

MECHANICAL TECHNOLOGY INC
Form 10-Q
August 07, 2014

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

T QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2014

or

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

Mechanical Technology, Incorporated

(Exact name of registrant as specified in its charter)

New York
(State or other jurisdiction

000-06890
(Commission File Number)

14-1462255
(I.R.S. Employer

of incorporation or organization)

Identification No.)

325 Washington Avenue Extension, Albany, New York 12205

(Address of principal executive offices)

(Zip Code)

(518) 218-2550

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(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

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

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

Smaller reporting company

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

The number of shares of common stock, par value of \$0.01 per share, outstanding as of August 1, 2014 was 5,256,883.

MECHANICAL TECHNOLOGY, INCORPORATED AND SUBSIDIARIES

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PART I. FINANCIAL INFORMATION**Item 1. Financial Statements****Mechanical Technology, Incorporated and Subsidiaries****Condensed Consolidated Balance Sheets as of June 30, 2014 (Unaudited) and December 31, 2013**

(Dollars in thousands, except per share)

	June 30, 2014	December 31, 2013
Assets		
Current Assets:		
Cash	\$ 774	\$ 1,211
Accounts receivable	1,342	824
Inventories	818	742
Deferred income taxes, net	24	25
Prepaid expenses and other current assets	88	111
Total Current Assets	3,046	2,913
Deferred income taxes, net	1,476	1,475
Property, plant and equipment, net	132	146
Total Assets	\$ 4,654	\$ 4,534
Liabilities and Equity		
Current Liabilities:		
Accounts payable	\$ 529	\$ 149
Accrued liabilities	949	993
Total Current Liabilities	1,478	1,142
Commitments and Contingencies (Note 9)		
Equity:		
Common stock, par value \$0.01 per share, authorized 75,000,000; 6,261,975 issued in both 2014 and 2013	63	63
Additional paid-in capital	135,650	135,612
Accumulated deficit	(118,783)	(118,529)
Common stock in treasury, at cost, 1,005,092 shares in both 2014 and 2013	(13,754)	(13,754)
Total MTI stockholders' equity	3,176	3,392
Total Liabilities and Equity	\$ 4,654	\$ 4,534

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

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Mechanical Technology, Incorporated and Subsidiaries

Condensed Consolidated Statements of Operations (Unaudited)

For the Three and Six Months Ended June 30, 2014 and 2013

(Dollars in thousands, except per share)	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2014	2013	2014	2013
Product revenue	\$ 2,478	\$ 2,267	\$ 3,860	\$ 4,467
Operating costs and expenses:				
Cost of product revenue	997	801	1,576	1,776
Unfunded research and product development expenses	371	307	732	647
Selling, general and administrative expenses	932	927	1,806	1,746
Operating income (loss)	178	232	(254)	298
Other income, net		9		9
Income (loss) before income taxes and non-controlling interest	178	241	(254)	307
Income tax expense		(156)		(155)
Net income (loss)	178	85	(254)	152
Plus: Net loss attributed to non-controlling interest		15		34
Net income (loss) attributed to MTI	\$ 178	\$ 100	\$ (254)	\$ 186
Income (loss) per share attributable to MTI (Basic)	\$.03	\$.02	\$ (.05)	\$.04
Income (loss) per share attributable to MTI (Diluted)	\$.03	\$.02	\$ (.05)	\$.04
Weighted average shares outstanding (Basic)	5,256,883	5,256,883	5,256,883	5,256,883
Weighted average shares outstanding (Diluted)	5,495,461	5,258,901	5,256,883	5,256,883

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

MECHANICAL TECHNOLOGY, INCORPORATED AND SUBSIDIARIES

Condensed Consolidated Statements of Changes in Equity

For the Year Ended December 31, 2013

and the Six Months Ended June 30, 2014 (Unaudited)

	Common Stock				Treasury Stock		Total MTI Stockholders Equity (Deficit)	Non-Controlling Interest (NCI)	Total Equity
	Shares	Amount	Additional Paid- in Capital	Accumulated Deficit	Shares	Amount			
January 1, 2013	6,261,975	\$ 63	\$ 135,561	\$ (122,183)	1,005,092	\$ (13,754)	\$ (313)	\$ 3,311	\$ 2,998
Net income attributed to MTI	-	-	-	3,654	-	-	3,654	-	3,654
Stock based compensation	-	-	51	-	-	-	51	-	51
Net loss attributed to NCI	-	-	-	-	-	-	-	(75)	(75)
Equity contribution to NCI	-	-	-	-	-	-	-	25	25
Variable interest entity deconsolidation -	-	-	-	-	-	-	-	(3,261)	(3,261)
December 31, 2013	6,261,975	\$ 63	\$ 135,612	\$ (118,529)	1,005,092	\$ (13,754)	\$ 3,392	\$ -	\$ 3,392
Net loss attributed to MTI	-	-	-	(254)	-	-	(254)	-	(254)
Stock based compensation	-	-	38	-	-	-	38	-	38
June 30, 2014	6,261,975	\$ 63	\$ 135,650	\$ (118,783)	1,005,092	\$ (13,754)	\$ 3,176	\$ -	\$ 3,176

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

MECHANICAL TECHNOLOGY, INCORPORATED AND SUBSIDIARIES**Condensed Consolidated Statements of Cash Flows (Unaudited)****For the Six Months Ended June 30, 2014 and 2013**

(Dollars in thousands)

	Six Months Ended June 30,	
	2014	2013
Operating Activities		
Net (loss) income	\$ (254)	\$ 152
Adjustments to reconcile net (loss) income to net cash (used in) provided by operating activities:		
Depreciation	46	46
Gain on disposal of equipment		(9)
Deferred income taxes		156
Stock based compensation	38	24
Provision for excess and obsolete inventories	9	(16)
Changes in operating assets and liabilities:		
Accounts receivable	(518)	582
Inventories	(85)	295
Prepaid expenses and other current assets	23	10
Accounts payable	380	38
Deferred revenue		(591)
Accrued liabilities	(44)	(109)
Net cash (used in) provided by operating activities	(405)	578
Investing Activities		
Purchases of equipment	(32)	(41)
Proceeds from sale of equipment		9
Net cash used in investing activities	(32)	(32)
(Decrease) increase in cash	(437)	546
Cash beginning of period	1,211	289
Cash end of period	\$ 774	\$ 835

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

MECHANICAL TECHNOLOGY, INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Notes to Condensed Consolidated Financial Statements (Unaudited)

1. Nature of Operations

Description of Business

Mechanical Technology, Incorporated (MTI or the Company), a New York corporation, was incorporated in 1961. The Company's core business is conducted through MTI Instruments, Inc. (MTI Instruments), a wholly-owned subsidiary and the sole component of the Company's Test and Measurement Instrumentation segment. Through the year ended December 31, 2013, the Company also operated in a New Energy segment with business conducted through MTI MicroFuel Cells, Inc. (MTI Micro). On December 31, 2013, as a result of a stock warrant exercise, the Company transferred management of MTI Micro to Dr. Walter L. Robb (a member of the Company's and MTI Micro's board of directors) and his new management team. The Company is consequently no longer reporting MTI Micro as a variable interest entity (VIE) as of the close of business on December 31, 2013 (date of MTI Micro deconsolidation).

MTI Instruments was incorporated in New York on March 8, 2000 and is a supplier of: precision linear displacement solutions, vibration measurement and system balancing systems, and wafer inspection tools, consisting of electronic gauging instruments for position, displacement and vibration application within the industrial manufacturing/production markets, as well as the research, design and process development market; tensile stage systems for materials testing at academic and industrial research settings; and engine vibration analysis systems for both military and commercial aircraft. These tools, systems and solutions are developed for markets and applications that require the precise measurements and control of products, processes, and the development and implementation of automated manufacturing, assembly, and consistent operation of complex machinery.

MTI Micro was incorporated in Delaware on March 26, 2001, and, until its operations were suspended in late 2011, had been developing a handheld energy-generating device to replace current lithium-ion and similar rechargeable battery systems in many handheld electronic devices for the military and consumer markets.

Liquidity

The Company has incurred significant losses primarily due to its past efforts to fund MTI Micro's direct methanol fuel cell product development and commercialization programs, and has an accumulated deficit of approximately \$118.8 million and working capital of approximately \$1.6 million at June 30, 2014.

Based on the Company's projected cash requirements for operations and capital expenditures for 2014, its current available cash of approximately \$774 thousand, the \$1.0 million available from its existing line of credit at MTI Instruments, current cash flow requirements and revenue and expense projections, management believes it will have adequate resources to fund operations and capital expenditures for at least the next twelve months.

However, the Company may need to do one or more of the following to raise additional resources, or reduce its cash requirements:

- 1) Reduce its current expenditure run rate;
- 2) Defer its capital expenditures;
- 3) Defer its hiring plans; and
- 4) Secure additional debt or equity financing.

There is no guarantee that such resources will be available to the Company on terms acceptable to it, or at all, or that such resources will be received in a timely manner, if at all, or that the Company will be able to reduce its expenditure run-rate, defer its capital expenditures or hiring plans without materially and adversely effecting its business.

2. Basis of Presentation

In the opinion of management, the Company's condensed consolidated financial statements reflect all adjustments, which are of a normal recurring nature, necessary for a fair statement of the results for the periods presented in accordance with United States of America Generally Accepted Accounting Principles (U.S. GAAP) and with the instructions to Form 10-Q in Article 10 of the Securities and Exchange Commissions (SEC) Regulation S-X. The results of operations for the interim periods presented are not necessarily indicative of results for the full year.

Certain information and footnote disclosures normally included in the annual consolidated financial statements prepared in accordance with U.S. GAAP have been condensed or omitted. These unaudited condensed consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2013.

The information presented in the accompanying condensed consolidated balance sheet as of December 31, 2013 has been derived from the Company's audited consolidated financial statements. All other information has been derived from the Company's unaudited condensed consolidated financial statements for the three and six months ended June 30, 2014 and June 30, 2013.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary, MTI Instruments. The consolidated financial statements also include the accounts of a former VIE, MTI Micro, through December 31, 2013. The Company was considered the primary beneficiary of the VIE until December 31, 2013, when the Company transferred management of MTI Micro to Dr. Robb and his new management team. For purposes of these consolidated financial statements, the deconsolidation of MTI Micro was effective as of the close of business on December 31, 2013. All intercompany balances and transactions are eliminated in consolidation. The Company reflected the impact of the equity securities issuances in its investment in a VIE and additional paid-in-capital accounts for the dilution or anti-dilution of its ownership interest in the VIE.

The Company determined that the effect of the deconsolidation of the VIE was to remove MTI Micro in the consolidated balance sheet as of December 31, 2013 but include MTI Micro's activity in the consolidated statement of operations for the year ended December 31, 2013. The following assets and liabilities of MTI Micro were not included in the consolidated balance sheet as of December 31, 2013 as a result of the VIE deconsolidation:

(dollars in thousands)	2013
Cash	\$ 25
Prepaid expenses and other current assets	1
Accounts payable	3
Related party note payable (see Note 12 for more detail)	380

The fair value of the Company's current non-controlling interest (NCI) in MTI Micro has been determined to be \$0 as of December 31, 2013 (date of MTI Micro deconsolidation), based on MTI Micro's net position and expected cash flows. The Company records its investment in MTI Micro using the equity method of accounting. As of June 30, 2014, the Company owned an aggregate of approximately 47.5% of MTI Micro's outstanding common stock, or 75,049,937 shares, and 53.3% of the common stock and warrants issued, which includes 32,904,136 warrants outstanding.

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As of December 31, 2013, NCI is classified as equity in the consolidated financial statements. The consolidated statement of operations presents net income (loss) for both the Company and the non-controlling interests. The calculation of earnings per share is based on net income (loss) attributable to the Company.

3. Accounts Receivable

Accounts receivables consist of the following at:

(Dollars in thousands)	June 30, 2014	December 31, 2013
U.S. and State Government	\$ 674	\$ 37
Commercial	668	787
Total	\$ 1,342	\$ 824

For the six months ended June 30, 2014 and 2013, the largest commercial customer represented 14.0% and 8.4%, respectively, and the largest governmental agency represented 22.5% and 31.7%, respectively, of the Company's Test and Measurement Instrumentation segment product revenue. As of June 30, 2014 and December 31, 2013, the largest commercial receivable represented 6.4% and 12.8%, respectively, and the largest governmental receivable represented 50.3% and 3.9%, respectively, of the Company's Test and Measurement Instrumentation segment accounts receivable.

As of June 30, 2014 and December 31, 2013, the Company had no allowance for doubtful trade accounts receivable.

4. Inventories

Inventories consist of the following at:

(Dollars in thousands)	June 30, 2014	December 31, 2013
Finished goods	\$ 329	\$ 287
Work in process	178	188
Raw materials	311	267
Total	\$ 818	\$ 742

5. Property, Plant and Equipment

Property, plant and equipment consist of the following at:

	June 30, 2014	December 31, 2013
Leasehold improvements	\$ 32	\$ 32
Computers and related software	1,276	1,281
Machinery and equipment	842	810
Office furniture and fixtures	119	125
	2,269	2,248
Less:		
Accumulated depreciation	2,137	2,102
	\$ 132	\$ 146

Depreciation expense was \$46 thousand and \$91 thousand for the six months ended June 30, 2014 and the year ended December 31, 2013, respectively. In conjunction with the suspension of MTI Micro operations in late 2011, sales of certain surplus equipment on hand were made during 2013. This resulted in a net gain on sale of \$13 thousand for the year ended December 31, 2013. As of December 31, 2013, all \$13 thousand in sales proceeds have been received.

6. Income Taxes

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During the three months ended June 30, 2014, the Company's effective income tax rate was 0%. The projected annual effective tax rate is less than the Federal statutory rate of 34%, primarily due to permanent differences, the change in the valuation allowance and changes to estimated taxable income for 2014. For the three months ended June 30, 2013, the Company's effective income tax rate was 64.7%.

During the six months ended June 30, 2014, the Company's effective income tax rate was 0.0%. The projected annual effective tax rate is less than the Federal statutory rate of 34%, primarily due to permanent differences, the change in the valuation allowance and changes to estimated taxable income for 2014. For the six months ended June 30, 2013, the Company's effective income tax rate was 50.6%.

The Company provides for recognition of deferred tax assets if the realization of such assets is more likely than not to occur in accordance with accounting standards that address income taxes. Significant management judgment is required in determining the period in which the reversal of a valuation allowance should occur. The Company has considered all available evidence, both positive and negative, such as historical levels of income and future forecasts of taxable income amongst other items, in determining its valuation allowance. In addition, the Company's assessment requires us to schedule future taxable income in accordance with accounting standards that address income taxes to assess the appropriateness of a valuation allowance which further requires the exercise of significant management judgment.

The Company has determined that it expects to generate sufficient levels of pre-tax earnings in the future to realize the net deferred tax assets recorded on the balance sheet at June 30, 2014. The Company has projected such pre-tax earnings utilizing a combination of historical and projected results, taking into consideration existing levels of permanent differences, non-deductible expense and the reversal of significant temporary differences. We project that our taxable income for the next three years is adequate to ensure the realizability of the \$1.5 million of deferred tax assets recorded on our balance sheet at June 30, 2014. In the event that actual results differ from these estimates or we adjust these estimates in future periods, we may need to adjust the recorded valuation allowance, which could materially impact our financial position and results of operations. We will continue to evaluate the ability to realize our deferred tax assets and related valuation allowance on a quarterly basis.

The Company believes that the accounting estimate for the valuation of deferred tax assets is a critical accounting estimate, because judgment is required in assessing the likely future tax consequences of events that have been recognized in our financial statements or tax returns. The Company based the estimate of deferred tax assets and liabilities on current tax laws and rates and, in certain cases, business plans and other expectations about future outcomes. In the event that actual results differ from these estimates or the Company adjusts these estimates in future periods, the Company may need to adjust the recorded valuation allowance, which could materially impact our financial position and results of operations. The valuation allowance was \$16.9 million at June 30, 2014 and \$16.8 million at December 31, 2013. The Company will continue to evaluate the ability to realize its deferred tax assets and related valuation allowances on a quarterly basis.

7. Stockholders Equity

Common Stock

The Company has one class of common stock, par value \$.01. Each share of the Company's common stock is entitled to one vote on all matters submitted to stockholders. As of June 30, 2014 and December 31, 2013, there were 5,256,883 shares of common stock issued and outstanding.

Reservation of Shares

The Company had reserved common shares for future issuance as follows as of June 30, 2014:

Stock options outstanding	713,566
Common stock available for future equity awards or issuance of options	502,000
Number of common shares reserved	1,215,566

Earnings (Loss) per Share

The Company computes basic income (loss) per common share by dividing net income (loss) by the weighted average number of common shares outstanding during the reporting period. Diluted income (loss) per share reflects the potential dilution, if any, computed by dividing income (loss) by the combination of dilutive common share equivalents, comprised of shares issuable under outstanding investment rights, warrants and the Company's share-based compensation plans, and the weighted average number of common shares outstanding during the reporting period. Dilutive common share equivalents include the dilutive effect of in-the-money stock options, which are calculated based on the average share price for each period using the treasury stock method. Under the treasury stock method, the exercise price of a stock option, the amount of compensation cost, if any, for future service that the Company has not yet recognized, and the amount of windfall tax benefits that would be recorded in additional paid-in capital, if any, when the stock option is exercised are assumed to be used to repurchase shares in the current period.

Not included in the computation of earnings per share, assuming dilution, for the three months ended June 30, 2014, were options to purchase 176,566 shares of the Company's common stock. These potentially dilutive items were excluded even though the average market price of the

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common stock exceeded the exercise prices for a portion of the options because the calculation of incremental shares, which includes the unrecognized compensation expense, resulted in an anti-dilutive effect. Not included in the computation of earnings per share, assuming dilution, for the six months ended June 30, 2014, were options to purchase 713,566 shares of the Company's common stock. These potentially dilutive items were excluded because the Company incurred a loss during this period and their inclusion would be anti-dilutive.

Not included in the computation of earnings per share, assuming dilution, for the three and six months ended June 30, 2013, were options to purchase 454,256 and 464,256 shares, respectively, of the Company's common stock. These potentially dilutive items were excluded even though the average market price of the common stock exceeded the exercise prices for a portion of the options because the calculation of incremental shares resulted in an anti-dilutive effect.

8. Segment Information

During 2013, the Company operated in two business segments, Test and Measurement Instrumentation and New Energy. As a result of the deconsolidation of MTI Micro operations on December 31, 2013 (see Note 1), the New Energy segment will no longer remain in our consolidated operations. The Test and Measurement Instrumentation segment designs, manufactures, markets and services high performance test and measurement instruments and systems, wafer characterization tools for the semiconductor and solar industries, tensile stage systems for materials testing at academic and industrial settings, and computer-based balancing systems for aircraft engines. The New Energy segment was focused on commercializing direct methanol fuel cells. The Company's principal operations are located in North America.

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The accounting policies of the Test and Measurement Instrumentation and New Energy segments are similar to those described in the summary of significant accounting policies in the Company's Annual Report on Form 10-K for the year ended December 31, 2013 (Note 2). The Company evaluates performance based on profit or loss from operations before income taxes. Inter-segment sales and expenses are not significant.

Summarized financial information concerning the Company's reportable segments is shown in the following tables. The Other column includes corporate related items and items such as income taxes or unusual items, which are not allocated to reportable segments. The Reconciling Items column includes non-controlling interests in a consolidated entity. In addition, segments' non-cash items include any depreciation in reported profit or loss. The New Energy segment figures include the Company's direct micro fuel cell operations. As a result of the deconsolidation of MTI Micro operations on December 31, 2013 (see Note 2), the New Energy segment will no longer remain in our consolidated operations.

As of January 1, 2014, the Company operates in one segment and therefore segment information is not presented.

(Dollars in thousands)

	Test and Measurement Instrumentation	New Energy	Other	Reconciling Items	Condensed Consolidated Totals
<u>Three Months Ended June 30, 2013</u>					
Product revenue	\$ 2,267	\$	\$	\$	\$ 2,267
Unfunded research and product development expenses	307				307
Selling, general and administrative expenses	501	17	409		927
Segment profit (loss) from operations before non-controlling interest	499	(28)	(386)		85
Segment profit (loss)	499	(28)	(386)	15	100
Total assets	1,985	53	2,321		4,359
Capital expenditures					
Depreciation	20	1	1		22

(Dollars in thousands)

	Test and Measurement Instrumentation	New Energy	Other	Reconciling Items	Condensed Consolidated Totals
<u>Six Months Ended June 30, 2013</u>					
Product revenue	\$ 4,467	\$	\$	\$	\$ 4,467
Unfunded research and product development expenses	647				647
Selling, general and administrative expenses	1,010	41	695		1,746
Segment profit (loss) from operations before non-controlling interest	753	(66)	(535)		152
Segment profit (loss)	753	(66)	(535)	34	186
Total assets	1,985	53	2,321		4,359
Capital expenditures	41				41
Depreciation	41	4	1		46

The following table presents the details of Other segment loss:

(Dollars in thousands)	Three Months Ended	Six Months Ended
	June 30, 2013	June 30, 2013
Corporate and other (expenses) income:		
Salaries and benefits	\$ (189)	\$ (267)
Income tax expense	(156)	(155)
Other (expense) income, net	(41)	(113)
Total Other segment loss	\$ (386)	\$ (535)

9. Commitments and Contingencies

Commitments:

Leases

The Company and its subsidiary lease certain manufacturing, laboratory and office facilities. The lease provides for the Company to pay its allocated share of insurance, taxes, maintenance and other costs of the leased property. Under the May 2, 2014 agreement, MTI Instruments has an option to terminate the lease as of December 1, 2016. If MTI Instruments terminates the lease prior to November 2019, MTI Instruments is required to reimburse the landlord for all unamortized costs that the landlord is incurring for renovations to the leased space in conjunction with the lease renewal.

Future minimum rental payments required under non-cancelable operating leases (with initial or remaining lease terms in excess of one year) as of June 30, 2014 are (dollars in thousands): \$136 remaining in 2014, \$213 in 2015, \$214 in 2016, \$218 in 2017, \$218 in 2018 and \$204 thereafter.

Warranties

Product warranty liabilities are included in Accrued liabilities in the Condensed Consolidated Balance Sheets. Below is a reconciliation of changes in product warranty liabilities:

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(Dollars in thousands)

Six Months Ended

	June 30, 2014		2013	
Balance, January 1	\$ 17		\$ 20	
Accruals for warranties issued	10		14	
Settlements made (in cash or in kind)	(6)	(9)
Balance, end of period	\$ 21		\$ 25	

Employment Agreement

The Company has an employment agreement with one employee that provides certain payments upon termination of employment under certain circumstances, as defined in the agreement. As of June 30, 2014, the Company's potential minimum obligation to this employee was approximately \$70 thousand.

Contingencies:

Legal

We are subject to legal proceedings, claims and liabilities which arise in the ordinary course of business. We accrue for losses associated with legal claims when such losses are probable and can be reasonably estimated. These accruals are adjusted as additional information becomes available or circumstances change. Legal fees are charged to expense as they are incurred.

10. Line of Credit

On May 5, 2014, the Company entered into a new revolving line of credit with Bank of America, N.A. (the Bank) to replace MTI Instruments line of credit as discussed below. The Company may borrow under the line of credit from time to time up to \$1 million to support its working capital needs. The line of credit is available until July 31, 2015 and may be renewed subject to all the terms and conditions as set forth in the Loan Agreement (the Loan). The Loan is payable no later than the expiration date of the Loan and interest is payable on the last day of each month beginning on May 30, 2014 and until payment has been made in full. The interest rate on funds borrowed under the line of credit is equal to the LIBOR Daily Floating Rate plus 2.75%. The Loan is secured by equipment and fixtures, inventory and receivables owned by the Company and guaranteed by MTI Instruments. The Company is required to hold a balance of \$0 for 30 consecutive days during the period from May 5, 2014 through July 31, 2015, and each subsequent one-year period of the Loan, if any. Upon the occurrence of an event of default, the Bank may set off against our repayment obligations any amounts we maintain at the Bank. The Company is also subject to other restrictions as set forth in the Loan. As of June 30, 2014, there were no amounts outstanding under the line of credit.

On September 20, 2011, MTI Instruments entered into a working capital line of credit with First Niagara Bank, N.A. Under this agreement, MTI Instruments could borrow from time to time up to \$400 thousand to support its working capital needs. The note was payable upon demand, and the interest rate on the note was equal to the prime rate with a floor of 4.0% per annum. The note was secured by a lien on all of the assets of MTI Instruments and was guaranteed by the Company. The line of credit was renewed on September 23, 2013 and expired on June 30, 2014. Under this line of credit, MTI Instruments was required to maintain a line balance of \$0 for 30 consecutive days during each calendar year. As of December 31, 2013, there were no amounts outstanding under the line of credit.

11. Stock Based Compensation

The Mechanical Technology, Incorporated 2014 Equity Incentive Plan (the 2014 Plan) was adopted by the Company's Board of Directors on March 12, 2014 and approved by its stockholders on June 11, 2014. The 2014 Plan provides an initial aggregate number of 500,000 shares of common stock that may be awarded or issued. The number of shares that may be awarded under the 2014 Plan and awards outstanding may be subject to adjustment on account of any stock dividend, spin-off, stock split, reverse stock split, split-up, recapitalization, reclassification, reorganization, combination or exchange of shares, merger, consolidation, liquidation, business combination, exchange of shares or the like. Under the 2014 Plan, the Board appointed administrator of the 2014 Plan is authorized to issue stock options (incentive and nonqualified), stock appreciation rights, restricted stock, restricted stock units, phantom stock, performance awards and other stock-based awards to employees, officers and directors of, and other individuals providing bona fide services to or for, the Company or any affiliate of the Company. Incentive stock options may only be granted to employees of the Company and its subsidiaries. As of June 30, 2014, no awards have been issued under the 2014 Plan.

The Mechanical Technology Incorporated 2012 Equity Incentive Plan (the 2012 Plan) was adopted by the Company's Board of Directors on April 14, 2012 and approved by stockholders on June 14, 2012. The 2012 Plan provides an initial aggregate number of 600,000 shares of common stock which may be awarded or issued. The number of shares which may be awarded under the 2012 Plan and awards outstanding can be subject to adjustment on account of any recapitalization, reclassification, stock split, reverse stock split and other dilutive changes in Common Stock. Under the 2012 Plan, the Board of Directors is authorized to issue stock options (incentive and nonqualified), stock appreciation rights, restricted stock, restricted stock units and other stock-based awards to employees, officers, directors, consultants and advisors of the Company and its subsidiaries. Incentive stock options may only be granted to employees of the Company and its subsidiaries.

During 2014, the Company granted 140,000 options to purchase the Company's common stock from the 2012 Plan, which generally vest 25% on each of the first four anniversaries of the date of the award. The exercise price of these grants was \$1.08 per share and was based on the closing

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market price of the Company's common stock on the dates of grant. Using a Black-Scholes Option Pricing Model, the weighted average fair value of these options was \$1.07 per share and was estimated at the date of grant.

During 2013, the Company granted 298,000 options to purchase the Company's common stock from the 2012 Plan, which generally vest 25% on each of the first four anniversaries of the date of the award. The exercise price of these grants was from \$0.46 to \$0.90 per share and was based on the closing market price of the Company's common stock on the dates of grant. Using a Black-Scholes Option Pricing Model, the weighted average fair value of these options was \$0.58 per share and was estimated at the date of grant.

12. Related Party Transactions

MTI Micro

On December 18, 2013, MTI Micro and the Company executed a Senior Demand Promissory Note (the Note) in the amount of \$380 thousand to secure the intercompany amounts due to the Company from MTI Micro upon the deconsolidation of MTI Micro. Interest accrues on the Note at the Prime Rate in effect on the first business day of the month, as published in the Wall Street Journal. Interest began accruing on January 1, 2014. At the Company's option, all or part of the principal and interest due on this Note may be converted to shares of common stock of MTI Micro at a rate of \$0.07 per share. As of June 30, 2014 and December 31, 2013, the Company has recorded a full allowance against the Note. As a result of this allowance, any interest earned on this Note will be recorded when received on a cash basis. As of June 30, 2014 and December 31, 2013, \$386 thousand and \$380 thousand, respectively of principal and interest are available to convert into shares of common stock of MTI Micro.

On December 31, 2013, Dr. Robb exercised a portion of his outstanding MTI Micro warrants to purchase 357,143 shares of MTI Micro Common Stock at an exercise price of \$0.07 per share.

As of June 30, 2014, the Company owned an aggregate of approximately 47.5% of MTI Micro's outstanding common stock, or 75,049,937 shares, and 53.3% of the common stock and warrants issued, which includes 32,904,136 warrants outstanding.

Consulting Services

During the year ended December 31, 2013, the Company paid \$80 thousand to Loudon Advisors for Kevin Lynch's services as the Acting Chief Executive Officer of the Company, through April 30, 2013.

13. New Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board issued Accounting Standards Update 2014-09 (Revenue from Contracts with Customers) to clarify the principles for recognizing revenue and to develop a common revenue standard for GAAP and International Financial Reporting Standards. The standard is principle-based and provides a five-step model to determine when and how revenue is recognized. The core principle is that a company should recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. This standard is effective for fiscal years and interim periods within those years beginning after December 15, 2016; early adoption is

not permitted. This standard is effective for the Company beginning in fiscal 2017 and may be applied retrospectively to each prior period presented or retrospectively with the cumulative effect recognized as of the date of initial application. This standard could impact the timing and amounts of revenue recognized. The Company is currently evaluating the impact of this standard on its consolidated financial statements.

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

Unless the context requires otherwise, the terms we, us, and our refer to Mechanical Technology, Incorporated, a New York Corporation, MTI Instruments refers to MTI Instruments, Incorporated, a New York corporation and our wholly-owned subsidiary, and MTI Micro refers to MTI MicroFuel Cells Incorporated, a Delaware corporation and variable interest entity that was included in our consolidated results through December 31, 2013.

The following discussion of our financial condition and results of operations should be read in conjunction with the Condensed Consolidated Financial Statements and the related notes thereto included in Item 1 of Part I of this Quarterly Report on Form 10-Q and the audited Consolidated Financial Statements and the related notes thereto and Management's Discussion and Analysis of Financial Condition and Results of Operations for the year ended December 31, 2013 contained in our 2013 Annual Report on Form 10-K.

In addition to historical information, the following discussion contains forward-looking statements, which involve risk and uncertainties. Our actual results could differ materially from those anticipated in the forward-looking statements. Important factors that could cause actual results to differ include those set forth in Part I Item 1A-Risk Factors in our Annual Report on Form 10-K for the fiscal year ended December 31, 2013, as filed on March 6, 2014, our Quarterly Report for the period ended March 31, 2014, as filed on May 8, 2014, and elsewhere in this Quarterly Report on Form 10-Q. Readers should not place undue reliance on our forward-looking statements. These forward-looking statements speak only as of the date on which the statements were made and are not guarantees of future performance. Except as may be required by applicable law, we do not undertake or intend to update any forward-looking statements after the date of this Quarterly Report on Form 10-Q. Please see Statement Concerning Forward-Looking Statements below.

Overview

MTI's core business is conducted through MTI Instruments, Inc., a wholly-owned subsidiary and the sole component of the Company's Test and Measurement Instrumentation segment. The Company also operated in a New Energy segment with business conducted through MTI MicroFuel Cells, Inc. until December 31, 2013 (date of MTI Micro deconsolidation).

Test and Measurement Instrumentation Segment MTI Instruments is a supplier of precision linear displacement solutions, vibration measurement and system balancing solutions, precision tensile measurement systems and wafer inspection tools, serving markets that require 1) the precise measurements and control of products and processes in automated manufacturing, assembly, and consistent operation of complex machinery, 2) metrology tools for semiconductor and solar wafer characterization, tensile stage systems for materials testing and precision linear displacement gauges all for use in academic and industrial research and development settings, and 3) engine balancing and vibration analysis systems for both military and commercial aircraft.

We are continuously working on ways to increase our sales reach, including expanded worldwide sales coverage and enhanced internet marketing.

New Energy Segment MTI Micro had been developing an off-the-grid power solution for various portable electronic devices. Its patented proprietary direct methanol fuel cell technology platform converts methanol fuel to usable electricity capable of providing continuous power, as long as necessary fuel flows are maintained.

Recent Developments

On April 7, 2014, MTI Instruments received International Organization for Standardization (ISO) ISO 9001:2008 certification, an internationally recognized standard issued to organizations with a quality management system. The certification was authorized by TÜVRheinland®, a premier global provider of independent testing and certification services with 15 locations throughout North America.

The Mechanical Technology, Incorporated 2014 Equity Incentive Plan (the 2014 Plan) was adopted by the Company's Board of Directors on March 12, 2014 and approved by its stockholders on June 11, 2014. The 2014 Plan provides an initial aggregate number of 500,000 shares of common stock that may be awarded or issued. The number of shares that may be awarded under the 2014 Plan and awards outstanding may be subject to adjustment on account of any stock dividend, spin-off, stock split, reverse stock split, split-up, recapitalization, reclassification, reorganization, combination or exchange of shares, merger, consolidation, liquidation, business combination, exchange of shares or the like. Under the 2014 Plan, the Board appointed administrator of the 2014 Plan is authorized to issue stock options (incentive and nonqualified), stock appreciation rights, restricted stock, restricted stock units, phantom stock, performance awards and other stock-based awards to employees, officers and directors of, and other individuals providing bona fide services to or for, the Company or any affiliate of the Company. Incentive stock options may only be granted to employees of the Company and its subsidiaries. As of June 30, 2014, no awards have been issued under the 2014 Plan.

Results of Operations

Results of Operations for the Three and Six Months Ended June 30, 2014 Compared to the Three and Six Months Ended June 30, 2013.

Test and Measurement Instrumentation Segment

Product Revenue: Product revenue consists of revenue recognized from the Test and Measurement Instrumentation product lines.

Product revenue in our Test and Measurement Instrumentation segment for the three months ended June 30, 2014 increased by \$211 thousand, or 9.3%, to \$2.5 million from \$2.3 million during the three months ended June 30, 2013. This increase in product revenue was attributable to additional shipments of aviation balancing systems to the U.S. Air Force under an existing contract and higher laser sales, which offset the impact of no sales of any new wafer metrology tools during the quarter, compared to sales of \$125 thousand of wafer metrology tools during the comparable 2013 period. For the three months ended June 30, 2014, the largest commercial customer for the segment was an Asian customer, which accounted for \$540 thousand, or 21.8%, of the second quarter 2014 revenue. In the second quarter of 2013, the largest commercial customer for the segment was an Asian distributor, which accounted for \$196 thousand, or 8.7%, of the second quarter 2013 revenue. The U.S. Air Force was the largest government customer for the three months ended June 30, 2014 and 2013, and accounted for \$770 thousand, or 31.1%, of the second quarter 2014 revenue and \$740 thousand, or 32.6%, of the second quarter 2013 revenue.

Product revenue in our Test and Measurement Instrumentation segment for the six months ended June 30, 2014 decreased by \$607 thousand, or 13.6%, to \$3.9 million from \$4.5 million for the same period in 2013. This decrease in product revenue was attributable to a decline in commercial aviation balancing system activity and the lack of semi-automated wafer metrology tool sales during 2014, compared to \$274 thousand of such sales during the six months ended June 30, 2013. These declines were partially offset by increases in laser and capacitance product sales. For the six months ended June 30, 2014, the largest commercial customer for the segment was an Asian customer, which accounted for \$540 thousand, or 14.0%, of the year-to-date revenue. During the six months ended June 30, 2013, the largest commercial customer for the segment was an Asian distributor, which accounted for \$374 thousand, or 8.4%, of the year-to-date revenue. The U.S. Air Force was the largest government customer for the six months ended June 30, 2014 and 2013, accounting for \$870 thousand, or 22.5%, and \$1.4 million, or 31.7%, respectively, of revenue for the six month periods ended June 30, 2014 and 2013.

Information regarding government contracts included in product revenue is as follows:

(Dollars in thousands)		Revenues for the Three Months Ended	Revenues for the Six Months Ended	Contract Revenues to Date	Total Contract Orders Received

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Contract ⁽¹⁾	Expiration	June 30,				June 30,				June 30,				to Date June 30,			
		2014		2013		2014		2013		2014		2014		2014			
Aviation Balancing Systems																	
\$6.5 million U.S. Air Force Maintenance	09/27/2014 ⁽²⁾	\$	139	\$	133	\$	228	\$	177	\$	4,499	\$	4,542				
\$4.1 million U.S. Air Force Systems	08/29/2015 ⁽²⁾	\$	627	\$	342	\$	627	\$	342	\$	1,881	\$	1,938				
\$917 thousand U.S. Air Force Kit	09/30/2014 ⁽³⁾	\$		\$	73	\$		\$	585	\$	769	\$	769				

(1) Contract values represent maximum potential values at time of contract placement and may not be representative of actual results.

(2) Date represents expiration of contract, which includes the exercise of all four option extensions.

(3) Date represents expiration of contract, which includes the exercise of two option extensions.

Cost of Product Revenue: Cost of product revenue includes the direct material and labor cost as well as an allocation of overhead costs that relate to the manufacturing of products we sell. In addition, cost of product revenue also includes the labor and material costs incurred for product maintenance, replacement parts and service under our contractual obligations.

Cost of product revenue in our Test and Measurement Instrumentation segment for the three months ended June 30, 2014 increased by \$196 thousand, or 24.5%, to \$997 thousand from \$801 thousand during the three months ended June 30, 2013. This increase is primarily a result of the increased sales as discussed above under *Product Revenue*. Gross profit, as a percentage of product revenue, decreased to 59.8%, compared to 64.7% for the same period in 2013 due to the composition of the product sales mix and competitive pricing strategies in Asia.

Cost of product revenue in our Test and Measurement Instrumentation segment for the six months ended June 30, 2014 decreased by \$200 thousand, or 11.3%, to \$1.6 million from \$1.8 million for the same period in 2013. This decrease is primarily a result of the decreased sales as discussed above under *Product Revenue*. Gross profit, as a percentage of product revenue, decreased to 59.2%, compared to 60.2% for the same period in 2013 due to the composition of the product sales mix and competitive pricing strategies in Asia.

Unfunded Research and Product Development Expenses: Unfunded research and product development expenses (meaning research and development that we conduct that is not reimbursed by customers) includes the costs of materials to build development and prototype units, cash and non-cash compensation and benefits for the engineering and related staff, expenses for contract engineers, fees paid to outside suppliers for subcontracted components and services, fees paid to consultants for services provided, materials and supplies consumed, facility related costs such as computer and network services, and other general overhead costs associated with our research and development activities.

Unfunded research and product development expenses in our Test and Measurement Instrumentation segment for the three months ended June 30, 2014 increased by \$64 thousand, or 20.8%, to \$371 thousand from \$307 thousand during the three months ended June 30, 2013. This increase was due to higher labor costs and additional material spending on current development projects.

Unfunded research and product development expenses in our Test and Measurement Instrumentation segment for the six months ended June 30, 2014 increased by \$85 thousand, or 13.1%, to \$732 thousand from \$647 thousand for the same period in 2013. This increase was due to higher labor costs and additional material spending on current development projects.

Selling, General and Administrative Expenses: Selling, general and administrative expenses includes cash and non-cash compensation, benefits and related costs in support of our general corporate functions, including general management, finance and accounting, human resources, selling and marketing, information technology and legal services.

Selling, general and administrative expenses in our Test and Measurement Instrumentation segment for the three months ended June 30, 2014 increased by \$68 thousand, or 13.6%, to \$569 thousand from \$501 thousand during the three months ended June 30, 2013. This increase is the result of additional staffing in the sales department, increased international travel and higher commissions to external sales representatives.

Selling, general and administrative expenses in our Test and Measurement Instrumentation segment for the six months ended June 30, 2014 increased by \$99 thousand, or 9.8%, to \$1.1 million from \$1.0 million for the same period in 2013. This increase is the result of additional staffing in the sales department, higher commissions to external sales representatives due to the change in product mix and increased international travel.

New Energy Segment

Selling, General and Administrative Expenses: Selling, general and administrative expenses in our New Energy segment for the three and six months ended June 30, 2013 were \$17 thousand and \$42 thousand, respectively. As of December 31, 2013, the Company no longer reported the New Energy segment as a VIE and therefore there were no expenses related to this segment for 2014. Refer to the Condensed Consolidated Financial Statements Note 2 regarding the deconsolidation of the VIE.

MTI Parent Corporate Entity

Selling, General and Administrative Expenses: Selling, general and administrative expenses incurred by the Corporate Entity for the three months ended June 30, 2014 decreased by \$46 thousand, or 11.2%, to \$363 thousand from \$409 thousand during the three months ended June 30, 2013. This decrease is primarily the result of consulting costs incurred during 2013 in connection with the termination of Peng K. Lim, the Company's former Chief Executive Officer, in 2012.

Selling, general and administrative expenses incurred by the Corporate Entity for the six months ended June 30, 2014 increased by \$3 thousand, or 0.4%, to \$698 thousand from \$695 thousand for the same period in 2013.

Results of Consolidated Operations

Operating Income (Loss): Operating income for the three months ended June 30, 2014 was \$178 thousand compared to operating income of \$232 thousand during the comparable 2013 period. This change in operating income was a result of the factors noted above, primarily due to the composition of the product sales mix and competitive pricing strategies in Asia.

Operating loss for the six months ended June 30, 2014 was \$254 thousand compared to operating income of \$298 thousand during the comparable 2013 period. The change in operating income (loss) was a result of the factors noted above, primarily the decrease in product revenue.

Income Tax Expense: Income tax expense for the three months ended June 30, 2014 and 2013 was \$0 and \$156 thousand, respectively. Our income tax rate for the three months ended June 30, 2014 and 2013 was 0% and 64.7%, respectively.

Income tax expense for the six months ended June 30, 2014 and 2013 was \$0 and \$155 thousand, respectively. Our income tax rate for the six months ended June 30, 2014 and 2013 was 0% and 50.6%, respectively.

Net Loss Attributed to Non-Controlling Interests (of MTI Micro): The net loss attributed to non-controlling interests for the three and six months ended June 30, 2013 was \$15 thousand and \$34 thousand, respectively. As of December 31, 2013, the Company no longer reported the New Energy segment as a VIE. Refer to the Condensed Consolidated Financial Statements Note 2 regarding the deconsolidation of the VIE.

Net Income (Loss) Attributed to MTI: Net income attributed to MTI for the three months ended June 30, 2014 was \$178 thousand compared to \$100 thousand during the comparable 2013 period. The \$78 thousand increase in net income is primarily attributable to the fact that we had no income tax expense during the period compared to a \$156 thousand income tax expense during the three months ended June 30, 2013, partially offset by the \$131 thousand decrease in MTI Instruments net income for the three months ended June 30, 2014 as compared to the same period in 2013.

Net loss attributed to MTI for the six months ended June 30, 2014 was \$254 thousand compared to net income of \$186 thousand during the comparable 2013 period. The \$440 thousand decrease in net income is primarily attributable to the \$646 thousand decrease in MTI Instruments net income for the six months ended June 30, 2014, as compared to the same period in 2013, partially offset by the fact that we had no income tax expense during the 2014 period compared to a \$155 thousand income tax expense for the six months ended June 30, 2013.

Management's Plan, Liquidity and Capital Resources

Several key indicators of our liquidity are summarized in the following table:

(Dollars in thousands)	Six Months Ended June 30,	Six Months Ended June 30,	Year Ended Dec 31,
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	2014		2013		2013
Cash	\$ 774		\$ 835		\$ 1,211
Working capital	1,568		1,687		1,771
Net (loss) income attributed to MTI	(254)		186		3,654
Net cash (used in) provided by operating activities	(405)		578		1,017
Purchase of property, plant and equipment	(32)		(41)		(108)

The Company has historically incurred significant losses, until 2012 the majority stemming from the direct methanol fuel cell product development and commercialization programs of MTI Micro, and had a consolidated accumulated deficit of \$118.8 million as of June 30, 2014. During the six months ended June 30, 2014, the Company had a net loss attributed to MTI of \$254 thousand, had cash used in operating activities totaling \$405 thousand and had working capital of \$1.6 million. Management believes that the Company currently has adequate resources to avoid cost cutting measures that could adversely affect the business. As of June 30, 2014, we had no debt, no capital expenditure commitments and approximately \$774 thousand of cash available to fund our operations.

If production levels rise at MTI Instruments, additional capital equipment may be required in the foreseeable future. We expect to spend approximately \$225 thousand on capital equipment and \$1.5 million in research and development on MTI Instruments products during 2014. We expect to finance any future expenditures and continue funding our operations from our current cash position and our projected 2014 cash flow pursuant to management's current plan. We may also seek to supplement our resources through sales of stock or assets. Besides the Company's line of credit, the Company has no other commitments for funding future needs of the organization at this time and such additional financing during 2014, if required, may not be available to us on acceptable terms or at all.

While it cannot be assured, management believes that, due in part to our current working capital level, recent replacements in sales staff and projected inventory reductions, the Company should, for the full-year 2014, continue the positive cash flows it experienced during 2013 to fund the Company's active operations for the foreseeable future. However, if near-term revenue estimates are delayed or missed, the Company may need to implement additional steps to ensure liquidity including, but not limited to, the deferral of planned capital spending and/or delaying existing or pending product development initiatives. Such steps, if required, could potentially have a material and adverse effect on our business, results of operations and financial condition.

Line of Credit

On May 5, 2014, the Company entered into a new revolving line of credit with Bank of America, N.A. (the Bank) to replace MTI Instruments line of credit as discussed below. The Company may borrow under the line of credit from time to time up to \$1 million to support its working capital needs. The line of credit is available until July 31, 2015 and may be renewed subject to all the terms and conditions as set forth in the Loan Agreement (the Loan). The Loan is payable no later than the expiration date of the Loan, currently July 31, 2015, and interest is payable on the last day of each month beginning on May 30, 2014 and until payment has been made in full. The interest rate on funds borrowed under the line of credit is equal to the LIBOR Daily Floating Rate plus 2.75%. The Loan is secured by equipment and fixtures, inventory and receivables owned by the Company and guaranteed by MTI Instruments. The Company is required to hold a balance of \$0 for 30 consecutive days during the period from May 5, 2014 through July 31, 2015, and each subsequent one-year period of the Loan, if any. Upon the occurrence of an event of default, the Bank may set off against our repayment obligations any amounts we maintain at the Bank. The Company is also subject to other restrictions as set forth in the Loan. As of June 30, 2014, there were no amounts outstanding under the line of credit.

On September 20, 2011, MTI Instruments entered into a working capital line of credit with First Niagara Bank, N.A. Under this agreement, MTI Instruments could borrow from time to time up to \$400 thousand to support its working capital needs. The note was payable upon demand, and the interest rate on the note was equal to the prime rate with a floor of 4.0% per annum. The note was secured by a lien on all of the assets of MTI Instruments and was guaranteed by the Company. The line of credit was renewed on September 23, 2013 and expired on June 30, 2014. Under this line of credit, MTI Instruments was required to maintain a line balance of \$0 for 30 consecutive days during each calendar year. As of December 31, 2013, there were no amounts outstanding under the line of credit.

Backlog, Inventory and Accounts Receivable

At June 30, 2014, our order backlog was \$709 thousand compared to \$667 thousand at June 30, 2013 and \$198 thousand at December 31, 2013. The increase in backlog from December 2013 was due to increased capacitance and tensile stage order activity during the first quarter of 2014 and increased laser and aviation balancing system order activity during the second quarter of 2014.

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Our inventory turnover ratios and average accounts receivable days outstanding for the trailing twelve month periods and their changes at June 30, 2014 and 2013 are as follows:

	2014	2013	Change
Inventory turnover	3.8	2.8	1.0
Average accounts receivable days outstanding	42	40	2

The increase in the current twelve-month inventory turns is due to improved inventory management producing a 32% decrease in average inventory balances over the last year.

The average accounts receivable days outstanding increased 2 days in 2014 compared with 2013 due to a growth in direct sales to Asia, rather than through regional distributors.

Off-Balance Sheet Arrangements

We have no off balance sheet arrangements.

Critical Accounting Policies and Significant Judgments and Estimates

The discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. Note 2, Accounting Policies, to the consolidated financial statements in our Annual Report on Form 10-K for the year ended December 31, 2013 includes a summary of our most significant accounting policies. There have been no material changes to the critical accounting policies previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2013. The preparation of these condensed consolidated financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues, expenses, and related disclosure of assets and liabilities. On an ongoing basis, we evaluate our estimates and judgments, including those related to revenue recognition, inventories, income taxes and stock-based compensation. We base our estimates on historical experience and on various other factors that we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. Periodically, our management reviews our critical accounting estimates with the Audit Committee of our Board of Directors.

Recent Accounting Pronouncements

A discussion of recent accounting pronouncements is included in Note 13, New Accounting Pronouncements, of the unaudited condensed consolidated financial statements in Part I, Item 1 of this Form 10-Q.

Statement Concerning Forward-Looking Statements

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (Securities Act) and Section 21E of the Securities Exchange Act of 1934, as amended (Exchange Act). Any statements contained in this Form 10-Q that are not statements of historical fact may be forward-looking statements. When we use the words anticipate, estimate, plans, projects, continuing, ongoing, expects, management believes, we believe, we intend, should, could, may, will and similar words or phrases identifying forward-looking statements. Such forward-looking statements include, but are not limited to, statements regarding:

- projected taxable income and the ability to use deferred tax assets;
- management's belief that it will have adequate resources to fund the Company's operations and capital expenditures over at least the next twelve months;
- anticipated levels of future earnings and continued positive cash flow for 2014;
- the expectation that cost-cutting measures will be avoided;
- future capital expenditures and spending on research and development;
- needing to purchase equipment;
- expected funding of future cash expenditures; and
- projected inventory reductions.

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Forward-looking statements involve risks, uncertainties, estimates and assumptions which may cause our actual results, performance or achievements to be materially different from those expressed or implied by forward-looking statements. Important factors that could cause these differences include the following:

- statements with respect to management's strategy and planned initiatives;
- sales revenue growth may not be achieved or maintained;

- the dependence of our business on a small number of customers and potential loss of government contracts particularly in light of expected defense department spending reductions resulting from the sequestration implemented in 2013 or cuts that may be imposed as a result of ongoing Congressional budget negotiations;
- our lack of long-term purchase commitments from our customers and the ability of our customers to cancel, reduce, or delay orders for our products;

- our inability to build and maintain relationships with our customers;
- our inability to develop and utilize new technologies that address the needs of our customers;
- the cyclical nature of the electronics and military industries;
- the uncertainty of the U.S. and global economy;
- the impact of future exchange rate fluctuations;
- failure of our strategic alliances to achieve their objectives or perform as contemplated and the risk of cancellation or early termination of such alliance by either party;
- the loss of services of one or more of our key employees or the inability to hire, train, and retain key personnel;

- risks related to protection and infringement of intellectual property;
- our occasional dependence on sole suppliers or a limited group of suppliers;

- our ability to generate income to realize the tax benefit of our historical net operating losses;

- risks related to the limitation of the use, for tax purposes, of our net historical operating losses in the event of certain ownership changes; and
- other factors discussed under the heading "Risk Factors" in our Annual Report on Form 10-K for the fiscal year ended December 31, 2013 and our Quarterly Report on Form 10-Q for the period ended March 31, 2014.

Forward-looking statements speak only as of the date they are made. You should not put undue reliance on any forward-looking statements. We assume no obligation to update forward-looking statements to reflect actual results, changes in assumptions, or changes in other factors affecting forward-looking information, except to the extent required by applicable securities laws. If we do update one or more forward-looking statements, no inference should be drawn that we will make additional updates with respect to those or other forward-looking statements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Not applicable.

Item 4. Controls and Procedures

The certifications of our Chief Executive Officer and Chief Financial Officer attached as Exhibits 31.1 and 31.2 to this Quarterly Report on Form 10-Q include, in paragraph 4 of such certifications, information concerning our disclosure controls and procedures and internal control over financial reporting. Such certifications should be read in conjunction with the information contained in this Item 4 for a more complete understanding of the matters covered by such certifications.

(a) Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and our Chief Financial Officer, evaluated the effectiveness of MTI's disclosure controls and procedures as of June 30, 2014. The term "disclosure controls and procedures," as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. We recognize that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and we necessarily apply our judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the evaluation of our disclosure controls and procedures as of June 30, 2014, our Chief Executive Officer and Chief Financial Officer concluded that, as of such date, our disclosure controls and procedures were effective at the reasonable assurance level.

(b) Changes in Internal Control Over Financial Reporting

There have been no changes in our internal control over financial reporting, as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act, during our fiscal quarter ended June 30, 2014 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

At any point in time, we may be involved in various lawsuits or other legal proceedings. Such lawsuits could arise from the sale of products or services or from other matters relating to our regular business activities, compliance with various governmental regulations and requirements, or other transactions or circumstances. We do not believe there are any such proceedings presently pending. See Note 9, Commitments and Contingencies, to our condensed consolidated financial statements for further information.

Item 1A. Risk Factors

Part II, Item 1A (Risk Factors) of our most recently filed Annual Report on Form 10-K with the Securities and Exchange Commission (SEC), filed on March 6, 2014, sets forth information relating to important risks and uncertainties that could materially adversely affect our business, financial condition and operating results. Except to the extent that information disclosed elsewhere in this Quarterly Report on Form 10-Q relates to such risk factors (including, without limitation, the matters described in Part I, Item 2 (Management's Discussion and Analysis of Financial Condition and Results of Operations - Statement Concerning Forward Looking Statements), there have been no material changes to our risk factors disclosed in our most recently filed Annual Report on Form 10-K and our Quarterly Report on Form 10-Q for the period ended March 31, 2014. However, those risk factors continue to be relevant to an understanding of our business, financial condition and operating results and, accordingly, you should review and consider such risk factors in making any investment decision with respect to our securities.

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

None

Item 3. Defaults Upon Senior Securities

None

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

Not applicable.

Item 6. Exhibits

<u>Exhibit</u>	<u>Description</u>
<u>No.</u>	

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- 10.1# Mechanical Technology, Incorporated 2014 Equity Incentive Plan (incorporated by reference to Exhibit A to the Registrant's Proxy Statement on Schedule 14A filed with the Commission on April 25, 2014)
- 10.2# Form of Restricted Stock Grant Agreement under the Mechanical Technology, Incorporated 2014 Equity Incentive Plan (incorporated by reference from Exhibit 4.2 of the Company's Registration Statement on Form S-8 (File No. 333-196989) filed with the Commission on June 24, 2014)
- 10.3# Form of Nonstatutory Stock Option Grant Agreement under the Mechanical Technology, Incorporated 2014 Equity Incentive Plan (incorporated by reference from Exhibit 4.3 of the Company's Registration Statement on Form S-8 (File No. 333-196989) filed with the Commission on June 24, 2014)
- 10.4# Form of Incentive Stock Option Grant Agreement under the Mechanical Technology, Incorporated 2014 Equity Incentive Plan (incorporated by reference from Exhibit 4.4 of the Company's Registration Statement on Form S-8 (File No. 333-196989) filed with the Commission on June 24, 2014)
- 10.5 Amendment No. 2 to Lease Agreement Between MTI Instruments Inc. and Carl E. Touhey dated May 2, 2014 (incorporated by reference from Exhibit 10.1 of the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2014)
- 31.1 Rule 13a-14(a)/15d-14(a) Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, of Kevin G. Lynch
- 31.2 Rule 13a-14(a)/15d-14(a) Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, of Frederick W. Jones
- 32.1 Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, of Kevin G. Lynch
- 32.2 Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, of Frederick W. Jones

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<u>Exhibit No.</u>	<u>Description</u>
101.INS*	XBRL Instance Document
101.SCH*	XBRL Taxonomy Extension Schema Document
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF*	XBRL Taxonomy Definition Linkbase Document
101.LAB*	XBRL Taxonomy Extension Label Linkbase Document
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase Document

All other exhibits for which no other filing information is given are filed herewith.

* Submitted electronically herewith. Attached as Exhibit 101 are the following materials from the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2014, formatted in eXtensible Business Reporting Language (XBRL) and tagged as blocks of text and including detailed tags: (i) Condensed Consolidated Balance Sheets at June 30, 2014 and December 31, 2013; (ii) Condensed Consolidated Statements of Operations for the Three and Six Months Ended June 30, 2014 and 2013; (iii) Condensed Consolidated Statements of Cash Flows for the Six Months Ended June 30, 2014 and 2013; and (iv) related notes.

Represents management contract or compensation plan or arrangement.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Mechanical Technology, Incorporated

Date: August 7, 2014

By: /S/ Kevin G. Lynch
Kevin G. Lynch
Chief Executive Officer

By: /S/ Frederick W. Jones
Frederick W. Jones
Chief Financial Officer

