KIRBY CORP
Form 10-Q
May 05, 2011

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**Form 10-Q**

**[X] Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the quarterly period ended March 31, 2011

**[ ] Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
**Commission File Number 1-7615**

# KIRBY CORPORATION

(Exact name of registrant as specified in its charter)

| **Nevada** | **74-1884980** |
|---|---|
| (State or other jurisdiction of incorporation or organization) | (IRS Employer Identification No.) |
| **55 Waugh Drive, Suite 1000, Houston, TX** | **77007** |
| (Address of principal executive offices) | (Zip Code) |

**(713) 435-1000**

(Registrant s telephone number, including area code)

**No Change**

(Former name, former address and former fiscal year, if changed since last report)

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 [ Ö ] 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 Regulations S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes [ Ö ] No [ ]

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of large accelerated filer and accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer [ Ö ] Accelerated filer [ ] Non-accelerated filer [ ] Smaller reporting company [ ]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes [ ] No [ Ö ]

The number of shares outstanding of the registrant s Common Stock, $.10 par value per share, on May 3, 2011 was 53,674,000.

## PART I FINANCIAL INFORMATION

**Item 1. Financial Statements**

**KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES**

**CONDENSED BALANCE SHEETS**

**(Unaudited)**

**ASSETS**

| | March 31, 2011 | December 31, 2010 |
|---|---|---|
| | ($ in thousands) | |
| Current assets: | | |
| Cash and cash equivalents | $ 172,093 | $ 195,600 |
| Accounts receivable: | | |
| Trade less allowance for doubtful accounts | 153,806 | 146,359 |
| Other | 18,181 | 21,612 |
| Inventory finished goods | 35,839 | 38,821 |
| Prepaid expenses and other current assets | 22,553 | 17,105 |
| Deferred income taxes | 6,308 | 6,418 |
| Total current assets | 408,780 | 425,915 |
| Property and equipment | 1,932,650 | 1,862,311 |
| Less accumulated depreciation | (755,904) | (744,150) |
| Property and equipment net | 1,176,746 | 1,118,161 |
| Goodwill net | 237,137 | 228,873 |
| Other assets | 21,429 | 21,988 |
| Total assets | $ 1,844,092 | $ 1,794,937 |

See accompanying notes to condensed financial statements.

**KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES**

**CONDENSED BALANCE SHEETS**

**(Unaudited)**

**LIABILITIES AND STOCKHOLDERS EQUITY**

| | March 31, 2011 | December 31, 2010 |
|---|---|---|
| | ($ in thousands) | |
| Current liabilities: | | |
| Current portion of long-term debt | $ 120 | $ 128 |
| Income taxes payable | 4,966 | 3,065 |
| Accounts payable | 81,917 | 71,354 |
| Accrued liabilities | 61,081 | 74,079 |
| Deferred revenues | 9,558 | 11,633 |
| Total current liabilities | 157,642 | 160,259 |
| Long-term debt less current portion | 200,004 | 200,006 |
| Deferred income taxes | 246,086 | 231,775 |
| Other long-term liabilities | 42,646 | 43,758 |
| Total long-term liabilities | 488,736 | 475,539 |
| Contingencies and commitments | | |
| Equity: | | |
| Kirby stockholders equity: | | |
| Common stock, $.10 par value per share. Authorized 120,000,000 shares, issued 57,337,000 shares | 5,734 | 5,734 |
| Additional paid-in capital | 236,104 | 237,014 |
| Accumulated other comprehensive income net | (32,426) | (33,642) |
| Retained earnings | 1,079,045 | 1,046,615 |
| Treasury stock at cost, 3,669,000 at March 31, 2011 and 3,780,000 at December 31, 2010 | (97,834) | (99,622) |
| Total Kirby stockholders equity | 1,190,623 | 1,156,099 |
| Noncontrolling interests | 7,091 | 3,040 |
| Total equity | 1,197,714 | 1,159,139 |
| Total liabilities and equity | $ 1,844,092 | $ 1,794,937 |

See accompanying notes to condensed financial statements.

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**KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES**

**CONDENSED STATEMENTS OF EARNINGS**

**(Unaudited)**

| | Three months ended March 31, | |
|---|---|---|
| | 2011 | 2010 |
| | ($ in thousands, except per share amounts) | |
| Revenues: | | |
| Marine transportation | $ 241,677 | $ 219,562 |
| Diesel engine services | 57,682 | 48,691 |
| Total revenues | 299,359 | 268,253 |
| Costs and expenses: | | |
| Costs of sales and operating expenses | 185,499 | 164,952 |
| Selling, general and administrative | 29,457 | 33,371 |
| Taxes, other than on income | 3,501 | 3,503 |
| Depreciation and amortization | 25,193 | 23,370 |
| Loss on disposition of assets | 66 | 44 |
| Total costs and expenses | 243,716 | 225,240 |
| Operating income | 55,643 | 43,013 |
| Other income | 51 | 12 |
| Interest expense | (2,833) | (2,668) |
| Earnings before taxes on income | 52,861 | 40,357 |
| Provision for taxes on income | (19,961) | (15,446) |
| Net earnings | 32,900 | 24,911 |
| Less: Net earnings attributable to noncontrolling interests | (470) | (237) |
| Net earnings attributable to Kirby | $ 32,430 | $ 24,674 |
| Net earnings per share attributable to Kirby common stockholders: | | |
| Basic | $ .60 | $ .46 |
| Diluted | $ .60 | $ .46 |

See accompanying notes to condensed financial statements.

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**KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES**

**CONDENSED STATEMENTS OF CASH FLOWS**

**(Unaudited)**

| | Three months ended March 31, 2011 | 2010 |
|---|---|---|
| | ($ in thousands) | |
| Cash flows from operating activities: | | |
| Net earnings | $ 32,900 | $ 24,911 |
| Adjustments to reconcile net earnings to net cash provided by operations: | | |
| Depreciation and amortization | 25,193 | 23,370 |
| Provision for deferred income taxes | 13,810 | 2,237 |
| Amortization of unearned compensation | 1,960 | 4,669 |
| Other | (20) | (45) |
| Increase (decrease) in cash flows resulting from changes in operating assets and liabilities, net | (10,087) | 1,449 |
| Net cash provided by operating activities | 63,756 | 56,591 |
| Cash flows from investing activities: | | |
| Capital expenditures | (31,114) | (34,423) |
| Acquisitions of businesses and marine equipment | (58,500) | |
| Proceeds from disposition of assets | 1,759 | 1,897 |
| Net cash used in investing activities | (87,855) | (32,526) |
| Cash flows from financing activities: | | |
| Payments on long-term debt, net | (10) | (14) |
| Proceeds from exercise of stock options | 135 | 297 |
| Excess tax benefit (expense) from equity compensation plans | 777 | (122) |
| Other | (310) | (698) |
| Net cash provided by (used in) financing activities | 592 | (537) |
| Increase (decrease) in cash and cash equivalents | (23,507) | 23,528 |
| Cash and cash equivalents, beginning of year | 195,600 | 97,836 |
| Cash and cash equivalents, end of period | $ 172,093 | $ 121,364 |
| Supplemental disclosures of cash flow information: | | |
| Cash paid during the period: | | |
| Interest | $ 2,675 | $ 2,561 |
| Income taxes | $ 247 | $ 996 |

See accompanying notes to condensed financial statements.

**KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES**

**NOTES TO CONDENSED FINANCIAL STATEMENTS**

**(Unaudited)**

In the opinion of management, the accompanying unaudited condensed financial statements of Kirby Corporation and consolidated subsidiaries (the Company ) contain all adjustments (consisting of only normal recurring accruals) necessary to present fairly the financial position as of March 31, 2011 and December 31, 2010, and the results of operations for the three months ended March 31, 2011 and 2010.

**(1) BASIS FOR PREPARATION OF THE CONDENSED FINANCIAL STATEMENTS**

The condensed financial statements included herein have been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. Although the Company believes that the disclosures are adequate to make the information presented not misleading, certain information and footnote disclosures, including significant accounting policies normally included in annual financial statements, have been condensed or omitted pursuant to such rules and regulations. It is suggested that these condensed financial statements be read in conjunction with the Company s Annual Report on Form 10-K for the year ended December 31, 2010.

**(2) ACQUISITIONS**

On April 15, 2011, the Company purchased United Holdings LLC ( United ), a distributor and service provider of engine and transmission related products for the oil and gas services, power generation and transportation industries, and manufacturer of oilfield service equipment. The base purchase price was $270,000,000 in cash (before post-closing adjustments), plus a three-year earnout provision for up to an additional $50,000,000 payable in 2014, dependent on achieving certain financial targets. United, headquartered in Oklahoma City, Oklahoma with 21 locations across 13 states, distributes and services equipment and parts for Allison Transmission, MTU Detroit Diesel Engines, Daimler Trucks NA, and other diesel and natural gas engines. United also manufactures oilfield service equipment, including hydraulic fracturing equipment. United s principal customers are oilfield service companies, oil and gas operators and producers, compression service companies and transportation companies.

On March 13, 2011, the Company announced the signing of an agreement to acquire K-Sea Transportation Partners L.P. ( K-Sea ), an operator of tank barges and tugboats participating in the coastwise transportation primarily of refined petroleum products in the United States, pursuant to which a subsidiary of the Company will merge with K-Sea, with K-Sea surviving the merger as a wholly owned subsidiary of the Company. The total consideration of the transaction is approximately $600,000,000, before fees, and will consist of cash, the Company s common stock and the refinancing of K-Sea debt.

K-Sea s fleet, comprised of 58 tank barges with a capacity of 3.8 million barrels and 63 tugboats, operates along the East Coast, West Coast and Gulf Coast of the United States, as well as in Alaska and Hawaii. K-Sea s tank barge fleet, 54 of which are doubled hulled, has an average age of approximately nine years and is one of the youngest fleets in the coastwise trade. K-Sea s customers include major oil companies and refiners, many of which are current Company customers for inland tank barge services. Headquartered in East Brunswick, New Jersey, K-Sea has major operating facilities in New York, Philadelphia, Norfolk, Seattle and Honolulu.

Under the terms of the agreement, the total consideration of the transaction is approximately $600,000,000, before fees, consisting of $335,000,000 for K-Sea s equity and the refinancing of $265,000,000 of K-Sea debt. K-Sea s common and preferred unitholders will receive $8.15 per unit in consideration in the

**KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES**

**NOTES TO CONDENSED FINANCIAL STATEMENTS**

**(Unaudited)**

form of cash and Company common stock. K-Sea s common unitholders will have the election to receive for each common unit either $8.15 in cash or $4.075 in cash and 0.0734 of a share of Company common stock. K-Sea s preferred unitholders will receive for each preferred unit $4.075 in cash and 0.0734 of a share of Company common stock. K-Sea s general partner will receive $8.15 in cash for each general partner unit and $18,000,000 in cash for its incentive distribution rights. On April 13, 2011, the Federal Trade Commission granted the Company early termination of the Hart-Scott-Rodino waiting period for the acquisition of K-Sea. The transaction is anticipated to close in the 2011 third quarter.

On February 24, 2011, the Company purchased 21 inland and offshore tank barges and 15 inland towboats and offshore tugboats from Enterprise Marine Services LLC ( Enterprise ) for $53,200,000 in cash. Enterprise provided transportation and delivery services for ship bunkers (engine fuel) to cruise ships, container ships and freighters primarily in the Miami, Port Everglades and Cape Canaveral, Florida area, the three largest cruise ship ports in the United States, as well as Tampa, Florida, Mobile, Alabama and Houston, Texas.

On February 9, 2011, the Company purchased from Kinder Morgan Petcoke, L.P. ( Kinder Morgan ) for $4,050,000 in cash a 51% interest in Kinder Morgan s shifting operation and fleeting facility for dry cargo barges and tank barges on the Houston Ship Channel. Kinder Morgan retained the remaining 49% interest and the Company will manage the operation. In addition, the Company purchased a towboat from Kinder Morgan for $1,250,000 in cash.

Pro forma results of the acquisitions completed in the first three months of 2011 have not been presented as the pro forma revenues, earnings before taxes on income, net earnings attributable to Kirby and net earnings per share attributable to Kirby common stockholders would not be materially different from the Company s actual results.

**(3) FAIR VALUE MEASUREMENTS**

The accounting guidance for using fair value to measure certain assets and liabilities establishes a three tier value hierarchy, which prioritizes the inputs to valuation techniques used in measuring fair value. These tiers include: Level 1, defined as observable inputs such as quoted prices in active markets for identical assets or liabilities; Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and Level 3, defined as unobservable inputs in which little, if any, market data exists, therefore requiring an entity to develop its own assumptions about the assumptions that market participants would use in pricing the asset or liability.

**KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES**

**NOTES TO CONDENSED FINANCIAL STATEMENTS**

**(Unaudited)**

The following table summarizes the assets and liabilities measured at fair value on a recurring basis at March 31, 2011 (in thousands):

| | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total Fair Value Measurements |
|---|---|---|---|---|
| Assets: | | | | |
| Derivatives | $ | $ | $ | $ |
| Liabilities: | | | | |
| Derivatives | $ | $ 16,462 | $ | $ 16,462 |

The following table summarizes the assets and liabilities measured at fair value on a recurring basis at December 31, 2010 (in thousands):

| | Identical Assets | Identical Assets | Identical Assets | Identical Assets |
|---|---|---|---|---|
| | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total Fair Value Measurements |
| Assets: | | | | |
| Derivatives | $ | $ | $ | $ |
| Liabilities: | | | | |
| Derivatives | $ | $ 17,576 | $ | $ 17,576 |

The fair value of the Company s derivative instruments is more fully described below in Note 4, Derivative Instruments.

Cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities have carrying values that approximate fair value due to the short-term maturity of these financial instruments. The Company is of the opinion that amounts included in the consolidated financial statements for outstanding debt materially represent the fair value of such debt due to their variable interest rates.

Certain assets are measured at fair value on a nonrecurring basis and therefore are not included in the table above. These assets are adjusted to fair value when there is evidence of impairment. During the three months ended March 31, 2011, there was no indication that the Company s long-lived assets were impaired, and accordingly, measurement at fair value was not required.

**(4) DERIVATIVE INSTRUMENTS**

The Company recognizes all derivative instruments (including certain derivative instruments embedded in other contracts) at fair value in the balance sheet as either assets or liabilities. The accounting for changes in the fair value of a derivative instrument depends on the intended use of

the derivative and the resulting designation, which is established at the inception date of a derivative. Special accounting for derivatives qualifying as fair value hedges allows a derivative s gains and losses to offset related results on the hedged item in the statement of earnings. For derivative instruments designated as cash flow hedges, changes in fair value, to the extent the hedge is effective, are recognized in other comprehensive income ( OCI ) until the hedged item is recognized in earnings. Hedge effectiveness is measured at least quarterly

**KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES**

**NOTES TO CONDENSED FINANCIAL STATEMENTS**

**(Unaudited)**

based on the cumulative difference between the fair value of the derivative contract and the hedged item over time. Any change in fair value resulting from ineffectiveness is recognized immediately in earnings.

***Interest Rate Risk Management***

From time to time, the Company has utilized and expects to continue to utilize derivative financial instruments with respect to a portion of its interest rate risks to achieve a more predictable cash flow by reducing its exposure to interest rate fluctuations. These transactions generally are interest rate collar and swap agreements and are entered into with large multinational banks. Derivative financial instruments related to the Company s interest rate risks are intended to reduce the Company s exposure to increases in the benchmark interest rates underlying the Company s floating rate senior notes and variable rate bank credit facility.

From time to time, the Company hedges its exposure to fluctuations in short-term interest rates under its variable rate bank credit facility and floating rate senior notes by entering into interest rate collar and swap agreements. The interest rate collar and swap agreements are designated as cash flow hedges, therefore, the changes in fair value, to the extent the collar and swap agreements are effective, are recognized in OCI until the hedged interest expense is recognized in earnings. The swap agreements effectively convert the Company s interest rate obligation on the Company s variable rate senior notes from quarterly floating rate payments based on the London Interbank Offered Rate ( LIBOR ) to quarterly fixed rate payments. As of March 31, 2011, the Company had a total notional amount of $200,000,000 of interest rate swaps designated as cash flow hedges for its variable rate senior notes as follows (dollars in thousands):

| **Notional** | | | **Fixed** | |
|---|---|---|---|---|
| **Amount** | **Effective date** | **Termination date** | **pay rate** | **Receive rate** |
| $ 100,000 | March 2006 | February 2013 | 5.45% | Three-month LIBOR |
| $ 50,000 | November 2008 | February 2013 | 3.50% | Three-month LIBOR |
| $ 50,000 | May 2009 | February 2013 | 3.795% | Three-month LIBOR |

***Foreign Currency Risk Management***

From time to time, the Company has utilized and expects to continue to utilize derivative financial instruments with respect to its forecasted foreign currency transactions to attempt to reduce the risk of its exposure to foreign currency rate fluctuations in its transactions denominated in foreign currency. These transactions, which relate to foreign currency obligations for the purchase of equipment from foreign suppliers or foreign currency receipts from foreign customers, generally are forward contracts or purchased call options and are entered into with large multinational banks.

As of March 31, 2011, the Company has forward contracts with notional amounts aggregating $13,978,000 to hedge its exposure to foreign currency rate fluctuations in expected foreign currency transactions. These contracts expire on various dates beginning in the second quarter of 2011 and ending in the first quarter of 2014. These forward contracts are designated as cash flow hedges, therefore, the changes in fair value, to the extent the forward contracts are effective, are recognized in OCI until the forward contracts expire and are recognized in cost of sales and operating expenses.

**KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES**

**NOTES TO CONDENSED FINANCIAL STATEMENTS**

**(Unaudited)**

***Fair Value of Derivative Instruments***

The following table sets forth the fair value of the Company s derivative instruments recorded as liabilities located on the consolidated balance sheet at March 31, 2011 and December 31, 2010 (in thousands):

| Liability Derivatives | Balance Sheet Location | March 31, 2011 | December 31, 2010 |
|---|---|---|---|
| **Derivatives designated as hedging instruments under ASC 815:** | | | |
| Foreign currency contracts | Other accrued liabilities | $ 1,363 | $ 798 |
| Foreign currency contracts | Other long-term liabilities | 851 | 569 |
| Interest rate contracts | Other long-term liabilities | 14,248 | 16,209 |
| Total derivatives designated as hedging instruments under ASC 815 | | $ 16,462 | $ 17,576 |
| Total liability derivatives | | $ 16,462 | $ 17,576 |

Fair value amounts were derived as of March 31, 2011 and December 31, 2010 utilizing fair value models of the Company and its counterparties on the Company s portfolio of derivative instruments. These fair value models use the income approach that relies on inputs such as yield curves, currency exchange rates and forward prices. The fair value of the Company s derivative instruments is described above in Note 3, Fair Value Measurements.

***Cash Flow Hedges***

For derivative instruments that are designated and qualify as cash flow hedges, the effective portion of the gain or loss on the derivative is reported as a component of OCI and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. Gains and losses on the derivative representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings. Any ineffectiveness related to the Company s hedges was not material for any of the periods presented.

The following table sets forth the location and amount of gains and losses on the Company s derivative instruments in the consolidated statements of earnings for the three months ended March 31, 2011 and 2010 (in thousands):

| Derivatives in ASC 815 Cash Flow Hedging Relationships: | Location of Gain (Loss) Reclassified from Accumulated OCI into Income (Effective Portion) | Amount of Gain (Loss) Recognized in OCI on Derivatives (Effective Portion) Three months ended March 31, 2011 | 2010 | Amount of Gain (Loss) Reclassified from Accumulated OCI into Income (Effective Portion) Three months ended March 31, 2011 | 2010 |
|---|---|---|---|---|---|
| Interest rate contracts | Interest expense | $ 1,961 | $ (1,332) | $ (2,125) | $ (2,147) |
| Foreign exchange contracts | Cost and sales of operating expenses | (860) | (52) | | 22 |

| | | | | |
|---|---|---|---|---|
| Total | $ 1,101 | $ (1,384) | $ (2,125) | $ (2,125) |

**KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES**

**NOTES TO CONDENSED FINANCIAL STATEMENTS**

**(Unaudited)**

The Company anticipates $5,209,000 of net losses on interest rate swap agreements included in accumulated OCI will be transferred into earnings over the next year based on current interest rates. Gains or losses on interest rate swap agreements offset increases or decreases in rates of the underlying debt, which results in a fixed rate for the underlying debt. The Company also expects $1,034,000 of net losses on foreign currency contracts included in accumulated OCI will be transferred into earnings over the next year based current spot rates.

**(5) STOCK AWARD PLANS**

The Company has share-based compensation plans which are described below. The compensation cost that has been charged against earnings for the Company s stock award plans and the income tax benefit recognized in the statement of earnings for stock awards for the three months ended March 31, 2011 and 2010 were as follows (in thousands):

| | Three months ended March 31, | |
|---|---|---|
| | **2011** | **2010** |
| Compensation cost | $ 1,960 | $ 4,669 |
| Income tax benefit | $ 747 | $ 1,797 |

The Company has two employee stock award plans for selected officers and other key employees which provide for the issuance of stock options and restricted stock. For both of the plans, the exercise price for each option equals the fair market value per share of the Company s common stock on the date of grant. The terms of the options granted prior to January 25, 2010 are five years and vest ratably over three years. Options granted on or after January 25, 2010 have terms of seven years and vest ratably over three years. At March 31, 2011, 1,225,948 shares were available for future grants under the employee plans and no outstanding stock options under the employee plans were issued with stock appreciation rights.

The following is a summary of the stock option activity under the employee plans described above for the three months ended March 31, 2011:

| | Non-Qualified or Outstanding Non-Qualified or Nonincentive Stock Awards | Non-Qualified or Weighted Average Exercise Price |
|---|---|---|
| Outstanding at December 31, 2010 | 434,447 | $33.53 |
| Granted | 100,569 | $46.74 |
| Exercised | (24,536) | $27.60 |
| Outstanding at March 31, 2011 | 510,480 | $36.42 |

**KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES**

**NOTES TO CONDENSED FINANCIAL STATEMENTS**

**(Unaudited)**

The following table summarizes information about the Company s outstanding and exercisable stock options under the employee plans at March 31, 2011:

| | $10,653,000 | $10,653,000 | $10,653,000 | $10,653,000 | $10,653,000 | $10,653,000 | $10,653,000 |
|---|---|---|---|---|---|---|---|
| | **Options Outstanding** | | | | **Options Exercisable** | | |
| **Range of Exercise Prices** | **Number Outstanding** | **Weighted Average Remaining Contractual Life in Years** | **Weighted Average Exercise Price** | **Aggregate Intrinsic Value** | **Number Exercisable** | **Weighted Average Exercise Price** | **Aggregate Intrinsic Value** |
| $23.98 - $34.40 | 252,850 | 4.02 | $ 28.15 | | 133,097 | $27.15 | |
| $35.66 - $36.94 | 64,858 | 1.14 | $ 35.78 | | 62,191 | $35.76 | |
| $46.74 - $48.65 | 192,772 | 4.46 | $ 47.48 | | 92,203 | $48.28 | |
| $23.98 - $48.65 | 510,480 | 3.82 | $ 36.42 | $10,653,000 | 287,491 | $35.79 | $6,182,000 |

The following is a summary of the restricted stock award activity under the employee plans described above for the three months ended March 31, 2011:

| | **Restricted Stock** | **Restricted Stock** |
|---|---|---|
| | **Unvested Restricted Stock Award Shares** | **Weighted Average Grant Date Fair Value Per Share** |
| Nonvested balance at December 31, 2010 | 499,335 | $ 31.98 |
| Granted | 130,999 | $ 44.84 |
| Vested | (161,420) | $ 33.31 |
| Nonvested balance at March 31, 2011 | 468,914 | $ 35.57 |

The Company has two director stock award plans for nonemployee directors of the Company which provide for the issuance of stock options and restricted stock. No additional options can be granted under one of the plans. The 2000 Director Plan provides for the automatic grants of stock options and restricted stock to nonemployee directors on the date of first election as a director and after each annual meeting of stockholders. In addition, the 2000 Director Plan allows for the issuance of stock options or restricted stock in lieu of cash for all or part of the annual director fee at the option of the director. The exercise prices for all options granted under the plans are equal to the fair market value per share of the Company s common stock on the date of grant. The terms of the options are ten years. The options granted to a director when first elected vest immediately. The options granted and restricted stock issued after each annual meeting of stockholders vest six months after the date of grant. Options granted and restricted stock issued in lieu of cash director fees vest in equal quarterly increments during the year to which they relate. At March 31, 2011, 324,766 shares were available for future grants under the 2000 Director Plan. The director stock award plans are intended as an incentive to attract and retain qualified and competent independent directors.

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**KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES**

**NOTES TO CONDENSED FINANCIAL STATEMENTS**

**(Unaudited)**

The following is a summary of the stock option activity under the director plans described above for the three months ended March 31, 2011:

| | Outstanding Non-Qualified or Nonincentive Stock Awards | Weighted Average Exercise Price |
|---|---|---|
| Outstanding at December 31, 2010 | 356,429 | $ 34.88 |
| Exercised | (13,356) | $ 10.14 |
| Outstanding at March 31, 2011 | 343,073 | $ 36.30 |

The following table summarizes information about the Company s outstanding and exercisable stock options under the director plans at March 31, 2011:

| | Options Outstanding | | | | Options Exercisable | | |
|---|---|---|---|---|---|---|---|
| Range of Exercise Prices | Number Outstanding | Weighted Average Remaining Contractual Life in Years | Weighted Average Exercise Price | Aggregate Intrinsic Value | Number Exercisable | Weighted Average Exercise Price | Aggregate Intrinsic Value |
| $10.06 - $17.88 | 51,814 | 1.54 | $ 15.12 | | 51,814 | $ 15.12 | |
| $20.28 - $29.60 | 68,433 | 7.03 | $ 27.15 | | 68,433 | $ 27.15 | |
| $35.17 - $36.82 | 96,036 | 5.46 | $ 35.81 | | 96,036 | $ 35.81 | |
| $41.24 - $55.49 | 126,790 | 7.98 | $ 49.03 | | 126,790 | $ 49.03 | |
| $10.06 - $55.49 | 343,073 | 6.16 | $ 35.84 | $ 7,358,000 | 343,073 | $ 35.84 | $ 7,358,000 |

The following is a summary of the restricted stock award activity under the director plan described above for the three months ended March 31, 2011:

| | Unvested Restricted Stock Award Shares | Weighted Average Grant Date Fair Value Per Share |
|---|---|---|
| Nonvested balance at December 31, 2010 | 525 | $ 41.33 |
| Vested | (525) | $ 41.33 |

| Nonvested balance at March 31, 2011 | $ |
| --- | --- |

The total intrinsic value of all stock options exercised under all of the Company s plans was $998,000 and $353,000 for the three months ended March 31, 2011 and 2010, respectively. The actual tax benefit realized for tax deductions from stock option exercises was $380,000 and $136,000 for the three months ended March 31, 2011 and 2010, respectively.

The total intrinsic value of all the restricted stock vestings under all of the Company s plans was $7,185,000 and $8,308,000 for the three months ended March 31, 2011 and 2010, respectively. The actual tax benefit realized for tax deductions from restricted stock vestings was $2,737,000 and $3,199,000 for the three months ended March 31, 2011 and 2011, respectively.

As of March 31, 2011, there was $2,649,000 of unrecognized compensation cost related to nonvested stock options and $15,546,000 related to restricted stock. The stock options are expected to be recognized over a weighted average period of approximately 2.0 years and restricted stock over

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approximately 3.4 years. The total fair value of options vested was $1,202,000 and $2,461,000 during the three months ended March 31, 2011 and 2010, respectively. The fair value of the restricted stock vested was $7,185,000 and $8,308,000 for the three months ended March 31, 2011 and 2010, respectively.

The weighted average per share fair value of stock options granted during the three months ended March 31, 2011 and 2010 was $16.55 and $12.09, respectively. The fair value of the stock options granted during the three months ended March 31, 2011 and 2010 was $1,664,000 and $1,257,000, respectively. The Company currently uses treasury stock shares for restricted stock grants and stock option exercises. The fair value of each stock option was determined using the Black-Scholes option pricing model. The key input variables used in valuing the options during the three months ended March 31, 2011 and 2010 were as follows:

| | Three months ended March 31, | |
|---|---|---|
| | **2011** | **2010** |
| Dividend yield | None | None |
| Average risk-free interest rate | 2.2% | 3.1% |
| Stock price volatility | 33% | 33% |
| Estimated option term | Six years | Six years |

**(6) COMPREHENSIVE INCOME**

The Company s total comprehensive income for the three months ended March 31, 2011 and 2010 was as follows (in thousands):

| | Three months ended March 31, | |
|---|---|---|
| | **2011** | **2010** |
| Net earnings | $ 32,900 | $ 24,911 |
| Other comprehensive income (loss), net of taxes: | | |
| Pension and postretirement benefits | 339 | 306 |
| Change in fair value of derivative financial instruments | 877 | (896) |
| Total other comprehensive income (loss), net of taxes | 1,216 | (590) |
| Total comprehensive income, net of taxes | 34,116 | 24,321 |
| Net earnings attributable to noncontrolling interests | (470) | (237) |
| Comprehensive income attributable to Kirby | $ 33,646 | $ 24,084 |

**(7) SEGMENT DATA**

The Company s operations are classified into two reportable business segments as follows:

*Marine Transportation* Marine transportation by United States flag vessels on the United States inland waterway system and, to a lesser extent, offshore transportation of dry-bulk cargoes. The principal products transported on the United States inland waterway system include petrochemicals, black oil products, refined petroleum products and agricultural chemicals.

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*Diesel Engine Services* Overhaul and repair of medium-speed and high-speed diesel engines, reduction gear repair, and sale of related parts and accessories for customers in the marine and power generation industries.

The following table sets forth the Company s revenues and profit or loss by reportable segment for the three months ended March 31, 2011 and 2010 and total assets as of March 31, 2011 and December 31, 2010 (in thousands):

| | Three months ended | | Three months ended | |
|---|---|---|---|---|
| | **Three months ended March 31,** | | | |
| | **2011** | | **2010** | |
| Revenues: | | | | |
| Marine transportation | $ | 241,677 | $ | 219,562 |
| Diesel engine services | | 57,682 | | 48,691 |
| | $ | 299,359 | $ | 268,253 |
| Segment profit (loss): | | | | |
| Marine transportation | $ | 52,698 | $ | 42,309 |
| Diesel engine services | | 6,606 | | 5,043 |
| Other | | (6,443) | | (6,995) |
| | $ | 52,861 | $ | 40,357 |

| | **March 31, 2011** | | **December 31, 2010** | |
|---|---|---|---|---|
| Total assets: | | | | |
| Marine transportation | $ | 1,460,433 | $ | 1,383,252 |
| Diesel engine services | | 183,222 | | 185,824 |
| Other | | 200,437 | | 225,861 |
| | $ | 1,844,092 | $ | 1,794,937 |

The following table presents the details of Other segment loss for the three months ended March 31, 2011 and 2010 (in thousands):

| | Three months ended | | Three months ended | |
|---|---|---|---|---|
| | **Three months ended March 31,** | | | |
| | **2011** | | **2010** | |
| General corporate expenses | $ | (3,595) | $ | (4,295) |
| Loss on disposition of assets | | (66) | | (44) |
| Interest expense | | (2,833) | | (2,668) |
| Other income | | 51 | | 12 |

| | | |
|---|---|---|
| | $ (6,443) | $ (6,995) |

The following table presents the details of Other total assets as of March 31, 2011 and December 31, 2010 (in thousands):

| | **Three months ended March 31, 2011** | **Three months ended December 31, 2010** |
|---|---|---|
| General corporate assets | $ 197,015 | $ 222,525 |
| Investment in affiliates | 3,422 | 3,336 |
| | $ 200,437 | $ 225,861 |

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**(8) TAXES ON INCOME**

Earnings before taxes on income and details of the provision for taxes on income for the three months ended March 31, 2011 and 2010 were as follows (in thousands):

| | Three months ended March 31, | |
|---|---|---|
| | 2011 | 2010 |
| Earnings before taxes on income United States | $ 52,861 | $ 40,357 |
| | | |
| Provision for taxes on income: | | |
| Federal: | | |
| Current | $ 4,003 | $ 11,444 |
| Deferred | 13,810 | 2,237 |
| State and local | 2,148 | 1,765 |
| | | |
| | $ 19,961 | $ 15,446 |

**(9) EARNINGS PER SHARE**

The following table presents the components of basic and diluted earnings per share for the three months ended March 31, 2011 and 2010 (in thousands, except per share amounts):

| | Three months ended March 31, | |
|---|---|---|
| | 2011 | 2010 |
| Net earnings attributable to Kirby | $ 32,430 | $ 24,674 |
| Undistributed earnings allocated to restricted shares | (286) | (253) |
| | | |
| Income available to Kirby common stockholders basic | 32,144 | 24,421 |
| Undistributed earnings allocated to restricted shares | 286 | 253 |
| Undistributed earnings reallocated to restricted shares | (285) | (252) |
| | | |
| Income available to Kirby common stockholders diluted | $ 32,145 | $ 24,422 |
| | | |
| Shares outstanding: | | |
| Weighted average common stock issued and outstanding | 53,640 | 53,957 |
| Weighted average unvested restricted stock | (473) | (552) |
| | | |
| Weighted average common stock outstanding basic | 53,167 | 53,405 |
| Dilutive effect of stock options | 201 | 122 |
| | | |
| Weighted average common stock outstanding diluted | 53,368 | 53,527 |

| | | | | |
|---|---|---|---|---|
| Net earnings per share attributable to Kirby common stockholders: | | | | |
| Basic | $ | .60 | $ | .46 |
| Diluted | $ | .60 | $ | .46 |

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Certain outstanding options to purchase approximately 101,000 and 340,000 shares of common stock were excluded in the computation of diluted earnings per share as of March 31, 2011 and 2010, respectively, as such stock options would have been antidilutive.

**(10) RETIREMENT PLANS**

The Company sponsors a defined benefit plan for vessel personnel and shore based tankermen. The plan benefits are based on an employee s years of service and compensation. The plan assets consist primarily of equity and fixed income securities.

The Company s pension plan funding strategy has historically been to contribute an amount equal to the greater of the minimum required contribution under ERISA or the amount necessary to fully fund the plan on an accumulated benefit obligation ( ABO ) basis at the end of the fiscal year. The ABO is based on a variety of demographic and economic assumptions, and the pension plan assets returns are subject to various risks, including market and interest rate risk, making an accurate prediction of the pension plan contribution difficult. Based on current pension plan assets and market conditions, the Company does not expect to make a contribution to its pension plan prior to December 31, 2011 to fund its 2011 pension plan obligations. As of March 31, 2011, no 2011 year contributions have been made.

The Company sponsors an unfunded defined benefit health care plan that provides limited postretirement medical benefits to employees who meet minimum age and service requirements, and to eligible dependents. The plan limits cost increases in the Company s contribution to 4% per year. The plan is contributory, with retiree contributions adjusted annually. The Company also has an unfunded defined benefit supplemental executive retirement plan ( SERP ) that was assumed in an acquisition in 1999. That plan ceased to accrue additional benefits effective January 1, 2000.

The components of net periodic benefit cost for the Company s defined benefit plans for the three months ended March 31, 2011 and 2010 were as follows (in thousands):

| | Pension Benefits | | | |
|---|---|---|---|---|
| | Pension Plan | | SERP | |
| | Three months ended March 31, | | Three months ended March 31, | |
| | 2011 | 2010 | 2011 | 2010 |
| Components of net periodic benefit cost: | | | | |
| Service cost | $ 1,825 | $ 1,715 | $ | $ |
| Interest cost | 2,417 | 2,227 | 20 | 21 |
| Expected return on plan assets | (2,821) | (2,332) | | |
| Amortization: | | | | |
| Actuarial loss | 694 | 581 | 2 | 1 |
| Prior service credit | (10) | (22) | | |
| Net periodic benefit cost | $ 2,105 | $ 2,169 | $ 22 | $ 22 |

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The components of net periodic benefit cost for the Company s postretirement benefit plan for the three months ended March 31, 2011 and 2010 were as follows (in thousands):

| | Other Postretirement Benefits Postretirement Welfare Plan Three months ended March 31, | |
|---|---|---|
| | **2011** | **2010** |
| Components of net periodic benefit cost: | | |
| Service cost | $ | $ 64 |
| Interest cost | 36 | 84 |
| Amortization: | | |
| Actuarial gain | (143) | (73) |
| Prior service cost | 10 | 10 |
| Net periodic benefit cost | $ (97) | $ 85 |

**(11) CONTINGENCIES**

In 2000, the Company and a group of approximately 45 other companies were notified that they are Potentially Responsible Parties ( PRPs ) under the Comprehensive Environmental Response, Compensation and Liability Act ( CERCLA ) with respect to a Superfund site, the Palmer Barge Line Superfund Site ( Palmer ), located in Port Arthur, Texas. In prior years, Palmer had provided tank barge cleaning services to various subsidiaries of the Company. The Company and three other PRPs entered into an agreement with the United States Environmental Protection Agency ( EPA ) to perform a remedial investigation and feasibility study and, subsequently, a limited remediation was performed and is now complete. During the 2007 third quarter, five new PRPs entered into an agreement with the EPA related to the Palmer site. In July 2008, the EPA sent a letter to approximately 30 PRPs for the Palmer site, including the Company, indicating that it intends to pursue recovery of $2,949,000 of costs it incurred in relation to the site. The Company and the other PRPs continue to discuss suggested pro rata allocations of all PRPs with the EPA and the U.S. Department of Justice ( DOJ ) in order to resolve the EPA s past cost claim.

In 2000, the Company and approximately 50 other companies were notified that they are PRPs under the CERCLA with respect to a Superfund site, the State Marine of Port Arthur Superfund Site ( State Marine ), located in Port Arthur, Texas. In the past, State Marine had performed tank barge cleaning and services for various subsidiaries of the Company. In March 2010, the DOJ and EPA issued a letter to seven PRPs, which include the former owners/operator of the site and others, including the Company, indicating their intent to pursue reimbursement of its past costs of approximately $2,977,000 in connection with clean-up activities in relation to the site. The Company and the other PRPs have requested documentation concerning the site activities related to all PRPs in order to determine appropriate allocation of past costs relative to activities at the site to develop suggested pro rata sharing to resolve the EPA s past cost claim.

With respect to the above sites, the Company has recorded reserves for its estimated potential liability for its portion of the EPA s past costs claim based on information developed to date including various factors such as the Company s liability in proportion to other responsible parties and the extent to which such costs are recoverable from third parties.

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In addition, the Company is involved in various legal and other proceedings which are incidental to the conduct of its business, none of which in the opinion of management will have a material effect on the Company s financial condition, results of operations or cash flows. Management believes that it has recorded adequate reserves and believes that it has adequate insurance coverage or has meritorious defenses for these other claims and contingencies.

The Company has issued guaranties or obtained standby letters of credit and performance bonds supporting performance by the Company and its subsidiaries of contractual or contingent legal obligations of the Company and its subsidiaries incurred in the ordinary course of business. The aggregate notional value of these instruments is $9,972,000 at March 31, 2011, including $7,490,000 in letters of credit and debt guarantees, and $2,482,000 in performance bonds. All of these instruments have an expiration date within four years. The Company does not believe demand for payment under these instruments is likely and expects no material cash outlays to occur in connection with these instruments.

**(12) SUBSEQUENT EVENT**

On April 15, 2011, the Company completed the purchase of United, a distributor and service provider of engine and transmission related products for the oil and gas services, power generation and transportation industries, and manufacturer of oilfield service equipment. The base purchase price was $270,000,000 in cash (before post-closing adjustments), plus a three-year earnout provision for up to an additional $50,000,000 payable in 2014, dependent on achieving certain financial targets. United, headquartered in Oklahoma City, Oklahoma with 21 locations across 13 states, distributes and services equipment and parts for Allison Transmission, MTU Detroit Diesel Engines, Daimler Trucks NA, and other diesel and natural gas engines. United also manufactures oilfield service equipment, including hydraulic fracturing equipment. United s principal customers are oilfield service companies, oil and gas operators and producers, compression service companies and transportation companies.

**Item 1A. Risk Factors**

The Company continues to be subject to the risk factors previously disclosed in its Risk Factors in the Company s Annual Report on Form 10-K for the year ended December 31, 2010, as well as the following risk factor:

*The Company s diesel engine services segment could be adversely impacted by future legislation or additional regulation of hydraulic fracturing practices.* The Company, through its United subsidiary, is a distributor and service provider of engine and transmission related products for the oil and gas services, power generation and transportation industries, and a manufacturer of oilfield service equipment, including hydraulic fracturing equipment. The EPA is studying hydraulic fracturing practices, and legislation may be introduced in the Congress that would authorize the EPA to impose additional regulations on hydraulic fracturing. In addition, a number of states are evaluating the adoption of legislation or regulations governing hydraulic fracturing. Such federal or state legislation and/or regulations could materially impact our customers operations and greatly reduce or eliminate demand for the Company s hydraulic fracturing equipment and related products. We are unable to predict whether the future legislation or any other regulations will ultimately be enacted, and if so, the impact on the Company s diesel engine services segment.

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

Statements contained in this Form 10-Q that are not historical facts, including, but not limited to, any projections contained herein, are forward-looking statements and involve a number of risks and uncertainties. Such statements can be identified by the use of forward-looking terminology such as may, will, expect, anticipate, estimate, or continue or the negative thereof or other variations thereon or com terminology. The actual results of the future events described in such forward-looking statements in this Form 10-Q could differ materially from those stated in such forward-looking statements. Among the factors that could cause actual results to differ materially are: adverse economic conditions, industry competition and other competitive factors, adverse weather conditions such as high water, low water, tropical storms, hurricanes, fog and ice, marine accidents, lock delays, fuel costs, interest rates, construction of new equipment by competitors, government and environmental laws and regulations, and the timing, magnitude and number of acquisitions made by the Company. For a more detailed discussion of factors that could cause actual results to differ from those presented in forward-looking statements, see Item 1A-Risk Factors found in the Company s annual report on Form 10-K for the year ended December 31, 2010. Forward-looking statements are based on currently available information and the Company assumes no obligation to update any such statements.

For purposes of the Management s Discussion, all net earnings per share attributable to Kirby common stockholders are diluted earnings per share. The weighted average number of common shares applicable to diluted earnings per share for the first quarter of 2011 and 2010 were 53,368,000 and 53,527,000, respectively. The decrease in the weighted average number of common shares for the 2011 first quarter compared with the 2010 first quarter primarily reflected the common stock repurchases in the 2010 second, third and fourth quarters, partially offset by the issuance of restricted stock and the exercise of stock options.

**Overview**

The Company is the nation s largest domestic inland tank barge operator with a fleet of 829 active tank barges, including 45 leased barges, and 16.1 million barrels of capacity as of March 31, 2011. The Company operated an average of 230 inland towing vessels during the 2011 first quarter of which an average of 48 was chartered. The Company uses the United States inland waterway system to transport bulk liquids including petrochemicals, black oil products, refined petroleum products and agricultural chemicals. The Company also owns and operates four ocean-going barge and tug units transporting dry-bulk commodities in United States coastwise trade. Through its diesel engine services segment, the Company provides after-market services for medium-speed and high-speed diesel engines used in marine and power generation applications.

For the 2011 first quarter, net earnings attributable to Kirby were $32,430,000, or $.60 per share, on revenues of $299,359,000, compared with 2010 first quarter net earnings attributable to Kirby of $24,674,000, or $.46 per share, on revenues of $268,253,000.

KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

**Marine Transportation**

For the 2011 first quarter, 81% of the Company s revenue was generated by its marine transportation segment. The segment s customers include many of the major petrochemical and refining companies that operate in the United States. Products transported include raw materials for many of the end products used widely by businesses and consumers  plastics, fiber, paints, detergents, oil additives and paper, among others. Consequently, the Company s business tends to mirror the general performance of the United States economy and volumes produced by the Company s customer base.

The Company s marine transportation segment s revenue for the 2011 first quarter increased 10% and operating income increased 25% compared with the 2010 first quarter revenues and operating income. The higher marine transportation revenues reflected an improvement in tank barge demand and equipment utilization due to continued strong production volumes from United States petrochemical customers, for both domestic and foreign destinations, and from black oil products customers due to the continued exportation of heavy fuel oil and refinery maintenance activity. Diesel fuel prices for the 2011 first quarter increased 24% compared with the 2010 first quarter, thereby positively impacting marine transportation revenues as fuel is escalated and de-escalated through revenue adjustment clauses in customers  term contracts.

During the 2011 first quarter, approximately 75% of the marine transportation revenues were under term contracts and 25% were spot contract revenues. Time charters, which insulate the Company from revenue fluctuations caused by weather and navigational delays and temporary market declines, represented 56% of the revenues under term contracts during the 2011 first quarter compared with 49% during the 2010 first quarter. Term contract rates renewed in the 2011 first quarter increased an average of 2% to 4% compared with term contract rate renewals in the first quarter of 2010. Spot contract rates, which include the cost of fuel, increased an average of 5% to 7% compared with the 2010 fourth quarter. Effective January 1, 2011, annual escalators for labor and the producer price index on a number of multi-year contracts resulted in rate increases on those contracts by 1% to 2%, excluding fuel.

The marine transportation operating margin for the 2011 first quarter was 21.8% compared with 19.3% for the 2010 first quarter, reflecting the improved petrochemical and black oil products demand and equipment utilization levels, modestly higher term contract and spot contract pricing, and the positive impact of cost reduction initiatives. These were partially offset by the cost impact of rising diesel fuel prices and increased delay days from more difficult winter weather operating conditions and lock delays.

**Diesel Engine Services**

For the 2011 first quarter, 19% of the Company s revenue was generated by the diesel engine services segment, of which 62% was generated through service and 38% from direct parts sales. The results of the diesel engine services segment are largely influenced by the economic cycles of the marine and power generation industries it serves.

The Company s diesel engine services segment s 2011 first quarter revenue increased 18% and operating income increased 31% when compared with the first quarter of 2010. The increase in revenues and operating income reflected a stronger medium-speed power generation market with engine-generator set upgrade projects and higher parts and engine sales, and stronger maintenance cycles for Midwest and West Coast medium-speed marine customers. These increases were offset by continued weak service levels and direct parts sales for both the medium-speed and high-speed Gulf Coast oil services markets.

The diesel engine services segment s operating margin for the 2011 first quarter was 11.5% compared with 10.4% for the first quarter of 2010, reflecting overall higher service and direct parts sales and resulting higher labor utilization.

**Cash Flow and Capital Expenditures**

The Company continued to generate strong operating cash flow during the 2011 first quarter, with net cash provided by operating activities of $63,756,000 compared with net cash provided by operating activities for the 2010 first quarter of $56,591,000. The 13% increase was primarily from higher net earnings attributable to Kirby during the 2011 first quarter and a higher deferred tax provision in 2011 versus 2010. In addition, during the 2011 and 2010 first quarters, the Company generated cash of $135,000 and $297,000, respectively, from the exercise of stock options and $1,759,000 and $1,897,000, respectively, from proceeds from the disposition of assets. For the 2011 first quarter, cash generated and cash and cash equivalents were used for capital expenditures of $31,114,000, including $12,733,000 for new tank barge and towboat construction and $18,381,000 primarily for upgrading the existing marine transportation fleet, $53,200,000 for the purchase of 21 inland and offshore tank barges, with approximately 400,000 barrels of capacity, and 15 inland towboats and offshore tugboats from Enterprise, $4,050,000 for a 51% interest in Kinder Morgan s shifting operation and fleeting facility for dry cargo barges and tank barges on the Houston Ship Channel and $1,250,000 for the purchase of a towboat from Kinder Morgan. The Company s debt-to-capitalization ratio decreased to 14.3% at March 31, 2011 from 14.7% at December 31, 2010, primarily due to the increase in total equity from net earnings attributable to Kirby for the 2011 first quarter of $32,430,000, exercise of stock options and the amortization of unearned equity compensation. As of March 31, 2011, the Company had no outstanding balance under its $250,000,000 revolving credit facility and had $172,093,000 of cash and cash equivalents.

The Company projects that capital expenditures for 2011 will be in the $220,000,000 to $230,000,000 range, including approximately $100,000,000 for the construction of 40 inland tank barges and three 1800 horsepower inland towboats, and approximately $36,000,000 in progress payments on the construction of a new offshore integrated dry-bulk barge and tugboat unit with an estimated total cost of $50,000,000. The remaining payments on the new offshore integrated dry-bulk barge and tug unit will be made in 2012. During the 2011 first quarter, the Company took delivery of five new inland tank barges and three chartered tank barges with a total capacity of approximately 175,000 barrels. During the 2011 first quarter, the Company also retired 23 inland tank barges, reducing its capacity by approximately 400,000 barrels.

**Outlook**

Petrochemical and black oil products tank barge utilization levels continued to improve during the 2011 first quarter, reaching the highest utilization levels, in the low 90% range, since the third quarter of 2008. While the United States economy continues to remain sluggish, with consistently high unemployment levels and negative consumer confidence, the United States petrochemical industry has seen a steady improvement in production for both domestic consumption and exports. Lower priced domestic natural gas, a basic feedstock for the United States petrochemical industry, provides the industry with a competitive advantage against foreign petrochemical producers. As a result, United States petrochemical production improved as the 2010 year progressed and has continued to improve during the 2011 first quarter, thereby producing increased marine transportation volumes for basic petrochemicals to both domestic consumers and terminals for export destinations. The black oil products market also continued to improve during the 2011 first quarter, primarily due to exportation of heavy fuel oil and refinery maintenance.

The United States petrochemical industry is globally competitive based on a number of factors including a highly integrated and efficient transportation system of pipelines, rails, trucks and tank barges, a largely depreciated yet well maintained and operated asset base, and a low cost feedstock slate, which includes natural gas. Certain United States producers have announced plans for plant capacity expansions and the reopening of idled petrochemical facilities. The current production volumes from the Company s petrochemical customers has resulted in Company s tank barge utilization levels in the low 90% range and any increased production from current facilities, plant expansions or the reopening of idled facilities should drive feedstock and production volumes higher, in turn leading to higher tank barge utilization levels.

During 2009 and 2010, the marine transportation segment was negatively impacted by excess industry tank barge capacity. At the end of 2010, the Company estimated there were approximately 3,100 tank barges in the industry fleet, of which approximately 500 were over 35 years old and approximately 250 of those over 40 years old. Given the age profile of the industry fleet, we expect older tank barges will continue to be removed from service and replaced by new barges that will enter the fleet. The Company estimates that 150 tank barges will be constructed during 2011 and a similar number retired.

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In the diesel engine services segment, the Gulf Coast oil services markets remained depressed during the 2011 first quarter. However, with Gulf of Mexico drilling permits beginning to be issued, this market should see a slow improvement as 2011 progresses.

**Acquisitions**

On April 15, 2011, the Company purchased United, a distributor and service provider of engine and transmission related products for the oil and gas services, power generation and transportation industries, and manufacturer of oilfield service equipment. The base purchase price was $270,000,000 in cash, before post-closing adjustments. In addition, there is a three-year earnout provision for up to an additional $50,000,000 payable in 2014, dependent on achieving certain financial targets. United, headquartered in Oklahoma City, Oklahoma with 21 locations across 13 states, distributes and services equipment and parts for Allison Transmission, MTU Detroit Diesel Engines, Daimler Trucks NA, and other diesel and natural gas engines. United also manufactures oilfield service equipment, including hydraulic fracturing equipment. United s principal customers are oilfield service companies, oil and gas operators and producers, compression service companies and transportation companies. Financing of the acquisition was through the Company s operating cash flows and borrowings under the Company s revolving credit facility.

On March 13, 2011, the Company signed an agreement to acquire K-Sea, an operator of tank barges and tugboats participating in the coastwise transportation primarily of refined petroleum products in the United States. The total consideration of the transaction is approximately $600,000,000, before fees. The consideration will consist of cash, Company common stock and the refinancing of K-Sea s debt. K-Sea s fleet, consisting of 58 tank barges with a capacity of 3.8 million barrels and 63 tugboats, operates along the East Coast, West Coast and Gulf Coast of the United States, as well as in Alaska and Hawaii. K-Sea s tank barge fleet, 54 of which are double hulled, has an average age of approximately nine years and is one of the youngest fleets in the coastwise trade. K-Sea s customers include major oil companies and refiners, many of which are current customers of the Company. Under the terms of the agreement, the total consideration of the transaction is approximately $600,000,000, before fees, consisting of $335,000,000 for K-Sea s equity and the refinancing of $265,000,000 of K-Sea debt. K-Sea s common and preferred unitholders will receive $8.15 per unit in consideration in the form of cash and Company common stock. K-Sea s common unitholders will have the election to receive for each common unit either $8.15 in cash or $4.075 in cash and 0.0734 of a share of Company common stock. K-Sea s preferred unitholders will receive for each preferred unit $4.075 in cash and 0.0734 of a share of Company common stock. K-Sea s general partner will receive $8.15 in cash for each general partner unit and $18,000,000 in cash for incentive distribution rights. On April 13, 2011, the Federal Trade Commission granted the Company early termination of the Hart-Scott-Rodino waiting period for the acquisition of K-Sea. The transaction is anticipated to close in the 2011 third quarter. The acquisition will be financed through borrowings under the Company s revolving credit facility and a new $540,000,000 five-year senior unsecured term loan.

On February 24, 2011, the Company purchased 21 inland and offshore tank barges and 15 inland towboats and offshore tugboats from Enterprise for $53,200,000 in cash. Enterprise provided transportation and delivery services for ship bunkers (engine fuel) to cruise ships, container ships and freighters primarily in the Miami, Port Everglades and Cape Canaveral, Florida area, the three largest cruise ship ports in the United States, as well as Tampa, Florida, Mobile, Alabama and Houston, Texas. Financing of the acquisition was through the Company s operating cash flows.

On February 9, 2011, the Company purchased from Kinder Morgan for $4,050,000 in cash a 51% interest in Kinder Morgan s shifting operation and fleeting facility for dry cargo barges and tank barges on the Houston Ship Channel. Kinder Morgan retained the remaining 49% interest and the Company will manage the operation. In addition, the Company purchased a towboat from Kinder Morgan for $1,250,000 in cash. Financing of the acquisition was through the Company s operating cash flows.

**KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES**

**Results of Operations**

The Company reported first quarter 2011 net earnings attributable to Kirby of $32,430,000, or $.60 per share, on revenues of $299,359,000, compared with 2010 first quarter net earnings attributable to Kirby of $24,674,000, or $.46 per share, on revenues of $268,253,000.

Marine transportation revenues for the 2011 first quarter were $241,677,000, or 81% of total revenues, compared with $219,562,000, or 82% of total revenues, for the 2010 first quarter. Diesel engine services revenues for the 2011 first quarter were $57,682,000, or 19% of total revenues, compared with $48,691,000, or 18% of total revenues, for the 2010 first quarter.

**Marine Transportation**

The Company, through its marine transportation segment, is a provider of marine transportation services, operating inland tank barges and towing vessels, transporting petrochemicals, black oil products, refined petroleum products and agricultural chemicals along the United States inland waterways. As of March 31, 2011, the Company operated 829 active inland tank barges, with a total capacity of 16.1 million barrels, compared with 861 active inland tank barges at March 31, 2010, with a total capacity of 16.6 million barrels. The Company operated an average of 230 active inland towing vessels during the 2011 first quarter compared with 224 during the first quarter of 2010. The Company owns and operates four offshore dry-bulk barge and tug units engaged in the offshore transportation of dry-bulk cargoes. The Company also owns a two-thirds interest in Osprey Line, L.L.C., which transports project cargoes and cargo containers by barge, as well as a 51% interest in a shifting operation and fleeting facility for dry cargo barges and tank barges on the Houston Ship Channel.

The following table sets forth the Company s marine transportation segment s revenues, costs and expenses, operating income and operating margins for the three months ended March 31, 2011 compared with the three months ended March 31, 2010 (dollars in thousands):

| | Three months ended March 31, | | | | |
|---|---|---|---|---|---|
| | | 2011 | | 2010 | % Change |
| Marine transportation revenues | $ | 241,677 | $ | 219,562 | 10% |
| Costs and expenses: | | | | | |
| Costs of sales and operating expenses | | 142,626 | | 129,814 | 10 |
| Selling, general and administrabgcolor="#CCEEFF" style="background:#CCEEFF;padding:0in 0in 0in 0in;width:1.24%;"> | | | | | |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Net loss | | | | | (13,215,076) | | (13,215,076) |
| Unrealized gain on investments | | | | | | 331,068 | 331,068 |
| **Total comprehensive loss** | | | | | (13,215,076) | 331,068 | (12,884,008) |
| **Balance, December 31, 2008** | 20,946,382 | $ 2,095 | $ | $ 164,391,585 | $ (25,106,641) | $ 331,068 | $ 139,618,107 |
| Exercise of stock options (1/09 - 3/09 @ $0.10) | 11,002 | 1 | | 1,099 | | | 1,100 |
| Issuance of Restricted Stock | 16,486 | 1 | | (1) | | | |
| Stock based compensation | | | | 409,808 | | | 409,808 |
| **Components of comprehensive loss** | | | | | | | |
| Net loss | | | | | (4,412,558) | | (4,412,558) |
| Unrealized loss on investments | | | | | | (205,012) | (205,012) |
| **Total comprehensive loss** | | | | | (4,412,558) | (205,012) | (4,617,570) |
| **Balance, March 31, 2009** | 20,973,870 | $ 2,097 | $ | $ 164,802,491 | $ (29,519,199) | $ 126,056 | $ 135,411,445 |

The accompanying notes are an integral part of these condensed financial statements.

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**ASCENT SOLAR TECHNOLOGIES, INC.**

**(A Development Stage Company as Defined by SFAS No. 7)**

**CONDENSED STATEMENTS OF CASH FLOWS**

**(Unaudited)**

| | For the Three Months Ended March 31, 2009 | For the Three Months Ended March 31, 2008 | For the Period from inception (October 18, 2005) through March 31, 2009 |
|---|---|---|---|
| **Operating Activities:** | | | |
| Net loss | $ (4,412,558) | $ (2,398,691) | $ (29,519,199) |
| Adjustments to reconcile net loss to cash used in operating activities: | | | |
| Depreciation and amortization | 450,655 | 268,142 | 1,982,409 |
| Stock based compensation | 409,808 | 171,393 | 5,334,153 |
| Realized loss on forward contract | 556,373 | | 878,803 |
| Unrealized (gain)loss on forward contracts | (154,191) | | 612,212 |
| Charge off of deferred financing costs to interest expense | | | 198,565 |
| Charge off of bridge loan discount to interest expense | | | 800,000 |
| Changes in operating assets and liabilities: | | | |
| Accounts receivable | (112,476) | (58,751) | (448,712) |
| Related party receivables | (24,765) | (1,305) | (24,765) |
| Other current assets | 68,412 | 31,777 | (678,275) |
| Accounts payable | (30,683) | 202,405 | 234,732 |
| Related party payable | 101,838 | (58,121) | 365,118 |
| Deferred rent | (2,002) | (2,002) | 10,010 |
| Accrued expenses | 58,585 | 236,961 | 993,019 |
| Net cash used in operating activities | (3,091,004) | (1,608,192) | (19,261,930) |
| **Investing Activities:** | | | |
| Purchases of available-for-sale-securities | (55,441,495) | (46,267,031) | (751,115,244) |
| Maturities and sales of available for-sale securities | 67,769,996 | 50,321,965 | 711,637,911 |
| Purchase of property and equipment | (3,451,896) | (5,886,368) | (29,715,449) |
| Deposits on manufacturing equipment | (9,609,345) | (398,073) | (45,538,130) |
| Restricted cash for manufacturing equipment | | | (2,300,000) |
| Patent activity costs | (4,021) | (3,193) | (123,240) |
| Deposit on Building | | | (100,000) |
| Net cash used in investing activities | (736,761) | (2,232,700) | (117,254,152) |
| **Financing Activities:** | | | |
| Proceeds from bridge loan financing | | | 1,600,000 |
| Repayment of bridge loan financing | | | (1,600,000) |
| Payment of debt financing costs | | (75,000) | (273,565) |
| Payment of equity offering costs | | (314,598) | (6,829,237) |
| Proceeds from debt | 262,948 | 4,136,475 | 7,700,000 |
| Repayment of debt | (33,194) | | (233,194) |
| Proceeds from shareholder under Section 16(b) | | 148,109 | 148,109 |
| Proceeds from issuance of stock and warrants | 1,100 | 30,047,429 | 165,368,490 |
| Redemption of Class A warrants | | | (48,128) |
| Net cash provided by financing activities | 230,854 | 33,942,415 | 165,832,475 |

| | | | | | | |
|---|---|---|---|---|---|---|
| **Net change in cash and cash equivalents** | | (3,596,911) | | 30,101,523 | | 29,316,393 |
| **Cash and cash equivalents at beginning of period** | | 32,913,304 | | 580,746 | | |
| **Cash and cash equivalents at end of period** | $ | 29,316,393 | $ | 30,682,269 | $ | 29,316,393 |
| **Supplemental Cash Flow Information:** | | | | | | |
| Cash paid for interest | $ | 82,407 | $ | 16,435 | $ | 168,588 |
| Cash paid for income taxes | $ | | $ | | $ | |
| **Non-Cash Transactions:** | | | | | | |
| ITN initial contribution of assets for equity | $ | | $ | | $ | 31,200 |

The accompanying notes are an integral part of these condensed financial statements.

**ASCENT SOLAR TECHNOLOGIES, INC.**

**(A Development Stage Company as Defined by SFAS No. 7)**

**NOTES TO CONDENSED FINANCIAL STATEMENTS**

**NOTE 1. ORGANIZATION**

Ascent Solar Technologies, Inc. (Ascent or the Company) was incorporated on October 18, 2005 from the separation by ITN Energy, Inc. (ITN) of its Advanced Photovoltaic Division and all of that division s key personnel and core technologies. ITN, a private company incorporated in 1994, is an incubator dedicated to the development of thin-film, photovoltaic (PV) battery, fuel cell and nano technologies. Through its work on research and development contracts for private and governmental entities, ITN developed proprietary processing and manufacturing know-how applicable to PV products generally, and to Copper-Indium-Gallium-diSelenide (CIGS) PV products in particular. ITN formed Ascent to commercialize its investment in CIGS PV technologies. In January 2006, in exchange for 1,028,000 shares of common stock of Ascent, ITN assigned to Ascent all ITN s CIGS PV technologies and trade secrets and granted to Ascent a perpetual, exclusive, royalty-free worldwide license to use ITN s proprietary process, control and design technologies in the production of CIGS PV modules. Upon receipt of the necessary government approvals in January 2007, ITN assigned government-funded research and development contracts to Ascent and also transferred the key personnel working on the contracts to Ascent. Today, ITN still provides Ascent a variety of administrative and technical services such as facilities management, equipment maintenance, procurement, and technical support services.

**NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Basis of Presentation:** The Company s activities to date have substantially consisted of raising capital, research and development, and the development of a 1.5 MW production plant and additional 30 MW expansion plant. Revenues to date have been generated from the Company s governmental research and development (R&D) contracts and have not been significant. The Company s planned principal operations to commercialize flexible PV modules have not yet commenced. Accordingly, the Company is considered to be in the development stage, as defined in Statement of Financial Accounting Standards No. 7 (SFAS No. 7), *Accounting and Reporting by Development Stage Enterprises*.

**Cash Equivalents:** The Company considers all highly liquid debt securities purchased with an original maturity of three months or less to be cash equivalents. The Company maintains cash balances which may exceed federally insured limits. The Company does not believe that this results in significant credit risk.

**Investments:** The Company accounts for investments in accordance with SFAS No. 115, *Accounting for Certain Investments in Debt and Equity Securities.* The Company has classified its investments as available-for-sale. Such investments are carried at fair value, based on quoted market prices with the unrealized holding gains and losses reported as Accumulated other comprehensive income (loss) in the stockholders equity section of the balance sheet. Realized gains and losses on sales of securities are computed using the specific identification method. The Company evaluates declines in market value for potential impairment. If the decline results in a value below cost and is determined to be other than temporary, the investment is written down to its impaired value and a new cost basis is established.

**Fair Value estimates:** The fair value of an asset or liability is the amount at which it could be exchanged or settled in a current transaction between willing parties. The carrying value for cash and cash equivalents, investments, restricted cash, accounts receivable, accounts payable, accrued property and equipment, accrued expenses and other assets and liabilities approximate their fair values due to their short maturities. Effective January 1, 2008, the Company adopted SFAS No. 157, *Fair Value Measurements* (SFAS 157). In February 2008, the FASB issued FASB Staff Position No. FAS 157-2, *Effective Date of FASB Statement No. 157,* which provided a one year deferral of the effective date of SFAS 157 for non-financial assets and non-financial liabilities, except those that are recognized or disclosed in the financial statements at fair value at least annually. The Company adopted this statement for financial assets and financial liabilities and nonfinancial assets and nonfinancial liabilities recognized or disclosed at fair value on a recurring basis as of January 1, 2008. The Company adopted this statement for nonfinancial assets and nonfinancial liabilities recognized or disclosed at fair value on a nonrecurring basis as of January 1, 2009. The effect of the adoption of this statement was not material, resulting only in additional disclosures. SFAS 157 defines fair value, establishes a framework for measuring fair value under generally accepted accounting principles and enhances disclosures about fair value measurements. Fair value is defined under SFAS 157 as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date.

**Foreign Currency translation:** Bank account balances related to our forward contracts are translated to U.S. dollars utilizing the period end exchange rate. Gains or losses on foreign currency transactions are recorded in other income/loss in the Condensed Statements of Operations.

**Revenue Recognition:** Revenue to date is from governmental research and development contracts under terms that are cost plus fee or firm fixed price. Revenue from cost plus fee contracts is recognized as costs are incurred on the basis of direct costs plus allowable indirect costs and an allocable portion of the firm fixed fee. Revenue from firm fixed price contracts is recognized under the percentage-of-completion method of accounting, with costs and estimated profits included in contract revenue as work is performed. If actual and estimated costs to complete a contract indicate a loss, provision is made currently for the loss anticipated on the contract.

**Patents:** At such time as the Company is awarded patents, patent costs are amortized on a straight-line basis over the legal life, or over their estimated useful lives, whichever is shorter. As of March 31, 2009, the Company had $140,524 of net patent costs of which $28,138 represent costs net of amortization incurred for an awarded patent, and the remaining $112,386 represents costs incurred for patent applications filed. Amortization expense for the three months ended March 31, 2009 and 2008 was $1,279.

**Property and Equipment:** Property and equipment are recorded at the original cost to the Company. Assets are being depreciated over estimated useful lives of one to ten years using the straight-line method, commencing when the asset is placed in service. Leasehold improvements are depreciated over the shorter of the remainder of the lease term or the life of the improvements. Upon retirement or disposal, the cost of the asset disposed of and the related accumulated depreciation are removed from the accounts and any gain or loss is reflected in income. Expenditures for repairs and maintenance are expensed as incurred.

The Company computes depreciation expense using the straight-line method over the estimated useful lives of the assets, as presented in the table below. We amortize leasehold improvements over the shorter of their estimated useful lives or the remaining term of the lease.

| | Useful Lives in Years |
|---|---|
| Buildings | 40 |
| Manufacturing machinery and equipment | 5 - 10 |
| Furniture, fixtures, computer hardware/software | 3 - 7 |
| Leasehold improvements | life of lease |

**Long-lived assets:** We account for our long-lived, tangible assets and definitive-lived intangible assets in accordance with Statement of Financial Accounting Standards No. (SFAS, 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*). As a result, we assess long-lived assets classified as held and used, including our property, plant and equipment, for impairment whenever long-lived asset may not be recoverable. These events would include significant current period operating or cash flow losses associated with the use of a long-lived asset or group of assets combined with a history of such losses, significant changes in the manner of use of assets and significant negative industry or economic trends. We evaluated our long-lived assets for impairment for the period ending March 31, 2009 and concluded that no valuation allowances were required.

**Risks and Uncertainties:** The Company s operations are subject to certain risks and uncertainties, including those associated with: the ability to meet obligations; continuing losses; fluctuation in operating results; funding expansions; strategic alliances; financing arrangement terms that may restrict operations; regulatory issues; and competition. The recent financial crisis and the resulting tightening in the credit markets have made it more difficult to raise additional capital to fulfill our expansion business plan. Additionally, U.S. government contracts may be terminated prior to completion of full funding by the U.S. government.

**Net loss per Common Share:** Statement of Financial Accounting Standards No. 128, *Earnings Per Share,* provides for the calculation of Basic and Diluted earnings per share. Basic earnings per share include no dilution and are computed by dividing income available to common stockholders by the weighted-average number of shares outstanding during the period. Diluted earnings per share reflect the potential of securities that could share in the earnings of the Company, similar to fully diluted earnings per share. Common stock equivalents consisting of Class B warrants, IPO warrants (representative warrants), stock options and restricted stock units outstanding as of March 31, 2009 and 2008 of approximately 12.1 million and 11.5 million shares, respectively, have been omitted from loss per share because they are anti-dilutive. Basic and diluted loss per share was the same in each of the periods ended March 31, 2009 and 2008.

**Research and Development Costs:** Research and development costs are incurred during the process of researching and developing new products and enhancing our manufacturing processes and consist primarily of compensation and related costs for personnel, materials, supplies and equipment depreciation. We expense these costs as incurred until the resulting product has been completed and tested and is ready for commercial manufacturing. We also incur research and development expenses on our U.S. federal government research and development contracts and expense as incurred.

**Income Taxes:** Deferred income taxes are provided using the liability method whereby deferred tax assets are recognized for deductible temporary differences and operating loss and tax credit carry forwards and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of the changes in tax laws and rates as of the date of enactment. Interest and penalties, if applicable, would be recorded in operations.

In July 2006, the FASB issued FASB Interpretation (FIN 48), *Accounting for Uncertainty in Income Taxes*. The Company adopted the provisions of FIN 48 on January 1, 2007. As defined, FIN 48 seeks to reduce the diversity in practice associated with certain aspects of the recognition and measurement related to accounting for income taxes. The Company became subject to the provisions of FIN 48 as of January 1, 2007, and has analyzed filing positions in all of the federal and state jurisdictions where it is required to file income tax returns, as well as all open tax years in these jurisdictions. The Company has identified its federal tax return and its Colorado tax return as major tax jurisdictions, as defined. The periods subject to examination for the Company s federal and state tax returns are tax years 2005 through 2007. The Company believes that its income tax filing positions and deductions will be sustained on audit and does not anticipate any adjustments that will result in a material adverse effect on the Company s financial condition, results of operations, or cash flows. Therefore, no reserves for uncertain income tax positions have been recorded pursuant to FIN 48. In addition, the Company did not record a cumulative effect adjustment related to the adoption of FIN 48.

**Stock Based Compensation:** The Company accounts for share-based payments under the provisions of Statement of Financial Accounting Standards No. 123 (revised 2004), *Share-Based Payment,* (SFAS 123(R)) which requires the measurement and recognition of compensation expense for all share-based payment awards made to employees, officers, directors, and consultants, including employee stock options based on estimated fair values. SFAS 123(R) requires companies to estimate the fair value of share-based payment awards on the date of grant using an option-pricing model. The value of the portion of the award that is ultimately expected to vest is recognized as expense over the requisite service period in the Company s Condensed Statements of Operations. Stock based compensation is based on awards ultimately expected to vest and is reduced for estimated forfeitures. SFAS 123(R) requires forfeitures to be estimated at the time of grant and revised, as necessary, in subsequent periods if actual forfeitures differ from those estimates.

For purposes of determining estimated fair value of share-based payment awards on the date of grant under SFAS 123(R), the Company uses the Black-Scholes option-pricing model (Black-Scholes Model). The Black-Scholes Model requires the input of highly subjective assumptions. Because the Company s employee stock options may have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management s opinion, the existing models may not provide a reliable single measure of the fair value of the Company s employee stock options. Management will continue to assess the assumptions and methodologies used to calculate estimated fair value of share-based compensation. Circumstances may change and additional data may become available over time, which result in changes to these assumptions and methodologies, which could materially impact the Company s fair value determination.

The application of the SFAS 123(R) accounting principles may be subject to further interpretation and refinement over time. There are significant differences among option valuation models, and this may result in a lack of comparability with other companies that use different models, methods and assumptions. If factors change and the Company employs different assumptions in the application of SFAS 123(R) in future periods, or if the Company decides to use a different valuation model, the compensation expense that the Company records in the future

under SFAS 123(R) may differ significantly from what it has recorded in the current period and could materially affect its loss from operations, net loss and net loss per share.

**Comprehensive income (loss):** Our comprehensive income (loss) consists of our net income (loss), and changes in unrealized gains or losses on available for sale investments, the impact of which has been excluded from net loss. We present our comprehensive income (loss) in the Condensed Statements of Stockholders Equity and Comprehensive Income and (Loss). Our accumulated other comprehensive income (loss) is presented as a component of equity in our Condensed Balance

Sheets and consists of the cumulative amount of unrealized gains or losses on available-for-sale investments that we have incurred since the inception of our business.

**Reclassifications:** Certain reclassifications have been made to the 2008 financial information to conform to the 2009 presentation. Such reclassifications had no effect on net loss and are primarily related to reclassifying costs between Research and development costs and General and administrative expenses in the Condensed Statements of Operations.

**Use of Estimates:** The preparation of financial statements in conformity with generally accepted accounting principles 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 financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**Unaudited Information:** The accompanying interim financial information as of March 31, 2009 and for the three months ended March 31, 2009 and 2008 and the period from inception (October 18, 2005) through March 31, 2009 was taken from the Company s books and records without audit. However, in the opinion of management, such information includes all adjustments (consisting only of results of normal recurring accruals) that are necessary to properly reflect the financial position of the Company as of March 31, 2009 and the results of operations for the three months ended March 31, 2009 and 2008 and the period from inception (October 18, 2005) through March 31, 2009 so that the financial statements are not misleading.

**Recent Accounting Pronouncements:** In May 2008, the FASB issued SFAS No. 162, The Hierarchy of Generally Accepted Accounting Principles, which becomes effective upon approval by the SEC. The standard sets forth the sources of accounting principles and provides entities with a framework for selecting the principles used in the preparation of financial statements that are presented in conformity with GAAP. It is not expected to change any of our current accounting principles or practices and therefore, is not expected to have a material impact on our financial statements.

**NOTE 3. LIQUIDITY AND CONTINUED OPERATIONS**

As discussed in Note 1, the Company is in the development stage and is currently incurring significant losses from operations. As of March 31, 2009, the Company had $71.2 million in cash, restricted cash and investments of which approximately $40 million we intend to use in 2009 for progress payments to our equipment suppliers for our 30 MW line and $2 million for facility infrastructure for our 30 MW expansion. An additional $26 million is required in 2010 for final payments to our equipment suppliers on the 30MW line.

The Company commenced commercial production on its 1.5 MW production line in the first quarter 2009. We do not expect that sales revenue from the 1.5 MW production line will be sufficient to support operations and cash requirements, and it is unlikely that sales revenue will support operating cash requirements unless we achieve actual production capacity of at least 30 MW per year. Our original equipment delivery schedule called for installation of all of the 30 MW production equipment during 2009. Due to the recent financial crisis affecting the financial markets, our ability to obtain credit or to raise additional capital has become increasingly difficult. In order to preserve cash, we have extended the equipment delivery schedule related to the first 30MW of annual rated production capacity to 2010. We now expect to begin production using equipment with an annual rated production capacity of approximately 15 MW in early 2010, and full 30 MW of annual rated production capacity by the end of 2010.

The Company expects its current cash balance to be sufficient to cover its operational expenditures through 2009 based on currently known factors, although it expects that it will need to raise additional capital prior to early 2010 to complete its expansion plans.

**NOTE 4. FAIR VALUE MEASUREMENTS**

Effective January 1, 2008, the Company adopted SFAS No. 157, *Fair Value Measurements* (SFAS 157). In February 2008, the FASB issued FASB Staff Position No. FAS 157-2, *Effective Date of FASB Statement No. 157*, which provided a one year deferral of the effective date of SFAS 157 for non-financial assets and non-financial liabilities, except those that are recognized or disclosed in the financial statements at fair value at least annually. The Company adopted this statement for financial assets and financial liabilities and nonfinancial assets and nonfinancial liabilities recognized or disclosed at fair value on a recurring basis as of January 1, 2008. The Company adopted this statement for nonfinancial assets and nonfinancial liabilities recognized or disclosed at fair value on a nonrecurring basis as of January 1, 2009. The effect of the adoption of this statement was not material, resulting only in additional disclosures. SFAS 157 defines fair value,

establishes a framework for measuring fair value under generally accepted accounting principles and enhances disclosures about fair value measurements. Fair value is defined under SFAS 157 as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value under SFAS 157 must maximize the use of observable inputs and minimize the use of unobservable inputs. The standard describes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value which are the following:

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

- Level 2 Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

- Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

In accordance with SFAS 157, the following table represents the Company s fair value hierarchy for its financial assets measured at fair value on a recurring basis and its classification on the balance sheet as of March 31, 2009:

| | Level 1 | Level 2 | Level 3 | Total | Cash Equivalents | Investments |
|---|---|---|---|---|---|---|
| **Financial Assets:** | | | | | | |
| U.S. government securities | $ | $ 34,874,916 | $ | $ 34,874,916 | $ | $ 34,874,916 |
| Money market funds | 22,103,325 | | | 22,103,325 | 22,103,325 | |
| Corporate securities | | 4,728,471 | | 4,728,471 | | 4,728,471 |
| Municipal bonds | | | | | | |
| | $ 22,103,325 | $ 39,603,387 | $ | $ 61,706,712 | $ 22,103,325 | $ 39,603,387 |
| **Financial Liabilities:** | | | | | | |
| Derivative liability | $ | $ 612,212 | $ | $ 612,212 | | |

**NOTE 5. INVESTMENTS**

The Company accounts for investments in accordance with SFAS No. 115, *Accounting for Certain Investments in Debt and Equity Securities.* Securities held by the Company as of March 31, 2009 are classified as available-for-sale and consisted of U.S. government securities, corporate securities, and municipal bonds. Such investments are carried at fair value, based on quoted market prices with the unrealized holding gains and losses reported as Accumulated other comprehensive income in the stockholders equity section of the balance sheet. Realized gains and losses on sales of securities are computed using the specific identification method. The Company evaluates declines in market value for potential impairment. If the decline results in a value below cost and is determined to be other than temporary, the investment is written down to its impaired value and a new cost basis is established. A summary of available-for-sale securities as of March 31, 2009 is as follows:

| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Fair Value |
|---|---|---|---|---|
| U.S. government securities | $ 34,748,883 | $ 180,836 | $ (54,803) | $ 34,874,916 |
| Corporate securities | 4,728,448 | 13,397 | (13,374) | 4,728,471 |
| Municipal bonds | | | | |
| Total | $ 39,477,331 | $ 194,233 | $ (68,177) | $ 39,603,387 |

Contractual maturities of our available-for-sale investments as of March 31, 2009 were as follows:

| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Fair Value |
|---|---|---|---|---|
| One year or less | $ 35,041,632 | $ 141,661 | $ (68,177) | $ 35,115,116 |
| One year to two years | 4,435,699 | 52,572 | | 4,488,271 |
| Total | $ 39,477,331 | $ 194,233 | $ (68,177) | $ 39,603,387 |

We typically invest in highly-rated securities with low probabilities of default. Our investment policy specifies minimum investment grade criteria, types of acceptable investments, concentration limitations and duration.

**NOTE 6. ACCOUNTS RECEIVABLE**

Effective January 1, 2007, the Company completed the novation, or transfer, of approximately $3.5 million in government funded research and development contracts (R&D contracts) from ITN to the Company. The various contracts are being performed for U.S. government customers that include the Air Force Research Laboratory and the National Aeronautics and Space Administration. In addition to approximately $1.6 million of future revenues to be provided under the transferred contracts, the key scientists, engineers, and process technicians responsible for deliverables under the transferred contracts were also transferred from ITN to become full-time Ascent employees. In 2007 and 2008, additional R&D contracts were awarded to the Company of approximately $3.4 million.

Accounts receivable consists mainly of billed and unbilled amounts under these R&D contracts. Management deems all accounts receivable to be collectible.

The following table summarizes components of accounts receivable related to R&D contracts:

| | | **As of March 31, 2009** | | **As of December 31, 2008** |
|---|---|---|---|---|
| Billed receivables | $ | 398,126 | $ | 273,995 |
| Unbilled receivables | | 11,026 | | 62,241 |
| Total | $ | 409,152 | $ | 336,236 |

Unbilled receivables represent costs incurred but not yet billed, including retainage amounts by the government on contracts that have not been closed out at the end of the period.

*Provisional Indirect Cost Rates* During 2007, 2008 and 2009, the Company billed the government under cost-based R&D contracts at provisional billing rates which permit the recovery of indirect costs. These rates are subject to audit on an annual basis by the government agencies cognizant audit agency. The cost audit will result in the negotiation and determination of the final indirect cost rates. The Company has not been audited and has not received final rate determinations for the year ended December 31, 2007 or December 31, 2008. The final rates, if different from the actual, may create an additional receivable or liability. In the opinion of management, re-determination of any cost-based contracts will not have a material effect on the Company s financial position or results of operations.

*Contract Status* The Company has authorized but not completed contracts on which work is in process as follows:

| | As of March 31, 2009 | As of December 31, 2008 |
|---|---|---|
| Total contract price of initial contract awards, including exercised options and approved change orders (modifications) | $ 6,889,991 | $ 6,889,991 |
| Completed to date(1) | (4,777,896) | (4,307,951) |
| Authorized backlog | $ 2,112,095 | $ 2,582,040 |

(1) Includes work performed by ITN prior to January 1, 2007.

**NOTE 7. PROPERTY AND EQUIPMENT**

The following table summarizes property and equipment:

| | As of March 31, 2009 | As of December 31, 2008 |
|---|---|---|
| Furniture, fixtures, computer hardware and computer software | $ 776,780 | $ 715,310 |
| Manufacturing machinery and equipment | 12,375,755 | 12,257,585 |
| Leasehold improvements | 789,342 | 789,342 |
| Net depreciable property, plant and equipment | 13,941,877 | 13,762,237 |
| Building | 5,653,685 | 5,634,060 |
| Building construction in process | 10,738,313 | 9,050,136 |
| Net property, plant and equipment | 30,333,875 | 28,446,433 |
| Less: Accumulated depreciation and amortization | (1,970,359) | (1,521,922) |
| Property and equipment, net | $ 28,363,516 | $ 26,924,511 |

Property and Equipment depreciation and amortization expense for the three months ended March 31, 2009 and 2008 was $448,437 and $264,959, respectively.

**NOTE 8. DEPOSITS ON MANUFACTURING EQUIPMENT**

As of March 31, 2009, the Company had entered into purchase agreements of approximately $102 million for the acquisition of manufacturing production tools and approximately $7 million for one meter wide manufacturing development tools for the Company s planned expansion to approximately 30 MW of rated capacity and planned future implementation of one meter wide substrates. As of March 31, 2009, the Company had made or accrued progress payments of approximately $49.4 million on these purchase agreements which are reflected on the Balance Sheet as Deposits on manufacturing equipment. Generally, these purchase agreements have milestone-based deliverables, such as the Company s acceptance of design requirements and successful installation and commissioning of the equipment.

**NOTE 9. DEBT**

In January 2006, the Company completed a $1.6 million bridge loan (Bridge Financing) from lenders (Bridge Noteholders) to help meet the Company s working capital needs. The loans (Bridge Loans) accrued interest at an annual rate of 10% and were due and payable upon the earlier of January 2007 or the completion of Ascent s public offering of equity securities with gross proceeds of at least $5,000,000 (Qualified Public Offering). In July 2006, with the proceeds from a Qualified Public Offering (*i.e.,* the Company s initial public offering or IPO), the Company repaid the Bridge Loans including accrued interest.

In connection with the Bridge Loans, the Company issued rights (Bridge Rights) to the Bridge Noteholders. One Bridge Right was issued for every $25,000 loaned. In July 2006, upon completion of the IPO, the holders of Bridge Rights received restricted units. The holder of each Bridge Right received that number of units equal to $25,000 divided by the IPO price of the units of $5.50 for a total of 290,894 units. The units are identical to those offered in Ascent s IPO and consisted of one share of common stock, one redeemable Class A public warrant and two non-redeemable Class B warrants. In September 2006, the SEC declared effective the Company s Registration Statement on Form SB-2 (Reg. No. 333-137008)

for the shares and warrants underlying the 290,894 units issued in connection with the Bridge Rights. The Registration Statement on Form SB-2 subsequently was converted to a Registration Statement on Form S-3.

Paulson Investment Company, Inc. acted as the placement agent for the Bridge Financing. The Company paid Paulson Investment Company, Inc. a commission equal to 10% of the gross proceeds from the Bridge Financing, plus reasonable out-of-pocket expenses. The Bridge Loans and the Bridge Rights were allocated for accounting purposes based on the relative fair values of the Bridge Loans without the Bridge Rights and the Bridge Rights themselves at the time of issuance. The actual value of the Bridge Loans and the Bridge Rights was computed at $1,600,000 each for a total value of $3,200,000. Since they were each of equal value, the $1,600,000 of proceeds was allocated 50% to the Bridge Loans and 50% to the Bridge Rights (*i.e.,* $800,000 each). The Bridge Rights of $800,000 were accounted for as paid-in capital.

The discount for the commission ($160,000) and the Bridge Rights ($800,000) were amortized into interest expense over the life of the loans. In July 2006 with the repayment of the Bridge Loans, the remaining unamortized balance of the discount for commission and Bridge Rights of $960,000 was recognized as interest expense in the Condensed Statements of Operations.

On February 8, 2008, the Company acquired an approximately 120,000 square foot manufacturing and office facility in Thornton, Colorado, for approximately $5.5 million. The purchase was financed by a promissory note, deed of trust and construction loan agreement with the Colorado Housing and Finance Authority ( CHFA ) ( Construction Loan ), which provided the Company borrowing availability of up to $7.5 million for the building and building improvements. The Company paid approximately $1.3 million in cash and was advanced approximately $4.2 million from CHFA to fund the initial acquisition of the property. The terms of the Construction Loan required payments of interest only at 6.6% on the outstanding balance. On January 29, 2009, the Construction Loan was converted into a permanent loan pursuant to a loan modification agreement between the Company and CHFA ( Permanent Loan ). The Permanent Loan has an interest rate of 6.6% and the principal will be amortized over a period of approximately 19 years and 1 month consistent with a maturity date 20 years after the incurrence of the Construction Loan on February 8, 2008. An additional $75,000 loan commitment fee was paid in 2008 and reflected on the balance sheet in non-current assets. This fee is being amortized into interest expense over the 20 year life of the Construction and the Permanent Loan. As of March 31, 2009, we have expended approximately $9.8 million in building improvements of which $3.4 million was funded by CHFA. As of March 31, 2009, the renovation was substantially complete. Additional infrastructure costs related to the build-out of two additional structures, electrical upgrade and other utilities have increased our budget for our building improvements since originally projected early in 2008. We will incur a prepayment penalty if the Permanent Loan is prepaid prior to December 31, 2015 equal to the sum of (i) the present value of the total principal and interest payments due under the Note from the prepayment date to December 31, 2015, and (ii) the present value of the remaining principal balance of the Note that would have been due as of December 31, 2015, less the principle amount of the Note outstanding. Further, pursuant to certain negative covenants contained in the deed of trust associated with the permanent loan, until the Permanent Loan is repaid and all of our secured obligations performed in full, we may not, among other things, without CHFA s prior written consent: create or incur additional indebtedness; merge or consolidate with any other entity; or make loans or advances to our officers, shareholders, directors or employees, which consent will not be unreasonably withheld.

On January 29, 2009, the date of the closing of our Permanent Loan of $7,500,000, our future principal payments were due as follows:

| | | |
|---|---|---|
| 2009 | $ | 187,150 |
| 2010 | | 217,463 |
| 2011 | | 232,257 |
| 2012 | | 248,059 |
| 2013 | | 264,935 |
| Thereafter | | 6,350,136 |
| | $ | 7,500,000 |

**NOTE 10. DERIVATIVE FINANCIAL INSTRUMENTS**

The Company is actively engaged in purchasing manufacturing equipment internationally and is exposed to foreign currency risk. In July 2008 and March 2009, the Company entered into fair value hedges utilizing forward contracts designed to match scheduled contractual payments to equipment suppliers which are denominated in Euros and Yen. The total notional value of the Euro forward contracts was 6.4 million with various contract settlement dates beginning September 15, 2008 through July 31, 2009. The total notional value of the Yen forward contracts was ¥521.4 million with contract settlement

dates of March and April 2009. The Company elected not to use hedge accounting under SFAS 133 and accordingly, the unrealized losses on each forward contract were determined at each balance sheet date based upon current market rates and are reported as Unrealized losses on forward contracts in the Condensed Statement of Operations. Upon settlement of the forward contracts, realized gains or losses are reported in the Condensed Statement of Operations as Realized gains or losses on forward contracts. As of March 31, 2009, the unrealized gain on these forward contracts was $154,191 and the realized loss was $566,373. Although the hedging activity is designed to fix the dollar amount to be expended, the asset purchased is recorded at the spot rate in effect as of the date of the payment to the supplier. The difference between the spot rate and the forward rate has been reported as a loss on forward contract. During the first quarter 2009, forward contracts for delivery of 1,820,560 and ¥393,750,000 were settled and deposited in a bank account for future payments to our equipment suppliers. Period end translation adjustments related to the Euros and Yen on deposit in our bank account are accounted for as realized gains and losses on forward contract transactions. Included in cash and cash equivalents is $2,518,027 related to 1,892,336 Euros and $3,973,660 related to 393,750,000 Yen held as of March 31, 2009. In connection with the forward contracts, the Company has a $2.3 million deposit account with the bank holding the forward contracts which is reflected as restricted cash on the March 31, 2009 balance sheet. Derivative financial instruments are not used for speculative or trading purposes. See Note 4 for information about the fair value measurement of our derivative financial instruments.

**NOTE 11. STOCKHOLDERS EQUITY**

The Company s authorized capital stock consists of 75,000,000 shares of common stock, $0.0001 par value, and 25,000,000 shares of preferred stock, $0.0001 par value. In November 2005, the Company issued 972,000 shares of common stock at a price of $0.04 per share. The Company has recorded for financial statement purposes the 972,000 shares at a fair value of $1.00 per share. The Condensed Statements of Stockholders Equity reflects compensation expense of $933,120 related to the recording of this stock transaction. In January 2006, in consideration of certain asset transfers, licenses and service agreements, the Company issued 1,028,000 shares of common stock to ITN Energy Systems, Inc.

Preferred stock, $0.0001 par value per share, may be issued in classes or series. Designations, powers, preferences, rights, qualifications, limitations and restrictions are determined by the Company s Board of Directors.

**Initial Public Offering:** On July 10, 2006, the SEC declared effective the Company s Registration Statement on Form SB-2 (Reg. No. 333-131216), and the Company completed its IPO of 3,000,000 units on July 14, 2006. Each unit consisted of one share of common stock, one redeemable Class A warrant and two non-redeemable Class B warrants. The managing underwriter of the IPO was Paulson Investment Company, Inc. The IPO price was $5.50 per unit. The gross proceeds of the offering were $16,500,000. Ascent s net proceeds from the offering, after deducting the underwriter s discount of $1,097,250 and other fees and expenses, aggregated approximately $14,000,000.

The common stock and Class A and Class B warrants traded only as a unit through August 9, 2006, after which the common stock, the Class A warrants and the Class B warrants began trading separately.

*Class A warrants.* On May 24, 2007, the Company publicly announced that it intended to redeem its outstanding Class A warrants. The Class A warrants became eligible for redemption by the Company at $0.25 per warrant on April 16, 2007, when the last reported sale price of the Company s common stock had equaled or exceeded $9.35 for five consecutive trading days. There were 3,290,894 Class A warrants issued in connection with the Company s initial public offering, including the warrants issued to the Bridge Noteholders. The Class A warrants were exercisable at a price of $6.60 per share.

The exercise period ended June 22, 2007. During the exercise period, 3,098,382 Class A warrants (94.1% of the total outstanding) were exercised for an equal number of shares of common stock, and the Company received $20,449,321 in proceeds from the warrant exercises. At the end of the exercise period, 192,512 Class A warrants remained outstanding. The Company has set aside funds with its warrant transfer agent to redeem the outstanding warrants for $0.25 per warrant, or a total cost of $48,128. As of March 31, 2009, 9,090 Class A warrants remain unredeemed.

*Class B warrants.* The Class B warrants included in the units became exercisable on August 10, 2006. The exercise price of a Class B public warrant is $11.00. The Class B warrants expire on July 10, 2011. The Company does not have the right to redeem the Class B warrants. During the years ended December 31, 2008 and 2007, 98,800 and 11,000 Class B warrants, respectively were exercised resulting in proceeds to the Company of approximately $1,086,800 and $121,000 respectively. As of March 31, 2009, 10,502,583 Class B warrants were outstanding.

*IPO warrants.* Warrants to purchase 300,000 units at $6.60 were issued to underwriters of the Company s initial public offering in July 2006 (representative s warrants). A unit consists of one share of common stock, one Class A redeemable warrant and two Class B non-redeemable warrants. The warrants expire on July 10, 2011. Upon exercise of the

representative s warrants, holders will be forced to choose whether to exercise the underlying Class A warrants or hold them for redemption. As noted above, on June 25, 2007, any Class A warrants then outstanding expired and became redeemable.

Representative s warrants to purchase 150,000 units have been exercised as of December 31, 2007, as have the 150,000 underlying Class A warrants resulting in an issuance of 300,000 shares of common stock and 300,000 Class B warrants for total proceeds to the Company of $1.98 million. During the year ended December 31, 2008 an additional 37,500 units were exercised, as well as 37,500 underlying Class A warrants resulting in an issuance of 75,000 shares of common stock and 75,000 Class B warrants for total proceeds to the Company of $495,000. To the extent that holders of representative s warrants are entitled to receive Class A warrants upon exercise of the representative s warrants, those warrants will be immediately subject to call for redemption at $0.25 per warrant. The holders will then have to decide whether to exercise their Class A warrants or hold them for redemption. As of March 31, 2009, 112,500 representative s warrants remained unexercised.

**Private Placement of Securities:** The Company completed a private placement of securities with Norsk Hydro Produksjon AS (Hydro) in March 2007. Hydro is a subsidiary of Norsk Hydro ASA. Hydro purchased 1,600,000 shares of the Company s common stock (representing 23% of the Company s outstanding common stock post transaction) for an aggregate purchase price of $9,236,000. The Company recorded $75,807 of costs associated with the private placement as a reduction to Additional paid in capital on the Company s Balance Sheets. In connection with the private placement, Hydro was granted options to purchase additional shares and warrants.

In August 2007, Hydro acquired an additional 934,462 shares of the Company s common stock and 1,965,690 Class B warrants through the exercise of an option previously granted to Hydro and approved by Ascent s stockholders in June 2007. Gross proceeds to the Company were $10.48 million, and reflected per share and per warrant purchase prices equal to the average of the closing bids of each security, as reported by NASDAQ, for the five consecutive trading days preceding exercise. After acquiring these additional shares, Hydro again held 23% of the total outstanding common shares, after its holdings were diluted as the result of the redemption of Class A warrants and 23% of total outstanding Class B warrants. Pursuant to a second option that was approved by Ascent s stockholders in June 2007, beginning December 13, 2007, Hydro was entitled to purchase additional shares and Class B warrants up to a maximum of 35% of each class of security.

In March 2008, Hydro acquired an additional 2,341,897 shares of the Company s common stock and 1,689,905 Class B warrants through the exercise of the second option previously granted to Hydro and approved by Ascent s stockholders in June 2007, resulting in Hydro ownership of approximately 35% of each class of security. Gross proceeds to the Company were $28.4 million, and reflected per share and per warrant purchase prices were equal to the average of the closing bids of each security, as reported by NASDAQ, for the five consecutive trading days preceding exercise. As a result of the Company s Secondary Public Offering in May 2008, Hydro s holdings were diluted to approximately 27%.

On October 8, 2008, Hydro acquired an additional 2,421,801 shares of the Company s common stock. The purchase resulted in a return to Hydro s ownership of approximately 35% of the Company s common stock. Gross proceeds to the company from the follow on investment were approximately $15 million, and reflect per share purchase prices equal to the average of the closing bids of each security, as reported by NASDAQ, for the five consecutive trading days preceding exercise. Until June 15, 2009, the second option entitles Hydro to purchase from the Company additional restricted shares of common stock and Class B warrants to maintain ownership of up to 35% of issued and outstanding common stock and Class B warrants.

**Other Proceeds:** During the three months ended March 31, 2008, the Company received proceeds from a greater than 10% shareholder equal to the profits realized on the sale of the Company s stock that was purchased and sold within a six month or less time frame. Under Section 16(b) of the Securities and Exchange Act, the profit realized from this transaction by the greater than 10% shareholder must be disgorged to the Company under certain circumstances. The Company has recorded the proceeds received on this transaction of $148,109 as Additional paid in capital and is reflected on the Condensed Statements of Stockholders Equity.

**Secondary Public Offering:** On May 15, 2008, the SEC declared effective the Company s Registration Statement on Form S-3 (Reg. No. 333-149740), and the Company completed its Secondary Public Offering of 4,370,000 shares of common stock, which included 570,000 shares issued upon the underwriter s exercise of their overallotment in full. The offering price of $14.00 per share resulted in proceeds of $61,180,000. After deducting underwriting discounts and commissions and offering expenses of approximately $4,361,000, net proceeds to the Company were approximately $56,819,000. JP Morgan was the managing underwriter of the Secondary Public Offering.

As of March 31, 2009, the Company had 20,973,870 shares of common stock and no shares of preferred stock outstanding.

**NOTE 12. STOCK BASED COMPENSATION**

**Stock Option Plan:** The Company s 2005 Stock Option Plan, as amended (Stock Option Plan) provides for the grant of incentive or non-statutory stock options to the Company s employees, directors and consultants. The Board of Directors adopted and the stockholders approved an increase in the total shares of common stock reserved for issuance under the Stock Option Plan from 1,000,000 to 1,500,000 on July 1, 2008.

**Restricted Stock Plan:** The Board of Directors adopted the Company s 2008 Restricted Stock Plan with stockholder approval on July 1, 2008. The Restricted Stock Plan reserves up to 750,000 shares of our common stock for restricted stock awards and restricted stock units to eligible employees, directors and consultants of the Company.

The Stock Option Plan and the Restricted Stock Plan are administered by the Compensation Committee of the Board of Directors, which determines the terms of the options and shares, including the exercise price, expiration date, vesting schedule and number of shares. Equity Compensation awards to executive officers and directors are also subject to approval by the Board of Directors. The term of any incentive stock option granted under the Stock Option Plan may not exceed ten years, or five years for options granted to an optionee owning more than 10% of the Company s voting stock. The exercise price of an incentive stock option granted under the Option Plan must be equal to or greater than the fair market value of the shares of the Company s common stock on the date the option is granted. An incentive stock option granted to an optionee owning more than 10% of the Company s voting stock must have an exercise price equal to or greater than 110% of the fair market value of the Company s common stock on the date the option is granted. The exercise price of a non-statutory option granted under the Option Plan must be equal to or greater than 85% of the fair market value of the shares of the Company s common stock on the date the option is granted. According to the terms of the Restricted Stock Plan, no individual may be granted, in any fiscal year, more than 200,000 shares. Vesting of shares of restricted stock granted under the Restricted Stock Plan may occur over a specified period of time or based upon performance metrics announced at the time of grant.

**Stock Based Compensation:** The Company accounts for share-based payments under the provisions of Statement of Financial Accounting Standards No. 123 (revised 2004), *Share-Based Payment,* (SFAS 123(R)) which requires the measurement and recognition of compensation expense for all share-based payment awards made to employees, officers, directors and consultants, including employee stock options based on estimated fair values. Stock based compensation expense recognized in the Condensed Statements of Operations for the three months ended March 31, 2009 and 2008 and for the period from inception (October 18, 2005) through March 31, 2009 is based on awards ultimately expected to vest and it has been reduced for estimated forfeitures.

The weighted average estimated fair value of stock options granted for the three months ended March 31, 2009 was $3.49. There were no stock options granted in the three months ended March 31, 2008. Fair value was calculated using the Black-Scholes Model with the following weighted average assumptions:

| | For the Three Months Ended March 31, | |
|---|---|---|
| | 2009 | 2008 |
| Expected volatility | 108.9% | |
| Risk free interest rate | 1.9% | |
| Expected dividends | | |
| Expected life (in years) | 6.45 | |

For the three months ended March 31, 2009, the Company based its estimate of expected volatility, expected life and expected forfeiture rate on historical company experience.

Stock-based compensation expense is calculated on a straight-line basis over the vesting periods of the related options. In future periods, the compensation expense that the Company records under SFAS 123(R) may differ significantly from what the Company recorded in the current period, as the Company builds company-specific performance history.

As of March 31, 2009, the Company had approximately $1,651,000 of total compensation cost related to non-vested stock option awards not yet recognized and expects to recognize these costs over a weighted average period of approximately 2.2 years. As of March 31, 2009, approximately 1,027,000 shares were expected to vest in the future at a weighted average

exercise price of $4.91. As of March 31, 2009, approximately 77,500 shares remained available for future grants under the Option Plan.

In addition to the stock options discussed above, the Company recognized share-based compensation expense related to restricted stock awards and restricted stock units of $118,974 and $0 for the three months ended March 31, 2009 and 2008, respectively. The weighted average grant date fair value of restricted stock for the three months ended March 31, 2009 and 2008 was $3.76 and $16.51 per share respectively. Total unrecognized share-based compensation expense from unvested restricted stock awards and restricted stock units as of March 31, 2009 was approximately $593,000 which is expected to be recognized over a weighted average period of approximately 2.1 years.

Total stock-based compensation expense related to both stock options and restricted stock awards and units is reflected in our Condensed Statements of Operations as follows:

| | For the three months ended March 31, | | | |
|---|---|---|---|---|
| | | 2009 | | 2008 |
| **Stock-based compensation cost included in:** | | | | |
| Research and development | $ | 175,643 | $ | 90,415 |
| Selling, general and administrative | | 234,165 | | 80,978 |
| Total stock-based compensation cost | $ | 409,808 | $ | 171,393 |

**NOTE 13. RELATED PARTY TRANSACTIONS**

Included in General and administrative expenses for the three months ended March 31, 2009 and 2008 are $201,057 and $247,259 respectively, of costs to ITN for facility sublease costs, administrative support expenses and reimbursement of shared expenses.

Included in Research and development expenses for the three months ended March 31, 2009 and 2008 are $594,398 (including $31,312 of fee) and $243,390, respectively, of R&D and manufacturing support activities provided by ITN. Beginning January 1, 2009, all R&D and manufacturing activity provided by ITN included cost plus 7% fee. Related party payables of $365,119 and $263,280 as of March 31, 2009 and December 31, 2008 respectively, represent costs remaining to be paid to ITN for these expenditures and amounts payable to officers and directors for Board of Directors fees and reimbursement of travel expenditures. Related party receivables of $24,765 and $0 as of March 31, 2009 and December 31, 2008 respectively, represent insurance related costs paid by the Company on behalf of ITN.

Included in Property and equipment and Deposits on manufacturing equipment as of March 31, 2009 is $1,708,956 of costs to ITN for the construction of manufacturing and research and development equipment incurred during the period January 1, 2006 to March 31, 2009.

**NOTE 14. COMMITMENTS**

**Sublease Agreement:** On November 1, 2005, the Company entered into a sublease agreement with ITN, a greater than five percent stockholder of the Company, to lease office space in Littleton, Colorado. In 2005 and 2006, two Board

members of Ascent were partial owners of the company that leased this office space to ITN. As of January 1, 2007, they no longer have an investment in the building the Company is subleasing from ITN. Future minimum payments due under the sublease as of December 31, 2008 are as follows:

| **Year ending December 31:** | | |
|---|---|---|
| 2009 | $ | 227,896 |
| 2010 | $ | 113,948 |

The Company is also responsible for payment of pass-through expenses such as property taxes, insurance, water and utilities. Rent expense for the three months ended March 31, 2009 and 2008 was $59,265 and $56,973, respectively.

**Patent License Agreements:** In 2006, the Company entered into two non-exclusive patent license agreements. In consideration for the right to license certain inventions, the Company is required to pay annual royalty payments based on net sales of products manufactured using the licensed technology. If there are no net sales of products manufactured using the

licensed technology, then a minimum royalty payment is required. The Company has made payments for the annual minimum royalties due associated with these patent license agreements.

**NOTE 15. RETIREMENT PLAN**

On July 1, 2006, the Company adopted a qualified 401(k) plan ( Plan ) which provides retirement benefits for all of its eligible employees. Under the plan, employees become eligible to participate at the first entry date, provided that they are at least 21 years of age. The participants may elect through salary reduction to contribute up to ceilings established in the Internal Revenue Code and the Plan documents. The Company will match 100% of the first six percent of employee eligible compensation contributions per pay period. In addition, the Company may make discretionary contributions to the Plan as determined by the Board of Directors. Employees are immediately vested in all salary reduction contributions. Rights to benefits provided by the Company s discretionary and matching contributions vest 100% after the first year of service.

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

*The following discussion of our financial condition and results of operations should be read in conjunction with our audited financial statements and the notes to those financial statements appearing elsewhere in this Form 10-Q. This discussion and analysis contains statements of a forward-looking nature relating to future events or our future financial performance. As a result of many factors, our actual results may differ materially from those anticipated in these forward-looking statements. These statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by these forward-looking statements.*

**Overview**

We are a development stage company formed to commercialize flexible PV modules using proprietary technology. For the three months ended March 31, 2009, we generated approximately $516,000 in revenues. A majority of revenue was from government research and development contracts not from our planned principal operations to commercialize flexible PV modules. As of March 31, 2009, we had an accumulated deficit of approximately $29.5 million. Under our current business plan, we expect losses to continue through 2009 at which point we plan to commence production on our initial 30 MW manufacturing line that is currently in development. To date, we have financed our operations primarily through public and private equity financings including our recent secondary public offering of 4,370,000 shares of common stock with net proceeds of approximately $56.8 million completed in May 2008, and an additional investment of approximately $15 million by our largest shareholder Norsk Hydro in October 2008. The proceeds from these stock sales are primarily being utilized to fund the equipment purchases for our 30 MW production facility in Thornton, Colorado.

While focused on speed to market, we believe that quality and consistency of product will be paramount to our success in the marketplace. Consequently, our path to commercialization is defined by a highly disciplined, staged progression based upon the achievement of key milestones and supported by over fourteen years of concerted research and development activity by our scientists. Our progression also takes into account market conditions, as well as financing options. In keeping with our philosophy, we completed construction of a 1.5 MW production line in December 2007. In March 2008, we demonstrated initial operating capability (IOC) of our 1.5 MW production line by initiating production trials as an end-to-end integrated process. Early IOC production trials resulted in average thin-film device efficiencies of 9.5% and small area monolithically integrated module efficiencies of over 7%. Recent and ongoing production optimization trials have resulted in thin-film device efficiencies in the 9.5% to 11.5% range and corresponding module efficiencies in the 7.0% to 9.0% range. In the fourth quarter 2008 the U.S. Department of Energy s National Renewable Energy Laboratory (NREL) independently verified that the modules produced on our 1.5 MW line measured as high as 9.64% in conversion efficiency. The test modules measured six inches wide by one foot long and serve as our building block for both building integrated PV ( BIPV ) and portable power products. During 2008 we focused on testing and qualifying our 1.5 MW production line in anticipation of commencing limited regular production. During the first quarter of 2009, we began regular production of monolithically integrated flexible CIGS modules from our 1.5 MW production line. We expect that process optimization will be an ongoing effort as we continuously strive for improvements in production yield, production throughput, and product efficiency that have a direct bearing on our cost competitiveness in the marketplace.

During 2008, we initiated the critical tasks of internal product testing and product development with customers. In 2009, we continued those tasks further and have commenced prototype development with our BIPV, electronic integrated PV ( EIPV ) and military customers by providing them test samples from our 1.5MW production line. At the same time we expect to complete the internal testing and product certification in the second half of 2009.

The Company s new manufacturing facility in Thornton, Colorado is in the final stages of completion and will be ready to accommodate installation of the equipment in the second quarter of 2009. Production tooling and equipment for the 30 MW plant began arriving in the first

quarter of 2009 and installation is scheduled to be completed in the first half of 2010. We expect to begin production with an annual rated capacity of 15 MW by the middle of 2010, and 30 MW of annual capacity by the end of 2010. We intend to incrementally expand our production capacity to 110 MW or greater by adding more capacity based on manufacturing developments, market conditions and availability of financing.

**Commercialization and Manufacturing Expansion Plan**

We intend to be the first company to manufacture large, roll-format, PV modules in commercial quantities that use CIGS on a flexible, plastic substrate. Our manufacturing expansion plan entails the design, installation, qualification, testing

and operation of additional production tools to increase our rated production capacity. We intend to incrementally expand our aggregate production capacity to 30 MW by attaining the following milestones within the time frames indicated:

- Second half of 2009: complete product certification with Underwriters Laboratory (UL) in the U.S. and Technischer Überwachungs-Verein (TÜV) in Europe from 1.5 MW production line.

- Fourth quarter of 2009: begin qualification of production tools for the first 30 MW.

- First half of 2010: begin production and ramp up of the first half of initial 30 MW capacity.

- Second half of 2010: commence ramp up to full 30 MW of rated capacity.

Although we currently plan to expand our production capacity to 110 MW or more by adding more capacity, the actual timing and amount of production capacity for the initial 30 MW and follow on capacity that we install may significantly deviate due to market conditions, availability of financing, timeliness of delivery of production tools, product performance and other factors.

Rated production capacity refers to our expected level of annual production upon optimization of our production process and is based on assumed production yields and module efficiencies. The actual production levels that we are able to realize at any point during our planned expansion will depend on a variety of factors, including our ability to optimize our production process to achieve targeted production yields and module efficiencies.

Although we currently plan to expand our production capacity in accordance with the timeline above, the actual timing and amount of production capacity that we install may significantly deviate from the above plan due to market conditions, availability of financing, timeliness of delivery of production tools, product performance and other factors. See Significant Trends, Uncertainties and Challenges below. We also recognize the importance of developing strategies and plans that may allow for the timely acceleration of our production beyond the current plan in order to meet market demand and the challenges from competitors who are presently expanding their operations.

Although we do not expect that minor delays in product certifications would significantly affect our ability to continue developing product applications with our customers, delays that extend significantly beyond mid-2009 likely would impact our ability to develop demand for our PV modules, and would affect our planned sales and results of operations in 2010, when we expect to have commenced production using our planned production tools for approximately 30 MW of rated capacity.

Using our 1.5 MW production line as a model, we have consummated the fixed price delivery contracts for the majority of the production tools for the 30 MW line. The equipment supplier schedules in the supply agreements provide for the installation of the majority of the production tools by the end of the third quarter of 2009. We plan to commence production ramp up to 30 MW of rated capacity by the end of the first quarter 2010. In order to qualify approximately 30 MW of rated capacity by the end of 2009, we intend to purchase and install production tools

that will process one-third meter wide plastic rolls similar to those used in our existing 1.5 MW production line. Significant delays in achieving desired production yields, module efficiencies or other performance metrics on the 1.5 MW production line and/or delays in the delivery, installation and qualification of the 30 MW production tools may impact our real and projected product sales in 2010.

We have initiated engineering and development of the one meter wide production tools to support future expansion of rated capacity. Successfully transitioning to one meter wide rolls should significantly increase our throughput, thereby reducing the number of manufacturing tools and, hence, the amount of capital expenditures required for equipment and facilities. Generally speaking, we believe that all other process variables, such as speed, thickness and composition, should remain unchanged. Based upon discussions with our equipment suppliers, we have identified deposition of the CIGS layer in the one meter wide format as the most challenging aspect of transitioning to one meter wide rolls; consequently, we have initiated the development of one meter wide prototype CIGS and molybdenum production tools to enable us to begin evaluating and testing one meter wide area deposition sources and process control systems. The one meter CIGS prototype production tool is scheduled for installation in 2009 and the one meter molybdenum production tool is scheduled for delivery in 2010. We plan to conduct six to nine months of testing and evaluation prior to committing the capital in to procure the one meter format production tools to support further expansion of rated capacity. Our planned expansion to approximately 110 MW of rated capacity will require additional capital, which we may not be able to obtain on favorable terms, if at all or without dilution to our stockholders.

**Capital Equipment Expenditures and Manufacturing Costs**

Since our formation in October 2005, most of our cash outlays have gone toward the investment in capital equipment necessary to develop our manufacturing capabilities for producing the commercial products we envision. We expect this trend to continue into the foreseeable future as we expand to approximately 110 MW of rated capacity by the end of 2011. We will require additional capital and additional facilities to achieve our manufacturing expansion plans. If we are unable to secure the necessary capital or to manage the disbursement of capital taking into consideration any unforeseen factors, such as cost increases from our equipment suppliers and the potential negative changes in the value of the U.S. dollar against foreign currencies, our ability to expand our manufacturing capacity as planned, as well as our financial performance and results of operations, may be adversely affected.

We currently expect the capital expenditures to support the first 30 MW of rated capacity to total approximately $95 million to $100 million for manufacturing equipment and approximately $17 million for the acquisition and renovations of our new manufacturing facility in Thornton, Colorado. We also expect capital expenditures of approximately $8 million for installation, qualification and other associated pre-operating expenses related to the first 30 MW expansion. In addition, we have budgeted approximately $7 million in 2008 and 2009 for the procurement and installation of the one meter wide manufacturing development tools, sources, and sensor control systems. In order to install the next 30 MW and then additional 50 MW of rated capacity, we expect that we will require another approximately $225 million to $235 million for property, plant and equipment and approximately $15 million for installation, qualification and other associated pre-operating expenses. Capital expenditure estimates for our expansion reflect an increase from our previous estimates primarily due to higher costs for equipment infrastructure, as well as higher estimated costs for certain equipment.

Our major equipment suppliers are located in Japan, the United Kingdom and Germany. To manage the uncertainties related to the procurement of capital equipment, we have continued to work closely with our equipment suppliers to complete the engineering of our new tools and refine the estimates of our planned capital outlays. The production tool costs are subject to change until we place firm procurement orders with our suppliers. To manage the fluctuations of foreign exchange rates, we have implemented forward pricing contracts for certain agreements denominated in foreign currencies.

**Significant Trends, Uncertainties and Challenges**

We believe that the significant trends, uncertainties and challenges that directly or indirectly affect our financial performance and results of operations are:

- Our ability to achieve desired production yields, module efficiencies and other performance targets, and to obtain necessary or desired certifications for our PV modules;

- Our ability to expand production in accordance with our plans set forth above under Commercialization and Manufacturing Expansion Plan ;

- Our ability to achieve projected operational performance and cost metrics;

- Our ability to consummate strategic relationships with key partners, including original equipment manufacturer (OEM) customers, system integrators, and distributors who deal directly with end-users in the BIPV, EIPV, portable power, and commodity solar panel markets;

- The effect that currency fluctuations may have on our capital equipment purchases, manufacturing costs and the price of our planned PV modules;

- Our ability to manage the planned expansion of our manufacturing facilities, operations and personnel;

- Our ability and the ability of our distributors, suppliers and customers to manage operations and orders during the global financial crisis; and

- Our ability to identify and retain a qualified permanent president and chief executive officer.

**Basis of Presentation:** The Company s activities to date have substantially consisted of raising capital, research and development, and the development of a 1.5 MW production plant and additional 30 MW expansion plant. Revenues to

date have been generated from the Company s governmental research and development (R&D) contracts and have not been significant. The Company s planned principal operations to commercialize flexible PV modules have not yet commenced. Accordingly, the Company is considered to be in the development stage, as defined in Statement of Financial Accounting Standards No. 7 (SFAS No. 7), *Accounting and Reporting by Development Stage Enterprises*.

**Cash Equivalents:** The Company considers all highly liquid debt securities purchased with an original maturity of three months or less to be cash equivalents. The Company maintains cash balances which may exceed federally insured limits. The Company does not believe that this results in significant credit risk.

**Investments:** The Company accounts for investments in accordance with SFAS No. 115, *Accounting for Certain Investments in Debt and Equity Securities.* The Company has classified its investments as available-for-sale . Such investments are carried at fair value, based on quoted market prices with the unrealized holding gains and losses reported as Accumulated other comprehensive income (loss) in the stockholders equity section of the balance sheet. Realized gains and losses on sales of securities are computed using the specific identification method. The Company evaluates declines in market value for potential impairment. If the decline results in a value below cost and is determined to be other than temporary, the investment is written down to its impaired value and a new cost basis is established.

**Fair Value estimates:** The fair value of an asset or liability is the amount at which it could be exchanged or settled in a current transaction between willing parties. The carrying value for cash and cash equivalents, investments, restricted cash, accounts receivable, accounts payable, accrued property and equipment, accrued expenses and other assets and liabilities approximate their fair values due to their short maturities. Effective January 1, 2008, the Company adopted SFAS No. 157, *Fair Value Measurements* (SFAS 157). In February 2008, the FASB issued FASB Staff Position No. FAS 157-2, *Effective Date of FASB Statement No. 157* , which provided a one year deferral of the effective date of SFAS 157 for non-financial assets and non-financial liabilities, except those that are recognized or disclosed in the financial statements at fair value at least annually. The Company adopted this statement for financial assets and financial liabilities and nonfinancial assets and nonfinancial liabilities recognized or disclosed at fair value on a recurring basis as of January 1, 2008. The Company adopted this statement for nonfinancial assets and nonfinancial liabilities recognized or disclosed at fair value on a nonrecurring basis as of January 1, 2009. The effect of the adoption of this statement was not material, resulting only in additional disclosures. SFAS 157 defines fair value, establishes a framework for measuring fair value under generally accepted accounting principles and enhances disclosures about fair value measurements. Fair value is defined under SFAS 157 as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date.

**Foreign Currency translation:** Bank account balances related to our forward contracts are translated to U.S. dollars utilizing the period end exchange rate. Gains or losses on foreign currency translations are recorded in other income/loss in the Condensed Statements of Operations.

**Revenue Recognition:** Revenue to date is from governmental research and development contracts under terms that are cost plus fee or firm fixed price. Revenue from cost plus fee contracts is recognized as costs are incurred on the basis of direct costs plus allowable indirect costs and an allocable portion of the firm fixed fee. Revenue from firm fixed price contracts is recognized under the percentage-of-completion method of accounting, with costs and estimated profits included in contract revenue as work is performed. If actual and estimated costs to complete a contract indicate a loss, provision is made currently for the loss anticipated on the contract.

**Patents:** At such time as the Company is awarded patents, patent costs are amortized on a straight-line basis over the legal life, or over their estimated useful lives, whichever is shorter. As of March 31, 2009, the Company had $140,524 of net patent costs of which $28,138 represent costs net of amortization incurred for an awarded patent, and the remaining $112,386 represents costs incurred for patent applications filed. Amortization expense for the three months ended March 31, 2009 and 2008 was $1,279.

**Property and Equipment:** Property and equipment are recorded at the original cost to the Company. Assets are being depreciated over estimated useful lives of one to ten years using the straight-line method, commencing when the asset is placed in service. Leasehold improvements are depreciated over the shorter of the remainder of the lease term or the life of the improvements. Upon retirement or disposal, the cost of the asset disposed of and the related accumulated depreciation are removed from the accounts and any gain or loss is reflected in income. Expenditures for repairs and maintenance are expensed as incurred.

The Company computes depreciation expense using the straight-line method over the estimated useful lives of the assets, as presented in the table below. We amortize leasehold improvements over the shorter of their estimated useful lives or the remaining term of the lease.

| | Useful Lives in Years |
|---|---|
| Buildings | 40 |
| Manufacturing machinery and equipment | 5 - 10 |
| Furniture, fixtures, computer hardware/software | 3 - 7 |
| Leasehold improvements | life of lease |

**Long-lived assets:** We account for our long-lived, tangible assets and definitive-lived intangible assets in accordance with Statement of Financial Accounting Standards No. (SFAS, 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*). As a result, we assess long-lived assets classified as held and used , including our property, plant and equipment, for impairment whenever long-lived asset may not be recoverable. These events would include significant current period operating or cash flow losses associated with the use of a long-lived asset or group of assets combined with a history of such losses, significant changes in the manner of use of assets and significant negative industry or economic trends. We evaluated our long-lived assets for impairment for the period ending March 31, 2009 and concluded that no valuation allowances were required.

**Risks and Uncertainties:** The Company s operations are subject to certain risks and uncertainties, including those associated with: the ability to meet obligations; continuing losses; fluctuation in operating results; funding expansions; strategic alliances; financing arrangement terms that may restrict operations; regulatory issues; and competition. Additionally, U.S. government contracts may be terminated prior to completion of full funding by the U.S. government.

**Net loss per Common Share:** Statement of Financial Accounting Standards No. 128, *Earnings Per Share,* provides for the calculation of Basic and Diluted earnings per share. Basic earnings per share include no dilution and are computed by dividing income available to common stockholders by the weighted-average number of shares outstanding during the period. Diluted earnings per share reflect the potential of securities that could share in the earnings of the Company, similar to fully diluted earnings per share. Common stock equivalents consisting of Class B warrants, IPO warrants (representative warrants), stock options and restricted stock units outstanding as of March 31, 2009 and 2008 of approximately 12.1 million and 11.5 million shares, have been omitted from loss per share because they are anti-dilutive. Basic and diluted loss per share was the same in each of the periods ended March 31, 2009 and 2008.

**Research and Development Costs:** Research and development costs are incurred during the process of researching and developing new products and enhancing our manufacturing processes and consist primarily of compensation and related costs for personnel, materials, supplies and equipment depreciation. We expense these costs as incurred until the resulting product has been completed and tested and is ready for commercial manufacturing. We also incur

research and development expenses on our U.S. federal government research and development contracts and expense as incurred.

**Income Taxes:** Deferred income taxes are provided using the liability method whereby deferred tax assets are recognized for deductible temporary differences and operating loss and tax credit carry forwards and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of the changes in tax laws and rates as of the date of enactment. Interest and penalties, if applicable would be recorded in operations.

In July 2006, the FASB issued FASB Interpretation (FIN 48), *Accounting for Uncertainty in Income Taxes*. The Company adopted the provisions of FIN 48 on January 1, 2007. As defined, FIN 48 seeks to reduce the diversity in practice associated with certain aspects of the recognition and measurement related to accounting for income taxes. The Company became subject to the provisions of FIN 48 as of January 1, 2007, and has analyzed filing positions in all of the federal and state jurisdictions where it is required to file income tax returns, as well as all open tax years in these jurisdictions. The Company has identified its federal tax return and its Colorado tax return as major tax jurisdictions, as defined. The periods subject to examination for the Company s federal and state tax returns are tax years 2005 through 2007. The Company believes that its income tax filing positions and deductions will be sustained on audit and does not anticipate any adjustments that will result in a material adverse effect on the Company s financial condition, results of operations, or cash flows. Therefore, no reserves for uncertain income tax positions have been recorded pursuant to FIN 48. In addition, the Company did not record a cumulative effect adjustment related to the adoption of FIN 48.

**Stock Based Compensation:** The Company accounts for share-based payments under the provisions of Statement of Financial Accounting Standards No. 123 (revised 2004), *Share-Based Payment,* (SFAS 123(R)) which requires the measurement and recognition of compensation expense for all share- based payment awards made to employees, officers, directors, and consultants, including employee stock options based on estimated fair values.
SFAS 123(R) requires companies to estimate the fair value of share-based payment awards on the date of grant using an option-pricing model. The value of the portion of the award that is ultimately expected to vest is recognized as expense over the requisite service period in the Company s Condensed Statements of Operations. Stock based compensation is based on awards ultimately expected to vest and is reduced for estimated forfeitures.
SFAS 123(R) requires forfeitures to be estimated at the time of grant and revised, as necessary, in subsequent periods if actual forfeitures differ from those estimates.

For purposes of determining estimated fair value of share-based payment awards on the date of grant under SFAS 123(R), the Company uses the Black-Scholes option-pricing model (Black-Scholes Model). The Black-Scholes Model requires the input of highly subjective assumptions. Because the Company s employee stock options may have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management s opinion, the existing models may not provide a reliable single measure of the fair value of the Company s employee stock options. Management will continue to assess the assumptions and methodologies used to calculate estimated fair value of share-based compensation. Circumstances may change and additional data may become available over time, which result in changes to these assumptions and methodologies, which could materially impact the Company s fair value determination.

The application of the SFAS 123(R) accounting principles may be subject to further interpretation and refinement over time. There are significant differences among option valuation models, and this may result in a lack of comparability with other companies that use different models, methods and assumptions. If factors change and the Company employs different assumptions in the application of SFAS 123(R) in future periods, or if the Company decides to use a different valuation model, the compensation expense that the Company records in the future under SFAS 123(R) may differ significantly from what it has recorded in the current period and could materially affect its loss from operations, net loss and net loss per share.

**Comprehensive income (loss):** Our comprehensive income (loss) consists of our net income (loss), and changes in unrealized gains or losses on available for sale investments, the impact of which has been excluded from net loss. We present our comprehensive income (loss) in the Condensed Statements of Stockholders Equity and Comprehensive Income and (Loss). Our accumulated other comprehensive income (loss) is presented as a component of equity in our Condensed Balance Sheets and consists of the cumulative amount of unrealized gains or losses on available-for-sale investments that we have incurred since the inception of our business.

**Reclassifications:** Certain reclassifications have been made to the 2008 financial information to conform to the 2009 presentation. Such reclassifications had no effect on net loss and are primarily related to reclassifying costs between Research and development costs and General and administrative expenses in the Condensed Statements of Operations.

**Use of Estimates:** The preparation of financial statements in conformity with generally accepted accounting principles 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 financial statements and the reported amounts of revenues

and expenses during the reporting period. Actual results could differ from those estimates.

**Unaudited Information:** The accompanying interim financial information as of March 31, 2009 and for the three months ended March 31, 2009 and 2008 and the period from inception (October 18, 2005) through March 31, 2009 was taken from the Company s books and records without audit. However, in the opinion of management, such information includes all adjustments (consisting only of results of normal recurring accruals) that are necessary to properly reflect the financial position of the Company as of March 31, 2009 and the results of operations for the three months ended March 31, 2009 and 2008 and the period from inception (October 18, 2005) through March 31, 2009 so that the financial statements are not misleading.

**Recent Accounting Pronouncements:** In May 2008, the FASB issued SFAS No. 162, The Hierarchy of Generally Accepted Accounting Principles, which becomes effective upon approval by the SEC. The standard sets forth the sources of accounting principles and provides entities with a framework for selecting the principles used in the preparation of financial statements that are presented in conformity with GAAP. It is not expected to change any of our current accounting principles or practices and therefore, is not expected to have a material impact on our financial statements.

**Results of Operations**

**Comparison of the Three Months Ended March 31, 2009 and 2008**

Certain reclassifications have been made to the 2008 financial information to conform to the 2009 presentation. Such reclassifications had no effect on net loss and are primarily related to reclassifying costs between R&D costs and G&A expenses in the Statement of Operations. Our activities to date have substantially consisted of raising capital, business and product development, research and development and the development of our 1.5 MW production line and the construction of our 30 MW production line.

*Research and Development Revenues.* Our R&D revenues were $516,133 for the three months ended March 31, 2009 compared to $304,898 for the three months ended March 31, 2008 an increase of $211,235. The majority of our R&D revenues during the three months ended March 31, 2009 and 2008 were revenues earned on our government R&D contracts. The increase in 2009 primarily relates to two government contracts awarded in June 2008.

*Research and Development.* R&D costs include the costs incurred for pre-production activities on our 1.5 MW line and our planned 30 MW line and costs related to our governmental contracts. R&D costs were $3,195,653 for the three months ended March 31, 2009 compared to $1,824,970 for the three months ended March 31, 2008, an increase of $1,370,683. Costs related to pre-production activities increased $1,251,302. The pre-production cost increases were comprised primarily of costs related to material and equipment production start-up activity of approximately $325,000, depreciation and amortization of approximately $159,000, personnel related costs of approximately $470,000, facility related costs of approximately $212,000, and stock compensation expense of approximately $85,000. Governmental R&D expenditures increased by $119,381 related to the contracts awarded June 2008.

*General and Administrative.* G&A expenses were $1,580,878 for the three months ended March 31, 2009 compared to $1,191,152 for the three months ended March 31, 2008, an increase of $389,726. This increase is comprised of costs associated with increased headcount, increased consulting costs, and increased infrastructure costs of approximately $135,000, and an increase in stock compensation expense of approximately $153,000.

*Interest Expense.* Interest expense was $83,345 for the three months ended March 31, 2009 compared to $39,514 for the three months ended March 31, 2008, an increase of $43,831. Interest expense relates to our CHFA loan utilized for our 30M production facility expansion in Thornton, Colorado. The increase in Interest expense relates to an increased CHFA loan balance as of March 31,2009 compared to March 31, 2008.

*Interest Income.* Interest income was $333,367 for the three months ended March 31, 2009 compared to $352,047 for the three months ended March 31, 2008, a decrease of $18,680. Interest income represents interest on cash and investments. The decrease in Interest income is due to significantly lower interest rates in the three months ended

March 31, 2009 compared to the three months ended March 31, 2008 offset by a higher average cash balance for the three months ended March 31, 2009 compared to March 31, 2008.

*Realized Loss on Forward Contracts and Unrealized Losses on Forward Contracts.* For the three months ended March 31, 2009, the unrealized gain on forward contracts was $154,191 and the realized loss was $556,373. Although the hedging activity is designed to fix the dollar amount to be expended, the asset purchased is recorded at the spot rate in effect as of the date of the payment to the supplier. The difference between the spot rate and the forward rate has been reported as a loss on forward contract.

*Net Loss.* Our Net Loss was $4,412,558 for the three months ended March 31, 2009 compared to a Net Loss of $2,398,691 for the three months ended March 31, 2008, an increase in Net Loss of $2,013,867. The increase in Net Loss can be summarized in variances in significant account activity as follows:

| | | Increase (decrease) of Net Loss For the Three Months Ended March 31, 2009 compared to March 31, 2008 |
|---|---|---|
| Contract revenues | $ | (211,235) |
| Research and development costs | | |
| Manufacturing R&D | | 1,193,559 |
| Government R&D | | 91,906 |
| Non-cash stock based compensation | | 85,218 |
| General and administrative expenses | | |
| Corporate G&A | | 236,538 |
| Non-cash stock based compensation | | 153,188 |
| Interest expense | | 43,831 |
| Interest income | | 18,680 |
| Realized Loss on forward contract | | 556,373 |
| Unrealized Gain on forward contracts | | (154,191) |
| Increase of Net Loss | $ | 2,013,867 |

**Liquidity and Capital Resources**

For the three months ended March 31, 2009, our cash used in operations was approximately $3.1 million compared to approximately $1.6 million for the three months ended March 31, 2008. For the three months ended March 31, 2009 approximately $13.1 million had been expended in capital to complete our 1.5 MW production line and facility modifications, initial payments on our 30 MW and one meter wide development and production tools, and acquisition and renovations to the Thornton, Colorado facility for our manufacturing expansion.

As of March 31, 2009, we had approximately $71.2 million in cash, restricted cash and investments. We currently expect the capital expenditures needed to support the first 30 MW of rated capacity will total approximately $95 million to $100 million for production and manufacturing equipment and approximately $17 million for the acquisition of the building and renovations of our 30 MW Thornton facility. We also expect capital expenditures of approximately $8 million for installation, qualification and other associated pre-operating expenses related to the expansion. In addition, we have budgeted approximately $7 million for the procurement and installation of the one meter wide manufacturing development tools, sources, and sensor control systems. We made actual cash payments of approximately $45.7 million for the 30 MW production and manufacturing development tools as of March 31, 2009 and expect to make the remaining payments in 2009 and the first half of 2010. Remaining expenditures to complete the Thornton facility in the second quarter 2009 are estimated to be approximately $2 million.

During the three months ended March 31, 2009, the use of cash for operational expenses averaged approximately $1 million per month and was related to pre-manufacturing activities, research and technology development, business development and general corporate expenses. We expect operational expenses to increase in 2009 as we commence commercial production and increase the size of our workforce. Our average monthly operational expense for three months ended March 31, 2009 of approximately $1 million is net of average monthly R&D revenues from our governmental contracts of approximately $ 0.2 million and average monthly interest income net of interest expense of approximately $ 0.1 million. A significant component of our costs for the three months ended March 31, 2009 related to the ongoing qualification of our 1.5 MW line and continuing corporate costs related to building the required infrastructure to support our 1.5 MW manufacturing operations and expansion plans. We anticipate that our operational expenditures will continue to increase throughout 2009 due to the planned hiring of additional personnel for both our 1.5 MW production line and the installation and qualification of our new 30 MW of rated production capacity in Thornton, Colorado. As of March 31, 2009, we had 64 full-time employees of which 40 were manufacturing personnel. We plan to continue to increase our staff during 2009, principally in the manufacturing area.

We do not expect that our sales revenue from the 1.5 MW production line will be sufficient to support our operations and cash requirements, and it is unlikely that our sales revenue will support our operating cash requirements unless we achieve actual production capacity of at least 30 MW per year. Our original equipment delivery schedule called for installation of all of the 30MW production equipment during 2009. Due to the recent financial crisis affecting the financial markets, our ability to obtain credit or to raise additional capital has become increasingly difficult. In order to preserve cash we have extended the equipment delivery schedule related to the first 30 MW of annual rated production capacity to 2010. We now expect to begin production using equipment with an annual rated production capacity of approximately 15 MW in early 2010, and full 30 MW of annual rated production capacity by the middle of 2010.

On January 9, 2009, we filed a shelf Registration Statement on Form S-3 with the Securities and Exchange Commission ( SEC ). The SEC declared the registration statement effective on January 16, 2009. With the shelf registration, we may from time to time sell common stock, preferred stock, warrants or some combination in one or more offerings totaling up to $150 million.

**Off Balance Sheet Transactions**

As of March 31, 2009, we did not have any off balance sheet arrangements as defined in Item 303(a)(4)(ii) of SEC Regulation S-K.

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

**Foreign Currency Exchange Risk**

The Company is actively engaged in purchasing manufacturing equipment internationally and is exposed to foreign currency risk. Our objective is to fix the dollar amount of our foreign currency denominated manufacturing equipment purchases at time of order. Although the hedging activity is designed to fix the dollar amount to be expended, the asset

purchased is recorded at the spot rate in effect as of the date of the payment to the supplier. The difference between the spot rate and the forward rate has been reported as a loss on forward contract.

In July 2008 and March 2009, the Company entered into fair value hedges utilizing forward contracts designed to match scheduled contractual payments to equipment suppliers which are denominated in Euros and Yen. The total notional value of the Euro forward contracts was 6.4 million with various contract settlement dates beginning September 15, 2008 through July 31, 2009. The total notional value of the Yen forward contracts was ¥521.4 million with contract settlement dates of March and April 2009. Derivative financial instruments are not used for speculative or trading purposes.

Although our reporting currency is the U.S. dollar, we may conduct business and incur costs in the local currencies of other countries in which we may operate, make sales and buy materials. As a result, we are subject to currency translation risk. Further, changes in exchange rates between foreign currencies and the U.S. dollar could affect our future net sales and cost of sales and could result in exchange losses.

We cannot accurately predict future exchange rates or the overall impact of future exchange rate fluctuations on our business, results of operations and financial condition.

**Interest Rate Risk**

Our exposure to market risks for changes in interest rates relates primarily to our cash equivalents and investment portfolio. As of March 31, 2009, our cash equivalents consisted of money market funds and investments represented U.S. government securities, and high quality corporate securities. The primary objective of our investment activities is to preserve principal and provide liquidity on demand, while at the same time maximizing the income we receive from our investments without significantly increasing risk. The direct risk to us associated with fluctuating interest rates is limited to our investment portfolio and we do not believe that a change in interest rates will have a significant impact on our financial position, results of operations or cash flows.

**Commodity and Component Risk**

Failure to receive timely delivery of production tools from our equipment suppliers could delay our planned expansion of manufacturing capacity and materially and adversely affect our results of operations and financial condition. Our planned expansion of manufacturing capacity and commercialization timeline depend on the timely delivery of production tools from our equipment suppliers. The relationships with our chosen equipment suppliers are relatively new, and at this point in time we cannot be certain that the equipment orders we place with these suppliers will be fulfilled as we expect or in a timely manner.

We are exposed to price risks for the raw materials used in the manufacture of our PV modules. We depend on a limited number of third-party suppliers for key raw materials, and their failure to perform could cause manufacturing delays and impair our ability to deliver PV modules to customers in the required quality and quantity and at a price that is profitable to us. Our failure to obtain raw materials and components that meet our quality, quantity and cost requirements in a timely manner could interrupt or impair our ability to manufacture our PV modules or increase our manufacturing cost. Most of our key raw materials are either sole-sourced or sourced by a limited number of third-party suppliers. As a result, the failure of any of our suppliers to perform could disrupt our supply chain and impair our operations. In addition, many of our suppliers

are small companies that may be unable to supply our increasing demand for raw materials as we implement our planned expansion. We may be unable to identify new suppliers in a timely manner or on commercially reasonable terms. Raw materials from new suppliers may also be less suited for our technology and yield PV modules with lower conversion efficiencies, higher failure rates and higher rates of degradation than PV modules manufactured with the raw materials from our current suppliers.

If delivery of production tools or raw materials are not made on schedule or at all, then we might be unable to carry out our commercialization and manufacturing expansion plans, produce PV modules in the volumes and at the times that we expect or generate sufficient revenue from operations, and our business, results of operations and financial condition could be materially and adversely affected.

**Credit Risk**

We have certain financial and derivative instruments that potentially subject us to credit risk.  These consist primarily of cash, cash equivalents, restricted cash, investments, and forward foreign exchange contracts.  We are exposed to credit losses in the event of nonperformance by the counter parties to our financial and derivative instruments.  We place

cash, cash equivalents, investments and forward foreign exchange contracts with various high-quality financial institutions, and exposure is limited at any one institution. We continuously evaluate the credit standing of our counter party financial institutions.

**Item 4. Controls and Procedures**

**Evaluation of Disclosure Controls and Procedures**

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our reports filed or submitted under the Securities Exchange Act of 1934, as amended (Exchange Act) is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission (SEC) rules and forms. Our disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed in our reports filed under the Exchange Act is accumulated and communicated to management as appropriate to allow timely decisions regarding required disclosures. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures, including the possibility of human error and the circumvention or overriding of the controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives, and management necessarily is required to use its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Our management conducted an evaluation required by Rules 13a-15 and 15d-15 under the Exchange Act of the effectiveness of our disclosure controls and procedures as defined in Rules 13a-15 and 15d-15 under the Exchange Act as of March 31, 2009. Based on this evaluation, our management concluded that as of March 31, 2009, the design and operation of our disclosure controls and procedures were effective.

**Changes in Internal Control over Disclosure and Reporting**

There was no change in our internal control over financial reporting that occurred during the quarterly period ended March 31, 2009 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**PART II. OTHER INFORMATION**

**Item 1. Legal Proceedings**

**None**

**Item 1A. Risk Factors**

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, Item 1A: Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2008, which could materially affect our business, financial condition or future results. The risks described in our Annual Report on Form 10-K are not the only risks facing our company. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition or future results.

**Item 6. Exhibits**

a. The following exhibits are filed as part of, or are incorporated by reference into, this report:

| Exhibit No. | | Description |
|---|---|---|
| | | |
| 3.1 | | Registrant s Amended and Restated Certificate of Incorporation (incorporated by reference to Exhibit 3.2 to our Registration Statement on Form SB-2 filed January 23, 2006 (Reg. No. 333-131216), as amended) |
| | | |
| 3.2 | | Registrant s Second Amended and Restated Bylaws (incorporated by reference to Exhibit 3.2 to our current report on Form 8-K filed February 17, 2009) |
| | | |
| 10.1 | | Loan Modification Agreement with Colorado Housing and Finance Authority (incorporated by reference to Exhibit 10.52 to our Annual Report on Form 10-K filed March 12, 2009) |
| | | |
| 31.1 | | Chief Executive Officer Certification pursuant to section 302 of the Sarbanes-Oxley Act of 2002* |
| | | |
| 31.2 | | Chief Financial Officer Certification pursuant to section 302 of the Sarbanes-Oxley Act of 2002* |

| Exhibit No. | | Description |
|---|---|---|
| 32.1 | | Chief Executive Officer Certification pursuant to section 906 of the Sarbanes-Oxley Act of 2002* |
| | | |
| 32.2 | | Chief Financial Officer Certification pursuant to section 906 of the Sarbanes-Oxley Act of 2002* |

* Filed herewith

**ASCENT SOLAR TECHNOLOGIES, INC.**

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized on the 7th day of May, 2009.

ASCENT SOLAR TECHNOLOGIES

By: /s/ GARY GATCHELL
Gary Gatchell
*Chief Financial Officer (Principal Finacial Officer and Authorized Signatory)*