PRINCIPAL SOLAR, INC.
CONSOLIDATED BALANCE SHEETS
(Unaudited)

	September 30, 2014	December 31, 2013
ASSETS		
Current Assets		
Cash and equivalents	$ 429,080	$ 122,533
Accounts receivable	172,892	105,989
Deposits	500,000	10,000
Prepaid assets	12,617	23,867
Option to acquire noncontrolling interest in subsidiary	-	46,010
Total current assets	1,114,588	308,399
Other Assets		
Solar arrays at cost, net	6,735,590	6,984,936
Restricted cash	179,875	140,644
Total other assets	6,915,465	7,125,580
Total assets	$ 8,030,054	$ 7,433,979
LIABILITIES AND STOCKHOLDERS' DEFICIT		
Current Liabilities		
Liabilities arising from reverse merger	$ 991,371	$ 953,967
Compensation payable	596,044	559,998
Accounts payable	381,990	59,968
Current portion of acquisition note payable, net of discount	229,454	215,574
Interest payable	54,280	26,753
Note payable for insurance premiums	-	9,040
Convertible notes payable, related parties	500,000	-
Accrued expenses and other liabilities	13,378	3,378
Total current liabilities	2,766,517	1,828,678
Other Liabilities		
Acquisition note payable, net of discount	4,480,889	4,652,979
Derivative liability on warrants	1,121,989	1,123,149
Total other liabilities	5,602,878	5,776,128
Total liabilities	8,369,395	7,604,806
Commitments and contingencies		
Stockholders' Deficit		
Preferred stock: $0.01 par value, 100,000,000 shares authorized; none issued	-	-
Common stock: $0.01 par value, 300,000,000 shares authorized, 20,373,327 and 19,017,227 shares issued and outstanding at September 30, 2014 and December 31, 2013, respectively	203,732	190,171
Additional paid-in capital	8,394,738	5,954,387
Stock subscriptions receivable	-	-
Accumulated deficit	(9,759,546)	(7,102,188)
Deficit attributable to common stockholders	(1,161,076)	(957,630)
Noncontrolling interest in subsidiary	821,735	786,803
Total stockholders' deficit	(339,341)	(170,827)
Total liabilities and stockholders' deficit	$ 8,030,054	$ 7,433,979

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

PRINCIPAL SOLAR, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	**2013**	**2014**	**2013**
Revenues				
Power generation	$ 283,582	$ 232,842	$ 784,188	$ 332,627
Other	-	167	-	2,984
Total revenues	283,582	233,008	784,188	335,611
Cost of revenues				
Depreciation	93,972	72,258	249,345	105,689
Direct operating costs	65,285	25,593	192,034	45,414
Total cost of revenues	159,257	97,851	441,379	151,103
Gross profit	124,324	135,158	342,809	184,508
General and administrative expenses	1,597,837	481,382	2,597,365	1,708,916
Operating loss	(1,473,512)	(346,224)	(2,254,557)	(1,524,408)
Other expense				
Interest expense	147,129	118,667	368,729	174,609
Inducement for conversion of notes payable	-	-	-	102,193
(Gain) loss on derivative liability on warrants	-	67,158	(1,160)	67,158
Total other expense	147,129	185,825	367,569	343,960
Loss before provision for income taxes	(1,620,641)	(532,048)	(2,622,126)	(1,868,368)
Provision for state income taxes	-	300	300	1,227
Net loss	(1,620,641)	(532,347)	(2,622,426)	(1,869,595)
Less: Income attributable to noncontrolling interest in subsidiary	14,509	8,852	34,932	8,852
Net loss attributable to common stockholders	$ (1,635,152)	$ (541,200)	$ (2,657,358)	$ (1,878,447)
Net loss per share - basic and diluted	$ (0.08)	$ (0.03)	$ (0.14)	$ (0.11)
Weighted average shares outstanding - basic and diluted	19,965,719	15,691,761	19,523,960	16,452,951

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

PRINCIPAL SOLAR, INC.
CONSOLIDATED STATEMENT OF STOCKHOLDERS' DEFICIT
(Unaudited)

	Common Stock		Additional Paid-in	Accumulated	Stock Subscriptions	Principal Solar, Inc.	Non-Controlling	
	Shares	Amount	Capital	Deficit	Receivable	Total	Interest	Total
December 31, 2013	**19,017,227**	**$ 190,171**	**$ 5,954,387**	**$ (7,102,188)**	**$ -**	**$ (957,630)**	**$ 786,803**	**$ (170,827)**
Common stock issued for cash	1,356,100	13,561	1,342,539	-	-	1,356,100	-	1,356,100
Stock-based employee compensation expense	-	-	1,073,990	-	-	1,073,990	-	1,073,990
Stock-based advisor compensation expense	-	-	23,822	-	-	23,822	-	23,822
Net income (loss)	-	-	-	(2,657,358)	-	(2,657,358)	34,932	(2,622,426)
September 30, 2014	**20,373,327**	**$ 203,732**	**$ 8,394,738**	**$ (9,759,546)**	**$ -**	**$ (1,161,076)**	**$ 821,735**	**$ (339,341)**

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

PRINCIPAL SOLAR, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Nine Months Ended September 30, 2014	2013
OPERATING ACTIVITIES		
Net loss	$ (2,622,426)	$ (1,869,595)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	249,346	188,192
Stock-based employee compensation expense	1,073,989	171,970
Stock-based advisor compensation expense	23,822	106,930
Inducement cost for conversion of notes payable	-	102,193
Interest expense, paid in stock	-	7,816
(Gain) loss on derivative liability on warrants	(1,160)	67,158
Amortization of discount on acquisition note payable	15,272	8,355
Option to acquire noncontrolling interest	46,010	-
Change in operating assets and liabilities:		
Accounts receivable	(66,903)	18,441
Deposits	(490,000)	47,000
Prepaid assets	11,250	-
Liabilities arising from reverse merger	37,404	41,560
Compensation payable	36,046	260,676
Accounts payable	322,022	(32,726)
Interest payable	27,527	-
Accrued expenses and other liabilities	10,000	-
Net cash used in operating activities	(1,327,801)	(882,030)
INVESTING ACTIVITIES		
Powerhouse One acquisition, net of cash acquired	-	(6,077,215)
FINANCING ACTIVITIES		
Proceeds from acquisition note payable	-	5,050,000
Payments on acquisition note payable	(173,482)	-
Proceeds from sale of common stock and warrants	1,356,101	2,300,000
Proceeds from convertible notes payable, related party	500,000	121,000
Payments on note payable for insurance premiums	(9,040)	-
Change in restricted cash	(39,231)	(297,196)
Net cash provided by financing activities	1,634,348	7,173,804
Increase in cash and equivalents	306,547	214,559
Cash and equivalents, beginning of period	122,533	11,418
Cash and equivalents, end of period	$ 429,080	$ 225,977
Supplemental Disclosures		
Interest paid	$ 288,527	$ 45,386
Income taxes paid	$ -	$ -
Non-Cash Transactions:		
Discount on acquisition note payable	$ -	107,064
Option to acquire noncontrolling interest in subsidiary	-	46,010
Derivative liability on investor warrants	-	1,600,000
Redemption of convertible notes payable and accrued interest for stock	-	145,990
Issuance for stock subscription receivable	-	200,000

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

PRINCIPAL SOLAR, INC.
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

1 - OVERVIEW

Basis of Presentation

The unaudited consolidated financial statements and related notes have been prepared pursuant to Article 8-03 of the rules and regulations of the Securities and Exchange Commission (the "SEC"). Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been omitted. In the opinion of management, the accompanying unaudited consolidated financial statements contain all adjustments and information (consisting only of normal recurring accruals) considered necessary for a fair presentation.

The year-end balance sheet was derived from the Company's audited financial statements. The accompanying unaudited consolidated financial statements and related notes should be read in conjunction with the Company's audited financial statements included in its Registration Statement on Form S-1/A dated October 20, 2014, as amended. The results of operations for the periods reflected herein are not necessarily indicative of the results to be expected for the full year.

Going Concern

The accompanying consolidated financial statements have been prepared assuming the Company will continue as a going concern. As of September 30, 2014, the Company has an accumulated deficit of approximately $9.8 million, and the Company has had negative cash flows from operations since inception. Its ability to continue as a going concern is dependent upon the ability of the Company to obtain the necessary financing, likely through the continued sale of its equity and equity-linked securities, to meet its obligations and pay its liabilities arising from normal business operations when they come due. The outcome of these matters cannot be predicted with any certainty at this time and raise substantial doubt that the Company will be able to continue as a going concern. These consolidated financial statements do not include any adjustments to the amounts and classification of assets and liabilities that may be necessary should the Company be unable to continue as a going concern.

Concentration

Since June 2013, 96% of our consolidated power generation revenue arose from our Powerhouse One solar installation under an index-priced Power Purchase Agreement ("PPA") having a fixed premium of $0.12 per kilowatt-hour ("kWh") over the GSA-1 scheduled rate (currently approximately $0.10 per kWh) through 2021, and a market rate based upon the then current GSA-1 scheduled rate for the remaining 10 years of the initial 20 year term ending in 2031. The buyer and counterparty of the PPA is Fayetteville Public Utility of Lincoln County Tennessee. A similar percentage of the accounts receivable also stems from this single relationship.

2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Recent Accounting Pronouncements

In May 2014, the FASB issued Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers (ASU 2014-09), which supersedes nearly all existing revenue recognition guidance under U.S. GAAP. The core principle of ASU 2014-09 is to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration to which an entity expects to be entitled for those goods or services. ASU 2014-09 defines a five step process to achieve this core principle and, in doing so, more judgment and estimates may be required within the revenue recognition process than are required under existing U.S. GAAP. We expect the new guidance will have no impact on the Company's current revenue recognition policy.

Principles of Consolidation

The Company consolidates the financial position, results of operations, and cash flows of all majority-owned subsidiaries. The consolidated financial statements include the accounts of the Company (including the dba Principal Solar Institute) and its subsidiaries SunGen Mill 77, LLC; SunGen StepGuys, LLC; and Powerhouse One, LLC. Significant intercompany accounts and transactions have been eliminated in consolidation. Certain previously reported amounts have been reclassified to conform to the current presentation.

Fair Value

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants on the measurement date. We believe the carrying values of cash and equivalents, accounts receivable, and other current assets, accounts payable, accrued expenses, and other current liabilities approximate their fair values. We believe the carrying value of our notes payable approximate their estimated fair value for debts with similar terms, interest rates, and remaining maturities currently available to companies with similar credit ratings.

We do not engage in hedging activities, but we do have a derivative instrument treated as a liability whose value is measured on a recurring basis (see "Fair Value Instruments" and "Derivative Liability on Warrants" included herein).

Fair Value Instruments

In June 2013, in connection with a sale of its par value $.01 common stock ("Common Stock"), the Company issued complex non-traded warrants with the potential for downward adjustments of the exercise price. The Company estimated the value of these warrants upon issuance using a binomial lattice-based option valuation model. Increases or decreases in the Company's share price, the volatility of the share price, changes in interest rates in general, and the passage of time will all impact the value of these warrants. The Company re-values these warrants at the end of each reporting period and any changes are reflected as gains or losses in current period results.

Use of Estimates

The preparation of our financial statements in accordance with GAAP requires us to, on an ongoing basis, make significant estimates and judgments that affect the reported values of assets, liabilities, revenues, expenses and related disclosure of contingent assets and liabilities. We base our estimates on historical experience and on various other assumptions we believe are reasonable under the circumstances, the results of which form the basis for our conclusions. Actual results may differ from these estimates under different assumptions or conditions. Such differences could have a material impact on our future financial position, results of operations, and cash flows.

Cash and Equivalents

We consider cash, deposits, and short-term investments with original maturities of three months or less as cash and equivalents. Our deposits are maintained primarily in two financial institutions and, at times, may exceed amounts covered by U.S. Federal Deposit Insurance Corporation insurance.

Restricted Cash

As part of the June 2013 financing with Bridge Bank, National Association (see "Acquisition Note Payable" herein), the Company agreed to maintain in a restricted cash account all proceeds, less debt service and approved expenses, generated by our Powerhouse One subsidiary. Such account provides a minimum of $108,000 replacement reserve ("module reserve") on solar panels found to be defective and potentially not covered under the manufacturer's warranty. Funds in excess of the modular reserve may be accessed by the Company following one year of operations and four consecutive quarters of performance exceeding covenants.

Accounts Receivable

Accounts receivable are stated at amounts management expects to collect from outstanding balances. Management provides for probable uncollectible amounts through a charge to earnings and a credit to a valuation allowance based on

its assessment of individual accounts. No allowance has been recorded in the accompanying financial statements.

Solar Arrays

Solar arrays are stated at historical cost, net of accumulated depreciation. Depreciation is computed using the straight-line method over the remaining estimated useful lives of the assets. The estimated useful lives of solar arrays are 25 years from the date first placed in service. Accumulated depreciation was $457,196 and $207,851 at September 30, 2014 and December 31, 2013, respectively. The value of the Power Purchase Agreement is included in the recorded cost of the associated array.

Long-Lived Assets

The recoverability of the carrying value of long-lived assets is assessed when an indicator of impairment has been identified. The Company judgmentally reviews its long-lived assets each quarter to assess whether impairment indicators are present.

For purposes of recognition and measurement of an impairment loss, a long-lived asset or group of assets is combined with other assets and liabilities at the lowest level for which identifiable cash flows are largely independent of the cash flows of other assets and liabilities.

For long-lived assets, when impairment indicators are present, the Company compares undiscounted future cash flows, including the eventual disposition of the asset group at market value, to the asset group's carrying value to determine if the asset group is recoverable. If undiscounted cash flows are less than carrying value, the excess of carrying value over fair value is expensed in the period in which it is estimated to have occurred. No impairment was recorded in the accompanying financial statements.

Revenue Recognition

Power generation revenue is recognized as generated based upon electrical meters affixed to the solar array and measuring kilowatt-hours produced. Our current power generation operations do not generate renewable energy credits, performance-based incentives, or similar credits to the benefit of the Company.

Income Taxes

Income taxes are recorded under the asset and liability method under which deferred tax assets and liabilities are determined based on the differences between the financial statement and tax bases of assets and liabilities using the enacted tax rates in effect for the year 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.

We account for uncertain income tax positions in accordance with Financial Accounting Standards Board Accounting Standards Codification ("FASB ASC") 740, *Income Taxes.* Interest costs and penalties related to income taxes are classified as interest expense and general and administrative costs, respectively, in our consolidated financial statements. Income tax returns are subject to a three-year statute of limitations during which they are subject to audit and adjustment. We file income tax returns in the United States federal jurisdiction. The tax years that remain subject to examination by major tax jurisdictions include 2010 through 2013.

Equity Transaction Fair Values

The estimated fair value of our Common Stock issued in share-based payments is measured by the more relevant of (1) the prices received in private placement sales of our stock or, (2) its publically-quoted market price. We estimate the fair value of simple warrants and stock options when issued or, in the case of issuances to non-employees, when vested using the Black-Scholes option-pricing ("Black-Scholes") model that requires the input of subjective assumptions. When valuing more complex warrants, options, or other derivative equity instruments, we use a binomial lattice-based option pricing model or Monte Carlo option pricing model, whichever management deems more appropriate in the circumstances. Recognition in stockholders' equity and expense of the fair value of stock options awarded to employees is on the straight-line basis over the requisite service period. Subsequent changes in fair value are not recognized.

Net Income (Loss) per Share

Basic net income or loss per share is computed by dividing the net income or loss for the period by the weighted average number of shares of Common Stock outstanding for the period. Diluted income per share reflects the potential dilution of derivative securities by including other potential issuances of Common Stock including shares to be issued upon exercise of options and warrants and upon conversion of convertible debt. Potentially dilutive shares are not included in the event of a loss as the effect of doing so would be anti-dilutive. As of September 30, 2014, options to purchase 2,843,341 shares and warrants to purchase 2,350,368 shares of our Common Stock have been excluded from the calculation of diluted loss per share, as their effect would have been anti-dilutive. As of September 30, 2013, options to purchase 1,611,333 shares and warrants to purchase 2,350,368 shares of our Common Stock have been excluded from the calculation of diluted loss per share as their effect would have been anti-dilutive.

NOTE 3 - LIABILITIES ARISING FROM REVERSE MERGER

Liabilities arising from the reverse merger represent long term real estate leases which had been abandoned, general unsecured liabilities, commercial liens, and tax liens filed with various states all associated with the Company's pre-reverse merger operations, which were unknowingly assumed in the March 2011 reverse merger transaction. The statute of limitations for most of such liabilities is five years and for most liens is ten years, subject to renewal at the lien holders' option, depending upon the jurisdiction. The liens accrue interest at between 8% and 12%. Liabilities not associated with a lien have been accrued based upon management's estimation of the amount to be paid. Liabilities associated with a lien have been accrued at face value. Management believes all such liabilities have been indemnified by Pegasus Funds, LLC (and/or its affiliates or related parties) to which (including its assigns) the Company issued 2,138,617 shares of its common stock as part of the reverse merger transaction. However, as the Company is obligor, the Company has recorded the liability. To date, only one lien holder has approached the Company concerning payment. Such lien holder is pursuing the former management of the Company first through litigation. To the extent such lien holder recovers the liability from the former management, the lien against the Company will be reduced.

NOTE 4 - COMPENSATION PAYABLE

Certain members of the management team have deferred payment of their compensation for the benefit of the Company. No formal terms of payment have been established.

NOTE 5 - ACQUISITIONS

Powerhouse One

Effective June 17, 2013, PSI entered into an acquisition agreement with Vis Solis, LLC ("Vis Solis"), a Tennessee Limited Liability Company and AstroSol, Inc., a Tennessee corporation (together "Co-Sellers") of Powerhouse One, LLC ("Powerhouse"), whereby 89% of the outstanding membership interests of Powerhouse were exchanged for $6,200,000 in cash. At the time of acquisition, the four solar arrays owned by Powerhouse had a remaining estimated useful life of 23 years (being first placed in service in 2011), and power generated is sold to a utility in Lincoln County Tennessee under an index-priced Power Purchase Agreement having a fixed premium of $0.12 per kilowatt-hour over the GSA-1 scheduled rate (currently approximately $0.10 per kWh) through 2021, and a market rate based upon the then current GSA-1 scheduled rate for the remaining 10 years of the initial 20 year term ending in 2031.

The acquisition was accounted for as a business combination under ASC 805 and was entered into in order to acquire the solar arrays. As part of the acquisition, 46,010 shares were issued to Co-Sellers in consideration for the right to acquire their remaining 11% noncontrolling interest for $766,827 within one year from the initial acquisition date. The value of the noncontrolling interest was pro-rated based upon the negotiated value of the equity interest acquired by the Company.

In June 2014, the option to acquire the remaining 11% non-controlling interest of Powerhouse One from the Co-Sellers expired. However, the parties have re-confirmed their intent to transfer the non-controlling interest to the

Company over the next several months as the Company obtains sufficient financing to do so, and on the same terms contained in the option as if it were still in full force and effect. The Company does not believe there are any material risks to the Company if the acquisition is not completed. The option value was expensed upon expiration.

The Company incurred $277,287 in acquisition related fees as part of the transaction which are included in general and administrative expenses in the nine months ended September 30, 2013.

Accounting for Power Purchase Agreement

The Company evaluated the PPA with reference to ASC 805-20-25-10 entitled "Identifiable Intangible Assets" and determined that, while it is not a separately identifiable asset, it does meet contractual-legal criteria. However, ASC 805-50-55-2(b) provides that the acquirer may recognize the fair value of the intangible asset and the fair value of the solar array "as a single asset for purposes of financial reporting purposes if the useful lives of those assets are similar." At the time of acquisition, the useful lives of the PPA and the solar array were 18 years and 23 years, respectively, which the Company determined were similar enough to report them as a single asset for financial reporting purposes. The company also determined the PPA was neither a lease nor a derivative instrument pursuant to ASC 840-10-16-6 "Arrangements That Qualify as a Lease", and ASC 815-10-15 "Derivatives and Hedging", respectively. The Company accounts for the PPA as an executory contract.

Allocation of Purchase Price

Final allocation of the purchase price as of the acquisition date was determined based upon estimates developed internally by management. Given the high level of predictability in future revenues stemming from the PPA, the stability and predictability in maintenance stemming from a multi-year outsourced contract to perform such, and the long-term warranties on primary components (PV modules generally carry 25-year warranties), the Company determined the best method to value the acquired fixed asset was using a discounted cash flow analysis, further supported by reference to the historical cost to build and place the facility in service just 20 months earlier.

Cash	$ 122,786
Accounts receivable	178,723
Solar arrays	6,665,318
Noncontrolling interest	(766,827)
Net purchase price	$6,200,000

The operating results of Powerhouse have been included in the consolidated financial statements since the acquisition date. On a pro forma basis, had the acquisition of Powerhouse occurred on January 1, 2013, the consolidated revenues and loss of PSI for the nine months ended September 30, 2013, would have been:

Revenue	$ 676,803
Net Loss	$ (1,905,046)

NOTE 6 - NOTES PAYABLE

Acquisition Note Payable

On June 17, 2013, Powerhouse One, LLC secured financing of $5,050,000 from Bridge Bank, National Association to acquire the membership interest (and the underlying solar arrays) of Co-Sellers. The note matures on June 17, 2017, and bears a fixed interest rate of 7.5% annually. Interest is paid monthly and principal is paid quarterly beginning in September 2013 based on an 11-year amortization schedule. Covenants include the maintenance of a restricted cash account, routine reporting, and a minimum debt service coverage ratio calculated separately for Powerhouse One of not less than 1.10:1, measured quarterly following the first anniversary of the debt. The debt also restricts the payment of dividends, and it is secured by all the assets of Powerhouse and further guaranteed by Principal Solar, Inc.

In conjunction with the acquisition note payable, warrants to purchase 151,050 shares of Common Stock were issued to Bridge Bank with an exercise price of $1.00 and a contractual life of 10 years. The value of the warrants issued in connection with this debt, as determined using the Black-Scholes model, was $81,449 and is recorded as a discount to the debt. The discount is being amortized as interest expense over the life of the note.

The Bridge Bank warrants have cashless exercise rights, redemption rights providing the Company the right to redeem the warrants for $604,200, anti-dilution rights associated with offerings of equity securities, a term expiring on the first to occur of (i) the 10 year anniversary of the grant, (ii) the closing of the Company's initial public offering (which is being affected pursuant to Registration Statement on Form S-1), or (iii) the liquidation of the Company (each a "Termination Event"). In each case, unless exercised earlier, the warrants are automatically exercised on a cashless basis upon a Termination Event. The Company also provided the holder registration rights in connection with the grant of the warrants.

Convertible Notes Payable, Related Parties

In June 2014, the Company issued convertible notes of $250,000 each to two of its Board members, Messrs. Heller and Marmol, to fund deposits on potential future acquisitions. Such potential acquisitions remain subject to significant uncertainties including due diligence, obtaining construction and permanent financing, and negotiating PPA's, developer agreements, and interconnection agreements. The notes bear interest at a rate of 18% per year and mature on December 5, 2014, and all principal and interest is due at maturity. Principal and interest is payable in cash or shares of Common Stock, at the option of the holder, at a conversion price of $1.00 per share. The notes are secured pursuant to a security agreement by the Company's interest in the otherwise unencumbered net cash flow, if any, from the operations of its Powerhouse One subsidiary. The Company may prepay the notes at any time, but the holders of the notes have been guaranteed to receive a minimum of six months interest on the notes.

NOTE 7 - LEASES

The Company's solar arrays sit on properties subject to long-term real estate leases (or similar agreements in the case of rooftop installations) with initial terms equal to the PPA and having one or more renewal options. Rental payments under the leases vary in type between fixed price, percentage of revenue, or, in the case of rooftop installations, no separate charge. The Company's current solar array installations are as follows:

Installation	Location	kWh	Date	Term	Rent
Powerhouse One	Fayetteville, TN	3,000	Aug 2011	20 yr. + 2 5-yr renewals	4% of revenue
SunGen StepGuys	Alfred, ME	110	Sep 2009	25 yr. + 2 25-yr renewals	None
SunGen Mill 77	Amesbury, MA	63	June 2010	25 yr. + 2 25-yr renewals	None

The Company recognized expenses of $11,086 and $30,494 in rent under the Powerhouse One lease in the three and nine months ended September 30, 2014, respectively.

In each case, the Company is obligated to remove such installations at the end of the lease terms. As the expected termination dates are decades off; there is little experience de-installing solar arrays anywhere in the world; and, costs are expected to be minimal; such removal costs have not been separately accounted for.

The Company maintains its headquarters in Dallas, Texas pursuant to a month-to-month lease at a cost of $500 per month.

NOTE 8 - DERIVATIVE LIABILITY ON WARRANTS

In June 2013, the Company issued warrants to purchase 2,181,818 shares of Common Stock with a 10-year contractual term to Steuben Investment Company II, L.P. in connection with the issuance of Common Stock to fund the Powerhouse One acquisition. The warrants were immediately exercisable into the Company's Common Stock with an exercise price of $1.00 per share. However, as the warrants have "down round" protection, they are treated as a derivative liability and were valued using a binomial lattice-based option valuation model using holding period

assumptions developed from the Company's business plan and management assumptions, and expected volatility from comparable companies including OTC Pink® and small-cap companies. Input assumptions at September 30, 2014, were as follows:

Estimated fair value	$0.51
Expected life (years)	5.21 Years
Risk free interest rate	1.78%
Volatility	227.71%

The fair value of the warrant derivative liability outstanding as of September 30, 2014, was determined using "Level 2 Observable Inputs" as defined in FASB ASC 820, *Fair Value Measurement*.

The following table sets forth a summary of changes in fair value of the warrants in 2014:

Beginning balance December 31, 2013	$	1,123,149
Derivative warrants issued		-
Change in fair value included in net loss		1,160
Balance at June 30, 2014	$	1,121,989

NOTE 9 – CAPITAL STOCK

Preferred Stock

The Company has authorized 100,000,000 shares of $.01 par value Class A preferred stock but had none outstanding during 2014 or 2013.

Common Stock

The Company has authorized 300,000,000 shares of $.01 par value Common Stock, and it trades on the OTC Pink® under the symbol "PSWW." Holders of our Common Stock are entitled to one vote per share and receive dividends or other distributions when, and if, declared by our Board of Directors. In addition to shares outstanding, we have reserved 2,864,359 shares for issuance upon exercise of equity incentive awards with options to purchase 2,843,341 shares of Common Stock granted to date.

Stueben Investment

Effective June 14, 2013, the Company entered into a Subscription Agreement with Steuben Investment Company II, L.P. ("Steuben"). Pursuant to the subscription agreement, Steuben purchased 2,909,091 shares of the Company's common stock for an aggregate of $1,600,000 or $0.55 per share. As additional consideration in connection with the subscription, the Company granted Steuben warrants to purchase 2,181,818 shares of the Company's common stock with an exercise price of $1.00 per share and a term of 10 years. The Company also provided Steuben registration rights pursuant to a Registration Rights Agreement entered into with Steuben in connection with the shares sold and shares of common stock issuable upon exercise of the warrants (collectively, the "Registrable Securities"). Pursuant to the registration rights agreement, the Company was required to file a registration statement to register the Registrable Securities within 90 days after the date of the subscription and to obtain effectiveness of the registration statement within 180 days after the date of the subscription (which deadlines were not met); provided that the Company does not incur fees as a consequence of such delay under the registration rights agreement unless it fails to file the registration statement within 120 days of the subscription (which date was October 12, 2013) or fails to obtain effectiveness of the registration statement within 210 days of the subscription (which date was January 10, 2014). The registration rights agreement required certain penalties to be paid in the event the above filing deadlines were not met.

In a letter agreement dated February 5, 2014, and made effective March 27, 2014 (the "Letter Agreement"), the Company and Steuben set a new deadline for making effective the registration statement, and provided a waiver of penalties if the new deadline was met. The new deadline was not met.

Subsequent to the Letter Agreement, email and verbal agreements were made by the Company and Steuben to provide an additional extension for an effective date of the registration statement to not later than July 1, 2015, and to fix the penalty at $216,000 for failing to a) meet the extended effectiveness date of July 1, 2015, and b) take all necessary actions to maintain the availability of Rule 144 for a period of two years following the effective date of the registration statement pursuant to which Steuben could sell shares. Also, subsequent to the Letter Agreement, the Company and Steuben verbally agreed that the Company is required to initially register only 1,300,936 of the shares of common stock held by Steuben.

On October 7, 2014, the Company and Steuben entered into "Amendment No. 1 to Registration Rights Agreement" memorializing our earlier email and verbal agreements regarding 1) the extension of the effectiveness deadline to July 1, 2015, 2) fixing at $216,000 the penalty for failing to meet that extended deadline of July 1, 2015, and maintaining the availability of Rule 144, 3) reconfirming the request to register 1,300,936 shares of Steuben's current holdings in the registration statement of which the prospectus is a part, and 4) nullifying in its entirety the earlier Letter Agreement.

The Company has not accrued a liability stemming from this penalty as it believes the payment of any such penalty is not probable.

Stock Options

In 2013, the Company issued to its independent Directors options to acquire an aggregate of 432,000 shares of its Common Stock. The options have an exercise price of $1.00 per share and vest over 24 months. The options were valued using the Black-Scholes model and the resulting equity-based compensation expense in the three and nine months ended September 30, 2014, was $17,737 and $53,211, respectively.

In June 2014, the Company re-priced 96,000 options granted to independent advisors between February 2012 and September 2012. The options, originally issued having exercise prices ranging from $1.41 to $1.71 per share, were re-priced to $1.00 per share. Because of the small change in inputs to the Black-Scholes model since they were initially issued (especially volatility), there was no expense recorded in connection with this action.

Recent Grant

In August and September 2014, the Company granted to its key executives, independent contractors, new Board members, and a key advisor (and former CFO), options to acquire 1,208,008 shares of its Common Stock. The options have an exercise price of $1.00 per share and have expiration dates of 2 years for the advisor and 10 years for key executives, independent contractors, and Board members. Vesting ranges from (i) immediately upon grant with pro-rata forfeiture provisions for non-employee executives and independent contractors should their services to the Company terminate within three years from the date of grant, (ii) 24 months for Board members starting when they joined the Board, and (ii) 36 months for employees.

All options were valued using the Black-Scholes options pricing model and resulted in an expense of $1,232,008 including $1,020,778 to be recognized during the three months ended September 30, 2014; $26,334 for each three-month period thereafter through December 31, 2015; $5,778 for each month from January 2016 through August 2016; and $2,778 for each month from September 2016 through August 2017.

The fair value of the common shares was based upon a "market approach" reflected by multiple recent issuances of identical shares, at an identical price ($1.00 per share), to unrelated accredited investors. As the Company does not have a significant history of post vesting exercises to estimate an expected life of the option, the simplified method was applied. The risk free rate was determined with reference to interest rates published by the U.S. Federal Reserve System constant maturity U.S. Treasury securities having terms most closely approximating the expected life for each option issued. The expected lives based upon the simplified method ranged from 2.5 years for independent contractors and key advisors to 7.25 years for executives and Board members, and interest rates ranged from .44% to 2.19% per annum, respectively. Expected volatility was calculated as 227.71% based upon the computed volatility of comparable companies using a binomial lattice-based option-pricing model.

The valuation of non-traded options involves the use of estimates and, therefore, involves a degree of subjectivity. In addition, because there is not a robust and active public market in the Company's securities, our use of estimates in determining the valuation of the options was expanded somewhat. As such, the Company considers the valuation in this instance to be highly subjective.

Summary

As the Company does not have a significant history of post vesting exercises to estimate an expected life of the option, the simplified method was used wherein the expected life becomes the mid-point of the options vesting date and their contractual life.

At September 30, 2014, the Company had a total of 2,843,241 options outstanding and $264,443 of compensation expense related to options not yet vested remains unrecognized. Such amount is expected to be recognized through 2017.

The weighted average exercise price of those options currently outstanding is $1.16 and those currently exercisable are $1.06. Based upon the Company's stock price at September 30, 2014, of $1.45 as quoted on the OTC Pink® market, the options then outstanding had an intrinsic value of $835,336 and those exercisable had an intrinsic value of $715,983.

Warrants

At September 30, 2014, the Company has warrants to purchase 2,350,368 shares of Common Stock outstanding having an exercise price of $1.00 per share. See notes herein entitled "Acquisition Notes Payable" and "Derivative Liability on Warrants" for detailed descriptions of their issuances. The Company had warrants to purchase 2,350,368 shares of Common Stock outstanding at September 30, 2013.

NOTE 10 - NONCONTROLLING INTEREST

The original owners of Powerhouse One continue to own approximately 11% of the membership interest of the limited liability company. The noncontrolling interests of equity investors in Powerhouse One is reported on the consolidated balance sheet and statement of operations as "Noncontrolling interest in subsidiary" ("noncontrolling interest") and reflects their respective interests in the equity and the income or loss of the limited liability company.

The following table sets forth the activity in the noncontrolling interest equity account during 2014:

Balance December 31, 2013	$ 786,803
Earnings allocated to noncontrolling interest	34,932
Balance September 30, 2014	$ 821,735

NOTE 11 – RELATED PARTY TRANSACTIONS

Other than the Board member options described herein in a note entitled "Stock Options," the issuance of convertible notes described herein in the note entitled "Convertible Notes Payable, Related Parties", no other related party transactions occurred during the nine months ended September 30, 2014 and 2013.

NOTE 12 - TAXES

Our estimated $8,184,785 federal income tax net operating loss carryover expires over the period from 2030 through 2034. Our federal and state income tax returns are no longer subject to examination for years before 2010. We have taken no tax positions that, more likely than not, may not be realized.

The Company has established a valuation allowance to fully reserve the net deferred tax assets in the accompanying financial statements, due to the uncertainty of the timing and amounts of future taxable income.

NOTE 13 - COMMITMENTS AND CONTINGENCIES

The Company may be subject to rescission rights from certain investors who purchased shares of our common stock based on their review of the presentation which we furnished as Exhibit 99.1 to our Current Report on Form 8-K,

filed with the Securities and Exchange Commission on May 5, 2014, which may have constituted a communication of an “offer to sell” as described in Section 5(c) of the Securities Act of 1933, as amended (the “Securities Act”) in violation of Section 5 of the Securities Act. If a claim were brought by any ‘recipients’ of such presentation and a court were to conclude that such presentation constituted a violation of Section 5 of the Securities Act, we could be required to repurchase the shares sold to the investors who reviewed such presentation at the original purchase price, plus statutory interest from the date of purchase, for claims brought during a period of one year from the date of their purchase of common stock. We could also incur considerable expense in contesting any such claims. The prospectus included in the Form S-1/A and dated October 20, 2014, included an additional risk factor stating:

> "You should not rely on any information set forth in the presentation attached as Exhibit 99.1 to our Current Report on Form 8-K, filed with the Securities and Exchange Commission on May 5, 2014 in making an investment decision."

As of the date of these statements, no legal proceedings or claims have been made or threatened by any investors in the Company and the Company considers the likelihood that the investors will file suit to be remote. Therefore, in accordance with ASC 450-20 “Loss Contingencies”, the Company has not recorded a liability for the potential rescission.