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We may be unable to acquire companies that we identify as targets for various reasons, including:
our inability to interest such companies in a proposed transaction;

our inability to agree on the terms of an acquisition;

incompatibility between our management and management of a target company; and

our inability to obtain the approval of the holders of our common stock, if required.

If we cannot consummate acquisitions on a timely basis or agree on terms at all, or if we cannot acquire companies with complementary technologies, products and/or services on terms acceptable to us, our future growth may be impaired.

Our growth may be impaired and our current business may suffer if we do not successfully address risks associated with acquisitions.

Since January 1, 2000, we have acquired five companies; Switchboard Apparatus Inc., Great Lakes Controlled Energy Corporation, Maximum Performance Group, Inc., Parke P.A.N.D.A. Corporation (now called Parke Industries, LLC) and Kapadia Consulting, Inc. (now called Kapadia Energy Services, Inc.), two of which (Switchboard Apparatus and Great Lakes Controlled Energy) we subsequently sold at a loss. Our future growth may depend, in part, upon our ability to successfully identify, acquire and operate other complementary businesses. We may encounter problems associated with such acquisitions, including the following:

difficulties in integrating acquired operations and products with our existing operations and products;

difficulties in meeting operating expectations for acquired businesses;

diversion of management's attention from other business concerns;

adverse impact on earnings of amortization or write-offs of goodwill and other intangible assets relating to acquisitions; and

issuances of equity securities that may be dilutive to existing stockholders to pay for acquisitions.

In addition, often an acquired company's performance is largely dependent on a few key people, particularly in smaller companies. If these key people leave the company, become less focused on the business or less motivated to make the business successful after the acquisition, the performance of the acquired company may suffer.

If our products and services do not achieve or sustain market acceptance, our ability to compete will be adversely affected.

To date, we have not sold our eMAC or EnergySaver product lines in very large quantities and a sufficient market may not develop for them. Significant marketing will be required in order to establish a sufficient market for these products. The technology underlying our products may not become a preferred technology to address the energy management needs of our customers and potential customers. Failure to successfully develop, manufacture and commercialize products on a timely and cost-effective basis will have a material adverse effect on our ability to compete in the energy management market or survive as a business.

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Failure to meet customers' expectations or deliver expected technical performance could result in losses and negative publicity.

Customer engagements involve the installation of energy management equipment to help our clients reduce energy/power consumption. We often rely on outside contractors to install our EnergySaver and eMAC products. Any defects in this equipment and/or its installation or any other failure to meet our customers' expectations could result in: delayed or lost revenues due to adverse customer reaction;

requirements to provide additional products, replacement parts and/or services to a customer at no charge;

negative publicity regarding us and our products, which could adversely affect our ability to attract or retain customers; and

claims for substantial damages against us, regardless of whether we have any responsibility for such failure.

If sufficient additional funding is not available to us, the commercialization of our products and services and our ability to grow is likely to be hindered.

Our operations have not generated positive cash flow since the inception of the Company in 1997. We have funded our operations through the issuance of common and preferred stock and secured debt. Our ability to continue to operate until our cash flow turns positive may depend on our ability to continue to raise funds through the issuance of equity or debt. If that becomes necessary and we are not successful in raising additional funds, we might have to significantly scale back or delay our growth plans, or possibly cease operations altogether. Any reduction or delay in our growth plans could materially adversely affect our ability to compete in the marketplace, take advantage of business opportunities and develop or enhance our products. If we should have to cease operations altogether, your investment is likely to be lost.

Raising additional capital or consummation of additional acquisitions through the issuance of equity or equity-linked securities could dilute your ownership interest in us.

We have recently raised additional capital through the issuance of common stock to repay debt, fund an acquisition, grow our product development, manufacturing, marketing and sales activities at the pace that we intend, and to continue to fund operating losses until our cash flow turns positive. We may find it necessary to raise capital again some time in the future. If we determine that we do need to raise additional capital in the future and we are not successful in doing so, we might have to significantly scale back or delay our growth plans, reduce staff and delay planned expenditures on research and development and capital expenditures in order to continue as a going concern. Any reduction or delay in our growth plans could materially adversely affect our ability to compete in the marketplace, take advantage of business opportunities and develop or enhance our products.

If we raise additional funds in the future through the issuance of equity securities or convertible debt securities, our existing stockholders will likely experience dilution of their present equity ownership position and voting rights. Depending on the number of shares issued and the terms and conditions of the issuance, new equity securities could have rights, preferences, or privileges senior to those of our common stock. Depending on the terms, common stock holders may not have approval rights with respect to such issuances. For example, we may issue shares of our authorized but unissued preferred stock without stockholder approval.

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Failure to effectively market our energy management products and services could impair our ability to sell significant quantities of these products and services.

One of the challenges we face in commercializing our energy management products and services is demonstrating the advantages of our products and services over competitive products and services. To do this, we will need to further develop our marketing and sales force. If we do not successfully develop and expand our internal sales force, our ability to generate significant revenues may be harmed.

If we do not successfully compete with others in the very competitive energy management market, we may not achieve profitability.

In the energy management market, we compete with other manufacturers of energy management products that are currently used by our potential customers. Many of these companies have substantially greater financial resources, larger research and development staffs and greater manufacturing and marketing capabilities than we do. Our competitors may provide energy management products at lower prices and/or with superior performance. If we are unable to successfully compete with conventional and new technologies, our business may be materially harmed.

Product liability claims could result in losses and could divert our management's time and resources.

The manufacture and sale of our products creates a risk of product liability claims. Any product liability claims, with or without merit, could result in costly litigation and reduced sales, cause us to incur significant expenses and divert our management's time, attention and resources. We do have product liability insurance coverage; however, there is no assurance that such insurance is adequate to cover all potential claims. The successful assertion of any such claim against us could materially harm our liquidity and operating results.

Risks Related to the Rights Offering

If you do not exercise your full basic subscription right, your percentage ownership and voting rights in us will be lower than it would have been in the absence of the rights offering.

If you choose not to exercise your basic subscription right in full, your relative ownership interest in us will be lower than it would have been in the absence of the rights offering if and to the extent others exercise their basic subscription and over-subscription rights. Your voting rights and percentage interest in any potential future earnings will also be lowered if you do not exercise your rights in full.

The subscription price determined for this offering is not an indication of our value.

The subscription price does not necessarily bear any relationship to the book value of our assets, past operations, cash flows, losses, financial condition or any other established criteria for value. You should not consider the subscription price as an indication of our value. In addition, you should not rely on the decision of the PIPE Investors (which included three of our directors) to purchase shares of common stock at a price equal to the subscription price or the decision of Dan Parke, another of our directors, to accept the merger consideration which included \$5.0 million of common stock valued at a price per share equal to the subscription price to be a recommendation or an indication that the subscription price is reflective of our value.

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You may not revoke your subscription exercise and could be committed to buying shares above the prevailing market price.

Once you exercise your subscription rights, you may not revoke the exercise for any reason unless we amend the offering. The public trading market price of our common stock may decline before the subscription rights expire. If you exercise your subscription rights and, afterwards, the public trading market price of our common stock decreases below \$1.00, you will have committed to buying shares of common stock at a price above the prevailing market price. Once you have exercised your subscription rights, you may not revoke your exercise. Moreover, you may be unable to sell your shares of our common stock at a price equal to or greater than the offering price.

Because we may terminate the offering at any time, your participation in the offering is not assured.

We may terminate the offering at any time. If we decide to terminate the offering, we will not have any obligation with respect to the subscription rights except to return any subscription payments, without interest or deduction.

You will need to act promptly and carefully follow subscription instructions.

Stockholders who desire to purchase shares in the rights offering must act promptly to ensure that all required forms and payments are actually received by the subscription agent prior to 5:00 pm on ____, 2007, the expiration date. If you fail to complete and sign the required subscription forms, send an incorrect payment amount, or otherwise fail to follow the subscription procedures that apply to your desired transaction the subscription agent may, depending on the circumstances, reject your subscription or accept it to the extent of the payment received. Neither we nor our subscription agent undertakes to contact you concerning, or attempt to correct, an incomplete or incorrect subscription form or payment. We have the sole discretion to determine whether a subscription exercise properly follows the subscription procedures.

If you use a personal check to pay for the shares, it may not clear in time.

Any personal check used to pay for shares must clear prior to the expiration date, and the clearing process may require seven or more business days. If you wish to pay the subscription price by uncertified personal check, we urge you to make payment sufficiently in advance of the time the rights offering expires to ensure that your payment is received and clears by that time.

Risks Related to Our Common Stock Generally

Due to the current market price of our common stock, in conjunction with the fact that we are a relatively small company with a history of operating losses, the future trading market for our stock may not be active on a consistent basis, which may make it difficult for you to sell your shares.

The trading volume of our stock in the future depends in part on our ability to increase our revenue and reduce or eliminate our operating losses, which should increase the attractiveness of our stock as an investment, thereby leading to a more liquid market for our stock on a consistent basis. If we are unable to achieve these goals, the trading market for our stock may be negatively affected, which may make it difficult for you to sell your shares. In addition, we have recently moved from The American Stock Exchange to the OTC Bulletin Board because we no longer meet AMEX listing criteria. Our move to the OTC Bulletin Board may result in reduced liquidity and increased volatility for our stock. If an active and liquid trading market does not exist for our common stock, you may have difficulty selling your shares.

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Due to the move from The American Stock Exchange to the OTC Bulletin Board, holders of our common stock no longer have certain approval rights available under the AMEX Rules.

The American Stock Exchange has rules which listed companies must comply with. Among other things, the AMEX Rules require shareholder approval as a prerequisite to approving applications to list additional shares to be issued in connection with certain transactions. For example, AMEX Rule 713 requires shareholder approval if a company issues shares equal to or greater than 20% of its currently outstanding shares, if such issuance is at a price below the greater of book or market value of the shares. Although we are subject to the Delaware General Corporation Law, it is less restrictive and does not require stockholder approval of such a transaction. Accordingly, now that our stock is no longer listed on the AMEX, we may issue shares for less than the greater of book or market value and take certain other actions without stockholder approval which we could not have taken without stockholder approval when our common stock was listed on AMEX.

Due to the concentration of holdings of our stock, a limited number of investors may be able to control matters requiring common stockholder approval or could cause our stock price to decline through future sales because they beneficially own a large percentage of our common stock.

There were 50,093,527 shares of our common stock outstanding as of January 24, 2007, of which the PIPE Investors (a total of 17 investors) and The Parke Family Trust beneficially own in the aggregate approximately 90%. As a result of their significant ownership, these investors may have the ability to exercise a controlling influence over our business and corporate actions requiring stockholder approval, including the election of our directors, a sale of substantially all of our assets, a merger between us and another entity or an amendment to our certificate of incorporation. This concentration of ownership could delay, defer or prevent a change of control and could adversely affect the price investors might be willing to pay in the future for shares of our common stock. Also, in the event of a sale of our business, these investors could be able to seek to receive a control premium to the exclusion of other common stockholders.

A significant percentage of the outstanding shares of our common stock, including the shares beneficially owned by these holders, can be sold in the public market from time to time, subject to limitations imposed by Federal securities laws. The market price of our common stock could decline as a result of sales of a large number of our presently outstanding shares of common stock by these investors or other stockholders in the public market or due to the perception that these sales could occur. This could also make it more difficult for us to raise funds through future offerings of our equity securities or for you to sell your shares if you choose to do so.

The large concentration of our shares held by this small group of shareholders could result in increased volatility in our stock price due to the limited number of shares available in the market.

Provisions of our charter and by-laws, in particular our blank check preferred stock, could discourage an acquisition of our company that would benefit our stockholders.

Provisions of our charter and by-laws may make it more difficult for a third party to acquire control of our company, even if a change in control would benefit our stockholders. In particular, shares of our preferred stock may be issued in the future without further stockholder approval and upon those terms and conditions, and having those rights, privileges and preferences, as our Board of Directors may determine. In the past, we have issued preferred stock with dividend and liquidation preferences over our common stock, and with certain approval rights not accorded to our common stock, and which was convertible into shares of our common stock at a price lower than the market price of our common stock. The rights of the holders of our common stock will be subject to, and may be adversely affected by, the rights of the holders of any preferred stock we may issue in the future. The issuance of our preferred stock, while providing desirable flexibility in pursuing possible additional equity financings and other corporate

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purposes, could have the effect of making it more difficult for a third party to acquire control of us. This could limit the price that certain investors might be willing to pay in the future for shares of our common stock and discourage these investors from acquiring a majority of our common stock. In addition, the price that future investors may be willing to pay for our common stock may be lower due to the conversion price and exercise price granted to investors in any such private financing.

We do not intend to pay dividends on shares of our common stock in the foreseeable future.

We currently expect to retain our future earnings, if any, for use in the operation and expansion of our business. We do not anticipate paying any cash dividends on shares of our common stock in the foreseeable future.

Compliance with changing regulation of corporate governance and public disclosure may result in additional expenses.

Changing laws, regulations and standards relating to corporate governance and public disclosure, including the Sarbanes-Oxley Act of 2002, are creating uncertainty for companies such as ours. We are committed to maintaining high standards of corporate governance and public disclosure. As a result, we intend to invest reasonably necessary resources to comply with evolving standards, and this investment may result in increased general and administrative expenses and a diversion of management time and attention from revenue-generating activities to compliance activities, which could harm our business prospects.

USE OF PROCEEDS

The proceeds from the rights offering will be used for general corporate purposes. We are also continuously seeking to acquire or invest in businesses, products and technologies that we believe are complementary to our own, thus may use a portion of the proceeds for this purpose if such an opportunity arises. Pending these uses, the net proceeds will be invested in investment-grade, interest-bearing securities.

CAPITALIZATION

As of September 30, 2006, we had cash of \$6,825,874, total stockholders' equity of \$21,136,866 and total capitalization of \$21,867,717. If holders of 10,000,000 subscription rights were to exercise their rights our cash, total stockholders' equity and total capitalization would all increase by \$10,000,000, to \$16,825,874, \$31,136,866 and \$31,867,717, respectively.

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THE RIGHTS OFFERING

Reasons for the Rights Offering

The rights offering is being made to raise equity capital in a cost-effective manner and to offer our common stockholders an opportunity to reduce the dilution they sustained as a result of the recently completed PIPE Transaction, Series E Conversion and Parke acquisition through the purchase of shares of our common stock at the same per share price paid by the PIPE Investors and used as the common stock value for the Parke acquisition and the Series E Conversion.

The Rights

We will distribute to each holder of our common stock who is a record holder of our common stock (except the members of the Excluded Group, who have all waived their rights to receive subscription rights in the rights offering in order to maximize the number of shares available for purchase by other stockholders) on the record date, which is ___, 2007, at no charge, five non-transferable subscription rights for each share of common stock owned, for a total of 38,825,160 subscription rights. The subscription rights will be evidenced by non-transferable subscription rights certificates. Each subscription right will allow you to purchase one share of our common stock at a price of \$1.00 per share. Stockholders who elect to exercise their basic subscription privilege in full may also subscribe, at the subscription price, for additional shares of our common stock under their respective over-subscription privileges to the extent that other rights holders do not exercise their basic subscription privileges in full. The total shares issuable pursuant to the over-subscription privilege shall be limited the number of shares that are not subscribed to by other rights holders. If a sufficient number of shares of our common stock is unavailable to fully satisfy the over-subscription privilege requests, the available shares of common stock will be sold pro rata among subscription rights holders who exercised their over-subscription privilege based on the number of shares each subscription rights holder subscribed for under the basic subscription privilege. If you hold your shares in a brokerage account or through a dealer or other nominee, please see the information included below the heading Beneficial Owners.

Expiration of the Rights Offering and Extensions, Amendments and Termination

You may exercise your subscription rights at any time prior to 5:00 p.m., New York City time, on ___, 2007, the expiration date for the rights offering. We may, in our sole discretion, extend the time for exercising the subscription rights. If the commencement of the rights offering is delayed for a period of time, the expiration date of the rights offering may be similarly extended. We will extend the duration of the rights offering if required by applicable law, and may choose to extend it if we decide that changes in the market price of our common stock warrant an extension or if we decide to give investors more time to exercise their subscription rights in the rights offering. We may extend the expiration date of the rights offering by giving oral or written notice to the subscription agent on or before the scheduled expiration date. If we elect to extend the expiration of the rights offering, we will issue a press release announcing such extension no later than 9:00 a.m., New York City time, on the next business day after the most recently announced expiration date.

We reserve the right, in our sole discretion, to amend or modify the terms of the rights offering. If you do not exercise your subscription rights before the expiration date of the rights offering, your unexercised subscription rights will be null and void of no value. We will not be obligated to honor your exercise of subscription rights if the subscription agent receives the documents relating to your exercise after the rights offering expires, regardless of when you transmitted the documents, except if you have timely transmitted the documents under the guaranteed delivery procedures described below.

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Subscription Privileges

Your subscription rights entitle you to a basic subscription privilege and an over-subscription privilege.

Basic Subscription Privilege. With your basic subscription privilege you may purchase one share of our common stock per subscription right, upon delivery of the required documents and payment of the subscription price of \$1.00 per share. You are not required to exercise all of your subscription rights unless you wish to purchase shares under your over-subscription privilege. We will deliver to the record holders who purchase shares in the rights offering certificates representing the shares purchased with a holder's basic subscription privilege as soon as practicable after the rights offering has expired.

Over-Subscription Privilege. In addition, if you exercise your basic subscription privilege in full you may subscribe for additional shares of our common stock at the same cash price of \$1.00 per share for shares of common stock that are not purchased by other rights holders pursuant to their basic subscription privilege (the Excess Shares). To subscribe for additional shares you must properly complete the required documents and pay the subscription price of \$1.00 per share before the expiration of the rights offering. Excess Shares will be allocated as follows:

on a pro rata basis among those that fully exercised their basic subscription rights and have subscribed for additional shares pursuant to their over-subscription privilege (the Initial Allocation). In this instance pro rata means in proportion to the number of shares of our common stock that you and the other subscribers for Excess Shares have purchased by exercising your and their basic subscription privileges. This Initial Allocation may result in you receiving fewer shares than you requested pursuant to your over-subscription privilege. If the Initial Allocation results in you receiving an allocation of a greater number of shares than you subscribed for under your over-subscription privilege, we will allocate to you only the number of shares for which you subscribed; and

if, following the Initial Allocation there remain any unfilled requests for additional shares pursuant to over-subscription privileges, we will allocate any remaining Excess Shares to the holders of the unfilled requests on a pro rata basis, in proportion to their unfilled requests (such allocation shall be referred to as the Secondary Allocation).

Full Exercise of Basic Subscription Privilege. You may exercise your over-subscription privilege only if you exercise your basic subscription privilege in full. To determine if you have fully exercised your basic subscription privilege, we will consider only the basic subscription privileges held by you in the same capacity. For example, suppose that you were granted subscription rights for shares of our common stock that you own individually and shares of our common stock that you own collectively with your spouse. If you wish to exercise your over-subscription privilege with respect to the subscription rights you own individually, but not with respect to the subscription rights you own collectively with your spouse, you only need to fully exercise your basic subscription privilege with respect to your individually owned subscription rights. You do not have to subscribe for any shares under the basic subscription privilege owned collectively with your spouse to exercise your individual over-subscription privilege.

When you complete the portion of your subscription rights certificate to exercise your over-subscription privilege, you will be representing and certifying that you have fully exercised your subscription privileges as to shares of our common stock that you hold in that capacity. You must exercise your over-subscription privilege at the same time you exercise your basic subscription privilege in full.

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Return of Excess Payment. If you exercised your over-subscription privilege and are allocated less than all of the shares of our common stock for which you wished to subscribe, your excess payment for shares that were not allocated to you will be returned to you by mail, without interest or deduction, as soon as practicable after the expiration date of the rights offering. We will deliver to the record holders who purchase shares in the rights offering certificates representing the shares of our common stock that they purchased as soon as practicable after the expiration date of the rights offering and after all pro rata allocations and adjustments have been completed.

Conditions to the Rights Offering

We may terminate the rights offering, in whole or in part, if at any time before completion of the rights offering there is any judgment, order, decree, injunction, statute, law or regulation entered, enacted, amended or held to be applicable to the rights offering that in the sole judgment of our board of directors would or might make the rights offering or its completion, whether in whole or in part, illegal or otherwise restrict or prohibit completion of the rights offering. We may waive any of these conditions and choose to proceed with the rights offering even if one or more of these events occur. If we terminate the rights offering, in whole or in part, all affected subscription rights will expire without value and all subscription payments received by the subscription agent will be returned promptly, without interest or deduction. See also Cancellation Rights.

Method of Subscription Exercise of Rights

You may exercise your subscription rights by delivering the following to the subscription agent, prior to 5:00 p.m., New York City time, on ____, 2007, the expiration date of the rights offering:

Your properly completed and executed subscription rights certificate with any required signature guarantees or other supplemental documentation; and

Your full subscription price payment for each share subscribed for under your subscription privileges.

If you are a beneficial owner of shares of our common stock whose shares are registered in the name of a broker, custodian bank or other nominee, you should instruct your broker, custodian bank or other nominee to exercise your rights and deliver all documents and payment on your behalf prior to 5:00 p.m. New York City time on ____, 2007, the expiration date of the rights offering.

Your subscription rights will not be considered exercised unless the subscription agent receives from you, your broker, custodian or nominee, as the case may be, all of the required documents and your full subscription price payment prior to 5:00 p.m., New York City time, on ____, 2007, the expiration date of the rights offering.

Method of Payment

Your payment of the subscription price must be made in United States dollars for the full number of shares of common stock for which you are subscribing by check or bank draft drawn upon a United States bank, or by postal, telegraphic or express money order, payable to the subscription agent.

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Receipt of Payment

Your payment will be considered received by the subscription agent only upon:
Clearance of any uncertified check;

Receipt by the subscription agent of any certified check or bank draft drawn upon a United States bank or of any postal, telegraphic or express money order payable to the subscription agent; or

Receipt of collected funds in the subscription account designated above.

Clearance of Uncertified Checks

If you are paying by uncertified personal check, please note that uncertified checks may take seven to ten business days to clear. If you wish to pay the subscription price by uncertified personal check, we urge you to make payment sufficiently in advance of the time the rights offering expires to ensure that your payment is received by the subscription agent and clears by the rights offering expiration date. We urge you to consider using a certified or cashier's check, money order or wire transfer of funds to avoid missing the opportunity to exercise your subscription rights should you decide to exercise your subscription rights.

Delivery of Subscription Materials and Payment

You should deliver your subscription rights certificate and payment of the subscription price or, if applicable, notice of guaranteed delivery, to the subscription agent by one of the methods described below:

By Mail, Overnight Courier or by Hand:

LaSalle Bank N.A.
135 S. LaSalle Street
Suite 1811
Chicago, IL 60603-4298

Your delivery to an address or by any method other than as set forth above will not constitute valid delivery.

Calculation of Subscription Rights Exercised

If you do not indicate the number of subscription rights being exercised, or do not forward full payment of the total subscription price payment for the number of subscription rights that you indicate are being exercised, then you will be deemed to have exercised your basic subscription privilege with respect to the maximum number of subscription rights that may be exercised with the aggregate subscription price payment you delivered to the subscription agent. If your aggregate subscription price payment is greater than the amount you owe for your subscription, you will be deemed to have exercised your over-subscription privilege to purchase the maximum number of shares of our common stock with your over-payment. If we do not apply your full subscription price payment to your purchase of shares of our common stock, we or the subscription agent will return the excess amount to you by mail, without interest or deduction, as soon as practicable after the expiration date of the rights offering.

Your Funds will be Held by the Subscription Agent Until Shares of Our Common Stock are Issued

The subscription agent will hold your payment of the subscription price in a segregated account with other payments received from other subscription rights holders until we issue your shares of our common stock to you upon consummation of the rights offering.

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Medallion Guarantee May be Required

Your signature on each subscription rights certificate must be guaranteed by an eligible institution, such as a member firm of a registered national securities exchange or a member of the National Association of Securities Dealers, Inc., or a commercial bank or trust company having an office or correspondent in the United States, subject to standards and procedures adopted by the subscription agent, unless:

Your subscription rights certificate provides that shares are to be delivered to you as record holder of those subscription rights; or

You are an eligible institution.

Notice to Beneficial Holders

If you are a broker, a trustee or a depository for securities who holds shares of our common stock for the account of others on ____, 2007, the record date, you should notify the respective beneficial owners of such shares of the rights offering as soon as possible to find out their intentions with respect to exercising their subscription rights. You should obtain instructions from the beneficial owners with respect to their subscription rights, as set forth in the instructions we have provided to you for your distribution to beneficial owners. If a beneficial owner so instructs, you should complete the appropriate subscription rights certificates and submit them to the subscription agent with the proper payment. If you hold shares of our common stock for the account(s) of more than one beneficial owner, you may exercise the number of subscription rights to which all such beneficial owners in the aggregate otherwise would have been entitled had they been direct record holders of our common stock on the record date, provided that you, as a nominee record holder, make a proper showing to the subscription agent by submitting the form entitled Nominee Holder Certification that we will provide to you with your rights offering materials. If you did not receive this form, you should contact the subscription agent to request a copy.

Beneficial Owners

If you are a beneficial owner of shares of our common stock or will receive your subscription rights through a broker, custodian bank or other nominee, we will ask your broker, custodian bank or other nominee to notify you of the rights offering. If you wish to exercise your subscription rights, you will need to have your broker, custodian bank or other nominee act for you. If you hold certificates of our common stock directly and would prefer to have your broker, custodian bank or other nominee act for you, you should contact your nominee and request it to effect the transactions for you. To indicate your decision with respect to your subscription rights, you should complete and return to your broker, custodian bank or other nominee the form entitled Beneficial Owners Election Form. You should receive this form from your broker, custodian bank or other nominee with the other rights offering materials. If you wish to obtain a separate subscription rights certificate, you should contact the nominee as soon as possible and request that a separate subscription rights certificate be issued to you. You should contact your broker, custodian bank or other nominee if you do not receive this form but you believe you are entitled to participate in the rights offering. We are not responsible if you do not receive the form from your broker, custodian bank or nominee or if you receive it without sufficient time to respond.

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Instructions for Completing Your Subscription Rights Certificate

You should read and follow the instructions accompanying the subscription rights certificates carefully. You are responsible for the method of delivery of your subscription rights certificate(s) with your subscription price payment to the subscription agent. If you send your subscription rights certificate(s) and subscription price payment by mail, we recommend that you send them by registered mail, properly insured, with return receipt requested. You should allow a sufficient number of days to ensure delivery to the subscription agent prior to the time the rights offering expires. Because uncertified personal checks may take seven to ten business days to clear, you are strongly urged to pay, or arrange for payment, by means of a certified or cashier's check, money order or wire transfer of funds.

Determinations Regarding the Exercise of Your Subscription Rights

We will decide all questions concerning the timeliness, validity, form and eligibility of the exercise of your subscription rights and any such determinations by us will be final and binding. We, in our sole discretion, may waive, in any particular instance, any defect or irregularity, or permit, in any particular instance, a defect or irregularity to be corrected within such time as we may determine. We will not be required to make uniform determinations in all cases. We may reject the exercise of any of your subscription rights because of any defect or irregularity. We will not accept any exercise of subscription rights until all irregularities have been waived by us or cured by you within such time as we decide, in our sole discretion.

Neither we, nor the subscription agent, will be under any duty to notify you of any defect or irregularity in connection with your submission of subscription rights certificates and we will not be liable for failure to notify you of any defect or irregularity. We reserve the right to reject your exercise of subscription rights if your exercise is not in accordance with the terms of the rights offering or in proper form. We will also not accept the exercise of your subscription rights if our issuance of shares of our common stock to you could be deemed unlawful under applicable law.

Regulatory Limitation

We will not be required to issue to you shares of our common stock pursuant to the rights offering if, in our opinion, you would be required to obtain prior clearance or approval from any state or federal regulatory authorities to own or control such shares if, at the time the rights offering expires, you have not obtained such clearance or approval.

Guaranteed Delivery Procedures

If you wish to exercise your subscription rights, but you do not have sufficient time to deliver the subscription rights certificate evidencing your subscription rights to the subscription agent on or before the time the rights offering expires, you may exercise your subscription rights by the following guaranteed delivery procedures:

Deliver to the subscription agent prior to the rights offering expiration date your subscription price payment in full for each share you subscribed for under your subscription privileges in the manner set forth above in Method of Payment ;

Deliver to the subscription agent prior to the expiration date the form entitled Notice of Guaranteed Delivery, substantially in the form provided with the Instructions as to Use of Lime Energy Co. Subscription Rights Certificates distributed with your subscription rights certificate; and

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Deliver the properly completed subscription rights certificate evidencing your subscription rights being exercised and the related nominee holder certification, if applicable, with any required signature guarantee, to the subscription agent within three (3) business days following the date of your Notice of Guaranteed Delivery.

Your Notice of Guaranteed Delivery must be delivered in substantially the same form provided with the Instructions as to the Use of Lime Energy Co. Subscription Rights Certificates, which have been distributed to you with your subscription rights certificate. Your Notice of Guaranteed Delivery must come from an eligible institution, or other eligible guarantee institution, that is a members of, or a participant in, a signature guarantee program acceptable to the subscription agent.

In your Notice of Guaranteed Delivery, you must state:

Your name;

The number of subscription rights represented by your subscription rights certificate(s), the number of shares of our common stock for which you are subscribing under your basic subscription privilege and the number of shares of our common stock for which you are subscribing under your over-subscription privilege, if any; and

Your guarantee that you will deliver to the subscription agent any subscription rights certificates evidencing the subscription rights you are exercising within three (3) business days following the date the subscription agent receives your Notice of Guaranteed Delivery.

You may deliver your Notice of Guaranteed Delivery to the subscription agent in the same manner as your subscription rights certificates at the address set forth above under Delivery of Subscription Materials and Payment. You may alternatively transmit your Notice of Guaranteed Delivery to the subscription agent by facsimile transmission (Fax No.: 312-904-2079). To confirm facsimile deliveries, you may call 312-904-5761.

The subscription agent will send you additional copies of the form of Notice of Guaranteed Delivery if you request them. Please call 312-904-5761 to request any copies of the form of Notice of Guaranteed Delivery.

Questions About Exercising Subscription Rights

If you have any questions or require assistance regarding the method of exercising your subscription rights or requests for additional copies of this document, the Instructions as to the Use of Lime Energy Co. Subscription Rights Certificates or the Notice of Guaranteed Delivery, you should contact the subscription agent at the address and telephone number set forth above under Questions and Answers About the Rights Offering included elsewhere in this document.

Subscription Agent

We have appointed LaSalle Bank N.A. to act as subscription agent for the rights offering. We will pay all fees and expenses of the subscription agent related to the rights offering and have also agreed to indemnify the subscription agent from liabilities that it may incur in connection with the rights offering.

No Revocation

Once you have exercised your subscription privileges, you may not revoke your exercise. Subscription rights not exercised prior to the expiration date of the rights offering will expire and will have no value.

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Procedures for DTC Participants

We expect that the exercise of your basic subscription privilege and your over-subscription privilege may be made through the facilities of the Depository Trust Company (DTC). If your subscription rights are held of record through DTC, you may exercise your basic subscription privilege and your over-subscription privilege by instructing DTC to transfer your subscription rights from your account to the account of the subscription agent, together with certification as to the aggregate number of subscription rights you are exercising and the number of shares of our common stock you are subscribing for under your basic subscription privilege and your over-subscription privilege, if any, and your subscription price payment for each share of our common stock that you subscribed for pursuant to your basic subscription privilege and your over-subscription privilege.

Subscription Price

The subscription price is \$1.00 per share. For more information with respect to how the subscription price was determined, see Questions and Answers About the Rights Offering included elsewhere in this document.

Foreign and Other Stockholders

We will not mail subscription rights certificates to stockholders on the record date, or to subsequent transferees, whose addresses are outside the United States. Instead, we will have the subscription agent hold the subscription rights certificates for those holders' accounts. To exercise its subscription rights, a foreign holder must notify the subscription agent before 11:00 a.m., New York City time, on ____, 2007, three business days prior to the expiration date, and must establish to the satisfaction of the subscription agent that it is permitted to exercise its subscription rights under applicable law. If these procedures are not followed prior to the expiration date and you are a foreign holder, your rights will expire.

Non-Transferability of the Rights

Except in the limited circumstances described below, only you may exercise the basic subscription privilege and the over-subscription privilege. You may not sell, give away or otherwise transfer the basic subscription privilege or the over-subscription privilege. Notwithstanding the foregoing, your rights may be transferred by operation of law; for example a transfer of rights to the estate of the recipient upon the death of the recipient would be permitted. If the rights are transferred as permitted, evidence satisfactory to us that the transfer was proper must be received by us prior to the expiration date of the rights offering.

Cancellation Rights

Our board of directors may cancel the rights offering, in whole or in part, in its sole discretion at any time prior to the time the rights offering expires for any reason (including a change in the market price of our common stock). If we cancel the rights offering, any funds you paid to the subscription agent will be promptly refunded, without interest or deduction.

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No Board Recommendation

An investment in shares of our common stock must be made according to each investor's evaluation of its own best interests and after considering all of the information herein, including the Risk Factors section of this document. Neither we nor our board of directors nor their financial advisors make any recommendation to subscription rights holders regarding whether they should exercise their subscription rights. In addition, you should not rely on the decision of the PIPE Investors (which included three of our directors) to purchase shares of common stock at a price equal to the subscription price, or the decision of Dan Parke, another of our directors, when selling Parke to us to accept the consideration which included \$5.0 million of common stock valued at a price per share equal to the subscription price, to be a recommendation or an indication that the subscription price is reflective of our value.

Shares of Common Stock Outstanding After the Rights Offering

Based on the 50,093,527 shares of our common stock currently outstanding, and the potential that we may issue as many as 38,825,160 shares pursuant to this rights offering, 88,918,687 shares of our common stock may be issued and outstanding following the rights offering, an increase in the number of outstanding shares of our common stock of approximately 78%.

Other Matters

We are not making the rights offering in any state or other jurisdiction in which it is unlawful to do so, nor are we distributing or accepting any offers to purchase any shares of our common stock from subscription rights holders who are residents of those states or of other jurisdictions or who are otherwise prohibited by federal or state laws or regulations to accept or exercise the subscription rights. We may delay the commencement of the rights offering in those states or other jurisdictions, or change the terms of the rights offering, in whole or in part, in order to comply with the securities laws or other legal requirements of those states or other jurisdictions. We may decline to make modifications to the terms of the rights offering requested by those states or other jurisdictions, in which case, if you are a resident in one of those states or jurisdictions or if you are otherwise prohibited by federal or state laws or regulations from accepting or exercising the subscription rights you will not be eligible to participate in the rights offering.

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MATERIAL UNITED STATES FEDERAL INCOME TAX CONSEQUENCES

The following discussion is a summary of the material United States Federal income tax consequences of the rights offering to holders of our common stock. This discussion assumes that the holders of our common stock hold such common stock as a capital asset for United States Federal income tax purposes. This discussion is based on the Internal Revenue Code of 1986, as amended, Treasury Regulations promulgated thereunder, Internal Revenue Service rulings and pronouncements and judicial decisions in effect on the date hereof, all of which are subject to change (possibly with retroactive effect) and to differing interpretations. This discussion applies only to holders that are United States persons and does not address all aspects of United States federal income taxation that may be relevant to holders in light of their particular circumstances or to holders who may be subject to special tax treatment under the Internal Revenue Code, including, without limitation, holders who are dealers in securities or foreign currency, foreign persons, insurance companies, tax-exempt organizations, banks, financial institutions, broker-dealers, holders who hold our common stock as part of a hedge, straddle, conversion or other risk reduction transaction, or who acquired our common stock pursuant to the exercise of compensatory stock options or otherwise as compensation.

We have not sought, and will not seek, an opinion of counsel or a ruling from the Internal Revenue Service regarding the United States Federal income tax consequences of the rights offering or the related share issuance. The following summary does not address the tax consequences of the rights offering or the related share issuance under foreign, state, or local tax laws. **ACCORDINGLY, EACH HOLDER OF OUR COMMON STOCK SHOULD CONSULT ITS TAX ADVISOR WITH RESPECT TO THE PARTICULAR TAX CONSEQUENCES OF THE RIGHTS OFFERING AND THE RELATED SHARE ISSUANCE TO SUCH HOLDER.**

The United States Federal income tax consequences to a holder of our common stock of the receipt and exercise of subscription rights under the rights offering should be as follows:

1. A holder should not recognize taxable income for United States Federal income tax purposes in connection with the receipt of subscription rights in the rights offering.
2. Except as provided in the following sentence, a holder's tax basis in the subscription rights received in the rights offering should be zero. If either (i) the fair market value of the subscription rights on the date such subscription rights are distributed is equal to at least 15% of the fair market value on such date of the common stock with respect to which the subscription rights are received or (ii) the holder elects, in its United States Federal income tax return for the taxable year in which the subscription rights are received, to allocate part of its tax basis in such common stock to the subscription rights, then upon exercise or transfer of the subscription rights, the holder's tax basis in the common stock should be allocated between the common stock and the subscription rights in proportion to their respective fair market values on the date the subscription rights are distributed. A holder's holding period for the subscription rights received in the rights offering should include the holder's holding period for the common stock with respect to which the subscription rights were received.
3. A holder which allows the subscription rights received in the rights offering to expire should not recognize any gain or loss, and the tax basis in the common stock owned by such holder with respect to which such subscription rights were distributed should be equal to the tax basis in such common stock immediately before the receipt of the subscription rights in the rights offering.
4. A holder should not recognize any gain or loss upon the exercise of the subscription rights received in the rights offering. The tax basis in the common stock acquired through exercise of the subscription rights should equal the sum of the subscription price for the common stock and the holder's tax basis, if any, in the rights as described above. The holding period for the common stock acquired through exercise of the subscription rights should begin on the date the subscription rights are exercised.

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PLAN OF DISTRIBUTION

We are making this rights offering directly to you, the holders of our common stock, on a pro rata basis for each share of our common stock held at the close of business on ____, 2007, the record date for this rights offering. The members of the Excluded Group have all waived their rights to participate in the rights offering in order to maximize the number of shares available for purchase by other stockholders.

We will pay LaSalle Bank N.A., the subscription agent, a fee of approximately \$6,000 for its services in connection with this rights offering (which includes the subscription agent's fees associated with the exercise of rights). We have also agreed to reimburse LaSalle Bank N.A., the subscription agent, its reasonable expenses and indemnify it from liabilities it may incur in connection with the rights offering.

We estimate that our total expenses in connection with the rights offering, including registration, legal and accounting fees, will be approximately \$100,000.

We have not employed any brokers, dealers or underwriters in connection with the solicitation or exercise of rights. Except as described in this section, we are not paying any other commissions, fees or discounts in connection with the rights offering. Some of our employees may solicit responses from you as a holder of rights, but we will not pay our employees any commissions or compensation for such services other than their normal employment compensation.

LEGAL PROCEEDINGS

From time to time, the Company has been a party to pending or threatened legal proceedings and arbitrations that are routine and incidental to its business. Based upon information presently available, and in light of legal and other defenses available to the Company, management does not consider the liability from any threatened or pending litigation to be material to the Company.

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The table below shows certain information about our directors, executive officers and significant employees:

Name	Age	Principal Positions
David R. Asplund	48	Chief Executive Officer and Director
Gregory T. Barnum	51	Director (1)
William R. Carey, Jr.	59	Director (1)(3)
Richard P. Kiphart	65	Director (2)(3)
Jeffrey R. Mistarz	48	Executive Vice President, Chief Financial Officer, Treasurer and Secretary
Daniel W. Parke	51	President, Chief Operating Officer, President Parke Industries and Director
Gerald A. Pientka	50	Director (2)(3)
Leonard Pisano	44	Executive Vice President, President of Maximum Performance Group
David W. Valentine	37	Director (1)(2)

(1) Member of our Audit Committee.

(2) Member of our Compensation Committee.

(3) Member of our Governance and Nominating Committee.

Our Board of Directors is currently authorized for a membership of twelve directors. As of January 24, 2007, our Board of Directors had five vacancies.

David R. Asplund has been one of our directors since June 2002 and has been our Chief Executive Officer since January 2006. Mr. Asplund has a degree in mechanical engineering from the University of Minnesota. Prior to becoming CEO of Lime Energy, Mr. Asplund was president of Delano Group Securities, LLC, an investment banking firm in Chicago, Illinois, which he founded in 1999 and continues to own. Mr. Asplund also serves on the board of Agenet, Inc.

Gregory T. Barnum has been one of our directors since March 2006. Mr. Barnum is currently the vice president of finance and chief financial officer of Datalink Corporation, an information storage architect. Prior to joining Datalink in March 2006, Mr. Barnum was the vice president of finance, chief financial officer and corporate secretary of Computer Network Technology Corporation. From September 1992 to July 1997, Mr. Barnum served as senior vice president of finance and administration, chief financial officer and corporate secretary at Tricord Systems, Inc., a manufacturer of enterprise servers. From May 1988 to September 1992, Mr. Barnum served as the executive vice president, finance, chief financial officer, treasurer and corporate secretary for Cray Computer Corporation, a development stage company engaged in the design of supercomputers. Prior to that time, Mr. Barnum served in various accounting and financial management capacities for Cray Research, Inc., a manufacturer of supercomputers. Mr. Barnum is a Certified Public Accountant and a member of the American Institute of Certified Public Accountants.

William R. (Max) Carey has been one of our directors since March 2006. Mr. Carey is the chairman and founder of Corporate Resource Development, a sales and marketing consulting firm he founded in 1981. He is also a managing director of Entrepreneur Equity Corporation, an insurance broker that creates specialty products for middle market companies. Mr. Carey also serves on the boards of Outback Steakhouse Inc., Kforce, Inc., Crosswalk.com and

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Richard P. Kiphart has been one of our directors since January 2006, when he also became chairman of our board of directors. Mr Kiphart is the head of the Corporate Finance Department and a Principal of William Blair & Company, an investment firm. In addition, Mr. Kiphart currently serves as a member of the board of directors of First Data Corp., and previously served on the Concord EFS board of directors from 1997 until 2004 and was chairman of the Concord board of directors from February 2003 until March 2004. Mr. Kiphart is also currently a director of SAFLINK Corporation, Advanced Biotherapy, Inc. and Nature Vision, Inc. In addition he is the former chairman of the Merit Music School, is the president and chief executive officer of the Lyric Opera of Chicago, and the vice chairman of the Erikson Institute. He also serves on the board of DATA (Debt AIDS Trade Africa). Mr. Kiphart is the father in-law of David Valentine, one of our directors.

Jeffrey R. Mizarz has been our Chief Financial Officer since January 2000, our treasurer since October 2000, an executive vice president since November 2002 and our assistant secretary/secretary since February 2003. From January 1994 until joining us, Mr. Mizarz served as chief financial officer for Nucon Corporation, a privately held manufacturer of material handling products and systems, responsible for all areas of finance and accounting, managing capital and stockholder relations. Prior to joining Nucon, Mr. Mizarz was with First Chicago Corporation (now JPMorgan Chase & Co.) for 12 years where he held several positions in corporate lending, investment banking and credit strategy.

Daniel W. Parke has been our President and Chief Operating Officer since we acquired Parke P.A.N.D.A. Corporation, which he owned and served as its president from its founding in 2001. In addition to serving as our President and Chief Operating Officer, Mr. Parke continues to serve as the president of Parke, which is now named Parke Industries LLC. Mr. Parke was previously a founder of Parke Industries, Inc., an energy solutions provider which was acquired in February 1998 by Strategic Resource Solutions, an unregulated subsidiary of Carolina Power & Light.

Gerald A. Pientka has been one of our directors since May 2000. Mr. Pientka is currently, and has been since February 2006 the executive vice president of development for First Industrial Realty Trust, Inc. From September 2003 to February 2006 he was the founder and principal of Verus Partners, a real estate development company located in Chicago, Illinois. Prior to this, from May 1999 through March 2003, Mr. Pientka was president of Higgins Development Partners, LLC (the successor to Walsh, Higgins & Company), a national real estate development company controlled by the Pritzker family interests. From May 1992 until May 1999, Mr. Pientka served as president of Walsh, Higgins & Company. Mr. Pientka is also a member of Leaf Mountain Company, LLC. Mr. Pientka is also board president of Christopher House, a Chicago-based social services agency.

Leonard Pisano has been our executive vice president of sales since June 7, 2006, prior to this, from May 3, 2005, the date we acquired Maximum Performance Group, Inc., he served as our Chief Operating Officer. He is also Maximum Performance Group's president and has been from its founding in February 2003. Prior to that, Mr. Pisano founded Maximum Energy Services in early 2001 and served as its president until it merged with Pentech Solutions to form Maximum Performance Group in February 2003. During his career, Mr. Pisano has held various senior management positions at companies within the energy services sector, including Parke Industries Inc. and SRS, a division of Carolina Power and Light. Prior to entering the energy services sector, Mr. Pisano spent ten years in facilities management at New York University, leaving NYU in 1996 when he was Director of Facilities.

David W. Valentine has been one of our directors since May 2004. Mr. Valentine is currently a senior investment professional of a private investment firm. Prior to taking his current position, Mr. Valentine was the Global Head of Debt Private Placements at UBS Investment Bank where he had been a Director of Leveraged Finance. Before joining UBS, Mr. Valentine held various investment banking positions at Nesbitt Burns Securities Inc. and ABN Amro Chicago Corporation. Mr. Valentine is the son in-law of Richard Kiphart, our chairman.

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DESCRIPTION OF SECURITIES

In the following summary, we describe the material terms of our capital stock by summarizing material provisions of our charter and by-laws. We have incorporated by reference these organizational documents as exhibits to the registration statement of which this prospectus is a part.

General

As of January 24, 2007, we had 200,000,000 authorized shares of common stock, par value \$.0001 per share, and 5,000,000 shares of authorized preferred stock, par value \$.01 per share, of which:

50,093,527 shares are issued and outstanding (excluding the escrow shares described below);

166,149 shares of common stock were being held in escrow for the benefit of the selling shareholders of Maximum Performance Group (MPG) to be released over the two year period following the purchase of MPG (May 3, 2005) if it achieves certain revenue targets during the period. Any shares not issued to the selling shareholders will be returned to the Company at the end of the two year period. To date, no shares have been released from such Escrow.

1,125,869 shares of common stock are issuable upon exercise of outstanding common stock warrants;

10,959,604 shares of common stock are issuable upon exercise of outstanding stock options; and

No shares of preferred stock or other rights or options, warrants to acquire preferred stock are outstanding.

Common Stock

Holders of our common stock are entitled to one vote per share on all matters submitted to a vote of our stockholders and will share ratably on a per share basis in any dividends declared on our common stock. Holders of our common stock have no preemptive, subscription, redemption or conversion rights. Upon our liquidation, dissolution or winding up and after payment of all prior claims, the holders of shares of common stock would share ratably on a per share basis in all of our assets. All shares of common stock currently outstanding are fully paid and nonassessable. Any shares of common stock which the selling stockholders acquire through exercise of their warrants will also be fully paid and nonassessable.

Preferred Stock

Our board of directors, without further stockholder approval, may authorize the issuance of preferred stock in one or more series from time to time and fix or alter the designations, relative rights, priorities, preferences, qualifications, limitations and restrictions of the shares of each series. The rights, preferences, limitations and restrictions of different series of preferred stock may differ with respect to dividend rates, amounts payable on liquidation, voting rights, conversion rights, redemption provisions, sinking fund provisions and other matters. Our board of directors (1) may authorize the issuance of preferred stock that ranks senior to our common stock for the payment of dividends and the distribution of assets on liquidation, (2) can fix limitations and restrictions upon the payment of dividends on our common stock to be effective while any shares of preferred stock are outstanding, and (3) can also issue preferred stock with voting and conversion rights that could adversely affect the voting power of the holders of common stock.

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Delaware Anti-Takeover Law

We are subject to the provisions of Section 203 of the Delaware General Corporation Law. In general, this section prohibits a publicly held Delaware corporation from engaging in a business combination with an interested stockholder for a period of three years after the date of the transaction in which the person becomes an interested stockholder, unless:

before the date on which the stockholder became an interested stockholder, the corporation's board of directors approved either the business combination or the transaction in which the person became an interested stockholder;

the stockholder acquires more than 85% of the outstanding voting stock of the corporation, excluding shares held by directors who are officers or held in certain employee stock plans, upon consummation of the transaction in which the stockholder becomes an interested stockholder; or

the business combination is approved by the board of directors and is approved by two-thirds of the outstanding voting stock of the corporation that is not held by the interested stockholder at a meeting of the stockholders held on or after the date of the business combination.

An interested stockholder is a person who, together with affiliates and associates, owns, or at any time within the prior three years did own, 15% or more of the corporation's voting stock. Business combinations include, without limitation, mergers, consolidations, stock sales, asset sales or other transactions resulting in a financial benefit to interested stockholders.

Anti-Takeover Effects of Certain Charter and By-Law Provisions

Our charter and by-laws contain provisions relating to corporate governance and to the rights of stockholders. Our by-laws provide that special meetings of stockholders may only be called by our Board of Directors, our Chairman of the Board or our President and shall be called by our Chairman, President or Secretary at the request in writing of stockholders owning at least one-fifth of the outstanding shares of capital stock entitled to vote. In addition, our charter provides that our Board of Directors may authorize the issuance of preferred stock without further stockholder approval and upon those terms and conditions, and having those rights, privileges and preferences, as our Board of Directors may determine.

Transfer Agent and Registrar

The transfer agent and registrar for our common stock is LaSalle Bank N.A.

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DESCRIPTION OF BUSINESS

Overview/History

We are a developer, manufacturer and integrator of energy saving technologies. Our energy saving products include the eMAC system, which provides intelligent control and continuous monitoring of HVAC and lighting equipment via wireless communication technology to reduce energy usage and improve system reliability and the EnergySaver system, which reduces energy consumed by lighting with minimal lighting level reduction. Our technology has been installed in applications in commercial buildings, factories and office structures, as well as street lighting and parking lot lighting. Our GlobalCommander integrates with the EnergySaver, allowing us to link multiple EnergySaver units together and to provide remote communications, measurement and verification of energy savings.

From June 2001 through March 2006 we also provided, through our subsidiary, Great Lakes Controlled Energy Corporation, a Delaware Corporation (Great Lakes), integrated building and environmental control solutions for commercial and industrial facilities.

Until June 1, 2003, we also manufactured custom electrical switchgear through our subsidiary Switchboard Apparatus Inc. (Switchboard)

On December 5, 1997, we were initially formed as Electric City LLC, a Delaware limited liability company. On June 5, 1998, we changed from a limited liability company into a corporation by merging Electric City LLC into Electric City Corp., a Delaware corporation.

On June 10, 1998, Electric City issued shares of our common stock with a fair market value of \$1,200,272, representing approximately six (6%) percent of Electric City's then issued and outstanding common stock, to the approximately 330 shareholders of Pice Products Corporation (Pice), an inactive, unaffiliated company with minimal assets, pursuant to a merger agreement under which Pice was merged with and into Electric City. The purpose of the merger was to substantially increase the number of our shareholders to facilitate the establishment of a public trading market for our common stock. Trading in our common stock commenced on August 14, 1998 through the OTC Bulletin Board under the trading symbol ECCC .

In May 1999, we purchased most of the assets of Marino Electric, Inc., an entity engaged in the business of designing and manufacturing custom electrical switchgear and distribution panels.

On August 31, 2000 we acquired Switchboard Apparatus.

On June 7, 2001 we acquired Great Lakes.

On June 3, 2003, we entered into an asset purchase agreement with Hoppensteadt Acquisition Corp., whereby Hoppensteadt acquired all of the assets, except for certain receivables and cash, and assumed all of the liabilities, except for bank debt, of Switchboard Apparatus, as of May 31, 2003.

On May 3, 2005, we acquired Maximum Performance Group, Inc. (MPG). MPG is a technology based provider of energy and asset management products and services. MPG manufactures and markets its eMAC line of controllers for HVAC and lighting applications. The eMAC line of controllers provide intelligent control and continuous monitoring of HVAC and lighting equipment via wireless communication technology to reduce energy usage and improve system reliability. MPG has offices in New York City and San Diego, California.

On April 3, 2006, we sold all of the capital stock of Great Lakes Controlled Energy Corporation to its former owners, effective as of March 31, 2006.

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On June 30, 2006, we acquired Parke P.A.N.D.A. Corporation (Parke). Parke (now named Parke Industries, LLC) is an energy services provider specializing in the design, engineering and installation of energy efficient lighting upgrades for commercial and industrial users. Parke has 30 employees and is headquartered in Glendora, California, with offices in Danville and Carmel, California.

On September 13, 2006 we changed our name to Lime Energy Co. after merging with a wholly owned subsidiary which was set up solely for the purpose of effecting a name change. On September 22, 2006 our stock began trading on the OTC Bulletin Board under the trading symbol LMEC,

On September 27, 2006, we acquired Kapadia Consulting, Inc. (now named Kapadia Energy Services, Inc.). Kapadia is an engineering firm that specializes in energy management consulting and energy efficient lighting upgrades for commercial and industrial users. Kapadia has seven employees, is headquartered in Peekskill, New York, and has an office in Ventura, California.

Products And Services

The Company currently manufactures products and provides services under two distinct business segments. The energy technology segment includes the manufacturing and sale of the eMAC and uMAC product lines and the EnergySaver, GlobalCommander. Commencing June 30, 2006, we formed an energy services business segment, which is served by our subsidiaries, Parke Industries, LLC and Kapadia Energy Services, Inc. Parke specializes in the design, engineering and installation of energy efficient lighting upgrades for commercial and industrial users and Kapadia is an engineering consulting firm that specializes in energy efficiency and energy management.

eMAC & uMAC

The eMAC system is comprised of a heating, ventilating and air conditioning (HVAC) controller with wireless communication capabilities and a central, server based, Internet accessible software that monitors and controls the operation of the connected HVAC units. The eMAC system is designed for use in commercial and industrial applications with packaged (primarily rooftop) HVAC equipment of 2 to 40 tons (1 ton = 12,000 Btu/hr cooling capacity) and up to 500,000 Btu/hr of heating capacity.

The eMAC controller is contained in a small box that is mounted on the exterior of a customer s HVAC unit. The controller is wired into the HVAC equipment and monitors up to 126 points of the equipment s operation. In addition, each eMAC contains a Pentech Energy Recovery Controller (PERC), a patented third generation microprocessor-based technology.

PERC was developed by Pentech Solutions, a predecessor company to MPG, and is designed to dynamically match a HVAC system s output to any given load condition, thereby improving the operating efficiency of the equipment. Since most HVAC systems are designed to maintain comfortable environmental conditions on both the hottest and coldest days likely to be experienced, there exists substantial excess system capacity on most days of the year. Due to this excess capacity, the system quickly satisfies a thermostat s call for heating or cooling, and in doing so overshoots the thermostat set point and leaves Btu s of heat or cooling in the heat exchanger, cooling coils and air ducts. The PERC controller acts to correct this by periodically turning off the air conditioner s compressor and condenser fan while continuing to run the evaporator fan, thereby continuing to deliver cooling to the conditioned space utilizing the energy stored in the cooling coils, heat exchanger and air ducts. In heating applications, PERC periodically closes the gas valve while continuing to operate the indoor air fan, delivering heated air into the space utilizing the heat stored in the heat exchanger and air ducts. At the same time, the PERC controller is monitoring the rate of temperature change in the conditioned space in order to avoid overshooting the desired temperature setting. The PERC technology typically will result in energy savings of 15% to 20% for our end user customers.

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The wireless communication capabilities of the eMAC allow us to monitor and remotely manage the operation of a customer's HVAC equipment. A customer can log on to our eMAC web site and obtain information regarding the operation of its HVAC equipment and change equipment operating parameters, such as hours of operation and temperature. The eMAC will also send alarms to our central server when any of the up to 126 monitored points of operation fall outside predetermined operating ranges. This often permits us to react to a potential equipment problem before the occupants of the space are aware of an equipment malfunction. We charge our customers for this ability to communicate and remotely monitor and manage their equipment, though we often include an initial monitoring period with the purchase of the eMAC so that our customers can become familiar with the benefits of this service.

The uMAC is a version of the eMAC which has been simplified to remotely control the operation of a facility's lights via wireless communications. Using the uMAC a customer can remotely, via the Internet, turn lights on and off and change the daily schedule for the operation of a facility's lighting.

EnergySaver

The EnergySaver system is a lighting control system that reduces energy consumption of indoor and outdoor commercial, institutional and industrial ballasted lighting systems, while maintaining appropriate lighting levels. The EnergySaver is a freestanding enclosure that contains control panels with electrical parts and is connected between the incoming power line and the building's electrical lighting circuits. The EnergySaver also contains a microprocessor with software that allows the customer to control the amount of energy savings desired which, depending on the application, is typically between 20% and 30%, and provides self-diagnosis and self-correction. The customer can access the EnergySaver's microprocessor directly or remotely via modem, network or two-way radio.

The EnergySaver is manufactured to varying sizes and capacities to address differing lighting situations. We can interface our EnergySaver products with most new and existing lighting panels, ballasts and lamps without modification. In addition, the EnergySaver system reduces the power consumed by lamps, resulting in a reduction of heat generated within the lighting system, which enhances ballast and lamp life and reduces the amount of air conditioning necessary to cool the building.

Due to changes in lighting technology we expect revenue from the EnergySaver system (which includes the GlobalCommander) to decline in future periods, but we believe this will be more than offset by increases in eMAC revenue and revenue from our other recently acquired business: Parke Industries and Kapadia Energy Services.

GlobalCommander

The GlobalCommander system is an advanced lighting controller designed to permit central control and monitoring of multiple EnergySaver units and allows for large-scale demand side management and savings measurement and verification without turning off the user's lights. The GlobalCommander bundles the EnergySaver technology with an area-wide communication package to allow for energy reductions across entire systems in response to the guidelines of a customer's facility manager. In addition, the GlobalCommander has the ability to measure and store information about the actual savings generated from the use of the EnergySaver. This information, which can be viewed in a tabular or graphical format and can be downloaded to a user's computer, is often required for a customer to qualify for utility incentives for energy savings and curtailment. The GlobalCommander also allows customers to control their facilities' loads and lighting requirements from a single control point. This single-point control is available for a virtually unlimited number of remote facilities and can be accessed through the Internet, intranet or over standard telephone lines through dial-up modems.

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Energy Services

Through our wholly owned subsidiary, Parke Industries, LLC, which we acquired on at the end of June 2006, we market, design, engineer and install energy efficient lighting upgrades for commercial and industrial users. Parke will determine the best lighting solutions for its customers, taking into consideration factors such as lighting requirements, building environmental conditions, energy costs, available utility and/or tax incentives, and installation, operating and maintenance costs of various lighting alternatives, to select the best solution for its customers. It will then remove the existing lighting system and replace it with the new lighting system using its own installation crews. In most situations, Parke's customer will realize paybacks of 12 to 24 months on their lighting system upgrade and very often also improve the overall quality of lighting in their facilities.

Our other recently acquired subsidiary, Kapadia Energy Services, Inc., provides energy engineering services to assist customers in improving their energy efficiency and to better manage their energy costs. Some of the services that Kapadia offers its customers include building energy audits to determine ways to improve energy efficiency, HVAC and boiler system optimization, energy management planning, engineering design review with a view to optimizing energy efficiency and energy rebates, energy project management, and lighting engineering and design. Kapadia will also provide turnkey lighting upgrades in which it will purchase all of the materials and labor for energy efficient lighting upgrades, much like Parke does, except that it does not have its own installation crews.

Marketing, Sales and Distribution

The majority of our sales are derived through the efforts of our internal sales force. Prior to late 2005, each of our subsidiaries had their own sales force which primarily sold only their products. In late 2005, we began to integrate our subsidiaries and establish geographic profit centers in which our salespeople will sell all of the Company's subsidiaries' products. Initially we will be organized into three profit centers: East Coast (managed out of our New York office), Midwest (managed out of our Chicago office) and West Coast (managed out of our San Diego office). We believe our proprietary energy technologies differentiate us from other providers of energy solutions and provide our customers with superior returns on their investments.

Customers

During 2005, two customers, Kohl's Department Stores and Duane Read Inc., accounted for approximately 37% and 11% of our consolidated billings, respectively. During 2004, sales to five customers accounted for approximately 86% of our total consolidated revenue. Our largest customers for 2004 were Public Energy Solutions (39%), Electric City of New Jersey (14%), Electric City of Pennsylvania (12%), Control Ambiente Y Mantenimiento (11%) and the New York Power Authority (10%). During 2003, three customers accounted for approximately 72% of our total consolidated revenue. The top three customers during 2003 were M&A Railroad and Electric Supply (34%), Electric City of Pennsylvania (24%), and Morrow Meadow Corp. (15%). M&A Railroad and Electric Supply ceased to be a dealer in December 2003 and Electric City of Pennsylvania ceased to be a dealer in June 2005.

As of August 25, 2006 we have two ongoing VNPP (Virtual Negawatt Power Plan) programs, one with Commonwealth Edison in northern Illinois and the other with PacifiCorp in Salt Lake City, Utah. Under these contracts, we place our EnergySaver equipment in commercial and industrial Customer Host buildings at no cost to the Customer Host. In exchange for allowing us to reduce the power to their lighting system (without turning off their lights) during periods of peak energy demand, the Customer Host is allowed to operate the EnergySaver at a 3% to 5% level during non-curtailment periods. The utility companies agreed to pay us for the availability of this demand reduction and we recognize revenue under these contracts over the period for which demand reduction is actually provided. As of August 25, 2006 we had installed 135 EnergySavers at 85 different Customer Host sites under these programs at a cost of approximately \$1.4 million. We recognized our first revenue under the program and began amortizing the

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cost of the related EnergySaver units during the fourth quarter of 2005. Further shipments under these programs were postponed in late 2005 due to the high capital requirements of these programs and we are currently working with the utilities seeking to modify the programs to change them so we will be paid for delivering energy efficiency rather than energy curtailment.

Competition

While there are other HVAC controllers that provide energy saving benefits similar to the eMAC, we are not aware of any competing product available at a comparable cost to the eMAC that provides the communications, remote monitoring and diagnostic features of the eMAC. Large, national control companies provide systems that can do much of what the eMAC can do, but the installed cost of such systems make them impractical for smaller applications, which is the market we are targeting with the eMAC.

There are many competitors in the energy services business, including small regional lighting retrofit companies and large national energy service companies. The large national energy service companies tend to market to large national companies and compete for large energy retrofit projects in which lighting is one piece of the total project. Parke focuses on providing lighting retrofit services to the under-served market for small to mid-sized commercial and industrial users and niche markets where installations are more difficult. In these markets Parke sells its services based on the financial return to its customers and differentiates itself through its experience and reputation for quality work and superior service.

There are a number of products on the market that directly or indirectly compete with the EnergySaver products. These competing products can be categorized into three general types:

those that convert AC to DC at a central location,

those that pulsate the power to the lighting system; and

other control products similar to the EnergySaver system.

Products that fall into the first category convert AC to DC at a central location and do so more efficiently than it is done by the standard electronic ballast in each light fixture. The main drawback to this technology is that the transmission of DC power over any distance is generally less efficient and more dangerous than transmitting AC power. This technology also requires the rewiring of every light fixture on the circuit.

Products that pulsate the power in the lighting system turn the power off and on so quickly (120 times/second) that the lights remain on. This process, which is generally known as wave chopping, distorts the AC waveform and thereby produces harmonics in a building's electrical system that can damage other electrical components such as electric motors and electronic devices. The process also contributes to the reduction of life of lamps and ballasts in lighting fixtures.

Control products control power consumption at the lights, at the lighting circuit or at the control panel. Products that control the power at the lights or at the lighting circuit must be wired to each fixture or to each circuit, resulting in high installation cost, which makes these products less competitive from an economic perspective. The EnergySaver controls power consumption at the lighting panel, making it much simpler and less expensive to install and maintain. There are other products on the market that also control power consumption at the lighting panel, but the EnergySaver is the only product that we are aware of that offers total real-time variability of savings levels, remote communications and savings measurement and verification capabilities.

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Energy engineering services such as those provided by Kapadia are also generally widely available, though not as widely available as lighting retrofits due to the skills and experience required to provide the services. The certifications held by Kapadia's staff of engineers include: Professional Engineer (PE); Certified Energy Engineer (CEM); and Certified Lighting Efficiency Professional (CLEP). To obtain these certifications requires a high level of experience and demonstrated knowledge of engineering and energy engineering concepts. Kapadia differentiates itself from its competitors through its reputation for quality work and its 26 years of experience as an energy engineering firm. Most of Kapadia's business comes from repeat customers or referrals.

Manufacturing

Our EnergySaver product line is manufactured at our facilities in Elk Grove Village, Illinois, with manufacturing and assembly scaled to order. Since the manufacturing process that we are currently performing only involves the assembly of components manufactured by others, we believe there are many contract manufacturers located across the country that could assemble our EnergySaver product for us with relatively little lead time should we decide to outsource some or all of the manufacturing to contract manufacturers.

The eMAC is manufactured for us by a contract manufacturer in southern California. We believe that this contract manufacturer has sufficient capacity to handle our anticipated growth in eMAC sales for the foreseeable future. In addition, we believe that there are many contract manufacturers across the country that could manufacture the eMAC for us if for some reason our current contract manufacturer could not meet our needs.

The primary components for the EnergySaver and eMAC are sourced from multiple manufacturers. We are in continuous discussion with additional parts suppliers, seeking to ensure lowest cost pricing and reliability of supply.

During 2005, approximately 20% of our consolidated material purchases were made from four suppliers. Purchases from any one supplier will vary year-to-year depending on sales and inventory levels. None of these four suppliers sell the Company proprietary products that we could not purchase from other vendors.

Compliance With Environmental Laws

Neither the Company's production, nor sale of its products, in any material way generate activities or materials that require compliance with federal, state or local environmental laws. Parke and Kapadia use licensed disposal firms to dispose of old lamps, lighting ballasts or other products that may contain heavy metals or other potential environmental hazards.

Research and Development

The Company, through the day-to-day use of the EnergySaver and eMAC and their components and their use at various testing sites around the country, develops modifications and improvements to its products. Total research and development costs charged to operations were approximately \$395,000, \$150,000, and \$70,000 for the years ended December 31, 2005, 2004 and 2003, respectively.

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Intellectual Property

Certain technologies underlying the EnergySaver products have been patented in the U.S. and Italy by Giorgio Reverberi. A U.S. patent application was filed by Mr. Reverberi in November 1997, and a patent was issued in June 2000.

Since January 1, 1998, we, along with Mr. Reverberi and Mr. Joseph Marino, have entered into a number of agreements relating to the license of the EnergySaver technology, which grant us the exclusive license rights of Mr. Reverberi's patent of the EnergySaver technology in all of North America, Central America, South America (excluding the countries of Argentina, Brazil, Chile, Paraguay and Uruguay) and the Caribbean (except Cuba), as well as Africa (excluding the countries of Algeria, Libya, Morocco and Tunisia). Our license expires upon the expiration of Mr. Reverberi's last expiring patent, which we expect to be on or around November 2017. If either party materially breaches the license and fails to cure the breach within 180 days after notice by the other party of the breach, the other party can terminate the license. We pay Mr. Reverberi a royalty of \$200 and Mr. Marino a royalty of \$100 for each EnergySaver product we make or sell in territories in which Mr. Reverberi holds a valid patent.

We have applied for and/or received several patents on improvements we have made to the core technology developed by Mr. Reverberi. In addition, MPG has several patents on various aspects of the eMAC system. As of December 31, 2005, we had nine issued patents and three patents pending before the U.S. Patent and Trademark Office, as well as foreign patent offices. In addition we have registered three trademarks with the U.S. Trademark Office and have three additional federal trademark registrations pending.

Employees

As of January 24, 2007, we had 78 employees, of which 15 were management and corporate staff, eight were engineers, 20 were engaged in sales and marketing and 35 were engaged in field service

SELECTED CONSOLIDATED FINANCIAL DATA

The selected financial data set forth below as of December 31, 2005 and 2004 and for each of the three years in the period ended December 31, 2005 are derived from our audited financial statements included with this prospectus. The selected financial data set forth below for the years ended December 31, 2001 and 2000, and the balance sheet data for the three years ended December 31, 2003 have been derived from our audited financial statements and are not included with this prospectus. All of the Statement of Operations data has been revised from the original presentation in the audited financial statements to reflect the Company's Building Control and Automation segment as a discontinued operation, which was sold effective March 31, 2006. The selected financial data for the nine month periods ended September 30, 2005 and 2006 has been derived from our unaudited financial statements; however, such information reflects all adjustments (consisting solely of normal recurring adjustments), which, in the opinion of management, are necessary for a fair statement of results for the interim periods.

In the year ended December 31, 2002, we adopted FAS 142 Goodwill and Other Intangible Assets, which among other things, provides that goodwill no longer be amortized. As a result, the Company recorded no good will amortization during 2002, 2003, 2004 or 2005, where as it recorded approximately \$555,000 during 2001. For a detailed discussion on the application of these and other accounting policies, see note 3 in the notes to the consolidated financial statements attached as an exhibit.

Effective January 1, 2006, the Company adopted SFAS 123(R). Prior to then it accounted for employee stock options using the method of accounting prescribed by Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, and the associated interpretations using the intrinsic method. Generally, no expense was recognized related to its stock options under this method

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because the stock options exercise price were set at the stock's fair market value on the date the options were granted. Whereas, as a result of adopting SFAS123(R) \$2,053,540 of share based compensation expense was included in the results for the first nine months of 2006.

The historical results presented below are not necessarily indicative of the results to be expected for any future period. The data set forth below should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations and our financial statements, including the notes thereto, included elsewhere in this prospectus.

	Year ended December 31,					Nine Months Ended September 30,	
	2001	2002	2003	2004	2005	2005 (unaudited)	2006 (unaudited)
Statement of Operations Data:							
Revenue	\$ 1,886,210	\$ 3,627,113	\$ 2,280,532	\$ 733,630	\$ 3,693,429	\$ 2,924,162	\$ 4,611,321
Cost of sales	1,616,467	3,273,150	1,945,554	862,366	3,691,854	2,748,311	3,474,496
Selling, general and administrative	8,150,183	5,464,950	3,921,121	4,234,239	6,078,098	4,383,158	7,957,736
Impairment loss		108,000					760,488
Operating loss	(7,880,440)	(5,218,987)	(3,586,143)	(4,362,975)	(6,076,523)	(4,207,307)	(7,581,399)
Other income (expense)	(3,396,009)	(32,920)	(354,941)	(626,049)	(544,253)	(384,180)	(3,131,109)
Loss from continuing operations	(11,276,449)	(5,251,907)	(3,941,084)	(4,989,024)	(6,620,776)	(4,591,487)	(10,712,508)
Income (loss) from discontinued operations	(1,694,628)	(1,756,020)	(1,540,858)	(170,338)	(251,962)	77,501	(21,425)
Cumulative effect of accounting change		(4,103,872)					
Net loss	(12,971,077)	(11,111,799)	(5,481,942)	(5,159,362)	(6,872,738)	(4,513,986)	(10,733,933)
	(20,118,939)	(4,111,107)	(4,817,917)	(4,639,259)	(1,851,345)	(1,017,800)	(24,347,725)

Preferred
Stock
DividendsNet Loss
Available to
Common

Shareholders	\$ (33,090,016)	\$ (15,222,906)	\$ (10,299,859)	\$ (9,798,621)	\$ (8,724,083)	\$ (5,531,786)	\$ (35,081,658)
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Basic and
diluted loss
per common
share from
continuing
operations

	\$ (15.67)	\$ (6.98)	\$ (3.90)	\$ (3.62)	\$ (2.65)	\$ (1.79)	\$ (1.83)
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Basic and
diluted loss
per common
share

	(16.52)	(7.32)	(4.58)	(3.68)	(2.73)	(1.77)	(1.83)
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Weighted
average
common
shares
outstanding
(1)

	2,003,203	2,080,878	2,250,766	2,660,093	3,190,664	3,124,609	19,198,805
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Balance Sheet**Data:**

Cash and cash equivalents	\$ 5,486,073	\$ 1,555,904	\$ 2,467,023	\$ 1,789,808	\$ 4,229,150	\$ 1,574,368	\$ 6,825,874
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Working
capital

(deficiency)	7,470,046	3,546,270	2,050,157	263,304	646,483	(2,604,102)	4,815,498
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Total assets	16,435,863	8,908,551	7,353,627	6,479,320	17,098,974	14,110,436	27,548,721
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Long-term
debt, including
current portion

	1,434,018	1,089,791	1,348,645	1,230,353	4,980,032	986,826	580,851
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Total
stockholders
equity

	12,465,333	4,284,291	3,040,932	1,780,271	4,377,637	5,830,267	21,136,866
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(1) Adjusted for 1
for 15 reverse
stock split
effected
January 23,
2007

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with the consolidated financial statements and related notes which appear elsewhere in the registration statement of which this prospectus forms a part. The discussion contains forward-looking statements within the meaning of the Private Securities Litigation Act of 1995. Such statements consist of any statement other than a recitation of historical fact and can be identified by the use of forward-looking terminology such as may, expect, anticipate, estimate or continue or the negative of such terms or other variations of such terms or comparable terminology. You are cautioned that all forward-looking statements are necessarily speculative and there are certain risks and uncertainties that could cause actual events or results to differ materially from those referred to in such forward-looking statements. We do not have a policy of updating or revising forward-looking statements and, therefore, you should not assume that our silence over time means that actual events are bearing out as estimated in such forward-looking statements.

We have a limited operating history. All risks inherent in an inexperienced enterprise are inherent in our business.

Critical Accounting Policies and Estimates

The discussion and analysis of our financial condition and results of operations are 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 amount of assets and liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities at the date of our financial statements. Actual results may differ from these estimates under different assumptions or conditions. Critical accounting policies are defined as those that are reflective of significant judgments and uncertainties, and potentially result in materially different results under different assumptions and conditions. We believe that our critical accounting policies are limited to those described below. For a detailed discussion on the application of these and other accounting policies, see note 3 in the notes to the consolidated financial statements attached as an exhibit.

Use of Estimates

Preparation of the consolidated financial statements in accordance with accounting principles generally accepted in the United States requires management to make estimates and assumptions affecting the reported amounts of assets, liabilities, revenues and expenses and related contingent liabilities. On an on-going basis, the Company evaluates its estimates, including those related to revenues, bad debts, warranty accrual, income taxes and contingencies and litigation. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions.

Revenue Recognition

We recognize revenue when all four of the following criteria are met: (i) persuasive evidence has been received that an arrangement exists; (ii) delivery of the products and/or services has occurred; (iii) the selling price is fixed or determinable; and (iv) collectibility is reasonably assured. In addition, we follow the provisions of the Securities and Exchange Commission's Staff Accounting Bulletin No. 104, Revenue Recognition, which sets forth guidelines in the timing of revenue recognition based upon factors such as passage of title, installation, payments and customer acceptance. Any amounts received prior to satisfying our revenue recognition criteria are recorded as deferred revenue.

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Our MPG subsidiary often bundles contracts to provide monitoring services and web access with the sale of its eMAC hardware. As a result, these sales are considered to be contracts with multiple deliverables which at the time the hardware is delivered and installed includes undelivered services essential to the functionality of the product. Accordingly, we defer the revenue for the product and services and the cost of the equipment and installation and recognize them over the term of the monitoring contract. The monitoring contracts vary in length from 1 month to 5 years.

We have entered into agreements in which we have contracted with utilities to establish a Virtual Negawatt Power Plan (VNPP). Under these contracts, we install Energy Saver units at participating Customer Host locations, within the utility s territory. The participating Customer Hosts receive the benefit of reduced utility costs through the operation of the units. We are able to reduce electric demand requirements during periods of peak demand, providing nearly instantaneous control, measurement and verification of load reduction. The utility companies pay us for the availability of this demand reduction and we recognize revenue under these contracts over the period for which the demand reduction is provided. Revenue of \$15,781 was recognized from these contracts during the fourth quarter of 2005 and \$34,868 for the first nine months of 2006. No revenue was recognized under such contracts for the years ended December 31, 2004 and 2003. The cost of the Energy Saver units currently at host locations under such VNPP programs is included in fixed assets and depreciated over the term these units will be used under the contracts.

Profit Recognition on Long-Term Contracts

We account for revenues on long-term contracts under the percentage of completion method in conjunction with the cost-to-cost method of measuring the extent of progress toward completion. Any anticipated losses on contracts are charged to operations as soon as they are determinable. Prior to the second quarter of 2005, due to our limited experience estimating the profitability on our long-term building automation and control contracts, we deferred all building automation and control contract related profits (i.e. assumed zero profit) until completion of the contract when the actual profit on the contract was known. Starting in the second quarter of 2005 we began recognizing contract related profits based on the projected profits for the contract, consistent with the AICPA s Statement of Position 81-1 (SOP 81-1).

Allowance for Doubtful Accounts

We maintain an allowance for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. The allowance is largely based upon specific knowledge of customers from whom collection is determined to be doubtful and our historical collection experience with such customers. If the financial condition of our customers or the economic environment in which they operate were to deteriorate, resulting in an inability to make payments, or if our estimates of certain customers ability to pay are incorrect, additional allowances may be required. During 2005, we increased our allowance by \$97,000 and wrote-off \$13,000. As of December 31, 2005 our allowance for doubtful accounts was approximately \$325,000, or 15.7% of the outstanding accounts receivable.

Impairment of Long-Lived Assets.

We record impairment losses on long-lived assets used in operations when events and circumstances indicate that the assets might be impaired and the undiscounted cash flows estimated to be generated by those assets are less than the carrying amount of those items. Our cash flow estimates are based on historical results adjusted to reflect our best estimate of future market and operating conditions. The net carrying value of assets not recoverable is reduced to fair value. Our estimates of fair value represent our best estimate based on industry trends and reference to market rates and transactions.

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We have made acquisitions in the past that included a significant amount of goodwill and other intangible assets. Under generally accepted accounting principles in effect through December 31, 2001, these assets were amortized over their estimated useful lives, and were tested periodically to determine if they were recoverable from operating earnings on an undiscounted basis over their useful lives. Effective in 2002, goodwill is no longer amortized but is subject to an annual (or under certain circumstances more frequent) impairment test based on its estimated fair value. Estimated fair value is less than value based on undiscounted operating earnings because fair value estimates include a discount factor in valuing future cash flows. There are many assumptions and estimates underlying the determination of an impairment loss, including economic and competitive conditions, operating costs and efficiencies. Another estimate using different, but still reasonable, assumptions could produce a significantly different result. As part of our 2003 and 2004 year-end assessment, we updated our long-term projections for the building automation and controls business and estimated the fair value based on the discounted current value of the expected future cash flows. We then compared the implied fair value of the goodwill to its carrying value and determined that the value of the goodwill was not impaired. In February 2006 we signed a non-binding letter of intent to sell Great Lakes Controlled Energy. To determine if our goodwill would be impaired as a result of the expected sale, we compared the carrying value of the goodwill related to Great Lakes to the expected sale price of the business and determined that the goodwill is impaired. As a result we recorded an impairment loss as of December 31, 2005 of \$242,830. It is possible that upon completion of future impairment tests, as the result of changes in facts or circumstances, we may have to take additional charges in future periods to recognize a further write-down of the value of the goodwill attributed to our acquisitions to their estimated fair values.

Material Trends and Uncertainties

From time to time changes occur in our industry or our business that make it reasonably likely that aspects of our future operating results will be materially different than historical operating results. Sometimes these matters have not occurred, but their existence is sufficient to raise doubt regarding the likelihood that historical operating results are an accurate gauge of future performance. We attempt to identify and describe these trends, events, and uncertainties to assist investors in assessing the likely future performance of the Company. Investors should understand that these matters typically are new, sometimes unforeseen, and often are fluid in nature. Moreover, the matters described below are not the only issues that can result in variances between past and future performance nor are they necessarily the only material trends, events, and uncertainties that will affect the Company. As a result, investors are encouraged to use this and other information to judge for themselves the likelihood that past performance will be indicative of future performance.

The trends, events, and uncertainties set out in the remainder of this section have been identified as those we believe are reasonably likely to materially affect the comparison of historical operating results reported herein to either other past period results or to future operating results. These trends, events and uncertainties include:

Changes in our senior management and on our Board of Directors. In October, 2005, Daniel Parke became a Member of our Board of Directors. In January 2006, our Chief Executive Officer for the past six years, Mr. John Mitola, resigned and was replaced by one of our Board members, Mr. David Asplund. Mr. Mitola also resigned as a director at that time. At approximately the same time, Mr. Robert Manning, the Chairman of our Board of Directors for the past 5-1/2 years announced his retirement. Mr. Manning's seat on the Board of Directors was filled by Mr. Richard Kiphart, an investor in the Company, and Mr. Kiphart was also elected to serve as our Chairman. We also recently added Messrs. William Carey and Gregory Barnum to our Board of Directors. Mr. Parke also became our Chief Operating Officer and President on June 30, 2006. These changes in our Senior Management and Board of Directors have resulted in changes to our business plan, including the sale of Great Lakes Controlled Energy. The disposal of this business will result in a reduction in revenue during 2006. The Building Automation Controls business was

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responsible for approximately 25% of our 2005 revenue and posted an operating loss of \$305,497 during 2005, including a \$242,830 charge related to the impairment of goodwill and the allocation of corporate overhead. This business was expected to record revenue of approximately \$2 million during 2006 and little to no operating profit.

The acquisition of Maximum Performance Group. In May of 2005, we acquired Maximum Performance Group, Inc. (MPG), the manufacturer of the eMAC line of HVAC and lighting controllers. MPG was responsible for approximately 20% of our consolidated revenue for 2005 and 33% of our operating loss. We believe that MPG has the potential for significantly better performance in future periods and that the 2005 results were heavily influenced by disruptions related to the acquisition and integration with Lime Energy. MPG's products have historically had margins that are generally better than those of our existing businesses, therefore we believe its profitability should improve with increases in revenue. We recently announced new contracts at MPG that should contribute to improved results during 2006.

Customer concentrations. We have historically relied on a small number of customers each year for a significant portion of our revenue. Seldom has a customer that represented 10% or more of our revenues in one year also represented more than 10% of our revenue in the following year. This means that we have had to find major new customers each year to replace major customers whose needs have been satisfied from the prior year. We hope that some of the changes that we are currently implementing to our sales strategy will decrease our dependence on large customers, thereby diversifying our customer base and reducing the risk associated with having to replace a customer once we have completed our contract with them. We believe that the monitoring services MPG sells will also help to mitigate this risk because they represent a base of recurring contract revenue. While this monitoring revenue only represented approximately 10% of our 2005 consolidated revenue, we believe it will continue to grow with the continued sale of eMACs.

Results of Operations

Our revenues reflect the sale of our products and services, net of allowances for returns and other adjustments. Revenues of Lime Energy and its subsidiaries are generated from the sale of products and services, the vast majority of which are sold in the U.S.

Our cost of goods sold consists primarily of materials and labor. Also included in our cost of goods sold are freight, charges from third parties for installation of our products, costs of operating our manufacturing facility, charges for potential future warranty claims, and royalty costs related to licenses of the technology used in our EnergySaver line of lighting controllers.

Sales and gross profits depend, in part, on the volume and mix of products sold during any given period. Generally, products that we manufacture have a higher gross profit margin than products that we purchase and resell.

A portion of our operating expense is relatively fixed, such as the cost of our facilities and supervisory labor. Accordingly, an increase in the volume of sales will generally result in an increase to our gross margins since these fixed expenses do not increase in direct proportion to our sales. Since the majority of the products we sell are manufactured by third parties, we believe that we can significantly increase our sales without a significant investment in fixed assets.

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Selling, general and administrative (SG&A) expenses include the following components:
direct labor and commission costs related to our employee sales force;

expenses related to our non-manufacturing management, supervisory and staff salaries and employee benefits;

commission costs related to our independent sales representatives and our distributors;

costs related to insurance, travel and customer entertainment and office supplies costs and the cost of non-manufacturing utilities;

costs related to marketing and advertising our products;

costs of outside professionals such as lawyers, accountants, and investor relations professionals;

research and development expenses;

costs related to administrative functions that serve to support the existing businesses of the Company, as well as to provide the infrastructure for future growth.

Interest expense for the most recent three month period includes the costs associated with the mortgage on our headquarters building, a note payable, capitalized leases and various auto loans. Interest expense for the nine month period ended September 30, 2006 also includes the costs and expenses associated with our working capital line and our convertible term loans, both of which were retired on June 29, 2006. Included in these costs is amortization of the debt discount on the convertible term loans and amortization of deferred financing costs related to the working capital facility.

Three Months Ended September 30, 2006 Compared to Three Months Ended September 30, 2005.

Our total revenue for the three-month period ended September 30, 2006 increased \$1,006,798 or 89.6% to \$2,130,158 as compared to \$1,123,360 for the three month period ended September 30, 2005. All of this increase was generated by our Energy Services segment, which was created with the acquisition of Parke effective June 30, 2006. Total revenue for the Energy Technology segment decreased slightly, from \$1,123,000 to \$1,110,000.

Cost of sales for the three-month period ended September 30, 2006 increased \$394,673 or 32.9% to \$1,592,613 from \$1,197,940 for the three-month period ended September 30, 2005. The increase in cost of sales was due to the increase in sales. Gross profit for the third quarter of 2006 increased \$612,125 to \$537,545 from a loss of \$74,580 in the third quarter of 2005, and the gross margin increased from a negative 6.6% in 2005 to a positive 25.2% in 2006. Both the Energy Technology and Energy Services segments contributed in approximately equal amounts to the increase in the gross profit. The improvement in gross profit in the Energy Technology segment was the result of an increase in sales of more profitable products. We believe that the gross profit should continue to increase in future periods as sales increase in both segments of our business.

SG&A for the three-month period ended September 30, 2006 increased \$2,160,589, or 119.1% to \$3,974,564 from \$1,813,975 for the three-month period ended September 30, 2005. The adoption of SFAS 123 (R) (which relates to stock-based compensation see Note 2 to the financial statements) was responsible for \$1,485,698 or 69% of the increase, while the inclusion of Parke, which was acquired on June 30, 2006, was responsible for the majority of the remaining increase. We expect our SG&A expense to increase during the balance of the year due to the acquisition of Kapadia and as we add additional sales people in an attempt to increase our sales of our products and services.

As is more fully explained in Note 8 to the financial statements, during the quarter ended September 30, 2006, we determined that the carrying value of the ComEd VNPP (Virtual Negawatt Power Plan) asset exceeded its fair value by \$760,488. In order to reduce the carrying value to the fair value we took a non-cash charge of \$760,488 during the period.

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Other income for the three-month period ending September 30, 2006 increased \$157,449, to \$79,997 from an expense of \$77,452 for the three-month period ended September 30, 2005. Interest income increased \$79,998 to \$96,877 during the most recent quarter as compared to \$16,879 earned in the same quarter during 2005. The increase in interest income was the result of increase invested cash balances and higher interest rates. Interest expense decreased \$77,451 to \$16,880 during the three months ended September 30, 2006 from \$94,331 during the same period during 2005. This decrease was the result of lower outstanding debt balances due to the retirement of our working capital line and term loans (other than the mortgage loan on our Elk Grove Village, Illinois headquarters) at the end of June 2006.

Effective March 31, 2006, we sold all of the outstanding capital stock of Great Lakes Controlled Energy Corporation to its former owners. As required by SFAS 144 we have presented the operating results for this business as discontinued operations. During the three month period ended September 30, 2005 this business recorded a loss of \$48,088.

All of the outstanding shares of Series E Convertible Preferred Stock were converted to common stock on June 29, 2006, thus there was no dividends recorded during the three month period ended September 30, 2006, as compared to \$344,000 in dividend expense during the same period in 2005.

Nine Months Ended September 30, 2006 Compared to Nine Months Ended September 30, 2005.

Total revenue for the nine-month period ended September 30, 2006 increased \$1,687,159 or 57.7% to \$4,611,321 as compared to \$2,924,162 for the nine-month period ended September 30, 2005. All of the increase is the result of contributions from MPG and Parke. MPG was acquired effective April 30, 2005, thus was only included for five of the nine months in 2005 and Parke was acquired on June 30, 2006, therefore was not included in the 2005 results at all. We expect to see continued growth in revenue as a result of these acquisitions and the recent acquisition of Kapadia.

Cost of sales for the nine-month period ended September 30, 2006 increased 26.4% to \$3,474,496 from \$2,748,311 for the same period in 2005. The increase in cost of sales was related to the increase in sales. Gross profit for the first nine months of 2006 increased \$960,974, or 546% to \$1,136,825 from \$175,851 earned in the first nine months of 2005, and the gross profit margin improved from 6.0% earned during 2005 to 24.7% for 2006. Approximately one third of the increase in the gross profit is attributable to the acquisition of Parke with the remaining increase attributable to a shift in sales in the Energy Technology segment to more profitable products.

SG&A for the nine-month period ended September 30, 2006 increased \$3,574,578 to \$7,957,736 from \$4,383,158 for the same period during 2005. The adoption of SFAS 123(R) was responsible for approximately \$2,000,000, or 56% of this increase, while the inclusion of four additional months of expense for MPG and three months of expense from Parke was responsible for approximately \$1,600,000 of the increase

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Other expense increased \$2,746,929, to \$3,131,109 from \$384,180 for the nine-month period ended September 30, 2006 and 2005, respectively. Interest expense increased \$2,830,408 to \$3,256,755 during the first nine months of 2006 from \$426,347 during the first nine months of 2005. The components of interest expense for the nine month periods ended September 30, 2006 and 2005 are as follows:

	Nine Months Ended September 30	
	2006	2005
Contractual interest	\$ 347,624	\$ 161,257
Amortization of deferred issuance costs and debt discount	1,175,970	105,090
Value of warrant		160,000
Value of adjustment in conversion price	950,865	
Prepayment penalties	516,071	
Termination of post re-payment interest obligation	266,225	
Total Interest Expense	\$ 3,256,755	\$ 426,347

Contractual interest expense (the interest on outstanding loan balances) increased \$186,367 or 116% to \$347,624 during the first nine months of 2006 from \$161,257 during the same period in 2005. The increase in contractual interest was the result of higher average outstanding balances, due in part to the issuance of the \$5 million term loan in November 2005 (which was repaid in June 2006), and higher average interest rates. Amortization of the deferred issuance costs and the debt discount related to the Laurus revolver and convertible term loans, which is included in interest expense, increased \$1,070,880 to \$1,175,970 during the first nine months of 2006 from \$105,090 during the first nine months of 2005. With the repayment of all of the Laurus loans in June 2006, we were required to recognize as interest expense the remaining unamortized balances of the capitalized issuance costs and the debt discount of \$978,525. The balance of the increase in amortization expense is related to the amortization of deferred issuances costs associated with the \$5 million term loan issued in November 2005. The 2006 interest expense also includes prepayment penalties of \$516,071 for the early repayment of the Laurus term loans and \$266,225 for the cost of terminating the obligation to pay Laurus a portion of the cash flows generated by certain VNPP projects for the next five years. Upon the closing of the PIPE Transaction and repayment of the term loans in June 2006, Laurus elected to convert the outstanding balance on the revolving note into shares of our common stock. The revolving note contained antidilution provisions which automatically adjusted the conversion price of the note to \$1.00 per share: the price at which we issued shares as part of the PIPE Transaction. Laurus would have received 59,902 shares of common stock upon conversion of the revolving note utilizing the conversion price prior to the adjustment, but as a result of this adjustment it received 943,455 shares. The market value of the 883,553 additional shares it received as a result of the adjustment was recorded as interest expense in the amount of \$950,865.

During April 2005 we issued a warrant to purchase 400,000 shares of our common stock to Laurus in exchange for its consent to a private equity issuance and the acquisition of MPG, as well as waiving its right to adjust the conversion price on its convertible term note and convertible revolving note. The warrant was valued at \$160,000 using a modified Black-Scholes option pricing model and charged to interest expense during the period.

Effective March 31, 2006, we sold all of the outstanding capital stock of Great Lakes Controlled Energy Corporation to its former owners. As required by SFAS 144 we have presented the operating results for this business as discontinued operations. During the nine months ended September 30, 2006 Great Lakes operating loss was \$21,425, compared to an operating profit of \$77,501 earned during the same period in 2005.

Preferred stock dividends for the first nine months of 2006 increased \$23,329,925 to \$24,347,725 from \$1,017,800 for the same period in 2005. We accrued dividends of \$698,000 and \$1,017,800 on our Series E Convertible Preferred Stock during the first nine months of 2006 and 2005, respectively. The

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dividends accrued during the first nine months of 2006 and 2005 were satisfied through the issuance of additional shares of our preferred stock.

On June 29, 2006, in connection with the PIPE Transaction, all of the outstanding shares of Series E Convertible Preferred stock converted into shares of common stock. The Series E Preferred Stock as originally issued was convertible at \$6.67 per share into 1,574,027 shares of our common stock (adjusted for the reverse stock split), however, the Series E contained antidilution provisions which automatically reduced the conversion price of the Series E to the \$1.00 per share issuance price of common stock in the PIPE Transaction. This adjustment in the conversion price resulted in 20,074,319 additional shares being issued upon conversion of the Series E. The value of these additional shares of \$23,085,467 (valued at the market price of \$1.15 per share) was recorded as a deemed dividend during the second quarter of 2006.

During the first quarter of 2006 we were required to reduce the exercise price on warrants to purchase 4,064,830 shares of our common stock held by a preferred stock holder. The exercise price on the warrants was reduced to \$0.62 per share (\$9.30 post split) from an average exercise price of \$0.92 per share (\$13.80 post split). This was because we issued stock options to our new CEO with an exercise price of \$0.62 per share (\$9.30 post split)(which was the market price of our common stock on the date the options were issued). The warrant exercise price automatically adjusted to the same price. We compared the value of the warrants, as determined through the use of a modified Black-Scholes option pricing model, with the old exercise price to the value of the warrants with the reduced exercise price and determined that the reduction in the exercise price had increased the value of the warrants by \$266,390. Since these warrants were issued as part of a security offering the increase in value was considered to be a deemed dividend to the security holders. We recorded the deemed dividend by offsetting the dividend charge to additional paid-in-capital, without any effect on total stockholders equity. Also during 2006, a number of our common stock warrants held primarily by the former holders of our Series E Convertible Preferred Stock, contained similar antidilution provisions. Prior to the PIPE Transaction the exercise price on these warrants ranged from \$13.50 per share to \$15.00 per share (adjusted for the reverse split). The issuance of common stock in the PIPE Transaction caused the exercise price on these warrants to be automatically reduced to \$1.00 per share. We compared the value of the warrants prior to the adjustment to the value of the warrants after the adjustment, using a modified Black-Scholes Option Pricing Model, and determined that the value had increased by \$297,868. This increase in value was treated as a deemed dividend and recorded during the second quarter of 2006 by offsetting the dividend charge to additional paid-in-capital, without any effect on total stockholders equity.

As the result of the conversion of the Series E Convertible Preferred Stock we will not be accruing dividends on the Series E Preferred Stock in future periods.

Twelve-Month Period Ended December 31, 2005 Compared With the Twelve-Month Period Ended December 31, 2004

Revenue. Our revenue increased \$2,959,799, or 403% to \$3,693,429 during the year ended December 31, 2005 from \$733,630 during the year ended December 31, 2004. Approximately \$950,000 or 39% of the increase was due to the acquisition of Maximum Performance Group in May 2005. EnergySaver related sales increased approximately \$1,700,000 during 2005 over the year earlier period as the result of increased EnergySaver sales. Unit sales of EnergySavers increased 198% from 67 units in 2004 to 200 units in 2005. One customer was responsible for a significant portion of this increase. We are continuing to ship product to this customer into 2006, but at a reduced level. Approximately \$325,000 of the increase in revenue was due to a short term utility consulting project completed in May 2005. Revenue for 2005 also included VNPP curtailment services of approximately \$16,000. We hope to see continued improvement in EnergySaver and eMAC sales as a result of a recent restructuring of our sales strategy that places an increase emphasis on commercial sales.

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Gross Profit. Our consolidated gross profit increased \$130,311 in 2005 to \$1,575 from a loss of \$128,736 in 2004. The increase in gross profit was due to a consulting assignment completed in May 2005 by the Energy Technology segment, and to improved margins on EnergySaver sales primarily as the result of increased volume. The profit on the consulting assignment is not likely to be repeated in future periods. Our margins on EnergySaver and eMAC sales are expected to improve during 2006 as sales of these products increase.

SG&A Expenses. Selling, general and administrative expenses increased \$1,843,859 or 44% to \$6,078,098 during 2005 from \$4,234,239 in 2004. The acquisition and integration of Maximum Performance Group in May 2005 was responsible for approximately \$1,840,000 of the increase. We expect SG&A to increase moderately during 2006 as the result of a full twelve months of expense from Maximum Performance Group and the implementation of FAS 123 (R) which requires that we expense employee options beginning in the first quarter of 2006.

Other Non-Operating Income (Expense). Other non-operating expense is comprised of interest expense and interest income. Interest expense declined \$45,564 to \$602,990 during 2005 from \$648,554 during 2004. Amortization of the deferred issuance costs and debt discount related to the Laurus revolver and convertible term loans, which are included in interest expense, declined \$409,026 to \$165,411 for 2005 from \$574,437 during 2004. The deferred issuance costs and debt discount are being amortized using the effective interest method, thus decline as the outstanding balance on the related term loan is repaid or converted. During January 2004, Laurus converted a portion of its term loan resulting in accelerated recognition of \$193,000 in amortization expense. No such conversions occurred during 2005. Other interest expense increased \$203,149 primarily as a result of borrowings under the revolver, a new \$5,000,000 term loan entered into in late November 2005, and higher interest rates. There were no borrowings under the revolver during 2004. During the second quarter of 2005 we issued a 5 year warrant to purchase 26,667 shares of our common stock at \$15.00 per share to Laurus in exchange for its consent and waiver to permit us to complete a sale of common stock and warrants to a group of investors for gross proceeds of \$5,625,000 and to acquire MPG. This warrant was valued at \$160,000 using a modified Black-Sholes option pricing model and the value was charged to interest expense during the period. Interest income increased \$36,232 to \$58,737 during 2005 from \$22,505 earned in 2004. The increase in interest income was due to higher average invested cash balances and increases in the interest rates paid on the invested balances.

Discontinued Operations. Effective March 31, 2006, we sold our Building Controls and Automation business its former owners. As required by SFAS 144 we have presented the operating results for this segment as discontinued operations. During 2005 this segment reported a loss of \$251,962 as compared to a loss of \$170,338 in 2004. The 2005 results include a goodwill impairment charge of \$242,830.

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Preferred Stock Dividends. The dividend expense recognized during 2005 and 2004 was comprised of the following:

<i>Year ended December 31,</i>	2005	2004
Accrual of dividend on Series A Convertible Preferred	\$	\$ 540,705
Accrual of Series C Preferred dividend		53,206
Accrual of Series D Preferred dividend		35,932
Accrual of Series E Preferred dividend	1,366,900	1,006,937
Deemed dividend associated with beneficial conversion price on shares issuable in satisfaction preferred dividends		1,127,021
Deemed dividend associated with the redemption and exchange of outstanding preferred stock		1,860,458
Deemed dividend associated with change in the expiration date of warrants to purchase shares of preferred stock		15,000
Deemed dividend associated with change in the exercise price of warrants to purchase shares of common stock	484,455	
Total	\$ 1,851,345	\$ 4,639,259

Our dividend expense for 2005 declined \$2,787,914 or 60.1% to \$1,851,345 from \$4,639,259 in 2004. We accrued dividends of \$1,366,900 and \$1,636,780 on our Convertible Preferred Stock during 2005 and 2004, respectively. This decline in accrued dividends was the result of the reduction in the number of preferred shares outstanding and a reduction in the dividend rate that resulted from the redemption and exchange effected in March 2004. The dividends accrued during 2005 and 2004 were satisfied through the issuance of 13,669 shares of preferred stock (convertible into 91,127 shares of common stock) and 16,368 shares of preferred stock (convertible into 109,120 shares of common stock), respectively. We were required to recognize a non-cash deemed dividend of \$1,127,021 during 2004 due to the fact that the conversion price on these dividend shares was lower than the market price of our common stock on the date of issue.

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On April 28, 2005 we issued to five (5) institutional investors, for an aggregate gross purchase price of \$5,625,000, 416,667 shares of the Company's common stock and 42 month warrants to purchase 208,333 additional shares of common stock at \$15.75 per share. Due to the sale price of the securities issued as part of this transaction we were required to adjust the exercise price on warrants to purchase 336,989 shares if its common stock held by two investors who had participated in earlier equity offerings. The exercise prices on these warrants were reduced from \$36.30 and \$15.00, respectively to \$13.50. We compared the value of the warrants with the old exercise price to the value of the warrants with the reduced exercise price, through the use of a modified Black-Scholes option pricing model, and determined that the reduction in the exercise price had increased the value of the warrants by \$484,445. Since these warrants were issued as part of a security offering the increase in value is considered to be a deemed dividend to the security holders. We recorded the deemed dividend by offsetting charges and credits to additional paid-in capital, without any effect on total stockholders equity.

As part of the redemption and exchange completed in March 2004, shares of old preferred stock were exchanged for shares of the new Series E Preferred Stock at the rate of 10 shares of old preferred for each share of new Series E preferred stock. Additionally, each share of old preferred stock was convertible into 10 shares of common stock, whereas each share of new Series E Preferred Stock is convertible into 6.67 shares of common stock. Despite the fact that we believe the redemption and exchange transaction was favorable for the Company and its common stockholders (see note 17(k) to the financial statements), we were required to record a non-cash deemed dividend on the transaction of \$1,860,458. For accounting purposes the transaction was viewed as a redemption for cash and shares of Series E Preferred Stock. The non-cash deemed dividend was determined by comparing the fair value of the consideration given (the cash and the market value of the Series E Preferred Stock) to the carrying value of the old preferred stock that was redeemed. The fair value of the consideration given exceeded the carrying value of the old preferred primarily due to the fact that the market price of our common stock was higher on the day the redemption and exchange transaction closed than it was when the shares of the old preferred stock were originally issued.

We also incurred a \$15,000 deemed dividend during 2004 when we agreed to extend the expiration date on warrants to purchase shares of our Series E Preferred Stock from September 30, 2004 to December 31, 2004. We agreed to extend these warrants to permit holders who participated in the redemption and exchange more time to exercise their warrants without violating the short swing trading rules of section 16(b) of the Securities Act of 1934 or our insider trading policy, which prohibits the trading of our securities during certain blackout periods prior to the filing of our financial statements.

As is more fully described in note 17(k) to our financial statements, we completed a redemption and exchange offering on March 22, 2004 in which we redeemed 538,462 shares of our outstanding Series A, Series C and Series D Convertible Preferred Stock (the "Old Preferred"), and exchanged the remaining 2,104,509 shares of Old Preferred into 210,451 shares of a new Series E Preferred Stock at the rate of 10 shares of Series E Preferred Stock for each share of Old Preferred. The Old Preferred Stock carried a dividend rate of 10% payable at the Company's election in cash or in additional shares of Preferred Stock during the first three years following issuance. After the third anniversary of issuance we were required to pay all dividends in cash and the dividend rate was to increase by 1/2% every six months until it reached 15%, where it would remain until the shares were converted or redeemed. The Series E Preferred Stock carries a 6% dividend that is payable at the Company's election in cash or additional shares of Series E Preferred Stock for as long as the shares remain outstanding. The reduction in the number of outstanding shares of preferred stock, in combination with the reduction in the dividend rate, significantly reduces the dilutive effect of the payment-in-kind dividend on our preferred stock for periods after March 22, 2004.

Table of Contents**Twelve-Month Period Ended December 31, 2004 Compared With the Twelve-Month Period Ended December 31, 2003**

Revenue. Our revenue declined \$1,546,902 or 68% to \$733,630 during the year ended December 31, 2004 from \$2,280,532 during the year earlier period. Energy Saver unit sales declined 69.1% from 217 units in 2003 to 67 units during 2004 (excluding units shipped under the ComEd VNPP program). The decline in EnergySaver related revenue was directly attributable to our decision to focus on utility programs such as the ComEd and PacifiCorp VNPP programs, rather than on commercial sales as we had in past years. As of December 31, 2004, we had shipped 89 EnergySavers to 52 customer hosts under the ComEd program, but we had not recognized revenue related to this program pending completion of an amendment to the existing agreement with ComEd. This amendment was never completed due to a delay in approval of regulatory changes necessary to implement portions of the amendment.

The ComEd VNPP is structured as a service agreement with a 13 year term in which Lime Energy will provide up to 50 MWs of curtailment capacity to ComEd at a fixed price per kilowatt of installed capacity, payable quarterly in arrears whether the capacity is used or not as the capacity is installed. We will recognize revenue and expense under the ComEd program over the life of the contract. The PacifiCorp program is similar to the existing ComEd contract, as a result, revenue and expenses will be recognized over the 10-year term of the contract. Both contracts are structured such that there are no penalties for delivering less than the targeted curtailment capacities, but we will only be compensated for the actual curtailment capacity delivered.

Gross Profit. Our consolidated gross profit declined \$463,714 to a loss of \$128,736 during 2004, as compared to \$334,978 earned during 2003. The decline in profitability was due primarily to the decline in revenue and the shift in focus to our utility programs.

SG&A Expenses. Selling, general and administrative expenses increased \$313,118 or 8% to \$4,234,239 in 2004 from \$3,921,121 in 2003. The increase in SG&A expense was primarily due to legal costs related to an arbitration we were involved in with a dealer which contributed to a \$640,000 increase in legal expenses during 2004. If it were not for this legal expense our SG&A would have declined year over year as a result of reductions in labor costs, sales commissions to third party dealers and distributors and travel and entertainment expenses. The dealer arbitration was settled in February 2005.

Other Non-Operating Income (Expense). Other non-operating expense is comprised of interest expense and interest income. Interest expense increased \$283,302 to \$648,554 during 2004 from \$365,252 in 2003. Almost all of the increase in interest expense during 2004 was due to a \$268,815 increase in amortization of deferred issuance costs and the original issue discount. Interest expense included amortization expense totaling \$574,437 for 2004 as compared to \$305,622 for 2003. Interest income increased \$12,194 or 118.3% to \$22,505 for 2004 as compared to \$10,311 for 2003. The increase in interest income was the result of higher interest rates earned on invested balances and higher average invested balances.

Discontinued Operations. During 2003 we agreed to sell substantially all of the assets and to transfer most of the liabilities of our Power Management segment to a group of investors that included members of the segment's management. The sale closed on June 3, 2003, effective as of May 31, 2003. As required by SFAS 144 we have presented the operating results as well as the loss on disposal for this segment as discontinued operations. Also, effective March 31, 2006, we sold our Building Controls and Automation business to its former owners. The operating results for this business are also included in the loss from operations of discontinued operations. During the twelve-month period ended December 31, 2003 the operating loss for these two segments totaled \$776,710 and in addition, we recognized a \$764,148 loss on the disposal of the Power Management segment during 2003.

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Preferred Stock Dividends. The dividend expense recognized during 2004 and 2003 was comprised of the following:

<i>Year ended December 31,</i> 	2004	2003
Accrual of dividend on Series A Convertible Preferred	\$ 540,705	\$ 2,253,978
Accrual of Series C Preferred dividend	53,206	219,712
Accrual of Series D Preferred dividend	35,932	77,689
Accrual of Series E Preferred dividend	1,006,937	
Deemed dividend associated with beneficial conversion price on shares issuable in satisfaction of preferred dividends	1,127,021	1,879,554
Deemed dividend associated with beneficial conversion feature of Series D Preferred stock		386,984
Deemed dividend associated with the redemption and exchange of outstanding preferred stock	1,860,458	
Deemed dividend associated with change in the expiration date of warrants to purchase shares of preferred stock	15,000	
Total	\$ 4,639,259	\$ 4,817,917

Our dividend expense for 2004 declined \$178,658 or 3.7% to \$4,639,259 from \$4,817,917 for 2003. We accrued dividends of \$1,636,780 and \$2,551,379 on our Convertible Preferred Stock during 2004 and 2003, respectively. This decline in accrued dividends was the result of the reduction in the number of preferred shares outstanding and a reduction in the dividend rate that resulted from the redemption and exchange effected in March 2004. Also contributing to the decline was a reduction in the number of preferred shares outstanding resulting from the voluntary conversion of shares of preferred stock into 130,447 shares of common stock. The dividends accrued during 2004 and 2003 were satisfied through the issuance of 16,368 shares of preferred stock (convertible into 109,120 shares of common stock) and 255,138 shares of preferred stock (convertible into 170,092 shares of common stock), respectively. We were required to recognize non-cash deemed dividends of \$1,127,021 and \$1,879,554 during 2004 and 2003, respectively, due to the fact that the conversion price on these dividend shares was lower than the market price of our common stock on the date of issue. As part of the redemption and exchange completed in March 2004, shares of Old Preferred stock were exchanged for shares of the Series E Preferred Stock at the rate of 10 shares of Old Preferred for each share of new Series E preferred stock. Additionally, each share of Old Preferred stock was convertible into 0.67 shares of common stock, whereas each share of new Series E Preferred Stock is convertible into 6.67 shares of common stock. The decline in this deemed dividend is primarily the result of the reduction in the difference between the market price of our common stock and the conversion price of the dividend shares on the date of issuance of these dividend shares. In addition, despite the fact that we believe the redemption and exchange transaction was favorable for the Company and its common stockholders (see note 17(k) to the financial statements), we were required to record a non-cash deemed dividend on the transaction of \$1,860,458. For

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accounting purposes the transaction was viewed as a redemption for cash and shares of Series E Preferred stock. The non-cash deemed dividend was determined by comparing the fair value of the consideration given (the cash and the market value of the Series E Preferred Stock) to the carrying value of the preferred stock that was redeemed. The fair value of the consideration given exceeded the carrying value of the existing preferred primarily due to the fact that the market price of our common stock was higher on the day the redemption and exchange transaction closed than it was when the shares of the Old Preferred stock were originally issued. We also incurred a \$15,000 deemed dividend during 2004 when we agreed to extend the expiration date on warrants to purchase shares of our Series E Preferred stock from September 30, 2004 to December 31, 2004. We agreed to extend these warrants to permit holders who participated in the redemption and exchange more time to exercise their warrants so that if they chose to exercise they could do so without violating the short swing trading rules of section 16(b) of the Securities Act of 1934 or our insider trading policy, which prohibits the trading of our securities during certain blackout periods prior to the filing of our financial statements. Dividend expenses for 2003 also included \$386,984 of non-cash deemed dividends associated with the issuance of the Series D Convertible Preferred Stock. Again this was due to the fact that the conversion price on the Series D was lower than the market price when the shares of Series D were issued.

Liquidity and Capital Resources

During the twelve-month period ended December 31, 2005 we incurred a net loss of \$6.9 million and used \$7.0 million of cash for operating activities. Primarily as a result of our continuing losses and lack of liquidity our independent registered public accounting firm modified their opinion on our December 31, 2005 Consolidated Financial Statement to contain a paragraph wherein they expressed a substantial doubt about our ability to continue as a going concern. We have taken steps to improve our current liquidity and provide the growth capital necessary to fund our plan for 2006 and for future growth. Our efforts to raise additional capital are discussed below.

As of September 30, 2006 we had cash and cash equivalents of \$6,825,874 compared to \$4,229,150 on December 31, 2005. Our debt obligations as of September 30, 2006 consisted of a mortgage of \$535,000 on our facility in Elk Grove Village Illinois, vehicle loans of \$45,186, capitalized leases of \$665 and a demand note payable to a shareholder of \$150,000.

Our principal cash requirements are for operating expenses, including employee costs, the costs related to research and development, advertising costs, the cost of outside services including those providing accounting, legal, engineering and consulting services, rent, the funding of inventory and accounts receivable, and capital expenditures and the costs of servicing our outstanding debt. We have financed our operations since inception through the private placement of our common stock and preferred stock and through various secured and unsecured loans.

The following table summarizes, for the periods indicated, selected items in our consolidated statement of cash flows:

<i>Nine months ended September 30,</i>	2006	2005
Net cash used in operating activities	\$ (4,335,193)	\$ (5,117,933)
Net cash used in investing activities	(4,043,271)	(2,114,761)
Net cash provided by financing activities	10,975,188	7,017,254
Net Increase (Decrease) in Cash and Cash Equivalents	2,596,724	(215,440)
Cash and Cash Equivalents, at beginning of period	4,229,150	1,789,808
Cash and Cash Equivalents, at end of period	\$ 6,825,874	\$ 1,574,368

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Nine Months Ended September 30, 2006 Compared to Nine Months Ended September 30, 2005.

Net cash increased \$2,596,724 during the first nine months of 2006 as compared to decreasing \$215,440 during the same period in 2005.

Operating Activities

Cash consumed by operating activities decreased \$782,740 or 15% to \$4,335,193 during the first nine months of 2006 as compared to consuming \$5,117,933 during the same period in 2005. Cash used to fund the net loss before changes in working capital, increased \$620,794 or 17%, to \$4,325,001 during the first nine months of 2006 from \$3,704,207 during the first nine months of 2005. This increase was due to increases in SG&A and interest expense.

Changes in working capital (adjusted for business acquisitions and disposals) consumed cash of \$10,192 during the first nine months of 2006 as compared to consuming cash of \$1,413,726 during the first nine months of 2005. During the first nine months of 2006, reductions in accounts payable and accrued expenses were largely offset by declines in accounts receivable, inventories and the advances to suppliers. The decline in accounts receivable was the result of an improvement in collections, while a deliberate effort to reduce our inventories led in part to the reduction in inventory balances. During 2005, approximately \$900,000 was used to satisfy liabilities assumed as part of the acquisition of MPG, including accounts payable and accrued expenses. Increases in inventory and reductions in accounts payable, accrued expenses and deferred revenue at our other businesses also contributed to the increase in cash used for working capital purposes. The inventory increase was related to jobs we were working to complete before the end of the year. The reduction in accounts payable and deferred revenue was the result of completion of the long-term contract in our building automation controls segment. Accrued expenses declined as we paid certain accrued liability during the first half of 2005. These uses of cash were partially offset by a decline in our accounts receivable as we received payment during the first nine months of 2005 for the building automation control projects completed during the fourth quarter of 2004 and first quarter of 2005.

Investing Activities

Cash used in investing activities increased \$1,928,510 to \$4,043,271 during the nine-month period ended September 30, 2006, from \$2,114,761 for the same period in 2005. As part of the June 30, 2006 acquisition of Parke we paid the selling stockholder \$2.72 million in cash and incurred expenses related to the transaction of \$134,680. This was partially offset by cash balances of \$1,710 acquired as part of the transaction. Cash used to fund the Kapadia acquisition included \$1,106,064 for the cash portion of the acquisition consideration and \$18,415 for legal expenses, offset by \$47,329 of cash in Kapadia's bank accounts on the date of acquisition. Also during 2006 we sold all of the stock of Great Lakes Controlled Energy Corporation to the former owners of that company. Great Lakes' cash balances of \$83,586 were transferred with the sale of the company. During 2005 we acquired MPG, which closed in May 2005. We paid the selling MPG stockholders \$1,643,525 in cash and incurred \$137,386 in transaction related costs. This was partially offset by cash balances of \$136,492 acquired as part of the transaction. Purchases of property and equipment declined \$440,777 largely due to reduced rate of investment in assets associated with the ComEd Virtual Negawatt Power Plant (VNPP).

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Financing Activities

Financing activities generated cash of \$10,975,188 during the first nine months of 2006 as compared to \$7,017,254 during the first nine months of 2005. In June 2006 we raised \$17,875,000 in gross proceeds through the sale of our common stock, while incurring \$101,162 in costs related to the issuance. We used \$5,038,030 million of the proceeds to pre-pay the principal on two Laurus convertible term loans and Laurus converted \$943,455 outstanding on the revolving note to common stock. Also during 2006 we used \$1,056,545 to pay down our revolver, \$304,075 for scheduled principal payments and \$400,000 to pay off the balance on Parke's revolver.

During the first nine months of 2005, we generated cash of \$5,625,000 through the issuance of common stock and warrants to a group of investors and \$2 million through borrowing on our line of credit. This was partially offset by issuance costs of \$216,787 and scheduled principal payments on our various loans of \$390,959.

LIQUIDITY

Our primary sources of liquidity are our available cash reserves. As of September 30, 2006 our cash balance was \$6,825,874.

Our ability to continue the development, manufacturing and expansion of sales of our products and services will require the continued commitment of significant funds. The actual timing and amount of our future funding requirements will depend on many factors, including the amount and timing of future revenues, the level and amount of product marketing and sales efforts, the magnitude of research and development, and our ability to improve margins on our products.

During the last five years we have raised net proceeds of approximately \$60 million through the issuance of shares of our common and preferred stock, which has allowed us to continue to execute our business plan. Most of these funds have been consumed by operating activities, either to fund our losses, for working capital requirements or for acquisitions. In an attempt to move the Company to a position where it can start to generate positive cash flow our management has set the following key objectives for 2006:

Focus on increasing the commercial sales of our products and services. In June 2006 we acquired Parke Industries and as part of this acquisition Dan Parke became our President and Chief Operating Officer. During the last 3 months Dan has spent a great deal of time and effort expanding, training and integrating the sales and marketing staffs of our three companies (now four with the addition of Kapadia). His goal is to have at least 20 fully trained sales people on our staff by the end of the year, each with the ability to sell \$1 million to \$2 million annually. If we are successful in achieving these goals we believe we will begin to see a significant increase in revenue beginning in the first quarter of 2007.

Expand and improve the product line through internal development or acquisition. An expanded product line would allow us to offer additional solutions to our customers, thereby increasing the value of each customer relationship. We have recently begun an internal R&D process to improve our existing products in order to expand their markets, reduce their costs and extend their useful lives. We are also constantly evaluating acquisition opportunities with the view toward adding new products and services to our product line and expanding our geographic market.

Aggressively manage our costs in order to conserve cash. We have made some progress in reducing our costs during the last several years, but we plan to focus on eliminating redundant operations and leveraging the synergies available as a result of the acquisition of MPG, Parke and Kapadia to further reduce our costs.

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Sell our Building Automation Controls business. This sale, which was completed effective March 31, 2006 will allow us to focus exclusively on the sale of our Energy Technology and Energy Services products and services and is expected to reduce the cash consumed in future periods.

Secure additional capital to continue to fund operations until the business turns cash flow positive. The PIPE Transaction that closed in June 2006 satisfied this objective. While we may be able to raise additional capital through the recently announced rights offering, the purpose of the rights offering is primarily to allow our stockholders the opportunity to reduce some of the dilution in ownership sustained as a result of the PIPE Transaction. We hope that the capital raised this year will be sufficient to carry us to the point that our business begins to generate positive cash flow, thereby alleviating the need to raise additional capital in the future.

We believe that if we are successful in achieving these priorities we should have sufficient liquidity to allow us to operate until our operations turn cash flow positive. If we are not able to achieve some or all of these priorities we may begin to experience a liquidity shortage sometime in the future which could force us to scale back our growth plans, or, in the worst case, cease operations.

If we raise additional capital in future periods (which may require stockholder approval), our existing stockholders will likely experience dilution of their present equity ownership position and voting rights, depending upon the number of shares issued and the terms and conditions of the issuance. Any new equity securities could have rights, preferences or privileges senior to those of our common stock.

Contractual Obligations

Our obligations to make future payments under contracts as of December 31, 2005 were as follows:

	Total	Payments due by period			More than 5 years
		Less than 1 year	1 to 3 years	3 to 5 years	
Contractual Obligations					
Long-term debt (1)(2)	\$ 5,873,702	\$ 654,695	\$ 1,578,657	\$ 3,640,350	\$
Capital leases	4,739	4,386	353		
Operating leases	336,358	78,753	134,506	123,099	
Employment agreements	525,000	225,000	300,000		
Total	\$ 6,739,799	\$ 962,834	\$ 2,013,516	\$ 3,763,449	\$

(1) Excludes floating rate interest on the long-term debt. Interest payments required during 2006, based on the debt outstanding at December 31, 2005 and the then current interest rates, are projected to

be \$515,000.

- (2) On June 29, 2006 we repaid the convertible term loans which represented \$5,291,790 of the long term debt obligations and \$472,000 of the projected future interest expense as of December 31, 2005.

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Recent Accounting Pronouncements

In June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48 (FIN 48), *Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109*, which establishes that the financial statement effects of a tax position taken or expected to be taken in a tax return are to be recognized in the financial statements when it is more likely than not, based on the technical merits, that the position will be sustained upon examination. FIN 48 is effective for fiscal years beginning after December 15, 2006. The adoption of FIN 48 is not expected to have a material impact on our results of operations or our financial position.

In September 2006, the SEC staff issued Staff Accounting Bulletin No. 108 (SAB 108), *Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements*. SAB 108 was issued in order to eliminate the diversity of practice in how public companies quantify misstatements of financial statements, including misstatements that were not material to prior years' financial statements. We will initially apply the provisions of SAB 108 in connection with the preparation of our annual financial statements for the year ending December 31, 2006. We have evaluated the potential impact SAB 108 and do not believe it will have any impact on our financial position and results of operations.

Quantitative and Qualitative Disclosures About Market Risk

The only significant exposure the Company has to market risk is the risk of changes in market interest rates. The interest rates on the Company's mortgage is variable and changes with changes in the prime rate. The interest rate on the mortgage is equal to the prime rate plus 1/2%. As of September 30, 2006, the prime rate was 8.25%. If the prime rate were to increase 1 percentage point, the aggregate annual interest cost on the mortgage, term loans and revolving loan would increase by approximately \$5,400.

DESCRIPTION OF PROPERTY

Our headquarters and the EnergySaver system production facility are located at 1280 Landmeier Road in Elk Grove Village, Illinois. This facility is approximately 13,000 square feet and houses the corporate headquarters, manufacturing operations and warehouse. We acquired this facility in August 1998 with a combination of stock and cash. The cash portion of the purchase price was financed through a mortgage on the building. The mortgage was refinanced in December 2005, bears interest at the rate of prime (currently 8.25%) plus 0.5%, and is payable in monthly installments of \$3,000 plus interest, until a final balloon payment which is due on February 2007. There is no penalty for prepayment of the mortgage. As of November 15, 2006, the outstanding principal amount of the mortgage was \$529,000.

On May 3, 2005, we acquired Maximum Performance Group, Inc (MPG). MPG currently leases a 2,800 square foot office in New York City and a 3,100 square foot office in San Diego, California. The New York office lease has a term of five years and will expire in September 2010. The San Diego lease expired during 2005 and is currently operating on a month to month basis with a 90 day termination notice requirement.

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On June 30, 2006, we acquired Parke P.A.N.D.A. Corporation (now known as Parke Industries, LLC) (Parke). Parke leases 5,000 square foot office in Glendora, California. The lease which expires on December 31, 2009 provides for monthly rent of \$3,500, increasing 3% on the first of each year beginning on January 1, 2007. The building is owned by the former stockholder of Parke, Daniel Parke, who is currently Lime Energy s President, Chief Operating Officer and a Director.

On September 26, 2006, we acquired Kapadia Consulting, Inc. (now known as Kapadia Energy Services, Inc.), effective September 27, 2006. Kapadia leases a 2,000 square foot office in Peekskill, NY and a 918 square foot office in Ventura, California. The New York lease expired in 2000 and is operating on a month to month basis. The California lease expires on October 31, 2007.

We believe that the space and location of our current facilities in combination with the current and planned outsourcing of a portion of our manufacturing will be sufficient to reach a level of production projected for the current year. See Manufacturing under Description of Our Business .

CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

During January 2006, we entered into a consulting agreement with Parke P.A.N.D.A. Corporation to provide sales and marketing consulting services. Parke is a company which at the time was beneficially owned by Daniel Parke, one of our directors. Pursuant to the consulting agreement we agreed to pay Parke \$10,000 per month and to reimburse it for any expenses incurred as a result of its work. We paid Parke a total of \$61,155 during the six months ended June 30, 2006. This agreement was terminated in May 2006.

On June 29, 2006 we completed a sale of 17,875,000 shares of our common stock, at a price of \$1.00 per share, to a group of 17 investors, including 10 (of the 11) holders of our Series E Convertible Preferred Stock (the PIPE Transaction), and the holders of the Series E converted all of the outstanding shares into shares of common stock, based on a conversion price of \$1.00 per share for the common stock. Three of the former Series E Preferred stockholders (Messrs. Kiphart, Asplund and Valentine) are members of our Board of directors. Also, on June 30, 2006, we acquired Parke P.A.N.D.A. Corporation (Parke), a company owned by Daniel Parke, another of our directors.

Due to potential conflicts of interest resulting from (i) the beneficial ownership of Parke P.A.N.D.A. Corporation by Daniel Parke, and (ii) certain members of our Board (Messrs. Kiphart, Asplund and Valentine) beneficially owning shares of Series E Preferred Stock and agreeing to purchase shares of common stock in the PIPE Transaction and concurrently convert their shares of Series E Preferred Stock into shares of our common stock, our board established a special committee comprised solely of disinterested, independent directors to review, negotiate and approve the acquisition of Parke P.A.N.D.A. and the PIPE Transaction. The special committee retained Rittenhouse Capital Partners, LLC (Rittenhouse) to act as its financial advisor, and legal counsel to assist it in its review of these transactions. Rittenhouse reviewed the Parke acquisition and delivered to the special committee an opinion to the effect that the purchase price paid for Parke was fair to us from a financial point of view. It also provided information, advice and analysis to assist the committee in its review of the structure and pricing of the PIPE Transaction. Legal counsel assisted the special committee in its review of these transactions and advised the committee on its duties and responsibilities. After considering all of the information it had gathered, the committee concluded that these transactions were in the best interests of the Company and its stockholders, and approved the Parke acquisition and the PIPE Transaction.

As part of the acquisition of Parke P.A.N.D.A. Corporation, we assumed its existing office lease for space in a building owned by Daniel Parke in Glendora California. We believe that the terms of the lease are fair as they are comparable to the terms of leases with other third party tenants located in the building.

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In August 2006, the Company retained Corporate Resource Development, Inc. (CRD), a company owned by William Carey, one of Lime Energy's directors, to provide sales and marketing training and support. Under the agreement, which was reviewed and approved by Lime Energy's Board of Directors, the Company will pay CRD \$52,500, plus expenses for its services. In January 2006, prior to Mr. Carey's appointment to Lime's Board, CRD was retained to provide sales consulting services to the Company and was paid \$10,000 plus expenses for its services.

MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

From December 12, 2000 to June 9, 2006, our common stock was listed on the American Stock Exchange under the trading symbol ELC. From June 12, 2006 through September 21, 2006, our common stock traded on the OTC Bulletin Board under the trading symbol ELCY. Since September 22, 2006 our stock has traded on the OTC Bulletin Board under the symbol LMEC.

In June, 2006, we announced a 1 for 15 reverse split of our common stock, effective on June 15, 2006 and since that date, our common stock has been trading on that basis. See Recent Events *Reverse Stock Split* for more information about the matter.

The closing price of our common stock on January 24, 2007 was \$1.10. The following table sets forth the quarterly high and low selling prices for our common stock as reported on The American Stock Exchange and OTC Bulletin Board since January 1, 2004, adjusted for the reverse split.

	Common Stock	
	High	Low
Fiscal Year Ended December 31, 2004:		
Fiscal Quarter Ended March 31, 2004	\$37.05	\$25.50
Fiscal Quarter Ended June 30, 2004	\$31.20	\$23.25
Fiscal Quarter Ended September 30, 2004	\$28.95	\$16.65
Fiscal Quarter Ended December 31, 2004	\$21.30	\$15.75
Fiscal Year Ended December 31, 2005:		
Fiscal Quarter Ended March 31, 2005	\$19.50	\$12.90
Fiscal Quarter Ended June 30, 2005	\$16.05	\$12.15
Fiscal Quarter Ended September 30, 2005	\$18.60	\$10.05
Fiscal Quarter Ended December 31, 2005	\$13.65	\$ 7.50
Fiscal Year Ended December 31, 2006:		
Fiscal Quarter Ended March 31, 2006	\$16.80	\$ 8.40
Fiscal Quarter Ended June 30, 2006	\$10.20	\$ 0.70
Fiscal Quarter Ended September 30, 2006	\$ 1.40	\$ 0.75
Fiscal Quarter Ended December 31, 2006	\$ 1.29	\$ 0.76

 Holders

As of January 23, 2007 we had approximately 4,850 holders of record of our common stock and 50,093,527 shares of common stock outstanding.

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Dividends

For the nine months ended September 30, 2006, we declared and paid the following dividends on our preferred stock:

On March 8, 2006, our Board of Directors declared dividends payable on our Series E Convertible Stock for the calendar quarter ending March 31, 2006 to shareholders of record of the Series E Preferred Stock as of March 31, 2006. The dividends were paid with 3,489 additional shares of Series E Preferred Stock. Each share of Series E Preferred Stock is convertible into 6.67 shares of our common stock.

Effective June 29, 2006, our Board of Directors declared dividends payable on our Series E Preferred Stock of \$349,100. The dividends were paid with 3,491 additional shares of Series E Convertible Preferred Stock.

On June 29, 2006 all of the outstanding shares of Series E Convertible Preferred stock were converted into shares of common stock, thus there will not be any dividends in future periods related to this issue of preferred stock

For a further discussion regarding preferred stock dividends, see Management's Discussion and Analysis of Financial Condition and Results of Operations Preferred Stock Dividends.

We have never declared or paid any cash dividends on our common stock and we do not anticipate paying any cash dividends in the foreseeable future. See Management's Discussion and Analysis and Results of Operations Liquidity and Capital Resources.

Table of Contents**EXECUTIVE COMPENSATION****Summary Compensation Table**

The following table summarizes the total compensation paid or awarded to each of our named executive officers whose total compensation exceeded \$100,000 during the fiscal year ended December 31, 2005 and for each of our fiscal years ended December 31, 2004 and 2003. No bonuses were earned during any of the fiscal years reported on the following table.

Name and Principal Position	Year Ended	Salary (1)	Bonus	Annual	Long	All Other
				Compensation	Term	
				Other	Securities	
				Annual	Underlying	Compensation
					Options	(2)
					(#)	
John P. Mitola	12/31/05	\$246,875		\$ 6,600(4)		\$ 8,690
<i>our former chief executive officer</i> (3)	12/31/04	\$247,396		\$ 6,600(4)		\$ 8,294
	12/31/03	\$233,844		\$ 6,660(4)	50,000	\$ 3,552
Leonard Pisano (5)	12/31/05	\$151,322		\$49,773(6)	31,667	
<i>our chief operating officer</i>	12/31/04					
	12/31/03					
Jeffrey R. Mistarz	12/31/05	\$207,375				\$ 6,238
<i>our chief financial officer and treasurer</i>	12/31/04	\$207,812				\$ 6,084
	12/31/03	\$159,070			26,667	\$ 8,312
Denis Enberg	12/31/05	\$207,375				
<i>our former executive vice president of engineering</i>	12/31/04	\$193,594			3,333	
	12/31/03	\$160,417				\$ 759
Eugene Borucki (7)	12/31/05	\$148,125			6,667	
<i>the former President of Great Lakes Controlled Energy</i>	12/31/04	\$144,375			667	
	12/31/03	\$128,333				\$ 759

(1) Certain employees of the Company, including Messrs. Mitola, Pisano, Mistarz, Enberg and Borucki voluntarily reduced their salaries for all of 2003 and

portions of 2004
and 2005.

(2) Amounts of All
Other
Compensation
are the amounts
paid for
long-term
disability
insurance for
the Named
Officers and the
cost of life
insurance for
Messrs. Mitola
and Mistarz.

(3) Mr. Mitola
resigned as our
Chief Executive
Officer effective
January 22,
2006.

(4) This represents
a monthly auto
allowance of
\$550 for
Mr. Mitola.

(5) Mr. Pisano
became our
Chief Operating
Officer in
May 2005 after
the acquisition
of Maximum
Performance
Group, Inc.
where he served
as president
both before and
after we
acquired it.

(6) This represents
a monthly auto
allowance of
\$500 and the
payment of

\$45,773 of
deferred salary.

- (7) Mr. Borucki is not an executive officer of the Company but is included for purposes of compensation disclosure.

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Employment Contracts, Termination of Employment and Change-in-Control Arrangements

John Mitola

Effective January 1, 2003, we entered into an employment agreement with John Mitola for a three-year period ending on December 31, 2005. This agreement, which was structured to place more emphasis on achieving important corporate milestones, reduced Mr. Mitola's base salary to \$250,000 per year, but provided for a discretionary bonus of up to one hundred percent of his annual salary payable if he met or exceeded certain annual goals as established by the Board of Directors, and a guaranteed bonus of \$250,000 upon the achievement of two consecutive calendar quarters of positive net income by the Company (such net income to be that as reflected in the Company's quarterly reports filed with the Securities and Exchange Commission). The agreement also provided for a monthly automobile allowance of \$550.00 and the reimbursement of Mr. Mitola's business-related expenses.

As part of the employment agreement, we granted to Mr. Mitola an option to purchase 50,000 shares of our common stock at a price per share of \$12.68, which was equal to the average closing price of the Company's common stock as measured over the thirty (30) trading day period prior to the effective date of the contract. The option granted vested in amounts of 16,667 shares on each December 31st of 2003, 2004 and 2005, except on a change of control in which case all the options would have immediately vest. Except as specifically set forth in the employment agreement, such options are governed by the Company's 2001 Stock Incentive Plan.

The employment agreement imposed on Mr. Mitola non-competition, non-solicitation and confidentiality obligations.

Mr. Mitola resigned from the Company in January 2006.

David R. Asplund

Effective January 23, 2006 we entered an employment contract with David Asplund for a three year period ending January 22, 2009 to serve as the Company's Chief Executive Officer. The contract provides for a base annual salary of \$285,000 and eligibility for up to \$65,000 of cash bonus compensation each year, based on the Company's performance. For 2006, the bonus will be based on consolidated gross revenue, with \$15,000 payable if gross revenue exceeds \$10 million, an additional \$15,000 payable if gross revenue exceeds \$12.5 million, an additional \$15,000 payable if gross revenue exceeds \$16 million and an additional \$20,000 payable if gross revenue exceeds \$18 million. The bonus formula for the second and third contract years has not been determined but is to be based on our consolidated net income for such years.

In addition to base salary and bonus, we granted to Mr. Asplund ten-year options to purchase up to 100,000 shares for each of the three contract years, with such options vesting in arrears on the following January 22nd. The option price for the first 100,000 shares is \$9.30, which was the 30 day average closing price of our common stock, determined on Friday, January 20, 2006, which was the last business day prior to the day Mr. Asplund began serving as CEO. Those options became vested on January 23, 2007. The option price for each of the subsequent grants is to be based on the market price on January 23, 2007 and January 23, 2008, respectively, using greater of (x) the 30 day average closing price of our common stock, determined on each such date, or (y) the closing price of the common stock on January 22, 2007 or 2008 (as applicable). All such options are governed by our 2001 Incentive Stock Plan, as amended, except as set forth in the employment agreement.

Vesting of any unvested options will accelerate upon termination by the Company of Mr. Asplund's employment under the employment agreement (if such termination is for reasons other than "Due Cause" (as defined in the employment agreement)). Vesting will also accelerate upon termination due to Mr. Asplund's death and upon a change of control. In the event of termination for Due Cause, all unexercised options

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terminate immediately, whether vested or unvested. In the event of termination due to Mr. Asplund's disability or due to his resignation (other than resignation pursuant to the Company's breach), unvested options will terminate immediately, and vested options will be exercisable only for 180 days (if termination is due to disability) or for 90 days (if termination is due to Mr. Asplund's resignation). In the event of termination for the convenience of the Company, or by Mr. Asplund because of a breach by the Company, then all options which are scheduled to vest within one year shall vest immediately and be exercisable for one year thereafter. These options will otherwise expire on the January 22, 2016.

Change of control is defined as a merger or consolidation of the Company resulting in an unrelated entity acquiring the power to elect a majority of the Company's Board of Directors, or a sale of substantially all of the Company's assets to an entity that is not then controlled by or affiliated with the Company. In the event that a change of control occurs and Mr. Asplund's employment period is terminated by the Company, any unvested options will vest and be exercisable for one year. All stock options which are not exercised within one year following such termination shall thereupon expire and no longer be exercisable.

The employment agreement imposes on Mr. Asplund non-competition, non-solicitation and confidentiality obligations, which are not separately compensated. The non-competition obligation covers the employment period and extends for two years after termination.

On July 11, 2006, Mr. Asplund was granted additional options to purchase up to 4.3 million shares, with his right to exercise such options vesting with respect to 1.5 million options on December 31, 2006; 1.4 million options on December 31, 2007 and 1.4 million options on December 31, 2008. The exercise price on the 1.5 million options vesting on December 31, 2006 is \$1.02 per share. The exercise price on the 1.5 million options vesting on December 31, 2007 shall be equal to the average closing market price of the Company's common stock on the 30 days prior to December 31, 2007, or the closing market price on December 31, 2007, whichever is greater. The exercise price on the 1.5 million options vesting on December 31, 2008 shall be equal to the average closing market price of the Company's common stock on the 30 days prior to December 31, 2008, or the closing market price on December 31, 2008, whichever is greater. Vesting of the options will accelerate upon termination for reasons other than due cause (as defined in the option agreement), death, disability or resignation and upon a change of control. These options will expire on the earlier of January 22, 2016, or six months following the date that Mr. Asplund is no longer an employee of the Company, unless his termination was for due cause (as defined in the option agreement) in which case they will expire immediately, or due to a change of control (as defined in the option agreement) in which case they will expire twelve months following the change of control. These options contain a cashless exercise provision permitting Mr. Asplund to pay the purchase price for any shares acquired by exercising the option by surrendering to the Company a number of shares of common stock having an aggregate market value equal to the purchase price.

Leonard Pisano

Effective May 3, 2005 our subsidiary, Maximum Performance Group, entered into an employment agreement with Leonard Pisano to serve as its president for a three-year period ending May 2, 2008. We also appointed him Chief Operating Officer of Lime Energy, a position which he held until June 30, 2006, when he became executive vice president of sales of Lime Energy. The employment agreement provides for a base salary of \$225,000 plus a monthly auto allowance of \$500. In addition, Mr. Pisano is eligible to receive a \$50,000 bonus upon the Company's achievement of two consecutive quarters of positive EBITDA and to participate in an annual bonus plan with certain other management employees as determined by the Board of Directors. The employment agreement also provides that Mr. Pisano shall have board observation rights such that he may attend meeting of the Company's Board of Directors as an observer during the employment term. The agreement also provides that Mr. Pisano is to be granted options to purchase 31,667 shares of our common stock at \$15.00 per share. These options vest 5,000 on the effective date of the agreement, 8,889 shares on the each of the remaining anniversaries of the agreement, except on a change of control in which case all the options will immediately vest.

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The employment agreement imposes on Mr. Pisano non-competition, non-solicitation and confidentiality obligations, which are not separately compensated. The non-competition obligation covers the employment period and extends for two years after termination.

On July 11, 2006, Mr. Pisano was awarded options to purchase up to 1,350,000 shares of the Company's stock at \$1.02 per share. The options vest in three equal amounts, with 450,000 vesting on December 31, 2006, 450,000 vesting on December 31, 2007 and 450,000 vesting on December 31, 2008, in each case assuming that Mr. Pisano continues to be employed by the Company on such date. Vesting of the options will accelerate upon termination for reasons other than due cause (as defined in his option agreement), death, disability or resignation and upon a change of control. These options will expire on the earlier of July 11, 2016, or six months following the date that Mr. Pisano is no longer an employee of the Company, unless his termination is for due cause (as defined in the option agreement) in which case they will expire immediately, or due to a change of control (as defined in the option) in which case they will expire twelve months following the change of control. These options contain a cashless exercise provision permitting Mr. Pisano to pay the purchase price for any shares acquired by exercising the option by surrendering to the Company a number of shares of common stock having an aggregate market value equal to the purchase price.

Jeffrey Mistarz

Effective January 1, 2003, we entered into an employment agreement with Mr. Mistarz for a three-year period ending on December 31, 2005. This agreement provided for an annual base salary of \$175,000 through December 31, 2003, which increased to \$210,000 effective January 1, 2004. In addition, Mr. Mistarz was eligible to participate in an annual bonus plan with certain other management employees. The agreement provided Mr. Mistarz with options to purchase 26,667 shares of our common stock at a price of \$15.00 per share, which options vested 8,889 shares each on December 31, 2003, 2004 and 2005. Except as specifically set forth in the employment agreement, such options are governed by the Company's 2001 Stock Incentive Plan.

On August 15, 2006, we entered into a new employment agreement with Mr. Mistarz to serve as our Executive Vice President and Chief Financial Officer for a two-year period ending August 14, 2008. The employment agreement provides for a base salary of \$210,000. In addition, Mr. Mistarz is eligible to participate in an annual bonus plan with certain other management employees as determined by the Board of Directors. The employment contract also provides that Mr. Mistarz is to be granted options to purchase 300,000 shares of our common stock at \$1.00 per share. The options vest in three equal amounts, with one third vesting upon signing of the employment contract, the second third vesting on the first anniversary of the employment contract and the final third vesting on the second anniversary of the employment contract. Vesting of the options will accelerate upon termination for reasons other than Due Cause (as defined in the contract) death, disability or resignation and upon a change of control. The employment agreement also imposes non-competition, non-solicitation and confidentiality obligations on Mr. Mistarz, which are not separately compensated. The non-competition obligation covers the employment period and extends for two years after termination.

On July 11, 2006, Mr. Mistarz was awarded options to purchase up to 750,000 shares of the Company's stock at \$1.02 per share. The options vest in three equal amounts, with 250,000 vesting on December 31, 2006, 250,000 vesting on December 31, 2007 and 250,000 vesting on December 31, 2008, in each case assuming that Mr. Mistarz continues to be employed by the Company on such date. Vesting of the options will accelerate upon termination for reasons other than due cause (as defined in his option agreement), death, disability or resignation and upon a change of control. These options will expire on the earlier of July 11, 2016, or six months following the date that Mr. Mistarz is no longer an employee of the Company, unless his termination is for due cause (as defined in the option agreement) in which case they will expire immediately, or due to a change of control (as defined in the option) in which case they will expire twelve months following the change of control. These options contain a cashless exercise

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provision permitting Mr. Mistarz to pay the purchase price for any shares acquired by exercising the option by surrendering to the Company a number of shares of common stock having an aggregate market value equal to the purchase price.

Daniel Parke

Effective June 30, 2006, Parke Industries, LLC entered into an employment agreement with Daniel Parke to serve as its president for a two-year period ending June 30, 2008. We also appointed him President and Chief Operating Officer of Lime Energy Co. The employment agreement provides for a base salary of \$250,000 plus a monthly auto allowance of \$800. In addition, Mr. Parke is eligible to participate in an annual bonus plan with certain other management employees as determined by the Board of Directors. The employment contract also provides that Mr. Parke is granted options to purchase 46,667 shares of our common stock at \$1.10 per share. These options vest 15,555 on the effective date of the agreement, 15,556 shares on the first anniversary of the agreement and 15,556 on the second anniversary of the agreement. Vesting of the options will accelerate upon termination for reasons other than Due Cause (as defined in the contract) death, disability or resignation and upon a change of control. In the event that Mr. Parke's employment terminates for Due Cause (as defined therein), all unexercised options terminate immediately, whether or not vested. In the event of termination of such employment by reason of death or disability, any unvested options terminate and any vested options must be exercised within 90 days. In the event of termination of such employment for the convenience of the employer, or by Mr. Parke because of a breach by the employer, then all options which are scheduled to vest within one year shall vest immediately and be exercisable for one year thereafter. Change of control is defined as a merger or consolidation of the Company resulting in an unrelated entity acquiring the power to elect a majority of the Company's Board of Directors, or a sale of substantially all of the Company's assets to an entity that is not then controlled by or affiliated with the Company. In the event that a change of control occurs and Mr. Parke's employment period is terminated, any unvested options will vest and be exercisable for one year. All stock options which are not exercised within one year following such termination shall thereupon expire and no longer be exercisable. These options will otherwise expire on June 30, 2016. The employment agreement also imposes confidentiality obligations on Mr. Parke.

Also effective on June 30, 2006, the Company, Parke Industries, LLC and Mr. Parke entered into a non-competition agreement which imposes on Mr. Parke non-competition obligations until June 30, 2008. This non-competition obligation is not separately compensated and was part of the consideration in the acquisition of Parke P.A.N.D.A. Corporation.

On July 11, 2006, Mr. Parke was granted additional options to purchase up to 653,333 shares of the Company common stock at \$1.02 per share. Mr. Parke's right to exercise these options vest with respect to 217,765 options on December 31, 2006; 217,784 options on each of December 31, 2007 and December 31, 2008, in each case assuming that Mr. Parke continues to be employed by the Company on such date. Vesting of the options will accelerate upon termination for reasons other than due cause (as defined in his option agreement), death, disability or resignation and upon a change of control. These options will expire on the earlier of July 11, 2016, or six months following the date that Mr. Parke is no longer an employee of the Company, unless his termination is for due cause (as defined in the option agreement) in which case they will expire immediately, or due to a change of control (as defined in the option) in which case they will expire twelve months following the change of control. These options contain a cashless exercise provision permitting Mr. Parke to pay the purchase price for any shares acquired by exercising the option by surrendering to the Company a number of shares of common stock having an aggregate market value equal to the purchase price.

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2005 Option Grants

The following table sets forth information regarding stock option grants made to each of the above named executive and principal officers during the fiscal year ended December 31, 2005.

Number of Shares Underlying	Percent of Total Options	Potential Realizable Value at Assumed Annual Rates of
------------------------------------------------	-----------------------------------------	--------------------------------------------------------------------------