SUPERCONDUCTOR TECHNOLOGIES INC
Form 10-Q
May 09, 2012
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2012

¨ **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 0-21074

SUPERCONDUCTOR TECHNOLOGIES INC.

(Exact name of registrant as specified in its charter)

Delaware	**77-0158076**
(State or other jurisdiction of incorporation or organization)	**(IRS Employer Identification No.)**

460 Ward Drive,

Santa Barbara, California 93111-2356

(Address of principal executive offices & zip code)

(805) 690-4500

(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 x 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 x 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 definition 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 ¨ (do not check if smaller reporting company)	Smaller reporting company x

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

We had 40,268,376 shares of our common stock outstanding as of the close of business on May 1, 2012.

Table of Contents

SUPERCONDUCTOR TECHNOLOGIES INC.

INDEX TO FORM 10-Q

Three Months Ended March 31, 2012

Table of Contents

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. We claim the protection of the safe harbor contained in the Private Securities Litigation Reform Act of 1995 for these forward looking statements. Our forward-looking statements relate to future events or our future performance and include, but are not limited to, statements concerning our business strategy, future commercial revenues, market growth, capital requirements, new product introductions, expansion plans and the adequacy of our funding. Other statements contained in this Report that are not historical facts are also forward-looking statements. We have tried, wherever possible, to identify forward-looking statements by terminology such as may, will, could, should, expects, anticipates, intends, plans, believes, seeks, estimates and other comparable terminology.

We caution investors that any forward-looking statements presented in this Report, or that we may make orally or in writing from time to time, are based on our beliefs and assumptions made by, and information currently available to, us. Such statements are based on assumptions and the actual outcome will be affected by known and unknown risks, trends, uncertainties and factors that are beyond our control or ability to predict. Although we believe that our assumptions are reasonable, they are not guarantees of future performance and some will inevitably prove to be incorrect. As a result, our actual future results can be expected to differ from our expectations, and those differences may be material. Accordingly, investors should use caution in relying on past forward-looking statements, which are based on known results and trends at the time they are made, to anticipate future results or trends.

Some of the risks and uncertainties that may cause our actual results, performance or achievements to differ materially from those expressed or implied by forward-looking statements include the following:

limited cash and a history of losses;

our need to raise additional capital for our business;

our need to overcome additional technical challenges necessary to develop and commercialize HTS wire;

limited number of potential customers;

decreases in average selling prices for our products;

rapidly advancing technology in our target markets;

the impact of competitive products, technologies and pricing;

limited number of suppliers for some of our components;

no significant backlog from quarter to quarter;

fluctuations in sales and product demand from quarter to quarter can be significant;

our proprietary rights, while important to our business, are difficult and costly to protect;

manufacturing capacity constraints and difficulties;

the current worldwide recession; and

cost and uncertainty from compliance with environmental regulations.

For further discussion of these and other factors see, Management s Discussion and Analysis of Financial Condition and Results of Operations and Risk Factors in our Annual Report on Form 10-K for 2011.

This Report and all subsequent written and oral forward-looking statements attributable to us or any person acting on our behalf are expressly qualified in their entirety by the cautionary statements contained or referred to in this section. We do not undertake any obligation to release publicly any revisions to our forward-looking statements to reflect events or circumstances after the date of this Report.

Table of Contents

PART I

FINANCIAL INFORMATION

Item 1. Financial Statements.

SUPERCONDUCTOR TECHNOLOGIES INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

	Three Months Ended	
	March 31, 2012	**April 2, 2011**
Net revenues:		
Commercial product revenues	$ 344,000	$ 1,603,000
Government and other contract revenues	55,000	17,000
Total net revenues	**399,000**	**1,620,000**
Costs and expenses:		
Cost of commercial product revenues	844,000	1,669,000
Cost of government and other contract revenue	52,000	15,000
Research and development	1,161,000	1,988,000
Selling, general and administrative	1,348,000	1,656,000
Total costs and expenses	**3,405,000**	**5,328,000**
Loss from operations	**(3,006,000)**	**(3,708,000)**
Other Income and Expense		
Other income	16,000	
Interest income	2,000	2,000
Interest expense		(7,000)
Net loss	**$ (2,988,000)**	**$ (3,713,000)**
Basic and diluted loss per common share	**$ (0.08)**	**$ (0.12)**
Weighted average number of common shares outstanding	35,577,732	30,219,318

See accompanying notes to the unaudited interim condensed consolidated financial statements.

Table of Contents

SUPERCONDUCTOR TECHNOLOGIES INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

	March 31, 2012 (Unaudited)	December 31, 2011 (See Note)
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 9,530,000	$ 6,165,000
Accounts receivable, net	181,000	61,000
Inventory, net	1,356,000	1,609,000
Prepaid expenses and other current assets	388,000	472,000
Total Current Assets	**11,455,000**	**8,307,000**
Property and equipment, net of accumulated depreciation of $19,442,000 and $19,748,000, respectively	4,697,000	2,871,000
Patents, licenses and purchased technology, net of accumulated amortization of $2,362,000 and $2,342,000, respectively	1,393,000	1,409,000
Other assets	361,000	362,000
Total Assets	**$ 17,906,000**	**$ 12,949,000**
LIABILITIES AND STOCKHOLDERS EQUITY		
Current Liabilities:		
Accounts payable	$ 1,599,000	$ 534,000
Accrued expenses	713,000	612,000
Total Current Liabilities	**2,312,000**	**1,146,000**
Other long term liabilities	593,000	628,000
Total Liabilities	**2,905,000**	**1,774,000**
Commitments and contingencies-Notes 6 and 7		
Stockholders Equity:		
Preferred stock, $.001 par value, 2,000,000 shares authorized, 564,642 shares issued and outstanding	1,000	1,000
Common stock, $.001 par value, 250,000,000 shares authorized, 40,268,376 and 33,362,281 shares issued and outstanding, respectively	40,000	33,000
Capital in excess of par value	268,964,000	262,157,000
Accumulated deficit	(254,004,000)	(251,016,000)
Total Stockholders Equity	**15,001,000**	**11,175,000**
Total Liabilities and Stockholders Equity	**$ 17,906,000**	**$ 12,949,000**

See accompanying notes to the unaudited interim condensed consolidated financial statements.

Note December 31, 2011 balances were derived from audited financial statements.

Table of Contents

SUPERCONDUCTOR TECHNOLOGIES INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Three Months Ended	
	March 31, 2012	**April 2, 2011**
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (2,988,000)	$ (3,713,000)
Adjustments to reconcile net loss to net cash used for operating activities:		
Depreciation and amortization	66,000	211,000
Stock-based compensation expense	321,000	395,000
Write-off of intangibles		770,000
Provision for excess and obsolete inventories	92,000	
Gain on disposal of property and equipment	(15,000)	
Changes in assets and liabilities:		
Accounts receivable	(119,000)	(471,000)
Inventories	161,000	277,000
Prepaid expenses and other current assets	37,000	120,000
Patents and licenses	30,000	(42,000)
Other assets	2,000	2,000
Accounts payable, accrued expenses and other current liabilities	237,000	405,000
Net cash used in operating activities	(2,176,000)	(2,046,000)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment	(966,000)	(35,000)
Net proceeds from the sale of property and equipment	15,000	
Net cash used in investing activities	(951,000)	(35,000)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Repurchase of common shares for withholding obligations	(129,000)	(278,000)
Net proceeds from the sale of common stock	6,621,000	12,402,000
Net cash provided by financing activities	6,492,000	12,124,000
Net increase in cash and cash equivalents	3,365,000	10,043,000
Cash and cash equivalents at beginning of period	6,165,000	6,069,000
Cash and cash equivalents at end of period	$ 9,530,000	$ 16,112,000

See accompanying notes to the unaudited interim condensed consolidated financial statements.

Table of Contents

SUPERCONDUCTOR TECHNOLOGIES INC.

NOTES TO UNAUDITED INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. General

We are a leading company in developing and commercializing high temperature superconductor (HTS) materials and related technologies. Superconductivity is the unique ability to conduct various signals or energy (e.g., electrical current or radio frequency (RF) signals) with little or no resistance when cooled to critical temperatures. HTS materials are a family of elements that demonstrate superconducting properties at temperatures significantly warmer than previous superconducting materials. Electric currents that flow through conventional conductors encounter resistance that requires power to overcome and generates heat. HTS materials can substantially improve the performance characteristics of electrical systems, reducing power loss, lowering heat generation, and decreasing electrical noise.

We were established in 1987 shortly after the discovery of HTS materials, a family of elements that demonstrate superconducting properties at temperatures significantly warmer than previous superconducting materials. Our stated objective was to develop products based on these materials for the commercial marketplace.

After analyzing the market opportunities available, we decided to pursue a strategic revenue opportunity developing products for the electronics industry.

Our initial product was completed in 1998 and we began delivery to a number of wireless network providers. In the following 13 years, we continued to refine and improve the platform, with the primary focus on improving reliability, increasing performance and runtime, and most importantly, removing cost from the manufacturing process of the required subsystems. Our cost reducing efforts led to the invention of our proprietary, high-yield and high throughput HTS material deposition manufacturing process.

In the last several years we have focused our research and development efforts on adapting our successful HTS materials deposition techniques to production of high performance second generation 2G HTS wire for next generation power applications. While all our current commercial product revenues come from the sale of high performance wireless infrastructure products, we now see production of our Conductus® HTS wire as an excellent strategic opportunity to grow our future revenue.

For the three months ended March 31, 2012 and April 2, 2011, commercial product revenues accounted for 86% and 99%, respectively, of our net revenues.

Our research and development contracts are used as a source of funds for our commercial technology development. We continue to be involved as either contractor or subcontractor on a number of contracts with the U.S. government. For the three months ended March 31, 2012 and April 2, 2011, government and other contract revenues accounted for 14% and 1%, respectively, of our net revenues.

The unaudited condensed consolidated financial information furnished herein has been prepared in accordance with generally accepted accounting principles and reflects all adjustments, consisting only of normal recurring adjustments, which in the opinion of management, are necessary for a fair statement of the results of operations for the periods presented.

The preparation of the condensed consolidated financial statements in conformity with generally accepted accounting principles requires us to make estimates and assumptions that affect the amounts reported in the condensed consolidated financial statements and the accompanying notes. Actual results could differ from those estimates and such differences may be material to the condensed consolidated financial statements. This quarterly report on Form 10-Q should be read in conjunction with our Form 10-K for 2011, The results of operations for the three months ended March 31, 2012 are not necessarily indicative of the results for all of 2012.

2. Summary of Significant Accounting Policies

Basis of Presentation

For the three months ended March 31, 2012, we incurred a net loss of $3.0 million and negative cash flows from operations of $2.2 million. For all of 2011, we incurred a net loss of $13.4 million and had negative cash flows from operations of $10.0 million.

5

Table of Contents

At March 31, 2012, we had $9.5 million in cash and cash equivalents. Our current cash resources will not be sufficient to fund our business for the next 12 months. We believe the key factors to our future liquidity will be our ability to successfully use our expertise and our technology to generate revenues in various ways, including commercial operations, government contracts, joint ventures and licenses. Because of the uncertainty of these factors, we will need to raise funds to meet our working capital needs. Additional financing may not be available on acceptable terms or at all. If we issue additional equity securities to raise funds, the ownership percentage of our existing stockholders would be reduced. New investors may demand rights, preferences or privileges senior to those of existing holders of common stock. If we cannot raise any needed funds, we might be forced to make further substantial reductions in our operating expenses, which could adversely affect our ability to implement our current business plan and ultimately our viability as a company.

Our condensed consolidated financial statements do not include any adjustments that might result from this uncertainty. Our condensed consolidated financial statements have been prepared assuming that we will continue as a going concern.

Principles of Consolidation

The interim condensed consolidated financial statements include the accounts of Superconductor Technologies Inc. and its wholly owned subsidiaries. All significant intercompany transactions have been eliminated from the condensed consolidated financial statements.

Cash and Cash Equivalents

Cash and cash equivalents consist of highly liquid investments with original maturities of three months or less. Cash and cash equivalents are maintained with what we believe to be quality financial institutions and from time to time exceed FDIC limits. Historically, we have not experienced any losses due to such concentration of credit risk.

Accounts Receivable

We sell predominantly to entities in the wireless communications industry and to entities of the U.S. government. We grant uncollateralized credit to our customers. We perform usual and customary credit evaluations of our customers before granting credit. Trade accounts receivable are recorded at the invoiced amount and do not bear interest. The allowance for doubtful accounts is our best estimate of the amount of probable credit losses in our existing accounts receivable. We determine the allowance based on historical write-off experience. Past due balances are reviewed for collectibility. Accounts balances are charged off against the allowance when we deem it is probable the receivable will not be recovered. We do not have any off -balance sheet credit exposure related to our customers.

Revenue Recognition

Commercial revenues are principally derived from the sale of our SuperLink, AmpLink and SuperPlex family of products and are recognized once all of the following conditions have been met: a) an authorized purchase order has been received in writing, b) the customer s credit worthiness has been established, c) shipment of the product has occurred, d) title has transferred, and e) if stipulated by the contract, customer acceptance has occurred and all significant vendor obligations, if any, have been satisfied.

Contract revenues are principally generated under research and development contracts. Contract revenues are recognized utilizing the percentage-of-completion method measured by the relationship of costs incurred to total estimated contract costs. If the current contract estimate were to indicate a loss, utilizing the funded amount of the contract, a provision would be made for the total anticipated loss. Revenues from research related activities are derived primarily from contracts with agencies of the U.S. Government. Credit risk related to accounts receivable arising from such contracts is considered minimal. These contracts include cost-plus, fixed price and cost sharing arrangements and are generally short-term in nature.

All payments to us for work performed on contracts with agencies of the U.S. Government are subject to adjustment upon audit by the Defense Contract Audit Agency. Contract audits through 2003 are closed. Based on historical experience and review of current projects in process, we believe that the audits will not have a significant effect on our financial position, results of operations or cash flows.

Shipping and Handling Fees and Costs

Shipping and handling fees billed to customers are included in net commercial product revenues. Shipping and handling fees associated with freight are generally included in cost of commercial product revenues.

Warranties

We offer warranties generally ranging from one to five years, depending on the product and negotiated terms of purchase agreements with our customers. Such warranties require us to repair or replace defective product returned to us during such warranty period at no cost to the customer. An estimate by us for warranty related costs is recorded by us at the time of sale based on our actual historical product return rates and expected repair costs. Such costs have been within our expectations.

Table of Contents

Indemnities

In connection with the sales and manufacturing of our commercial products, we indemnify, without limit or term, our customers and contract manufacturers against all claims, suits, demands, damages, liabilities, expenses, judgments, settlements and penalties arising from actual or alleged infringement or misappropriation of any intellectual property relating to our products or other claims arising from our products. We cannot reasonably develop an estimate of the maximum potential amount of payments that might be made under our indemnities because of the uncertainty as to whether a claim might arise and how much it might total. Historically, we have not incurred any expenses related to these indemnities.

Research and Development Costs

Research and development costs are charged to expense as incurred and include salary, facility, depreciation and material expenses. Research and development costs are charged to research and development expense. Research and development costs incurred solely in connection with research and development contracts are charged to government and other contract expense. Additionally, in 2011, we decided to use certain of our own technologies and we therefore voluntarily terminated a patent license we had with a third party along with certain other related intangible assets. As a result, capitalized cost of $0.8 million was charged to research and development during the first quarter of 2011. There were no such charges in the first quarter of 2012.

Inventories

Inventories are stated at the lower of cost or market, with costs primarily determined using standard costs, which approximate actual costs utilizing the first-in, first-out method. We review inventory quantities on hand and on order and record, on a quarterly basis, a provision for excess and obsolete inventory and/or vendor cancellation charges related to purchase commitments. If the results of the review determine that a write-down is necessary, we recognize a loss in the period in which the loss is identified, whether or not the inventory is retained. Our inventory reserves establish a new cost basis for inventory and are not reversed until we sell or dispose of the related inventory. Such provisions are established based on historical usage, adjusted for known changes in demands for such products, or the estimated forecast of product demand and production requirements. Costs associated with idle capacity are charged to expense immediately.

Property and Equipment

Property and equipment are recorded at cost. Equipment is depreciated using the straight-line method over their estimated useful lives ranging from three to seven years. Leasehold improvements and assets financed under capital leases are amortized over the shorter of their useful lives or the lease term. Furniture and fixtures are depreciated over seven years. Expenditures for additions and major improvements are capitalized. Expenditures for minor tooling, repairs and maintenance and minor improvements are charged to expense as incurred. When property or equipment is retired or otherwise disposed of, the related cost and accumulated depreciation are removed from the accounts. Gains or losses from retirements and disposals are recorded in selling, general and administration expenses. In the first quarter of 2012, there were disposals totaling $344,000 and gains of $15,000 from these disposals. In 2011, there were disposals totaling $2.9 million and gains of $269,000 from these disposals.

Patents, Licenses and Purchased Technology

Patents and licenses are recorded at cost and are amortized using the straight-line method over the shorter of their estimated useful lives or approximately seventeen years. Purchased technology acquired through the acquisition of Conductus, Inc. in 2002 was recorded at our estimated fair value and was amortized using the straight-line method over seven years ending in 2009.

Long-Lived Assets

The realizability of long-lived assets is evaluated periodically as events or circumstances indicate a possible inability to recover the carrying amount. Long-lived assets that will no longer be used in business are written off in the period identified since they will no longer generate any positive cash flows for us. Long-lived assets that will continue to be used by us are periodically evaluated for recoverability. Such evaluation is based on various analyses, including cash flow and profitability projections. The analyses necessarily involve significant management judgment. In the event the projected undiscounted cash flows are less than net book value of the assets, the carrying value of the assets is written down to its estimated fair value. We tested our long lived assets for recoverability during 2011 and did not believe that there was any impairment.

7

Table of Contents

While we believe the expected cash flows from these long-lived assets, including intangible assets, exceed the carrying amounts, materially different assumptions regarding future performance and discount rates could result in future impairment losses. In particular, if we no longer believe we will achieve our long-term projected sales or operating expenses, we may conclude, in connection with any future impairment tests, that the estimated fair value of our long-lived assets, including intangible assets, is less than the book value and recognize an impairment charge. Any impairment charge would adversely affect our earnings.

Other Investments

From time to time we may pursue joint ventures with other entities to commercialize our technology. In 2007, we formed a joint venture with Hunchun BaoLi Communication Co. Ltd. to manufacture and sell our SuperLink interference elimination solution in China. We use the equity method of accounting for our 45 percent joint venture interest. The joint venture agreement called for our joint venture partner to supply the capital and local expertise, and for us to provide a license of certain technology and supply key parts for manufacturing. Since 2007, we have been conducting lab and field trials in the existing China 2G market using our TD-SCDMA and SuperLink solutions. Although those activities continue, the parties have not completed their contributions to the joint venture, including most of the funding and our license, within the two year period specified by the agreement and Chinese law. The future of the joint venture, including any commencement of manufacturing and the transfer of our processes, will depend on product demand in China, completion of funding by our joint venture partner, as well as a number of other conditions, including certain critical approvals from the Chinese and U.S. governments. There continues to be no assurance that these conditions will be met and even if these conditions are met and the approvals received, the results from our joint venture will be subject to a number of significant risks associated with international operations and new ventures, some of which are set forth in our public filings, including in particular the Risk Factors included in Item 1A of our Annual Report on Form 10-K for 2011. We incurred no expenses in the quarter ended March 31, 2012 or in the full year 2011 as a result of this joint venture.

Loss Contingencies

In the normal course of our business we are subject to claims and litigation, including allegations of patent infringement. Liabilities relating to these claims are recorded when it is determined that a loss is probable and the amount of the loss can be reasonably estimated. The costs of our defense in such matters are expensed as incurred. Insurance proceeds recoverable are recorded when deemed probable.

Income Taxes

We recognize deferred tax liabilities and assets based on the differences between the financial statement carrying amounts and the tax bases of assets and liabilities, using enacted tax rates in effect in the years the differences are expected to reverse. Deferred income tax benefit (expense) results from the change in net deferred tax assets or deferred tax liabilities. A valuation allowance is recorded when it is more likely than not that some or all deferred tax assets will not be realized. The guidance further clarifies the accounting for uncertainty in income taxes and sets a consistent framework to determine the appropriate level of tax reserve to maintain for uncertain tax positions. This interpretation uses a two-step approach wherein a tax benefit is recognized if a position is more-likely-than-not to be sustained. The amount of the benefit is then measured to be the highest tax benefit that is greater than 50% likely to be realized and sets out disclosure requirements to enhance transparency of our tax reserves. The adoption of this guidance has not had a material impact on our consolidated financial statements as we concluded our tax positions are highly certain of being settled at 100% of the benefit claimed. Guidance is also provided on the accounting for the related interest and penalties, financial statement and disclosure. We are currently not under examination by any taxing authority nor have we been notified of an impending examination. The oldest tax year that remains open to possible evaluation and interpretation of our tax position is 1996.

As of December 31, 2011, we had net operating loss carryforwards for federal and state income tax purposes of approximately $308.4 million and $181.5 million, respectively, which expire in the years 2012 through 2031. Due to the uncertainty surrounding their realization, we recorded a full valuation allowance against our net deferred tax assets. Accordingly, no deferred tax asset has been recorded in the accompanying condensed consolidated balance sheets.

Marketing Costs

All costs related to marketing and advertising our products are charged to expense as incurred or at the time the advertising takes place. Advertising costs were not material in each of the quarters ended March 31, 2012 and April 2, 2011.

Net Loss Per Share

Basic and diluted net loss per share is computed by dividing net loss available to common stockholders by the weighted average number of common shares outstanding in each year. Potential common shares are not included in the calculation of diluted loss per share because their

effect is anti-dilutive.

Table of Contents

Stock-based Compensation

We grant both restricted stock awards and stock options to our key employees, directors and consultants. For the quarters ended March 31, 2012 and April 2, 2011, the weighted average fair value of options was estimated at the date of the grant using the Black-Scholes option-pricing model. The following are the significant weighted average assumptions used for estimating the fair value under our stock option plans:

	Three months ended	
	March 31, 2012	**April 2, 2011**
Expected life in years	4.0	4.0
Risk free interest rate	0.6%	1.52%
Expected volatility	100%	111%
Dividend yield	0%	0%

The expected life was based on the contractual term of the options and expected employee exercise behavior. Typically, options to our employees have a 2 to 4 year vesting term and a 10 year contractual term. The risk-free interest rate is based on U.S. Treasury zero-coupon issues with a remaining term equal to the expected option life assumed at the grant date. The future volatility is based on our 4 year historical volatility. We used an expected dividend yield of 0% because we have never paid a dividend and do not anticipate paying dividends. We assumed a 10% forfeiture rate based on our historical stock option cancellation rates over the last 4 years.

The stock-based compensation expense for our restricted stock awards is measured at fair value on the date of grant based on the number of shares expected to vest and the quoted market price of our common stock. We also assumed a 10% forfeiture rate for our restricted stock awards based on our historical cancellation rates over the last 4 years.

The following table presents details of total stock-based compensation expense that is included in each functional line item on our condensed consolidated statements of operations:

	Three months ended	
	March 31, 2012	**April 2, 2011**
Cost of Revenue	$ 5,000	$ 4,000
Research and development	101,000	114,000
Selling, general and administrative	215,000	277,000
Total stock-based compensation expense	$ 321,000	$ 395,000

Use of Estimates

The preparation of the condensed consolidated financial statements in conformity with generally accepted accounting principles requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. The significant estimates in the preparation of the financial statements relate to the assessment of the carrying amount of accounts receivable, inventory, fixed assets, intangibles, estimated provisions for warranty costs, contract revenues, income taxes and disclosures related to litigation. Actual results could differ from those estimates and such differences may be material to the condensed consolidated financial statements.

Fair Value of Financial Instruments

We have estimated the fair value amounts of our financial instruments using the available market information and valuation methodologies considered appropriate. We determined the book value of our cash and cash equivalents, accounts receivable, inventory, prepaid expenses and other current assets and other current liabilities as of March 31, 2012 approximate fair value.

Comprehensive Income

We have no items of other comprehensive income in any period and consequently have not included a Statement of Comprehensive Income.

9

Table of Contents

Segment Information

We operate in a single business segment, the research, development, manufacture and marketing of high performance products used in cellular base stations to maximize the performance of wireless telecommunications networks by improving the quality of uplink signals from mobile wireless devices. We currently derive net commercial product revenues primarily from the sales of our SuperLink, AmpLink and SuperPlex products. We currently sell most of our products directly to wireless network operators in the United States. Net revenues derived principally from government research and development contracts are presented separately on the condensed consolidated statement of operations for all periods presented.

Certain Risks and Uncertainties

Our long-term prospects are dependent upon the successful commercialization and market acceptance or our 2G HTS products.

We currently sell most of our products directly to wireless network operators in the United States and our product sales have historically been concentrated in a small number of customers. At March 31, 2012, we had two customers that represented 60% and 18% of total net revenues and 63% of accounts receivable. In 2011, these two customers represented 79% and 14% of total net revenues and 34% of accounts receivable. The loss of or reduction in sales, or the inability to collect outstanding accounts receivable, from any of these customers could have a material adverse effect on our business, financial condition, results of operations and cash flows.

We currently rely on a limited number of suppliers for key components of our products. The loss of any of these suppliers could have material adverse effect on our business, financial condition, results of operations and cash flows.

In connection with the sales of our commercial products, we indemnify, without limit or term, our customers against all claims, suits, demands, damages, liabilities, expenses, judgments, settlements and penalties arising from actual or alleged infringement or misappropriation of any intellectual property relating to our products or other claims arising from our products. We cannot reasonably develop an estimate of the maximum potential amount of payments that might be made under our indemnity obligations because of the uncertainty as to whether a claim might arise and how much it might total.

3. Short Term Borrowings

We had a line of credit with a bank. The agreement was structured as a sale of accounts receivable and provided for the sale of up to $3.0 million of eligible accounts receivable, with advances to us totaling 80% of the receivables sold. We had not used this line of credit for several years and therefore allowed it to expire without renewal on July 11, 2011.

4. Stockholders Equity

The following is a summary of stockholders equity transactions for the three months ended March 31, 2012:

	Convertible Preferred Stock		Common Stock		Capital in Excess of	Accumulated	
	Shares	Amount	Shares	Amount	Par Value	Deficit	Total
Balance at December 31, 2011	564,642	$ 1,000	33,362,281	$ 33,000	$ 262,157,000	$ (251,016,000)	$ 11,175,000
Issuance of common stock, net			6,808,591	7,000	6,615,000		6,622,000
Repurchase of common stock to satisfy tax withholding obligations			(89,996)		(129,000)		(129,000)
Issuance of awards and stock based compensation			187,500		321,000		321,000
Net loss						(2,988,000)	(2,988,000)
Balance at March 31, 2012	564,642	$ 1,000	40,268,376	$ 40,000	$ 268,964,000	$ (254,004,000)	$ 15,001,000

Equity Offering

In a registered direct offering completed in February 2012 we raised proceeds of $6.5 million, net of offering costs of $577,000, from the sale of 6,711,219 shares of common stock and warrants to purchase up to 5,033,414 shares of common stock. The securities were sold in multiples of a fixed combination consisting of one share of common stock and a warrant to purchase up to 0.75 of a share of common stock, at a price of $1.05, for an aggregate offering price of $7.1 million. Each warrant has an exercise price of $1.35 per share, for total potential additional proceeds to us of up to $6.8 million upon exercise of the warrants. The warrants are exercisable at any time but not prior to the six-month anniversary of the issuance of the warrants and have a five-year term. The warrants are exercisable by paying cash or, solely in the absence of an effective registration statement or prospectus, by cashless exercise for unregistered shares of common stock. The exercise price of the warrants is subject to standard antidilutive provision adjustment in the case of stock dividends or other distributions on shares of common stock or any other equity or equity equivalent securities payable in shares of common stock, stock splits, stock combinations, reclassifications or similar events affecting our common stock, and also, subject to limitations, upon any distribution of assets, including cash, stock or other property to our stockholders. The exercise price of the warrants is not subject to price-based anti-dilution adjustment.

Table of Contents

Prior to the February direct offering and commensurate with a previously announced plan, on various dates in January and February 2012, we raised $151,000, net of commission costs of $5,000, from at-the-market sales to or through Citadel Securities of 97,372 shares of our common stock at an average price of $1.60 per share.

Stock Options

At March 31, 2012, we had two equity award option plans, the 1999 Stock Option Plans and the 2003 Equity Incentive Plan (collectively, the Stock Option Plans), although we can only grant new options under the 2003 Equity Incentive Plan. Under the 2003 Equity Incentive Plan, stock awards may be made to our directors, key employees, consultants, and non-employee directors and may consist of stock options, stock appreciation rights, restricted stock awards, performance awards, and performance share awards. Stock options must be granted at prices no less than the market value on the date of grant. There were no stock option exercises during the three months ended March 31, 2012 or during the three months ended April 2, 2011.

The impact to the condensed consolidated statements of operations for the quarter ended March 31, 2012 on net loss was $154,000 and less than $0.01 on basic and diluted loss per common share and for the quarter ended April 2, 2011 the impact was $171,000 and $0.01 on basic and diluted loss per common share. No stock compensation cost was capitalized during either period. The total compensation cost related to nonvested awards not yet recognized was $926,000 and the weighted-average period over which the cost is expected to be recognized was 1.6 years at March 31, 2012.

The following is a summary of stock option transactions under our stock option plans at March 31, 2012:

	Number of Shares	Price Per Share	Weighted Average Exercise Price	Number of Options Exercisable	Weighted Average Exercise Price
Balance at December 31, 2011	1,376,513	$ 1.43 -$ 74.50	$ 4.44	735,701	$ 6.64
Granted	192,500	.82 - 1.46	1.44		
Exercised					
Canceled	(36,256)	1.75 - 66.40	8.77		
Balance at March 31, 2012	1,532,757	$ .82 - $74.50	$ 3.96	950,113	$ 5.27

The outstanding options expire on various dates through the end of March 2022. The weighted-average contractual term of options outstanding is 7.2 years and the weighted-average contractual term of stock options currently exercisable is 6.0 years. The exercise prices for these options range from $0.82 to $74.50 per share, for an aggregate exercise price of approximately $6.1 million. At March 31, 2012, no outstanding options had an exercise price less than the current market value.

Restricted Stock Awards

The grant date fair value of each share of our restricted stock awards is equal to the fair value of our common stock at the grant date. Shares of restricted stock under awards all have service conditions and vest over one to four years. Some of our grants also have performance conditions. The following is a summary of our restricted stock award transactions at March 31, 2012:

	Number of Shares	Weighted Average Grant Date Fair Value
Balance nonvested at December 31, 2011	641,813	$ 1.92
Granted	187,500	1.46
Vested	(213,586)	1.58
Forfeited		
Balance nonvested at March 31, 2012	615,727	$ 1.90

11

Table of Contents

For the majority of restricted stock awards granted, the number of shares issued on the date the restricted stock awards vest is net of the minimum statutory withholding requirements that we pay in cash to the appropriate taxing authorities on behalf of our employees. During the three months ended March 31, 2012 and April 2, 2011, we withheld 89,996 shares and 170,653 shares, respectively, to satisfy $129,000 and $278,000, respectively, of employees tax obligations.

The impact to the condensed consolidated statements of operations for the three months ended March 31, 2012 was $168,000 and less than $0.01 on basic and diluted loss per common share and for the quarter ended April 2, 2011 the impact was $224,000 and $0.01 on basic and diluted loss per common share. No stock compensation cost was capitalized during the period. The total compensation cost related to nonvested awards not yet recognized was $598,000 and the weighted-average period over which the cost is expected to be recognized was 9 months.

Warrants

The following is a summary of outstanding warrants at March 31, 2012:

	Total	Common Shares Currently Exercisable	Price per Share	Expiration Date
Warrants related to February 2012 financing	5,033,414	0	$ 1.35	February 22, 2017*

* The warrants are exercisable at any time but not prior to the six-month anniversary of the issuance of the warrants and have a five-year term. The warrants are exercisable by paying cash or, solely in the absence of an effective registration statement or prospectus, by cashless exercise for unregistered shares of common stock. The exercise price of the warrants is subject to standard antidilutive provision adjustment in the case of stock dividends or other distributions on shares of common stock or any other equity or equity equivalent securities payable in shares of common stock, stock splits, stock combinations, reclassifications or similar events affecting our common stock, and also, subject to limitations, upon any distribution of assets, including cash, stock or other property to our stockholders. The exercise price of the warrants is not subject to price-based anti-dilution adjustment.

We have determined that these 5,033,414 warrants related to issuance of common stock are subject to equity treatment because the warrant holder has no right to demand cash settlement and there are no unusual anti-dilution rights.

5. Earnings Per Share

Basic and diluted earnings (loss) per share is based on the weighted-average number of common shares outstanding.

Since their impact would be anti-dilutive, our loss per common share does not include the effect of the assumed exercise or vesting of the following shares:

	March 31, 2012	April 2, 2011
Outstanding stock options	1,532,757	1,700,028
Unvested restricted stock awards	615,727	864,043
Outstanding warrants	5,033,414	10,000
Total	7,181,898	2,574,071

Also, the preferred stock convertible into 5,646,420 shares of common stock was not included since its impact would be anti-dilutive.

6. Commitments and Contingencies

Operating Leases

We lease our offices and production facilities under non-cancelable operating leases that expire in November 2016 and April 2017. The leases contain escalation clauses for increases in annual renewal options and require us to pay utilities, insurance, taxes and other operating expenses. Commencing January 1, 2012 and expiring in November 2016 we sublet 26,000 square feet of our Santa Barbara facility and leased 35,000 square foot facility in Austin, Texas that expires in April 2017.

For the three months ended March 31, 2012 and April 2, 2011, rent expense was $309,000 and $277,000, respectively.

Table of Contents

Patents and Licenses

We have entered into various licensing agreements requiring royalty payments ranging from 0.13% to 2.5% of specified product sales. Certain of these agreements contain provisions for the payment of guaranteed or minimum royalty amounts. In the event that we fail to pay minimum annual royalties, these licenses may automatically become non-exclusive or be terminated. These royalty obligations terminate at various times from 2012 to 2020. For the three months ended March 31, 2012 and April 2, 2011, royalty expense totaled $6,000 and $43,000, respectively. Under the terms of certain royalty agreements, royalty payments made may be subject to audit. There have been no audits to date and we do not expect future audit adjustments to be significant.

The minimum lease payments under operating leases and license obligations are as follows:

Years ending December 31,	Licenses	Operating Leases
Remainder of 2012	$ 25,000	$ 1,185,000
2013	25,000	1,594,000
2014	30,000	1,644,000
2015	45,000	1,695,000
2016	45,000	1,621,000
Thereafter	90,000	67,000
Total payments	$ 260,000	$ 7,806,000

7. Contractual Guarantees and Indemnities

During our normal course of business, we make certain contractual guarantees and indemnities pursuant to which we may be required to make future payments under specific circumstances. We have not recorded any liability for these contractual guarantees and indemnities in the accompanying condensed consolidated financial statements.

Warranties

We establish reserves for future product warranty costs that are expected to be incurred pursuant to specific warranty provisions with our customers. Our warranty reserves are established at the time of sale and updated throughout the warranty period based upon numerous factors including historical warranty return rates and expenses over various warranty periods.

Intellectual Property Indemnities

We indemnify certain customers and our contract manufacturers against liability arising from third-party claims of intellectual property rights infringement related to our products. These indemnities appear in development and supply agreements with our customers as well as manufacturing service agreements with our contract manufacturers, are not limited in amount or duration and generally survive the expiration of the contract. Given that the amount of potential liabilities related to such indemnities cannot be determined until an infringement claim has been made, we are unable to determine the maximum amount of losses that we could incur related to such indemnities.

Director and Officer Indemnities and Contractual Guarantees

We have entered into indemnification agreements with our directors and executive officers which require us to indemnify such individuals to the fullest extent permitted by Delaware law. Our indemnification obligations under such agreements are not limited in amount or duration. Certain costs incurred in connection with such indemnities may be recovered under certain circumstances under various insurance policies. Given that the amount of any potential liabilities related to such indemnities cannot be determined until a lawsuit has been filed against a director or executive officer, we are unable to determine the maximum amount of losses that we could incur relating to such indemnities. Historically, any amounts payable pursuant to such director and officer indemnities have not had a material negative effect on our business, financial condition or results of operations.

We have also entered into severance and change in control agreements with certain of our executives. These agreements provide for the payment of specific compensation benefits to such executives upon the termination of their employment with us.

General Contractual Indemnities/Products Liability

During the normal course of business, we enter into contracts with customers where we agree to indemnify the other party for personal injury or property damage caused by our products. Our indemnification obligations under such agreements are not generally limited in amount or duration. Given that the amount of any potential liabilities related to such indemnities cannot be determined until a lawsuit has been filed, we are unable to determine the maximum amount of losses that we could incur relating to such indemnities. Historically, any amounts payable pursuant to such indemnities have not had a material negative effect our business, financial condition or results of operations. We maintain general and product liability insurance as well as errors and omissions insurance which may provide a source of recovery to us in the event of an indemnification claim.

Table of Contents

8. Details of Certain Financial Statement Components and Supplemental Disclosures of Cash Flow Information and Non-Cash Activities

Balance Sheet Data:

	March 31, 2012	December 31, 2011
Accounts receivable:		
Accounts receivable-trade	$ 95,000	$ 15,000
U.S. government accounts receivable-billed	88,000	48,000
Less: allowance for doubtful accounts	(2,000)	(2,000)
	$ 181,000	**$ 61,000**

	March 31, 2012	December 31, 2011
Inventories:		
Raw materials	$ 1,197,000	$ 1,169,000
Work-in-process	336,000	338,000
Finished goods	1,658,000	1,887,000
Less inventory reserve	(1,835,000)	(1,785,000)
	$ 1,356,000	**$ 1,609,000**

	March 31, 2012	December 31, 2011
Property and Equipment:		
Equipment	$ 17,077,000	$ 15,557,000
Leasehold improvements	6,675,000	6,675,000
Furniture and fixtures	387,000	387,000
	24,139,000	22,619,000
Less: accumulated depreciation and amortization	(19,442,000)	(19,748,000)
	$ 4,697,000	**$ 2,871,000**

Depreciation expense amounted to $34,000 and $182,000 for the three month periods ended March 31, 2012 and April 2, 2011, respectively.

	March 31, 2012	December 31, 2011
Patents and Licenses:		
Patents pending	$ 580,000	$ 522,000
Patents issued	1,468,000	1,523,000
Less accumulated amortization	(655,000)	(636,000)
Net patents issued	813,000	887,000
Purchase technology	1,706,000	1,706,000

Less accumulated Amortization	(1,706,000)	(1,706,000)
Net purchase technology		
	$ 1,393,000	**$ 1,409,000**

Amortization expense related to these items totaled $30,000 and $29,000, for the three month periods ended March 31, 2012 and April 2, 2011, respectively. Amortization expenses are expected to total $66,000 for the remainder of 2012 and $89,000 in of 2013 and $86,000 for 2014.

Table of Contents

	March 31, 2012	December 31, 2011
Accrued Expenses and Other Long Term Liabilities:		
Salaries Payable	$ 132,000	$ 68,000
Compensated Absences	278,000	272,000
Compensation related	82,000	20,000
Warranty reserve	177,000	225,000
Deferred rent	466,000	422,000
Other	171,000	233,000
	1,306,000	**1,240,000**
Less current portion	**(713,000)**	**(612,000)**
Long term portion	**$ 593,000**	**$ 628,000**

	For the three months ended, March 31, 2012	April 2, 2011
Warranty Reserve Activity:		
Beginning balance	$ 225,000	$ 289,000
Additions	5,000	13,000
Deductions	(53,000)	(3,000)
Ending balance	$ 177,000	$ 299,000

9. Subsequent Events

We evaluated subsequent events through the date the accompanying condensed consolidated financial statements were issued. Pursuant to the requirements of ASC 855, *Subsequent Events*, we have included all accounting and disclosure requirements related to subsequent events in our condensed consolidated financial statements.

Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

General

We are a leading company in developing and commercializing high temperature superconductor (HTS) materials and related technologies. Superconductivity is the unique ability to conduct various signals or energy (e.g., electrical current or radio frequency (RF) signals) with little or no resistance when cooled to critical temperatures. HTS materials are a family of elements that demonstrate superconducting properties at temperatures significantly warmer than previous superconducting materials. Electric currents that flow through conventional conductors encounter resistance that requires power to overcome and generates heat. HTS materials can substantially improve the performance characteristics of electrical systems, reducing power loss, lowering heat generation, and decreasing electrical noise.

Commercialization

Our development efforts over the last 25 years have yielded an extensive patent portfolio as well as critical trade secrets, unpatented technology and proprietary knowledge. We have commercialized wireless products using our proprietary technology and are currently focusing our efforts on this technology in superconducting power applications, RF filters and cryocoolers.

Wireless Networks. Our current commercial products help maximize the performance of wireless telecommunications networks by improving the quality of uplink signals from mobile wireless devices. Our products increase capacity utilization, lower dropped and blocked calls, extend coverage, and enable higher wireless data throughput all while reducing capital and operating costs.

Superconducting Power Applications. We are adapting our unique HTS materials deposition techniques to deliver energy efficient, cost-effective and high performance 2G HTS wire technology for next generation power applications. We have identified several large initial target markets for our 2G HTS wire including energy (wind turbines, smart grid) and industrial (motors, generators) applications. To accelerate development and manufacturing processes for our 2G HTS wire, we are partnering with HTS industry leaders and the United States National Labs. In July 2011, we renewed our three year Cooperative Research and Development Agreement with Los Alamos National Laboratory. These technological interchanges will help us meet the technical challenges and performance metrics for both high performance and cost effective 2G HTS wire.

Table of Contents

RF Filters. Our RF filter structures resemble a circuit on a semiconductor using a circuit that is etched into HTS materials that are deposited on a wafer. Our unique and innovative circuits allow us to utilize the characteristics of the HTS materials for this application, and we have developed unique tuning methods that allow us to produce a frequency specific filter. We are also leveraging our unique technology to design advanced reconfigurable filters, which have the potential to drastically reduce the size and cost of mobile devices.

Cryocoolers. We developed a unique cryocooler that can efficiently and reliably cool HTS circuits to the critical temperature (77 degrees Kelvin), and as a result, our wireless products are maintenance free and reliable enough to be deployed for many years.

Our development efforts can take a significant number of years to commercialize, and we must overcome significant technical barriers and deal with other significant risks.

Our Wireless Business

Our current revenue comes from the design, manufacture, and sale of high performance infrastructure products for wireless communication applications. We have three current product lines all of which relate to wireless base stations:

SuperLink®, a highly compact and reliable receiver front-end HTS wireless filter system to eliminate out-of-band interference for wireless base stations, combining filters with a proprietary cryogenic cooler and a cooled low-noise amplifier;

AmpLink®, a ground-mounted unit for wireless base stations that includes a high-performance amplifier and up to six dual duplexers; and

SuperPlex, a high-performance multiplexer that provides extremely low insertion loss and excellent cross-band isolation designed to eliminate the need for additional base station antennas and reduce infrastructure costs.

We sell most of our current commercial products to a small number of wireless carriers in the United States, including AT&T and Verizon Wireless. Verizon Wireless and AT&T each accounted for more than 10% of our commercial revenues in each of the last three years. Demand for wireless communications equipment fluctuates dramatically and unpredictably and recently has been trending downward. The wireless communications infrastructure equipment market is extremely competitive and is characterized by rapid technological change, new product development, product obsolescence, evolving industry standards and price erosion over the life of a product. We expect these trends to continue and may cause significant fluctuations in our quarterly and annual revenues.

Our Strategic Initiatives

In addition to our ongoing sale of products for wireless applications described above, we have created several unique capabilities and an HTS manufacturing system related to a new HTS wire platform, RF filters and cryocoolers that we are seeking to commercially deploy by leveraging our leadership in superconducting technologies, extensive intellectual property, and HTS manufacturing expertise.

HTS Wire Platform

Our 2G HTS wire product development is focused on large markets where the advantages of HTS wire are recognized by the industry. Our initial product roadmap targets three important applications: superconducting high power transmission cable, superconducting fault current limiters (SFCL) and superconducting rotating machines such as motors and generators.

Superconducting High Power Transmission Cable:

Superconducting high power transmission and distribution cable transmit 5 to 10 times the electrical current of traditional copper or aluminum cables with significantly improved efficiency. HTS power cable systems consist of the cable, which is comprised of hundreds of strands of HTS wire wrapped around a copper core, and the cryogenic cooling system to maintain proper operating conditions. HTS superconducting cables offer solutions for utilities facing challenges that include: substation footprint availability, lack of available rights of way, and high load connections between substations. HTS power cables are particularly suited to high load areas such as the dense urban business districts of large

cities, where purchases of easements and construction costs for traditional low capacity cables may be cost prohibitive.

Table of Contents

Superconducting Fault Current Limiter (SFCL):

With power demand on the rise and new power generation sources being added, the grid has become overcrowded and vulnerable to catastrophic faults. Faults are abnormal flows of electrical current like a short circuit. As the grid is stressed, faults and power blackouts increase in frequency and severity. SFCLs act like powerful surge protectors, preventing harmful faults from taking down substation equipment by reducing the fault current to a safer level (20 50% reduction) so that the existing switchgear can still protect the grid. SFCLs protect against damaging fault currents and blackouts while enhancing system safety, stability, and efficiency. A critical benefit for new build outs is the improved system reliability when renewables, like solar and wind, are added. When compared to a complete substation upgrade, SFCLs are a significantly lower capital investment.

Superconducting Rotating Machines Motors and Generators:

Superconducting motors, generators, turbines and other rotating machines are expected to generate large future demand for 2G HTS wire. Coils utilizing HTS wire will enable electric motors and generators to operate at much higher power densities. When compared to a copper wire based electric machine with equivalent output power, future superconducting motors and generators will enable a significant size reductions for the motors with higher efficiency. One potential application for high-powered HTS generators is expected to be 10+ megawatt offshore wind turbines. Offshore superconducting wind turbines promise to capture clean energy at a lower cost than competing renewables, while delivering power directly to growing coastal cities. Offshore superconducting wind turbines are a long-term initiative for HTS technologies. Wind energy is taking shape as a critical world resource for electric power. Today, wind energy is primarily land based. The expected future trend is to exploit a largely untapped supply of offshore wind energy. However, it will take time to build enough infrastructure for offshore wind power to significantly contribute to the power grid. Superconducting wind turbines are expected to play a unique role offshore since conventional technology cannot achieve the necessary power per tower . The increase in power density provided by superconducting turbines significantly reduces generator weight and maximizes power per tower, turning wind power into an economically viable alternative. Size reduction translates directly to cost savings by greatly reducing the amount of magnetic steel and structural steel required. Superior 2G HTS wire power handling performance at a lower cost will enable superconducting wire to replace incumbent and competing technologies.

RF Filters

Conventional RF filters are fabricated primarily from aluminum blocks with hollow cavities, resonators, and tuning elements incorporated to make a frequency specific filter. Our filter structures resemble a circuit on a semiconductor using a circuit that is etched into HTS materials that are deposited on a wafer. Our unique and innovative circuits allow us to utilize the characteristics of the HTS materials for this application. We have also developed unique tuning methods that allow us to produce a frequency specific filter.

In February 2012 our newly formed subsidiary, Resonant Inc., entered into an agreement to develop its innovative Reconfigurable Resonance (RcR) technology in the rapidly growing mobile communications products industry. Resonant will require financing in order to commence active development, and STI is currently exploring financing options. While there is no assurance as to whether Resonant will obtain the necessary financing.

Cryocoolers

HTS circuits need to be cooled to the critical temperature that enables the superconducting properties of the materials to be utilized. To meet this need, we developed a unique cryocooler that can efficiently and reliably cool the circuit to the critical temperature (77 degrees Kelvin). As a result, our wireless products are maintenance free and reliable enough to be deployed for many years.

Results of Operations

Quarter Ended March 31, 2012 compared to the Quarter Ended April 2, 2011

Net revenues decreased by $1.2 million, or 75%, to $0.4 million in the first quarter of 2012 from $1.6 million in the first quarter of 2011. Net revenues consist primarily of commercial product revenues and government contract revenues.

Net commercial product revenues decreased by $1.3 million, or 79%, to $0.3 million in the first quarter of 2012 from $1.6 million in the first quarter of 2011. The decrease is the result of lower sales volume for all of our products. We sell our SuperLink and other performance enhancement products to large North American wireless operators. As our customers continue to invest in 4G networks, spending on 3G data networks, where our products are deployed, has become a secondary priority. This market dynamic has impacted and we believe will continue to impact our commercial revenue. Sales prices for our products were essentially unchanged. Our three largest customers accounted for 98% and

99%, respectively, of our total net commercial product revenues in the first quarter of both 2012 and 2011. These customers generally purchase products through non-binding commitments with minimal lead-times. We also continue to experience challenges to revenue growth in the commercial wireless market. Consequently, our commercial product revenues can fluctuate dramatically from quarter to quarter based on changes in our customers capital spending patterns, and revenues may continue to be impacted by such challenges.

Table of Contents

Government contract and other revenues increased by $38,000 from $17,000 in the first quarter of 2011 to $55,000 in the first quarter of 2012. This increase is attributable to the addition of a minor contract in 2012 and our current use of our relatively fixed engineering resources for research and development.

Cost of commercial product revenues includes all direct costs, manufacturing overhead and provision for excess and obsolete inventories. The cost of commercial product revenues decreased to $844,000 in the first quarter of 2012 compared to $1,669,000 for the first quarter of 2012, a decrease of $825,000 or 49%. The lower costs resulted principally from lower production as a result of lower sales. We had additional expense provisions for obsolete inventories of $92,000 and $90,000, respectively, in the first quarter of 2012 and 2011.

Our cost of commercial sales includes both variable and fixed cost components. The variable component consists primarily of materials, assembly and test labor, overhead, which includes equipment and facility depreciation, transportation costs and warranty costs. The fixed component includes test equipment and facility depreciation, purchasing and procurement expenses and quality assurance costs. Given the fixed nature of such costs, the absorption of our production overhead costs into inventory decreases and the amount of production overhead variances expensed to cost of sales increases as production volumes decline since we have fewer units to absorb our overhead costs against. Conversely, the absorption of our production overhead costs into inventory increases and the amount of production overhead variances expensed to cost of sales decreases as production volumes increase since we have more units to absorb our overhead costs against. As a result, our gross profit margins generally decrease as revenue and production volumes decline due to lower sales volume and higher amounts of production overhead variances expensed to cost of sales; and our gross profit margins generally increase as our revenue and production volumes increase due to higher sales volume and lower amounts of production overhead variances expensed to cost of sales.

The following is an analysis of our commercial product gross profit and margins:

	For the quarters ended			
	March 31, 2012		April 2, 2011	
	(Dollars in thousands)			
Net commercial product sales	$ 344	100.0%	$ 1,603	100.0%
Total cost of commercial product sales	844	245.3%	1,669	104.1%
Gross loss	$ (500)	(145.3%)	$ (66)	(4.1%)

We had a gross loss of $500,000 in the first quarter of 2012 from the sale of our commercial products compared to a gross loss of $66,000 in the first quarter of 2011. We experienced a gross loss in the first quarter of 2012, and to a lesser extent in 2011, because the level of commercial sales was insufficient to cover our fixed manufacturing overhead costs. We regularly review inventory quantities on hand and provide an allowance for excess and obsolete inventory based on numerous factors including sales backlog, historical inventory usage, forecasted product demand and production requirements for the next twelve months. Gross margin in the first quarter of 2012 and 2011 was not impacted by the sale of previously written-off inventory.

Cost of government and other contract revenues totaled $52,000 in the first quarter of 2012 compared to $15,000 in the first quarter of 2011. Because these contracts are generally priced on a cost plus basis, increases in revenue generally result in increases in associated costs. As a percentage of government and other contract revenues, these costs were 95% and 88%, respectively, in the first quarter of 2012 and 2011.

Research and development expenses relate principally to development of new products, including our wireless commercial products, HTS wire products and our other products. Total expenses totaled $1.2 million in the first quarter of 2012 compared to $2.0 million in the same quarter of 2011. In April 2011 we decided to use certain of our own technologies and as a result we voluntarily terminated a patent license we had with a third party along with certain other intangible assets. As a result, capitalized cost of $0.8 million was expensed during the first quarter of 2011.

Excluding the 2011 capitalized patent license expense, our research and development expenses are relatively unchanged from 2011 to 2012, while we have redirected our efforts. We have expanded our HTS wire research and development expense and reduced our expense to both expand our wireless product line and improve the manufacturability of our wireless products.

Selling, general and administrative expenses totaled $1.3 million in the first quarter of 2012, compared to $1.7 million in the first quarter of 2011. The reduction was primarily from lower sales expenses.

Interest income was $2,000 in both the first quarter of 2012 and the first quarter 2011.

18

Table of Contents

There was no interest expense in the first quarter of 2012. Interest expense of $7,000 for the first quarter of 2011 was the result of our line of credit with a bank.

We had a net loss of $3.0 million for the quarter ended March 31, 2012, compared to a net loss of $3.7 million in the first quarter of 2011.

The net loss available to common stockholders totaled $0.08 per common share in the first quarter of 2012, compared to a net loss of $0.12 per common share in the first quarter of 2011.

Liquidity and Capital Resources

Cash Flow Analysis

As of March 31, 2012, we had working capital of $9.1 million, including $9.5 million in cash and cash equivalents, compared to working capital of $7.2 million at December 31, 2011, which included $6.2 million in cash and cash equivalents. We currently invest our excess cash in short-term, investment-grade, money-market instruments with maturities of three months or less.

Cash and cash equivalents increased by $3.3 million from $6.2 million at December 31, 2011 to $9.5 million at March 31, 2012. Cash was provided by financing activities offset principally by uses in operations and for purchase property and equipment.

Cash used in operations totaled $2.2 million in the first quarter of 2012. We used $2.5 million to fund the cash portion of our net loss. We also used cash to fund a $0.1 million increase in accounts receivable, offset by cash provided by a $0.4 million decrease in inventory, prepaid expenses and other assets, patents and licenses, as well as an increase in accounts payable and accrued expenses.

Net cash used in investing activities totaled $951,000 in the first quarter of 2012. Purchases of equipment for our HTS wire initiative were $966,000 and $15,000 was provided by equipment sales. In the first quarter of 2011 there were no equipment sales and only $35,000 was used to purchase property and equipment.

We used $129,000 and $278,000, respectively, in financing activities in the first quarter of 2012 and 2011 to repurchase common shares from our employees to satisfy tax withholding obligations that arose upon the vesting of restricted stock awards.

Financing Activities

We have historically financed our operations through a combination of cash on hand, cash provided from operations, equipment lease financings, available borrowings under bank lines of credit and both private and public equity offerings.

Net cash provided by financing activities in the first quarter of 2012 totaled $6.6 million, net of $582,000 in expenses. The financing was from two activities: the registered direct sale of 6,711,219 shares of common stock at $1.05 per share in February 2012 and at-the-market sales to or through Citadel Securities of 97,372 shares of common stock at an average price of $1.60 per share in January and early February 2012. During the quarter we also used $129,000 to repurchase common shares from our employees to satisfy withholding taxes due upon the vesting of their restricted stock awards.

Contractual Obligations and Commercial Commitments

We have not had any material changes outside of the ordinary course of business in our contractual obligations as disclosed in our Annual Report on Form 10-K for 2011.

Capital Expenditures

We plan to invest approximately $3.0 million in fixed assets during the remainder of 2012. This $3.0 million and the $1.0 million already spent in the first quarter of 2012 are for the purchase of equipment and facilities improvements for our HTS wire initiative. There have been no fixed asset expenditures in the first quarter, and we do not plan any additional fixed asset expenditures in 2012 for our existing wireless business.

Future Liquidity

For the quarter ended March 31, 2012, we incurred a net loss of $3.0 million and had negative cash flows from operations of $2.2 million. In the full 2011 year, we incurred a net loss of $13.4 million and had negative cash flows from operations of $10.0 million. Our independent registered public accounting firm has included in its audit reports for 2011 and 2010 an explanatory paragraph expressing doubt about our ability to continue as a going concern.

Table of Contents

At March 31, 2012, we had $9.5 million in cash and cash equivalents. We believe our current cash resources will not be sufficient to fund our business for the next twelve months. We believe the key factors to our liquidity will be our ability to successfully use our expertise and our technology to generate revenues in various ways, including commercial operations, government contracts, joint ventures and licenses and we plan to leverage our leadership in superconducting technologies, extensive intellectual property, and HTS manufacturing expertise to develop and produce HTS wire. Because of the uncertainty of these factors, we will need to raise funds to meet our working capital needs. If we require additional financing, we cannot assure you that additional financing will be available on acceptable terms or at all. If we issue additional equity securities to raise funds, the ownership percentage of our existing stockholders would be reduced. New investors may demand rights, preferences or privileges senior to those of existing holders of common stock. If we cannot raise any needed funds, we might be forced to make further substantial reductions in our operating expenses, which could adversely affect our ability to implement our current business plan and ultimately our viability as a company.

Net Operating Loss Carryforward

As of December 31, 2011, we had net operating loss carryforwards for federal and state income tax purposes of approximately $308.4 million and $181.5 million, respectively, which expire in the years 2012 through 2031. However, during 2011 we concluded that under the Internal Revenue Code change of control limitations, a maximum of $94.4 million and $70.2 million, respectively, would be available for reduction of taxable income and reduced both the deferred tax asset and valuation allowance accordingly. Due to the uncertainty surrounding their realization, we recorded a full valuation allowance against our net deferred tax assets. Accordingly, no deferred tax asset has been recorded in the accompanying balance sheets.

Critical Accounting Policies and Estimates

Our discussion and analysis of our historical financial condition and results of operations are based upon our condensed consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these condensed consolidated financial statements in conformity with those principles requires us to make estimates of certain items and judgments as to certain future events including for example those related to bad debts, inventories, recovery of long-lived assets (including intangible assets), income taxes, warranty obligations, and contingencies. These determinations, even though inherently subjective and subject to change, affect the reported amounts of our assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. While we believe that our estimates are based on reasonable assumptions and judgments at the time they are made, some of our assumptions, estimates and judgments will inevitably prove to be incorrect. As a result, actual outcomes will likely differ from our accruals, and those differences positive or negative could be material. Some of our accruals are subject to adjustment, as we believe appropriate, based on revised estimates and reconciliation to the actual results when available.

In addition, we identified certain critical accounting policies which affect certain of our more significant estimates and assumptions used in preparing our consolidated financial statements in our Annual Report on Form 10-K for 2011. We have not made any material changes to these policies.

Backlog

Our commercial backlog consists of accepted product purchase orders with scheduled delivery dates during the next twelve months. We had commercial backlog of $152,000 at March 31, 2012, compared to $13,000 at December 31, 2011.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

We do not believe that there was a material change in our exposure to market risk at March 31, 2012 compared with our market risk exposure on December 31, 2011. See *Management s Discussion and Analysis of Financial Condition and Results of Operations Market Risk* in our Annual Report on Form 10-K for 2011.

Item 4. Controls and Procedures.

We have established disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended). As of the end of the period covered by this report we carried out an evaluation under the supervision and with the participation of our management, including the our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Rule 13a-15 of the Securities and Exchange Act of 1934, as amended. Based

upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective.

There were no changes in our internal controls over financial reporting during the quarter ended March 31, 2012 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Table of Contents

We do not expect that our disclosure controls and procedures or our internal controls will prevent all error and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, have been detected.

PART II

OTHER INFORMATION

Item 1. Legal Proceedings.
From time to time, we are party to various lawsuits, claims and other legal proceedings that arise in the ordinary course of our business. Excluding ordinary, routine litigation incidental to our business, we are not currently a party to any legal proceedings that we believe would reasonably be expected to have a material adverse effect on our business, financial condition or results of operation or cash flow.

Item 1A. Risk Factors.
A description of the risk factors associated with our business is contained in Item 1A, Risk Factors, of our Annual Report on Form 10-K for 2011 filed with the Securities and Exchange Commission on March 30, 2012. We are not aware of any material changes to those risk factors.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.
The following table summarizes repurchases of our stock in the quarter ended March 31, 2012:

Period	Total Number of Shares Purchased	Average Price Paid Per Share
January 1-28, 2012	89,996(1)	$ 1.43
January 29-February 25, 2012		
February 26-March 31, 2012		
Total	89,996	$ 1.43

(1) Shares surrendered to us by employees to satisfy tax withholding obligations that arose upon the vesting of restricted stock awards. These repurchases were not made pursuant to publicly announced plans or programs.

Item 3. Defaults Upon Senior Securities.
None.

Item 4. Mine Safety Disclosures.
None.

Item 5. Other Information.
None.

Item 6. Exhibits.

Number	Description of Document
31.1	Statement of CEO Pursuant to 302 of the Sarbanes-Oxley Act of 2002*
31.2	Statement of CFO Pursuant to 302 of the Sarbanes-Oxley Act of 2002*
32.1	Statement of CEO Pursuant to 906 of the Sarbanes-Oxley Act of 2002*
32.2	Statement of CFO Pursuant to 906 of the Sarbanes-Oxley Act of 2002*

* Filed herewith.

Table of Contents

SIGNATURES

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

SUPERCONDUCTOR TECHNOLOGIES INC.

Dated: May 9, 2012

/s/ William J. Buchanan
William J. Buchanan
Chief Financial Officer

/s/ Jeffrey A. Quiram
Jeffrey A. Quiram
President and Chief Executive Officer