ENOVA SYSTEMS INC
Form 10-K
March 31, 2006

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

For Annual and Transition Reports
Pursuant to Sections 13 or 15(d) of the
Securities and Exchange Act of 1934

[x] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2005

Commission File No. 0-25184

ENOVA SYSTEMS, INC.
(Exact name of registrant as specified in its charter)

California	95-3056150
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

19850 South Magellan Drive, Torrance, California 90502
(Address of principal executive offices, including zip code)

(310) 527-2800
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section 12(g) of the Act:

Common Stock, no par value
(Title of class)

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [ ]

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act). Yes [ ] No [X]

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant as of June 30, 2005 (the last business day of the registrant's more recently completed second quarter) was $15,568,662. For purposes of this calculation only, (i) shares of Series A and Series B Preferred Stock have been included in the calculation, (ii) shares of Common Stock and

Series A Preferred Stock are deemed to have a market value of $2.03 per share, and the Series B Preferred Stock is deemed to have a market value of $4.05 per share, based on the closing price of the Common Stock on June 30, 2005, and (iii) each of the executive officers, directors and persons holding 5% or more of the outstanding Common Stock (including Series A and B Preferred Stock on an as-converted basis) is deemed to be an affiliate.

The number of shares of Common Stock outstanding as of March 22, 2006 was 14,786,000.

ENOVA SYSTEMS, INC.

2004 FORM 10-K ANNUAL REPORT

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Disclosure Regarding Forward-Looking Statements

This annual report on Form 10-K, including the documents that we incorporate by reference, contains statements indicating expectations about future performance and other forward-looking statements that involve risks and uncertainties. We usually use words such as "may," "will," "should," "expect," "plan," "anticipate," "believe," "estimate," "predict," "future," "intend," "potential," or "continue" or the negative of these terms or similar expressions to identify forward-looking statements. These statements appear throughout the Form 10-K and are statements regarding our current intent, belief, or expectation, primarily with respect to our operations and related industry developments. Examples of these statements include, but are not limited to, statements regarding the following: our expansion plans, our future operating expenses, our future losses, our future expenditures for research and development and the sufficiency of our cash resources. You should not place undue reliance on these forward-looking statements, which apply only as of the date of this annual report. Our actual results could differ materially from those anticipated in these forward-looking statements for many reasons, including the risks faced by us and described in the section of Item 1A. entitled "Risk Factors," and elsewhere in this annual report. Any forward-looking statement speaks only as of the date on which it is made, and we undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date on which the statement is made or to reflect the occurrence of unanticipated events.

Enova Systems is a trademark of Enova Systems, Inc . All other brand names or trademarks appearing in this annual report are the property of their respective holders.

PART I

The matters addressed in this report on Form 10-K, with the exception of the historical information presented, may contain certain forward-looking statements involving risks and uncertainties. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including those set forth under the heading "Certain Factors That May Affect Future Results" in the Management's Discussion and Analysis section and elsewhere in this report.

Item 1. Business

General

In July 2000, we changed our name to Enova Systems, Inc. Our company, previously known as U.S. Electricar, Inc., a California corporation (the "Company"), was incorporated on July 30, 1976.

Enova believes it is a leader in the development and production of proprietary, commercial digital power management systems for transportation vehicles and stationary power generation systems. Power management systems

control and monitor electric power in an automotive or commercial application such as an automobile or a stand-alone power generator. Drive systems are comprised of an electric motor, an electronics control unit and a gear unit which power an electric vehicle. Hybrid systems, which are similar to pure electric drive systems, contain an internal combustion engine in addition to the electric motor, eliminating external recharging of the battery system. A hydrogen fuel cell based system is similar to a hybrid system, except that instead of an internal combustion engine, a fuel cell is utilized as the power source. A fuel cell is a system which combines hydrogen and oxygen in a chemical process to produce electricity. Stationary power systems utilize similar components to those which are in a mobile drive system in addition to other elements. These stationary systems are effective as power-assist or back-up systems, alternative power, for residential, commercial and industrial applications.

A fundamental element of Enova's strategy is to develop and produce advanced proprietary software, firmware and hardware for applications in these alternative power markets. Our focus is digital power conversion, power management, and system integration, for two broad market applications - vehicle power generation and stationary power generation.

Specifically, we develop, design and produce drive systems and related components for electric, hybrid-electric, fuel cell and microturbine-powered vehicles. We also develop, design and produce power management and power conversion components for stationary distributed power generation systems. These stationary applications can employ hydrogen fuel cells, microturbines, or advanced batteries for power storage and generation. Additionally, we perform research and development to augment and support others' and our own related product development efforts.

Our product development strategy is to design and introduce to market successively advanced products, each based on our core technical competencies. In each of our product / market segments, we provide products and services to leverage our core competencies in digital power management, power conversion and system integration. We believe that the underlying technical requirements shared among the market segments will allow us to more quickly transition from one emerging market to the next, with the goal of capturing early market share.

Enova's primary market focus centers on both series and parallel heavy-duty drive systems for multiple vehicle and marine applications. We believe series-hybrid and parallel hybrid medium and heavy-duty drive system sales offer Enova the greatest return on investment in both the short and long term. We believe the medium and heavy-duty hybrid market's best chances of significant growth lie in identifying and pooling the largest possible numbers of early adopters in high-volume applications. Enova will attempt to utilize its competitive advantages, including customer alliances, to gain greater market share. By aligning ourselves with key customers in our target market(s), Enova believes that the alliance will result in the latest technology being implemented and customer requirements being met, with a minimal level of additional time or expense. Additionally, Enova management believes that this area will see significant growth over the next several years. As the Company penetrates more market areas, we are continually refining and optimizing both our market strategy and our product line to maintain our leading edge in power management and conversion systems for mobile applications.

Our website, www.enovasystems.com, contains up-to-date information on the Company, its products, programs and current events. Enova is implementing an aggressive strategy to utilize its website and the internet as a prime focal point for current and prospective customers, investors and other affiliated

parties seeking data on the Company.

During 2005, our recapitalization initiatives were successful. We entered into an agreement with a placement agent relating to the sale of 5,300,000 new shares of our common stock, after the 1 for 45 reverse stock split described in Item 5 below. We received approximately $18,000,000 of net proceeds from the offering. The Company believes that we have the operating resources to continue our market penetration efforts.

The reorganization of senior management continued in 2005. During the fourth quarter of 2005, both our Chief Financial Officer, Larry Lombard, and our Chief Operating Officer, Edward Moore, resigned to seek other opportunities. Their resignations were not the results of any disagreements with the Company. In the first quarter of 2006, we appointed John Dexter as our new Director of Operations and Planning. In the absence of a financial executive at the end of 2005, and to facilitate the year end financial reporting process, we have relied on increased involvement from Edwin Riddell, Chief Executive Officer, as well as the services of qualified Certified Public Accountants as management consultants.

During 2005, the Company experienced an increase in production revenues. We believe our development and market penetration initiatives are proving successful. By defining our market focus, the Company has been able to better identify potential opportunities.

We continue to pursue privately and governmental funded development programs. This allows us to increase our revenue base, form new alliances with major OEMs and participate in the latest trends in alternative fuel technologies. The increase in R&D revenues for the year ended December 31, 2005 is primarily due to renewed customer requirements after a slow year in 2004.

The Company continues to receive greater recognition from both governmental and private industry with regards to both commercial and military application of its hybrid drive systems and fuel cell power management technologies. Although the Company believes that current negotiations with several parties may result in development and production contracts during 2006 and beyond, there are no assurances that such additional agreements will be realized.

During 2005, the Company continued to advance its technologies and products for greater market penetration for 2006 and beyond. We continue to develop independently and in conjunction with the Hyundai-Enova Innovative Technology Center (ITC) progress on several fronts to produce commercially available heavy-duty, series and parallel hybrid drive systems.

During the year ended December 31, 2005, we continued to develop and produce electric and hybrid electric drive systems and components for First Auto Works of China, Ford Motor Company (Ford), Hyundai Motor Car, US Military, Wright Bus and Eneco of the United Kingdom, and Tomoe of Japan and several other domestic and international vehicle and bus manufacturers. We also were successful in introducing our technology to companies such as Concurrent Technology Corporation (CTC), PUES (Tokyo Research and Development), Volvo/Mack and Navistar (International Truck and Engine, IC Corporation). The continued relationships, in addition to our newest customers helped Enova surpass, since Enova's inception, the manufacturing of its 900th system. Our various electric and hybrid-electric drive systems, power management and power conversion systems are being used in applications including Class 8 trucks, train locomotives, transit buses and industrial vehicles as well as in non-transportation applications such as fuel-cell management and power management systems, including the EDO minesweeper. Enova has furthered its development and production of systems for both mobile and stationary fuel cell powered systems with major companies such as Ford and Hydrogenics, a fuel cell developer in Canada.

For the year ended December 31, 2005, the following customers each accounted for more than ten percent (10%) of the Company's total revenues:

Customer	Percent
Tomoe Electro Mechanical Engineering & Mfg.	49.3%
Hyundai Motor Company	12.5%

Medium and Heavy-Duty Drive Systems - Buses, Trucks, Vans and Other Industrial Vehicle Applications

Enova's primary market focus centers on both series and parallel medium and heavy-duty drive systems for multiple vehicle and marine applications. We believe series-hybrid and parallel hybrid medium and heavy-duty drive system sales offer Enova the greatest return on investment in both the short and long term. Although this market sector has developed more slowly than anticipated, management believes that this area will see significant growth over the next several years. As the Company penetrates more market areas, we are continually refining and optimizing both our market strategy and our product line to maintain our leading edge in power management and conversion systems for mobile applications.

In Japan, Tomoe Electro-Mechanical Engineering and Manufacturing, Inc. has entered into a development and production contract with Enova for eight battery-electric locomotives for the Singapore Land Transport Authority (LTA) for service vehicles for the Seoul Mass Rapid Transit (SMRT) Circle Line system for maintenance, repair, shunting and recovery of passenger trains. Over the last several years, Enova successfully integrated its HybridPowerTM drive systems into Tomoe's heavy-duty Isuzu dump truck application, three passenger trams and a mine tunnel crawler. The hybrid drive train components were delivered in late 2005 at Tomoe's Japan-based facilities. Enova anticipates the total contract to exceed US$3 million over the life of the contract. This latest market penetration in Asia enhances not only Enova's alliances with both Tomoe and HHI, but also advances Enova's hybrid-electric technologies in high voltage power management components. As part of this contract, Enova will develop a high voltage charging system to enable the locomotive to receive a direct battery charge from the high voltage rail. Tomoe and Enova continue to develop other commercial and industrial applications for our drive systems including potential light rail applications. During the first quarter of 2005, Tomoe issued a purchase order for three post transmission parallel hybrid drive systems for another train project in South Korea.

In 2005, Enova Systems delivered a Post Transmission 80Kw Hybrid Drive 4200 series truck to International Truck and Engine (International). This is in addition to the delivery of the , as represented by IC Corporation, Hation's 1st functional Hybrid Drive school bus that was delivered to International in January of 2006. Both the truck and bus are currently being evaluated at International's Fort Wayne Technical Center. International and IC Corporation claims to be a leading manufacturer of medium duty trucks and school buses, with approximately 40% of the medium duty truck build and approximately 60% of the school bus build in North America.

Additionally in 2005, Enova's Post Transmission system was also integrated into a US Air Force "refueler" vehicle built by Volvo/Mack Truck Corporation. Enova, via Concurrent Technologies Corporation (CTC), also supplied its 120kW hybrid drive system to the US Air Force for a Fuel Cell Hybrid "TUG" vehicle In 2005, First Auto Works (FAW) of China ordered an additional five HybridPower

120kW drive systems. These units have been delivered. Additionally, FAW introduced its Hybrid City Bus, which is powered by Enova's 80kW Parallel Hybrid Drive System. FAW is China's largest vehicle manufacturer, producing in excess of 900,000 vehicles annually.

In 2005, we continued our work with Tsinghua University of China, and their fuel cell bus development program. China intends to use hybrid-electric buses to shuttle athletes and guests at the 2008 Beijing Summer Olympics and the 2010 World's Expo in Shanghai. China is seeking up to 1,000 full-size hybrid-electric buses to support these global events.

WrightBus, one of the largest low-floor bus manufacturers in the United Kingdom, continues to purchase our diesel genset-powered, series hybrid drive systems for their medium and large bus applications. WrightBus ordered two additional 120kW drive systems in 2005. Six of Enova's systems provided to Wrightbus, have been integrated into six Hybrid Buses, which are currently being evaluated in London's public bus fleet.

Eneco of the United Kingdom, a vehicle integrator which utilizes Enova's HybridPower 120kW drive systems in its hybrid bus applications, purchased 21 120kW systems in 2005.

EcoPower Technology of Italy continues to purchase components for its hybrid electric drive systems during 2005 for service and maintenance parts for its fleet of buses powered by HybridPowerTM 120kw drive systems. Since our teaming with EcoPower, we have sold 47 drive systems forming one of the largest fleets of hybrid buses in the world. EcoPower is one of the largest integrators of medium size transit buses for the European shuttle bus market, with key customers in five Italian cities namely Turin, Genoa, Brescia, Ferrara and Vicenza.

MTrans of Malaysia has integrated two of our standard HybridPower 120kW drive system into a hybrid 10-meter bus with a Capstone microturbine as its power source. This drive system is currently on demonstration in Hong Kong, PRC.

Additionally, we are in discussions with other bus manufacturers and industrial, commercial and military vehicle manufacturers regarding the purchase of our heavy-duty, high performance, 120kW and 240kW drive systems in 2005. There are no assurances, however, that these discussions will result in any sales of the HyrbidPower 240kW or 120kW drive systems.

Light-Duty Drive Systems and Fuel Cell Technologies - Automobiles and Delivery vehicles

The High Voltage Energy Converter (HVEC) development program with Ford Motor Company for their fuel cell vehicle was essentially completed in 2003. This converter is a key component in Ford's Focus Fuel Cell Vehicle (FCV) which utilizes the Ballard fuel cell system. It converts high voltage power from the fuel cell into a lower voltage for use by the drive system and electronic accessories. Ford currently is evaluating thirty vehicles utilizing Enova's technology, throughout the United States, Canada, and Germany. Enova's fuel cell enabling components continue to be part of the proposed fleets of fuel cell vehicles being utilized by both Ford Motor Company - the Ford Focus FCV- and Hyundai Motor Company - the Hyundai Tucson fuel cell hybrid electric vehicle - in response to the U.S. Department of Energy's solicitation, entitled "Controlled Hydrogen Fleet and Infrastructure Demonstration and Validation Project." This government-funded project will last over five years, evaluating the economic and performance feasibility of fuel cell vehicles and infrastructure across the U.S. In 2005, we delivered sixteen additional

converters to Hyundai. Furthermore, an additional 16 units are scheduled for delivery in 2006.

The Company will continue to explore new applications for this versatile technology in both mobile and stationary systems.

Research and Development Programs

We continue to aggressively pursue government and commercially sponsored development programs for both ground and marine heavy-duty drive system applications.

Our development contract with EDO Corporation of New York for the design and fabrication of a high voltage DC-DC power conversion system utilizing a Capstone microturbine as the primary power source for the U.S. Navy unmanned minesweeper project also continues to progress during 2005. The electronics package will include Enova's advanced power components including a new, enhanced 50V, 700A DC-DC power converter, our Battery Care Unit and Hybrid Control Unit which will power the minesweeper's electromagnetic detection system. Our power management and conversion system will be used to provide on-board power to other accessories on the platform.

The all-electric Hyundai Santa Fe SUV demonstration project in Honolulu Hawaii was completed in 2005. Fast-charging capabilities and performance will be the primary focus of this continued evaluation. This is a continuation of the State of Hawaii and Hyundai Motor Company's program for pure electric vehicle performance.

In the fourth quarter of 2004, Enova completed the design and integration of its 120kw drive system with a Capstone microturbine into a MB4 tow tractor for the U.S. Air Force through a contract with the Volpe National Transportation Systems Center. The objectives of this program include the integration of microturbine technology into the hybrid electric tow tractor, field testing and evaluation of the benefits of microturbine technology in a hybrid electric vehicle, integration of grid-charging technology, DC-DC converter, and a data acquisition system into an electric tow tractor, and validation of the technology effect on the original system and performance. During 2004, the program generated $165,000 in revenues for Enova. There is a potential for other upgrades of this type and we anticipate entering into more of these contracts in 2005 with the U.S. Air Force. There can be no assurances at this time, however, that such contracts will be realized.

We also commenced a program with Hydrogenics to integrate a HybridPower 120kW hybrid drive system into a step-van for Purolator as a hydrogen fuel cell hybrid vehicle. In integrating this new system, we utilized several new power management systems including our dual 8kW inverter and our Mobile Fuel Cell Generator that utilizes our High Voltage Converters. This fuel cell vehicle application utilized a Hydrogenics 20kW fuel cell power generation module underscoring our technologies ability to optimize fuel cell performance across a range of fuel cell products. The program is in its final stage of evaluation. As a result of this program, we have also commenced a similar fuel cell step van conversion program for HCATT and the U.S. Air Force.

In 2005, we commenced integration of a fuel cell powered step-van similar to the aforementioned Hydrogenics program for HCATT and the U.S. Air Force.

We intend to establish new development programs with the Hawaii Center for Advanced Transportation Technologies in mobile and marine applications as well as other state and federal government agencies as funding becomes available.

Environmental Initiatives and Legislation

Because vehicles powered by internal combustion engines cause pollution, there has been significant public pressure in Europe and Asia, and enacted or pending legislation in the United States at the federal level and in certain states, to promote or mandate the use of vehicles with no tailpipe emissions ("zero emission vehicles") or reduced tailpipe emissions ("low emission vehicles"). We believe legislation requiring or promoting zero or low emission vehicles is necessary to create a significant market for electric vehicles. The California Air Resources Board (CARB) is continually modifying its limits for low emission vehicles. Recently, CARB proposed additional amendments to the regulations. Furthermore, several car manufacturers have challenged these mandates in court and have obtained injunctions to delay these mandates. There

can be no assurance that further legislation will be enacted or that current legislation or state mandates will not be repealed or amended, or that a different form of zero emission or low emission vehicle will not be invented, developed and produced, and achieve greater market acceptance than electric vehicles. Extensions, modifications or reductions of current federal and state legislation, mandates and potential tax incentives could adversely affect the Company's business prospects if implemented.

Our products are subject to federal, state, local and foreign laws and regulations, governing, among other things, emissions as well as laws relating to occupational health and safety. Regulatory agencies may impose special requirements for implementation and operation of our products or may significantly impact or even eliminate some of our target markets. We may incur material costs or liabilities in complying with government regulations. In addition, potentially significant expenditures could be required in order to comply with evolving environmental and health and safety laws, regulations and requirements that may be adopted or imposed in the future.

Strategic Alliances, Partnering and Technology Developments

Our continuing strategy is to adapt ourselves to the ever-changing environment of alternative power markets for both stationary and mobile applications. Originally focusing on pure electric drive systems, we believe we are now positioned as a global supplier of drive systems for electric, hybrid and fuel cell applications. Enova is now entering stationary power markets with its power management systems and intends to develop other systems to monitor and control the complex fuel cell and ancillary device systems being developed for distributed generation and mobile applications.

Enova continues to seek and establish alliances with major players in the automotive, stationary power and fuel cell fields. 2005 allowed Enova to further its penetration into the European and Asian markets, as well as allow them to begin relationships with significant North American companies. We believe the medium and heavy-duty hybrid market's best chances of significant growth lie in identifying and pooling the largest possible numbers of early adopters in high-volume applications. Enova will utilize its competitive advantages, including customer alliances, to gain greater market share. By aligning ourselves with key customers in our target market(s), Enova believes that the alliance will result in the latest technology being implemented and customer requirements being met, with a minimal level of additional time or expense.

Enova's alliances with other major OEMs in the automotive, transit, commercial and energy sectors continue to expand. In 2005, Enova continued our endeavors related to the Chinese hybrid vehicle market, and with alliances with First Auto Works and Tsinghua University for heavy-duty hybrid drive systems and technologies. Additionally, we expanded on our alliances with, Tomoe, Hyundai

Motor Company (HMC), MTrans of Malaysia, Eneco, Hydrogenics of Canada, the Southwest Research Institute, the U.S. Air Force and other commercial and industrial intermediaries and OEMs to find new markets and applications for our products and technologies. We continue our strategy as a "systems integrator" by establishing relationships to utilize other independently developed technologies such as those provided by HHI, UTC Fuel Cells, Hydrogenics and national universities. We have implemented our plans to outsource manufacturing of our components to companies such as HHI, Ricardo, and other Asian manufacturers. We believe that one of our competitive advantages is our ability to identify, attract and integrate the latest technology available to produce state of the art products at competitive prices.

Our joint venture alliance with Hyundai Heavy Industries (HHI) is a prime example of our partnering strategy to maximize the utilization of Enova's knowledge and expertise in power management and control. Teaming with HHI may lead to other additive technologies and products which Enova can market to current and prospective customers. The joint venture corporation, Hyundai-Enova Innovative Technology Center (ITC), commenced operations in the second quarter of 2003. The advanced technology center focuses on leading-edge technologies in power management and power conversion for industrial, commercial, residential and vehicle applications. The ITC has been instrumental in bringing our diesel genset system into commercialization. Other projects slated for development for the ITC include commercial inverters and other power management systems which build on Enova's and HHI's technology base. It is our intent to utilize the resources provided through the ITC to optimize Enova's current product line for greater performance and production cost efficiencies, while we continue new research and development for the next generation of digital power management systems for mobile and stationary applications. For instance, the Hyundai Group of Korea and Enova are partnering in the development of advanced hybrid and hydrogen fuel cell drive-train technology and related systems.

Products

Enova's focus is digital power management, power conversion, and system integration. Our proprietary software, firmware and hardware manage and control the power that drives a vehicle or device. They convert the power into the appropriate forms required by the vehicle or device, whether DC to AC, AC to DC or DC to DC, and they manage the flow of this energy to protect the battery, the vehicle or device, and the driver or operator. Enova's systems work "from drive train to drive wheel" for both vehicle and stationary applications.

The latest state-of-the-art technologies, such as hybrid vehicles, fuel cell and micro turbine based systems, and stationary power generation, all require some type of power management and conversion mechanism. Enova, utilizing our enabling technologies, supplies these essential components. We believe our drive train systems will work with any kind of fuel/power source, from electric to hybrid to fuel cell to turbine. They are essential components for any vehicle, system or device that uses power.

Enova is moving to expand its product base into new markets outside of the traditional electric and hybrid-electric automotive fields. Key areas which Enova has begun to penetrate include energy management in distributed generation in the utility industry, and stand-by/backup power generation in the commercial electronics industry. Both of these markets can be served with our existing energy management and power control products. Enova has entered into agreements,

or commenced negotiations, with various alternative power generation manufacturers such as Hydrogenics, Capstone Turbine and Ballard Power as well as others. We believe our enabling technologies will prove beneficial to these

types of companies in their strategies to bring these new power systems to commercialization.

Enova has embraced fuel cell technology and has begun to develop various power management and control systems to enable fuel cell manufacturers and their ancillary industries to achieve greater efficiencies from their systems. These systems are also designed to provide added reliability and safety by monitoring, adjusting and reporting on operation of the unit.

HybridPowerTM Electric and Hybrid-Electric Drive Systems

Enova's HybridPower drive system family, along with its drive system accessories are designed to provide our customers with a complete solution to their drive system needs for both light-duty through heavy-duty vehicle markets. Enova's HybridPower hybrid electric drive system provides all the functionality one would find under the hood of an internal combustion engine powered vehicle. The HybridPower system consists of an enhanced electric motor and the electronic controls that regulate the flow of electricity to and from the batteries at various voltages and power to propel the vehicle. In addition to the motor and controller, the system includes a gear reduction/differential unit which ensures the desired propulsion and performance. The system is designed to be installed as a "drop in," fully integrated turnkey fashion, or on a modular, "as-needed" basis. Regardless of power source (battery, fuel cell, diesel generator or turbine) the HybridPower electric motor is designed to meet the customer's drive cycle requirements.

The HybridPower drive system family is targeted to meet the demands of light-duty through heavy-duty vehicle markets. Enova's family of light-duty drive systems includes:

- 30kW, 60kW, 90kW all-electric drives
- 90kW series-hybrid drive
- combinations of these systems based on customer requirements.

Our family of heavy-duty electric drive systems includes:

- 120kW all-electric drive o 120/60kW peak series hybrid system
- 240/60kW peak series hybrid system
- 90kW peak mild, pre-transmission parallel hybrid system
- 100kW peak post-transmission parallel hybrid systems
- 100kW peak pre-transmission parallel hybrid system.

Enova's drive systems, in conjunction with, internal combustion engines, microturbines, fuel cells, flywheels, and generators sets provide state of the art hybrid-electric propulsion systems.

Hybrid vehicles are those that utilize an electric motor and batteries in conjunction with an internal combustion engine (ICE), whether piston or turbine. With a hybrid system, a small piston or turbine engine - fueled by gasoline or diesel, CNG, methane, etc., in a tank - supplements the electric motor and battery. These systems are self-charging, in that the operating ICE recharges the battery.

There are two types of hybrid systems: series and parallel. A series hybrid system is one where only the electric motor connects to the drive shaft; a parallel hybrid system is one where both the internal combustion engine and the electric motor are connected to the drive shaft. In a series hybrid system, the ICE turns the generator, which charges the battery, which -- through a control unit - powers the electric motor, which turns the wheels. In a parallel hybrid system, both the electric motor and the ICE can operate simultaneously to drive the wheels. (See diagrams below.) In both hybrid systems and in pure electric systems, regenerative braking occurs, which assists in the charging of the

batteries.

The parallel hybrid system is ideally suited for conditions where most of the driving is done at constant speed cruising, with a smaller amount of the driving involving random acceleration, such as "up hill" or with "stop and go"

conditions. For acceleration, the controller causes the electric motor to kick in to assist the ICE, both running simultaneously. When speed is steady or the ground is flat, only the ICE runs. Additionally, when the batteries are low, the controller causes the ICE and motor to charge the batteries. As a result, the series hybrid system is best suited for starts and stops, and is ideal for applications such as urban transit buses and urban garbage trucks. The design of the series hybrid system is based on a driving cycle with a high percentage of random acceleration conditions.

System	Applications	Advantages
Series Hybrid	Driving with high percentage stop and go and/or hilly terrain	Optimally-sized IC engine Advanced engine/turbine may be used Simplified transmission Independent control
Parallel Hybrid	Driving with high percentage constant speed cruising	No generator and converter needed The drive system may be smaller

Hybrid Drive Configurations

Enova has identified three primary configurations based upon how well they meet market needs economic requirements. The company has developed all of the relevant technology required to produce these drive systems and is currently introducing the Hybrid Power product line worldwide. All of our innovative hybrid drive systems are compatible with wide range of fuel sources and engine configurations.

Hybrid Drive Motors

The electric drive unit is essentially an electric motor with additional features and functionality. The motor is liquid-cooled, environmentally sealed, designed to handle automotive shock and vibration, and includes parking pawl, which stops the vehicle when the driver parks the car. It also permits regenerative braking to provide power recovery, in which the mechanical energy of momentum is converted into electrical energy as the motor slows during braking or deceleration. The optional gear reduction unit takes the electric motor's high rpm and gears it down to the lower rpm required by the vehicle's conventional drive shaft. As the revolutions per minute (rpm) go down, the torque of the electric motor increases.

The HybridPower drive systems exclusively utilize induction AC motors for their high performance, power density, and low cost. The AC drive system is scaleable and can be customized for different applications. Due to the large operating range that these propulsion systems offer, all parameters can be

optimized; the user will not have to choose between acceleration, torque or vehicle speed.

Hybrid Motor Controllers

The controller houses all the components necessary to control the powering of a vehicle, in one easy-to-install package. Our main component is an inverter, which converts DC electricity to AC electricity. Enova also offers optional controllers for the air conditioning, power steering and heat pump, 12VDC/24VDC DC-to-DC converter for vehicle auxiliary loads such as cell phones, radio, lights, and a 6.6kW AC-to-DC on-board conductive charger which allows for direct 110 VAC or 220 VAC battery charging. These are located in the same housing as the controller, thus extra interconnects are not required. This approach simplifies the vehicle wiring harness and increases system reliability.

Using our proprietary Windows based software package, vehicle interfaces and control parameters can be programmed in-vehicle. Real-time vehicle performance parameters can be monitored and collected.

Hybrid Drive Systems

The Enova hybrid drive family currently includes a 120/60kW peak series hybrid system, a 240/60kW peak series hybrid system, a 90kW peak mild, pre-transmission parallel hybrid system, a 100kW peak post-transmission parallel hybrid systems and our 100kW peak pre-transmission parallel hybrid system to be introduced later this year.

The Enova HybridPower hybrid-electric drive systems are based on the component building blocks of the electric drive family, including the motor, controller and optional components. As an example, the 120/60 kW series hybrid system uses the 120kW electric drive components to propel the vehicle, and uses a 60kW diesel generator (genset)to generate power while the vehicle is in operation. This synergy of design reduces the development cost of the Company's hybrid systems by taking advantage of existing designs. The diesel genset has been designed to take advantage of many different models of internal combustion engines for greater penetration into the burgeoning heavy-duty hybrid vehicle markets. Enova's genset will accept any engine with an industry standard bell housing and flywheel. Enova's control protocols are designed to easily interface with any standard engine controller with analog throttle inputs. Accessories for these drives include battery management, chargers and 12-volt power supplies.

The Company's hybrid systems are designed to work with a variety of hybrid power generation technologies. In the Company's 120/60kW hybrid system, an internal combustion engine connected to a motor and motor controller performs the power generation. Other power options include liquid fueled turbines, such

as the Capstone system, fuel cells, such as the Hydrogenics or Ballard system, or many others. In all of these examples, Enova's battery management system provides the power management to allow for proper power control.

Drive System Accessories

Enova's drive system accessories range from battery management systems to hybrid controllers, to rapid charging systems. These critical components are designed to complement the HybridPower drive system family by providing the elements necessary to create a complete technical solution for alternative energy drive systems.

Enova's drive system accessories are not only integral, but are also the

perfect complement to our drive systems and are designed to provide our customers with a complete solution to their drive system needs.

Battery Care Unit

Enova's Battery Care Unit (BCU) monitors, manages, protects, and reports on the condition of the vehicles battery pack. It controls and manages battery performance, temperature, voltage and current to avoid harm to the batteries, to the entire system, and to the driver, operator and passengers. It also allows for monitoring for service to the battery and drive system. The BCU reports state-of-charge, amp hours and kilowatt-hours.

The BCU monitors the battery pack voltage and 28 additional individual voltages with a range of 0 to 18vDC. Optional expansion modules allow 28 additional inputs per module, with up to 16 modules permitted. The BCU has eight user-programmable outputs and four user-programmable inputs to allow full integration into the vehicle. These can be used to customize input and output parameters, and to provide for other custom monitoring and battery pack control. The device is approximately 7.1 inches by 4.3 inches by 1.6 inches.

The BCU directly interfaces with the HybridPower and other drive systems, and controls the Safety Disconnect Unit (SDU). It is capable of supporting any battery technology, and provides each type with optimized charging and protection algorithms. An internal real-time clock allows the BCU to wake up at user-specified times to initiate battery charging or pack monitoring. A precision shunt allows it to offer a wide dynamic range for monitoring charging and motoring current, without the errors commonly associated with other types of sensors.

The non-volatile RAM allows the BCU to update, store and report key battery pack parameters such as amp hours, kilowatt-hours and state of change. Using Enova's proprietary Windows -based diagnostic software, the BCU control parameters can be programmed "live" in-vehicle. Additionally, battery performance can be monitored in real-time. Reports can be output to a laptop computer for precise results and "customer friendly" usage.

Hybrid Control Unit

Enova's Hybrid Control Unit (HCU) continuously monitors the condition of the battery pack through communications with the BCU, monitors the driver commands through communications with the motor controller, and the state of the hybrid generator. Based upon the data received, the HCU provides continuous updates to the hybrid generator with instructions on mode of operation and power level. This innovative control loop ensures that the entire system is optimized to provide quick response to driver commands while providing the best possible system efficiency.

Safety Disconnect Unit

The Safety Disconnect Unit (SDU) is under the control of the BCU, and allows vehicle systems to easily connect and disconnect from the battery pack, when necessary, to prevent damage or harm. It also disconnects the battery pack during charging, protects it from surges, and constantly verifies that the battery pack is isolated from the vehicle chassis. In the event a ground isolation fault is detected, the BCU commands the SDU to break the battery connection, thus ensuring a safe environment for the vehicle and operator. The SDU is available in two configurations to match the requirements of the drive systems.

High Voltage Disconnect Unit

The High Voltage Disconnect Unit (HVDU) is a reduced feature version of the

Safety Disconnect Unit. The pre-charge board has been eliminated in order to provide a lower cost method of safely switching high voltage systems on the vehicle that do not require the soft start feature.

Wiring Harness Connector Kits

Enova provides complete mating connector kits to help the vehicle OEM with their production process. By using the Enova supplied kit the vehicle manufacturer is ensuring that they will have all of the necessary connectors to complete the vehicle build.

Distributed Power Generation for Industrial / Commercial / Residential Applications

Enova's distributed generation products are virtually identical in system configuration to that of a series hybrid vehicle, including a controller and battery management. For this market segment, we intend to provide DC-DC and DC-AC power conversion components to convert power supplied by batteries, fuel cells, generators and turbines to AC power that will be used by the end customer. Additionally, our BCU will provide power management functions to control the entire system. The main difference is that the 3-phase AC power typically supplied to the motor for propulsion power is, in this case, sent to the customer to supply power for their household or business.

20kW bi-directional Fuel Cell Power Conditioning System

Enova's 20kW bi-directional Fuel Cell Power Conditioning System, originally designed to meet the demands of an automotive Fuel Cell propulsion system, is now being applied to the stationary market for distributed generation applications.

This unique unit, not much larger than a conventional briefcase, provides a transparent interface between the Fuel Cell or Turbine, the battery pack, accessory loads, and the output load. Fast response time allows the output load to be serviced without interruption while the Fuel Cell or Turbine ramps up.

This unit is designed to interface directly with the Master Controller of the Stationary Generation System over a CAN bus. Other communications protocols supported are SAE J-1850, RS-232, and RS-485. Our proprietary package diagnostic software allows all key parameters of the Power Conditioner to be monitored and control boundaries to be adjusted.

Fuel Cell Management Unit

Enova has reconfigured its Battery Management Unit to perform the functions required to monitor, manage, and report on the status of a Fuel Cell Stack. The FCU monitors the fuel cell voltage and 28 additional individual voltages with a range of 0 to 18vDC. Optional expansion modules allow 28 additional inputs per module, with up to 16 modules permitted. The FCU has eight (8) user-programmable outputs and four (4) user-programmable inputs to allow full integration into the distributed generation system. These can be used to customize input and output parameters, and to provide for other custom monitoring and battery pack control.

Research and Development Strategy

Enova maintains a strategy of continual enhancement of its current product line and development of more efficient and reliable products for the ever-changing alternative energy sectors. Management believes R&D must be continued in order to remain competitive, minimize production cost and meet our

customers' specifications. Because microprocessors and other components continue to advance in speed, miniaturization and reduction of cost, Enova must re-examine its designs to take advantage of such developments. Enova endeavors to fund its R&D through customer contracts where applicable, however it will provide internal funding where technology developed is critical to its future.

Enova's commitment to advancing technological superiority is evidenced by its internal efforts as well as its joint venture with HHI for future technologies.

Manufacturing Strategy

Our products are "production-engineered," meaning they are designed so they can be commercially produced without additional development. All formats and files are designed with manufacturability in mind from the start. For the automotive market, Enova designs its products to ISO 900X manufacturing and quality standards. We believe that our redundancy of systems, robustness of design, and rigorous quality standards result in higher performance and reduced risk. For every component and piece of hardware, there are detailed performance specifications. Each piece is tested and evaluated against these specifications, which enhances the value of the systems to OEM customers.

We have developed a multi-tiered manufacturing strategy that allows the company to meet the market's demand for high quality production goods while optimizing cost of goods sold across the spectrum of low to high volumes. At the core of this strategy is a strong reliance on pre-selected highly qualified outside manufacturing houses that specialize in various aspects of the manufacturing process. It is through this closely managed outsourcing strategy that Enova is able to achieve improved gross margins while minimizing fixed costs within the organization.

All tiers of manufacturing of electronic components begin with a complete engineering design package that includes a drawing tree, bill of material, electrical and mechanical drawings, and control software where appropriate. The

control software and the design package are internally reviewed, validated, and released through our configuration management process.

For low volume manufacturing, where volumes are less than 10 to 20 units, the process is similar to that for prototyping. Low volume manufacturing and testing is performed in-house.

For higher volume manufacturing, Enova has established strategic alliances with ISO-900X certified manufacturers that can take on all aspects of the process from component sourcing, to circuit card assembly, to component assembly, to final unit assembly and test. These completed components and units are shipped to our facility where complete drive systems that meet the customer's unique requirements are packaged and shipped.

As our market continues to grow and individual customers begin to order higher quantities of fixed drive system configurations, we will transition to a system where the final assembly is drop shipped directly to the end customer. This critical concept has already been discussed with our strategic manufacturing partners.

Competitive Conditions

Competition within the mobile and stationary hybrid power sector is still somewhat fragmented, although there are indications of some consolidation at this time. The market is still divided into very large players such as Allison,

Siemens, BAE and Eaton; or smaller competitors such as ISE Research, Azure Dynamics/Solectria; PEI, Unique Mobility and others. The larger companies tend to still focus on single solutions but maintain the capital and wherewithal to aggressively market such. The smaller competitors offer a more diversified product line, but do not have the market presence to generate significant penetration at this juncture.

Our research and experience has indicated that our target market segments certainly focus on price, but would buy based on reliability, performance and quality support when presented the life-cycle business model for hybrid technologies for their application. Enova has good indications that many would pay a 10-20% premium for hybrids from a secure vendor providing warrantied performance, quality service and support.

The competition to develop and market electric, hybrid and fuel cell powered vehicles has increased during the last year and we expect this trend to continue. The competition consists of development stage companies as well as major U.S. and international companies. Our future prospects are highly dependent upon the successful development and introduction of new products that are responsive to market needs and can be manufactured and sold at a profit. There can be no assurance that we will be able to successfully develop or market any such products.

The development of hybrid-electric and alternative fuel vehicles, such as compressed natural gas, fuel cells and hybrid cars poses a competitive threat to our markets for low emission vehicles or LEVs but not in markets where government mandates call for zero emission vehicles or ZEVs. Enova is involved in the development of hybrid vehicles and fuel cell systems in order to meet future requirements and applications.

Various providers of electric vehicles have proposed products or offer products for sale in this emerging market. These products encompass a wide variety of technologies aimed at both consumer and commercial markets. The critical role of technology in this market is demonstrated through several product offerings. As the industry matures, key technologies and capabilities are expected to play critical competitive roles. Our goal is to position ourselves as a long term competitor in this industry by focusing on electric, hybrid and fuel cell powered drive systems and related sub systems, component integration, technology application and strategic alliances. The addition of new strategies to penetrate stationary power markets with current technologies will assist in creating a more diversified product mix. We believe that this strategy will enhance our position as a power management and conversion components supplier to both the mobile and stationary power markets.

Research and Development

Enova believes that timely development and introduction of new technology and products are essential to maintaining a competitive advantage. We are currently focusing our development efforts primarily in the following areas:

*Power Control and Drive Systems and related technologies for vehicle applications;
*Stationary Power Management and Conversion and related technologies;
*Heavy Duty Drive System development for Buses; Trucks, Industrial, Military and Marine applications
*Fuel Cell Generation system power management and process control
*Systems Integration of these technologies;
*Technical and product development under DOE/DOT/DOD and Hyundai Group Contracts
*OEM Technical and Product development.

For the years ended December 31, 2005, 2004, 2003 and 2002, we spent

$804,000, $925,000, $799,000, and $1,152,000, respectively, on internal research and development activities. Enova is continually evaluating and updating the

technology and equipment used in developing each of its products. The power management and conversion industry utilizes rapidly changing technology and we will endeavor to modernize our current products as well as continue to develop new leading edge technologies to maintain our competitive edge in the market.

Intellectual Property

Enova currently holds four U.S. patents and has one patent pending, relating to power management and control, with an additional patent relating to crash management safety, which was originally issued in 1997. We also have trademarks or service marks in the United States and have been filing for international patents as well. We continually review and append our protection of proprietary technology. We continue to place emphasis on the development and acquisition of patentable technology, however, a majority of our intellectual property is contained within our software which we believe is best protected under trade secret provision of U.S. patent law. Under such provisions, Enova does not have to publish its proprietary code in order to maintain protection.

We maintain an internal review and compensation process to encourage our employees to create new patentable technologies. The status of patents involves complex legal and factual questions, and the breadth of claims allowed is uncertain. Accordingly, there can be no assurance that patent applications filed by us will result in patents being issued. Moreover, there can be no assurance that third parties will not assert claims against us with respect to existing and future products. Although we intend to vigorously protect our rights, there can be no assurance that these measures will be successful. In the event of litigation to determine the validity of any third party claims, such litigation could result in significant expense to Enova. Additionally, the laws of certain countries in which our products are or may be developed, manufactured or sold may not protect our products and intellectual property rights to the same extent as the laws of the United States.

Enova's success depends in part on its ability to protect its proprietary technologies. Enova's pending or future patent applications may not be approved and the claims covered by such applications may be reduced. If allowed, patents may not be of sufficient scope or strength, others may independently develop similar technologies or products, duplicate any of Enova's products or design around its patents, and the patents may not provide Enova with competitive advantages. Further, patents held by third parties may prevent the commercialization of products incorporating Enova's technologies or third parties may challenge or seek to narrow, invalidate or circumvent any of Enova's pending or future patents. Enova also believes that foreign patents, if obtained, and the protection afforded by such foreign patents and foreign intellectual property laws, may be more limited than that provided under United States patents and intellectual property laws. Litigation, which could result in substantial costs and diversion of effort by Enova, may also be necessary to enforce any patents issued or licensed to Enova or to determine the scope and validity of third-party proprietary rights. Any such litigation, regardless of outcome, could be expensive and time-consuming, and adverse determinations in any such litigation could seriously harm Enova's business.

Enova relies on unpatented trade secrets and know-how and proprietary technological innovation and expertise which are protected in part by confidentiality and invention assignment agreements with its employees, advisors and consultants and non-disclosure agreements with certain of its suppliers and distributors. These agreements may be breached, Enova may not have adequate

remedies for any breach or Enova's unpatented proprietary intellectual property may otherwise become known or independently discovered by competitors. Further, the laws of certain foreign countries may not protect Enova's products or intellectual property rights to the same extent as do the laws of the United States.

Employees

As of December 31, 2005, we had 29 full time employees. Additionally, we employ 4 individuals as independent contractors, engaged on an hourly basis, one of whom is domiciled in South Korea. The departmental breakdown of these individuals includes 4 in administration, 1 in sales, 12 in engineering and research and development, and 12 in production.

Available Information

Our website address is www.enovasystems.com; however, information found on, or that can be accessed through, our website is not incorporated by reference into this annual report. We file electronically with the SEC our annual report, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934. We make available free of charge on or through our website copies of these reports as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC. The SEC maintains an internet site that contains reports, proxy and information statements and other information regarding our filings at www.sec.gov. You may also read and copy any of our materials filed with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington, DC 20549. Information regarding the operation of the Public Reference Room can be obtained by calling the SEC at 1-800-SEC-0330.

Item 1A. Risk Factors

This Form 10-K contains forward looking statements concerning our existing and future products, markets, expenses, revenues, liquidity, performance and cash needs as well as our plans and strategies. These forward-looking statements involve risks and uncertainties and are based on current management's expectations and we are not obligated to update this information. Many factors could cause actual results and events to differ significantly from the results anticipated by us and described in these forward looking statements including, but not limited to, the following risk factors. You should carefully consider these risk factors as each of these risks could adversely affect our business, operating results and financial condition. In those cases, the trading of our common stock could decline and you may lose all or a part of your investment.

We may not have net operating losses in the future against which to offset our future profits, if any.

We have experienced recurring losses from operations and had an accumulated deficit of $102,586,000 at December 31, 2005. There is no assurance, however, that any net operating losses will be available to us in the future as an offset against future profits, if any, for income tax purposes.

We have experienced continued losses and may never become profitable.

For the years ended December 31, 2005, 2004, 2003 and 2002, we had net losses of $2,127,000, $3,382,000, $3,186,000, and $3,598,000, respectively, on sales of $6,084,000, $2,554,000, $4,310,000, and $4,455,000, respectively. We may never become profitable, which may cause the market price of our common stock to drop.

The nature of our industry is dependent on technological advancement and highly competitive.

The mobile and stationary power markets, including electric vehicle and hybrid electric vehicles, continue to be subject to rapid technological change. Most of the major domestic and foreign automobile manufacturers: (1) have already produced electric and hybrid vehicles, and/or (2) have developed improved electric storage, propulsion and control systems, and/or (3) are now entering or have entered into production, while continuing to improve technology or incorporate newer technology. Various companies are also developing improved electric storage, propulsion and control systems. In addition, the stationary power market is still in its infancy. A number of established energy companies are developing new technologies. Cost-effective methods to reduce price per kilowatt have yet to be established and the stationary power market is not yet viable.

Our current products are designed for use with, and are dependent upon, existing technology. As technologies change, and subject to our limited available resources, we plan to upgrade or adapt our products in order to continue to provide products with the latest technology. We cannot assure you, however, that we will be able to avoid technological obsolescence, that the market for our products will not ultimately be dominated by technologies other than ours, or that we will be able to adapt to changes in or create "leading-edge" technology. In addition, further proprietary technological development by others could prohibit us from using our own technology.

Our industry is affected by political and legislative changes.

In recent years there has been significant public pressure to enact legislation in the United States and abroad to reduce or eliminate automobile pollution. Although states such as California have enacted such legislation, we cannot assure you that there will not be further legislation enacted changing current requirements or that current legislation or state mandates will not be repealed or amended, or that a different form of zero emission or low emission vehicle will not be invented, developed and produced, and achieve greater market acceptance than electric or hybrid electric vehicles. Extensions, modifications or reductions of current federal and state legislation, mandates and potential tax incentives could also adversely affect our business prospects if implemented.

We are subject to increasing emission regulations in a changing legislative climate.

Because vehicles powered by internal combustion engines cause pollution, there has been significant public pressure in Europe and Asia, and enacted or pending legislation in the United States at the federal level and in certain states, to promote or mandate the use of vehicles with no tailpipe emissions ("zero emission vehicles") or reduced tailpipe emissions ("low emission vehicles"). Legislation requiring or promoting zero or low emission vehicles is necessary to create a significant market for electric vehicles. The California Air Resources Board (CARB) is continuing to modify its regulations regarding its mandatory limits for zero emission and low emission vehicles. Furthermore, several car manufacturers have challenged these mandates in court and have obtained injunctions to delay these mandates.

There are substantial risks involved in the development of unproven products.

In order to remain competitive, we must adapt existing products as well as develop new products and technologies. In fiscal years 2005, 2004 and 2003, we spent collectively in excess of $2.5 million on research and development of new products and technology. Despite our best efforts a new product or technology

may prove to be unworkable, not cost effective, or otherwise unmarketable. We

cannot assure you that any new product or technology we may develop will be successful or that an adequate market for such product or technology will ever develop.

We may be unable to effectively compete with other companies who have significantly greater resources than we have.

Many of our competitors, in the automotive, electronic and other industries, are larger, more established companies that have substantially greater financial, personnel, and other resources than we do. These companies may be actively engaged in the research and development of power management and conversion systems. Because of their greater resources, some of our competitors may be able to adapt more quickly to new or emerging technologies and changes in customer requirements, or to devote greater resources to the promotion and sales of their products than we can. We believe that developing and maintaining a competitive advantage will require continued investment in product development, manufacturing capability and sales and marketing. We cannot assure you however that we will have sufficient resources to make the necessary investments to do so. In addition, current and potential competitors may establish collaborative relationships among themselves or with third parties, including third parties with whom we have relationships. Accordingly, new competitors or alliances may emerge and rapidly acquire significant market share.

Future equity financings may dilute your holdings in our Company.

We may need to obtain additional funding through public or private equity or debt financing, collaborative agreements or from other sources. If we raise additional funds by issuing equity securities, current shareholders may experience significant dilution of their holdings. We may be unable to obtain adequate financing on acceptable terms, if at all. If we are unable to obtain adequate funds, we may be required to reduce significantly our spending and delay, scale back or eliminate research, development or marketing programs, or cease operations altogether.

Potential intellectual property, shareholder or other litigation could adversely impact our business.

Because of the nature of our business, we may face litigation relating to intellectual property matters, labor matters, product liability or shareholder disputes. Any litigation could be costly, divert management attention or result in increased costs of doing business. Although we intend to vigorously defend any future lawsuits, we cannot assure you that we would ultimately prevail in these efforts. An adverse judgment could negatively impact the price of our common stock and our ability to obtain future financing on favorable terms or at all.

We may be exposed to product liability or tort claims if our products fail, which could adversely impact our results of operations.

A malfunction or the inadequate design of our products could result in product liability or other tort claims. Accidents involving our products could lead to personal injury or physical damage. Any liability for damages resulting from malfunctions could be substantial and could materially adversely affect our business and results of operations. In addition, a well-publicized actual or perceived problem could adversely affect the market's perception of our products. This could result in a decline in demand for our products, which would materially adversely affect our financial condition and results of operations.

We are highly subject to general economic conditions.

The financial success of our company is sensitive to adverse changes in general economic conditions, such as inflation, unemployment, and consumer demand for our products. These changes could cause the cost of supplies, labor, and other expenses to rise faster than we can raise prices. Such changing conditions also could significantly reduce demand in the marketplace for our products. We have no control over any of these changes.

We are an early growth stage company.

Although our Company was originally founded in 1976, many aspects of our business are still in the early growth stage development, and our proposed operations are subject to all of the risks inherent in a start-up or growing business enterprise, including the likelihood of continued operating losses. Enova is relatively new in focusing its efforts on electric systems, hybrid systems and fuel cell management systems. The likelihood of our success must be considered in light of the problems, expenses, difficulties, complications, and delays frequently encountered in connection with the growth of an existing business, the development of new products and channels of distribution, and current and future development in several key technical fields, as well as the competitive and regulatory environment in which we operate.

We operate in a highly regulated business environment and changes in regulation could impose costs on us or make our products less economical.

Our products are subject to federal, state, local and foreign laws and regulations, governing, among other things, emissions as well as laws relating to occupational health and safety. Regulatory agencies may impose special requirements for implementation and operation of our products or may significantly impact or even eliminate some of our target markets. We may incur material costs or liabilities in complying with government regulations. In addition, potentially significant expenditures could be required in order to comply with evolving environmental and health and safety laws, regulations and requirements that may be adopted or imposed in the future.

We are highly dependent on a few key personnel and will need to retain and attract such personnel in a labor competitive market.

Our success is largely dependent on the performance of our key management and technical personnel, including Edwin Riddell, our Chief Executive Officer and Acting Chief Financial Officer and Don Kang, our Vice President of Engineering, the loss of one or more of whom could adversely affect our business. Additionally, in order to successfully implement our anticipated growth, we will be dependent on our ability to hire additional qualified personnel. There can be no assurance that we will be able to retain or hire other necessary personnel. We do not maintain key man life insurance on any of our key personnel. We believe that our future success will depend in part upon our continued ability to attract, retain, and motivate additional highly skilled personnel in an increasingly competitive market.

There are minimal barriers to entry in our market.

We presently license or own only certain proprietary technology and, therefore, have created little or no barrier to entry for competitors other than the time and significant expense required to assemble and develop similar production and design capabilities. Our competitors may enter into exclusive arrangements with our current or potential suppliers, thereby giving them a competitive edge which we may not be able to overcome, and which may exclude us from similar

relationships.

We extend credit to our customers, which exposes us to credit risk.

Most of our outstanding accounts receivable are from a limited number of large customers. At December 31, 2005, the five highest outstanding accounts receivable balances totaled $2.3 million, representing 99% of our gross accounts receivable, with one customer accounting for $1.8 million, representing 77% of our gross accounts receivable. If we fail to monitor and manage effectively the resulting credit risk and a material portion of our accounts receivable is not paid in a timely manner or becomes uncollectible, our business would be significantly harmed, and we could incur a significant loss associated with any outstanding accounts receivable.

We are exposed to risks relating to evaluations of our internal controls.

In connection with the audit of our financial statements for the year ended December 31, 2005, Singer Lewak Greenbaum & Goldstein LLP, our independent registered public accounting firm, notified our management and audit committee of the existence of "significant deficiencies in internal controls," which is an accounting term for internal controls deficiencies that, in the judgment of our independent registered public accounting firm, are significant and which could adversely affect our ability to record, process, summarize and report financial information.

Singer Lewak Greenbaum & Goldstein LLP concluded that these significant deficiencies constituted a "material weakness" in our internal controls. Auditing literature defines "material weakness" as a particularly serious reportable condition where the internal control does not reduce to a relatively low level the risk that misstatements caused by error or fraud may occur in amounts that would be material in relation to the financial statements and the risk that such misstatements would not be detected within a timely period by employees in the normal course of performing their assigned functions. A "material weakness" is a control deficiency, or combination of control deficiencies, that results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected.

As of December 31, 2005, we did not maintain effective controls over the inventory pricing, tracking, and the reserve analysis process. This control deficiency resulted in an audit adjustment to our 2005 financial statements and could result in a misstatement to cost of sales that would result in a material misstatement to the annual and interim financial statements that would not be prevented or detected. Furthermore, our management has determined that, as of December 31, 2005, we do not have sufficient segregation of duties in relation to the accounting function. This deficiency could result in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected. Accordingly, our management has determined that these deficiencies constitute a material weakness. Because of these material weaknesses, our management has concluded that we did not maintain effective internal control over financial reporting as of December 31, 2005.

Under the current SEC rules and regulations as we understand them, for the year ending on or after July 15, 2007, our management will be required to assess, and our independent registered public accounting firm will be required to attest as to our assessment regarding, the effectiveness of our internal controls in order to satisfy the requirements of Section 404 of the Sarbanes-Oxley Act and the related SEC rules. While we intend to address these material weaknesses and have begun efforts to remediate these material weaknesses, including, subsequent to the filing of this annual report on Form 10-K, the hiring of a Chief Financial Officer and a Controller to oversee the remedial process, there is no assurance that this will be accomplished. These efforts may necessitate significant time

and attention of our management and additional resources. If we fail to satisfactorily strengthen the effectiveness of our internal controls, neither we nor our independent registered public accounting firm may be able to conclude on an ongoing basis that we have effective internal control over financial reporting in accordance with Section 404 of the Sarbanes-Oxley Act.

Item 2. Properties

Enova's corporate offices are located in Torrance, California, in leased office space of approximately 20,000 square feet. This facility houses our various departments, including engineering, operations, executive, finance, planning, purchasing, investor relations and human resources. This lease terminates in February 2008. The monthly lease expense is approximately $14,000. Enova also has a leased office in Hawaii which is rented on a month-to-month basis at $1,500 per month, and a sales office in Michigan that it leases on a month-to-month basis at $500 per month.

Item 3. Legal Proceedings

We may from time to time become a party to various legal proceedings arising in the ordinary course of business. At December 31, 2005, the Company had no known material current, pending or threatened litigation.

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

No matters were submitted to a vote of security holders during the fourth quarter of fiscal 2005.

PART II

Item 5. Market for Registrant's Common Equity, Related Shareholder Matters and Issuer Purchases of Equity Securities

During 2005, the Company effected a reverse stock split into a fraction thereof of 1/45th of a share of our outstanding common stock. In lieu of any fractional shares to which a holder of Common Stock would otherwise be entitled, we paid cash equal to (a) the average of the high-bid and low-asked per share prices of the Common Stock as reported on the NASDAQ electronic "Bulletin Board" on the Effective Date multiplied by (b) the number of shares of Common Stock

held by such holder that would otherwise have been exchanged for such fractional share interest.. As such, the number of issued and outstanding shares of common stock as of December 31, 2005 reflects the effects of the reverse-split. The number of shares of common stock authorized remains at 750,000,000. These are reflected in the financial statements as of December 31, 2005.

The shares of the Company's Common stock are traded on the NASDAQ Over-the-Counter Bulletin Board System under the trading symbol "ENOV" and on the London Stock Exchange AIM Market under the symbol "ENVS.L" or "ENV.L". The following table sets forth the high and low bid prices of the Common Stock as reported on the NASD Bulletin Board by the National Quote Bureau for the fiscal quarters indicated. The following over-the-counter market quotations reflect inter-dealer prices, without retail mark-up, markdown or commission, and may not necessarily represent actual transactions. Quotations have been restated to reflect the 1-45 reverse stock split, effective July 20, 2005.

	Common Stock		Average Daily
	High Price	Low Price	Volume

Calendar 2004			
First Quarter	$ 9.45	$ 4.05	22,237
Second Quarter	$ 8.55	$ 4.05	10,663
Third Quarter.	$ 6.75	$ 5.40	6,529
Fourth Quarter.	$ 6.75	$ 4.05	6,847
Calendar 2005			
First Quarter	$ 5.40	$ 4.05	5,285
Second Quarter	$ 5.18	$ 3.38	4,164
Third Quarter.	$ 5.90	$ 2.50	6,461
Fourth Quarter.	$ 4.50	$ 3.25	7,976

On March 28, 2006, the last reported high bid price of the Common Stock was $5.05 and the last reported low bid price was $5.05. As of March 28, 2006, there were approximately 1,489 holders of record of our Common Stock. As of March 28, 2005, approximately 106 shareholders, many of who are also Common Stock shareholders, held our Series A Preferred Stock. Approximately 34 shareholders as of March 28, 2006 held our Series B Preferred Stock. The number of holders of record excludes beneficial holders whose shares are held in the name of nominees or trustees.

Stock Issuances

On July 19, 2005, we entered into an agreement with a placement agent relating to the sale of up to 5,350,000 new shares of our common stock, after the reverse 1-45 stock split as described above. Pursuant to the agreement, we sold all such shares of common stock at a price of $3.78 per share to certain eligible investors located outside the United States pursuant to the requirements of Regulation S under the Securities Act of 1933, as amended. The gross proceeds from the sale are approximately $20,000,000, before fees to Investec Bank, which served as our nominated advisor and broker, and other costs associated with the listing and placement of approximately $2,000,000. We received approximately $18,000,000 of net proceeds from the offering.

We listed our common stock for trading on the AIM Market of the London Stock Exchange on July 25, 2005.

Dividend Policy

To date, we have neither declared nor paid any cash dividends on shares of our Common Stock or Series A or B Preferred Stock. We presently intend to retain all future earnings for our business and do not anticipate paying cash dividends on our Common Stock or Series A or B Preferred Stock in the foreseeable future. We are required to pay dividends on our Series A and B Preferred Stock before dividends may be paid on any shares of Common Stock. At December 31, 2005, Enova had an accumulated deficit of approximately $102,586,000 and, until this deficit is eliminated, will be prohibited from paying dividends on any class of stock except out of net profits, unless it meets certain asset and other tests under Section 500 et. seq. of the California Corporations Code.

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Item 6. Selected Financial Data

The following selected financial data tables set forth selected financial data for the years ended December 31, 2005, 2004, 2003, 2002 and 2001. The

statement of operations data and balance sheet data for and as of the end of the years ended December 31, 2005, 2004, 2003, 2002 and 2001 are derived from the audited financial statements of Enova. The following selected financial data should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the Financial Statements, including the notes thereto, appearing elsewhere in this Form 10K.

	As of and for the year ended December 31 (in thousands, except per share data),				
	2005	2004	2003	2002	2001
Net revenues	$ 6,084	$ 2,554	$ 4,310	$ 4,455	$ 3,7
Cost of revenues	6,001	2,239	3,304	3,784	2,7
Gross margin	83	315	1,006	671	9
Operating expenses					
Research and development	804	925	799	1,152	8
Asset impairment			200		
Selling, general and administrative	2,870	2,325	2,919	2,837	2,8
Total operating expense	3,674	3,250	3,918	3,989	3,7
Other income and expense					
Interest and financing income and (fees)	13	(255)	(234)	(199)	(1
Equity in losses	(118)	(192)	(40)	--	
Legal settlements	--	--	--	(81)	(9
Gain on debt restructuring	1,569	--	--	--	3
Total other income and (expense)	1,464	(447)	(274)	(280)	(6
Net loss	$ (2,127)	$ (3,382)	$ (3,186)	$ (3,598)	$ (3,4
Per common share:					
Net loss per common share	$ (0.18)	$ (0.38)	$ (0.43)	$ (0.49)	$ (0.
Weighted average number common shares outstanding	11,644	8,832	7,441	7,253	6,1
Total assets	$ 21,973	$ 5,888	$ 4,870	$ 6,224	$ 4,3
Long-term debt	$ 2,321	$ 3,341	$ 3,347	$ 3,332	$ 3,3
Shareholders' equity (deficit)	$ 16,604	$ 103	$ (864)	$ 287	$ (2

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

You should read this Management's Discussion and Analysis of Financial Condition and Results of Operations in conjunction with our 2005 Financial

Statements and Notes thereto. The matters addressed in this Management's Discussion and Analysis of Financial Condition and Results of Operations, may contain certain forward-looking statements involving risks and uncertainties. Our actual results, levels of activity, performance, achievements and events could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including those set forth under the heading "Risk Factors" and elsewhere in this report.

These forward-looking statements are made as of the date of this Form 10-K, and, except as required under applicable securities law, we assume no obligation to update them or to explain the reasons why actual results may differ.

OVERVIEW

Enova Systems believes it is a leading supplier of efficient, environmentally-friendly digital power components and systems products in conjunction with our associated engineering services. Our core competencies are focused on the development and commercialization of power management and conversion systems for mobile and stationary applications. Enova applies unique `enabling technologies' in the areas of alternative energy propulsion systems for light and heavy-duty vehicles as well as power conditioning and management systems for distributed generation systems. The Company's products can be found in a variety of OEM vehicles including those from Hyundai Motor Company and Ford Motor Company, trucks and buses for First Auto Works of China, Mack Truck, WrightBus of the U.K. and the U.S. Military, as well as digital power systems for EDO, Hydrogenics and UTC Fuel Cells, a division of United Technologies.

Enova's product focus is digital power management and power conversion systems. Its software, firmware, and hardware manage and control the power that drives either a vehicle or stationary device(s). They convert the power into the appropriate forms required by the vehicle or device and manage the flow of this energy to optimize efficiency and provide protection for both the system and its users. Our products and systems are the enabling technologies for power systems.

The latest state-of-the-art technologies, such as hybrid vehicles, fuel cell and micro turbine based systems, and stationary power generation, all require some type of power management and conversion mechanism. Enova Systems supplies these essential components. Enova drive systems are 'fuel-neutral,' meaning that they have the ability to utilize any type of fuel, including diesel, liquid natural gas (LNG) or bio-diesel fuels. We also develop, design and produce power management and power conversion components for stationary power generation - both on-site distributed power and on-site telecommunications back-up power applications. These stationary applications also employ fuel cells, microturbines and advanced batteries for power storage and generation. Additionally, Enova performs significant research and development to augment and support others' and our internal related product development efforts.

Our products are "production-engineered." This means they are designed so they can be commercially produced (i.e., all formats and files are designed with manufacturability in mind, from the start). For the automotive market, Enova designs its products to ISO 9000X manufacturing and quality standards. We believe Enova's redundancy of systems and rigorous quality standards result in high performance and reduced risk. For every component and piece of hardware, there are detailed performance specifications. Each piece is tested and evaluated against these specifications, which enhances and confirms the value of the systems to OEM customers. The Company's engineering services focus on system integration support for product sales and custom product design.

The financial statements present the financial position of Enova Systems, Inc. as of December 31, 2005 and 2004 and the results of operations and cash flows for the years ended December 31, 2005, 2004 and 2003.

CRITICAL ACCOUNTING POLICIES

Financial Reporting Release No. 60 requires all companies to include a discussion of critical accounting policies or methods used in the preparation of financial statements. Note 1 of the notes to the financial statements includes a summary of the significant accounting policies and methods used in the preparation of our financial statements. The following is a brief discussion of the more significant accounting policies and methods that we use.

Our discussion and analysis of our financial condition and result of operations are based on our financial statements, which have been prepared in conformity with accounting principles generally accepted in the United States of America. Our preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. We based our estimates on historical experience

and on various other assumptions that we believe to be reasonable under the circumstances. The most significant estimates and assumptions relate to revenue recognition and potential allowances for doubtful accounts. Actual amounts may differ from such estimates under different assumptions or conditions. The following summarizes our critical accounting policies and significant estimates used in preparing our financial statements:

- The first-in, first-out (FIFO) method to value our inventories;
- The intrinsic value method, or APB Opinion No. 25, to account for our stock options;
- Review of customers' receivables to determine the need for an allowance for credit losses based on estimates of customers' ability to pay. If the financial condition of our customers were to deteriorate, an additional allowance may be required.
- Revenue recognition - The Company is required to make judgments based on historical experience and future expectations, as to the reliability of shipments made to its customers. These judgments are required to assess the propriety of the recognition of revenue based on Staff Accounting Bulletin ("SAB") No. 104, "Revenue Recognition," and related guidance. The Company makes these assessments based on the following factors: i) customer-specific information, ii) return policies, and iii) historical experience for issues not yet identified. Under FAS Concepts No. 5, revenues are not recognized until earned. The percentage-of-completion method can be used to recognize revenues when estimates of costs to complete and the extent of progress toward completion of contracts are reasonably dependable. If reasonably dependable estimates are not available, the percentage-of-completion method should not be used.

These accounting policies are applied consistently for all years presented. Our operating results would be affected if other alternatives were used. Information about the impact on our operating results is included in the footnotes to our financial statements.

LIQUIDITY AND CAPITAL RESOURCES

We have experienced cash flow shortages due to operating losses primarily attributable to research, development, marketing and other costs associated with

our strategic plan as an international developer and supplier of electric propulsion and power management systems and components. Cash flows from operations have not been sufficient to meet our obligations. Therefore, we have had to raise funds through several financing transactions. At least until we reach breakeven volume in sales and develop and/or acquire the capability to manufacture and sell our products profitably, we will need to continue to rely on cash from external financing sources.

Our operations during the year ended December 31, 2005 were financed by development contracts and product sales, as well as from working capital reserves.

During the year ended December 31, 2005, our operations required $2,997,000 more in cash than was generated, versus $2,157,000 in 2004 and $2,319,000 in 2003. Enova continues to increase marketing and development spending as well as administrative expenses necessary for expansion to meet customer demand. Accounts receivable increased by $1,651,000 from $522,000, or approximately 318% from the balance at December 31, 2004 (net of write-offs). The decrease is due to a continued delay in acquiring new business in the third and fourth quarters of 2004. We are beginning to observe an increase in sales activity for our drive systems, components and development services which commenced in the fourth quarter of 2004, which we anticipate will increase receivables in future quarters.

Inventory decreased slightly by $20,000 from $1,036,000 or 2% from the December 31, 2004 balance. The decrease was due to utilization of inventory stock for sales as well as write-offs for obsolete and slow-moving inventory. We charged off approximately $376,000 of this reduction of our inventory relating to obsolete and slow moving raw materials. We believe that the relatively slight fluctuation in the inventory balances compared to the increased sales volume (as noted in the "Results of Operations" below), illustrates Enova's continuing efforts to monitor and control inventory utilization.

Prepaid expenses and other current assets decreased by net $122,000 during 2005 from the December 31, 2004 balance of $304,000 or almost 40%. In 2005 we realized approximately $220,000 in deposits that Enova had made to Hyundai Heavy Industries to assist in the production of hybrid motors for the Tomoe Engineering contract. These deposits were recognized as cost of sales as the final drives were delivered to Tomoe. Furthermore, unbilled revenue associated with the Hyundai Motor Corporation fuel cell bus project, which is accounted for using the percentage of completion milestone method, increased by $91,000 in 2005.

Gross fixed assets increased by $247,000 or 14%, for the year ended December 31, 2005 from the prior year balance of $1,754,000 primarily due to the purchase of additional production tooling, machinery, and equipment associated with production. Additionally, purchased test machines that allow us to test load limits and stresses on the drives. These machines will be integral in supporting Enova's quality control initiatives as well as ISO 9000X requirements.

Investments decreased by $118,000 during 2005, net of our pro-rata share of losses attributable to the investment, which reflects our forty percent (40%) interest in the Hyundai-Enova Innovative Technology Center (ITC) as noted elsewhere in this Form 10-K. For the year ended December 31, 2005, the ITC generated a net loss of approximately $296,000, resulting in a charge to Enova of $118,000 utilizing the equity method of accounting for our interest in the ITC. Based on contractual obligations of our Joint Venture Agreement with Hyundai Heavy Industries Co., we made an additional investment of $1,000,000 in

2004 which was funded by HHI through a stock purchase in September 2004 as noted in the Hyundai-Enova Innovative Technology Center description later in this Form 10-K.

Other assets decreased by $106,000 during 2005 from $296,000 in 2004 as we continued to amortize the asset relating to the Ford Value Participation Agreement. Intellectual property assets, including patents and trademarks increased $1,000 to $93,000 at December 31, 2005.

Accounts payable increased in 2005 by over 2,000% from $66,000 at December 31, 2004 to $1,396,000 at December 31, 2005. At December 31, 2005, Enova has an outstanding trade payable to Hyundai Heavy Industries for approximately $1,250,000, associated with their assistance in the production of hybrid motors for the Tomoe Engineering contract.

Accrued interest decreased by $265,000 for the year ended December 31, 2005, a decrease of 19%. The decrease is associated with the net effect of interest accrued on the Note due the Credit Managers Association of California (CMAC) for $3.2 million per the terms of the Note, combined with the settlement and forgiveness of certain portions of the CMAC note. See additional explanation in the RESULTS OF OPERATIONS section below.

Other accrued expenses and payables increased by $289,000 during 2005 from $13,000 at December 31, 2004. The increase is attributable to additional warranty exposures of $116,000 in 2005. Additionally, there are received but un-invoiced parts for which the company owes Hyundai Heavy Industries of approximately $70,000 associated with their production assistance on the Tomoe Engineering contract. Finally, we accrued an additional $18,000 associated with telephone and network equipment purchased and delivered in the fourth quarter of 2005, but invoiced in January 2006.

The future unavailability or inadequacy of financing to meet future needs could force us to delay, modify, suspend or cease some or all aspects of our planned operations.

RESULTS OF OPERATIONS

Years Ended December 31, 2005 and 2004

Net sales of $6,084,000 for the twelve months ended December 31, 2005 increased by $3,530,000 or 138% from $2,554,000 during the same period in 2004. The increase in sales was a result of Enova's expanding research and development initiatives with Hyundai Motor Company (HMC) as well as the production associated with the Tomoe Machinery contract. In 2005, sales attributable to the Tomoe production contract were about $3,000,000. Additionally, sales related to the HMC development project were approximately $758,000.

Cost of sales consists of component and material costs, direct labor costs, integration costs and overhead related to manufacturing our products. Product development costs incurred in the performance of engineering development contracts for the U.S. Government and private companies are charged to cost of sales for this contract revenue. During 2005, our trend of establishing new customers and strengthening current alliances with customers, such as Tomoe and MTrans in the heavy-duty drive system market continued. Our new customers continue to require additional integration and support services to customize, integrate and evaluate our products. We believe these costs to be initial, one-time costs for these customers and anticipate similar costs to be incurred with respect to new customers as we gain additional market share. Customers who have been using our products over one year do not incur these same type of initial costs. Cost of sales for the year ended December 31, 2005 increased 3,762,000, or 168%, from $2,239,000 for the year ended December 31, 2004. This increase is primarily attributable to the increase in sales for the year and the

scrapping of $376,000 of raw materials that were no longer usable.

Research and development expenses consist primarily of personnel, facilities, equipment and supplies for our research and development activities. Non-funded development costs are reported as research and development expense. Research and development expense decreased in 2005 to $804,000 from $925,000 for the same period in 2004, a decrease of $121,000 or 13%. During 2005, externally funded research and development from partners such as FAW, Mack/Volvo, Hyundai, and the U.S. Government offset the costs of development for new products in the areas of mobile and stationary power management and conversion thereby reducing the need for internal funding. We believe that this trend is continuing. Programs included our new parallel hybrid drive systems, our diesel generation engine/motor system for our heavy-duty drive systems, and upgrades and improvements to our current power conversion and management components. Additionally, we continued to enhance our technologies to be more universally adaptable to the requirements of our current and prospective customers. By modifying our software and firmware, we believe we should be able to provide a more comprehensive, adaptive and effective solution to a larger base of customers and applications. We will continue to research and develop new technologies and products, both internally and in conjunction with our alliance partners and other manufacturers as we deem beneficial to our global growth strategy.

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Selling, general and administrative expenses consist primarily of personnel and related costs of sales and marketing employees, consulting fees and expenses for travel, trade shows and promotional activities and personnel and related costs for general corporate functions, including finance, accounting, strategic and business development, human resources and legal. Selling, general and administrative expenses increased by $545,000 at 2005 from 2004 levels due to increased headcount and the associated increases in wages, health and workers compensation insurance, and taxes of approximately $279,000 and from a $266,000 increase in the allowance for doubtful accounts. For the year ended December 31, 2005, these expenses totaled $2,870,000 up from $2,325,000 for the similar period in 2004. This represents an 23 % increase in these expenses. We are continually reviewing operations to control overhead costs and increase operational efficiencies

For the year ended December 31, 2005, interest and financing fees shifted to a net other income of $13,000 from a net expense of $255,000. The change is a result of the Company's comparatively higher cash balance at 2005 and the associated interest revenue as well as a $50,000 gain on a foreign currency transaction in the United Kingdom. The comparatively higher cash balance was the result of the equity offering that occurred in the third quarter of 2005.

In 2005, we charged off approximately $376,000 of our inventory relating to obsolete and slow moving raw materials. We believe that the relatively slight fluctuation in the inventory balances compared to the increased sales volume illustrates Enova's continuing efforts to monitor and control inventory utilization.

In December 2005, the Company was informed by the Credit Managers Association of California that $1,011,000 of principal and $447,000 accrued interest under the secured note payable had been disclaimed and extinguished by the beneficiaries of such principal amount. The extinguishment result from the resolution of a substantially aged negotiation regarding consideration paid in settlement of the principal amount. The company has recognized a gain on the extinguishment of the principal and associated accrued interest. The Company evaluated this transaction under the guidance set forth in SFAS 140 "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of

Liabilities" and noted that the extinguishment of these liabilities were consistent with the guidance.

In October 2005, the Company agreed to a settlement on the unsecured 10% note payable. In exchange for immediate payment of the full principal balance of $120,000, the beneficiary of the note agreed to forgive the entire accrued interest balance of $111,000. The company has recognized a gain on the extinguishment of the associated accrued interest. The Company evaluated this transaction under the guidance set forth in SFAS 140 "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities" and noted that the extinguishment of these liabilities were consistent with the guidance.

Years Ended December 31, 2004 and 2003

Net sales of $2,554,000 for the twelve months ended December 31, 2004 decreased $1,756,000 or 41% from $4,310,000 during the same period in 2003. During 2004, we experienced a slowdown in sales due to a number of internal and external developments, including personnel changes, and customer delays in ordering caused by continued evaluation or awaiting orders for their products.

Our sources of revenue for 2004 came relatively equally from product sales and development contracts. Product sales as a percentage of total revenues of 57% in 2004 were consistent with the 2003 product sales to total revenues percentage of 56%. Sales of our HybridPower 120kW drive systems accounted for a majority of our product sales in 2004. We believe this trend will continue over the next several years. However we continue to seek out and contract for new development programs with both our current partners such as Ford, Mack/Volvo, FAW, Tomoe, Hyundai and our other U.S., Asian and European alliance partners, as well as with new alliances with other vehicle manufacturers and energy companies.

Cost of sales consists of component and material costs, direct labor costs, integration costs and overhead related to manufacturing our products. Product development costs incurred in the performance of engineering development contracts for the U.S. Government and private companies are charged to cost of sales for this contract revenue. During 2004, our trend of establishing new customers and strengthening current alliances with customers, such as Tomoe and MTrans in the heavy-duty drive system market continued. Our new customers continue to require additional integration and support services to customize, integrate and evaluate our products. We believe these costs to be initial, one-time costs for these customers and anticipate similar costs to be incurred with respect to new customers as we gain additional market share. Customers who have been using our products over one year do not incur these same type of initial costs. Cost of sales for the year ended December 31, 2004 decreased $1,065,000, or 32%, from $3,304,000 for the year ended December 31, 2003. This decrease is primarily attributable to the decrease in sales for the year, although we are experiencing a reduction in integration support costs. We anticipate there may be an increase in cost of sales for products in 2005 due to foreign exchange rate fluctuations of the U.S. dollar versus those currencies of our primary manufacturers. We anticipate this to be offset by a reduction in costs associated with manufacturing these products should as quantities rise, improving our gross margins.

Research and development expenses consist primarily of personnel, facilities, equipment and supplies for our research and development activities. Non-funded development costs are reported as research and development expense. Research and development expense increased in 2004 to $925,000 from $799,000 for the same period in 2003, an increase of $126,000, or 16%. During 2004, externally funded research and development from partners such as FAW,

Mack/Volvo, Hyundai, and the U.S. Government offset the costs of development for new products in the areas of mobile and stationary power management and conversion, thereby reducing the need for internal funding. Programs included our new parallel hybrid drive systems, our diesel generation engine/motor system for our heavy-duty drive systems, and upgrades and improvements to our current power conversion and management components. Additionally, we continued to enhance our technologies to be more universally adaptable to the requirements of our current and prospective customers. By modifying our software and firmware, we believe we should be able to provide a more comprehensive, adaptive and effective solution to a larger base of customers and applications. We will continue to research and develop new technologies and products, both internally and in conjunction with our alliance partners and other manufacturers as we deem beneficial to our global growth strategy.

Selling, general and administrative expenses consist primarily of personnel and related costs of sales and marketing employees, consulting fees and expenses for travel, trade shows and promotional activities and personnel and related costs for general corporate functions, including finance, accounting, strategic and business development, human resources and legal. Selling, general and administrative expenses increased 2004 from 2003 levels due to increased consulting, legal, and accounting costs and expenses related to the annual shareholders meeting and fund raising activities. For the year ended December 31, 2004, these expenses totaled $2,325,000 from $2,919,000 for the similar period in 2003. This represents a $594,000 decrease, or 20%, in these expenses. We are continually reviewing operations to lower overhead costs and increase operational efficiencies

For the year ended December 31, 2004, interest and financing fees increased by $21,000 to $255,000, an increase of 8%. The increase was due solely to an increase in 2004 in the interest rate on the note due the Credit Managers Association of California for $3.2 million per the terms of the note.

In 2004, we charged off approximately $275,000 in obsolete and slow moving inventory from our books. Approximately half of this consisted of raw materials associated with the Ford Th!nk city program which was terminated in 2003. We do not anticipate further write downs of our inventory.

Our $3,382,000 net loss for the year ended December 31, 2004 is $196,000 more than the loss incurred in 2003 of $3,186,000, an increase of 6%. The increase is due primarily to write-offs on obsolete and slow-moving inventory during the year and costs associated with the annual meeting and other regulatory compliance. Management will continue to seek operational efficiencies and methods to reduce manufacturing and overhead costs as well as increase revenues to enhance our achieve this goal of profitability.

Hyundai-Enova Innovative Technology Center

In September 2003, Enova and Hyundai Heavy Industries, Co. Ltd. (HHI) funded the Hyundai-Enova Innovative Technology Center (HEITC) to be located at Enova's Torrance headquarters. In connection with the Joint Venture Agreement entered into between the two parties in March 2003, HHI purchased $1,500,000 of common stock of Enova Systems, Inc. HHI purchased 23,076,923, shares representing a 6.2% ownership in Enova. Of this amount, Enova invested $1,000,000 in the HEITC for a forty percent (40%) ownership interest. HHI invested an additional $1,500,000 for a sixty percent (60%) ownership interest in the HEITC. In September 2004, HHI invested an additional $1,500,000 in Enova and $1,500,000 in the HEITC under the same terms as the initial investment. In this second tranche, HHI purchased 11,335,315 restricted shares of common stock in accordance with the Joint Venture Agreement increasing HHI's ownership to 8.0% in Enova. The joint venture company officially opened in November 2003 to pursue advanced research and development in hybrid automotive and stationary

applications for fuel cell technologies. Share amounts do not include the effect of the July 2005 1 for 45 reverse stock split executed by the Company.

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Contractual Obligations

As of December 31, 2005, our contractual obligations for the next five years, and thereafter, were as follows (in thousands):

	Payments Due by Period				
	Total	Less than 1 Year	1-3 Years	3-5 Years	More than 5 Years
Long-Term Debt Obligations	$2,363	$ 42	$ --	$ --	$2,321
Capital Lease Obligations	--	--	--	--	--
Operating Lease Obligations	362	166	196	--	--
Purchase Obligations	--	--	--	--	--
Accrued Interest	1,113	--	--	--	1,113
Total	$3,833	$ 208	$ 196	$ --	$3,434

Recent Accounting Pronouncements

In November 2004, the FASB issued SFAS No. 151,"Inventory Costs". SFAS No. 151 amends the accounting for abnormal amounts of idle facility expense, freight, handling costs, and wasted material (spoilage) under the guidance in ARB No. 43, Chapter 4, "Inventory Pricing". Paragraph 5 of ARB No. 43, Chapter 4, previously stated that ". . . under some circumstances, items such as idle facility expense, excessive spoilage, double freight, and rehandling costs may be so abnormal as to require treatment as current period charges. . . ." This statement requires that those items be recognized as current-period charges regardless of whether they meet the criterion of "so abnormal." In addition, this statement requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. This statement is effective for inventory costs incurred during fiscal years beginning after June 15, 2005. Management does not expect adoption of SFAS No. 151 to have a material impact, if any, on the Company's financial position or results of operations.

In December 2004, the FASB issued SFAS No. 153, "Exchanges of Nonmonetary Assets," an amendment to Opinion No. 29, "Accounting for Nonmonetary Transactions". SFAS No. 153 eliminates certain differences in the guidance in Opinion No. 29 as compared to the guidance contained in standards issued by the International Accounting Standards Board. The amendment to Opinion No. 29 eliminates the fair value exception for nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. Such an exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. SFAS No. 153 is effective for nonmonetary asset exchanges occurring in periods beginning after June 15, 2005. Earlier application is permitted for nonmonetary asset exchanges occurring in periods beginning after December 16, 2004. Management does not expect adoption

of SFAS No. 153 to have a material impact, if any, on the Company's financial position or results of operations.

In December 2004, the FASB issued SFAS No. 123(R),"Share-Based Payment". SFAS 123(R) amends SFAS No. 123, "Accounting for Stock-Based Compensation", and APB Opinion No. 25, "Accounting for Stock Issued to Employees". SFAS No.123(R) requires that the cost of share-based payment transactions (including those with employees and non-employees) be recognized in the financial statements. SFAS No. 123(R) applies to all share-based payment transactions in which an entity acquires goods or services by issuing (or offering to issue) its shares, share options, or other equity instruments (except for those held by an ESOP) or by incurring liabilities (1) in amounts based (even in part) on the price of the company's shares or other equity instruments, or (2) that require (or may require) settlement by the issuance of a company's shares or other equity instruments. In April 2005, the Securities and Exchange Commission (SEC) deferred the effective date of SFAS 123R for SEC registrants to the first fiscal year beginning after December 15, 2005. Accordingly, we expect to implement the revised standard in the first quarter of 2006. Currently, we account for stock-based employee awards issued after December 31, 2002, using the fair value method preferred by SFAS 123. We expect that the adoption of SFAS 123R will have a material effect on the financial statements.

In March 2005, the FASB issued FIN 47, "Accounting for Conditional Asset Retirement Obligations - an Interpretation of FASB Statement No. 143, Accounting for Asset Retirement Obligations." This interpretation addresses the timing of liability recognition for legal obligations associated with the retirement of a tangible long-lived asset when the timing and/or method of settlement of the obligation are conditional on a future event. The interpretation requires an entity to recognize a liability for the fair value of a conditional asset retirement obligation when incurred if the liability's fair value can be reasonably estimated. The adoption of this interpretation did not have any impact on our financial statements.

In May 2005, the FASB issued SFAS No. 154, "Accounting Changes and Error Corrections--a replacement of APB Opinion No. 20 and FASB Statement No. 3" (SFAS 154). This statement changes the requirements for the accounting for and reporting of a change in accounting principle and applies to all voluntary changes in accounting principle. It also applies to changes required by an

accounting pronouncement in the unusual instance that the pronouncement does not include specific transition provisions. APB No. 20 required that most voluntary changes in accounting principle be recognized by including in net income of the period of the change the cumulative effect of changing to the new accounting principle. This statement requires retrospective application to prior period financial statements of changes in accounting principle, unless it is impracticable to determine either the period-specific effects or the cumulative effect of the change. The provisions of SFAS 154 are effective for fiscal years beginning after December 15, 2005. As such we are required to adopt SFAS 154 starting January 1, 2006. We do not expect the adoption of this statement to have a material impact on our Financial Statements.

In February 2006, the FASB issued SFAS No. 155, Accounting for Certain Hybrid Financial Instruments--an amendment of FASB Statements No. 133 and 140 ("SFAS 155"). This statement amends SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities ("SFAS 133"), and SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities and resolves issues addressed in SFAS 133 Implementation Issue No. D1, Application of Statement 133 to Beneficial Interest in Securitized Financial Assets. The Company is required to apply SFAS 155 to all financial instruments

acquired, issued or subject to a remeasurement event beginning January 1, 2007, although early adoption is permitted as of the beginning of an entity's fiscal year. The provisions of SFAS 155 are not expected to have an impact recorded at adoption.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk

None.

Item 8. Financial Statements and Supplementary Data

All information required by this Item is included on pages F-1 to F-18 in Item 15 of Part IV of this annual report on form 10-K and is incorporated into this Item by reference. See Item 15.

Item 9A. Controls and Procedures

We conducted an evaluation of the effectiveness of the design and operation of our "disclosure controls and procedures" (Disclosure Controls) as of the end of the period covered by this Annual Report. The controls evaluation was done under the supervision and with the participation of management, including our Chief Executive Officer (CEO) and Acting Chief Financial Officer (CFO).

Attached as exhibits to this Annual Report are certifications of the CEO and CFO, which are required in accordance with Rule 13a-15(e) of the Exchange Act. This Controls and Procedures section includes the information concerning the controls evaluation referred to in the certifications and it should be read in conjunction with the certifications for a more complete understanding of the topics presented.

Definition of Disclosure Controls

Disclosure Controls are controls and procedures designed to reasonably assure that information required to be disclosed in our reports filed under the Exchange Act, such as this Annual Report, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. Disclosure Controls are also designed to reasonably assure that such information is accumulated and communicated to our management, including the CEO and CFO, as appropriate to allow timely decisions regarding required disclosure. Our Disclosure Controls include components of our internal control over financial reporting, which consists of control processes designed to provide reasonable assurance regarding the reliability of our financial reporting and the preparation of financial statements in accordance with US generally accepted accounting principles. To the extent that components of our internal control over financial reporting are included within our Disclosure Controls, they are included in the scope of our periodic controls evaluation.

Limitations on the Effectiveness of Controls

The Company's management, including the CEO and CFO, does not expect that our Disclosure Controls or our internal control over financial reporting will prevent all error and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide

absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of a simple error or mistake. Controls can also be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

Scope of the Controls Evaluation

The evaluation of our Disclosure Controls included a review of the controls' objectives and design, the Company's implementation of the controls and the effect of the controls on the information generated for use in this Annual Report. In the course of the controls evaluation, we sought to identify data errors, controls problems or acts of fraud and confirm that appropriate corrective action, including process improvements, were being undertaken. This type of evaluation is performed on a quarterly basis so that the conclusions of management, including the CEO and CFO, concerning controls effectiveness can be reported in our Quarterly Reports on Form 10-Q and in our Annual Report on Form 10-K. Many of the components of our Disclosure Controls are also evaluated on an ongoing basis by personnel in our Finance organization, as well as our independent auditors who evaluate them in connection with determining their auditing procedures related to their report on our annual financial statements and not to provide assurance on our controls. The overall goals of these various evaluation activities are to monitor our Disclosure Controls, and to modify them as necessary.

Among other matters, we also considered whether our evaluation identified any "significant deficiencies" or "material weaknesses" in our internal control over financial reporting, and whether the Company had identified any acts of fraud involving personnel with a significant role in our internal control over financial reporting. This information was important both for the controls evaluation generally, and because item 5 in the certifications of the CEO and CFO require that the CEO and CFO disclose that information to our Board's Audit Committee and to our independent auditors. In the professional auditing literature, "significant deficiencies" are referred to as "reportable conditions," which are deficiencies in the design or operation of controls that could adversely affect our ability to record, process, summarize and report financial data in the financial statements. Auditing literature defines "material weakness" as a particularly serious reportable condition where the internal control does not reduce to a relatively low level the risk that misstatements caused by error or fraud may occur in amounts that would be material in relation to the financial statements and the risk that such misstatements would not be detected within a timely period by employees in the normal course of performing their assigned functions.

Conclusions

A "material weakness" is a control deficiency, or combination of control deficiencies, that results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected.

As of December 31, 2005, we did not maintain effective controls over the inventory pricing, tracking, and the reserve analysis process. This control deficiency resulted in an audit adjustment to our 2005 financial statements and could result in a misstatement to cost of sales that would result in a material misstatement to the annual and interim financial statements that would not be prevented or detected.

Furthermore, Management has determined that, as of December 31, 2005, we did not have sufficient segregation of duties in relation to the accounting function. This deficiency could result in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected.

Accordingly, Management has determined that these deficiencies constitute a material weakness. Because of these material weaknesses, Management has concluded that we did not maintain effective internal control over financial reporting as of December 31, 2005. In 2006, the Company plans to hire a Chief Financial Officer who will oversee the implementation of controls and procedures designed to remediate the Company's internal control deficiencies.

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PART III

Item 10. Directors and Executive Officers of the Registrant

The following table sets forth certain information with respect to the current Directors and executive officers of Enova:

Name	Age	Position
Anthony N. Rawlinson	49	Chairman of the Board
Edwin O. Riddell	62	Chief Executive Officer, President and Director
Bjorn Ahlstrom (1) (2)	70	Director
Dr. Malcolm Currie (1)	77	Director
Donald H. Dreyer (2)	68	Director
John Wallace (2) (3)	56	Director

(1) Member of the Compensation Committee.
(2) Member of the Audit Committee.
(3) Financial Expert on Audit Committee.

Anthony Rawlinson, Chairman of the Board. Mr. Rawlinson was appointed Chairman of the Board in July 1999. He is Managing Director of The Global Value Investment Portfolio Management Pte. Ltd., a Singapore-based international fund management company, managing discretionary equity portfolios for institutions, pension funds and clients globally since 1996. Mr. Rawlinson is also Chairman of Cardsoft Inc., a privately-held company based in San Mateo California since

2001. Cardsoft develops and markets embedded Java software solutions that provide security and interoperability for applications running on disparate fixed and wireless payment devices.

Edwin O. Riddell, President, CEO and Director. Mr. Riddell was appointed President and Chief Executive Officer on August 20, 2004. Mr. Riddell has been a Director of the Company since 1995. Since 1999, Mr. Riddell has been President of CR Transportation Services, a consultant to the electric vehicle industry. From 1992 to 1999, Mr. Riddell was Product Line Manager of the Transportation Business Unit at the Electric Power Research Institute, and from 1985 until 1992, he served with the Transportation Group, Inc. as Vice President, Engineering, working on electric public transportation systems. From 1979 to 1985, he was Vice President, General Manager and COO of Lift-U, Inc., the leading manufacturer of handicapped wheelchair lifts for the transit industry. Mr. Riddell has also worked with Ford, Chrysler, and General Motors in the area of auto design, and has worked as a member of senior management for a number of public transit vehicle manufacturers. Mr. Riddell has been a member of the American Public Transportation Association's (APTA) Member Board of Governors for over 15 years, and has served on APTA's Board of Directors. Mr. Riddell was also Managing Partner of the U.S. Advanced Battery Consortium.

Bjorn Ahlstrom, Director. Mr. Ahlstrom was elected to the Board of Directors in June 2004. Mr. Ahlstrom currently is a consultant in the heavy-duty vehicle industry. Mr. Ahlstrom retired as Chairman of Volvo Group North America, Inc. on April 1, 2004. Prior to that, Mr. Ahlstrom was President and Chief Executive Officer of Volvo North America Corporation from 1971 until 1994. During this term, Volvo North America Corporation owned and operated Volvo's businesses in the United States and Canada. Under Mr. Ahlstrom's leadership, VNAC grew from a $50 million car importer in the early 1970s to a $6 billion company with manufacturing and marketing operations for cars, trucks, marine engines, and financial services. In 1981, Mr. Ahlstrom received the Royal Order of the North Star from King Carl XVI Gustaf of Sweden. The United States Government awarded him the Medal of Peace and Commerce in 1983. He received the Ellis Island Medal of Honor in 1990. Mr. Ahlstrom has been awarded honorary Doctor of Law degree from St John's University, NY, and Ramapo College of New Jersey.

Malcolm R. Currie, Ph.D, Director. Dr. Currie was re-elected to the Board of Directors in 1999. Dr. Currie had served as a Director of the Company from 1995 through 1997. From 1986 until 1992, Dr. Currie served as Chairman and Chief Executive Officer of Hughes Aircraft Co., and from 1985 until 1988, he was the Chief Executive Officer of Delco Electronics. His career in electronics and management has included research with many patents and papers in microwave and millimeter wave electronics, laser, space systems, and related fields. He has led major programs in radar, commercial satellites, communication systems, and defense electronics. He served as Undersecretary of Defense for Research and Engineering, the Defense Science Board, and currently serves on the Boards of Directors of LSI Logic, Inamed Corp., Innovative Micro Technology, Regal One, and Currie Technologies. He is past president of the American Institute of Aeronautics and Astronautics, and is a Member of the Board of Trustees of the University of Southern California.

John R. Wallace, Director. Mr. Wallace was elected as a Director of the Company in 2002. Since November of 2005, he has held the position of CEO, Xantrex Technology, Inc. in Burnaby, B.C., Canada. From 2002 to 2005, he worked independently as a consultant in the alternative energy sector. Mr. Wallace retired from the Ford Motor Company in 2002. Prior to his retirement, he was executive director of TH!NK Group. He has been active in Ford Motor Company's alternative fuel vehicle programs since 1990, serving first as: Director,

Technology Development Programs; then as Director, Electric Vehicle Programs; Director, Alternative Fuel Vehicles and finally Director, Environmental Vehicles. He is past Chairman of the Board of Directors of TH!NK Nordic; he is past chairman of the United States Advanced Battery Consortium; Co-Chairman of the Electric Vehicle Association of the Americas, and past Chairman of the California Fuel Cell Partnership. He served as Director of Ford's Electronic Systems Research Laboratory, Research Staff, from 1988 through 1990. Prior to joining Ford Research Staff, he was president of Ford Microelectronics, Inc., in Colorado Springs. His other experience includes work as program manager with Intel Corporation. He also served as Director, Western Development Center, for Perkin-Elmer Corporation and as President of Precision Microdesign, Inc.

Donald H. Dreyer, Director. Mr. Dreyer was elected a Director of the Company in January 1997. Mr. Dreyer is President and CEO of Dreyer & Company, Inc., a consultancy in credit, accounts receivable and insolvency services, which he founded in 1990. Mr. Dreyer has served as Chairman of the Board of Credit Managers Association of California during the 1994 to 1995 term and remains a current member. Mr. Dreyer is also a member of the American Bankruptcy Institute and the National Advisory Committee of Dun & Bradstreet, Inc.

Relationships Among Directors or Executive Officers

There are no family relationships among any of the Directors or executive officers of Enova.

Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Securities Exchange Act requires our Directors, executive officers and persons who own more than 10% of our Common Stock (collectively, "Reporting Persons") to file reports of ownership and changes in ownership of our Common Stock to the Securities and Exchange Commission ("SEC"). Copies of these reports are also required to be delivered to Enova.

We believe, based solely on our review of the copies of such reports received or written representations from certain Reporting Persons, that each of Messrs. Rawlinson, Riddell, Currie, Micek, Wallace and Dreyer, each of whom is a Director of Enova, failed to file on a timely basis one Form 4, each of which Form 4 reported one transaction, namely the issuance of shares of Common Stock in partial payment of directors' fees for August 2004.

Code of Ethics

Enova has adopted a code of ethics that applies to its principal executive officer, principal financial officer, principal accounting officer or controller and all persons performing similar functions, if any. We will provide to any person without charge, upon request, a copy of such code of ethics. Requests should be made in writing to:

Enova Systems, Inc.
Edwin O. Riddell, Chief Executive Officer and Acting Chief Financial Officer
19850 S. Magellan Drive
Torrance, CA 90502

Item 11. Executive Compensation

Summary Compensation Table

The following table sets forth all compensation earned by our Chief Executive Officer and each of the other most highly compensated executive officers of Enova whose annual salary and bonus exceeded $100,000 for the years ended December 31, 2005, 2004 and 2003 (collectively, the "Named Executive

Officers"). Mr. Carl D. Perry was the sole executive officer of Enova whose salary currently exceeded $100,000 prior to December 31, 2003.

Name and Principal Position

SUMMARY COMPENSATION TABLE
ANNUAL COMPENSATION

Name and Principal Position	Year	Salary	Bonus
Edwin O. Riddell (1)	2005	$204,000	$43,500 (10,000 000 Commo
Chief Executive Officer and President	2004	--	--
	2003	--	--
Larry B. Lombard (2)	2005	$148,812	$21,750 (5,000 Common sha
Chief Financial Officer	2004	$126,825	--
	2003	--	
Edward M. Moore (3)	2005	$154,943	$ 21,750 (5,000 Common sh
Chief Operating Officer	2004	$146,635	(earned in 200
	2003	--	
Carl D. Perry (4)	2005	$ 78,232	--
Former Chief Executive Officer and	2004	$120,000	--
President	2003	$139,615	$30,000 (earned in 2000)

(1) Mr. Riddell was elected Chief Executive Officer and president in August 2004. Mr. Riddell commenced employment as a full-time employee in January 2005 at a salary of $208,000 per year. For the period from August 2004 to December 2004, Mr. Riddell was compensated for services on a contractual basis at the rate of $4,000 per week.

(2) Mr. Lombard was elected Chief Financial Officer in March 2004. Mr. Lombard's annual salary was $145,000 per year. On December 9, 2005 Mr. Lombard resigned from the Company. Prior to 2004, Mr. Lombard was not an officer of the Company.

(3) Mr. Moore was elected Chief Operating Officer in March 2004. Mr. Moore's annual salary was $150,000 per year. On December 9, 2005 Mr. Moore resigned from the Company. Prior to 2004, Mr. Moore was not an officer of the Company.

(4) Mr. Perry was elected Chief Executive Officer and president in November 1997 and resigned those positions in August 2004. Mr. Perry's salary was $120,000 per year which terminated per agreement at December 31, 2004. Compensation earned in 2005 consisted of $2,308 of regular earnings and $75,924 of severance. Mr. Perry served as Acting Chief Financial Officer during the periods reflected in the above chart through March 6, 2004.

Option/SAR Grants

The following grants of stock options or stock appreciation rights ("SARs") were made during 2005 to the Named Executive Officers.

Option Grants During Fiscal 2005

Name of Individual and Position	Number of Securities Underlying Options Granted	Percentage of Total Options Granted to Employee in Fiscal 2005	Exercise Price Per Share	Expiration Date
Edwin Riddell, Chief Executive Officer	60,000	19%	4.35	9-12-15
Larry B. Lombard, Chief Financial Officer	46,000	15%	4.35	9-12-15
Edward M. Moore, Chief Operating Officer	46,000	15%	4.35	9-12-15

(1) Calculated on the basis of $4.35 representing the average of the high bid and low ask prices of the Common Stock on December 31, 2005

Option Exercises and Option Values

The following table sets forth information concerning option exercises during 2005, and the aggregate value of unexercised options as of December 31, 2005, held by each of the Named Executive Officers:

	Aggregated Option/SAR Exercises in 2005 and Option Values at December 31, 2005				
	Aggregate Option Exercises in 2005		Number of Securities Underlying Unexercised Options at December 31, 2005 (#)		Val In-th Decemb
Name	Shares Acquired on Exercise (#)	Value Realized ($)	Exercisable	Unexercisable	Exercis
Edwin O. Riddell	--	--	--	--	--(
Larry B. Lombard	--	--	--	--	--(
Edward M. Moore	--	--	--	--	--(

(1) Calculated on the basis of $0.00 representing the average of the high bid and low ask prices of the Common Stock on December 31, 2005 of $3.65 per share, minus the exercise price.

Compensation of Directors

During 2005, we issued, or accrued for issuance, an aggregate of 81,000

shares of common stock to the non-executive board directors in accordance with the September 1999 Board of Directors compensation package for outside directors, as amended to date. Prior to September, 2005, for each meeting attended in person, each outside director received $2,000 in cash and $4,000 of stock valued on the date of the meeting at the average of the closing ask and bid prices; for each telephonic Board meeting, each outside director received $500 in cash and $500 of stock valued on the date of the meeting at the average of the closing ask and bid prices; and for each meeting of a Board committee attended in person, a committee member received $1,000 in cash and $1,000 of stock valued on the date of the meeting at the average of the closing ask and bid prices. In September, 2005, the compensation structure for Directors was changed. Effective in the fourth quarter of 2005, Directors receive quarterly compensation at a flat rate of $4,000 in cash and $6,000 in stock valued on the date of the meeting at the average of the closing ask and bid prices. The flat rate is not dependent on the amount or type of services performed by the Directors. All Directors are also reimbursed for out-of-pocket expenses incurred in connection with attending Board and committee meetings.

We relied on Rule 506 of Regulation D and Section 4(2) of the Securities Act of 1933, as amended, for the exemption from registration of the sale of such shares.

Edwin O. Riddell

In 2004, the Company entered into a consulting agreement with Edwin Riddell doing business as CR Transportation Services wherein the Company compensated CR Transportation at the rate of $4,000 per week plus reasonable expenses for consulting services rendered. Upon Mr. Riddell becoming an employee of Enova in January 2005, this agreement was terminated. Mr. Riddell was not compensated per this agreement when acting in the capacity of a director of the Company. During 2004, the Company paid Mr. Riddell $99,000 in cash for consulting services and expenses and $15,000 for directors fees (which latter amount includes the cash paid and the value of the stock issued to him pursuant to the outside directors' compensation package described above).

Donald Dreyer

In 2004, the Company utilized the consulting service of Donald Dreyer wherein the Company compensated Mr. Dreyer at the rate of $150 per hour plus reasonable expenses for consulting services rendered. Mr. Dreyer is not compensated when acting in the capacity of a director of the Company other than the fees noted above. During 2004, the Company paid Mr. Dreyer $2,000 in cash for consulting services and expenses and $29,000 for directors fees (which latter amount includes the cash paid and the value of the stock issued to him pursuant to the outside directors' compensation package described above).

Audit Committee

The Audit Committee held three meetings in the year ended December 31, 2005. As of February 2006 the Audit Committee consists of Mr. Bjorn Ahlstrom, Mr. John Wallace, and Mr. Don Dreyer. Mr. Wallace is the committee's designated financial expert and Mr. Dreyer serves as the committee's chairman.

Compensation Committee Interlocks and Insider Participation

The Compensation Committee held two meetings in the year ended December 31, 2005. The Compensation Committee currently consists of Mr. Bjorn Ahlstrom and Dr. Malcolm Currie, neither of who have been officers of the Company. Prior to August 2004, Mr. Edwin Riddell was a member of the Compensation Committee. Mr.

Riddell resigned from the committee upon his appointment as Chief Executive Officer. The Compensation Committee's functions are to establish and apply the Company's compensation policies with respect to the Company's Executive Officers, and to administer the Company's stock option plans.

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The following table sets forth certain information known to the Company with respect to beneficial ownership of the Company's Common Stock as of December 31, 2005, by (i) each shareholder known to the Company to own beneficially more than 5% of the Company's Common Stock; (ii) each of the Company's Directors; (iii) the Named Executive Officer; and (iv) all Executive Officers and Directors as a group. Except as indicated in the footnotes to this table and subject to applicable community property laws, the persons named in the table, based on information provided by such persons, have sole voting and investment power with respect to all shares of Common Stock shown as beneficially owned by them.

Name	Shares Beneficially Owned (1)	Percentage of Shares Beneficially Owned (
Jagen, Pty., Ltd. 9 Oxford Street, South Ybarra 3141 Melbourne, Victoria Australia	3,222,222	21.16%
Hyundai Heavy Industries, Co. 1 Cheona-Dong, Dong-Ku Ulsan, Korea	764,716	5.02%
Citibank N.A. 111 Wall Street, 8th Floor New York, NY 10043	619,676	4.07%
Anthony N. Rawlinson c/o Enova Systems, Inc. 19850 South Magellan Drive Torrance, CA 90502	572,665	3.76%
Edwin O. Riddell c/o Enova Systems, Inc. 19850 South Magellan Drive Torrance, CA 90502	108,047(4)	*
Carl D. Perry	208,476	1.37%
John J. Micek III	17,872(5)	*
Bjorn Ahlstrom	7,873	*
Dr. Malcolm Currie	20,555	*
Donald H. Dreyer	19,242	*
John R. Wallace	6,144	*
Delphi Delco Electronics	28,406(6)	*

Jean Schulz	77,062(7)	*
Larry B. Lombard	113,221(8)	*
Edward M. Moore	79,333(9)	*
All directors and executive officers as a group (10 persons)	1,153,429(10)	7.57%

* Indicates less than 1%

(1) Number of Common Stock shares includes Series A Preferred Stock, Series B Preferred Stock and Common Stock shares issuable pursuant to stock options, warrants and other securities convertible into Common Stock beneficially held by the person or class in question which may be exercised or converted within 60 days after December, 31 2005.

(2) The percentages are based on the number of shares of Common Stock, Series A Preferred Stock and Series B Preferred Stock owned by the shareholder divided by the sum of: (i) the total Common Stock outstanding, (ii) the Series A Preferred Stock owned by such shareholder; (iii) the Series B Preferred Stock owned by such shareholder; and (iv) Common Stock issuable pursuant to warrants, options and other convertible securities exercisable or convertible by such shareholder within sixty (60) days after December 31, 2005.

(3) The percentages are based on the number of shares of Common Stock, Series A Preferred Stock and/or Series B Preferred Stock owned by the shareholder divided by the sum of: (i) the total Common Stock outstanding, (ii) the total Series A Preferred Stock outstanding and (iii) the total Series B Preferred Stock outstanding. This percentage calculation has been included to show more accurately the actual voting power of each of the shareholders, since the calculation takes into account the fact that the outstanding Series A Preferred Stock and Series B Preferred Stock are entitled to vote together with the Common Stock as a single class on certain matters to be voted upon by the shareholders.

(4) Includes 82,222 (post reverse split) shares of Common Stock issuable pursuant to stock options exercisable at a price of $4.35 to $5.18

(5) Includes 22,222 (post reverse split) shares of Common Stock issued to Silicon Prairie Partners, LP, a limited partnership in which John J. Micek III is the general partner.

(6) The number of shares shown represents the ownership of 639,360 shares of Series B Preferred Stock, each of which is convertible into two shares of Common Stock. These 639,360 shares represent more than 5% of the outstanding shares of Series B Preferred Stock.

(7) The number of shares shown represents the ownership of 1,329,111 shares of Series A Preferred Stock, each of which is convertible into one share of Common Stock. These 1,329,111 shares represent more than 5% of the outstanding shares of Series A Preferred Stock.

(8) Includes 90,000 (post reverse split) shares of Common Stock issuable pursuant to stock options exercisable at a price from $4.35 to $5.18.

(9) Includes 90,000 (post reverse split) shares of Common Stock issuable pursuant to stock options exercisable at prices from $4.35 to $5.18.

(10) Includes 111,111 (post reverse split) shares of Common Stock issuable pursuant to stock options exercisable at prices from $5.18 to $9 per share and 22,222 (post reverse split) shares of Common Stock issued to Silicon Prairie Partners, LP, a limited partnership in which John J. Micek III is the general partner.

Equity Compensation Plan Information

The following table provides information regarding our equity compensation plans as of December 31, 2005:

Equity Compensation Plan Information

Plan category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of utstanding options, warrants and rights (b)
Equity compensation plans approved by security holders	436,000	$4.46
Equity compensation plans not approved by security holders	--	--
Total	436,000	$4.46

Our board of directors adopted the 1996 Employee and Consultant Stock Option Plan in October 1996 which was subsequently approved by our shareholders in May 1997. A total of 15,000,000 shares were reserved for issuance under the 1996 Plan. Options granted under the 1996 Plan may be either incentive stock options, as defined in Section 422 of the Internal Revenue Code of 1986, or nonstatutory stock options. The 1996 Plan provides that options may be granted to employees (including officers and directors who are also employees),

directors and consultants. Incentive stock options may only be granted to employees. In 1999, our board of directors and shareholders approved an amendment to the 1996 Plan to increase the number of shares of common stock reserved for issuance thereunder by 30,000,000 shares and in 2004, our board of directors and shareholders approved an amendment to the 1996 Plan to increase the number of shares of common stock reserved for issuance thereunder by 20,000,000 shares, bringing the total number of shares issuable under the 1996 Plan to 65,000,000. The share increases to the 1996 Plan assured that a sufficient reserve of common stock are available to provide us with the continuing opportunity to utilize equity incentives to attract and retain the services of employees essential to our long-term growth and financial success. A copy of the actual 1996 Plan document was previously filed with the Securities and Exchange Commission.

Options granted under the amended 1996 Plan will vest over such periods as may be determined by the board of directors and will generally have an exercise price equal to the closing price for our stock on the NASDAQ OTC Bulletin Board on the last trading day immediately prior to the date of grant. Options to purchase 2,55,000 shares of Enova common stock were granted to employees in 2005.

Item 13. Certain Relationships and Related Transactions

The following are certain transactions entered into between Enova and its officers, directors and principal shareholders and their affiliates since January 1, 2004.

During 2004, Hyundai Heavy Industries, Co. (HHI) purchased 11,076,923 (before the effects of the reverse stock split) shares increasing their ownership in Enova Systems, Inc. to 7.98%. Additionally, during 2005, we purchased from HHI approximately $2,516,000 in components, materials and services for manufacture of our drive systems and power management systems. These purchases were made on terms and conditions equal to or better than our standard commercial terms with other vendors. At the year ended December 31, 2005, our outstanding payables balance due HHI was approximately $1,317,000.

Item 14. Principal Accountant Fees and Services

Singer Lewak Greenbaum & Goldstein LLP were engaged on November 22, 2005 to audit our financial statements for the fiscal year ended December 31, 2005, having previously been engaged to audit our financial statements for the years ended December 31, 2004 and 2003.

Audit Fees

The aggregate fees billed during the last two fiscal years for professional services rendered by Singer Lewak Greenbaum & Goldstein LLP for the audit of Enova's financial statements for the fiscal year ended December 31, 2005 and for its review of financial statements included in Enova's Forms 10Q during the last two fiscal years and other services that are normally provided by an accountant in connection with statutory and regulatory filings or engagements during such fiscal years were $143,000 for fiscal 2005 and $73,970 for fiscal 2004.

Audit-Related Fees

Singer Lewak Greenbaum & Goldstein LLP did not perform for Enova any assurance and related services that were reasonably related to the performance of the audit of our financial statements for the fiscal year ended December 31, 2005.

Tax Fees

Singer Lewak Greenbaum & Goldstein LLP did not perform for Enova any tax compliance, tax advice and tax planning services in fiscal 2004 or fiscal 2005.

All Other Fees

Neither Singer Lewak Greenbaum & Goldstein LLP nor Moss Adams, LLP performed any other services for fees other than audit fees in fiscal 2005 or 2004.

The Audit Committee's policy is to pre-approve the annual engagement of the

independent auditors to render services to the company. These services may include audit services, audit-related services, tax services, and other services.

PART IV

Item 15. Exhibits, Financial Statement Schedules, and Reports on Form 8-K

(a)1. Financial Statements

The financial statements filed as a part of this report are identified in the Index to Financial Statements on page F-1.

(a)2. Financial Statement Schedule

No financial statement schedules are filed as a part of this report.

(a)3. Exhibits

See Item 15 (c) for Index of Exhibits.

(b) Reports on Form 8-K

On February 2, 2005, Registrant filed a Form 8-K, with date of earliest event reported of September 20, 2004, reporting under items 1 and 3.

(c) Exhibits

Exhibit Number	Description
3.1	Amended and Restated Articles of Incorporation of the Registrant (filed as Exhibit 3.1 to the Registrant's Annual Report on Form 10K for the year ended December 31, 2000 filed on March 30, 2001 and incorporated herein by reference).
3.2	Bylaws of Registrant (filed as Exhibit 3.12 to the Registration Statement on Form 10 filed on November 29, 1994, and incorporated herein by reference).
4.1	Cashless Exercise Warrants dated October 25, 1996 issued to Fontal International, Ltd. (filed as Exhibit 4.1 to the Registrant's Annual Report on Form 10-K for the year ended July 31, 1996, as filed on November 12, 1996, and incorporated herein by reference).
10.1	Form of Stock Option Agreement under 1993 Employee and Consultant Stock Plan (filed as Exhibit 10.15 to the Registration Statement on Form 10 filed on November 29, 1994, and incorporated herein by reference).
10.2	Form of Solar Electric Engineering, Inc. 1993 Employee and Consultant Stock Plan (filed as Exhibit 10.16 to the Registration Statement on Form 10 filed on November 29, 1994, and incorporated herein by reference).
10.3	Form of Confidential Private Placement Memorandum and Debt Restructuring Disclosure Statement of U.S. Electricar, Inc., dated January 2, 1996, delivered by Enova to certain of its unsecured trade creditors, including exhibits (filed as Exhibit 10.91 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended January 31, 1996, as filed on March 18, 1996, and incorporated herein

by reference).

10.4 Form of Stock Purchase, Note and Debt Exchange Agreement dated January 2, 1996 between Enova and certain unsecured trade creditors (filed as Exhibit 10.92 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended January 31, 1996, as filed on March 18, 1996, and incorporated herein by reference).

10.5 Form of Indemnification Agreement (filed as Exhibit 10.63 to the Registration Statement on Form 10 filed on November 29, 1994, and incorporated herein by reference).

10.6 Form of Security Agreement made as of May 31, 1995, between Enova and Credit Managers Association of California, Trustee (filed as Exhibit 10.85 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended April 30, 1996, as filed on June 14, 1996, and incorporated herein by reference).

10.7 Amended 1996 Employee and Consultant Stock Option Plan (filed as Exhibit 10.7 to the Registrant's Annual Report on Form 10-K for fiscal year ended July 31, 1999, as filed on October 29, 1999, and incorporated herein by reference).

10.8 Stock Purchase Agreement and Technology License Agreement dated February 27, 1997, by and between Enova and Hyundai Motor Company and Hyundai Electronics Industries Co., Ltd. (filed as Exhibit 10.98 to the Registrant's Quarterly Report on Form 10-Q for fiscal quarter ended January 31, 1997, as filed on March 14, 1997, and incorporated herein by reference).

10.9 Letter of Intent between Registrant and a domestic supplier, dated December 9, 1999, to design, develop and manufacture low voltage electric drive system components (filed as Exhibit 10.16 to the Registrant's Annual Report on Form 10-K for fiscal year ended December 31, 2000 and incorporated herein by reference).

10.10 Put/Call Option to sell Itochu shares between Registrant and Carl D. Perry dated September 1, 1999 (filed as Exhibit 10.16 to the Registrant's Annual Report on Form 10-K for fiscal year ended December 31, 2000 and incorporated herein by reference).

10.11 Agreement (redacted) between the Registrant and a customer dated June 14, 2001, to develop and produce power management systems. (filed as Exhibit 10.1 to the Registrant's Quarterly Report on Form 10-Q for Six Months ended June 30, 2001 and incorporated herein by reference).

10.12 Agreement (redacted) between the Registrant and Eco Power Technology, dated June 12, 2001, to produce and sell power drive systems (filed as Exhibit 10.19 to Amendment No. 6 to the Registrant's Registration Statement on Form S-1, No. 333-85308, and incorporated herein by reference).

10.13 Agreement (redacted) between the Registrant and Tomoe Electro-Mechanical Engineering and Manufacturing, Inc., dated November 19, 2001, to produce and sell power drive systems (filed as Exhibit 10.20 to Amendment No. 6 to the Registrants Registration Statement on Form S-1, No. 333-85308, and incorporated herein by reference).

10.14 Agreement (redacted) between the Registrant and Moriah Corporation,

dated January 22, 2002, to produce and sell power drive systems (filed as Exhibit 10.21 to Amendment No. 6 to the Registrant's Registration Statement on Form S-1, No. 333-85308, and incorporated herein by reference).

10.15 Form of Stock Purchase Agreement dated June 7, 2002 between Registrant and each of the selling shareholders listed in a Prospectus dated July 26, 2002 (filed as Exhibit 10.22 to Amendment No. 1 to the Registrant's Registration Statement on Form S-1, No. 333-96829, and incorporated herein by reference).

10.16 Form of Registration Rights Agreement dated June 7, 2002 between Registrant and each of the selling shareholders listed in a Prospectus dated July 26, 2002 (filed as Exhibit 10.23 to Amendment No. 1 to the Registrant's Registration Statement on Form S-1, No. 333-96829, and incorporated herein by reference).

10.17 Joint Venture Agreement (redacted**) to form advanced research and development corporation, dated as of March 18, 2003, by and between the Registrant and Hyundai Heavy Industries Co. Ltd. (filed as Exhibit 10.24 to the Registrant's Quarterly Report on Form 10-Q for Three Months ended March 31, 2003 and incorporated herein by reference).

10.18 Securities Purchase Agreement dated as of March 18, 2003, by and between the Registrant and Hyundai Heavy Industries Co. Ltd. (filed as Exhibit 10.25 to the Registrant's Quarterly Report on Form 10-Q for Three Months ended March 31, 2003 and incorporated herein by reference).

10.19 Form of Stock Purchase Agreement dated March 30, 2004 between Registrant and various investors. (filed as Exhibit 10.19 to the Registrant's Quarterly Report on Form 10-Q for Three Months ended March 31, 2004 and incorporated herein by reference).

10.20 Form of Registration Rights Agreement dated March 30, 2004 between Registrant and various investors. (filed as Exhibit 10.20 to the Registrant's Quarterly Report on Form 10-Q for Three Months ended March 31, 2004 and incorporated herein by reference).

10.21 Form of Finder's Fee agreement dated April 1, 2004 between Registrant and The Global Value Investment Portfolio Management Pte Ltd as disclosed in our Form 10-Q for the quarter ended March 31, 2004. (filed as Exhibit 10.21 to the Registrant's Quarterly Report on Form 10-Q for Six Months ended June 30, 2004 and incorporated herein by reference).

23.1 Consent of Independent Registered Public Accounting Firm

24* Power of Attorney (included on signature page)

37

31.1* Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act Of 2002

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

32* Certification Pursuant to 18 U.S.C. Section 1350

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* Filed herewith.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

ENOVA SYSTEMS, INC.

By: /s/ Edwin O. Riddell

Edwin O. Riddell, Chief Executive Officer, President and Acting Chief Financial Officer

Dated: March 31, 2006

POWER OF ATTORNEY

KNOW ALL MEN BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Edwin O. Riddell, with full power to act alone, his true and lawful attorney-in-fact and agent, with full power of substitution for him and in his name, place and stead, in any and all capacities, to sign any and all amendments to the annual report on Form 10-K, and to file the same, with all exhibits thereto, and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorney-in-fact full power and authority to do and perform each and every act and thing requisite and necessary to be done in connection as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorney-in-fact and agent may lawfully do or cause to be done by virtue hereof.

IN WITNESS WHEREOF, each of the undersigned has executed this Power of Attorney as of the date indicated. Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed by the following persons on behalf of the registrant and in the capacities and on the date indicated.

Signature	Title	
/s/ Edwin O. Riddell --- Edwin O. Riddell	Acting Chief Financial Officer (Principal Financial Officer)	March
/s/ Edwin O. Riddell --- Edwin O. Riddell	Chief Executive Officer and Director (Principal Executive Officer)	March
/s/ Anthony N. Rawlinson --- Anthony N. Rawlinson	Chairman	March
/s/ Malcolm Currie	Director	March

Malcolm Currie		
/s/ Bjorn Ahlstrom	Director	March
Bjorn Ahlstrom		
/s/ Donald H. Dreyer	Director	March
Donald H. Dreyer		
/s/ John R. Wallace	Director	March
John R. Wallace		

ENOVA SYSTEMS, INC.
FINANCIAL STATEMENTS
FOR THE YEARS ENDED
DECEMBER 31, 2005, 2004, AND 2003

ENOVA SYSTEMS, INC.
CONTENTS
December 31, 2005

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders
Enova Systems, Inc.

Torrance, California

We have audited the balance sheets of Enova Systems, Inc. as of December 31, 2005 and 2004, and the related statements of operations, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2005. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provided a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Enova Systems, Inc. as of December 31, 2005 and 2004, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2005, in conformity with U.S. generally accepted accounting principles.

SINGER LEWAK GREENBAUM & GOLDSTEIN LLP

Los Angeles, California
March 9, 2006

ENOVA SYSTEMS, INC.
BALANCE SHEETS
December 31, 2005 and 2004

ASSETS

	2005	2004
Current assets		
Cash and cash equivalents	$16,187,000	$ 1,575,000
Accounts receivable, net	2,173,000	522,000
Inventories and supplies, net	1,016,000	1,036,000
Prepaid expenses and other current assets	182,000	304,000
Total current assets	19,558,000	3,437,000
Property and equipment, net	576,000	387,000
Equity method investment	1,649,000	1,768,000
Other assets	190,000	296,000
Total assets	$21,973,000	$ 5,888,000

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

ENOVA SYSTEMS, INC.
BALANCE SHEETS
December 31, 2005 and 2004

LIABILITIES AND STOCKHOLDERS' EQUITY

	2005	2004
Current liabilities		
Accounts payable	$1,396,000	$ 66,000
Deferred revenues	--	392,000
Line of credit	--	229,000
Accrued payroll and related expense	195,000	194,000
Other accrued expenses	302,000	13,000
Current portion of notes payable	42,000	166,000
Current portion of capital lease obligations	--	6,000
Total current liabilities	1,935,000	1,066,000
Accrued interest payable	1,113,000	1,378,000
Notes payable, net of current portion	2,321,000	3,341,000
Total liabilities	$5,369,000	$5,785,000

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

ENOVA SYSTEMS, INC.
BALANCE SHEETS
December 31, 2005 and 2004

LIABILITIES AND STOCKHOLDERS' EQUITY (continued)

	2005	2004
Stockholders' equity		
Series A convertible preferred stock - no par value		
30,000,000 shares authorized		
2,674,000 and 2,748,000 shares issued and outstanding		
Liquidating preference at $0.60 per share, aggregating		

$1,604,000 and $1,649,000	$ 1,679,000	$ 1,774,000
Series B convertible preferred stock - no par value		
5,000,000 shares authorized		
1,217,000 and 1,217,000 shares issued and outstanding		
Liquidating preference at $2 per share	2,434,000	2,434,000
Common Stock, no par value		
750,000,000 shares authorized		
14,783,000 and 9,228,000 shares issued and		
outstanding	109,323,000	90,465,000
Common stock subscribed	30,000	165,000
Stock notes receivable	(1,176,000)	(1,176,000)
Additional paid-in capital	6,900,000	6,900,000
Accumulated deficit	(102,586,000)	(100,459,000)
Total stockholders' equity	16,604,000	103,000
Total liabilities and stockholders' equity	$ 21,973,000	$ 5,888,000

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

ENOVA SYS
STATEMENTS OF O
For the Years Ended December 31, 2005, 2004,

	2005	2004	
Net revenues			
Research and development contracts	$ 1,555,000	$ 1,070,000	$
Production	4,529,000	1,484,000	
Total net revenues	6,084,000	2,554,000	
Cost of revenues			
Research and development contracts	1,188,000	499,000	
Production	4,813,000	1,627,000	
Writedown Ford Think program inventory	--	113,000	
Total cost of revenues	6,001,000	2,239,000	
Gross profit	83,000	315,000	
Operating expenses			
Research and development	804,000	925,000	
Asset impairment	--	--	
Selling, general & administrative	2,870,000	2,325,000	
Total operating expenses	3,674,000	3,250,000	
Other income and (expense)			
Interest and financing fees, net	13,000	(255,000)	

Equity in losses of equity method investee	(118,000)	(192,000)	
Debt extinguishment	1,011,000	--	
Interest extinguishment	558,000	--	
Total other income and (expense)	1,464,000	(447,000)	
Loss from operations	(2,127,000)	(3,382,000)	(
Net loss	$ (2,127,000)	$ (3,382,000)	$ (
Basic loss and diluted loss per share	$ (0.18)	$ (0.38)	$
Weighted-average number of shares outstanding	11,664,320	8,831,893	

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

STATEMEN
For th

	Convertible Preferred Stock				
	Series A		Series B		
	Shares	Amount	Shares	Amount	Sh
Balance, December 31, 2002	2,824,000	$ 1,842,000	1,217,000	$ 2,434,000	7,6
Conversion of Series A preferred stock	(4,000)	(5,000)			
Issuance of common stock for Cash					5
Issuance of subscribed common stock					
Exercise of options					1
Stock option Services					
Net loss					
Balance, December 31, 2003	2,820,000	$1,837,000	1,217,000	$2,434,000	8,4
Conversion of Series A preferred stock	(73,000)	(63,000)			
Issuance of common stock for Cash					6
Issuance of subscribed common stock					
Exercise of options					1
Stock option conversions					
Services					
Net loss					

Balance, December 31, 2004	2,747,000	$1,774,000	1,217,000	$2,434,000	9,2
Conversion of Series A preferred stock	(73,000)	(95,000)			
Issuance of common stock for					
Cash					5,4
Issuance of common stock for director services					
Director bonus					
Subscribed Common Stock					
Net loss					
Balance, December 31, 2005	2,674,000	$1,679,000	1,217,000	$2,434,000	14,7

	Common Stock Subscribed		Stock Notes	Additional Paid-In	Ac
	Shares	Amount	Receivable	Capital	
Balance, December 31, 2002	30,000	$ 130,000	$ (1,203,000)	$6,949,000	$ (
Conversion of Series A preferred stock					
Issuance of common stock for					
Cash					
Issuance of subscribed common stock	(22,000)	(100,000)			
Exercise of options					
Stock option				82,000	
Services	17,000	30,000			
Net loss					
Balance, December 31, 2003	25,000	$ 60,000	$ (1,203,000)	$7,031,000	$ (
Conversion of Series A preferred stock					
Issuance of common stock for					
Cash			27,000		
Issuance of subscribed common stock	(25,000)	(60,000)			
Exercise of options					
Stock option conversions				(39,000)	
Services	27,000	165,000		(92,000)	
Net loss					
Balance, December 31, 2004	27,000	$ 165,000	$(1,176,000)	$6,900,000	$(1
Conversion of Series A preferred stock					
Issuance of common stock for					
Cash					
Issuance of common stock for director services	(27,000)	(165,000)			
Director bonus					
Subscribed Common Stock	8,000	30,000			
Net loss					

Balance, December 31, 2005	8,000	$ 30,000	$(1,176,000)	$6,900,000	$(1

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

ENOVA SYSTEMS, INC.
STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2005, 2004, and 2003

	2005	2004	2003
Cash flows from operating activites			
Net loss	$(2,127,000)	$(3,382,000)	$(3,186,000)
Adjustments to reconcile net loss to net cash used by operating activities			
Debt extinguishment	(1,011,000)	--	--
Interest extinguishment	(558,000)	--	--
Depreciation and amortization	304,000	376,000	351,000
Provision for asset impairment	--	--	200,000
Equity in losses of equity method investee	118,000	192,000	40,000
Issuance of common stock for services	158,000	89,000	34,000
Issuance of common stock for bonuses	109,000	--	--
(Increase) decrease in			
Accounts receivable	(1,651,000)	281,000	457,000
Inventory and supplies	20,000	570,000	48,000
Note receivable - related party	--	8,000	24,000
Prepaid expenses and other current assets	122,000	(226,000)	29,000
Other assets	(2,000)	--	(14,000)
Increase (decrease) in			
Accounts payable	1,330,000	(702,000)	(424,000)
Accrued expenses	290,000	(11,000)	(112,000)
Deferred revenues	(392,000)	392,000	--
Accrued interest payable	293,000	256,000	234,000
Net cash used by operating activities	(2,997,000)	(2,157,000)	(2,319,000)
Cash flows from investing activites			
Purchases of property and equipment	$ (384,000)	$ (174,000)	$ (113,000)
Net cash used in investing activities	(384,000)	(174,000)	(113,000)
Cash flows from financing activites			
Net increase from line of credit	$ --	$ 109,000	$ 106,000
Payment on notes payable and capital lease obligations	(368,000)	(33,000)	(1,000)
Proceeds from notes payable	--	40,000	--
Net Proceeds from sales of common stock	18,361,000	2,450,000	600,000
Proceeds from exercise of stock options	--	783,000	389,000
Payments on stock notes receivable	--	27,000	--
Net cash provided by financing activities	17,993,000	3,376,000	1,094,000

Net increase (decrease) in cash and cash equivalents	14,612,000	1,045,000	(1,338,000)
Cash and cash equivalents, beginning of year	1,575,000	530,000	1,868,000
Cash and cash equivalents, end of year	$16,187,000	$1,575,000	$ 530,000

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

	2005	2004	2003
Interest paid	$ 2,000	$ 10,000	$ 9,000
Income taxes paid	$ --	$ --	$ --
Conversion of preferred stock to common stock	$ 94,000	$ 63,000	$ (5,000)
Acquired investment under common stock purchase	$ --	$ 1,000,000	$ 1,000,000
Offering costs on common stock purchases	$ --	$ 93,000	$ --
Common Stock issued for purchase of options	$ --	$ 39,000	$ --

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

ENOVA SYSTEMS, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2005

NOTE 1 - Organization and Line of Business

General

Enova Systems, Inc. (the "Company") is a California corporation that develops drive trains and related components for electric, hybrid electric, and fuel cell systems for mobile and stationary applications. The Company retains development and manufacturing rights to many of the technologies created, whether such research and development is internally or externally funded. The Company develops and sells components in the United States and Asia, and sells components in Europe.

Liquidity

At December 31, 2005, the Company had a net working capital of

approximately $17,623,000 as compared to $2,371,000 at December 31, 2004, representing an increase of $15,252,000. This increase is due primarily to capital raised in the third quarter of 2005, as described in Note 10.

Stock Purchase Agreement

The Company has entered into a joint venture agreement (the Agreement) with Hyundai Heavy Industries of Korea ("HHI") to create a joint venture corporation, Hyundai-Enova Innovative Technology Center (the "ITC") to be domiciled in Torrance, California. In conjunction with this Agreement, HHI and the Company entered into a stock purchase agreement in which HHI agreed to make a $3 million investment in the Company through the purchase of shares of the Company's authorized and unissued common stock pursuant to Regulation D of the Securities Act of 1933. This investment was made in two installments of $1.5 million each. The first installment was made in June 2003 upon incorporation of the ITC and in consideration for the issuance to HHI by the Company of 23,076,923 shares of common stock at $0.065 per share. Share amounts are reported before the effects of the reverse stock split, as described in Note 10.

The second installment was made in September 2004 in consideration for the issuance to HHI by the Company of 11,335,315 shares of common stock at $0.1323 per share. Share amounts are reported before the effects of the reverse stock split, as described in Note 10.

The Company invested $1 million of each installment into the ITC in consideration for the issuance to the Company of a 40% equity interest in the ITC (the balance of the installments, in the amount of $500,000 each, is to be retained by the Company). HHI acquired a 60% equity interest in ITC by investing $3 million in the ITC in two installments of $1.5 million each, to be made concurrently with the two installment payments to be paid by HHI for the Company's common stock. HHI and the Company have invested an aggregate of $5 million in the ITC.

NOTE 2- Summary of Significant Accounting Policies

Contract Services Revenue and Cost Recognition

The Company manufactures proprietary products and other products based on design specifications provided by its customers. Revenue from sales of products are generally recognized at the time title to the goods and the benefits and risks of ownership passes to the customer which is typically when products are shipped based on the terms of the customer purchase agreement.

Revenue relating to long-term fixed price contracts is recognized using the percentage of completion method. Under the percentage of completion method, contract revenues and related costs are recognized based on the percentage that costs incurred to date bear to total estimated costs.

Changes in job performance, estimated profitability and final contract settlements may result in revisions to cost and revenue, and are recognized in the period in which the revisions are determined.

Contract costs include all direct materials, subcontract and labor costs and other indirect costs. General and administrative costs are charged to expense as incurred. At the time a loss on a contract becomes known, the entire amount of the estimated loss is accrued. The aggregate of costs incurred and estimated earnings recognized on uncompleted contracts in excess of related billings is shown as a current asset, and billings on uncompleted contracts in excess of costs incurred and estimated earnings is shown as a current liability.

Comprehensive Income

The Company utilizes Statement of Financial Accounting Standards ("SFAS") No. 130, "Reporting Comprehensive Income." This statement establishes standards for reporting comprehensive income and its components in a financial statement. Comprehensive income as defined includes all changes in equity (net assets) during a period from non-owner sources. Examples of items to be included in comprehensive income, which are excluded from net income, include foreign currency translation adjustments, minimum pension liability adjustments, and unrealized gains and losses on available-for-sale securities. Comprehensive income is not presented in the Company's financial statements since the Company did not have any changes in equity from non-owner sources.

Cash and Cash Equivalents

Highly liquid investments with an original maturity of three months or less are considered cash equivalents.

Accounts Receivable

Receivables are reported at net realizable value and are considered past due when payments have not been received for 90 days. In general, receivables are charged off as uncollectible upon exhausting all avenues of collection. Receivables older than 90 days totaled $209,000.

NOTE 2- Summary of Significant Accounting Polices (Continued)

Allowance for Doubtful Accounts

The Company maintains allowances for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. A considerable amount of judgment is required in assessing the ultimate realization of accounts receivable including the current credit-worthiness of each customer. If the financial condition of the Company's customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required. As of December 31, 2005, the Company maintained a reserve for $266,000 of potentially doubtful accounts receivable. Bad debt expense totaled $267,000, $98,000, and $596,000 for the years ended December 31, 2005, 2004, and 2003 respectively.

Inventories and Supplies

Inventories and supplies are comprised of materials used in the design and

development of electric, hybrid electric, and fuel cell drive systems, and other power and ongoing management and control components for production and ongoing development contracts, and is stated at the lower of cost (first-in, first-out) or market. In 2005, the Company charged off $376,000 for obsolete or slow moving inventory.

Property and Equipment

Property and equipment are stated at cost and depreciated using the straight-line method over the estimated useful lives of the related assets, which range from three to seven years. Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate the sum of expected cash flows from use of the asset is less than its carrying value. Long-lived assets that management commits to sell or abandon are reported at the lower of carrying amount or fair value less cost to sell.

Equity Method Investment

Investment in joint venture (see Note 1) is accounted for by the equity method.

Fair Value of Financial Instruments

The carrying amount of financial instruments, including cash and cash equivalents, accounts receivable, accounts payable and accrued expenses, approximate fair value due to the short maturity of these instruments. The carrying value of all other financial instruments is representative of their fair values. The Company's short and long term debt may be substantially less than the carrying value since there is no readily ascertainable market for the debt given the financial position of the Company.

Stock-Based Compensation

SFAS No. 123, "Accounting for Stock-Based Compensation," establishes and encourages the use of the fair value based method of accounting for stock-based compensation arrangements under which compensation cost is determined using the fair value of stock-based compensation determined as of the date of grant and is recognized over the periods in which the

NOTE 2- Summary of Significant Accounting Polices (Continued)

Stock Based Compensation (Continued)

related services are rendered. The statement also permits companies to elect to continue using the current implicit value accounting method specified in Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees," to account for stock-based compensation.

SFAS No. 148 "Accounting for Stock-Based Compensation--Transition and Disclosure" amends SFAS No. 123 to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, this

Statement amends the disclosure requirements of Statement 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results.

The Company has elected to use the intrinsic value based method and has disclosed the pro forma effect of using the fair value based method to account for its stock-based compensation. The Company has adopted only the disclosure provisions of SFAS No. 123. It applies APB Opinion No. 25 and related interpretations in accounting for its plans and does not recognize compensation expense for its stock-based compensation plans other than for restricted stock and options issued to outside third parties.

For purposes of adjusted pro forma disclosures, the estimated fair value of the options is amortized to expense over the vesting period.

If the Company had elected to recognize compensation expense based upon the fair value at the grant date for awards under this plan consistent with the methodology prescribed by SFAS No. 123, the Company's net loss and loss per share would be reduced to the pro forma amounts indicated below for the years ended December 31, 2005, 2004, and 2003. Per share amounts have been restated to illustrate the effects of the reverse stock split, as described in Note 10.

	2005	2004	2003
Loss applicable to common stockholders	$(2,127,000)	$(3,382,000)	$(3,186,000)
Compensation under APB Opinion 25	--	--	--
Stock-based employee compensation expense determined under fair value presentation for all options	(222,000)	(94,000)	(315,000)
Pro forma net loss	$(2,349,000)	$(3,476,000)	$(3,501,000)
Basic and diluted loss per common share			
As reported	$ (0.18)	$ (0.38)	$ (0.43)
Pro forma	$ (0.20)	$ (0.39)	$ (0.47)

NOTE 2- Summary of Significant Accounting Polices (Continued)

Stock Based Compensation (Continued)

For purposes of computing the pro forma disclosures required by SFAS No. 123, the fair value of each option granted to employees and directors is estimated using the Black-Scholes option-pricing model with the following weighted-average assumptions for the years ended December 31, 2005, 2004, and 2003: dividend yields of 0%, 0%, and 0%, respectively; expected volatility of 67%, 73%, and 88%, respectively; risk-free interest rates of

4%, 4%, and 4%, respectively; and expected lives of two, one, and three years, respectively. The weighted-average fair value of options granted during the year ended December 31, 2005 for which the exercise price equals the market price on the grant date was $.87, and the weighted-average exercise price was $4.35.

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options, which do not have vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions, including the expected stock price volatility. Because the Company's employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

Advertising Expense

The Company expenses all advertising costs, including direct response advertising, as they are incurred. Advertising expense for the years ended December 31, 2005, 2004, and 2003 was $9,000, $12,000, and $21,000, respectively.

Research and Development

Costs of researching and developing new technology or significantly altering existing technology is expensed as incurred.

Income Taxes

The Company utilizes SFAS No. 109, "Accounting for Income Taxes," which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements or tax returns. Under this method, deferred income taxes are recognized for the tax consequences in future years of differences between the tax bases of assets and liabilities and their financial reporting amounts at each year-end based on enacted tax laws and statutory tax rates applicable to the periods in which the differences are expected to affect taxable income. Valuation allowances are established, when necessary, to reduce deferred tax assets to the amount expected to be realized.

NOTE 2- Summary of Significant Accounting Policies (Continued)

Loss Per Share

The Company utilizes SFAS No. 128, "Earnings per Share." Basic loss per share is computed by dividing loss available to common stockholders by the weighted-average number of common shares outstanding. Diluted loss per share is computed similar to basic loss per share except that the denominator is increased to include the number of additional common shares that would have been outstanding if the potential common shares had been

issued and if the additional common shares were dilutive. Common equivalent shares are excluded from the computation if their effect is anti-dilutive. The Company's common share equivalents consist of stock options.

Estimates

The preparation of financial statements 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. Actual results could differ from those estimates.

Concentration of Credit Risk

Financial instruments which potentially subject the Company to concentrations of credit risk consist of cash and cash equivalents and accounts receivable. The Company places its cash and cash equivalents with high credit, quality financial institutions. At times, such cash and cash equivalents may be in excess of the Federal Deposit Insurance Corporation insurance limit of $100,000. The Company has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk on cash and cash equivalents. With respect to accounts receivable, the Company routinely assesses the financial strength of its customers and, as a consequence, believes that the receivable credit risk exposure is limited.

Major Customers

During the year ended December 31, 2005, the Company conducted business with five customers whose sales comprised 49%, 13%, 8%, 7% and 4% of total revenues. As of December 31, 2005, three customers accounted for 77%, 13%, and 8% of total accounts receivable.

In addition, one of the Company's stockholders accounted for 13%, 10%, and 1% of total revenues during the years ended December 31, 2005, 2004, and 2003, respectively. This stockholder holds less than 5% of the total issued and outstanding common stock as of December 31, 2005. Demand deposits are placed with known, creditable financial institutions.

NOTE 2- Summary of Significant Accounting Policies (Continued)

Recently Issued Pronouncements

In November 2004, the FASB issued SFAS No. 151,"Inventory Costs". SFAS No. 151 amends the accounting for abnormal amounts of idle facility expense, freight, handling costs, and wasted material (spoilage) under the guidance in ARB No. 43, Chapter 4, "Inventory Pricing". Paragraph 5 of ARB No. 43, Chapter 4, previously stated that ". . . under some circumstances, items such as idle facility expense, excessive spoilage,

Recently Issued Pronouncements (Continued)

double freight, and rehandling costs may be so abnormal as to require

treatment as current period charges. . . ." This statement requires that those items be recognized as current-period charges regardless of whether they meet the criterion of "so abnormal." In addition, this statement requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. This statement is effective for inventory costs incurred during fiscal years beginning after June 15, 2005. Management does not expect adoption of SFAS No. 151 to have a material impact, if any, on the Company's financial position or results of operations.

In December 2004, the FASB issued SFAS No. 153, "Exchanges of Nonmonetary Assets," an amendment to Opinion No. 29, "Accounting for Nonmonetary Transactions". SFAS No. 153 eliminates certain differences in the guidance in Opinion No. 29 as compared to the guidance contained in standards issued by the International Accounting Standards Board. The amendment to Opinion No. 29 eliminates the fair value exception for nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. Such an exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. SFAS No. 153 is effective for nonmonetary asset exchanges occurring in periods beginning after June 15, 2005. Earlier application is permitted for nonmonetary asset exchanges occurring in periods beginning after December 16, 2004. Management does not expect adoption of SFAS No. 153 to have a material impact, if any, on the Company's financial position or results of operations.

In December 2004, the FASB issued SFAS No. 123(R),"Share-Based Payment". SFAS 123(R) amends SFAS No. 123, "Accounting for Stock-Based Compensation", and APB Opinion No. 25, "Accounting for Stock Issued to Employees". SFAS No.123(R) requires that the cost of share-based payment transactions (including those with employees and non-employees) be recognized in the financial statements. SFAS No. 123(R) applies to all share-based payment transactions in which an entity acquires goods or services by issuing (or offering to issue) its shares, share options, or other equity instruments (except for those held by an ESOP) or by incurring liabilities (1) in amounts based (even in part) on the price of the company's shares or other equity instruments, or (2) that require (or may require) settlement by the issuance of a company's shares or other equity instruments. In April 2005, the Securities and Exchange Commission (SEC) deferred the effective date of SFAS 123R for SEC registrants to the first fiscal year beginning after December 15, 2005. Accordingly, we expect to implement the revised standard in the first quarter of 2006. Such implementation is prospective and is expected to have a material effect on the financial statements.

NOTE 2- Summary of Significant Accounting Policies (Continued)

In March 2005, the FASB issued FIN 47, "Accounting for Conditional Asset Retirement Obligations - an Interpretation of FASB Statement No. 143, Accounting for Asset Retirement Obligations." This interpretation addresses the timing of liability recognition for legal obligations associated with the retirement of a tangible long-lived asset when the timing and/or method of settlement of the obligation are conditional on a future event.

Recently Issued Pronouncements (Continued)

The interpretation requires an entity to recognize a liability for the fair value of a conditional asset retirement obligation when incurred if the liability's fair value can be reasonably estimated. The adoption of this interpretation did not have any impact on our financial statements.

In May 2005, the FASB issued SFAS No. 154, "Accounting Changes and Error Corrections--a replacement of APB Opinion No. 20 and FASB Statement No. 3" (SFAS 154). This statement changes the requirements for the accounting for and reporting of a change in accounting principle and applies to all voluntary changes in accounting principle. It also applies to changes required by an accounting pronouncement in the unusual instance that the pronouncement does not include specific transition provisions. APB No. 20 required that most voluntary changes in accounting principle be recognized by including in net income of the period of the change the cumulative effect of changing to the new accounting principle. This statement requires retrospective application to prior period financial statements of changes in accounting principle, unless it is impracticable to determine either the period-specific effects or the cumulative effect of the change. The provisions of SFAS 154 are effective for fiscal years beginning after December 15, 2005. As such we are required to adopt SFAS 154 starting January 1, 2006. We do not expect the adoption of this statement to have a material impact on our financial statements.

In February 2006, the FASB issued SFAS No. 155, "Accounting for Certain Hybrid Financial Instruments--an amendment of FASB Statements No. 133 and 140" ("SFAS 155"). This statement amends SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS 133"), and SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities" and resolves issues addressed in SFAS 133 Implementation Issue No. D1, "Application of Statement 133 to Beneficial Interest in Securitized Financial Assets". The Company is required to apply SFAS 155 to all financial instruments acquired, issued or subject to a remeasurement event beginning January 1, 2007, although early adoption is permitted as of the beginning of an entity's fiscal year. The provisions of SFAS 155 are not expected to have an impact on the financial statements at adoption.

NOTE 3- Property and Equipment

Property and equipment at December 31, 2005 and 2004 consisted of the following:

	2005	2004
Computers	$ 296,000	$ 229,000
Machinery and equipment	975,000	709,000
Furniture and office equipment	242,000	192,000
Demonstration vehicles and buses	324,000	461,000
Equipment under capital lease obligations	94,000	94,000
Leasehold improvements	70,000	68,000
	2,001,000	1,753,000

Less accumulated depreciation and amortization	1,425,000	1,366,000
Total	$ 576,000	$ 387,000

Depreciation and amortization expense was $304,000, $376,000, and $351,000 for the years ended December 31, 2005, 2004, and 2003, respectively.

NOTE 4 - Equity Method Investment

During the year ended December 31, 2004, the Company invested $1,000,000 of the proceeds received from a sale of common stock to HHI into a joint venture formed with HHI in 2003 (see Note 1). The Company's share of income and losses is 40% as stated in the agreement. During the year ended December 31, 2005, the Company recorded $118,000 as its proportionate share of losses in the joint venture.

The following is the condensed financial position and results of operations of ITC, as of and for the year ended December 31, 2005:

Financial position	
Current assets	$4,105,000
Property and equipment, net	22,000
Liabilities	(5,000)
Equity	$4,122,000
Operations	
Net revenues	$ 126,000
Expenses	$ 423,000
Net loss	$ (297,000)
Company's proportionate share of net loss	$ (118,000)

NOTE 5- Other Assets

During the year ended December 31, 2002, the Company incurred legal costs of $112,000 associated with two patents. These patents have been capitalized and are being amortized over their estimated useful lives.

In June 2001, a strategic relationship with Ford Motor Company was entered into to develop and manufacture a high power, high voltage conversion module for Ford's fuel cell vehicle. Warrants were issued to Ford Motor Company in exchange for Ford's commitment to enter into a five-year agreement. The issuance of the warrants was recorded as a non-current asset (Value Participation Agreement) at its fair market value of $577,000, which was determined using the Black-Scholes option pricing model, and is being amortized on a straight-line basis over the life of the contract.

The following table illustrates the types and carrying values of the Company's other assets:

	2005	2004
Patents	$ 93,000	$ 92,000
Valuation Participation Agreement	577,000	577,000
	670,000	669,000
Less accumulated amortization	481,000	373,000
Total	$ 190,000	$ 296,000

NOTE 6- Line of Credit

The Company had available $250,000 revolving line of credit from a bank with interest payable monthly at 3.25%. The line of credit was secured by a $250,000 Certificate of Deposit. During 2005 the line of credit was paid in full, including all related interest obligations.

NOTE 7- Deferred Revenues - Tomoe LTA Long-Term Contract

The Company has entered into a development and production contract with Tomoe Electro-Mechanical Engineering and Manufacturing, Inc. for eight battery-electric locomotives for the Singapore Land Transport Authority for service vehicles for the Singapore Mass Rapid Transit Circle Line system for maintenance, repair, shunting and recovery of passenger trains. The contract commenced in August 2004 and completion of the contract will take approximately 15-18 months and was valued at approximately $3,022,000. The Company is recording revenues for this long-term, fixed price contract on the basis of the percentage-of-completion method. The contract contains several deliverables over its life and therefore the Company will divide these deliverables into separate units of accounting based on relative fair values. Revenue recognition criteria will be assessed separately for each separate unit of accounting. Revenues recorded for this contract were $2,928,000 and $68,000 as of December 31, 2005 and 2004, respectively. There is no deferred revenue relating to this contract as of December 31, 2005.

NOTE 8- Notes Payable

In December 2005, the Company was informed by the Credit Managers Association of California that $1,011,000 of principal and $447,000 accrued interest under the secured note payable had been disclaimed and extinguished by the beneficiaries of such principal amount. The Company has recognized a gain on the extinguishment of the principal and associated accrued interest of $1,458,000 in relation to this extinguishment. The Company evaluated this transaction under the guidance set forth in SFAS 140

"Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities" and noted that the extinguishment of these liabilities was consistent with the guidance.

In October 2005, the Company agreed to a settlement on an unsecured 10% note payable. In exchange for immediate payment of the full principal balance of $120,000, the beneficiary of the note agreed to forgive the entire accrued interest balance of $111,000. The Company has recognized a

NOTE 8- Notes Payable (Continued)

gain on the extinguishment of the associated accrued interest. The Company evaluated this transaction under the guidance set forth in SFAS 140 "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities" and noted that the extinguishment of these liabilities was consistent with the guidance.

Notes payable at December 31, consisted of the following:

	2005	2004
Secured note payable to Credit Managers Association of California, bearing interest at prime plus 3% in 2005 and through maturity. Principal and unpaid interest due in April 2016. A sinking fund escrow is required to be funded with 10% of future equity financing, as defined in the agreement.	$2,321,000	$3,332,000
Unsecured note payable, bearing interest at 10% per annum.	--	120,000
Secured note payable to a Coca Cola Enterprises in the original amount of $40,000, bearing interest at 5% per annum. Principal and unpaid interest due now.	40,000	40,000
Secured note payable to a financial institution in the original amount of $33,000, bearing interest at 8% per annum, payable in 36 equal monthly installments.	2,000	15,000
	2,363,000	3,507,000
Less current portion	42,000	166,000
Long-term portion	$2,321,000	$3,341,000

Future minimum principal payments of notes payable at December 31, 2005 consisted of the following:

Year Ending December 31,	
2006	$ 42,000
2007	--
2008	--
2009	--
2010	--
Thereafter	2,321,000
Total	$2,363,000

NOTE 9- Commitments and Contingencies

Leases

The Company leases its facilities under an operating lease agreement, which requires monthly payments of $13,700 and expires in February 2008. In addition, the Company rents manufacturing and office equipment under various capital lease agreements.

Future minimum lease payments under these non-cancelable operating and capital lease obligations at December 31, 2005 were as follows:

Year Ending December 31,	Operating Leases
2006	$166,000
2007	168,000
2008	