

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

FORM 10-Q

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

For the quarterly period ended June 30, 2022

or

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

For the transition period from _____ to _____

Commission file number: 001-37673

WORKHORSE GROUP INC.

(Exact name of registrant as specified in its charter)

Nevada

(State or other jurisdiction of
incorporation or organization)

26-1394771

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

3600 Park 42 Drive, Suite 160E, Sharonville, Ohio 45241

(Address of principal executive offices, including zip code)

1 (888) 646-5205

(Registrant's telephone number, including area code)

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

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, \$0.001 par value per share	WKHS	The NASDAQ Capital Market

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

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

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

The number of shares of the Registrant's Common Stock, \$0.001 par value per share, outstanding as of July 31, 2022, was 163,740,917.

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Forward-Looking Statements

The discussions in this Quarterly Report on Form 10-Q (this "Report") contain forward-looking statements reflecting our current expectations that involve risks and uncertainties. These statements are made under the "safe harbor" provisions of the U.S. Private Securities Litigation Reform Act of 1995. When used in this Report, the words "anticipate," "expect," "plan," "believe," "seek," "estimate" and similar expressions are intended to identify forward-looking statements. These are statements that relate to future periods and include, but are not limited to, statements about the features, benefits and performance of our products, our ability to introduce new product offerings and increase revenue from existing products, expected expenses including those related to selling and marketing, product development and general and administrative, our beliefs regarding the health and growth of the market for our products, anticipated increase in our customer base, expansion of our products functionalities, expected revenue levels and sources of revenue, expected impact, if any, of legal proceedings, the adequacy of liquidity and capital resources, and expected growth in business. Forward-looking statements are statements that are not historical facts. Such forward-looking statements are subject to risks and uncertainties, which could cause actual results to differ materially from the forward-looking statements contained in this Report. Factors that could cause actual results to differ materially include, but are not limited to: our ability to develop and manufacture our new product portfolio, including the recently announced W750, W56 and W34 platforms; our ability to attract and retain customers for our existing and new products; risks associated with obtaining orders and executing upon such orders; supply chain disruptions, including constraints on steel, semiconductors and other material inputs and resulting cost increases impacting our company, our customers, our suppliers or the industry; our ability to implement modifications to vehicles to achieve compliance with Federal Motor Vehicle Safety Standards and to meet customer demands with respect to the C-1000s; the results of our ongoing review of the Company's business and go-forward operating and commercial plans; our ability to capitalize on opportunities to deliver products to meet customer requirements; our limited operations and need to expand and enhance elements of our production process to fulfill product orders; the ability to protect our intellectual property; negative impacts stemming from the continuing COVID-19 pandemic; market acceptance for our products; our ability to control our expenses; potential competition, including without limitation shifts in technology; global and local business conditions; acts of war (including without limitation the conflict in Ukraine) and/or terrorism; the prices being charged by our competitors; our inability to retain key members of our management team; our inability to raise additional capital to fund our operations and business plan; our inability to maintain our listing of our securities on the Nasdaq Capital Market; our inability to satisfy our customer warranty claims; the outcome of any regulatory or legal proceedings; our liquidity and other risks and uncertainties and other factors discussed from time to time in our filings with the Securities and Exchange Commission ("SEC"), including our annual report on Form 10-K filed with the SEC. Forward-looking statements speak only as of the date hereof. We expressly disclaim any obligation or undertaking to release publicly any updates or revisions to any forward-looking statements contained herein to reflect any change in our expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based, except as required by law.

All references in this Report that refer to the "Company", "Workhorse Group", "Workhorse", "we," "us" or "our" are to Workhorse Group Inc.

PART I – FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

Workhorse Group Inc.
Condensed Consolidated Balance Sheets
(Unaudited)

	June 30, 2022	December 31, 2021
Assets		
Current assets:		
Cash and cash equivalents	\$ 140,060,575	\$ 201,647,394
Accounts receivable, less allowance for credit losses of zero as of June 30, 2022 and December 31, 2021	784,668	149,776
Inventory, net	12,557,319	10,067,367
Prepaid expenses and other current assets	11,749,364	4,357,829
Total current assets	165,151,926	216,222,366
Property, plant and equipment, net	13,582,936	7,897,807
Lease right-of-use assets	11,666,276	1,538,852
Other assets	126,310	2,479,865
Total Assets	\$ 190,527,448	\$ 228,138,890
Liabilities		
Current liabilities:		
Accounts payable	\$ 3,787,194	\$ 7,849,607
Accrued and other current liabilities	9,596,353	14,752,827
Warranty liability	3,322,212	4,583,916
Current portion of lease liabilities	1,050,585	363,714
Total current liabilities	17,756,344	27,550,064
Lease liabilities, long-term	8,942,651	1,191,053
Convertible notes, at fair value	—	24,705,000
Total Liabilities	26,698,995	53,446,117
Commitments and contingencies		
Stockholders' Equity:		
Series A preferred stock, par value \$0.001 per share, 75,000,000 shares authorized, zero shares issued and outstanding as of June 30, 2022 and December 31, 2021	—	—
Common stock, par value \$0.001 per share, 250,000,000 shares authorized, 160,058,512 shares issued and outstanding as of June 30, 2022 and 151,915,455 shares issued and outstanding as of December 31, 2021	160,059	151,916
Additional paid-in capital	717,258,045	686,318,201
Accumulated deficit	(553,589,651)	(510,374,844)
Accumulated other comprehensive loss	—	(1,402,500)
Total stockholders' equity	163,828,453	174,692,773
Total Liabilities and Stockholders' Equity	\$ 190,527,448	\$ 228,138,890

See accompanying notes to the condensed consolidated financial statements.

Workhorse Group Inc.
Condensed Consolidated Statements of Operations
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2022	2021	2022	2021
Sales, net of returns and allowances	\$ 12,555	\$ 1,202,876	\$ 26,854	\$ 1,723,936
Cost of sales	3,020,204	14,796,130	6,943,555	21,021,429
Gross loss	(3,007,649)	(13,593,254)	(6,916,701)	(19,297,493)
Operating expenses				
Selling, general and administrative	13,030,143	7,005,537	24,940,402	13,891,367
Research and development	5,027,061	2,123,860	9,038,995	5,987,575
Total operating expenses	18,057,204	9,129,397	33,979,397	19,878,942
Loss from operations	(21,064,853)	(22,722,651)	(40,896,098)	(39,176,435)
Interest expense (income), net	95,419	10,478,717	2,318,709	(4,441,756)
Other loss	—	11,699,666	—	148,305,618
Loss before benefit for income taxes	(21,160,272)	(44,901,034)	(43,214,807)	(183,040,297)
Benefit for income taxes	—	(1,281,947)	—	(18,914,439)
Net loss	\$ (21,160,272)	\$ (43,619,087)	\$ (43,214,807)	\$ (164,125,858)
Net loss per share of common stock				
Basic	\$ (0.13)	\$ (0.35)	\$ (0.28)	\$ (1.33)
Diluted	\$ (0.13)	\$ (0.35)	\$ (0.28)	\$ (1.33)
Weighted average shares used in computing net loss per share of common stock				
Basic	159,107,776	123,414,045	155,543,436	122,984,218
Diluted	159,107,776	123,414,045	155,543,436	122,984,218

See accompanying notes to the condensed consolidated financial statements.

Workhorse Group Inc.
Condensed Consolidated Statements of Comprehensive Loss
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2022	2021	2022	2021
Net loss	\$ (21,160,272)	\$ (43,619,087)	\$ (43,214,807)	\$ (164,125,858)
Other comprehensive loss				
Change in fair value of convertible notes attributable to credit spread	—	(10,200,000)	—	(10,200,000)
Comprehensive loss	\$ (21,160,272)	\$ (53,819,087)	\$ (43,214,807)	\$ (174,325,858)

See accompanying notes to the condensed consolidated financial statements.

Workhorse Group Inc.
Condensed Consolidated Statements of Stockholders' Equity
(Unaudited)

	Common Stock		Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total Stockholders' Equity
	Number of Shares	Amount				
Balance as of March 31, 2021	123,254,853	\$ 123,255	\$ 505,017,758	\$ (229,536,802)	\$ —	\$ 275,604,211
Stock options and warrants exercised, and vesting of restricted shares*	159,192	159	(83,795)	—	—	(83,636)
Stock-based compensation	—	—	1,139,913	—	—	1,139,913
Net loss for the three months ended June 30, 2021	—	—	—	(43,619,087)	—	(43,619,087)
Other comprehensive loss	—	—	—	—	(10,200,000)	(10,200,000)
Balance as of June 30, 2021	<u>123,414,045</u>	<u>\$ 123,414</u>	<u>\$ 506,073,876</u>	<u>\$ (273,155,889)</u>	<u>\$ (10,200,000)</u>	<u>\$ 222,841,401</u>

	Common Stock		Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total Stockholders' Equity
	Number of Shares	Amount				
Balance as of December 31, 2020	121,922,532	\$ 121,923	\$ 504,112,442	\$ (109,030,031)	\$ —	\$ 395,204,334
Stock options and vesting of restricted shares*	1,491,513	1,491	(70,907)	—	—	(69,416)
Stock-based compensation	—	—	2,032,341	—	—	2,032,341
Net loss for the six months ended June 30, 2021	—	—	—	(164,125,858)	—	(164,125,858)
Other comprehensive loss	—	—	—	—	(10,200,000)	(10,200,000)
Balance as of June 30, 2021	<u>123,414,045</u>	<u>\$ 123,414</u>	<u>\$ 506,073,876</u>	<u>\$ (273,155,889)</u>	<u>\$ (10,200,000)</u>	<u>\$ 222,841,401</u>

*Net of tax payments related to shares withheld for option exercises and vested stock.

See accompanying notes to the condensed consolidated financial statements.

Workhorse Group Inc.
Condensed Consolidated Statements of Stockholders' Equity
(Unaudited)

	Common Stock		Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total Stockholders' Equity
	Number of Shares	Amount				
Balance as of March 31, 2022	151,993,870	\$ 151,994	\$ 688,472,154	\$ (532,429,379)	\$ —	\$ 156,194,769
Common stock issued in exchange of convertible notes	7,833,666	7,834	25,373,244	—	—	25,381,078
Common stock issued through At-The-Market offering	98,986	99	248,596	—	—	248,695
Stock options and warrants exercised, and vesting of restricted shares*	131,990	132	(128,358)	—	—	(128,226)
Stock-based compensation	—	—	3,292,409	—	—	3,292,409
Net loss for the three months ended June 30, 2022	—	—	—	(21,160,272)	—	(21,160,272)
Balance as of June 30, 2022	160,058,512	\$ 160,059	\$ 717,258,045	\$ (553,589,651)	\$ —	\$ 163,828,453

	Common Stock		Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total Stockholders' Equity
	Number of Shares	Amount				
Balance as of December 31, 2021	151,915,455	\$ 151,916	\$ 686,318,201	\$ (510,374,844)	\$ (1,402,500)	\$ 174,692,773
Common stock issued in exchange of convertible notes	7,833,666	7,834	25,373,244	—	—	25,381,078
Common stock issued through At-The-Market offering	98,986	99	248,596	—	—	248,695
Stock options and vesting of restricted shares*	210,405	210	(324,698)	—	—	(324,488)
Stock-based compensation	—	—	5,642,702	—	—	5,642,702
Net loss for the six months ended June 30, 2022	—	—	—	(43,214,807)	—	(43,214,807)
Other comprehensive loss	—	—	—	—	1,402,500	1,402,500
Balance as of June 30, 2022	160,058,512	\$ 160,059	\$ 717,258,045	\$ (553,589,651)	\$ —	\$ 163,828,453

*Net of tax payments related to shares withheld for option exercises and vested stock.

See accompanying notes to the condensed consolidated financial statements.

Workhorse Group Inc.
Condensed Consolidated Statements of Cash Flows
(Unaudited)

	Six Months Ended June 30,	
	2022	2021
Cash flows from operating activities:		
Net loss	\$ (43,214,807)	\$ (164,125,858)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	710,348	787,846
Change in fair value and loss on exchange of convertible notes	1,769,857	(7,000,000)
Change in fair value of Investment in LMC	—	148,305,618
Stock-based compensation	5,642,702	2,032,341
Change in inventory and prepaid purchases reserve	425,130	(7,560,774)
Forgiveness of PPP Term Note	—	(1,411,000)
Deferred taxes	—	(18,914,439)
Non-cash lease expense	583,406	—
Other non-cash items	175,750	—
Effects of changes in operating assets and liabilities:		
Accounts receivable	(634,892)	(822,445)
Inventory	(3,187,163)	(26,477,331)
Prepaid expenses and other current assets	(7,119,454)	(7,499,919)
Other assets	(34,401)	—
Accounts payable, accrued liabilities and other	(9,317,242)	1,952,104
Warranty liability	(1,261,704)	(533,787)
Net cash used in operating activities	<u>(55,462,470)</u>	<u>(81,267,644)</u>
Cash flows from investing activities:		
Capital expenditures	(5,658,776)	(3,281,213)
Net cash used in investing activities	<u>(5,658,776)</u>	<u>(3,281,213)</u>
Cash flows from financing activities:		
Proceeds from issuance of common stock	248,695	—
Payments on finance lease	(389,780)	—
Exercise of warrants and options and restricted share award activity	(324,488)	(69,416)
Net cash used in financing activities	<u>(465,573)</u>	<u>(69,416)</u>
Change in cash and cash equivalents	(61,586,819)	(84,618,273)
Cash, cash equivalents and restricted cash, beginning of the period	201,647,394	241,229,067
Cash and cash equivalents, end of the period	<u>\$ 140,060,575</u>	<u>\$ 156,610,794</u>

See accompanying notes to the condensed consolidated financial statements.

Workhorse Group Inc.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

1. SUMMARY OF BUSINESS AND SIGNIFICANT ACCOUNTING PRINCIPLES

Overview

We are a technology company with a vision to pioneer the transition to zero-emission commercial vehicles. Our primary focus is to provide sustainable and cost-effective solutions to the commercial transportation sector. We design and manufacture all-electric delivery trucks and drone systems, including the technology that optimizes the way these vehicles operate. We are focused on our core competency of bringing our electric delivery vehicle platforms to market.

Principles of Consolidation

The accompanying condensed consolidated financial statements have been prepared in conformity with U.S. generally accepted accounting principles (“GAAP”) and reflect our accounts and operations and those of our wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated upon consolidation.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, costs and expenses and related disclosures in the accompanying notes.

In the opinion of our management, the Unaudited Condensed Consolidated Financial Statements include all adjustments that are necessary for the fair presentation of Workhorse’s financial condition, results of operations and cash flows for the interim periods presented. Such adjustments are of a normal, recurring nature. The results of operations and cash flows for the interim periods presented may not necessarily be indicative of full-year results. Reference should be made to the financial statements contained in our Annual Report on Form 10-K for the year ended December 31, 2021.

2. INVENTORY, NET

Inventory, net consisted of the following:

	June 30, 2022	December 31, 2021
Raw materials	\$ 58,629,245	\$ 66,238,615
Work in process	23,991,215	20,826,644
Finished goods	—	—
	82,620,460	87,065,259
Less: inventory reserves	(70,063,141)	(76,997,892)
Inventory, net	\$ 12,557,319	\$ 10,067,367

We reserve inventory for any excess or obsolete inventories or when we believe the net realizable value of inventories is less than the carrying value.

As of June 30, 2022 and December 31, 2021, the Company recorded inventory reserves of \$0.1 million and \$77.0 million, respectively. During 2021, the Company significantly increased its inventory reserves due to its decision to produce the C-1000 vehicle platform at low-volume and transition to a new all-electric delivery truck platform in the future. This decision was based on results of extensive testing performed on the C-1000 vehicles, which concluded in early 2022. The \$6.9 million decrease in inventory reserves as compared to December 31, 2021 is primarily driven by the Company’s efforts to dispose of inventory that is not expected to be used in future production.

3. PREPAID EXPENSES AND OTHER CURRENT ASSETS

Prepaid and other current assets consisted of the following:

	June 30, 2022	December 31, 2021
Prepaid purchases ⁽¹⁾	\$ 32,928,751	\$ 24,101,695
Less: prepaid purchases reserve ⁽²⁾	(22,020,805)	(23,912,025)
Prepaid purchases, net	10,907,946	189,670
Prepaid insurance	327,035	2,205,608
Right of return asset	—	1,620,000
Other	514,383	342,551
Prepaid expenses and other current assets	<u>\$ 11,749,364</u>	<u>\$ 4,357,829</u>

⁽¹⁾The Company's prepaid purchases balance consists primarily of deposits made to our suppliers for non-recurring engineering costs, capital expenditures, and production parts. The increase in prepaid purchases as compared to December 31, 2021 is primarily due to deposits on orders related to the Company's W750 vehicle platform.

⁽²⁾We record reserves on prepaid purchase balances that are significantly aged, for balances that represent deposits for certain production parts related to the Company's C-Series vehicle platform, and for balances specifically identified as having a carrying value in excess of net realizable value. The reserve represents our best estimate of deposits on orders that we do not expect to recover.

4. REVENUE

Revenue Recognition

The following table provides a summary of sales activity for the period indicated:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2022	2021	2022	2021
Sales, net of returns and allowances	\$ 12,555	\$ 1,202,876	\$ 26,854	\$ 1,723,936

Revenue is recognized when obligations under the terms of a contract with our customer are satisfied. Generally, this occurs when we transfer control of our vehicles, parts, or accessories, or provide services. Revenue is measured as the amount of consideration we expect to receive in exchange for transferring goods or providing services. For the majority of sales, this occurs when products are shipped from our manufacturing facility. At the time of revenue recognition, we reduce the transaction price and record a sales return reserve against revenue for estimated variable considerations related to future product returns. Such estimates are based on an analysis of known pending returns and historical experience. We adjust our estimate of revenue at the earlier of when the value of consideration we expect to receive changes or when the consideration becomes fixed.

Sales and other taxes we collect concurrent with revenue-producing activities are excluded from revenue. The expected costs associated with our base warranties and field service actions are recognized as expense when the products are sold. We do not have any material significant payment terms as payment is received at or shortly after the point of sale.

We have elected to recognize the cost for freight and shipping when control over vehicles, parts, or accessories has transferred to the customer as an expense in Cost of Sales.

Accounts Receivable

Accounts receivable primarily include amounts related to sales of our products and services rendered. We provide an allowance against accounts receivable for the amount we expect to be uncollectible. We write-off accounts receivable against the allowance when they are deemed uncollectible.

5. DEBT

4.0% Senior Secured Convertible Notes Due 2024 (“2024 Notes”)

The fair value of the 2024 Notes as of June 30, 2022 and December 31, 2021 was zero and \$24.7 million, respectively. The contractual principal balance of the 2024 Notes as of June 30, 2022 and December 31, 2021 was zero and \$27.5 million, respectively.

In April 2022, the Company exchanged the remaining \$27.5 million in aggregate principal of the 2024 Notes for approximately 7.8 million shares of the Company’s common stock. The number of shares issued was calculated by dividing \$29.4 million, which represented 107% of the principal amount of the notes, plus \$0.3 million of interest accrued on the notes, by the average of the daily volume weighted average price for the 10 days immediately preceding April 21, 2022. The Company recognized a loss of \$1.8 million in the first quarter of 2022, which included a \$0.4 million adjustment to the fair value of the convertible notes to the value of the shares issued under the exchange and a \$1.4 million adjustment related to the realization of the amount previously recognized in Accumulated Other Comprehensive Loss. The total loss was recorded in Interest Expense for the six months ended June 30, 2022.

Subsequent to the exchange, the Company has no convertible notes outstanding and the indenture and related security agreement under which the 2024 Notes were issued have been terminated.

Interest on the 2024 Notes was payable quarterly beginning January 15, 2021 at a rate of 4.0% per annum. The following table summarizes contractual interest expense related to the 2024 Notes for the period indicated:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2022	2021	2022	2021
Contractual interest expense	\$ —	\$ 1,977,777	\$ 332,707	\$ 3,977,777

See Note 13, *Fair Value Measurements*, for additional information regarding the fair value measurement of the 2024 Notes.

PPP Term Note

On April 14, 2020, the Company entered into a Paycheck Protection Program Term Note (“PPP Term Note”) under the Paycheck Protection Program of the Coronavirus Aid, Relief, and Economic Security Act (“CARES Act”). The Company received total proceeds of approximately \$1.4 million. In accordance with the requirements of the CARES Act, the Company used the proceeds primarily for payroll costs. Interest accrued on the PPP Term Note at the rate of 1.0% per annum. The Company elected to account for the PPP Term Note as debt and accrued interest over the term of the note.

On January 15, 2021, the outstanding principal and interest accrued on the PPP Term Note were fully forgiven. The Company recognized approximately \$1.4 million in gain on the forgiveness of the PPP Term Note, which was recorded in Interest Income for the six months ended June 30, 2021.

6. ACCRUED AND OTHER CURRENT LIABILITIES

Accrued liabilities and other current liabilities consisted of the following:

	June 30, 2022	December 31, 2021
Accrued commissions	\$ 1,750,000	\$ 4,000,000
Compensation and related costs	3,294,304	4,030,085
Accrued interest	—	232,222
Sales return reserve	—	2,410,000
Other	4,552,049	4,080,520
Total accrued and other current liabilities	\$ 9,596,353	\$ 14,752,827

Warranties

We generally offer warranty coverage for our products. We accrue warranty related costs under standard warranty terms and for certain claims outside the contractual obligation period that we choose to pay as accommodations to our customers.

Provisions for estimated assurance warranties are recorded at the time of sale and are periodically adjusted to reflect actual experience. The amount of warranty liability accrued reflects management's best estimate of the expected future cost of honoring Company obligations under its warranty plans. Historically, the cost of fulfilling the Company's warranty obligations has principally involved replacement parts, towing and transportation costs, labor and travel for any field retrofit campaigns. The Company's estimates are based on historical experience, the extent of pre-production testing, the number of units involved, and the extent of features/components included in product models. The Company reviews actual warranty claims experience to determine if there are systemic defects that would require a field campaign.

Although we believe the estimates and judgments discussed herein are reasonable, actual results could differ and we may be exposed to increases or decreases in our warranty accrual that could be material.

Warranty liability activity consisted of the following:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2022	2021	2022	2021
Warranty liability, beginning of period	\$ 4,315,463	\$ 5,255,043	\$ 4,583,916	\$ 5,400,000
Warranty costs incurred	(348,005)	(488,830)	(698,958)	(733,787)
Provision for warranty	(645,246)	100,000	(562,746)	200,000
Warranty liability, end of period	\$ 3,322,212	\$ 4,866,213	\$ 3,322,212	\$ 4,866,213

7. LEASES

We have entered into various operating and finance lease agreements for offices, manufacturing and warehouse facilities. We determine if an arrangement is a lease, or contains a lease, at inception and record the leases in our financial statements upon lease commencement, which is the date when the underlying asset is made available for our use by the lessor.

Our leases may include options to extend the lease term for up to 5 years. Some of our leases also include options to terminate the lease prior to the end of the agreed upon lease term. For purposes of calculating lease liabilities, lease terms include options to extend or terminate the lease when it is reasonably certain that we will exercise such options.

During the second quarter of 2022, we entered into a lease agreement for additional office and warehouse space. We obtained a Letter of Credit ("LOC") in the amount of \$0.5 million to secure the lease, which bears interest at five percent per annum. Under the terms of the agreement, the landlord may use the whole or any part of the LOC for the payment of any amount as to which we are in default or to compensate the landlord for certain specified losses or damage.

Lease expense for operating leases is recognized on a straight-line basis over the lease term as cost of sales or operating expenses depending on the nature of the leased asset.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2022	2021	2022	2021
Short-term lease expense	\$ 248,103	\$ 226,268	\$ 424,008	\$ 349,783
Operating lease expense	465,544	—	762,967	—
Total lease expense	\$ 713,647	\$ 226,268	\$ 1,186,975	\$ 349,783

Lease right-of-use assets consisted of the following:

	June 30, 2022	December 31, 2021
Operating leases	\$ 5,743,960	\$ 1,538,852
Finance leases	5,922,316	—
Total lease right-of-use assets	<u>\$ 11,666,276</u>	<u>\$ 1,538,852</u>

Lease liabilities consisted of the following:

	June 30, 2022	December 31, 2021
Operating leases	\$ 6,540,730	\$ 1,554,767
Finance leases	3,452,506	—
Total lease liabilities	9,993,236	1,554,767
Less: current portion	(1,050,585)	(363,714)
Long-term portion	<u>\$ 8,942,651</u>	<u>\$ 1,191,053</u>

Supplemental cash flow information related to leases where we are the lessee is as follows:

	Six Months Ended June 30,	
	2022	2021
Cash paid for amounts included in the measurement of lease liabilities:		
Leased assets obtained in exchange for finance lease liabilities	6,022,694	—
Leased assets obtained in exchange for operating lease liabilities	5,024,284	—

8. STOCK-BASED COMPENSATION

The Company maintains, as approved by the board of directors, the 2017 Incentive Stock Plan and the 2019 Incentive Stock Plan (the “Plans”) providing for the issuance of stock-based awards to employees, officers, directors or consultants of the Company. Non-qualified stock options may only be granted with an exercise price equal to the market value of the Company’s common stock on the grant date. Awards under the Plan may be either vested or unvested options, or unvested restricted stock. The Plans have authorized 13.0 million shares for issuance of stock-based awards. As of June 30, 2022 there were approximately 2.0 million shares available for issuance of future stock awards under the Plans.

Stock-based compensation expense

The following table summarizes stock-based compensation expense:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2022	2021	2022	2021
Stock options	\$ 254,585	\$ 21,210	\$ 486,963	\$ 91,622
Restricted stock awards	2,226,865	1,118,703	3,906,109	1,940,719
Performance-based restricted stock awards	810,959	—	1,249,630	—
Total stock-based compensation expense	<u>\$ 3,292,409</u>	<u>\$ 1,139,913</u>	<u>\$ 5,642,702</u>	<u>\$ 2,032,341</u>

Stock options

A summary of stock option activity for the six months ended June 30, 2022 is as follows:

	Number of Options	Weighted Average Exercise Price per Option	Weighted Average Remaining Contractual Life (Years)
Balance, December 31, 2021	495,836	\$ 6.80	6.5
Exercised	(51,198)	1.36	
Forfeited	(625)	22.30	
Balance, June 30, 2022	<u>444,013</u>	\$ 7.45	6.7
Number of options exercisable at June 30, 2022	<u>188,988</u>	\$ 4.03	3.2

As of June 30, 2022, unrecognized compensation expense was \$2.1 million for unvested options which is expected to be recognized over the next 2.2 years.

Restricted stock awards

A summary of restricted stock award activity for the six months ended June 30, 2022 is as follows:

	Number of Unvested Shares	Weighted Average Grant Date Fair Value per Share
Balance, December 31, 2021	1,617,192	\$ 9.33
Granted	2,829,992	3.10
Vested	(282,504)	9.06
Forfeited	(145,016)	6.05
Balance, June 30, 2022	<u>4,019,664</u>	\$ 5.07

As of June 30, 2022, unrecognized compensation expense was \$17.4 million for unvested restricted stock awards which is expected to be recognized over the next 2.4 years.

Performance share units ("PSUs")

On February 23, 2022, the Company issued 0.9 million PSUs to certain executives. The PSUs will vest upon achievement of the performance objectives over a performance period ending December 31, 2024 as defined in the agreement. Fifty percent of the PSUs vest based upon the Company's total shareholder return as compared to a group of peer companies ("TSR PSUs"), and fifty percent of the PSUs vest based upon the Company's performance on certain measures including a cumulative adjusted EBITDA target ("EBITDA PSUs"). Depending on the actual achievement on the performance objectives, the grantee may earn between 0% and 200% of the target PSUs.

A summary of the activity for PSU awards with total shareholder return performance objectives for the six months ended June 30, 2022 is as follows:

	Number of Unvested Shares	Weighted Average Grant Date Fair Value per Share
Balance, December 31, 2021	306,197	\$ 11.79
Granted	454,832	11.79
Forfeited	(11,138)	11.79
Balance, June 30, 2022	<u>749,891</u>	<u>\$ 11.79</u>

The grant date fair value of \$11.79 per TSR PSU was estimated using a Monte-Carlo simulation model using a volatility assumption of 17% and risk-free interest rate of 0.69%.

As of June 30, 2022, unrecognized compensation expense was \$7.8 million for unvested TSR PSUs, which is expected to be recognized over the next 2.5 years.

A summary of the PSU awards with cumulative adjusted EBITDA targets for the six months ended June 30, 2022 is as follows:

	Number of Unvested Shares
Balance, December 31, 2021	—
Granted	454,822
Forfeited	(11,138)
Balance, June 30, 2022	<u>443,684</u>

The fair value of performance share units is calculated based on the stock price on the date of grant. The stock-based compensation expense recognized each period is dependent upon our estimate of the number of shares that will ultimately vest based on the achievement of EBITDA-based performance conditions. Future stock-based compensation expense for unvested EBITDA PSUs will be based on the fair value of the awards as of the grant date, which has not yet occurred, as the cumulative adjusted EBITDA target condition is not yet defined.

9. **INCOME TAXES**

As of June 30, 2022 and December 31, 2021, the Company's deferred tax liability was zero. Cumulative deferred tax assets are fully reserved as there is not sufficient evidence to conclude that it is more likely than not the deferred tax assets are realizable. No current liability for federal or state income taxes has been included in these Condensed Consolidated Financial Statements due to the loss for the periods.

10. EARNINGS PER SHARE

Basic loss per share of common stock is calculated by dividing net loss by the weighted-average shares outstanding for the period. Potentially dilutive shares, which are based on the weighted-average shares of common stock underlying outstanding stock-based awards and warrants using the treasury stock method, and convertible notes using the if-converted method, are included when calculating the diluted net loss per share of common stock when their effect is dilutive.

The following table presents the potentially dilutive shares that were excluded from the computation of diluted net loss per share of common stock, because their effect was anti-dilutive:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2022	2021	2022	2021
Stock-based awards and warrants	6,765,581	3,827,804	6,765,581	3,827,804
Convertible notes ⁽¹⁾	7,833,666	5,667,328	7,833,666	5,667,328

⁽¹⁾Represents shares issued in exchange of convertible notes in April 2022. See Note 5 *Debt*, for additional information regarding shares issued subsequent to the date of the Condensed Consolidated Financial Statements.

11. RECENT ACCOUNTING PRONOUNCEMENTS

Accounting Standards Recently Adopted

In August 2020, the Financial Accounting Standards Board issued Accounting Standards Update (“ASU”) 2020-06, *Accounting for Convertible Instruments and Contracts in an Entity’s Own Equity*. The ASU simplifies the accounting for certain convertible instruments, amends the guidance on derivative scope exceptions for contracts in an entity’s own equity and requires the use of the if-converted method for calculating diluted earnings per share. The ASU removes separation models for convertible debt with a cash conversion feature. Such convertible instruments will be accounted for as a single liability measured at amortized cost. The Company adopted the ASU as of January 1, 2022. The adoption of this guidance did not have a material impact on the Company’s financial condition and results of operations.

12. OTHER TRANSACTION

On October 31, 2019, the Company and ST Engineering Hackney, Inc. (“Hackney”) entered into an Asset Purchase Agreement to purchase certain assets and assume certain liabilities of Hackney. Upon execution of the agreement, the Company deposited approximately 2.3 million shares of its common stock into an escrow account that were to be released to Hackney if certain conditions were met.

The Company believes that such conditions were not met and does not expect to make further payments to Hackney in connection with the Asset Purchase Agreement. Further, the Company expects the shares of its common stock to be released from escrow in 2022.

13. FAIR VALUE MEASUREMENTS

Accounting guidance on fair value measurements for certain financial assets and liabilities requires that assets and liabilities carried at fair value be classified and disclosed in one of the following three categories:

Level 1 — Quoted market prices in active markets for identical assets or liabilities.

Level 2 — Observable market-based inputs or unobservable inputs that are corroborated by market data.

Level 3 — Unobservable inputs reflecting the reporting entity's own assumptions or external inputs from inactive markets.

A financial asset or liability's classification within the hierarchy is determined based on the lowest level of input that is significant to the fair value measurement. Assets and liabilities measured at fair value and fair value measurement level were as follows:

	June 30, 2022				December 31, 2021			
	Fair Value	Level 1	Level 2	Level 3	Fair Value	Level 1	Level 2	Level 3
Liabilities								
Convertible notes	\$ —	\$ —	\$ —	\$ —	\$ 24,705,000	\$ —	\$ —	\$ 24,705,000
Total liabilities at fair value	\$ —	\$ —	\$ —	\$ —	\$ 24,705,000	\$ —	\$ —	\$ 24,705,000

Convertible Notes

The Company's convertible notes were measured at fair value using Level 3 inputs upon issuance and at each reporting date. Considerable judgment was required in interpreting market data to develop the estimates of fair value. Accordingly, the Company's estimates are not necessarily indicative of the amounts that the Company, or holders of the instruments, could have realized in a current market exchange. Significant assumptions used in the fair value model included estimates of the redemption dates, credit spreads and the market price and volatility of the Company's common stock. The use of different assumptions and/or estimation methodologies could have had a material effect on the estimated fair values.

The Company recognized changes in fair value of the convertible notes related to changes in credit spread, if any, in Other Comprehensive Loss and the remaining changes in fair value in Interest Expense (Income).

14. COMMITMENTS AND CONTINGENCIES

General Matters

The Company is party to various negotiations and legal proceedings arising in the normal course of business. The Company provides reserves for these matters when a loss is probable and reasonably estimable. The Company does not disclose a range of potential loss because the likelihood of such a loss is remote. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the Company's financial position, results of operations, cash flows or liquidity.

Federal Motor Vehicle Safety Standards ("FMVSS") Certification and Other Regulatory Matters

On September 22, 2021, we announced the Company decided to suspend deliveries of C-1000 vehicles and recall the vehicles we had already delivered to customers. The new leadership team determined additional testing and modifications to existing vehicles are required to bring the C-1000 vehicles into full compliance with FMVSS. The Company further announced we filed a report with the National Highway Traffic Safety Administration ("NHTSA") regarding the need for additional testing and vehicle modifications to bring our C-1000 vehicles into full compliance with FMVSS. We indicated our previous statements related to the C-1000's compliance with NHTSA standards cannot be relied upon and so notified the Securities and Exchange Commission. We also disclosed we identified a number of enhancements to our production process and the design of the C-1000 vehicles to address customer feedback, primarily related to payload capacity.

The certification testing was completed in February 2022. Upon completion of this review, the C-1000 platform was determined to be eligible for certification and reintroduction as a limited production vehicle with constrained cargo capacity. In 2022, Workhorse decided to repurchase all of the C-1000 vehicles involved in the recall announced in September 2021 instead

of repairing them and so notified NHTSA. Because the Company repurchased all of the C-1000 vehicles involved in the recall, it has no further obligations under the recall.

Due to the uncertainties and many variables involved in NHTSA matters, we cannot estimate the ultimate resolution of this matter and whether it will have a material adverse effect on the Company's financial position, results of operations, cash flows or liquidity. We cooperated with NHTSA with respect to the now-completed recall that was announced in September 2021. However, we cannot assure that NHTSA or other government authorities will not attempt to impose potentially significant fines and penalties in response to the recall.

On October 19 and November 1, 2021, the Company received letters from the SEC requesting that it voluntarily provide information relating to (a) the events and trading in its securities leading up to the announcement of the award of a contract by the U.S. Postal Service (the "USPS") for the manufacture of a postal service vehicle fleet and (b) recognition of revenue, if any, related to purchases of vehicles by certain of the Company's customers. On November 5, 2021, the Department of Justice ("DOJ") orally informed the Company that it had a related open investigation covering the Company. The Company has not received any subpoena or other request for documents or other information from the DOJ with respect to this investigation. On May 9, 2022, the Company received a letter from the SEC requesting that it voluntarily provide information relating to certain customer sales and customer complaints. The Company is cooperating with the SEC and DOJ investigations. At this point, the Company cannot predict the eventual scope, duration, or outcome of these matters.

During the second quarter of 2021, the Company became aware of a regulatory compliance issue related to our E-Series vehicles that will require retrofitting of such vehicles. Management continues to work on remediation of this issue and does not expect it to have a material impact on the Company's financial condition and operations. Due to the uncertainties and many variables involved in regulatory matters, we cannot estimate the ultimate resolution of this issue and actual results may differ from our expectations.

Legal Proceedings

Securities Litigation

The Company, Duane Hughes, Steve Schrader, Robert Willison and Gregory Ackerson are defendants in a putative class action (the "Securities Class Action") brought in the Central District of California (Case No.2:21-cv-02072) on behalf of purchasers of the Company's securities from March 10, 2020 through May 10, 2021. The amended complaint in this action, filed by lead plaintiff, Timothy M. Weis, on July 16, 2021, alleges the defendants violated the federal securities laws by intentionally or recklessly making material misrepresentations and/or omissions regarding the Company's participation in the bidding process to manufacture the new fleet of USPS next generation delivery vehicles, the prospect of the USPS awarding the contract to Workhorse given alleged deficiencies in Workhorse's proposal, the Company's manufacturing abilities generally and the Company's nonbinding "backlog" in its vehicles. Lead plaintiff seeks certification of a class and monetary damages in an indeterminate amount. The Court denied the Company's motion to dismiss in substantial part, and the Securities Class Action is currently scheduled to begin trial on March 19, 2024. The parties are now engaged in discovery. The Company believes the Securities Class Action is without merit. The parties have scheduled a mediation of the Securities Class Action for August 23, 2022 and there can be no assurance as to the results, if any, of the mediation.

Shareholder Derivative Litigation

A total of seven nearly identical derivative actions were originally filed for breach of fiduciary duty and unjust enrichment against Duane Hughes, Steve Schrader, Stephen Fleming, Robert Willison, Anthony Furey, Gregory Ackerson, H. Benjamin Samuels, Raymond J. Chess, Harry DeMott, Gerald B. Budde, Pamela S. Mader, Michael L. Clark and Jacqueline A. Dedo in state court in Nevada and federal courts in Ohio and California. In these actions, the plaintiffs allege the defendants breached their fiduciary duties by allowing or causing the Company to violate the federal securities laws as alleged in the Securities Class Action discussed above and by selling Company stock and receiving other compensation while allegedly in possession of material non-public information about the prospect of the USPS awarding the contract to an electric vehicle manufacturer given electrifying the USPS's entire fleet allegedly would be impractical and expensive. The plaintiffs seek damages and disgorgement in an indeterminate amount.

The three derivative cases filed in the Central District of California were consolidated into a single action on June 21, 2021 (under Case No. 2:21-cv-04202). On April 18, 2022, the plaintiffs filed their consolidated amended complaint in the consolidated action. On June 2, 2022, the defendants filed motions to dismiss, which the Company joined in with respect to the arguments related to the plaintiffs' lack of standing, as well as a motion to stay the case pending resolution of the Securities Class Action. In accordance with the Court's Scheduling Order of June 22, 2022, plaintiffs filed their opposition to the motion

to stay on July 20, 2022 and have until August 17, 2022 to file their oppositions to the motions to dismiss. The hearing on all of these motions will be on October 17, 2022.

A fourth case, originally filed in the Southern District of Ohio, was transferred to the Central District of California on November 5, 2021 (under Case No. 2:21-cv-08734) and assigned to the same judge who presides over the Securities Class Action and the consolidated Central District of California derivative action. Plaintiffs filed their first amended complaint on May 2, 2022. On July 22, 2022, the Court granted the Defendants' motion to stay the action pending resolution of the Securities Class Action.

Two further actions, both filed in the Eight Judicial District Court of the State of Nevada in and for Clark County, were consolidated on January 7, 2022 (under Case No. A-21-833050-B). On January 24, 2022, the plaintiffs in the consolidated action in Nevada state court filed their consolidated amended complaint, which was also revised to include the additional allegations made in the Amended Complaint in the Securities Class Action discussed above. On March 22, 2022, the defendants and the Company filed a motion to stay the Nevada state court consolidated action, and the defendants filed motions to dismiss the consolidated action, which the Company joined in with respect to the arguments related to the plaintiffs' lack of standing. Plaintiffs' oppositions to these motions were filed on June 3, 2022. Defendants' replies were filed on July 15, 2022. On August 4, 2022, the court denied the defendants' motion to dismiss the consolidated action, but granted the defendants' motion to stay the action pending resolution of the Securities Class Action.

The most recent shareholder derivative action was filed on June 22, 2022 in the Nevada District Court under Case No. 2:22-cv-00980. The Company's response is currently due on September 13, 2022.

Although these actions purport to seek recovery on behalf of the Company, the Company will incur certain expenses due to indemnification and advancement obligations with respect to the defendants. The Company understands that defendants believe these actions are without merit and intends to support them as they pursue all legal avenues to defend themselves fully.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

We are a technology company with a vision to pioneer the transition to zero-emission commercial vehicles. Our primary focus is to provide sustainable and cost-effective solutions to the commercial transportation sector. We design and manufacture all-electric delivery trucks and drone systems, including the technology that optimizes the way these vehicles operate. We are focused on our core competency of bringing our electric delivery vehicle platforms to market.

Recent Developments

GreenPower Motor Company Inc. Supply Agreement

In February 2022, we entered into a multi-year vehicle purchase and supply agreement (the "Supply Agreement") with GreenPower Motor Company Inc. ("GreenPower") to facilitate the manufacturing and delivery of medium-duty Class 4 step vans into the North American market. Under the Supply Agreement, we will purchase 1,500 base vehicles from GreenPower, and complete the manufacturing process on the base vehicles. We will market two versions of the vehicle, a cab chassis version known as the W4 CC and a complete vehicle with a step van body, known as the W750, to customers in the United States and Canada. The W4 CC will have a payload capacity of 7,000 pounds and the W750 will have a payload capacity of 5,000 pounds. Both the W4 CC and the W750 will feature up to 150 miles of all-electric range. Delivery of base vehicles began in July of 2022.

Securities Exchange Agreement

In April 2022, we entered into a securities exchange agreement to exchange the remaining \$27.5 million in aggregate principal of our convertible notes for approximately 7.8 million shares of our common stock. The number of shares issued was calculated by dividing \$29.4 million, which represents 107% of the principal amount of the notes, plus \$0.3 million of interest accrued on the notes, by the average of the daily volume weighted average price for the 10 days immediately preceding April 21, 2022. We recognized a loss of \$1.8 million in the first quarter of 2022, which includes a \$0.4 million adjustment to the fair value of the convertible notes to the value of the shares issued under the exchange and a \$1.4 million adjustment related to the realization of the amount previously recognized in Accumulated Other Comprehensive Loss. The total loss was recorded in Interest Expense for the six months ended June 30, 2022.

Subsequent to the exchange, we have no convertible notes outstanding, and the indenture and related security agreement under which the 2024 Notes were issued have been terminated.

Recent Trends and Market Conditions

COVID-19. The impact of COVID-19, including pandemic fears and market downturns, and restrictions on business and individual activities, has created significant volatility in the global economy. Recent COVID-19 outbreaks in certain regions have continued to cause intermittent disruptions to our supply chain and, although we have been relatively successful in navigating the impact of the COVID-19 pandemic, we have previously been affected by temporary manufacturing closures. As of June 30, 2022, our locations and most of our primary suppliers are in operation and we continue to work through supplier constraints as a result of the COVID-19 pandemic, as well as other supply chain difficulties.

Commodities. Prices for commodities remain volatile, and we expect to experience price increases for base metals and raw materials that are used in batteries for electric vehicles (e.g., lithium, cobalt, and nickel) as well as steel, aluminum and other material inputs. Global demand and differences in output across sectors as a result of the COVID-19 pandemic have generated divergence in price movements across different commodities. We expect the net impact on us overall will be higher material costs. The help ensure supply of raw materials for critical components (such as batteries), we have engaged in multi-year sourcing agreements.

Inflation. Inflation has significantly risen during the first half of 2022, resulting from both supply and demand imbalances as economies continue to recover from the COVID-19 pandemic as well as the impact on the availability and cost of energy and other commodities resulting from Russia's invasion of Ukraine in February 2022, which is ongoing. We are seeing a near-term impact on our business due to inflationary pressure. In an effort to dampen inflationary pressures, central banks have started to raise interest rates which will likely raise the cost of any financing the Company may undertake in the future.

Results of Operations

Our condensed consolidated statements of operations data are as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2022	2021	2022	2021
Sales, net of returns and allowances	\$ 12,555	\$ 1,202,876	\$ 26,854	\$ 1,723,936
Cost of sales	3,020,204	14,796,130	6,943,555	21,021,429
Gross loss	(3,007,649)	(13,593,254)	(6,916,701)	(19,297,493)
Operating expenses				
Selling, general and administrative	13,030,143	7,005,537	24,940,402	13,891,367
Research and development	5,027,061	2,123,860	9,038,995	5,987,575
Total operating expenses	18,057,204	9,129,397	33,979,397	19,878,942
Loss from operations	(21,064,853)	(22,722,651)	(40,896,098)	(39,176,435)
Interest expense (income), net	95,419	10,478,717	2,318,709	(4,441,756)
Other loss	—	11,699,666	—	148,305,618
Loss before benefit for income taxes	(21,160,272)	(44,901,034)	(43,214,807)	(183,040,297)
Benefit for income taxes	—	(1,281,947)	—	(18,914,439)
Net loss	\$ (21,160,272)	\$ (43,619,087)	\$ (43,214,807)	\$ (164,125,858)

Sales, net of returns and allowances

Sales, net of returns and allowances for the three months ended June 30, 2022 and 2021 were \$12,555 and \$1,202,876, respectively. Sales, net of returns and allowances for the six months ended June 30, 2022 and 2021 were \$26,854 and \$1,723,936, respectively. The decrease in net sales was primarily due to a decrease in volume of automotive vehicle sales.

Cost of sales

Cost of sales for the three months ended June 30, 2022 and 2021 were \$3.0 million and \$14.8 million, respectively. The decrease in cost of sales was primarily due to a \$6.7 million decrease in inventory write-downs and a \$2.0 million decrease in cost due to a reduction in volume of automotive vehicle sales. Additionally, the decrease in cost of sales was due to a reduction in costs associated with the initial production of the C-Series vehicle platform.

Cost of sales for the six months ended June 30, 2022 and 2021 were \$6.9 million and \$21.0 million, respectively. The decrease in cost of sales was primarily due to a \$6.5 million decrease in inventory write-downs and a \$2.9 million decrease in cost due to a reduction in volume of automotive vehicle sales. Additionally, the decrease in cost of sales was due to a reduction in costs associated with the initial production of the C-Series vehicle platform.

Selling, general and administrative expenses

Selling, general and administrative (“SG&A”) expenses during the three months ended June 30, 2022 and 2021 were \$13.0 million and \$7.0 million, respectively. The increase was primarily driven by an increase of \$4.8 million in employee compensation and related expenses due to increased headcount, non-cash stock-based compensation expense, and the appointments of our new executive leadership team.

SG&A expenses during the six months ended June 30, 2022 and 2021 were \$24.9 million and \$13.9 million, respectively. The increase was primarily driven by an increase of \$7.5 million in employee compensation and related expenses from increased headcount, non-cash stock-based compensation expense, and the appointments of our new executive leadership team. Additionally, there was a \$2.4 million increase in professional and legal services primarily related to litigation. The increases were partially offset by a \$2.5 million decrease in consulting fees as a result of an initiative to reduce reliance on external resources by hiring internal resources.

Research and development expenses

Research and development (“R&D”) expenses during the three months ended June 30, 2022 and 2021 were \$5.0 million and \$2.1 million, respectively. The increase was primarily driven by an increase of \$1.3 million in employee compensation and related expenses due to increased headcount. Additionally, there was a \$1.1 million increase in consulting and prototype expenses related to the continued development of our HorseFly™, W56, and W750 vehicle programs.

R&D expenses during the six months ended June 30, 2022 and 2021 were \$9.0 million and \$6.0 million, respectively. The increase was primarily driven by an increase of \$2.0 million in employee compensation and related expenses due to increased headcount. Additionally, there was a \$0.5 million increase in prototype expenses related to the continued development of our HorseFly™, W56, and W750 vehicle programs.

Net Interest Expense (Income)

Net interest expense (income) is comprised of the following:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2022	2021	2022	2021
Realization of accumulated other comprehensive loss	\$ —	\$ —	\$ 1,402,500	\$ —
Change in fair value of convertible notes and loss on conversion to common stock	—	8,500,000	367,357	(7,000,000)
Contractual interest expense	—	1,977,777	332,707	3,977,777
Gain on forgiveness of PPP Term Note	—	—	—	(1,411,000)
Other	95,419	940	216,145	(8,533)
Total interest expense (income), net	\$ 95,419	\$ 10,478,717	\$ 2,318,709	\$ (4,441,756)

Net interest expense for the three months ended June 30, 2022 and 2021 was \$0.1 million and \$10.5 million, respectively. The decrease in net interest expense was primarily due to a \$8.5 million increase in fair value of the 2024 Notes during the three months ended June 30, 2021, as compared to no changes in fair value during the three months ended June 30, 2022. Additionally, contractual interest expense on the 2024 Notes for the three months ended June 30, 2021 was \$2.0 million, as compared to zero for the three months ended June 30, 2022.

Net interest expense for the six months ended June 30, 2022 was \$2.3 million as compared to \$4.4 million of interest income for the six months ended June 30, 2021. The change in net interest expense (income) was primarily due to a \$7.0 million net decrease in fair value of our convertible notes during the six months ended June 30, 2021, as compared to no changes in fair value during the six months ended June 30, 2022. Additionally, contractual interest expense on the 2024 Notes for the six months ended June 30, 2021 was \$4.0 million, as compared to \$0.3 million for the six months ended June 30, 2022. Further, we recognized a gain of \$1.4 million on the forgiveness of our prior PPP Term Note during the six months ended June 30, 2021.

The changes in expense described above are primarily due to the exchange of the remaining aggregate principal of 2024 Notes for shares of the Company's common stock during the second quarter of 2022. A description of the exchange is contained in Note 5, *Debt*, of the Condensed Consolidated Financial Statements included elsewhere in this Quarterly Report on Form 10-Q.

Other loss

Other loss during the three and six months ended June 30, 2022 was zero. During the three and six months ended June 30, 2021, we recognized a loss of \$11.7 million and \$148.3 million, respectively, attributable to unfavorable changes in fair value of our prior investment in Lordstown Motors Corp (“LMC”).

Benefit for income taxes

Benefit for income taxes during the three and six months ended June 30, 2022 was zero. During the three and six months ended June 30, 2021, we recognized a benefit for income taxes of \$1.3 million and \$18.9 million, respectively, attributable to an increase to the valuation allowance recorded against deferred tax assets due to the sale of our prior investment in LMC and the uncertainty about our ability to utilize our remaining deferred tax assets in future years.

Liquidity and Capital Resources

From inception, we have financed our operations primarily through sales of equity securities and issuance of debt. We have utilized this capital for R&D and to fund designing, building and delivering vehicles to customers and for working capital purposes.

As of June 30, 2022, we had approximately \$140.1 million in cash and cash equivalents, compared to approximately \$201.6 million as of December 31, 2021, resulting in a decrease of \$61.6 million. The decrease was primarily attributable to cash used in operations related to employee and related costs, consulting and professional services, capital expenditures and inventory build.

On March 10, 2022, we entered into an At-The-Market Sales Agreement, which established an at-the-market equity program (the "2022 ATM Program"). Under the 2022 ATM Program, we may offer and sell shares of our common stock having an aggregate sales price of up to \$175.0 million, in amounts and at times determined by management. During the three and six months ended June 30, 2022, we issued 0.1 million shares under the 2022 ATM Program for net proceeds of \$0.2 million, leaving shares of common stock having an aggregate offering price of up to \$174.8 million available for issuance under the 2022 ATM Program.

We believe our existing capital resources will be sufficient to support our current and projected funding requirements for at least the next twelve months, after which time additional funding may be required. However, if market conditions are appropriate, we may raise additional capital during the remainder of 2022, including utilization of our 2022 ATM Program.

Cash Requirements

From time to time in the ordinary course of business, we enter into agreements with vendors for the purchase of components and raw materials to be used in the manufacture of our products. However, due to contractual terms, variability in the precise growth curves of our development and production ramps, and opportunities to renegotiate pricing, we generally do not have binding and enforceable purchase orders under such contracts beyond the short term, and the timing and magnitude of purchase orders beyond such period is difficult to accurately project.

We currently expect our capital expenditures to upgrade our facilities in Indiana, Ohio and Michigan to be between \$15.0 and \$25.0 million in 2022.

As of June 30, 2022, we have no convertible notes outstanding following the Company's exchange of the remaining \$27.5 million in aggregate principal of the 2024 Notes for shares of the Company's common stock during the second quarter of 2022. A description of the exchange is contained in Note 5, *Debt*, of the Condensed Consolidated Financial Statements included elsewhere in this Quarterly Report on Form 10-Q.

As of June 30, 2022, our total minimum future lease payments are \$13.4 million. A description of our lease obligations is contained in Note 7, *Leases*, of the Condensed Consolidated Financial Statements included elsewhere in this Quarterly Report on Form 10-Q.

Sources and Condition of Liquidity

With the exception of contingent and royalty payments we may receive under our existing collaborations, we do not currently have any committed future funding. To the extent we raise additional capital by issuing equity securities, including under the 2022 ATM Program, our stockholders could at that time experience substantial dilution. Any debt financing that we can obtain may include operating covenants that restrict our business.

Our future funding requirements will depend upon many factors, including, but not limited to:

- our ability to acquire or license other technologies we may seek to pursue;
- our ability to manage our growth;
- competing technological and market developments;
- the costs and timing of obtaining, enforcing and defending our patent and other intellectual property rights; and
- expenses associated with any unforeseen litigation.

For the three and six months ended June 30, 2022, we maintained an investment in a bank money market fund. Cash in excess of immediate requirements is invested with regard to liquidity and capital preservation. Wherever possible, we seek to minimize

the potential effects of concentration and degrees of risk. We will continue to monitor the impact of the changes in the conditions of the credit and financial markets to our investment portfolio and assess if future changes in our investment strategy are necessary.

Summary of Cash Flows

	Six Months Ended June 30,	
	2022	2021
Net cash used in operating activities	\$ (55,462,470)	\$ (81,267,644)
Net cash used in investing activities	\$ (5,658,776)	\$ (3,281,213)
Net cash used in financing activities	\$ (465,573)	\$ (69,416)

Cash Flows from Operating Activities

Our cash flows from operating activities are affected by our cash investments to support the business in R&D, manufacturing, selling, general and administration. Our operating cash flows are also affected by our working capital needs to support fluctuations in inventory, personnel expenses, accounts payable and other current assets and liabilities.

During the six months ended June 30, 2022 and 2021, net cash used in operating activities was \$55.5 million and \$81.3 million, respectively. The decrease in net cash used in operations was primarily attributable to a decrease in spend related to the initial production of the C-Series vehicle platform.

Cash Flows from Investing Activities

Cash flows from investing activities and their variability across each period related primarily to capital expenditures, which were \$5.7 million for the six months ended June 30, 2022 and \$3.3 million for the six months ended June 30, 2021. The increase in cash used in operations was primarily attributable to capital expenditures to upgrade our administrative, research, and production facilities.

Cash Flows from Financing Activities

Net cash used in financing activities during the six months ended June 30, 2022 was \$0.5 million, which consisted primarily of payments on financing leases and tax payments related to shares withheld for option exercises and vesting of restricted share awards.

Net cash used in financing activities during the six months ended June 30, 2021 was \$0.1 million, which consisted of proceeds from the exercise of stock options and warrants, and vesting of restricted share awards, net of tax payments related to shares withheld for option exercises and vested stock.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that are material to investors.

Critical Accounting Estimates

A discussion of our critical accounting estimates is contained in our Annual Report on Form 10-K for the year ended December 31, 2021, under the caption "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Recent Accounting Pronouncements

A description of recently issued and adopted accounting pronouncements is contained in Note 11, *Recent Accounting Pronouncements*, of the Condensed Consolidated Financial Statements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

For a discussion of our quantitative and qualitative disclosures about market risk, see “Quantitative and Qualitative Disclosures About Market Risks” included in our Annual Report on Form 10-K for the year ended December 31, 2021, under the caption “Management’s Discussion and Analysis of Financial Condition and Results of Operations.” There have been no material changes to the information provided in our Annual Report on Form 10-K for the year ended December 31, 2021.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Pursuant to Rules 13a-15(b) and 15-d-15(b) under the Securities Exchange Act of 1934, as amended (“Exchange Act”), we evaluated, with the participation of management, including our Chief Executive Officer and Chief Financial Officer, the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. The term “disclosure controls and procedures”, as defined under Rules 13a-15(e) and 15d-15(e) under the Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC’s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company’s management, including its principal executive and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

Our management, with the participation of our Principal Executive Officer and Principal Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on such evaluation, our Principal Executive Officer and Principal Financial Officer have concluded that, as of the end of the covered by this Quarterly Report, our disclosure controls and procedures were effective.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting (as that term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during the three months ended June 30, 2022 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

For a description of certain material legal proceedings, please see Note 14, *Commitments and Contingencies*, to the consolidated financial statements included elsewhere in this Quarterly Report on Form 10-Q.

ITEM 1A. RISK FACTORS

For a detailed discussion of risk factors affecting us, see “Part I – Item 1A. Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2021. Except as set forth below, there have been no material changes in the current period regarding our risk factors.

Increased economic and political instability, including as a result of inflationary pressures, rising interest rates and the conflict between Russia and Ukraine, may adversely affect our business, financial condition, and results of operations.

Recent events that are impacting global and local business conditions include the ongoing effects of COVID-19, the semiconductor shortage, other supply chain challenges, and the effects of inflation and rising interest rates. We are experiencing challenges and increases in costs for logistics and supply chains, such as increased port congestion, intermittent supplier delays, and volatility in prices of commodities such as base metals and raw materials used in batteries (e.g., lithium, cobalt, and nickel). In addition, we are experiencing varying levels of inflation resulting in part from various supply chain disruptions, increased shipping and transportation costs, increased raw material and labor costs, and other disruptions caused by the COVID-19 pandemic and general economic conditions. Further unfavorable conditions such as a general slowdown of the U.S. economy, uncertainty and volatility in the financial markets, uncertainty or volatility in commodity prices or additional inflationary factors and rising interest rates could result in higher operating costs and expenses for our Company and could make it more difficult and expensive for us to obtain financing.

In addition, in late February 2022, Russia launched a military attack on Ukraine. In response, many countries have imposed sanctions against Russian businesses and citizens. Although we do not have operations outside the United States, the potentially destabilizing effects of the Russia and Ukraine conflict, or potential for a larger conflict, could have other effects on our business.

In addition, these factors could heighten many of our known risks described in Part I, Item 1A. “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2021.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

Exhibit No.	Description
+10.1*	2017 Incentive Stock Plan
10.2	Form of Securities Exchange Agreement (incorporated by reference to the Company's Current Report on Form 8-K filed with the Securities and Exchange Commission April 6, 2022)
31.1*	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1*	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2*	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS	Inline XBRL INSTANCE DOCUMENT
101.SCH	Inline XBRL Taxonomy Extension Schema Document
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	Inline XBRL Taxonomy Extension Labels Linkbase Document
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase Document
104	Inline XBRL Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101)

* Filed herewith.

+ Indicates a management contract or compensatory arrangement.

SIGNATURES

Pursuant to the requirements 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.

Dated: August 9, 2022

WORKHORSE GROUP INC.

By: /s/ Richard Dauch
Name: Richard Dauch
Title: Chief Executive Officer
(Principal Executive Officer)

Dated: August 9, 2022

By: /s/ Robert M. Ginnan
Name: Robert M. Ginnan
Title: Chief Financial Officer
(Principal Financial Officer)

Dated: August 9, 2022

By: /s/ Gregory T. Ackerson
Name: Gregory T. Ackerson
Title: Chief Accounting Officer
(Principal Accounting Officer)

**WORKHORSE GROUP INC.
2017 INCENTIVE STOCK PLAN**

This WORKHORSE GROUP INC. 2017 Incentive Stock Plan (the "**Plan**") is designed to retain directors, executives, selected employees and consultants and reward them for making major contributions to the success of the Company. These objectives are accomplished by making long-term incentive awards under the Plan thereby providing Participants with a proprietary interest in the growth and performance of the Company.

1. Definitions.

- (a) "**Board**" - The Board of Directors of the Company.
- (b) "**Cause**" means (a) embezzlement or misappropriation of funds; (b) conviction of, or entry of a plea of *nolo contendere* to, a felony involving moral turpitude; (c) commission of material acts of dishonesty, fraud, or deceit; (d) breach of any material provisions of any employment agreement, confidentiality agreement or invention assignment agreement; (e) habitual or willful neglect of duties; (f) breach of fiduciary duty; or (g) material violation of any other duty whether imposed by law or the Board.
- (c) "**Code**" - The Internal Revenue Code of 1986, as amended from time to time.
- (d) "**Committee**" - The Compensation Committee of the Company's Board, or such other committee of the Board that is designated by the Board to administer the Plan, composed of not less than two members of the Board who are disinterested persons, as contemplated by Rule 16b-3 ("**Rule 16b-3**") promulgated under the Securities Exchange Act of 1934, as amended (the "**Exchange Act**").
- (e) "**Company**" - WORKHORSE GROUP INC. and its subsidiaries including subsidiaries of subsidiaries.
- (f) "**Exchange Act**" - The Securities Exchange Act of 1934, as amended from time to time.
- (g) "**Fair Market Value**" - The fair market value of the Company's issued and outstanding Stock as determined in good faith by the Board or Committee.
- (h) "**Grant**" - The grant of any form of stock option, stock award, or stock purchase offer, whether granted singly, in combination or in tandem, to a Participant pursuant to such terms, conditions and limitations as the Committee may establish in order to fulfill the objectives of the Plan.
- (i) "**Grant Agreement**" - An agreement between the Company and a Participant that sets forth the terms, conditions and limitations applicable to a Grant.

- (j) "**Option**" - Either an Incentive Stock Option, in accordance with Section 422 of Code, or a Nonstatutory Option, to purchase the Company's Stock that may be awarded to a Participant under the Plan. A Participant who receives an award of an Option shall be referred to as an "**Optionee**."
 - (k) "**Participant**" - A director, officer, employee or consultant of the Company to whom an Award has been made under the Plan.
 - (l) "**Restricted Stock Purchase Offer**" - A Grant of the right to purchase a specified number of shares of Stock pursuant to a written agreement issued under the Plan.
 - (m) "**Securities Act**" - The Securities Act of 1933, as amended from time to time.
 - (n) "**Stock**" - Authorized and issued or unissued shares of common stock of the Company.
 - (o) "**Stock Award**" - A Grant made under the Plan in stock, denominated in units of stock or denominated in some other method reflecting an increase in value of stock or some other security of the Company, for which the Participant is not obligated to pay additional consideration.
2. Administration. The Plan shall be administered by the Board, provided however, that the Board may delegate such administration to the Committee. Subject to the provisions of the Plan, the Board and/or the Committee shall have authority to (a) grant, in its discretion, Incentive Stock Options in accordance with Section 422 of the Code, or Nonstatutory Options, Stock Awards or Restricted Stock Purchase Offers; (b) determine in good faith the fair market value of the Stock covered by any Grant; (c) determine which eligible persons shall receive Grants and the number of shares, restrictions, terms and conditions (including performance terms and conditions or market criteria) to be included in such Grants; (d) construe and interpret the Plan; (e) promulgate, amend and rescind rules and regulations relating to its administration, and correct defects, omissions and inconsistencies in the Plan or any Grant; (f) consistent with the Plan and with the consent of the Participant, as appropriate, amend any outstanding Grant or amend the exercise date or dates thereof; (g) determine the duration and purpose of leaves of absence which may be granted to Participants without constituting termination of their employment for the purpose of the Plan or any Grant; and (h) make all other determinations necessary or advisable for the Plan's administration. The interpretation and construction by the Board of any provisions of the Plan or selection of Participants shall be conclusive and final. No member of the Board or the Committee shall be liable for any action or determination made in good faith with respect to the Plan or any Grant made thereunder.
3. Eligibility; Cancellation.
- (a) General: The persons who shall be eligible to receive Grants shall be directors, officers, employees or consultants to the Company. The term consultant shall mean any person, other than an employee, who is engaged by the Company to render services and is compensated for such services. An Optionee may hold more than one Option. Any issuance of a Grant to an officer or director of the Company subsequent to the first registration of any of the securities of the Company under the Exchange Act shall comply with the requirements of Rule 16b-3.

- (b) Incentive Stock Options: Incentive Stock Options may only be issued to employees of the Company. Incentive Stock Options may be granted to officers or directors, provided they are also employees of the Company. Payment of a director's fee shall not be sufficient to constitute employment by the Company.

The Company shall not grant an Incentive Stock Option under the Plan to any employee if such Grant would result in such employee holding the right to exercise for the first time in any one calendar year, under all Incentive Stock Options granted under the Plan or any other plan maintained by the Company, with respect to shares of Stock having an aggregate fair market value, determined as of the date of the Option is granted, in excess of \$100,000. Should it be determined that an Incentive Stock Option granted under the Plan exceeds such maximum for any reason other than a failure in good faith to value the Stock subject to such option, the excess portion of such option shall be considered a Nonstatutory Option. To the extent the employee holds two (2) or more such Options which become exercisable for the first time in the same calendar year, the foregoing limitation on the exercisability of such Option as Incentive Stock Options under the Federal tax laws shall be applied on the basis of the order in which such Options are granted. If, for any reason, an entire Option does not qualify as an Incentive Stock Option by reason of exceeding such maximum, such Option shall be considered a Nonstatutory Option.

- (c) Nonstatutory Option: The provisions of the foregoing Section 3(b) shall not apply to any Option designated as a "Nonstatutory Option" or which sets forth the intention of the parties that the Option be a Nonstatutory Option.
- (d) Stock Awards and Restricted Stock Purchase Offers: The provisions of this Section 3(b) shall not apply to any Stock Award or Restricted Stock Purchase Offer under the Plan.
- (e) Cancellation and Rescission of Grants: Unless an agreement with a directors, officers, employees or consultants specifies otherwise, the Board or Committee, as applicable, may cancel any unexpired, unpaid, or deferred Grants at any time if the Optionee or Participant is not in compliance with all other applicable provisions of its agreement pertaining to the Grant and/or the Plan.

Upon exercise, payment or delivery pursuant to a Grant, the Optionee or Participant shall certify on a form acceptable to the Board that he or she is in compliance with the terms and conditions of the Plan. Failure to comply with all of the provisions of this Section 3(e) prior to, or during the six months after, any exercise, payment or delivery pursuant to a Grant shall cause such exercise, payment or delivery to be rescinded. The Company shall notify the Optionee or Participant in writing of any such rescission within two years after such exercise, payment or delivery. Within ten days after receiving such a notice from the Company, the Optionee or Participant shall pay to the Company the amount of any gain realized or payment received as a result of the rescinded exercise, payment or delivery pursuant to a Grant. Such payment shall be made either in cash or by returning to the Company the number of shares of Stock that the Optionee or Participant received in connection with the rescinded exercise, payment or delivery.

4. Stock.

- (a) Authorized Stock: Stock subject to Grants may be either unissued or reacquired Stock.
- (b) Number of Shares: Subject to adjustment as provided in Section 5(i) of the Plan, the total number of shares of Stock which may be purchased or granted directly by Options, Stock Awards or Restricted Stock Purchase Offers, or purchased indirectly through exercise of Options granted under the Plan shall not exceed 5,000,000. If any Grant shall for any reason terminate or expire, any shares allocated thereto but remaining unpurchased upon such expiration or termination shall again be available for Grants with respect thereto under the Plan as though no Grant had previously occurred with respect to such shares. Any shares of Stock issued pursuant to a Grant and repurchased pursuant to the terms thereof shall be available for future Grants as though not previously covered by a Grant.
- (c) Reservation of Shares: The Company shall reserve and keep available at all times during the term of the Plan such number of shares as shall be sufficient to satisfy the requirements of the Plan. If, after reasonable efforts, which efforts shall not include the registration of the Plan or Grants under the Securities Act, the Company is unable to obtain authority from any applicable regulatory body, which authorization is deemed necessary by legal counsel for the Company for the lawful issuance of shares hereunder, the Company shall be relieved of any liability with respect to its failure to issue and sell the shares for which such requisite authority was so deemed necessary unless and until such authority is obtained.
- (d) Application of Funds: The proceeds received by the Company from the sale of Stock pursuant to the exercise of Options or rights under Stock Purchase Agreements will be used for general corporate purposes.

(e) No Obligation to Exercise: The issuance of a Grant shall impose no obligation upon the Participant to exercise any rights under such Grant.

5. Terms and Conditions of Options. Options granted hereunder shall be evidenced by agreements between the Company and the respective Optionees, in such form and substance as the Board or Committee shall from time to time approve. Option agreements need not be identical, and in each case may include such provisions as the Board or Committee may determine, but all such agreements shall be subject to and limited by the following terms and conditions:

(a) Number of Shares: Each Option shall state the number of shares to which it pertains.

(b) Exercise Price: Each Option shall state the exercise price, which shall be determined as follows:

(i) Any Incentive Stock Option granted to a person who at the time the Option is granted owns (or is deemed to own pursuant to Section 424(d) of the Code) stock possessing more than ten percent (10%) of the total combined voting power or value of all classes of stock of the Company ("**Ten Percent Holder**") shall have an exercise price of no less than 110% of the Fair Market Value of the Stock as of the date of grant; and

(ii) Incentive Stock Options granted to a person who at the time the Option is granted is not a Ten Percent Holder and Nonstatutory Options shall have an exercise price of no less than 100% of the Fair Market Value of the Stock as of the date of grant.

For the purposes of this Section 5(b), Fair Market Value, unless otherwise required by any applicable provision of the Code or any regulations issued thereunder, means, as of any given date: (i) if the common stock is listed on a national securities exchange, the closing price of the common stock in the principal trading market for the common stock on such date, as reported by the exchange (or on the last preceding trading date if such security was not traded on such date); (ii) if the common stock is not listed on a national securities exchange, but is traded in the over-the-counter market, the average of the bid and asked prices on such date, as reported by the OTC Bulletin Board or the OTC Markets Inc. or similar publisher of such quotations; and (iii) if the fair market value of the common stock cannot be determined pursuant to clause (i) or (ii) above or if there is no or limited trading volume or limited liquidity in the common stock as determined by the Board in its sole discretion, the Fair Market Value shall be determined by the Board, which determination shall be conclusive and binding.

(c) Medium and Time of Payment: The exercise price shall become immediately due upon exercise of the Option and shall be paid in cash or check made payable to the Company. Should the Company's outstanding Stock be registered under Section 12(g) of the Exchange Act at the time the Option is exercised, then the exercise price may also be paid as follows:

(i) in shares of Stock held by the Optionee for the requisite period necessary to avoid a charge to the Company's earnings for financial reporting purposes and valued at Fair Market Value on the exercise date, or

(ii) through a special sale and remittance procedure pursuant to which the Optionee shall concurrently provide irrevocable written instructions (a) to a Company designated brokerage firm to effect the immediate sale of the purchased shares and remit to the Company, out of the sale proceeds available on the settlement date, sufficient funds to cover the aggregate exercise price payable for the purchased shares plus all applicable Federal, state and local income and employment taxes required to be withheld by the Company by reason of such purchase and (b) to the Company to deliver the purchased shares directly to such brokerage firm in order to complete the sale transaction.

At the discretion of the Board, exercisable either at the time of Option grant or of Option exercise, the exercise price may also be paid (i) by Optionee's delivery of a promissory note in form and substance satisfactory to the Company and permissible under applicable securities rules and bearing interest at a rate determined by the Board in its sole discretion, but in no event less than the minimum rate of interest required to avoid the imputation of compensation income to the Optionee under the Federal tax laws, or (ii) in such other form of consideration permitted by the State of Nevada corporations law as may be acceptable to the Board.

- (d) Term and Exercise of Options: Any Option granted to an employee of the Company shall become exercisable over a period of no longer than five (5) years and no less than twenty percent (20%) of the shares covered thereby shall become exercisable annually unless the Board determines otherwise. No Option shall be exercisable, in whole or in part, prior to one (1) year from the date it is granted unless the Board shall specifically determine otherwise, as provided herein. In no event shall any Option be exercisable after the expiration of ten (10) years from the date it is granted, and no Incentive Stock Option granted to a Ten Percent Holder shall, by its terms, be exercisable after the expiration of five (5) years from the date of the Option. Unless otherwise specified by the Board or the Committee in the resolution authorizing such Option, the date of grant of an Option shall be deemed to be the date upon which the Board or the Committee authorizes the granting of such Option.

Each Option shall be exercisable to the nearest whole share, in installments or otherwise, as the respective Option agreements may provide. During the lifetime of an Optionee, the Option shall be exercisable only by the Optionee and shall not be assignable or transferable by the Optionee, and no other person shall acquire any rights therein. To the extent not exercised, installments (if more than one) shall accumulate, but shall be exercisable, in whole or in part, only during the period for exercise as stated in the Option agreement, whether or not other installments are then exercisable.

- (e) Termination of Status as Employee, Consultant or Director: If Optionee's status as an employee shall terminate for any reason other than Optionee's disability or death, then Optionee (or if the Optionee shall die after such termination, but prior to exercise, Optionee's personal representative or the person entitled to succeed to the Option) shall have the right to exercise the portions of any of Optionee's Incentive Stock Options which were exercisable as of the date of such termination, in whole or in part, not less than 30 days nor more than three (3) months after such termination (or, in the event of "*termination for Cause*", the Option shall automatically terminate as of the termination of employment as to all shares covered by the Option).

With respect to Nonstatutory Options granted to employees, directors or consultants, the Board may specify such period for exercise, not less than 30 days (except that in the case of "*termination for Cause*" or removal of a director, the Option shall automatically terminate as of the termination of employment or services as to shares covered by the Option, following termination of employment or services as the Board deems reasonable and appropriate. The Option may be exercised only with respect to installments that the Optionee could have exercised at the date of termination of employment or services. Nothing contained herein or in any Option granted pursuant hereto shall be construed to affect or restrict in any way the right of the Company to terminate the employment or services of an Optionee with or without cause.

In the event the terms contained in this Section 5(e) conflict with that of an employment agreement entered between the Company and an Optionee, then the terms of the employment agreement shall govern.

- (f) Disability of Optionee: If an Optionee is disabled (within the meaning of Section 22(e)(3) of the Code) at the time of termination, the three (3) month period set forth in Section 5(e) shall be a period, as determined by the Board and set forth in the Option, of not less than six months nor more than one year after such termination.
- (g) Death of Optionee: If an Optionee dies while employed by, engaged as a consultant to, or serving as a Director of the Company, the portion of such Optionee's Option which was exercisable at the date of death may be exercised, in whole or in part, by the estate of the decedent or by a person succeeding to the right to exercise such Option at any time within (i) a period, as determined by the Board and set forth in the Option, of not less than six (6) months nor more than one (1) year after Optionee's death, which period shall not be more, in the case of a Nonstatutory Option, than the period for exercise following termination of employment or services, or (ii) during the remaining term of the Option, whichever is the lesser. The Option may be so exercised only with respect to installments exercisable at the time of Optionee's death and not previously exercised by the Optionee.

- (h) Nontransferability of Option: No Option shall be transferable by the Optionee, except by will or by the laws of descent and distribution.
- (i) Recapitalization: Subject to any required action of shareholders, the number of shares of Stock covered by each outstanding Option, and the exercise price per share thereof set forth in each such Option, shall be proportionately adjusted for any increase or decrease in the number of issued shares of Stock of the Company resulting from a stock split, stock dividend, combination, subdivision or reclassification of shares, or the payment of a stock dividend, or any other increase or decrease in the number of such shares affected without receipt of consideration by the Company; provided, however, the conversion of any convertible securities of the Company shall not be deemed to have been "*effected without receipt of consideration*" by the Company.

In the event of a proposed dissolution or liquidation of the Company, a merger or consolidation in which the Company is not the surviving entity, or a sale of all or substantially all of the assets or capital stock of the Company (collectively, a "**Reorganization**"), unless otherwise provided by the Board, this Option shall terminate immediately prior to such date as is determined by the Board, which date shall be no later than the consummation of such Reorganization. In such event, if the entity which shall be the surviving entity does not tender to Optionee an offer, for which it has no obligation to do so, to substitute for any unexercised Option a stock option or capital stock of such surviving entity, as applicable, which on an equitable basis shall provide the Optionee with substantially the same economic benefit as such unexercised Option, then the Board may grant to such Optionee, in its sole and absolute discretion and without obligation, the right for a period commencing thirty (30) days prior to and ending immediately prior to the date determined by the Board pursuant hereto for termination of the Option or during the remaining term of the Option, whichever is the lesser, to exercise any unexpired Option or Options without regard to the installment provisions of Paragraph 6(d) of the Plan; provided, that any such right granted shall be granted to all Optionees not receiving an offer to receive substitute options on a consistent basis, and provided further, that any such exercise shall be subject to the consummation of such Reorganization.

Subject to any required action of shareholders, if the Company shall be the surviving entity in any merger or consolidation, each outstanding Option thereafter shall pertain to and apply to the securities to which a holder of shares of Stock equal to the shares subject to the Option would have been entitled by reason of such merger or consolidation.

In the event of a change in the Stock of the Company as presently constituted, which is limited to a change of all of its authorized shares without par value into the same number of shares with a par value, the shares resulting from any such change shall be deemed to be the Stock within the meaning of the Plan.

To the extent that the foregoing adjustments relate to stock or securities of the Company, such adjustments shall be made by the Board, whose determination in that respect shall be final, binding and conclusive.

Except as expressly provided in this Section 5(i), the Optionee shall have no rights by reason of any subdivision or consolidation of shares of stock of any class or the payment of any stock dividend or any other increase or decrease in the number of shares of stock of any class, and the number or price of shares of Stock subject to any Option shall not be affected by, and no adjustment shall be made by reason of, any dissolution, liquidation, merger, consolidation or sale of assets or capital stock, or any issue by the Company of shares of stock of any class or securities convertible into shares of stock of any class.

The Grant of an Option pursuant to the Plan shall not affect in any way the right or power of the Company to make any adjustments, reclassifications, reorganizations or changes in its capital or business structure or to merge, consolidate, dissolve, or liquidate or to sell or transfer all or any part of its business or assets.

- (j) Rights as a Shareholder: An Optionee shall have no rights as a shareholder with respect to any shares covered by an Option until the effective date of the issuance of the shares following exercise of such Option by Optionee. No adjustment shall be made for dividends (ordinary or extraordinary, whether in cash, securities or other property) or distributions or other rights for which the record date is prior to the date such stock certificate is issued, except as expressly provided in Section 5(i) hereof.
- (k) Modification, Acceleration, Extension, and Renewal of Options: Subject to the terms and conditions and within the limitations of the Plan, the Board may modify an Option, or, once an Option is exercisable, accelerate the rate at which it may be exercised, and may extend or renew outstanding Options granted under the Plan or accept the surrender of outstanding Options (to the extent not theretofore exercised) and authorize the granting of new Options in substitution for such Options, provided such action is permissible under Section 422 of the Code and applicable state securities rules. Notwithstanding the provisions of this Section 5(k), however, no modification of an Option shall, without the consent of the Optionee, alter to the Optionee's detriment or impair any rights or obligations under any Option theretofore granted under the Plan.
- (l) Exercise Before Exercise Date: At the discretion of the Board, the Option may, but need not, include a provision whereby the Optionee may elect to exercise all or any portion of the Option prior to the stated exercise date of the Option or any installment thereof. Any shares so purchased prior to the stated exercise date shall be subject to repurchase by the Company upon termination of Optionee's employment as contemplated by Section 5(n) hereof prior to the exercise date stated in the Option and such other restrictions and conditions as the Board or Committee may deem advisable.
- (m) Other Provisions: The Option agreements authorized under the Plan shall contain such other provisions, including, without limitation, restrictions upon the exercise of the Options, as the Board or the Committee shall deem advisable. Shares shall not be issued pursuant to the exercise of an Option, if the exercise of such Option or the issuance of shares thereunder would violate, in the opinion of legal counsel for the Company, the provisions of any applicable law or the rules or regulations of any applicable governmental or administrative agency or body, such as the Code, the Securities Act, the Exchange Act, applicable state securities rules, Nevada corporation law, and the rules promulgated under the foregoing or the rules and regulations of any exchange upon which the shares of the Company are listed. Without limiting the generality of the foregoing, the exercise of each Option shall be subject to the condition that if at any time the Company shall determine that (i) the satisfaction of withholding tax or other similar liabilities, or (ii) the listing, registration or qualification of any shares covered by such exercise upon any securities exchange or under any state or federal law, or (iii) the consent or approval of any regulatory body, or (iv) the perfection of any exemption from any such withholding, listing, registration, qualification, consent or approval is necessary or desirable in connection with such exercise or the issuance of shares thereunder, then in any such event, such exercise shall not be effective unless such withholding, listing registration, qualification, consent, approval or exemption shall have been effected, obtained or perfected free of any conditions not acceptable to the Company.
- (n) Repurchase Agreement: The Board may, in its discretion, require as a condition to the Grant of an Option hereunder, that an Optionee execute an agreement with the Company, pursuant to forms which shall be approved by the Board of Directors from time to time ("**Repurchase Agreement**"), (i) restricting the Optionee's right to transfer shares purchased under such Option without first offering such shares to the Company or another shareholder of the Company upon the same terms and conditions as provided therein; and (ii) providing that upon termination of Optionee's employment with the Company, for any reason, the Company (or another shareholder of the Company, as provided in the Repurchase Agreement) shall have the right at its discretion (or the discretion of such other shareholders) to purchase and/or redeem all such shares owned by the Optionee on the date of termination of his or her employment at a price equal to: (A) the fair value of such shares as of such date of termination; or (B) if such repurchase right lapses at 20% of the number of shares per year, the original purchase price of such shares, and upon terms of payment permissible under applicable state securities rules; provided that in the case of Options or Stock Awards granted to officers, directors, consultants or affiliates of the Company, such repurchase provisions may be subject to additional or greater restrictions as determined by the Board or Committee.

6. Stock Awards and Restricted Stock Purchase Offers.

(a) Types of Grants.

- (i) Stock Award. All or part of any Stock Award under the Plan may be subject to conditions established by the Board or the Committee, and set forth in the Stock Award Agreement, which may include, but are not limited to, continuous service with the Company, achievement of specific business objectives, increases in specified indices, attaining growth rates and other comparable measurements of Company performance. Such Awards may be based on Fair Market Value or other specified valuation. All Stock Awards will be made pursuant to the execution of a Stock Award Agreement pursuant to forms which shall be approved by the Board of Directors from time to time.
- (ii) Restricted Stock Purchase Offer. A Grant of a Restricted Stock Purchase Offer under the Plan shall be subject to such (i) vesting contingencies related to the Participant's continued association with the Company for a specified time and (ii) other specified conditions as the Board or Committee shall determine, in their sole discretion, consistent with the provisions of the Plan. All Restricted Stock Purchase Offers shall be made pursuant to a Restricted Stock Purchase Offer pursuant to forms which shall be approved by the Board of Directors from time to time.

- (b) Conditions and Restrictions. Shares of Stock which Participants may receive as a Stock Award under a Stock Award Agreement or Restricted Stock Purchase Offer under a Restricted Stock Purchase Offer may include such restrictions as the Board or Committee, as applicable, shall determine, including restrictions on transfer, repurchase rights, right of first refusal, and forfeiture provisions. When transfer of Stock is so restricted or subject to forfeiture provisions it is referred to as "**Restricted Stock**". Further, with Board or Committee approval, Stock Awards or Restricted Stock Purchase Offers may be deferred, either in the form of installments or a future lump sum distribution. The Board or Committee may permit selected Participants to elect to defer distributions of Stock Awards or Restricted Stock Purchase Offers in accordance with procedures established by the Board or Committee to assure that such deferrals comply with applicable requirements of the Code including, at the choice of Participants, the capability to make further deferrals for distribution after retirement. Any deferred distribution, whether elected by the Participant or specified by the Stock Award Agreement, Restricted Stock Purchase Offers or by the Board or Committee, may require the payment be forfeited in accordance with the provisions of Section 6(c). Dividends or dividend equivalent rights may be extended to and made part of any Stock Award or Restricted Stock Purchase Offers denominated in Stock or units of Stock, subject to such terms, conditions and restrictions as the Board or Committee may establish.

(c) Intentionally left blank.

(d) Nonassignability.

- (i) Except pursuant to Section 6(e)(iii) and except as set forth in Section 6(d)(ii), no Grant or any other benefit under the Plan shall be assignable or transferable, or payable to or exercisable by, anyone other than the Participant to whom it was granted.
- (ii) Where a Participant terminates employment and retains a Grant pursuant to Section 6(e)(ii) in order to assume a position with a governmental, charitable or educational institution, the Board or Committee, in its discretion and to the extent permitted by law, may authorize a third party (including but not limited to the trustee of a "blind" trust), acceptable to the applicable governmental or institutional authorities, the Participant and the Board or Committee, to act on behalf of the Participant with regard to such Awards.

(e) Termination of Employment. If the employment or service to the Company of a Participant terminates, other than pursuant to any of the following provisions under this Section 6(e), all unexercised, deferred and unpaid Stock Awards or Restricted Stock Purchase Offers shall be cancelled immediately, unless the Stock Award Agreement or Restricted Stock Purchase Offer provides otherwise:

(i) Retirement Under a Company Retirement Plan. When a Participant's employment terminates as a result of retirement in accordance with the terms of a Company retirement plan, the Board or Committee may permit Stock Awards or Restricted Stock Purchase Offers to continue in effect beyond the date of retirement in accordance with the applicable Grant Agreement and the exercisability and vesting of any such Grants may be accelerated.

(ii) Rights in the Best Interests of the Company. When a Participant resigns from the Company and, in the judgment of the Board or Committee, the acceleration and/or continuation of outstanding Stock Awards or Restricted Stock Purchase Offers would be in the best interests of the Company, the Board or Committee may (i) authorize, where appropriate, the acceleration and/or continuation of all or any part of Grants issued prior to such termination and (ii) permit the exercise, vesting and payment of such Grants for such period as may be set forth in the applicable Grant Agreement, subject to earlier cancellation pursuant to Section 9 or at such time as the Board or Committee shall deem the continuation of all or any part of the Participant's Grants are not in the Company's best interest.

(iii) Death or Disability of a Participant.

(1) In the event of a Participant's death, the Participant's estate or beneficiaries shall have a period up to the expiration date specified in the Grant Agreement within which to receive or exercise any outstanding Grant held by the Participant under such terms as may be specified in the applicable Grant Agreement. Rights to any such outstanding Grants shall pass by will or the laws of descent and distribution in the following order: (a) to beneficiaries so designated by the Participant; if none, then (b) to a legal representative of the Participant; if none, then (c) to the persons entitled thereto as determined by a court of competent jurisdiction. Grants so passing shall be made at such times and in such manner as if the Participant were living.

(2) In the event a Participant is deemed by the Board or Committee to be unable to perform his or her usual duties by reason of mental disorder or medical condition which does not result from facts which would be grounds for termination for cause, Grants and rights to any such Grants may be paid to or exercised by the Participant, if legally competent, or a committee or other legally designated guardian or representative if the Participant is legally incompetent by virtue of such disability.

(3) After the death or disability of a Participant, the Board or Committee may in its sole discretion at any time (1) terminate restrictions in Grant Agreements; (2) accelerate any or all installments and rights; and (3) instruct the Company to pay the total of any accelerated payments in a lump sum to the Participant, the Participant's estate, beneficiaries or representative; notwithstanding that, in the absence of such termination of restrictions or acceleration of payments, any or all of the payments due under the Grant might ultimately have become payable to other beneficiaries.

(4) In the event of uncertainty as to interpretation of or controversies concerning this Section 6, the determinations of the Board or Committee, as applicable, shall be binding and conclusive.

7. Investment Intent. All Grants under the Plan are intended to be exempt from registration under the Securities Act provided by Rule 701 thereunder. Unless and until the granting of Options or sale and issuance of Stock subject to the Plan are registered under the Securities Act or shall be exempt pursuant to the rules promulgated thereunder, each Grant under the Plan shall provide that the purchases or other acquisitions of Stock thereunder shall be for investment purposes and not with a view to, or for resale in connection with, any distribution thereof. Further, unless the issuance and sale of the Stock have been registered under the Securities Act, each Grant shall provide that no shares shall be purchased upon the exercise of the rights under such Grant unless and until (i) all then applicable requirements of state and federal laws and regulatory agencies shall have been fully complied with to the satisfaction of the Company and its counsel, and (ii) if requested to do so by the Company, the person exercising the rights under the Grant shall (i) give written assurances as to knowledge and experience of such person (or a representative employed by such person) in financial and business matters and the ability of such person (or representative) to evaluate the merits and risks of exercising the Option, and (ii) execute and deliver to the Company a letter of investment intent and/or such other form related to applicable exemptions from registration, all in such form and substance as the Company may require. If shares are issued upon exercise of any rights under a Grant without registration under the Securities Act, subsequent registration of such shares shall relieve the purchaser thereof of any investment restrictions or representations made upon the exercise of such rights.

8. Amendment, Modification, Suspension or Discontinuance of the Plan. The Board may, insofar as permitted by law, from time to time, with respect to any shares at the time not subject to outstanding Grants, suspend or terminate the Plan or revise or amend it in any respect whatsoever, except that without the approval of the shareholders of the Company, no such revision or amendment shall (i) increase the number of shares subject to the Plan, (ii) decrease the price at which Grants may be granted, (iii) materially increase the benefits to Participants, or (iv) change the class of persons eligible to receive Grants under the Plan; provided, however, no such action shall alter or impair the rights and obligations under any Option, or Stock Award, or Restricted Stock Purchase Offer outstanding as of the date thereof without the written consent of the Participant thereunder. No Grant may be issued while the Plan is suspended or after it is terminated, but the rights and obligations under any Grant issued while the Plan is in effect shall not be impaired by suspension or termination of the Plan.

In the event of any change in the outstanding Stock by reason of a stock split, stock dividend, combination or reclassification of shares, recapitalization, merger, or similar event, the Board or the Committee may adjust proportionally (a) the number of shares of Stock (i) reserved under the Plan, (ii) available for Incentive Stock Options and Nonstatutory Options and (iii) covered by outstanding Stock Awards or Restricted Stock Purchase Offers; (b) the Stock prices related to outstanding Grants; and (c) the appropriate Fair Market Value and other price determinations for such Grants. In the event of any other change affecting the Stock or any distribution (other than normal cash dividends) to holders of Stock, such adjustments as may be deemed equitable by the Board or the Committee, including adjustments to avoid fractional shares, shall be made to give proper effect to such event. In the event of a corporate merger, consolidation, acquisition of property or stock, separation, reorganization or liquidation, the Board or the Committee shall be authorized to issue or assume stock options, whether or not in a transaction to which Section 424(a) of the Code applies, and other Grants by means of substitution of new Grant Agreements for previously issued Grants or an assumption of previously issued Grants.

9. Tax Withholding. The Company shall have the right to deduct applicable taxes from any Grant payment and withhold, at the time of delivery or exercise of Options, Stock Awards or Restricted Stock Purchase Offers or vesting of shares under such Grants, an appropriate number of shares for payment of taxes required by law or to take such other action as may be necessary in the opinion of the Company to satisfy all obligations for withholding of such taxes. If Stock is used to satisfy tax withholding, such stock shall be valued based on the Fair Market Value when the tax withholding is required to be made.
10. Intentionally Left Blank.
11. Notice. Any written notice to the Company required by any of the provisions of the Plan shall be addressed to the chief financial officer or to the chief executive officer of the Company, and shall become effective when it is received by the office of the chief personnel officer or the chief executive officer.
12. Indemnification of Board. In addition to such other rights or indemnifications as they may have as directors or otherwise, and to the extent allowed by applicable law, the members of the Board and the Committee shall be indemnified by the Company against the reasonable expenses, including attorneys' fees, actually and necessarily incurred in connection with the defense of any claim, action, suit or proceeding, or in connection with any appeal thereof, to which they or any of them may be a party by reason of any action taken, or failure to act, under or in connection with the Plan or any Grant granted thereunder, and against all amounts paid by them in settlement thereof (provided such settlement is approved by independent legal counsel selected by the Company) or paid by them in satisfaction of a judgment in any such claim, action, suit or proceeding, except in any case in relation to matters as to which it shall be adjudged in such claim, action, suit or proceeding that such Board or Committee member is liable for negligence or misconduct in the performance of his or her duties; provided that within sixty (60) days after institution of any such action, suit or Board proceeding the member involved shall offer the Company, in writing, the opportunity, at its own expense, to handle and defend the same.
13. Governing Law. The Plan and all determinations made and actions taken pursuant hereto, to the extent not otherwise governed by the Code or the securities laws of the United States, shall be governed by the law of the State of Nevada and construed accordingly.
14. Effective and Termination Dates. The Plan shall become effective on the date it is approved by the holders of a majority of the shares of Stock then outstanding. The Plan shall terminate ten years later, subject to earlier termination by the Board pursuant to Section 8.

**CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO SECTION 302 OF THE
SARBANES-OXLEY ACT OF 2002**

I, Richard Dauch, Chief Executive Officer, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Workhorse Group Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal controls over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant) and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal controls over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial data information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

Date: August 9, 2022

/s/ Richard Dauch

Richard Dauch,
Chief Executive Officer
(Principal Executive Officer)

**CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO SECTION 302 OF THE
SARBANES-OXLEY ACT OF 2002**

I, Robert M. Ginnan, Chief Financial Officer, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Workhorse Group Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal controls over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant) and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal controls over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial data information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

Date: August 9, 2022

/s/ Robert M. Ginnan

Robert M. Ginnan,
Chief Financial Officer
(Principal Financial Officer)

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO**

SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly report of Workhorse Group Inc. (the "Company") on Form 10-Q for the period ended June 30, 2022 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Richard Dauch, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities and Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: August 9, 2022

/s/ Richard Dauch

Richard Dauch,
Chief Executive Officer
(Principal Executive Officer)

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO**

SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly report of Workhorse Group Inc. (the "Company") on Form 10-Q for the period ended June 30, 2022 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Robert M. Ginnan, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities and Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: August 9, 2022

/s/ Robert M. Ginnan
Robert M. Ginnan,
Chief Financial Officer
(Principal Financial Officer)