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

FORM 10-Q

☑ QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2012

OR

☐ TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE EXCHANGE ACT

For the transition period from ______ to ______

Commission file number 000-33155

COATES INTERNATIONAL, LTD.

(Exact Name of Registrant as Specified in its Charter)

Delaware	**22-2925432**
(State or other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

Highway 34 & Ridgewood Road, Wall Township, New Jersey 07719
(Address of Principal Executive Office) (Zip Code)

(732) 449-7717
(Registrant's telephone number including area code)

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

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

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

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

Large accelerated filer	☐	Accelerated filer Non-accelerated filer	☐
Non-accelerated filer (Do not check if a smaller reporting company)	☐	Smaller reporting company	☑

As of May 11, 2012, 297,803,294 shares of the Registrant’s common stock, par value $0.001 per share were issued and outstanding.

COATES INTERNATIONAL, LTD.
QUARTERLY REPORT ON FORM 10-Q

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MARCH 31, 2012

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Coates International, Ltd.
Consolidated Balance Sheets

	March 31, 2012 (Unaudited)	December 31, 2011
Assets		
Current Assets		
Cash	$ 932	$ 52,955
Inventory, net	344,333	387,483
Deferred offering costs	27,382	33,969
Total Current Assets	372,647	474,407
Property, plant and equipment, net	2,289,075	2,303,073
Deferred licensing costs, net	58,512	59,583
Total Assets	$ 2,720,234	$ 2,837,063
Liabilities and Stockholders' Deficiency		
Current Liabilities		
Accounts payable and accrued liabilities	$ 1,444,861	$ 1,304,309
Deferred stock-based compensation payable	451,800	451,800
Mortgage loan payable	1,620,000	1,630,000
Promissory notes to related parties	465,040	447,440
Convertible promissory notes, net of unamortized discount	105,713	111,775
Derivative liability related to convertible promissory notes	214,261	243,306
Unearned revenue	29,124	29,124
10% Convertible note	10,000	10,000
Total Current Liabilities	4,340,799	4,227,754
License deposits	355,800	360,600
Total Liabilities	4,696,599	4,588,354
Commitments and Contingencies		
Stockholders' Deficiency		
Preferred Stock, $0.001 par value, 100,000,000 shares authorized, 72,883 shares issued and outstanding at March 31, 2012 and December 31, 2011.	73	73
Common Stock, $0.0001 par value, 1,000,000,000 shares authorized, 291,409,978 and 284,127,846 shares issued and outstanding at March 31, 2012 and December 31, 2011, respectively	29,141	28,413
Additional paid-in capital	26,090,743	24,917,261
Accumulated deficit	(28,096,322)	(26,697,038)
Total Stockholders' Deficiency	(1,976,365)	(1,751,291)
Total Liabilities and Stockholders' Deficiency	$ 2,720,234	$ 2,837,063

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

Coates International, Ltd.
Consolidated Statements of Operations
Unaudited

	For the Three Months Ended March 31,	
	2012	**2011**
Sublicensing fee revenue	$ 4,800	$ -
Total Revenues	4,800	-
Expenses:		
Research and development costs	186,066	20,858
General and administrative expenses	1,054,776	349,265
Depreciation and amortization	15,068	16,654
	1,255,910	386,777
	(1,251,110)	(386,777)
Other Operating Expense:		
Decrease (increase) in estimated fair value of embedded derivative liabilities	28,592	(17,160)
Loss from Operations	(1,222,518)	(403,937)
Interest expense, net	176,767	139,332
Loss Before Income Taxes	(1,399,285)	(543,269)
Provision for income taxes	-	-
Net Loss	$ (1,399,285)	$ (543,269)
Basic net loss per share	$ -	$ -
Basic weighted average shares outstanding	287,565,082	276,531,131
Diluted net loss per share	$ -	$ -
Diluted weighted average shares outstanding	287,565,082	276,531,131

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

Coates International Ltd.
Condensed Consolidated Statements of Cash Flows
Unaudited

	For the Three Months Ended March 31,	
	2012	**2011**
Net Cash Flows Used in Operating Activities	$ (361,766)	$ (280,570)
Cash Flows Used in Investing Activities:		
Acquisition of property, plant and equipment	-	(4,790)
Net Cash Used in Investing Activities	-	(4,790)
Cash Flows Provided by (Used in) Financing Activities:		
Issuance of common stock and warrants	250,143	200,000
Issuance of convertible promissory note	52,000	32,500
Issuance of promissory notes to related parties	42,600	37,000
Repayment of promissory notes to related party	(25,000)	(12,000)
Release from Interest reserve	-	30,000
Repayment of Mortgage Loan	(10,000)	(30,000)
Net Cash Provided by Financing Activities	309,743	257,500
Net Decrease in Cash	(52,023)	(27,860)
Cash, beginning of period	52,955	53,360
Cash, end of period	$ 932	$ 25,500
Supplemental Disclosure of Cash Flow Information:		
Cash paid during the period for interest	$ 20,349	$ 31,885
Supplemental Disclosure of Non-cash Financing Activities:		
Conversion of convertible promissory notes	$ 135,720	$ 93,500
Conversion of promissory notes to related parties	-	180,000
	$ 135,720	$ 273,500

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

Coates International, Ltd.
Notes to Consolidated Financial Statements
(All amounts rounded to thousands of dollars)
(Unaudited)

1. BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements of Coates International, Ltd. and its wholly-owned subsidiary (the "Company") have been prepared in accordance with accounting principles generally accepted for interim financial information and rules and regulations of the Securities and Exchange Commission (the "SEC"). Accordingly, they do not include all of the information and notes required by generally accepted accounting principles in the United States ("GAAP") for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. The results of operations for the three months ended March 31, 2012 and 2011 are not necessarily indicative of the results that may be expected for any other interim period or for the full year. The unaudited consolidated financial statements should be read in conjunction with the financial statements and notes thereto included in the Company's annual report on Form 10-K for the year ended December 31, 2011.

The Company incurred a net loss for the three months ended March 31, 2012 of ($1,399,000), and has incurred substantial net losses since inception while engaging primarily in research and development. As of March 31, 2012, the Company had an accumulated deficit of ($28,096,000) and had negative working capital of ($3,968,000). In addition, the current economic environment, which is characterized by tight credit markets, investor uncertainty about how to safely invest funds and low investor confidence, has introduced additional risk and difficulty in the Company's challenge to secure needed additional working capital. These factors raise substantial doubt about the Company's ability to continue as a going concern.

The Company has been actively undertaking efforts to secure new sources of working capital. During the three months ended March 31, 2012, the Company raised new working capital of $320,000 consisting of proceeds of $225,000 from the sale of common stock to Dutchess Opportunity Fund II, LP, proceeds from issuance of convertible promissory notes amounting to $52,000, consideration received from the sale of common stock to the son of a director amounting to $25,000 and proceeds from issuance of promissory notes to related parties, net of repayments of $18,000. Subsequent to March 31, 2012, the Company raised additional working capital aggregating $163,000, consisting of proceeds from the sale of common stock and warrants of $84,000, proceeds from issuance of an additional convertible promissory note of $43,000 and proceeds from the issuance of promissory notes to related parties of $36,000. The Company continues to actively seek out new sources of working capital; however, there can be no assurance that it will be successful in these efforts. The accompanying consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

The doubt about the Company's ability to continue to operate as a going concern has existed for a number of years. Management has been successful in raising sufficient new working capital throughout that time to enable the Company to continue as a going concern and, although management cannot provide assurances that it can be successful, management believes that it can continue to do so in the future. Management has instituted a cost control program intended to cut variable costs to only those expenses that are necessary to carry out its activities related to research and development and manufacturing natural gas-fueled industrial electric power Coates Spherical Rotary Valve ("CSRV") Gen Sets, entering the production phase of operations, developing additional commercially feasible applications of the CSRV system technology, seeking additional sources of working capital and covering the general and administrative expenses in support of such activities.

2. ACCOUNTING POLICIES

Principles of Consolidation

For the quarter ended March 31, 2012, the financial statements of the Company were consolidated with the accounts of Coates Oklahoma Engine Manufacturing, Ltd., a wholly owned subsidiary which was formed in August 2011. All significant intercompany transactions and accounts were eliminated in consolidation.

Net Loss per Share

Basic net income (loss) per share is based on the weighted average number of common shares outstanding without consideration of potentially dilutive shares of common stock. Diluted net income (loss) per share is based on the weighted average number of common and potentially dilutive common shares outstanding, when applicable.

Use of Estimates

The preparation of the Company's consolidated financial statements in conformity with GAAP for interim financial information and rules and regulations of the SEC requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. These significant estimates include determining a value for the Series A Preferred Stock issued and certain limited anti-dilution rights granted to George J. Coates, determining the amount of discount on convertible promissory notes, measuring the estimated fair value of embedded derivative liabilities related to convertible promissory notes outstanding, assigning useful lives to property, plant and equipment, determining an appropriate amount to reserve for obsolete and slow moving inventory, determining the amount of the allowance for deferred tax assets, assigning expected lives to and estimating the rate of forfeitures of stock options granted and selecting a volatility factor for stock options in order to estimate the fair value of the Company's stock options on the date of grant.

3. CONCENTRATIONS OF CREDIT AND BUSINESS RISK

At March 31, 2012, the Company maintained cash balances with one financial institution. The current balances in the accounts at this institution are fully insured by the Federal Deposit Insurance Corporation.

The Company's operations are devoted to the development, application and marketing of the CSRV system technology which was invented by George J. Coates, the Company's founder and his son Gregory Coates. George J. Coates is the Chairman, Chief Executive Officer, President and controlling stockholder of the Company. From July 1982 through May 1993, seven U.S. patents as well as a number of foreign patents were issued with respect to the CSRV system technology. Since the inception of the Company in 1988, all aspects of the business have been completely dependent upon the activities of George J. Coates. The loss of George J. Coates' availability or service due to death, incapacity or otherwise would have a material adverse effect on the Company's business and operations. The Company does not presently have any key-man life insurance in force for Mr. Coates.

The Company is highly dependent on Almont Energy, Inc. ("Almont") for cash flows, revenues and profits from a research and development agreement and exclusive sublicensing agreements covering sale and distribution of natural gas fueled, industrial electric power CSRV engine generators ("Gen Sets") within the territories of Canada and the United States. As discussed in more detail in Note 5, at March 31, 2012, Almont owed the Company approximately $5.8 million dollars due under the research and development, sublicensing and escrow agreements. Payment of this balance is dependent on Almont's success in securing working capital financing and/or raising new equity capital. Almont has been unable to make substantial payments towards this balance due. Almont made a payment of $150,000 during the year ended December 31, 2011 and did not make any payments in the first quarter of 2012.

4. LICENSING AGREEMENT AND DEFERRED LICENSING COSTS

The Company holds a manufacturing, use, lease and sale license from George J. Coates and Gregory Coates for the CSRV system technology in the territory defined as the Western Hemisphere (the “License Agreement”). Under the License Agreement, George J. Coates and Gregory Coates granted to the Company an exclusive, perpetual, royalty-free, fully paid-up license to the intellectual property that specifically relates to an internal combustion engine that incorporates the CSRV system technology (the “CSRV Engine”) and that is currently owned or controlled by them (the “CSRV Intellectual Property”), plus any CSRV Intellectual Property that is developed by them during their employment with the Company. In the event of insolvency or bankruptcy of the Company, the licensed rights would terminate and ownership would revert back to George J. Coates and Gregory Coates.

Under the License Agreement, George J. Coates and Gregory Coates agreed that they will not grant any licenses to any other party with respect to the CSRV Intellectual Property.

At March 31, 2012, deferred licensing costs, comprised of expenditures for patent costs incurred pursuant to the CSRV licensing agreement, net of accumulated amortization, amounted to $59,000. Amortization expense for the three months ended March 31, 2012 and 2011 amounted to $1,000 and $1,000, respectively.

5. AGREEMENTS ASSIGNED TO ALMONT ENERGY INC.

Almont Energy Inc. (“Almont”), a privately held, independent third party entity based in Alberta, Canada is the assignee of a sublicense which provides for a $5,000,000 license fee to be paid to the Company and covers the use of the CSRV system technology in the territory of Canada in the oil and gas industry (the “Canadian License”). Almont is also the assignee of a separate research and development agreement (“R&D Agreement”) which requires that Almont pay the remaining balance of an additional $5,000,000 fee to the Company in consideration for the development and delivery of certain prototype engines. The Company completed development of the prototypes in accordance with this agreement at the end of 2007. The research and development agreement had not been reduced to the form of a signed, written agreement.

Almont is also the assignee of an escrow agreement that provides conditional rights to a second sublicense agreement from the Company for the territory of the United States (the “US License”). The US License has been deposited into an escrow account and the grant of the license will not become effective until the conditions for release from escrow are satisfied. The US License provides for a license fee of $50 million.

The Escrow Agreement requires that Almont, as the assignee, make a payment (“Release Payment”) to the Company equal to the then remaining unpaid balance of the Canadian License licensing fee, the R&D Agreement fee and the down payment of $1,000,000 required under the US License. Almont made a $150,000 nonrefundable payment to the Company to pay down the Release Payment during the year ended December 31, 2011. At March 31, 2012, the remaining balance of the Release Payment was $5,847,000. It is not likely that Almont will be able to make additional payments of the Release Payment unless it can raise new working capital and/or experience positive cash flow from its operations. This has delayed the Company’s plans to commence production of the Gen Sets.

In connection with the assignment of the Canadian License and the rights to the US License, Almont has also assumed all of the obligations set forth in the escrow agreement, with the following modifications:

- At the time of the assignment, the remaining unpaid balance of the Release Payment was approximately $6 million. Provided that Almont remits this entire unpaid balance to the Company on or before the Release Payment Date, the US License will be released from escrow and granted to Almont. The Release Payment Date, as defined in the Escrow Agreement lapsed in March. The Company has verbally agreed to extend the Release Payment Date under the Escrow Agreement to compensate for the delay caused by the late delivery of Gen Sets. Almont is required to remit to the Company 60% of all monies it raises from future equity or debt transactions, exclusive of proceeds from equipment purchase financing transactions, until the Release Payment is paid in full.

- Almont also became obligated to pay the $49 million balance of the US License Fee to the Company. Payment shall be made quarterly in an amount equal to 5% of Almont's quarterly net profits. In addition, Almont is required to remit a portion of the proceeds it receives from equity or debt transactions, exclusive of equipment financing transactions to the Company until the entire balance of the US License fee is paid in full. In any event, the entire $49 million licensing fee is required to be paid on or before February 19, 2015. The Company has also verbally agreed to extend this date to compensate for the delay caused by the late delivery of Gen Sets.

Payment of the Release Payment is dependent on us starting up production to fulfill Almont's orders. To the extent that Almont is not successful or experiences delays in remitting the balance of the Release Payment, the Company's cash flow, results of operations and financial condition will be adversely affected.

The Canadian License

The Canadian License exclusively sublicenses within Canada the use of the CSRV system technology for industrial engines designed to generate electrical power. Additional provisions of the Canadian License agreement are as follows:

- Sublicensee shall have the exclusive right to use, lease and sell electric power generators designed with the CSRV system technology within Canada.
- Sublicensee will have a specified right of first refusal to market the electric power generators worldwide.
- Upon commencement of the production and distribution of the electric power generators, the minimum annual number of generators to be purchased by Sublicensee in order to maintain exclusivity is 120. The Company has temporarily waived this provision due to the delay in delivery of Gen Sets. In the event Sublicensee fails to purchase the minimum 120 CSRV generator engines during any year, Sublicensee will automatically lose its exclusivity. In such a case, Sublicensee would retain non-exclusive rights to continue to use and sell the CSRV generator engines in the territory of Canada. Until otherwise agreed between the parties, the price per generator shall be $159,000. The Company has agreed to pass along to Almont savings, if any, realized from economies of scale inherent in high volume production of the CSRV units.
- Sublicensee is required to pay a royalty to the Company equal to 5% of its annual modified gross profit (which has been defined as sales, less cost of sales, plus $400,000.
- All licensed rights under this license agreement related to the CSRV system technology will remain with the Company.

The US License

The US License will, upon Almont satisfying the Release Payment, grant to Almont the right to use, sell and lease within the defined territory, Licensed Products manufactured by the Company which are designed to generate electrical power. Licensed Products consist of CSRV Valve Systems, CSRV Valve Seals, CSRV Rotary Valve Spheres, CSRV Valve Components and CSRV Engines. Almont is also obligated to pay a royalty to the Company equal to 2.5% of its annual modified gross profit (which has been defined as sales, less cost of sales, plus $400,000.

The manufacture of any Licensed Products by Sublicensee is prohibited. Sublicensee is required to procure all internal combustion engines incorporating the CSRV Valve System from the Company or its designee. The license granted to Sublicensee is exclusive within the Territory, provided that Sublicensee satisfies the minimum annual purchase commitment of 120 internal combustion engines incorporating the CSRV system technology, the Coates Engines and all component parts. The Company has temporarily waived this provision due to the delay in delivery of Gen Sets. The agreement also grants Sublicensee a right of first refusal in the event that the Company negotiates an offer with another third party for a worldwide license to use the Licensed Products for the generation of electrical power.

The business plan of Almont, which is highly dependent on its ability to raise sufficient additional working capital, assumes the purchase of a substantial number of CSRV units over the next 5 years. Almont's purchase of CSRV Units from the Company will be made by way of standard purchase orders, issued based on market and customer demand. Over the 5-year period, Almont anticipates that the volume of total purchases from the Company will be similar to, or potentially exceed the 7,400 CSRV Gen Set quantity contemplated in our previous arrangement with WWE. We are unable to confirm these order s until we have sufficient working capital in place to manufacture generators on a large scale. Almont plans to finance its purchases from cash flow and by way of project and/or equipment financing, proceeds from issuance of equity or corporate debt instruments and conventional bank financing.

6. NON-BINDING PRELIMINARY LETTER OF INTENT TO MERGE WITH S.W.T. IN CHINA

In May 2011, the Company entered into a non-binding letter of intent with S.W.T., an established heavy equipment manufacturer in China and The Coates Trust. The letter expressed the mutual intent of the parties to exchange shares of common stock between the Company and S.W.T., a cash payment to the shareholders of S.W.T. and the issuance of shares of the Company's common stock to The Coates Trust in consideration of a CSRV technology license for China. The transaction would be subject to required governmental approvals and a number of other prerequisite conditions. In September 2011, the Company determined that the risk of proceeding with this merger transaction as contemplated at that time was greater than anticipated. Accordingly, the Company will either continue to explore the possibility of restructuring the merger transaction or taking a simpler approach that would enable it to have access to the manufacturing capabilities of S.W.T. while affording both companies the opportunity to benefit from CSRV system technology related manufacturing activities. At this time, further discussions with S.W.T. are on hold for at least the next 90 days, while the Company focuses on raising working capital and starting production.

7. COOPERATION AGREEMENT WITH TONGJI UNIVERSITY OF CHINA

In June 2010, the Company and the Coates Trust (collectively "Coates") entered into a Cooperation Agreement with Tongji University of China (the "University") for the purpose of enabling the University to undertake an evaluation and testing of the CSRV engine technology. The results of the evaluation and testing will be used to determine if, and to what extent, the engine technology could be applied in the manufacture and distribution of products in China. Coates is required to deliver to the University a 1600cc, 4-cylinder CSRV engine and a 1600cc, 4-cylinder poppet valve engine to facilitate comparison. The University is responsible for obtaining any required regulatory approvals in connection with the evaluation and testing activities. The costs and expenses of testing and evaluation of the engine shall be the responsibility of the University. Coates is required to provide technical assistance, as needed, to optimize the success of the evaluation and testing.

The University is to promptly furnish Coates with a copy of its findings. Provided the results of the evaluation and testing of the CSRV engines are deemed satisfactory, Coates has agreed that it will sublicense the CSRV technology to Chinese engine manufacturers. The parties also entered into a Confidentiality and Non-Disclosure Agreement which provides for protection of the CSRV technical information and patents. The Coates Trust has expressed its intention to license the CSRV system technology rights to the Company for the territory to be defined in connection with any such licenses granted to Chinese manufacturers. To date, the terms of any such license have not been determined. At this time, the parties are not actively working on this cooperation agreement, but may agree to do so at some point in the future.

8. INVESTMENT IN COATES OKLAHOMA ENGINE MANUFACTURING, LTD.

In August 2011, the Company formed a new wholly-owned subsidiary, Coates Oklahoma Engine Manufacturing, Ltd., a Delaware corporation for the purpose of raising working capital and establishing manufacturing operations in the state of Oklahoma. At this time, it has not commenced operations and has only incurred minimal start up expenses. It is working on opportunities to raise working capital, continuing to negotiate for a package of business and tax incentives with the State of Oklahoma and is searching for a suitable manufacturing facility within the State.

9. LICENSE DEPOSITS

License deposits, which are non-refundable, primarily relate to a $300,000 sublicense deposit received in prior years from WWE as a down payment on the Canadian License. The Company is recognizing the license deposit of $300,000 on the Canadian Licensee as revenue on a straight-line basis over the approximately 16-year remaining life of the last CSRV technology patent in force at that date. Sublicensing fee revenue for the three months ended March 31, 2012 and 2011, amounted to $5,000 and $-0-, respectively.

10. INVENTORY

Inventory was comprised of the following:

	March 31, 2012	December 31, 2011
Raw materials	$ 447,000	$ 473,000
Work-in-process	48,000	65,000
Finished goods	-	-
Reserve for obsolescence	(151,000)	(151,000)
Total	$ 344,000	$ 387,000

11. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment were comprised of the following:

	March 31, 2012	December 31, 2011
Land	$ 1,235,000	$ 1,235,000
Building	964,000	964,000
Building improvements	83,000	83,000
Machinery and equipment	658,000	658,000
Furniture and fixtures	39,000	39,000
	2,979,000	2,979,000
Less: Accumulated depreciation	(690,000)	(676,000)
Total	$ 2,289,000	$ 2,303,000

12. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities at March 31, are as follows:

	2012	2011
Legal and professional fees	$ 1,145,000	$ 1,004,000
Accrued compensation and benefits	148,000	156,000
General and administrative expenses	83,000	111,000
Accrued interest expense	69,000	88,000
Total	$ 1,445,000	$ 1,359,000

13. MORTGAGE LOAN PAYABLE

The Company has a mortgage loan on the land and building that serves as its headquarters and research and development facility which bears interest at the rate of 7.5% per annum and which matures in July 2012. Interest expense for the three months ended March 31, 2012 and 2011 on this mortgage amounted to $31,000 and $32,000, respectively. The loan requires monthly payments of interest, plus $5,000 which is being applied to the principal balance. The remaining principal balance at March 31, 2012, was $1,620,000. The Company will be required to renegotiate the terms of a further extension of the mortgage loan or successfully refinance the property with another mortgage lender, if possible. Failure to do so would have an adverse affect the Company's financial position and results of operations.

The Company incurred $17,000 of expenses in connection with extending this mortgage loan in 2011, which is being amortized to interest expense over the one year term. The loan is collateralized by a security interest in all of the Company's assets, the pledge of five million shares of common stock of the Company owned by George J. Coates, which were deposited into escrow for the benefit of the lender and the personal guarantee of George J. Coates. The Company is not permitted to create or permit any secondary mortgage or similar liens on the property or improvements thereon without prior consent of the lender. Up to $500,000 of the principal balance of the mortgage loan may be prepaid each year without penalty. A prepayment penalty of 2% of the outstanding loan amount would be imposed if the loan is repaid in full at or before maturity unless such prepayment funds are obtained from a permanent mortgage loan with the lender.

14. PROMISSORY NOTES TO RELATED PARTIES

The Company has received proceeds from promissory notes issued from time to time to George J. Coates and has also made partial repayments of these promissory notes. At March 31, 2012, the outstanding balance of these notes amounted to $295,000. These notes are due on demand and bear interest at the rate of 17% per annum, compounded monthly. During the three months ended March 31, 2012 and 2011, $42,000 and $37,000, respectively of promissory notes were issued and $25,000 and $22,000, respectively, of these promissory notes was repaid.

The Company has also issued promissory notes to two of its directors with an aggregate principal balance of $170,000. These notes are due on demand and bear interest at the rate of 17% per annum, compounded monthly.

For the three months ended March 31, 2012 and 2011, interest expense on all of these promissory notes amounted to $21,000 and $22,000, respectively. At March 31, 2012, unpaid accrued interest on these promissory notes amounting to $50,000 is included in accounts payable and accrued liabilities in the accompanying consolidated balance sheet.

15. CONVERTIBLE PROMISSORY NOTES AND EMBEDDED DERIVATIVE LIABILITIES

The Company entered into a series of securities purchase agreements (the "Purchase Agreements") in 2011 and 2012 with an investor and issued convertible promissory notes, as follows:

Issued	Principal Amount	Nominal Interest Rate	Maturity	Balance, March 31, 2012
February 2011	$ 33,000	8.00%	November 2011	$ -
May 2011	100,000	8.00%	February 2012	-
July 2011	78,000	8.00%	April 2012	-
September 2011	52,000	8.00%	June 2012	-
October 2011	52,000	8.00%	July 2012	52,000
November 2011	52,000	8.00%	August 2012	52,000
January 2012	52,000	8.00%	October 2012	52,000
	$ 419,000			$ 156,000

The Notes may be converted into unregistered shares of the Company's common stock, par value $0.0001 per share (the "Common Stock"), at the Conversion Price, as defined below, in whole, or in part, at any time beginning 180 days after the date of issuance of the Notes, at the option of the holder. The Conversion Price shall be equal to 61% multiplied by the Variable Conversion Rate which is equal to the average of the three (3) lowest closing bid prices of the Common Stock during the ten (10) trading day period prior to the date of conversion. The Notes also contain a prepayment option whereby the Company may make a payment to the holder equal to between 130% and 150% of the then outstanding unpaid principal, interest and any other amounts that might be due for penalties or any event of a default under the Notes during the 179-day period following the date of issuance of the Notes, upon three (3) trading days' prior written notice to the holder.

The 61% discounted Conversion Price establishes a beneficial conversion feature ("BCF") which is required to be valued and accreted to interest expense over the six month minimum conversion period of the Convertible Notes. The Company is also required to record additional unamortized discount to recognize the estimated value of the derivative liabilities arising from the convertible promissory notes. Accordingly, the Company recorded a total initial amount of unamortized discount on the Convertible Notes outstanding at March 31, 2012, of $125,000. For the three months ended March 31, 2012 and 2011, the amount of interest expense resulting from accretion of the unamortized discount on the convertible promissory notes amounted to $117,000 and $82,000, respectively.

The total unamortized discount represented by the value of the BCF is being accreted over the six month period until the conversion of the convertible promissory notes into common stock is permitted. This resulted in an overall effective interest rate of 147%, 147%, 147%, 123%, 147%, 92% and 130% on the $33,000, $100,000, $78,000 and $52,000, $52,000, $52,000 and $52,000 convertible notes, respectively. The remaining unamortized balance of this discount, which amounted to $50,000 at March 31, 2012, has been netted against the face amount of the convertible promissory notes resulting in a net carrying amount of $106,000. This net amount is presented in the accompanying consolidated balance sheet at March 31, 2012.

In accordance with GAAP, the conversion features associated with the convertible promissory notes represent derivatives. The Company initially recorded the estimated value of the embedded derivative liabilities related to the convertible promissory notes outstanding at March 31, 2012 of $83,000. The estimated fair value of the embedded derivative liability is required to be remeasured at each balance sheet date. The estimated fair value of the embedded derivative liabilities, which were measured at their aggregate estimated fair value, based on Level 2 inputs, amounted to $214,000, at March 31, 2012. The (decrease) increase in the estimated fair value of the embedded derivative liabilities amounted to ($29,000) and $17,000 for the three months ended March 31, 2012 and 2011, respectively. This amount is included in the accompanying consolidated statements of operations as increase in estimated fair value of embedded derivative liabilities.

The embedded derivative liabilities arise because, based on historical trading patterns of the Company's stock, the formula for determining the Conversion Rate is expected to result in a lower Conversion Rate than the closing price of the stock on the actual date of conversion (hereinafter referred to as the "Variable Conversion Rate Differential". The estimated fair value of the derivative liabilities have been calculated based on a Black-Scholes option pricing model.

The Company made the private placement of these securities in reliance upon Section 4(2) of the Securities Act of 1933, as amended (the "Act"), Rule 506 of Regulation D, and the rules and regulations promulgated thereunder, and/or upon any other exemption from the registration requirements of the Act, as applicable.

16. 10% CONVERTIBLE NOTE TO RELATED PARTY

The 10% Convertible Note, which is held by one of the Company's directors, is convertible at the option of the holder, into shares of the Company's common stock at an initial conversion rate that is determined by dividing the principal amount of the note being converted by $0.45. This convertible note is payable on demand. Interest shall accrue at the rate of 10% per annum and shall be payable at the time of repayment of principal. All interest shall be forfeited upon conversion, in which case the holder would be entitled to dividends declared, if any, on the Company's common stock during the time the convertible note was outstanding. The Company has reserved 22,222 shares of its common stock for conversion of the remaining $10,000 balance of this note.

17. CONTRACTUAL OBLIGATIONS

The following table summarizes the Company's contractual obligations at March 31, 2012 (rounded to thousands of dollars):

	Total	2012
Mortgage loan payable	$ 1,620,000	$ 1,620,000
Promissory notes to related parties	465,000	465,000
Deferred compensation	452,000	452,000
Convertible promissory notes	156,000	156,000
10% promissory note	10,000	10,000
Total	$ 2,703,000	$ 2,703,000

18. CAPITAL STOCK

Common Stock and Anti-dilution Rights

The Company's common stock is traded on the Over the Counter Bulletin Board ("OTCBB") market system and Pink Sheets under the ticker symbol COTE. The Company is authorized to issue up to 1,000,000,000 shares of common stock, par value, $0.0001 per share (the "Common Stock").

During the three months ended March 31, 2012 and 2011, the Company sold 1,726,677 and -0- registered shares of its common stock, respectively, under an equity line of credit with Dutchess Opportunity Fund II, LP and received proceeds of $225,000 and $-0-, respectively. There were no offering costs related to the sale of these shares.

During the three months ended March 31, 2012, the Company sold 190,185 restricted shares of its common stock in consideration for 185,185 tradable shares of its common stock received from the son of a director, which were used to pay for contractual services in lieu of a cash payment. During the three months ended March 31, 2011, the Company sold 600,000 shares of its common stock and 600,000 warrants to purchase one share of its common stock at an exercise price of $0.25 per share in consideration for $150,000 received from the son of a director. These transactions were private sales of unregistered, restricted securities pursuant to a stock purchase agreement.

During the three months ended March 31, 2011, the Company sold 200,000 shares of its common stock in consideration for $50,000 to one of its directors. This transaction was a private sale of unregistered, restricted securities pursuant to a stock purchase agreement.

During the three months ended March 31, 2012, convertible promissory notes with a total principal amount of $131,000, plus accrued interest thereon totaling $5,000 were converted by the holder into 1,726,704 unregistered shares of the Company's common stock. During the three months ended March 31, 2011, convertible promissory notes with a total principal amount of $94,000, plus accrued interest thereon totaling $3,000 were converted by the holder into 883,434 unregistered shares of the Company's common stock.

A new anti-dilution program became effective as of January 1, 2012, pursuant to which George J. Coates, majority shareholder, is to be issued one share of common stock of the Company for each new share issued to any person or entity that is not a member of the Coates family. For the three months ended March 31, 2012, pursuant to this anti-dilution arrangement, the Company issued 3,638,566 unregistered, restricted shares of its common stock to George J. Coates and recorded stock-based compensation expense aggregating $502,000.

There were no other sales of, or conversions into, common stock during the three months ended March 31, 2012.

At March 31, 2012, Company had reserved 19,152,519 shares of its common stock to cover the potential conversion of convertible securities and exercise of stock options and warrants.

Preferred Stock and anti-dilution rights

The Company is authorized to issue 100,000,000 new shares of preferred stock, par value, $0.001 per share (the "Preferred Stock"). The Company may issue any class of the Preferred Stock in any series. The Board shall have authority to establish and designate series, and to fix the number of shares included in each such series and the relative rights, preferences and limitations as between series, provided that, if the stated dividends and amounts payable on liquidation are not paid in full, the shares of all series of the same class shall share ratably in the payment of dividends including accumulations, if any, in accordance with the sums which would be payable on such shares if all dividends were declared and paid in full, and in any distribution of assets other than by way of dividends in accordance with the sums which would be payable on such distribution if all sums payable were discharged in full. Shares of each such series when issued shall be designated to distinguish the shares of each series from shares of all other series.

The Board has designated 100,000 shares of Preferred Stock as Series A Preferred Stock, $0.001 par value per share. Each share of Series A Preferred Stock entitles the holder of record to the right to vote 10,000 shares of common stock with respect to all matters that are submitted to a vote of shareholders. The Series A Preferred Stock does not provide the holder any rights to share in dividends or any distribution of assets to any other shareholders of any other class of the Company's securities in a liquidation or for any other purpose. No new shares of Series A Preferred Stock were issued during the three months ended March 31, 2012 and 2011.

Each issuance of shares of Series A Preferred Stock to George J. Coates does not have any effect on the share of dividends or liquidation value of the holders of the Company's common stock. However, the voting rights of the holders of the Company's common stock are diluted with each issuance. This anti-dilution arrangement was terminated as of December 31, 2011.

19. INVESTMENT AGREEMENTS WITH DUTCHESS OPPORTUNITY FUND II, LP

In June 2011, the Company entered into an investment agreement (the "Investment Agreement") with Dutchess Opportunity Fund II, LP, a Delaware limited partnership ("Dutchess"). Pursuant to the terms of the Investment Agreement, Dutchess committed to purchase, in a series of purchase transactions ("Puts") up to Twenty Million ($20,000,000) Dollars of the Company's common stock over a period of up to thirty-six (36) months.

The amount that the Company is entitled to request with each Put delivered to Dutchess is equal to, at its option, either (i) two hundred percent (200%) of the average daily volume (U.S. market only) of its common stock for the three (3) Trading Days prior to the applicable Put Notice Date, multiplied by the average of the three (3) daily closing prices immediately preceding the Put Date or (ii) five hundred thousand dollars ($500,000). The purchase price to be paid by Dutchess for the shares of common stock covered by each Put will be equal to ninety-four percent (94%) of the lowest daily volume weighted average prices of the common stock during the period beginning on the Put Notice Date and ending on and including the date that is five (5) trading days after such Put Notice Date (the "Pricing Period"). "Put Notice Date" is the trading day immediately following the day on which Dutchess receives a Put Notice from the Company.

In connection with the Investment Agreement, the Company also entered into a registration rights agreement (the "Registration Rights Agreement") with Dutchess. Pursuant to the Registration Rights Agreement, the Company filed a registration statement with the Securities and Exchange Commission ("SEC") covering 17,500,000 shares of the common stock underlying the Investment Agreement which became effective in August 2011. In addition, during the term of the Registration Rights Agreement, the Company is obligated to maintain the effectiveness of such registration statement.

During the three months ended March 31, 2012 and 2011, the Company sold 1,726,677 and -0- registered shares of its common stock, respectively, under this equity line of credit with Dutchess and received proceeds of $225,000 and $-0-, respectively. There were no offering costs related to the sale of these shares.

20. UNEARNED REVENUE

The Company has remaining non-refundable deposits amounting to $19,000 from Almont in connection with the future shipment of natural gas fueled electric power CSRV engine generators and a $10,000 refundable deposit related to the future potential issuance of a license for the CSRV technology. This amount is included in unearned revenue in the accompanying consolidated balance sheets at March 31, 2012 and 2011.

21. LOSS PER SHARE

At March 31, 2012, the Company had 11,911,107 shares of common stock potentially issuable upon assumed conversion of:

Description	Number of Underlying Shares of Common Stock	Exercise Price	Number Vested	Number Non-Vested
Common stock options	1,800,000	$ 0.250	200,000	1,600,000
Common stock options	2,800,000	0.240	-	2,000,000
Common stock options	50,000	0.390	50,000	-
Common stock options	360,000	0.400	-	360,000
Common stock options	100,000	0.430	100,000	-
Common stock options	1,750,000	0.440	1,750,000	-
Common stock options	30,000	1.000	30,000	-
Common stock warrants	1,200,000	0.250	N/A	N/A
Common stock warrants	833,333	0.270	N/A	N/A
Common stock warrants	333,333	0.300	N/A	N/A
Common stock warrants	153,846	0.325	N/A	N/A
Common stock warrants	1,028,570	0.350	N/A	N/A
Common stock warrants	210,000	1.100	N/A	N/A
$10,000, 10% Convertible promissory note	22,222	0.450	N/A	N/A
8% Convertible promissory notes	2,039,803	(1)	N/A	N/A
Total	11,911,107			

(1) The principal amount of convertible promissory notes outstanding, none of which were eligible for conversion at March 31, 2012, was $156,000. The conversion rate is variable as it is equal to the average of the three lowest closing bid prices during the ten trading days prior to the date of conversion. The actual number of shares underlying these convertible instruments will likely vary from the number assumed above. The number of shares underlying these convertible notes was determined based on the three lowest closing bid prices during the ten trading days prior to March 31, 2012.

At March 31, 2011, the Company had 10,292,606 shares of common stock potentially issuable upon assumed conversion.

For the three months ended March 31, 2012 and 2011, none of the potentially issuable shares of common stock were assumed to be converted because the Company incurred a net loss in those periods and the effect of including them in the calculation would have been anti-dilutive.

22. STOCK OPTIONS

The Company's 2006 Stock Option and Incentive Plan (the "Stock Plan") was adopted by the Board in October 2006. In September 2007, the Stock Plan, by consent of George J. Coates, majority shareholder, was adopted by the Company's shareholders. The Stock Plan provides for the grant of stock-based awards to employees, officers and directors of, and consultants or advisors to, the Company and its subsidiaries, if any. Under the Stock Plan, the Company may grant options that are intended to qualify as incentive stock options ("incentive stock options") within the meaning of Section 422 of the Internal Revenue Code of 1986, as amended (the "Code"), options not intended to qualify as incentive stock options ("non-statutory options"), restricted stock and other stock-based awards. Incentive stock options may be granted only to employees of the Company. A total of 12,500,000 shares of common stock may be issued upon the exercise of options or other awards granted under the Stock Plan. The maximum number of shares with respect to which awards may be granted to any employee under the Stock Plan shall not exceed 25% of the 12,500,000 total number of shares of common stock permitted to be granted under the Stock Plan.

The Stock Plan is administered by the Board and the Compensation Committee. Subject to the provisions of the Stock Plan, the Board and the Compensation Committee each has the authority to select the persons to whom awards are granted and determine the terms of each award, including the number of shares of common stock subject to the award. Payment of the exercise price of an award may be made in cash, in a "cashless exercise" through a broker, or if the applicable stock option agreement permits, shares of common stock or by any other method approved by the Board or Compensation Committee. Unless otherwise permitted by the Company, awards are not assignable or transferable except by will or the laws of descent and distribution.

Upon the consummation of an acquisition of the business of the Company, by merger or otherwise, the Board shall, as to outstanding awards (on the same basis or on different bases as the Board shall specify), make appropriate provision for the continuation of such awards by the Company or the assumption of such awards by the surviving or acquiring entity and by substituting on an equitable basis for the shares then subject to such awards either (a) the consideration payable with respect to the outstanding shares of common stock in connection with the acquisition, (b) shares of stock of the surviving or acquiring corporation or (c) such other securities or other consideration as the Board deems appropriate, the fair market value of which (as determined by the Board in its sole discretion) shall not materially differ from the fair market value of the shares of common stock subject to such awards immediately preceding the acquisition. In addition to or in lieu of the foregoing, with respect to outstanding stock options, the Board may, on the same basis or on different bases as the Board shall specify, upon written notice to the affected optionees, provide that one or more options then outstanding must be exercised, in whole or in part, within a specified number of days of the date of such notice, at the end of which period such options shall terminate, or provide that one or more options then outstanding, in whole or in part, shall be terminated in exchange for a cash payment equal to the excess of the fair market value (as determined by the Board in its sole discretion) for the shares subject to such stock options over the exercise price thereof. Unless otherwise determined by the Board (on the same basis or on different bases as the Board shall specify), any repurchase rights or other rights of the Company that relate to a stock option or other award shall continue to apply to consideration, including cash, that has been substituted, assumed or amended for a stock option or other award pursuant to these provisions. The Company may hold in escrow all or any portion of any such consideration in order to effectuate any continuing restrictions.

The Board may at any time provide that any stock options shall become immediately exercisable in full or in part, that any restricted stock awards shall be free of some or all restrictions, or that any other stock-based awards may become exercisable in full or in part or free of some or all restrictions or conditions, or otherwise realizable in full or in part, as the case may be.

The Board or Compensation Committee may, in its sole discretion, amend, modify or terminate any award granted or made under the Stock Plan, so long as such amendment, modification or termination would not materially and adversely affect the participant.

During the three months ended March 31, 2012 no stock options were issued. During the three months ended March 31, 2011, stock options to purchase 200,000 shares of the Company's common stock at an exercise price of $0.25 per share were granted to one of the Company's directors. These stock options vested in February 2012 and expire in 2026.

During the three months ended March 31, 2012, 200,000 stock options with an exercise price of $0.25 per share became vested. During the three months ended March 31, 2011, no stock options became vested. The weighted-average fair value of 3,600,000 nonvested stock options at March 31, 2012 was $882,000. Total compensation cost related to nonvested stock options at March 31, 2012 that had not been recognized was $294,000. This non-cash compensation expense will be recognized in the future over a remaining weighted average period of approximately four months.

For the three months ended March 31, 2012 and 2011, the Company recorded non-cash stock-based compensation expense related to employee stock options amounting to $241,000 and $38,000, respectively. For the three months ended March 31, 2012 and 2011, $88,000 and $3,000, respectively, of this amount is included in research and development expenses, $-0- and $2,000, respectively, of this amount was allocated to work in process inventory and $153,000 and $33,000, respectively, of this amount is included in general and administrative expenses in the accompanying consolidated statements of operations.

A summary of the activity in the Company's Stock Option Plan is as follows:

	Exercise Price Per Share	Number Outstanding	Weighted Average Remaining Contractual Life	Number Exercisable	Weighted Average Exercise Price	Weighted Average Fair Value Per Stock Option at Date of Grant
Balance, 1/1/12	$ 0.25 -1.00	6,090,000	12	2,290,000	$ 0.32	$ 0.28
Vested	$ 0.25		11	200,000	0.25	$ 0.17
Balance, 3/31/12	$ 0.25 -1.00	6,090,000	12	2,490,000	$ 0.32	$ 0.28

No stock options were exercised, forfeited or expired during the three months ended March 31, 2012.

The weighted average fair value of the Company's stock options was estimated using the Black-Scholes option pricing model which requires highly subjective assumptions including the expected stock price volatility. These assumptions were as follows:

● Historical stock price volatility	139-180%
● Risk-free interest rate	0.62%-4.64%
● Expected life (in years)	4
● Dividend yield	0.00%

The valuation assumptions were determined as follows:

- Historical stock price volatility: The Company initially obtained the volatility factor of other publicly traded engine manufacturers that were also in the research and development stage. Subsequently, once sufficient trading history became available, the volatility factor was calculated based on the historical daily closing prices of the Company's common stock on the OTCBB.

- Risk-free interest rate: The Company bases the risk-free interest rate on the interest rate payable on U.S. Treasury securities in effect at the time of the grant for a period that is commensurate with the assumed expected option life.

- Expected life: The expected life of the options represents the period of time options are expected to be outstanding. The Company very limited historical data on which to base this estimate. Accordingly, the Company estimated the expected life based on its assumption that the executives will be subject to frequent black out periods during the time that the stock options will be exercisable and based on the Company's expectation that it will complete its research and development phase and commence its initial production phase. The vesting period of these options was also considered in the determination of the expected life of each stock option grant.

- No expected dividends.

The same methodology and assumptions were utilized in estimating the fair value of non-employee stock options granted to the Company's general corporate counsel, as discussed above.

23. INCOME TAXES

Deferred income taxes are determined using the liability method for the temporary differences between the financial reporting basis and income tax basis of the Company's assets and liabilities. Deferred income taxes are measured based on the tax rates expected to be in effect when the temporary differences are included in the Company's tax return. Deferred tax assets and liabilities are recognized based on anticipated future tax consequences attributable to differences between financial statement carrying amounts of assets and liabilities and their respective tax bases.

Deferred tax assets increased by $617,000 and decreased by $442,000 for the three months ended March 31, 2012 and 2011, respectively. These amounts were fully offset by a corresponding decrease in the tax valuation allowance resulting in no net change in deferred tax assets, respectively during these periods.

No liability for unrecognized tax benefits was required to be reported at March 31, 2012 and 2011. Based on the Company's evaluation, it has concluded that there are no significant uncertain tax positions requiring recognition in the Company's financial statements. The Company's evaluation was performed for tax years ended 2006 through 2011, the only periods subject to examination. The Company believes that its income tax positions and deductions will be sustained on audit and does not anticipate that adjustments, if any, will result in a material change to its financial position. For the three months ended March 31, 2012 and 2011, there were no penalties or interest related to the Company's income tax returns.

24. RELATED PARTY TRANSACTIONS

Compensation and Benefits Paid

The approximate amount of compensation and benefits paid to George J. Coates, Gregory Coates and Bernadette Coates is summarized as follows:

	For the Three Months Ended March 31,	
	2012	2011
George J. Coates	$ 689,000	$ 89,000
Gregory Coates	153,000	42,000
Bernadette Coates	21,000	20,000

Included in compensation paid to George J. Coates during the three months ended March 31, 2012 is $502,000 of stock-based compensation expense representing the estimated fair value of 3,638,566 shares of common stock issued to George J. Coates pursuant to an anti-dilution agreement in effect and $113,000 representing stock-based compensation expense for stock options. Included in compensation paid to George J. Coates during the three months ended March 31, 2011 is $10,000 representing the estimated fair value of 4,001 shares of Series A Preferred Stock awarded pursuant to an anti-dilution agreement in effect and $14,000 representing stock-based compensation expense for stock options.

Included in compensation paid to Gregory Coates for the three months ended March 31, 2012, is $108,000 representing stock-based compensation expense for stock options. There was no stock-based compensation expense for Gregory Coates during the three months ended March 31, 2011.

Promissory Notes to Related Parties

During the three months ended March 31, 2012 and 2011, $42,000 and $37,000, respectively of promissory notes due to George J. Coates were issued and $25,000 and $22,000, respectively, of promissory notes due to George J. Coates were repaid.

For the three months ended March 31, 2012 and 2011, interest expense on promissory notes due to George J. Coates and two of the Company's directors aggregated $21,000 and $22,000, respectively.

Other

During the three months ended March 31, 2012 and 2011, Barry C. Kaye, Treasurer and Chief Financial Officer was paid compensation of $24,000 and $17,000, respectively.

As discussed in Note 18, during the three months ended March 31, 2012, the Company sold 190,185 restricted shares of its common stock in consideration for 185,185 tradable shares of its common stock received from the son of a director. During the three months ended March 31, 2011, the Company sold 600,000 shares of its common stock and 600,000 warrants to purchase one share of its common stock at an exercise price of $0.25 per share in consideration for $150,000 received from the son of a director. These transactions were private sales of unregistered, restricted securities pursuant to a stock purchase agreement.

During the three months ended March 31, 2011, the Company sold 200,000 shares of its common stock in consideration for $50,000 to one of its directors. This transaction was a private sale of unregistered, restricted securities pursuant to a stock purchase agreement.

25. LITIGATION AND CONTINGENCIES

Mark D. Goldsmith, a former executive of the Company, filed a lawsuit in January 2008 in which he asserts that the Company is liable to him for breach of an employment contract that never became effective. In the opinion of management, Mr. Goldsmith's performance was unsatisfactory and, accordingly, he was offered the opportunity to resign. Further, management is of the opinion that the claim of Mr. Goldsmith is baseless because the Company had cause to terminate its relationship with Mr. Goldsmith. The Company intends to vigorously defend this lawsuit and has instituted a counterclaim against Mr. Goldsmith. The Company believes that Mr. Goldsmith misrepresented his background and capabilities in order to induce it and/or Coates Motorcycle Company, Ltd. ("CMC") to hire him. The Company is also contending that certain of Mr. Goldsmith's business decisions were made to further his self interest rather than the interests of the Company. The Company believes that Mr. Goldsmith's claims have no basis in fact and, accordingly, that the outcome of this legal action will not be material to its financial condition or results of operations. Efforts by the court to settle this matter have been unsuccessful. The Company filed a new motion for summary judgment contending that based on its corporate by-laws, Mr. Goldsmith's employment contract required approval by the board of directors which was never given. Goldsmith filed a cross-motion for summary judgment. Both of these motions were denied by the court in December 2011. Unless postponed again, the start of the trial is anticipated imminently. The Company intends to vigorously defend against Mr. Goldsmith's claims and pursue its counterclaims.

The Company has, in prior years, without prejudice to its position, accrued compensation under his employment agreement for accounting purposes only, of $96,000 of his salary. Although the Company does not intend to make any payments to Mr. Goldsmith in connection with this employment agreement, this amount is included in accounts payable and accrued liabilities in the accompanying consolidated balance sheets.

In March 2010, one of the Company's vendors notified the Company of its contention that it is owed $160,000, plus accrued interest, for services rendered in 2007. The vendor acknowledged that it does not have documentation to support its claim. The Company believes there is no basis in fact to support the vendor's contention and it is not likely that the vendor can prevail with its position. Accordingly, no amount has been recorded for this unasserted claim.

The Company is not a party to any other litigation that is material to its business.

26. RECENTLY ISSUED ACCOUNTING STANDARD

In December 2011, the Financial Accounting Standards Board issued Accounting Standards Update No. 2011-11, "Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities". This update requires an entity to disclose information about offsetting and related arrangements to enable users of its financial statements to understand the effect of those arrangements on its financial position. Such disclosures are required for:

- Recognized financial instruments and derivative instruments that are offset in accordance with either Section 210-20-45 or Section 815-10-45
- Recognized financial instruments and derivative instruments that are subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset in accordance with either Section 210-20-45 or Section 815-10-45.

This standard is effective for interim periods and fiscal years beginning on or after January 1, 2013. The Company does not believe that adoption of this standard will have a material effect on its consolidated financial statements.

27. SUBSEQUENT EVENTS

Convertible Promissory Note

In April 2012, the Company entered into a securities purchase agreement with an investor and issued an 8% convertible promissory note which matures in January 2013 and received cash proceeds of $41,000, net of financing costs of $2,000. This note contains the same terms and conditions as the previous convertible promissory notes more fully discussed in Note 15.

Conversion of Convertible Promissory Note

In May 2012, a $32,000 principal amount of convertible promissory notes was converted by the holder into 516,658 unregistered shares of the Company's common stock.

Promissory Notes to Related Parties

Subsequent to March 31, 2012, the Company issued additional 17% promissory notes to George J. Coates and Bernadette Coates and received proceeds therefrom of $18,000 and $18,00, respectively. Mr. and Mrs. Coates have made loans to the Company from time to time for working capital purposes but they are not obligated to continue to do so in the future.

Sale of Common Stock and Warrants

Subsequent to March 31, 2012, the Company sold, in two transactions, 750,000 shares of its common stock, 416,667 warrants to purchase one share of its common stock at an exercise price of $0.12 per share and 666,666 warrants to purchase one share of its common stock at an exercise price of $0.09 per share in consideration for $80,000 received from the son of a director. These transactions were private sales of unregistered, restricted securities pursuant to a stock purchase agreement.

Issuance of Common Stock for Anti-dilution

Subsequent to March 31, 2012, the Company issued 2,636,658 shares of its common stock to George J. Coates pursuant to an anti-dilution agreement in effect and recorded related stock-based compensation expense of $306,000.

Compensatory Awards of Common Stock

Subsequent to March 31, 2012, the Company issued 620,000 restricted shares of common stock to George J. Coates and 1,340,000 restricted shares of common stock to two of its directors, which were originally awarded in 2011. The compensation expense of $452,000 related to these compensatory awards was recorded during the year ended December 31, 2011.

Shares of Common Stock Sold to Dutchess Opportunity Fund II, LP

Subsequent to March 31, 2012, the Company sold 30,000 registered shares of its common stock to Dutchess and received cash proceeds of $4,000.

Issuance of Shares of Common Stock to Dutchess

In connection with the equity line of credit with Dutchess, the Company issued 500,000 shares of its common stock to Dutchess which may only be used to fulfill the execution of future Puts issued to Dutchess by the Company. The Company has the right, at any time, to request that Dutchess promptly return any shares not sold pursuant to a Put, for cancelation and retirement.

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

Forward-Looking Statements

This quarterly report on Form 10-Q contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 and Federal securities laws, and is subject to the safe-harbor created by such Act and laws. Forward-looking statements may include our statements regarding our goals, beliefs, strategies, objectives and plans, including product and service developments, current dependence on our agreements with Almont Energy, Inc., future financial conditions, results or projections or current expectations. In some cases, you can identify forward-looking statements by terminology such as "may," "will," "should," "expect," "plan," "anticipate," "believe," "estimate," "predict," "potential" or "continue," the negative of such terms, or other comparable terminology. These statements are subject to known and unknown risks, uncertainties, assumptions and other factors that may cause actual results to be materially different from those contemplated by the forward-looking statements. The business and operations of the Company are subject to substantial risks, which increase the uncertainty inherent in the forward-looking statements contained in this report. Except as required by law, we undertake no obligation to release publicly the result of any revision to these forward-looking statements that may be made to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events. Further information on potential factors that could affect our business is described in our various periodic reports filed with the SEC. Readers are also urged to carefully review and consider the various disclosures we have made in this and such previously filed reports.

Background

Coates International, Ltd. ("we", "CIL" or the "Company") has been developing over a period of more than 15 years a patented Coates spherical rotary valve ("CSRV") system technology which is adaptable for use in piston-driven internal combustion engines of many types. Independent testing of various engines in which we incorporated our CSRV system technology ("CSRV Engines") confirmed meaningful fuel savings when compared with internal combustion engines based on the conventional "poppet valve" assembly prevalent in most internal combustion engines throughout the world. In addition, our CSRV Engines produced only ultra low levels of harmful emissions while in operation. Engines operating on the CSRV system technology can be powered by a wide selection of fuels. We believe that these three major advantages of the CSRV system technology constitute the first revolutionary technological advancement of the internal combustion engine suitable for large scale production since its introduction more than one hundred years ago.

We have completed development of the Coates spherical rotary valve engine technology. This technology has been successfully applied to natural gas fueled industrial electric power generator engines, automobile engines, residential generators and high performance racing car engines. We have also designed and retrofitted the CSRV system technology into a diesel engine which is suitable for and can be applied to heavy trucks. We have been primarily investing our management time and resources in securing new working capital and developing plans for transitioning to large scale production in order to be properly positioned to take advantage of this technology as it achieves acceptance in the marketplace. This includes consideration of an optimal location, shipping logistics, manufacturing capacity and quality of the labor pool for such large scale manufacturing. In the fourth quarter of 2011, we identified cracks on the lower engine heads that resulted from a defect in the manufacturing by one of our suppliers. Based on our testing of the Gen Set to confirm our resolution of this problem, we believe we have determined the cause of this cracked head condition. As soon as we raise sufficient working capital in excess of our fixed expenses and current obligations, we will procure new cast-steel head castings and will begin larger scale production, after which, we intend to undertake field testing of the generators. We continue to be engaged in new research and development activities in connection with applying this technology to other commercially feasible internal combustion engine applications and intend to manufacture engines and/or license the CSRV system technology to third party Original Equipment Manufacturers ("OEM's") for multiple other applications and uses.

We believe that the CSRV system technology delivers significant competitive advantages over technology currently applied in conventional internal combustion engines, including substantial improvement in fuel efficiency, a substantial reduction in harmful emissions, adaptability to almost any type of engine fuel and longer intervals between scheduled engine maintenance. This technology has been successfully applied to CSRV Gen Sets, automobile engines, a 35-KW synchronous residential generator and a high performance racing car engine.

We may also conduct new research and development activities in connection with applying this technology to other commercially feasible internal combustion engine applications and it is our plan to manufacture engines and/or license the technology to third party Original Equipment Manufacturers ("OEMs") for multiple other applications and uses. We believe the CSRV system technology has wide applicability to products of all types powered by internal combustion engines.

Initially, we intend to sell the CSRV Gen Sets to Almont, the successor in interest to Well to Wire Energy, Inc. ("WWE") with respect to (i) a sublicense agreement covering the territory of Canada; and, (ii) certain rights to a sublicense covering the territory of the United States. Almont is a privately held, independent third party entity based in Alberta, Canada. The business plan of Almont assumes the purchase of a substantial number of CSRV Gen Sets over a 5-year period commencing upon our ramp up of production to fulfill their orders. Almont's purchase of CSRV Gen Sets from us will be made by way of standard purchase orders, issued based on market and customer demand. Over the 5-year period, Almont anticipates that the volume of total purchases from us will be similar to, or potentially exceed the 7,400 CSRV Gen Sets contemplated in our previous arrangement with WWE. Almont plans to finance its purchases from cash flow and by way of project and/or equipment financing, proceeds from issuance of equity or corporate debt instruments and conventional bank financing.

Our ability to establish large scale manufacturing operations, recruit plant workers, finance initial manufacturing inventories and fund capital expenditures is highly dependent on our ability to successfully raise substantial new working capital in an amount and at a pace which matches our business plans.

Potential sources of such new working capital include sales of our common stock to Dutchess Opportunity Fund II, LP under the equity line of credit, sales of our equity and/or debt securities through private placement offerings, issuances of promissory notes to related parties, issuances of convertible promissory notes, pursuing and entering into additional sublicensing agreements with OEM's and/or distributors, additional payments from Almont towards the escrow agreement Release Payment, US Licensing fees and positive working capital generated from sales of our CSRV products to Almont and others. There can be no assurance that we will be successful in raising adequate new working capital or even any new working capital to carry out our business plans. The current economic environment, which is characterized by tight credit markets, investor uncertainty about how to safely invest funds and low investor confidence, has introduced additional risk and difficulty to our challenge to secure such additional working capital.

We are actively engaged in efforts to raise working capital to fund our ongoing operations and the ramp up of production of our products incorporating the CSRV system technology.

Non-binding Preliminary Letter of Intent to Merge with S.W.T. in China

In May 2011, we entered into a non-binding letter of intent with S.W.T., an established heavy equipment manufacturer in China and The Coates Trust. The letter expressed the mutual intent of the parties to exchange shares of common stock between us and S.W.T., a cash payment to the shareholders of S.W.T. and the issuance of shares of our common stock to The Coates Trust in consideration of a CSRV technology license for China. The transaction would be subject to required governmental approvals and a number of other prerequisite conditions. In September 2011, we determined that the risk of proceeding with this merger transaction as contemplated at that time, was greater than anticipated. Accordingly, we will either continue to explore the possibility of restructuring the merger transaction or taking a simpler approach that would enable us to have access to the manufacturing capabilities of S.W.T., while affording both companies the opportunity to benefit from CSRV system technology related manufacturing activities. At this time, further discussions with S.W.T. are on hold for at least the next 90 days, while we focus on raising working capital and starting production.

Coates Oklahoma Engine Manufacturing, Ltd.

In August 2011, we formed a new wholly-owned subsidiary, Coates Oklahoma Engine Manufacturing, Ltd., a Delaware corporation for the purpose of raising working capital and establishing manufacturing operations in the state of Oklahoma. At this time, it has not commenced operations and has only incurred minimal start up expenses. It is working on opportunities to raise working capital, continuing to negotiate for a package of business and tax incentives with the State of Oklahoma and is searching for a suitable manufacturing facility within the State.

Sublicense Agreements Almont Energy, Inc.

In January 2010, we consented to the assignment of our sublicensing agreement with WWE to Almont. This sublicense agreement exclusively licenses within Canada the use of the CSRV system technology for industrial engines to be fueled by natural gas to generate electrical power for the oil and gas industry (the "Canadian License"). The Canadian Sublicense provided for a license fee of $5,000,000, of which a deposit payment in the amount of $300,000 was made upon execution. A separate research and development agreement provided a $5,000,000 fee payable to us in consideration for the development and delivery of certain prototype engines. We completed development of the prototypes in accordance with this agreement at the end of 2007. The research and development agreement has not been reduced to the form of a signed, written agreement. To date, we have been paid a total of approximately $5,153,000 by WWE and Almont under these agreements. Additional provisions of the Canadian License agreement are as follows:

- Sublicensee shall have the exclusive right to use, lease and sell electric power generators designed with the CSRV system technology within Canada.
- Sublicensee will have a specified right of first refusal to market the electric power generators worldwide.
- Upon commencement of the production and distribution of the electric power generators, the minimum annual number of generators to be purchased by Sublicensee in order to maintain exclusivity is 120. Until otherwise agreed between the parties, the price per generator shall be $159,000. We have agreed to pass along to Almont savings, if any, realized from economies of scale inherent in high volume production of the CSRV units. In the event Sublicensee fails to purchase the minimum 120 Coates generator engines during any year, Sublicensee will automatically lose its exclusivity. We have temporarily waived this provision due to the delay in delivery of Gen Sets. In such a case, Licensee would retain non-exclusive rights to continue to use and sell the CSRV generator engine in the territory of Canada.
- Sublicensee is required to pay a royalty to us equal to 5% of its annual modified gross profit (which has been defined as sales, less cost of sales, plus $400,000).
- All licensed rights under this sublicense agreement related to the CSRV system technology will remain with the Company.

In January 2010, we also consented to the assignment of the rights to a conditional sublicensing agreement with WWE covering the territory of the United States of America (the "US License") to Almont. The US License, which has been placed in escrow and has not yet been granted or become effective, provides for a license fee of $50 million and annual minimum purchases of CSRV Units as a condition of exclusivity. The US license has been deposited into an escrow account and the grant of the license is not effective until the conditions for release from escrow are satisfied.

The escrow agreement was established to provide a more secure mechanism for us to collect payments due under both the prior Canadian sublicensing and research and development agreements and the new $50 million US License (the "Escrow Agreement"). The Escrow Agreement provides that the US License shall be held until we receive a release payment (the "Release Payment"). The Release Payment consists of (i) an initial down payment required under the US License of $1 million and (ii) an $8.5 million payment of the balance of the monies due to us at the date of the Escrow Agreement, in connection with the sublicense for the territory of Canada, including the Canadian License Agreement and the research and development agreement (the "Canadian Agreements"). While the US License is held in escrow, there shall not be any grant of license. As successor to WWE, Almont is expected to continue to make non-refundable periodic payments to us in unspecified amounts as partial payments of the Release Payment until the Release Payment has been paid in full. The first $3.8 million of the Release Payment, which has been designated as payment of the fees due under the research and development agreement, is being recognized as revenue at the time the cash payments are received. We have received approximately $3,653,000 million of the Release Payment to date. In addition, WWE had made nonrefundable payments to us totaling $1.5 million prior to establishment of the Escrow Agreement. Upon full satisfaction of the Release Payment, Almont would be granted a sublicense for the territory of the United States under the US License agreement.

The remaining balance of the Release Payment is currently $5,847,000. To the extent that Almont is not successful or experiences delays in remitting the balance of the Release Payment, the Company's cash flow, results of operations and financial condition could be adversely affected.

In connection with the assignment of the Canadian and US License from WWE to Almont, we waived all events of default by WWE under the Escrow Agreement in existence and extended the date by which the entire Release Payment must be paid (the "Release Payment Due Date"), which lapsed in March 2012. We have verbally agreed to extend the Release Payment Date under the Escrow Agreement to compensate for the delay caused by the late delivery of Gen Sets. Almont is required to remit to us 60% of any and all proceeds from funds raised from any equity, debt or lending transactions, exclusive of equipment financing transactions, until the Release Payment is paid in full. Payment of the Release Payment is dependent on us starting up production to fulfill Almont's orders.

The US License would, if Almont is able to satisfy the Escrow Agreement release provisions, grant to Almont the right to use, sell and lease Licensed Products manufactured by us as the power source for the generation of electrical energy for the oil and gas industry and landfills. Licensed Products consist of CSRV Valve Systems, CSRV Valve Seals, CSRV Rotary Valve Spheres, CSRV Valve Components and CSRV Engines for the oil and gas industry and landfills. Almont is also obligated to pay a royalty to us equal to 2.5% of its annual modified gross profit (which has been defined as sales, less cost of sales, plus $400,000).

The manufacture of our licensed products by Almont is prohibited. Almont is required to procure all internal combustion engines incorporating the CSRV system technology from us or our designee. The license granted to Almont is exclusive within the Territory, provided that Almont satisfies the minimum annual purchase commitment of 120 internal combustion engines incorporating the CSRV system technology, the Coates Engines and all component parts. The agreement also grants Almont a right of first refusal in the event that we negotiate an offer with another third party for a worldwide license to use the licensed product in the oil and gas industry and landfill operations.

The remaining balance of the US License fee of $49 million is payable in quarterly installments in an amount equal to 5% of Almont's prior quarter net profits. In any event, the entire balance of the licensing fee must be paid in full on or before February 19, 2015. We have also verbally agreed to extend this date to compensate for the delay caused by the late delivery of Gen Sets.

Acceleration of the balance of the licensing fee payments shall be required in the event that Almont completes a stock offering or private placement offering. The entire unpaid balance of the licensing fee shall become due and payable if Almont raises $100 million or more from such offerings.

Significant Estimates

The preparation of our financial statements in conformity with United States generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. These significant estimates include determining the fair value of convertible promissory notes containing embedded derivatives as a result of variable conversion rate provisions, determining a value for Series A Preferred Stock issued and certain limited anti-dilution rights granted to George J. Coates, assigning useful lives to the Company's property, plant and equipment, determining an appropriate amount to reserve for obsolete and slow moving inventory, providing a valuation allowance for deferred tax assets, assigning expected lives to and estimating the rate of forfeitures of stock options granted and selecting a volatility factor for the Company's stock options in order to estimate the fair value of the Company's stock options on the date of grant. Actual results could differ from those estimates.

Results of Operations – Three Months Ended March 31, 2012 Compared to the Three Months Ended March 31, 2011 (All amounts rounded to thousands of dollars)

There were no sales and no revenues from research and development for the three months ended March 31, 2012 and 2011.

Sublicensing fee revenue for the three months ended March 31, 2012 amounted to $5,000. There was no sublicensing fee revenue for the three months ended March 31, 2011. The Company is recognizing the license deposit of $300,000 on the Canadian License as revenue over the approximately 16-year remaining life of the last CSRV technology patent in force at that date.

Research and development expenses were $186,000 and $21,000 for the three months ended March 31, 2012 and 2011, respectively. Included in research and development expenses for the three months ended March 31, 2012 and 2011 were $54,000 and $18,000, respectively, of allocated compensation and benefits and $88,000 and $3,000, respectively, of allocated stock-based compensation expense. Also, included in research and development expenses were $44,000 and $-0-, respectively, of parts and materials.

General and administrative expenses increased to $1,066,000 for the three months ended March 31, 2012 from $349,000 in the corresponding period in 2011. This net increase of $706,000 primarily resulted from the following: An increase in non-cash stock-based compensation expense of $623,000 which resulted from the charge to expense for employee stock options issued in the third quarter of 2011 and the issuance of restricted shares of common stock pursuant to an anti-dilution agreement, an increase in investor relations expense of $45,000, an increase in legal and professional fees of $40,000, an increase in insurance expense of $8,000, an increase in miscellaneous taxes of $4,000, an increase in tools of $3,000 and a net increase in other general and administrative expenses of $10,000, offset by a decrease in financing costs of ($12,000), a decrease in marketing costs of ($6,000), a decrease in compensation and benefits of ($5,000) and a decrease in patent maintenance costs of ($4,000).

Depreciation and amortization decreased by $2,000 to $15,000 for the three months ended March 31, 2012 from $17,000 for the three months ended March 31, 2011.

Other operating income (expense) for the three months ended March 31, 2012, consisted of a decrease in the fair value of embedded derivative liabilities amounting to $29,000, compared to an increase in the fair value of embedded derivative liabilities amounting to $17,000 for the three months ended March 31, 2011, in connection with convertible promissory notes outstanding. In accordance with GAAP, the fair value of these embedded liabilities is required to be remeasured at each balance sheet reporting date.

Interest expense, net, amounted to $177,000 for the three months ended March 31, 2012, an increase of $37,000 from interest expense, net of $140,000 incurred in the comparable 2011 period.

The change in deferred tax assets for the three months ended March 31, 2012 and 2011 was fully offset by a valuation allowance, resulting in a $-0- net income tax provision.

We incurred net losses of ($1,399,000) and ($543,000) for the three months ended March 31, 2012 and 2011, respectively. This included non-cash expenses of $918,000 and $179,000 for the three months ended March 31, 2012 and 2011, respectively.

Liquidity and Capital Resources (All amounts rounded to thousands of dollars)

Our cash position at March 31, 2012 was $1,000, a decrease of $52,000 from the cash position of $53,000 at December 31, 2011. We had negative working capital of ($3,968,000) at March 31, 2012 which represents a ($215,000) decline from the ($3,753,000) of negative working capital at December 31, 2011. Current liabilities of $4,341,000 at March 31, 2012, increased by $113,000 from the $4,228,000 balance at December 31, 2011. Current liabilities are primarily comprised of a mortgage loan in the amount of $1,620,000, accounts payable and accrued liabilities of $1,445,000, promissory notes to related parties totaling $475,000, deferred compensation payable of $452,000, embedded derivative liabilities related to convertible promissory notes of $214,000, the net carrying value of convertible promissory notes of $106,000 and unearned revenue of $29,000.

Operating activities utilized cash of ($362,000) during the three months ended March 31, 2012, which primarily consisted of a net loss for the period of ($1,399,000), decreased by non-cash stock-based compensation expense of $744,000, non-cash interest expense of $156,000, depreciation and amortization of $15,000 and non-cash financing costs of $3,000 and increased by a non-cash decrease of ($29,000) in the fair value of the embedded liabilities related to convertible promissory notes and non-cash licensing revenues of sublicensing revenues of ($5,000). In addition, we realized additional operating cash from a net reduction in inventory of $43,000, a reduction in deferred offering costs and other assets of $7,000 and a net increase in accounts payable and accrued liabilities of $104,000.

There were no investing activities for the three months ended March 31, 2012.

Financing activities generated net cash of $310,000 for the three months ended March 31, 2012, consisting of proceeds from issuance of common stock of $250,000, issuance of convertible notes amounting to $52,000 and issuance of promissory notes to related parties, net of repayment amounting to $18,000, offset by a $10,000 partial repayment of the principal amount of a mortgage loan.

Subsequent to March 31, 2012, we raised additional working capital aggregating $163,000, consisting of proceeds from the sale of common stock and warrants to the son of a director amounting to $80,000, proceeds of $43,000 from the issuance of a convertible promissory note, $36,000 from the issuance of promissory notes to George J. Coates and Bernadette Coates and proceeds from the sale of common stock to Dutchess of $4,000 under our equity line of credits.

In the opinion of management, we will be required to continue to raise additional working capital to fully achieve our objectives as we are entering the production phase of our operations and continue research and development activities in connection with developing other commercially viable applications of our CSRV system technology to internal combustion engines. Various potential sources of such additional working capital is anticipated to come from one or more of the following: sales of shares of common stock to Dutchess Opportunity Fund II, LP under the equity line of credit, sales and shipments of natural gas-fueled industrial electric power CSRV Gen Sets to Almont, cash flows from payments by Almont under the escrow agreement, additional issuances of convertible promissory notes and private sales of common stock and common stock warrants. The current economic environment, which is characterized by tight credit markets, investor uncertainty about how to safely invest funds and low investor confidence, has introduced additional risk and difficulty in our challenge to secure needed additional working capital. There can be no assurance that we will be able to obtain the necessary working capital for our production phase on a time frame that will enable us to carry out our current business plans.

Contractual Obligations and Commitments

The following table summarizes our contractual obligations at March 31, 2012 (rounded to thousands of dollars):

	Total	Amount Due Within 2012
Mortgage loan payable	$ 1,620,000	$ 1,620,000
Promissory notes to related parties	465,000	465,000
Deferred compensation payable	452,000	452,000
Convertible promissory notes	156,000	156,000
10% promissory note	10,000	10,000
Total	$ 2,703,000	$ 2,703,000

Total non-cash compensation cost related to nonvested stock options at March 31, 2012 that has not been recognized was approximately $294,000. This non-cash stock-based compensation expense will be recognized in the future over a remaining weighted average period of approximately four months.

Plan of Operation

We have completed development of the CSRV system technology-based generator engine and are prepared to commence the production phase of our operations. Initially, we intend to sell the engine generators to Almont Energy, Inc., ("Almont") the successor in interest to Well to Wire Energy, Inc. ("WWE") for (i) a license agreement covering the territory of Canada; and, (ii) certain rights to a license covering the territory of the United States. Almont is a privately held, independent third party entity based in Alberta, Canada. We shipped the first CSRV system technology-based generator to Almont in the fourth quarter of 2010 and another such generator was shipped in 2011. In the fourth quarter of 2011, we identified cracks on the lower engine heads that resulted from a defect in the manufacturing by one of our suppliers. Based on our testing of the Gen Set to confirm our resolution of this problem, we believe we have determined the cause of this cracked head condition.

As soon as we raise sufficient working capital in excess of our fixed expenses and current obligations, we will procure new cast-steel head castings and will begin larger scale production, after which, we intend to undertake field testing of the generators. The business plan of Almont assumes the purchase of a substantial number of CSRV Units over the next 5 years. Almont's purchase of CSRV Units from us will be made by way of standard purchase orders, issued based on market and customer demand. Over the 5-year period, Almont anticipates that the volume of total purchases from us will be similar to, or potentially exceed the 7,400 CSRV Unit quantity contemplated in our previous arrangement with WWE. We are unable to confirm these orders until we have sufficient working capital in place to manufacture generators on a larger scale. Almont plans to finance its purchases from cash flow and by way of project and/or equipment financing, proceeds from issuance of equity or corporate debt instruments and conventional bank financing.

We intend to take advantage of the fact that essentially all the components of the CSRV generator engine may be readily sourced and acquired from subcontractors, and, accordingly, expect to manufacture the engine generator in the two following ways:

- Assembly – to develop assembly lines within owned manufacturing facilities. We intend to initially commence production of CSRV Units on a small scale. This will enable us to prove our concept for the CSRV system technology and we expect this will lead to substantial demand in the marketplace. We plan to address this demand by establishing large scale manufacturing operations in the United States. We have already taken steps to identify a suitable size and appropriate location for a high capacity manufacturing plant. Transitioning to large scale manufacturing is expected to require a substantial increase in our work force and substantial capital expenditures.

- Licensing the CSRV system technology to Original Equipment Manufacturers ("OEM's") – to take advantage of third party manufacturers' production capacity and resources by signing OEM agreements.

Our ability to establish such manufacturing operations, recruit plant workers, finance initial manufacturing inventories and fund capital expenditures is highly dependent on our ability to successfully raise substantial new working capital in an amount and at a pace which matches our business plans.

Going Concern (All amounts rounded to thousands of dollars)

As shown in the accompanying consolidated financial statements, we incurred a net loss for the three months ended March 31, 2012 of ($1,399,000), and have incurred substantial net losses since inception while engaging primarily in research and development. As of March 31, 2012, we had accumulated losses of ($28,096,000) and had negative working capital of ($3,968,000). In addition, we must either obtain an extension or refinance our mortgage loan which matures on July 1, 2012. The current economic environment, which is characterized by tight credit markets, investor uncertainty about how to safely invest funds and low investor confidence, has introduced additional risk and difficulty in our challenge to secure needed additional working capital. These factors raise substantial doubt about our ability to continue as a going concern. Our Independent Registered Public Accounting Firm has stated in its independent auditors' report on our financial statements as of December 31, 2011 and for the year then ended that these factors raise substantial doubt about our ability to continue as a going concern.

The doubt about our ability to continue to operate as a going concern has existed for a number of years. We have been successful in raising sufficient new working capital throughout that time to enable us to continue as a going concern and, although we can not provide assurances that we can be successful, we believe that we can continue to do so in the future. Management is continuing to carefully monitor its costs and is restricting variable costs to only those expenses that are necessary to carry out our business plans. We continue to actively seek out new sources of working capital; however, there can be no assurance that we will be successful in these efforts.

Potential sources of such new working capital include sales of our equity and/or debt securities through private placement and/or secondary public offerings, pursuing and entering into additional sublicensing agreements with OEM's and/or distributors, additional payments from Almont towards the Escrow Agreement Release Payment and US Licensing fees, positive working capital generated from sales of our CSRV products to Almont and others. Although we have been successful in raising sufficient working capital to continue our ongoing operations, we have encountered very challenging credit and equity investment markets, and have not been able to raise sufficient new working capital to enable us to commence production of our CSRV products. There can be no assurance that we will be successful in raising adequate new working capital or even any new working capital to carry out our business plans.

The accompanying consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not applicable.

ITEM 4. CONTROLS AND PROCEDURES

a) Evaluation of Disclosure Controls. Pursuant to Rule 13a-15(b) under the Securities Exchange Act of 1934 (the "Exchange Act"), we carried out an evaluation, with the participation of our management, including our Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO") (our principal financial and accounting officer), of the effectiveness of our disclosure controls and procedures (as defined under Rule 13a-15(e) under the Exchange Act) as of the end of the period covered by this report. Based upon that evaluation, our CEO and CFO concluded that our disclosure controls and procedures are effective to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our CEO and CFO, as appropriate, to allow timely decisions regarding required disclosure.

(b) Changes in internal control over financial reporting. There have been no changes in our internal control over financial reporting that occurred during the last fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Not applicable.

ITEM 1A. RISK FACTORS

Not required.

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

In January 2012, we issued a $52,000 principal amount, 8% convertible promissory note and received net proceeds of $50,000, net of financing costs of $2,000. The note is convertible into unregistered shares of our common stock at any time beginning six months after issuance. The conversion rate is equal to 61% of the average of the three lowest closing bid prices of the stock during the ten trading days prior to the date of conversion.

In January 2012, an aggregate of $78,500 principal amount of a convertible promissory note, plus interest thereon amounting $3,640, was converted by the holder into 1,079,322 unregistered shares of our common stock.

In March 2012, an aggregate of $52,000 principal amount of a convertible promissory note, plus interest thereon amounting $2,080, was converted by the holder into 647,382 unregistered shares of our common stock.

In March 2012, 190,185 unregistered shares of our common stock were sold to the son of a director in consideration of 185,185 tradable shares of common stock which were used to make a non-cash payment for services rendered to us.

During the three months ended March 31, 2012, we issued 3,638,566 unregistered shares of common stock to George J. Coates pursuant to an anti-dilution agreement.

All of the above shares were issued pursuant to an exemption from registration contained in Section 4(2) of the Securities Act of 1933.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS.

Exhibit Number	Description
31.1 *	Section 302 Certification of Chief Executive Officer pursuant to Rule 13a-14(a)/15d-14(a) under the Securities Exchange Act of 1934 as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2 *	Section 302 Certification of Principal Financial Officer pursuant to Rule 13a-14(a)/15d-14(a) under the Securities Exchange Act of 1934 as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1 **	Certification of Chief Executive Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2 **	Certification of Principal Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS +	XBRL Instance Document
101.SCH +	XBRL Taxonomy Schema
101.CAL +	XBRL Taxonomy Calculation Linkbase
101.DEF +	XBRL Taxonomy Definition Linkbase
101.LAB +	XBRL Taxonomy Label Linkbase
101.PRE +	XBRL Taxonomy Presentation Linkbase
101.DEF+	XBRL Taxonomy Extension Definition Linkbase Document

* Filed herewith.

**Furnished herewith.

+ XBRL (eXtensible Business Reporting Language) information is furnished and not filed or a part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, is deemed not filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and otherwise is not subject to liability under these sections.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

COATES INTERNATIONAL, LTD.

Date: May 14, 2012

By: /s/ George J. Coates
George J. Coates
President, Chief Executive Officer
and Principal Executive Officer

Date: May 14, 2012

By: /s/ Barry C. Kaye
Barry C. Kaye
Treasurer, Chief Financial Officer
and Principal Financial Officer

EXHIBIT 31.1

CERTIFICATION PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, George J. Coates, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Coates International, Ltd. (the "Company");

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the Company as of, and for the periods presented in this quarterly report;

4. I am responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the Company and I have:

(a) designed such disclosure controls and procedures to ensure that material information relating to the Company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

(b) evaluated the effectiveness of the Company's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

(c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. I have disclosed, based on our most recent evaluation, to the Company's auditors and to the audit committee of the Company's board of directors:

(a) all significant deficiencies in the design or operation of internal controls which could adversely affect the Company's ability to record, process, summarize and report financial data and have identified for the Company's auditors any material weaknesses in internal controls; and

(b) any fraud, whether or not material, that involves management or other employees who have a significant role in the Company's internal controls; and

6. I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Dated: May 14, 2012

By: /s/ George J. Coates

George J. Coates
President, Chief Executive Officer
and Principal Executive Officer

EXHIBIT 31.2

CERTIFICATION PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Barry C. Kaye, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Coates International, Ltd. (the "Company");

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the Company as of, and for the periods presented in this quarterly report;

4. I am responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the Company and I have:

(a) designed such disclosure controls and procedures to ensure that material information relating to the Company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

(b) evaluated the effectiveness of the Company's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

(c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. I have disclosed, based on our most recent evaluation, to the Company's auditors and to the audit committee of the Company's board of directors:

(a) all significant deficiencies in the design or operation of internal controls which could adversely affect the Company's ability to record, process, summarize and report financial data and have identified for the Company's auditors any material weaknesses in internal controls; and

(b) any fraud, whether or not material, that involves management or other employees who have a significant role in the Company's internal controls; and

6. I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Dated: May 14, 2012

By: /s/ Barry C. Kaye

Barry C. Kaye
Treasurer, Chief Financial Officer
and Principal Financial Officer

EXHIBIT 32.1

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the quarterly report of Coates International, Ltd. (the "Company") on Form 10-Q for the quarter ended March 31, 2012 (the "Form 10-Q"), I, George J. Coates, President, Chief Executive Officer and Principal Executive Officer of the Company, certify, as of the date hereof, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to the best of my knowledge, the Company's Form 10-Q fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that the information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: May 14, 2012

By: /s/ George J. Coates
George J. Coates
President, Chief Executive Officer
and Principal Executive Officer

EXHIBIT 32.2

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the quarterly report of Coates International, Ltd. (the "Company") on Form 10-Q for the quarter ended March 31, 2012 (the "Form 10-Q"), I, Barry C. Kaye, Treasurer, Chief Financial Officer and Principal Financial Officer of the Company, certify, as of the date hereof, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to the best of my knowledge, the Company's Form 10-Q fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that the information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: May 14, 2012

By: /s/ Barry C. Kaye

Barry C. Kaye
Treasurer, Chief Financial Officer
and Principal Financial Officer