

ZAP
Form 10-Q
November 16, 2009

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-Q

(Mark One)

☒ QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2009

☐ 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 001-32534

ZAP

(Exact name of registrant as specified in its charter)

California
(State or other jurisdiction of incorporation or
organization)

94-3210624
(IRS Employer Identification No.)

501 4th Street, Santa Rosa, CA 95401

(Address of principal executive offices) (Zip Code)

(707) 525-8658

(Registrant's telephone number)

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

Indicate by check mark whether the registrant (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 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 is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a small reporting company.

Edgar Filing: ZAP - Form 10-Q

Large accelerated
filer ☐

Accelerated filer ☐

Non-accelerated
filer ☐

Small reporting
company ☒

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

APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY

PROCEEDINGS DURING THE PRECEDING FIVE YEARS

Check whether the registrant filed all documents and reports required to be filed by Section 12, 13 or 15(d) of the Exchange Act after the distribution of securities under a plan confirmed by a court. Yes ☐ No ☒

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date.

103,448,400 shares of common stock as of November 12, 2009.

ZAP

FORM 10-Q

INDEX

		Page No.
PART I. Financial Information		
Item 1.	Condensed Consolidated Financial Statements (unaudited) :	
	Condensed Consolidated Balance Sheets as of September 30, 2009 and December 31, 2008 unaudited.	1
	Condensed Consolidated Statements of Operations for the Three and Nine Months Ended September 30, 2009 and 2008, unaudited.	2
	Condensed Consolidated Statements of Cash Flows for the Nine Months Ended September 30, 2009 and 2008, unaudited.	3
	Notes to Condensed Consolidated Financial Statements, unaudited.	4
Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations	12
Item 4.	Controls and Procedures	26
PART II. Other Information		
Item 1.	Legal Proceedings	26
Item 2.	Unregistered Sales of Equity Securities and Use of Proceeds	27
Item 3.	Defaults Upon Senior Securities	27
Item 4.	Submission of Matters to a Vote of Security Holders	28
Item 5.	Other Information	28
Item 6.	Exhibits	28
SIGNATURES		33

Part I. FINANCIAL INFORMATION

Item 1. Financial Statements

ZAP AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS (Unaudited)

(In thousands except per share data)

	September 30, 2009	December 31, 2008
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$5,328	\$341
Accounts receivable, net of allowance for doubtful accounts of \$29 and \$33	150	377
Inventories, net	2,423	3,043
Prepaid non-cash professional fees	211	105
Other prepaid expenses and other current assets	263	765
Total current assets	8,375	4,631
Property, and equipment, net of accumulated depreciation	3,841	4,335
OTHER ASSETS		
Deposits and other assets	289	260
TOTAL ASSETS	\$12,505	\$9,226
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Current portion of long-term debt and short-term notes	\$5,890	\$2,976
Accounts payable	263	474
Accrued liabilities	1,988	1,575
Deferred revenue	188	587
Total current liabilities	8,329	5,612
LONG-TERM LIABILITIES		
Long-term debt, less current portion	—	1,772
Total liabilities	8,329	7,384
SHAREHOLDERS' EQUITY		
Common stock, authorized 400 million shares; no par value; and 103,308,587 shares and 64,630,608 shares issued and outstanding at September 30, 2009 and December 31 2008, respectively	137,157	126,347
Subscription receivable from shareholders	(1,000)	—
Accumulated deficit	(131,981)	(124,505)
Total shareholders' equity	4,176	1,842
Total liabilities and shareholders' equity	\$12,505	\$9,226

See accompanying notes to condensed consolidated financial statements (unaudited).

ZAP AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)

(Thousands, except net loss per share amounts)

	Three Months ended September 30, 2009	Three Months ended September 30, 2008	Nine Months ended September 30, 2009	Nine Months ended September 30, 2008
NET SALES	\$1,246	\$3,062	\$3,091	\$6,041
COST OF GOODS SOLD	845	2,692	2,581	5,354
GROSS PROFIT	401	370	510	687
OPERATING EXPENSES				
Sales and marketing	254	438	948	1,240
General and administrative (non-cash stock-based compensation of \$1.5 million and \$1.5 million and \$3.6 million and \$4.1 million for the three and nine months ended September 30, 2009 and 2008, respectively)	2,641	2,224	5,783	6,133
Impairment of assets	218	—	674	—
Research and development	81	138	163	456
	3,194	2,800	7,568	7,829
LOSS FROM OPERATIONS	(2,793)	(2,430)	(7,058)	(7,142)
OTHER INCOME (EXPENSE)				
Interest expense, net	(134)	(54)	(431)	(284)
Other income (expense), net	5	1	8	(42)
	(129)	(53)	(423)	(326)
LOSS BEFORE INCOME TAXES	\$(2,922)	\$(2,483)	\$(7,481)	\$(7,468)
PROVISION FOR INCOME TAXES	—	—	(4)	(4)
NET LOSS	\$(2,922)	\$(2,483)	\$(7,485)	\$(7,472)
NET LOSS PER COMMON SHARE				
--- BASIC AND DILUTED	\$(0.03)	\$(0.04)	\$(0.09)	\$(0.13)
WEIGHTED AVERAGE OF COMMON SHARES OUTSTANDING				
--- BASIC AND DILUTED	93,557	59,372	77,965	58,665

See accompanying notes to condensed consolidated financial statements (unaudited).

ZAP AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(In thousands)

	For the Nine Months Ended September 30,	
	2009	2008
Net loss	\$(7,485)	\$(7,472)
Items not requiring the use of cash:		
Amortization of note discount and deferred offering costs	—	156
Stock-based compensation for consulting and other services	886	2,679
Excess tax benefit from share based payment arrangements	951	469
Stock-based employee compensation		
	2,718	1,381
Depreciation and amortization	185	199
Allowance for doubtful accounts	24	(123)
Changes in other items affecting operations:		
Receivables	203	(42)
Inventories	620	(618)
Prepaid expenses and other assets	475	(657)
Accounts payable	(198)	116
Accrued liabilities	409	(791)
Deferred revenue	(399)	(126)
Net cash used for operating activities	(1,611)	(4,829)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of equipment	(22)	(236)
Disposal of equipment	333	176
Net cash provided by (used) for investing activities	311	(60)
CASH FLOWS FROM FINANCING ACTIVITIES		
Issuance of common stock	6,100	
Payoff of convertible debt	—	(431)
Re-issuance of convertible debt		475
Proceeds from short-term debt	1,138	1,917
Repayments of long-term debt	—	54
Excess tax benefit from share based payment arrangements	(951)	(469)
Net cash provided by financing activities	6,287	1,546
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	4,987	(3,343)
CASH AND CASH EQUIVALENTS, beginning of period	341	4,339
CASH AND CASH EQUIVALENTS, end of period	\$5,328	\$996

See accompanying notes to condensed consolidated financial statements (unaudited).

ZAP AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 1 BASIS OF PRESENTATION

The accompanying unaudited condensed financial statements have been prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. All adjustments (all of which are of a normal recurring nature) considered necessary for a fair presentation have been included. Operating results for the three and nine months ended September 30, 2009 are not indicative of the results that may be expected for the year ending December 31, 2009 or for any other future period. These condensed consolidated financial statements and the notes thereto should be read in conjunction with the audited financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2008 filed with the Securities and Exchange Commission (the “SEC”) on March 31, 2009 (our “2008 10-K”).

We face intense competition, which could cause us to lose market share. Changes in the market for electrical or fuel-efficient vehicles could cause our products to become obsolete or lose popularity. We cannot assure you that growth in the electric vehicle industry or fuel-efficient cars will continue and our business may suffer if growth in the electric vehicle industry or fuel-efficient market decreases or if we are unable to maintain the pace of industry demands. We may be unable to keep up with changes in electric vehicle or fuel-efficient technology and, as a result, may suffer a decline in our competitive position. The failure of certain key suppliers to provide us with components could have a severe and negative impact upon our business. Product liability or other claims could have a material adverse effect on our business. We may not be able to protect our Internet address. Our success is heavily dependent upon protecting our intellectual property rights.

NOTE 2 SIGNIFICANT ACCOUNTING POLICIES

NET INCOME (LOSS) PER SHARE ATTRIBUTABLE TO COMMON STOCKHOLDERS

Basic and diluted net income (loss) per common share is based on net income (loss) for the relevant period, divided by the weighted average number of common shares outstanding in each period. Diluted net income per share gives effect to all potentially dilutive common shares outstanding during the period such as options, warrants, convertible preferred stock, and contingently issuable shares. Potentially dilutive securities associated with stock options, warrants have been excluded from the diluted net loss per share amounts, since the effect of these securities would be anti-dilutive. At September 30, 2009, these potentially dilutive securities include options for 26.8 million shares of common stock and warrants for 68.2 million shares of common stock.

PRINCIPLES OF CONSOLIDATION - The accounts of the Company and its consolidated subsidiaries are included in the condensed consolidated financial statements after elimination of significant inter-company accounts and transactions.

REVENUE RECOGNITION

The Company records revenues only upon the occurrence of all of the following conditions:

- The Company has received a binding purchase order or similar commitment from the customer or distributor authorized by a representative empowered to commit the purchaser (evidence of a sale);
- The purchase price has been fixed, based on the terms of the purchase order;
- The Company has delivered the product from its distribution center to a common carrier acceptable to the purchaser. The Company's customary shipping terms are FOB shipping point; and
- The Company deems the collection of the amount invoiced probable.

The Company provides no price protection. Product sales are net of promotional discounts, rebates and return allowances. The Company does not recognize sales taxes collected from customers as revenue.

FAIR VALUE OF FINANCIAL INSTRUMENTS

The carrying amount reported in the balance sheet for cash and cash equivalents, accounts payable and accrued expenses approximates fair value because of the immediate or short-term maturity of these financial instruments. The carrying amount reported for notes payable approximates fair value because in general, the interest on the underlying instruments fluctuates with market rates.

COMMON STOCK ISSUED FOR OTHER THAN CASH

Services performed and other transactions settled in the company's common stock are recorded at the estimated fair value of the stock issued if that value is more readily determinable, than the fair value of the consideration received.

DEFERRED REVENUE - One of the Company's subsidiaries, Voltage Vehicles, sold licenses to auto dealerships under the ZAP name. The license agreements call for the licensee to purchase a minimum number of vehicles from ZAP each year. As the Company collects monies related to these agreements, it is classified as deferred revenue until the Company begins delivering a substantial number of vehicles to these dealerships on a regular basis over the terms of the agreement. The Company has recognized approximately \$275,000 and \$395,000 of license revenue and other adjustments for the three and nine month period ended September 30, 2009, resulting in an ending balance of \$188,000.

USE OF ESTIMATES - The preparation of financial statements in accordance with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the Company's consolidated financial statements and accompanying notes. Estimates were made relating to the useful lives of fixed assets, valuation allowances, impairment of assets and valuation of stock-based compensation and contingencies. Actual results could differ materially from those estimates.

- 5 -

ACCOUNTS RECEIVABLE - The Company performs ongoing credit evaluations of its customers' financial condition and generally requires no collateral from its customers. The Company maintains allowances for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. If the financial condition of the Company's customers should deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required.

INVENTORY - The Company maintains reserves for estimated excess, obsolete and damaged inventory based on projected future shipments using historical selling rates, and taking into account market conditions, inventory on-hand, purchase commitments, product development plans and life expectancy, and competitive factors. If markets for the Company's products and corresponding demand were to decline, then additional reserves may be deemed necessary. Inventories consist primarily of vehicles, both gas and electric, parts and supplies, and finished goods and are carried at the lower of cost (first-in, first-out method) or market.

RECOVERY OF GOODWILL AND LONG-LIVED ASSETS - The Company evaluates the recovery of its goodwill and long-lived assets at least annually by analyzing its operating results and considering significant events or changes in the business environment.

WARRANTY - The Company provides 30 to 90 day warranties on its personal electric products and records the estimated cost of the product warranties at the date of sale. The estimated cost of warranties has not been significant to date. Should actual failure rates and material usage differ from our estimates, revisions to the warranty obligation may be required.

The Company has provided a 6 month warranty for the Xebra® and the safety recall, ZAP Truck and ZAP Shuttle Van vehicles and other varying warranties. At September 30, 2009, the Company has recorded a warranty liability for \$343,000 for estimated repair costs and the Xebra Safety Recall.

CASH AND CASH EQUIVALENTS - The Company considers highly liquid investments with maturities from the date of purchase of three months or less to be cash equivalents.

NOTE 3 STOCK-BASED COMPENSATION

We have stock compensation plans for employees and directors, which are described in Note 7 to our consolidated financial statements in our 2008 Annual Report on Form 10-K as filed with the SEC on March 31, 2009. We recognize the stock-based compensation expense over the requisite service period of the individual grantees, which generally equals the vesting period. All of our stock-based compensation is accounted for as an equity instrument.

Under the provisions of SFAS 123R, we recorded \$ 963,000 of stock compensation, net of estimated forfeitures, in general and administrative expenses, in our unaudited condensed consolidated statement of operations for the three months ended September 30, 2009 . We utilized the Black-Scholes valuation model for estimating the fair value of the stock compensation granted after the adoption of SFAS 123R, with the following range of assumptions.

	Three Months Ended September 30, 2009
Expected Dividend yield	0%
Expected volatility	137.8-158.2
Risk-free interest rate	2.30 to 3.15 %
Expected life (in years) from grant date	5 to 5.75
Exercise price	\$0.36 to \$0.78

The dividend yield of zero is based on the fact that we have never paid cash dividends and have no present intention to pay cash dividends. Expected volatility is based upon historical volatility of our common stock over the period commensurate with the expected life of the options. The risk-free interest rate is derived from the average U.S. Treasury Constant Maturity Rate during the period, which approximates the rate in effect at the time of the grant. Our unvested options vest over the next three years. Our options generally

- 6 -

have a 10-year term. The expected term is calculated using the simplified method prescribed by the SEC's Staff Accounting Bulletin 107. Based on the above assumptions, the weighted-average fair values of the options granted under the stock option plans for the three and nine months ended September 30, 2009 was \$0.39. We estimate forfeitures of employee stock options and recognize compensation cost only for those awards expected to vest. Forfeiture rates are determined based on historical experience. Estimated forfeitures are adjusted to actual forfeiture experience as needed.

A summary of options under the Company's stock option plans from December 31, 2008 through September 30, 2009 is as follows:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value
Outstanding December 31, 2008	11,666,000	\$.96	8.0	
Options granted under the plan	—	—	—	
Options exercised	—	—	—	
Options forfeited and expired	—	—	—	
Outstanding March 31, 2009	11,666,000	\$ 1.03	8.0	
Options granted under the plan	1,150,000	\$ 0.40	10.0	
Options exercised	—	—	—	
Options forfeited and expired	(2,542,000)	—	—	
Outstanding June 30, 2009	10,274,000	\$ 0.97	8.9	
Options granted under the plan	17,034,000	\$ 0.39	10.0	
Options exercised	—	—	—	
Options forfeited and expired	(444,000)	—	—	
Outstanding September 30, 2009	26,864,000	\$ 0.56	7.74	

Aggregate intrinsic value is the sum of the amounts by which the quoted market price of our stock exceeded the exercise price of the options at September 30, 2009, for those options for which the quoted market price was in excess of the exercise price ("in-the-money— options"). There were no options in the money at September 30, 2009.

As of September 30, 2009, total compensation cost of unvested employee stock options is \$5.3 million. This cost is expected to be recognized through September 2012.

NOTE 4 INVENTORIES, NET- Inventories are as follows:

	September 30, 2009	December 31, 2008
Advanced transportation vehicles	\$1,241	\$1,977
Vehicles - conventional	426	518
Parts and supplies	780	721
Finished goods	336	353
	\$2,783	\$3,569
Less - inventory reserve	\$(360)	\$(526)
	\$2,423	\$3,043

NOTE 5 SHORT-TERM DEBT PROMISSORY NOTE

On July 30, 2008, ZAP (the “Company”) executed a Promissory Note for a \$10 million credit line (the “Note”) and a Deed of Trust, Assignment of Leases and Rents and Security Agreement and Fixture Filing (the “Security Agreement”), both in favor of Al Yousuf LLC (the “Lender”). The Al Yousuf Group is a Dubai-based conglomerate and a major shareholder of ZAP. The President of Al Yousuf LLC is Mr. Eqbal Al Yousuf who is also a Director of ZAP.

The following description is a summary of the material terms and conditions of both the Note and the Security Agreement.

The maximum principal loan under the Note is \$10,000,000. The initial outstanding principal sum advanced to the Company is \$1,760,000. This advance was used to pay-off the existing secured note payable on the building which was held by an outside party. The Note matures February 28, 2010. Interest only payments are due under the Note monthly commencing August 30, 2008. Other advances shall be for (i) the purposes of inventory from June 1, 2008 consistent with the currently applicable budget of the Company, as approved by its board of directors (an “Inventory Advance”) or (ii) general working capital to be used consistently with the Company’s budget (a “Working Capital Advance”). The interest rate shall accrue daily at a rate per annum equal to the greater of (i) one month LIBOR plus 3% per annum and (ii) eight percent (8.00%) per annum, commencing on the date of the Note.

The Note matures February 28, 2010. Interest only payments are due under the Note monthly commencing August 30, 2008. Repayment of an Inventory Advance is due four (4) months after the date of such Advance. Repayment of a Working Capital Advance is due six (6) months after the date of such Advance. The repayment term may be extended upon written request of the Company and at the Lender’s sole discretion. The Note is pre-payable in whole or in part without penalty and upon 30 days’ written notice to Lender. All principal and interest due under the Note is secured by the corporate headquarters building in Santa Rosa, California.

The Note contains customary Events of Default, including but not limited to the following: (i) failure by the Company to make any scheduled payment of principal, interest or other amounts due under the Note, (ii) failure to pay-off the Note upon the Maturity Date, (iii) any representation or warranty made in the Loan Documents by the Company being found false in any material respect, (iv) consent by the Company to appoint a conservator or liquidator in a bankruptcy proceeding relating to the Company or all or substantially all of its assets and (v) failure of the Company to maintain insurance required pursuant to the Loan Documents. Upon the occurrence of an Event of Default, the Note shall become due and payable and the interest rate shall increase by 3.00% per annum. All principal and interest due under the Note is secured by the Company’s corporate headquarters building.

On May 14, 2009 we received a Notice of Delinquent Payments from Mr. Hossein Haghighi, the Chief Financial Officer of Al Yousuf LLC, notifying us that an outstanding principle for inventory advances of \$3.4 million plus monthly interest payments has not been paid as required by a \$10 million Promissory Note. Mr. Haghighi further indicated that AL Yousuf LLC intended to enforce the collection of the total amounts due under the terms of the note against the Company. The collateral for the note is our corporate headquarters building and land located in Santa Rosa California. The total due on the note is approximately \$5.6 million at September 30, 2009 with inventory advances totaling \$3.8 million and a building loan of \$1.8 million plus interest.

On September 25, 2009, a complaint captioned Al Yousuf LLC v ZAP (Case No. SW 245950) was filed in the Superior Court for the County of Sonoma. The complaint alleges causes of action for judicial foreclosure and deficiency judgment in connection with a loan agreement with Al Yousuf LLC. The President of Al Yousuf LLC, Eqbal Al Yousuf, is a member of ZAP’s board of directors. In its Complaint, Al Yousuf LLC claims that ZAP has failed to make scheduled payments required under the loan agreement which is secured by real property that serves as ZAP’s principal executive offices. Plaintiff seeks to foreclose on the property that secures the loan agreement and recover attorney’s fees of approximately \$125,000, and obtain such other and further relief as the Count may deem just and proper. ZAP has yet responded to the Complaint. The parties are engaged in settlement discussions.

In addition the Company borrowed \$750,000 from Portable Energy LLC; a private equity company equally owned 50% by ZAP and Al Yousuf. These borrowings are due on demand.

- 8 -

NOTE 6 INCOME TAXES

We adopted the provisions of FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes – an Interpretation of FASB Statement No. 109, or FIN 48, on January 1, 2007. Upon adoption of FIN 48, we commenced a review of our tax position taken in our tax returns that remain subject to examination. Based upon our review, we do not believe we have any unrecognized tax benefits or that there is a material impact on our financial condition or results of operations as a result of implementing FIN 48.

We file income tax returns in the U.S. federal jurisdiction and various state and foreign jurisdictions. We are subject to U.S. federal or state income tax examinations by tax authorities for all years in which we reported net operating losses that are being carried forward. We do not believe there will be any material changes in our unrecognized tax positions over the next 12 months.

We recognize interest and penalties accrued on any unrecognized tax benefits as a component of income tax expense. As of the date of adoption of FIN 48, we did not have any accrued interest or penalties associated with any unrecognized tax benefits, nor were any interest expense recognized for the period ended September 30, 2009.

NOTE 7 SHAREHOLDERS' EQUITY

ZAP's common stock is quoted on the OTC Bulletin Board under the symbol "ZAAP. OB"

NOTE 8 RELATED PARTY TRANSACTIONS

Rental agreements

The Company rents office space, land and warehouse space from Mr. Steven Schneider, its CEO and a major shareholder. These properties are used to operate the car outlet and to store inventory. Rental expense was approximately \$63,000 for both the nine months ended September 30, 2009 and 2008.

Notes Receivable Shareholders

In June 2009, the Company completed a private placement for \$2,000,000 in exchange for 8,000,000 shares of Common Stock at \$0.25 per share. The aggregate proceeds from the placement of the Common Stock of \$2,000,000 will be released in stages through the 4th quarter of 2010. The proceeds from the placement of the Common Stock will be used for general and administrative operating expenses and to continue the Company's accelerated R&D on the new electric vehicles in the planning pipeline. The transaction was done with one of our large existing shareholders and two of his controlled entities.

In addition warrants were also issued to the investors which grant the holders the right to purchase up to 8,000,000 shares of the Registrant's Common Stock at a price of \$0.50 per share. The warrants expire on June 14, 2014.

Financing provided to the Company by Cathaya Capital LLC whose General Partner is Priscilla Lu, Chairman of the Board of ZAP

On August 6, 2009, the Company entered into a Securities Purchase Agreement with Cathaya Capital, L.P., a Cayman Islands exempted limited partnership. Pursuant to the Agreement, the Investor purchased 20 million shares of the Company's Common Stock at a price of \$0.25 per share for an aggregate purchase price of \$5 million. In addition warrants were also issued to the investors which grant the holders the right to purchase up to 10,000,000 shares of the Registrant's Common Stock at a price of \$0.50 per share. The warrants expire on August 16, 2014.

The Company also entered into a Secured Loan Facility with the Investor pursuant to a Secured Convertible Promissory Note. The Note provides for an aggregate principal amount of up to \$10 million in advances to be made to the Company by the Investor prior to October 1, 2012. The aggregate principal amount of the advances made under the Note accrues interest at a rate per annum equal to the greater of (i) five percent (5%) and (ii) three percent (3%) plus prime. The aggregate principal amount of each advance made under the Note plus interest becomes due and payable to the Investor on the earlier of (i) the two year anniversary of the date such advance was made and (ii) December 31, 2012. The Note is

- 9 -

convertible into shares of the Company's Common Stock at a conversion rate, subject to any adjustments called for by the terms of the Note, of 2,000 shares of Common Stock for each \$1,000 principal amount of the Note being converted. The Note is secured by the terms and conditions of a security agreement covering all of the Company's assets other than those assets specifically excluded from the lien created by the Security Agreement. Additional warrants were also issued to the holder which grants the right to purchase up to six million shares of the Registrant's Common Stock at a price of \$0.50 per share. The warrants expire on August 16, 2014.

Financing provided to the Company by Al Yousuf LLC, Whose President is a Director of ZAP

The company entered into various financing arrangements during the second and third quarter 2008 with The Al Yousuf Group who is a Dubai-based conglomerate and a major shareholder of ZAP. The President of Al Yousuf LLC is Mr. Eqbal Al Yousuf, who is also a Director of ZAP who arranged for the note terms and provisions.

On July 30, 2008 we received a \$10 million financing arrangement from the Al Yousuf Group, a Dubai-based conglomerate to provide future working capital to ZAP and help meet the growing demand for ZAP electric vehicles. The financing arrangement allows for advances by ZAP over the next few years commencing on the date of the Note. The initial outstanding principal sum advanced to the Company is \$1,760,000. This advance was used to pay-off the existing secured note payable on the building. The Note matures February 28, 2010. Interest only payments are due under the Note monthly commencing August 30, 2008. All principal and interest due under the Note is secured by the corporate headquarters building in Santa Rosa, California.

On May 14, 2009 we received a Notice of Delinquent Payments from Mr. Hossein Haghighi, the Chief Financial Officer of Al Yousuf LLC, notifying us that an outstanding principle for inventory advances of \$2.8 million plus monthly interest payments has not been paid as required by a \$10 million Promissory Note. Mr. Haghighi further indicated that AL Yousuf LLC intended to enforce the collection of the total amounts due under the terms of the note against the Company. The collateral for the note is our corporate headquarters building and land located in Santa Rosa California. The total due on the note is approximately \$5.6 million at September 30, 2009 with inventory advances totaling \$3.8 million and a building loan of \$1.8 million including interest.

On September 25, 2009, a complaint captioned Al Yousuf LLC v ZAP (Case No. SW 245950) was filed in the Superior Court for the County of Sonoma. The complaint alleges causes of action for judicial foreclosure and deficiency judgment in connection with a loan agreement with Al Yousuf LLC. The President of Al Yousuf LLC, Eqbal Al Yousuf, is a member of ZAP's board of directors. In its Complaint, Al Yousuf LLC claims that ZAP has failed to make scheduled payments required under the loan agreement which is secured by real property that serves as ZAP's principal executive offices. Plaintiff seeks to foreclose on the property that secures the loan agreement and recover attorney's fees of approximately \$125,000, and obtain such other and further relief as the Court may deem just and proper. ZAP has yet responded to the Complaint. The parties are engaged in settlement discussions.

In addition the Company borrowed \$750,000 from Portable Energy LLC; a private equity company equally owned 50% by ZAP and Al Yousuf. These borrowings are due on demand.

NOTE 9 SEGMENT REPORTING

In accordance with the provisions of SFAS No. 131, the Company has identified three reportable segments consisting of sales and marketing of electronic consumer products, the Zappy 3 scooters and ATV's, operation of a retail car outlet and sales to and sales of advanced technology vehicles for the Xebra (TM), ZAP Truck and ZAP Shuttle Van electric vehicles. These segments are strategic business units that offer different services. They are managed separately because each business requires different resources and strategies. The Company's chief operating decision making group, which is comprised of the Chief Executive Officer and the senior executives of each of ZAP's strategic segments, regularly evaluate the financial information about these segments in deciding how to allocate resources and

in assessing performance. The performance of each segment is measured based on its profit or loss from operations before income taxes. Electric Consumer products and corporate expenses represent sales of our ZAPPY 3 which is a three wheeled electric scooter and the overall corporate expenses for the company. Many of these expenses relate to the overall development of our core business, Electric Consumer Products.

Car outlet represents the activity of a retail outlet that sells pre-owned conventional vehicles and advanced technology vehicles, now the Xebra, a three-wheeled plug in electric vehicles, ZAP Truck and ZAP Shuttle Van, four wheeled LSV plug in electric vehicles to retail customers.

- 10 -

Edgar Filing: ZAP - Form 10-Q

Advanced Technology Vehicles represents the sales activity of advanced technology vehicles, now the Xebra, a three-wheeled plug in electric vehicle, ZAP Truck and ZAP Shuttle Van, four wheeled LSV plug in electric vehicles to ZAP Dealers through-out the U.S.

Segment results are summarized as follow (in thousands):

	Electronic Consumer Products and Corporate Expenses	Car Outlet	Advanced Technology Vehicles	Totals
For the 3 months ended of September 30, 2009:				
Net Sales	\$83	\$435	\$728	\$1,246
Gross profit	7	88	306	401
Net Loss	(2,898)	(21)	(3)	(2,922)
Total Assets	10,106	465	1,934	12,505
For the 3 months ended of September 30, 2008:				
Net Sales	\$364	\$528	\$2,170	\$3,062
Gross profit (Loss)	(48)	156	262	370
Net Loss	(2,589)	42	64	(2,483)
Total Assets	7,316	537	1,815	9,668
For the 9 months ended of September 30, 2009:				
Net Sales	\$365	\$1,307	\$1,419	\$3,091
Gross profit	(34)	288	256	510
Net Loss	(6,580)	(20)	(885)	(7,485)
Total Assets	10,106	465	1,934	12,505
For the 9 months ended of September 30, 2008:				
Net Sales	\$611	\$1,250	\$4,180	\$6,041
Gross profit (Loss)	(126)	181	632	687
Net Loss	(7,279)	(146)	(43)	(7,472)
Total Assets	7,316	537	1,815	9,668

NOTE 10 SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:

	Nine months Ended September 30, (in thousands)	
	2009	2008
Cash paid during the period for interest	\$76	\$—
Cash paid during the period for income taxes	\$4	\$4
Non-cash investing and financing activities:		
Reclassification of long term debt to short term:		
Increase in short term debt	1,772	—
Decrease in long term debt	(1,772)	—
Stock and warrants issued for:		
Re-payment of 8% Senior debt	\$—	\$431

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

THIS QUARTERLY REPORT OF FORM 10-Q, INCLUDING THE FOLLOWING MANAGEMENT'S DISCUSSION AND ANALYSIS, AND OTHER REPORTS FILED BY THE REGISTRANT FROM TIME TO TIME WITH THE SECURITIES AND EXCHANGE COMMISSION (COLLECTIVELY THE "FILINGS") CONTAIN FORWARD-LOOKING STATEMENTS WHICH ARE INTENDED TO CONVEY OUR EXPECTATIONS OR PREDICTIONS REGARDING THE OCCURRENCE OF POSSIBLE FUTURE EVENTS OR THE EXISTENCE OF TRENDS AND FACTORS THAT MAY IMPACT OUR FUTURE PLANS AND OPERATING RESULTS. THESE FORWARD-LOOKING STATEMENTS ARE DERIVED, IN PART, FROM VARIOUS ASSUMPTIONS AND ANALYSES WE HAVE MADE IN THE CONTEXT OF OUR CURRENT BUSINESS PLAN AND INFORMATION CURRENTLY AVAILABLE TO US AND IN LIGHT OF OUR EXPERIENCE AND PERCEPTIONS OF HISTORICAL TRENDS, CURRENT CONDITIONS AND EXPECTED FUTURE DEVELOPMENTS AND OTHER FACTORS WE BELIEVE TO BE APPROPRIATE IN THE CIRCUMSTANCES. YOU CAN GENERALLY IDENTIFY FORWARD-LOOKING STATEMENTS THROUGH WORDS AND PHRASES SUCH AS "SEEK", "ANTICIPATE", "BELIEVE", "ESTIMATE", "EXPECT", "INTEND", "P", "BUDGET", "PROJECT", "MAY BE", "MAY CONTINUE", "MAY LIKELY RESULT", AND SIMILAR EXPRESSIONS. WHEN READING ANY FORWARD-LOOKING STATEMENT YOU SHOULD REMAIN MINDFUL THAT ALL FORWARD-LOOKING STATEMENTS ARE INHERENTLY UNCERTAIN AS THEY ARE BASED ON CURRENT EXPECTATIONS AND ASSUMPTIONS CONCERNING FUTURE EVENTS OR FUTURE PERFORMANCE OF OUR COMPANY, AND ARE SUBJECT TO RISKS, UNCERTAINTIES, ASSUMPTIONS AND OTHER FACTORS RELATING TO OUR INDUSTRY AND RESULTS OF OPERATIONS, INCLUDING BUT NOT LIMITED TO THE FOLLOWING FACTORS:

- WHETHER THE ALTERNATIVE ENERGY AND GAS-EFFICIENT VEHICLE MARKET FOR OUR PRODUCTS CONTINUES TO GROW AND, IF IT DOES, THE PACE AT WHICH IT MAY GROW;

- OUR ABILITY TO ATTRACT AND RETAIN THE PERSONNEL QUALIFIED TO IMPLEMENT OUR GROWTH STRATEGIES, ◦ OUR ABILITY TO OBTAIN APPROVAL FROM GOVERNMENT AUTHORITIES FOR OUR PRODUCTS;

- OUR ABILITY TO PROTECT THE PATENTS ON OUR PROPRIETARY TECHNOLOGY;

- OUR ABILITY TO FUND OUR SHORT-TERM AND LONG-TERM FINANCING NEEDS;

- OUR ABILITY TO COMPETE AGAINST LARGE COMPETITORS IN A RAPIDLY CHANGING MARKET FOR ELECTRIC AND GAS-EFFICIENT VEHICLES;

- CHANGES IN OUR BUSINESS PLAN AND CORPORATE STRATEGIES; AND

- OTHER RISKS AND UNCERTAINTIES DISCUSSED IN GREATER DETAIL IN VARIOUS SECTIONS OF THIS REPORT, PARTICULARLY THE SECTION CAPTIONED "RISK FACTORS."

SHOULD ONE OR MORE OF THESE RISKS OR UNCERTAINTIES MATERIALIZE, OR SHOULD THE UNDERLYING ASSUMPTIONS PROVE INCORRECT, ACTUAL RESULTS MAY DIFFER SIGNIFICANTLY FROM THOSE ANTICIPATED, BELIEVED, ESTIMATED, EXPECTED, INTENDED OR PLANNED.

EACH FORWARD-LOOKING STATEMENT SHOULD BE READ IN CONTEXT WITH, AND WITH AN UNDERSTANDING OF, THE VARIOUS OTHER DISCLOSURES CONCERNING OUR COMPANY AND OUR BUSINESS MADE IN OUR FILINGS. YOU SHOULD NOT PLACE UNDUE RELIANCE ON ANY FORWARD-LOOKING STATEMENT AS A PREDICTION OF ACTUAL RESULTS OR DEVELOPMENTS. WE

ARE NOT OBLIGATED TO UPDATE OR REVISE ANY FORWARD-LOOKING STATEMENT CONTAINED IN THIS REPORT TO REFLECT NEW EVENTS OR CIRCUMSTANCES UNLESS AND TO THE EXTENT REQUIRED BY APPLICABLE LAW.

- 12 -

In this quarterly report on Form 10-Q the terms “ZAP,” “Company,” “we,” “us” and “our” refer to ZAP and its subsidiaries.

Overview GENERAL

ZAP stands for Zero Air Pollution(R). With its new product offerings, the Company is positioned to become a leading brand and distribution portal of electric and other advanced technology vehicles. ZAP is committed to running its business based on a strong philosophical foundation that supports the environment, social responsibility and profitability.

ZAP’s strategy is to serve the growing and underrepresented consumer that seeks electric and fuel efficient vehicles. With the recent increases in the cost of oil and increasing concern about the environment and the effects of global warming, we believe there is a large and untapped demand in the areas of transportation and consumer products. During the energy crisis of the 1970s, Japanese automobile manufacturers penetrated the United States market when domestic automobile manufacturers failed to anticipate changes. ZAP believes a similar opportunity is present today, enhanced by heightened environmental awareness, climate changes and economic pressures. ZAP has assembled a complete line of products to meet the growing demands of the environmentally conscious consumer focused on two primary businesses: ZAP Automotive and ZAP Power Systems.

ZAP was incorporated under the laws of the State of California, on September 23, 1994, as “ZAP Power Systems.” The name of the Company was changed to “ZAPWORLD.COM” on May 16, 1999 in order to increase our visibility in the world of electronic commerce. We subsequently changed our name to ZAP on June 18, 2001 in order to reflect our growth and entry into larger, more traditional markets. Our principal executive offices are located at 501 Fourth Street Santa Rosa, California, 95401. Our telephone number is (707) 525- 8658. Our website is www.zapworld.com. Please refer to it for further information on ZAP.

SUBSIDIARIES

We have the following wholly owned subsidiaries : Voltage Vehicles, a Nevada company (“Voltage Vehicles”), ZAP Rental Outlet, a Nevada company (“ZAP Rentals”), ZAP Stores, Inc., a California company (“ZAP Stores”), ZAP Manufacturing, Inc., a Nevada company (“ZAP Manufacturing”) and ZAP World Outlet, Inc., a California company (“ZAP World”) ; Voltage Vehicles is engaged primarily in the distribution and sale of advanced technology and conventional automobiles; ZAP Stores is engaged primarily in consumer sales of ZAP products at one location and ZAP Manufacturing is engaged primarily in the distribution of ZAP products.

Recent Developments

Some of the noteworthy events for the Company that occurred during the Third quarter of 2009 and through the date of this report are as follows:

1. We secured up to \$25 million in new financing with Cathaya Capital, L.P. With offices in Silicon Valley, Cathaya, L.P. is backed by financier Jacques de Chateauvieux’s Paris-based Jaccar Holdings and intends to manage the investment through its affiliate Better World International Ltd. Financing includes a private placement of twenty million shares of common stock for aggregate proceeds of \$5 million and a secured loan facility of up to \$10 million that will be advanced to ZAP provided

certain conditions are met. In connection with the financing, the investor also was issued warrants exercisable for up to twenty million shares of common stock at \$0.50 per share.

2. To help automotive fleets reduce emissions and operating expenses we have begun distributing a five-passenger van and a new XL Truck both of which are 4-wheel, 100 percent, plug-in electric vehicles. The new Shuttle was designed for passenger transport or cargo. The seats are removable so it can convert into a cargo vehicle. Our new XL Truck was designed with a roomy cab for two and a sturdy bed platform capable of transporting 800 lbs. for on-road use and up to 1,600 lbs. capacity for private roads and facilities.
3. We also received a follow-on order from the U.S. military for additional Zaptruck XL electric vehicles and charging stations for shipment to a second international base. The reorder was based on an initial trial order placed in June. The new order includes eleven Zaptruck XLs as well as five 220-volt fast charging stations.

Results of Operations

The following table sets forth, as a percentage of net sales, certain items included in the Company's Statements of Operations (see Financial Statements and Notes) for the periods indicated:

	Three months ended September 30				Nine months ended September 30			
	2009	2008			2009	2008		
Statements of Operations Data:								
Net sales	100	%	100	%	100	%	100	%
Cost of sales	(67.8	)	(87.9	)	(83.5	)	(88.6)
Operating expenses	(255.5	)	(94.1	)	(244.4	)	(129.6)
Loss from operations	(223.1	)	(79.3	)	(227.9	)	(118.2)
Net loss	(233.5	)	(81.0	)	(241.7	)	(123.7)

Quarter Ended September 30, 2009 Compared to Quarter Ended September 30, 2008

Net sales for the quarter ended September 30, 2009 were \$1.2 million compared to \$3.1 million for the period ended September 30, 2008.

Our third quarter sales of Advanced Technology vehicles such as the ZAP Truck, ZAP Van and Xebra, our three wheeled electric car and Zapino a full size electric road scooter decreased from \$2.2 million in 2008 to \$727,000 in 2009. The decrease of \$1.5 million is primarily due to the phase out of our three wheeled Xebra vehicle with reduced selling prices. The introduction and sales of the four wheeled ZAP Truck and ZAP Van of \$125,000 in the third quarter partially offset the Xebra decline of \$1.7 million.

Our retail car lot experienced a decrease of \$93,000 in sales for the third quarters from \$528,000 in 2008 to \$435,000 in 2009. The decrease was due to the mix of available vehicles for resale. During the third quarter the retail car lot had many SUV's and trucks that experienced less consumer demand. The business segment was also affected by US government rebates to new large new car dealers.

In our Consumer Product segment third quarter sales decreased from \$364,000 in 2008 to \$83,000 in 2009 for the third quarter ended September 30. The decrease is primarily due to less consumer demand for the ZAPPY 3 Pro together with the Company's shift in marketing efforts to become a major distributor of advanced technology vehicles.

The current U. S. economic recession has also caused an overall decrease in sales of all products.

Gross profit increased by \$31,000 from a gross profit of \$370,000 for the third quarter ended September 30, 2008 to a gross profit of \$401,000 for the quarter ended September 30, 2009. As a percentage of sales the overall increase was from 12% to 32% primarily due to the advanced technology segment.

- 14 -

Edgar Filing: ZAP - Form 10-Q

Advanced Technology vehicles gross profit increased from a \$262,000 gross profit for the period ended September 30, 2008 to \$306,000 for the period ended September 30, 2009. As a percentage of sales the increase was from 12% to 43%. The major reason was due to the recognition of \$274,000 of dealer start-up fees for contracts that have expired during the quarter.

The Consumer Products segment experienced an increase in gross profits in the third quarter from a gross loss of \$48,000 in 2008 to a gross profit of \$7,000 in 2009. The increase was due less costs for quality control labor. In the third quarter of 2008, we experienced repairs for the ZAPPY 3 Pro model, since then we have changed manufacturers.

The gross profit in the third quarter for our car lot decreased from \$156,000 in 2008 to \$88,000. As a percentage of sales it is a decrease from 30% to 20%. The lower profits are due to the current recession and the mix of vehicle models sold during the quarter. The decrease was primarily due to lower sales volumes.

Sales and marketing expenses decreased by \$184,000 from \$438,000 for the quarter ended September 30, 2008 to \$254,000 in 2009. The decrease was due to the elimination of certain sales and marketing positions in the third quarter ended September 30, 2009. In addition, we decreased the use of outside consultants to assist our sales efforts.

General and administrative expenses increased by \$404,000 from \$2.2 million for the quarter ended September 30, 2008 to \$2.6 million in 2009. The reason for the increase was greater expense for legal fees for the financing arrangement with Cathaya Capital LLC. See further discussion in the liquidity section of this report. In addition, we incurred higher costs for the expensing of new employee stock options that were granted in the third quarter of 2009.

Research and development expenses decreased by \$57,000 from \$138,000 in 2008 to \$81,000 for the third quarter ended September 30, 2009. The decrease was due to less work on the development of the Alias prototype vehicle where in 2008, we used funds to develop various models of the vehicle.

Impairment of Assets represents the allowance for the phase out of our Latin American dealer and adjustments to certain of our building improvement projects.

Interest expense, net increased from an expense of \$54,000 in third quarter 2008 to \$134,000 in third quarter of 2009. The increase was due to the higher loan balance on the promissory note with Al Yousuf LLC see also note 5, short-term debt.

Other income net increased from of \$1,000 for the third quarter of 2008 to other income of \$5,000 in the third quarter of 2009. The increase was due to income from other minor customer fees.

Net loss for the third quarter ended September 30, 2009 was \$2.9 million as compared to a loss of \$2.5 million for the period ended September 30, 2008.

Nine months Ended September 30, 2009 Compared to Nine months Ended September 30, 2008

Net sales for the nine months ended September 30, 2009, were \$3.1 million compared to \$6 million for the nine months ended September 30 in the prior year.

Sales in the Advanced Technology segment decreased from \$4.1 million in 2008 to \$1.4 million in 2009. The tight U.S. credit and general economic conditions negatively impacted our dealer sales in the first nine months of 2009. In addition, we also decreased our production of our three wheel electric vehicle the Xebra to transition to 4 wheel electric vehicles, the ZAP Truck and the ZAP Van.

We experienced an decrease of \$246,000 in sales of consumer products from \$611,000 in 2008 to \$365,000 in 2009 due to fewer ZAPPY 3 scooters available for resale as we searched for a new outside contractor manufacturer in 2009. We also experienced less consumer demand as we focused our marketing efforts on becoming a major distributor of advanced technology vehicles.

- 15 -

Edgar Filing: ZAP - Form 10-Q

Our retail car lot experienced an increase in sales of \$57,000 from \$1.2 million in 2008 to \$1.3 million in 2009. The increase was due to strong sales in the first quarter of 2009. Due to the current recession many consumers chose lower priced pre-owned vehicles that are distributed through our retail car outlet.

Gross profit decreased by \$177,000 from \$687,000 for the nine months ended September 30, 2008 compared to \$510,000 for the nine months ended September 30, 2009. However the gross profit as a percentage of net sales increased from 10% to 17%. Overall the decrease in gross profits was due to \$3 million less sales for the nine month period ended September 30, 2009 versus 2008.

In our Advanced Technology segment our gross profit decreased by \$376,000 from a gross profit of \$632,000 for the nine months ended September 30, 2009. The decrease was primarily due to lower sales volumes and the establishment of an allowance of \$248,000 to repair Xebras for the safety recall.

In our Consumer Products segment we experienced a decrease of \$92,000 in gross loss from \$126,000 in 2008 to a gross loss of \$34,000 in 2009. The gross loss was less due to a sales decrease of \$246,000 for the first nine months of 2009 compared to 2008.

Gross profits in our retail car lot increased by \$107,000 from \$181,000 for the nine months ended September 30, 2008 to \$288,000 for the nine months ended September 30, 2009. The increase in gross profits was due to higher sales volumes and better mix of vehicle models with higher margins.

Sales and marketing expenses in the first nine months of 2009 decreased by \$292,000 from \$1.2 million in 2008 to \$948,000 in 2009. The decrease was due to less expenses for outside consultants and elimination of certain sales and marketing positions.

General and administrative expenses for the nine months ended September 30, 2009 decreased by \$363,000 from \$6.1 million in 2008 to \$5.8 million in 2009. The decrease was due to less legal and professional fees for the first nine months. In addition, various general and administrative positions were either eliminated or work time cut-back.

Research and development expenses decreased by \$293,000 from \$456,000 in 2008 to \$163,000 in 2009. The decrease was the result of less one time charges as in 2008 for the development of an R&D venture for various products to be developed in China.

Impairment of Assets represents disputes with foreign outside contract manufacturers over products, mostly parts, that we believe belong to us and are being held by them. In addition, we made certain payments for vehicle production that we believe were not shipped as promised. We are uncertain if these disputes can be favorably resolved by us and we are seeking full repayment for the products. In addition, we established an allowance to phase out our Latin American dealer.

Interest expense, net increased by \$147,000 from an interest expense of \$284,000 for the first nine months of 2008 to interest expense of \$431,000 in the nine months ended September 30, 2009. The increase was due to higher borrowings on the Financing arrangement with Al Yousuf.

Other Income (expense) decreased from an expense of \$42,000 for the nine months ended September 30, 2008 to other income of \$8,000 in the first nine months of 2009. The decrease was due less one time charges for charitable contributions that were done in 2008.

Net loss for the both of the nine months ended September 30, 2009 and 2008 was approximately \$7.5 million.

Liquidity and Capital Resources

In the first nine months of 2009 net cash used for operating activities was \$1.6 million. Cash used in the first nine months of 2009 was comprised of the net loss incurred for the first nine months of \$7.5 million plus net non-cash expenses of \$4.7 million and the net increase of \$1.1million in operating assets and liabilities. In the first nine months of 2008, the Company used cash for operations of \$4.8 million was comprised of the net loss of \$7.5 million plus net non-cash expenses of \$4.7 million, and the net decrease in operating assets and liabilities of \$2 million.

- 16 -

Investing activities provided cash of \$311,000 in the first nine months ended September 30, 2009 and . The disposal of equipment resulted in increases to cash.

Financing activities for the first nine months ended September 30, 2009 provided cash of \$6.3 million compared with \$1.5 million in 2008. In 2009, we received cash from private placements of \$6.1 million from four investors.

The Company had cash of \$5.3 million at September 30, 2009 as compared to \$996,000 at September 30, 2008. The Company had working capital of \$48,000 and working capital of \$235,00 for the periods ended September 30, 2009 and 2008 respectively.

On July 30, 2008 we received a \$10 million financing arrangement from the Al Yousuf Group, a Dubai-based conglomerate to provide future working capital to ZAP and help meet the growing demand for ZAP electric vehicles. The Al-Yousuf group is a major investor of ours and the President of Al-Yousuf, Mr. Eqbal Al-Yousuf is our Chairman of the Board. The financing arrangement allows for advances by ZAP over the next few years commencing on the date of the Note.

On May 14, 2009 we received a Notice of Delinquent Payments from Mr. Hossein Haghighi, the Chief Financial Officer of Al Yousuf LLC, notifying us that an outstanding principle for inventory advances of \$3.4 million plus monthly interest payments has not been paid as required by a \$10 million Promissory Note. Mr. Haghighi further indicated that AL Yousuf LLC intended to enforce the collection of the total amounts due under the terms of the note against the Company. The collateral for the note is our corporate headquarters building and land located in Santa Rosa California. The total due on the note is approximately \$5.6 million at September 30, 2009 with inventory advances totaling \$3.8 million and a building loan of \$1.8 million plus interest.

On September 25, 2009, a complaint captioned Al Yousuf LLC v ZAP (Case No. SW 245950) was filed in the Superior Court for the County of Sonoma. The complaint alleges causes of action for judicial foreclosure and deficiency judgment in connection with a loan agreement with Al Yousuf LLC. The President of Al Yousuf LLC, Eqbal Al Yousuf, is a member of ZAP's board of directors. In its Complaint, Al Yousuf LLC claims that ZAP has failed to make scheduled payments required under the loan agreement which is secured by real property that serves as ZAP's principal executive offices. Plaintiff seeks to foreclose on the property that secures the loan agreement and recover attorney's fees of approximately \$125,000, and obtain such other and further relief as the Count may deem just and proper. ZAP has yet responded to the Complaint. The parties are engaged in settlement discussions.

We have experienced the following transaction that strengthen our liquidity:

On August 6, 2009, the Company entered into a Securities Purchase Agreement with Cathaya Capital, L.P., a Cayman Islands exempted limited partnership. Pursuant to the Agreement, the Investor purchased 20 million shares of the Company's Common Stock at a price of \$0.25 per share for an aggregate purchase price of \$5 million. In addition warrants were also issued to the investors which grant the holders the right to purchase up to 10,000,000 shares of the Registrant's Common Stock at a price of \$0.50 per share. The warrants expire on August 16, 2014.

The Company also entered into a Secured Loan Facility with the Investor pursuant to a Secured Convertible Promissory Note. The Note provides for an aggregate principal amount of up to \$10 million in advances to be made to the Company by the Investor prior to October 1, 2012. The aggregate principal amount of the advances made under the Note accrues interest at a rate per annum equal to the greater of (i) five percent (5%) and (ii) three percent (3%) plus prime. The aggregate principal amount of each advance made under the Note plus interest becomes due and payable to the Investor on the earlier of (i) the two year anniversary of the date such advance was made and (ii) December 31, 2012. The Note is convertible into shares of the Company's Common Stock at a conversion rate, subject to any adjustments called for by the terms of the Note, of 2,000 shares of Common Stock for each \$1,000 principal amount of the Note being converted. The Note is secured by the terms and conditions of a security agreement covering all of the Company's assets other than those assets specifically excluded from the lien created by the Security

Agreement. Additional warrants were also issued to the holder which grants the right to purchase up to six million shares of the Registrant's Common Stock at a price of \$0.50 per share. The warrants expire on August 16, 2014.

In June of 2009, we completed a private placement with one of our large shareholders (two of his controlled entities) for a total of \$2 million for 8 million shares of common stock. One half or \$1 million was received and the other \$1 million is due throughout 2010 in accordance with the terms of the shareholder note receivable. In addition warrants were also issued to the investors which grant the holders the right to purchase up to 8,000,000 shares of the Registrant's Common Stock at a price of \$0.50 per share. The warrants expire on June 14, 2014.

- 17 -

CRITICAL ACCOUNTING POLICIES

Revenue Recognition

The Company records revenues only upon the occurrence of all of the following conditions:

The Company has received a binding purchase order or similar commitment from the customer or distributor authorized by a representative empowered to commit the purchaser (evidence of a sale);

The purchase price has been fixed, based on the terms of the purchase order;

The Company has delivered the product from its distribution center to a common carrier acceptable to the purchaser. The Company's customary shipping terms are FOB shipping point; and

The Company deems the collection of the amount invoiced probable.

The Company provides no price protection. Product sales are net of promotional discounts, rebates and return allowances. The Company does not recognize sales taxes collected from customers as revenue.

Allowance for Doubtful Accounts

The Company performs ongoing credit evaluations of its customers' financial condition and, generally, requires no collateral from its customers. The Company records an allowance for doubtful accounts receivable for credit losses at the end of each period based on an analysis of individual aged accounts receivable balances. As a result of this analysis, the Company believes that its allowance for doubtful accounts is adequate at September 30, 2009 and 2008, respectively. If the financial condition of the Company's customers should deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required.

Inventory Valuation

We adjust the value of our inventory for estimated obsolescence or unmarketable inventory equal to the difference between the cost of inventory and the estimated market value based upon assumptions about future demand and market conditions and development of new products by our competitors. Inventories consist primarily of vehicles, both gas and electric, parts and supplies, and finished goods, and are carried at the lower of cost (first-in, first-out method) or market.

Deferred Tax Asset Realization

We record a full valuation allowance to reduce our deferred tax assets to the amount that is more likely than not to be realized. While we have considered future taxable income and ongoing prudent and feasible tax planning strategies in assessing the need for the valuation allowance, in the event we were to determine that we would be able to realize our deferred tax assets in the future in excess of its net recorded amount, an adjustment to the deferred tax asset would increase income in the period such determination was made.

BUSINESS DEVELOPMENT

Founded in 1994, ZAP has invented, designed, manufactured, and marketed numerous innovative products since the Company's inception. In 1995, ZAP began marketing electric transportation on the Internet through our website, www.zapworld.com. ZAP has been a pioneer in developing and marketing electric vehicles such as a zero-emission ZAP(R) electric bicycle, ZAP Power System, which adapts to most bicycles, and the ZAPPY(R) folding electric scooter. From 1996 through 1998, we continued to add to our product line; in 1999, ZAP added electric motorbikes; in

2001, it added electric dive scooters; in 2003, ZAP announced its first electric automobiles, including the first-ever production electric automobile imported from its manufacturing partner in China; in 2004 ZAP introduced electric all-terrain vehicles and the fuel-efficient Smart Car; and in 2005 ZAP introduced multi-fuel vehicles, capable of running on ethanol and/or gasoline. To date, we have delivered more than 100,000 electric vehicles and consumer products to customers in more than 75 countries, which we believe establishes us as one of the leaders in the alternative transportation marketplace.

- 18 -

Today, ZAP is continuing its focus as one of the pioneers of advanced transportation technologies and leveraging its place in the market as a magnet for new technologies. The Company believes there is a growing and underrepresented market for fuel efficient transportation vehicles and we are capitalizing on the opportunities enhanced by heightened environmental awareness, climate changes and economic pressures. The technology is available to deliver transportation solutions that are practical and affordable. With our products such as the XEBRA, ZAP Truck, ZAP Shuttle Van and ZAPPY 3, ZAP is already delivering such solutions to the market. Our goal is to become one of the largest and most complete brand and distribution portals in the United States for advanced technology vehicles and 100% plug-in electrics.

To distribute our practical, affordable and advanced transportation technologies, we have established and are growing both our portal of qualified automotive dealers and our relationships with specialty dealers/distributors for our power system products. Through these distribution channels, coupled with the continued establishment of partnerships with select manufacturers, we intend to expand our market recognition by building awareness of the evolving technologies available for automotive transportation and in reducing our nation's dependency on foreign oil.

PRODUCT SUMMARY

Our existing product line, which includes completed, market ready products and planned introductions, is as follows:

ZAP AUTOMOTIVE

ZAP believes it is positioned to become one of the leading distributors of fuel efficient alternative energy vehicles in the United States. We believe that we are one of only a few companies distributing a 100% production electric vehicle capable of speeds up to 40 mph. Within the next twelve to thirty-nine months, we hope to have distribution agreements in place with vehicle manufacturers whose products fit ZAP's mission. To distribute our product to end consumers and fleets, we have established more than 50 licensed automotive dealers and intend to grow this base significantly over the next several years.

In 2006, ZAP Automotive introduced the following automobile products:

- othe 100% electric XEBRA sedan with an MSRP of approximately\$11,000;

- othe 100% electric XEBRA utility vehicle truck with an MSRP of approximately \$12,000; and

In 2007, ZAP Automotive introduced a new electric scooter, the ZAPINO, with an advanced 3,000 watt brushless DC hub motor, perfect for city commuting and able to reach speeds of 30 MPH with an MSRP of \$3,500.

In 2009, we introduced the ZAP Truck XL, which is a low speed 4 wheel utility truck and having a MSRP of approximately \$14,900. The ZAP Shuttle Van was also introduced, which is designed for passenger transport or cargo. The seats are removable so it can convert into a cargo vehicle

Our future offerings that are currently in the developmental stage include:

- oThe ZAP Alias, which has a target price of \$32,500 per vehicle and an estimated range of 100 miles per charge. This vehicle launch date is for 2010.

We are also in discussions with other foreign manufacturers and hope to establish additional relationships within the next twelve to thirty-nine months for other vehicle platforms.

XEBRA

We believe that XEBRA is the only series production electric vehicle in the United States that can legally travel faster than 25 mph. The car's suggested retail price of \$11,000 is significantly less expensive than most of its competitors, some of which cost more than \$100,000 and are not yet widely available today. XEBRA has three wheels and is being imported as a motor-driven cycle, yet, unlike most other motor-driven cycles, the XEBRA is enclosed with windows and a roof, affording it protection from inclement weather.

- 19 -

XEBRA Sedan (ZAPCAR (R))

ZAP launched the sedan version of its XEBRA ZAPCAR on July 11, 2006. The sedan has a seating capacity for four and is being targeted for city/commuter use. Based on initial feedback, ZAP will be marketing the XEBRA sedan to government and corporate fleets as well as to families with two or more cars, but with plenty of occasion to use their vehicles for short, city drives.

XEBRA PK (ZAPTRUCK(R))

ZAP launched its utility pick-up truck version of the XEBRA, the XEBRA ZAPTRUCK, on August 24, 2006. This electric vehicle seats two with a multi-purpose platform behind the passenger compartment that serves as a hauler, dump truck or flatbed. The XEBRA ZAPTRUCK is targeted to municipalities, maintenance facilities, universities, ranches and warehouses. Since its launch, we have received overwhelming inquiries for test drives. To date, we have focused on our west coast market and sales have exceeded our initial distribution and sales plans.

ZAP XL TRUCK

ZAP's new XL Truck was designed with a roomy cab for two and a sturdy bed platform capable of transporting 800 lbs. for on-road use and up to 1,600 lbs. capacity for private roads and facilities. This 100 percent electric workhorse has convertible, drop-side bed construction to convert to a flatbed. ZAP's XL Truck can be ordered with options like air conditioning, enclosed weatherproof cargo box, solar charger, above-bed utility rack and rapid charging system. MSRP is \$14,500.

ZAP SHUTTLE VAN

ZAP's new Shuttle was designed for passenger transport or cargo. The seats are removable so it can convert into a cargo vehicle with 108 cubic feet and a 900 lb. total carrying capacity. Large slider doors on both sides and a rear lift hatch provide convenient access to the rear compartment, which is weatherproof and secure. At 138 inches, its length is just shy of most mini-vans and at 6 ft 2 inches it has plenty of headroom. The ZAP Shuttle was designed for transportation around large campuses, to and from parking lots, and, because it produces zero emissions, through factories, warehouses and other indoor uses. Air conditioning, solar panels and a rapid charger are available options. MSRP: \$14,700.

LOTUS

In 2007, we announced and entered into a development and feasibility contract with Lotus Engineering to develop an electric all-wheel drive crossover high performance vehicle for the U.S. market.

We are also developing a \$32,000 all electric vehicle with a targeted 100 mile range, the ZAP Alias (TM), which is expected third quarter 2010.

Future Automotive Offerings

Over the next 36 months, we hope to establish relationships with additional manufacturers who can supply automobiles and related vehicles that meet our mission of affordable, advanced transportation technologies that are socially responsible and environmentally sustainable. In 2009, we have identified the following products as potential future offerings for the Company: (1) an affordable 100% electric two-seater sports coupe and a high performance highway all electric vehicle.

ZAP Power Systems

We launched the Company in 1994 with the invention of the ZAPPY electric scooter and quickly established a presence as one of the market leaders in the electric “personal” transportation product segment. Since inception, the Company has been able to maintain a steady business and committed buyers in this segment. In keeping with our initial product offerings, at the beginning of 2006, we revitalized our consumer products line (recently renamed “Power Systems”), including an updated version of the electric scooter. As part of the segment’s revitalization, we reduced the number of suppliers and placed more emphasis on upgrading existing models with newer component technology and more robust features in order to provide a higher quality consumer experience and product.

- 20 -

Our current product offerings include:

Three-wheeled personal transporters (ZAPPY3, ZAPPY3 Pro, ZAPPY3 EZ); o Off-road vehicles (electric quads and motorcycles); and The ZAPPY 3 Personal Transporters Seaway's highly publicized "human transporter to change the world" unearthed a growing need for a "scooter for adults," better known as personal electric transportation. The Company responded to this demand by designing the ZAPPY3. Unlike the Segway, the ZAPPY3's 3-wheeled vehicle design provides stability and maneuverability allowing just about anyone to ride this vehicle without training. It has a top speed of 15 mph, and the Pro has the farthest range of any personal transporter available today at 25 miles range per charge.

The Company initially thought that the ZAPPY3 would be great for the consumer market. Over the past year, the Company has revisited its sales strategy and come to recognize that the largest market opportunities are in the industrial and commercial applications. The Company's primary sales channels are now more clearly defined as security, sporting goods and material handling.

With the increased emphasis on homeland security, there are several product competitors in the security and police market segment. Segway, the most well known, can be found in select police departments and airports and sells for about \$5,500. American Chariot, which is a chariot-like transporter, has entered the market selling between \$1,500 to \$2,500. Newest to the security transporter business is T3Motion, which is built like a small tank and priced at up to \$8,000. The ZAPPY3 meets the need of a majority of the security transportation needs and with a selling price range of \$530 to \$900, depending on the model purchased, which we believe is the most economical of all offerings.

The ZAPPY3 retail focus has continued strong in 2009. As the product line has gained momentum and market acceptance, we plan to grow distribution in the retail channel through larger regional and specialized chain stores.

The material handling, warehousing, fabrication, and construction industries are the ideal markets for the ZAPPY3 Pro. We are not currently aware of any major competitors in this market. The traditional solution for short distance transportation has been bicycles.

The ZAPPY Pro offers the perfect utility vehicle for shuttling, picking and packing and getting into small areas like elevators. While the Company's entrance into this market is still in the early stages, the product response has been very favorable, demonstrated by our newly established relationship with Indoff, the largest distributor of material handling equipment in the United States.

The Zapino is an electric scooter that is a great link between ZAP's personal transporters and electric cars. Not only economical and eco-friendly, the Zapino is powerful with an advanced 3000-watt brushless DC hub motor, perfect for city commuting. Able to reach speeds of 30 MPH, the Zapino is able to keep up with city traffic without contributing to city pollution. The rear wheel hub motor on the Zapino creates more room on board for additional batteries and performance. This innovative drive system eliminates the need for belts or chains with lower overall maintenance. It also delivers a more enjoyable ride because it is nearly silent, accelerates smoothly with no shifting, has no engine vibration, no tailpipe or heat exhaust -- just good, clean fun.

Off-Road Vehicles

All terrain vehicle ("ATV") manufacturers recognized in excess of \$5.0 billion in revenues in 2006 with the market for ATVs. In the United States alone, approximately 800,000 units were sold in 2006. To date, all of the ATV's on the market are gas-powered. We believe electric ATV's have practical environmental benefits over their gas-powered counterparts: they are silent and generate no emissions. Moreover, there are now over 8,000 organic farms in the United States which are committed to reducing pollutants that may put organic certification at risk. The electric ATVs can provide the ruggedness of the traditional ATV in areas never before accessible, while being more versatile than golf carts.

We entered the electric ATV market in 2006 with our ZAP Buzz mini ATV. The Buzz has a 450 watt geared-motor and a top speed of 15 mph with a range of approximately 20 miles. In the 1st quarter of 2007, we introduced the 800 watt “mid size” ATV for sale in the United States and some of our existing ZAP dealers already have placed preorders. We hope to launch a heavy duty ATV in the 3rd quarter 2008 with product features and styling comparable to existing gas-models. We believe our position as an innovator in the electric vehicle market, coupled with first-mover advantage in the electric ATV market, will allow us to capitalize on this market segment. If we are able to capture 1% of the all terrain vehicle market share, it could equate to over \$40 million in revenues per year. However, there can be no assurances that we will be able to achieve such market share.

Risk factors

We have a history of losses and our future profitability on a quarterly or annual basis is uncertain, which could have a harmful effect on our business and the value of ZAP’s common stock.

We incurred net losses of \$7.5 million, \$9.8 million, \$28 million, for the nine months ended September 30, 2009 and the years ended December 31, 2008, 2007 respectively. We can give no assurance that we will be able to operate profitably in the future.

We face intense competition which could cause us to lose market share.

In the advanced technology vehicle market in the United States, we compete with large manufacturers, including Honda, Toyota, and Nissan, have more significant financial resources, established market positions, long-standing relationships with customers and dealers, and who have more significant name recognition, technical, marketing, sales, manufacturing, distribution, financial and other resources than we do. Each of these companies is currently working to develop, market, and sell advanced technology vehicles in the United States market. The resources available to our competitors to develop new products and introduce them into the marketplace exceed the resources currently available to us. We also face competition from smaller companies with respect to our consumer products, such as our electric bicycle and scooter. We expect to face competition from the makers of consumer batteries and small electronics with respect to the ZAP Portable Energy line. This intense competitive environment may require us to make changes in our products, pricing, licensing, services, distribution, or marketing to develop, maintain, and extend our current technology and market position.

Changes in the market for electric vehicles could cause our products to become obsolete or lose popularity.

The electric vehicle industry is in its infancy and has experienced substantial change in the last few years. To-date, demand for and interest in electric vehicles have been sporadic. As a result, growth in the electric vehicle industry depends on many factors, including: continued development of product technology; the environmental consciousness of customers; the ability of electric vehicles to successfully compete with vehicles powered by internal combustion engines; widespread electricity shortages and the resultant increase in electricity prices, especially in our primary market, California, which could derail our past and present efforts to promote electric vehicles as a practical solution to vehicles which require gasoline; and whether future regulation and legislation requiring increased use of nonpolluting vehicles is enacted.

We cannot assure you that growth in the electric vehicle industry will continue. Our business may suffer if the electric vehicle industry does not grow or grows more slowly than it has in recent years or if we are unable to maintain the pace of industry demands.

We may be unable to keep up with changes in electric vehicle technology and, as a result, may suffer a decline in our competitive position.

Our current products are designed for use with, and are dependent upon, existing electric vehicle technology. As technologies change, we plan to upgrade or adapt our products in order to continue to provide products with the latest technology. However, our products may become obsolete or our research and development efforts may not be sufficient to adapt to changes in or create necessary technology. As a result, our potential inability to adapt and develop the necessary technology may harm our competitive position.

- 22 -

The failure of certain key suppliers to provide us with components could have a severe and negative impact upon our business.

We rely on a small group of suppliers to provide us with components for our products, some of whom are located outside of the United States. If these suppliers become unwilling or unable to provide components, there are a limited number of alternative suppliers who could provide them. Changes in business conditions, wars, governmental changes, and other factors beyond our control or which we do not presently anticipate could affect our ability to receive components from our suppliers. Further, it could be difficult to find replacement components if our current suppliers fail to provide the parts needed for these products. A failure by our major suppliers to provide these components could severely restrict our ability to manufacture our products and prevent us from fulfilling customer orders in a timely fashion.

Product liability or other claims could have a material adverse effect on our business.

The risk of product liability claims, product recalls, and associated adverse publicity is inherent in the manufacturing, marketing, and sale of electrical vehicles. Although we have product liability insurance for our consumer products for risks of up to an aggregate of \$5,000,000, that insurance may be inadequate to cover all potential product claims. We also carry liability insurance on our automobile products. Any product recall or lawsuit seeking significant monetary damages either in excess of our coverage, or outside of our coverage, may have a material adverse effect on our business and financial condition. We may not be able to secure additional product liability insurance coverage on acceptable terms or at reasonable costs when needed. A successful product liability claim against us could require us to pay a substantial monetary award. Moreover, a product recall could generate substantial negative publicity about our products and business and inhibit or prevent commercialization of other future product candidates. We cannot assure you that such claims and/or recalls will not be made in the future.

We must devote substantial resources to implementing a product distribution network.

Our dealers are often hesitant to provide their own financing to contribute to our product distribution network. As a result, we anticipate that we may have to provide financing or other consignment sale arrangements for dealers who would like to participate as our regional distribution centers.

The further expansion of our product distribution network will require a significant capital investment and will require extensive amounts of time from our management. A capital investment such as this presents many risks, foremost among them being that we may not realize a significant return on our investment if the network is not profitable. Our inability to collect receivables from our dealers could cause us to suffer losses. Lastly, the amount of time that our management will need to devote to this project may divert them from performing other functions necessary to assure the success of our business.

Failure to manage our growth effectively could adversely affect our business.

We plan to increase sales and expand our operations substantially during the next several years through internally-generated growth and the acquisition of businesses and products.

To manage our growth, we believe we must continue to implement and improve our operational, manufacturing, and research and development departments. We may not have adequately evaluated the costs and risks associated with this expansion, and our systems, procedures, and controls may not be adequate to support our operations. In addition, our management may not be able to achieve the rapid execution necessary to successfully offer our products and services and implement our business plan on a profitable basis. The success of our future operating activities will also depend upon our ability to expand our support system to meet the demands of our growing business. Any failure by our management to effectively anticipate, implement, and manage changes required to sustain our growth would have a material adverse effect on our business, financial condition, and results of operations. We cannot assure you that we

will be able to successfully operate acquired businesses, become profitable in the future, or effectively manage any other change. An inability to successfully operate recently acquired businesses and manage existing business would harm our operations.

- 23 -

The loss of certain key personnel could significantly harm our business.

The Company's performance is substantially dependent upon the services of its executive officers and other key employees, as well as on its ability to recruit, retain, and motivate other officers and key employees. Competition for qualified personnel is intense and there are a limited number of people with knowledge of and experience in the advanced technology vehicle industry. The loss of services of any of our officers or key employees, or our inability to hire and retain a sufficient number of qualified employees, will harm our business. Specifically, the loss of Mr. Schneider, our Chief Executive Officer or Mr. Starr, our co-founder, whose specialized knowledge of the electric vehicle industry is essential to our business, would be detrimental. We have employment agreements with Mr. Schneider and Mr. Starr that provide for their continued service to the Company until October 1, 2013.

Regulatory requirements may have a negative impact upon our business.

While our products are subject to substantial regulation under federal, state, and local laws, we believe that the products we have sold are materially in compliance with all applicable laws. However, to the extent the laws change, or if we introduce new products in the future, some or all of our products may not comply with applicable federal, state, or local laws. Further, certain federal, state, and local laws and industrial standards currently regulate electrical and electronics equipment. Although standards for electric vehicles are not yet generally available or accepted as industry standards, our products may become subject to federal, state, and local regulation in the future. Compliance with this regulation could be burdensome, time consuming, and expensive.

Our automobile products are subject to environmental and safety compliance with various federal and state regulations, including regulations promulgated by the EPA, NHTSA, and Air Resource Board of the State of California, and compliance certification is required for each new model year. The cost of these compliance activities and the delays and risks associated with obtaining approval can be substantial.

Manufacturing overseas may cause problems for us.

We have been shifting our manufacturing overseas. There are many risks associated with international business. These risks include, but are not limited to, language barriers, fluctuations in currency exchange rates, political and economic instability, regulatory compliance difficulties, problems enforcing agreements, and greater exposure of our intellectual property to markets where a high probability of unlawful appropriation may occur. A failure to successfully mitigate any of these potential risks could damage our business.

We may not be able to protect our internet address.

We currently hold the internet address, <http://www.zapworld.com>, a portal through which we sell our products. We may not be able to prevent third parties from acquiring internet addresses that are confusingly similar to our address, which could adversely affect our business. Governmental agencies and their designees generally regulate the acquisition and maintenance of internet addresses. However, the regulation of internet addresses in the United States and in foreign countries is subject to change. As a result, we may not be able to acquire or maintain relevant internet addresses in all countries where we conduct business.

Our success is heavily dependent on protecting our intellectual property rights.

We rely on a combination of patent, copyright, trademark, and trade secret protections to protect our proprietary technology. Our success will, in part, depend on our ability to obtain trademarks and patents. We hold several patents registered with the United States Patent and Trademark Office. These registrations include both design patents and utility patents. In addition, we have recently submitted provisional patents which may or may not be afforded the limited protection associated with provisional patents. We have also registered numerous trademarks with the United States Patent and Trademark Office, and have several pending at this time. We cannot assure you that the trademarks

and patents issued to us will not be challenged, invalidated, or circumvented, or that the rights granted under those registrations will provide competitive advantages to us.

- 24 -

We also rely on trade secrets and new technologies to maintain our competitive position. Although we have entered into confidentiality agreements with our employees and consultants, we cannot be certain that others will not gain access to these trade secrets. Others may independently develop substantially equivalent proprietary information and techniques or otherwise gain access to our trade secrets.

We may be exposed to liability for infringing intellectual property rights of other companies.

Our success will, in part, depend on our ability to operate without infringing on the proprietary rights of others. Although we have conducted searches and are not aware of any patents and trademarks which our products or their use might infringe, we cannot be certain that infringement has not or will not occur. We could incur substantial costs, in addition to the great amount of time lost, in defending any patent or trademark infringement suits or in asserting any patent or trademark rights, in a suit with another party.

Risk of Unregistered Securities Offering.

In the past, we have had numerous sales of our securities which were not registered under federal or state securities laws. We have strived to comply with all applicable Federal and state securities laws in connection with our issuances of unregistered securities. However, to the extent we have not complied, there may be liability for the purchase price of the securities sold together with interest and the potential of regulatory sanctions.

Our stock price and trading volume may be volatile, which could result in substantial losses for our stockholders.

The equity trading markets may experience periods of volatility, which could result in highly variable and unpredictable pricing of equity securities. The market price of our common stock could change in ways that may or may not be related to our business, our industry or our operating performance and financial condition. In addition, the trading volume in our common stock may fluctuate and cause significant price variations to occur. We have experienced significant volatility in the price of our stock over the past few years. We cannot assure you that the market price of our common stock will not fluctuate or decline significantly in the future. In addition, the stock markets in general can experience considerable price and volume fluctuations.

We have not paid cash dividends on our common stock and do not anticipate paying any cash dividends on our common stock in the foreseeable future.

We have not achieved profitable operations and if we do realize a profit in the future, we anticipate that we will retain all future earnings and other cash resources for the future operation and development of our business. Accordingly, we do not intend to declare or pay any cash dividends on our common stock in the foreseeable future. Payment of any future dividends will be at the direction of our board of directors after taking into account many factors, including our operating results, financial conditions, current and anticipated cash needs and plans for expansion.

Seasonality and Quarterly Results

The Company's business is subject to seasonal influences for consumer products. Sales volumes in this industry typically slow down during the winter months, November to March in the U.S. The Company's auto distribution network is affected by the availability of cars ready to sell to dealers.

Inflation

Our raw materials and finished products and automobiles are sourced from stable, cost-competitive industries. As such, we do not foresee any material inflationary trends for our product sources.

Item 4. Controls and Procedures

Disclosure Controls and Procedures

Our management, under the supervision and with the participation of the Chief Executive Officer and Chief Financial Officer, conducted an evaluation of the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”)) as of the end of the period covered by this report. Based on this evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of such period, our disclosure controls and procedures are effective in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by us in the reports filed, furnished or submitted under the Exchange Act. Our Chief Executive Officer and Chief Financial Officer also concluded that our disclosure controls and procedures are effective to ensure that information required to be disclosed in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosures.

Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting (as defined in Rule 13a-15(f) of the Exchange Act) that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

In the normal course of business, we may become involved in various legal proceedings. Except as stated below, we know of no pending or threatened legal proceeding to which we are or will be a party which, if successful, might result in a material adverse change in our business, properties or financial condition. However, as with most businesses, we are occasionally parties to lawsuits incidental to our business, none of which are anticipated to have a material adverse impact on our financial position, results of operations, liquidity or cash flows. The Company estimates the amount of potential exposure it may have with respect to litigation claims and assessments.

On September 25, 2009, a complaint captioned Al Yousuf LLC v ZAP (Case No. SW 245950) was filed in the Superior Court for the County of Sonoma. The complaint alleges causes of action for judicial foreclosure and deficiency judgment in connection with a loan agreement with Al Yousuf LLC. The President of Al Yousuf LLC, Eqbal Al Yousuf, is a member of ZAP’s board of directors. In its Complaint, Al Yousuf LLC claims that ZAP has failed to make scheduled payments required under the loan agreement which is secured by real property that serves as ZAP’s principal executive offices. Plaintiff seeks to foreclose on the property that secures the loan agreement and recover attorney’s fees of approximately \$125,000, and obtain such other and further relief as the Court may deem just and proper. ZAP has yet responded to the Complaint. The parties are engaged in settlement discussions.

Voltage Vehicles v. Rajun Cajun, et al., Superior Court of California, County of Sonoma, Case No. SCV 240179, filed February 9, 2007. In its Complaint, Voltage Vehicles requests Declaratory Relief against Rajun Cajun, asking the Court to declare that the License Agreement between those two parties does not grant Rajun Cajun an exclusive dealership in

northern Nevada to distribute Voltage Vehicle products and that Voltage Vehicles has performed its obligations under the License Agreement. On April 19, 2007, Rajun Cajun filed a Motion to Quash and/or for Dismissal or Stay. On May 7, 2007 Rajun Cajun voluntarily withdrew its Motion to Quash and/or for Dismissal or Stay. On May 24, 2007 Rajun Cajun filed both an Answer to Voltage Vehicles' Complaint and a Cross-Complaint against Voltage Vehicles. Various complaints and cross complaints were filed by the both parties through April of 2009. On April 29, 2009 Rajun Cajun served its Fourth Amended Cross-complaint and Third Party Complaint ("Fourth Amended Cross-complaint"). The Fourth Amended Cross complaint contains six causes of action, specifically: fraudulent misrepresentation; breach of written contracts—asset purchase agreements; negligence; negligent misrepresentation; securities fraud; and contract rescission for fraud in the inducement. The Fourth Amended Cross-complaint seeks general damages in an amount in excess of \$500,000, damages for Cross-complainants' lost earnings, both past and future, in a sum to be proven at trial, a sum in excess of \$500,000 for Cross-complainants' mental pain, a sum in excess of \$500,000 for willful and wanton misconduct, rescission of the license agreement and consideration paid to Cross-complainants, with interest, costs and attorneys' fees, and such other and further relief the court may deem just and equitable. ZAP and Voltage Vehicles have both responded to the Fourth Amended Cross-complaint and filed a motion for summary judgment, or in the alternative summary adjudication. On September 18, 2009, the court granted ZAP and Voltage Vehicles' motion for summary judgment on the Fourth Amended Cross-Complaint. Cross-complainants have stated that they will appeal the ruling. In that all substantive issues have been resolved in ZAP's and Voltage Vehicles' favor with the granting of summary judgment, Voltage Vehicles dismissed its Complaint without prejudice on October 23, 2009.

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

The following lists sales of unregistered securities during the quarter ended September 30, 2009 that were not previously included in a Quarterly Report on Form 10-Q or a Current Report on Form 8-K. We relied on the exemption from registration afforded by Section 4(2) of the Securities Act of 1933, as amended (the "Securities Act") for the issuance of these securities. Except as stated below, no underwriting discounts or commissions were payable with respect to any of the following transactions. The offer and sale of the following securities was exempt from the registration requirements of the Securities Act under Rule 506 insofar as (1) except as stated below, each of the investors was accredited within the meaning of Rule 501(a); (2) the transfer of the securities were restricted by the company in accordance with Rule 502(d); (3) there were no more than 35 non-accredited investors in any transaction within the meaning of Rule 506(b), after taking into consideration all prior investors under Section 4(2) of the Securities Act within the twelve months preceding the transaction; and (4) none of the offers and sales were effected through any general solicitation or general advertising within the meaning of Rule 502(c).

On July 27, 2009, the Company issued 400,000 shares of common stock for a private placement valued at \$100,000.

On August 17, 2009, the Company issued 22,222 shares valued at \$10,000 for marketing services.

Item 3. Defaults upon Senior Securities

Related Party Dispute

Please note the indebtedness is due to a related party—Al Yousuf LLC whose President Mr. Eqbal Al Yousuf is also a Director of ZAP.

On July 30, 2008 we received a \$10 million financing arrangement from the Al Yousuf Group, a Dubai-based conglomerate to provide future working capital to ZAP and help meet the growing demand for ZAP electric vehicles. The financing arrangement allows for advances by ZAP over the next few years commencing on the date of the Note. The initial outstanding principal sum advanced to the Company is \$1,760,000. This advance was used to pay-off the existing secured note payable on the building. The Note matures February 28, 2010. Interest only payments are due

under the Note monthly commencing August 30, 2008. All principal and interest due under the Note is secured by the corporate headquarters building in Santa Rosa, California

- 27 -

On May 14, 2009 we received a Notice of Delinquent Payments from Mr. Hossein Haghighi, the Chief Financial Officer of Al Yousuf LLC, notifying us that an outstanding principle for inventory advances of \$3.8 million plus monthly interest payments has not been paid as required by a \$10 million Promissory Note. Mr. Haghighi further indicated that AL Yousuf LLC intended to enforce the collection of the total amounts due under the terms of the note against the Company. The collateral for the note is our corporate headquarters building and land located in Santa Rosa California. The total due on the note, including interest, is approximately \$5.6 million at September 30, 2009 with inventory advances totaling \$3.8 million and a building loan of \$1.8 million plus interest.

On September 25, 2009, a complaint captioned Al Yousuf LLC v ZAP (Case No. SW 245950) was filed in the Superior Court for the County of Sonoma. The complaint alleges causes of action for judicial foreclosure and deficiency judgment in connection with a loan agreement with Al Yousuf LLC. The President of Al Yousuf LLC, Eqbal Al Yousuf, is a member of ZAP's board of directors. In its Complaint, Al Yousuf LLC claims that ZAP has failed to make scheduled payments required under the loan agreement which is secured by real property that serves as ZAP's principal executive offices. Plaintiff seeks to foreclose on the property that secures the loan agreement and recover attorney's fees of approximately \$125,000, and obtain such other and further relief as the Count may deem just and proper. ZAP has yet responded to the Complaint. The parties are engaged in settlement discussions.

Item 6.Exhibits

2.1Approved Second Amended Plan of Reorganization, dated as June 20, 2002. (5)

3.1Amended and Restated Articles of Incorporation. (4)

3.2Certificate of Determination of Series SA Convertible Preferred Stock. (14)

4.1Form of common share purchase warrant of the Company held by Fusion Capital Fund II, L.P. (6)

4.2Form of Series B common stock purchase warrant of the Company. (14)

4.3Form of Series K common stock purchase warrant of the Company. (14)

10.1Settlement Agreement between ZAPWORLD.COM, Ridgewood ZAP, LLC, and the Shareholders dated June 27, 2001. (3)

10.32004 Consultant Stock Plan. (7)

Edgar Filing: ZAP - Form 10-Q

- 10.4 Convertible Promissory Note, dated April 26, 2004, issued to Banks Living Trust. (1)
- 10.5 Purchase and Sale Agreement dated March 7, 2003 between ATOCHA Land LLC and ZAP. (3)
- 10.6 Promissory Note \$2,000,000 - Atocha Land LLC and ZAP. (3)
- 10.7 Warrant Agreement dated April 26, 2004, issued to Banks Living Trust. (1)
- 10.8 Common Stock Purchase Agreement between ZAP and Fusion Capital Fund II, LLC. (6)
- 10.9 Registration Rights Agreement between ZAP and Fusion Capital Fund II, LLC. (6)
- 10.10 Form of Common Stock Purchase Warrant between ZAP and Fusion Capital Fund II, LLC (6)
- 10.11 Agreement for Consulting Services with Evan Rapoport dated January 8, 2004. (1)
- 10.12 Asset Purchase Agreement dated April 12, 2004 with Jeffrey Banks for purchase of various autos (1)
- 10.13 Agreement for Private Placement Investment received dated April 14, 2004 with Phi-Nest Fund LLP (1)
- 10.14 Consulting Agreement dated April 21, 2004 with Elexis International (1)
- 10.15 Consulting Agreement dated April 21, 2004 with Sunshine 511 Holdings (1)
- 10.16 Definitive Stock Agreement dated October 25, 2004 with Smart-Automobile, LLC (2)
- 10.17 Master Distribution Agreement between Apollo Energy Systems, Inc. and Voltage Vehicles Corporation, a subsidiary of ZAP. (8)
- 10.18 ZAP Floor Line and Dealer Development Agreement with Clean Air Motors, LLC for a \$45 Million Floor Plan Line of Credit for Qualified ZAP Dealers (9)
- 10.19 Exclusive Purchase, License and Supply Agreement between Smart Automobile, LLC and ZAP. (10)
- 10.20 Amendment dated November 15, 2004 to previous consulting agreement with Sunshine Holdings 511 (14)
- 10.21 Secured Promissory Note Payable dated December 30, 2004 with Phi-Nest Fund, LLP. (14)
- 10.22 ZAP assignment of 2.9 million shares of Restricted Common Stock to Phi-Nest Fund, LLP as collateral on note payable (14)
- 10.23 Promissory note receivable dated January 6, 2005 for \$1 million loan due from Smart Automobile, LLC and Thomas Heidemann (President Smart Automobile, LLC) (14)
- 10.24 Security Agreement dated January 6, 2005 from Smart Automobile, LLC and Thomas Heidemann (President Smart Automobile, LLC) to secure loan above. (14)
- 10.25 Common Stock Purchase Agreement between ZAP and Platinum Partners Value Arbitrage Fund LP (14)
- 10.26 Form of Common Stock Purchase Warrant between ZAP and Platinum Partners Value Arbitrage Fund LP (14)
- 10.27 Common Stock Purchase Agreement between ZAP and Lazarus Investment Partners LLP (14)

10.28 Form of Common Stock Purchase Warrant between ZAP and Lazarus Investment Partners LLP (14)

10.29 Termination of Common Stock Purchase Agreement between ZAP and Fusion Capital Fund II, LLC (11)

- 29 -

Edgar Filing: ZAP - Form 10-Q

- 10.30 Financing Agreement between ZAP and Surge Capital II, LLC (12)
- 10.31 Exclusive Purchase, License, and Supply Agreement between ZAP and Obvio! Automotoveiculos S.P.E. Ltda (13)
- 10.36 Agreement dated July 14, 2006 between ZAP, Thomas Heidemann and Smart Automobile (15)
- 10.37 Amendment Agreement Dated August 30, 2006 between ZAP and Smart Automobile LLC (16)
- 10.38 Exclusive Distribution Agreement dated May 1, 2005, as supplemented by a letter dated June 9, 2006 (17)
- 10.39 ZAP Guarantee (18)
- 10.40 Shandong Jindalu Vehicle Co., Ltd. Guarantee (19)
- 10.41 Joint Venture Negotiations dated September 21, 2006 (20)
- 10.42 Security Purchase Agreement between ZAP and Certain Institutional Investors (21)
- 10.43 Purchase and Amendment Agreement between ZAP and Certain Institutional Investors (22)
- 10.44 Form of Convertible
- 10.45 Form of Warrant
- 10.46 Purchase order from the Electric Vehicle Company, LLC (“EVC”) for 10,000 of its Xebra 2007 model year electric vehicles
- 10.47 Distribution agreement this week with PML FlightLink Limited (PML) for the purchase of an advanced wheel motor and control system
- 10.48 Joint Venture Agreement with Youngman Automobile Co., Ltd to manufacture, market and distribute electric and hybrid vehicles for the worldwide passenger car, truck and bus
- 10.49 Form SB-2 Registration of Common Stock incorporated by reference to SEC filing on September 24, 2007 effective on October 2, 2007.
- 10.50 Settlement and Mutual Release Agreement with Gemini Master Fund, LTD and Gemini Strategies, LLC dated May 7, 2008. (22)
- 10.51 Note Purchase Agreement with Al Yousuf dated May 8, 2008. (22)
- 10.52 Promissory Note in favor of AlYousuf LLC, dated July 30, 2008 and Deed of Trust, Assignment of Leases, Rents and Security Agreement and Fixture Filing by ZAP in favor of Al Yousuf LLC, dated July 30, 2008.(23)
- 10.53 Subscription Agreement dated June 9, 2009 from The Banks Group, LLC. (24)
- 10.54 Subscription Agreement dated June 9, 2009 from The Banks Development Trust. (24)
- 10.55 Warrant to Purchase Common Stock dated June 9, 2009 issued to The Banks Group, LLC. (24)

Edgar Filing: ZAP - Form 10-Q

10.56 Warrant to Purchase Common Stock dated June 9, 2009 issued to The Banks Development Trust (24)

10.57 Employment Agreement with Gary Dodd President of ZAP (25)

- 30 -

Edgar Filing: ZAP - Form 10-Q

10.58 Securities Purchase Agreement dated August 6, 2009 with Cathaya Capital L.P (26)

10.59 Secured Convertible Promissory Note dated August 6, 2009 with Cathaya Capital L.P (26)

10.60 Security Agreement dated August 6, 2009 with Cathaya Capital L.P (26)

10.61 Warrant (First) to Purchase Common Stock dated August 6, 2009 with Cathaya Capital L.P (26)

10.62 Warrant (Second) to Purchase Common Stock dated August 6, 2009 with Cathaya Capital L.P (26)

10.63 Registration Rights Agreement dated August 6, 2009 with Cathaya Capital L.P (26)

10.64 Voting Agreement dated August 6, 2009 with Cathaya Capital L.P (26)

10.65 Indemnification Agreement dated August 6, 2009 with Priscilla Lu (26)

10.66 Amendment to Prior Employment Agreements dated August 6, 2009 with Steven Schneider (26)

21.1 List of subsidiaries. (3)

31.1 Certification of Principal Executive Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Exchange Act, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. (22)

31.2 Certification of Principal Financial Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Exchange Act, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. (22)

32.1 Certification of Principal Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. (22)

32.2 Certification of Principal Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes Oxley Act of 2002. (22)

(1) Previously filed as an exhibit to the Registrant's Form 8-K for the quarter ended March 31, 2004 and incorporated by reference.

(2) Previously filed as an exhibit to the Registrant's Form 8-K of November 6, 2004 and incorporated by reference.

(3) Previously filed as an exhibit to the Registrant's Annual Report on Form 10-KSB for the year ended December 31, 2003 and incorporated by reference.

(4) Previously filed with Pre-effective Amendment Number 3 to Form SB-2 registration statement filed with the Securities and Exchange Commission on October 3, 2001.

(5) Previously filed as an exhibit to the Registrant's Form 8-K of October 20, 2002 and incorporated by reference.

(6) Previously filed as an exhibit to the Registrant's Current Report on Form 8-K dated July 22, 2004 and incorporated by reference.

(7) Previously filed as an exhibit to the Registrant's Registration Statement on Form S-8 (File No. 333-117560) on July 22, 2004.

(8) Previously filed as an exhibit to the Registrant's Current Report on Form 8K filed with the Securities and Exchange Commission on October 6, 2004 and incorporated herein by reference.

(9) Previously filed as an exhibit to the Registrant's Quarterly Report on Form 10QSB for the period ended September 30, 2004 and incorporated herein by reference.

(10) Previously filed as an exhibit to the Registrant's Current Report on Form 8K filed with the Securities and Exchange Commission on April 21, 2004 and incorporated herein by reference.

(11) Previously filed as an exhibit to the Registrant's Current Report on Form 8K filed with the Securities and Exchange Commission on February 25, 2005 and incorporated herein by reference.

(12) Previously filed as an exhibit to the Registrant's Current Report on Form 8K filed with the Securities and Exchange Commission on September 16, 2005 and incorporated herein by reference.

- 31 -

- (13) Previously filed as an exhibit to the Registrant's Current Report on Form 8K filed with the Securities and Exchange Commission on September 21, 2005 and incorporated herein by reference.
- (14) Previously filed as an exhibit to the Registrant's Current Report on Form 8K filed with the Securities and Exchange Commission on July 20, 2006 and incorporated herein by reference.
- (15) Previously filed as an exhibit to the Registrant's Current Report on Form 8K filed with the Securities and Exchange Commission on September 6, 2006 and incorporated herein by reference.
- (16) Previously filed as an exhibit to the Registrant's Current Report on Form 8K filed with the Securities and Exchange Commission on November 6, 2006 and incorporated herein by reference.
- (17) Previously filed as an exhibit to the Registrant's Current Report on Form 8K filed with the Securities and Exchange Commission on November 6, 2006 and incorporated herein by reference.
- (18) Previously filed as an exhibit to the Registrant's Current Report on Form 8K filed with the Securities and Exchange Commission on November 6, 2006 and incorporated herein by reference.
- (19) Previously filed as an exhibit to the Registrant's Current Report on Form 8K filed with the Securities and Exchange Commission on November 6, 2006 and incorporated herein by reference.
- (20) Previously filed as an exhibit to the Registrant's Current Report on Form 8K filed with the Securities and Exchange Commission on December 11, 2006 and incorporated herein by reference.
- (21) Previously filed as an exhibit to the Registrant's Current Report on Form 8K filed with the Securities and Exchange Commission on February 26, 2007 and incorporated herein by reference.
- (22) Previously filed as an exhibit to the Registrant's Quarterly Report on Form 10Q for the period ended September 30, 2008 and incorporated herein by reference.
- (23) Previously filed as an exhibit to the Registrant's Current Report on Form 8K filed with the Securities and Exchange Commission on August 5, 2008 and incorporated herein by reference.
- (24) Previously filed as an exhibit to the Registrant's Current Report on Form 8K filed with the Securities and Exchange Commission on June 11, 2009 and incorporated herein by reference.
- (25) Previously filed as an exhibit to the Registrant's Current Report on Form 8K filed with the Securities and Exchange Commission on June 18, 2009 and incorporated herein by reference.
- (26) Previously filed as an exhibit to the Registrant's Current Report on Form 8K filed with the Securities and Exchange Commission on August 10, 2009 and incorporated herein by reference.

SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

ZAP

Dated: November 16, 2009

By: /s/ Steven Schneider
Name: Steven Schneider
Title: Chief Executive Officer
(Principal Executive Officer)

Dated: November 16, 2009

By: /s/ William Hartman
Name: William Hartman
Title: Chief Financial Officer
(Principal Financial and Accounting
Officer)