

**UQM TECHNOLOGIES, INC.  
AND SUBSIDIARIES**

**Consolidated Balance Sheets**

	<u>March 31, 2009</u>	<u>March 31, 2008</u>
<b><u>Assets</u></b>		
Current assets:		
Cash and cash equivalents	\$ 2,501,999	3,176,084
Short-term investments	3,291,667	6,589,808
Accounts receivable	917,099	1,304,139
Costs and estimated earnings in excess of billings on uncompleted contracts	643,098	649,670
Inventories	1,307,171	961,489
Prepaid expenses and other current assets	<u>117,768</u>	<u>119,647</u>
Total current assets	<u>8,778,802</u>	<u>12,800,837</u>
Property and equipment, at cost:		
Land	181,580	181,580
Building	2,464,213	2,460,103
Machinery and equipment	<u>4,040,406</u>	<u>3,558,524</u>
	6,686,199	6,200,207
Less accumulated depreciation	<u>(3,556,796)</u>	<u>(3,317,812)</u>
Net property and equipment	<u>3,129,403</u>	<u>2,882,395</u>
Patent and trademark costs, net of accumulated amortization of \$733,594 and \$677,957	438,184	477,765
Other assets	<u>76,443</u>	<u>241,549</u>
Total assets	<u>\$ 12,422,832</u>	<u>16,402,546</u>

(Continued)

*See accompanying notes to consolidated financial statements.*

**UQM TECHNOLOGIES, INC.  
AND SUBSIDIARIES**

**Consolidated Balance Sheets, Continued**

	<u>March 31, 2009</u>	<u>March 31, 2008</u>
<b><u>Liabilities and Stockholders' Equity</u></b>		
Current liabilities:		
Accounts payable	\$ 651,129	740,527
Other current liabilities	600,672	372,285
Current portion of long-term debt	416,923	106,002
Short-term deferred compensation under executive employment agreements	397,834	364,000
Billings in excess of costs and estimated earnings on uncompleted contracts	<u>71,367</u>	<u>707,848</u>
Total current liabilities	<u>2,137,925</u>	<u>2,290,662</u>
Long-term debt, less current portion	-	416,923
Long-term deferred compensation under executive employment agreements	<u>675,715</u>	<u>633,873</u>
	<u>675,715</u>	<u>1,050,796</u>
Total liabilities	<u>2,813,640</u>	<u>3,341,458</u>
Commitments and contingencies		
Stockholders' equity:		
Common stock, \$0.01 par value, 50,000,000 shares authorized; 26,727,694 and 26,526,737 shares issued and outstanding	267,277	265,267
Additional paid-in capital	78,767,154	77,819,041
Accumulated deficit	<u>(69,425,239)</u>	<u>(65,023,220)</u>
Total stockholders' equity	<u>9,609,192</u>	<u>13,061,088</u>
Total liabilities and stockholders' equity	<u>\$ 12,422,832</u>	<u>\$ 16,402,546</u>

*See accompanying notes to consolidated financial statements.*

**UQM TECHNOLOGIES, INC.  
AND SUBSIDIARIES**

**Consolidated Statements of Operations**

	Year Ended March 31, 2009	Year Ended March 31, 2008	Year Ended March 31, 2007
Revenue:			
Contract services	\$ 2,717,246	2,591,939	2,907,536
Product sales	<u>6,011,065</u>	<u>4,916,383</u>	<u>3,745,658</u>
	<u>8,728,311</u>	<u>7,508,322</u>	<u>6,653,194</u>
Operating costs and expenses:			
Costs of contract services	2,279,956	2,039,017	2,666,316
Costs of product sales	4,682,711	4,392,442	3,323,577
Research and development	593,209	461,791	321,160
Production engineering	1,869,848	1,706,978	1,286,761
Selling, general and administrative	3,782,840	3,905,495	2,855,213
Loss (gain) on disposal of assets	<u>( 510)</u>	<u>(2,159)</u>	<u>889</u>
	<u>13,208,054</u>	<u>12,503,564</u>	<u>10,453,916</u>
Loss before other income (expense)	(4,479,743)	(4,995,242)	(3,800,722)
Other income (expense):			
Interest income	198,947	463,248	445,578
Interest expense	(33,387)	(40,652)	(47,422)
Impairment of investment	(89,369)	-	-
Other	<u>1,533</u>	<u>(13,459)</u>	<u>(28,791)</u>
	<u>77,724</u>	<u>409,137</u>	<u>369,365</u>
Net loss	\$ <u>(4,402,019)</u>	<u>(4,586,105)</u>	<u>(3,431,357)</u>
Net loss per common share-basic and diluted:	\$( <u>0.17</u> )	( <u>0.18</u> )	( <u>0.14</u> )
Weighted average number of shares of common stock outstanding - basic and diluted	<u>26,651,130</u>	<u>26,196,278</u>	<u>25,116,354</u>

*See accompanying notes to consolidated financial statements.*

**UQM TECHNOLOGIES, INC.  
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**Consolidated Statements of Stockholders' Equity**

	Number of common shares <u>issued</u>	Common stock <u>\$</u>	Additional paid-in capital	Accumulated deficit	Total stockholders' equity
<b>Balances at April 1, 2006</b>	24,776,042	\$ 247,760	69,293,461	(56,796,847)	12,744,374
Issuance of common stock under employee stock purchase plan	7,095	71	17,695	-	17,766
Issuance of common stock upon exercise of employee options	215,440	2,154	681,539	-	683,693
Issuance of common stock upon exercise of warrants	165,812	1,659	426,136	-	427,795
Issuance of common stock to directors	12,500	125	39,875	-	40,000
Compensation expense from employee and director stock option and common stock grants	-	-	917,756	-	917,756
Cumulative effect of adoption of SAB 108	-	-	-	(208,911)	(208,911)
Net loss	<u>-</u>	<u>-</u>	<u>-</u>	<u>(3,431,357)</u>	<u>(3,431,357)</u>
<b>Balances at March 31, 2007</b>	25,176,889	251,769	71,376,462	(60,437,115)	11,191,116
Issuance of common stock in follow-on offering, net of offering costs	1,250,000	12,500	5,171,177	-	5,183,677
Issuance of common stock under employee stock purchase plan	14,664	146	40,644	-	40,790
Issuance of common stock upon exercise of employee options	24,362	244	56,431	-	56,675
Issuance of common stock under stock bonus plan	60,822	608	46,623	-	47,231
Compensation expense from employee and director stock option and common stock grants	-	-	1,127,704	-	1,127,704
Net loss	<u>-</u>	<u>-</u>	<u>-</u>	<u>(4,586,105)</u>	<u>(4,586,105)</u>
<b>Balances at March 31, 2008</b>	26,526,737	265,267	77,819,041	(65,023,220)	13,061,088
Issuance of common stock under employee stock purchase plan	22,268	223	33,994	-	34,217
Purchase of treasury stock	(70,269)	(703)	(156,434)	-	(157,137)
Issuance of common stock under stock bonus plan	248,958	2,490	(2,490)	-	-
Compensation expense from employee and director stock option and common stock grants	-	-	1,073,043	-	1,073,043
Net loss	<u>-</u>	<u>-</u>	<u>-</u>	<u>(4,402,019)</u>	<u>(4,402,019)</u>
<b>Balances at March 31, 2009</b>	<u>26,727,694</u>	<u>\$ 267,277</u>	<u>78,767,154</u>	<u>(69,425,239)</u>	<u>9,609,192</u>

*See accompanying notes to consolidated financial statements.*

**UQM TECHNOLOGIES, INC.  
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**Consolidated Statements of Cash Flows**

	<u>Year Ended</u> <u>March 31, 2009</u>	<u>Year Ended</u> <u>March 31, 2008</u>	<u>Year Ended</u> <u>March 31, 2007</u>
Cash flows from operating activities:			
Net loss	\$(4,402,019)	(4,586,105)	(3,431,357)
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation and amortization	546,843	437,799	414,322
Gain on disposal of assets	(510)	(13,314)	-
Impairment of long-lived assets	-	11,155	889
Impairment of investment	89,369	-	-
Impairment of inventories	41,613	-	-
Non-cash equity based compensation	1,073,043	1,174,935	957,756
Change in operating assets and liabilities:			
Accounts receivable and costs and estimated earnings in excess of billings on uncompleted contracts	393,612	(255,113)	(736,243)
Inventories	(387,295)	(61,604)	(432,400)
Prepaid expenses and other current assets	1,879	159,696	(160,904)
Other assets	-	2,101	2,102
Accounts payable and other current liabilities	138,989	(228,918)	436,201
Billings in excess of costs and estimated earnings on uncompleted contracts	(636,481)	395,311	90,911
Deferred compensation under executive employment agreements	<u>75,676</u>	<u>452,334</u>	<u>125,767</u>
Net cash used in operating activities	<u>(3,065,281)</u>	<u>(2,511,723)</u>	<u>(2,732,956)</u>
Cash flows from investing activities:			
Maturities (purchases) of short-term investments	3,208,772	(607,980)	27,566
Increase in other long-term assets	(2,122)	(2,217)	(52,699)
Prepayments on property and equipment	(188,427)	(186,633)	-
Acquisition of property and equipment	(382,559)	(616,488)	(397,008)
Increase in patent and trademark costs	(16,056)	(51,099)	(6,773)
Proceeds from sale of assets	<u>510</u>	<u>17,665</u>	<u>-</u>
Net cash provided by (used in) investing activities	<u>\$ 2,620,118</u>	<u>(1,446,752)</u>	<u>(428,914)</u>

*See accompanying notes to consolidated financial statements.*

(Continued)

**UQM TECHNOLOGIES, INC.  
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**Consolidated Statements of Cash Flows, Continued**

	<u>Year Ended March 31, 2009</u>	<u>Year Ended March 31, 2008</u>	<u>Year Ended March 31, 2007</u>
Cash flows from financing activities:			
Repayment of debt	\$ (106,002)	(98,760)	(92,013)
Issuance of common stock in follow-on offering, net of offering costs	-	5,183,677	-
Issuance of common stock upon exercise of employee options	-	56,675	683,693
Purchase of treasury stock	(157,137)	-	-
Issuance of common stock upon exercise of warrants	-	-	427,795
Issuance of common stock under employee stock purchase plan	<u>34,217</u>	<u>40,790</u>	<u>17,766</u>
Net cash provided by (used in) financing activities	<u>(228,922)</u>	<u>5,182,382</u>	<u>1,037,241</u>
Increase (decrease) in cash and cash equivalents	(674,085)	1,223,907	(2,124,629)
Cash and cash equivalents at beginning of year	<u>3,176,084</u>	<u>1,952,177</u>	<u>4,076,806</u>
Cash and cash equivalents at end of year	\$ <u>2,501,999</u>	<u>3,176,084</u>	<u>1,952,177</u>
Supplemental Cash Flow Information:			
Interest paid in cash during the year	\$ <u>33,738</u>	<u>40,979</u>	<u>47,726</u>

*See accompanying notes to consolidated financial statements.*

**UQM TECHNOLOGIES, INC.  
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements**

**(1) Summary of Significant Accounting Policies**

**(a) Description of Business**

UQM Technologies, Inc. and our wholly-owned subsidiary UQM Power Products, Inc. are engaged in the research, development and manufacture of permanent magnet electric motors and the electronic controls for such motors. Our facility is located in Frederick, Colorado. Our revenue is derived primarily from product sales to customers in the automotive, agriculture, industrial, medical and aerospace markets, and from contract research and development services. We are impacted by other factors such as the continued receipt of contracts from industrial and governmental parties, our ability to protect and maintain the proprietary nature of our technology, continued product and technological advances and our ability together with our partners, to commercialize our products and technology.

**(b) Principles of Consolidation**

The consolidated financial statements include the accounts of UQM Technologies, Inc. and those of all majority-owned or controlled subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation.

**(c) Cash and Cash Equivalents and Short-term Investments**

We consider cash on hand and investments with original maturities of three months or less to be cash and cash equivalents. Investments with original maturities of greater than three months and less than one year from the balance sheet date are classified as short-term.

**(d) Investments**

We have an investment policy approved by the Board of Directors that governs the quality, acceptability and dollar concentration of our investments. Investments are comprised of marketable securities and consist primarily of commercial paper, asset-backed and mortgage-backed notes and bank certificates of deposits with original maturities beyond three months. All marketable securities are held in our name at two major financial institutions who hold custody of the investments. All of our investments are held-to-maturity investments that we have the positive intent and ability to hold until maturity. These securities are recorded at amortized cost. Investments with an original maturity of greater than three months and less than one year from the balance sheet date are classified as short-term.

The amortized cost and unrealized gain or loss of our investments were:

	<u>March 31, 2009</u>		<u>March 31, 2008</u>	
	<u>Amortized Cost</u>	<u>Gain (Loss)</u>	<u>Amortized Cost</u>	<u>Gain (Loss)</u>
<u>Short-term investments:</u>				
U.S. government and government agency securities	\$ 2,055,176	2,755	1,656,515	(3,193)
Commercial paper, corporate and foreign bonds	137,418	(3,454)	1,912,779	(9,050)
Certificates of deposit	<u>1,099,073</u>	<u>-</u>	<u>3,020,514</u>	<u>-</u>
	<u>3,291,667</u>	<u>(699)</u>	<u>6,589,808</u>	<u>(12,243)</u>
<u>Long-term investment:</u>				
Certificates of deposit (included in other assets)	<u>57,038</u>	<u>-</u>	<u>54,916</u>	<u>-</u>
	<u>\$ 3,348,705</u>	<u>(699)</u>	<u>6,644,724</u>	<u>(12,243)</u>

**UQM TECHNOLOGIES, INC.  
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**Notes to Consolidated Financial Statements, Continued**

The time to maturity of held-to-maturity securities were:

	<u>March 31,</u>	
	<u>2009</u>	<u>2008</u>
Three to six months	\$ -	1,311,373
Six months to one year	3,291,667	5,278,435
Over one year	<u>57,038</u>	<u>54,916</u>
	<u>\$ 3,348,705</u>	<u>6,644,724</u>

**(e) Accounts Receivable**

We extend unsecured credit to most of our customers following a review of the customers' financial condition and credit history. We establish an allowance for doubtful accounts based upon a number of factors including the length of time trade receivables are past due, the customer's ability to pay its obligation to us, the condition of the general economy, estimates of credit risk, historical trends and other information. We write off accounts receivable when they become uncollectible against our allowance for uncollectible accounts receivable. At March 31, 2009 and 2008, no allowance for uncollectible accounts receivable was deemed necessary. Accounts receivable are deemed to be past due when they have not been paid by their contractual due date.

**(f) Inventories**

Inventories are stated at the lower of cost or market. Cost is determined by the first-in, first-out method. Inventory reserves are based on our assessment of recoverability of slow moving or obsolete inventory items. We did not have any reserves recorded as of March 31, 2009 and 2008.

**(g) Property and Equipment**

Property and equipment is stated at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, which range from 3 to 5 years, except for buildings, which are depreciated over 27.5 years. Maintenance and repairs are charged to expense as incurred. Depreciation expense for the fiscal years ended March 31, 2009, 2008 and 2007 was \$491,206, \$382,162 and \$337,470, respectively.

**(h) Patent and Trademark Costs**

Patent and trademark costs consist primarily of legal expenses, and represent those costs incurred by us for the filing of patent and trademark applications. Amortization of patent and trademark costs is computed using the straight-line method over the estimated useful life of the asset, typically 17 years for patents, and 40 years for trademarks. Amortization expense for the fiscal years ended March 31, 2009, 2008 and 2007 was \$55,637, \$55,637 and \$76,852, respectively.

**(i) Impairment of Long-Lived Assets**

We periodically evaluate whether circumstances or events have affected the recoverability of long-lived assets including intangible assets with finite useful lives. The assessment of possible impairment is based on our ability to recover the carrying value of the asset or groups of assets from expected future cash flows (undiscounted and without interest charges) estimated by management. If expected future cash flows are less than the carrying value, an impairment loss is recognized to adjust the asset to fair value as determined by expected discounted future cash flows.

**(j) Product Warranties**

Our warranty policy generally provides three months to three years of coverage depending on the product. We record a liability for estimated warranty obligations at the date products are sold. The estimated cost of warranty

**UQM TECHNOLOGIES, INC.  
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**Notes to Consolidated Financial Statements, Continued**

coverage is based on our actual historical experience with our current products or similar products. For new products, the required reserve is based on historical experience of similar products until sufficient historical data has been collected on the new product. Adjustments are made as new information becomes available.

**(k) Revenue and Cost Recognition**

We manufacture proprietary products and other products. Revenue from sales of products are generally recognized at the time title to the goods and the benefits and risks of ownership passes to the customer which is typically when products are shipped based on the terms of the customer purchase agreement.

Revenue relating to long-term fixed price contracts is recognized using the percentage of completion method. Under the percentage of completion method, contract revenues and related costs are recognized based on the percentage that costs incurred to date bear to total estimated costs.

Changes in job performance, estimated profitability and final contract settlements may result in revisions to cost and revenue, and are recognized in the period in which the revisions are determined.

Contract costs include all direct materials, subcontract and labor costs and other indirect costs. Selling, general and administrative costs are charged to expense as incurred. At the time a loss on a contract becomes known, the entire amount of the estimated loss is accrued.

The aggregate of costs incurred and estimated earnings recognized on uncompleted contracts in excess of related billings is shown as a current asset, and billings on uncompleted contracts in excess of costs incurred and estimated earnings is shown as a current liability.

**(l) Income Taxes**

The Company accounts for income taxes in accordance with Statement of Financial Accounting Standards No. 109, *Accounting for Income Taxes* ("SFAS 109"). Under the asset and liability method of SFAS 109, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis and operating loss and tax credit carry-forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The valuation of deferred tax assets may be reduced if future realization is not assured. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enactment date.

**(m) Research and Development**

Costs of researching and developing new technology, or significantly altering existing technology, are expensed as incurred.

**(n) Loss per Common Share**

Basic earnings per share is computed by dividing income or loss available to common stockholders by the weighted average number of common shares outstanding during the periods presented. Diluted earnings per share is computed by dividing income or loss available to common stockholders by all outstanding and potentially dilutive shares during the periods presented, unless the effect is antidilutive. At March 31, 2009, 2008 and 2007, respectively, issued but not yet earned common shares of 225,870, 283,480, and 136,035 were being held in safekeeping by the Company. For the fiscal years 2009, 2008, and 2007, shares in the amount of zero, 7,887, and 9,767 shares were potentially included in the calculation of diluted loss per share under the treasury stock method but were not included, because to do so would be antidilutive. At March 31, 2009, 2008 and 2007, options to purchase 2,995,214, 2,679,740 and 2,771,914 shares of common stock, respectively, and warrants to purchase zero, 85,267 and 157,267 shares of common stock, respectively, were outstanding. For the

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**Notes to Consolidated Financial Statements, Continued**

fiscal years ended March 31, 2009, 2008 and 2007, respectively, options and warrants for 2,957,734, 1,400,051 and 1,582,262 shares were not included in the computation of diluted loss per share because the option or warrant exercise price was greater than the average market price of the common stock. In-the-money options and warrants determined under the treasury stock method to acquire 3,554 shares, 335,477 shares and 381,096 shares of common stock for the fiscal years ended March 31, 2009, 2008 and 2007, respectively, were potentially includable in the calculation of diluted loss per share but were not included, because to do so would be antidilutive.

**(o) Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America, requires management 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 revenue and expenses during the reporting period. Actual results could differ from those estimates.

**(p) Reclassifications**

Certain prior year amounts have been reclassified to conform to the current year presentation.

**(q) New Accounting Pronouncements**

In September 2006, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* ("SFAS No. 157"). SFAS No. 157 defines fair value, establishes a framework for measuring fair value and requires additional disclosures about fair value measurements. In February 2008, the FASB issued FASB Staff Position (FSP) 157-2, *Effective Date of FASB Statement No. 157* which delayed the effective date of SFAS No. 157 for all nonrecurring fair value measurements of nonfinancial assets and liabilities. We adopted the provisions of SFAS No. 157 related to financial instruments on April 1, 2008, and the provisions related to nonfinancial assets and liabilities on April 1, 2009 (except for those that are recognized or disclosed at fair value in the financial statements on a recurring basis). The provisions of this standard adopted by us on April 1, 2008 did not have a material effect on our financial statements and the adoption of the provisions effective April 1, 2009 will not have a material effect on our financial statements.

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 141 (revised 2007), *Business Combinations* ("FAS 141(R)") and Statement of Financial Accounting Standards No. 160, *Noncontrolling Interests in Consolidated Financial Statements* ("FAS 160"). These standards goals are to improve, simplify, and converge internationally the accounting for business combinations and the reporting of noncontrolling interests in consolidated financial statements. The provisions of FAS 141(R) and FAS 160 are effective for our fiscal year beginning April 1, 2009. We intend to adopt these standards for future acquisitions after the effective date.

In April 2008, the FASB issued FASB Staff Position (FSP) 142-3, *Determination of the Useful Life of Intangible Assets* ("FSP 142-3"). FSP 142-3 amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under SFAS No. 142, *Goodwill and Other Intangible Assets*. FSP 142-3 is effective for fiscal years beginning after December 15, 2008. The adoption of this standard will not have a material effect on our financial statements.

In May 2008, the FASB issued Statement of Financial Accounting Standards No. 162, *The Hierarchy of Generally Accepted Accounting Principles* ("SFAS No. 162"). SFAS No. 162 identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements. SFAS No. 162 is effective 60 days following the SEC's approval of the Public Company Accounting Oversight Board amendments to AU Section 411, *The Meaning of Present Fairly in Conformity with Generally Accepted Accounting Principles*". The adoption of this standard will not have a material effect on our

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**Notes to Consolidated Financial Statements, Continued**

financial statements.

In June 2008, the FASB ratified Emerging Issues Task Force (EITF) Issue No. 08-3, *Accounting for Lessees for Maintenance Deposits Under Lease Arrangements ("EITF 08-3")*. EITF 08-3 provides guidance for accounting for nonrefundable maintenance deposits. It also provides revenue recognition accounting guidance for the lessor. EITF 08-3 is effective for fiscal years beginning after December 15, 2008. The adoption of this EITF will not have a material effect on our financial statements.

In October 2008, the FASB issued FASB Staff Position (FSP) 157-3, *Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active ("FSP 157-3")*. FSP 157-3 clarifies the application of SFAS No. 157 in a market that is not active, and addresses application issues such as the use of internal assumptions when relevant observable data does not exist, the use of observable market information when the market is not active, and the use of market quotes when assessing the relevance of observable and unobservable data. FSP 157-3 is effective for all periods presented in accordance with SFAS No. 157. The adoption of FSP 157-3 did not have a material effect on our financial statements.

In April 2009, the FASB issued FASB Staff Position (FSP) 157-4, *Determining Fair Value When Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly ("FSP 157-4")*. FSP 157-4 provides guidance on how to determine the fair value of assets and liabilities when the volume and level of activity for the asset/liability has significantly decreased. FSP 157-4 also provides guidance on identifying circumstances that indicate a transaction is not orderly. In addition, FSP 157-4 requires disclosure in interim and annual periods of the inputs and valuation techniques used to measure fair value and a discussion of changes in valuation techniques. FSP 157-4 is effective for us beginning in the first quarter of fiscal year 2010. The adoption of FSP 157-4 will not have a material impact on our consolidated financial statements.

In April 2009, the FASB issued FASB Staff Position (FSP) 115-2 and Statement of Financial Accounting Standards (FAS) No. 124-2, *Recognition and Presentation of Other-Than-Temporary Impairment ("FSP 115-2/FAS No. 124-2")*. FSP 115-2/FAS No. 124-2 amends the requirements for the recognition and measurement of other-than-temporary impairments for debt securities by modifying the pre-existing "intent and ability" indicator. Additionally, FSP 115-2/FAS No. 124-2 changes the presentation of an other-than-temporary impairment in the income statement for those impairments involving credit losses. FSP 115-2/FAS No. 124-2 is effective for us beginning in the first quarter of fiscal year 2010. The adoption of this standard will not have a material effect on our financial statements.

In April 2009, the FASB issued FASB Staff Position (FSP) 107-1 and Accounting Principals Board (APB) Opinion 28-1, *Interim Disclosure about Fair Value of Financial Instruments ("FSP 107-1/APB 28-1")*. FSP 107-1/APB 28-1 requires interim disclosures regarding the fair values of financial instruments that are within the scope of FAS 107, *Disclosures about the Fair Value of Financial Instruments*. Additionally, FSP 107-1/APB 28-1 requires disclosure of the methods and significant assumptions used to estimate the fair value of financial instruments on an interim basis as well as changes of the methods and significant assumptions from prior periods. FSP 107-1/APB 28-1 does not change the accounting treatment for these financial instruments and is effective for us beginning in the first quarter of fiscal year 2010. The adoption of this standard will not have a material effect on our financial statements.

**(2) Stock Based Compensation**

*Stock Option Plans*

As of March 31, 2009 we had 805,966 shares of common stock available for future grant to employees, consultants and key suppliers under our 2002 Equity Incentive Plan ("Plan"). Under the Plan, the exercise price of each option is set at the fair value of the common stock on the date of grant and the maximum term of the option is 10 years from the date of grant. Options granted to employees generally vest ratably over a three-year period. The maximum

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number of options that may be granted to an employee under the Plan in any calendar year is 500,000 options. Forfeitures under the Plan are available for re-issuance at any time prior to expiration of the Plan in 2013. Options granted under the Plan to employees require the option holder to abide by certain Company policies, which restrict their ability to sell the underlying common stock. Prior to the adoption of the Plan, we issued stock options under our 1992 Incentive and Non-Qualified Option Plan, which expired by its terms in 2002. Forfeitures under the 1992 Incentive and Non-Qualified Option Plan may not be re-issued.

Non-Employee Director Stock Option Plan

In February 1994 our Board of Directors ratified a Stock Option Plan for Non-Employee Directors (“Directors Plan”) pursuant to which Directors may elect to receive stock options in lieu of cash compensation for their services as directors. As of March 31, 2009, we had 204,304 shares of common stock available for future grant under the Directors Plan. Option terms range from 3 to 10 years from the date of grant. Option exercise prices are equal to the fair value of the common shares on the date of grant. Options granted under the plan generally vest immediately. Forfeitures under the Directors Plan are available for re-issuance at a future date.

Stock Purchase Plan

We have established a Stock Purchase Plan under which eligible employees may contribute up to 10 percent of their compensation to purchase shares of our common stock at 85 percent of the fair market value at specified dates. As of March 31, 2009 we had 67,969 shares of common stock available for issuance under the Stock Purchase Plan. During the years ended March 31, 2009, 2008 and 2007, respectively, 22,268, 14,664 and 7,095 shares of common stock were issued under the Stock Purchase Plan. Cash received by us upon the issuance of shares under the Stock Purchase Plan for the years ended March 31, 2009, 2008 and 2007, was \$34, 217, \$40,790 and \$17,766, respectively.

Stock Bonus Plan

We have a Stock Bonus Plan (“Stock Plan”) administered by the Board of Directors. As of March 31, 2009 there were 6,794 shares of common stock available for future grant under the Stock Plan. Under the Stock Plan, shares of common stock may be granted to employees, key consultants, and directors who are not employees as additional compensation for services rendered. Vesting requirements for grants under the Stock Plan, if any, are determined by the Board of Directors at the time of grant. There were 191,348 and 204,558 shares granted under the Stock Plan during the years ended March 31, 2009, and March 31, 2008, respectively.

We use the straight-line attribution method to recognize share-based compensation costs over the requisite service period of the award. Options granted by us generally expire ten years from the grant date. Options granted to existing and newly hired employees generally vest over a three-year period from the date of the grant. The exercise price of options is equal to the market price of our common stock (defined as the closing price reported by the NYSE Amex) on the date of grant.

We use the Black-Scholes-Merton option pricing model for estimating the fair value of stock option awards. Total share-based compensation expense and the classification of these expenses for the last three fiscal years were as follows:

	Year Ended <u>March 31, 2009</u>	Year Ended <u>March 31, 2008</u>	Year Ended <u>March 31, 2007</u>
Cost of contract services	\$ 110,329	113,507	154,828
Cost of product sales	84,875	60,933	48,606
Research and development	37,903	25,652	22,612
Production engineering	128,553	132,494	113,013
Selling, general and administrative	<u>711,383</u>	<u>842,349</u>	<u>618,697</u>
	<u>\$ 1,073,043</u>	<u>1,174,935</u>	<u>957,756</u>

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Share-based compensation capitalized in inventories was insignificant as of March 31, 2009 and 2008.

In accordance with SFAS No. 123(R), we adjust share-based compensation on a quarterly basis for changes to the estimate of expected equity award forfeitures based on actual forfeiture experience. The effect of adjusting the forfeiture rate for all expense amortization is recognized in the period the forfeiture estimate is changed. The effect of forfeiture adjustments during the years ended March 31, 2009, 2008 and 2007 was insignificant.

All options granted under the Non-Employee Director Stock Option Plan are vested. A summary of the status of non-vested shares under the Equity Incentive Plan as of March 31, 2009, 2008 and 2007, and changes during the years ended March 31, 2009, 2008 and 2007 are presented below:

	Year Ended March 31, 2009		Year Ended March 31, 2008		Year Ended March 31, 2007	
	Shares Under Option	Weighted- Average Grant Date Fair Value	Shares Under Option	Weighted- Average Grant Date Fair Value	Shares Under Option	Weighted- Average Grant Date Fair Value
Non-vested at March 31	337,888	\$ 1.85	554,940	\$ 1.71	926,197	\$ 1.61
Granted	-	\$ -	-	\$ -	-	\$ -
Vested	(10,000)	\$ 2.10	(10,000)	\$ 2.10	(10,000)	\$ 2.10
Forfeited	<u>(2,000)</u>	\$ 1.61	<u>(2,387)</u>	\$ 2.01	<u>(14,481)</u>	\$ 1.17
Non-vested at June 30	325,888	\$ 1.84	542,553	\$ 1.70	901,716	\$ 1.61
Granted	381,615	\$ 1.08	106,159	\$ 1.89	119,605	\$ 1.53
Vested	(72,588)	\$ 1.69	(39,702)	\$ 1.52	-	\$ -
Forfeited	<u>(1,500)</u>	\$ 1.61	<u>(2,000)</u>	\$ 1.61	<u>(48,276)</u>	\$ 1.59
Non-vested at September 30	633,415	\$ 1.40	607,010	\$ 1.75	973,045	\$ 1.60
Granted	-	\$ -	-	\$ -	-	\$ -
Vested	(346,294)	\$ 1.39	(246,455)	\$ 1.63	(252,117)	\$ 1.63
Forfeited	-	\$ -	<u>(2,000)</u>	\$ 1.61	-	\$ -
Non-vested at December 31	287,121	\$ 1.41	358,555	\$ 1.83	720,928	\$ 1.60
Granted	-	\$ -	6,000	\$ 1.03	5,000	\$ 2.69
Vested	(3,667)	\$ 1.78	(26,667)	\$ 1.41	(165,520)	\$ 1.23
Forfeited	-	\$ -	-	\$ -	<u>(5,468)</u>	\$ 1.78
Non-vested at March 31	<u>283,454</u>	\$ <u>1.40</u>	<u>337,888</u>	\$ <u>1.85</u>	<u>554,940</u>	\$ <u>1.71</u>

As of March 31, 2009, there was \$266,896 of total unrecognized compensation costs related to stock options granted under our stock option plans. The unrecognized compensation cost is expected to be recognized over a weighted average period of 22 months. The total fair value of stock options that vested during the years ended March 31, 2009, 2008 and 2007 was \$633,106, \$519,978 and \$635,894, respectively.

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A summary of the non-vested shares under the Stock Bonus Plan as of March 31, 2009 and 2008 and changes during the years ended March 31, 2009, 2008 and 2007 is presented below:

	Year Ended March 31, 2009		Year Ended March 31, 2008		Year Ended March 31, 2007	
	Shares Under Contract	Weighted- Average Grant Date Fair Value	Shares Under Contract	Weighted- Average Grant Date Fair Value	Shares Under Contract	Weighted- Average Grant Date Fair Value
Non-vested at March 31	283,480	\$ 3.34	136,035	\$ 3.20	-	\$ -
Granted	-	\$ -	-	\$ -	-	\$ -
Vested	-	\$ -	-	\$ -	-	\$ -
Forfeited	-	\$ -	-	\$ -	-	\$ -
Non-vested at June 30	283,480	\$ 3.34	136,035	\$ 3.20	-	\$ -
Granted	191,348	\$ 2.18	-	\$ -	149,735	\$ 3.20
Vested	(184,692)	\$ 2.43	(45,349)	\$ 3.20	(12,500)	\$ 3.20
Forfeited	-	\$ -	-	\$ -	(1,200)	\$ 3.20
Non-vested at September 30	290,136	\$ 3.15	90,686	\$ 3.20	136,035	\$ 3.20
Granted	-	\$ -	204,558	\$ 3.40	-	\$ -
Vested	(64,266)	\$ 3.40	(11,764)	\$ 3.40	-	\$ -
Forfeited	-	\$ -	-	\$ -	-	\$ -
Non-vested at December 31	225,870	\$ 3.08	283,480	\$ 3.34	136,035	\$ 3.20
Granted	-	\$ -	-	\$ -	-	\$ -
Vested	-	\$ -	-	\$ -	-	\$ -
Forfeited	-	\$ -	-	\$ -	-	\$ -
Non-vested at March 31	<u>225,870</u>	<u>\$ 3.08</u>	<u>283,480</u>	<u>\$ 3.34</u>	<u>136,035</u>	<u>\$ 3.20</u>

As of March 31, 2009 there was \$184,997 of total unrecognized compensation costs related to common stock granted under our Stock Bonus Plan. The unrecognized compensation cost is expected to be recognized over a weighted average period of 23 months. The total fair value of common stock granted under the Stock Bonus Plan that vested during the years ended March 31, 2009, 2008 and 2007 was \$667,384, \$185,114 and \$40,000, respectively.

During the years ended March 31, 2009, 2008 and 2007 options to acquire 550,358, 201,060 and 148,344 shares of common stock, respectively, were granted under our Equity Incentive and Non-Employee Director Stock Option Plans. The weighted average estimated values of employee and director stock option grants, as well as the weighted average assumptions that were used in calculating such values during the years ended March 31, 2009, 2008 and 2007, were based on estimates at the date of grant as follows:

	Year Ended March 31,		
	2009	2008	2007
Weighted average estimated fair value of grant	\$ 2.19 Per option	3.41 Per option	3.24 Per option
Expected life (in years)	3.4 years	3.3 years	3.5 years
Risk free interest rate	3.20 %	4.17 %	4.9 %
Expected volatility	60.56 %	60.03 %	59.7 %
Expected dividend yield	0.0 %	0.0 %	0.0 %

Expected volatility is based on historical volatility. The expected life of options granted prior to January 1, 2008 was based on the simplified calculation of expected life described in the U.S. Securities and Exchange Commission's Staff Accounting Bulletin 107 ("SAB 107"). In addition, options granted to members of the board of directors and executives on July 23, 2008 with option terms of less than ten years utilize the simplified calculation

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of expected life described by SAB 107 because we do not have sufficient historical experience for option grants with option terms of less than ten years. The expected life of all other options granted subsequent to December 31, 2007 are based on historical experience.

Additional information with respect to stock option activity during the year ended March 31, 2009 under our incentive and non-qualified stock option plans is as follows:

	<u>Shares Under Option</u>	<u>Weighted Average Exercise Price</u>	<u>Weighted Average Remaining Contractual Life</u>	<u>Aggregate Intrinsic Value</u>
Outstanding at March 31, 2008	2,543,306	\$ 3.94	5.2 years	\$ -
Granted	-	\$ -		
Exercised	-	\$ -		\$ <u>-</u>
Forfeited	<u>(2,000)</u>	\$ 3.57		
Outstanding at June 30, 2008	2,541,306	\$ 3.94	5.0 years	\$ 3,060
Granted	381,615	\$ 2.18		
Exercised	-	\$ -		\$ <u>-</u>
Forfeited	<u>(1,500)</u>	\$ 3.57		
Outstanding at September 30, 2008	2,921,421	\$ 3.71	4.9 years	\$ 584,914
Granted	-	\$ -		
Exercised	-	\$ -		\$ <u>-</u>
Forfeited	<u>-</u>	\$ -		
Outstanding at December 31, 2008	2,921,421	\$ 3.71	4.6 years	\$ -
Granted	-	\$ -		
Exercised	-	\$ -		\$ <u>-</u>
Forfeited	<u>(180,606)</u>	\$ 4.38		
Outstanding at March 31, 2009	<u>2,740,815</u>	\$ <u>3.66</u>	<u>4.7 years</u>	\$ <u>-</u>
Exercisable at March 31, 2009	<u>2,457,361</u>	\$ <u>3.78</u>	<u>4.5 years</u>	\$ <u>-</u>
Vested and expected to vest at March 31, 2009	<u>2,726,859</u>	\$ <u>3.67</u>	<u>4.6 years</u>	\$ <u>-</u>

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Additional information with respect to stock option activity during the year ended March 31, 2008 under our incentive and non-qualified stock option plans is as follows:

	<u>Shares Under Option</u>	<u>Weighted Average Exercise Price</u>	<u>Weighted Average Remaining Contractual Life</u>	<u>Aggregate Intrinsic Value</u>
Outstanding at March 31, 2007	2,692,400	\$ 4.33	5.7 years	\$ 1,972,876
Granted	-	\$ -		
Exercised	(1,599)	\$ 2.41		\$ <u>2,942</u>
Forfeited	<u>(3,579)</u>	\$ 2.68		
Outstanding at June 30, 2007	2,687,222	\$ 4.33	5.4 years	\$ 2,070,665
Granted	106,159	\$ 3.57		
Exercised	(4,245)	\$ 2.41		\$ <u>8,193</u>
Forfeited	<u>(2,000)</u>	\$ 3.57		
Outstanding at September 30, 2007	2,787,136	\$ 4.30	5.2 years	\$ 1,343,718
Granted	-	\$ -		
Exercised	-	\$ -		\$ <u>-</u>
Forfeited	<u>(2,000)</u>	\$ 3.57		
Outstanding at December 31, 2007	2,785,136	\$ 4.30	5.0 years	\$ 1,006,016
Granted	6,000	\$ 1.69		
Exercised	-	\$ -		\$ <u>-</u>
Forfeited	<u>(247,830)</u>	\$ 8.00		
Outstanding at March 31, 2008	<u>2,543,306</u>	<u>\$ 3.94</u>	<u>5.2 years</u>	\$ <u>-</u>
Exercisable at March 31, 2008	<u>2,205,418</u>	<u>\$ 3.99</u>	<u>4.9 years</u>	\$ <u>-</u>
Vested and expected to vest at March 31, 2008	<u>2,523,959</u>	<u>\$ 3.94</u>	<u>5.2 years</u>	\$ <u>-</u>

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Additional information with respect to stock option activity during the year ended March 31, 2007 under our incentive and non-qualified stock option plans is as follows:

	<u>Shares Under Option</u>	<u>Weighted Average Exercise Price</u>	<u>Weighted Average Remaining Contractual Life</u>	<u>Aggregate Intrinsic Value</u>
Outstanding at March 31, 2006	3,006,329	\$ 4.28		
Granted	-	\$ -		
Exercised	(186,814)	\$ 3.29		\$ <u>306,117</u>
Forfeited	<u>(9,037)</u>	\$ 2.26		
Outstanding at June 30, 2006	2,810,478	\$ 4.35	6.1 years	\$ 518,535
Granted	119,605	\$ 3.20		
Exercised	-	\$ -		
Forfeited	<u>(99,758)</u>	\$ 5.61		
Outstanding at September 30, 2006	2,830,325	\$ 4.26	6.0 years	\$ 330,706
Granted	-	\$ -		
Exercised	-	\$ -		
Forfeited	<u>(11,666)</u>	\$ 2.17		
Outstanding at December 31, 2006	2,818,659	\$ 4.27	5.7 years	\$ 307,679
Granted	5,000	\$ 4.31		
Exercised	(28,626)	\$ 2.43		\$ <u>51,606</u>
Forfeited	<u>(102,633)</u>	\$ <u>3.31</u>		
Outstanding at March 31, 2007	<u>2,692,400</u>	\$ <u>4.33</u>	<u>5.7 years</u>	\$ <u>1,972,876</u>
Exercisable at March 31, 2007	<u>2,137,460</u>	\$ <u>4.58</u>	<u>4.9 years</u>	\$ <u>1,540,910</u>
Vested and expected to vest at March 31, 2007	<u>2,666,940</u>	\$ <u>4.33</u>	<u>5.6 years</u>	\$ <u>1,957,156</u>

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Additional information with respect to stock option activity during the year ended March 31, 2009 under our non-employee director stock option plan is as follows:

	<u>Shares Under Option</u>	<u>Weighted Average Exercise Price</u>	<u>Weighted Average Remaining Contractual Life</u>	<u>Aggregate Intrinsic Value</u>
Outstanding at March 31, 2008	131,644	\$ 3.33	2.7 years	\$ -
Granted	-	\$ -		
Exercised	-	\$ -		\$ <u>-</u>
Forfeited	<u>-</u>	\$ -		
Outstanding at June 30, 2008	131,644	\$ 3.33	2.4 years	\$ 1,736
Granted	109,302	\$ 2.18		
Exercised	-	\$ -		\$ <u>-</u>
Forfeited	<u>(18,027)</u>	\$ 3.22		
Outstanding at September 30, 2008	222,919	\$ 2.77	3.2 years	\$ 71,345
Granted	59,441	\$ 3.39		
Exercised	-	\$ -		\$ <u>-</u>
Forfeited	<u>(59,441)</u>	\$ 3.39		
Outstanding at December 31, 2008	222,919	\$ 2.77	3.0 years	\$ -
Granted	-	\$ -		
Exercised	-	\$ -		\$ <u>-</u>
Forfeited	<u>-</u>	\$ -		
Outstanding at March 31, 2009	<u>222,919</u>	<u>\$ 2.77</u>	<u>2.7 years</u>	<u>\$ -</u>
Exercisable at March 31, 2009	<u>222,919</u>	<u>\$ 2.77</u>	<u>2.7 years</u>	<u>\$ -</u>
Vested and expected to vest at March 31, 2009	<u>222,919</u>	<u>\$ 2.77</u>	<u>2.7 years</u>	<u>\$ -</u>

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Additional information with respect to stock option activity during the year ended March 31, 2008 under our non-employee director stock option plan is as follows:

	Shares Under Option	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Aggregate Intrinsic Value
Outstanding at March 31, 2007	70,520	\$ 2.91	1.4 years	\$ 87,911
Granted	-	\$ -		
Exercised	-	\$ -		\$ <u>-</u>
Forfeited	<u>-</u>	\$ -		
Outstanding at June 30, 2007	70,520	\$ 2.91	1.2 years	\$ 92,083
Granted	24,039	\$ 3.57		
Exercised	(18,518)	\$ 2.30		\$ <u>21,111</u>
Forfeited	<u>(9,259)</u>	\$ 2.30		
Outstanding at September 30, 2007	66,782	\$ 3.40	2.0 years	\$ 21,111
Granted	57,918	\$ 3.40		
Exercised	-	\$ -		\$ <u>-</u>
Forfeited	<u>-</u>	\$ -		
Outstanding at December 31, 2007	124,700	\$ 3.40	2.8 years	\$ 7,614
Granted	6,944	\$ 1.95		
Exercised	-	\$ -		\$ <u>-</u>
Forfeited	<u>-</u>	\$ -		
Outstanding at March 31, 2008	<u>131,644</u>	<u>\$ 3.33</u>	<u>2.7 years</u>	\$ <u>-</u>
Exercisable at March 31, 2008	<u>131,644</u>	<u>\$ 3.33</u>	<u>2.7 years</u>	\$ <u>-</u>
Vested and expected to vest at March 31, 2008	<u>131,644</u>	<u>\$ 3.33</u>	<u>2.7 years</u>	\$ <u>-</u>

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Additional information with respect to stock option activity during the year ended March 31, 2007 under our non-employee director stock option plan is as follows:

	<u>Shares Under Option</u>	<u>Weighted Average Exercise Price</u>	<u>Weighted Average Remaining Contractual Life</u>	<u>Aggregate Intrinsic Value</u>
Outstanding at March 31, 2006	59,281	\$ 2.90	1.2 years	\$ 16,666
Granted	-	\$ -		
Exercised	-	\$ -		
Forfeited	<u>-</u>	<u>\$ -</u>		
Outstanding at June 30, 2006	59,281	\$ 2.90	1.2 years	\$ 16,666
Granted	23,739	\$ 3.20		
Exercised	-	\$ -		
Forfeited	<u>-</u>	<u>\$ -</u>		
Outstanding at September 30, 2006	83,020	\$ 2.99	1.6 years	\$ 12,222
Granted	-	\$ -		
Exercised	-	\$ -		
Forfeited	<u>-</u>	<u>\$ -</u>		
Outstanding at December 31, 2006	83,020	\$ 2.99	1.4 years	\$ 11,666
Granted	-	\$ -		
Exercised	-	\$ -		
Forfeited	(12,500)	\$ 3.40		
Outstanding at March 31, 2007	<u>70,520</u>	<u>\$ 2.91</u>	<u>1.4 years</u>	<u>\$ 87,911</u>
Exercisable at March 31, 2007	<u>70,520</u>	<u>\$ 2.91</u>	<u>1.4 years</u>	<u>\$ 87,911</u>
Vested and expected to vest at March 31, 2007	<u>70,520</u>	<u>\$ 2.91</u>	<u>1.4 years</u>	<u>\$ 87,911</u>

Cash received by us upon the exercise of stock options for the years ended March 31, 2009, 2008 and 2007 was zero, \$56,675 and \$683,693, respectively. The source of shares of common stock issuable upon the exercise of stock options is from authorized and previously unissued common shares.

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**(3) Costs and Estimated Earnings in Excess of Billings on Uncompleted Contracts and Billings in Excess of Costs and Estimated Earnings on Uncompleted Contracts**

At March 31, 2009, the estimated period to complete contracts in process ranged from one to six months, and we expect to collect substantially all related accounts receivable arising therefrom within sixty days of billing.

The following summarizes contracts in process:

	<u>March 31, 2009</u>	<u>March 31, 2008</u>
Costs incurred on uncompleted contracts	\$ 4,414,886	3,018,470
Estimated earnings	<u>194,861</u>	<u>377,822</u>
	4,609,747	3,396,292
Less billings to date	<u>(4,038,016)</u>	<u>(3,454,470)</u>
	<u>\$ 571,731</u>	<u>(58,178)</u>
Included in the accompanying balance sheets as follows:		
Costs and estimated earnings in excess of billings on uncompleted contracts	\$ 643,098	649,670
Billings in excess of costs and estimated earnings on uncompleted contracts	<u>(71,367)</u>	<u>(707,848)</u>
	<u>\$ 571,731</u>	<u>(58,178)</u>

**(4) Inventories**

Inventories consist of:

	<u>March 31, 2009</u>	<u>March 31, 2008</u>
Raw materials	\$ 794,663	721,291
Work-in-process	419,270	179,385
Finished products	<u>93,238</u>	<u>60,813</u>
	<u>\$ 1,307,171</u>	<u>961,489</u>

Our raw material inventory is subject to obsolescence and potential impairment due to bulk purchases in excess of customers' requirements. We periodically assess our inventory for recovery of its carrying value based on available information, expectations and estimates, and adjust inventory carrying-value to the lower of cost or market for estimated declines in the realizable value. For the fiscal year ended March 31, 2009 we impaired obsolete inventory with a carrying value of \$41,613.

**(5) Impairment of Long-Lived Assets**

During the fiscal years ended March 31, 2009, 2008 and 2007, we recorded total impairment charges of zero, \$11,155 and \$889, respectively, for obsolete equipment and abandoned patent applications.

Average annual depreciation expense for the equipment impaired during the fiscal year ended March 31, 2008, for years preceding the year of impairment, was \$4,308.

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**(6) Patents and Trademarks**

Intangible assets, which consist entirely of patents and trademarks owned by the Company, had a gross carrying amount of \$1,171,778 and \$1,155,722, accumulated amortization of \$733,594 and \$677,957, and a net carrying amount of \$438,184 and \$477,765, at March 31, 2009 and 2008, respectively. Amortization expense for the years ended March 31, 2009, 2008 and 2007, was \$55,637, \$55,637 and \$76,852, respectively. Patents and trademarks are amortized on a straight-line basis over a period of 17 years and 40 years, respectively.

Estimated future amortization of these intangible assets is as follows:

2010	\$ 54,906
2011	47,207
2012	39,493
2013	38,363
2014	34,221
Thereafter	<u>223,994</u>
	<u>\$ 438,184</u>

**(7) Other Current Liabilities**

Other current liabilities consist of:

	<u>March 31, 2009</u>	<u>March 31, 2008</u>
Accrued payroll and employee benefits	\$ 165,221	125,677
Accrued personal property and real estate taxes	82,396	58,184
Accrued warranty costs	84,445	117,645
Accrued losses on engineering contracts	520	5,209
Unearned revenue	149,355	20,690
Accrued royalties	73,773	33,923
Other	<u>44,962</u>	<u>10,957</u>
	<u>\$ 600,672</u>	<u>372,285</u>

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**(8) Long-Term Debt**

Long-term debt consists of:

	<u>March 31, 2009</u>	<u>March 31, 2008</u>
Note payable to bank, payable in monthly installments with interest at 7.0%; matures November 2009; secured by land and building	\$ <u>416,923</u>	<u>522,925</u>

**(9) Income Taxes**

Income tax benefit attributable to loss from operations differed from the amounts computed by applying the U.S. federal income tax rate of 34 percent as a result of the following:

	<u>Year Ended March 31, 2009</u>	<u>Year Ended March 31, 2008</u>	<u>Year Ended March 31, 2007</u>
Computed "expected" tax benefit	\$(1,497,208)	(1,554,700)	(1,156,872)
Increase (decrease) in taxes resulting from:			
Adjustment of expiring net operating loss carry-forwards	1,450,222	1,124,302	825,774
Adjustment to deferred tax assets and liabilities for prior period corrections	-	(104,562)	865,148
Increase (decrease) in valuation allowance for net deferred tax assets	(67,423)	588,902	(525,326)
Other, net	<u>114,409</u>	<u>(53,942)</u>	<u>(8,724)</u>
Income tax benefit	\$ <u>-</u>	<u>-</u>	<u>-</u>

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The tax effects of temporary differences that give rise to significant portions of the net deferred tax asset are presented below:

	<u>March 31, 2009</u>	<u>March 31, 2008</u>
Deferred tax assets:		
Research and development credit carry-forwards	\$ 113,471	130,798
Net operating loss carry-forwards	20,050,531	20,259,647
Deferred compensation	397,835	369,790
Property and equipment	333,382	343,429
Intangible assets	6,180	-
Stock compensation	383,514	363,974
Other	<u>126,658</u>	<u>26,197</u>
Total deferred tax assets	21,411,571	21,493,835
Deferred tax liabilities:		
Intangible assets	<u>-</u>	<u>14,841</u>
Total deferred tax liabilities	-	14,841
Net deferred tax assets	21,411,571	21,478,994
Less valuation allowance	<u>(21,411,571)</u>	<u>(21,478,994)</u>
Net deferred tax assets, net of valuation allowance	\$ <u>-</u>	<u>-</u>

As of March 31, 2009 we had net operating loss carry-forwards (NOL) of approximately \$59 million for U.S. income tax purposes that expire in varying amounts through 2029. Approximately \$4.5 million of the net operating loss carry-forwards are attributable to stock options, the benefit of which will be credited to additional paid-in capital if realized. However, due to the provisions of Section 382 of the Internal Revenue Code, the utilization of a portion of these NOLs may be limited. Future ownership changes under Section 382 could occur that would result in additional Section 382 limitations, which could further restrict the use of NOLs. In addition, any Section 382 limitation could reduce our ability for utilization to zero if we fail to satisfy the continuity of business enterprise requirement for the two-year period following an ownership change.

The valuation allowance for deferred tax assets of \$21.4 million and \$21.5 million at March 31, 2009 and March 31, 2008, respectively, relates principally to the uncertainty of the utilization of certain deferred tax assets, primarily net operating loss carry forwards in various tax jurisdictions. The Company continually assesses both positive and negative evidence to determine whether it is more-likely-than-not that the deferred tax assets can be realized prior to their expiration. Based on the Company's assessment it has determined the deferred tax assets are not currently realizable.

**(10) Stockholders' Equity**

In June 2007 we completed a private placement of 1,250,000 shares of our common stock to two institutional investors. Cash proceeds, net of offering costs, were \$5,183,677.

In November 2004 we completed a follow-on offering of 3,600,000 shares of our common stock. The placement agent was issued four-year warrants to acquire 360,000 shares of common stock at an exercise price of \$2.58 per share, which were recorded at fair value. Cash proceeds, net of offering costs, were \$6,767,465. Warrants to acquire zero and 85,267 shares of our common stock were outstanding at March 31, 2009 and 2008, respectively.

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**(11) Significant Customers**

We have historically derived significant revenue from a few key customers. Revenue from Quantum Fuel Systems Technologies Worldwide Inc. totaled \$1,360,909, \$256,393 and zero for the years ended March 31, 2009, 2008 and 2007, respectively, which was 16 percent, 3 percent and nil of total consolidated revenue, respectively. Revenue from Invacare Corporation totaled \$292,414, \$508,903 and \$830,637 for the years ended March 31, 2009, 2008 and 2007, respectively, which was 3 percent, 7 percent and 12 percent of total revenue, respectively. Revenue from Lippert Components, Inc. totaled \$635,144, \$1,271,502 and \$1,059,930 for the years ended March 31, 2009, 2008 and 2007, respectively, which was 7 percent, 17 percent and 16 percent of total revenue, respectively. Revenue from the Denver Regional Transportation District totaled \$3,337, \$864,540 and \$417,750 for the years ended March 31, 2009, 2008 and 2007, respectively, which was nil, 12 percent and 6 percent of total revenue, respectively.

Trade accounts receivable from Quantum Fuel Systems Technologies Worldwide Inc. were 16 percent and 8 percent of total accounts receivable as of March 31, 2009 and 2008, respectively. Inventories consisting of raw materials, work-in-progress and finished goods for this customer totaled zero as of March 31, 2009 and 2008. Trade accounts receivable from Invacare Corporation were 2 percent and 16 percent of total accounts receivable as of March 31, 2009 and 2008, respectively. Inventories consisting of raw materials, work-in-progress and finished goods for this customer totaled zero and \$45,615 as of March 31, 2009 and 2008, respectively. Trade accounts receivable from Lippert Components, Inc. were nil and 8 percent of total accounts receivable as of March 31, 2009 and 2008, respectively. Inventories consisting of raw materials, work-in-progress and finished goods for this customer totaled \$349,066 and \$211,571 as of March 31, 2009 and 2008, respectively. Trade accounts receivable from the Denver Regional Transportation District were nil and 20 percent of total accounts receivable as of March 31, 2009 and 2008, respectively. Inventories consisting of raw materials, work-in-progress and finished goods for this customer totaled zero as of March 31, 2009 and 2008.

Contract services revenue derived from contracts with agencies of the U.S. Government and from subcontracts with U.S. Government prime contractors totaled \$1,989,872, \$2,329,248 and \$2,313,856 for the years ended March 31, 2009, 2008 and 2007, respectively, which was 23 percent, 31 percent and 35 percent of total consolidated revenue, respectively. Accounts receivable from government-funded contracts represented 6 percent and 12 percent of total accounts receivable as of March 31, 2009 and 2008, respectively.

**(12) Fair Value of Financial Instruments**

The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

*Cash and cash equivalents, certificates of deposit, accounts receivable and accounts payable:*

The carrying amounts approximate fair value because of the short maturity of these instruments.

*Short-term investments:*

The carrying value of these instruments is the amortized cost of short-term investments which approximates fair value. See Note 1(d).

*Long-term debt:*

The carrying amount of our long-term debt approximates fair value because the interest rate on this debt approximates the interest rate currently available on similar financing offering comparable security to the lender.

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**(13) Fair Value Measurements**

Liabilities measured at fair value on a recurring basis as of March 31, 2009 are summarized below:

	<u>Total</u>	<u>Fair Value Measurements at Reporting Date Using</u>		
		<u>Quoted Prices In Active Markets For Identical Liabilities (Level 1)</u>	<u>Significant Other Observable Inputs (Level 2)</u>	<u>Significant Unobservable Inputs (Level 3)</u>
Deferred Compensation under executive employment agreements <sup>(1)</sup>	\$ 1,073,549	-	-	1,073,549

*Note(1) \$397,834 included in current liabilities and \$675,715 included in long term liabilities on our consolidated balance sheet as of March 31, 2009.*

Liabilities measured at fair value on a recurring basis as of March 31, 2008 are summarized below:

	<u>Total</u>	<u>Fair Value Measurements at Reporting Date Using</u>		
		<u>Quoted Prices In Active Markets For Identical Liabilities (Level 1)</u>	<u>Significant Other Observable Inputs (Level 2)</u>	<u>Significant Unobservable Inputs (Level 3)</u>
Deferred Compensation under executive employment agreements <sup>(1)</sup>	\$ 997,873	-	-	997,873

*Note(1) \$364,000 included in current liabilities and \$633,873 included in long term liabilities on our consolidated balance sheet as of March 31, 2008.*

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Deferred compensation under executive employment agreements represents the future compensation potentially payable under the retirement and voluntary termination provisions of executive employment agreements. The value of the Level 3 liability in the foregoing table was determined under the income approach, using inputs that are both unobservable and significant to the value of the obligation including changes in the company's credit worthiness and changes in interest rates.

A summary of the liability measured at fair value on a recurring basis using significant unobservable inputs (Level 3) follows:

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3) for the Fiscal Year Ended	
	<u>March 31, 2009</u>	<u>March 31, 2008</u>
	Deferred Compensation On Executive Employment Agreements	Deferred Compensation On Executive Employment Agreements
Balance at beginning of fiscal year	\$ 997,873	545,539
Total gains or losses (realized and unrealized):		
Included in earnings	75,676	452,334
Included in other comprehensive income	-	-
Purchases, sales, issuances, and settlements, net	-	-
Transfers in (out) of Level 3	-	-
Balance at the end of fiscal year	<u>\$ 1,073,549</u>	<u>997,873</u>
Loss for the period included in earnings attributable to the Level 3 liability still held at the end of the period	<u>\$ 75,676</u>	<u>452,334</u>

**(14) 401(k) Employee Benefit Plan**

We have established a 401(k) Savings Plan ("401K Plan") under which eligible employees may contribute up to 15 percent of their compensation. Employees over the age of 18 who have been employed by us at least six months are eligible to participate in the 401K Plan. At the direction of the participants, contributions are invested in several investment options offered by the 401K Plan. We currently match 33 percent of participants' contributions, subject to certain limitations. These matching contributions vest ratably over a three-year period. Matching contributions to the 401K Plan were \$82,355, \$75,028 and \$65,658, for the years ended March 31, 2009, 2008, and 2007, respectively.

**(15) Segments**

At March 31, 2009, we had two reportable segments: technology and power products. Our reportable segments are strategic business units that offer different products and services. They are managed separately because each business requires different business strategies. The technology segment encompasses our technology-based operations including core research to advance our technology, application and production engineering and product development and job shop production of prototype components. The power products segment encompasses the manufacture and sale of permanent magnet motors and electronic controllers. Salaries of the executive officers and corporate general and administrative expense are allocated to our segments annually based on factors established at the beginning of each fiscal year. The percentage allocated to the technology segment and power products segment for the fiscal year ended March 31, 2009 was 76 percent and 24 percent, respectively. The percentage allocated to the technology segment and power products segment for the fiscal years ended March 31, 2008, and 2007 were 75

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percent and 25 percent, and 61 percent and 39 percent, in each year, respectively. Intersegment sales or transfers, which were eliminated upon consolidation, were \$970,277, \$710,416 and \$143,880 for the years ended March 31, 2009, 2008, and 2007, respectively.

The technology segment leases office, production and laboratory space in a building owned by the power products segment, based on a negotiated rate for the square footage occupied. Intercompany lease payments, were \$174,000, \$169,562 and \$184,164 for the years ended March 31, 2009, 2008, and 2007, respectively, and were eliminated upon consolidation.

The following table summarizes significant financial statement information after deducting intersegment eliminations of each of the reportable segments as of and for the year ended March 31, 2009:

	<u>Technology</u>	<u>Power Products</u>	<u>Total</u>
Revenue	\$ 5,455,934	3,272,377	8,728,311
Interest income	\$ 194,384	4,563	198,947
Interest expense	\$ -	(33,387)	(33,387)
Depreciation and amortization	\$ (312,154)	(234,689)	(546,843)
Impairment of long-lived assets	\$ -	-	-
Impairment of inventories	\$ (28,546)	(13,067)	(41,613)
Impairment of investment	\$ (89,369)	-	(89,369)
Segment loss	\$ (4,123,174)	(278,845)	(4,402,019)
Total assets	\$ 8,840,077	3,582,755	12,422,832
Expenditures for long-lived segment assets	\$ (579,932)	(7,110)	(587,042)

The following table summarizes significant financial statement information after deducting intersegment eliminations of each of the reportable segments as of and for the year ended March 31, 2008:

	<u>Technology</u>	<u>Power Products</u>	<u>Total</u>
Revenue	\$ 4,391,213	3,117,109	7,508,322
Interest income	\$ 454,466	8,782	463,248
Interest expense	\$ -	(40,652)	(40,652)
Depreciation and amortization	\$ (223,815)	(213,984)	(437,799)
Impairment of long-lived assets	\$ ( 820)	(10,335)	(11,155)
Impairment of inventories	\$ -	-	-
Impairment of investment	\$ -	-	-
Segment loss	\$ (3,874,639)	(711,466)	(4,586,105)
Total assets	\$ 12,511,384	3,891,162	16,402,546
Expenditures for long-lived segment assets	\$ (610,303)	(243,917)	(854,220)

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The following table summarizes significant financial statement information after deducting intersegment eliminations of each of the reportable segments as of and for the year ended March 31, 2007:

	<u>Technology</u>	<u>Power Products</u>	<u>Total</u>
Revenue	\$ 4,026,255	2,626,939	6,653,194
Interest income	\$ 439,460	6,118	445,578
Interest expense	\$ -	(47,422)	(47,422)
Depreciation and amortization	\$ (244,401)	(169,921)	(414,322)
Impairment of long-lived assets	\$ -	(889)	(889)
Impairment of inventories	\$ -	-	-
Impairment of investment	\$ -	-	-
Segment loss	\$ (2,870,307)	(561,050)	(3,431,357)
Total assets	\$ 10,168,939	3,843,668	14,012,607
Expenditures for long-lived segment assets	\$ (162,690)	(241,091)	(403,781)

**(16) Commitments and Contingencies**

**Employment Agreements**

The Company has entered into Employment Agreements with Messrs. Rankin, French, Burton and Lutz pursuant to which each has agreed to serve in his present capacity for a five year term expiring on August 22, 2012. Pursuant to the Employment Agreements, Messrs. Rankin, French, Burton and Lutz shall receive an annual base salary of \$327,000, \$217,000, \$195,000 and \$177,000, respectively. Each executive also receives the use of an automobile and may receive bonuses, stock awards and stock options.

Messrs. Rankin and French's Employment Agreements provide that if employment is terminated by the Company or the executive without cause during or after the term of the agreement upon attaining twenty years of service as an officer, or upon retirement after attaining age 62 1/2, the officer shall receive 24 months salary. If the officer voluntarily terminates his employment after attaining twenty years of service as an officer and provides at least six months notice, he shall receive one month of pay for each year of service as an officer up to a maximum payment of 24 months pay. If the executive has less than twenty years of service or does not provide at least six months notice, he shall receive three months salary, unless the Company is in default under the Agreement, which shall be considered termination by the Company without cause.

Messrs. Burton and Lutz's Employment Agreements provide that if employment is terminated by the Company or the executive without cause during or after the term of the agreement, the officer shall receive the greater of six months pay or one month of pay for each year of service as an officer. If the officer voluntarily terminates his employment and provides at least six months notice, he shall receive six months pay. If the executive does not provide at least six months notice, he shall receive two months salary, unless the Company is in default under the Agreement, which shall be considered termination by the Company without cause. If the Executive provides at least six months notice of his voluntary retirement after attaining 62 1/2 years of age, executive shall receive a total payment consisting of one month of pay for each year of service as an officer plus six months of pay, up to a maximum total payment of 24 months pay.

Messrs. Rankin, French, Burton and Lutz's Employment Agreements provide that upon termination by the Company following a hostile change of control of the Company, the officer shall receive twice the payment due on a termination by the Company. If an officer dies during employment, his estate shall receive three months compensation. If the officer elects to retire at 62 1/2 years of age or upon attaining 20 years of service with the Company, the officer shall be entitled to continue to participate in the Company's group health insurance plan (at the same cost as employees) until attaining age 65.

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The employment agreements further provide that the Company shall maintain at its expense, life insurance coverage on Messrs. Rankin, French, Burton and Lutz payable to their designees in an amount equal to three times the annual compensation payable to each executive.

The aggregate future base salary payable to these four executive officers under the Employment Agreements over their remaining forty-one month term is \$3,129,667. In addition, the Company has recorded a liability of \$1,073,549 representing the potential future compensation payable to Messrs. Rankin, French, Burton and Lutz under the retirement and voluntary termination provisions of their Employment Agreements.

**Lease Commitments**

At March 31, 2009 there were no operating leases with initial non-cancelable terms in excess of one year.

Rental expense, after deducting sublease payments of zero, zero and \$185,500 for the years ended March 31, 2009, 2008 and 2007, respectively, was \$59,648, \$59,400 and \$66,644.

**Litigation**

In November 2007, we filed an arbitration claim with the American Arbitration Association ("AAA") against Phoenix MC, Inc., as successor by merger to Phoenix Motorcars, Inc. ("Phoenix") seeking damages for Phoenix's breach of the Purchase and Supply Agreement between Phoenix and UQM Technologies, Inc. dated January 12, 2007. The matter was heard by an AAA arbitration panel (the "Panel") in December 2008. On February 24, 2009, the AAA notified us of the Panel's findings that Phoenix had materially breached the Agreement and awarded monetary damages to us in the amount of \$5,309,649. In addition, the Panel awarded us post-award interest at the rate of 10 percent per annum on the unpaid amount of the award subsequent to February 6, 2009. On April 27, 2009, Phoenix filed a Chapter 11 Bankruptcy petition with the U.S. Bankruptcy Court. As a result of the bankruptcy filing, efforts to collect on the arbitration award are stayed. At this time, whether, to what extent, and when, we will be able to recover any of the amounts that Phoenix owes is uncertain.

We are involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, and based on current available information, the ultimate disposition of these matters is not expected to have a material adverse effect on our financial position, results of operations or cash flow, although adverse developments in these matters could have a material impact on a future reporting period.

**(17) Interim Financial Data (Unaudited)**

	<u>Quarters Ended</u>			
	<u>June 30</u>	<u>September 30</u>	<u>December 31</u>	<u>March 31</u>
<u>Fiscal year 2009</u>				
Sales	\$ 1,793,355	2,277,331	2,873,595	1,784,030
Gross profit	\$ 194,260	415,114	863,560	292,710
Net loss	\$ (999,715)	(1,538,111)	(764,101)	(1,100,092)
Net loss per common share basic and diluted:	\$( <u>0.04</u> )	( <u>0.06</u> )	( <u>0.03</u> )	( <u>0.04</u> )

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	<u>Quarters Ended</u>			
	<u>June 30</u>	<u>September 30</u>	<u>December 31</u>	<u>March 31</u>
<u>Fiscal year 2008</u>				
Sales	\$ 1,454,452	1,990,591	1,714,858	2,348,421
Gross profit	\$ 28,903	363,902	273,570	410,488
Net loss	\$ (1,128,751)	(1,139,894)	(1,306,996)	(1,010,464)
Net loss per common share basic and diluted:	\$( <u>0.05</u> )	( <u>0.04</u> )	( <u>0.05</u> )	( <u>0.04</u> )

	<u>Quarters Ended</u>			
	<u>June 30</u>	<u>June 30</u>	<u>June 30</u>	<u>June 30</u>
<u>Fiscal year 2007</u>				
Sales	\$ 1,301,332	1,614,218	1,726,526	2,011,118
Gross profit	\$ 122,131	121,840	153,186	266,144
Net loss	\$ (762,796)	(879,570)	(824,019)	(964,972)
Net loss per common share basic and diluted:	\$( <u>0.03</u> )	( <u>0.04</u> )	( <u>0.03</u> )	( <u>0.04</u> )

**(18) Valuation and Qualifying Accounts**

	<u>Additions</u>				<u>Balance at End of Year</u>
	<u>Balance at Beginning of Year</u>	<u>Charged to Costs and Expenses</u>	<u>Charged to Other Accounts</u>	<u>Deductions</u>	
<u>Year ended March 31, 2009</u>					
Not deducted from asset accounts:					
Accrued warranty cost	\$ 117,645	121,776	-	154,976 <sup>(A)</sup>	84,445
<u>Year ended March 31, 2008</u>					
Not deducted from asset accounts:					
Accrued warranty cost	\$ 74,850	98,434	-	55,639 <sup>(A)</sup>	117,645
<u>Year ended March 31, 2007</u>					
Not deducted from asset accounts:					
Accrued warranty cost	\$ 39,480	85,955	-	50,585 <sup>(A)</sup>	74,850

*Note (A) Represents actual warranty payments for units returned under warranty.*