SUPERCONDUCTOR TECHNOLOGIES INC
Form 10-Q
May 09, 2014
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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 29, 2014

¨ **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 13,119,348 shares of our common stock outstanding as of the close of business on May 2, 2014.

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SUPERCONDUCTOR TECHNOLOGIES INC.

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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 Conductus 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 economic uncertainty; 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 2013.

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.

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PART I

FINANCIAL INFORMATION

Item 1. Financial Statements.

SUPERCONDUCTOR TECHNOLOGIES INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

	Three Months Ended	
	March 29, 2014	**March 30, 2013**
Net revenues	**$ 389,000**	**$ 776,000**
Costs and expenses:		
Cost of revenues	370,000	226,000
Research and development	1,470,000	1,438,000
Selling, general and administrative	1,348,000	1,345,000
Total costs and expenses	**3,188,000**	**3,009,000**
Loss from operations	**(2,799,000)**	**(2,233,000)**
Other Income and Expense:		
Loss from joint venture investment in Resonant LLC		(182,000)
Adjustments to fair value of warrant derivatives	(232,000)	
Other income	96,000	6,000
Interest income		1,000
Net loss	**$ (2,935,000)**	**$ (2,408,000)**
Basic and diluted net loss per common share	**$ (0.25)**	**$ (0.58)**
Basic and diluted weighted average number of common shares outstanding	11,880,889	4,152,036

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

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SUPERCONDUCTOR TECHNOLOGIES INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

	March 29, 2014 (Unaudited)	December 31, 2013 (See Note)
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 7,768,000	$ 7,459,000
Accounts receivable, net	308,000	6,000
Inventory, net	79,000	76,000
Prepaid expenses and other current assets	328,000	437,000
Total Current Assets	8,483,000	7,978,000
Property and equipment, net of accumulated depreciation of $11,938,000 and $11,626,000, respectively	6,658,000	5,473,000
Patents, licenses and purchased technology, net of accumulated amortization of $740,000 and $722,000, respectively	890,000	888,000
Other assets	469,000	501,000
Total Assets	**$ 16,500,000**	**$ 14,840,000**
LIABILITIES AND STOCKHOLDERS EQUITY		
Current Liabilities:		
Accounts payable	$ 1,089,000	$ 703,000
Accrued expenses	709,000	637,000
Total Current Liabilities	1,798,000	1,340,000
Other long term liabilities	6,393,000	6,194,000
Total Liabilities	8,191,000	7,534,000
Commitments and contingencies-Notes 5 and 6		
Stockholders Equity:		
Preferred stock, $.001 par value, 2,000,000 shares authorized, 328,925 and 328,925 shares issued and outstanding, respectively		
Common stock, $.001 par value, 250,000,000 shares authorized, 13,119,348 and 11,634,950 shares issued and outstanding, respectively	13,000	12,000
Capital in excess of par value	285,348,000	281,411,000
Accumulated deficit	(277,052,000)	(274,117,000)
Total Stockholders Equity	8,309,000	7,306,000
Total Liabilities and Stockholders Equity	**$ 16,500,000**	**$ 14,840,000**

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

Note December 31, 2013 balances were derived from the audited consolidated financial statements.

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SUPERCONDUCTOR TECHNOLOGIES INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Three Months Ended	
	March 29, 2014	**March 30, 2013**
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (2,935,000)	$ (2,408,000)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	330,000	234,000
Stock-based compensation expense	187,000	166,000
Write-off of intangibles		79,000
Adjustments to fair value of warrant derivatives	232,000	
Gain on sale of property and equipment	(96,000)	(6,000)
Loss from joint venture investment in Resonant LLC		182,000
Changes in assets and liabilities:		
Accounts receivable	(302,000)	(220,000)
Inventories	(3,000)	(94,000)
Prepaid expenses and other current assets	108,000	87,000
Patents and licenses	(20,000)	(23,000)
Other assets	32,000	32,000
Accounts payable, accrued expenses and other current liabilities	426,000	165,000
Net cash used in operating activities	(2,041,000)	(1,806,000)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment	(1,497,000)	(178,000)
Net proceeds from the sale of property and equipment	96,000	6,000
Net cash used in investing activities	(1,401,000)	(172,000)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net proceeds from the exercise of outstanding warrants	3,751,000	
Net cash provided by financing activities	3,751,000	
Net (decrease) increase in cash and cash equivalents	309,000	(1,978,000)
Cash and cash equivalents at beginning of period	7,459,000	3,634,000
Cash and cash equivalents at end of period	$ 7,768,000	$ 1,656,000

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

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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. 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 HTS Conductus® wire for next generation power applications. While most our current commercial product revenues come from the sale of high performance wireless infrastructure products, production of our Conductus HTS wire is our principal opportunity to grow our future revenue.

The unaudited condensed consolidated financial information furnished herein has been prepared in accordance with generally accepted accounting principles 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 2013. The results of operations for the three months ended March 29, 2014 are not necessarily indicative of the results for all of 2014.

2. Summary of Significant Accounting Policies

Basis of Presentation

We have incurred significant net losses since our inception and had an accumulated deficit of $277.0 million as of March 29, 2014. For the three months ended March 29, 2014, we incurred a net loss of $2.9 million and negative cash flows from operations of $2.0 million. For all of 2013, we incurred a net loss of $12.2 million and had negative cash

flows from operations of $8.3 million. These factors raise substantial doubt about our ability to continue as a going concern.

At March 29, 2014, we had $7.8 million in cash and cash equivalents, including more than $3.7 million from the exercise of 1,459,398 outstanding warrants during the quarter. Since March 29, 2014, through May 2, 2014, there have been no additional warrant exercises. Our cash resources will not be sufficient to fund our business for the next twelve months. We may need to additional funds to meet our working capital needs and 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 independent registered public accounting firm has also included in their audit reports for 2013 and 2012 an explanatory paragraph expressing substantial doubt about our ability to continue as a going concern.

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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 significant capital 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. The accompanying consolidated financial statements do not include any adjustments that may result from the outcome of these uncertainties.

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 sell predominantly to entities in the wireless communications industry. 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.

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

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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 were charged to government and other contract expense.

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 2014, there were no retirements or disposals and we realized gains of $96,000 from the sale of previously retired equipment. In 2013, there were disposals and retirements totaling $9.4 million and gains of $98,000 from 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.

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 the business are written off in the period identified since they will no longer generate any positive cash flows for us. Periodically, long lived assets that will continue to be used by us must be 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 will be written down to their estimated fair value. We tested our long lived assets for recoverability during 2013 and determined there was no impairment.

In July 2012, we contributed 14 issued and pending patents regarding our innovative Reconfigurable Resonance (RcR) technology, limited use of our Santa Barbara facility, experienced executive leadership and technical expertise as our minority investment in Resonant LLC. As of December 31, 2012 and June 18, 2013, our interest in Resonant was 30%, and the net value of the assets contributed, estimated to approximate fair value, was $423,000 and $185,000, respectively. We had accounted for it using the equity method and included it in *Other assets* for both periods.

On June 18, 2013, we announced via a press release, that we exchanged our equity interest in Resonant LLC, a wholly owned subsidiary of Resonant Inc., for a $2.4 million subordinated convertible note receivable from the new Resonant Inc. No gain was recognized for the exchange of our net equity interest on the date of issuance for the note receivable due to uncertainties in connection with the collectability of this subordinated note receivable. Our note is subordinated to a third party lender and is only convertible in the event Resonant Inc. conducts an initial public offering and certain other conditions are met. We determined that our net equity interest of $185,000 approximated the fair value of the note receivable at December 31, 2013 and March 29, 2014, respectively. Resonant Inc. filed a registration statement with the Securities and Exchange Commission in January 2014. Upon conversion of our note, we would own, before any such public offering, approximately 18.5% of Resonant Inc. We cannot estimate the value of such interest or predict the outcome of the offering by Resonant Inc.

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We have invested and will continue to invest significant capital in our Austin, Texas manufacturing facility to enable us to produce our Conductus wire products.

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 this Report. We incurred no expenses in the quarter ended March 29, 2014 or in the full year 2013 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 2010.

As of December 31, 2013, we had net operating loss carryforwards for federal and state income tax purposes of approximately $313.8 million and $160.6 million, respectively, which expire in the years 2014 through 2033.

However, during 2013, we concluded that under the Internal Revenue Code change of control limitations, a maximum of $17.4 million and $16.8 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 March 29, 2014 and March 30, 2013.

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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.

Stock-based Compensation

We grant both restricted stock awards and stock options to our key employees, directors and consultants. For the quarters ended March 29, 2014 and March 30, 2013, 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 29, 2014	**March 30, 2013**
Expected life in years	4.0	4.0
Risk free interest rate	1.1%	0.6%
Expected volatility	100.2%	93.3%
Dividend yield	0%	0%

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. 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. Our actual 2013 forfeiture rate was 25% and we assumed a 20% forfeiture rate in the period ending March 29, 2014 based on our historical stock option 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 29, 2014	**March 30, 2013**
Research and development	$ 48,000	$ 55,000
Selling, general and administrative	139,000	111,000
Total stock-based compensation expense	$ 187,000	$ 166,000

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, inventory, 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

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, inventories, prepaid expenses and other current assets and other current liabilities as March 29, 2014 approximate fair value.

The fair value of our warrant derivative liability was estimated using the binomial lattice option valuation model.

Fair value for financial reporting purposes is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly

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transaction between market participants on the measurement date, ASC 820, Fair Value Measurement and Disclosures , also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. ASC 820 describes three levels of inputs that may be used to measure fair value:

Level 1 quoted prices in active markets for identical assets or liabilities

Level 2 quoted prices for similar assets and liabilities in active markets or inputs that are observable

Level 3 inputs that are unobservable (for example cash flow modeling inputs based on assumptions)

The fair value of our warrant liabilities was determined based on level 3 inputs. These derivative liabilities are adjusted to reflect fair value at each period end, with any increase or decrease in the fair value being recorded in results of operations as Adjustments to fair value of derivatives. See Note 3 Stockholder s Equity: *Warrants*.

Comprehensive Income

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

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.

Certain Risks and Uncertainties

Our long-term prospects are dependent upon the successful commercialization and market acceptance or our Conductus wire 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 29, 2014, we had two customers that represented 86% and 10% of total net revenues and 99% of accounts receivable. In 2013, these two customers represented 63% and 33% of total net revenues and 89% 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. Stockholders Equity

The following is a summary of stockholders equity transactions for the three months ended March 29, 2014:

	Convertible Preferred Stock		Common Stock		Capital in Excess of	Accumulated	
	Shares	Amount	Shares	Amount	Par Value	Deficit	Total
Balance at December 31, 2013	328,925	$	11,634,950	$ 12,000	$ 281,411,000	$ (274,117,000)	$ 7,306,000
Issuance of common stock from exercise of outstanding warrants			1,459,398	1,000	3,750,000		3,751,000
Stock-based compensation			25,000		187,000		187,000
Net loss						(2,935,000)	(2,935,000)
Balance at March 29, 2014	328,925	$	13,119,348	$ 13,000	$ 285,348,000	$ (277,052,000)	$ 8,309,000

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Stock Options

At March 29, 2014, we had two active equity award option plans, the 2003 Equity Incentive Plan and the 2013 Equity Incentive Plan (collectively, the Stock Option Plan), although we can only grant new options under the 2013 Equity Incentive Plan. Under the Stock Option Plans, stock awards were made to our directors, key employees, consultants, and non-employee directors and consisted of stock options, stock appreciation rights, restricted stock awards, performance awards, and performance share awards. Stock options were 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 29, 2014 or during the three months ended March 30, 2013.

The impact to the condensed consolidated statements of operations for the quarter ended March 29, 2014 on net loss was $152,000 and $0.01 on basic and diluted net loss per common share and for the quarter ended March 30, 2013 the impact was $80,000 and $0.02 on basic and diluted net 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 $1.5 million and the weighted-average period over which the cost is expected to be recognized was 1.9 years at March 29, 2014.

The following is a summary of stock option transactions under our stock option plans at March 29, 2014:

	Number of Shares	Price Per Share	Weighted Average Exercise Price	Number of Options Exercisable	Weighted Average Exercise Price
Balance at December 31, 2013	1,152,074	$ 2.12 - $ 843.60	$ 5.58	91,738	$ 44.18
Granted	50,000	2.85	2.85		
Exercised					
Canceled	(120)	96.00 - 843.60	404.81		
Balance at March 29, 2014	1,201,954	$ 2.12 - $555.00	$ 5.43	114,174	$ 36.46

The outstanding options expire on various dates through the end of December 2023. The weighted-average contractual term of options outstanding is 9.3 years and the weighted-average contractual term of stock options currently exercisable is 5.6 years. The exercise prices for these options range from $2.52 to $555 per share, for an aggregate exercise price of approximately $6.5 million. At March 29, 2014, outstanding options covering 1,053,334 shares, with an intrinsic value of $661,000, had an exercise price less than the current market value and 16,668 of these options were exercisable, with an intrinsic value of $4,000.

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 29, 2014:

	Number of Shares	Weighted Average Grant Date Fair Value
Balance nonvested at December 31, 2013	43,165	$ 4.28
Granted	25,000	2.76
Vested	(13,932)	7.38
Forfeited		
Balance nonvested at March 29, 2014	54,233	$ 3.13

The impact to the condensed consolidated statements of operations for the three months ended March 29, 2014 was $35,000 and less than $0.01 on basic and diluted net loss per common share and for the quarter ended March 30, 2013 the impact was $86,000 and $0.02 on basic and diluted net 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 $149,000 and the weighted-average period over which the cost is expected to be recognized was 1.2 years.

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Warrants

The following is a summary of outstanding warrants at March 29, 2014:

		Total	Common Shares Currently Exercisable	Price per Share	Expiration Date
(1)	Warrants related to February 2012 financing	419,451	419,451	$ 16.20	February 22, 2017
(2)	Warrants related to November 2012 financing	8,333	8,333	4.50	November 26, 2015
(3)	Warrants related to December 2012 financing	15,625	15,625	4.50	December 18, 2015
(4)	Warrants related to April 2013 financing	256,914		5.45	April 26, 2015
(5)	Warrants related to April 2013 financing	256,913		5.45	April 26, 2019
(6)	Warrants related to August 2013 financing	117,670	117,670	2.25	August 5, 2016
(7)	Warrants related to August 2013 financing	6,117,383	6,117,383	2.57	August 9, 2018
(8)	Warrants related to August 2013 financing	2,436,733	2,436,733	2.57	August 9, 2015

Warrants (1)-(6) 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 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.

We have determined that warrants (7) and (8) are not considered indexed to our common shares under ASC 815-40, and require separate accounting as derivative instruments with changes in fair value recognized in earnings each period. The warrants contain a provision whereby the warrant exercise price would be decreased in the event that future common stock issuances are made at a price less than the then exercise price. Due to the potential variability of their exercise price, these warrants do not qualify for equity treatment, and therefore are recognized as a liability. The warrant liability is adjusted to fair value each reporting period, and any change in value is recognized in the statement of operations. Their initial August 9, 2013 valuation was determined using the binomial lattice valuation model, including an equal probabilities tree and early exercise factor of 30%, the significant weighted average assumptions for estimating the fair value of these warrants were, respectively, as follows: expected life of five years and two years; risk free interest rates of 1.36% and 0.32%; expected volatility of 111% and 116% and; dividend yield of 0% and 0%. The initial fair value at August 9, 2013 was estimated to be slightly less than $4.2 million.

The significant weighted average assumptions for estimating the fair value of these warrants at December 31, 2013 were, respectively, as follows: expected life of 4.6 years and 1.6 years; risk free interest rates of 1.75% and 0.38%; expected volatility of 97% and 126% and; dividend yield of 0% and 0%., and the December 31, 2013 fair value of these warrants was estimated to be $5.7 million. The fair value change from August 9, 2013 to December 31, 2013 was $1.6 million.

At March 29, 2014 the significant weighted average assumptions for estimating the fair value of these warrants were, respectively, as follows: expected life of 4.4 years and 1.4 years; risk free interest rates of 1.49% and 0.25%; expected volatility of 99% and 136% and; dividend yield of 0% and 0%., and the March 29, 2014 fair value of these warrants was estimated to be $5.9 million. The fair value change from December 31, 2013 to March 29, 2014 was $0.2 million.

From January 1, 2014 through March 29, 2014, we have received more than $3.7 million from the exercise of 1,459,398 outstanding warrants issued in connection with our August 2013 underwritten public offering. Since March 29, 2014, through May 2, 2014, there have been no additional warrant exercises.

4. Earnings Per Share

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

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

	March 29, 2014	March 30, 2013
Outstanding stock options	1,201,954	137,534
Unvested restricted stock awards	54,233	45,803
Outstanding warrants	9,629,022	443,409
Total	10,885,209	626,746

Also, the preferred stock convertible into 274,104 shares of common stock was not included since its impact would be anti-dilutive.

5. Commitments and Contingencies

Operating Leases

We lease our offices and production facilities under non-cancelable operating leases in Santa Barbara, CA and Austin, TX that expire in November 2016 and March 2017, respectively. The leases contain minimum rent escalation clauses that require additional rental amounts after the first year. Rent expense for these leases with minimum annual rent escalation is recognized on a straight line basis over the minimum lease term. These leases also require us to pay utilities, insurance, taxes and other operating expenses and contain one five-year renewal option. The January 1, 2012 partial sublease of our Santa Barbara facility has offset some of these expenses.

In April 2014 documents were signed to amend our Santa Barbara, CA building operating lease and reduced our lease commitment. Instead of leasing approximately 71,000 square feet and partially subleasing to other tenants, we will now lease approximately 35,000 square feet and our former principal tenant will lease their portion of the building directly from our landlord. Other terms and conditions of the lease remain the same. Our table of minimum operating lease payments listed below has not yet been updated to reflect this reduced commitment going forward.

For the three months ended March 29, 2014 and March 30, 2013, rent expense was $229,000 and $221,000 respectively.

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 2014 to 2021. For each of the three months ended March 29, 2014 and March 30, 2013, royalty expense totaled $6,000. 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 as of March 29, 2014 are as follows:

Years ending December 31,	Licenses	Operating Leases
Remainder of 2014	$ 30,000	$ 1,253,000
2015	45,000	1,723,000
2016	45,000	1,654,000
2017	45,000	87,000
2018	45,000	
Thereafter		
Total payments	$ 210,000	$ 4,717,000

6. 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.

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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.

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

Balance Sheet Data:

	March 29, 2014	December 31, 2013
Accounts receivable:		
Accounts receivable-trade	$ 309,000	$ 7,000
U.S. government accounts receivable-billed		
Less: allowance for doubtful accounts	(1,000)	(1,000)
	$ 308,000	**$ 6,000**

	March 29, 2014	December 31, 2013
Inventories:		
Raw materials	$ 565,000	$ 563,000
Less: Raw material reserves	(542,000)	(542,000)
Work-in-process	30,000	31,000
Less: Work-in-process reserves	(25,000)	(25,000)
Finished goods	213,000	204,000
Less: Finished goods reserves	(162,000)	(155,000)
	$ 79,000	**$ 76,000**

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	March 29, 2014	December 31, 2013
Property and Equipment:		
Equipment	$ 10,812,000	$ 9,315,000
Leasehold improvements	7,397,000	7,397,000
Furniture and fixtures	387,000	387,000
	18,596,000	17,099,000
Less: accumulated depreciation and amortization	(11,938,000)	(11,626,000)
	$ 6,658,000	**$ 5,473,000**

Depreciation expense amounted to $312,000 and $218,000 for the three month periods ended March 29, 2014 and March 30, 2013, respectively.

	March 29, 2014	December 31, 2013
Patents and Licenses:		
Patents pending	$ 454,000	$ 434,000
Patents issued	1,176,000	1,176,000
Less accumulated amortization	(740,000)	(722,000)
Net patents issued	436,000	454,000
	$ 890,000	**$ 888,000**

Amortization expense related to these items totaled $18,000 and $16,000, for the three month periods ended March 29, 2014 and March 30, 2013, respectively. Amortization expenses are expected to total $59,000 for the remainder of 2014 and $70,000 for 2015 and $69,000 for 2016.

	March 29, 2014	December 31, 2013
Accrued Expenses and Other Long Term Liabilities:		
Salaries Payable	$ 125 000	$ 98,000
Compensated Absences	217,000	206,000
Compensation related	64,000	25,000
Warranty reserve	146,000	151,000
Deferred rent	431,000	443,000
Other	179,000	200,000
Fair value of warrant derivatives	5,940,000	5,708,000
	7,102,000	**6,831,000**

Less current portion	**(709,000)**	**(637,000)**
Long term portion	**$ 6,393,000**	**$ 6,194,000**

	For the three months ended,	
	March 29, 2014	**March 30, 2013**
Warranty Reserve Activity:		
Beginning balance	$ 151,000	$ 227,000
Additions		2,000
Deductions	(5,000)	(18,000)
Ending balance	$ 146,000	$ 211,000

8. Subsequent Events

In April 2014 documents were signed to amend our Santa Barbara, CA building operating lease and reduced our lease commitment. Instead of leasing approximately 71,000 square feet and partially subleasing to other tenants, we will now lease approximately 35,000 square feet and our former principal tenant will lease their portion of the building directly from our landlord. Other terms and conditions of the lease remain the same. Our table of minimum operating lease payments listed above has not yet been updated to reflect this reduced commitment going forward.

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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 27 years have yielded an extensive patent portfolio as well as critical trade secrets, unpatented technology and proprietary knowledge. We have commercialized wireless products and cryogenic coolers using our proprietary technology and are currently focusing our efforts on this technology in superconducting power applications.

Wireless Communications. 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.

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.

Electric Power Utilities. As discussed above, we are adapting our unique HTS materials deposition techniques to deliver energy efficient, cost-effective and high performance Conductus wire technology for next generation power applications. We have identified several large initial target markets for our Conductus wire including energy (wind turbines, cables, fault current limiters) and industrial (motors, generators) applications. We are partnering with HTS industry leaders to accelerate our development and manufacturing processes for our Conductus wire, which we expect to begin commercial production later this year.

Our development efforts (including those described under Our Strategic Initiatives below) can take a significant number of years to commercialize, and we must overcome significant technical barriers and deal with other significant risks, some of which are set out in our public filings, including in particular the Risk Factors included in Item 1A of this Report.

Our Wireless Business

Although our current efforts are focused on our strategic initiatives described below, substantially all 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. As a result of this downward trend, we have managed our inventory to historically low levels, which may result in longer delivery lead times, which may not be acceptable to our customers. If this downward trend continues we may be compelled to refocus our manufacturing away from wireless products altogether. We continue to evaluate the various options available for our wireless business as we transform ourselves into a Conductus wire manufacturer. Our commercial operations are subject to a number of significant risks, some of which are set out in our public filings, including in particular the Risk Factors included in Item 1A of this Report.

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Our Strategic Initiatives

We have created several unique capabilities and a HTS manufacturing system related to our new Conductus wire platform, 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 Conductus 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 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. The primary application for HTS cables is medium voltage feeds to load pockets in dense urban areas. In these high demand zones the grid is often saturated with aging infrastructure. HTS technology brings a considerable amount of power to new locations where the construction of additional transmission to distribution substations, with major transformer assets, is not feasible. Another potential use of HTS power cable is to improve grid power transmission by connecting two existing substations. In dense urban environments many substations often reach capacity limits and require redundant transformer capacity to improve reliability HTS cables can tie these existing stations together, avoiding very costly transformer upgrades and construction costs.

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. Currently, electrical-utilities use massive 80kA circuit breakers, oversized transformers and fuses to prevent faults from damaging their equipment and protecting against surges. However, once a fault has occurred, standard circuit breakers suffer destructive failure and need to be replaced before service can be restored. In addition, Smart Grid and embedded alternative energy generation enhancements will increase the need for SCFLs. Grid operators face a major challenge in moving power safely and efficiently, from generators to consumers, through several stages of voltage transformation step downs and step ups. At each stage, valuable energy is lost in the form of waste heat. Moreover, while demands are continually rising, space for transformers and substations - especially in dense urban areas - is severely limited. Conventional oil-cooled transformers pose a fire and environmental hazard. Compact, efficient superconducting transformers, by contrast, are cooled by safe, abundant and environmentally benign liquid nitrogen. As an additional benefit, these actively-cooled devices will offer the capability of operating in overload, to twice the nameplate rating, without any loss of life to meet occasional utility peak load demands.

Superconducting Rotating Machines - Motors and Generators:

Superconducting motors, generators, turbines and other rotating machines are expected to generate large future demand for our Conductus wire. Coils utilizing Conductus 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 superconducting 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. Superconducting wind turbines are expected to play a unique role offshore since conventional technology cannot achieve the power per tower requirement.

Superconducting High Field magnets:

There are a variety of applications that utilize superconducting magnets in order to capitalize on their unique ability to create extremely high magnetic fields. The NMR (Nuclear Magnetic Resonance) and MRI (Magnetic Resonance Imaging) machines of today utilize such superconducting magnets for this very reason. Currently, high-field superconducting magnets

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are manufactured using commercially available superconducting wire such as niobium-titanium (NbTi) or niobium-tin (Nb3Sn). NMR and MRI device manufacturers look towards advances in superconducting technologies to improve the overall performance of their systems by dramatically increasing the magnetic fields while reducing size. High demand for a robust, high performance and low cost superconducting wire has spurred rapid development of a next generation alternative. In the last 10 years, new second generation (2G) Rare Earth, Barium, Copper Oxide (ReBCO) superconducting materials have been proven to drastically increase magnetic field strengths, especially at low temperatures. These advanced ReBCO based superconductors now provide an excellent alternative to NbTi and Nb3Sn based materials.

Advanced RF Filters for mobile communications

In February 2012 our newly formed subsidiary, Resonant LLC., entered into an agreement to develop its innovative Reconfigurable Resonance (RcR) technology in the rapidly growing mobile communications products industry. See further explanation below in *Other Assets and Investments.*

Other Assets and Investments

From time to time we may pursue joint ventures with other entities to commercialize our technology. As mentioned above, in July 2012, we contributed 14 issued and pending patents regarding our innovative Reconfigurable Resonance (RcR) technology, limited use of our Santa Barbara facility, experienced executive leadership and technical expertise as our minority investment in Resonant LLC. As of December 31, 2012 and June 18, 2013, our interest in Resonant was 30%, and the net value of the assets contributed, estimated to approximate fair value, was $423,000 and $185,000, respectively. We had accounted for this investment using the equity method and included it in *Other assets* for both periods.

On June 18, 2013, we announced via a press release, that we exchanged our equity interest in Resonant LLC, a wholly owned subsidiary of Resonant Inc., for a $2.4 million subordinated convertible note receivable from the new Resonant Inc. No gain was recognized for the exchange of our net equity interest on the date of issuance for the note receivable due to uncertainties in connection with the collectability of this subordinated note receivable. Our note is subordinated to a third party lender and is only convertible in the event Resonant, Inc. conducts an initial public offering and certain other conditions are met. We determined that our net equity interest of $185,000 approximated the fair value of the note receivable at December 31, 2013 and March 29, 2014, respectively. Resonant Inc. filed a registration statement with the Securities and Exchange Commission in January 2014. Upon conversion of our note, we would own, before any such public offering, approximately 18.5% of Resonant Inc. We cannot estimate the value of such interest or predict the outcome of the offering by Resonant Inc.

In 2007, we formed a joint venture with Hunchun BaoLi Communication Co. Ltd. (BAOLI) 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 United States 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 this Report.

Results of Operations

Quarter Ended March 29, 2014 compared to the Quarter Ended March 30, 2013

Net revenues decreased by $387,000 to $389,000 in the first quarter of 2014 from $776,000 in the first quarter of 2013. Net revenues consist of commercial product revenues.

Net commercial product revenues decreased by $387,000, or 50%, to $389,000 in the first quarter of 2014 from $776,000 in the first quarter of 2013. The decrease is the result of lower sales volume for all of our wireless products. Sales of our Conductus wire products are not yet significant. 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. As our sales have declined in the current period, we believe this market dynamic will continue to impact our commercial revenue. Sales prices for our products were essentially unchanged. Our three largest customers accounted for 99% of our total net commercial product revenues in the first quarter of both 2014 and 2013. These customers generally purchase

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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. Sales of our Conductus wire products are not yet material.

Cost of commercial product revenues includes all direct costs, manufacturing overhead and provision for excess and obsolete inventories. The cost of commercial product revenues increased to $370,000 in the first quarter of 2014 compared to $226,000 for the first quarter of 2013, an increase of $144,000 or 64%. The lower 2013 costs were primarily the result of the sale of $300,000 of previously reserved inventory in the first quarter of 2013.

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 charged 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 29, 2014		March 30, 2013	
	(Dollars in thousands)			
Net commercial product sales	$ 389	100.0%	$ 776	100.0%
Total cost of commercial product sales	370	95%	226	29%
Gross profit	$ 19	5%	$ 550	71%

We had a gross profit of $19,000 in the first quarter of 2014 from the sale of our commercial products compared to a gross profit of $550,000 in the first quarter of 2013. We experienced a reduced gross profit in the first quarter of 2014 due to lower sales being insufficient to cover our overhead. The gross profit in 2013 was the result of higher sales, the reduction of warranty reserves, reduced manufacturing use of our facilities and the sale of $300,000 of previously reserved inventory mentioned above.

Research and development expenses relate to development of new Conductus wire products and new wire products manufacturing processes. Total expenses totaled $1,470,000 in the first quarter of 2014 compared to $1,438,000 in the same quarter of 2013, an increase of 2%. The increase is the result of our efforts for improving the manufacturability of our new Conductus wire products, which included increased use of our facilities and increases in depreciation from placing new equipment into service.

Selling, general and administrative expenses were $1.3 million in both the first quarter of 2014 and 2013.

We recognized an expense for an adjustment to the fair value of warrant derivatives of $232,000 in the first quarter of 2014. See Note 3 Stockholder s Equity: *Warrants*. There was no such expense in the first quarter of 2013.

Other income from the sale of property and equipment was $96,000 in the first quarter of 2014 and $6,000 in the first quarter of 2013.

We had a net loss of $2.9 million for the quarter ended March 29, 2014, compared to a net loss of $2.4 million in the first quarter of 2013.

The net loss available to common stockholders totaled $0.25 per common share in the first quarter of 2014, compared to a net loss of $0.58 per common share in the first quarter of 2013. The reduction in net loss available to common stockholders is largely due to the difference in shares outstanding used in computing the net loss.

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Liquidity and Capital Resources

Cash Flow Analysis

As of March 29, 2014, we had working capital of $6.7 million, including $7.8 million in cash and cash equivalents, compared to working capital of $6.6 million at December 31, 2013, which included $7.5 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 $309,000 from $7.5 million at December 31, 2013 to $7.8 million at March 29, 2014. In the first quarter of 2014, cash was used principally in operations and for the purchase of equipment. These uses were offset by net cash proceeds of $3.7 million provided by the sale of common stock from the exercise of outstanding warrants.

Cash used in operations totaled $2.0 million in the first quarter of 2014. We used $2.3 million to fund the cash portion of our net loss. We also used cash to fund a $0.3 million increase in accounts receivable, and a decrease in inventory and patents and licenses. These uses were offset by a $0.6 million decrease provided by a reduction in prepaid expenses and other assets, and increases in accounts payable, accrued expenses and other liabilities.

Net cash used in investing activities totaled $1.4 million in the first quarter of 2014. Purchases of equipment for our Conductus wire initiative were $1.5 million and $96,000 was provided by equipment sales. In the first quarter of 2013, $178,000 was used to purchase property and equipment and there were $6,000 in equipment sales.

Net cash provided by financing activities in the first quarter of 2014 was $3.7 million from the exercise of 1,459,398 outstanding warrants issued in connection with our August 2013 underwritten public offering. Since March 29, 2014, through May 2, 2014, there have been no additional warrant exercises.

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. During the first quarter ended March 29, 2014, we have received more than $3.7 million from the exercise of 1,459,398 outstanding warrants issued in connection with our August 2013 underwritten public offering.

Contractual Obligations and Commercial Commitments

In April 2014 documents were signed to amend our Santa Barbara, CA building operating lease and reduced our lease commitment. Instead of leasing approximately 71,000 square feet and partially subleasing to other tenants, we will now lease approximately 35,000 square feet and our former principal tenant will lease their portion of the building directly from our landlord. Other terms and conditions of the lease remain the same. Our table of minimum operating lease payments listed above has not yet been updated to reflect this reduced commitment going forward. We have not had other material changes outside of the ordinary course of business in our contractual obligations as disclosed in our Annual Report on Form 10-K for 2013.

Capital Expenditures

We invested $1.5 million for fixed assets in the first quarter of 2014 and we plan to invest approximately $2.1 million in fixed assets during the remainder of 2014. These amounts, and the amounts spent in 2013, are for the purchase of

equipment and facilities improvements for our Conductus wire initiative. We do not plan any additional fixed asset expenditures in 2014 for our existing wireless business.

Future Liquidity

For the quarter ended March 29, 2014, we incurred a net loss of $2.9 million and had negative cash flows from operations of $2.0 million. In the full 2013 year, we incurred a net loss of $12.2 million and had negative cash flows from operations of $8.3 million. Our independent registered public accounting firm has included in its audit reports for 2013 and 2012 an explanatory paragraph expressing substantial doubt about our ability to continue as a going concern.

At March 29, 2014, we had $7.8 million in cash and cash equivalents. During the first quarter of 2014 we raised $3.7 million from the exercise of outstanding warrants. Since March 29, 2014, through May 2, 2014, there have been no additional warrant exercises. We believe our current cash resources and these recently raised proceeds will not be sufficient to fund our business for the next twelve 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, joint ventures, licenses and we plan to leverage our leadership in superconducting technologies, extensive intellectual property, and HTS manufacturing expertise to develop and produce Conductus wire. Because of the expected timing and uncertainty of these factors, we may need to raise funds to meet our working capital needs.

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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.

Net Operating Loss Carryforward

As of December 31, 2013, we had net operating loss carryforwards for federal and state income tax purposes of approximately $313.8 million and $160.6 million, respectively, which expire in the years 2014 through 2033. However, during 2013, we concluded that under the Internal Revenue Code change of control limitations, a maximum of $17.4 million and $16.8 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 generally accepted accounting principles 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 2013. 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 $26,000 at March 29, 2014, compared to $88,000 at December 31, 2013.

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 29, 2014 compared with our market risk exposure on December 31, 2013. See *Management s Discussion and Analysis of Financial Condition and Results of Operations Market Risk* in our Annual Report on Form 10-K for 2013.

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 29, 2014 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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.

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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 2013 filed with the Securities and Exchange Commission on March 28, 2014. We are not aware of any material changes to those risk factors.

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

None.

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*
101.INS	XBRL Instance Document*
101.SCH	XBRL Taxonomy Extension Schema Document*

101.CAL	XBRL Calculation Linkbase Document*
101.LAB	XBRL Label Linkbase Document*
101.PRE	XBRL Taxonomy Presentation Linkbase Document*
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document*

* Filed herewith.

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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, 2014

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

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