

10-Q 1 probe10q32013\_10q.htm FORM 10Q

[Table of Contents](#)

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549**

**FORM 10-Q**

(Mark One)

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

For the quarterly period ended **September 30, 2013**

or

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: **333-125678 (1933 Act)**

**PROBE MANUFACTURING, INC.**

(Exact name of registrant as specified in its charter)

<b>Nevada</b>	<b>20-2675800</b>
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

<b>17475 Gillette Avenue, Irvine CA</b>	<b>92614</b>
(Address of principal executive offices)	(Zip Code)

**(949) 273-4990**

(Registrant's telephone number, including area code)

N/A

(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).  Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller

reporting company” in Rule 12b-2 of the Exchange Act. (check one)

Large accelerated filer   
Non-accelerated filer  (Do not check if a smaller reporting company)

Accelerated filer   
Smaller reporting company

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

As of November 1, 2013 there were 23,451,945 shares of common stock of Probe Manufacturing, Inc. outstanding.

Page 1 of 31

[Table of Contents](#)

**PROBE MAUFACTURING, INC.**  
**(A Nevada Corporation)**

**TABLE OF CONTENTS**

**PART I — FINANCIAL INFORMATION**

<a href="#">Item 1. Financial Statements</a>	3
<a href="#">Report of Independent Registered Public Accounting Firm</a>	3
<a href="#">Balance Sheet as of September 30, 2013 (Unaudited) and December 31, 2012</a>	4
<a href="#">Statement of Operations for the Three and Nine Months Ended September 30, 2013 (Unaudited) and September 30, 2012 (Unaudited)</a>	5
<a href="#">Statement of Cash Flows for the Nine Months Ended September 30, 2013 (Unaudited) and September 30, 2012 (Unaudited)</a>	6
<a href="#">Notes to Condensed Financial Statements (Unaudited)</a>	7
<a href="#">Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</a>	20
<a href="#">Item 3. Quantitative and Qualitative Disclosures About Market Risk</a>	26
<a href="#">Item 4. Controls and Procedures</a>	26

**PART II — OTHER INFORMATION**

<a href="#">Item 1. Legal Proceedings</a>	26
<a href="#">Item 1A. Risk Factors</a>	27
<a href="#">Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</a>	27
<a href="#">Item 3. Defaults Upon Senior Securities</a>	27
<a href="#">Item 4. [Removed and Reserved.]</a>	27
<a href="#">Item 5. Other Information</a>	28
<a href="#">Item 6. Exhibits</a>	28
<a href="#">Signatures</a>	29
<a href="#">Exhibit 31.1</a>	
<a href="#">Exhibit 31.2</a>	
<a href="#">Exhibit 32.1</a>	
<a href="#">Exhibit 32.2</a>	

[EX-101 INSTANCE DOCUMENT](#)  
[EX-101 SCHEMA DOCUMENT](#)  
[EX-101 CALCULATION LINKBASE DOCUMENT](#)  
[EX-101 LABELS LINKBASE DOCUMENT](#)  
[EX-101 PRESENTATION LINKBASE DOCUMENT](#)  
[EX-101 DEFINITION LINKBASE DOCUMENT](#)

Page 2 of 31

[Table of Contents](#)

## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors:

Probe Manufacturing, Inc.  
17475 Gillette Avenue  
Irvine, CA 92614

We have reviewed the accompanying balance sheet of Probe Manufacturing, Inc. as of September 30, 2013 and the related statements of operations and cash flows for the nine-month period ended September 30, 2013. These financial statements are the responsibility of the Company's management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the accompanying interim financial statements referred to above for them to be in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 1, conditions exist which raise substantial doubt about the Company's ability to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of the uncertainty.

/s/William.T. Uniack

W.T. UNIACK & CO, CPA's, P.C.  
November 19, 2013

[Table of Contents](#)**PART I - FINANCIAL INFORMATION****Item 1. Financial Statements****PROBE MANUFACTURING, INC.**

## Condensed Balance Sheet

	Un-Audited September 30, 2013	December 31, 2012
<b>Assets</b>		
<b>Current Assets:</b>		
Cash	\$ 3,398	\$ 19,260
Accounts receivable - net	720,182	908,697
Inventory	752,664	629,841
Total Current Assets	1,476,244	1,557,798
<b>Property And Equipment - Net</b>		
	166,832	131,587
		-
Goodwill	420,673	
Other Assets	42,444	22,376
<b>Total Assets</b>	<b>\$ 2,106,193</b>	<b>\$ 1,711,761</b>
<b>Liabilities And Stockholders' ( Deficit )</b>		
<b>Current Liabilities:</b>		
Bank Overdraft	\$ 41,124	\$ -
Accounts payable - trade	687,211	453,913
Accrued Expenses	115,051	105,668
Notes Payable - Line of Credit	229,789	858,543
Notes Payable - Current	78,690	8,664
Total Current Liabilities	1,151,865	1,426,788
<b>Long-Term Debt:</b>		
Notes Payable	-	-
Less Current portion of Long Term Debt	-	-
Net Long-Term Debt	-	-
<b>Total Liabilities</b>	<b>1,151,865</b>	<b>1,426,788</b>
<b>Stockholders' ( Deficit )</b>		
Preferred D stock, stated value \$100 per share; 20,000 shares authorized; 7,500 shares and 0 shares issued and outstanding respectively	750,000	-
Common stock, \$.001 par value; 400,000,000 shares authorized; 23,251,945 and 20,331,906 shares issued and outstanding respectively	40,073	20,332
Additional paid-in capital	1,119,912	620,130
Treasury Stock	(1,113)	(633)
Accumulated deficit	(954,544)	(354,856)
<b>Total Stockholders' ( Deficit )</b>	<b>954,328</b>	<b>284,973</b>

**Total Liabilities And Stockholders' Deficit** \$ 2,106,193 \$ 1,711,761

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

**Probe Manufacturing, Inc.**  
Statement of Operations  
for the three and nine month periods ended  
September 30, 2013 and 2012 respectively

	Un-audited		Un-audited	
	Three month period ended		Nine month period ended	
	2013	2012	2013	2012
Sales	\$ 1,049,732	\$ 1,079,931	\$ 2,785,727	\$ 3,969,084
Cost of Goods Sold	700,291	748,425	1,887,122	2,729,474
Gross Profit	349,441	331,506	898,605	1,239,610
General And Administrative	383,889	368,084	1,115,051	1,081,348
Share Based Compensation	-	-	2,124	13,300
Net Profit / (Loss) From Operations	(34,448)	(36,578)	(218,570)	144,962
Other Income / (Expenses)	-	-	55,777	230
Interest Expense	(52,828)	(35,270)	(155,495)	(132,870)
Net Profit / (Loss) Before Income Taxes	(87,276)	(71,848)	(318,288)	12,322
Income Tax Expense	-	-	-	-
Net Profit / (Loss)	\$ (87,276)	\$ (71,848)	\$ (318,288)	\$ 12,322
Per Share Information:				
Basic weighted average number of common shares outstanding	23,251,906	19,831,906	21,793,884	19,831,543
Net Profit / (Loss) per common share	0.00	0.00	0.00	0.00
Per Share Information:				
Diluted, weighted average number of common shares outstanding	23,251,906	20,415,439	21,793,884	20,410,784
Diluted, Net Profit / (Loss) per common share	0.00	0.00	0.00	0.00

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

**PROBE MANUFACTURING, INC.**  
Consolidated Statements of Cash Flows  
for the nine months ended September 30,

Un-Audited

Un-Audited

	2013	2012
<b>Cash Flows from Operating Activities:</b>		
Net Income / ( Loss )	\$ (318,288)	\$ 12,323
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	27,226	31,323
Share based compensation	2,124	13,300
Gain from issuance of Shares for acquisition	(41,694)	
Net Assets Acquired	(262,979)	-
Changes in assets and liabilities:		
(Increase) decrease in accounts receivable	188,515	(111,724)
(Increase) decrease in inventory	(122,823)	(161,021)
(Increase) decrease in other assets	(20,068)	328
(Decrease) increase in accounts payable	233,298	73,770
Other (Decrease) increase in accrued expenses	9,382	(88,511)
Net Cash provided / (Used) In Operating Activities	(305,307)	(230,212)
<b>Cash Flows from Investing Activities</b>		
Purchase of Equipment	(62,471)	(41,752)
Cash Flows Used In Investing Activities	(62,471)	(41,752)
<b>Cash Flows from Financing Activities</b>		
Bank Overdraft / (Repayment)	41,124	-
(Decrease) increase in advances line of credit	(628,754)	277,909
Conversion of Note payable to Common Stock	120,000	
Proceeds / (Payments) on notes payable	70,026	-
Payments for Treasury stock repurchase	(480)	-
Proceeds from issuance of Preferred stock	750,000	-
Cash Flows Provided / (used) By Financing Activities	351,916	277,909
Net (Decrease) Increase in Cash and Cash Equivalents	(15,862)	5,945
Cash and Cash Equivalents at Beginning of Period	19,260	18,349
<b>Cash and Cash Equivalents at End of Period</b>	<b>\$ 3,398</b>	<b>\$ 24,294</b>
<b>Supplemental Information:</b>		
Interest Paid	\$ 155,495	\$ 132,360

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



[Table of Contents](#)**PROBE MANUFACTURING, INC.****NOTES TO CONDENSED FINANCIAL STATEMENTS (UNAUDITED)**

*The use of the words "Probe," "PMI," "we," "us," "our" or "the Company" refers to Probe Manufacturing, Inc. and its subsidiaries, except where the context otherwise requires.*

**1. Organization and Description of the Business.**

Probe Manufacturing Industries, Inc. was incorporated on July 7, 1995. On April 21, 2005, the Company was re-domiciled from California to Nevada, and changed its name to Probe Manufacturing, Inc. Probe is an electronics design & manufacturing services (EMS) company. We provide a full range of engineering, manufacturing and supply chain management services to original equipment manufacturers (OEM), who design and market electronic products. We manufacture products primarily for customers in the medical, aerospace, alternative fuel, industrial and instrumentation industries. Probe's EMS offerings include collaborative design, materials management, proto-typing, product manufacturing, full system integration, product testing and product warranty repair, and end-of-life support. We support our customers from concept to fulfillment of their products resulting in improved return on investment, reduced materials acquisition time and cost and accelerating time to market.

**Going Concern**

The financial statements have been prepared on a going concern basis, which contemplates continuity of operations, realization of assets and liquidation of liabilities in the normal course of business. The Company had a total stockholder's equity of \$954,328 and a working capital surplus of \$324379; however, we still had net loss of \$(318,288) for the nine months ended September 30, 2013 and an accumulated deficit of \$(954544) as of September 30, 2013. Therefore, the ability of the Company to operate as a going concern is still dependent upon its ability to: (1) obtain sufficient debt and/or equity capital; and/or (2) generate positive cash flow from operations.

**Plan of Operation**

Management is taking the following steps to obtain & sustain profitability and growth: (i) organic growth through vertical integration (ii) diversification of sales and industries by continually driving new sales; (iii) participating in the growth of our foundry companies in return for manufacturing rights and equity; (iv) expansion of capabilities and competencies through mergers & acquisitions providing scale, cost synergies and revenue opportunities.

Our future success is dependent on our ability to sustain profitable growth and attain additional growth. Capital. There can be no assurance that we will be successful in obtaining any such financing, or that it will be able to generate sufficient positive cash flow from operations. The successful outcome of these or any future activities cannot be determined at this time and there is no assurance that if achieved, we will have sufficient funds to execute our business plan. The financial statements do not include any adjustments relating to the recoverability and classification of asset carrying amounts or the amount and classification of liabilities that might result should we be unable to continue as a going concern.

[Table of Contents](#)

**2. Basis of Presentation and Summary of Significant Accounting Policies.**

Our accompanying condensed financial statements have been prepared by us in accordance with generally accepted accounting principles in the United States of America, or GAAP, in conjunction with the rules and regulations of the U. S. Securities and Exchange Commission, or the SEC. Certain information and footnote disclosures required for annual financial statements have been condensed or excluded pursuant to SEC rules and regulations. Accordingly, our accompanying condensed financial statements do not include all of the information and footnotes required by GAAP for complete financial statements. Our accompanying condensed financial statements reflect all adjustments which are, in our view, of a normal recurring nature and necessary for a fair presentation of our financial position, results of operations and cash flows for the interim period. Interim results of operations are not necessarily indicative of the results to be expected for the full year; such full year results may be less favorable.

In preparing our accompanying financial statements, management has evaluated subsequent events through the financial statement issuance date. We believe that although the disclosures contained herein are adequate to prevent the information presented from being misleading, our accompanying condensed financial statements should be read in conjunction with our audited consolidated financial statements and the notes thereto included in our 2012 Annual Report on Form 10-K, as filed with the SEC on April 1, 2013.

**Cash and Cash Equivalents**

We maintain the majority of our cash accounts at a commercial bank. The total cash balance is insured by the Federal Deposit Insurance Corporation (“FDIC”) up to \$250,000 per commercial bank. For purposes of the statement of cash flows we consider all cash and highly liquid investments with initial maturities of one year or less to be cash equivalents.

Cash and cash equivalents consisted of the following as of:

	September 30, 2013	December 31, 2012
Cash and bank balances	\$ 3,398	\$ 19,260

**Estimates**

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Such estimates may be materially different from actual financial results. Significant estimates include the recoverability of long-lived assets, the collection of accounts receivable and valuation of inventory and reserves.

**Accounts Receivable**

We grant credit to our customers located within the United States of America; and do not require collateral. Our ability to collect receivables is affected by economic fluctuations in the geographic areas and industries served by us.

Reserves for un-collectable amounts are provided, based on past experience and a specific analysis of the accounts. Although we expect to collect amounts due, actual collections may differ from the estimated amounts. As of September 30, 2013, we had a reserve for potentially un-collectable accounts of \$43,550. Six (6) customers accounted for approximately 71% of accounts receivable at September 30, 2013 and four

customers accounted for more 12% each for a total of 54%. Our trade accounts primarily represent unsecured receivables. Historically, our bad debt write-offs related to these trade accounts have been insignificant.

Page 9 of 31

## [Table of Contents](#)

### **Inventory**

Inventories are valued at the lower of weighted average cost or market value. Our industry experiences changes in technology, changes in market value and availability of raw materials, as well as changing customer demand. We make provisions for estimated excess and obsolete inventories based on regular audits and cycle counts of our on-hand inventory levels and forecasted customer demands and at times additional provisions are made. Any inventory write offs are charged to the reserve account. As of September 30, 2013, we had a reserve for potentially obsolete inventory of \$256,000.

Inventories by major classification were comprised of the following as of:

	September 30, 2013	December 31, 2012
Raw Material	\$ 783,005	\$ 658,241
Work in Process	215,119	156,175
Finished Goods	10,460	5,426
Total	1,008,664	816,561
Less reserve for excess or obsolete inventory	(256,000)	(190,000)
Total Inventory	\$ 752,664	\$ 629,841

### **Property and Equipment**

Property and equipment are stated at cost. Assets held under capital leases are recorded at lease inception at the lower of the present value of the minimum lease payments or the fair market value of the related assets. The cost of ordinary maintenance and repairs is charged to operations. Depreciation and amortization are computed on the straight-line method over the following estimated useful lives of the related assets:

Furniture and fixtures	3 to 7 years
Equipment	7 to 10 years
Leasehold improvements	2 years (life of the lease)

Property and equipment were comprised of the following at:

	September 30, 2013	December 31, 2012
Furniture and Equipment	\$ 2,504,235	\$ 2,055,778
Accumulated Depreciation	(2,337,403)	(1,924,193)
Net Fixed Assets	\$ 166,832	\$ 131,585

### **Long –Lived Assets**

Our management assesses the recoverability of its long-lived assets by determining whether the depreciation and amortization of long lived assets over their remaining lives can be recovered through projected undiscounted future cash flows. The amount of long-lived asset impairment if any, is measured based on fair value and is charged to operations in the period in which long-lived assets impairment is determined by management. There can be no assurance however, that market conditions will not change or demand for our services will continue, which could result in impairment of long-lived assets in the future.

### **Revenue Recognition**

Revenue from product and services are recognized at the time goods are shipped or services are provided to the customer, with an appropriate provision for returns and allowances. Terms are generally FOB origination with the right of inspection and acceptance. We have not experienced a material amount of rejected or damaged product.

Page 10 of 31

[Table of Contents](#)

The Company provides services for its customers that range from contract design to original product design to repair services. The Company recognizes service revenue when the services have been performed, and the related costs are expensed as incurred.

**Fair Value of Financial Instruments**

The carrying amount of accounts payable and accrued expenses are considered to be representative of their respective fair values because of the short-term nature of these financial instruments.

**Other Comprehensive Income**

We have no material components of other comprehensive income (loss) and accordingly, net loss is equal to comprehensive loss in all periods.

**Segment Disclosure**

FASB Codification Topic 280, *Segment Reporting*, establishes standards for reporting financial and descriptive information about an enterprise’s reportable segments. We have determined that we have one reportable segment, with contract electronics manufacturing. As such, our operations have been aggregated into one reportable segment for all periods presented.

**Acquisition of Trident Manufacturing**

On March 15, 2013, we entered into an Agreement and Plan of Acquisition with Trident Manufacturing, Inc., a Utah corporation, (“Trident”), and the shareholders of Trident, to acquire 100% of the issued and outstanding common stock shares of Trident. Trident is a full-service electronics manufacturing service company with a 16,000 sq. ft. manufacturing facility based in Salt Lake City, Utah and has been servicing the industrial, aerospace, military, instrumentation, and medical markets since 2005.

On March 20, 2013, we completed the acquisition of Trident whereby we acquired 100% of the issued and outstanding common stock shares of Trident and all its operational assets in exchange for 1,600,000 shares of our restricted shares of common stock. As a result of the acquisition, Trident has become a wholly-owned subsidiary of Probe Manufacturing, Inc. As a result we recognized \$420,673 in goodwill.

The allocation of the purchase price and adjustment to stockholders’ equity is summarized in the tables below:

Net book value of the company's net assets acquired

Cash	\$	4,472
Inventory-net		19,254
Accounts Receivable-net		195,146
Other Assets		46,620
Accounts payable and accrued expenses		(361,055)
Notes payable		(167,416)
Net Assets Acquired	\$	(262,978)
Adjustments to Stockholders equity		
Reduction Opening balance Equity	\$	(18,419)
Adjustment to accumulated deficit		281,397
Equity adjustment from acquisition	\$	262,978



[Table of Contents](#)

**3. Share Based Compensation**

The company has adopted the use of Statement of Financial Accounting Standards No. 123R, “Share-Based Payment” (SFAS No. 123R) (now contained in FASB Codification Topic 718, *Compensation-Stock Compensation*, or Topic 718), which supersedes APB Opinion No. 25, “Accounting for Stock Issued to Employees”, and its related implementation guidance and eliminates the alternative to use Opinion 25’s intrinsic value method of accounting that was provided in Statement 123 as originally issued. This Statement requires an entity to measure the cost of employee services received in exchange for an award of an equity instruments, which includes grants of stock options and stock warrants, based on the fair value of the award, measured at the grant date, (with limited exceptions). Under this standard, the fair value of each award is estimated on the grant date, using an option-pricing model that meets certain requirements. We use the Black-Scholes option-pricing model to estimate the fair value of our equity awards, including stock options and warrants. The Black-Scholes model meets the requirements of Topic 718; however the fair values generated may not reflect their actual fair values, as it does not consider certain factors, such as vesting requirements, employee attrition and transferability limitations. The Black-Scholes model valuation is affected by our stock price and a number of assumptions, including expected volatility, expected life, risk-free interest rate and expected dividends. We estimate the expected volatility and estimated life of our stock options at grant date based on historical volatility; however, due to the thinly traded nature of our stock, we have chosen to use an average of the annual volatility of like companies in our industry. For the “risk-free interest rate”, we use the Constant Maturity Treasury rate on 90 day government securities. The term is equal to the time until the option expires. The dividend yield is not applicable, as the company has not paid any dividends, nor do we anticipate paying them in the foreseeable future. The fair value of our restricted stock is based on the market value of our free trading common stock, on the grant date calculated using a 20 trading day average. At the time of grant, the share based-compensation expense is recognized in our financial statements based on awards that are ultimately expected to vest using historical employee attrition rates and the expense is reduced accordingly. It is also adjusted to account for the restricted and thinly traded nature of the shares. The expense is reviewed and adjusted in subsequent periods if actual attrition differs from those estimates.

We re-evaluate the assumptions used to value our share-based awards on a quarterly basis and if changes warrant different assumptions, the share-based compensation expense could vary significantly from the amount expensed in the past. We may be required to adjust any remaining share-based compensation expense, based on any additions, cancellations or adjustments to the share based awards. The expense is recognized over the period during which an employee is required to provide service in exchange for the award—the requisite service period (usually the vesting period). No compensation cost is recognized for equity instruments for which employees do not render the requisite service. For the nine months ended, September 30, 2013 and 2012 we recognized \$2,124 and \$13,300, respectively.

The following table summarizes the Company’s stock-based compensation expense:

	Un-audited Three month period ended September 30, 2013		Un-audited Nine month period ended September 30, 2012	
Stock based compensation expense	\$ 0	\$ 0	\$ 2,124	\$ 13,300

**4. Net Profit / (Loss) per Common Share**



Basic profit / (loss) per share is computed on the basis of the weighted average number of shares of our common Stock outstanding. As of September 30, 2013, we had outstanding common stock shares of 23,251,945 used in the calculation of basic earnings per share. Basic Weighted average common stock shares and equivalents for the nine months ended September 30, 2013, were 21,025,790. As of September 30, 2013, we had outstanding warrants to purchase 800,000 additional common stock shares, options to

Page 12 of 31

## [Table of Contents](#)

purchase 110,386 additional common stock shares and common stock shares to be issued of 2,000,000, which may dilute future earnings per share; however, these were excluded from the calculation of fully diluted earnings per share, as they were anti dilutive in effect.

### **5. Income Taxes**

The Company accounts for income taxes under SFAS No. 109 (now contained in FASB Codification Topic 740-10-25, Accounting for Uncertainty in Income Taxes), which requires the asset and liability approach to accounting for income taxes. Under this method, deferred tax assets and liabilities are measured based on differences between financial reporting and tax bases of assets and liabilities measured using enacted tax rates and laws that are expected to be in effect when differences are expected to reverse. As of September 30, 2013, we had a net operating loss carry forward of \$(585,667) and a deferred tax asset of \$199,195 using the statutory rate of 34%. The deferred tax asset may be recognized in future periods, not to exceed 20 years. However, due to the uncertainty of future events we have booked valuation allowance of \$199,195.

	September 30, 2013
Deferred Tax Asset	\$ 228,869
Valuation Allowance	(228,869)
Deferred Tax Asset (Net)	\$ -

### **6. Accrued Expenses**

Accrued expenses were comprised of the following at:

	September 30, 2013	December 31, 2012
Accrued Wages	\$ 46,032-	\$ 28,362
Accrued Interest	6,262	4,549
Accrued Rent	48,190	48,190
Accrued Vacation	14,567	24,567
Total Accrued Expenses	\$ 115,051	\$ 105,668

## [Table of Contents](#)

### **7. Notes Payable**

On February 18, 2011 we entered into an Accounts Receivable Purchasing Agreement (the "ARPA") with DSCH Capital Partners, LLC d/b/a Far West Capital ("FWC"), an unaffiliated third party. Pursuant to the ARPA, FWC may purchase, in its sole discretion, eligible accounts receivable of our company on a revolving basis up to a maximum of \$750,000. Under the terms of the ARPA, FWC may purchase eligible receivables from us with full recourse for the face amount of such eligible receivables less a discount of 1.0%. In addition, we are required to pay FWC a monthly cost of funds fee equal to the net funds employed by FWC at a rate equal to the Wall Street Journal Prime Lending Rate plus 4.75%, with a floor of 7.00%. FWC will retain 20% of the purchase price of the receivables as a reserve amount.

The ARPA also provides that FWC has the right to require us to repurchase any purchased accounts receivable: (a) if there is a dispute as to the validity of such receivable by the account debtor, (b) if certain covenants, warranties or representations made by us with respect to such receivables are breached, (c) upon and during the continuance of an event of default under the ARPA or upon the termination of the ARPA, or (d) if such receivable remains unpaid 90 days after the invoice date. The ARPA has an initial term of one year with automatic renewals for successive one-year periods. Notwithstanding that, FWC may terminate the ARPA at any time upon 90 days prior written notice or without notice upon and during the continuance of an event of default.

Additionally, provided there does not exist an event of default under the ARPA or the rider thereto (the "Rider"), FWC may make advances to or for the benefit of the company in an aggregate amount up to and not to exceed \$250,000.00 from time to time during the term of the Rider and upon our request therefore, which advances shall be subject to all of the terms and conditions of the ARPA and shall be revolving consisting of advances against our eligible inventory as defined in the Rider as follows: (i) the advances against eligible inventory, at FWC's discretion, will be in amounts up to the sum 50% of all eligible inventory; provided, however, the advances against eligible inventory shall at no time exceed 33% of the net outstanding purchased accounts under the ARPA plus the outstanding amount due, or net funds employed, from advances made on eligible inventory within conditions contained within the Rider. The balance cap percentage shall be 25% after 120 days from date of the Rider. Eligible inventory will be valued at the lower of cost or market value.

On August 26, 2013, we terminated our agreement with FWC due to the level of the advance fees. Pursuant to the ARPA, the agreement will terminate 90 days after the date of our termination agreement and we will also pay a nominal early termination fee.

On September 6, 2013 we entered into a short term note for \$50,000 with an individual with a fixed fee of \$3,000 and it is due upon demand.

#### **Related Party – Notes payable**

We entered into an unsecured term note, dated November 03, 2009, payable to Linwood Goddard, our Vice President of Quality Control at a 12.00% interest rate, with a 36 month amortization and monthly payments of \$334.14. As of September 30, 2013 the outstanding balance was \$4,332.

We entered into an unsecured term note, dated December 24, 2009, payable to Linwood Goddard our Vice President of Quality Control at a 12.00% interest rate, with a 36 month amortization and monthly payments of \$334.14. As of September 30, 2013 the outstanding balance was \$4,332.

On February 15, 2013 we entered into a convertible promissory note with Luxus Micro Cap S.A. for \$120,000. The note bears interest at the rate of 10% simple interest and is convertible at \$0.10 per share and is due on February 15, 2015. On May 22, 2013 this note was converted into 1,200,000 shares of common

stock.

Page 14 of 31

## [Table of Contents](#)

### 8. Commitments and Contingencies

#### Operating Rental Leases

On October 14, 2009 we entered into a 5 year lease with Bernard family trust, with a commencement date of December 31, 2009. The facility is approximately 19,701 square feet and located at 17475 Gillette, Irvine CA, 92614.

On March 28, 2011 we signed an amendment to our facility lease with an increase of 1,600 square feet. The increase in the lease commences on April 1, 2011 and continues through year five. The amended lease has the following payments:

Year	Original Lease Monthly Rent	Amended lease Monthly Rent
1	7,880	7,880
2	9,850	10,650
3	10,835	11,715
4	11,820	12,780
5	12,805	13,845

#### Series D Preferred Stock Special Dividend

On August 7, 2013, we held our initial closing of our Series D Preferred Stock private financing offering with two related parties, whereby we received \$750,000 in financing, \$500,000 of which was received in a first tranche on June 17, 2013. Our Series D Preferred Stock offering terms allow us to raise up to \$1,000,000 US with an over-allotment of \$500,000 in multiple closings over the course of 6 months.

The following are primary terms of the Series D Preferred Stock Offering. The Series D Preferred holders will be paid a special monthly dividend at the rate of 17.5% per annum or at the option of the investor they may accrue such special dividends. If the Company does not pay the special dividend within five (5) business days from the end of the calendar month for which the payment of such dividend is owed, the Company will pay the investor a penalty of 3.5%. Any unpaid or accrued special dividends will be paid upon a liquidation or redemption. For any other dividends or distributions, participation will be with common stock on an as-converted basis. The Series D Preferred holders may elect to convert the Series D Preferred Stock, in his sole discretion, at any time after a one year (1) year holding period, by sending the Company a notice to convert.

The conversion rate shall be equal to the greater of \$0.08 or a 20% discount to the average of the three (3) lowest closing market prices of the common stock during the ten (10) trading day period prior to conversion. The Series D Preferred shall be redeemable from funds legally available for distribution at the option of the individual holders of the Series D Preferred commencing any time after the one (1) year period from the Closing (the "Redemption Period") at a price equal to the Purchase Price plus all accrued but unpaid dividends. If Company is not in a financial position to pay it back the company needs to notify the Investors thirty (30) days prior the Redemption Period commencing and both parties will negotiate in good faith for an extension of the Redemption Period. Notwithstanding, the Company may elect to redeem the Series D Preferred shares any time after the Closing at a price equal to Purchase Price plus all accrued but unpaid dividends subject to the Investors right to convert by providing the Investors written notice about its intent to redeem whereby the Investor shall have the right to convert per the terms of the conversion terms at least ten (10) days prior to such redemption by the Company.

#### Litigation

We are not presently subject to any material litigation nor, to our knowledge, is any material litigation threatened against us, which if determined unfavorably to us, would have a material adverse effect on our

financial position, results of operations or cash flows.

Page 15 of 31

## [Table of Contents](#)

### **9. Capital Stock Transactions**

For the nine months ended September 30, 2013, we issued the following securities without registration under the Securities Act of 1933, as amended. These securities were issued on the reliance of an exemption provided by Section 4(2) of the Securities Act.

On January 21, 2013 we issued 10,000 shares of common stock as for legal services.

On January 21, 2013 we issued 10,000 shares of common stock for consulting services.

On January 21, 2013 we issued 10,000 shares of common stock to employees as additional compensation.

On January 25, 2013, we issued 400,000 shares to our Chief Financial Officer, John Bennett, pursuant to his employment agreement with the Company.

On February 15, 2013 we entered into a convertible promissory note with Luxus Micro Cap S.A. for \$120,000. The note bears interest at the rate of 10% simple interest and is convertible at \$0.10 per share and is due on February 15, 2015. On May 22, 2013 this note was converted into 1,200,000 shares of common stock.

On August 7, 2013, we held our initial closing of our Series D Preferred Stock private financing offering with two related parties, whereby we received \$750,000 in financing, \$500,000 of which was received in a first tranche on June 17, 2013. Our Series D Preferred Stock offering terms allow us to raise up to \$1,000,000 US with an over-allotment of \$500,000 in multiple closings over the course of 6 months. During the initial close Luxus Micro Cap S.A. purchased 5,000 shares of our Series D Preferred Stock for \$500,000 and RDK Enterprises, LLC, an entity affiliated with our board of directors member Robert Young, purchased 2,500 Series D Preferred Stock for \$250,000.

### **Common Stock**

Our Articles of Incorporation authorizes us to issue 400,000,000 shares of common stock, par value \$0.001 per share. As of September 30, 2013 there were 23,251,945 shares of common stock issued and outstanding, respectively. All outstanding shares of common stock are, and the common stock to be issued will be, fully paid and non-assessable. Each share of our common stock has identical rights and privileges in every respect. The holders of our common stock are entitled to vote upon all matters submitted to a vote of our shareholders and are entitled to one vote for each share of common stock held. There are no cumulative voting rights.

The holders of our common stock are entitled to share equally in dividends and other distributions that our Board of Directors may declare from time to time out of funds legally available for that purpose, if any, after the satisfaction of any prior rights and preferences of any outstanding preferred stock. If we liquidate, dissolve or wind up, the holders of shares of common stock will be entitled to share ratably in the distribution of all of our assets remaining available for distribution after satisfaction of all our liabilities and our obligations to holders of our outstanding preferred stock.

### **Reverse Stock Split**

Effective January 22, 2013, we completed a one-for-ten reverse stock split of the Company's issued and outstanding shares of common stock. The reverse stock split was previously approved by the our board of directors and by shareholders at the 2012 Annual General Meeting of Shareholders held on November 28, 2012. Upon effectiveness of the reverse stock split, each ten (10) shares of the company's issued and





## [Table of Contents](#)

outstanding common stock was automatically combined and converted into one (1) issued and outstanding share of common stock. This reduced the number of issued and outstanding shares of the company's common stock from approximately 200 million to approximately 20 million. The reverse stock split affected only the issued and outstanding shares of the company's common stock, as well as common stock underlying stock options outstanding immediately prior to the effectiveness of the reverse stock split. The number of authorized shares of the company's common stock was not affected by the reverse split. All Shares referenced in this report have been retroactively adjusted to reflect the post-split shares.

### **Preferred Stock**

Our Articles of Incorporation authorize us to issue 10,000,000 shares of preferred stock. We authorized 440 shares of Series A Convertible Preferred Stock and 20,000 shares of Series B Convertible Preferred Stock. On May 25, 2006 we authorized 15,000 shares Series C Convertible Preferred Stock. As of August 20, 2006 all shares Series A, B and C preferred stock has been converted into common stock and there were no outstanding preferred shares of the series A, B, C as of September 30, 2013. On June 17, 2013 we authorized the issuance of 15,000 shares of Series D Preferred stock.

On August 7, 2013, we held our initial closing of our Series D Preferred Stock private financing offering with two related parties, whereby we received \$750,000 in financing, \$500,000 of which was received in a first tranche on June 17, 2013. Our Series D Preferred Stock offering terms allow us to raise up to \$1,000,000 US with an over-allotment of \$500,000 in multiple closings over the course of 6 months. During the initial close Luxus Micro Cap S.A. purchased 5,000 shares of our Series D Preferred Stock for \$500,000 and RDK Enterprises, LLC, an entity affiliated with our board of directors member Robert Young, purchased 2,500 Series D Preferred Stock for \$250,000.

The following are primary terms of the Series D Preferred Stock Offering. The Series D Preferred holders will be paid a special monthly dividend at the rate of 17.5% per annum or at the option of the Investor such special may accrue such special dividends. If the Company does not pay the special dividend within five (5) business days from the end of the calendar month for which the payment of such dividend to owed, the Company will pay the investor a penalty of 3.5%. Any unpaid or accrued special dividends will be paid upon a liquidation or redemption. For any other dividends or distributions, participation with common stock on an as-converted basis. The Series D Preferred holders may elect to convert the Series D Preferred Stock, in his sole discretion, at any time after a one year (1) year holding period, by sending the Company a notice to convert. The conversion rate shall be equal to the greater of \$0.08 or a 20% discount to the average of the three (3) lowest closing market prices of the common stock during the ten (10) trading day period prior to conversion. The Series D Preferred shall be redeemable from funds legally available for distribution at the option of the individual holders of the Series D Preferred commencing any time after the one (1) year period from the Closing (the "Redemption Period") at a price equal to the Purchase Price plus all accrued but unpaid dividends. If Company is not in a financial position to pay it back the company needs to notify the Investors thirty (30) days prior the Redemption Period commencing and both parties will negotiate in good faith for an extension of the Redemption Period. Notwithstanding, the Company may elect to redeem the Series D Preferred shares any time after the Closing at a price equal to Purchase Price plus all accrued but unpaid dividends subject to the Investors right to convert by providing the Investors written notice about its intent to redeem whereby the Investor shall have the right to convert per the terms of the conversion terms at least ten (10) days prior to such redemption by the Company.

### **Stock Repurchase Program**

On November 1, 2011, the Company adopted a plan to repurchase up to 5,000,000 shares of its issued and outstanding common stock in accordance with the guidelines specified in Rule 10b-18 and Rule 10b5-1 of the Securities Exchange Act of 1934, as amended.

The plan allows the Company to purchase its issued and outstanding common shares in the open market or in negotiated transactions, from time to time, depending on market conditions and other factors as well as being subject to relevant rules under United States securities regulations. The plan does not obligate the Company to make any purchases, at any specific time or in any particular situation. The plan may be

Page 17 of 31

[Table of Contents](#)

suspended or discontinued at any time at the sole discretion of the Company. Share repurchases will be funded with the Company's available cash, after determining the working capital requirements of the Company. Accordingly, there is no guarantee as to the exact number of shares that will be repurchased under the plan.

The company's Board of Directors authorized the repurchase plan because it believes recent market conditions may have caused the Company's common stock to be undervalued. The timing and number of any shares repurchased will depend on the terms and conditions of the plan and no assurance can be given that any specific amount of common stock will be repurchased.

As of September 30, 2013, we had repurchased 21,100 shares of our common stock.

**Warrants**

*Series E – Common Stock warrants*

On April 8, 2011, we issued 300,000 series E Warrants. Each warrant gives the holder the right to purchase 1 share of common stock (300,000 total shares) at \$0.50 per share. The Series E Warrants will expire on April 8, 2016.

*Series F & G – Common Stock warrants*

Investors in the Series D Preferred Stock private offering shall receive one (1) warrant to purchase 50,000 shares of common stock for every \$100,000 invested in the offering at a price per share equal to \$0.10 per share and one (1) warrant to purchase 50,000 shares of common stock at a price per share equal to \$0.20 (the "Series F and G Warrants"). The Series F and G Warrants be valid for a period of 5 years from the date of the Closing. The amount and price per share shall be subject to adjustments for stock dividends, splits, combinations and similar events.

***Warrants Activity for the Period and Summary of Outstanding Warrants (ADD IN SERIES F & G WARRANTS)***

**A summary of warrant activity for the periods is as follows:**

	Warrants - Common Share Equivalents		Warrants exercisable - Common Share Equivalents	
	Weighted Average Exercise price	Weighted Average Exercise price	Weighted Average Exercise price	Weighted Average Exercise price
Outstanding December 31, 2012	300,000	0.50	300,000	0.50
Granted	500,000	0.15	500,000	0.15
Expired	-	-	-	-
Exercised	-	-	-	-
Outstanding September 30, 2013	800,000	0.50	800,000	0.50

Note: The weighted average exercise price has been adjusted retroactively due to price decreases in the warrant strike prices.

Range of Warrant Exercise Price	Warrants Outstanding			Warrants Exercisable	
	Warrants - Common Share Equivalents	Weighted Average Exercise price	Remaining Contractual life in years	Warrants - Common Share Equivalents	Weighted Average Exercise price
\$ 0.50	300,000	\$0.50	2.77	300,000	\$0.50
\$ 0.10	250,000	\$0.10	4.75	250,000	\$0.10
\$ 0.20	250,000	\$0.20	4.75	25,000	\$0.20
Total	800,000	\$0.28		300,000	\$0.28

**Stock Options**

On February 8, 2007 pursuant to our 2006 Qualified Incentive Option Plan which was adopted by our Board of Directors granted Company employees an incentive stock option to purchase up to 652,766 shares of our common stock. These options were granted at \$.173 cents, the fair market value of the Company at the time of the grant. These options expire on February 8, 2017. As of September 30, 2013, there were 194,780 outstanding options under this plan.

On February 8, 2008, we granted stock options to our key employees, to purchase up to 75,000 shares of our common stock, which was approved by our Board of Directors. These options were granted at \$1.73 cents, the fair market value of the Company at the time of the grant. These options expire on February 8, 2017. As a result, we recognized share-based compensation expense in the amount of \$5,313 for the year ended December 31, 2007; \$2,657 for the year ended December 31, 2008; \$2,656 for the year ended December 31, 2009; \$2,656 for the year ended December 31, 2010 and \$0 for the year ended December 31, 2011.

On February 28, 2008 our granted stock options to a key employee, to purchase up to 30,000 shares of our common stock, which was approved by our Board of Directors. These options were granted at \$.33 cents, the fair market value of the Company at the time of the grant. These options expire on February 8, 2017. As a result, we recognized share-based compensation expense in the amount of \$5,574 for year ended December 31, 2008; \$5,576 for the year ended December 31, 2009; \$2,786 for the year ended December 31, 2010; and \$0 for the year ended December 31, 2011.

On April 7, 2011 our board of directors approved of the Probe Manufacturing, Inc. 2011 Omnibus Incentive Plan to assist in attracting and retaining highly competent employees, directors and consultants to act as an incentive in motivating selected employees, directors and consultants of the Company to achieve long-term corporate objectives and to enable stock-based and cash-based incentive awards to qualify as performance-based compensation for purposes of the tax deduction limitations under Section 162(m) of the Code.

As of September 30, 2013 we have issued 50,000 shares pursuant to our 2011 Omnibus Incentive Plan.

**Stock to be issued under option and warrant plans**

Page 19 of 31

## [Table of Contents](#)

Any shares issued under the existing option or warrant plans will come from the company's authorized but un-issued, un-registered shares.

### **10. Related Party Transactions**

Kambiz Mahdi, our Chief Executive Officer, owns Billet Electronics, which is an independent distributor of electronic components. From time to time we purchase parts from Billet Electronics for the 9 months ended September 30, 2013 we purchase approximately \$47,000 in material from Billet electronics. In addition, from time to time we provide assembly and value added services to Billet Electronics. In addition Billet was a supplier of parts and had dealings with current and former customers of our company. Our board of directors has approved such transactions of our chief executive officer.

We entered into an unsecured term note, dated November 03, 2009, payable to Linwood Goddard, our Vice President of Quality Control at a 12.00% interest rate, with a 36 month amortization and monthly payments of \$334.14. As of September 30, 2013 the outstanding balance was \$4,332.

We entered into an unsecured term note, dated December 24, 2009, payable to Linwood Goddard our Vice President of Quality Control at a 12.00% interest rate, with a 36 month amortization and monthly payments of \$334.14. As of September 30, 2013 the outstanding balance was \$4,332.

On February 15, 2013 we entered into a convertible promissory note with Luxus Micro Cap S.A. for \$120,000. The note bears interest at the rate of 10% simple interest and is convertible at \$0.10 per share and is due on February 15, 2015. On May 22, 2013 this note was converted into 1,200,000 shares of common stock.

On August 7, 2013, we held our initial closing of our Series D Preferred Stock private financing offering with two related parties, whereby we received \$750,000 in financing, \$500,000 of which was received in a first tranche on June 17, 2013. Our Series D Preferred Stock offering terms allow us to raise up to \$1,000,000 US with an over-allotment of \$500,000 in multiple closings over the course of 6 months. During the initial close Luxus Micro Cap S.A. purchased 5,000 shares of our Series D Preferred Stock for \$500,000 and RDK Enterprises, LLC, an entity affiliated with our board of directors member Robert Young, purchased 2,500 Series D Preferred Stock for \$250,000.

Investors in the Series D Preferred Stock private offering shall receive one (1) warrant to purchase 50,000 shares of common stock for every \$100,000 invested in the offering at a price per share equal to \$0.10 per share and one (1) warrant to purchase 50,000 shares of common stock at a price per share equal to \$0.20 (the "Series F and G Warrants"). The Series F and G Warrants be valid for a period of 5 years from the date of the Closing. The amount and price per share shall be subject to adjustments for stock dividends, splits, combinations and similar events.

### **11. Subsequent Events**

**None.**

## [Table of Contents](#)

### **Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operation**

Unless otherwise specifically stated, references in this report to "Probe," "PMI," "the Company," "we," "us," "our" and similar terms mean Probe Manufacturing, Inc. and its subsidiaries.

This report on Form 10-Q contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, and Section 27A of the Securities Act of 1933, as amended. The words "expects," "anticipates," "believes," "intends," "plans" and similar expressions identify forward-looking statements. In addition, any statements which refer to expectations, projections or other characterizations of future events or circumstances are forward-looking statements. We undertake no obligation to publicly disclose any revisions to these forward-looking statements to reflect events or circumstances occurring subsequent to filing this Form 10-Q with the Securities and Exchange Commission. These forward-looking statements are subject to risks and uncertainties, including, without limitation, those risks and uncertainties discussed in this section, as well as any risks and uncertainties discussed in Part II, Item 1A, "Risk Factors" of this report on Form 10-Q, and in Part I, Item 1A, "Risk Factors" and in Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" in our Annual Report on Form 10-K for the year ended December 31, 2012. In addition, new risks emerge from time to time and it is not possible for management to predict all such risk factors or to assess the impact of such risk factors on our business. Accordingly, our future results may differ materially from historical results or from those discussed or implied by these forward-looking statements. Given these risks and uncertainties, the reader should not place undue reliance on these forward-looking statements.

#### **OVERVIEW**

Probe Manufacturing Industries, Inc. was incorporated on July 7, 1995. On April 21, 2005, the Company was re-domiciled from California to Nevada, and changed its name to Probe Manufacturing, Inc. (the "Company," "Probe," or "PMI"). We provide electronics design and manufacturing services to original electronic equipment manufacturers (OEM) from our 23,000 sq-ft facility in Irvine, California and Trident Manufacturing's 16,000 sq-ft. facility in Salt Lake City, Utah, which we acquired in the first quarter of 2013. Our revenue is generated from sales of our services. We manufacture electronics products primarily for customers in the medical device, aerospace/military, telecommunication, alternative fuel, industrial and instrumentation industries. We provide our domestic customers with low cost, flexible and scalable manufacturing services. We utilize innovative manufacturing solutions, automated management systems and global sourcing strategies to provide our customers with onshore, scalable manufacturing solutions. The services that we provide are commonly referred to as Electronics Manufacturing Services (EMS). Our EMS offerings include new product introduction, collaborative design, procurement and materials management, product manufacturing, full system integration, product warranty repair, and end-of-life support. We offer our customers comprehensive and integrated design and manufacturing services, from initial product design to production and direct order fulfillment. Our engineering services include product design, printed circuit board layout, prototyping, and test development. Our supply chain management solutions include purchasing, management of materials, and order fulfillment. Our manufacturing services include printed circuit board assembly, cable assembly, mechanical assembly, and fully integrated box build systems for high complexity electronics.

The majority of our revenue is driven from manufacturing a mix of complex printed circuit board assemblies (PCB), and box build assemblies. Some examples of our customer's finished goods products includes Ultrasound Therapeutic medical devices, Sensors, electronic control units for precision laser welding equipment, PCB's for landing gear systems and flap controllers, fluid control units for airliners, and devices for defense industry.

We believe that US should no longer be the center for innovation but once again should become the center for manufacturing of American innovation.

Page 21 of 31



## Table of Contents

As innovation, cost, and time to market become hyper-competitive, domestic OEM's are now compelled to use EMS partners with easy onshore access, providing local program management during product conceptualization, development, and integration. Many of the mid-tier OEMs in industries such as military/aerospace, medical, industrial/instrumentation, and green-tech products tend to be too small for \$1 billion-plus revenue EMS companies. Most of these OEMs value close proximity and the ability to provide complex manufacturing and personal customer service, which often favors regional providers that truly value and foster their relationships.

Furthermore, with the recent cost increases in labor, currency movements and freight concerns, the ability to also provide near-shore manufacturing is expected to generate increased interest. The low to medium EMS market compared to high volume has proved to be a higher margin with higher gross profits and sustained growth momentum. Our target accounts are mid-tier, U.S. based OEMs with annual sales from \$15 million to \$500 million.

We believe that the combination of: (i) our management expertise; (ii) low overhead and cost structure; (iii) sophisticated management system developed internally to oversee operational systems; (iv) innovative manufacturing solutions and now multiple domestic facilities; and (v) global sourcing solutions and domestic customer centric program management team, PMI is well positioned to take advantage of the projected increase in outsourced onshore manufacturing.

### ***Our Products and Services***

Engineering. Our global engineering team supports technology customers and innovative start-ups with a broad range of electrical, mechanical and software engineering services. PMI has assembled a team of experts from around the globe to assist customers at any point in the design cycle. These services include design processes from electrical, software, mechanical, Industrial and PCB design. Utilization of PMI's design services will enable rapid market entry for our customers. It provides flexibility by becoming the extension of their engineering and allowing customers to focus on their business strategy.

Supply Chain Management. PMI's supply chain solution provides maximum flexibility and responsiveness through a collaborative and strategic approach with our customers. PMI can assume supply chain responsibility from component sourcing through delivery of finished product. PMI's supply chain focus is on building internal and external systems and relationships, which allow us to capitalize on our expertise to align with our customer's objectives and integrate with their processes today and in the future.

Manufacturing. Flexibility, responsiveness, communication, global supply chain management and speed are key values in what we offer our customers. We establish clear communication about our customer needs and requirements enabling a seamless integration with their objectives and processes. PMI's manufacturing capability supports high and low-mix assemblies for prototypes, to medium-volume quantities in California and high-volume production in Asia. Our manufacturing operations include printed circuit board assembly and testing; cable and harness assembly; mechanical assembly; and complex system integration.

### **GOING CONCERN**

The financial statements have been prepared on a going concern basis, which contemplates continuity of operations, realization of assets and liquidation of liabilities in the normal course of business. The Company had a total stockholder's equity of \$954,328 and a working capital surplus of \$324,379; however, we still had net loss of \$(318,288) for the nine months ended September 30, 2013 and an accumulated deficit of \$(954,544) as of September 30, 2013. Therefore, the ability of the Company to operate as a going concern is still dependent upon its ability to: (1) obtain sufficient debt and/or equity capital; and/or (2) generate positive cash flow from operations.

Our operating results are affected by a number of factors, including the following:

Page 22 of 31

## Table of Contents

- changes in the macro-economic environment and related changes in consumer demand;
- the mix of the manufacturing services we are providing, the number and size of new manufacturing programs, the degree to which we utilize our manufacturing capacity, seasonal demand, shortages of components and other factors;
- the effects on our business when our customers are not successful in marketing their products, or when their products do not gain widespread commercial acceptance;
- our components offerings which have required that we make substantial investments in the resources necessary to design and develop these products;
- our ability to achieve commercially viable production yields and to manufacture components in commercial quantities to the performance specifications demanded by our OEM customers;
- our customers' ability to cancel or delay orders or change production quantities;
- our customers' decision to choose internal manufacturing instead of outsourcing for their product requirements;
- our exposure to financially troubled customers; and
- integration of acquired businesses and facilities.

## **CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from those estimates and assumptions.

Refer to the accounting policies under Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" in our Annual Report on Form 10-K for the fiscal year ended December 31, 2012, where we discuss our more significant judgments and estimates used in the preparation of the condensed consolidated financial statements.

## **RESULT OF OPERATIONS**

The following table sets forth, for the periods indicated, certain statements of operations data expressed as a percentage of net sales. The financial information and the discussion below should be read in conjunction with the condensed consolidated financial statements and notes thereto included in this document. In addition, reference should be made to our audited consolidated financial statements and notes thereto and related Management's Discussion and Analysis of Financial Condition and Results of Operations included in our 2012 Annual Report on Form 10-K.

**Probe Manufacturing, Inc.**  
Statement of Operations  
for the three and nine month periods ended  
September 30, 2013 and 2012 respectively

	Un-audited		Un-audited	
	Three month period ended		Nine month period ended	
	2013	2012	2013	2012
Sales	\$ 1,049,732	\$ 1,079,931	\$ 2,785,727	\$ 3,969,084
Cost of Goods Sold	750,291	748,425	1,937,122	2,729,474
Gross Profit	299,441	331,506	848,605	1,239,610
General And Administrative	333,889	368,084	1,065,051	1,081,348
Share Based Compensation	-	-	2,124	13,300
Net Profit / (Loss) From Operations	(34,448)	(36,578)	(218,570)	144,962
Other Income / (Expenses)	-	-	55,777	230
Interest Expense	(52,828)	(35,270)	(155,495)	(132,870)
Net Profit / (Loss) Before Income Taxes	(87,276)	(71,848)	(318,288)	12,322
Income Tax Expense	-	-	-	-
Net Profit / (Loss)	\$ (87,276)\$	(71,848)\$	(318,288)\$	12,322

### *Net Sales*

For the nine month period ended September 30, 2013, we had a net sales of \$2,785,727 compared to net sales of \$3,969,084 for the same period in 2012.

Our top five customers accounted for approximately 62% of our net sales for the nine month period ended September 30, 2013, compared to 61%, for the same period in 2012. We believe that our ability to grow our core business depends on increasing sales to existing customers, and on successfully attracting new customers. Customer contracts can be canceled and volume levels can be changed or delayed based on our customer's performance and the end users' markets which we have no control over. The timely replacement of delayed, canceled or reduced orders with new business cannot be ensured. In addition, we cannot assume that any of our current customers will continue to utilize our services. Consequently, our results of operations may be materially adversely affected.

### *Gross Profit*

Gross profit is affected by a number of factors, including the number and size of new manufacturing programs, product mix, component costs and availability, product life cycles, unit volumes, pricing, competition, new product introductions, capacity utilization and the expansion and consolidation of manufacturing facilities. The flexible design of our manufacturing processes allows us to build a broad range of products in our facilities, which allows us to better utilize our manufacturing capacity. In the cases of new programs, profitability normally lags revenue growth due to product start-up costs, lower manufacturing program volumes in the start-up phase, operational inefficiencies, and under-absorbed overhead. Gross margin often improves over time as manufacturing program volumes increase, as our utilization rates and overhead absorption improves, and as we increase the level of vertically-integrated manufacturing services content. As a result of these various factors, our gross margin varies from period to period.

[Table of Contents](#)

Gross profit during the nine month period ended September 30, 2013 was \$848,605 at 30% of sales compared to \$1,239,610 at 31% of sales for the same period in 2012.

***Selling, General and Administrative Expenses***

Selling, general and administrative expenses (“SG&A”) amounted to \$1,065,051 during the nine month period ended September 30, 2013, compared to \$1,081,348 for the same period in 2012.

***Interest Expense***

For the nine month period ended September 30, 2013, our interest expense was \$155,495, compared to \$132,870 for the same period in 2012; this was due to the interest generated from our accounts receivable financing line referenced in Note 7 of the notes in this document.

***Key performance indicators***

	September 30,	
	2013	2012
Inventory Turns	3.33	3.52
Days Sales in Backlog	174	89
Days Receivables Outstanding	71	52
Days Payables Outstanding	95	54

**Inventory turns:** are calculated as the ratio of cost of material compared to the average inventory for the nine months ended September 30, 2013. For the nine months ended September 30, 2013, our inventory turns were 2.8 compared to 3.52 for the same period in 2012.

Days Sales in Backlog is calculated based on our back log divided by average daily sales during that period. For the nine months ended September 30, 2013, days sales in backlog was 174 days compared to 89 days for the same period in 2012.

Days receivables outstanding is calculated as the ratio of average accounts receivable during that period compared to average daily sales for the same period. For the nine months ended September 30, 2013, days receivables outstanding was 71 days compared to 52 days for the same period in 2012.

Days Payable outstanding is calculated as the ratio of average accounts payable during that period compared to average daily sales for the same period. For the nine months ended September 30, 2013, days payable outstanding was 95 days compared to 54 days for the same period in 2012.

***Liquidity and Capital Resources***

**PROBE MANUFACTURING, INC.**  
Condensed consolidated Balance sheet  
as of

	September 30, 2013	December 31, 2012
Working Capital	\$ 324,379	\$ 131,010
Total Assets	2,106,193	1,711,761
Long term Debt	-	-

Stockholder Equity

\$ 954,328 \$ 284,973

Page 25 of 31

## Table of Contents

### *Accounts Receivable Financing*

On February 18, 2011 we entered into an Accounts Receivable Purchasing Agreement (the “ARPA”) with DSCH Capital Partners, LLC d/b/a Far West Capital (“FWC”), an unaffiliated third party. Pursuant to the ARPA, FWC may purchase, in its sole discretion, eligible accounts receivable of our company on a revolving basis up to a maximum of \$750,000. Under the terms of the ARPA, FWC may purchase eligible receivables from us with full recourse for the face amount of such eligible receivables less a discount of 1.0%. In addition, we are required to pay FWC a monthly cost of funds fee equal to the net funds employed by FWC at a rate equal to the Wall Street Journal Prime Lending Rate plus 4.75%, with a floor of 7.00%. FWC will retain 20% of the purchase price of the receivables as a reserve amount.

The ARPA also provides that FWC has the right to require us to repurchase any purchased accounts receivable: (a) if there is a dispute as to the validity of such receivable by the account debtor, (b) if certain covenants, warranties or representations made by us with respect to such receivables are breached, (c) upon and during the continuance of an event of default under the ARPA or upon the termination of the ARPA, or (d) if such receivable remains unpaid 90 days after the invoice date. The ARPA has an initial term of one year with automatic renewals for successive one-year periods. Notwithstanding that, FWC may terminate the ARPA at any time upon 90 days prior written notice or without notice upon and during the continuance of an event of default.

Additionally, provided there does not exist an event of default under the ARPA or the rider thereto (the “Rider”), FWC may make advances to or for the benefit of the company in an aggregate amount up to and not to exceed \$250,000.00 from time to time during the term of the Rider and upon our request therefore, which advances shall be subject to all of the terms and conditions of the ARPA and shall be revolving consisting of advances against our eligible inventory as defined in the Rider as follows: (i) the advances against eligible inventory, at FWC’s discretion, will be in amounts up to the sum 50% of all eligible inventory; provided, however, the advances against eligible inventory shall at no time exceed 33% of the net outstanding purchased accounts under the ARPA plus the outstanding amount due, or net funds employed, from advances made on eligible inventory within conditions contained within the Rider. The balance cap percentage shall be 25% after 120 days from date of the Rider. Eligible inventory will be valued at the lower of cost or market value.

On August 21, 2013, we terminated our agreement with FWC. Pursuant to the ARPA, the agreement will terminate 90 days after the date of our termination agreement and we will also pay a nominal early termination fee.

### *Series D Preferred Stock Offering*

On August 7, 2013, we held our initial closing of our Series D Preferred Stock private financing offering with two related parties, whereby we received \$750,000 in financing, \$500,000 of which was received in a first tranche on June 17, 2013. Our Series D Preferred Stock offering terms allow us to raise up to \$1,000,000 US with an over-allotment of \$500,000 in multiple closings over the course of 6 months. During the initial close Luxus Micro Cap S.A. purchased 5,000 shares of our Series D Preferred Stock for \$500,000 and RDK Enterprises, LLC, an entity affiliated with our board of directors member Robert Young, purchased 2,500 Series D Preferred Stock for \$250,000.

The following are primary terms of the Series D Preferred Stock Offering. The Series D Preferred holders will be paid a special monthly dividend at the rate of 17.5% per annum or at the option of the Investor such special may accrue such special dividends. If the Company does not pay the special dividend within five (5) business days from the end of the calendar month for which the payment of such dividend to owed, the Company will pay the investor a penalty of 3.5%. Any unpaid or accrued special dividends will be paid upon a liquidation or redemption. For any other dividends or distributions, participation with common stock on an as-converted basis. The Series D Preferred holders may elect to convert the Series D Preferred Stock, in his sole discretion, at any time after a one year (1) year holding period, by sending the Company a notice to convert. The conversion rate shall be equal to the greater of \$0.08 or a 20% discount to the average of the three (3) lowest closing market prices of the common stock during the ten (10) trading day





## Table of Contents

period prior to conversion. The Series D Preferred shall be redeemable from funds legally available for distribution at the option of the individual holders of the Series D Preferred commencing any time after the one (1) year period from the Closing (the "Redemption Period") at a price equal to the Purchase Price plus all accrued but unpaid dividends. If Company is not in a financial position to pay it back the company needs to notify the Investors thirty (30) days prior the Redemption Period commencing and both parties will negotiate in good faith for an extension of the Redemption Period. Notwithstanding, the Company may elect to redeem the Series D Preferred shares any time after the Closing at a price equal to Purchase Price plus all accrued but unpaid dividends subject to the Investors right to convert by providing the Investors written notice about its intent to redeem whereby the Investor shall have the right to convert per the terms of the conversion terms at least ten (10) days prior to such redemption by the Company.

### ***Capital Requirements for long-term Obligations***

	2014	2013
Notes - Payable	\$0	\$58,664
Total	\$0	\$58,664

### ***Off-balance Sheet Arrangement***

We currently have no off-balance sheet arrangements.

### **Item 3. Quantitative and Qualitative Disclosure about Market Risk.**

Not applicable to smaller reporting companies.

### **Item 4. Controls and Procedures.**

- (a) *Evaluation of disclosure controls and procedures.* We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our reports under the Securities Exchange Act of 1934, as amended, or the Exchange Act, is recorded, processed, summarized and reported within the time periods specified in the rules and forms and that such information is accumulated and communicated to us, including our chief executive officer and our chief financial officer, as appropriate, to allow timely decisions regarding required disclosure.

As required by Rules 13a-15(b) and 15d-15(b) of the Exchange Act, an evaluation as of September 30, 2013 was conducted under the supervision and with the participation of our chief executive officer and our chief financial officer, of the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act). Based on this evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures, as of September 30, 2013, were effective.

- (b) *Changes in internal control over financial reporting.* There were no changes in our internal control over financial reporting that occurred during the quarter ended September 30, 2013 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**PART II--OTHER INFORMATION**

**Item 1. Legal Proceedings**

Page 27 of 31

## [Table of Contents](#)

None.

### **Item 1A. Risk Factors.**

There are no material changes from the risk factors previously disclosed in our 2012 Annual Report on Form 10-K, as filed with the United States Securities and Exchange Commission on April 1, 2013, except as disclosed below.

#### **RISKS ABOUT OUR BUSINESS**

*If we cannot obtain additional financing and/or reduce our operating costs sufficiently, and the effect of other unknown adverse factors could threaten our existence as a going concern. Therefore, we may have to curtail operations and may ultimately cease to exist.*

The financial statements have been prepared on a going concern basis, which contemplates continuity of operations, realization of assets and liquidation of liabilities in the normal course of business. The Company had a total stockholder's equity of \$954,328 and a working capital surplus of \$324,379; however, we still had net loss of \$(318,288) for the nine months ended September 30, 2013 and an accumulated deficit of \$(954,544) as of September 30, 2013. Therefore, the ability of the Company to operate as a going concern is still dependent upon its ability to: (1) obtain sufficient debt and/or equity capital; and/or (2) generate positive cash flow from operations.

*We have an accumulated deficit and may incur additional losses; therefore we may not be able to obtain the additional financing needed for working capital, capital expenditures and to meet our debt service obligations.*

As of September 30, 2013, we had current liabilities of \$1,151,865. As a result, our debt could limit our ability to obtain additional financing for working capital, capital expenditures, debt service requirements, or other purposes in the future, as needed; to plan for, or react to, changes in technology and in our business and competition; and to react in the event of an economic downturn.

Furthermore, On August 7, 2013, we held our initial closing of our Series D Preferred Stock private financing offering with two related parties, whereby we received \$750,000 in financing, \$500,000 of which was received in a first tranche on June 17, 2013. Our Series D Preferred Stock offering terms allow us to raise up to \$1,000,000 US with an over-allotment of \$500,000 in multiple closings over the course of 6 months. The Series D Preferred holders will be paid a special monthly dividend at the rate of 17.5% per annum or at the option of the Investor such special may accrue such special dividends. If the Company does not pay the special dividend within five (5) business days from the end of the calendar month for which the payment of such dividend is owed, the Company will pay the investor a penalty of 3.5%.

We may not be able to meet our debt service obligations. If we are unable to generate sufficient cash flow or obtain funds for required payments, or if we fail to comply with covenants in our revolving lines of credit or dividend payments to our Series D Preferred stockholder we will be in default which will have a material adverse impact on our business and working capital.

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

None.

### **Item 3. Defaults upon Senior Securities**

None.

**Item 4. [Removed and Reserved.]**

Page 28 of 31

[Table of Contents](#)

**Item 5. Other Information**

None.

**Item 6. Exhibits**

The exhibit listed on the Exhibit Index (following the signatures section of this Quarterly Report on Form 10-Q are included, or incorporated by reference, in this Quarterly Report on Form 10-Q.

[Table of Contents](#)**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the date indicated.

Signature	Title	Date
<u>/s/ Kambiz Mahdi</u> Kambiz Mahdi	Chief Executive Officer	November 19, 2013
<u>/s/ John Bennett</u> John Bennett	Chief Financial Officer	November 19, 2013

Page 30 of 31

[Table of Contents](#)**EXHIBIT INDEX**

Pursuant to Item 601(a)(2) of Regulation S-K, this Exhibit Index immediately precedes the exhibits.

The following exhibits are included, or incorporated by reference, in this Quarterly Report on Form 10-Q for the period ended September 30, 2013 (are numbered in accordance with Item 601 of Regulation S-K).

**EXHIBIT**  
**NUMBERDESCRIPTION**

3.1 Articles of Incorporation (included as exhibit 3.1 to the Form SB-2/A filed on June 10, 2005 and incorporated herein by reference)

3.2 Bylaws (included as exhibit 3.2 to the Form SB-2/A filed on June 10, 2005 and incorporated herein by reference)

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

31.2\* Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1\*\* Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2\*\* Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

101.INS\*\* XBRL Instance Document

101.SCH\*\* XBRL Taxonomy Extension Schema Document

101.CAL\*\* XBRL Taxonomy Extension Calculation Linkbase Document

101.LAB\*\* XBRL Taxonomy Extension Label Linkbase Document

101.PRE\*\* XBRL Taxonomy Extension Presentation Linkbase Document

101.DEF\*\* XBRL Taxonomy Extension Definition Linkbase Document

---

\*Filed herewith.

\*\*Furnished herewith.