

# SUPERCONDUCTOR TECHNOLOGIES INC

## FORM 10-K (Annual Report)

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

**FORM 10-K**  
**ANNUAL REPORT**  
**PURSUANT TO SECTIONS 13 OR 15(d)**  
**OF THE SECURITIES EXCHANGE ACT OF 1934**

(Mark One)

☒ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.**

**For the fiscal year ended December 31, 2007**

**OR**

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

**For the transition period from            to**

**Commission File Number 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.)*

**460 Ward Drive, Santa Barbara, California 93111-2310**

*(Address of principal executive offices) (Zip Code)*

**Registrant's telephone number, including area code: ( 805) 690-4500**

**Securities registered pursuant to Section 12(b) of the Act:**

**Title of each class**

**Name of each exchange on which registered**

Common stock, \$0.001 par value

The NASDAQ Capital Market

**Securities registered pursuant to Section 12(g) of the Act:**

**None**

Indicate by check mark if the registrant is a well known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☐  
or No ☒

Indicate by check mark whether the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ☐ or No ☒

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 ☒ or No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☐

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 "accelerated filer, large accelerated filer, and smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer ☐ Accelerated Filer ☐ Non-Accelerated Filer ☐ 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 ☒

The aggregate market value of the common stock held by non-affiliates was \$15.9 million as of June 30, 2007 (the last business day of our most recently completed second fiscal quarter). The closing price of the common stock on that date was \$1.49 as reported by the NASDAQ Capital Market. For purposes of this determination, we excluded the shares of common stock held by each officer and director and by each person who owns 5% or more of the outstanding common stock. The exclusion of shares owned by the aforementioned individuals and entities from this calculation does not constitute an admission by any of such individuals or entities that he or it was or is an affiliate of ours.

We had 15,612,775 shares of common stock outstanding as of the close of business on February 29, 2008.

## **DOCUMENTS INCORPORATED BY REFERENCE**

Item 5 of Part II and Items 10, 11, 12, 13 and 14 of Part III incorporate information by reference from the definitive proxy statement for the Registrant's 2008 Annual Meeting of Stockholders.

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# SUPERCONDUCTOR TECHNOLOGIES INC.

## FORM 10-K ANNUAL REPORT

Year Ended December 31, 2007

*Unless otherwise noted, the terms “we,” “us,” “our” and “STI” refer to the combined and ongoing business operations of Superconductor Technologies Inc. and its subsidiaries*

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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. You can find many (but not all) of these statements by looking for words such as “approximates,” “believes,” “expects,” “anticipates,” “estimates,” “intends,” “plans,” “would,” “may” or other similar expressions in this Report. We claim the protection of the safe harbor contained in the Private Securities Litigation Reform Act of 1995. We caution investors that any forward-looking statements presented in this Report, or which we may make orally or in writing from time to time, are based on the beliefs of, 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 assets and a history of losses; limited number of potential customers; limited number of suppliers for some of our components; no significant backlog from quarter to quarter; our market is characterized by rapidly advancing technology. For further discussion of these and other factors see “Item 1A. Risk Factors” of this Report.*

*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.*

## **WHERE YOU CAN FIND MORE INFORMATION**

As a public company, we are required to file annually, quarterly and special reports, proxy statements and other information with the SEC. You may read and copy any of our materials on file with the SEC at the SEC’s Public Reference Room at 450 Fifth Street, N.W., Judiciary Plaza, Washington, DC 20549, as well as at the SEC’s regional office at 5757 Wilshire Boulevard, Suite 500, Los Angeles, California 90036. Our filings are available to the public over the Internet at the SEC’s website at <http://www.sec.gov>. Please call the SEC at 1-800-SEC-0330 for further information on the Public Reference Room. We also provide copies of our Forms 8-K, 10-K, 10-Q, Proxy and Annual Report at no charge to investors upon request and make electronic copies of our most recently filed reports available through our website at [www.suptech.com](http://www.suptech.com) as soon as reasonably practicable after filing such material with the SEC.

## PART I

### **ITEM 1. BUSINESS**

#### **Our Company**

We design, manufacture, market and sell high performance infrastructure products for wireless voice and data applications. Our products are utilized in major wireless networks throughout the United States which support voice and data communications by use of cell phones and other wireless communication devices.

Our 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. Our SuperLink utilizes patented high-temperature superconductor (HTS) technology to create a receiver front-end that enhances network performance. Today, we are leveraging our expertise and proprietary technology in radio frequency (RF) engineering to expand our product line beyond HTS technology. We believe our RF engineering expertise provides us with a significant competitive advantage in the development of high performance, cost-effective solutions for wireless telecommunications networks.

We currently sell most of our commercial products directly to wireless network operators in the United States. Our customers to date include ALLTEL, AT&T, Sprint Nextel, T-Mobile, and Verizon Wireless. We have a concentrated customer base. Verizon Wireless and AT&T each accounted for more than 10% of our commercial revenues in 2007 and Verizon Wireless, ALLTEL, and T-Mobile each accounted for more than 10% of our commercial revenues in 2006. We plan to continue to expand our customer base by selling directly to other wireless network operators and manufacturers of base station equipment, including internationally. During 2007, we formed a joint venture to gain access to the Chinese market.

*Industry Background.* The ability to provide high quality service to subscribers is becoming increasingly difficult for wireless operators as the number of users grows, minutes of use increase and the market for wireless data services expands. Wireless service providers in both rural and urban areas are encountering radio frequency interference due to greater subscriber density and a larger number of users on adjacent channels. This reduced signal quality and higher percentage of dropped calls can lead to lower system utilization, decreased revenue and, ultimately, higher rates of customer churn. Some service providers are also facing network capacity constraints.

As a result, wireless carriers are seeking to cost-effectively reduce interference, increase capacity, expand coverage to improve the quality of their systems and, utilize their spectrum in the most efficient manner possible.

*Our Solution.* We leverage our expertise in RF technology to cost effectively deliver interference protection and increased sensitivity to our wireless carrier customers. Our solutions provide the following quality-of-service improvements:

- reduction of dropped calls and network access failures;
- elimination of interference from other sources such as specialized mobile radio handsets and other base stations;
- increased in-building penetration;
- reduction in base station noise figure; and
- improved handset power consumption

*Our Products.* Our solutions consist of the following three product lines:

- *SuperLink* combines HTS filters with a proprietary cryogenic cooler and an ultra low-noise amplifier to create a highly compact and reliable receiver front-end that can simultaneously deliver both high selectivity (interference rejection) and high sensitivity (detection of low level signals).

- *AmpLink* is a ground-mounted unit which includes a high-performance amplifier that provides increased sensitivity.
- *SuperPlex* is a line of multiplexers that provides extremely low insertion loss and excellent cross-band isolation.

*Our Strategy.* Our objective is to provide a full range of performance improvement solutions to wireless carriers by offering our field-proven solutions, innovative duplexer designs for antenna sharing and network overlays, ground-based sensitivity improvement solutions and high-performance multiplexers. The primary elements of our strategy include:

- diversifying our customer base,
- expanding our current product offerings,
- enhancing our productivity and lowering our costs,
- maintaining our focus on technical excellence and innovation, and
- pursuing strategic partnerships, alliances and acquisitions.

*Government Contracts.* We also generate significant revenues from government contracts. We primarily pursue government research and development contracts which complement our commercial product development, but we also pursue government product opportunities. We undertake government contract work which has the potential to add to or improve our commercial product line. These contracts often yield valuable intellectual property relevant to our commercial business. We typically own the intellectual property developed under these contracts, and the Federal Government receives a royalty-free, non-exclusive and nontransferable license to use the intellectual property in the United States.

*Corporate Information.* Our facilities and executive offices are located at 460 Ward Drive, Santa Barbara, California 93111, and our telephone number is (805) 690-4500. We were incorporated in Delaware on May 11, 1987. Additional information about us is available on our website at [www.suptech.com](http://www.suptech.com). The information on our web site is not incorporated herein by reference.

### **Our Wireless Products**

Wireless service providers can use our solutions to keep pace with the growing demand for wireless communications. Wireless providers may deploy our products in connection with the installation of additional base stations in a network, as well as with the installation of an entirely new network. Wireless service providers can also improve the performance of existing base stations and networks by retrofitting their equipment with our link enhancement products.

Our performance improvement solutions fit into three product families: SuperLink, AmpLink and SuperPlex.

- *SuperLink.* In order to receive uplink signals from wireless handsets, base stations require a filter system to eliminate out-of-band interference, and amplification to enhance the base station's sensitivity. To address this need, we offer the SuperLink product line for the receiver front-end of base stations. These products combine specialized filters using HTS technology with a proprietary cryogenic cooler and ultra low-noise amplifiers. The result is a highly compact and reliable receiver front-end that can simultaneously deliver both high selectivity (interference rejection) and high sensitivity (detection of low level signals). SuperLink products offer significant performance advantages over conventional filter and amplifier systems.
- *AmpLink.* AmpLink is designed to address the sensitivity requirements of wireless base stations. AmpLink is a ground-mounted unit which utilizes a high-performance amplifier. The enhanced uplink performance provided by AmpLink improves network coverage immediately and avoids the installation and maintenance costs associated with tower mounted alternatives.
- *SuperPlex.* SuperPlex is our line of multiplexers that provides extremely low insertion loss and excellent cross-band isolation. Products in our SuperPlex family of high-performance multiplexers are designed to facilitate base station antenna sharing and reduce infrastructure costs. SuperPlex can be used in conjunction



with AmpLink and SuperLink products to optimize performance in networks where 1900 MHz EV-DO capabilities are added to existing 850 MHz networks. Relative to competing technologies, this portfolio of STI solutions offers increased transmit power delivered to the base station antenna, higher sensitivity to subscriber handset signals, interference rejection and fast and cost-effective network overlays.

### **Marketing and Sales**

We sell solutions to wireless communication service providers in the United States and pursue selected international opportunities.

We have a concentrated customer base. Verizon Wireless and AT&T each accounted for more than 10% of our commercial revenues in 2007; Verizon Wireless, ALLTEL and T-Mobile each accounted for more than 10% of our commercial revenues in 2006 and 2005. We sell using a direct sales force in the U.S. to focus on the Tier I wireless carriers. We use indirect channels to market our products to select customers internationally.

We demonstrate our products at trade shows, and participate in industry conferences. Advertising, email campaigns, direct mailings, and contribution of technical and application reports to recognized trade journals, are all employed to communicate our solutions to potential customers. We also advertise our products through our website, brochures, data sheets, application notes, trade journal reports and press releases.

Our sales and marketing efforts are complemented by a team of sales applications engineers who manage field trials and initial installations, as well as provide ongoing pre- and post-sales support.

Our marketing efforts are focused on establishing and developing long-term relationships with potential customers. The initial sales cycle for our solutions can be lengthy, typically ranging from six months to twelve months. Our customers typically conduct significant technical evaluations of products before making purchase commitments. We typically negotiate general purchase agreements with our customers. These agreements specify the terms and conditions for the business relationship with our customers. Standard purchase orders are subject to cancellation, postponement or other types of delays.

We purchase inventory components and manufacture inventory based on sales forecasts.

### **Backlog**

Our commercial backlog consists of accepted product purchase orders with scheduled delivery dates during the next twelve months. We had commercial backlog of \$352,000 at December 31, 2007, as compared to \$75,000 at December 31, 2006.

### **How We Use Government Contracts to Fund Technology Development**

Our strategy is to continue to pursue government research and development contract awards which complement our commercial product and technology development and allow for commercialization of the underlying technology. Since our inception in 1987, a substantial part of our revenues have been from research and development contracts with the U.S. government or as a subcontractor to a supplier to the U.S. government. Nearly all of these revenues were paid under contracts with the U.S. Department of Defense. We interact with various government agencies to identify opportunities and actively solicit partners for product development proposals. Since 1988, we have successfully obtained a number of classified and non-classified government contracts for superconductor research, including one of the largest non-classified HTS awards from the Defense Advanced Research Projects Agency (DARPA) through the Office of Naval Research. In addition to actively soliciting government contracts, we have participated in the Small Business Innovative Research, (SBIR) and Small Business Technology Transfer (STTR) programs. We have been awarded 34 Phase I SBIR/STTR contracts, each of which typically generates up to \$100,000 in revenues. We have been successful in converting nine of these Phase I contracts into Phase II programs, each of which typically generates up to \$750,000 in revenues, and we converted one of these contracts into a Phase III program valued at \$2.2 million. Since our formation, government contracts have provided us approximately \$98 million of revenue and remain a significant source of revenue today. We also develop and sell RF transceiver front-end products that utilize our unique HTS filter and cryogenics technologies to the US Government and we intend to continue growing this government products business.

**Our Manufacturing Capabilities**

Our manufacturing process involves the assembly of numerous individual components and precision tuning by production technicians. The parts and materials used by us and our contract manufacturers consist primarily of printed circuit boards, specialized subassemblies, fabricated housing, relays and small electric circuit components, such as integrated circuits, semiconductors, resistors and capacitors. Principal components of our AmpLink and SuperPlex products are produced by foreign manufacturers. We currently manufacture our SuperLink systems at our facilities in Santa Barbara, California.

In 1998, we opened a state-of-the-art manufacturing facility in Santa Barbara. We renovated these manufacturing areas in early 2003, the first in a series of moves that have enabled us to produce larger quantities of our SuperLink products. In 2003 and 2004, we expanded our controlled clean rooms, continued to develop and introduce new, state-of-the-art production and test equipment and processes, and implemented a continuous flow manufacturing strategy. In addition, performance testing and systems screening methods, along with optimized quality improvement techniques, have been instrumental in enabling our SuperLink units to reach Mean Time Between Failure (MTBF) levels of more than 500,000 hours.

We have the physical infrastructure to manufacture up to 2,800 SuperLink units per year. This capacity is unchanged from the prior year. We are holding physical capacity and staffing at their current levels to conserve cash resources. We could expand manufacturing capacity to approximately 5,000 units per year in our current facility with minor additional equipment purchases and staffing increases.

Our internal capabilities include a proprietary manufacturing process for thin-film materials that is scaleable for high volume production. In addition, we have established a production operation that we use to produce thin films on wafers for wireless applications. Our radio frequency circuitry is designed, modeled and tested by internal engineering resources. We have in-house capabilities to pattern the superconducting material and all other aspects of radio frequency component production, including packaging the filters. We also have in-house capabilities to manufacture our cryogenic coolers. We have refined our supplier base to improve the quality of received parts, while lowering the cost and decreasing lead-times.

In early 2006, we launched our high volume AmpLink assembly and distribution center within the existing Santa Barbara site. The 3,200 square foot production facility has the capacity to produce 10,000 AmpLink units annually which can be increased to 20,000 units with no additional capital expenditure. The production line is supported by a newly refurbished 8,000 square foot warehouse and distribution center. The manufacturing and distributions centers are tightly linked to provide the most efficient and rapid order fulfillment capabilities for up to 200 AmpLink units per week.

A number of the parts used in our products are available from only one or a limited number of outside suppliers due to unique component designs as well as certain quality and performance requirements.

**Intellectual Property**

We rely upon trade secrets and patents to protect our intellectual property. We execute confidentiality and non-disclosure agreements with our employees and suppliers and limit access to, and distribution of, our proprietary information. We have an on-going program to identify and file applications for both U.S. and international patents for various aspects of our technology. We regard our product designs, design tools, fabrication equipment and manufacturing processes as proprietary and seek to protect our rights in them through a combination of patent, trademark, trade secret and copyright law and internal procedures and non-disclosure agreements. We also seek licenses from third parties for HTS materials and processes used by us, which have been patented by other parties. We believe that our success will depend, in part, on the protection of our proprietary information, patents and the licensing of key technologies from third parties.

We have an extensive patent portfolio for the technology relevant to our SuperLink products, government products and related business. As of December 31, 2007, we held 53 U.S. patents in the following categories which are currently relevant to this business:

- 6 patents for technologies directed toward producing thin-film materials and structures expiring in 2010 to 2024;
- 26 patents for cryogenic and non-microwave circuit designs expiring in 2010 to 2024;
- 16 patents covering cryogenics, packaging and systems expiring in 2013 to 2024; and
- 5 patents covering other superconducting technologies expiring in 2013 to 2015.

We also had 24 U.S. patent applications pending as of December 31, 2007 which are currently relevant to our business. As of that date, we held 14 foreign issued patents and 31 foreign patents pending.

We have trade secrets, unpatented technology and proprietary knowledge about the sale, promotion, operation, development and manufacturing of our products. We have confidentiality agreements with our employees and consultants to protect these rights.

We own federally registered trademarks to Superconductor Technologies, Conductus and Improving the Quality of Wireless and have several other trademark registrations pending. We own other registered and unregistered trademarks, and have certain trademark rights in foreign jurisdictions.

From time to time we grant licenses for our technology to other companies for fields of use that are not relevant to our business. Specifically, we have granted licenses to, among others, (1) Bruker for Nuclear Magnetic Resonance application, (2) General Dynamics for government applications and (3) Star Cryoelectronics for Superconducting Quantum Interference Device applications, among others.

We use superconducting technology in our SuperLink solution to improve both the selectivity (rejection of adjacent band interference) and the sensitivity (ability to “hear” signals better) of a base station receiver. Superconducting materials have the ability to conduct electrical energy with little or no resistance when cooled to “critical” temperatures. In contrast, electric currents that flow through conventional conductors encounter resistance that requires power to overcome and generates heat. Substantial improvement in the performance characteristics of electrical systems can be made with superconductors, including reduced power loss, lower heat generation and decreased electrical noise. As these properties have been applied to radio and microwave frequency applications, new products, such as wireless filters, have been developed that are extremely small, highly sensitive and highly frequency selective.

The discovery of superconductors was made in 1911. However, a fundamental understanding of the phenomenon of superconductivity eluded physicists until J. Robert Schrieffer (a former director and Chairman of our Technical Advisory Board), John Bardeen (co-inventor of the transistor) and Leon Cooper proposed a theory explaining superconductivity, for which they were awarded the Nobel Prize in Physics in 1972. Until 1986, all superconductor utilization was done at extremely low temperatures, below 23K (-250°C). Superconductors were not widely used in commercial applications because of the high cost and complexities associated with reaching and maintaining such low temperatures. In 1986, high temperature superconductors with critical temperatures greater than 30K (-243°C) were discovered. In early 1987, yttrium barium copper oxide (“YBCO”) was discovered, which has a critical temperature of 93K (-180°C). Shortly thereafter, thallium barium calcium copper oxide (“TBCCO”) was discovered, which has a critical temperature of 125K (-148°C). These discoveries were important because these high temperature superconductors allowed for operating temperatures higher than 77K (-196°C), or the point at which nitrogen liquefies at atmospheric pressure. These high critical temperatures allow superconductors to be cooled using less expensive and more efficient refrigeration processes. We were formed following this discovery for the initial purpose of developing and commercializing high temperature superconductors.

We have historically TBCCO as the primary HTS material in our SuperLink product line. In the fourth quarter of 2004, we shifted all of our production from TBCCO to YBCO to lower the product manufacturing cost of the SuperLink. We have a non-exclusive license in the U.S. and selected foreign countries to the primary patents on YBCO from Lucent and TBCCO from the University of Arkansas. We use HTS materials as the base material to

produce “thin film” microelectronics, primarily RF filters, in our SuperLink product line. We manufacture YBCO using proprietary processes, including proprietary manufacturing techniques. We believe that the process technology we have developed produces state of the art HTS thin-films of the highest quality using YBCO.

As part of our strategy to maintain our technological leadership, we have focused our research and development activities on HTS materials, RF circuitry, cryogenic design and product application. We utilize a proprietary manufacturing process for HTS thin-film production, the base material for our filtering products. An in-house design team develops the filters, which are packaged into a vacuum-sealed container for thermal insulation. The filter package is integrated with our cryogenic cooler and the necessary control electronics into a complete system that is deployed in conjunction with new or existing wireless base stations.

We have devoted a significant portion of our engineering resources to design and model the complex RF circuitry that is basic to our products. The expertise of this highly qualified team has allowed us to design and fabricate very precise individual components, such as RF signal filters. We have developed computer simulation systems to design our products and this RF circuitry design capability has allowed us to produce extremely small, high-performance circuits. Some of our design and engineering innovations have been patented; others are the subjects of pending patent applications. We believe that our RF engineering expertise provides us with a unique competitive advantage. These capabilities also allow us to begin pursuing additional market segments, such as in the area of handset filters.

The availability of a low-cost, highly reliable, compact cooling technology is critical to the successful commercialization of our superconducting products. Prior to our efforts, no such cryogenic cooler had been commercially available. In response to this lack of availability, we developed a low-cost, highly reliable low-power cooler designed to cool to 77K (-196°C) with sufficient cooling capacity for our superconducting applications. Our SuperLink systems have logged in excess of 200 million hours of cumulative operation. The cryogenic coolers in our current models have demonstrated a “mean time between failure” (the industry standard measurement) of greater than one million hours. The design was based in part on patents licensed by us from Sunpower, Inc. We believe our internally developed cooler, which is both compact enough and reliable enough to meet the most demanding wireless industry standards, provides us with a significant and unique competitive advantage.

Cooling to cryogenic temperatures requires proper thermal isolation and packaging. Any superconducting or other cryogenically cooled device must be maintained at its optimal operating temperature, and its interaction with higher temperature components must be controlled. We have developed a variety of proprietary and patented cryogenic packaging innovations to satisfy this requirement.

## Competition

The wireless communication market is intensely competitive. We face competition in various aspects of our technology and product development and in each of our target markets. Our products compete on the basis of performance, functionality, reliability, pricing, quality, and compliance with industry standards. Our current and potential competitors include conventional RF filter manufacturers and both established and newly emerging companies developing similar or competing HTS technologies. We also compete with companies that design, manufacture and sell antenna-optimizing multiplexers and companies that seek to enhance base station range and selectivity by means other than a superconducting filter. The primary competitors use tower mounted and ground mounted amplifiers, conventional filters, repeaters or “smart antenna” technologies. Tower mounted and ground mounted amplifiers pass an RF signal received by an antenna through a broad filter, followed by a low noise amplifier. These units are produced by a number of companies, which include most of the base station original equipment manufacturers (OEMs) such as Ericsson and Nokia. Filter manufacturers, including Andrew, Powerwave, and Radio Frequency Systems, also produce these units. Smart antennas allow base stations to focus energy more directly on individual wireless devices in order to improve capacity. Some competitors have significantly greater financial, technical, manufacturing, sales, marketing and other resources. Some competitors have achieved greater name recognition for their products and technologies.

In addition, we currently supply components and license technology to several companies that may eventually decide to manufacture or design their own HTS components, rather than purchasing or licensing our technology. With respect to our HTS materials, we compete with THEVA among others. In the government sector, we compete

with universities, national laboratories and both large and small companies for research and development contracts, and with larger defense contractors, such as Raytheon and Northrop Grumman for government products.

### Employees

We employed a total of 129 people as of December 31, 2007: 54 in manufacturing, 35 in research and development, 19 in sales and marketing and 21 in administration. Nine of our employees have Ph.D.s, and fourteen others hold advanced degrees in physics, materials science, electrical engineering and other fields. Our employees are not represented by a labor union and we believe that our employee relations are good.

### Environmental Issues

We use certain hazardous materials in our research, development and manufacturing operations. As a result, we are subject to stringent federal, state and local regulations governing the storage, use and disposal of such materials. Current or future laws and regulations could require substantial expenditures for preventative or remedial action, reduction of chemical exposure, waste treatment or disposal. Although we believe that our safety procedures for the handling and disposing of hazardous materials comply with the standards prescribed by state and federal regulations, there is always the risk of accidental contamination or injury from these materials. To date, we have not incurred substantial expenditures for preventive action with respect to hazardous materials or for remedial action with respect to any hazardous materials accident, but the use and disposal of hazardous materials involves the risk that we could incur substantial expenditures for such preventive or remedial actions. If such an accident occurred, we could be held liable for resulting damages. The liability in the event of an accident or the costs of such remedial actions could exceed our resources or otherwise have a material adverse effect on our financial condition, results of operations or cash flows.

### ITEM 1A. RISK FACTORS

The following section includes some of the material factors that may adversely affect our business and operations. This is not an exhaustive list, and additional factors could adversely affect our business and financial performance. Moreover, we operate in a very competitive and rapidly changing environment. New risk factors emerge from time to time and it is not possible for us to predict all such risk factors, nor can we assess the impact of all such risk factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements. This discussion of risk factors includes many forward-looking statements. For cautions about relying on such forward looking statements, please refer to the section entitled "Forward Looking Statements" at the beginning of this Report immediately prior to Item 1.

#### Risks Related to Our Business

***We have a history of losses and may never become profitable.***

In each of our last five years, we have experienced significant net losses and negative cash flows from operations. If we fail to increase our revenues, we may not achieve and maintain profitability and may not meet our expectations or the expectations of financial analysts who report on our stock.

***We may need to raise additional capital, and if we are unable to raise capital our ability to implement our current business plan and ultimately our viability as a company could be adversely affected.***

In 2007, we incurred a net loss of \$9.1 million and had negative cash flows from operations of \$5.4 million. In 2006, we incurred a net loss of \$29.6 million and had negative cash flows from operations of \$7.3 million. Our independent registered public accounting firm has included in their audit report for fiscal 2007 and 2006 an explanatory paragraph expressing doubt about our ability to continue as a going concern. Our prior independent registered public accounting firm included a similar explanatory paragraph in their audit report for 2005.

Our principal sources of liquidity consist of existing cash balances and funds expected to be generated from future operations. We believe one of the key factors to our liquidity will be our ability to successfully execute on our

plans to increase sales levels in a highly concentrated industry where we experience significant fluctuations in sales from quarter to quarter. Our cash requirements will also depend on numerous other variable factors, including the rate of growth of sales, the timing and levels of products purchased, payment terms and credit limits from manufacturers, and the timing and level of accounts receivable collections.

At December 31, 2007 we had \$3.9 million in cash and in January 2008 we received the remaining \$11.0 million from our investment agreement with Hunchun BaoLi Communication Co. Ltd., or BAOLI, whereby in exchange for \$15.0 million in cash we issued to BAOLI and two related purchasers a total of (a) 3,101,361 shares of our common stock and (b) 611,523 shares of our Series A Preferred Stock (convertible under certain conditions into 6,115,230 shares of our common stock). If actual cash flows deviate significantly from forecasted amounts or if we believe operations require additional funding we cannot assure you that additional financing will be available on acceptable terms or at all.

If we issue additional equity securities to raise funds, the ownership percentage of our existing stockholders would be reduced. New investors may demand rights, preferences or privileges senior to those of existing holders of common stock. If we cannot raise any needed funds, it 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.

***We rely on a small number of customers for the majority of our commercial revenues and the loss of any one of these customers, or a significant loss, reduction or rescheduling of orders from any of these customers, could have a material adverse effect on our business, results of operations and financial condition.***

We sell most of our products to a small number of wireless carriers. We derived 75% of our commercial product revenues from Verizon Wireless and AT&T in 2007 and 96% of our commercial product revenues from ALLTEL, Verizon Wireless and T-Mobile in 2006. Our future success depends upon the wireless carriers continuing to purchase our products, and fluctuations in demand from such customers could negatively impact our results. Unanticipated demand fluctuations can have a negative impact on our revenues and business and an adverse effect on our results of operations and financial condition.

In addition, our dependence on a small number of major customers exposes us to numerous other risks, including:

- a slowdown or delay in the deployment, upgrading or improvement of wireless networks by any one customer could significantly reduce demand for our products;
- reductions in a single customer's forecasts and demand could result in excess inventories;
- each of our customers have significant purchasing leverage over us to require changes in sales terms including pricing, payment terms and product delivery schedules; and
- concentration of accounts receivable credit risk, which could have a material adverse effect on our liquidity and financial condition if one of our major customers declared bankruptcy or delayed payment of their receivables.

Many of our customers also provide minimal lead-time prior to the release of their purchase orders and have non-binding commitments to purchase from us. If we fail to forecast our customer's demands accurately, we could experience delays in manufacturing which could result in customer dissatisfaction. Additionally, these factors further impact our ability to forecast future revenue.

***The wireless communication industry is highly concentrated, which limits the number of potential customers, and further industry consolidation could result in the loss of key customers.***

The wireless communication industry is highly concentrated in nature and may become more concentrated due to anticipated industry consolidation. As a result, we believe that the number of potential customers for our products



may be limited. We also face significant risks in the event any of our key customers is acquired by a company that has not adopted our technology or not adopted it to the same extent. In that event, we could face a significant decline in our sales to the acquired customer.

***We experience significant fluctuations in sales and operating results from quarter to quarter.***

Our quarterly results fluctuate due to a number of factors, including:

- the lack of any contractual obligation by our customers to purchase their forecasted demand for our products;
- variations in the timing, cancellation, or rescheduling of customer orders and shipments; and
- high fixed expenses that may disproportionately impact operating expenses, especially during a quarter with a sales shortfall.

The nature of our business requires that we promptly ship products after we receive orders. This means that we typically do not have a significant backlog of unfilled orders at the start of each quarter. We have also regularly generated a large percentage of our revenues in the last month of a quarter. Our major customers generally have no contractual obligation to purchase forecasted amounts and may cancel orders, change delivery schedules or change the mix of products ordered with minimal notice and minimal penalty. As a result of these factors, we may not be able to accurately predict our quarterly sales. Any shortfall in sales relative to our quarterly expectations or any delay of customer orders would adversely affect our revenues and results of operations.

Order deferrals and cancellations by our customers, declining average sales prices, changes in the mix of products sold, increases in inventory and finished goods, delays in the introduction of new products and longer than anticipated sales cycles for our products have, in the past, adversely affected our results of operations. Despite these factors, we maintain significant finished goods, work-in-progress and raw materials inventory to meet estimated order forecasts. If our customers purchase less than the forecasted amounts or cancel or delay existing purchase orders, there will be higher levels of inventory that face a greater risk of obsolescence. If our customers desire to purchase products in excess of the forecasted amounts or in a different product mix, there may not be enough inventory or manufacturing capacity to fill their orders.

Due to these and other factors, our past results may not be reliable indicators of our future performance. Future revenues and operating results may not meet the expectations of stock analysts and investors. In either case, the price of our common stock could be materially adversely affected.

***Our sales cycles are unpredictable, making future performance uncertain.***

The sales cycle for telecommunications products includes identification of decision makers within the customers' organizations, development of an understanding of customer-specific performance and economic issues, convincing the customer through field trial reports of the benefits of systems offered, negotiation of purchase orders and deployment. Customers who purchase our systems must commit a significant amount of capital and other resources. Our customers must consider budgetary constraints, comply with internal procedures for approving large expenditures and complete whatever testing is necessary for them to integrate new technologies that will impact their key operations. Customer delays can lengthen the sales cycles and have a material adverse effect on our business.

***We depend on the capital spending patterns of wireless network operators, and if capital spending is decreased or delayed, our business may be harmed.***

Because we rely on wireless network operators for product purchases, any substantial decrease or delay in capital spending patterns in the wireless communication industry may harm our business. Demand from customers for our products depends to a significant degree upon the amount and timing of capital spending by these customers for constructing, rebuilding or upgrading their systems. The capital spending patterns of wireless network operators depend on a variety of factors, including access to financing, the status of federal, local and foreign government regulation and deregulation, changing standards for wireless technology, overall demand for wireless services, competitive pressures and general economic conditions. In addition, capital spending patterns in the wireless

industry can be subject to some degree of seasonality, with lower levels of spending in the first and third calendar quarters, based on annual budget cycles.

***Our reliance on a limited number of suppliers and the long lead time of components for our products could impair our ability to manufacture and deliver our systems on a timely basis.***

A number of components used in our products are available from only one or a limited number of outside suppliers due to unique designs as well as certain quality and performance requirements. We currently purchase substrates for growth of high-temperature superconductor thin-films from a single supplier because of the quality of their substrates. A thin film is a thin layer of high-temperature superconductor material. There are additional components that we source from a single vendor due to the present volume. Key components of our conventional products are manufactured by sole foreign manufacturer. Our reliance on sole or limited source suppliers involves certain risks and uncertainties, many of which are beyond our control. These include the possibility of a shortage or the discontinuation of certain key components. Any reduced availability of these parts or components when required could impair our ability to manufacture and deliver our systems on a timely basis and result in the delay or cancellation of orders, which could harm our business.

In addition, the purchase of some of our key components involves long lead times and, in the event of unanticipated increases in demand for our solutions, we may be unable to obtain these components in sufficient quantities to meet our customers' requirements. We do not have guaranteed supply arrangements with any of these suppliers, do not maintain an extensive inventory of parts or components and customarily purchase sole or limited source parts and components pursuant to purchase orders. Business disruptions, quality issues, production shortfalls or financial difficulties of a sole or limited source supplier could materially and adversely affect us by increasing product costs, or eliminating or delaying the availability of such parts or components. In such events, our inability to develop alternative sources of supply quickly and on a cost-effective basis could impair our ability to manufacture and deliver our systems on a timely basis and could harm our business.

***Our reliance on a limited number of suppliers exposes us to quality control issues.***

Our reliance on certain single-source and limited-source components exposes us to quality control issues if these suppliers experience a failure in their production process or otherwise fail to meet our quality requirements. A failure in single-source or limited-source components or products could force us to repair or replace a product utilizing replacement components. If we cannot obtain comparable replacements or effectively return or redesign our products, we could lose customer orders or incur additional costs, which could have a material adverse effect on our gross margins and results of operations.

***We expect decreases in average selling prices, requiring us to reduce product costs in order to achieve and maintain profitability.***

The average selling price of our products has decreased over the years. We anticipate customer pressure on our product pricing will continue for the foreseeable future. We have plans to further reduce the manufacturing cost of our products, but there is no assurance that our future cost reduction efforts will keep pace with price erosion. We will need to further reduce our manufacturing costs through engineering improvements and economies of scale in production and purchasing in order to achieve adequate gross margins. We may not be able to achieve the required product cost savings at a rate needed to keep pace with competitive pricing pressure. Additionally, we may be forced to discount future orders. If we fail to reach our cost saving objectives or we are required to offer future discounts, our business may be harmed.

***Our ability to protect our patents and other proprietary rights is uncertain, exposing us to possible losses of competitive advantage.***

Our efforts to protect our proprietary rights may not succeed in preventing infringement by others or ensure that these rights will provide us with a competitive advantage. Pending patent applications may not result in issued patents and the validity of issued patents may be subject to challenge. Third parties may also be able to design around the patented aspects of the products. Additionally, certain of the issued patents and patent applications are



owned jointly with third parties. Because any owner or co-owner of a patent can license its rights under jointly-owned patents or applications, inventions made by us jointly with others are not subject to our exclusive control. Any of these possible events could result in losses of competitive advantage.

***We depend on specific patents and licenses to technologies, and we will likely need additional technologies in the future that we may not be able to obtain.***

We utilize technologies under licenses of patents from others for our products. These patents may be subject to challenge, which may result in significant litigation expense (which may or may not be recoverable against future royalty obligations). Additionally, we continually try to develop new products, and, in the course of doing so, we may be required to utilize intellectual property rights owned by others and may seek licenses to do so. Such licenses may not be obtainable on commercially reasonable terms, or at all. It is also possible that we may inadvertently utilize intellectual property rights held by others, which could result in substantial claims.

***Intellectual property infringement claims against us could materially harm results of operations.***

Our products incorporate a number of technologies, including high-temperature superconductor technology, technology related to other materials, and electronics technologies. Our patent positions, and that of other companies using high-temperature superconductor technology, is uncertain and there is significant risk that others, including our competitors or potential competitors, have obtained or will obtain patents relating to our products or technologies or products or technologies planned to be introduced by us.

We believe that patents may be or have been issued, or applications may be pending, claiming various compositions of matter used in our products. We may need to secure one or more licenses of these patents. There can be no assurances that such licenses could be obtained on commercially reasonable terms, or at all. We may be required to expend significant resources to develop alternatives that would not infringe such patents or to obtain licenses to the related technology. We may not be able to successfully design around these patents or obtain licenses to them and may have to defend ourselves at substantial cost against allegations of infringement of third party patents or other rights to intellectual property. In those circumstances, we could face significant liabilities and also be forced to cease the use of key technology.

***We currently rely on specific technologies and may not successfully adapt to the rapidly changing wireless telecommunications equipment market.***

Wireless telecommunication equipment is characterized by rapidly advancing technology. Our success depends upon our ability to keep pace with advancing wireless technology, including materials, processes and industry standards. For example, we had to redesign our SuperLink product to convert from thallium barium calcium copper oxide to yttrium barium copper oxide in order to reduce the product cost and compete with other technologies. However, even with the lower cost HTS material, SuperLink may not ultimately prove commercially competitive against other current technologies or those that may be discovered in the future.

We will have to continue to develop and integrate advances to our core technologies. We will also need to continue to develop and integrate advances in complementary technologies. We cannot guarantee that our development efforts will not be rendered obsolete by research efforts and technological advances made by others.

***Other parties may have the right to utilize technology important to our business.***

We utilize certain intellectual property rights under non-exclusive licenses or have granted to others the right to utilize certain intellectual property rights licensed from a third party. Because we may not have the exclusive rights to utilize such intellectual property, other parties may be able to compete with us, which may harm our business.

***Our failure to anticipate and respond to developments in the wireless telecommunications market could substantially harm our business.***

Our efforts are focused on the wireless telecommunications market, including the 2G, 2.5G and 3G markets. The dedication of our resources to the wireless telecommunications market makes us potentially vulnerable to

changes in this market, such as new technologies like WIMAX, future competition, changes in availability of capital resources or regulatory changes that could affect the competitive position and rate of growth of the wireless industry.

***We may not be able to compete effectively against alternative technologies.***

Our products compete with a number of alternative approaches and technologies that increase the capacity and improve the quality of wireless networks. Some of these alternatives may be more cost effective or offer better performance than our products. Wireless network operators may opt to increase the number of transmission stations, increase tower heights, install filters and amplifiers at the top of towers or use advanced antenna technology in lieu of purchasing our products. We may not succeed in competing against these alternatives.

***We depend upon government contracts for a substantial amount of revenue and our business may suffer if significant contracts are terminated, adversely modified, or we are unable to win new contracts.***

We derive a portion of our revenue from a few large contracts with the U.S. government. As a result, a reduction in, or discontinuance of, the government's commitment to current or future programs could materially reduce government contract revenue.

Contracts involving the U.S. government may include various risks, including:

- termination by the government;
- reduction or modification in the event of changes in the government's requirements or budgetary constraints;
- increased or unexpected costs causing losses or reduced profits under contracts where prices are fixed or unallowable costs under contracts where the government reimburses for costs and pays an additional premium;
- risks of potential disclosure of confidential information to third parties;
- the failure or inability of the main contractor to perform its contract in circumstances where we are a subcontractor;
- the failure of the government to exercise options for additional work provided for in the contracts; and
- the government's right in certain circumstances to freely use technology developed under these contracts.

The programs in which we participate may extend for several years, but are normally funded on an annual basis. The U.S. government may not continue to fund programs under which we have entered into contracts. Even if funding is continued, we may fail to compete successfully to obtain funding within such programs.

All costs for services under government contracts are subject to audit, and the acceptance of such costs as allowable and allocable is subject to federal regulatory guidelines. We record contract revenues in amounts which we expect to be realized upon final audit settlement. Any disallowance of costs by the government could have an adverse effect on our business, operating results and financial condition. Audits and adjustments may result in decreased revenues and net income for those years. Additionally, because of our participation in government contracts, we are subject to audit from time to time for our compliance with government regulations by various agencies. Government agencies may conduct inquiries or investigations that may cover a broad range of activity. Responding to any such audits, inquiries or investigations may involve significant expense and divert management's attention. In addition, an adverse finding in any such audit, inquiry or investigation could involve penalties that may harm our business.

***Because competition for target employees is intense, we may be subject to claims of unfair hiring practices, trade secret misappropriation or other related claims.***

Companies in the wireless telecommunications industry whose employees accept positions with competitors frequently claim that competitors have engaged in unfair hiring practices, trade secret misappropriation or other related claims. We may be subject to such claims in the future as we seek to hire qualified personnel, and such

claims may result in material litigation. If this should occur, we could incur substantial costs in defending against these claims, regardless of their merits.

***If we are unable to forecast our inventory needs accurately, we may be unable to obtain sufficient manufacturing capacity or may incur unnecessary costs and produce excess inventory.***

We forecast our inventory needs based on anticipated purchase orders to determine manufacturing requirements. If we overestimate demand, we may have excess inventory, and our suppliers may as well, which could increase our costs. If we underestimate our requirements, our suppliers may have inadequate inventory, which could interrupt manufacturing and result in delays in shipments and recognition of revenues. In addition, lead times for ordering materials and components vary significantly and depend on factors such as the specific supplier, contract terms and demand for any component at a given time. Accordingly, if we inaccurately forecast demand, we may be unable to obtain adequate manufacturing capacity from our suppliers to meet customers' delivery requirements, which would harm our business.

***Our success depends on the attraction and retention of senior management and technical personnel with relevant expertise.***

As a competitor in a highly technical market, we depend heavily upon the efforts of our existing senior management and technical teams. The loss of the services of one or more members of these teams could slow product development and commercialization objectives. Due to the specialized nature of our products, we also depend upon our ability to attract and retain qualified technical personnel with substantial industry knowledge and expertise. Competition for qualified personnel is intense and we may not be able to continue to attract and retain qualified personnel necessary for the development of our business.

We have experienced difficulty recruiting senior management due to the high cost of living in the Santa Barbara area. We have a limited pool of qualified executives in Santa Barbara and may attempt to recruit qualified candidates from across the country. Some candidates have cited the high cost of housing in Santa Barbara as a significant negative factor when considering our employment offers. We have mitigated this problem to a limited extent by allowing some executives to maintain their existing residences in other parts of the country and effectively "commute" to our corporate headquarters in Santa Barbara as needed to perform their duties. Regardless, we expect the cost of housing in our area will continue to present a significant obstacle to recruiting senior executives.

***Regulatory changes negatively affecting wireless communications companies could substantially harm our business.***

The Federal Communications Commission strictly regulates the operation of wireless base stations in the United States. Other countries also regulate the operation of base stations within their territories. Base stations and equipment marketed for use in base stations must meet specific technical standards. Our ability to sell our high-temperature superconductor filter subsystems will depend upon the rate of deployment of other new wireless digital services, the ability of base station equipment manufacturers and of base station operators to obtain and retain the necessary approvals and licenses, and changes in regulations that may impact the product requirements. Any failure or delay of base station manufacturers or operators in obtaining necessary approvals could harm our business.

***We may acquire or make investments in companies or technologies that could cause loss of value to stockholders and disruption of business.***

We may explore opportunities to acquire companies or technologies in the future. Other than the acquisition of Conductus, Inc. in 2002, we have not made any such acquisitions or investments to date and, therefore, our ability as an organization to make acquisitions or investments is unproven. Entering into an acquisition entails many risks, any of which could adversely affect our business, including:

- failure to integrate operations, services and personnel;
- the price paid may exceed the value eventually realized;
- loss of share value to existing stockholders as a result of issuing equity securities to finance an acquisition;

- potential loss of key employees from either our then current business or any acquired business;
- entering into markets in which we have little or no prior experience;
- diversion of financial resources and management's attention from other business concerns;
- assumption of unanticipated liabilities related to the acquired assets; and
- the business or technologies acquired or invested in may have limited operating histories and may be subjected to many of the same risks to which we are exposed.

In addition, future acquisitions may result in potentially dilutive issuances of equity securities, or the incurrence of debt, contingent liabilities or amortization expenses or charges related to goodwill or other intangible assets, any of which could harm our business. As a result, if we fail to properly evaluate and execute acquisitions or investments, our business and prospects may be seriously harmed.

***If we are unable to implement appropriate controls and procedures to manage our expected growth, we may not be able to successfully offer our products and implement our business plan.***

Our ability to successfully offer our products and implement our business plan in a rapidly evolving market requires an effective planning and management process. Anticipated growth in future operations will continue to place a significant strain on management systems and resources. We expect that we will need to continue to improve our financial and managerial controls, reporting systems and procedures, and will need to continue to expand, train and manage our work force worldwide. Furthermore, we expect that we will be required to manage multiple relationships with various customers and other third parties.

***Compliance with environmental regulations could be especially costly due to the hazardous materials used in the manufacturing process.***

We are subject to a number of federal, state and local governmental regulations related to the use, storage, discharge and disposal of toxic, volatile or otherwise hazardous chemicals used in our business. Any failure to comply with present or future regulations could result in fines being imposed, suspension of production or interruption of operations. In addition, these regulations could restrict our ability to expand or could require us to acquire costly equipment or incur other significant expense to comply with environmental regulations or to clean up prior discharges.

***The reliability of market data included in our public filings is uncertain.***

Since we operate in a rapidly changing market, we have in the past, and may from time to time in the future, include market data from industry publications and our own internal estimates in some of the documents we file with the Securities Exchange Commission. The reliability of this data cannot be assured. Industry publications generally state that the information contained in these publications has been obtained from sources believed to be reliable, but that its accuracy and completeness is not guaranteed. Although we believe that the market data used in our SEC filings is and will be reliable, it has not been independently verified. Similarly, internal company estimates, while believed by us to be reliable, have not been verified by any independent sources.

***Our international operations expose us to certain risks.***

In November 2007, we signed a binding definitive agreement for a joint venture with BAOLI to manufacture and market our SuperLink<sup>®</sup> interference elimination solution for the China market. In addition to facing many of the risks faced by our domestic business, if that joint venture or any other international operation we may have is to be successful, we (together with any joint venture partner) must recruit the necessary personnel and develop the facilities needed to manufacture and sell the products involved, must learn about the local market (which may significantly differ from our domestic market), must build brand awareness among potential customers and must compete successfully with local organizations with greater market knowledge and potentially greater resources than we have. We must also obtain a number of critical governmental approvals from both the United States and the local country governments on a timely basis, including those related to any transfers of our technology. We must establish

sufficient controls on any foreign operations to ensure that those operations are operated in accordance with our interests, that our intellectual property is protected and that our involvement does not inadvertently create potential competitors. There can be no assurance that these conditions will be met. Even if they are met, the process of building our international operations could divert financial resources and management attention from other business concerns. Finally, our international operations will also be subject to the general risks of international operations, such as:

- changes in exchange rates;
- international political and economic conditions;
- changes in government regulation in various countries;
- trade barriers;
- adverse tax consequences; and
- costs associated with expansion into new territories.

### **Risks Related to Our Common Stock**

#### ***Our stock price is volatile.***

The market price of our common stock has been, and we expect will continue to be, subject to significant volatility. The value of our common stock may decline regardless of our operating performance or prospects. Factors affecting our market price include:

- our perceived prospects;
- variations in our operating results and whether we have achieved key business targets;
- changes in, or our failure to meet, earnings estimates;
- changes in securities analysts' buy/sell recommendations;
- differences between our reported results and those expected by investors and securities analysts;
- announcements of new contracts by us or our competitors;
- market reaction to any acquisitions, joint ventures or strategic investments announced by us or our competitors; and
- general economic, political or stock market conditions.

Recent events have caused stock prices for many companies, including ours, to fluctuate in ways unrelated or disproportionate to their operating performance. The general economic, political and stock market conditions that may affect the market price of our common stock are beyond our control. The market price of our common stock at any particular time may not remain the market price in the future.

#### ***We have a significant number of outstanding warrants and options, and future sales of these shares could adversely affect the market price of our common stock.***

As of December 31, 2007, we had outstanding warrants and options exercisable for an aggregate of 1,210,603 shares of common stock at a weighted average exercise price of \$25.92 per share. We have registered the issuance of all these shares, and they will be freely tradable by the exercising party upon issuance. The holders may sell these shares in the public markets from time to time, without limitations on the timing, amount or method of sale. As our stock price rises, the holders may exercise their warrants and options and sell a large number of shares. This could cause the market price of our common stock to decline.

***Our corporate governance structure may prevent our acquisition by another company at a premium over the public trading price of STI shares.***

It is possible that the acquisition of a majority of our outstanding voting stock by another company could result in our stockholders receiving a premium over the public trading price for our shares. Provisions of our restated certificate of incorporation and bylaws and of Delaware corporate law could delay or make more difficult an acquisition of our company by merger, tender offer or proxy contest, even if it would create an immediate benefit to our stockholders. For example, our restated certificate of incorporation does not permit stockholders to act by written consent and our bylaws generally require ninety days advance notice of any matters to be brought before the stockholders at an annual or special meeting.

In addition, our board of directors has the authority to issue up to 2,000,000 shares of preferred stock and to determine the terms, rights and preferences of this preferred stock, including voting rights of those shares, without any further vote or action by the stockholders. The rights of the holders of common stock may be subordinate to, and adversely affected by, the rights of holders of preferred stock that may be issued in the future. The issuance of preferred stock could also make it more difficult for a third party to acquire a majority of our outstanding voting stock, even at a premium over our public trading price.

Further, our certificate of incorporation also provides for a classified board of directors with directors divided into three classes serving staggered terms. These provisions may have the effect of delaying or preventing a change in control of STI without action by our stockholders and, therefore, could adversely affect the price of our stock or the possibility of sale of shares to an acquiring person.

***We do not anticipate declaring any cash dividends on our common stock.***

We have never declared or paid cash dividends on our common stock and do not plan to pay any cash dividends in the near future. Our current policy is to retain all funds and earnings for use in the operation and expansion of our business. In addition, our debt agreements prohibit the payment of cash dividends or other distributions on any of our capital stock except dividends payable in additional shares of capital stock.

**ITEM 1B. UNRESOLVED STAFF COMMENTS**

None.

**ITEM 2. PROPERTIES**

We lease all of our properties. All of our operations, including our manufacturing facility, are located in an industrial complex in Santa Barbara, California. We occupy approximately 71,000 square feet in this complex under a long-term lease that expires in 2011. We believe that our Santa Barbara facilities are adequate to meet current and reasonably anticipated needs for approximately the next two years.

**ITEM 3. LEGAL PROCEEDINGS**

**Settlement of Shalvoy Litigation**

Mr. Shalvoy, a director and stockholder, executed two notes aggregating \$820,244 in principal in connection with the exercise in December 2000 of two options to purchase Conductus, Inc. common stock prior our acquisition of Conductus, Inc. in December 2002. Through the third quarter of, 2005, we carried the principal (as "Notes Receivable from Stockholder") and accrued interest (as "Prepaid Expenses and Other Current Assets") for both notes as assets on our balance sheet.

We filed a lawsuit against Mr. Shalvoy on December 21, 2005 in the California Superior Court (Case No. 1186812) to collect both notes. In that same quarter, due to Mr. Shalvoy's refusal to pay the notes voluntarily we recorded a reserve for the value of the notes (principal plus accrued interest) in excess of the market value of the collateral securing the notes.

On March 2, 2007, we entered into a Settlement Agreement and Mutual Release of All Claims with Mr. Shalvoy to settle the lawsuit. As per the agreement, we received a payment of \$610,000 on April 2, 2007

in payment of one note, including interest and attorneys' fees, and the rescission of Mr. Shalvoy's second purported option exercise including cancellation of the related note.

### **Routine Litigation**

We may be involved in routine litigation arising in the ordinary course of our business, and, while the results of the proceedings cannot be predicted with certainty, we believe that the final outcome of such matters will not have a material adverse effect on our financial position, operating results or cash flow.

### **ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

Our 2007 Annual Meeting of Shareholders was held on October 23, 2007. The following matters were submitted to a vote of our shareholders:

1. Election of two Class 3 Directors. The following directors were elected to hold office until the 2010 Annual Meeting or until their successors are elected and qualified:

<u>Directors</u>	<u>Votes For</u>	<u>Votes Withheld</u>
John D. Lockton	10,279,801	210,743
David W. Vellequette	10,287,800	202,744

2. Approval to Amend the 2003 Equity Incentive Plan:

<u>In Favor Of</u>	<u>Against</u>	<u>Abstain</u>
2,425,588	148,018	18,737

3. Ratification of the appointment of Stonefield Josephson, Inc. as the Company's Independent Registered Public Accounting Firm for the year ending December 31, 2007.

<u>In Favor Of</u>	<u>Against</u>	<u>Abstain</u>
10,277,793	53,137	159,614

## **PART II**

### **ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES**

#### **Market for Common Stock**

Our common stock is traded on the NASDAQ Capital Market under the symbol "SCON." The following table shows the high and low intraday sales prices for our common stock as reported by NASDAQ for each calendar quarter in the last two fiscal years:

	<u>High</u>	<u>Low</u>
<b>2007</b>		
Quarter ended March 31, 2007	\$ 2.60	\$1.60
Quarter ended June 30, 2007	\$ 2.16	\$1.40
Quarter ended September 29, 2007	\$10.90	\$1.38
Quarter ended December 31, 2007	\$13.77	\$5.50
<b>2006</b>		
Quarter ended April 1, 2006	\$ 6.70	\$3.21
Quarter ended July 1, 2006	\$ 4.54	\$1.90
Quarter ended September 30, 2006	\$ 2.10	\$1.30
Quarter ended December 31, 2006	\$ 3.24	\$1.43



**Holders of Record**

We had 123 holders of record of our common stock on February 29, 2008. This number does not include stockholders for whom shares were held in a “nominee” or “street” name. We estimate that there are more than 15,000 round lot beneficial owners of our common stock.

**Dividends**

We have never paid cash dividends and intend to employ all available funds in the development of our business. We have no plans to pay cash dividends in the near future, and our line of credit does not allow the payment of dividends.

Our ability to declare or pay dividends on shares of our common stock is subject to the requirement that we pay an equivalent dividend on each outstanding share of Series A Preferred (on an as converted basis).

**Sales of Unregistered Securities**

We did not conduct any offerings of equity securities during the fourth quarter of 2007 that were not registered under the Securities Act of 1933.

**Repurchases of Equity Securities**

We did not repurchase any shares of our common stock during the fourth quarter of 2007.

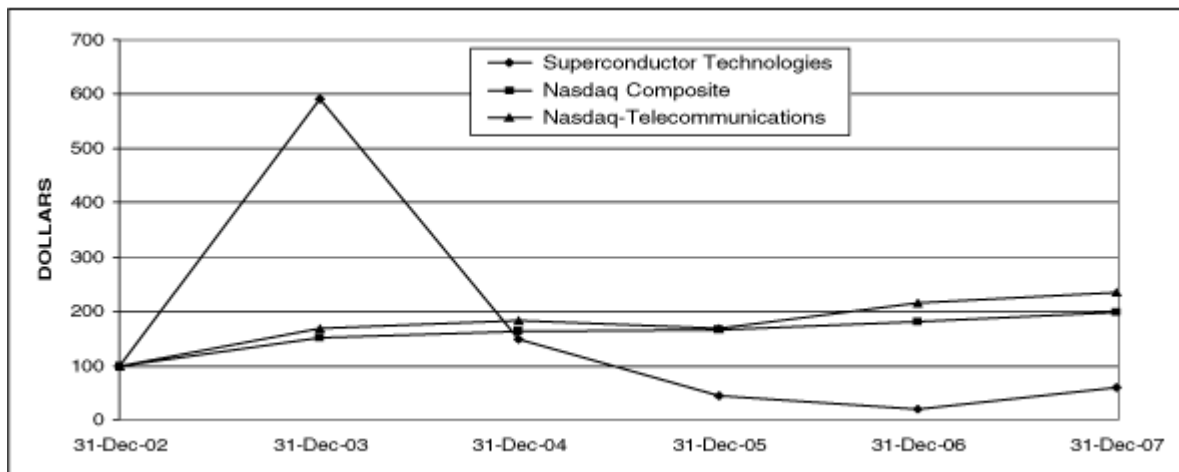
**Securities Authorized for Issuance Under Equity Compensation Plans**

<u>Plan Category</u>	<u>Number of Securities to Be Issued Upon Exercise of Outstanding Options, Warrants and Rights</u>	<u>Weighted-Average Exercise Price of Outstanding Options, Warrants and Rights</u>	<u>Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column(a))</u>
Equity compensation plans approved by security holders	741,858	\$ 34.24	1,575,397
Equity compensation plans not approved by security holders	—	—	—
<b>Total</b>	<b>741,858</b>	<b>\$ 34.24</b>	<b>1,575,397</b>



## Stock Performance Graph

The graph and table below compare the cumulative total stockholders' return on our common stock since December 31, 2002 with the Nasdaq Composite Index, and the Nasdaq Telecommunications Index over the same period (assuming the investment of \$100 in our common stock and in the two other indices, and reinvestment of all dividends).



	31-Dec-02	31-Dec-03	31-Dec-04	31-Dec-05	31-Dec-06	31-Dec-07
Superconductor Technologies	\$100.00	\$591.49	\$147.87	\$ 45.74	\$ 18.83	\$ 59.04
Nasdaq Composite	100.00	150.01	162.89	165.13	180.85	198.60
Nasdaq-Telecommunications	100.00	168.74	182.23	169.09	216.03	235.85

**ITEM 6. SELECTED FINANCIAL DATA**

The information set forth below is not necessarily indicative of results of future operations and should be read in conjunction with our Financial Statements and Notes thereto appearing in Item 15 of Part IV of this Report and “Management’s Discussion and Analysis of Financial Condition and Results of Operations”.

	Year Ended December 31,				
	2003	2004	2005	2006	2007
(In thousands, except per share data)					
<b>Statement of Operations Data:</b>					
Net revenues:					
Net commercial product revenues	\$ 38,577	\$ 16,787	\$ 21,080	\$ 17,697	\$12,787
Government contract revenues	10,759	6,189	3,107	3,361	5,115
Sub license royalties	58	28	22	20	—
Total net revenues	49,394	23,004	24,209	21,078	17,902
Costs and expenses:					
Cost of commercial product revenues	28,249	23,421	18,989	15,922	12,944
Contract research and development	6,899	4,465	2,806	2,407	2,906
Other research and development	4,697	5,036	4,214	3,488	3,172
Selling, general and administrative	20,567	16,051	11,442	9,086	8,123
Restructuring expenses and impairment charges	—	4,128	1,197	38	—
Write off of Goodwill	—	—	—	20,107	—
Total costs and expenses	60,412	53,101	38,648	51,048	27,145
Loss from operations	(11,018)	(30,097)	(14,439)	(29,970)	(9,243)
Other income (expense), net	(327)	(1,120)	226	346	117
Net loss	<u>\$(11,345)</u>	<u>\$(31,217)</u>	<u>\$(14,213)</u>	<u>\$(29,624)</u>	<u>\$(9,126)</u>
Basic and diluted net loss per share:					
Net loss per common share	<u>\$ (1.81)</u>	<u>\$ (3.71)</u>	<u>\$ (1.24)</u>	<u>\$ (2.37)</u>	<u>\$ (0.73)</u>
Weighted average number of shares Outstanding	6,269	8,424	11,419	12,483	12,488

	December 31,				
	2003	2004	2005	2006	2007
<b>Balance Sheet Data:</b>					
Cash and cash equivalents	\$11,144	\$12,802	\$13,018	\$ 5,487	\$ 3,939
Working capital	15,576	16,146	17,218	10,158	3,293
Total assets	68,123	62,358	52,045	21,904	16,625
Long-term debt, including current portion	721	76	33	618	563
Total stockholders’ equity	52,220	49,249	47,257	17,951	9,190

## **ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

*This Management's Discussion and Analysis of Financial Condition and Results of Operations includes many forward-looking statements. For cautions about relying on such forward looking statements, please refer to the section entitled "Forward Looking Statements" at the beginning of this Report immediately prior to Item 1.*

### **General**

We design, manufacture, market and sell high performance infrastructure products for wireless voice and data applications. Our products are utilized in major wireless networks throughout the United States which support voice and data communications by use of cell phones and other wireless communication devices.

Our 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. Our SuperLink solution utilizes patented high-temperature superconductor (HTS) technology to create a receiver front-end that enhances network performance. Today, we are leveraging our expertise and proprietary technology in radio frequency (RF) engineering to continue to expand our product line beyond HTS technology. We believe our RF engineering expertise provides us with a significant competitive advantage in the development of high performance, cost-effective solutions for wireless telecommunications networks.

We have three product offerings:

- SuperLink. In order to receive uplink signals from wireless handsets, base stations require a wireless filter system to eliminate out-of-band interference. SuperLink combines HTS filters with a proprietary cryogenic cooler and an ultra low-noise amplifier. The result is a highly compact and reliable receiver front-end that can simultaneously deliver both high selectivity (interference rejection) and high sensitivity (detection of low level signals). SuperLink delivers significant performance advantages over conventional filter systems.
- AmpLink. AmpLink is designed to address the sensitivity requirements of wireless base stations. AmpLink is a ground-mounted unit which utilizes a high-performance amplifier. The enhanced uplink performance provided by AmpLink improves network coverage immediately and avoids the installation and maintenance costs associated with tower mounted alternatives.
- SuperPlex. SuperPlex is our line of multiplexers that provides extremely low insertion loss and excellent cross-band isolation. SuperPlex high-performance multiplexers are designed to eliminate the need for additional base station antennas and reduce infrastructure costs. Relative to competing technologies, these products offer increased transmit power delivered to the base station antenna, higher sensitivity to subscriber handset signals, and fast and cost-effective network overlays.

We currently sell most of our commercial products directly to wireless network operators in the United States. Our customers to date include ALLTEL, Cingular, Sprint Nextel, T-Mobile, U.S. Cellular and Verizon Wireless. We have a concentrated customer base. Verizon Wireless and AT&T each accounted for more than 10% of our commercial revenues in 2007 and Verizon Wireless, ALLTEL, and T-Mobile each accounted for more than 10% of our commercial revenues in 2006. We plan to expand our customer base by selling directly to other wireless network operators and manufacturers of base station equipment, but we cannot assure that this effort will be successful.

We also generate significant revenues from government contracts. We primarily pursue government research and development contracts which compliment our commercial product development. We undertake government contract work which has the potential to improve our commercial product offering. These contracts often yield valuable intellectual property relevant to our commercial business. We typically own the intellectual property developed under these contracts, and the Federal Government receives a royalty-free, non-exclusive and nontransferable license to use the intellectual property for the United States.

We sell most of our products to a small number of wireless carriers, and their demand for wireless communications equipment fluctuates dramatically and unpredictably. We expect these trends to continue and may cause significant fluctuations in our quarterly and annual revenues.

The wireless communications infrastructure equipment market is extremely competitive and is characterized by rapid technological change, new product development, product obsolescence, evolving industry standards and price erosion over the life of a product. We face constant pressures to reduce prices. Consequently, we expect the average selling prices of our products will continue decreasing over time. We have responded in the past by successfully reducing our product costs, and expect further cost reductions over the next twelve months. However, we cannot predict whether our costs will decline at a rate sufficient to keep pace with the competitive pricing pressures.

### Recent Developments

#### ***BAOLI Investment.***

Under a previously announced investment agreement with Hunchun BaoLi Communication Co. Ltd, or BAOLI, in August 2007, on February 27, 2008, we issued to BAOLI and two related purchasers a total of (a) 3,101,361 shares of our common stock (of which 953,065 must be voted in accordance with the votes of our other shares, effectively giving BAOLI no voting power over such shares) and (b) 611,523 shares of our Series A Convertible Preferred Stock, or Series A Preferred (convertible under certain conditions into 6,115,230 shares of our common stock). We received \$15.0 million in cash, of which \$4.0 million was funded in 2007 and the \$11.0 million balance was funded in January 2008.

Subject to the terms and conditions of our Series A Preferred and to customary adjustments to the conversion rate, each share of our Series A Preferred is convertible into ten shares of our common stock so long as the number of shares of our common stock beneficially owned by BAOLI following such conversion does not exceed 9.9% of our outstanding common stock. Except for a preference on liquidation of \$.01 per share, each share of Series A Preferred is the economic equivalent of the ten shares of common stock into which it is convertible. Except as required by law, the Series A Preferred will not have any voting rights. For a complete description of the terms of the Series A Preferred, please see the certificate of designations, a copy of which is available through our website at [www.supotech.com](http://www.supotech.com) or in our SEC filings available at the SEC's website at <http://www.sec.gov>.

With the issuance of the Series A Preferred, our ability to declare or pay dividends on shares of our common stock will be subject to the requirement that we pay an equivalent dividend on each outstanding share of Series A Preferred (on an as converted basis).

#### ***BAOLI Joint Venture.***

We and BAOLI continue to work on our recently established joint venture to manufacture and market our SuperLink<sup>®</sup> interference elimination solution for the China market. As previously announced, our agreements provide that BAOLI will provide the manufacturing expertise and financing in exchange for 55 percent of the equity and we will provide an exclusive license in the China market of the enabling technology in exchange for 45 percent of the equity and a royalty on sales. We continue to work on preliminary matters relating to the joint venture, including administrative and logistical matters, exploratory marketing initiatives, technical and market analysis and discussions with governmental officials.

The commencement of manufacturing and any actual sales by the joint venture, and the transfer of our technology to the joint venture, remain subject to success in these efforts and to a number of other conditions including certain critical approvals from the Chinese and United States governments. In particular, we are in discussions with the Committee on Foreign Investment in the United States (or CFIUS), an inter-agency committee of the United States government that reviews the national security implications of foreign acquisitions of U.S. companies regarding our joint venture with and investment from BAOLI. There continues to be no assurance that these conditions will be met, or that all required approvals (if obtained) will be obtained on a timely basis. 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 (which are similar to those involved in acquisitions), some of which are set out in our public filings, including in particular the "Risk Factors" included in Item 1A of this document.

**Critical Accounting Policies and Estimates**

Our discussion and analysis of our financial condition and results of operations are based upon our financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. We continually evaluate our estimates, including those related to bad debts, inventories, recovery of long-lived assets, income taxes, warranty obligations, contract revenue and contingencies. We base our estimates on historical experience and on various other assumptions that we believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Any future changes to these estimates and assumptions could cause a material change to our reported amounts of revenues, expenses, assets and liabilities. Actual results may differ from these estimates under different assumptions or conditions.

We believe the following critical accounting policies affect our significant judgments and estimates used in the preparation of the financial statements. We maintain allowances for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. If the financial condition of our customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required. We write down our inventory for estimated obsolescence or unmarketable inventory equal to the difference between the cost of inventory and the estimated market value based upon assumptions about future demand and market conditions. If actual market conditions are less favorable than those projected by management, additional inventory write-downs may be required.

Our inventory is valued at the lower of its actual cost or the current estimated market value of the inventory. 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 or disposed. Our inventory reserves establish a new cost basis for inventory and are not reversed until the related inventory is sold or otherwise disposed. 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. Our business is characterized by rapid technological change, frequent new product development and rapid product obsolescence that could result in an increase in the amount of obsolete inventory quantities on hand. Demand for our products can fluctuate significantly. Our estimates of future product demand may prove to be inaccurate and we may understate or overstate the provision required for excess and obsolete inventory.

Our net sales consist of revenue from sales of products net of trade discounts and allowances. We recognize revenue when evidence of an arrangement exists, contractual obligations have been satisfied, title and risk of loss have been transferred to the customer and collection of the resulting receivable is reasonably assured. At the time revenue is recognized, we provide for the estimated cost of product warranties if allowed for under contractual arrangements and return products. Our warranty obligation is affected by product failure rates and service delivery costs incurred in correcting a product failure. Should such failure rates or costs differ from these estimates, accrued warranty costs would be adjusted.

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 guarantees because of the uncertainty as to whether a claim might arise and how much it might total.

Contract revenues are principally generated under research and development contracts. Contract revenues are recognized utilizing the percentage-of-completion method measured by the relationship of costs incurred to total estimated contract costs. If the current contract estimate were to indicate a loss, utilizing the funded amount of the contract, a provision would be made for the total anticipated loss. Contract revenues are derived primarily from research contracts with agencies of the United States Government. Credit risk related to accounts receivable arising

from such contracts is considered minimal. These contracts include cost-plus, fixed price and cost sharing arrangements and are generally short-term in nature.

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

In connection with the acquisition of Conductus we recognized \$20.1 million of goodwill. At July 1, 2006, our market capitalization had declined to \$25.5 million, an amount less than our total book value. We concluded that our declining stock price constituted an event under FAS 142 and required us to test for goodwill impairment as of July 1, 2006. We then proceeded with step two of the impairment analysis — determining the fair values of all our tangible and intangible assets and then aggregating and subtracting these values from our fair value. Our analysis led us to reasonably estimate at that time that our fair market value was less than our net assets excluding goodwill. Accordingly, we recorded a full write-down of the goodwill (\$20.1 million) in the second quarter 2006.

We periodically evaluate the realizability of long-lived assets as events or circumstances indicate a possible inability to recover the carrying amount. Long-lived assets that will no longer be used in business are written off in the period identified since they will no longer generate any positive cash flows for us. Periodically, long-lived assets that will continue to be used by we 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. 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. Our future cash flows may vary from estimates.

Effective January 1, 2006, we adopted the provisions of Statement of Financial Accounting Standards (“SFAS”) No. 123 (revised 2004), “Share-Based Payment” (“SFAS No. 123(R)”). Under this provision, the share-based compensation cost recognized beginning January 1, 2006 includes compensation cost for (i) all share-based payments granted prior to, but not vested as of January 1, 2006, based on the grant date fair value originally estimated in accordance with the provisions of SFAS No. 123, “Accounting for Stock-Based Compensation,” (“SFAS No. 123”) and (ii) all share-based payments granted subsequent to January 1, 2006, based on the grant date fair value estimated in accordance with the provisions of SFAS No. 123(R). Compensation cost under SFAS No. 123(R) is recognized ratably using the straight-line attribution method over the expected vesting period. Prior periods are not restated under this transition method.

Prior to 2006, as permitted under Statement of Financial Accounting Standards No. 123 (SFAS 123), “Accounting for Stock-Based Compensation”, we elected to follow Accounting Principles Board Opinion No. 25, “Accounting for Stock Issued to Employees” in accounting for stock options and other stock-based employee awards. Pro forma information regarding net loss and loss per share, as calculated under the provisions of SFAS 123, are disclosed in the notes to the financial statements. We accounted for equity securities issued to non-employees in accordance with the provision of SFAS 123 and Emerging Issues Task Force 96-18.

Prior to 2006, we did not recognize compensation expense for issuance of stock options to employees. If we had elected to recognize compensation expense for employee awards prior to 2006 based upon the fair value at the

grant date consistent with the methodology prescribed by SFAS 123, our net loss and net loss per share would have been increased to the pro forma amounts indicated below:

	<b>For the Year Ended December 31, 2005</b>
	<b>(In thousands, except per share data)</b>
<b>Net loss:</b>	
As reported	\$ (14,213)
Stock-based employee compensation included in net loss	—
Stock-based compensation expense determined under fair value method	(6,459)
Pro forma	<u>(20,672)</u>
<b>Basic and Diluted Loss per Share:</b>	
As reported	\$ (1.24)
Stock-based compensation expense determined under fair value method	(0.57)
Pro forma	<u>\$ (1.81)</u>

On December 1, 2005, the Compensation Committee of our Board of Directors approved the accelerated vesting of all time-vested outstanding out-of-the-money stock options held by current employees or consultants. For this purpose, the Compensation Committee defined “out-of-the-money options” as options having an exercise price equal to or greater than \$5.80 per share (the market price on the date of the committee’s decision to accelerate the vesting). If we had elected to recognize compensation expense for employee awards, the pro forma cost impact of these accelerated options in 2005 would have been \$3.7 million.

Our valuation allowance against the deferred tax assets is based on our assessments of historical losses and projected operating results in future periods. If and when we generate future taxable income in the U.S. against which these tax assets may be applied, some portion or all of the valuation allowance would be reversed and an increase in net income would consequently be reported in future years.

We have a contract to deliver several custom products to a government contractor. We are unable to manufacture the products for technical reasons. We have discussed the problem with the contractor and its government customer. They are considering the problem, and we expect further discussions. We do not believe that a loss is reasonably estimable at this time and therefore have not recorded any liability relating to this matter. We will periodically reassess our potential liability as additional information becomes available. If we later determine that a loss is probable and the amount reasonably estimable, we would record a liability for the potential loss.

## **Backlog**

Our commercial backlog consists of accepted product purchase orders with scheduled delivery dates during the next twelve months. We had commercial backlog of \$352,000 at December 31, 2007, as compared to \$75,000 at December 31, 2006.

## **Results of Operations**

### ***2007 Compared to 2006***

Net revenues decreased by \$3.2 million, or 15%, from \$21.1 million in 2006 to \$17.9 million in 2007. Net revenues consist primarily of commercial product revenues and government contract revenues. We also generate some additional revenues from sublicensing our technology.

Net commercial product revenues decreased by \$4.9 million, or 28%, to \$12.8 million in 2007 from \$17.7 million in 2006. The decrease is primarily the result of lower sales volume for some of our products. Average sales prices for our products decreased only slightly in 2007. Our two largest customers accounted for 75% of our net commercial revenues in 2007, as compared to 76% in 2006. These customers generally purchase products



through non-binding commitments with minimal lead-times. Consequently, our commercial product revenues can fluctuate dramatically from quarter to quarter based on changes in our customers' capital spending patterns.

Government contract revenues increased to \$5.1 million in 2007 from \$3.4 million in 2006, an increase of \$1.7 million, or 52%. This increase is primarily attributable to the addition of new or amended contracts in 2007.

Cost of commercial product revenues includes all direct costs, manufacturing overhead, provision for excess and obsolete inventories. The cost of commercial product revenues totaled \$12.9 million for 2007 as compared to \$15.9 million for 2006, a decrease of \$3.0 million, or 19%. The lower costs resulted principally from lower production as a result of lower sales. There was also no restructuring expenses in 2007 and a lower provision for obsolete inventory. Our provision for obsolete inventories totaled \$160,000 in 2007 as compared to \$360,000 in 2006.

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

The following is an analysis of our commercial product gross profit margins for 2006 and 2007:

	For the Years Ended December 31,			
	2006		2007	
	Dollars in thousands			
Net commercial product sales	\$17,697	100.0%	\$12,787	100.0%
Cost of commercial product sales	<u>15,922</u>	<u>90%</u>	<u>12,944</u>	<u>101.2%</u>
Gross profit	\$ 1,775	10%	\$ (157)	(1.2)%

We had a negative gross margin of \$157,000 in 2007 from the sale of our commercial products as compared to a positive gross margin of \$1.8 million in 2006. We experienced negative gross profits in 2007 primarily because the reduced level of commercial sales was insufficient to cover our fixed manufacturing overhead costs. Our gross margins were also adversely impacted by a \$160,000 charge for excess and obsolete inventory. Gross margins were favorably impacted by \$195,000 in 2007 and \$700,000 in 2006 by the sale of previously written-off inventory. We regularly review inventory quantities on hand and provide an allowance for excess and obsolete inventory based on numerous factors including sales backlog, historical inventory usage, forecasted product demand and production requirements for the next twelve months.

Contract research and development expenses totaled \$2.9 million in 2007 as compared to \$2.4 million in 2006, an increase of \$499,000 or 20%. The increase was primarily the result of higher expenses associated with performing a greater number of government contracts.

Other research and development expenses relate to development of new wireless commercial products. We also incur design expenses associated with reducing the cost and improving the manufacturability of our existing products. These expenses totaled \$3.2 million in 2007 as compared to \$3.5 million in 2006, a decrease of \$316,000,



or 9%. The decrease is due to lower expenses associated with commercial products development and the result of our cost reduction efforts.

Selling, general and administrative expenses totaled \$8.1 million in 2007 as compared to \$9.1 million in 2006, a decrease of \$1.0 million, or 11%. The lower expenses resulted primarily from \$610,000 received from a settlement agreement with a former director and lower insurance premiums.

In connection with the acquisition of Conductus in December 2002 we recognized \$20.1 million of goodwill. At July 1, 2006, we concluded that our declining stock price constituted an event under FAS 142 and required us to test for goodwill impairment. Our analysis led us to reasonably estimate at that time that our fair market value was less than our net assets excluding goodwill. Accordingly, we recorded a full write-down of the goodwill (\$20.1 million) in the second quarter of 2006. We also recorded an impairment charge of \$38,000 related to a note receivable from a Board member in 2006.

The following table summarizes our restructuring and impairment charges for 2006 and 2007:

	For the Year Ended December 31,					
	Restructuring Charges for 2006	Impairment Charges for 2006	Total for 2006	Restructuring Charges for 2007	Impairment Charges for 2007	Total for 2007
Severance costs	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Fixed assets write offs	—	—	—	—	—	—
Facility consolidation costs	—	—	—	—	—	—
Employee relocation cost	—	—	—	—	—	—
Goodwill Write-off	—	20,107,000	20,107,000	—	—	—
Impairment charge for notes receivable from shareholder and board member	—	38,000	38,000	—	—	—
<b>Total</b>	<b>—</b>	<b>20,145,000</b>	<b>20,145,000</b>	<b>—</b>	<b>—</b>	<b>—</b>
Fixed Asset write off and severance costs included in cost of goods sold	—	—	—	—	—	—
<b>Expense included in operating expenses</b>	<b>\$ —</b>	<b>\$20,145,000</b>	<b>\$20,145,000</b>	<b>\$ —</b>	<b>\$ —</b>	<b>\$ —</b>

Interest income decreased to \$156,000 in 2007, as compared to \$391,000 in 2006, primarily because of lower cash balances in 2007.

Interest expense in 2007 amounted to \$39,000, as compared to \$45,000 in 2006, as a result of lower borrowing levels.

Our loss totaled \$9.1 million in 2007 as compared to \$29.6 million in 2006.

The net loss available to common shareholders totaled \$0.73 per common share in 2007, as compared to \$2.37 per common share in 2006.

### ***2006 Compared to 2005***

Net revenues decreased by \$3.1 million, or 13%, from \$24.2 million in 2005 to \$21.1 million in 2006. Net revenues consist primarily of commercial product revenues and government contract revenues. We also generate some additional revenues from sublicensing our technology.

Net commercial product revenues decreased by \$3.4 million, or 16%, to \$17.7 million in 2006 from \$21.1 million in 2005. The decrease is primarily the result of lower sales and lower average sale prices of our products. Our three largest customers accounted for 96% of our net commercial revenues in 2006, as compared to 95% in 2005. These customers generally purchase products through non-binding commitments with minimal lead-times. Consequently, our commercial product revenues can fluctuate dramatically from quarter to quarter based on changes in our customers' capital spending patterns.

Government contract revenues increased to \$3.4 million in 2006 from \$3.1 million in 2005, an increase of \$254,000, or 8%. This increase is primarily attributable to the addition of new or amended contracts in 2006.

Cost of commercial product revenues includes all direct costs, manufacturing overhead, provision for excess and obsolete inventories. The cost of commercial product revenues totaled \$15.9 million for 2006 as compared to \$19.0 million for 2005, a decrease of \$3.1 million, or 16%. The lower costs resulted from no restructuring expenses in 2006 and a lower provision for obsolete inventory. Restructuring and impairment expenses from severance and “fixed assets write off included in cost of goods sold” were zero in 2006 as compared to \$109,000 in 2005. Our provision for obsolete inventories totaled \$360,000 in 2006 as compared to \$1.0 million in 2005.

Our cost of sales includes both variable and fixed cost components. The variable component consists primarily of materials, assembly and test labor, overhead, which includes equipment and facility depreciation, transportation costs and warranty costs. The fixed component includes test equipment and facility depreciation, purchasing and procurement expenses and quality assurance costs. Given the fixed nature of such costs, the absorption of our production overhead costs into inventory decreases and the amount of production overhead variances expensed to cost of sales increases as production volumes decline since we have fewer units to absorb our overhead costs against. Conversely, the absorption of our production overhead costs into inventory increases and the amount of production overhead variances expensed to cost of sales decreases as production volumes increase since we have more units to absorb our overhead costs against. As a result, our gross profit margins generally decrease as revenue and production volumes decline due to lower sales volume and higher amounts of production overhead variances expensed to cost of sales; and our gross profit margins generally increase as our revenue and production volumes increase due to higher sales volume and lower amounts of production overhead variances expensed to cost of sales. Our inventory is valued at the lower of its actual cost or the current estimated market value of the inventory. 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 recognizes a loss in the period in which the loss is identified, whether or not the inventory is retained or disposed.

The following is an analysis of our commercial product gross profit margins for 2005 and 2006:

	For the Years Ended December 31,			
	2005		2006	
	Dollars in thousands			
Net commercial product sales	\$21,080	100.0%	\$17,697	100.0%
Cost of commercial product sales	18,989	90.1%	15,922	90%
Gross profit	\$ 2,091	9.9%	\$ 1,775	10%

We had a positive gross margin of \$1.8 million in 2006 from the sale of our commercial products as compared to a positive gross margin of \$2.1 million in 2005. The gross margin percentage improved slightly on lower sales volumes primarily due to lower restructuring expenses, a lower provision for obsolete inventory and the positive results of our cost reduction efforts. Gross margin was also favorably impacted \$700,000 by the sale of previously written-off inventory. We regularly review inventory quantities on hand and provide an allowance for excess and obsolete inventory based on numerous factors including sales backlog, historical inventory usage, forecasted product demand and production requirements for the next twelve months.

Contract research and development expenses totaled \$2.4 million in 2006 as compared to \$2.8 million in 2005, a decrease of \$399,000 or 14%. The decrease was primarily the result of 2005 expenses totaling \$759,000 on a contract for which no revenue was recognized. See “*Contractual Contingency*” under the Contractual Guarantees and Indemnities Note to the Financial Statements for a description of the non-revenue generating contract.

Other research and development expenses relate to development of new wireless commercial products. We also incur design expenses associated with reducing the cost and improving the manufacturability of our existing products. These expenses totaled \$3.5 million in 2006 as compared to \$4.2 million in 2005, a decrease of \$726,000, or 17%. The decrease is due to lower expenses associated with commercial products development and the result of our cost reduction efforts.

Selling, general and administrative expenses totaled \$9.1 million in 2006 as compared to \$11.4 million in 2005, a decrease of \$2.3 million, or 20%. The lower expenses resulted primarily from lower auditor fees, lower insurance premiums, lower legal expenses for other matters, no restructuring activities in 2006 and the payment in 2005 of retirement benefits for our previous Chief Executive Officer.

We implemented several restructuring programs since 2004. These activities were completed in 2005. In connection with the acquisition of Conductus in December 2002 we recognized \$20.1 million of goodwill. At July 1, 2006, we concluded that our declining stock price constituted an event under FAS 142 and required us to test for goodwill impairment. Our analysis led us to reasonably estimate at that time that our fair market value was less than our net assets excluding goodwill. Accordingly, we recorded a full write-down of the goodwill (\$20.1 million) in the second quarter. We also recorded an impairment charge of \$38,000 related to a note receivable from a Board member.

The following table summarizes our restructuring and impairment charges for 2005 and 2006:

	For the Year Ended December 31,					
	Restructuring Charges for 2005	Impairment Charges for 2005	Total for 2005	Restructuring Charges for 2006	Impairment Charges for 2006	Total for 2006
Severance costs	\$ 178,000	\$ —	\$ 178,000	\$ —	\$ —	\$ —
Fixed assets write offs	137,000	—	137,000	—	—	—
Facility consolidation costs	6,000	—	6,000	—	—	—
Employee relocation cost	16,000	—	16,000	—	—	—
Goodwill Write-off	—	—	—	—	20,107,000	20,107,000
Impairment charge for notes receivable from shareholder and board member	—	969,000	969,000	—	38,000	38,000
<b>Total</b>	<b>\$ 337,000</b>	<b>\$ 969,000</b>	<b>\$1,306,000</b>	<b>—</b>	<b>20,145,000</b>	<b>20,145,000</b>
Fixed Asset write off and severance costs included in cost of goods sold	(109,000)	—	(109,000)	—	—	—
<b>Expense included in operating expenses</b>	<b>\$ 228,000</b>	<b>\$ 969,000</b>	<b>\$1,197,000</b>	<b>\$ —</b>	<b>\$20,145,000</b>	<b>\$20,145,000</b>

Interest income increased to \$391,000 in 2006, as compared to \$342,000 in 2005, primarily because of increased interest rates.

Interest expense in 2006 amounted to \$45,000, as compared to \$116,000 in 2005, as a result of lower borrowing levels.

Our loss totaled \$29.6 million in 2006 as compared to \$14.2 in 2005.

The net loss available to common shareholders totaled \$2.37 per common share in 2006, as compared to \$1.24 per common share in 2005.

## **Liquidity and Capital Resources**

### ***Cash Flow Analysis***

As of December 31, 2007, we had working capital of \$3.3 million, including \$3.9 million in cash and cash equivalents, as compared to working capital of \$10.2 million at December 31, 2006, which included \$5.5 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. Our investments have zero exposure to the auction rate securities market. We believe that all of our cash investments would be readily available to us should the need arise.

Cash and cash equivalents decreased by \$1.6 million from \$5.5 million at December 31, 2006 to \$3.9 million at December 31, 2007. (In January 2008 we received the remaining \$11.0 million from our investment agreement with BAOLI. *See notes below in Financing Activities and Future Liquidity* ). Cash was used principally in operations and to a lesser extent for the purchase of property and equipment and for the payment of short and long-term borrowings. Cash and cash equivalents decreased by \$7.5 million from \$13.0 million at December 31, 2005 to \$5.5 million at December 31, 2006. Cash was used in operations, for the purchase of property and equipment, for the payment of short and long-term borrowings. These uses were offset by gross cash proceeds of \$12.5 million received from the sale of common stock in a public offering during the third quarter of 2005.

Cash used in operations totaled \$5.4 million in 2007. We used \$9.1 million to fund the cash portion of our net loss. We also used cash to fund a \$2.1 million increase in accounts payable payments, accounts receivable and patents and licenses. These uses were offset by cash generated from lower inventory, lower prepaid and other assets totaling \$3.0 million. Cash used in operations totaled \$7.3 million in 2006. In 2006 we used \$6.2 million to fund the cash portion of our net loss. We also used cash to fund a \$1.8 million increase in inventory and accounts payable payments. These uses were offset by cash generated from lower accounts receivables and prepaid balances totaling \$746,000.

Net cash used in investing activities totaled \$165,000 in 2007. In 2007, sales of fixed assets generated \$26,000 and were offset by fixed asset purchases totaling \$191,000. Net funds used in investing activities totaled \$229,000 in 2006 and \$45,000 in 2005. In 2006 we purchased \$229,000 of fixed assets and there were no sales of fixed assets. In 2005, sales of fixed assets generated \$216,000 and essentially offset purchases of property and equipment totaling \$261,000.

Net cash provided by financing activities totaled \$4.0 million in 2007. In 2007, \$4.0 million was received from BAOLI as an installment toward completion of a \$15.0 million financing which was completed in February 2008. Cash used to pay long term debt was \$14,000 and was offset by \$26,000 provided by the exercise of stock options. Net cash used in financing activities totaled \$19,000 in 2006 and was used to pay long term debt. In 2005 gross cash received from the sale of common stock totaled \$12.5 million and borrowings against our line of credit totaled \$662,000, offset by cash used to pay down our line of credit and long term debt of \$1.6 million. Cash was also used to pay \$1.9 million of offering expenses related to the sale of common stock in November 2004 and August 2005.

### ***Financing Activities***

We have historically financed our operations through a combination of cash on hand, equipment lease financings, available borrowings under bank lines of credit and both private and public equity offerings. We have effective registration statements on file with the SEC covering the public resale by investors of all the common stock issued in our private placements, as well as any common stock acquired upon exercise of their warrants.

We have an existing line of credit from a bank. It is a material source of funds for our business. The line of credit expires in July 2008. The loan agreement is structured as a sale of our accounts receivable and provides for the sale of up to \$5.0 million of eligible accounts receivable, with advances to us totaling 80% of the receivables sold. Advances bear interest at the prime rate (7.25% at December 31, 2007) plus 2.50% subject to a minimum monthly charge. Advances are collateralized by a lien on all of our assets. Under the terms of the agreement, we continue to service the sold receivables and are subject to recourse provisions. There was no amount outstanding under this borrowing facility at December 31, 2007.

In 2007 and 2006, we did not complete a financing transaction. However, on August 17, 2007, we entered into the previously noted investment agreement with BAOLI and on February 27, 2008, the transactions contemplated by this investment agreement closed and in exchange for \$15.0 million in cash we issued to BAOLI and two related purchasers a total of (a) 3,101,361 shares of our common stock and (b) 611,523 shares of our Series A Preferred Stock (convertible under certain conditions into 6,115,230 shares of our common stock).

### ***Contractual Obligations and Commercial Commitments***

We incur various contractual obligations and commercial commitments in our normal course of business. They consist of the following:

- *Operating Lease Obligations*

Our operating lease obligations consist of a facility lease in Santa Barbara, California and several copier leases.

- *Patents and Licenses*

We have entered into various licensing agreements requiring royalty payments ranging from 0.13% to 2.5% of specified product sales. Some of these agreements contain provisions for the payment of guaranteed or minimum royalty amounts. Typically, the licensor can terminate our license if we fail to pay minimum annual royalties.

- *Purchase Commitments*

In the normal course of business, we incur purchase obligations with vendors and suppliers for the purchase of inventory, as well as other goods and services. These obligations are generally evidenced by purchase orders that contain the terms and conditions associated with the purchase arrangements. We are committed to accept delivery of such material pursuant to the purchase orders subject to various contract provisions which allow us to delay receipt of such orders or cancel orders beyond certain agreed upon lead times. Cancellations may result in cancellation costs payable by us.

- *Quantitative Summary of Contractual Obligations and Commercial Commitments*

At December 31, 2007, we had the following contractual obligations and commercial commitments:

<u>Contractual Obligations</u>	<u>Payments Due by Period</u>				
	<u>Total</u>	<u>Less than 1 year</u>	<u>2-3 years</u>	<u>4-5 years</u>	<u>After 5 years</u>
Operating leases	5,870,000	1,425,000	2,999,000	1,445,000	1,000
Minimum license commitment	1,800,000	150,000	300,000	300,000	1,050,000
Fixed asset and inventory purchase commitments	3,184,000	3,184,000	—	—	—
Total contractual cash obligations	<u>\$10,854,000</u>	<u>\$4,759,000</u>	<u>\$3,299,000</u>	<u>\$1,745,000</u>	<u>\$1,051,000</u>

### ***Capital Expenditures***

We plan to invest approximately \$700,000 in fixed assets during 2008.

### ***Future Liquidity***

Our principal sources of liquidity consist of existing cash balances and funds expected to be generated from future operations. We believe one of the key factors to our liquidity will be our ability to successfully execute on our plans to increase sales levels in a highly concentrated industry where we experience significant fluctuations in sales from quarter to quarter. Our cash requirements will also depend on numerous other variable factors, including the rate of growth of sales, the timing and levels of products purchased, payment terms and credit limits from manufacturers, and the timing and level of accounts receivable collections.

In 2007, we incurred a net loss of \$9.1 million and had negative cash flows from operations of \$5.4 million. In 2006, we incurred a net loss of \$29.6 million and had negative cash flows from operations of \$7.3 million. Our independent registered public accounting firm has included in their audit report for fiscal 2007 and 2006 an explanatory paragraph expressing doubt about our ability to continue as a going concern. Our prior independent registered public accounting firm included a similar explanatory paragraph in their audit report for 2005.

At December 31, 2007 we had \$3.9 million in cash and in January 2008 we received the remaining \$11.0 million from our previously noted investment agreement with BAOLI whereby in exchange for \$15.0 million

in cash we issued to BAOLI and two related purchasers a total of (a) 3,101,361 shares of our common stock and (b) 611,523 shares of our Series A Preferred Stock (convertible under certain conditions into 6,115,230 shares of our common stock). If actual cash flows deviate significantly from forecasted amounts or if we believe operations require additional funding we cannot assure you that additional financing will be available on acceptable terms or at all.

### **Net Operating Loss Carryforward**

As of December 31, 2007, we had net operating loss carryforwards for federal and state income tax purposes of approximately \$285.1 million and \$154.7 million, respectively, which expire in the years 2008 through 2027. Of these amounts \$88.3 million and \$23.5 million, respectively, resulted from the acquisition of Conductus. Included in the net operating loss carryforwards are deductions related to stock options of approximately \$24.1 million and \$13.1 million for federal and California income tax purposes, respectively. To the extent net operating loss carryforwards are recognized for accounting purposes the resulting benefits related to the stock options will be credited to stockholders' equity. In addition, we had research and development and other tax credits for federal and state income tax purposes of approximately \$2.7 million and \$1.3 million, respectively, which expire in the years 2008 through 2027. Of these amounts \$661,000 and \$736,000, respectively resulted from the acquisition of Conductus.

Due to the uncertainty surrounding their realization, we have recorded a full valuation allowance against our net deferred tax assets. Accordingly, no deferred tax asset has been recorded in the accompanying balance sheet.

Section 382 of the Internal Revenue Code imposes an annual limitation on the utilization of net operating loss carryforwards based on a statutory rate of return (usually the "applicable federal funds rate", as defined in the Internal Revenue Code) and the value of the corporation at the time of a "change of ownership" as defined by Section 382. We had changes in ownership in August 1999 and December 2002. Therefore, the ability to utilize net operating loss carryforwards of \$97.3 million incurred prior to the ownership changes will be subject in future periods to an annual limitation of \$1.3 million. In addition, we acquired the right to Conductus' net operating losses, which are also subject to the limitations imposed by Section 382. Conductus underwent three ownership changes, which occurred in February 1999, February 2001 and December 2002. Therefore, the ability to utilize Conductus' net operating loss carryforwards of \$88.3 million incurred prior to the ownership changes will be subject in future periods to annual limitation of \$700,000. Net operating losses incurred by us subsequent to the ownership changes totaled \$99.5 million and are not subject to this limitation. We are currently evaluating the potential limitations on our ability to utilize our net operating loss carryforwards as a result of the recent investment by BAOLI.

### **Future Accounting Requirements**

In February 2008, the FASB issued FSP 157-2 "Partial Deferral of the Effective Date of Statement 157" (FSP 157-2). FSP 157-2 delays the effective date of SFAS No. 157, for all non-financial assets and non-financial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually) to fiscal years beginning after November 15, 2008. We are currently assessing the impact of SFAS No. 157 for non-financial assets and non-financial liabilities on our consolidated financial position and results of operations. We do not expect that the implementation of this standard, for financial assets and financial liabilities, will have a material impact on our consolidated financial position and results of operations.

In December 2007 the FASB issued Statement of Financial Accounting Standards No. 141 (revised 2007), "Business Combinations" (FAS 141(R) and No. 160, "Noncontrolling Interests in Consolidated Financial Statements, an amendment of ARB No. 51 (FAS 160)". FAS 141(R) will change how business acquisitions are accounted for and FAS 160 will change the accounting and reporting for minority interests, which will be recharacterized as noncontrolling interests and classified as a component of equity. FAS 141(R) and FAS 160 are effective for fiscal years beginning on or after December 15, 2008 (January 1, 2009 for the Company). The adoption of FAS 141(R) and FAS 160 are not expected to have a material impact on the Company's consolidated financial statements.

In June 2007 the FASB ratified EITF No. 07-3, or EITF 07-3, *Accounting for Nonrefundable Advance Payments for Goods or Services to Be Used in Future Research and Development Activities*. EITF 07-3 requires non-refundable advance payments for goods and services to be used in future research and development activities to



be recorded as an asset and the payments to be expensed when the research and development activities are performed. EITF 07-3 is effective for fiscal years beginning after December 15, 2007. We are currently evaluating the impact of adopting EITF 07-3 on our results of operations and financial condition.

In June 2007, the FASB ratified EITF 06-11 “Accounting for the Income Tax Benefits of Dividends on Share-Based Payment Awards” (“EITF 06-11”). EITF 06-11 provides that tax benefits associated with dividends on share-based payment awards be recorded as a component of additional paid-in capital. EITF 06-11 is effective, on a prospective basis, for fiscal years beginning after December 15, 2007. We are currently assessing the impact of EITF 06-11 on our consolidated financial position and results of operations.

In May 2007, the FASB issued FASB Staff Position (“FSP”) FIN 48-1 “Definition of Settlement in FASB Interpretation No. 48” (FSP FIN 48-1). FSP FIN 48-1 provides guidance on how to determine whether a tax position is effectively settled for the purpose of recognizing previously unrecognized tax benefits. FSP FIN 48-1 is effective retroactively to January 1, 2007. The implementation of this standard did not have a material impact on our consolidated financial position or results of operations.

In February 2007, the FASB issued SFAS No. 159 “The Fair Value Option for Financial Assets and Financial Liabilities” (SFAS No. 159). SFAS No. 159 permits entities to choose to measure many financial assets and financial liabilities at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. We do not expect that the implementation of this standard will have a material impact on our consolidated financial position and results of operations.

### **Market Risk**

We are exposed to various market risks, including changes in interest rates. Market risk is the potential loss arising from adverse changes in market rates and prices. We do not enter into derivatives or other financial instruments for trading or speculation purposes. Our money market investments have zero exposure to the auction rate securities market.

At December 31, 2007, we had approximately \$3.7 million invested in a money market account yielding approximately 4.63%. Assuming a 1% decrease in the yield on this money market account and no liquidation of principal for the year, our total interest income would decrease by approximately \$37,000 per annum. Also, at December 31, 2007, we had no amounts outstanding under a \$5.0 million bank borrowing arrangement bearing interest at the prime rate (7.25% at December 31, 2007) plus 2.50%. Assuming a 1% increase in the prime rate interest and that the entire line was used for the entire year, interest expense would increase approximately \$40,000 per annum.

### **Inflation**

We do not foresee any material impact on our operations from inflation.

### **ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

See “*Management’s Discussion and Analysis of Financial Condition and Results of Operations — Market Risk*.”

### **ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

All information required by this item is listed in the Index to Financial Statements in Part IV, Item 15(a)1.

### **ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

Not applicable.

**ITEM 9A. CONTROLS AND PROCEDURES**

**Controls and Procedures**

We have established disclosure controls and procedures to ensure that material information relating to us and our consolidated subsidiaries is made known to the officers who certify the Company's financial reports, as well as other members of senior management and the Board of Directors, to allow timely decisions regarding required disclosures. 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 Controller ("Principal 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. Based upon that evaluation, the Chief Executive Officer and Controller concluded that our disclosure controls and procedures are effective in timely alerting them to material information related to us that is required to be included in our annual and periodic SEC filings.

There were no changes in our internal controls over financial reporting during the fourth quarter of the year ended December 31, 2007 that have materially affected, or are reasonably likely to materially affect our internal controls 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.

**Management's Report on Internal Control Over Financial Reporting**

Our management is responsible for establishing and maintaining adequate internal control over our financial reporting (as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934, as amended). Our management assessed the effectiveness of our internal controls over financial reporting as of December 31, 2007. In making its assessment of the effectiveness of our internal controls over financial reporting, our management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") in Internal Control-Integrated Framework. Based on these criteria, our management has concluded that, as of December 31, 2007, our internal controls over financial reporting are effective. This annual report does not include an attestation report of our independent registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by our independent registered public accounting firm pursuant to temporary rules of the SEC that permit the company to provide only management's report in this annual report.

**ITEM 9B. OTHER INFORMATION**

We disclosed all the information required to be disclosed pursuant to Form 8-K during the fourth quarter of 2007.

**PART III**

**ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE**

Information regarding our executive officers and directors is incorporated by reference to the information set forth under the caption "*Directors and Executive Officers*" in our Proxy Statement for the Annual Meeting of Stockholders to be filed with the Commission within 120 days after the end of our year ended December 31, 2007.

We have a Code of Business Conduct and Ethics for all of our employees, including our Chief Executive Officer, Chief Financial Officer and Principal Accounting Officer. The purpose of the code is to ensure that our business is conducted in a consistently legal and ethical matter. We have posted the text of the code on our website at [www.suptech.com](http://www.suptech.com). We will post any material amendments or waivers to the code on our website. We will provide a



copy of our code free of charge to any person upon request by writing to us at the following address: Superconductor Technologies Inc., 460 Ward Drive, Santa Barbara, California 93111-2310, Attn: Corporate Secretary.

**ITEM 11. EXECUTIVE COMPENSATION**

Information regarding executive compensation is incorporated by reference to the information set forth under the caption “*Executive Compensation*” in our Proxy Statement for the Annual Meeting of Stockholders to be filed with the Commission within 120 days after the end of our year ended December 31, 2007.

**ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

Information regarding security ownership of certain beneficial owners and management is incorporated by reference to the information set forth under the caption “Voting Securities and Principal Shareholders — *Security Ownership of Certain Beneficial Owners and Management*” in our Proxy Statement for the Annual Meeting of Stockholders to be filed with the Commission within 120 days after the end of our year ended December 31, 2007.

**ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE**

Information regarding certain relationships and related transactions is incorporated by reference to the information set forth under the caption “*Transactions With Related Persons*” and “*Corporate Governance — Director Independence*” in our Proxy Statement for the Annual Meeting of Stockholders to be filed with the Commission within 120 days after the end of our year ended December 31, 2007.

**ITEM 14. PRINCIPAL ACCOUNTING FEES AND DISCLOSURES**

Information regarding accounting fees and disclosures is incorporated by reference to the information set forth under the caption “*Fees Paid to Independent Auditors*” in our Proxy Statement for the Annual Meeting of Stockholders to be filed with the Commission within 120 days after the end of our year ended December 31, 2007.

**PART IV**

**ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES**

(a) The following documents are filed as part of this Report:

1. Index to Financial Statements. Our financial statements and the Reports of Stonefield Josephson, Inc., Independent Registered Public Accounting Firm and PricewaterhouseCoopers LLP, our former Independent Registered Public Accounting Firm, are included in Part IV of this Report on the pages indicated:

	<u>Page</u>
Reports of Independent Registered Public Accounting Firms	F-1
Consolidated Balance Sheets as of December 31, 2006 and 2007	F-3
Consolidated Statement of Operations for the years ended December 31, 2005, 2006 and 2007	F-4
Consolidated Statement of Stockholders' Equity for the years ended December 31, 2005, 2006 and 2007	F-5
Consolidated Statement of Cash Flows for the years ended December 31, 2005, 2006 and 2007	F-6
Notes to Consolidated Financial Statements	F-7

2. Financial Statement Schedule Covered by the Foregoing Report of Independent Registered Public Accounting Firms.

All other schedules are omitted because they are not applicable or the required information is shown in the financial statements or the notes thereto.

### 3. Exhibits

<u>Number</u>	<u>Description of Document</u>
3.1	Amended and Restated Certificate of Incorporation of the registrant(1)
3.2	Certificate of Amendment of Restated Certificate of Incorporation(2)
3.3	Certificate of Amendment of Restated Certificate of Incorporation(3)
3.4	Certificate of Designations of the Registrant relating to the Series A Preferred Stock(26)
3.5	Amended and Restated Bylaws of the Registrant(4)
4.1	Form of Common Stock Certificate(5)
4.2	Third Amended and Restated Stockholders Rights Agreement(6)
4.3	Form of Warrant to Purchase Common Stock dated March 28, 2003, issued to Silicon Valley Bank(8)
4.4	Form of Warrant(9)
4.5	Form of Registration Rights Agreement(9)
4.6	Silicon Valley Bank Warrant dated May 2004(10)
4.7	Form of Warrant dated August 2005(11)
10.1	Amended and Restated 1988 Stock Option Plan, as amended, with form of stock option agreement(12)
10.2	1999 Stock Option Agreement(7)***
10.3	1998 Stock Option Plan (13)***
10.4(a)	Form of Change of Control Agreement dated March 28, 2003 (14)***
10.4(b)	Form of Amendment to Change of Control Agreement dated as of May 24, 2005 (12)***
10.4(c)	Form of Amendment to Change of Control Agreement dated as of December 31, 2006 (23)***
10.5(a)	Accounts Receivable Purchase Agreement dated March 28, 2003 by and between Registrant and Silicon Valley Bank(14)
10.5(b)	Accounts Receivable Purchase Modification Agreement with Silicon Valley Bank dated March 17, 2004 (15)
10.5(c)	Accounts Receivable Purchase Modification Agreement with Silicon Valley Bank dated March 29, 2005 (16)
10.6	Unconditional Guaranty dated March 27, 2003 issued by Conductus, Inc. to Silicon Valley Bank(14)
10.7	Patent License Agreement between Telcordia Technologies, Inc. and Registrant dated July 13, 2002(14)
10.8(a)	Securities Purchase Agreement dated June 23, 2003(17)
10.8(b)	Form of Investor Warrant(17)
10.9	Form of Registration Rights Agreement(17)
10.10	Patent License Agreement by and between Lucent Technologies and the registrant**(18)
10.11	License Agreement with Sunpower**(23)
10.12(a)	Employment Agreement with Jeffrey Quiram (20)***
10.12(b)	Option Agreement with Jeffrey Quiram (20)***
10.12(c)	Amendment to Employment Agreement with Jeffrey Quiram dated as of December 31, 2006 (24)***
10.13(a)	2003 Equity Management Incentive Plan (as amended May 25, 2005)(4)***
10.13(b)	Form of Option Agreement for 2003 Equity Incentive Plan (20)***
10.13(c)	Management Incentive Plan (22)***
10.14(a)	Employment Agreement with Terry White (23)***
10.14(b)	Amendment to Employment Agreement with Terry White dated as of December 31, 2006 (24)***

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<u>Number</u>	<u>Description of Document</u>
10.15	Compensation Policy for Non-Employee Directors dated March 18, 2005 (23)***
10.15	Stipulation of Settlement to Class Action dated August 10, 2005(23)
10.16(a)	Placement Agency Agreement for August 2005(11)
10.16(b)	Form of Subscription Agreement for August 2005 offering(22)
10.17	Form of Director and Officer Indemnification Agreement(21)
10.18	Code of Business Conduct and Ethics(21)
10.19	Master Services Agreement dated as of September 8, 2006 with Cingular Wireless, LLC(24)
10.20	August 17, 2007 investment agreement with Hunchun BaoLi Communication Co. Ltd. (“BAOLI”)(25)
10.21	November 9, 2007 first amendment to investment agreement with BAOI*
10.22	January 8, 2008 second amendment to investment agreement with BAOI*
10.23	November 8, 2007 Framework Agreement with BAOI*
10.24	December 8, 2007 Sino-Foreign Equity Joint Venture between the Registrant and BAOI (Exhibit A to Framework Agreement with BAOI)*
10.25	Form of License Agreement between the Registrant and BAOI (Exhibit B to Framework Agreement with BAOI)*
21	List of Subsidiaries*
23.1	Consent of Stonefield Josephson Inc, Independent Registered Public Accounting Firm*
23.2	Consent of PricewaterhouseCoopers LLP, Independent Registered Public Accounting Firm*
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*

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- (1) Incorporated by reference from the Registrant’s Quarterly Report on Form 10-Q filed for the quarter ended April 3, 1999.
  - (2) Incorporated by reference from the Registrant’s Quarterly Report on Form 10-Q filed for the quarter ended June 30, 2001.
  - (3) Incorporated by reference from Registrant’s Form 8-K dated March 13, 2006.
  - (4) Incorporated by reference from Registrant’s Form 8-K dated May 25, 2005.
  - (5) Incorporated by reference from the Registrant’s Registration Statement on Form S-1 (Reg. No. 33-56714).
  - (6) Incorporated by reference from the Registrant’s Quarterly Report on Form 10-Q filed for the quarter ended July 3, 1999.
  - (7) Incorporated by reference from the Registrant’s Registration Statement on Form S-8 (Reg. No. 333-90293).
  - (8) Incorporate by reference from Registrant’s Quarterly Report on Form 10-Q for the quarter ended March 29, 2003.
  - (9) Incorporated by reference from Registrant’s Current Report on Form 8-K filed June 25, 2003.
  - (10) Incorporated by reference from Registrants’ Registration Statement of Form S-3 (Reg. 333-89184).
  - (11) Incorporated by reference from Registrant’s Form 8-K dated August 10, 2005.
  - (12) Incorporated by reference from the Registrant’s Annual Report on Form 10-K filed for the year ended December 31, 1994.
  - (13) Incorporated by reference from the Registrant’s Registration Statement on Form S-8 (Reg. No. 333-56606) filed March 6, 2001.
  - (14) Incorporate by reference from Registrant’s Quarterly Report on Form 10-Q for the quarter ended March 29, 2003.
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- (15) Incorporated by reference from Registrant's Quarterly Report on Form 10-Q for the quarter ended April 3, 2004.
  - (16) Incorporated by reference from Registrants' Form 8-K dated March 29, 2005.
  - (17) Incorporated by reference from Registrants' Form 8-K dated June 25, 2003.
  - (18) Incorporated by reference from Registrant's Annual Report on Form 10-K for the year ended December 31, 2003.
  - (19) Incorporated by reference from Registrant's Quarterly Report on Form 10-Q for the quarter ended October 2, 2004.
  - (20) Incorporated by reference from Registrant's Annual Report on Form 10-K for the year ended December 31, 2004.
  - (21) Incorporated by reference from Registrant's Annual Report on Form 10-K for the year ended December 31, 2005.
  - (22) Incorporated by reference from Registrant's Form 8-K dated July 27, 2006.
  - (23) Incorporated by reference from Registrant's Quarterly Report on Form 10-Q for the quarter ended April 2, 2005.
  - (24) Incorporated by reference from Registrant's Annual Report on Form 10-K for the year ended December 31, 2006.
  - (25) Incorporated by reference from Registrant's Quarterly Report on Form 10-Q for the quarter ended September 29, 2007.
  - (26) Incorporated by reference from Registrant's Report on Form 8-K/A dated February 25, 2008.
    - \* Filed herewith.
    - \*\* Confidential treatment has been previously granted for certain portions of these exhibits.
    - \*\*\* This exhibit is a management contract or compensatory plan or arrangement.
- (b) Exhibits. See Item 15(a) above.

**Report of Independent Registered Public Accounting Firm**

To: The Board of Directors and Stockholders of Superconductor Technologies, Inc.  
Santa Barbara, California

We have audited the accompanying consolidated balance sheets of Superconductor Technologies, Inc. and subsidiaries as of December 31, 2007 and 2006, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the two years in the period ended December 31, 2007. Our audits also included the consolidated financial statement schedule listed in the Index at Item 15(a)(2) as of and for the years ended December 31, 2007 and 2006. These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Superconductor Technologies, Inc. and subsidiaries as of December 31, 2007 and 2006, and the results of its operations and its cash flows for each of the two years in the period ended December 31, 2007 in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, the related consolidated financial statement schedules as of and for the years ended December 31, 2007 and 2006, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

The accompanying financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America, which contemplate continuation of the company as a going concern. As discussed in Note 2, the Company has incurred significant net losses since its inception and has an accumulated deficit of \$199,985,000 and expects to incur substantial additional losses and costs. The foregoing matters raise substantial doubt about the Company's ability to continue as a going concern. Management's plans in regard to these matters are described in Note 2 of the accompanying financial statements. These financial statements do not include any adjustments that might result from the outcome of these uncertainties.

/s/ STONEFIELD JOSEPHSON, INC.

Los Angeles, California  
March 27, 2008

To the Board of Directors and Stockholders of  
Superconductor Technologies Inc.

In our opinion, the consolidated statements of operations, stockholders' equity and cash flows for the year ended December 31, 2005 present fairly, in all material respects, the results of operations and cash flows of Superconductor Technologies Inc. and its subsidiaries for the year ended December 31, 2005, in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedule for the year ended December 31, 2005 presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. These financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and financial statement schedule based on our audit. We conducted our audit of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 2 to the consolidated financial statements, the Company has had recurring losses and used \$9.4 million in cash for operations in 2005. These matters raise a substantial doubt about the Company's ability to continue as a going concern. Management's plans in regard to these matters are also described in Note 2. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

/s/ PRICEWATERHOUSECOOPERS LLP

Los Angeles, California  
March 3, 2006, except for effects of  
the reverse stock split discussed in Note 2,  
as to which the date is March 13, 2006

**SUPERCONDUCTOR TECHNOLOGIES INC.**  
**CONSOLIDATED BALANCE SHEETS**

	December 31, 2006	December 31, 2007
<b>ASSETS</b>		
<b>Current Assets:</b>		
Cash and cash equivalents	\$ 5,487,000	\$ 3,939,000
Accounts receivable, net	1,535,000	2,413,000
Inventory, net	5,978,000	3,415,000
Prepaid expenses and other current assets	507,000	442,000
<b>Total Current Assets</b>	<b>13,507,000</b>	<b>10,209,000</b>
Property and equipment, net of accumulated depreciation of \$18,599,000 and \$19,129,000, respectively	5,770,000	3,961,000
Patents, licenses and purchased technology, net of accumulated amortization of \$1,391,000 and \$1,722,000, respectively	2,409,000	2,236,000
Other assets	218,000	219,000
<b>Total Assets</b>	<b>\$ 21,904,000</b>	<b>\$ 16,625,000</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>Current Liabilities :</b>		
Accounts payable	\$ 1,725,000	\$ 1,467,000
Accrued expenses	1,610,000	1,405,000
Proceeds for shares to be issued	—	4,000,000
Current portion of capitalized lease obligations and long term debt	14,000	45,000
<b>Total Current Liabilities</b>	<b>3,349,000</b>	<b>6,917,000</b>
Other long term liabilities	604,000	518,000
<b>Total Liabilities</b>	<b>3,953,000</b>	<b>7,435,000</b>
<b>Commitments and contingencies (Notes 9, 10 and 11)</b>		
<b>Stockholders' Equity:</b>		
Preferred stock, \$.001 par value, 2,000,000 shares authorized, none issued and outstanding	—	—
Common stock, \$.001 par value, 250,000,000 shares authorized, 12,483,367 and 12,511,414 shares issued and outstanding, respectively	12,000	12,000
Capital in excess of par value	208,825,000	209,163,000
Notes receivable from stockholder and board member	(27,000)	—
Accumulated deficit	(190,859,000)	(199,985,000)
<b>Total Stockholders' Equity</b>	<b>17,951,000</b>	<b>9,190,000</b>
<b>Total Liabilities and Stockholders' Equity</b>	<b>\$ 21,904,000</b>	<b>\$ 16,625,000</b>

See accompanying notes to the consolidated financial statements



**SUPERCONDUCTOR TECHNOLOGIES INC.**  
**CONSOLIDATED STATEMENT OF OPERATIONS**

	For the Year Ended December 31,		
	2005	2006	2007
<b>Net revenues:</b>			
Net commercial product revenues	\$ 21,080,000	\$ 17,697,000	\$12,787,000
Government and other contract revenues	3,107,000	3,361,000	5,115,000
Sub license royalties	22,000	20,000	—
<b>Total net revenues</b>	<b>24,209,000</b>	<b>21,078,000</b>	<b>17,902,000</b>
<b>Costs and expenses:</b>			
Cost of commercial product revenues	18,989,000	15,922,000	12,944,000
Contract research and development	2,806,000	2,407,000	2,906,000
Other research and development	4,214,000	3,488,000	3,172,000
Selling, general and administrative	11,442,000	9,086,000	8,123,000
Restructuring expenses and impairment charges	1,197,000	38,000	—
Write off Goodwill	—	20,107,000	—
<b>Total costs and expenses</b>	<b>38,648,000</b>	<b>51,048,000</b>	<b>27,145,000</b>
Loss from operations	(14,439,000)	(29,970,000)	(9,243,000)
Interest income	342,000	391,000	156,000
Interest expense	(116,000)	(45,000)	(39,000)
<b>Net loss</b>	<b>\$(14,213,000)</b>	<b>\$(29,624,000)</b>	<b>\$(9,126,000)</b>
<b>Basic and diluted net loss per common share</b>	<b>\$ (1.24)</b>	<b>\$ (2.37)</b>	<b>\$ (0.73)</b>
<b>Basic and diluted weighted average number of common shares outstanding</b>	<b>11,418,504</b>	<b>12,483,367</b>	<b>12,487,593</b>

See accompanying notes to the consolidated financial statements

**SUPERCONDUCTOR TECHNOLOGIES INC.**  
**CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY**

	<u>Convertible Preferred Stock</u>		<u>Common Stock</u>		<u>Capital in Excess of Par Value</u>	<u>Receivable From Stockholder</u>	<u>Accumulated Deficit</u>	<u>Total</u>
	<u>Shares</u>	<u>Amount</u>	<u>Shares</u>	<u>Amount</u>				
<b>Balance at December 31, 2004</b>	—	—	10,771,103	\$11,000	\$197,080,000	\$ (820,000)	\$(147,022,000)	\$ 49,249,000
Exercise of stock options Issuance of common stock			1,712,329	1,000	11,440,000			11,441,000
Issuance of options and warrants					25,000			25,000
Reserve for impairment						755,000		755,000
Net loss							(14,213,000)	(14,213,000)
<b>Balance at December 31, 2005</b>	—	—	12,483,431	12,000	208,545,000	(65,000)	(161,235,000)	47,257,000
Issuance of common stock and warrants			(64)					
Issuance of options					280,000			280,000
Reserve for impairment						38,000		38,000
Net loss							(29,624,000)	(29,624,000)
<b>Balance at December 31, 2006</b>	—	—	12,483,367	12,000	208,825,000	(27,000)	(190,859,000)	17,951,000
Exercise of stock options			3,350		26,000			26,000
Issuance of common stock					(27,000)			(27,000)
Issuance of options and warrants			24,697		339,000			339,000
Reserve for impairment						27,000		27,000
Net loss							(9,126,000)	(9,126,000)
<b>Balance at December 31, 2007</b>	—	—	12,511,414	\$12,000	\$209,163,000	\$ —	\$(199,985,000)	\$ 9,190,000

See accompanying notes to the consolidated financial statements.

**SUPERCONDUCTOR TECHNOLOGIES INC.**  
**CONSOLIDATED STATEMENT OF CASH FLOWS**

	For the Year Ended December 31		
	2005	2006	2007
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Net loss	\$(14,213,000)	\$(29,624,000)	\$(9,126,000)
Adjustments to reconcile net loss to net cash used for operating activities:			
Depreciation and amortization	3,225,000	2,600,000	2,333,000
Warrants and options charges	25,000	280,000	339,000
Provision for excess and obsolete inventories	984,000	360,000	160,000
Forgiveness of note receivable from former CEO	150,000	—	—
Reserve for impairment of note and interest receivable from stockholder	924,000	38,000	(583,000)
Write off Goodwill	—	20,107,000	—
Gain on disposal of property and equipment	(138,000)	—	—
Changes in assets and liabilities:			
Accounts receivable	(732,000)	631,000	(877,000)
Inventory	2,979,000	(974,000)	2,403,000
Prepaid expenses and other current assets	112,000	115,000	574,000
Patents and licenses	(154,000)	(217,000)	(169,000)
Other assets	(23,000)	128,000	16,000
Accounts payable and accrued expenses	(2,543,000)	(727,000)	(465,000)
Net cash used in operating activities	(9,404,000)	(7,283,000)	(5,395,000)
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>			
Proceeds from the sale of property and equipment	216,000	—	26,000
Purchase of property and equipment	(261,000)	(229,000)	(191,000)
Net cash used in investing activities	(45,000)	(229,000)	(165,000)
<b>CASH FLOW FROM FINANCING ACTIVITIES:</b>			
Proceeds from Shares to be issued	—	—	4,000,000
Proceeds from short-term borrowings	662,000	—	—
Payments on short-term borrowings	(1,600,000)	—	—
Payments on long-term obligations	(43,000)	(19,000)	(14,000)
Gross proceeds from sale of common stock and exercise of warrants and options	12,500,000	—	26,000
Payment of common stock issuance costs	(1,854,000)	—	—
Net cash provided by (used in) financing activities	9,665,000	(19,000)	4,012,000
Net increase (decrease) in cash and cash equivalents	216,000	(7,531,000)	(1,548,000)
Cash and cash equivalents at beginning of year	12,802,000	13,018,000	5,487,000
Cash and cash equivalents at end of year	<u>\$ 13,018,000</u>	<u>\$ 5,487,000</u>	<u>\$ 3,939,000</u>

See accompanying notes to the consolidated financial statements.

**SUPERCONDUCTOR TECHNOLOGIES INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 1 —The Company**

Superconductor Technologies Inc. (together with our subsidiaries, “we” or “us”) was incorporated in Delaware on May 11, 1987 and maintains its headquarters in Santa Barbara, California. We operate in a single industry segment, the research, development, manufacture and marketing of high-performance infrastructure products for wireless voice and data applications. Our commercial products are divided into three product offerings: SuperLink (high-temperature superconducting filters), AmpLink (high performance, ground-mounted amplifiers) and SuperPlex (high performance multiplexers). Our research and development contracts are used as a source of funds for our commercial technology development. From 1987 to 1997, we were engaged primarily in research and development and generated revenues primarily from government research contracts.

We continue to be involved as either contractor or subcontractor on a number of contracts with the United States government. These contracts have been and continue to provide a significant source of revenues for us. For the years ended December 31, 2005, 2006, and 2007, government related contracts account for 13%, 16% and 29%, respectively, of our net revenues.

**Note 2 —Summary of Significant Accounting Policies**

***Basis of Presentation***

Our financial statements have been prepared assuming that it will continue as a going concern.

In 2007, we incurred a net loss of \$9.1 million and negative cash flows from operations of \$5.4 million. In 2006 and 2005 we incurred net losses of \$29.6 million and \$14.2 million, respectively, and negative cash flows from operations of \$7.3 million and \$9.4 million, respectively.

Our principal sources of liquidity consist of existing cash balances and funds expected to be generated from future operations. On August 17, 2007, we entered into an agreement with Hunchun BaoLi Communication Co. Ltd. (“BAOLI”). On February 27, 2008, the transactions contemplated by our investment agreement with BAOLI closed and in exchange for \$15.0 million in cash we issued to BAOLI and two related purchasers a total of (a) 3,101,360 shares of our common stock and (b) 611,523 shares of our Series A Preferred Stock (convertible into 6,115,230 shares of our common stock).

We believe one of the key factors to our liquidity beyond 2008 will be our intention to successfully execute on our plans to increase sales levels. Our cash requirements will also depend on numerous other variable factors, including the rate of growth of sales, the timing and levels of products purchased, payment terms and credit limits from manufacturers, the timing and level of accounts receivable collections and the timing and levels of new product development.

There is no assurance that additional financing (public or private) will be available on acceptable terms or at all. If we issue additional equity securities to raise funds, the ownership percentage of our existing stockholders would be reduced. New investors may demand rights, preferences or privileges senior to those of existing holders of common stock. If we cannot raise any needed funds, it 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.

The factors described above raise substantial doubt about our ability to continue as a going concern. These financial statements do not include any adjustments that might result from this uncertainty.

***Principles of Consolidation***

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

**SUPERCONDUCTOR TECHNOLOGIES INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

***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 quality financial institutions and from time to time exceed FDIC limits. Historically, we have not experienced any losses due to such concentration of credit risk.

***Accounts Receivable***

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

***Revenue Recognition***

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

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

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

***Gross versus Net Presentation***

In accordance with EITF 06-03 "How Taxes Collected from Customers and Remitted to Governmental Authorities should be Presented in the Income Statement (Gross versus Net Presentation)", the Company collects sales tax on its sales to customers. These sales taxes are accounted for by the Company on a net basis and excluded from revenue. These amounts are included in both accounts receivable and accrued expenses.

***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

**SUPERCONDUCTOR TECHNOLOGIES INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

to us during such warranty period at no cost to the customer. Our estimate for warranty related costs is recorded at the time of sale based on our actual historical product return rates and expected repair costs. Such costs have been within our expectations.

***Guarantees***

In connection with the sales and manufacturing of our commercial products, we indemnify, without limit or term, our customers and contract manufactures 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 guarantee 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 guarantees.

***Research and Development Costs***

Research and development costs are expensed as incurred and include salary, facility, depreciation and material expenses. Research and development costs incurred solely in connection with research and development contracts are charged to contract research and development expense. Other research and development costs are charged to other research and development 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 or disposed. Our inventory reserves establish a new cost basis for inventory and are not reversed until the related inventory is sold or otherwise disposed. 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 expensed 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 five 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 2007, we disposed of \$1.3 million of older, fully depreciated equipment. There was no gain or loss on said disposition.

***Patents, Licenses and Purchased Technology***

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

**SUPERCONDUCTOR TECHNOLOGIES INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

***Goodwill***

Goodwill represents the excess of purchase price over fair value of net assets acquired in connection with the acquisition of Conductus in December 2002. Conductus was acquired primarily for the synergies the acquisition would bring to our existing business of developing, manufacturing and marketing products for the commercial wireless telecommunications business and for the synergies it would have on our fund raising abilities.

At July 2006, our market capitalization had declined to \$25.5 million, an amount less than our total book value. We concluded that our declining stock price constituted an event under FAS 142 and required us to test for goodwill impairment as of July 2006. Our analysis led us to reasonably estimate at that time that our fair market value was less than our net assets excluding goodwill. Accordingly, we recorded a full write-down of the goodwill (\$20.1 million) in the second quarter 2006.

***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 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. 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 fiscal 2007 and determined there was no impairment.

***Restructuring Expenses***

Liability for costs associated with an exit or disposal activity are recognized when the liability is incurred.

***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***

The Company accounts for income taxes in accordance with Statement of Financial Accounting Standards No. 109, *Accounting for Income Taxes* ("SFAS 109"), which requires that the Company 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.

In July 2006, the FASB issued Interpretation ("FIN") No. 48, *Accounting for Uncertainty in Income Taxes — An Interpretation of FASB Statement No. 109* ("FIN 48"). FIN 48 provides detailed guidance for the financial statement recognition, measurement and disclosure of uncertain tax positions recognized in an enterprise's financial statements in accordance with SFAS 109. Income tax positions must meet a more-likely-than-not recognition threshold at the effective date to be recognized upon the adoption of FIN 48 and in subsequent periods. We adopted FIN 48 effective January 1, 2007, and the provisions of FIN 48 have been applied to all income tax positions commencing from that date. There was no material impact from this adoption. As of December 31, 2007, we had net operating loss carryforwards for federal and state income tax purposes of approximately \$285.1 million and \$154.7 million, respectively. We are currently evaluating the potential limitations on our ability to utilize our net



**SUPERCONDUCTOR TECHNOLOGIES INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

operating loss carryforwards as a result of the recent investment by BAOLI. 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 sheet.

***Marketing Costs***

All costs related to marketing and advertising our products are expensed as incurred or at the time the advertising takes place. Advertising costs were not material in each of the three years in the period ended December 31, 2007.

***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***

Effective January 1, 2006, we adopted the provisions of Statement of Financial Accounting Standards (“SFAS”) No. 123(revised 2004), “Share-Based Payment” (“SFAS No. 123(R)”). Under this provision, the share-based compensation cost recognized beginning January 1, 2006 includes compensation cost for (i) all share-based payments granted prior to, but not vested as of January 1, 2006, based on the grant date fair value originally estimated in accordance with the provisions of SFAS No. 123, “Accounting for Stock-Based Compensation,” (“SFAS No. 123”) and (ii) all share-based payments granted subsequent to January 1, 2006, based on the grant date fair value estimated in accordance with the provisions of SFAS No. 123(R). Compensation cost under SFAS No. 123(R) is recognized ratably using the straight-line attribution method over the expected vesting period. Prior periods are not restated under this transition method.

As a result of adopting SFAS 123R, the impact to the Consolidated Statement of Operations for the years ended December 31, 2007 and 2006 on net income, for stock options and awards, was an expense of \$339,000 and \$280,000 and \$0.03 and \$0.02, respectively, on basic and diluted earnings per share. No stock compensation cost was capitalized during the period.

In the years prior to 2006, as permitted under Statement of Financial Accounting Standards No. 123 (“SFAS 123”), “Accounting for Stock-Based Compensation”, we elected to follow Accounting Principles Board Opinion No. 25, “Accounting for Stock Issued to Employees” in accounting for our stock options and other stock-based employee awards. Pro forma information regarding net loss and loss per share, as calculated under the provisions of SFAS 123, are disclosed in the notes to the financial statements. We accounted for equity securities issued to non-employees in accordance with the provision of SFAS 123 and Emerging Issues Task Force 96-18. If we had elected to recognize compensation expense for employee awards based upon the fair value at the grant date

**SUPERCONDUCTOR TECHNOLOGIES INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

consistent with the methodology prescribed by SFAS 123, our net loss and net loss per share in 2005 would have been increased to the pro forma amounts indicated below:

	<b>For the Year Ended December 31, 2005</b>
<b>Net loss:</b>	
As reported	\$ (14,213,000)
Stock-based employee compensation included in net loss	—
Stock-based compensation expense determined under fair value method	(6,459,000)
Pro forma	<u>\$ (20,672,000)</u>
<b>Basic and diluted loss per share</b>	
As reported	\$ (1.24)
Stock-based compensation expense determined under fair value method	(0.57)
Pro forma	<u>\$ (1.81)</u>

***Use of Estimates***

The preparation of financial statements in conformity with generally accepted accounting principles requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. The significant estimates in the preparation of the financial statements relate to the assessment of the carrying amount of accounts receivable, inventory, fixed assets, intangibles, goodwill, estimated provisions for warranty costs, accruals for restructuring and lease abandonment costs, contract revenues, income taxes and disclosures related to the litigation. Actual results could differ from those estimates and such differences may be material to the financial statements. At December 31, 2007, we reversed \$319,000 of product line exit cost accruals. This accrual was established in 2002 in the amount of \$1,042,000 and represented the estimated costs to be incurred with a customer to support commercial product units previously purchased from Conductus for a period of five years.

***Fair Value of Financial Instruments***

The carrying amount of cash and cash equivalents, accounts receivable, accounts payable and accrued expenses approximate fair value due to the short-term nature of these instruments. We estimate that the carrying amount of the debt approximates fair value based on our current incremental borrowing rates for similar types of borrowing arrangements.

***Comprehensive Income***

We have no items of other comprehensive income in any period and consequently do not report 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. Net commercial product revenues are primarily derived from the sales of our SuperLink, AmpLink and SuperPlex products. We currently sell most of our products directly to wireless network operators in the United States. Net revenues derived

**SUPERCONDUCTOR TECHNOLOGIES INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

principally from government research and development contracts are presented separately on the statement of operations for all periods presented.

**Reverse Stock Split**

On March 13, 2006, we made a one-for-ten (1:10) reverse stock split effective as of the open of business. All results prior to that time have been adjusted to reflect the impact of that split.

***Certain Risks and Uncertainties***

Our long-term prospects are dependent upon the continued and increased market acceptance for our 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. In 2007, we had three customers that represented 40%, 14% and 7% of total net revenues. At December 31, 2007, these three customers represented 26%, 15% and 2% of accounts receivable. In 2006, these three customers represented 44%, 20% and 16% of total net revenues and in 2005 we had three customers that represented 31%, 37% and 15% of total net revenues. 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 one supplier for purchase of high quality substrates for growth of high-temperature superconductor films and on a limited number of suppliers for other 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 guarantee because of the uncertainty as to whether a claim might arise and how much it might total.

***Recent Accounting Pronouncements***

In February 2008, the FASB issued FSP 157-2 “Partial Deferral of the Effective Date of Statement 157” (FSP 157-2). FSP 157-2 delays the effective date of SFAS No. 157, for all non-financial assets and non-financial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually) to fiscal years beginning after November 15, 2008. We are currently assessing the impact of SFAS No. 157 for non-financial assets and non-financial liabilities on our consolidated financial position and results of operations. We do not expect that the implementation of this standard, for financial assets and financial liabilities, will have a material impact on our consolidated financial position and results of operations.

In December 2007 the FASB issued Statement of Financial Accounting Standards No. 141 (revised 2007), “Business Combinations” (FAS 141(R)) and No. 160, “Noncontrolling Interests in Consolidated Financial Statements, an amendment of ARB No. 51 (FAS 160)”. FAS 141(R) will change how business acquisitions are accounted for and FAS 160 will change the accounting and reporting for minority interests, which will be recharacterized as noncontrolling interests and classified as a component of equity. FAS 141(R) and FAS 160 are effective for fiscal years beginning on or after December 15, 2008 (January 1, 2009 for the Company). The adoption of FAS 141(R) and FAS 160 are not expected to have a material impact on the Company’s consolidated financial statements.

In June 2007 the FASB ratified EITF No. 07-3, or EITF 07-3, *Accounting for Nonrefundable Advance Payments for Goods or Services to Be Used in Future Research and Development Activities*. EITF 07-3 requires

**SUPERCONDUCTOR TECHNOLOGIES INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

non-refundable advance payments for goods and services to be used in future research and development activities to be recorded as an asset and the payments to be expensed when the research and development activities are performed. EITF 07-3 is effective for fiscal years beginning after December 15, 2007. We are currently evaluating the impact of adopting EITF 07-3 on our results of operations and financial condition.

In June 2007, the FASB ratified EITF 06-11 “Accounting for the Income Tax Benefits of Dividends on Share-Based Payment Awards” (“EITF 06-11”). EITF 06-11 provides that tax benefits associated with dividends on share-based payment awards be recorded as a component of additional paid-in capital. EITF 06-11 is effective, on a prospective basis, for fiscal years beginning after December 15, 2007. We believe there will be no impact from EITF 06-11 on our consolidated financial position and results of operations.

In May 2007, the FASB issued FASB Staff Position (“FSP”) FIN 48-1 “Definition of Settlement in FASB Interpretation No. 48” (FSP FIN 48-1). FSP FIN 48-1 provides guidance on how to determine whether a tax position is effectively settled for the purpose of recognizing previously unrecognized tax benefits. FSP FIN 48-1 is effective retroactively to January 1, 2007. The implementation of this standard did not have a material impact on our consolidated financial position or results of operations.

In February 2007, the FASB issued SFAS No. 159 “The Fair Value Option for Financial Assets and Financial Liabilities” (SFAS No. 159). SFAS No. 159 permits entities to choose to measure many financial assets and financial liabilities at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. We do not expect that the implementation of this standard will have a material impact on our consolidated financial position and results of operations.

**Note 3 —Short Term Borrowings**

We have a line of credit with a bank. The line of credit expires July 2008 and is structured as a sale of accounts receivable. The agreement provides for the sale of up to \$5 million of eligible accounts receivable, with advances to us totaling 80% of the receivables sold. Advances under the agreement are collateralized by all of our assets. Under the terms of the agreement, we continue to service the sold receivables and are subject to recourse provisions.

Advances bear interest at the prime rate (7.25% at December 31, 2007) plus 2.50% subject to a minimum monthly charge. There was no amount outstanding under this borrowing facility at December 31, 2007.

The agreement contains representations and warranties, affirmative and negative covenants and events of default customary for financings of this type. The failure to comply with these provisions, or the occurrence of any one of the events of default, would prevent any further borrowings and would generally require the repayment of any outstanding borrowings. Such representations, warranties and events of default include (a) non-payment of debt and interest hereunder, (b) non-compliance with terms of the agreement covenants, (c) insolvency or bankruptcy, (d) material adverse change, (e) merger or consolidation where our shareholders do not hold a majority of the voting rights of the surviving entity, (f) transactions outside the normal course of business, or (g) payment of dividends.

**Note 4 —Retirement of Company’s Chief Executive Officer**

On March 15, 2005, our Chief Executive Officer and President retired. In connection with the retirement, we agreed to the continuation of his salary and benefits for one year and to immediately vest and extend all his outstanding stock options and the executive agreed to provide certain consulting services as requested by us. Also, in connection with the retirement, a \$150,000 loan made to our Chief Executive Officer in 2001, and in accordance with the existing terms of a promissory note in effect prior to the adoption of the Sarbanes-Oxley Act of 2002, was forgiven. We recognized expense of \$565,000 relating to the retirement of the CEO in 2005.

**SUPERCONDUCTOR TECHNOLOGIES INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

**Note 5 —Notes Receivable From Stockholder**

A former director and stockholder executed two notes aggregating \$820,244 in principal in connection with the exercise in December 2000 of two options. Through the third quarter of, 2005, we carried the principal (as “Notes Receivable from Stockholder”) and accrued interest (as “Prepaid Expenses and Other Current Assets”) for both notes as assets on our balance sheet. In December 2005, we filed a lawsuit to collect both notes and recorded a reserve for the value of the notes (principal plus accrued interest) in excess of the market value of the collateral securing the notes. In 2007, we received \$610,000 in full satisfaction of our claims including interest and attorneys’ fees, and the rescinded the second purported option exercise and canceled the related note.

**Note 6 —Income Taxes**

We incurred a net loss in each year of operation since inception resulting in no current or deferred tax expense for 2005, 2006 and 2007.

The benefit for income taxes differs from the amount obtained by applying the federal statutory income tax rate to loss before benefit for income taxes for the years ended December 31, 2005, 2006 and 2007 as follows:

	For the Year Ending December 31		
	2005	2006	2007
Tax benefit computed at Federal statutory rate	34.0%	34.0%	34.0%
Increase (decrease) in taxes due to:			
Change in valuation allowance	(39.8)	(16.7)	(39.8)
State taxes, net of federal benefit	5.8	5.8	5.8
Impairment of Goodwill (not deductible for tax)	—	(23.1)	—
	—%	—%	—%

The significant components of deferred tax assets (liabilities) at December 31 are as follows:

	For the Year Ended December 31,	
	2006	2007
Loss carryforwards	\$ 101,519,000	\$ 105,460,000
Capitalized research and development	3,972,000	2,710,000
Depreciation	2,430,000	2,582,000
Tax credits	3,226,000	3,822,000
Inventory	559,000	415,000
Purchase accounting adjustments	93,000	46,000
Acquired intellectual property	(286,000)	(190,000)
Other	640,000	437,000
Less: valuation allowance	(112,153,000)	(115,282,000)
	\$ —	\$ —

The valuation allowance increased by \$3,129,000 in 2007, increased by \$5,854,000 in 2006 and decreased by \$290,000 in 2005.

As of December 31, 2007, we had net operating loss carryforwards for federal and state income tax purposes of approximately \$285.1 million and \$154.7 million, respectively, which expire in the years 2008 through 2027. Of these amounts \$88.3 million and \$23.5 million, respectively, resulted from the acquisition of Conductus. Included in

**SUPERCONDUCTOR TECHNOLOGIES INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

the net operating loss carryforwards are deductions related to stock options of approximately \$24.1 million and \$13.1 million for federal and California income tax purposes, respectively. To the extent net operating loss carryforwards are recognized for accounting purposes the resulting benefits related to the stock options will be credited to stockholders' equity. In addition, we had research and development and other tax credits for federal and state income tax purposes of approximately \$2.7 million and \$1.3 million, respectively, which expire in the years 2008 through 2027. Of these amounts \$661,000 and \$736,000, respectively resulted from the acquisition of Conductus.

Due to the uncertainty surrounding their realization, we have recorded a full valuation allowance against our net deferred tax assets. Accordingly, no deferred tax asset has been recorded in the accompanying balance sheet.

Section 382 of the Internal Revenue Code imposes an annual limitation on the utilization of net operating loss carryforwards based on a statutory rate of return (usually the "applicable federal funds rate", as defined in the Internal Revenue Code) and the value of the corporation at the time of a "change of ownership" as defined by Section 382. We had changes in ownership in August 1999 and December 2002. Therefore, the ability to utilize net operating loss carryforwards of \$97.3 million incurred prior to the ownership changes will be subject in future periods to an annual limitation of \$1.3 million. In addition, we acquired the right to Conductus' net operating losses, which are also subject to the limitations imposed by Section 382. Conductus underwent three ownership changes, which occurred in February 1999, February 2001 and December 2002. Therefore, the ability to utilize Conductus' net operating loss carryforwards of \$88.3 million incurred prior to the ownership changes will be subject in future periods to annual limitation of \$700,000. Net operating losses incurred by us subsequent to the ownership changes totaled \$99.5 million and are not subject to this limitation. We are currently evaluating the potential limitations on our ability to utilize our net operating loss carryforwards as a result of the recent investment by BAOLI.

**Note 7 —Stockholders' Equity*****Preferred Stock***

Pursuant to our Certificate of Incorporation, the Board of Directors is authorized to issue up to 2,000,000 shares of preferred stock (par value \$.001 per share) in one or more series and to fix the rights, preferences, privileges, and restrictions, including the dividend rights, conversion rights, voting rights, redemption price or prices, liquidation preferences, and the number of shares constituting any series or the designation of such series.

***Common Stock***

On August 17, 2007, we entered into an agreement with Hunchun BaoLi Communication Co. Ltd. under which on February 27, 2008 we issued to BAOLI and two related purchasers a total of (a) 3,101,360 shares of our common stock and (b) 611,523 shares of our Series A Preferred Stock (convertible under certain conditions into 6,115,230 shares of our common stock) in exchange for \$15.0 million in cash. At December 31, 2007 we had received \$4.0 million from BAOLI and in January 2008 we received the remaining \$11.0 million. This transaction caused the exercise price and the number of shares of the warrants issued to a bridge lender under our 2004 bridge loan to be adjusted to \$8.34 and 110,880, respectively, under the anti-dilution provisions of the warrants. In November 2007, the holder of these warrants elected the net exercise provision of this warrant, where by the holder received 24,697 shares. The BAOLI transaction also caused the exercise price of the warrants issued to lenders under our 2005 financing to be adjusted to \$7.08 under the anti-dilution provisions of the warrants.

We raised no money from the sale of our common stock in 2006.

In August 2005, we raised net proceeds of \$11,441,000, net of offering costs of \$1,059,000, from the public sale of 1,712,329 shares of common stock at \$7.30 per share and 5-year warrants to purchase an additional 342,466 shares of common stock exercisable at \$11.10 per share. The warrants become exercisable on February 16, 2006. The warrant agreement also contains the following significant terms: (i) in the event of changes in our outstanding Common Stock, the number of shares and their price under the warrant shall be correspondingly



**SUPERCONDUCTOR TECHNOLOGIES INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

adjusted and (ii) if, at any time while the warrants are outstanding, we issue additional shares at an effective price less than the warrant price the number of shares and their price will be adjusted. This transaction caused the exercise price and the number of shares of the warrants issued to a bridge lender under our 2004 bridge loan to be adjusted to \$13.30 and 69,549, respectively, under the anti-dilution provisions of the warrants.

***Stock Options***

We have five stock option plans, the 1992 Stock Option Plan, the nonstatutory 1992 Directors Stock Option Plan, 1998 and 1999 Stock Option Plans and the 2003 Equity Incentive Plan (collectively, the “Stock Option Plans”). The 1988 Stock Option Plan expired in 1998 and the 1992 Stock Option Plan and the nonstatutory 1992 Directors Stock Option Plan expired in 2002. During 2003, the 1998 and 1999 Stock Option Plans were replaced by the 2003 Equity Incentive Plan. Under the 2003 Equity Incentive Plan, stock awards may consist of stock options, stock appreciation rights, restricted stock awards, performance awards, and performance share awards. Stock awards may be made to our directors, key employees, consultants, and non-employee directors. Stock options granted under these plans must be granted at prices no less than 100% of the market value on the date of grant. Both stock options and restricted stock awards have been granted under these plans. Generally, stock options become exercisable in installments over a minimum of four years, beginning one year after the date of grant, and expire not more than ten years from the date of grant, with the exception of 10% or greater stockholders which may have options granted at prices no less than the market value on the date of grant, and expire not more than five years from the date of grant. There were no stock option exercises in 2006 and 3,350 shares were exercised in 2007.

At our 2007 Annual Meeting, the stockholders approved an increase in the total shares available for grants under the 2003 Equity Plan from 1,200,000 shares of common stock to 2,500,000 shares of common stock.

During 2005, our President and Chief Executive Officer, as well as another board member, retired. In connection with these retirements, we modified the terms of all the stock options held by these individuals to fully vest them and to extend the term until the earlier of the fifth anniversary of the retirement or the normal expiration date. Since these options had no intrinsic value at the date of modification, the modifications did not impact our statement of operations.

In 2005, the Compensation Committee of the Board of Directors made grants of performance based stock options totaling 40,816 to our officers and certain managers. The Compensation Committee determined that the financial performance criteria for these options were not met and therefore these options were canceled.

On December 1, 2005, the Compensation Committee of our Board of Directors approved the accelerated vesting of all time-vested outstanding out-of-the-money stock options held by current employees or consultants. For this purpose, the Compensation Committee defined “out-of-the-money options” as options having an exercise price equal to or greater than \$5.80 per share (the market price on the date of the committee’s decision to accelerate the vesting). The acceleration of vesting increased the pro forma expense in 2005 by \$3.7 million. We accelerated the vesting of these options in anticipation of the impact of Statement of Financial Accounting Standard No. 123R (“SFAS 123R”) Share-Based Payment. The primary purpose of the accelerated vesting was to minimize the amount of compensation expense recognized in relation to the underwater options in future periods following our adoption of SFAS 123R. In addition, because these options had exercise prices in excess of current market values and were not fully achieving their original objectives of incentive compensation and employee retention, we believe that the acceleration has had a positive effect on employee morale and retention.



## SUPERCONDUCTOR TECHNOLOGIES INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

For the years ended December 31, 2006 and 2007, the weighted average fair value has been 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:

	Year Ended December 31,	
	2006	2007
Per share fair value at grant date	\$2.55	\$2.15
Risk free interest rate	4.82%	4.34%
Expected volatility	95%	98%
Dividend yield	0%	0%
Expected life in years	4.0	4.0

The expected life was based on the contractual term of the options and the expected employee exercise behavior. Typically, options to our employees have a 4 year vesting term and a 10 year contractual term. Four year vesting term options vest at 25% after one year and ratably, on a monthly basis, thereafter. Options to Board Members have a 2 year vesting term and a 10 year contractual term. Two year vesting term options vest at 50% after one year and 50% after two years. The risk-free interest rate is based on the U.S. Treasury zero-coupon issues with a remaining term equal to the expected option life assumed at the grant date. The future volatility is based on our 4 year historical volatility. We used an expected dividend yield of 0% because we have never paid a dividend and do not anticipate paying dividends. We assumed a 10% forfeiture rate based on historical stock option cancellation rates over the last 4 years.

The impact of the stock options to the Consolidated Statement of Operations for the years ended December 31, 2007 and 2006 on net income was an expense of \$115,000 and \$187,000 and \$0.01 and \$0.01, respectively, on basic and diluted earnings per share. No stock compensation cost was capitalized during the periods. The total compensation cost related to non-vested awards not yet recognized is \$175,000 and the weighted-average period over which the cost is expected to be recognized is 2.75 years. Prior to 2006, we did not recognize compensation expense for issuance of stock options.

**SUPERCONDUCTOR TECHNOLOGIES INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

At December 31, 2007, 1,585,397 shares of common stock were available for future grant of options and 741,858 options had been granted but not yet exercised. Option activity during the three years ended December 31, 2007 was as follows:

	Number of Shares	Weighted Average Exercise Price
<b>Outstanding at December 31, 2004</b>	<b>946,725</b>	<b>\$ 55.21</b>
Granted	453,206	8.02
Canceled	(197,555)	37.18
Exercised	—	—
<b>Outstanding at December 31, 2005</b>	<b>1,202,376</b>	<b>40.38</b>
Granted	80,900	3.70
Canceled	(128,335)	34.64
Exercised	—	—
<b>Outstanding at December 31, 2006</b>	<b>1,154,941</b>	<b>38.33</b>
Granted	45,670	2.96
Canceled	(455,403)	41.68
Exercised	(3,350)	7.42
<b>Outstanding at December 31, 2007</b>	<b>741,858</b>	<b>\$ 34.24</b>

The following table summarizes information concerning currently outstanding and exercisable stock options at December 31, 2007:

Range of Exercise Prices	Number Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Exercisable	
				Number Exercisable	Weighted Average Exercise Price
\$1.43 — \$5.90	102,800	8.62	\$ 3.28	35,367	\$ 3.85
\$6.10 — \$7.52	248,670	7.50	\$ 6.91	238,670	\$ 6.89
\$8.00 — \$10.40	97,615	4.96	\$ 9.66	96,364	\$ 9.68
\$10.80 — \$38.75	111,645	4.11	\$ 28.06	111,645	\$ 28.06
\$39.00 — \$493.75	181,128	2.67	\$ 106.40	181,128	\$ 106.40
	<u>741,858</u>	5.64	\$ 34.24	<u>663,174</u>	\$ 37.87

Our outstanding options expire by the end of December 2017. The weighted-average contractual term of stock options currently exercisable is slightly less than 5.6 years. At December 31, 2007, 100,400 shares of outstanding stock options and 32,967 exercisable options had an exercise price less than the current market value and had an intrinsic value of \$235,000 and \$61,000, respectively. The number of options exercisable and weighted average exercise price at December 31, 2005 and 2006 totaled 1,162,330 and \$41.32 and 1,067,296 and \$41.13, respectively.

Prior to 2006 we adopted the disclosure-only provisions of Statement of Financial Accounting Standards No. 123, ("SFAS 123"), "Accounting for Stock-Based Compensation." Accordingly, no compensation cost had been recognized for the stock-based compensation other than for non-employees.

The fair value of the options granted in 2005 was estimated for purposes of the pro forma amounts in Note 2 as of the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions for 2005: dividend yield of zero percent; expected volatilities of 93.85-95%; risk-free interest rates of 4.28-4.62%;

## SUPERCONDUCTOR TECHNOLOGIES INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

and expected life of 4.0 years. All options granted during 2005 were granted at the then fair market value of our common stock. The weighted average fair value of options granted in 2005 was \$5.50.

**Restricted Stock Awards**

In July 2006, for the first time we issued restricted stock awards. A total of 331,000 shares were granted and will fully vest in one single installment on the second anniversary of the grant date in July 2008. The per share weighted average grant-date fair value was \$1.50. A 10% forfeiture rate was assumed.

The impact to the Consolidated Statement of Operations for the year ended December 31, 2007 on net income was an expense of \$223,000 and \$0.02 on basic and diluted earnings per share. The 2006 impact on net income was an expense of \$93,000 and \$0.01 on basic and diluted earnings per share. No stock compensation cost was capitalized during either period. The total compensation cost related to non-vested awards not yet recognized is \$130,000 and the weighted-average period over which the cost is expected to be recognized is seven months.

**Warrants**

The following is a summary of outstanding warrants at December 31, 2007:

	Common Shares			
	Total	Currently Exercisable	Price per Share	Expiration Date
Warrants and options related to issuance of common stock	342,466	342,466	\$ 7.08	August 16, 2010* **
	116,279	116,279	29.00	June 24, 2008*
Warrants related to April 2004 Bridge Loans	10,000	10,000	18.50	April 28, 2011 *
Total	<u>468,745</u>	<u>468,745</u>		

\* The terms of these warrants contain net exercise provisions, wherein instead of a cash exercise holders can elect to receive common stock equal to the difference between the exercise price and the average closing sale price for common shares over 10-30 days immediately preceding the exercise date.

\*\* The terms of these warrants contain antidilution adjustment provisions related to issuances at certain prices.

No warrants were exercised during 2005 and 2006.

During 2007 the following warrants were exercised:

	Warrants		Common Shares Issued	
	Warrants Exercised	Price per Share	For Cash	In Accordance With Net Exercise Provisions
Warrants related to issuance of common stock	<u>24,697</u>	<u>\$ 10.73</u>	<u>—</u>	<u>24,697</u>

**Note 8 —Employee Savings Plan**

In December 1989, the Board of Directors approved a 401(k) savings plan (the “401(k) Plan”) for our employees that became effective in 1990. Eligible employees may elect to make contributions under the terms of the 401(k) Plan; however, contributions by us are made at the discretion of management. We made no contributions to the 401(k) Plan in 2007.

**SUPERCONDUCTOR TECHNOLOGIES INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

**Note 9 —Commitments and Contingencies**

***Operating Leases***

We lease our offices and production facilities under a non-cancelable operating lease that expires in four years. This lease contains a minimum rent escalation clause that requires additional rental amounts after the first year. Rent expense for this lease with minimum annual rent escalation is recognized on a straight line basis over the minimum lease term. This lease also requires us to pay utilities, insurance, taxes and other operating expenses and contains one five-year renewal option at 95% of the then current market rental value.

For 2005, 2006 and 2007, rent expense was \$1,158,000, \$1,152,000 and 1,104,000, respectively.

***Capital Leases***

Our property and equipment leases under a capital lease arrangement expired in 2007.

***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 be terminated. These royalty obligations terminate in 2009 to 2020. Royalty expenses totaled \$211,000 in 2005, \$156,000 in 2006 and \$172,000 in 2007. 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 any possible future audit adjustments to be significant.

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

<u>Year Ending December 31,</u>	<u>Licenses</u>	<u>Operating Leases</u>
2008	\$ 150,000	\$1,425,000
2009	150,000	1,474,000
2010	150,000	1,525,000
2011	150,000	1,436,000
2012	150,000	9,000
Thereafter	1,050,000	1,000
<b>Total payments</b>	<b><u>\$1,800,000</u></b>	<b><u>\$5,870,000</u></b>

**Note 10 —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 consolidated financial statements.

***Warranties***

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

**SUPERCONDUCTOR TECHNOLOGIES INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

**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 any 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 it could incur related to such indemnifications.

***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 indemnifications 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 it could incur relating to such indemnifications. Historically, any amounts payable pursuant to such director and officer indemnifications 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 it agreed 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 against a director or executive officer, we are unable to determine the maximum amount of losses that it could incur relating to such indemnifications. Historically, any amounts payable pursuant to such guarantees 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.

***Short Term Borrowings***

We have a line of credit with a bank. The line of credit expires July 2008 and is structured as a sale of accounts receivable. The agreement provides for the sale of up to \$5 million of eligible accounts receivable, with advances to us totaling 80% of the receivables sold. Advances under the agreement ( *See Note 3* ) are collateralized by all our assets. Under the terms of the agreement, we continue to service the sold receivables and are subject to recourse provisions. Under the terms of the agreement, if the bank determines that there is a material adverse change in our business, they can exercise all their rights and remedies under the agreement, including demanding immediate payment of outstanding amounts. There was no amount outstanding under this facility at December 31, 2007

***Contractual Contingency***

We have a contract to deliver several custom products to a government contractor. We are unable to manufacture the products for technical reasons. We have discussed the problem with the contractor and our government customer. They are considering the problem, and further discussions are expected. We do not believe that a loss, if any, is reasonably estimable at this time and therefore has not recorded any liability relating to this

**SUPERCONDUCTOR TECHNOLOGIES INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

matter. We will periodically reassess our potential liability as additional information becomes available. If we later determine that a loss is probable and the amount reasonably estimable, we will record a liability for the potential loss. All costs have been expensed and no revenues recognized on this contract.

**Note 11 — Legal Proceedings**

***Settlement of Shalvoy Litigation***

Mr. Shalvoy, a director and stockholder, executed two notes aggregating \$820,244 in principal in connection with the exercise in December 2000 of two options to purchase Conductus, Inc. common stock prior our acquisition of Conductus, Inc. in December 2002. Through the third quarter of, 2005, we carried the principal (as “Notes Receivable from Stockholder”) and accrued interest (as “Prepaid Expenses and Other Current Assets”) for both notes as assets on our balance sheet.

We filed a lawsuit against Mr. Shalvoy on December 21, 2005 in the California Superior Court (Case No. 1186812) to collect both notes. In that same quarter, due to Mr. Shalvoy’s refusal to pay the notes voluntarily we recorded a reserve for the value of the notes (principal plus accrued interest) in excess of the market value of the collateral securing the notes.

On March 2, 2007, we entered into a Settlement Agreement and Mutual Release of All Claims with Mr. Shalvoy to settle the lawsuit. As per the agreement, we received a payment of \$610,000 on April 2, 2007 in payment of one note, including interest and attorneys’ fees, and the rescission of Mr. Shalvoy’s second purported option exercise including cancellation of the related note.

***Routine Litigation***

We may be involved in routine litigation arising in the ordinary course of our business, and, while the results of the proceedings cannot be predicted with certainty, we believe that the final outcome of such matters will not have a material adverse effect on our financial position, operating results or cash flows.

**Note 12 —Earnings Per Share**

The computation of per share amounts for 2005, 2006 and 2007 is based on the average number of common shares outstanding for the period. Options and warrants to purchase 2,031,213, 1,983,779 and 1,210,603 shares of common stock during 2005, 2006 and 2007 respectively, were not considered in the computation of diluted earnings per share because their inclusion would have been antidilutive.

**Note 13 —Restructuring Expenses and Impairment Charges**

During the first quarter of 2005, we implemented another restructuring program and reduced our workforce by another 27 positions and vacated a portion of our leased facility in Santa Barbara.

As discussed in Notes Receivable from Stockholder we recorded an impairment charge of \$969,000 related to certain notes in the fourth quarter of 2005. The impairment charge is included in Restructuring Expenses and Impairment Charges.

## SUPERCONDUCTOR TECHNOLOGIES INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following summarizes the restructuring and impairment charges for the years ended December 31, 2005, 2006 and 2007:

	For the Years Ended December 31,								
	Restructuring Charges for 2005	Impairment Charges for 2005	Total for 2005	Restructuring Charges for 2006	Impairment Charges for 2006	Total for 2006	Restructuring Charges for 2007	Impairment Charges for 2007	Total for 2007
Severance costs	\$ 178,000	\$ —	\$ 178,000	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Fixed assets write-offs	137,000	—	137,000	—	—	—	—	—	—
Patent, licenses and purchased technology write-off	—	—	—	—	—	—	—	—	—
Lease abandonment costs	—	—	—	—	—	—	—	—	—
Facility consolidation costs	6,000	—	6,000	—	—	—	—	—	—
Employee relocation costs	16,000	—	16,000	—	—	—	—	—	—
Goodwill write-off	—	—	—	—	20,107,000	20,107,000	—	—	—
Impairment charge for notes receivable from shareholder and board member	—	969,000	969,000	—	38,000	38,000	—	—	—
<b>Total</b>	<b>337,000</b>	<b>969,000</b>	<b>1,306,000</b>	<b>—</b>	<b>20,145,000</b>	<b>20,145,000</b>	<b>—</b>	<b>—</b>	<b>—</b>
Fixed assets write-off and severance costs included in cost of goods sold	109,000	—	109,000	—	—	—	—	—	—
Expense included in operating expenses	\$ 228,000	\$ 969,000	\$1,197,000	\$ —	\$20,145,000	\$20,145,000	\$ —	\$ —	\$ —

**Note 14 —Details of Certain Financial Statement Components and Supplemental Disclosures of Cash Flow Information and Non-Cash Activities**

**Balance Sheet Data:**

	December 31, 2006	December 31, 2007
<b>Accounts receivable:</b>		
Accounts receivable-trade	\$ 1,117,000	\$ 1,242,000
U.S. government accounts receivable-billed	493,000	1,246,000
Less: allowance for doubtful accounts	(75,000)	(75,000)
	<b>\$ 1,535,000</b>	<b>\$ 2,413,000</b>
	December 31, 2006	December 31, 2007
<b>Inventories:</b>		
Raw materials	\$ 2,242,000	\$ 1,934,000
Work-in-process	569,000	679,000
Finished goods	4,534,000	1,817,000
Less: inventory reserves	(1,367,000)	(1,015,000)
	<b>\$ 5,978,000</b>	<b>\$ 3,415,000</b>



**SUPERCONDUCTOR TECHNOLOGIES INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

	<u>December 31, 2006</u>	<u>December 31, 2007</u>
<b>Property and Equipment:</b>		
Equipment	\$ 17,186,000	\$ 15,951,000
Leasehold improvements	6,732,000	6,732,000
Furniture and fixtures	451,000	407,000
	<u>24,369,000</u>	<u>23,090,000</u>
Less: accumulated depreciation and amortization	<u>(18,599,000)</u>	<u>(19,129,000)</u>
	<b><u>\$ 5,770,000</u></b>	<b><u>\$ 3,961,000</u></b>

At December 31, 2006 and December 31, 2007, equipment includes \$237,000 of assets financed under capital lease arrangements, net of \$226,000 and \$237,000 of accumulated amortization, respectively. Depreciation expense amounted to \$2,548,000, \$2,277,000 and \$1,877,000 respectively, in 2005, 2006 and 2007. At December 31, 2007 we disposed of \$1,344,000 of older, fully depreciated equipment. There was no gain or loss on said disposition.

	<u>December 31, 2006</u>	<u>December 31, 2007</u>
<b>Patents and Licenses:</b>		
Patents pending	\$ 632,000	\$ 705,000
Patents issued	899,000	983,000
Less accumulated amortization	<u>(286,000)</u>	<u>(345,000)</u>
Net patents issued	613,000	638,000
Licenses	563,000	563,000
Less accumulated amortization	<u>(100,000)</u>	<u>(134,000)</u>
Net licenses	463,000	429,000
Purchased technology	1,706,000	1,706,000
Less accumulated amortization	<u>(1,005,000)</u>	<u>(1,242,000)</u>
Net purchased technology	<u>701,000</u>	<u>464,000</u>
	<b><u>\$ 2,409,000</u></b>	<b><u>\$ 2,236,000</u></b>

Amortization expense related to these items totaled \$329,000, \$326,000 and \$331,000 respectively in 2005, 2006 and 2007. Amortization expenses related to these items are expected to total \$331,000 in 2008 and 2009 and approximately \$95,000 in 2010 and 2011.

**SUPERCONDUCTOR TECHNOLOGIES INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

	December 31, 2006	December 31, 2007
Accrued Expenses and Other Long Term Liabilities:		
Salaries payable	\$ 287,000	307,000
Compensated absences	379,000	371,000
Compensation related	299,000	369,000
Warranty reserve	428,000	380,000
Lease abandonment costs	8,000	—
Product line exit costs	319,000	—
Deferred rent	390,000	373,000
Other	104,000	123,000
	<b>2,214,000</b>	<b>1,923,000</b>
Less current portion	<b>(1,610,000)</b>	<b>(1,405,000)</b>
Long term portion	<b>\$ 604,000</b>	<b>\$ 518,000</b>

	For the Year Ended		
	December 31, 2005	December 31, 2006	December 31, 2007
<b>Warranty Reserve Activity:</b>			
Beginning balance	\$ 419,000	\$ 491,000	\$ 428,000
Additions	204,000	140,000	75,000
Deductions	(273,000)	(203,000)	(123,000)
Change in estimate relating to previous warranty accruals	141,000	—	—
Ending balance	<b>\$ 491,000</b>	<b>\$ 428,000</b>	<b>\$ 380,000</b>
<b>Lease Abandonment Costs:</b>			
Beginning balance	\$ 1,336,000	\$ 225,000	\$ 8,000
Additions	—	—	—
Transfers from unfavorable lease costs	—	—	—
Deductions	(1,111,000)	(217,000)	(8,000)
Ending balance	<b>\$ 225,000</b>	<b>\$ 8,000</b>	<b>\$ —</b>
<b>Product Line Exit Costs:</b>			
Beginning balance	\$ 885,000	\$ 402,000	\$ 319,000
Additions	—	—	—
Deductions	(483,000)	(83,000)	(319,000)
Change in estimate relating to previous exit costs accrual	—	—	—
Ending balance	<b>\$ 402,000</b>	<b>\$ 319,000</b>	<b>\$ —</b>

	For the Year Ended		
	December 31, 2005	December 31, 2006	December 31, 2007
<b>Severance Costs:</b>			
Beginning balance	\$ 36,000	\$ 32,000	
Additions	218,000	—	
Deductions	(222,000)	(32,000)	
Ending balance	<u>\$ 32,000</u>	<u>\$ —</u>	<u>\$ —</u>

	Dec. 31, 2005	Dec. 31, 2006	Dec. 31, 2007
<b>Supplemental Cash Flow Information:</b>			
Cash paid for interest	\$116,000	\$45,000	\$ 39,000
Cash paid for taxes	\$ (5,190)	\$15,592	\$183,249

## Note 15 —Subsequent Event

### *Unregistered Sales of Equity Securities*

Under a previously announced investment agreement with Hunchun BaoLi Communication Co. Ltd, or BAOLI in August 2007, on February 27, 2008, we issued to BAOLI and two related purchasers a total of (a) 3,101,361 shares of our common stock (of which 953,065 must be voted in accordance with the votes of our other shares, effectively giving BAOLI no voting power over such shares) and (b) 611,523 shares of our Series A Convertible Preferred Stock, or Series A Preferred (convertible under certain conditions into 6,115,230 shares of our common stock). We received \$15.0 million in cash, of which \$4.0 million was funded in 2007 and the \$11.0 million balance was funded in January 2008.

Subject to the terms and conditions of our Series A Preferred and to customary adjustments to the conversion rate, each share of our Series A Preferred is convertible into ten shares of our common stock so long as the number of shares of our common stock beneficially owned by BAOLI following such conversion does not exceed 9.9% of our outstanding common stock. Except for a preference on liquidation of \$.01 per share, each share of Series A Preferred is the economic equivalent of the ten shares of common stock into which it is convertible. Except as required by law, the Series A Preferred will not have any voting rights and there is currently no dividend.

With the issuance of the Series A Preferred, our ability to declare or pay dividends on shares of our common stock will be subject to the requirement that we pay an equivalent dividend on each outstanding share of Series A Preferred (on an as converted basis).

**Quarterly Financial Data (Unaudited)**

	<u>First Quarter</u>	<u>Second Quarter</u>	<u>Third Quarter</u>	<u>Fourth Quarter</u>
<b>2007</b>				
Net revenues(1)	\$ 4,183,000	\$ 4,685,000	\$ 4,120,000	\$ 4,914,000
Loss from operations(2)(3)	(2,977,000)	(2,006,000)	(2,040,000)	(2,220,000)
Net loss	(2,937,000)	(1,982,000)	(2,020,000)	(2,187,000)
Basic and diluted loss per common share	\$ (0.24)	\$ (0.16)	\$ (0.16)	\$ (0.17)
Weighted average number of shares outstanding	12,483,367	12,483,367	12,483,367	12,500,134
<b>2006</b>				
Net revenues(1)	\$ 4,840,000	\$ 5,021,000	\$ 5,910,000	\$ 5,307,000
Loss from operations(4)(5)	(3,340,000)	(22,755,000)	(2,164,000)	(1,712,000)
Net loss	(3,226,000)	(22,659,000)	(2,092,000)	(1,647,000)
Basic and diluted loss per common share	\$ (0.26)	\$ (1.81)	\$ (0.17)	\$ (0.13)
Weighted average number of shares outstanding	12,483,367	12,483,367	12,483,367	12,483,367

- (1) Our revenues vary from quarter to quarter as our customers provide minimal lead-time prior to the release of their purchase orders and have non-binding commitments to purchase from us.
- (2) Includes sale of previously written-off inventory of none, \$138,000, \$57,000 and none, respectively.
- (3) Includes increased reserve for inventory obsolescence of \$90,000, \$70,000, none and none, respectively.
- (4) Includes increased reserve for inventory obsolescence of \$90,000, \$90,000, \$90,000 and \$90,000, respectively.
- (5) Includes sale of previously written-off inventory of \$119,000, \$273,000, \$309,000 and none, respectively.

## SUPERCONDUCTOR TECHNOLOGIES INC.

**Schedule II — Valuation and Qualifying Accounts**

	<u>Beginning Balance</u>	<u>Charge to Costs &amp; Expenses</u>	<u>Additions Charge to Other Accounts</u>	<u>Charge to Other Deductions</u>	<u>Ending Balance</u>
<b>Year Ended December 31, 2007</b>					
Allowance for Uncollectible Accounts	\$ 75,000	\$ —	\$ —	\$ —	\$ 75,000
Impairment for Notes Receivable from Stockholder	1,007,000	(583,000)	—	(424,000)	—
Reserve for Inventory Obsolescence	1,367,000	(195,000)	—	(157,000)	1,015,000
Reserve for Warranty	428,000	75,000	—	(123,000)	380,000
Deferred Tax Asset Valuation Allowance	112,153,000	3,129,000	—	—	115,282,000
<b>Year Ended December 31, 2006</b>					
Allowance for Uncollectible Accounts	75,000	—	—	—	75,000
Impairment for Notes Receivable from Stockholder	969,000	38,000	—	—	1,007,000
Reserve for Inventory Obsolescence	—	3,209,000	360,000	(2,202,000)	1,367,000
Reserve for Warranty	491,000	140,000	—	(203,000)	428,000
Deferred Tax Asset Valuation Allowance	106,299,000	5,854,000	—	—	112,153,000
<b>Year Ended December 31, 2005</b>					
Allowance for Uncollectible Accounts	77,000	—	—	(2,000)	75,000
Impairment for Notes Receivable from Stockholder	—	969,000	—	—	969,000
Reserve for Inventory Obsolescence	5,402,000	984,000	—	(3,177,000)	3,209,000
Reserve for Warranty	419,000	204,000	—	(132,000)	491,000
Deferred Tax Asset Valuation Allowance	\$106,589,000	\$ (290,000)	\$ —	\$ —	\$106,299,000

## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized, on this 27th day of March 2008.

SUPERCONDUCTOR TECHNOLOGIES INC.

By: /s/ Jeffrey A. Quiram

\_\_\_\_\_  
Jeffrey A. Quiram

President and Chief Executive Officer

## POWER OF ATTORNEY

KNOW ALL THESE PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints William J. Buchanan, his attorney-in-fact, with full power of substitution, for him in any and all capacities, to sign any and all amendments to this Report on Form 10-K, and to file the same, with exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, hereby ratifying and confirming all that said attorney-in-fact or his substitute or substitutes, may do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this Report on Form 10-K has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated:

<u>Signature</u>	<u>Title</u>	<u>Date</u>
/s/ Jeffrey A. Quiram _____ Jeffrey A. Quiram	President, Chief Executive Officer and Director (Principal Executive Officer)	March 27, 2008
/s/ William J. Buchanan _____ William J. Buchanan	Controller (Principal Accounting Officer) (Principal Financial Officer)	March 27, 2008
/s/ David W. Vellequette _____ David W. Vellequette	Director	March 27, 2008
/s/ Lynn J. Davis _____ Lynn J. Davis	Director	March 27, 2008
/s/ Dennis J. Horowitz _____ Dennis J. Horowitz	Director	March 27, 2008
/s/ Martin A. Kaplan _____ Martin A. Kaplan	Director	March 27, 2008
/s/ John D. Lockton _____ John D. Lockton	Chairman of the Board	March 27, 2008





**FIRST AMENDMENT TO AGREEMENT**

This First Amendment, dated as of November 1<sup>st</sup>, 2007 (the “**Amendment**”), between Superconductor Technologies, Inc., a Delaware corporation (“**STI**”), and Hunchan BaoLi Communication Co., Ltd. (“**BAOLI**”) amends that certain Agreement, dated as of August 17, 2007 (the “**Agreement**”), between STI and BAOI.

**RECITALS**

- A. Pursuant to the Agreement, BAOI agreed to purchase and STI agreed to sell \$15,000,000 of shares of STI's Common Stock, par value \$0.001 per share (the “**Common Stock**”), at a per share price of \$1.6275. The Agreement provides that it may be amended by the written agreement of STI and BAOI, and STI and BAOI agree to amend the Agreement as set forth below.
- B. This Amendment provides: (i) that upon full payment of the Purchase Price by BAOI to STI, STI will instead be obligated to deliver 2,148,296 shares of Common Stock (the “Common Shares”) and 706,829 shares of newly created Series A Convertible Preferred Stock of the Corporation (the “**Preferred Shares**”) (with the rights and privileges set forth in the Certificate of Designations attached hereto as **Exhibit B** and convertible into 7,068,290 shares of Common Stock), and (ii) BAOI with registration rights with respect to the Common Shares as set forth in **Exhibit C**.

**1. PURCHASE AND SALE.**

The Agreement is hereby amended so that the term “**Shares**” consists of the Common Shares and the Preferred Shares. The purchase price per Common Share is \$1.6275 and the purchase price per Preferred Share is \$16.275, with the total purchase price for the Shares equal to \$15,000,000. On a fully converted basis, BAOI will receive the same number of Common Shares as under the Agreement,

**2. REGISTRATION RIGHTS**

STI hereby grants to BAOI the registration rights related to the Common Shares set forth in **Exhibit C**,

**3. LEGALITY OF INVESTMENT**

3.1. **Legal Consent to the Amendment.** BAOI and each Purchaser represents and warrants that the execution and performance of the Amendment are consented and approved by the Board of Directors of BAOI and such Purchaser and that the Amendment is legally binding on BAOI and such Purchaser. BAOI and each Purchaser also make the representations and warranties set forth in **Exhibit A**.

3.2. **Legality of the Offer to Amend.** STI represents and warrants that the execution and performance of the Amendment are for the corporate interest of STI's development and STI has obtained all and any necessary internal approval and STI is legally bound by each of the Agreement and the Amendment, and in addition, subject to the representations and warranties of each Purchaser contained in **Exhibit A** upon which STI hereby relies complies with the

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provisions of the laws and regulations of United States of America, including but not limited to the pertinent SEC requirements.

**4. TERMS AND EFFECT OF AMENDMENT**

Except as amended by this Amendment, the Agreement remains in full force and effect. Terms used in this Amendment that are not defined in this Amendment shall have the same meaning given to such terms in the Agreement. Terms defined in this Amendment shall be applicable to the Agreement, as amended hereby.

**IN WITNESS WHEREOF** , the parties have executed this Amendment as of the date first written above.

SUPERCONDUCTOR TECHNOLOGIES, INC

By: /s/ Jeffrey Quiram

Name: Jeffrey Quiram

Title: President & CEO

BAOLI COMMUNICATIONS CO. LTD

By: /s/ (Signature)

Name:

Title:



## SECOND AMENDMENT TO AGREEMENT

This Second Amendment, dated as of January 7, 2008 (the “**Amendment**”) between Superconductor Technologies Inc. a Delaware corporation (“**STI**”), and Hunchun BaoLi Communication Co. Ltd, (“**BAOLI**”) amends that certain Agreement, dated as of August 17, 2007 and subsequently amended as of November 1st, 2007 (the “**Agreement**”), between STI and BAOI.

### RECITALS

- A.** Pursuant to the Agreement, BAOI agreed to purchase and STI agreed to sell 2,148,296 shares of STI's common stock, par value \$0.001 per share (the “**Common Stock**”) and 706,829 shares of Series A Convertible Preferred Stock of STI (the “**Preferred Stock**”) in exchange for \$15,000,000, of which a deposit of \$4,000,000 has already been received by STI. The Agreement provides that it may be amended by the written agreement of STI and BAOI and STI and BAOI agree to amend the Agreement as set forth below.
- B.** This Amendment provides that if full payment of the Purchase Price is actually received from BAOI, STI will Instead be obligated to deliver 3,101,361 shares of Common Stock (the “**Common Shares**”) and 611,523 shares of Preferred Stock (the “**Preferred Shares**”) (convertible into 6,115,230 shares of Common Stock, for an aggregate of 9,216,519 shares of Common Stock including the Common Shares). As of the date hereof, STI has approximately 12,500,000 shares of common stock outstanding.

NOW, THEREFORE, the parties hereby agree as follows:

**1. PURCHASE AND SALE.** The Agreement is hereby amended so that (i) term “**Shares**” consists of 3,101,361 shares of Common Stock and 611,523 shares of Preferred Stock; (ii) BAOI agrees to increase its deposit from \$4,000,000 to \$6,000,000 not later than 1 PM on January 8, 2008 (Los Angeles time); and (iii) BAOI agrees to complete the purchase of all of the Shares by paying the remaining \$9,000,000 of the \$15,000,000 Purchase Price not later than 1 PM on January 21, 2008 (Los Angeles time). BAOI represents that the additional \$2,000,000 has been irrevocably wired to STI.

**2. VOTING AGREEMENT.** BAOI agrees that 953,065 of the Common Shares (any and all other shares or securities of STI issued or issuable in respect thereof on or after the date hereof, the “**Non Voting Shares**”) shall be covered by the Irrevocable Proxy and Voting Agreement executed simultaneously herewith. Each certificate representing any Non Voting Shares shall be endorsed by the Company with a legend reading substantially as follows:

**“THE SHARES EVIDENCED HEREBY ARE SUBJECT TO AN IRREVOCABLE PROXY AND VOTING AGREEMENT (A COPY OF WHICH MAY BE OBTAINED UPON WRITTEN REQUEST FROM THE COMPANY), AND BY ACCEPTING ANY INTEREST IN SUCH SHARES THE PERSON ACCEPTING SUCH INTEREST SHALL BE DEEMED TO AGREE TO AND SHALL BECOME BOUND BY ALL THE PROVISIONS OF THAT AGREEMENT.”**

Upon receipt by STI of reasonably acceptable evidence of bona fide transfer to a person not covered by the Irrevocable Proxy and Voting Agreement according to its terms, the legend

will be removed from the certificate representing such transferred shares.

**3. EXCHANGE.** STI has informed BAOLI that the issuance of additional Common Stock under the initial Agreement was not permitted by the NASDAQ Stock Market without a shareholder vote. Although NASDAQ has given preliminary approval of the issuance under Section 1, if final approval is denied, the parties will work together to overcome or respond to any objections. In addition if all necessary regulatory approvals, including the NASDAQ, can be obtained on or before February 15, 2008, the parties will take all steps needed to exchange the Preferred Shares for the Common Stock into which it would be convertible, provided that BAOLI signs the same form of Irrevocable Proxy and Voting Agreement with respect to all such shares of Common Stock issued in such exchange and such shares bear the same legend set forth in Section 2.

**4. LEGALITY OF INVESTMENT.**

**4.1. Legal Consent to the Amendment.** BAOLI represents and warrants that the execution and performance of the Amendment are consented and approved by the Board of Directors of BAOLI and that the Amendment is legally binding on BAOLI. BAOLI also makes the representations and warranties set forth in, **Exhibit A** to the First Amendment.

**4.2. Legality of the Offer to Amend.** STI represents and warrants that the execution and performance of the Amendment are for the corporate interest of STI's development and STI has obtained all and any necessary internal approval and STI is legally bound by each of the Agreement and the Amendment, and in addition, subject to the representations and warranties of each Purchaser contained in **Exhibit A** to the First Amendment upon which STI hereby relies, complies with the provisions of the laws and regulations of United States of America, including but not limited to the pertinent SEC requirements.

**5. FUNDING OF JOINT VENTURE.** Section 12 of the Sino-Foreign Equity Joint Venture Contract dated as of December 8, 2007 among BAOLI and Superconductor Investments (Mauritius) Ltd (the "**JV Contract**") relating to BAOLI Superconductor Technology Co, Ltd ("**BSTC**") is hereby amended to require the contributions of the parties be made not later than September 30, 2008; it being understood that the Effective Date under the STI Trademark and Technology License (when technology transfers can begin) is not until "ten days after the completion of the contribution to the capitalization of [BSTC] of [BAOLI] as contemplated by the [JV Contract]." Should BAOLI fail for any reason, including governmental decisions, to fully fund its contributions not later the date in the first sentence, (1) the Trademark and Technology License shall immediately terminate and neither BAOLI nor the BSTC shall have any rights to the technology or trademarks of STI, although both shall continue to bound by their obligations to maintain the confidentiality of all information provided by STI and its affiliates; (2) BAOLI shall be deemed to be in material breach under Article 15 of the JV Contract; (3) BSTC shall be immediately terminated and a liquidation application shall be submitted to the original Examination and Approval Authority for approval, with BAOLI agreeing to be responsible for promptly obtaining such approval and (4) STI and its affiliates shall be immediately relieved of all of its or their obligations under the JV Contract and the related Framework Agreement.

**6. TERMS AND EFFECT OF AMENDMENT.** Except as amended by this Amendment, the Agreement remains in full force and effect. Terms used in this Amendment that are not defined in this Amendment shall have the same meaning given to such terms in the

Agreement. Terms defined in this Amendment shall be applicable to the Agreement, as amended hereby.

**7. TIME IS OF THE ESSENCE. TIME IS OF THE ESSENCE UNDER THIS AGREEMENT. THERE WILL BE NO FURTHER EXTENSIONS OF TIME OF ANY LENGTH OF THESE DEADLINES FOR ANY REASON, EVEN IF GOVERNMENTAL APPROVAL IS NOT RECEIVED BY BAOLI.** BAOLI specifically agrees that, unless BOTH (1) the additional \$2,000,000 deposit is actually RECEIVED by STI NO LATER THAN the date and time set forth in Section 1 AND (2) FULL payment is actually RECEIVED by STI NO LATER THAN the date and time set forth in Section 1, BAOLI will FORFEIT its entire deposit, which may be retained by STI without any further obligations to BAOLI. BAOLI acknowledges that (i) STI could have sold its stock at amounts far in excess of either the price in the Agreement of the current market price, but refrained from doing so based on BAOLI's assurances that it would complete its obligations under the Agreement and (ii) STI will suffer significant damages as a result of any failure of BAOLI to complete the transactions contemplated by the Agreement. The parties have agreed that, under the circumstances, and in consideration of the additional extension of time for BAOLI to invest its money without increasing the price per share to reflect current market conditions, the current deposit is inadequate and that increasing it by an additional \$2,000,000 to a total of \$6,000,000 as contemplated by Section 1 is fair and reasonable in light of the repeated delays, and the significant benefits to BAOLI, and the risks to STI, of this extension. Accordingly, BAOLI agrees that STI retaining the full amount of its deposit in the event that either BAOLI fails to increase the deposit or fails to pay the full purchase price by the precise deadlines set forth above is fair and reasonable based on these and other factors.

**IN WITNESS WHEREOF**, the parties have executed this Amendment as of the date first written above.

SUPERCONDUCTOR TECHNOLOGIES INC.

By: /s/ JEFFREY QUIRAM  
 Name: Jeffrey Quiram  
 Title: President & CEO

HUNCHUN BAOLI COMMUNICATIONS  
 COMPANY., LTD

By: /s/ (SIGNATURE)  
 Name:  
 Title:

1. **Grant of Proxy.** Hunchun BaoLi Communication Co. Ltd. (“**BAOLI**”) hereby irrevocably appoints Superconductor Technologies Inc. a Delaware corporation (“**STI**”), as BAOli’s sole and exclusive attorney and proxy, with full power of substitution and resubstitution, to vote and exercise all voting, consent and similar rights (to the full extent that BAOli would be entitled to do so) with respect to the Non Voting Shares (including, without limitation, the power to execute and deliver written consents) at every annual, special or adjourned meeting of shareholders of STI and in every written consent in lieu of such a meeting, with respect to the Non Voting Shares, in the same proportion (for, against and abstaining) as the votes of the shares of common stock of STI other than the Non Voting Shares. “**NON VOTING SHARES**” means 953,060 shares of common stock of STI beneficially owned by BAOli as of the date hereof whose certificate is being legended to refer to this Agreement, and any and all other shares or securities of STI issued or issuable in respect thereof on or after the date hereof.

2. **Agreement to Vote.** In addition to the irrevocable proxy granted in Section 1, BAOli agrees to vote the Non Voting Shares at regular and special meetings of stockholders (and by written consent) in accordance with any written instructions of STI. STI may disregard any purported vote or consent with respect to the Non Voting Shares which is not in accordance with this Agreement.

3. **Binding.** This Proxy is irrevocable, is coupled with an interest and is granted pursuant to that certain agreement dated as of August 17, 2007 and subsequently amended, between STI and BAOli. The obligations of BAOli shall be binding upon it and on successors and assigns and any transferees of the Non Voting Shares, except that STI will cease to have the right to vote, and this Agreement will terminate with respect to any shares after BAOli provides STI with reasonably acceptable written evidence of a bona fide transfer of those shares (including, all voting rights) to a transferee which is not affiliated (i) with BAOli or (ii) with any other person or a “group” (within the meaning of Section S.3(d) of the U.S. Securities Exchange Act of 1934) of which such holder is or is deemed to be a part, “beneficially owns” (within the meaning of Rule 13d-3 under the U.S. Securities Exchange Act of 1934) more than 5% of the outstanding common stock of STI.

4. **Enforcement.** BAOli acknowledges and agrees that STI will be irreparably damaged if any of the provisions of this Agreement are not performed by BAOli in accordance with their specific terms or are otherwise breached. Accordingly, it is agreed that STI shall be entitled to an injunction without the necessity of posting a bond to prevent breaches of this Agreement and to specific enforcement of this Agreement and its terms and provisions in any action instituted in any court of the United States or any state having subject matter jurisdiction, in addition to any other remedy to which STI may be entitled at law or in equity. BAOli hereby consents to personal jurisdiction in any such action brought in the United States District Court for the Central District of California or in any court of the State of California having subject matter jurisdiction. In any dispute arising out of, or relating to, this Agreement or its performance or breach, (including any dispute which is the subject of judicial, arbitration or administrative proceedings, including appeals), the prevailing party shall be entitled to and awarded, in addition to any other relief, its reasonable costs incurred, including reasonable attorneys’ fees.

BAOLI COMMUNICATIONS CO. LTD

By: /s/ (Signature) \_\_\_\_\_

Name:

Title:





### Framework Agreement

Pursuant to this Framework Agreement (the “Agreement”), effective as of November 8th, 2007 Hunchun BaoLi Communications Co. Ltd., a Chinese enterprise (“BaoLi Communications”), and Superconductor Technologies Inc., a Delaware corporation (“STI”), agree as follows:

**1. Organization of HBST.** BaoLi Communications and STI (or such subsidiaries of STI as STI may designate) agree to establish the Hunchun BaoLi Superconductor Technology Co Ltd. (“HBST”) pursuant to the Sino-Foreign Equity Joint Venture Contract attached as Exhibit A and HBST and STI shall enter into a License Agreement in the form attached as Exhibit B (in each case, with any changes on which the parties mutually agree). STI may substitute its designated subsidiary or subsidiaries as parties to such Joint Venture Contract. BaoLi Communications will provide additional working capital to HBST as reasonable needed, without any dilution to the equity of STI without its consent and with the goal of minimizing any effect on HBST or the ownership interest of STI.

**2. Confidentiality.** The parties each agree to comply with the relevant provisions of Exhibits A and B concerning the confidentiality of all information concerning HBST and the licensed technology. Any news releases related to this Agreement and the proposed formation of HBST is subject to the review and approval of both STI and BaoLi Communications, not to be unreasonably withheld or delayed, and subject to the requirement that each party comply with applicable law and regulations of any stock exchange.

**3. Governing law.** This Agreement shall be governed by and construed under the laws of the State of California, except for the conflict of laws provisions thereof and without reference to the Vienna Convention on the International Sale of Goods. Any disputes concerning this Agreement will be arbitrated according to the arbitration provisions of the Trademark License.

**4. Termination.** This Agreement will terminate if the parties have not completed the formation HBST on or before January 31, 2008 and the parties will thereafter have no further obligations under this Agreement.

In witness whereof, having ready, understood and agreed to the terms and conditions of this Framework Agreement, and with full authority to execute this Agreement on behalf of the respective Parties, the undersigned hereby execute this Agreement as of the date first above written.

**Superconductor Technologies Inc., a Delaware Corporation**

By: /s/ Jeffery Quiram

Name: Jeffery Quiram

Title: President & CEO

**Hunchan BaoLi Communications Co.  
Ltd. a Chinese company**

By: /s/ (Signature)

Name:

Title:



**SINO-FOREIGN EQUITY JOINT VENTURE CONTRACT**

**中外合资经营企业合作合同**

**Between**

**Hunchun BaoLi Communication Co. Ltd**

**珲春宝力通信有限公司**

**And**

**Superconductor Investments (Mauritius) Limited**

**超导投资（毛里求斯）有限公司**

**December 8<sup>th</sup> 2007**



**Chapter 1 General Principles****第一章 总则****Article 1**

In accordance with the stipulations of the Law of the People's Republic of China on Chinese-Foreign Equity Joint Ventures, the Regulations for the Implementation of the Law of the People's Republic of China on Chinese-Foreign Equity Joint Ventures and other related laws and rules, Hunchun Baoli Communication Co., Ltd. (hereinafter referred to as Party A) from China and Superconductor Investments (Mauritius) Limited (hereinafter referred to as Party B) from the Mauritius hereby agree to form a Sino-Foreign Joint Venture Company (hereinafter referred to as "JV Company"), and enter into this contract.

**第一条**

根据《中华人民共和国中外合资经营企业法》及其实施条例以及其它相关法律法规，中国的琿春宝力通信有限公司（以下简称“甲方”）和毛里求斯的超导投资（毛里求斯）有限公司（以下简称“乙方”）同意组建一家中外合资经营公司（以下简称“合资公司”），特此订立本合同。

**Article 2**

Name of JV Company: The Chinese name of the JV Company is “宝力超导技术有限公司”, and the English name of the JV Company is “Baoli Superconductor Technology Co., Ltd.”

Statutory Address: Baoli Electronic Communication Industrial Park, Hunchun City, Jilin Province, China

**第二条**

合资公司的名称：合资公司的中文名称是“宝力超导技术有限公司”，英文名称是“Baoli Superconductor Technology Co., Ltd.”。

法定地址：中国吉林省琿春市宝力电子通信工业园区。

**Article 3**

Company Name, Statutory Address, and Legal Representative of the two parties to the JV Company are as follows:

Party A: Hunchun Baoli Communication Co., Ltd.

Statutory Address: Baoli Electronic Communication Industrial Park, Hunchun City, Jilin Province, China

Legal Representative: Mr. Yi Zhang, Chairman, Chinese Nationality

Party B: Superconductor Investments (Mauritius) Limited, a wholly owned subsidiary of Superconductor Technologies, Inc.

Statutory Address: 1<sup>st</sup> Floor, Felix House, 24 Dr. Joseph Riviere Street, Port Louis, Mauritius

Legal Representative: Mr. Jeff Quiram, President, President and Chief Executive Officer of Superconductor Technologies and lead director and designated legal representative for Superconductor Investments (Mauritius) Limited.

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**第三条**

合资双方的公司名称、法定地址和法定代表人如下：

甲方：珲春宝力通信有限公司

法定地址：中国吉林省珲春市宝力电子通信工业园区

法定代表人：张依先生 职务：董事长 国籍：中国

乙方：超导投资（毛里求斯）有限公司，一家美国超导技术有限公司全资拥有的子公司

法定地址：1<sup>st</sup> Floor, Felix House, 24 Dr. Joseph Riviere Street, Port Louis, Mauritius

法定代表人：Jeff Quiram 先生 美国超导技术有限公司总裁兼首席执行官，超导投资（毛里求斯）有限公司董事长及法定代表人

**Article 4**

The JV Company shall be a limited liability company.

**第四条**

合资公司的组织形式为有限责任公司。

**Article 5**

The JV Company has the status of a legal person and is subject to the jurisdiction and protection of Chinese laws concerned. All the activities of the JV Company shall be governed by the laws, decrees, pertinent rules and regulations of the People's Republic of China.

**第五条**

合资公司系独立法人并受相关中国法律的管辖与保护。合资公司的一切活动必须遵守中华人民共和国的法律、法令和有关法规和条例的规定。



**Chapter 2 Purpose and Business Scope of the JV Company****第二章 合资公司的宗旨与经营范围****Article 6**

Purpose of the JV Company: With Party B's superconductor wave-filtering technology, the JV Company aims to produce and market high temperature superconductor wave-filtering equipment in an effort to tap the market for telecommunication equipment and reap satisfactory economic benefits for the two parties of the JV Company.

**第六条**

合资公司的宗旨：凭借乙方的超导滤波技术，合资公司旨在生产和经营高温超导滤波装置，致力于开发通信装置市场，并使投资双方获得满意的经济利益。

**Article 7**

Business Scope of the JV Company: to design, produce and market high temperature superconductor wave-filtering system and equipment (Party B's SuperLink Product) and provide related technology support and services.

**第七条**

合资公司经营范围：设计、生产并销售乙方高温超导滤波系统和装置，提供相关的技术支持和服务。

**Article 8**

Production Scale of the JV Company: In the initial operation phase, it is planned that the JV Company will produce 500 units for the first year, 1,500 units for the second year, and 5,000 units for the third year. The Parties may decide to expand the production scale of the JV Company later.

**第八条**

合资公司的生产规模：在初始经营阶段，合资公司计划第一年生产 500 台设备，第二年生产 1,500 台设备，第三年生产 5,000 台设备。之后双方可以决定扩大合资公司的生产规模。

**Article 9**

The Parties plan that the JV Company will sell its products to the domestic and international market in the following proportions:

The first year: 20% of Product production by the JV Company is expected to be sold to HK and Macao and 80% to the domestic market;

The second year: 30% of Product production by the JV Company is expected to be sold to HK and Macao and 70% to the domestic market;

The third year: 50% of Product production by the JV Company is expected to be sold to HK and Macao and 50% to the domestic market.

Additional Product production by the JV Company may be sold to STI or its designees in the international market at any time.

Actual sales by the JV Company shall be decided by the JV Company's Board of Directors.

Marketing channel, method and responsibility shall be allocated as follows:

The Company JV shall be responsible for marketing in China (including HK and Macao, but not Taiwan) Party B shall retain all rights in Taiwan and the international market exclusive of China.

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第九条

双方计划将合资公司所生产的产品按如下比例销往国内及国际市场：

第一年：计划将合资公司所生产产品的 20%销往香港和澳门市场，80%销往国内市场；

第二年：计划将合资公司所生产产品的 30%销往香港和澳门市场，70%销往国内市场；

第三年：计划将合资公司所生产产品的 50%销往香港和澳门市场，50%销往国内市场；

合资公司超额生产的产品可以在任何时间销售给 Superconductor Technologies Inc.或其在国际市场指定的人士。

合资公司的董事会应决定合资公司的实际销售事宜。

销售渠道、方式和职责按下列规定分配：

合资公司负责在中国境内的销售（包括香港和澳门，但不包括台湾）；

乙方保有在台湾和中国以外的国际市场的所有销售权。



**Chapter 3 Total Amount of Investment and the Registered Capital**  
**第三章 投资总额与注册资本**

**EXHIBIT 10.24**

**Article 10**

The total amount of investment of the JV Company shall be thirty million US dollars (\$30,000,000.00) and the registered capital of the JV Company shall be twenty-five point five million US dollars (\$25,500,000.00).

**第十条**

合资公司的投资总额为三千万美元 (\$30,000,000.00)，注册资本为二千五百五十万美元 (\$25,500,000.00)。

**Article 11**

Capital Contribution to be made by the two parties of the JV Company shall be as follows:

Party A: to invest fourteen million and twenty-five thousand US dollars (\$14,025,000.00), which includes:

Cash \$7,012,500.00 US dollars  
Mechanical Equipment worth void US dollars  
Workshop worth \$2,000,000.00 US dollars  
Land Use Right worth \$5,012,500.00 US dollars  
Industrial Property Right worth void US dollars  
Others worth void US dollars

Party B: to invest eleven million and four hundred and seventy-five thousand US dollars (\$11,475,000.00), which includes:

Cash void US dollars  
Mechanical Equipment worth void US dollars  
Intellectual Property Rights worth \$11,475,000 US dollars  
Others worth void US dollars

**第十一条**

双方按照以下规定向合资公司缴付注册资本:

甲方: 出资一千四百零二万五千美元 (\$14,025,000.00), 包括:

现 金: 七百零一万二千五百 美元  
机器设备: 价值 零 美元  
厂 房: 价值 二百万 美元的  
土地使用权: 价值 五百零一万二千五百 美元  
知识产权: 价值 零 美元  
其 他: 价值 零 美元

乙方: 投资一千一百四十七万五千美元 (\$11,475,000.00), 包括:

现 金: 零 美元  
机器设备: 价值 零 美元  
知识产权: 价值 一千一百四十七万五千 美元  
其 他: 价值 零 美元

**Article 12**

Two parties of the JV Company shall effect their capital contribution within the following time limits:  
All capital will be contributed in two years in accordance with Chinese applicable laws.





**第十二条**

合资双方应在下列期限内缴清注册资本：  
所有注册资本将按中国相关法律在两年内缴清。

**Article 13**

When a capital contribution is effected, the JV Company shall issue a certificate for capital contribution on condition that such contribution has been verified by a certified accountant appointed by the JV Company. The main content of such certificate shall be: Name of JV Company, Date of Establishment, Two Parties of the JV Company and Respective Capital Contribution and the respective equity ratio, Date of Contribution and Date of Issue. Such certificate shall be signed by the Chairman, and affixed with the corporate chop of the JV Company. However, the non-issuance of such certificate shall not affect the Parties' rights as shareholders of the JV Company.

**第十三条**

当完成一次出资时，在该出资经合资公司指定的具有合格资质的会计师验资后，合资公司应签发一份出资证明。该出资证明的主要内容：合资公司的名称，设立的时间，合资双方和各自的注册资本和所占比例，出资时间和出资证明签发的时间。该出资证明应由董事长签字，并加盖合资公司的公章。但是未能签发该出资证书并不影响合资双方作为合资公司股东的权利。

**Article 14**

During the Joint Venture period, the JV Company shall not reduce the amount of the registered capital. However, in case of severe difficulties, registered capital reduction may be applied for to the original approval authority and implemented after obtaining such approval.

**第十四条**

在合资期间，合资公司不得减少注册资本总额。但在发生严重困难的情况下，可以向原审批机关申请减少注册资本，并在获得批准后方可实施。

**Article 15**

Any increase or decrease in registered capital of the JV Company must be agreed by both parties. Any such increase or decrease shall be approved by the original approval authority and registered with the original registration authority.

If any Party fails to make its capital increase contribution after both Parties have agreed to such capital increase, the other Party may at its discretion:

(a) give the failing Party a ninety (90) days' prior written notice, and contribute all or part of the shortfall amount not contributed by the failing Party if no contribution is made by the failing Party upon expiry of the said notice period, whereupon both Parties' shareholding percentages in the JV Company shall be adjusted so as to be in proportion to the registered capital of the Company actually contributed by each of them respectively, and the number of Directors appointed by each Party to the Board of Directors shall, without changing the total number of Directors of the Company, be reduced or increased accordingly to match to the fullest extent each Party's then shareholding percentage in the JV Company; or

(b) treat such failure as a material breach of this Contract by the failing Party.

Both Parties agree to execute all such documents and take all such steps as required to legally effect either of the above options taken by the non-failing Party in good faith.

**第十五条**

合资公司注册资本的增加或减少须经双方同意。任何注册资本的增加或减少都应经原审批机关



批准并在原登记机关变更登记。

如果在双方同意增加注册资本后，一方未能缴纳其增加的出资额，则另一方可以凭其判断：

(a) 提前 90 天给予未出资一方书面通知，如果未出资一方未能在上述 90 天内出资，则发出通知的一方可以自行缴付未出资一方未能缴付的全部或部分注册资本，而双方在合资公司中的持股比例也应根据双方实际缴付的注册资本比例而作相应调整，且双方有权任命的董事人数（在不改变合资公司董事会总人数的前提下）也应随之增加或减少，以最大程度地和当时双方在合资公司的持股比例相匹配；或

(b) 将该等未能缴付注册资本的行为视为未出资一方对本合同的实质违约。

双方同意，为使出资一方善意作出的上述任一选择产生法律效力，双方应签署所需的所有文件，并采取所需的所有步骤。

#### Article 16

If one party transfers its capital contribution or any interest in the JV Company, either partially or totally, it shall notify the other party in written form thirty (30) days in advance. The details of the conditions of the transfer shall be specified in the notice, such as the amount and the price of registered capital to be transferred, and the brief description of the proposed transferee. No transfer may occur without the approval of both parties. The non transferring party shall have the preemptive right to purchase the interest to be transferred, or, together with the transferring party, to transfer a similar portion of its interest on the same terms, in which case the non-transferring party shall reduce its portion of the interest to be transferred and shall cause the transferee to accept the transfer by the non-transferring party on the same terms as those applied to the transferring party.

#### 第十六条

如果一方转让其在合资公司的出资或任何权益，无论是部分转让或全部转让，该方应提前三十（30）天书面通知另一方。具体的转让条件应在通知中详细说明，如拟转让的注册资本的份额和价格，以及对拟受让方的简要介绍。股权转让必须经双方同意方可实施。非转让方对拟转让的股份享有优先购买权，或者有权与转让方一起以相同条件将其类似份额的权益予以转让，在这种情况下，转让方应适当减少其拟转让的股权比例，并促使受让方按照相同条件受让非转让方的股份。

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**Chapter 4 Board of Directors**

**第四章 董事会**

**Article 17**

The JV Company shall have Board of Directors with the highest authority over the JV Company.

**第十七条**

合资公司设立董事会，董事会是合资公司的最高权力机构。

**Article 18**

The Board of Directors shall consist of five (5) directors, of which three (3) directors shall be appointed by Party A and two (2) directors by Party B. The term of office for the directors is four (4) years unless sooner removed by the Party with the corresponding power of appointment, and may be renewed by that Party.

**第十八条**

董事会由五（5）名董事组成，其中，三（3）名由甲方委派，二（2）名由乙方委派。如非被委派方提前免职，董事的任期为四（4）年，并可由委派方委派后连任。

**Article 19**

The Board of Directors shall have one director designated as Chairman by Party A and one director designated as Vice Chairman by Party B.

**第十九条**

董事会会设董事长一名，由甲方指定，设副董事长一名，由乙方指定。

**Article 20**

When any party of the JV Company appoints or replaces a director, a written notice shall be submitted to the Board of Directors, and it shall also notify the other party.

**第二十条**

如任何一方委任或更换董事，应以书面形式通知董事会，并通知另一方。

**Article 21**

The Board of Directors shall convene one regular meeting every year. An interim meeting may be convened based on a proposal made by more than one third of all the directors.

**第二十一条**

董事会定期会议每年召开一次。经三分之一以上董事提议，可以召开临时会议。

**Article 22**

The Board meeting shall be held at the principal business location of the JV Company unless otherwise agreed by the Directors.

**第二十二条**

如非董事另行同意，董事会议在合资公司主要业务所在地召开。

**Article 23**

The Chairman shall convene and preside at any Board Meetings. Should the Chairman be unable to attend the Board meeting, the Vice Chairman shall convene and preside at the Board meeting.



**第二十三条**

董事长应召集并主持董事会议。如果董事长不能出席董事会议，副董事长应召集并主持董事会议。

**Article 24**

The Chairman shall issue a written notice thirty (30) days before the date of any Board meeting. The notice shall cover the agenda, time and place of the meeting. The agenda may only be changed with the consent of all of the directors.

**第二十四条**

董事长应在董事会召开前三十（30）天发出书面通知。通知应包括会议的议程、时间和地点。议程非经所有董事一致同意不得更改。

**Article 25**

Should a director be unable to attend the Board meeting, he may entrust another person (including another director) to attend on his behalf, provided that a written proxy signed by the non-attending director must be presented to the Board.

**第二十五条**

如果某一董事不能出席董事会议，其可以委托他人（包括其他董事）代为出席董事会，但条件是其应向董事会提交一份由其签署的书面委托书。

**Article 26**

The Board meeting requires a quorum of over two thirds of the total number of the directors (in person or by proxy) and at least one Director appointed by each of Party A and Party B attends. Each Director shall have one (1) vote. When the quorum is not present, any purported decisions adopted by the Board meeting are invalid.

**第二十六条**

董事会应有超过总数三分之二的董事（董事本人或委托他人）出席（而且至少有甲方和乙方委派的董事各一名）方可举行。每个董事享有一（1）票表决权。如果未满足上述法定人数的要求，董事会所作的任何决议均为无效。

**Article 27**

Detailed written records shall be made for each Board meeting and signed by all the attended directors or by the attended proxy. The record shall be made in Chinese and in English and shall be filed by a specially-assigned person by the Board. Each director shall be given a copy of such minutes and resolutions. No one shall amend or destroy the record during the Joint Venture term.

**第二十七条**

每次董事会都应制作详细的会议记录，并由全体董事（本人或其代理人）签字。会议记录应以中文和英文制作，且应由董事会特别指定的人归档保管。每名董事均应获得该等记录和决议的复印件。在合资期间，任何人不得修改或销毁这些记录。

**Article 28**

Directors are entitled to attend Board meetings via telephone, video conferencing or other electronic means, provided that a quorum is present and that each attendee can speak to each other attendee at the same time. In lieu of a Board meeting, resolutions in writing signed in person or via facsimile by all of the Directors of the JV Company shall have the same force and effect as if such resolutions had been passed at a duly constituted and convened meeting of the Board of Directors.



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## 第二十八条

董事可以通过电话会议、电视会议或其他电子方式出席董事会议，条件是满足法定人数的要求且出席者可以在同一时间互相交谈。作为董事会议的替代，一份经合资公司全体董事亲自签署或通过传真签署的书面董事会决议和一份由适当组织并召开的董事会会议所形成的决议具有同等效力。

## Article 29

As for the following issues, unanimous approval by the Board shall be required:

- 29.1 amendment to the articles of association of the JV Company
- 29.2 the termination and dissolution of the JV Company
- 29.3 adjustment to the registered capital of the JV Company
- 29.4 merger, break up or reorganization of the JV Company
- 29.5 transfer of registered capital by one or several parties
- 29.6 mortgage or pledge of registered capital by one or several parties to its creditor
- 29.7 sell, exchange or otherwise dispose of all or substantially all of the JV Company's assets, other than in the ordinary course of the JV Company's business;
- 29.8 license all or any substantial portion of the JV Company's intellectual property;
- 29.9 acquire or sell equity interests in other entities or be a promoter, incorporator, general partner, limited partner, owner of any other entity, except wholly owned subsidiaries;
- 29.10 authorize any sale, acquisition, mortgage, pledge, or other disposition of any asset of the JV Company, which would materially impair or change the conduct of the ordinary business of the JV Company.
- 29.11 authorize any activity or the JV Company entity commitment where the consideration to be paid by the JV Company entity is in excess of or as a result of which the JV Company entity may become obligated, directly or indirectly, for an amount in excess of or that would otherwise cause the JV Company entity to incur liability in excess of \$500,000 (or as specifically pre-authorized or delegated by a unanimous vote of the Board of Directors, or is a line item in the budget previously approved by the Board of Directors in the manner set forth herein),
- 29.12 authorize any activity that is outside the ordinary course of the JV Company's business;
- 29.13 incur indebtedness in excess of \$1,000,000 in the aggregate;
- 29.14 pledge or otherwise encumber any assets of the JV Company;
- 29.15 purchase, take, receive, lease or otherwise acquire, own, hold, improve, use and otherwise deal in or with real property or any interest in real property;
- 29.16 indemnify an owner, Director or any other person except pursuant to an agreement approved by both of the parties;
- 29.17 enter into any transaction with an owner of the JV Company or an affiliate of any owner;
- 29.18 sell any product at a gross margin of less than 30%;
- 29.19 change the principal accounting firm or auditor of the JV Company;
- 29.20 materially deviate from the JV Company's business plan; and
- 29.21 knowingly do any act in contravention of the Joint Venture Agreement or the JV Company's articles of association.

## 第二十九条

下列事项需经董事会一致同意：

- 29.1 修改合资公司章程；
- 29.2 合资公司的终止和解散；
- 29.3 调整合资公司的注册资本；
- 29.4 合资公司的合并、分立与重组；
- 29.5 一方或多方转让注册资本；
- 29.6 一方或多方向债权人抵押或质押其注册资本；



- 29.7 转让、交换或通过其他方式处置合资公司全部（或几乎全部）资产，除非该等处置为合资公司正常经营活动所致；
- 29.8 在合资公司全部（或任何实质部分的）知识产权上设置许可；
- 29.9 获得或者出售在其他实体中的权益，或者成为其他实体（其全资子公司除外）的发起人、设立人、一般合伙人，有限合伙人或其所有者；
- 29.10 批准任何将对合资公司的日常业务运作造成实质影响或改变的出售、获得合资公司资产以及在合资公司资产上设置抵押、质押或其他处置合资公司资产的行为；
- 29.11 批准任何将导致合资公司支付的对价超过500,000美元的行为或合资公司承诺，或者该行为或承诺将使合资公司直接或间接地承担超过500,000美元的义务（除非对于该事项已由董事会以一致投票的方式明确地予以事先批准或授权，或者该事项是由董事会以本合资合同规定的方式事先批准的预算中的一项）；
- 29.12 许可合资公司日常业务运作之外的行为；
- 29.13 发生总额超过1,000,000美元的债务；
- 29.14 在公司的资产上设置抵押或其他财产负担；
- 29.15 购买、占有、接受、出租或获得、拥有、持有、改善、使用或通过其他方式经营或处置不动产或不动产权益；
- 29.16 对股东、董事或其他人士予以赔偿，除非依据一份经双方同意的合同做出；
- 29.17 与合资公司的股东或者任何股东的关联方达成任何交易；
- 29.18 以小于30%的毛利润出售任何产品；
- 29.19 更换公司的主要会计师事务所或审计师；
- 29.20 严重偏离合资公司的经营计划；以及
- 29.21 明知违反合资合同和合资公司章程而行事。

#### Article 30

As for the following issues, approval by over two thirds of all the Board of Directors shall be required:

- 30.1 decide annual business principle, business plan (including proportion of sale in domestic and international markets) and budget and development plan;
- 30.2 exam and approve annual financial budget, final accounts and annual financial statement or increases in expenditures from the approved budget by more than 10%;
- 30.3 exam and approve the annual business report submitted by the general manager;
- 30.4 decide annual profit sharing scheme of the JV Company;
- 30.5 finalize labor contract and rules and regulations of the JV Company;
- 30.6 decide capital deployment and loan limit;
- 30.7 appoint and dismiss general manager, deputy general manager and other senior administrative personnel recommended by the general manager and decide their salary package;
- 30.8 formulate the welfare system for staff and workers of the JV Company in accordance with the relevant regulations of China; and
- 30.9 decide the organization structure of the JV Company and increase or remove subordinate functional departments.
- 30.10 decide bank account opening and signing procedures.

#### 第三十条

以下事项，需经董事会三分之二多数同意：

- 30.1 决定年度经营原则，经营计划（包括在国内市场和国际市场的销售比例），以及预算和发展计划；
- 30.2 审议并批准年度财务预算，决算和年度财务报表，审议并批准已批准预算中的支出

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超过10%的情况。

- 30.3 审议并批准总经理提交的年度经营报告；
- 30.4 决定合资公司的利润分配方案；
- 30.5 最终确定合资公司的劳动合同和规章制度；
- 30.6 决定资本配置和贷款额度；
- 30.7 聘任、解聘总经理，根据总经理的推荐聘任、解聘副总经理和其他由总经理推荐的高级管理人员，决定其薪酬事项；
- 30.8 根据中国的相关规定制定合资公司员工的福利制度；
- 30.9 决定合资公司的组织结构，增加或删减从属职能部门；以及
- 30.10 决定银行开户和签字权。

**Article 31**

Directors who do not hold positions in the Joint Venture Company shall not be compensated by the Joint Venture Company. All costs related to Board meetings shall be borne by the JV Company.

**第三十一条**

在合资公司未担任职务的董事，不得从合资公司领取薪金；与参加董事会会议有关的全部费用由合资公司承担。



**Chapter 5 Business Management Organization****第五章 经营管理机构****Article 32**

The JV Company shall establish a management organization/system under which there shall have production, technology, Human Resource, Finance and Administration Departments (subject to actual conditions of the JV Company).

**第三十二条**

合资公司应设立管理机构/系统，其下应包括生产、技术、人力资源、财务和行政部门（取决于合资公司的实际状况）

**Article 33**

The JV Company shall have one general manager and one deputy general manager appointed by the Board. The inaugural general manager shall be appointed by Party A and inaugural deputy general manager shall be appointed by Party B. Unless otherwise agreed by the parties, successors shall also be appointed by the party originally appointed such officer.

**第三十三条**

合资公司应有一名总经理和一名副总经理，由董事会任命。第一任总理由甲方任命，副总经理由乙方任命。除非双方另行同意，继任者仍应由原来任命相应职务的一方指定。

**Article 34**

The general manager shall be responsible to the Board of Directors directly, carry out the resolutions of the Board of Directors and organize the daily work on production, technology and management of the JV Company. The deputy general manager shall assist the general manager and perform the function of the general manager should the general manager be absent.

**第三十四条**

总经理直接对董事会负责，执行董事会决议并组织合资公司的生产、技术和管理的日常工作。副总经理应协助总经理工作，并在总经理缺席时行使总经理的职责。

**Article 35**

Decisions on important matters concerning JV Company's daily work require joint signatures from the general manager as well as the deputy general manager and such matters requiring joint signatures shall be specified by the Board of Directors. When dealing with other significant issues not requiring joint approval, the General Manager shall consult with the Deputy General Manager.

**第三十五条**

对与合资公司日常工作相关的重要事宜的决定应由总经理和副总经理的联合签署，且该等需要联合签署的重要事宜应由董事会明确列出。在处理不需要联合签署的其他重要问题时，总经理应与副总经理协商。

**Article 36**

The term of office for general manager and deputy general manager is four (4) years and may be renewed by the Board of Directors.

**第三十六条**

总经理和副总经理的任期为四（4）年，经董事会连续任命可连任。

**Article 37**





At the invitation of the Board of Directors, the Chairman, Vice Chairman and Directors of the Board may concurrently be the general manager, deputy general manager and other senior staffs of the JV Company.

### 第三十七条

经董事会邀请，董事长、副董事长和董事可以同时担任合资公司的总经理，副总经理和其他高级职员。

### Article 38

The general manager or deputy general manager of the JV Company shall not hold positions concurrently as general manager or deputy general manager of other economic organizations and shall not engage in activities of other economic organizations on commercial competition with the JV Company.

### 第三十八条

合资公司的总经理和副总经理不应同时在其他经济组织担任总经理或副总经理，且不得介入其他经济组织的与合资公司形成商业竞争的活动。

### Article 39

The JV Company shall have one Chief Engineer, one Chief Accountant and one Auditor appointed by the Board of Directors.

### 第三十九条

合资公司设一名总工程师，一名总会计师和一名审计师，由董事会委任。

### Article 40

The Chief Engineer, Chief Accountant and Auditor shall be under the leadership of the general manager. The Chief Accountant shall supervise accounting issues, carry out overall economic check and perform economic responsibility system. The Auditor shall conduct internal audit, check and verify financial income and spending, accounting statement, and file report to the general manager as well as the Board of Directors.

### 第四十条

总工程师，总会计师和审计师应接受总经理领导。总会计师应监督会计事宜，执行整体经济检查，并执行经济责任审计制度。审计师应进行内部审计，检查并核实财务收支、会计报表，并向总经理和董事会报告。

### Article 41

The general manager, deputy general manager, chief engineer, chief accountant, auditor and other senior administrative personnel who ask for resignation shall submit their written reports to the Board of Directors thirty (30) days before their resignation. In case any of the above-mentioned persons practice graft or be seriously derelict of duty, they may be dismissed at any time upon the decision of the Board, and if such conduct violates the criminal law, they may bear legal responsibilities.

### 第四十一条

总经理、副总经理、总工程师、总会计师、审计师和其他高级管理人员辞职的，应提前三十（30）天向董事会提交书面报告。在上述人员贪污受贿或者严重疏忽职守的情况下，经董事会决定可随时将其解聘，且如果相关行为触犯刑法的，其将承担刑事责任。



**Chapter 6 Finance and Accounting****第六章 财务与会计****Article 42**

The finance and accounting of the JV Company shall be handled in accordance with all applicable law and regulations.

**第四十二条**

合资公司的财务和会计应按照所有适用的法律、法规办理。

**Article 43**

The fiscal year of the JV Company shall be calendar year from January 1 to December 31, and the first fiscal year shall start from the JV Company's date of establishment till the end of that calendar year.

**第四十三条**

合资公司会计年度采用日历年制，从每年一月一日起至十二月三十一日止为一个会计年度。合资公司第一个财务年度应为合资公司设立之日起至当年的公历年底。

**Article 44**

All vouchers, accounting books, accounting statements and reports shall be written in Chinese and can put English notes if requested by other parties.

**第四十四条**

一切记账凭证、会计账簿、会计报表和报告应用中文书写，如经他方要求可加入英文注释。

**Article 45**

The JV Company shall adopt Renminbi (RMB) as its accounts keeping unit. The conversion of RMB into other currency shall be in accordance with the exchange rate of the converting day published by the Foreign Exchange Trading Center authorized by the People's Bank of China.

**第四十五条**

合资公司以人民币作为记账本位币。人民币与外币的折算应按照实际发生日中国人民银行授权的外汇交易中心所公布的汇价计算。

**Article 46**

The JV Company shall open accounts in RMB and foreign currency with Bank of China or other banks approved by the Board. Bank signature procedures shall be approved by the Board.

**第四十六条**

合资公司应在中国银行或董事会批准的其他银行开立人民币及外币账户。银行签字权应由董事会批准。

**Article 47**

The JV Company shall adopt internationally used accrual basis and debit and credit accounting system. The JV Company will operate so as to permit Party B to comply with its reporting obligations under United States public company reporting requirements in a manner which enables the JV Company to produce financial information that is to be provided to Party B within 25 days of the end of any calendar financial quarter. The JV Company will choose an audit partner and accountant approved by both parties. The chosen accounting partner will work closely with Party B's audit firm (Stonefield Josephson) and its Hong Kong office. The JV Company will cooperate as necessary in the preparation



of such financial reports and other compliance issues of Company B, and its books and records will be subject to quarterly audit by the parties and open at all times for reasonable review by each party and its agents.

#### 第四十七条

合资公司采用国际通用的权责发生制和借贷记账法记账。为了使乙方能够履行其在美国上市公司公告要求下的公告义务，合资公司所采取的运营模式应可以使其能够在每个日历财政季度的最后 25 天之内提供乙方进行公告所需的财务信息。合资公司将选择一个经双方同意的审查会计事务所。此会计事务所将与乙方的审查事务所（Stonefield Josephson）及其香港办公室通力合作。合资公司将在准备财务报告和合资公司的其它合规事宜中给予乙方必要协助，且合资公司的账簿和记录应由双方进行季度审计，且随时公开，以供各方和其代理人合理审阅。

#### Article 48

The accounting books of the JV Company shall include the follow contents:

- 48.1 all amount of income and payment in cash of the JV Company
- 48.2 situations concerning sale and purchasing the materials of the JV Company
- 48.3 situations concerning registered capital and debt of the JV Company
- 48.4 situations concerning date of settlement, increase and transfer of the registered capital of the JV Company

#### 第四十八条

合资公司的财务会计账册应记载如下内容:

- 48.1 合资公司所有和现金收入和支出的数额
- 48.2 合资公司资产的出售及购入情况
- 48.3 合资公司注册资本及负债情况
- 48.4 合资公司注册资本的缴付时间、增资及转让情况

#### Article 49

In the first three months of each fiscal year, the Finance Department shall prepare the previous fiscal year's balance sheet, profit and loss statement and cashflow statement, and prepare proposal regarding the disposal of profits which should be examined and signed by the auditor, then submit to the Board of Directors.

#### 第四十九条

合资公司财务部门应在每一个会计年度头三个月编制上一个会计年度的资产负债表、损益表和现金流量表，并准备须经审计师审核签字的利润分配建议书，提交董事会。

#### Article 50

The two parties of the JV Company have the right to invite an auditor to undertake annual financial check and examination at his own expense. The JV Company shall cooperate in all reasonable ways for the check and examination.

#### 第五十条

合资双方有权自费聘请审计师查阅合资公司账簿。查阅时，合资公司应以合理的方式对该查阅予以合作。

#### Article 51

The depreciation period for the fixed assets of the JV Company shall be decided by the Board of Directors in accordance with applicable law and regulations.

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第五十一条

合资公司固定资产的折旧年限应由董事会根据适用的中国法律法规决定。

**Article 52**

All matters concerning foreign exchange shall be handled in accordance with applicable law and regulations as well as the stipulations in the Joint Venture Contract.

第五十二条

一切外汇事宜应按照适用的法律法规和本合资合同的约定处理。





**Chapter 7 Profit Sharing**  
**第七章 利润分配**

**Article 53**

The JV Company shall allocate the reserve fund, the expansion fund and the bonuses welfare fund for staff and workers after payment of taxes and in accordance with law. The proportion of allocation shall be decided by the Board of Directors.

**第五十三条**

合资公司应依法从税后利润中提取储备基金、企业发展基金和职工奖励及福利基金。提取的比例由董事会决定。

**Article 54**

Unless otherwise agreed and stipulated by the Board of Directors, after paying the taxes in accordance with law and drawing various funds, the profits in net will be distributed according to the proportion of each party's investment in the registered capital.

**第五十四条**

除非董事会另行同意或决定，依法纳税和提取各项基金后的净利润，将按照每一方在注册资本中的出资比例进行分配。

**Article 55**

The JV Company shall distribute its profits once a year. The profit distribution plan and amount of profit to be distributed to each party shall be reported to the Board within the first three months following each fiscal year.

**第五十五条**

合资公司应每年分配一次利润。每年的利润分配方案及每一方应分的利润额应在下一个会计年度的前三个月内提交董事会。

**Article 56**

The JV Company shall not distribute its profits in case the losses in the previous years have not been made up. Profits not yet distributed in the previous year shall be allocated to the existing fiscal year.

**第五十六条**

在以往年度的亏损尚未弥补之前，合资公司不应分配利润。以往年度未分配利润，可并入本财务年度分配。



**Chapter 8 Staff and Workers****第八章 职工****Article 57**

The employment, dismissal, resignation of the staff and workers of the JV Company and their salary, welfare, labor insurance, labor protection, labor discipline and other matters shall be handled according to applicable law and regulations.

**第五十七条**

合资公司职工的招聘、解聘、辞职及员工的工资、福利、劳动保险、劳动保护、劳动纪律等事宜，应按照适用的法律和法规办理。

**Article 58**

The recruitment of the staff and workers of the JV Company shall be conducted by the JV Company publicly in open channels.

**第五十八条**

合资公司职工的招募应由合资公司通过公开渠道公开进行。

**Article 59**

The JV Company has the right to take disciplinary actions, such as warning, demerit recording and salary reducing against those staff and workers who violate the rules and regulations of the JV Company and labor disciplines. The JV Company's labor practices shall be in compliance with law.

**第五十九条**

合资公司有权对违反合资公司的规章制度和劳动纪律的职工给予处分，如警告、记过、降薪等。合资公司的劳动事宜应遵守法律。

**Article 60**

The salary treatment of the staff and workers shall be set by the Board of Directors according to the specific situation of the JV Company with reference to the regulations issued by the Government, and shall be specified in detail in the labor contract. The salary of the staff and workers shall be increased correspondently with the development of production and the progress of the worker's ability and technology.

**第六十条**

职工的工资待遇由董事会根据合资公司具体情况并参照政府公布的相关规定确定，并在劳动合同中具体规定。合资公司随着生产的发展和职工业务能力和技术水平的提高，相应提高职工的工资。

**Article 61**

Matters concerning welfare, bonus, labor insurance and labor protection shall be stipulated in rules and regulations of the JV Company to ensure that the staff and workers go in for production and work under normal condition.

**第六十一条**

有关福利、奖金、劳动保险和劳动保护的事宜应在合资公司的规章制度中规定，以确保职工在正常条件下生产、工作。



**Chapter 9 The Trade Union Organization**

**第九章 工会组织**

**Article 62**

The staff and workers of the JV Company have the right to establish trade union organization and carry out activities in accordance with the stipulation of the *Trade Union Law of the People's Republic of China*.

**第六十二条**

合资公司职工有权按照《中华人民共和国工会法》的规定，建立工会组织，开展工会活动。

**Article 63**

Trade union activities and the JV Company's dealings with the trade union shall be in compliance with law.

**第六十三条**

工会活动应依法活动，合资公司应依法处理与工会的关系。

**Article 64**

The JV Company shall annually allocate a total of 2% of all salaries of the staff and workers of the JV Company as trade union's funds which shall be used by trade union in accordance with the *Management Rules for the Trade Union Funds* formulated by All China Federation of Trade Union.

**第六十四条**

合资公司每月按合资公司职工工资总额的百分之二拨交工会经费。合资公司工会按照中华全国总工会制定的《工会经费管理办法》使用工会经费。



**Chapter 10 Duration, Termination and Liquidation of the Joint Venture**  
**第十章 期限、终止、清算**

**Article 65**

The duration of the JV Company is thirty (30) years. The establishment of the JV Company shall start from the date on which the business license of the JV Company is issued.

**第六十五条**

合资公司的期限为三十（30）年，自营业执照签发之日起计算。

**Article 66**

A written application for the extension of the duration unanimously proposed by two parties of the JV Company and embodied in the resolution of the Board of Directors shall be submitted to the relevant foreign investment authority six months prior to the expiry date of the Joint Venture Contract. The duration shall extend upon approval and shall file for amendment to registration information with the relevant company registration authority.

**第六十六条**

延长期限的书面申请应在合资合同终止前六个月内向相关外商投资审批机关提交，该提议应由合资双方一致提议并以董事会决议的方式体现。合资公司的延期应在取得批准时进行，并应到相应公司登记机关申请变更登记。

**Article 67**

With the agreement between both parties on the termination which should be pursuing the best benefits for the parties, the JV Company shall be terminated in advance of its term expiry. In this case, the decision for the termination shall be made by the plenary meeting of the Board of Directors and file for approval from the relevant foreign investment approval authority.

**第六十七条**

双方如一致认为终止合营符合双方最大利益时，可在期限届满之前终止合资公司。在这种情况下，终止决定应由全体董事出席的董事会议做出，并报相关外商投资审批机关批准。

**Article 68**

The JV Company and this Joint Venture Contract shall be terminated at the option of either Party if any of the following occurs, and a liquidation application shall be submitted to the original Examination and Approval Authority for approval:

- (a) one party materially breaches this Joint Venture Contract, and such breach (if capable of being rectified) is not rectified within 60 days of being notified by the other party;
- (b) neither Party intends or is able to continue the business cooperation;
- (c) the Company has suffered losses for a consecutive period of 3 years, causing the JV Company to be insolvent;
- (d) the Joint Venture Term expires and no resolution on the extension of the term is approved by the Board; or
- (e) the Board resolves to terminate the JV Company for any other reason.

**第六十八条**

发生下列情况之一时，任何一方有权依法终止合资公司和本合资合同，并且应向原审批机关提交一份清算申请，以获得批准：

- (a) 一方严重违反合资合同，并且违约行为（如果可以纠正的话）未能在收到另一方通知后60





天内得以纠正；

- (b) 任何一方均不愿或无法继续业务合作；
- (c) 合资公司连续三年遭受亏损，致使合资公司无法偿还到期债务；
- (d) 合资期限届满，且董事会没有作出延期的决议；或
- (e) 董事会因其他原因决定终止合资公司。

**Article 69**

Upon the expiration of the duration or termination of the JV Company, a liquidation committee for liquidating the assets of the JV Company shall be established in accordance with all applicable law.

**第六十九条**

合资公司期限届满或终止时，应依据所有适用的法律成立清算委员会，以对合资公司财产进行清算。

**Article 70**

The tasks of the liquidation committee are: to conduct thorough check of the property of the JV Company, its claims and indebtedness; to work out the statement of assets and liabilities and list of property; to formulate liquidation plan which shall be carried out upon the approval of the Board of Directors.

**第七十条**

清算委员会的任务是：对合资公司的财产、债权和债务进行全面清查，编制资产负债表和财产清单，制定清算方案，该方案应提请董事会通过后执行。

**Article 71**

During the liquidation period, the liquidation committee shall handle litigation matters on behalf of the JV Company.

**第七十一条**

在清算期间，清算委员会应代表合资公司处理诉讼事宜。

**Article 72**

The remuneration for the members of the liquidation committee shall have the priority to be effected from existing property of the JV Company.

**第七十二条**

清算委员会成员的报酬应以合资公司的现存财产优先支付。

**Article 73**

The liquidation committee shall revalue the assets of the JV Company based on depreciated book value with reference to current value.

**第七十三条**

清算委员会应在折旧账面价值的基础上参考现有价值，评估合资公司的资产。

**Article 74**

The remaining property after the clearance of debts of the JV Company shall be allotted according to two parties' contribution to the registered capital of the JV Company.

**第七十四条**



清算委员会对合资公司的债务全部清偿后，其剩余的财产按双方在注册资本中的出资比例进行分配。

**Article 75**

On completion of the liquidation, the JV Company shall submit a liquidation report to the foreign investment approval authority, go through the formalities for nullifying its registration relevant company registration authority and hand in its business license, at the same time, make an announcement to the public. After winding up of the JV Company, its accounting books shall be kept in the care of its Chinese party.

**第七十五条**

清算结束后，合资公司应向外商投资批准机构提交清算报告，并到相关公司注册机构办理注销登记手续，缴回营业执照，同时对外公告。合资公司结业后，其账册由中方保存。

**Article 76**

If either party breaches this Joint Venture Contract, it shall be liable for all direct economic losses suffered by the other party as a result of such breach. If both parties are at fault, their respective liability shall be proportional to their fault.

**第七十六条**

如果任何一方违反合资合同，其应对另一方因违约行为而遭受的所有直接经济损失负责。如果双方都有过错，则应根据双方的过错按比例承担责任。



**Chapter 11 Rules and Regulations****第十一章 规章制度****Article 77**

Following are the rules and regulations to be formulated by the Board of Directors of the JV Company;

- 77.1 Management regulations, including powers and functions of the management branches and its working rules and procedures;
- 77.2 Rules for the staff and workers;
- 77.3 System of labor and salary;
- 77.4 System of work attendance record, promotion and awards and punishment for the staff and workers;
- 77.5 Detailed rules of staff and workers' welfare;
- 77.6 Finance system;
- 77.7 Liquidation procedures upon the dissolution of the JV Company;
- 77.8 Other necessary rules and regulations.

**第七十七条**

合资公司董事会制定的规章制度如下：

- 77.1 经营管理制度，包括所属各个管理部门的职能和权利，及其工作规章与程序；
- 77.2 职工守则；
- 77.3 劳动工资制度；
- 77.4 职工考勤、升级与奖惩制度；
- 77.5 职工福利细则；
- 77.6 财务制度；
- 77.7 合资公司解散时的清算程序；
- 77.8 其它必要的规章制度。

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**Chapter 12 · Supplementary Articles****第十二章 附则****Article 78**

The amendment to the Joint Venture Contract shall be unanimously agreed and decided by the Board of Directors and submitted to the original examining and approving authority for approval.

**第七十八条**

本合资合同的修改须经董事会会议一致同意决定，并报原审批机关批准。

**Article 79**

The Joint Venture Contract shall be written in Chinese and in English. Both languages are of equal validity. In events of any discrepancy between the two aforementioned versions, the Chinese version shall prevail.

**第七十九条**

本合资合同用中文和英文书写，两种文本具有同等效力。两种文本如有不一致之处，以中文文本为准。

**Article 80**

The Joint Venture Contract shall come into effect upon the approval by the relevant foreign investment approval authority.

**第八十条**

本合资合同须经相关外商投资审批机关批准后方能生效。

**Article 81**

The Parties shall use reasonable efforts to resolve and settle amicably through consultations any dispute, controversy or claim (a "Dispute").

**第八十一条**

双方应尽合理努力，通过友好协商解决争议、分歧或权利主张（“争议”）。

If any Dispute is not settled amicably through consultations within one hundred twenty (120) days of one Party's receipt of the other Party's notice of a Dispute, then any Party involved in the Dispute may elect to submit such Dispute to arbitration, in which event such Dispute shall be exclusively and finally settled by binding arbitration in Singapore under the auspices of the Singapore International Arbitration Centre, by a sole arbitrator.

如果在一方收到另一方关于存在争议的通知后一百二十（120）天内，双方无法通过友好协商解决争议，则争议所涉及的任何一方可以选择将争议提交仲裁解决，在该等情况下，争议将在新加坡国际仲裁中心由独任仲裁员在新加坡终局地和排它地解决。

The arbitration proceedings shall be conducted in the English language, and all documentation to be reviewed by the arbitrator or submitted by the Parties shall be in the English language. The arbitration tribunal shall apply the Arbitration Rules of the United Nations Commission on International Trade Law in effect at the time of the arbitration. However, if such rules are in conflict with the provisions here set forth, including the provisions concerning the appointment of the arbitrator, these provisions shall prevail.

仲裁程序应以英文进行，且所有交由仲裁员审阅的文件或者双方提交的文件都应使用英文。在



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仲裁中仲裁庭应适用联合国国际贸易法委员会的仲裁规则。但是，如果上述规则与本合资合同的条款存在冲突，包括关于指定仲裁员的条款，则适用本合资合同中的条款。

During arbitration, the Parties shall perform this Joint Venture Contract to the fullest extent possible, except for the matter or matters in dispute.

在仲裁期间，除存在争议的事宜外，双方应尽可能全面地履行合资合同。

The arbitrator shall render a written decision in English stating their reasons for their decision within twelve (12) months of the request for arbitration, and such award shall be final and binding upon the Parties without any right of review or appeal. Any compensation shall be calculated and paid in United States Dollars if to be paid to Party B.

仲裁员应在申请仲裁之日起十二（12）个月之内以英文方式做出书面仲裁决定，陈述其做出决定的理由，且该仲裁裁决应是终局并对双方具有约束力，双方均无权申请再审和上诉。如果赔偿系对乙方作出，应用美元计算并以美元支付。

The Convention on the Recognition and Enforcement of Foreign Arbitral Awards (also known as the "New York Convention") shall apply to this Joint Venture Contract and to any arbitral award or order resulting from any arbitration conducted hereunder. Judgment upon the award rendered by the arbitrator may be entered in any court of record of competent jurisdiction in any country, or application may be made to such court for judicial acceptance of the award and an order of enforcement, as the law of such jurisdiction may require or allow. The Parties agree that the award of the arbitral tribunal shall be the sole and exclusive remedy among them regarding any and all claims and counterclaims presented to the tribunal. The Parties further agree that this arbitration clause is an explicit waiver of any immunity or defense that may apply against the enforcement and execution of any arbitral award or any judgment thereon.

《承认和执行外国仲裁裁决公约》（也称“纽约公约”）应适用于本合资合同和根据本合资合同进行的任何仲裁导致的任何仲裁裁决或命令。任何仲裁裁决均可通过在任何有适当管辖权的法院作出判决，或在该管辖区的法律要求或允许的情况下，向该法院申请对裁决的司法认可和强制执行令。双方同意仲裁庭的裁决是双方关于提交仲裁庭的任何及所有诉讼请求或反诉的唯一的和排他的救济方式。双方在此进一步同意，本仲裁条款表明双方明确放弃可能适用于任何仲裁裁决或与之相关的任何其他决定的执行或履行的任何豁免或抗辩。

The substantially prevailing Party in an arbitration proceeding shall be entitled, in addition to such other relief as may be granted, to recover its attorneys' fees and costs, and the other Party shall pay all costs of the arbitration. The arbitrator shall determine which of the Parties has substantially prevailed based upon an assessment of which Party's major arguments or positions taken in the proceedings could fairly be said to have prevailed over the other Party's major arguments or positions on major disputed issues.

仲裁程序的败诉一方应承担所有仲裁费用和支出，并应在仲裁庭裁决的其他赔偿之外，补偿胜诉一方的律师费和支出。仲裁员应根据仲裁过程中在主要争议的事项上，以哪一方的主要论点或立场公允地压倒了另一方的主要论点和立场，来决定胜诉方。

#### Article 82

This contract is governed by and construed in accordance with Chinese law.

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第八十二条

本合同受中国法律管辖并依据中国法律解释。

Article 83

This contract is executed in Shenzhen, China by the authorized representatives of the parties on December 8<sup>th</sup>, 2007.

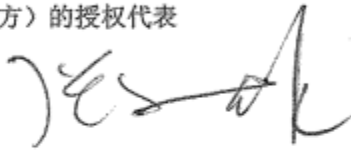
第八十三条

本合同有双方代表于 2007 年 12 月 8 日在中国深圳签署。

**Authorized representative of Hunchun Baoli Communication Co., Ltd. (Party A)**

珲春宝力通信有限公司（甲方）的授权代表

Signature（签字）：



Date（日期）：

**Authorized representative of Superconductor Investments (Mauritius) Limited (Party B)**

超导投资（毛里求斯）有限公司（乙方）的授权代表

Signature（签字）：



Date（日期）：

12/8/07





**Form of Technology and Trademark License Agreement**

Superconductor Technologies Inc., a Delaware corporation **Superconductor Investments (Mauritius) Ltd** (“**STI**”) and **BAOLI Superconductor Technology Co, Ltd**, a technologically-advanced contractual joint venture in the People’s Republic of China (“**BSTC**”), make this License of Technology and Trademark Agreement (“**License Agreement**”) as of \_\_\_\_\_, 2007. Certain capitalized terms are defined in Schedule A—Definitions.

**Recitals**

A. Hunchun BaoLi Communications Co. Ltd., a Chinese enterprise (“**BaoLi Communications**”) and STI have established BSTC as a technologically-advanced contractual joint venture, within the territory, and under the laws, of the People’s Republic of China to manufacture, market and sell the Product in the Territory and to manufacture the Product for export from the Territory by sale to STI and its designees.

B. STI makes this License Agreement with BSTC: (a) to enable it (i) to manufacture the Product in the Territory so that BSTC may market and sell such Product in the Territory and (ii) to manufacture the Product for export from the Territory by sale to STI and its designees pursuant to that certain Export Supply Agreement entered into by and between the parties (the “Export Supply Agreement”); and, (b) to use certain marks of STI in connection with the foregoing.

**Now therefore**, in consideration of the promises herein, and for good and valuable consideration, the sufficiency and receipt of which is hereby acknowledged, and intending to be legally bound, the parties hereby agree as follows:

**1. Grant of Technology License**

As of the Effective Date, STI grants to BSTC, subject to the limitations of this License Agreement, an exclusive license, for a term of thirty years (subject to earlier termination as provided herein), without any right to sub-license, to use the Technology within the Territory solely to the extent needed to make, reproduce, and manufacture, the Product: (i) to market, sell, and offer for sale such Product solely for use within the Territory, in every instance only for Qualified Uses, and (ii) to sell such Product to STI and its designees for use outside the Territory pursuant to the terms of the Export Supply Agreement. For the avoidance of doubt, BSTC expressly agrees that this license to use the Technology shall not serve to restrict in any manner STI’s exercise of rights with regard to the Technology outside the Territory. As an express condition of this license, BSTC shall not have the right to modify or create derivative works of the Technology without the express permission of STI, nor to use the Technology to make, reproduce, manufacture, market, sell, or offer for sale any products other than the Product. All rights not expressly granted herein regarding the Technology are reserved to STI.

**2. Grant of Trademark License**

As of the Effective Date, STI grants to BSTC, subject to the limitations of this License Agreement, an exclusive, royalty-free license, coterminous with the license of Section 1, without any right to sub-license, to use the Licensed Trademarks only in connection with the manufacture, sale and service of the Product within the Territory, in each case only for Qualified Uses and only as the Product is permitted to be manufactured, sold and serviced in conformity with the license granted in Section 1.

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**3. Related Services**

3.1 Transition Assistance During the first year after the Effective Date, (i) STI will supply BSTC with kits for up to 500 units of the Product, priced at direct material and labor cost plus 20%, as reasonably requested by BSTC on not less than 90 days' notice and (ii) STI will provide reasonable consulting support to BSTC's efforts in assembling the kits and acquiring and/or building the specialty equipment and fixtures necessary to manufacture the Product in accordance with the training plan attached to this Agreement as Schedule E—Training Plan. BSTC will pay for all costs required to send its technical staff to STI to be trained; as well as the expenses (living and travel costs within the Territory) of any STI staff while within the Territory. STI will pay for any travel costs to get its personnel to the Territory as required by the training plan. STI may sell any excess equipment and fixtures it may have to BSTC as mutually agreed.

**3.2 Manufacturing arrangements**

If STI determines that it wishes to have the Product made in China, upon STI's request from time to time, BSTC will manufacture the Product for sale by STI outside the Territory, priced to STI at direct material and labor cost plus 20%.

The parties acknowledge that certain aspects of the manufacturing process may be retained by STI based on factors including economics, feasibility and regulatory climate. To the extent consistent with compliance with any prohibitions as to export of pertinent technology, STI will sell to BSTC, priced to BSTC at direct material and labor cost plus 20%, any components as to which it retains the manufacturing process.

**4. Royalties; payment terms****4.1 Royalties**

In consideration, and as a condition to the continuance, of the license granted under Section 1, BSTC shall timely pay STI royalties equal to the greater of (i) 7% of Revenues for the corresponding quarter or (ii) any applicable Minimum Royalty for the corresponding quarter. No payment of Minimum Royalty hereunder is creditable towards royalty due for future quarters.

**4.2 Reporting; payment**

During the term of this Agreement and for a period of two (2) years thereafter, BSTC shall keep and maintain all books of account relating to Revenue reasonably needed to support the calculation of royalties under this Agreement at its principal offices, in conformity with generally accepted accounting practices as observed in the United States. Within 15 days after the end of each calendar quarter, BSTC shall render a Royalty Statement to STI. BSTC shall pay to STI the royalty due for each calendar quarter within 15 days after the end of each calendar quarter by wire transfer in United States Dollars in readily available funds to an account designated by STI in the United States or such other place as STI may identify.

STI may audit the books and records of BSTC relating to the calculation of any Royalty Statement. BSTC shall pay all costs and expenses of any audit if it shows an underpayment in connection with any such Royalty Statement by more than 5%.

**4.3 Taxes**

In the event that BSTC is required by the laws of the People's Republic of China to withhold or deduct any taxes, levies, fees, imposts, duties or similar charges ("Local Taxes") from any payments hereunder to STI, or in the event that payments by BSTC to STI hereunder are otherwise subject to Local Taxes (in each case other than the national withholding tax on Chinese-source royalties paid to nonresidents of China that is currently imposed under Chinese domestic law (the "Withholding

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Tax”), but only to the extent that the Withholding Tax does not exceed a rate of 10%) then BSTC will pay such additional amounts to STI as shall be necessary in order that the net amounts received by STI, after withholding, deduction or payment of such Local Taxes, equal the amounts that would otherwise have been receivable by STI pursuant to this License Agreement in the absence of such Local Taxes.

## **5. Ownership matters**

### **5.1 Technology**

As between the parties, STI retains all title, and (except as expressly granted in this License Agreement) all rights and interest in and to the Technology and any and all portions thereof. BSTC hereby grants to STI a perpetual royalty-free license, with right to sublicense, to all rights, title and interest in and to any BSTC Technology, which license shall be non-exclusive for the Territory and exclusive outside the Territory. STI consents to the grant by BSTC to BaoLi Communications of a perpetual, non-exclusive royalty-free license for the Territory to all rights, title and interest in and to any BSTC Technology.

### **5.2 Licensed Trademarks**

All right, title and interest in and to the Licensed Trademarks, other than the specific rights granted to BSTC in this License Agreement, are retained by STI for its own use or license to others. BSTC recognizes the value of the goodwill associated with the Licensed Trademarks and acknowledges that (as between the parties) such goodwill belongs exclusively to STI. BSTC agrees that (i) it will not assert any interest or property rights in any rights included in the Licensed Trademarks other than the license set forth herein; (ii) all permitted uses of the Licensed Trademarks by BSTC shall inure to the benefit of and be on behalf of STI; and (iii) nothing in this License Agreement shall give BSTC any interest in the Licensed Trademarks other than the right to use the Licensed Trademarks in accordance with this License Agreement. BSTC shall not attack, directly or indirectly, the validity of the Licensed Trademarks or STI’s title in or to the Licensed Trademarks. BSTC will not modify, enhance, or create a derivative work of the Licensed Trademarks (“ **Junior Marks** ”) without the prior written consent of STI, and STI will own all right, title and interest in and to the Junior Marks, including all intellectual property rights therein. BSTC irrevocably transfers and assigns to STI, and agrees to irrevocably transfer and assign to STI, all right, title and interest in and to the Junior Marks, including all intellectual property rights therein. At STI’s request and expense, during and after the term of this License Agreement, BSTC will assist and cooperate with STI in all respects (and will cause its employees and subcontractors to assist and cooperate with STI in all respects), and will execute documents (and will cause its employees and subcontractors to execute documents), and will take such further acts reasonably requested by STI to enable STI to acquire, perfect, maintain and enforce STI’s intellectual property rights in and to the Junior Marks. BSTC hereby appoints the officers of STI as BSTC’s attorney-in-fact to execute documents on behalf of BSTC and its employees and subcontractors for this limited purpose. BSTC also, on behalf of itself and its employees and subcontractors, irrevocably transfers and assigns to STI, and agrees to irrevocably transfer and assign to STI, and waives and agrees never to assert, any and all moral rights that BSTC or its employees or subcontractors may have in or with respect to the Junior Marks, even after termination of the licenses granted by this License Agreement. BSTC will not register, nor attempt to register, any trade name, domain name, service mark, or trademark which, in whole or in part, incorporates or is confusingly similar to the Licensed Trademarks.

### **5.3 Clearances**

BSTC will be responsible for verifying that its use of any patent rights, trademark rights or other intellectual property rights related to the manufacture, marketing or sale of the Product in the

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Territory, including the Technology and the Licensed Trademarks, does not violate intellectual property rights of any other person.

#### **5.4 Filings; costs**

BSTC agrees to assist STI: (i) in recording this License Agreement with appropriate government authorities where such recording is required by law or regulation or where such recording is permitted or desired by STI; and, (ii) in applying in the name of STI for patents and/or trademarks on all or any of the Technology or the Licensed Trademarks in the Territory. BSTC shall not apply for any patents on the Technology without the prior written consent of STI. All costs associated with recording this License Agreement, the licenses granted herein and registering, maintaining, or renewing rights in and to the Technology or Licensed Trademarks in the Territory shall be borne by BSTC.

#### **5.5 Infringements**

If, at any time, BSTC learns that another party is or may be making unauthorized use of the Licensed Trademarks or the Technology, BSTC agrees to give STI prompt notice of that infringement. STI, at its option and for its own account, may take actions with respect to any such infringement and any other infringements, and BSTC agrees to cooperate with STI (at the sole expense of STI) in connection with any action taken by STI with respect to infringements.

#### **5.6 Use**

During the term of this License Agreement, BSTC agrees sufficiently to use and employ the Licensed Marks so as to maintain and preserve the legal validity and enforceability of the Licensed Marks in the Territory.

#### **5.7 Quality Control**

(i) Maintenance of Quality. BSTC agrees that its manufacture of the Product and its marketing and service thereof will be of high quality and at least of the quality offered by STI at the time that this License Agreement is entered. BSTC agrees that it will maintain the same level of quality for its manufacture of the Product and its marketing and service thereof throughout the term of this License Agreement and throughout any renewals thereof.

(ii) Investigation. STI may periodically request samples of marketing materials showing use of the Licensed Trademarks to view how BSTC is using the Licensed Trademarks. BSTC shall comply with all reasonable instructions given by STI to BSTC as to the use of the Licensed Trademarks. STI will have the right to access BSTC's premises during normal business hours on reasonable advance notice for the purpose of inspecting the facilities used by BSTC in connection with the manufacturing, marketing and service of the Product associated with the Licensed Trademarks in order to ensure the quality thereof.

### **6. Competition**

#### **6.1 Direct or indirect competition**

During the term of this License Agreement, except as permitted hereunder BSTC will not directly or indirectly promote market or sell any products in or outside the Territory which compete directly or indirectly with any STI products, nor will it assist any other person in doing so.

#### **6.2 Notification of opportunities**

If STI learns of any opportunity for marketing the Product within the Territory, it will promptly notify BSTC, and if BSTC learns of any opportunity for marketing the Product outside the Territory, it will promptly notify STI.

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**7. Compliance with Law****7.1 Export**

BSTC agrees to comply strictly with any and all laws and regulations of the United States applicable to the transfer of Technology and Products, whether by sale, lease, license, technical assistance, or any other means of distribution. Without limitation, in no case may BSTC transfer any Technology or Products in any manner or to any party in violation of the Export Administration Regulations (15 CFR Parts 730—774.1) or the regulations of the Office of Foreign Assets Control, U.S. Treasury Department (31 CFR Parts 500—598), or other U.S. Government agency with jurisdiction of same. BSTC shall be responsible for obtaining any and all U.S. Governmental approvals of such transfers, with the reasonable assistance of STI. This Agreement, and the license in Section 1, shall not grant any license to any technology to the extent that such licensing is prohibited by any applicable laws, regulations or other US government policies.

**7.2 Civilian Use Only**

None of the Technology transferred to BSTC by STI will be applied to or in any other way used by BSTC to design or manufacture any Product for use in a military environment or by a military end-user. Without limiting the generality of the foregoing, no Product designed or manufactured by BSTC will be sold or otherwise distributed, directly or indirectly, to any “entity” identified by the U.S. Government in Part 744 of the Export Administration Regulations, or to any customer who is classified as a “military end user” by the U.S. Government without the express advance approval by the U.S. Government.

**7.3 Law; Foreign Corrupt Practices Act**

BSTC agrees to comply with all laws, statutes, regulations, rules, ordinances, orders, or other legal requirements, including, but not limited to the U.S. Foreign Corrupt Practices Act, and Chinese law covering a similar subject matter, and to obtain and maintain all licenses and permits required to perform its obligations hereunder. BSTC acknowledges that the U.S. Foreign Corrupt Practices Act, and Chinese law covering a similar subject matter, specifically prohibits employees or agents or consultants of Chinese or United States corporations and their domestic and foreign subsidiaries from offering or making payments (whether made in China, the United States or elsewhere) to employees or agents of foreign governments (or government controlled entities) for the purpose of influencing official acts or decisions. Payments or offers of payment intended for government officials disguised as compensation to agents, consultant fees and the like violate the law as much as direct payments and are not to be made. BSTC agrees that: (i) no undisclosed or unrecorded account, fund, or assets of the other shall be established by it for any purpose nor shall any account, fund, or assets of either be held in the name of another entity or person; (ii) no false, misleading, or artificial entries shall be made in the books and records of either by the other for any reason and no arrangement that results in such entries or in any arrangement that omits to make entries that properly should be made; (iii) no payment from funds of either shall be approved or made by the other with the intention or understanding that any part of such payment is to be used for any purpose other than that described by the documents supporting such payment; and (iv) all payments of any nature made by either on behalf of the other will be properly identified and recorded by it, and be made only in accord with the provisions of valid purchase orders, subcontracts, blanket orders, and written sales agency or consulting agreements and that full value will be received for each such payment. BSTC further agrees to adopt and apply the compliance procedures applicable thereto reasonably approved by Licensor and to conduct employee training and to audit business transactions in a manner and at such times appropriate to ensure compliance with the Foreign Corrupt Practices Act and similar laws and regulations of such other countries.

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**8. Default and termination****8.1 Causes of termination**

The licenses granted by Section 1 and 2 shall terminate if an Event of Default has occurred as provided in Section 8.2 and any non-defaulting party elects to terminate such licenses. Such licenses shall also terminate on the termination of the BSTC joint venture. The election by a party to terminate such licenses shall not be the exclusive remedy, and such party shall retain any and all remedies available under law, equity, or this License Agreement.

**8.2 Events of Default**

The occurrence of any of the following events shall constitute an **Event of Default** on the part of the party in respect of which such event occurs (the “**Defaulting Party**”):

- (i) any material default in performance of, or any material failure to comply with, this License Agreement or any other agreements, obligations or undertakings of such party to the other party, and the continuation of such default for thirty (30) days following notice of such default from the other party;
- (ii) the incorrectness in any material respect of any representation or warranty contained in this License Agreement or in any certificate or document delivered hereunder;
- (iii) the institution by a party of proceedings of any nature under any laws, whether now existing or subsequently enacted or amended, for the relief of debtors wherein such party is seeking relief as debtor;
- (iv) a general assignment by a party for the benefit of creditors, the admission by a party in writing of its inability to pay its debts as they mature, or the institution by a party of a proceeding under any provision of bankruptcy or insolvency law as now existing or hereafter amended or becoming effective; or
- (v) the appointment of a receiver for a party or a substantial portion of its assets which appointment is not vacated within sixty (60) days after the filing thereof.

**8.3 Effect of termination; remedies**

The termination under Section 8.2 of the licenses granted by Sections 1 and 2 shall not relieve any party from its other obligations hereunder, including any liability for past breaches.

**9. Indemnification****9.1 Indemnification by STI**

STI will defend, indemnify and hold harmless BSTC and its officers, directors, employees, shareholders, customers, agents, and permitted successors and assigns from and against any and all loss, damage, settlement or expense (including legal expenses), as incurred, resulting from or arising out of (i) any breach of this License Agreement by STI or (ii) any third-party claim based on Product sold by STI or its assignees outside the Territory, other than claims arising in conjunction with a breach by BSTC of its obligations pursuant to this License Agreement.

**9.2 Indemnity by BSTC**

BSTC will defend, indemnify and hold harmless STI and its officers, directors, employees, shareholders, customers, agents, and permitted successors and assigns from and against any and all loss, damage, settlement or expense (including legal expenses), as incurred, resulting from or arising out of (i) any breach of this License Agreement by BSTC or (ii) any third-party claim based on Product sold by BSTC or its assignees, or any other activities of BSTC, whether in connection with the Licensed Trademarks or otherwise, other than claims arising in conjunction with a breach by STI of its obligations pursuant to this License Agreement.

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### 9.3 Procedure

- (i) Notice. Promptly upon receipt by an indemnified party of a notice of a claim by a third party that may give rise to a claim hereunder, the indemnified party shall give written notice thereof to the indemnifying party, although failure to do so shall not affect the right to indemnification except to the extent of actual prejudice.
- (ii) Control of defense. The indemnified party shall allow the indemnifying party to assume control of the defense of any such action brought by a third party so long as such defense will be conducted by reputable attorneys retained by the indemnifying party at the indemnifying party's cost and expense and the indemnifying party agrees to be solely responsible for satisfying the claim. The indemnified party will have the right to participate in such proceedings and to be separately represented by attorneys of its own choosing at its own expense.
- (iii) Effect. The indemnifying party may contest or settle any third party claim on such terms as the indemnifying party may choose; however, the indemnifying party will not have the right, without the indemnified party's written consent, to settle any such claim if such settlement (i) arises from or is part of any criminal action, suit or proceeding, (ii) contains an admission of wrongdoing on the part of the indemnified party, or (iii) provides for injunctive relief which is binding on the indemnified party or limits its use of the Licensed Trademarks.

## **10. Confidentiality**

### 10.1 Obligations

Each party agrees that (a) except as provided in Section 10.3, it shall maintain the confidential nature of any Confidential Information received from the other party, and (b) it shall use such Confidential Information solely for the purpose of meeting its obligations under this License Agreement and not in connection with any other business or activity. At the termination of the licenses granted under Sections 1 and 2, or any time upon demand of a disclosing party, each of the parties agrees to return any and all materials containing any Confidential Information.

### 10.2 Limitations on confidentiality obligations and use restrictions

The restrictions on use and the obligations of confidentiality contained in this License Agreement will not apply to any item or combination of items of information (a) that the receiving party can demonstrate (i) is then in the public domain by acts not attributable to such party, (ii) is disclosed to a third party on an unrestricted basis by the party to whom it belonged, (iii) is hereafter received on an unrestricted basis by the receiving party from a third party source who to the receiving party's knowledge after due inquiry is not and was not bound by confidentiality obligations to the disclosing party, or (iv) was known to the receiving party as shown by its written records prior to the date of disclosure hereunder.

### 10.3 Actions if disclosure required

If the receiving party is requested pursuant to, or required by, applicable law or regulation or by legal process to make any disclosure otherwise prohibited hereunder, it shall provide the disclosing party with prompt notice of such requests or requirements prior to disclosure so that (a) the disclosing party (with the reasonable cooperation of the receiving party) may seek an appropriate protective order or other remedy and/or (b) the parties can seek in good faith to agree on the appropriate scope and approach to disclosure. If a protective order or other remedy is not obtained, the receiving party may furnish only that portion of the Confidential Information which, in the written opinion of counsel addressed to the disclosing party, it is legally compelled to disclose and shall use its reasonable efforts to obtain confidential treatment for the Confidential Information.

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**10.4 Injunctions**

The parties agree that remedies at law may be inadequate to protect against breach of this Article 10, and hereby agree to the granting of injunctive relief without proof of actual damage or requirement for posting of a bond.

**11. General****11.1 Relationship of parties**

Nothing contained in this License Agreement will be construed as creating any agency, partnership, or other form of joint enterprise between the parties. The relationship between the parties will at all times be that of independent contractors. Neither party will have authority to contract for or bind the other in any manner whatsoever. This License Agreement confers no rights upon either party except those expressly granted herein.

**11.2 Authority**

Each party represents that it has full corporate power and authority to enter into this License Agreement and comply with the terms and conditions hereof, and that the person signing this License Agreement on behalf of such party has been properly authorized and empowered to enter into this License Agreement.

**11.3 Warranty disclaimer**

STI does not warrant that the Product or the Technology will meet the needs of BSTC. STI warrants that any Product or component manufactured and delivered to BSTC by STI will, when delivered, conform to the documentation and specifications provided by STI. STI will replace any such STI Product that STI provides to BSTC and that is defective, upon request by BSTC made within thirty days after delivery of the defective item and upon return of the defective item. EXCEPT AS EXPRESSLY PROVIDED IN THIS SECTION 11.3, STI MAKES NO WARRANTIES TO ANY PERSON OR ENTITY, EXPRESS, IMPLIED, STATUTORY OR OTHERWISE, REGARDING THE SUBJECT MATTER OF THIS LICENSE AGREEMENT. STI SPECIFICALLY DISCLAIMS ANY IMPLIED WARRANTIES OF MERCHANTABILITY AND FITNESS FOR A PARTICULAR PURPOSE, NOR ARE THERE ANY WARRANTIES CREATED BY A COURSE OF DEALING, COURSE OF PERFORMANCE OR TRADE USAGE. STI DOES NOT WARRANT THAT THE PRODUCT WILL MEET BSTC'S OR ANY CUSTOMER'S NEEDS OR BE FREE FROM ERRORS, OR THAT THE OPERATION OF THE PRODUCT WILL BE UNINTERRUPTED. THE FOREGOING EXCLUSIONS AND DISCLAIMERS ARE AN ESSENTIAL PART OF THIS AGREEMENT AND FORMED THE BASIS FOR DETERMINING THE ROYALTIES ASSESSED HEREUNDER.

**11.4 Limitation of damages**

STI's liability for damages from any cause of action whatsoever, including liability for any claim of infringement of proprietary rights will not exceed the value of its ownership interest in BSTC. In no event will STI be liable for lost profits or other incidental or consequential damages of BaoLi Communications or of BSTC under any circumstances whatsoever, even if advised of the possibility of such damages.

**11.5 Governing law**

This License Agreement and all disputes arising out of or related to this License Agreement, or the performance, enforcement, breach or termination hereof, and any remedies relating thereto, will be construed, governed, interpreted and applied in accordance with the laws of California, without regard to conflict of laws principles. Except (i) with reference to enforcement of the obligations of Section 10, (ii) with reference to enforcement of any final judgment duly obtained, and (iii) as

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provided in this Section 11.5 and Section 11.6, the sole jurisdiction and venue for actions related to the subject matter hereof will be state and federal courts in Los Angeles, California and each of the parties hereto submits itself to this exclusive jurisdiction and venue of such courts for the purpose of such action. Each party acknowledges that its breach of this License Agreement may cause irreparable injury to the other for which monetary damages may not be an adequate remedy. Accordingly, and without prejudice from the dispute resolution mechanisms of Section 11.6, a party in the event of such a breach by the other will be entitled without the requirement for posting of any bond to seek injunctions or other equitable remedy in any jurisdiction through which the potential for irreparable injury may be mitigated or prevented.

#### 11.6 Arbitration of disputes

- (i) The parties shall use reasonable efforts to resolve and settle amicably through consultations any dispute, controversy or claim (a "Dispute") arising out of or in connection with this License Agreement or its validity, interpretation, performance, breach or enforceability.
- (ii) If any Dispute is not settled amicably through consultations within one hundred twenty (120) days of one party's receipt of the other party's notice of a Dispute, then any party involved in the Dispute may elect to submit such Dispute to arbitration, in which event such Dispute shall be exclusively and finally settled by binding arbitration in Singapore under the auspices of the Singapore International Arbitration Centre through a sole arbitrator.
- (iii) The arbitration proceedings shall be conducted in the English language, and all documentation to be reviewed by the arbitrator or submitted by the parties shall be in the English language. The arbitration tribunal shall apply the Arbitration Rules of the United Nations Commission on International Trade Law in effect at the time of the arbitration. However, if such rules are in conflict with the provisions here set forth, including the provisions concerning the appointment of the arbitrator, the provisions here set forth shall prevail.
- (iv) During arbitration, the parties shall perform this License Agreement to the fullest extent possible, except for the matter or matters in dispute.
- (v) The arbitrator shall render a written decision in English stating its reasons for its decision within twelve (12) months of the request for arbitration, and such award shall be final and binding upon the parties without any right of review or appeal. Any compensation shall be calculated and paid in United States Dollars.
- (vi) The Convention on the Recognition and Enforcement of Foreign Arbitral Awards (also known as the "New York Convention") shall apply to this License Agreement and to any arbitral award or order resulting from any arbitration conducted hereunder. Judgment upon the award rendered by the arbitrator may be entered in any court of record of competent jurisdiction in any country, or application may be made to such court for judicial acceptance of the award and an order of enforcement, as the law of such jurisdiction may require or allow. The parties agree that the award of the arbitral tribunal shall be the sole and exclusive remedy among them regarding any and all claims and counterclaims presented to the tribunal. The parties further agree that this arbitration clause is an explicit waiver of any immunity or defense that may apply against the enforcement and execution of any arbitral award or any judgment thereon.
- (vii) The substantially prevailing party in an arbitration proceeding shall be entitled, in addition to such other relief as may be granted, to recover its attorneys' fees and costs, and the other party shall pay all costs of the arbitration. The arbitrator shall determine which of the parties has substantially prevailed based upon an assessment of which party's major arguments or positions

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taken in the proceedings could fairly be said to have prevailed over the other party's major arguments or positions on major disputed issues.

**11.7 Attorneys fees**

If the services of an attorney are required by any party to secure the performance of this License Agreement or otherwise upon the breach or default of another party to this License Agreement, or if any judicial remedy or arbitration is necessary to enforce or interpret any provision of this License Agreement or the rights and duties of any person in relation thereto, the prevailing party shall be entitled to reasonable attorneys' fees, costs and other expenses, in addition to any other relief to which such party may be entitled. Any award of damages following judicial remedy or arbitration as a result of the breach of this License Agreement or any of its provisions shall include an award of prejudgment interest from the date of the breach at the maximum amount of interest allowed by law.

**11.8 Assignment; transfer**

This License Agreement and the rights and obligations hereunder are not transferable or assignable without the prior written consent of the parties hereto, except that a person or entity who acquires all or substantially all of the assets or business of STI, whether by sale, merger or otherwise will have the right to assume all the rights and obligations of STI hereunder.

**11.9 Notices**

All notices will be in writing and sent by express courier (with written acknowledgment of receipt), to the following addresses, or such other address as either party may provide under this Section 11.9:

To BSTC:

Jilin Province  
People's Republic of China

Attention: \_\_\_\_\_

To STI:

Superconductor Technologies Inc. (STI)  
460 Ward Drive  
Santa Barbara, CA 93111|  
USA

Attention: Chief Executive Officer

**11.10 Integration; severability**

This License Agreement and all schedules, exhibits and attachments hereto constitute the entire agreement between the parties concerning the subject matter hereof. This License Agreement replaces and supersedes any prior verbal or written understandings, communications, or representations between the parties with respect to its subject matter. If any provision of this License Agreement will be held to be illegal or unenforceable, that provision will be limited or eliminated to the minimum extent necessary so that this License Agreement will otherwise remain in full force and effect and enforceable.

**11.11 Construction; headings**

Unless the context otherwise requires, the term including means "including but not limited to." The section headings herein are provided for ease of reference only and will have no legal effect. This Agreement has been negotiated by the parties, which have had reasonable access to legal counsel. This Agreement will be fairly interpreted in accordance with its terms, without any construction in favor of or against either party as a result of having drafted any particular provision.

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11.12 Amendments; waivers; counterparts

This License Agreement may be amended or modified only with the prior written consent of both parties. The failure by a party to exercise any rights hereunder will not operate as a waiver of such party's right or any other right in the future. This License Agreement may be executed in counterparts, each of which will be deemed an original.

**In witness whereof**, each of the parties has caused this License Agreement to be executed as of the date first written above by its duly authorized officer.

**Superconductor Investments (Mauritius)  
LTD**, a Delaware corporation

**BAOLI Superconductor Technology Co,  
Ltd**, a technologically-advanced contractual joint  
venture within the territory of the People's  
Republic of China

By: \_\_\_\_\_  
Name:  
Title:

By: \_\_\_\_\_  
Name:  
Title:

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**Schedule A– Definitions**

“ **BaoLi Communications** ” means **BAOLI Superconductor Technology Co, Ltd .**, a Chinese enterprise.

“ **Confidential Information** ” means all oral, written or recorded information about or related to the party (or any of its subsidiaries or other affiliates) or its or their technology, assets, liabilities, or business, which is furnished by its officers, directors, employees, agents or controlling persons, whether furnished before or after the date hereof, and regardless of the manner in which it is furnished, together with any summaries, extracts, analyses, compilations, studies or other documents or records prepared by the receiving party which contain, reflect or are generated from such information, regardless of whether explicitly identified as confidential. Confidential Information also includes the Proprietary Information and the Technology. For purpose of clarification, the Licensed Trademarks are not Confidential Information.

“ **Documentation** ” means any documentation or materials including reference, user, installation, systems administrator and technical guides relating to the use of the Technology.

“ **Effective Date** ” means the date ten days after the completion of the contribution to the capitalization of BSTC of BaoLi Communications as contemplated by the Joint Venture Contract between BaoLi Communications and STI dated December 8, 2007.

“ **BSTC Technology** ” means inventions or proprietary information that BSTC accomplishes or creates or to which BSTC acquires rights, other than the Technology.

“ **BSTC** ” means Huichun BaoLi Superconductor Technology Co Ltd, a technologically-advanced contractual joint venture in the People’s Republic of China.

“ **Junior Marks** ” is defined in Section 5.2.

“ **Licensed Trademarks** ” means the marks identified on Schedule D—Description of Licensed Trademarks.

“ **Minimum Royalty** ” means (x) zero in each calendar quarter through December 31, 2009 and (y) \$250,000 per quarter in each calendar quarter thereafter.

“ **Product** ” means STI’s proprietary, cryogenic front-end receiver product to improve the performance of base stations in wireless telecommunication networks, more fully described as follows:

The Product is comprised of (i) a fixed frequency filter that passes the signals received from cell phone handsets and rejects other frequencies and (ii) an amplifier that increases the level of the signals that pass through the filter and adds very little noise in the process.

The filter is made using high temperature superconductor material, and because of the properties of this material, the filter can select frequencies to pass that are only slightly different than the frequencies that are rejected. This selectivity allows for example 849MHz to pass the filter, but 851MHz to be rejected, so that less than one millionth of the power leaks through the filter at that frequency.

The amplifier is a cryogenically-cooled, low-noise radio-frequency amplifier. All amplifiers add some electronic noise to the signal that is amplified, but because the Product’s amplifier is cooled to -320F, the electronic noise that it adds to the desired signal is minimized.

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The Product's use is limited to serving cellular base stations. Typically cellular base stations use six separate antennas to receive the signals for cell phones, so each unit of the Product has six filters and six amplifiers.

The filters and amplifiers are mounted in a small enclosure (called a micro-enclosure) which is then placed inside a larger enclosure (called a dewar). The dewar is then evacuated to provide thermal isolation between the cryo-cooled micro-enclosure and the ambient environment. A cooler is then attached to the dewar to achieve the low temperatures necessary for the high temperature superconductor to work. A control board is added to monitor and control the functions of the unit.

The Product will have each of two specific forms:

- 1) For use in the 850MHz CDMA cellular network, the only variation in the Product from that heretofore implemented in the United States is an optimization of the filter (China uses only a sub-set of the frequencies used by the United States so an optimum design would narrow the filter used in STI's SuperLink product), and a minor modification of the power supply.
- 2) For use in the TD-SCDMA network that is planned to operate in the 2,000MHz band, the only variation in the Product from that heretofore implemented in the United States is a modification to operate at 2,000MHz.

**“ Proprietary Information ”** means all information of STI that is not generally known to the public, whether of a technical, business or other nature (including trade secrets, know-how and information relating to the technology, customers, business plans, marketing activities, finances and other business affairs of STI), that is disclosed by STI to BSTC in written, oral, electronic and/or other form or that is otherwise learned by BSTC in the course of its discussions or dealings with, or its physical or electronic access to the premises of, STI, and that has been identified as being proprietary and/or confidential or that by the nature of the circumstances surrounding the disclosure or receipt should reasonably be construed as proprietary or confidential. Proprietary Information also includes (a) all information concerning the existence and progress of the parties' dealings and the identity of STI's vendors and strategic partners and (b) the existence of, and the data generated by, field trials involving STI's products.

**“ Qualified Uses ”** of the Product means use by commercial and civilian telecommunications industry customers and shall expressly not include military use of any type or nature, whether direct or indirect.

**“ Revenues ”** means (a) gross revenues of BSTC or any successor or assign received or earned from sales of the Product either (i) using any Technology or (ii) associated with any Licensed Trademarks less (b) sales commissions paid to any unaffiliated third party and less (c) discounts and allowances to customers on such revenues and less (d) related shipping and taxes on revenues, but excluding (e) revenues and sales commissions on (i) the first 500 units of Product built during the initial development period from the kits provided by STI as contemplated herein and (ii) any sales from BSTC to STI or its designees.

**“ Royalty Statement ”** means a statement in English setting forth the Revenues during such quarterly period and a calculation of royalty due for the period.

**“ Technology ”** means (a) the Proprietary Information pertinent to the technology described on Schedule B—Description of Proprietary Information included in the Technology included in the Technology, together with the Documentation, delivered by STI to BSTC (b) corrections, updates, upgrades, enhancements, releases, fixes, new versions or other improvements of, modifications to, and derivative works of, such technology, Proprietary Information and Documentation developed

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by BSTC, and (c) the inventions object of the patents issued in China and patent filings made in China that are identified on Schedule C— Patents and Patent Applications, but only to the extent of their embodiment in the Product and solely for the purpose of manufacture and sale of the Product as permitted by this License Agreement. The Technology does not include any technology pertinent to certain aspects of the manufacturing process retained by STI based on factors including economics, feasibility and regulatory climate. The Technology does not include any technology the licensing or transfer of which is prohibited by any United States laws, regulations or governmental policies. If any technology otherwise licensed hereunder is excluded by reason of such laws, regulations or policies and not addressed through STI's retention of aspects of the manufacturing process, STI will use reasonable efforts to obtain any required United States approval to include it in the Technology.

“ **Territory** ” means The People’s Republic of China, including its Special Administrative Regions of Hong Kong and Macau, but excluding Taiwan.

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Schedule A-3

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**Schedule B– Description of Proprietary Information included in the Technology**

A. Proprietary Information pertinent to the manufacture of the Product includes information relative to the following:

**1. Facility/factory layout**

- (a) locations and specifications for areas such as material receiving, inspection, material storage, assembly, test and shipping
- (b) facility specifications such as electrical power requirements, liquid nitrogen plumbing, chilled water flow rates and clean room class specifications
- (c) process flow descriptions using commercially available methodology for production planning such as Value Stream Mapping and Just In Time methods

**2. Purchasing and procurement for precision mechanical and electronic parts**

- (a) disclosure of known vendors to produce parts and equipment, such as electrical RF connectors, RF switches, vacuum test equipment, circuit boards, hermetic seals, and precision machining

**3. Final assembly and test**

- (a) final assembly and testing of RF filter assemblies using commercially available electrical test equipment
- (b) routinization of assembly steps so as not to require special methods or techniques such as screw drivers, torque wrenches, etc.
- (c) test equipment including noise figure meter, S-Parameter network analyzer, digital power meters, personal computers, and Agilent VEE or Lab View and Microsoft SQL software
- (d) Electrical testing including RF filter performance, system operating temperatures, and electrical power consumption at several different temperature conditions found in a typical indoor controlled environment

**4. Cooler assembly**

- (a) assembly of an enclosed cooler assembly using ultrasonic cleaning equipment, sand blasting, commercially available vacuum bake oven and epoxy curing ovens, TIG welding equipment, pressure testing, commercial vacuum leak tester, custom test equipment using commercially available components, temperature monitor, network analyzer (mechanical frequency tuning), and Lab View and Microsoft SQL software

**5. Micro Enclosure**

- (a) assembly of a mechanical/electrical assembly using ultrasonic cleaning equipment, mechanical hardware, Miyachi wire soldering equipment, Kulicke & Saffa (K&S) gold wire ball bonder, and spot welding
- (b) further elements of assembly including RF testing using S-Parameter network analyzer, digital power meter, personal computer, and Lab View and Microsoft SQL software

**6. Dewar**

- (a) assembly of a mechanical vacuum housing with ultrasonic cleaning, LN2 handling, mechanical hardware, TIG welding, and commercially available vacuum leak tester.
- (b) evacuating during assembly an enclosed housing with custom automated vacuum equipment which consists of commercial available ON-BOARD cryogenic vacuum pump and a Direct Logic 205 controller system
- (c) RF testing using noise figure meter, S-Parameter network analyzer, digital power meter, personal computers, and Lab View and Microsoft SQL software

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B. Proprietary Information pertinent to the cryogenic cooling technology to cool the filters and amplifiers in the Product includes information relative to the following:

There are two areas of application of the cryogenic cooling technology in the Product: the cooler and the Dewar.

The cooler works by moving a piston back and forth with an electro magnet: the piston pushes helium gas back and forth driving a displacer. The displacer expands cold gas in one spot and compresses hot gas in another spot, pumping heat away from the cryogenic end. Proprietary technology is used to ensure that there is no friction as the piston and displacer move back and forth about sixty times per second. The cryogenic end of the cooler cools the filter and amplifier to a temperature of -320F, while the heat reject end of the cooler stays just a few degrees above ambient. Proprietary technology is employed throughout the cooler to enable it to work correctly over an extended lifetime with a low failure rate.

The Dewar works by reducing the heat flow. The Dewar reduces all the three sources of heat flow: convection, conduction, and radiation. Convection is eliminated by maintaining a vacuum between cold and ambient parts. The high vacuum is maintained for years using proprietary technology. Conduction is reduced using proprietary technology to connect the cold and ambient parts together. Finally radiation is reduced with the careful choice of features and surfaces, using proprietary technology.

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Schedule B-2

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## Schedule C– Patents and Patent Applications

Issued Patents in China

<u>Patent No</u>	<u>Title</u>	<u>Inventors</u>	<u>Docket</u>	<u>Filing Date</u>	<u>Serial No</u>	<u>Issue Date</u>	<u>Description</u>
ZL01808625.X	Stirling Cycle Cryocooler with Optimized Cold End Design	Hanes	OMM 0164	16-Apr-01	01808625.X	16-Feb-05	STI's current cooler design

Pending Patent Applications in China

<u>Serial No</u>	<u>Title</u>	<u>Docket</u>	<u>Inventors</u>	<u>Filing Date</u>	<u>Status</u>	<u>Description</u>
3804170.7	Method and Apparatus for Minimizing Intermodulation With an Asymmetric Resonator	MNG 0056	Ye	19-Feb-03	published	
3805589.9	Resonator and Coupling Method and Apparatus for a Microstrip Filter	MNG 0057	Ye	10-Mar-03	published	
200480036124.X	Cryocooler Cold-end Assembly Apparatus and Method	MNG 0063	O'Baid, Hanes	23-Jun-06	published	deep drawn housing
200480035702.8	Growth of In-situ Thin Films by Reactive Evaporation	OMM 0349	Moeckly, Ruby	08-May-06	published	RCE
20058004737	RF-Properties-Optimized Compositions of (RE) Ba <sub>2</sub> Cu <sub>3</sub> O <sub>7-d</sub> Thin Film Superconductors	OMM 0365	Moeckly, Willemsen, Peng, Gilantsev	23-Jun-07	pending	substitution
PCT/US2005/042867	Systems and Methods for Tuning Filters	WAK 0004	Tsuzuki, Hernandez, Willemsen	30-Jul-07	pending	our "omnibus" tuning application
						Confidential

**Schedule D– Description of Licensed Trademarks**

<u>Trademark</u>	<u>Serial No.</u>	<u>Filing Date</u>	<u>Registration Date</u>	<u>Country</u>
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**Schedule E- Training Plan**

Confidential





**SUBSIDIARIES OF SUPERCONDUCTOR TECHNOLOGIES INC.**

Conductus, Inc., a Delaware corporation

STI Investments Limited, a British Virgin Islands company

Superconductor Investments (Mauritius) Limited, a Mauritius company



**CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

We hereby consent to the incorporation by reference in the Registration Statements on Form S-8 (File Nos. 333-50137, 333-90293, 333-56606, 333-89184, 333-102147, 333-105193, 333-106594 and 333-126121) and the Registration Statements on Form S-3 (File Nos. 333-65035, 333-48540, 333-71958, 333-84914, 333-99033, 333-102186, 333-106589, 333-111818, 333-117107 and 333-148115) of Superconductor Technologies Inc. of our report dated March 27, 2008 relating to the consolidated financial statements and financial statement schedule, which appears in this Form 10-K.

/s/ STONEFIELD JOSEPHSON, INC.

Los Angeles, California  
March 27, 2008



**CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

We hereby consent to the incorporation by reference in the Registration Statements on Form S-8 (File Nos. 333-50137, 333-90293, 333-56606, 333-89184, 333-102147, 333-105193, 333-106594 and 333-126121) and the Registration Statements on Form S-3 (File Nos. 333-65035, 333-48540, 333-71958, 333-84914, 333-99033, 333-102186, 333-106589, 333-111818, 333-117107 and 333-148115) of Superconductor Technologies Inc. of our report dated March 3, 2006 except for the reverse stock split discussed in note 2, as to which the date is March 13, 2006, relating to the consolidated financial statements and financial statement schedule, which appears in this Form 10-K.

/s/ PRICEWATERHOUSECOOPERS LLP

Los Angeles, California  
March 27, 2008



**Statement Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 by  
Principal Executive Officer and Principal Financial Officer  
Regarding Facts and Circumstances Relating to Exchange Act Filings**

I, Jeffrey A. Quiram, certify that:

1. I have reviewed this annual report on Form 10-K of Superconductor Technologies Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation;
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 27, 2008

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





**Statement Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 by  
Principal Executive Officer and Principal Financial Officer  
Regarding Facts and Circumstances Relating to Exchange Act Filings**

I, William J. Buchanan, certify that:

1. I have reviewed this annual report on Form 10-K of Superconductor Technologies Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation;
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 27, 2008

/s/ William J. Buchanan  
William J. Buchanan  
Controller, Principal Financial Officer,  
Principal Accounting Officer



**Statement Pursuant to Section 906 the Sarbanes-Oxley Act of 2002**  
**By**  
**Principal Executive Officer and Principal Financial Officer**  
**Regarding Facts and Circumstances Relating to Exchange Act Filings**

Dated: March 27, 2008

I, Jeffrey A. Quiram, Chief Executive Officer of Superconductor Technologies Inc, herby certify that, to my knowledge, that:

1. the accompanying Annual Report on Form 10-K of Superconductor Technologies for the annual period ended December 31, 2007 (the "Report") fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities and Exchange Act of 1934, as amended; and
2. the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of Superconductor Technologies Inc.

IN WITNESS WHEREOF, the undersigned has executed this Statement as of the date first written above.

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



**Statement Pursuant to Section 906 the Sarbanes-Oxley Act of 2002**  
**By**  
**Principal Executive Officer and Principal Financial Officer**  
**Regarding Facts and Circumstances Relating to Exchange Act Filings**

Dated: March 27, 2008

I, William J. Buchanan, Controller of Superconductor Technologies Inc, hereby certify that, to my knowledge, that:

1. the accompanying Annual Report on Form 10-K of Superconductor Technologies for the annual period ended December 31, 2007 (the "Report") fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities and Exchange Act of 1934, as amended; and
2. the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of Superconductor Technologies Inc.

/s/ William J. Buchanan  
William J. Buchanan  
Controller, Principal Financial Officer,  
Principal Accounting Officer