

---

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549**

**FORM 10-Q**

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the quarterly period ended June 30, 2015

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number: 000-30939

---

**ACTIVE POWER, INC.**

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

74-2961657

(I.R.S. Employer Identification No.)

2128 W. Braker Lane, BK 12, Austin, Texas

(Address of principal executive offices)

78758

(Zip Code)

(512) 836-6464

(Registrant's telephone number, including area code)

---

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company)

Smaller reporting company

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

The number of shares of common stock, par value of \$0.001 per share, outstanding at July 23, 2015 was 23,107,292.

---

---

ACTIVE POWER, INC.  
INDEX

|  |                    |
|--|--------------------|
| <a href="#">PART I – FINANCIAL INFORMATION</a>   | <a href="#">3</a>  |
| <a href="#">Item 1. Condensed Consolidated Financial Statements.</a>   | <a href="#">3</a>  |
| <a href="#">Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations.</a> | <a href="#">14</a> |
| <a href="#">Item 3. Quantitative and Qualitative Disclosures about Market Risk.</a>                            | <a href="#">22</a> |
| <a href="#">Item 4. Controls and Procedures.</a>   | <a href="#">22</a> |
| <a href="#">PART II – OTHER INFORMATION</a>  | <a href="#">22</a> |
| <a href="#">Item 1. Legal Proceedings.</a>   | <a href="#">22</a> |
| <a href="#">Item 1A. Risk Factors.</a>   | <a href="#">22</a> |
| <a href="#">Item 6. Exhibits.</a>  | <a href="#">22</a> |

## PART I – FINANCIAL INFORMATION

## Item 1. Condensed Consolidated Financial Statements.

**Active Power, Inc.**  
**Condensed Consolidated Balance Sheets**  
**(in thousands, except par value)**

|   | <u>June 30, 2015</u> | <u>December 31, 2014</u> |
|---|----------------------|--------------------------|
|   | (unaudited)          |                          |
| <b>ASSETS</b>   |                      |                          |
| Current assets:   |                      |                          |
| Cash and cash equivalents   | \$ 10,566            | \$ 14,824                |
| Restricted cash   | 539                  | 40                       |
| Accounts receivable, net of allowance for doubtful accounts of \$262 and \$212 at June 30, 2015 and December 31, 2014, respectively   | 16,016               | 11,222                   |
| Inventories, net  | 7,423                | 6,845                    |
| Prepaid expenses and other  | 605                  | 800                      |
| Total current assets  | 35,149               | 33,731                   |
| Property and equipment, net   | 1,923                | 2,076                    |
| Deposits and other  | 283                  | 291                      |
| Total assets  | <u>\$ 37,355</u>     | <u>\$ 36,098</u>         |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>   |                      |                          |
| Current liabilities:  |                      |                          |
| Accounts payable  | \$ 5,487             | \$ 4,044                 |
| Accrued expenses  | 4,532                | 4,134                    |
| Deferred revenue  | 3,550                | 2,771                    |
| Revolving line of credit  | 5,535                | 5,535                    |
| Total current liabilities   | 19,104               | 16,484                   |
| Long-term liabilities   | 670                  | 821                      |
| Commitments and contingencies   |                      |                          |
| Stockholders' equity:   |                      |                          |
| Preferred stock - \$0.001 par value; 2,000 shares authorized  | —                    | —                        |
| Common stock - \$0.001 par value; 40,000 shares authorized; 23,167 and 23,162 shares issued and 23,107 and 23,094 shares outstanding at June 30, 2015 and December 31, 2014, respectively | 23                   | 23                       |
| Treasury stock  | (237)                | (231)                    |
| Additional paid-in capital  | 303,341              | 302,667                  |
| Accumulated deficit   | (285,812)            | (283,995)                |
| Other accumulated comprehensive income  | 266                  | 329                      |
| Total stockholders' equity  | 17,581               | 18,793                   |
| Total liabilities and stockholders' equity  | <u>\$ 37,355</u>     | <u>\$ 36,098</u>         |

*See accompanying notes.*

**Active Power, Inc.**  
**Condensed Consolidated Statement of Operations and Comprehensive Loss**  
**(in thousands, except per share amounts; unaudited)**

|   | Three Months Ended June 30, |                   | Six Months Ended June 30, |                   |
|---|-----------------------------|-------------------|---------------------------|-------------------|
|   | 2015                        | 2014              | 2015                      | 2014              |
| Revenues:   |                             |                   |                           |                   |
| Product revenue   | \$ 12,905                   | \$ 7,484          | \$ 22,453                 | \$ 14,941         |
| Service and other revenue   | 3,950                       | 2,670             | 7,531                     | 6,151             |
| Total revenue   | <u>16,855</u>               | <u>10,154</u>     | <u>29,984</u>             | <u>21,092</u>     |
| Cost of goods sold:   |                             |                   |                           |                   |
| Cost of product revenue   | 9,089                       | 6,352             | 16,060                    | 12,257            |
| Cost of service and other revenue   | 2,268                       | 1,887             | 4,119                     | 3,992             |
| Total cost of goods sold  | <u>11,357</u>               | <u>8,239</u>      | <u>20,179</u>             | <u>16,249</u>     |
| Gross profit  | 5,498                       | 1,915             | 9,805                     | 4,843             |
| Operating expenses:   |                             |                   |                           |                   |
| Research and development  | 1,430                       | 1,600             | 2,946                     | 3,680             |
| Selling and marketing   | 2,715                       | 3,152             | 5,421                     | 6,040             |
| General and administrative  | 1,524                       | 1,469             | 3,082                     | 3,075             |
| Total operating expenses  | <u>5,669</u>                | <u>6,221</u>      | <u>11,449</u>             | <u>12,795</u>     |
| Loss from operations  | (171)                       | (4,306)           | (1,644)                   | (7,952)           |
| Interest expense, net   | (78)                        | (106)             | (157)                     | (207)             |
| Other income (expense), net   | (9)                         | (1)               | (16)                      | (128)             |
| Net loss  | <u>\$ (258)</u>             | <u>\$ (4,413)</u> | <u>\$ (1,817)</u>         | <u>\$ (8,287)</u> |
| Net loss per share, basic and diluted                                     | \$ (0.01)                   | \$ (0.19)         | \$ (0.08)                 | \$ (0.38)         |
| Shares used in computing net loss per share, basic and diluted            | 23,133                      | 23,114            | 23,131                    | 21,851            |
| Comprehensive loss:   |                             |                   |                           |                   |
| Net loss  | \$ (258)                    | \$ (4,413)        | \$ (1,817)                | \$ (8,287)        |
| Translation gain (loss) on subsidiaries denominated in foreign currencies | 97                          | 20                | (63)                      | 18                |
| Comprehensive loss  | <u>\$ (161)</u>             | <u>\$ (4,393)</u> | <u>\$ (1,880)</u>         | <u>\$ (8,269)</u> |

*See accompanying notes.*

**Active Power, Inc.**  
**Condensed Consolidated Statement of Stockholders' Equity**  
**(in thousands; unaudited)**

|  | <u>Common Stock</u>             |                      | <u>Treasury Stock</u>           |                 | <u>Additional<br/>Paid-In<br/>Capital</u> | <u>Accumulated<br/>Deficit</u> | <u>Other Accumulated<br/>Comprehensive<br/>Income<br/>(Loss)</u> | <u>Total<br/>Stockholders'<br/>Equity</u> |
|--|---------------------------------|----------------------|---------------------------------|-----------------|---|--------------------------------|--|---|
|  | <u>Number<br/>of<br/>Shares</u> | <u>Par<br/>Value</u> | <u>Number<br/>of<br/>Shares</u> | <u>At Cost</u>  |   |                                |  |   |
| Balance at December 31, 2014                 | 23,162                          | \$ 23                | 56                              | \$ (231)        | \$ 302,667                                | \$ (283,995)                   | \$ 329   | \$ 18,793                                 |
| Release of Restricted Stock                  | 5                               | —                    | —                               | —               | —   | —                              | —  | —   |
| Shares held in treasury                      | —                               | —                    | 4                               | (6)             | —   | —                              | —  | (6)                                       |
| Net translation loss on foreign subsidiaries | —                               | —                    | —                               | —               | —   | —                              | (63)   | (63)                                      |
| Stock-based compensation                     | —                               | —                    | —                               | —               | 674                                       | —                              | —  | 674                                       |
| Net loss                                     | —                               | —                    | —                               | —               | —   | (1,817)                        | —  | (1,817)                                   |
| Balance at June 30, 2015                     | <u>23,167</u>                   | <u>\$ 23</u>         | <u>60</u>                       | <u>\$ (237)</u> | <u>\$ 303,341</u>                         | <u>\$ (285,812)</u>            | <u>\$ 266</u>  | <u>\$ 17,581</u>                          |

*See accompanying notes.*

**Active Power, Inc.**  
**Condensed Consolidated Statement of Cash Flows**  
**(in thousands; unaudited)**

|   | <b>Six Months Ended June 30,</b> |                  |
|---|----------------------------------|------------------|
|   | <b>2015</b>                      | <b>2014</b>      |
| <b>Operating activities</b>   |                                  |                  |
| Net loss  | \$ (1,817)                       | \$ (8,287)       |
| Adjustments to reconcile net loss to cash used in operating activities: |                                  |                  |
| Depreciation expense  | 524                              | 620              |
| Net change to allowance for doubtful accounts                           | 50                               | (93)             |
| Loss (gain) on disposal of fixed assets                                 | 1                                | (19)             |
| Stock-based compensation  | 674                              | 552              |
| Changes in operating assets and liabilities:                            |                                  |                  |
| Restricted cash   | (499)                            | 513              |
| Accounts receivable   | (4,844)                          | 935              |
| Inventories   | (578)                            | 489              |
| Prepaid expenses and other assets                                       | 203                              | 209              |
| Accounts payable  | 1,443                            | (105)            |
| Accrued expenses  | 398                              | (1,321)          |
| Deferred revenue  | 779                              | 95               |
| Long term liabilities   | (151)                            | (44)             |
| Net cash used in operating activities                                   | (3,817)                          | (6,456)          |
| <b>Investing activities</b>   |                                  |                  |
| Purchases of property and equipment                                     | (392)                            | (189)            |
| Proceeds from sale of fixed assets                                      | —                                | 19               |
| Net cash used in investing activities                                   | (392)                            | (170)            |
| <b>Financing activities</b>   |                                  |                  |
| Proceeds from public offering of common stock, net of issuance costs    | —                                | 10,438           |
| Proceeds from employee stock option exercises                           | —                                | 108              |
| Taxes paid related to net share settlement of equity awards             | (6)                              | (11)             |
| Net cash (used in) provided by financing activities                     | (6)                              | 10,535           |
| Effects of exchange rates on cash                                       | (43)                             | 18               |
| Change in cash and cash equivalents                                     | (4,258)                          | 3,927            |
| Cash and cash equivalents, beginning of period                          | 14,824                           | 12,261           |
| Cash and cash equivalents, end of period                                | <u>\$ 10,566</u>                 | <u>\$ 16,188</u> |

*See accompanying notes.*

**Active Power, Inc.**  
**Notes to Condensed Consolidated Financial Statements**  
**June 30, 2015**  
(unaudited)

1. Basis of Presentation

Active Power, Inc. and its subsidiaries (collectively, “we”, “us”, “Active Power” or “Company”) design, manufacture, sell, and service flywheel-based uninterruptible power supply (“UPS”) products that use kinetic energy to provide short-term power as a cleaner alternative to conventional electrochemical battery-based energy storage. We also design, manufacture, sell, and service modular infrastructure solutions (“MIS”) that integrate critical power components into a pre-packaged, purpose built enclosure that may include our UPS products as a component. Our products and solutions are based on our patented flywheel and power electronics technology and are designed to ensure continuity for data centers and other mission critical operations in the event of power disturbances.

Our products and solutions are designed to deliver continuous conditioned power during power disturbances such as voltage sags and surges, and to provide ride-through power in the event of a brief utility failure, supporting operations until utility power is restored or a longer term alternative power source, such as a diesel generator, is started. We sell our products globally through our direct sales force, manufacturer’s representatives, distributors, original equipment manufacturers (“OEM”), and IT partners in the Americas, in Europe, Middle East, and Africa (“EMEA”), and in the Asia Pacific region (“APAC”).

We also offer services, including hardware and software maintenance, on all Active Power products, and other professional services such as assessment and implementation, for our customers’ infrastructure projects.

We were founded as a Texas Corporation in 1992 and reincorporated in Delaware in 2000. Our headquarters are in Austin, Texas, with international offices in the United Kingdom, Germany, and China.

The accompanying condensed consolidated balance sheet as of December 31, 2014, which has been derived from our audited financial statements, and the unaudited condensed consolidated financial statements as of June 30, 2015 have been prepared in accordance with accounting principles generally accepted in the United States of America (“US GAAP”) for interim financial statements and pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”) for interim reporting, and include the accounts of the Company and its consolidated subsidiaries. All intercompany transactions and balances have been eliminated upon consolidation. Certain information and note disclosures normally included in annual financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to those rules and regulations, although we believe the disclosures made are adequate to make the information not misleading. In the opinion of management, the accompanying unaudited condensed consolidated financial statements contain all adjustments (consisting only of normal recurring items) necessary to present fairly the consolidated financial position of the Company and its consolidated results of operations and cash flows. These interim financial statements should be read in conjunction with the financial statements and accompanying notes included in our Annual Report on Form 10-K for the year ended December 31, 2014.

2. Significant Accounting Policies and Supplemental Balance Sheet Information

For a complete description of our principal accounting policies see Note 1. “Summary of Significant Accounting Policies,” to our Consolidated Financial Statements and Notes thereto included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2014. Shown below are certain of our principal accounting policies.

**Restricted Cash**

Our restricted cash balance of \$0.5 million as of June 30, 2015 consists of a \$6,000 deposit guarantee for our building lease in Germany, which renews every six months through the term of the lease agreement, a \$31,000 performance guarantee to a customer that was secured with a letter of credit, which expires in June 2017, and a \$0.5 million performance guarantee to a customer that was secured with a letter of credit, which expires in July 2015. As of December 31, 2014, our restricted cash balance was \$40,000, which consisted primarily of secured performance and deposit guarantees.

**Receivables**

Accounts receivable consist of the following (in thousands):

|                                       | <b>June 30, 2015</b> | <b>December 31, 2014</b> |
|---------------------------------------|----------------------|--------------------------|
| Trade receivables                     | \$ 16,278            | \$ 11,434                |
| Less: Allowance for doubtful accounts | (262)                | (212)                    |
|                                       | <u>\$ 16,016</u>     | <u>\$ 11,222</u>         |

We estimate an allowance for doubtful accounts based on factors related to the credit risk of each customer. Historically, our credit losses have been minimal, primarily because the majority of our revenues were generated from large customers, such as Caterpillar, Inc. ("Caterpillar") and Hewlett Packard Corporation ("HP"). We perform credit evaluations of new customers and when necessary we require deposits, prepayments or use of bank instruments such as trade letters of credit to mitigate our credit risk. We write off uncollectable trade receivables, and record any recoveries of previous write offs against the allowance. Our standard payment terms are net 30 days; however we have agreements with certain larger customers and certain distributors that allow for more extended terms at or above net 60 days.

**Inventories, net**

Inventories, net are stated at the lower of cost or market, using the first-in-first-out method, and consisted of the following (in thousands, net of allowance):

|                 | <b>June 30, 2015</b> | <b>December 31, 2014</b> |
|-----------------|----------------------|--------------------------|
| Raw materials   | \$ 5,044             | \$ 5,440                 |
| Work in process | 2,012                | 473                      |
| Finished goods  | 367                  | 932                      |
|                 | <u>\$ 7,423</u>      | <u>\$ 6,845</u>          |

**Accrued Expenses**

Accrued expenses consist of the following (in thousands):

|                                      | <b>June 30, 2015</b> | <b>December 31, 2014</b> |
|--------------------------------------|----------------------|--------------------------|
| Compensation, severance and benefits | \$ 2,213             | \$ 1,296                 |
| Warranty liability                   | 570                  | 475                      |
| Taxes, other than income             | 581                  | 1,080                    |
| Professional fees                    | 404                  | 463                      |
| Other                                | 764                  | 820                      |
|                                      | <u>\$ 4,532</u>      | <u>\$ 4,134</u>          |

**Warranty Liability**

Generally, the warranty period for our products is 12 months from the date of commissioning or 18 months from the date of shipment from Active Power, whichever period is shorter. Occasionally, we provide longer warranty periods to certain customers. The warranty period for products sold to our primary OEM customer, Caterpillar, is 12 months from the date of shipment to the end-user, or up to 36 months from shipment from Active Power, whichever period is shorter. This is dependent upon Caterpillar complying with our storage requirements for our products in order to preserve this warranty period beyond the standard 18-month limit. We provide for the estimated cost of product warranties at the time revenue is recognized and this accrual is included in accrued expenses and long-term liabilities on the accompanying consolidated balance sheet.



Changes in our warranty liability are as follows (in thousands):

|  |    |       |
|--|----|-------|
| Balance at December 31, 2014                         | \$ | 527   |
| Warranty expense                                     |    | 449   |
| Payments   |    | (353) |
| Balance at June 30, 2015                             | \$ | 623   |
| Warranty liability included in Accrued expenses      | \$ | 570   |
| Warranty liability included in Long-term liabilities |    | 53    |
| Balance at June 30, 2015                             | \$ | 623   |

### Revenue Recognition

We recognize revenue when four criteria are met: (i) persuasive evidence that an arrangement exists; (ii) delivery has occurred or services have been rendered; (iii) the sales price is fixed or determinable; and (iv) collectability is reasonably assured. In general, revenue is recognized when revenue-generating transactions fall into one of the following categories of revenue recognition:

- We recognize product revenue at the time of shipment for a significant portion of all products sold directly to customers and through distributors because title and risk of loss typically pass on delivery to the common carrier. Our customers and distributors do not have the right to return products. If title and risk of loss pass at some other point in time, we recognize such revenue for our customers when the product is delivered to the customer and title and risk of loss have passed.
- Unless performed under a maintenance contract, we recognize installation, service and maintenance revenue at the time the service is performed.
- We recognize revenue associated with maintenance agreements over the life of the contracts using the straight-line method, which approximates the expected timing in which applicable services are performed. Amounts collected in advance of revenue recognition are recorded as a current liability in the deferred revenue line of the consolidated balance sheet or as a long-term liability based on the time from the balance sheet date to the future date of revenue recognition.
- We recognize revenue on certain rental programs over the life of the rental agreements using the straight-line method. Amounts collected in advance of revenue recognition are recorded as a current or long-term liability based on the time from the balance sheet date to the future date of revenue recognition.

When collectability is not reasonably assured, we defer revenue and will recognize revenue as payments are received.

Multiple element arrangements (“MEAs”) are arrangements to sell products to customers that frequently include multiple deliverables. Our most significant MEAs include the sale of one or more of our CleanSource® UPS or CleanSource PowerHouse products, combined with one or more of the following products or services: design services, project management, commissioning and installation services, spare parts or consumables, and maintenance agreements. Delivery of the various products or performance of services within the arrangement may or may not coincide. Certain services related to design and consulting may occur prior to product delivery. Commissioning and installation typically take place within six months of product delivery, depending upon customer requirements. Maintenance agreements, consumables, and repair, maintenance or consulting services are generally delivered over a period of one to five years. In certain arrangements revenue recognized is limited to the amount invoiced or received that is not contingent on the delivery of future products and services.

[Index](#)

When arrangements include multiple elements, we allocate revenue to each element based on the relative selling price and recognize revenue when the elements have standalone value and the four criteria for revenue recognition have been met. We establish the selling price of each element based on Vendor Specific Objective Evidence (“VSOE”) if available, Third Party Evidence (“TPE”) if VSOE is not available, or best estimate of selling price (“BESP”) if neither VSOE nor TPE is available. We generally determine selling price based on amounts charged separately for the delivered and undelivered elements to similar customers in standalone sales of the specific elements. When arrangements include a maintenance agreement, we recognize revenue related to the maintenance agreement at the stated contractual price on a straight-line basis over the life of the agreement.

Any taxes imposed by governmental authorities on our revenue-producing transactions with customers are shown in our consolidated statements of operations on a net-basis; that is, excluded from our reported revenues.

**Recently issued accounting pronouncements not yet adopted**

In April 2015, the Financial Accounting Standards Board (the “FASB”) issued Accounting Standards Update (“ASU”) No. 2015-03, (“ASU 2015-03”), “*Interest - Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs*”. ASU 2015-03 requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. For public entities, ASU 2015-03 is effective for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. Early adoption is permitted for financial statements that have not been previously issued. ASU 2015-03 is to be applied on a retrospective basis and represents a change in accounting principle. We do not expect the adoption of this standard will have a material effect on our consolidated financial statements.

In August 2014, the FASB issued ASU No. 2014-15, “*Disclosure of Uncertainties About an Entity’s Ability to Continue as a Going Concern*”. ASU 2014-15 requires management to perform interim and annual assessments of an entity’s ability to continue as a going concern within one year of the date the financial statements are issued and provides guidance on determining when and how to disclose going concern uncertainties in the financial statements. Certain disclosures will be required if conditions give rise to substantial doubt about an entity’s ability to continue as a going concern. ASU 2014-15 applies to all entities and is effective for annual and interim reporting periods ending after December 15, 2016, with early adoption permitted. We do not expect the adoption of this standard will have a material effect on our financial statements.

In May 2014, the FASB issued ASU 2014-09, “*Revenue from Contracts with Customers*”, “*Topic 606*”. This ASU will supersede the revenue recognition requirements in Topic 605, Revenue Recognition, and most industry-specific guidance, and creates a Topic 606 Revenue from Contracts with Customers. The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In April 2015, the FASB issued for public comment a proposed ASU, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date*, which would defer the effective date of its new revenue recognition standard by one year. At the June 9, 2015 meeting, the FASB voted to approve this deferral. We will adopt this guidance January 1, 2018. We are evaluating the new guidelines to see if they will have a significant impact on our consolidated results of operation, financial condition or cash flows.

3. Net Loss Per Share

The following table sets forth the computation of basic and diluted net loss per share (in thousands, except per share data):

|  | Three Months Ended June 30, |            | Six Months Ended June 30, |            |
|--|-----------------------------|------------|---------------------------|------------|
|  | 2015                        | 2014       | 2015                      | 2014       |
| Net loss   | \$ (258)                    | \$ (4,413) | \$ (1,817)                | \$ (8,287) |
| Basic and dilutive:  |                             |            |                           |            |
| Weighted-average shares of common stock outstanding used in computing basic and diluted net loss per share | 23,133                      | 23,114     | 23,131                    | 21,851     |
| Basic and diluted net loss per share   | \$ (0.01)                   | \$ (0.19)  | \$ (0.08)                 | \$ (0.38)  |

The calculation of diluted loss per share excludes 3,177,928 and 2,388,398 shares of common stock issuable upon exercise of employee stock options for the six months ended June 30, 2015 and 2014, respectively, and non-vested shares of

common stock issuable upon exercise of 13,765 and 30,656 restricted stock units for the six months ended June 30, 2015 and 2014, respectively, because their inclusion would be anti-dilutive.

#### 4. Fair Value of Financial Instruments

Fair value is measured based on an exit price, representing the amount that would be received to sell an asset or paid to satisfy a liability in an orderly transaction between market participants. Fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. As a basis for considering such assumptions, a fair value hierarchy is established, which categorizes the inputs used in measuring fair value as follows:

Level 1—Quoted prices in active markets for identical assets or liabilities.

Level 2—Significant observable inputs other than quoted prices in Level 1, such as quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3—One or more significant inputs that are unobservable and supported by little or no market data.

Highest priority is given for Level 1 input and lower priority to Level 3 inputs. A financial instrument's level is based on the lowest level of any input that is significant to the fair value measurement. No changes were made to our methodology.

Our Level 1 assets consist of cash equivalents, which are primarily invested in money-market funds. These assets are classified as Level 1 because they are valued using quoted prices in active markets and other relevant information generated by market transactions involving identical assets and liabilities. The fair value was \$3.1 million as of June 30, 2015 and December 31, 2014.

For cash and cash equivalents, accounts receivable, accounts payable and our revolving line of credit, the carrying amount approximates fair value because of the relative short maturity of those instruments.

#### 5. Guarantees

In certain geographical regions, particularly Europe, we are sometimes required to issue performance guarantees to our customers as a condition of sale. These guarantees usually provide financial protection to our customers in the event that we fail to fulfill our delivery or warranty obligations. We secure these guarantees with standby letters of credit through our bank. At June 30, 2015, we had a \$6,000 deposit guarantee outstanding for our building lease in Germany which renews every six months through the term of the lease agreement, a \$31,000 performance guarantee to a customer that was secured with a letter of credit, which expires in June 2017, and a \$0.5 million performance guarantee to a customer that was secured with a letter of credit, which expires in July 2015. At December 31, 2014, our restricted cash balance was \$40,000 which consisted primarily of secured performance and deposit guarantees. Our restricted cash, as shown on the balance sheet, is related to these guarantees.

#### 6. Revolving Line of Credit

On July 28, 2014, we entered into a Third Amended and Restated Loan and Security Agreement (“Loan Agreement”) with Silicon Valley Bank (“SVB”). This amended three-year loan facility provides for a secured revolving line of credit in an aggregate amount of up to eighty percent (80%) of the facility amount of \$18.8 million, or \$15.0 million, and increased our inventory and purchase order availability from \$3.5 million to \$7.0 million, subject to certain borrowing bases. Purchase orders and eligible inventory are subject to a sublimit of \$4.0 million, and accounts receivable in the UK and Germany have a \$5.0 million sublimit. If we maintain our Liquidity Ratio of 2.50:1.00 for the immediately preceding Reconciliation Period, the sublimit will be uncapped. We are currently in compliance with all loan covenants under the Loan Agreement. Further, the Third Amendment extends the maturity date to August 5, 2017 and reduces the finance charge to a per annum rate equal to SVB's prime rate, subject to a minimum prime rate of 4.00%, plus (a) 0.50% for eligible accounts, inventory and purchase orders when we are Borrowing Base Eligible (as defined in the Loan Agreement), or (b) 1.20% for eligible accounts when we are not Borrowing Base Eligible.

The loans made to us under the Loan Agreement are secured by a lien on substantially all of our assets, including the assets of Active Power Solutions Limited, our wholly-owned United Kingdom subsidiary, and the assets of Active Power (Germany) GmbH, our indirect wholly-owned German subsidiary. The only direct or indirect subsidiaries of Active Power, Inc. that are not guarantors under the Loan Agreement are Active Power China (Beijing) Co. Ltd. and immaterial subsidiaries that are not operating companies. There are no restrictions on the ability of any of the subsidiary guarantors to transfer funds to Active Power, Inc. in the form of loans, advances or dividends, except as provided by applicable law.

The other key terms of the Loan Agreement remain unchanged, including customary affirmative covenants, a minimum liquidity ratio, the borrowing base eligibility (formerly called the “streamline ratio”), reporting requirements, and other terms and conditions. We are currently in compliance with all loan covenants under the loan facility. As of June 30, 2015, we had outstanding borrowings of \$5.5 million under this loan facility and, based on the borrowing base formula, the additional amount available to us was \$9.5 million at June 30, 2015. For further information regarding this loan facility, refer to our Annual Report on Form 10-K for the year ended December 31, 2014, and to our Current Report on Form 8-K filed on July 29, 2014.

## 7. Commitments and Contingencies

We may be involved, either as plaintiff or defendant, in a variety of ongoing claims, demands, suits, investigations, tax matters and proceedings that arise from time to time in the ordinary course of its business. We evaluated all potentially significant litigation, government investigations, claims or assessments in which we are involved and determined there were no contingent losses, either accrued or reasonably possible of loss that could materially affect its results of operations, financial condition, or cash flows.

We record an accrual with respect to a claim, suit, investigation or proceeding when it is reasonably probable that a liability has been incurred and the amount of the loss can be reasonably estimated. Any recorded liabilities, including any changes to such liabilities for the quarter ended June 30, 2015, were not material to the Consolidated Financial Statements.

The following is a summary of our more significant legal matters.

### **SEC Inquiry**

By letter dated September 30, 2013, the SEC Division of Enforcement notified us that it is conducting an investigation regarding us, including matters relating to our public statements regarding Digital China Information Services Company Limited (“Digital China”) and our distribution relationships in China. We have been and intend to continue cooperating fully with the SEC. As of the date of this filing, we believe we have provided all requested material to the SEC.

### **Settled Stockholder Litigation**

#### *Class action complaint*

On September 10, 2013, a purported class action complaint was filed in the United States District Court for the Western District of Texas against us and certain of our former executives. The case was captioned *Don Lee v. Active Power, Inc., et. al.* (Civil Action No. 1:13-cv-00797-SS). The complaint alleged that on February 19, 2013, we reported that we had begun working with an unnamed Chinese distributor partner, and that on April 30, 2013, we announced in press releases and conference calls that we had entered into a strategic distribution partnership with Digital China. However, on September 5, 2013, after the close of trading, we disclosed that our partnership was with Qiyuan Network System Limited, which is neither an affiliate nor a subsidiary of Digital China. The amended complaint asserted claims under Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, as amended, and Rule 10b-5 promulgated thereunder, and sought unspecified damages on behalf of all stockholders who purchased common stock between February 19 and September 5, 2013. On March 7, 2014, we filed a motion to dismiss the class action complaint. Our motion was denied by the Court on July 2, 2014. On August 11, 2014, we filed an answer to the class action complaint, and on September 2, 2014, the Court declined to certify its order of July 2, 2014 for an interlocutory appeal to the United States Court of Appeals for the Fifth Circuit.

On September 23, 2014, we reached an agreement in principle and entered into a memorandum of understanding to settle the class action complaint. The parties to the class action signed a definitive settlement agreement on December 2, 2014, which was granted final approval by the Court on May 15, 2015. The settlement resolved for all defendants all of the issues that were pending in the class action complaint. The class action settlement resulted in a payment of \$1.5 million to the settlement class, inclusive of fees and expenses. This settlement amount was paid from insurance proceeds.

*Derivative actions*

On September 13, 2013 and October 14, 2013, two separate stockholders filed complaints in the District Court of Travis County, Texas, purporting to bring derivative actions on behalf of us against certain current and former officers and directors of the Company. The first derivative action was captioned *Okumura v. Almgren, et. al.* (Cause No. D-1-GN-13-003230), and the second derivative action was captioned *Shaev v. Milner, et. al.* (Cause No. D-1-GN-13-003557). The allegations of each derivative complaint mirrored those of the class action complaint, and they asserted claims for breach of fiduciary duty, unjust enrichment, and/or abuse of control and sought damages on our behalf. These derivative actions were stayed by agreement pending resolution of the motion to dismiss the securities class action. The stay was lifted and on August 4, 2014, the parties filed a joint motion to consolidate the two derivative cases. On September 18, 2014, the District Court appointed lead counsel in the consolidated derivative action.

On September 23, 2014, we reached an agreement in principle and entered into a memorandum of understanding to settle the consolidated derivative actions. The parties to the consolidated derivative actions signed a definitive settlement agreement on January 30, 2015, which was granted final approval by the Court on May 12, 2015. The settlement resolved for all defendants all of the issues that were pending in the consolidated derivative actions. The settlement fees and expenses were paid from insurance proceeds.

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

*The following discussion should be read in conjunction with, and is qualified in its entirety by reference to, the financial statements and notes thereto included in Item 1 of this Form 10-Q and the financial statements and notes thereto and our Management's Discussion and Analysis of Financial Condition and Results of Operations for the year ended December 31, 2014, included in our 2014 Annual Report on Form 10-K. This report contains forward-looking statements, within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, that involve risks and uncertainties. Our expectations with respect to future results of operations that may be embodied in oral and written forward-looking statements, including any forward-looking statements that may be included in this report, are subject to risks and uncertainties that must be considered when evaluating the likelihood of our realization of such expectations. Our actual results could differ materially. The words "believe," "expect," "intend," "plan," "project," "will," and similar phrases as they relate to us are intended to identify such forward-looking statements. For further discussion regarding forward-looking statements, please see "Cautionary Statement Regarding Forward-Looking Statements." In addition, please see the "Risk Factors" in Part I, Item 1A, of our 2014 Annual Report on Form 10-K and in Part II, Item 1A, of this Form 10-Q for a discussion of items that may affect our future results.*

### **Overview**

Active Power designs, manufactures, sells and services flywheel-based UPS products that use kinetic energy to provide short-term power as a cleaner alternative to conventional electro-chemical battery-based energy storage. We also design, manufacture, sell, and service MIS that integrate critical power components into a pre-packaged, purpose-built enclosure that may include our UPS products as a component. Our products and solutions are based on our patented flywheel and power electronics technology and are designed to ensure continuity for data centers and other mission critical operations in the event of power disturbances.

Our products and solutions are designed to deliver continuous conditioned power during power disturbances such as voltage sags and surges, and to provide ride-through power in the event of a brief utility failure, supporting operations until utility power is restored or a longer term alternative power source, such as a diesel generator, is started. We sell our products globally through our direct sales force, manufacturer's representatives, distributors, OEMs, and IT partners in the Americas, in Europe, Middle East, and Africa ("EMEA"), and in the Asia Pacific region ("APAC").

We also offer services, including hardware and software maintenance, on all Active Power products, and other professional services such as assessment and implementation, for our customers' infrastructure projects.

We were founded as a Texas Corporation in 1992 and reincorporated in Delaware in 2000. Our headquarters are in Austin, Texas with international offices in the United Kingdom, Germany and China.

**Results of Operations**

Below are our revenues and costs and expenses for the three-month and six-month periods ended June 30, 2015 and 2014. This information should be read in conjunction with our Consolidated Financial Statements and notes thereto contained in Item 1 of this Form 10-Q.

| (\$ in thousands)                 | Three Months Ended June 30, |            |           |          | Six Months Ended June 30, |            |           |          |
|-----------------------------------|-----------------------------|------------|-----------|----------|---------------------------|------------|-----------|----------|
|                                   | 2015                        | 2014       | \$ change | % change | 2015                      | 2014       | \$ change | % change |
| Product revenue                   | \$ 12,905                   | \$ 7,484   | \$ 5,421  | 72 %     | \$ 22,453                 | \$ 14,941  | 7,512     | 50 %     |
| Service and other revenue         | 3,950                       | 2,670      | 1,280     | 48 %     | 7,531                     | 6,151      | 1,380     | 22 %     |
| Total revenue                     | 16,855                      | 10,154     | 6,701     | 66 %     | 29,984                    | 21,092     | 8,892     | 42 %     |
| Cost of product revenue           | 9,089                       | 6,352      | 2,737     | 43 %     | 16,060                    | 12,257     | 3,803     | 31 %     |
| Cost of service and other revenue | 2,268                       | 1,887      | 381       | 20 %     | 4,119                     | 3,992      | 127       | 3 %      |
| Total cost of goods sold          | 11,357                      | 8,239      | 3,118     | 38 %     | 20,179                    | 16,249     | 3,930     | 24 %     |
| Gross profit                      | 5,498                       | 1,915      | 3,583     | 187 %    | 9,805                     | 4,843      | 4,962     | 102 %    |
| Operating expenses:               |                             |            |           |          |                           |            |           |          |
| Research and development          | 1,430                       | 1,600      | (170)     | (11)%    | 2,946                     | 3,680      | (734)     | (20)%    |
| Selling and marketing             | 2,715                       | 3,152      | (437)     | (14)%    | 5,421                     | 6,040      | (619)     | (10)%    |
| General and administrative        | 1,524                       | 1,469      | 55        | 4 %      | 3,082                     | 3,075      | 7         | — %      |
| Total operating expenses          | 5,669                       | 6,221      | (552)     | (9)%     | 11,449                    | 12,795     | (1,346)   | (11)%    |
| Loss from Operations              | (171)                       | (4,306)    | 4,135     | 96 %     | (1,644)                   | (7,952)    | 6,308     | (79)%    |
| Interest expense, net             | (78)                        | (106)      | 28        | 26 %     | (157)                     | (207)      | 50        | (24)%    |
| Other income (expense), net       | (9)                         | (1)        | (8)       | (800)%   | (16)                      | (128)      | 112       | (88)%    |
| Net loss                          | \$ (258)                    | \$ (4,413) | \$ 4,155  | (94)%    | \$ (1,817)                | \$ (8,287) | \$ 6,470  | (78)%    |

**Product revenue.** Our product revenue was derived from the following sources:

| (\$ in thousands)                | Three Months Ended June 30, |          |           |          | Six Months Ended June 30, |           |           |          |
|----------------------------------|-----------------------------|----------|-----------|----------|---------------------------|-----------|-----------|----------|
|                                  | 2015                        | 2014     | Variance  |          | 2015                      | 2014      | Variance  |          |
|                                  |                             |          | \$ change | % change |                           |           | \$ change | % change |
| Product revenue:                 |                             |          |           |          |                           |           |           |          |
| UPS product revenue              | \$ 8,838                    | \$ 6,159 | \$ 2,679  | 43%      | \$ 16,015                 | \$ 12,795 | \$ 3,220  | 25%      |
| Modular Infrastructure Solutions | 4,067                       | 1,325    | 2,742     | 207%     | 6,438                     | 2,146     | 4,292     | 200%     |
| Total product revenue            | \$ 12,905                   | \$ 7,484 | \$ 5,421  | 72%      | \$ 22,453                 | \$ 14,941 | \$ 7,512  | 50%      |

Total product revenue for the three-month period ended June 30, 2015 increased by \$5.4 million, or 72%, to \$12.9 million compared to \$7.5 million in the same period in 2014. The increase was driven primarily by an increase in MIS sales of \$2.7 million and an increase in UPS sales of \$2.7 million. The increase is due to a higher volume of large projects from our IT channel partner this quarter compared to prior year in MIS and increased shipments to our OEM channel.

Product revenue for the six-month period ended June 30, 2015 increased by \$7.5 million, or 50%, to \$22.5 million compared to \$14.9 million in the same period in 2014. The increase was driven primarily by the increase in MIS business that was driven by large project orders from our IT channel partner. The level of orders may continue to fluctuate depending on our partner's success and need for infrastructure solutions.

Product revenue from our OEM channel for the three-month period ended June 30, 2015 was \$4.7 million, an increase of approximately \$3.1 million, compared to revenue of \$1.6 million for the second quarter of 2014. For the six-month period ended June 30, 2015, product revenue from our OEM channel was \$8.7 million, an increase of \$5.6 million, compared to \$3.1 million for the same period in 2014. The size and volume of orders from our OEM channel can fluctuate significantly on a quarterly basis, and we continue to see a small number of large transactions from our OEM channel. Total sales inclusive of service and spare parts to Caterpillar, our primary OEM channel, represented \$5.5 million and \$10.2 million, or 33% and 34% of our total revenue for the three-month and six-month periods ended June 30, 2015, compared to \$1.7 million and \$3.7 million, or 17% and 17% of our total revenue, in the comparable periods of 2014.

Product revenue from our IT channel for the second quarter of 2015 was \$3.6 million, compared to \$0 for the second quarter of 2014. For the six-month period ended June 30, 2015, product revenue from our IT channel was \$4.5 million, an increase of \$3.7 million, compared to \$0.8 million for the same period of 2014. This increase was driven primarily by two large orders that were partially shipped in the second quarter of 2015.

Product revenue in the Americas was \$8.6 million, or 67% of our product revenue, for the three-month period ended June 30, 2015, compared to \$4.1 million, or 55% of our product revenue, for the same period in 2014. For the six-month period ended June 30, 2015, our sales in the Americas were \$15.9 million, or 71% of our total product revenue, compared to \$9.1 million, or 61% for the same period in 2014. The increase reflects higher MIS revenues of \$4.1 million due to higher volume of large projects during 2015 compared to 2014.



[Index](#)

We sell products directly to customers in APAC and EMEA and also through a network of international distributors. Product sales to customers in APAC were \$0.2 million, or 1% of our total product revenue, in the three-month period ended June 30, 2015, compared to \$0.5 million, or 7% for the same period in 2014. Our sales in APAC were \$0.3 million, or 1% of our total product revenue, in the six-month period ended June 30, 2015, compared to \$1.2 million, or 8% for the same period in 2014. The decrease was driven by lower UPS sales.

Product revenue in EMEA was \$4.1 million, or 32% of product revenue, in the three-month period ended June 30, 2015, compared to \$2.9 million, or 39%, for the same period of 2014. Our sales in EMEA were \$6.3 million, or 28% of product revenue, in the six-month period ended June 30, 2015, compared to \$4.6 million, or 31% for the same period in 2014. The increase in product revenue in EMEA is primarily attributable to an increase in our OEM channel partner sales during the quarter ending June 30, 2015.

**Service and other revenue.** Service and other revenue increased by approximately \$1.3 million, or 48%, to \$4.0 million for the three-month period ended June 30, 2015, compared to \$2.7 million in the same period of 2014. For the six-month period ended June 30, 2015, our service and other revenue increased by approximately \$1.4 million, or 22%, to \$7.5 million compared to \$6.2 million in the same period of 2014. The increase primarily reflects higher professional fees and an improved mix of spare parts.

**Cost of product revenue.** Cost of product revenue as a percentage of total product revenue was 70% and 72% for the three-month and six-month periods ended June 30, 2015, compared to 85% and 82% for the same periods in 2014. The decrease in costs as a percentage of revenue for the three-month and six-month periods ended June 30, 2015 reflects a favorable mix with higher margin UPS and MIS sales along with continued improvements in manufacturing absorption associated with increased production.

**Cost of service and other revenue.** Cost of service and other revenue as a percentage of total service and other revenue was 57% and 55% for the three-month and six-month periods ended June 30, 2015, compared to 71% and 65% for the same periods of 2014. These decreases reflect a favorable mix of higher service contracts along with a better mix of spare parts.

**Gross profit.** For the three-month periods ended June 30, 2015 and 2014, our gross profit was 33% and 19% of revenue, respectively. For the six-month period ended June 30, 2015, our gross profit was 33% of revenue, compared to 23% for the same period of 2014. The margin increase is related to a favorable mix of higher margin UPS sales along with higher MIS margins as we continue to improve manufacturing absorption.

**Research and development.** Research and development expenses were \$1.4 million, \$0.2 million, or 11%, lower in the second quarter of 2015 compared to \$1.6 million in the second quarter of 2014. The decrease was primarily due to lower payroll expense of \$0.1 million and reduced fees from external parties of \$0.1 million related to prototype and testing expenses which were incurred in fiscal 2014.

For the six-month period ended June 30, 2015, our research and development expense was \$2.9 million, compared to \$3.7 million or 20% lower for the same period of 2014. The decrease was primarily due to lower payroll expense of \$0.5 million and reduced fees from external parties of \$0.3 million related to prototype and testing expenses which were incurred in fiscal 2014.

**Selling and marketing.** Selling and marketing costs were approximately \$2.7 million in the second quarter of 2015, compared to \$3.2 million for the same period of 2014. The decrease was primarily due to lower payroll expense of \$0.2 million and \$0.1 million in professional fees in 2015 compared to 2014.

Selling and marketing expenses were approximately \$5.4 million for the six-month period ended June 30, 2015, compared to \$6.0 million for the same period of 2014. The decrease was primarily due to lower payroll expense of \$0.4 million and \$0.1 million in third party representative commissions.

**General and administrative.** General and administrative expenses for the three-month periods ended June 30, 2015 and 2014 were both approximately \$1.5 million. The decrease of legal expenses of \$0.2 million were offset by an increase in stock compensation expense of \$0.1 million. General and administrative expenses for the six-month period ending June 30, 2015 and 2014 were both approximately \$3.1 million. The decrease of legal expenses of \$0.1 million were offset by the increase in stock compensation expense of \$0.2 million.

**Interest expense, net.** Net interest expense decreased approximately \$28,000 and \$50,000 for the three months and six months ended June 30, 2015, respectively, compared to the same periods in 2014. The decrease is related to the lower interest rate related to our amended Loan Agreement (defined herein) in fiscal 2014 from the outstanding balance on our revolving credit facility.

**Other income (expense), net.** Other income (expense), net for the three months ended June 30, 2015 increased approximately \$8,000 compared to the same period of 2014 which primarily reflects foreign exchange losses or gains on settlement of intercompany balances and sales contracts held in foreign currencies.

Other income (expense), net for the six month period ended June 30, 2015 decreased approximately \$0.1 million, or 88%, compared to the same period of 2014, and primarily reflects foreign exchanges losses or gains on settlement of intercompany balances and sales contracts held in foreign currencies.

## Liquidity and Capital Resources

Our primary sources of liquidity at June 30, 2015 are our cash and cash equivalents, our bank credit facilities and projected cash flows from operating activities. If we meet our cash flow projections, we expect we will have adequate capital resources to continue operating our business for at least the next twelve months. Our projections and our assumptions around the adequacy of our liquidity are based on estimates regarding expected revenues and future costs. However, there are scenarios in which our revenues may not meet our projections, our costs may exceed our estimates or our working capital needs may be greater than anticipated. Further, our estimates may change and future events or developments may also affect our estimates. Any of these factors may change our expectation of cash usage in the remainder of 2015 and beyond or significantly affect our level of liquidity.

On July 28, 2014, we entered into a Third Amended and Restated Loan and Security Agreement (“Loan Agreement”) with Silicon Valley Bank (“SVB”). This new amended three-year loan facility provides for a secured revolving line of credit in an aggregate amount of up to eighty percent (80%) of the facility amount of \$18.8 million, or \$15.0 million, and increased our inventory and purchase order availability from \$3.5 million to \$7.0 million subject to certain borrowing bases. Purchase orders and eligible inventory are subject to a sublimit of \$4.0 million while our sublimit for accounts receivable for the UK and Germany is \$5.0 million each. In the event we maintain our Liquidity Ratio (as defined in the Loan Agreement) of 2.50:1.00 for the immediately preceding Reconciliation Periods (also as defined in the Loan Agreement) the sublimit will be uncapped during this time. We are currently in compliance with all loan covenants under the Loan Agreement. Further, the Loan Agreement extends the maturity date to August 5, 2017 and reduces the finance charge to a per annum rate equal to SVB's prime rate, subject to a minimum prime rate of 4.00%, plus (a) 0.50% for eligible accounts, inventory and purchase orders when we are Borrowing Base Eligible (as defined in the Loan Agreement), or (b) 1.20% for eligible accounts when we are not Borrowing Base Eligible.

The loans made to us under the Loan Agreement are secured by a lien on substantially all of our assets, including the assets of Active Power Solutions Limited, our wholly-owned United Kingdom subsidiary, and the assets of Active Power (Germany) GmbH, our indirect wholly-owned German subsidiary. The only direct or indirect subsidiaries of Active Power, Inc. that are not guarantors under the Loan Agreement are Active Power China (Beijing) Co. Ltd. and immaterial subsidiaries that are not operating companies. There are no restrictions on the ability of any of the subsidiary guarantors to transfer funds to Active Power, Inc. in the form of loans, advances or dividends, except as provided by applicable law.

The other key terms of the Loan Agreement remain unchanged, including customary affirmative covenants, a minimum liquidity ratio, the borrowing base eligibility (formerly called the “streamline ratio”), reporting requirements, and other terms and conditions. We are currently in compliance with all loan covenants under the loan facility. As of June 30, 2015, we had outstanding borrowings of \$5.5 million under this loan facility and, based on the borrowing base formula, the additional amount available to us for use ranged between \$4.3 million and \$9.5 million during the quarter. For further information regarding this loan facility, refer to our Annual Report on Form 10-K for the year ended December 31, 2014, and to our Current Report on Form 8-K filed on July 29, 2014.

In March 2014, we sold approximately 3.7 million shares of common stock at a purchase price of \$3.15 per share, for proceeds, net of fees and expenses, of approximately \$10.4 million, in a public underwritten offering made under a shelf registration statement that we had filed with the Securities and Exchange Commission and that had been declared effective in June 2013. The proceeds from this offering will be used by us to help fund our working capital requirements and for general corporate purposes.

Should additional funding be required or desirable, we would expect to raise the required funds through borrowings or public or private sales of debt or equity securities. If we raise additional funds through the issuance of convertible debt or equity securities, the ownership of our existing stockholders could be significantly diluted. If we obtain additional debt financing, a substantial portion of our operating cash flow may be dedicated to the payment of principal and interest on such indebtedness, and the terms of the debt securities issued could impose significant restrictions on our operations. We do not know whether we will be able to secure additional funding, or funding on terms acceptable to us, to continue our operations as planned. If financing is not available, we may be required to reduce, delay or eliminate certain activities or to license or sell to others some of our proprietary technology.

*Operating Activities*

The following table summarizes the changes in cash used in operating activities:

| (\$ in thousands)                 | Six Months Ended June 30, |            | Variance |     |
|-----------------------------------|---------------------------|------------|----------|-----|
|                                   | 2015                      | 2014       | \$       | %   |
| Cash used in operating activities | \$ (3,817)                | \$ (6,456) | \$ 2,639 | 41% |

Cash used in operating activities was \$3.8 million in the six-month period ended June 30, 2015 compared to \$6.5 million for the same period of 2014. Cash used in operating activities in 2015 was primarily derived from our \$4.8 million increase in accounts receivables along with our net loss of \$1.8 million offset by a \$1.8 million increase in accounts payables and accrued expenses. Cash used in operating activities includes \$0.5 million in restricted cash for a secured letter of credit which will become unrestricted in July 2015. These changes reflect the frequent changes in our working capital, which can be impacted by the timing of product orders and shipments and can result in very large fluctuations in inventory, payables and receivables based on the large size of some of our orders.

Cash used in operating activities in 2014 was primarily due to higher net losses combined with a reduction in accrued expenses.

*Investing Activities*

The following table summarizes the changes in cash used in investing activities:

| (\$ in thousands)                 | Six Months Ended June 30, |          | Variance |        |
|-----------------------------------|---------------------------|----------|----------|--------|
|                                   | 2015                      | 2014     | \$       | %      |
| Cash used in investing activities | \$ (392)                  | \$ (170) | \$ (222) | (131)% |

Investing activities consist of purchases of property and equipment. Capital expenditures were \$0.2 million higher in the six-month period ending June 30, 2015, compared to the same period of 2014, as we invested more in capital improvements during 2015.

*Financing Activities*

The following table summarizes the changes in cash provided by financing activities:

| (\$ in thousands)                               | Six Months Ended June 30, |           | Variance    |        |
|---|---------------------------|-----------|-------------|--------|
|   | 2015                      | 2014      | \$          | %      |
| Cash (used in) provided by financing activities | \$ (6)                    | \$ 10,535 | \$ (10,541) | (100)% |

Funds used in financing activities in the six-month ended June 30, 2015 primarily includes net share settlement of equity awards.

Funds provided by financing activities in the six-month period ended June 30, 2014 primarily includes the sale of common stock at a purchase price of \$3.15 per share, for proceeds, net of fees and expenses, of approximately \$10.4 million, in a public underwritten offering, and also reflects the proceeds from the exercise of employee stock options.

We believe that our cash and cash equivalents, projected cash flows from operations and sources of available liquidity will be sufficient to fund our operations for the next 12 months. However, a sudden change in business volume, positive or negative, from any of our business or channel partners, or in our direct business, or any customer-driven events such as order or delivery deferral, could significantly impact our revenues and cash needs. We do have some opportunity to adjust expenditures or take other measures to reduce our cash consumption or to identify additional sources of funding if we anticipate an increase in our working capital requirements due to increased revenues or changes in our revenue mix. A significant increase in sales, especially

[Index](#)

in our MIS business, would likely increase our working capital requirements, due to the longer production time and cash cycle of sales of these products.

**Off-Balance Sheet Arrangements, Guarantees and Other Contingent Obligations**

There have been no significant changes to our off-balance sheet arrangements or contractual commitments from those disclosed in our 2014 Annual Report on Form 10-K.

**Item 3. Quantitative and Qualitative Disclosures about Market Risk.**

For a description of our market risks, see Part I, Item 7A in our 2014 Annual Report on Form 10-K. There have been no material changes in our exposures to market risk since December 31, 2014.

**Item 4. Controls and Procedures.**

**Evaluation of disclosure controls and procedures.**

Our Chief Executive Officer and our Chief Financial Officer, based on the evaluation of our disclosure controls and procedures (as defined in Rule 13a-15(e) or 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), required by paragraph (b) of Rule 13a-15 or Rule 15d-15, have concluded that, as of June 30, 2015, our disclosure controls and procedures were effective at a reasonable assurance level to ensure that the information we are required to disclose in reports that we file or submit under the Exchange Act, (i) is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms, and (ii) is accumulated and communicated to our management, including our Chief Executive Officer and our Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

**Changes in internal control over financial reporting.**

During the three months ended June 30, 2015, there were no changes in our internal control over financial reporting identified in connection with the evaluation required by Rule 13a-15(d) and Rule 15d-15(d) under the Exchange Act that have materially affected, or that we believe are reasonably likely to materially affect, our internal control over financial reporting, as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act.

**PART II – OTHER INFORMATION**

**Item 1. Legal Proceedings.**

Refer to note 7, “Commitments and Contingencies,” on pages 12 to 13 of this Form 10-Q.

**Item 1A. Risk Factors.**

There have been no material changes from the risk factors described in our 2014 Annual Report on Form 10-K. You should carefully consider the risks described in Item 1A of our 2014 Annual Report on Form 10-K before making a decision to invest in our common stock or in evaluating Active Power and our business. The risks and uncertainties described in our 2014 Annual Report on Form 10-K are not the only ones we face. Additional risks and uncertainties that we do not presently know, or that we currently view as immaterial, may also impair our business operations.

**Item 6. Exhibits.**

See the Exhibit Index beginning on page 24 of this Form 10-Q.

**SIGNATURES**

Pursuant to the requirements 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.

**ACTIVE POWER, INC.**

(Registrant)

July 28, 2015  
(Date)

/s/ Mark A. Ascolese

---

**Mark A. Ascolese**  
**President and Chief Executive Officer**  
**(Principal Executive Officer)**

July 28, 2015  
(Date)

/s/ James A. Powers

---

**James A. Powers**  
**Chief Financial Officer and Vice President Finance**  
**(Principal Financial and Accounting Officer)**

[Index](#)

INDEX TO EXHIBITS

| Exhibit No. | Description of Exhibit   |
|-------------|--|
| 3.1*        | Restated Certificate of Incorporation of Active Power, Inc., as amended (filed as Exhibit 3.1 to Active Power Inc.'s Quarterly Report on Form 10-Q filed on August 1, 2014)  |
| 3.2*        | Second Amended and Restated Bylaws of Active Power, Inc., as amended (filed as Exhibit 3.2 to Active Power Inc.'s Quarterly Report on Form 10-Q filed on May 1, 2014)  |
| 4.1*        | Specimen certificate for shares of Common Stock (filed as Exhibit 4.1 to Active Power's IPO Registration Statement on Form S-1 (SEC File No. 333-36946))   |
| 4.2*        | See Exhibits 3.1 and 3.2 for provisions of the Certificate of Incorporation and Bylaws of the registrant defining the rights of holders of common stock  |
| 10.1*       | Active Power, Inc. Amended and Restated 2010 Equity Incentive Plan (filed as Exhibit 10.1 to Active Power's Current Report on Form 8-K filed on April 28, 2015)  |
| 31.1†       | Certification of Chief Executive Officer pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002  |
| 31.2†       | Certification of Chief Financial Officer pursuant to Exchange Act Rules 13a-14(a) and 15(d)-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002  |
| 32.1††      | Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002  |
| 32.2††      | Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002  |
| 101†        | The following financial statements from the Active Power's Quarterly Report on Form 10-Q for the quarter ended June 30, 2015, formatted in XBRL: (i) Condensed Consolidated Balance Sheets, (ii) Condensed Consolidated Statements of Operations and Comprehensive Loss, (iii) Condensed Consolidated Statements of Cash Flows, and (iv) Notes to Condensed Consolidated Financial Statements. |

---

\* Incorporated by reference to the indicated filing.

† Filed with this report.

†† Furnished with this report.



## CERTIFICATIONS

I, Mark A. Ascolese, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Active Power, 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(s) 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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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; and
  - (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; and
5. The registrant's other certifying officer(s) 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: July 28, 2015

/s/ Mark A. Ascolese

Mark A. Ascolese  
President and Chief Executive Officer  
(Principal Executive Officer)

## CERTIFICATIONS

I, James A. Powers, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Active Power, 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(s) 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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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; and
  - (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; and
5. The registrant's other certifying officer(s) 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: July 28, 2015

/s/ James A. Powers

James A. Powers

Chief Financial

Officer and Vice President Finance

(Principal Financial and Accounting Officer)

**CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO SECTION 906  
OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report on Form 10-Q of Active Power, Inc. (the "Company") for the period ending June 30, 2015, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Mark A. Ascolese, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities 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 the Company.

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

/s/ Mark A. Ascolese

Mark A. Ascolese

President and Chief Executive Officer

July 28, 2015

---

**CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO SECTION 906  
OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report on Form 10-Q of Active Power, Inc. (the "Company") for the period ending June 30, 2015 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, James A. Powers, Chief Financial Officer and Vice President of Finance of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities 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 the Company.

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

/s/ James A. Powers

James A. Powers

Chief Financial Officer and Vice President of  
Finance

July 28, 2015

---

