FUELCELL ENERGY INC
Form 10-Q
September 09, 2015

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

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

For the quarterly period ended July 31, 2015

OR

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

For the transition period from to

Commission file number: 1-14204

FUELCELL ENERGY, INC.
(Exact name of registrant as specified in its charter)

Delaware	06-0853042
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
3 Great Pasture Road Danbury, Connecticut	06810
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (203) 825-6000

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 ý 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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý 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	ý
Non-accelerated filer	¨ (Do not check if a smaller reporting company)	Smaller reporting company	¨

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

Number of shares of common stock, par value $.0001 per share, outstanding as of September 4, 2015: 305,078,416

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FUELCELL ENERGY, INC.
Consolidated Balance Sheets
(Unaudited)
(Amounts in thousands, except share and per share amounts)

	July 31, 2015	October 31, 2014
ASSETS		
Current assets:		
Cash and cash equivalents, unrestricted	$65,520	$83,710
Restricted cash and cash equivalents - short-term	6,968	5,523
Accounts receivable, net	55,315	64,375
Inventories	75,571	55,895
Project assets	11,639	784
Other current assets	10,133	7,528
Total current assets	225,146	217,815
Restricted cash and cash equivalents - long-term	20,600	19,600
Property, plant and equipment, net	27,015	25,825
Goodwill	4,075	4,075
Intangible assets	9,592	9,592
Other assets, net	3,457	3,729
Total assets	$289,885	$280,636
LIABILITIES AND EQUITY		
Current liabilities:		
Current portion of long-term debt	$6,908	$1,439
Accounts payable	19,207	22,969
Accrued liabilities	17,278	12,066
Deferred revenue	39,462	37,626
Preferred stock obligation of subsidiary	828	961
Total current liabilities	83,683	75,061
Long-term deferred revenue	23,160	20,705
Long-term preferred stock obligation of subsidiary	11,958	13,197
Long-term debt and other liabilities	13,150	13,367
Total liabilities	131,951	122,330
Redeemable preferred stock (liquidation preference of $64,020 as of July 31, 2015 and October 31, 2014)	59,857	59,857
Total equity:		
Shareholders' equity:		
Common stock ($.0001 par value); 475,000,000 and 400,000,000 shares authorized as of July 31, 2015 and October 31, 2014, respectively; 305,057,318 and 287,160,003 shares issued and outstanding as of July 31, 2015 and October 31, 2014, respectively.	30	29
Additional paid-in capital	928,933	909,431
Accumulated deficit	(829,813)	(809,314)
Accumulated other comprehensive loss	(563)	(159)
Treasury stock, Common, at cost (41,357 and 45,550 shares as of July 31, 2015 and October 31, 2014, respectively)	(56)	(95)
Deferred compensation	56	95
Total shareholders' equity	98,587	99,987

Noncontrolling interest in subsidiaries	(510)	(1,538)
Total equity	98,077	98,449
Total liabilities and equity	$289,885	$280,636

See accompanying notes to consolidated financial statements.

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FUELCELL ENERGY, INC.
Consolidated Statements of Operations and Comprehensive Loss
(Unaudited)
(Amounts in thousands, except share, per share and related party revenue amounts)

	Three Months Ended July 31,	
	2015	2014
Revenues:		
Product sales (including $27.8 million and $18.6 million of related party revenues)	$31,130	$32,315
Service agreements and license revenues (including $3.2 million and $3.9 million of related party revenues)	7,017	7,078
Advanced technologies contract revenues (including $0.001 million and $0.2 million of related party revenues)	3,209	3,783
Total revenues	41,356	43,176
Costs of revenues:		
Cost of product sales	28,849	29,308
Cost of service agreements and license revenues	5,719	6,629
Cost of advanced technologies contract revenues	3,193	3,278
Total costs of revenues	37,761	39,215
Gross profit	3,595	3,961
Operating expenses:		
Administrative and selling expenses	6,101	5,569
Research and development expenses	4,597	4,392
Total costs and expenses	10,698	9,961
Loss from operations	(7,103)	(6,000)
Interest expense	(905)	(649)
Other income (expense), net	1,464	(399)
Loss before provision for income taxes	(6,544)	(7,048)
Provision for income taxes	(84)	(91)
Net loss	(6,628)	(7,139)
Net loss attributable to noncontrolling interest	89	161
Net loss attributable to FuelCell Energy, Inc.	(6,539)	(6,978)
Preferred stock dividends	(800)	(800)
Net loss attributable to common shareholders	$(7,339)	$(7,778)
Loss per share basic and diluted:		
Net loss per share attributable to common shareholders	$(0.02)	$(0.03)
Basic and diluted weighted average shares outstanding	298,609,231	258,178,826

	Three Months Ended July 31,	
	2015	2014
Net loss	$(6,628)	$(7,139)
Other comprehensive loss:		
Foreign currency translation adjustments	(64)	(43)
Comprehensive loss	$(6,692)	$(7,182)

See accompanying notes to consolidated financial statements.

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FUELCELL ENERGY, INC.
Consolidated Statements of Operations and Comprehensive Loss
(Unaudited)
(Amounts in thousands, except share, per share and related party revenue amounts)

	Nine Months Ended July 31, 2015	2014
Revenues:		
Product sales (including $66.1 million and $75.3 million of related party revenues)	$84,769	$94,482
Service agreements and license revenues (including $8.1 million and $9.4 million of related party revenues)	15,506	19,215
Advanced technologies contract revenues (including $0.6 million and $0.3 million of related party revenues)	11,351	12,187
Total revenues	111,626	125,884
Costs of revenues:		
Cost of product sales	77,308	88,944
Cost of service agreements and license revenues	13,720	17,546
Cost of advanced technologies contract revenues	10,966	11,623
Total costs of revenues	101,994	118,113
Gross profit	9,632	7,771
Operating expenses:		
Administrative and selling expenses	18,002	16,169
Research and development expenses	12,656	13,945
Total costs and expenses	30,658	30,114
Loss from operations	(21,026)	(22,343)
Interest expense	(2,195)	(2,901)
Other income (expense), net	2,621	(8,480)
Loss before provision for income taxes	(20,600)	(33,724)
Provision for income taxes	(179)	(269)
Net loss	(20,779)	(33,993)
Net loss attributable to noncontrolling interest	280	568
Net loss attributable to FuelCell Energy, Inc.	(20,499)	(33,425)
Preferred stock dividends	(2,400)	(2,400)
Net loss to common shareholders	$(22,899)	$(35,825)
Loss per share basic and diluted:		
Net loss per share to common shareholders	$(0.08)	$(0.15)
Basic and diluted weighted average shares outstanding	291,747,961	233,933,636

	Nine Months Ended July 31, 2015	2014
Net loss	$(20,779)	$(33,993)
Other comprehensive (loss) income:		
Foreign currency translation adjustments	(404)	67
Comprehensive loss	$(21,183)	$(33,926)

See accompanying notes to consolidated financial statements.

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FUELCELL ENERGY, INC.
Consolidated Statements of Cash Flows
(Unaudited)
(Amounts in thousands)

	Nine Months Ended July 31, 2015	2014
Cash flows from operating activities:		
Net loss	$(20,779)	$(33,993)
Adjustments to reconcile net loss to net cash used in operating activities:		
Share-based compensation	2,317	2,182
Gain from change in fair value of embedded derivatives	(36)	(116)
Make whole derivative expense	—	8,347
Depreciation	2,998	3,297
Interest expense on preferred stock obligation	1,392	1,466
Unrealized foreign exchange gains	(1,807)	(199)
Other non-cash transactions, net	(182)	270
Decrease (increase) in operating assets:		
Accounts receivable	9,039	9,517
Inventories	(19,676)	424
Project assets	(10,855)	—
Other assets	(2,966)	1,599
Increase (decrease) in operating liabilities:		
Accounts payable	(3,762)	(8,618)
Accrued liabilities	4,545	(11,485)
Deferred revenue	4,291	(4,293)
Net cash used in operating activities	(35,481)	(31,602)
Cash flows from investing activities:		
Capital expenditures	(3,840)	(4,120)
Net cash used in investing activities	(3,840)	(4,120)
Cash flows from financing activities:		
Repayment of debt	(1,386)	(5,858)
Proceeds from debt	6,326	250
Increase in restricted cash and cash equivalents	(2,445)	(15,120)
Payment of preferred dividends and return of capital	(3,154)	(3,264)
Cash received for common stock issued for stock plans	133	161
Proceeds from sale of common stock, net of registration fees	22,061	99,728
Net cash provided by financing activities	21,535	75,897
Effects on cash from changes in foreign currency rates	(404)	67
Net (decrease) increase in cash and cash equivalents	(18,190)	40,242
Cash and cash equivalents-beginning of period	83,710	67,696
Cash and cash equivalents-end of period	$65,520	$107,938
Supplemental cash flow disclosures:		
Cash interest paid	$480	$1,728
Noncash financing and investing activity:		
Common stock issued for Employee Stock Purchase Plan in settlement of prior year accrued employee contributions	$168	$106
Common stock issued for convertible note conversions and make-whole settlements	$—	$46,186

See accompanying notes to consolidated financial statements.

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FUELCELL ENERGY, INC.
Notes to Consolidated Financial Statements
(Unaudited)
(Tabular amounts in thousands, except share and per share amounts)

Note 1. Nature of Business and Basis of Presentation

FuelCell Energy, Inc. and subsidiaries (the “Company”, “FuelCell Energy”, “we”, “us”, or “our”) is a leading integrated fuel ce company with a growing global presence. We design, manufacture, install, operate and service ultra-clean, efficient and reliable stationary fuel cell power plants. Our Direct FuelCell power plants produce reliable 24/7 base load electricity and usable high quality heat for commercial, industrial, government and utility customers. We have commercialized our stationary carbonate fuel cells and are also pursuing the complementary development of planar solid oxide fuel cells and other fuel cell technologies. We continue to invest in new product and market development and we are not currently generating net income from our operations. Our operations are funded primarily through cash generated from product sales, service and advanced technologies contracts, license fee and royalty income and sales of equity and debt securities. In order to continually produce positive cash flow from operations, we need to be successful at increasing annual order volume, production and cost reduction efforts.

Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission (“SEC”) regarding interim financial information. Accordingly, they do not contain all of the information and footnotes required by accounting principles generally accepted in the United States of America (“GAAP”) for complete financial statements. In the opinion of management, all normal and recurring adjustments necessary to fairly present our financial position and results of operation as of and for the three and nine months ended July 31, 2015 have been included. All intercompany accounts and transactions have been eliminated.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted. The balance sheet as of October 31, 2014 has been derived from the audited financial statements at that date, but it does not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. These financial statements should be read in conjunction with our financial statements and notes thereto for the year ended October 31, 2014, which are contained in our Annual Report on Form 10-K previously filed with the Securities and Exchange Commission. The results of operations for the interim periods presented are not necessarily indicative of results that may be expected for any other interim period or for the full fiscal year.

Certain reclassifications have been made to the prior year amounts to conform to the current year presentation.

Use of Estimates

The preparation of financial statements and related disclosures in conformity with accounting principles generally accepted in the U.S. requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and the disclosure of contingent assets and liabilities. Estimates are used in accounting for, among other things, revenue recognition, excess, slow-moving and obsolete inventories, product warranty costs, accruals for service agreements, allowance for uncollectible receivables, depreciation and amortization, impairment of goodwill, indefinite-lived intangible assets and long-lived assets, income taxes, and contingencies. Estimates and assumptions are reviewed periodically, and the effects of revisions are reflected in the consolidated financial statements in the period they are determined to be necessary. Due to the inherent uncertainty involved in making estimates, actual results in future periods may differ from those estimates.

Related Parties

POSCO Energy (“POSCO”), which is a related party, owned approximately 10.0 percent of the outstanding common shares of the Company as of July 31, 2015. Revenues from POSCO Energy for the three months ended July 31, 2015 and 2014 represent 75% and 53%, respectively, of consolidated revenues and revenues from POSCO Energy for the nine months ended July 31, 2015 and 2014 represent 65% and 68%, respectively, of consolidated revenues.
NRG Energy, Inc. ("NRG") is a related party and owned approximately 6.0 percent of the outstanding common shares of the Company as of July 31, 2015. NRG Yield is a dividend growth-oriented company formed by NRG Energy, Inc. that owns, operates and acquires a diversified portfolio of contracted renewable and conventional generation and thermal infrastructure assets in the United States. Revenues from NRG and NRG Yield for the three and nine months ended July 31, 2015 represents 0.0 percent and 2.0 percent, respectively, of consolidated revenues. There were no sales to NRG for the three and nine months ended July 31, 2014.

FUELCELL ENERGY, INC.
Notes to Consolidated Financial Statements
(Unaudited)
(Tabular amounts in thousands, except share and per share amounts)

Note 2. Recent Accounting Pronouncements

In April 2015, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2015-03, Interest – Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs. This ASU simplifies the presentation of debt issuance costs by requiring that such costs be presented in the balance sheet as a direct deduction from the carrying value of the associated debt instrument, consistent with debt discounts. The amendments in this ASU are effective for fiscal years beginning after December 15, 2015 and for interim periods therein. Adoption of this ASU is not expected to have a material impact on the Company's consolidated financial position.

In May 2014, the FASB issued ASU No. 2014-09, “Revenue from Contracts with Customers (Topic 606).” This topic provides for five principles which should be followed to determine the appropriate amount and timing of revenue recognition for the transfer of goods and services to customers. The principles in this ASU should be applied to all contracts with customers regardless of industry. The amendments in this ASU are effective for fiscal years, and interim periods within those years, beginning after December 15, 2016, with two transition methods of adoption allowed. Early adoption for reporting periods prior to December 15, 2016 is not permitted. In March 2015, the FASB voted to defer the effective date by one year, but allow early adoption as of the original adoption date. We are evaluating the financial statement impacts of the guidance in this ASU and determining which transition method we will utilize.

Note 3. Accounts Receivable

Accounts receivable as of July 31, 2015 and October 31, 2014 consisted of the following:

	July 31, 2015	October 31, 2014
Commercial Customers:		
Amount billed	$16,629	$8,871
Unbilled recoverable costs	32,541	50,101
	49,170	58,972
Advanced Technology (including U.S. Government[(1)]):		
Amount billed	2,500	2,517
Unbilled recoverable costs	3,645	2,886
	6,145	5,403
Accounts receivable, net	$55,315	$64,375

(1) Total U.S. Government accounts receivable outstanding as of July 31, 2015 and October 31, 2014 was $3.6 million and $1.7 million, respectively.

Accounts receivable from Commercial Customers includes billings for Product sales and Service and license agreements. Product sales include power plant, module, module kit sales, construction services and component part sales. Construction services includes engineering, procurement and construction (EPC) services of an overall fuel cell project. We bill customers for power plant and module kit sales based on certain contractual milestones being reached. We bill service agreements based on the contract price and billing terms of the contracts. Unbilled recoverable costs relate to revenue recognized on customer contracts that have not been billed. Commercial Customers accounts receivable (including Unbilled recoverable costs) included amounts due from POSCO Energy of $26.1 million and $29.9 million as of July 31, 2015 and October 31, 2014, respectively and amounts due from NRG and NRG Yield of $0.1 million as of July 31, 2015. There were no amounts outstanding from NRG and NRG Yield as of October 31, 2014.

Accounts receivable from Advance Technology contracts relate to research and development contracts with the U.S. government and certain third parties. Generally, our advanced technology contracts are billed based on actual recoverable costs incurred, typically in the month subsequent to incurring costs. Some advanced technology contracts are billed based on contractual milestones or costs incurred.

Accounts receivable are presented net of an allowance for doubtful accounts of $0.2 million and $0.1 million as of July 31, 2015 and October 31, 2014, respectively.

FUELCELL ENERGY, INC.
Notes to Consolidated Financial Statements
(Unaudited)
(Tabular amounts in thousands, except share and per share amounts)

Note 4. Inventories
The components of inventory as of July 31, 2015 and October 31, 2014 consisted of the following:

	July 31, 2015	October 31, 2014
Raw materials	$34,853	$25,460
Work-in-process [1]	40,718	30,435
Inventories	$75,571	$55,895

(1) Work-in-process includes the standard components of inventory used to build the typical modules or module components that are intended to be used in future power plant orders or to service our service agreements. Included in work-in-process as of July 31, 2015 and October 31, 2014 was $28.8 million and $19.2 million, respectively, of completed standard components.

Raw materials consist mainly of various nickel powders and steels, various other components used in producing cell stacks and purchased components for balance of plant. Work-in-process inventory is comprised of material, labor, and overhead costs incurred to build balance of plant components, fuel cell stacks and modules, which are subcomponents of a power plant.

Note 5. Project Assets

Project assets as of July 31, 2015 and October 31, 2014 were $11.6 million and $0.8 million, respectively. Project assets consist primarily of costs relating to our fuel cell projects in various stages of development that we capitalize prior to entering into a definitive sales or long-term financing agreement for the project. These projects are actively being marketed and intended to be sold, although we may choose to retain ownership of one or more of these projects after they become operational if we determine it would be of economic and strategic benefit. Project asset costs include costs for developing and constructing a complete turn-key fuel cell project. Development costs can include legal, consulting, permitting, interconnect, and other similar costs. Once we enter into a definitive sales agreement we expense project assets to cost of sales after the respective project asset is sold to a customer and all revenue recognition criteria have been met. We classify project assets as current if the expected commercial operation date is less than twelve months and long-term if it is greater than twelve months from the balance sheet date. All project assets are currently held for sale, however, should the Company elect to retain a project asset, it will be classified as long-term upon such election. We review project assets for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

Note 6. Other Current Assets
Other current assets as of July 31, 2015 and October 31, 2014 consisted of the following:

	July 31, 2015	October 31, 2014
Advance payments to vendors [1]	$3,683	$2,372
Deferred finance costs [2]	200	129
Notes receivable	719	529
Prepaid expenses and other [3]	5,531	4,498
Other current assets	$10,133	$7,528

(1) Advance payments to vendors relate to payments for inventory purchases ahead of receipt.
(2) Represents the current portion of direct deferred finance costs relating to securing a $40.0 million loan facility with NRG and is being amortized over the five-year life of the facility.

(3) Primarily relates to other prepaid vendor expenses including insurance, rent and lease payments.

Note 7. Goodwill and Intangible Assets

At July 31, 2015 and October 31, 2014, the Company had goodwill of $4.1 million and intangible assets of $9.6 million associated with the December 2012 Versa acquisition. The intangible asset represents indefinite lived in-process research and development for which the fair value was determined utilizing the cost approach which estimated the costs to replicate cumulative research and

FUELCELL ENERGY, INC.
Notes to Consolidated Financial Statements
(Unaudited)
(Tabular amounts in thousands, except share and per share amounts)

development efforts associated with the development of solid oxide fuel cells (SOFC) stationary power generation and had a 10 percent obsolescence factor applied to account for improvements that could be made on the current technology.

The Company has completed a qualitative assessment at July 31, 2015 and determined that the goodwill and indefinite-lived intangible assets recorded as a result of the Versa acquisition which are included within the Versa reporting unit are not impaired.

Note 8. Other Assets, net

Other assets, net as of July 31, 2015 and October 31, 2014 consisted of the following:

	July 31, 2015	October 31, 2014
Long-term stack residual value (1)	$2,725	$2,725
Deferred finance costs (2)	386	483
Other	346	521
Other assets, net	$3,457	$3,729

(1) Relates to expected residual value for module exchanges performed under the Company's service agreements where the useful life extends beyond the contractual term of the service agreement and the Company obtains title for the module from the customer upon expiration or non-renewal of the service agreement. If the Company does not obtain rights to title from the customer, the cost of the module is expensed at the time of the module exchange.

(2) Represents the long-term portion of direct deferred finance costs relating to securing a $40.0 million loan facility with NRG and will be amortized over the five-year life of the facility.

Note 9. Accrued Liabilities

Accrued liabilities as of July 31, 2015 and October 31, 2014 consisted of the following:

	July 31, 2015	October 31, 2014
Accrued payroll and employee benefits	$4,151	$4,432
Accrued contract and operating costs	34	34
Accrued product warranty cost (1)	698	1,156
Accrued material purchase (2)	4,512	—
Accrued service agreement costs	5,644	3,882
Accrued taxes, legal, professional and other	2,239	2,562
Accrued Liabilities	$17,278	$12,066

(1) Activity in the accrued product warranty costs for the nine months ended July 31, 2015 included additions for estimates of potential future warranty obligations of $0.4 million on contracts in the warranty period and reductions related to actual warranty spend of $0.9 million as contracts progress through the warranty period or are beyond the warranty period.

(2) The Company acts as a procurement agent for POSCO Energy under an Integrated Global Supply Chain Agreement whereby the Company procures materials on POSCO's behalf for their production facility. This liability represents amounts received for the purchase of materials on behalf of POSCO. Amounts due to vendors is recorded as Accounts Payable.

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FUELCELL ENERGY, INC.
Notes to Consolidated Financial Statements
(Unaudited)
(Tabular amounts in thousands, except share and per share amounts)

Note 10. Shareholders' Equity
Changes in shareholders' equity
Changes in shareholders' equity were as follows for the nine months ended July 31, 2015:

	Total Shareholders' Equity	Noncontrolling interest	Total Equity
Balance as of October 31, 2014	$99,987	$ (1,538)	$98,449
Share-based compensation	2,317	—	2,317
Sale of common stock, net of registration fees	21,428	—	21,428
Stock issued under benefit plans net of taxes paid upon vesting of restricted stock awards	(534)	—	(534)
Preferred dividends – Series B	(2,400)	—	(2,400)
Other comprehensive loss - foreign currency translation adjustments	(404)	—	(404)
Reclassification of noncontrolling interest due to liquidation of subsidiary	(1,308)	1,308	—
Net loss	(20,499)	(280)	(20,779)
Balance as of July 31, 2015	$98,587	$ (510)	$98,077

Common Stock Sales
The Company may sell common stock on the open market from time to time. The proceeds of these sales may be used for general corporate purposes or to pay obligations related to the Company's outstanding Series 1 and Series B preferred shares. During the nine months ended July 31, 2015, the Company sold 15,518,847 shares of the Company's common stock at prevailing market prices through periodic trades on the open market and raised approximately $21.4 million, net of fees.

Outstanding Warrants
On September 4, 2013, the Company entered into a co-marketing agreement with NRG for the marketing and sales of the Company's power plants. The terms of the agreement included the issuance of warrants to NRG that permit NRG to purchase up to 5.0 million shares of the Company's common stock at predetermined prices based on attaining minimum sales goals. The first tranche of 1.25 million warrants expired unvested on March 1, 2014 and the second tranche of 1.5 million warrants expired unvested on December 31, 2014. There is one tranche of 2.25 million warrants remaining with a strike price of $1.98 and a qualifying order vesting date through September 2015 and an expiration date of August 2018. Any costs associated with the warrants will be recorded as a reduction of potential future revenue recorded under the arrangement. No warrants were vested and no expense was recorded through July 31, 2015.
On July 30, 2014, the Company also issued a warrant to NRG in conjunction with the entry into a Securities Purchase Agreement for the sale of common stock. Pursuant to the warrant agreement, NRG has the right to purchase up to 2.0 million shares of the Company's common stock at an exercise price of $3.35 per share. The warrant has a term of three years from the Closing Date. The warrants qualified for permanent equity accounting treatment.

FUELCELL ENERGY, INC.
Notes to Consolidated Financial Statements
(Unaudited)
(Tabular amounts in thousands, except share and per share amounts)

Note 11. Loss Per Share
The calculation of basic and diluted loss per share was as follows:

	Three Months Ended July 31,		Nine Months Ended July 31	
	2015	2014	2015	2014
Numerator				
Net loss	$(6,628)	$(7,139)	$(20,779)	$(33,993)
Net loss attributable to noncontrolling interest	89	161	280	568
Preferred stock dividend	(800)	(800)	(2,400)	(2,400)
Net loss attributable to common shareholders	$(7,339)	$(7,778)	$(22,899)	$(35,825)
Denominator				
Weighted average basic common shares	298,609,231	258,178,826	291,747,961	233,933,636
Effect of dilutive securities (1)	—	—	—	—
Weighted average diluted common shares	298,609,231	258,178,826	291,747,961	233,933,636
Basic loss per share	$(0.02)	$(0.03)	$(0.08)	$(0.15)
Diluted loss per share (1)	$(0.02)	$(0.03)	$(0.08)	$(0.15)

(1) Diluted loss per share was computed without consideration to potentially dilutive instruments as their inclusion would have been antidilutive. Potentially dilutive instruments include stock options, unvested restricted stock awards, convertible preferred stock and warrants. As of July 31, 2015 and 2014, there were options to purchase 3.0 million and 3.1 million shares of common stock, respectively, and as of July 31, 2015 and 2014 there were warrants to purchase 4.3 million and 5.75 million shares of common stock, respectively, which were excluded from the computation as they would be antidilutive.

Note 12. Restricted Cash
As of July 31, 2015, there was $27.6 million of cash and cash equivalents pledged as collateral for letters of credit for certain banking requirements and contractual commitments, compared to $25.1 million of cash and cash equivalents pledged as of October 31, 2014. The restricted cash balance for both periods presented includes $15.0 million which has been placed in a Grantor's Trust account to secure certain obligations under a 15-year service agreement and has been classified as long-term. As of July 31, 2015, outstanding letters of credit totaled $9.2 million compared to $7.4 million as of October 31, 2014. These expire on various dates through April 2019.

FUELCELL ENERGY, INC.
Notes to Consolidated Financial Statements
(Unaudited)
(Tabular amounts in thousands, except share and per share amounts)

Note 13. Debt
Debt as of July 31, 2015 and October 31, 2014, consisted of the following:

	July 31, 2015	October 31, 2014
Revolving credit facility	$2,945	945
Connecticut Development Authority Note	2,873	3,033
Connecticut Clean Energy and Finance Investment Authority Note	6,052	6,052
NRG Energy, Inc. Loan Agreement	3,326	—
Capitalized lease obligations	825	721
Total debt	$16,021	$10,751
Current portion of long-term debt	(6,908)	(1,439)
Long-term debt	$9,113	$9,312

On July 30, 2014, the Company's subsidiary, FuelCell Energy Finance, LLC ("FuelCell Finance") entered into a Loan Agreement (the "Loan Agreement") with NRG Energy, Inc. ("NRG"). Pursuant to the Loan Agreement, NRG has extended a $40.0 million revolving construction and term financing facility to FuelCell Finance for the purpose of accelerating project development by the Company and its subsidiaries. FuelCell Finance and its subsidiaries may draw on the facility to finance the construction of projects through the commercial operating date of the power plants. FuelCell Finance has the option to continue the financing term for each project after the commercial operating date for a maximum term of five years per project. The interest rate is 8.5 percent per annum for construction-period financing and 8.0 percent thereafter. Fees that were paid by FuelCell Finance to NRG for making the loan facility available and related legal fees incurred were capitalized and are being amortized straight-line over the life of the related loan agreement, which is five years. In May 2015, our project finance subsidiary, UCI Fuel Cell LLC borrowed $3.3 million which is secured by project assets of this subsidiary. The term of this loan is up to five years but may be repaid early should the project be sold or refinanced at the option of the Company.
On August 1, 2014, the Company entered into a new revolving credit facility with JPMorgan Chase Bank, N.A. (the "Bank") which has a total borrowing capacity of $4.0 million. This credit facility replaces the Company's previous credit facility with the Bank. The credit facility is used for working capital to finance the manufacture and production and subsequent export sale of the Company's products or services. This agreement was extended on June 23, 2015 and the current expiration is November 28, 2015. The outstanding principal balance of the facility will bear interest, at the option of the Company of either the one-month LIBOR plus 1.5 percent or the prime rate of JP Morgan Chase. The facility is secured by certain working capital assets and general intangibles, up to the amount of the outstanding facility balance. The amount outstanding on the credit facility as of July 31, 2015 was $2.9 million.
In April 2008, the Company entered into a 10-year loan agreement with the Connecticut Development Authority to finance equipment purchases associated with manufacturing capacity expansion allowing for a maximum amount borrowed of $4.0 million. The interest rate is 5.0 percent and the loan is collateralized by the assets procured under this loan as well as $4.0 million of additional machinery and equipment. Repayment terms require monthly interest and principal payments through May 2018.

On March 5, 2013 the Company closed on a long-term loan agreement with the Connecticut Clean Energy and Finance Investment Authority (CEFIA, now known as the CT Green Bank) totaling $5.9 million in support of the Bridgeport Fuel Cell Park project. The loan agreement carries an interest rate of 5.0 percent. Interest only payments commenced in January 2014 and principal payments will commence on the eighth anniversary of the project's provisional acceptance date, which is December 20, 2021, payable in forty eight equal monthly installments.

Outstanding amounts are secured by future cash flows from the Bridgeport Fuel Cell Park service agreement.
We lease computer equipment under master lease agreements. Lease payment terms are generally thirty-six months from the date of acceptance for leased equipment.

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

FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q (including exhibits and any information incorporated by reference herein) contains both historical and forward-looking statements that involve risks, uncertainties and assumptions. The statements contained in this report that are not purely historical are forward-looking statements that are subject to the safe harbors created under the Securities Act of 1933, as amended, and the Securities Exchange Act of 1934, as amended, including statements regarding our expectations, beliefs, intentions and strategies for the future. These statements appear in a number of places in this Report and include all statements that are not historical statements of fact regarding our intent, belief or current expectations with respect to, among other things: (i) our ability to achieve our sales plans and cost reduction targets; (ii) trends affecting our financial condition or results of operations; (iii) our growth and operating strategy; (iv) our product development strategy; (v) our financing plans; (vi) the timing and magnitude of future contracts; (vii) changes in the regulatory environment; (viii) potential volatility of energy prices; and (ix) rapid technological change or competition. The words "may," "would," "could," "should," "will," "expect," "estimate," "anticipate," "believe," "intend," "plans" and similar expressions and variations thereof are intended to identify forward-looking statements. Investors are cautioned that any such forward-looking statements are not guarantees of future performance and involve risk and uncertainties, many of which are beyond our ability to control, and that actual results may differ materially from those projected in the forward-looking statements as a result of various factors discussed herein, including those discussed in detail in our filings with the Securities and Exchange Commission ("SEC"), including in our Annual Report on Form 10-K for the fiscal year ended October 31, 2014 in the section entitled "Item 1A. Risk Factors."

Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") is provided as a supplement to the accompanying financial statements and footnotes to help provide an understanding of our financial condition, changes in our financial condition and results of operations. The preparation of financial statements and related disclosures in conformity with accounting principles generally accepted in the U.S. requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and the disclosure of contingent assets and liabilities. Estimates are used in accounting for, among other things, revenue recognition, excess, slow-moving and obsolete inventories, product warranty costs, reserves on service agreements, allowance for uncollectible receivables, depreciation and amortization, impairment of goodwill, indefinite-lived intangible assets and long-lived assets, income taxes, and contingencies. Estimates and assumptions are reviewed periodically, and the effects of revisions are reflected in the consolidated financial statements in the period they are determined to be necessary. Due to the inherent uncertainty involved in making estimates, actual results in future periods may differ from those estimates. The following discussion should be read in conjunction with information included in our Annual Report on Form 10-K for the year ended October 31, 2014 filed with the SEC. Unless otherwise indicated, the terms "Company", "FuelCell Energy", "we", "us", and "our" refer to FuelCell Energy Inc. and its subsidiaries. All tabular dollar amounts are in thousands.

OVERVIEW AND RECENT DEVELOPMENTS

Overview

We are an integrated fuel cell company with an expanding global presence on three continents. We design, manufacture, sell, install, operate and service ultra-clean, highly efficient stationary fuel cell power plants for distributed power generation. Our power plants provide megawatt-class scalable on-site power and utility grid support, helping customers solve their energy, environmental and business challenges. Our plants are operating in more than 50 locations in nine countries on three different continents and have generated more than 3.9 billion kilowatt hours (kWh) of electricity, which is equivalent to powering more than 357,000 average size U.S. homes for one year. Our growing installed base and backlog exceeds 300 megawatts (MW).

We provide comprehensive turn-key power generation solutions to our customers including installation of the power plants as well as operating and maintaining the plants under multi-year service agreements. We target large-scale power users with our megawatt-class installations. As reference, one megawatt is adequate to power approximately 1,000 average sized US homes. Our customer base includes utility companies, municipalities, universities, government entities and businesses in a variety of Industrial and commercial enterprises. Our leading geographic markets are South Korea and the United States and we are pursuing expanding opportunities in Asia and Europe.

Our value proposition provides highly efficient and environmentally friendly power generation with easy-to-site stationary fuel cell power plants. The power plants are located in populated areas as they are virtually pollutant free, operate quietly and without vibrations, and have only modest space requirements. Locating the power generation near the point of use provides many advantages including less reliance on or even avoidance of the transmission grid leading to enhanced energy security and power reliability.

Our power plants provide electricity priced competitively to grid-delivered electricity in certain high cost regions and our strategy is to continue to reduce costs, which is expected to lead to wider adoption.

We are developing Advanced Technologies which leverage our commercial platform and expertise. Our Direct FuelCell® (DFC®) power plants utilize carbonate fuel cell technology, which is a very versatile type of fuel cell technology. Utilizing our core DFC plants, we have developed and are commercializing both a tri-generation distributed hydrogen configuration that generates electricity, heat and hydrogen for industrial or transportation uses, and a carbon capture application for coal or gas-fired power plants. We also are developing and working to commercialize solid oxide fuel cells (SOFC) for adjacent sub-megawatt applications to the markets for our megawatt-class DFC power plants as well as energy storage applications. These applications are complementary to our core products, leverage our existing customer base, project development, sales and service expertise, and are potentially large markets.

RESULTS OF OPERATIONS

Management evaluates the results of operations and cash flows using a variety of key performance indicators including revenues compared to prior periods and internal forecasts, costs of our products and results of our "cost-out" initiatives, and operating cash use. These are discussed throughout the 'Results of Operations' and 'Liquidity and Capital Resources' sections.

Comparison of Three Months Ended July 31, 2015 and 2014

Revenues and Costs of revenues

Our revenues and cost of revenues for the three months ended July 31, 2015 and 2014 were as follows:

	Three Months Ended July 31,		Change	
(dollars in thousands)	2015	2014	$	%
Total revenues	$ 41,356	$ 43,176	$ (1,820)	(4)
Total costs of revenues	$ 37,761	$ 39,215	$ (1,454)	(4)
Gross profit	$ 3,595	$ 3,961	$ (366)	(9)
Gross margin percentage	8.7 %	9.2 %		

Total revenues for the three months ended July 31, 2015 decreased $1.8 million to $41.4 million from $43.2 million during the same period last year. Total cost of revenues for the three months ended July 31, 2015 decreased by $1.5 million to $37.8 million from $39.2 million during the same period last year. A discussion of the changes in product sales and service and license revenues and advanced technologies contract revenues follows.

Product sales

Our product sales, cost of sales and gross profit for three months ended July 31, 2015 and 2014 were as follows:

	Three Months Ended July 31,		Change	
(dollars in thousands)	2015	2014	$	%
Product sales	$ 31,130	$ 32,315	$(1,185)	(4)
Cost of product sales	28,849	29,308	(459)	(2)
Gross profit from product sales	$ 2,281	$ 3,007	$(726)	(24)
Product sales gross margin	7.3 %	9.3 %		

Product sales for the three months ended July 31, 2015 included $0.9 million of power plant revenue, $22.9 million of fuel cell kits and module revenue and $7.3 million of revenue primarily related to power plant component sales and engineering and construction services. This is compared to product sales for the three months ended July 31, 2014 which included $14.1 million of power plant revenue, $16.9 million of fuel cell kits and module revenue and $1.3 million of revenue primarily from power plant component sales and engineering and construction services. The decline in revenue during the period is due to decreased power plant and kit sales offset by an increase for module sales and an increase in the level of engineering and construction services being performed compared to the prior period.

Cost of product sales decreased $0.5 million for the three months ended July 31, 2015 to $28.8 million, compared to $29.3 million in the same prior year period. Gross profit decreased $0.7 million to a gross profit of $2.3 million for the three months ended July 31, 2015 compared to a gross profit of $3.0 million for the three months ended July 31, 2014. The year-over-year decrease in gross margin reflects a change in product mix in the period with lower margins on power plant sales offset by favorable margins for module and kit sales and engineering and construction services. The decline in gross margin percentage from 9.3% to 7.3% is due to lower Multi-MW product revenue and margin on sales mix and higher installation costs in the quarter compared to the same period last year.

As the Company's development business expands, it is installing power plants for customers that have executed power purchase agreements. The power plants are recognized as Project assets on the balance sheet and revenue will be recognized once definitive sales agreements are executed.

Service agreements and license revenues

	Three Months Ended July 31,		Change	
(dollars in thousands)	2015	2014	$	%
Service agreements and license revenues	$ 7,017	$ 7,078	$(61)	(1)
Cost of service agreements and license revenues	5,719	6,629	(910)	(14)
Gross profit from service agreements and license revenues	$ 1,298	$ 449	$849	189
Service agreement and license revenues gross margin	18.5 %	6.3 %		

Revenues for the three months ended July 31, 2015 from service agreements and license fee and royalty agreements totaled $7.0 million, compared to $7.1 million the prior year period. Module exchanges in the third quarter of 2015 resulted in approximately $1.8 million of service revenue compared to approximately $1.9 million of service revenue recognized related to module replacements during the third quarter of 2014. Revenue from license and royalty agreements increased to $1.3 million for the three month period ended July 31, 2015, compared to $1.0 million for the comparable prior year period.

Cost of service agreements and license revenues decreased to $5.7 million from $6.6 million for the prior year period. Cost of service agreements includes maintenance and operating costs, module exchanges and performance guarantees.

Overall gross profit increased by $0.8 million which includes higher profit recognized from the growing fleet and engineering services of $1.1 million, higher license and royalty revenue of $0.3 million which was offset by higher performance guarantees of $0.6 million. These increases resulted in an overall gross margin percentage of 18.5 percent compared to 6.3 percent in the prior year period.

Service revenue from scheduled module exchanges is recognized at the time of the module exchange activity whereas the remaining portion of service revenue from service agreements is recognized ratably over the life of the service contract. As a result, quarterly revenue and gross profit related to module exchanges can fluctuate quarter to quarter. Additional power plant installations will lead to growth in service revenue.

Advanced technologies contract revenues

Advanced technologies contracts revenue and related costs for the three months ended July 31, 2015 and 2014 were as follows:

	Three Months Ended July 31,		Change	
(dollars in thousands)	2015	2014	$	%
Advanced technologies contract revenues	$ 3,209	$ 3,783	$(574)	(15)
Cost of advanced technologies contract revenues	3,193	3,278	(85)	(3)
Gross profit	$ 16	$ 505	$(489)	(97)
Advanced technologies contracts gross margin	0.5 %	13.3 %		

Advanced technologies contracts revenue for the three months ended July 31, 2015 was $3.2 million, which decreased $0.6 million when compared to $3.8 million of revenue for the three months ended July 31, 2014. Cost of advanced technologies contracts decreased $0.1 million to $3.2 million for the three months ended July 31, 2015, compared to $3.3 million for the same period in the prior year. Gross profit from advanced technologies contracts for the three months ended July 31, 2015 was essentially breakeven compared to gross profit of $0.5 million for the three months ended July 31, 2014. The decrease in gross profit is related to the mix of contracts currently being performed which include cost share obligations.

Administrative and selling expenses

Administrative and selling expenses were $6.1 million for the three months ended July 31, 2015 compared to $5.6 million during the three months ended July 31, 2014. Administrative and selling expenses increased due to higher project proposal and development related expenses for multiple power plant installations.

Research and development expenses

Research and development expenses were $4.6 million for the three months ended July 31, 2015 compared to $4.4 million during the three months ended July 31, 2014. The Company's internal research and development continues to be focused on initiatives that have near term product implementation potential and product cost reduction opportunities.

Loss from operations

Loss from operations for the three months ended July 31, 2015 was $7.1 million compared to $6.0 million for the three months ended July 31, 2014.

Interest expense

Interest expense for the three months ended July 31, 2015 and 2014 was $0.9 million and $0.6 million, respectively. Interest expense for the current year quarter was higher partly due to the inclusion of interest on the unused portion of the NRG Energy, Inc. Loan Agreement of $0.2 million. Interest expense for both periods includes interest for the amortization of the redeemable preferred stock of subsidiary discount of $0.5 million.

Other income (expense), net

Other income (expense), net, was income of $1.5 million for the three month period ended July 31, 2015 compared to expense of $0.4 million for the same period in 2014. The current period income primarily represents net unrealized foreign exchange gains

of $0.9 million related primarily to the preferred stock obligation of our Canadian subsidiary which is payable in Canadian dollars and research and development tax credits of $0.6 million. The prior period expense includes foreign exchange losses of $0.2 million and a charge of $0.1 million related to the make-whole payment upon conversion of the remaining $1.0 million of principal of the 8.0% Convertible Notes. The Company primarily used common stock to settle this make-whole obligation.

Provision for income taxes

We have not paid federal or state income taxes in several years due to our history of net operating losses (NOL), although we have paid foreign income and withholding taxes in South Korea. For the three months ended July 31, 2015 and 2014 our provision for income taxes was $0.1 million. We manufacture products that are gross margin profitable on a per unit basis; however, we cannot estimate when production volumes will be sufficient to generate taxable domestic income. Accordingly, no tax benefit has been recognized for net operating losses or other deferred tax assets as significant uncertainty exists surrounding the recoverability of these deferred tax assets.

Net loss attributable to noncontrolling interest

The net loss attributed to the noncontrolling interest for the three months ended July 31, 2015 and 2014 was $0.1 million and $0.2 million, respectively.

Preferred Stock dividends

Dividends recorded on the Series B Preferred Stock were $0.8 million for the three month periods ended July 31, 2015 and 2014.

Net loss attributable to common shareholders and loss per common share

Net loss attributable to common shareholders represents the net loss for the period less the net loss attributable to noncontrolling interest, less the preferred stock dividends on the Series B Preferred Stock. For the three month periods ended July 31, 2015 and 2014, net loss attributable to common shareholders was $7.3 million and $7.8 million, respectively, and loss per common share was $0.02 and $0.03, respectively.

Comparison of Nine Months Ended July 31, 2015 and 2014

Revenues and Costs of revenues

Our revenues and cost of revenues for the nine months ended July 31, 2015 and 2014 were as follows:

	Nine Months Ended July 31,		Change	
(dollars in thousands)	2015	2014	$	%
Total revenues	$ 111,626	$ 125,884	$ (14,258)	(11)
Total costs of revenues	$ 101,994	$ 118,113	$ (16,119)	(14)
Gross profit	$ 9,632	$ 7,771	$ 1,861	24
Gross margin percentage	8.6 %	6.2 %		

Total revenues for the nine months ended July 31, 2015 decreased $14.3 million, or 11 percent, to $111.6 million from $125.9 million during the same period last year. Total cost of revenues for the nine months ended July 31, 2015 decreased by $16.1 million, or 14 percent, to $102.0 million from $118.1 million during the same period last year. A discussion of the changes in product sales and service and license revenues and advanced technologies contract revenues follows.

Product sales

Our product sales, cost of sales and gross profit for nine months ended July 31, 2015 and 2014 were as follows:

	Nine Months Ended July 31,		Change	
(dollars in thousands)	2015	2014	$	%
Product sales	$ 84,769	$ 94,482	$(9,713)	(10)
Cost of product sales	77,308	88,944	(11,636)	(13)
Gross profit from product sales	$ 7,461	$ 5,538	$1,923	35
Product sales gross margin	8.8 %	5.9 %		

Product sales for the nine months ended July 31, 2015 included $10.8 million of power plant revenue, $55.2 million of fuel cell kits and module revenue and $18.8 million of revenue primarily related to power plant component sales and engineering and construction services. This is compared to product sales for the nine months ended July 31, 2014 which included $15.9 million of power plant revenue, $66.4 million of fuel cell kits and module revenue and $12.2 million of revenue primarily from power plant component sales and engineering and construction services. The decline in revenue during the period is due to the decreased sales of fuel cell kits and modules and power plant revenue partly offset by an increase in power plant component sales and engineering and construction services.

Cost of product sales decreased $11.6 million for the nine months ended July 31, 2015 to $77.3 million, compared to $88.9 million in the same prior year period. Gross profit increased $1.9 million to a gross profit of $7.5 million for the nine months ended July 31, 2015 compared to a gross profit of $5.5 million for the nine months ended July 31, 2014. The increase in gross profit was due to lower warranty and quality expenses and higher gross profit related to power plant component sales and engineering and construction services.

Service agreements and license revenues

	Nine Months Ended July 31,		Change	
(dollars in thousands)	2015	2014	$	%
Service agreements and license revenues	$ 15,506	$ 19,215	$(3,709)	(19)
Cost of service agreements and license revenues	13,720	17,546	(3,826)	(22)
Gross profit from service agreements and license revenues	$ 1,786	$ 1,669	$117	7
Service agreement and license revenues gross margin	11.5 %	8.7 %		

Revenues from service agreements and license fee and royalty agreements for the nine months ended July 31, 2015 totaled $15.5 million, compared to $19.2 million in the prior year period. Revenue has declined due to the timing of module exchanges for the nine months ended July 31, 2015 versus the comparable prior year period and a transition of service responsibilities to POSCO Energy under the Master Service Agreement. Revenue recorded relating to the module replacements during the nine months ended July 31, 2015 was $1.8 million compared to approximately $5.7 million of service revenue recognized related to module replacements during the nine months ended July 31, 2014.

Cost of service agreements and license revenues decreased to $13.7 million from $17.5 million for the prior year period. Cost of service agreements includes maintenance and operating costs, module exchanges and performance guarantees. The gross profit on service agreements and license and royalty agreements increased to $1.8 million for the nine month period ended July 31, 2015, compared to $1.7 million for the comparable prior year period on higher margins recognized on new service agreements related to the growing fleet.

Advanced technologies contract revenues

Advanced technologies contracts revenue and related costs for the nine months ended July 31, 2015 and 2014 were as follows:

	Nine Months Ended July 31,		Change	
(dollars in thousands)	2015	2014	$	%
Advanced technologies contract revenues	$ 11,351			