

SUPERCONDUCTOR TECHNOLOGIES INC
Form 10-Q
May 13, 2016
Table of Contents

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended April 2, 2016

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
(State or other jurisdiction of
incorporation or organization)

77-0158076
(IRS Employer
Identification No.)

9101 Wall Street, Suite 1300, Austin, Texas 78754
(Address of principal executive offices & zip code)

(512) 334-8900
(Registrant's telephone number including area code)

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

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

Indicate by check mark whether the registrant is a 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

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

We had 40,748,218 shares of our common stock outstanding as of the close of business on May 6, 2016.

Table of Contents

SUPERCONDUCTOR TECHNOLOGIES INC.

INDEX TO FORM 10-Q

Three Months Ended April 2, 2016

<u>SPECIAL NOTE REGARDING FORWARD LOOKING STATEMENTS</u>	1
<u>PART I - FINANCIAL INFORMATION</u>	
ITEM 1. <u>Financial Statements (unaudited)</u>	
<u>Condensed Consolidated Statements of Operations</u>	2
<u>Condensed Consolidated Balance Sheets</u>	3
<u>Condensed Consolidated Statements of Cash Flows</u>	4
<u>Notes to Unaudited Interim Condensed Consolidated Financial Statements</u>	5
<u>Management's Discussion and Analysis of Financial Condition and Results of</u>	
<u>Operations</u>	15
ITEM 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	20
ITEM 4. <u>Controls and Procedures</u>	20
<u>PART II - OTHER INFORMATION</u>	
ITEM 1. <u>Legal Proceedings</u>	20
ITEM 1A. <u>Risk Factors</u>	20
ITEM 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	21
ITEM 3. <u>Defaults Upon Senior Securities</u>	21
ITEM 4. <u>Mine Safety Disclosures</u>	21
ITEM 5. <u>Other Information</u>	21
ITEM 6. <u>Exhibits</u>	21
<u>SIGNATURES</u>	22

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:

our limited cash and a history of losses;

our need to materially grow our revenues from commercial operations and/or to raise additional capital (which financing may not be available on acceptable terms or at all) over the next 12-months to implement our current business plan and maintain our viability;

the performance and use of our equipment to produce wire in accordance with our timetable;

overcoming technical challenges in attaining milestones to develop and manufacture commercial lengths of our high temperature superconducting (HTS) wire;

the possibility of delays in customer evaluation and acceptance of our HTS wire;

the limited number of potential customers and customer pressures on the selling prices of our products;

the limited number of suppliers for some of our components and our HTS wire;

there being no significant backlog from quarter to quarter;

our market being characterized by rapidly advancing technology;

the impact of competitive products, technologies and pricing;

manufacturing capacity constraints and difficulties;

the impact of any financing activity on the level of our stock price;

the dilutive impact of any issuances of securities to raise capital;

cost and uncertainty from compliance with environmental regulations;

local, regional, and national and international economic conditions and events, and the impact they may have on us and our customers; and

if we fail to maintain the listing of our common stock with a U.S. national securities exchange, the liquidity of our common stock could be adversely affected.

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 2015.

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	
	April 2, 2016	March 28, 2015
Net revenues	\$ 89,000	\$ 55,000
Costs and expenses:		
Cost of revenues	864,000	755,000
Research and development	716,000	1,457,000
Selling, general and administrative	1,163,000	1,528,000
Total costs and expenses	2,743,000	3,740,000
Loss from operations	(2,654,000)	(3,685,000)
Other Income and Expense:		
Adjustments to fair value of warrant derivatives	21,000	2,633,000
Adjustments to warrant exercise price		(367,000)
Other income	3,000	1,000
Net loss	\$ (2,630,000)	\$ (1,418,000)
Basic and diluted net loss per common share	\$ (0.07)	\$ (0.10)
Basic and diluted weighted average number of common shares outstanding	39,402,361	13,712,906

See accompanying notes to the unaudited condensed consolidated financial statements.

Table of Contents

SUPERCONDUCTOR TECHNOLOGIES INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

	April 2, 2016 (Unaudited)	December 31, 2015 (See Note)
<u>ASSETS</u>		
Current Assets:		
Cash and cash equivalents	\$ 5,574,000	\$ 7,469,000
Accounts receivable, net	70,000	38,000
Inventories, net	78,000	121,000
Prepaid expenses and other current assets	183,000	122,000
Total Current Assets	5,905,000	7,750,000
Property and equipment, net of accumulated depreciation of \$7,851,000 and \$7,290,000, respectively	4,990,000	5,551,000
Patents, licenses and purchased technology, net of accumulated amortization of \$888,000 and \$869,000, respectively	969,000	938,000
Other assets		126,000
Total Assets	\$ 11,864,000	\$ 14,365,000
<u>LIABILITIES AND STOCKHOLDERS EQUITY</u>		
Current Liabilities:		
Accounts payable	\$ 329,000	\$ 432,000
Accrued expenses	551,000	418,000
Total Current Liabilities	880,000	850,000
Other long term liabilities	231,000	393,000
Total Liabilities	1,111,000	1,243,000
Commitments and Contingencies (Notes 5 and 6)		
Stockholders Equity:		
Preferred stock, \$.001 par value, 2,000,000 shares authorized, 330,474 and 330,873 shares issued and outstanding, respectively		
Common stock, \$.001 par value, 250,000,000 shares authorized, 40,748,218 and 39,608,218 shares issued and outstanding, respectively	40,000	39,000
Capital in excess of par value	304,313,000	304,053,000
Accumulated deficit	(293,600,000)	(290,970,000)
Total Stockholders Equity	10,753,000	13,122,000

Total Liabilities and Stockholders' Equity	\$ 11,864,000	\$ 14,365,000
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See accompanying notes to the unaudited condensed consolidated financial statements.

Note December 31, 2015 balances were derived from audited financial statements.

Table of Contents**SUPERCONDUCTOR TECHNOLOGIES INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(Unaudited)

	Three Months Ended	
	April 2, 2016	March 28, 2015
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	\$ (2,630,000)	\$ (1,418,000)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	580,000	727,000
Stock-based compensation expense	261,000	552,000
Adjustments to fair value of warrant derivatives	21,000	(2,633,000)
Adjustments to warrant exercise price		367,000
Provision for excess or obsolete inventory		58,000
Gain on disposal of property and equipment		(1,000)
Changes in assets and liabilities:		
Accounts receivable	(32,000)	50,000
Inventories	(43,000)	16,000
Prepaid expenses and other current assets	(61,000)	100,000
Patents and licenses	(50,000)	(6,000)
Other assets	126,000	32,000
Accounts payable, accrued expenses and other current liabilities	(67,000)	(62,000)
Net cash used in operating activities	(1,895,000)	(2,218,000)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment		(46,000)
Net proceeds from the sale of property and equipment		1,000
Net cash used in investing activities		(45,000)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net proceeds from the sale of common stock		4,596,000
Net proceeds from the exercise of outstanding warrants		1,687,000
Net cash provided by financing activities		6,283,000
Net increase (decrease) in cash and cash equivalents	(1,895,000)	4,020,000
Cash and cash equivalents at beginning of period	7,469,000	1,238,000
Cash and cash equivalents at end of period	\$ 5,574,000	\$ 5,258,000

Supplemental non-cash financing disclosure:

Warrant liability converted to capital in excess of par	\$	669,000
See accompanying notes to the unaudited condensed consolidated financial statements.		

Table of Contents

SUPERCONDUCTOR TECHNOLOGIES INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. General

Superconductor Technologies Inc. (together with our subsidiaries, we or us) was incorporated in Delaware on May 11, 1987. We develop and produce high temperature superconducting (HTS) materials and associated technologies. We have generated more than 100 patents as well as proprietary trade secrets and manufacturing expertise. We are now leveraging our key enabling technologies in HTS materials and cryogenics, to pursue emerging opportunities in the electrical grid and in equipment platforms that utilize electrical circuits. In January 2012, we took possession of a facility in Austin, Texas and have moved our HTS wire processes and our research and development to Austin. We continue to maintain a presence in Santa Barbara, California for certain business operations and our legacy wireless business.

Our initial superconducting products were completed in 1998, and we began delivery to a number of wireless network providers. In the following 13 years, 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 the production of our HTS Conductus® wire for next generation power applications. While most of our current commercial product revenues come from the sale of our legacy high performance wireless communications infrastructure products, production of our Conductus wire is our principal opportunity to grow our future revenue.

The unaudited condensed consolidated financial information furnished herein has been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) 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 U.S. GAAP 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 2015. The results of operations for the three months ended April 2, 2016 are not necessarily indicative of the results for all of 2016.

2. Summary of Significant Accounting Policies

Basis of Presentation

We have incurred significant net losses since our inception and have an accumulated deficit of \$293.6 million. In 2015, we incurred a net loss of \$8.6 million and had negative cash flows from operations of \$8.5 million. At April 2, 2016, we had \$5.6 million in cash compared to \$7.5 million in cash and cash equivalents as of December 31, 2015. Our cash resources will not be sufficient to fund our business for the next 12 months. We will need to grow our revenues from commercial operations and/or raise additional funds over the next 12 months 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. These factors raise substantial doubt about our ability to continue as a going concern.

Our plans regarding improving our future liquidity will require us to successfully use our expertise and our technology to generate revenues in various ways, including commercial operations, joint ventures and licenses. We have invested and will continue to invest in our Austin, Texas manufacturing facility to enable us to produce our Conductus wire products. Delays in the timing of our ability to, including but not limited to, raise additional capital, unexpected production delays, and our ability to sell our Conductus wire products in large scale could substantially impact our estimates used in the determination of expected future cash flows and/or expected future profitability. If we fail to increase our revenues, we may not achieve and may not maintain profitability and we may not realize our investment in infrastructure.

Table of Contents

The accompanying condensed consolidated financial statements do not include any adjustments that may result from the outcome of the uncertainties set forth above. 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 2015. We have not made any material changes to these policies.

We have reviewed recently issued Financial Accounting Standards Board pronouncements and do not believe they will have a material impact on our condensed consolidated financial statements.

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 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

Our revenues have principally been derived from the sale of our wireless communications products, and to an increasing extent our Conductus wire, 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.

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.

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.

Table of Contents

Inventories

Inventories were 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 April 2, 2016 net inventory value was \$78,000, compared to a December 31, 2015 value of \$121,000. 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 (minimal sales in the current quarter and no backlog of sales orders as of April 2, 2016 related to our legacy wireless business), 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 quarters of 2016 and 2015, there were no retirements or disposals and we realized gains of \$0 and \$1,000, respectively, from sale of previously retired equipment.

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 seventeen years.

Other Assets and Investments

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 the business are written off in the period identified since they will no longer be used in operations and generate any positive cash flows for us. Periodically, long-lived assets that will continue to be used by us will need to be evaluated for recoverability. Such evaluation is based on various analyses, including cash flow and profitability projections. The analyses necessarily involve significant management judgment. Market acceptance and significant revenues from our new Conductus wire is a key assumption in realization of our investment in long-lived assets. In the event the projected undiscounted cash flows are less than net book value of the assets, the carrying value of the assets will be written down to their estimated fair value. We tested our long-lived assets for recoverability during 2015 and at April 2, 2016 and did not believe there was any impairment.

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 California and federal tax years that remain open to possible evaluation and interpretation of our tax position are 2011 and 2012, respectively.

Table of Contents

As of December 31, 2015, we had net operating loss carryforwards for federal and state income tax purposes of \$334.7 million and \$150.5 million, respectively, which expire in the years 2018 through 2035. However, during 2015, we concluded that under the Internal Revenue Code change of control limitations, a maximum of \$38.3 million and \$37.7 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 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 April 2, 2016 and March 28, 2015.

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 period. Potential common shares are not included in the calculation of diluted loss per share because their effect is anti-dilutive.

Stock-based Compensation

We grant both restricted stock awards and stock options to our key employees, directors and consultants. For the quarters ended April 2, 2016 and March 28, 2015, no options or awards were granted. 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	
	April 2, 2016	March 28, 2015
Cost of revenues	\$ 1,000	\$
Research and development	37,000	91,000
Selling, general and administrative	223,000	461,000
Total stock-based compensation expense	\$ 261,000	\$ 552,000

Use of Estimates

The preparation of the condensed consolidated financial statements in conformity with U.S. GAAP 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, fixed assets, intangibles, estimated provisions for warranty costs, fair value of warrant derivatives, 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