Ocean Power Technologies, Inc.
Form 10-K
July 14, 2010

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-K

þ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended April 30, 2010

or

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

Commission File Number 001-33417

Delaware	**22-2535818**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*

1590 REED ROAD
PENNINGTON, NJ 08534
(Address of principal executive offices, including zip code)

Registrant s telephone number, including area code: (609) 730-0400

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

Title of Each Class	**Name of Exchange on Which Registered**
Common Stock, par value $0.001	The Nasdaq Global Market

Securities registered pursuant to Section 12(g) of the Act:
None

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

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

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 þ No o

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes o No o

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

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

Large accelerated filer o Accelerated filer þ Non-accelerated filer o Smaller reporting company o
(Do not check if a 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 o No þ

The aggregate market value of the common stock of the registrant held by non-affiliates as of October 31, 2009, the last business day of the registrant s most recently completed second fiscal quarter, was $57.8 million based on the closing sale price of the registrant s common stock on that date as reported on the Nasdaq Global Market.

The number of shares outstanding of the registrant s common stock as of June 30, 2010 was 10,390,563.

DOCUMENTS INCORPORATED BY REFERENCE

Document	Part of the Form 10-K into Which Incorporated
Proxy Statement for the registrant s 2010 Annual Meeting of Stockholders	III

OCEAN POWER TECHNOLOGIES, INC.

INDEX TO REPORT ON FORM 10-K

PowerBuoy® is a registered trademark of Ocean Power Technologies, Inc. The Ocean Power Technologies logo, CellBuoy™, Talk on Water™ and Making Waves in Power SM are trademarks or service marks of Ocean Power Technologies, Inc. All other trademarks appearing in this annual report are the property of their respective holders.

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Special Note Regarding Forward-Looking Statements

We have made statements in this Annual Report on Form 10-K (the Annual Report) in, among other sections, Item 1 Business, Item 1A Risk Factors, Item 3 Legal Proceedings, and Item 7 Management s Discussion and Analys Financial Condition and Results of Operations that are forward-looking statements. Forward-looking statements convey our current expectations or forecasts of future events. Forward-looking statements include statements regarding our future financial position, business strategy, budgets, projected costs, plans and objectives of management for future operations. The words may, continue, estimate, intend, plan, will, believe, project anticipate and similar expressions may identify forward-looking statements, but the absence of these words does not necessarily mean that a statement is not forward-looking.

Any or all of our forward-looking statements in this Annual Report may turn out to be inaccurate. We have based these forward-looking statements on our current expectations and projections about future events and financial trends that we believe may affect our financial condition, results of operations, business strategy and financial needs. They may be affected by inaccurate assumptions we might make or unknown risks and uncertainties, including the risks, uncertainties and assumptions described in Item 1A Risk Factors. In light of these risks, uncertainties and assumptions, the forward-looking events and circumstances discussed in this report may not occur as contemplated, and actual results could differ materially from those anticipated or implied by the forward-looking statements.

You should not unduly rely on these forward-looking statements, which speak only as of the date of this filing. Unless required by law, we undertake no obligation to publicly update or revise any forward-looking statements to reflect new information or future events or otherwise.

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PART I

ITEM 1. *BUSINESS*

Overview

We develop and are commercializing proprietary systems that generate electricity by harnessing the renewable energy of ocean waves. The energy in ocean waves is predictable, and electricity from wave energy can be produced on a consistent basis at numerous sites located near major population centers worldwide. Wave energy is an emerging segment of the renewable energy market. Based on our proprietary technology, considerable ocean experience, existing products and expanding commercial relationships, we believe we are a leading wave energy company.

We currently offer two products as part of our line of PowerBuoy® systems: a utility PowerBuoy system and an autonomous PowerBuoy system. Our PowerBuoy system is based on modular, ocean-going buoys, which we have been ocean testing for over a decade. The rising and falling of the waves moves the buoy-like structure creating mechanical energy that our proprietary technologies convert into electricity. We have tested and developed wave power generation and control technology using proven equipment and processes in novel applications and have deployed and maintained our systems in the ocean. The PowerBuoy technology has the unique, patented capability to electronically tune itself automatically as wave characteristics change. This enables the PowerBuoy to optimize its efficiency and resulting power output in dynamic ocean wave conditions. Our two PowerBuoy products are designed for the following applications:

Our utility PowerBuoy system is capable of supplying electricity to a local or regional electric power grid. Our wave power stations will be comprised of a single PowerBuoy system or an integrated array of PowerBuoy systems, plus the remaining components required to deliver electricity to a power grid. We intend to sell our utility PowerBuoy system to utilities and other electrical power producers seeking to add electricity generated by wave energy to their existing electricity supply. In July 2007, our PowerBuoy interface with the electrical utility power grid was certified as compliant with international standards. An independent laboratory provided testing and evaluation services to certify that our systems comply with designated national and international standards. The PowerBuoy grid interface bears the Electrical Testing Laboratories (ETL) listing mark, and can be connected to the utility grid.

Our autonomous PowerBuoy system is designed to generate power for use independent of the power grid in remote locations. There are a variety of potential applications for this system, including sonar and radar surveillance, tsunami warning, oceanographic data collection, offshore platforms and offshore aquaculture.

Our product development and engineering efforts currently are focused on increasing the reliability and peak-rated output of our utility PowerBuoy system to 150 kilowatts (kW), and, to a lesser extent increasing the peak rated output of the system to 500kW. In addition, we are researching and developing new products, product applications and complementary technologies. We believe that, by increasing the maximum rated output of our utility PowerBuoy system, we will be able to decrease the cost per kW of our PowerBuoy system and the cost per kilowatt hour of the energy generated.

We expect to market our undersea substation pod and undersea power connection infrastructure services to other companies in the marine energy sector. We completed the successful in-ocean trials of our undersea substation pod (USP) in 2009. The USP, based on our proprietary design, has been developed to facilitate the collection, networking and transforming of power and data generated by multiple offshore energy devices. The USP has been built as an open

platform, and can provide connectivity for the PowerBuoy as well as other offshore energy systems developed by other companies. The required switching and protection circuits for the individual PowerBuoys are also included in the USP.

In addition, we are focusing on expanding our key commercial opportunities for both the utility and the autonomous PowerBuoy systems. We currently have commercial relationships with the following:

The United States Navy

To develop and build wave power systems at the US Marine Corps base in Hawaii.

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To provide PowerBuoy technology to a unique program for ocean data gathering. Under this program, the Navy will conduct an ocean test of an advanced design of our autonomous PowerBuoy as the power source for the Navy s Deep Water Active Detection System.

To provide our PowerBuoy wave conversion system to the Navy s Littoral Expeditionary Autonomous PowerBuoy (LEAP) Program.

Pacific Northwest Generating Cooperative (PNGC Power) and the US Department of Energy, both of which are providing funding toward the fabrication and ocean installation of a 150kW PowerBuoy near Reedsport, Oregon.

The Scottish Government, to develop a 150kW PowerBuoy for deployment in Scotland.

Iberdrola S.A., or Iberdrola, which is a large electric utility company located in Spain and one of the largest renewable energy producers in the world, Total S.A., or Total, which is one of the world s largest oil and gas companies, and two Spanish governmental agencies, for the first phase of the construction of a wave power station off the coast of Santoña, Spain.

The US Department of Energy (DOE) to help fund the scale-up of the power output per PowerBuoy from the current level of 150kW to 500kW.

Mitsui Engineering and Shipbuilding, with which we are working to develop a wave power project in Japan.

Leighton Contractors, a major Australian construction and infrastructure company, for the development of a wave power station in Victoria, Australia.

We were incorporated under the laws of the State of New Jersey in April 1984 and began commercial operations in 1994. On April 23, 2007, we reincorporated in Delaware. Our principal executive offices are located at 1590 Reed Road, Pennington, New Jersey 08534, and our telephone number is (609) 730-0400. Our website address is *www.oceanpowertechnologies.com.* We make available free of charge on our website our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to those reports as soon as reasonably practicable after such material is filed electronically with the Securities and Exchange Commission, or SEC. The information on our website is not a part of this Annual Report. Our common stock has been listed on the AIM market of the London Stock Exchange plc since October 2003 and on the NASDAQ Global Market since April 24, 2007, the date on which we commenced our initial public offering in the United States.

Our Market

Global demand for electric power is expected to increase from 18.8 trillion kilowatt hours in 2007 to 35.2 trillion kilowatt hours by 2035, according to the Energy Information Administration, or the EIA. To meet this demand, the International Energy Agency, or the IEA, estimates that investments in new generating capacity will be $6.8 trillion in the period from 2007 to 2030, of which new renewable energy generation equipment is expected to account for approximately half of the total projected investment in electricity generation.

According to the EIA, fossil fuels such as coal, oil and natural gas generated over 67% of the world s electricity in 2007. However, a variety of factors are contributing to the increasing development of renewable energy systems that capture energy from replenishable natural resources, including ocean waves, flowing water, wind and sunlight, and convert it into electricity.

Rising cost of fossil fuels. Although subject to short-term fluctuations, the cost of fossil fuel used to generate electricity has been generally rising and is likely to continue to rise in the future.

Dependence on energy from foreign sources. Many countries, including the United States, Japan and much of Europe, depend on foreign resources for a majority of their domestic energy needs. Concerns over political and economic instability in some of the leading fossil fuel producing regions of the world are encouraging consuming countries to diversify their sources of energy.

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Environmental concerns. Environmental concerns regarding the contamination, pollution and by-products from fossil fuels have led many countries and several US states to agree to reduce emissions of carbon dioxide and other gases associated with the use of fossil fuels and to adopt policies promoting the development of cleaner technologies.

Government incentives. Many countries have adopted policies to provide incentives for the development and use of renewable energy sources, such as subsidies to encourage the commercialization of renewable energy power generation.

As a result of these and other factors, the EIA projects that grid-connected renewable generating capacity will continue to grow over the next 25 years.

Wave Energy

The energy in ocean waves is a form of renewable energy that can be harnessed to generate electricity. Ocean waves are created when wind moves across the ocean surface. The interaction between the wind and the ocean surface causes energy to be exchanged. At first, small waves occur on the ocean surface. As this process continues, the waves become larger and the distance between the tops of the waves becomes longer. The size of the waves, and the amount of energy contained in the waves, depends on the wind speed, the time the wind blows over the waves and the distance covered. The rising and falling of the waves move our PowerBuoy system creating mechanical energy that our proprietary technologies convert into usable electricity.

There are a variety of benefits to using wave energy for electricity generation.

Scalability within a small site area. Due to the tremendous energy in ocean waves, wave power stations with high capacity 50 MegaWatts (MW) and above can be installed in a relatively small area. We estimate that, upon completion of the development of our 500kW PowerBuoy system, we would be able to construct a wave power station that would occupy approximately one-tenth of the ocean surface occupied by an offshore wind power station of equivalent capacity.

Predictability. The supply of electricity from wave energy can be forecasted in advance. The amount of energy a wave hundreds of miles away will have when it arrives at a wave power station days later can be calculated based on satellite images and meteorological data with a high degree of accuracy. Power producers can use this information to develop sourcing plans to meet their short-term electricity needs.

Constant source of energy. The annual flow of waves at specific sites can be relatively constant. Based on our studies and analysis of our target sites, we believe our wave power stations will be able to produce usable electricity for approximately 90% of all hours during a year.

Close to population centers. The proximity of wave energy resources to large population areas means that power transmission infrastructure is often already in place and may be utilized for wave energy generation projects.

There are currently several approaches, in different stages of development, for capturing wave energy and converting it into electricity. Methods for generating electricity from wave energy can be divided into two general categories: onshore systems and offshore systems. Our PowerBuoy system is an offshore system. Offshore systems are typically located one to five miles offshore and in water depths of between 100 and 200 feet. The system can be above, on or below the ocean surface. Many offshore systems utilize a floatation device to harness wave energy. The heaving or

pitching of the floatation device due to the force of the waves creates mechanical energy, which is converted into electricity by various technologies. Onshore systems are located at the edge of the shore, often on a sea cliff or a breakwater, and typically must concentrate the wave energy first before using it to drive an electrical generator. Although maintenance costs of onshore systems may be less than those associated with offshore systems, there are a variety of disadvantages with these systems. As waves approach the shore, the energy in the waves decreases; therefore, onshore wave power stations do not take full advantage of the amount of energy that waves in deeper water produce. In addition, there are a limited number of suitable sites for onshore systems and there are environmental and possible aesthetic issues with these wave power stations due to their size and location on the seashore.

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Our Products

We offer two types of PowerBuoy systems: our utility PowerBuoy system, which is designed to supply electricity to a local or regional electric power grid, and our autonomous PowerBuoy system, which is designed to generate power for use independent of the power grid in remote locations. Both products use the same PowerBuoy technology.

Pictured below is our 40kW-rated PowerBuoy system installed during fiscal year 2010 and in operation off Oahu, Hawaii:

Our PowerBuoy system consists of a floating buoy-like device that is loosely moored to the seabed so that it can freely move up and down in response to the rising and falling of the waves, as well as a power take-off device, an electrical generator, a power electronics system and our control system, all of which are sealed in the unit.

The power take-off device converts the mechanical stroking created by the movement of the unit caused by ocean waves into rotational mechanical energy, which, in turn, drives the electrical generator. The power electronics system then conditions the output from the generator into usable electricity. The operation of the PowerBuoy system is controlled by our customized control system.

The control system uses sophisticated sensors and an onboard computer to continuously monitor the PowerBuoy subsystems as well as the height, frequency and shape of the waves interacting with the PowerBuoy system. The control system collects data from the sensors and uses proprietary algorithms to electronically adjust the performance of the PowerBuoy system in real-time and on a wave-by-wave basis. By making these electrical adjustments automatically, the PowerBuoy system is able to maximize the amount of usable electricity generated from each wave. We believe that this ability to optimize the performance of the PowerBuoy system in real-time is a significant advantage of our product.

In the event of storm waves larger than 23 feet, the control system for the PowerBuoy automatically locks down the PowerBuoy system and electricity generation is suspended. When the wave heights return to a normal operating range of 23 feet or less, the control system automatically unlocks the PowerBuoy system and electricity generation and transmission recommence. This safety feature prevents the PowerBuoy system from being damaged by the increased amount of energy in storm waves.

Our 150kW PowerBuoy system has a maximum diameter of 36 feet near the surface, and is 135 feet long, with approximately 30 feet of the PowerBuoy system protruding above the surface of the ocean.

Utility PowerBuoy System

The utility PowerBuoy system is designed to transmit electricity to shore by an underwater power cable, which would then be connected to a power grid. Our current utility PowerBuoy systems presently being marketed to customers have rated capacities of 40kW and 150kW. The utility PowerBuoy system is designed to be positioned in

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water with a depth of 100 to 200 feet, which can usually be found one to five miles offshore. This depth allows the system to capture meaningful amounts of energy from the waves, since decreasing water depth depletes the energy in the waves.

The mooring system for keeping a utility PowerBuoy system in position connects it by lines to three floats that, in turn, are connected by lines to three anchors. This is a well-established mooring system, referred to as three-point mooring, which we have improved upon with various techniques that reduce cost and deployment time.

We refer to the entire utility power generation system at one location as a wave power station, which can either be comprised of a single PowerBuoy system or an integrated array of PowerBuoy systems connected by our USP to an underwater cable to transmit the electricity to shore. Our system is designed to be scalable, as multiple PowerBuoy units can be integrated to create a wave power station with a larger output capacity. An array of PowerBuoy systems would likely be configured in three staggered rows parallel to the incoming wave front to form a long rectangle. This staggered arrangement would maximize the level of wave energy that the wave power station can capture.

We are also exploring the use of our utility PowerBuoy system for applications that include generating electricity for desalination of water, hydrogen production, water treatment and natural resource processing. In these instances, the power generated by the utility PowerBuoy system would bypass the grid and be delivered directly to the point of electricity consumption for these special applications.

Status of Utility PowerBuoy System

We expect that our first 150kW PowerBuoy will be ready for deployment during the second half of calendar year 2010. We have also initiated product development efforts in connection with our 500kW PowerBuoy.

We completed the successful in-ocean trials of our USP in October 2009. The USP, based on our proprietary design, has been developed to facilitate the collection, networking and transforming of power and data generated by multiple offshore energy devices. The USP has been built as an open platform, and can provide connectivity for the PowerBuoy as well as other offshore energy systems developed by other companies.

The following is a picture of the USP being lowered into the water for ocean trials:

Our PowerBuoy interface with the electrical utility power grid has been certified as compliant with international standards. An independent laboratory provided testing and evaluation services to certify that our systems comply with designated national and international standards. The PowerBuoy grid interface bears the ETL listing mark, and can be connected to the utility grid.

Autonomous PowerBuoy System

The autonomous PowerBuoy system is based on similar technology to the utility PowerBuoy system, but is designed for electricity generation of relatively low amounts of power for use independent of the power grid in

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remote locations. The autonomous PowerBuoy system currently has a maximum rated output ranging from 300 Watts to 40kW, depending on the application. Our autonomous PowerBuoy system is designed to operate anywhere in the ocean and in any depth of water.

We believe that the autonomous PowerBuoy system is suitable for use on a stand-alone basis for providing power for a variety of applications in deep ocean conditions, such as sonar and radar surveillance, tsunami warning, offshore data collection, offshore platforms and offshore aquaculture.

Status of Autonomous PowerBuoy System

We have received several contracts from the US Navy to provide our PowerBuoy technology to a unique program for ocean data gathering. Under this program, the Navy has conducted an ocean test of our autonomous PowerBuoy as the power source for the Navy s Deep Water Active Detection System and we are performing work under a new contract for the next phase of work under this program. This new contract is for ocean testing by the Navy of an advanced version of the autonomous PowerBuoy for the Navy s operational requirements.

We also received a contract from the US Navy to provide our PowerBuoy to the Navy s Littoral Expeditionary Autonomous PowerBuoy (LEAP) program. The LEAP program has been established to enhance the US Navy s anti-terrorism and force protection capability by providing persistent power at sea for port maritime surveillance in the near coast, harbors, piers and offshore areas.

Our Competitive Advantages

We believe that our technology for generating electricity from wave energy and our commercial relationships give us several potential competitive advantages in the renewable energy market.

Our PowerBuoy system uses an ocean-tested technology to generate electricity.

We have been conducting ocean tests for over a decade in order to demonstrate the viability of our technology. We initiated our first ocean installation in 1997 and have had several deployments of our systems for testing and operation since then, the longest of which has had continuous operation of 12 months. Our PowerBuoy systems have survived several hurricanes and winter storms while installed in the ocean. Since its installation in Hawaii in December 2009, our 40kW-rated PowerBuoy has produced power consistent with our predictive models.

Our PowerBuoy system s grid connection has been certified.

In July 2007, we announced that our PowerBuoy grid connection system had been certified as compliant with designated national and international standards. This qualifies our technology for integration into utility grid systems.

Our PowerBuoy system design is efficient in harnessing wave energy.

Our PowerBuoy system is designed to efficiently convert wave energy into electricity by using onboard sensors to detect actual wave conditions and then to automatically adjust, or tune , the performance of the generator using our proprietary electrical and electronics-based control systems in response to that information.

One measure of the efficiency of an electric power generation system is capacity factor. The capacity factor is the percent of kilowatt hours produced by a specific system in a given period as compared to the maximum

kilowatt hours that could be produced by the system in that period. A high capacity factor indicates a high degree of utilization of the capacity of the system and provides a means to compare the effectiveness of different energy sources. Since we have not yet operated a complete wave power station, we do not have a measured capacity factor. However, based on our research and analysis, we believe the design capacity factor for a PowerBuoy wave power station located at many of our targeted sites would be favorably positioned in the range of 30% to 45%.

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Numerous potential sites for our wave power stations are located near major population centers worldwide.

Our systems are designed to work in sites with average annual wave energy of at least 20kW per meter of wave front, which can be found in many coastal locations around the world. In particular, we are currently targeting the west coast of North America, the west coast of Europe, the coasts of Australia and the east coast of Japan. These potential sites not only have appropriate natural resources for harnessing wave energy, but they are also located near large population centers with significant and increasing electricity requirements and access to existing power transmission infrastructure.

We have significant commercial relationships.

Our current projects with PNGC Power, the US Department of Energy, the US Navy, the Scottish Government, and Iberdrola provide us with an initial opportunity to sell our wave power stations for utility applications. By collaborating with leaders in renewable energy development, we believe we are able to accelerate both our in-house knowledge of the utility power generation market and our reputation as a credible renewable energy equipment supplier. If these projects are successful, we intend to leverage our experiences with our projects to add wave power stations, new customers and complementary revenue streams from operations and maintenance contracts.

With the funding from the US Navy, we have been able to refine our PowerBuoy system while simultaneously preparing for commercial deployment to address a particular customer need. We believe that the successful deployment of our PowerBuoy system for the US Navy will significantly enhance market visibility.

Our PowerBuoy system has the potential to offer a cost competitive renewable energy power generation solution.

Our product development and engineering efforts are focused on increasing the maximum rated output and reliability of the design of our utility PowerBuoy system. Currently we are marketing PowerBuoys rated at 40kW and 150kW. Assuming we are able to reach manufacturing levels of at least 300 units of 500kW PowerBuoy systems per year, we believe, based upon our research and analysis, that the economies of scale we would have with our fabricators would allow us to offer a renewable electricity solution that competes with other existing renewable energy systems and, in certain cases, with existing fossil fuel systems in key markets.

Prior to achieving full production levels of the 500kW PowerBuoy system, if we achieve economies of scale for our 150kW PowerBuoy systems, we expect to be able to offer a renewable electricity solution that competes with the price of electricity in certain local markets where the current retail price of electricity is relatively high or where sufficient subsidies are available.

Our systems are environmentally benign and aesthetically non-intrusive.

We believe that our PowerBuoy system does not present significant risks to marine life and does not emit significant levels of pollutants. In connection with our project at the US Marine Corps Base in Hawaii, our customer, the US Navy, obtained an independent environmental assessment of our PowerBuoy system prior to installation, as required by the National Environmental Policy Act. This assessment resulted in a Finding of No Significant Impact, the highest such level of approval. Although our project for the US Navy only contemplates an array of up to six PowerBuoy systems in Hawaii, we believe that PowerBuoy systems deployed in other geographic locations, including larger PowerBuoy systems under development and multiple- buoy wave power stations, would have minimal environmental impact due to the physical similarities with the tested system.

Since our PowerBuoy systems are typically located one to five miles offshore, PowerBuoy wave power stations are usually not visible from the shore. Visual impact is often cited as one of the reasons that many communities have opposed plans to develop power stations, in particular wind power stations. Our PowerBuoy system has the distinct advantage of having only a minimal visual profile. Only a small portion of the unit is visible at close range, with the bulk of the unit hidden below the water.

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Customers/Projects

The table below shows the percentage of our revenue we derived from significant customers for the periods indicated:

Customer	Fiscal 2010	Fiscal 2009	Fiscal 2008
US Navy	80%	67%	58%
Iberdrola and Total	4%	18%	31%
Scottish Government	5%	8%	10%

We expect an increasing proportion of our future revenues to be contributed by commercial customers.

Our potential customer base for our utility PowerBuoy systems consists of public utilities, independent power producers and other governmental entities and agencies. Our potential customer base for our autonomous PowerBuoy systems consists of different public and private entities who use electricity in and near the ocean. Our efforts to identify new customers are concentrated on four geographic markets: the west coast of North America, the west coast of Europe, the coasts of Australia and the east coast of Japan. Our efforts to identify new customers are currently led and coordinated by our Executive Chairman and our Vice President of North America Business Development and Marketing. We also use consultants and other personnel to assist us in locating potential customers.

US Navy

Since September 2001, we have entered into a series of contracts with the United States Office of Naval Research for the development and construction of wave power systems at the Marine Corps base in Oahu, Hawaii. Under the contract for the current phase of the project, which was entered into in September 2005 and expires in September 2010, we are reimbursed for costs and paid a fixed fee, and over this period have been awarded contracts for total potential revenue of $5.9 million. The current PowerBuoy now in operation at the Marine Corps base was deployed in December 2009 and has produced power consistent with our predictive models.

Pictured below are views of our 40kW-rated PowerBuoy system being lowered into the ocean in Oahu, and after deployment.

In June 2007, we received a $1.7 million contract from the US Navy to provide our PowerBuoy technology to a unique program for data gathering in the ocean. Under this 18-month program, the US Navy conducted an ocean test in October 2008 of our autonomous PowerBuoy as the power source for the Navy s Deep Water Active Detection System. In October 2008, we received a $3.0 million contract from the US Navy to expand the program and ocean-test an advanced version of our autonomous PowerBuoy.

In September 2009, we received a $2.4 million contract from the US Navy to provide our PowerBuoy to the Navy s LEAP program. The LEAP program is being developed to enhance the US Navy s anti-terrorism and force

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protection capability by providing persistent power at sea for port maritime surveillance in the near coast, harbors, piers and offshore areas.

Reedsport, Oregon Project

In February 2007, the US Federal Energy Regulatory Commission (FERC) granted us a preliminary permit to evaluate the feasibility of a location off the coast of Reedsport, Oregon for the proposed construction and operation of a wave power station with a total potential maximum rated output of up to 50MW, of which up to the first 2MW would be a demonstration wave power station. In February 2007, we signed a cooperative agreement with PNGC Power, an Oregon-based electric power cooperative, as our utility partner for the development of a wave power station. In July 2007, we filed a Pre-Application Document and Notice of Intent with FERC for the Reedsport project, which provides notice of our intent to seek a license for the Reedsport power station and information regarding the project. We believe this was the first Pre-Application Document and Notice of Intent filed by a wave power company, and is an important step in the full licensing process for the Reedsport project. We will need additional authorization from FERC to sell electric power generated from the Reedsport wave power station into the wholesale or retail markets. In February 2010, we filed with FERC a full application to build, deploy and connect to the grid a 10-PowerBuoy array (1.5MW).

In August 2007, we announced the award of a $0.5 million contract from PNGC Power, providing funding toward the fabrication and installation of a 150kW PowerBuoy system for the Reedsport project. In October 2008, we received a $2.0 million award from the DOE in support of the project. The DOE grant will be used to help fund the fabrication and factory testing of the first PowerBuoy to be installed at the Reedsport site. This is the first award for the building of ocean wave energy systems by the DOE, and we believe it is indicative of the growing recognition and support of wave energy in the US federal and state governments.

This project remains on schedule, with the PB150 construction expected to be completed by the end of 2010, and ocean testing is expected to commence in 2011.

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The following photographs show manufacturing activity associated with our PB150 PowerBuoy being built in Oregon:

We continue to make progress on the overall permitting and licensing process while working extensively with interested stakeholder groups at local, county, state and federal agency levels.

Next Generation PowerBuoy

In April 2010, we won a $1.5 million award from the DOE for the development of our next generation PowerBuoy wave power system. The DOE grant will be used to help fund the scale-up of the power output per PowerBuoy from the current level of 150kW to 500kW. In addition, the technology development effort will focus on increasing the power extraction efficiency and reliability.

Scotland Project

In 2007, we received a $1.8 million contract from the Scottish Executive for the construction of a 150kW grid-connected PowerBuoy system at the European Marine Energy Centre (EMEC) in Orkney, Scotland. EMEC is a test facility for marine energy technologies, for which the Scottish Government has built the infrastructure for grid connection. In 2008, we signed a Berth Agreement with EMEC. This agreement provides for the deployment and operation of PowerBuoys as well as their connection to the wave energy berth s dedicated 2MW subsea cable already installed and connected to the Scottish grid. The Berth Agreement also enables us to sell power to the grid up to the 2MW capacity limit. The construction phase of the buoy has been completed and we expect the buoy to be ready for deployment during the second half of calendar year 2010. This deployment will be for the conduct of in-ocean trials of the PB150 PowerBuoy at a location in Scotland following which a decision will be made regarding deployment at EMEC.

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The following pictures show manufacturing activity in Scotland associated with our PB150 PowerBuoy:

Spain

In July 2004, we entered into a development agreement, which we refer to as the Spain development agreement, with Iberdrola Energias Renovables II, S.A. (Iberdrola Energias), an affiliate of Iberdrola, Sociedad para el Desarrollo Regional de Cantabria, S.A., or SODERCAN, which is the industrial development agency of the Spanish region of Cantabria, and Instituto para la Diversificacion y Ahorro de la Energia, S.A., or IDAE, a Spanish government agency dedicated to energy conservation and diversification efforts, to jointly study the possibility of developing a wave power station off the coast of Santoña located in the Cantabria region in northern Spain. Total Eolica S.A., an affiliate of Total, joined the development agreement in June 2005. In January 2006, we completed

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the assessment phase of the project, which included an assessment of wave energy resources at the site, a feasibility analysis for deployment at the site, a determination of capacity and design, and an estimation of investments needed for the project as well as anticipated costs for operation, maintenance and repairs. Expenses associated with this phase were shared among the parties to the agreement based on agreed upon percentages.

In July 2006, Iberdrola Energias Marinas de Cantabria, S.A., or Iberdrola Cantabria, was formed for the purpose of constructing and operating a wave power station off the coast of Santoña, Spain. Iberdrola Energias is the largest shareholder of Iberdrola Cantabria. Total Eolica, SODERCAN, IDAE and we each have minority ownership positions. Funding is shared among the parties to the agreement based on agreed upon percentages that reflect the parties anticipated ownership interest in the wave power station. We own 10% of Iberdrola Cantabria.

In July 2006, we entered into an agreement for the first phase of the construction of a wave power station off the coast of Santoña, Spain, with our customer, Iberdrola Cantabria. We refer to this agreement as the Spain construction agreement. Iberdrola Cantabria was formed by affiliates of Iberdrola and Total, two Spanish governmental agencies and us for the purpose of constructing and operating a wave power station off the coast of Spain. Under the Spain construction agreement, we agreed to manufacture and deploy one 40kW PowerBuoy system and the ocean-based substation and infrastructure required to connect nine additional 150kW PowerBuoy systems that together are contemplated to constitute a 1.39MW wave power station by no later than December 31, 2009. We are currently in discussions with Iberdrola Cantabria regarding the timing and completion of this project. In February 2008, the Spain construction agreement was amended to provide for the current phase of the construction of the PowerBuoy system plus the fabrication of the underwater power transmission cable and underwater substation pod for all ten PowerBuoy systems. The terms of the installation of the underwater transmission cable and underwater substation pod will be separately negotiated and, if so agreed, could provide for additional funding for the installation work. Because the amended Spain construction agreement does not cover the terms for deployment of the underwater transmission cable and substation pod and the manufacture and deployment of the nine additional PowerBuoy units, we would need to enter into a subsequent contract with Iberdrola Cantabria before we complete these elements of construction of the full wave power station.

The initial PB40 PowerBuoy system for this project was deployed in September 2008. After a short testing period, the buoy was removed from the water for work on improvements to the power take-off and control systems. We are currently in discussions with Iberdrola Cantabria regarding the nature and costs of these improvements and their effects on plans for the redeployment of the buoy and the next phases of the project. If no modification is agreed to by the parties, the customer may, subject to certain conditions in the agreement, terminate the agreement and would not be obligated to make any more milestone payments. In addition, if we and Iberdrola Cantabria decide not to redeploy the PB40 PowerBuoy, the total contract value for the current phase of the contract may be reduced. If we are unable to successfully meet the terms of the Spain construction agreement, or if we are not able to successfully negotiate a subsequent contract or contracts with Iberdrola Cantabria for the manufacture and deployment of the nine additional PowerBuoy units, or if Iberdrola Cantabria were to terminate the Spain construction agreement for any of these reasons, we may lose a component of our current and anticipated revenue stream. If we are unable to agree to the necessary contract modifications, Iberdrola Cantabria will have the right to terminate the agreement if the first phase of construction is not completed on time for reasons attributable to us, or if we interrupt our services for more than 180 days and do not resume within a 30-day period, or for a serious and repeated breach of a major obligation that is not cured within a 30-day period after we receive notice of the breach. In addition, we have made guarantees to Iberdrola Cantabria associated with the current phase of construction in respect of the quality, repair and replacement of the 40kW PowerBuoy system and ocean-based substation and the level of power output of the 40kW PowerBuoy system. If we are found to be in default of our obligations under the Spain construction agreement, Iberdrola Cantabria will have the right to seek reimbursement for direct damages only, limited to amounts specified in the contract.

We are paid under the Spain construction agreement as we complete certain milestones for a total potential payment for the current phase of construction of approximately 2.7 million. From inception to April 30, 2010, we had recognized revenue of approximately $3.0 million and a recognized loss of $3.9 million under the Spain construction agreement. The anticipated loss at completion of the contract also reflects our decision made in the fourth quarter of fiscal year 2008 to absorb $1.9 million of additional costs of the project beyond our obligation for the initial cost overruns and certain other costs as set forth in the agreement. This decision was based on the progress

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of the project up to that point, the benefits to be derived from a successful initial project and the prospect of incremental contract value to be received in connection with additional work under this contract.

In March 2010, we announced the award of 2.2 million under the European Commission s Seventh Framework Programme (FP7) by the European Commission s Directorate responsible for new and renewable sources of energy, energy efficiency and innovation. This grant is part of a total award of 4.5 million to a consortium of companies, including us, to deliver a PowerBuoy wave energy device under a project entitled WavePort, with an innovative wave prediction capability and a wave-by-wave tuning system. It is anticipated that the PowerBuoy will be deployed at the Santoña site in Spain. Our work under the award is conditional on our obtaining significant additional funding to enable completion of the WavePort project.

Pictured below are views of our 40kW-rated PowerBuoy system during tow-out to the deployment site off Santoña, Spain, and after deployment.

Other Projects

In February 2006, we received approval from the South West of England Regional Development Agency (SWRDA) to install a 5MW demonstration wave power station off the coast of Cornwall, England as part of SWRDA s Wave Hub project, a planned offshore facility for demonstrating and testing wave energy generation devices. SWRDA has obtained the necessary permits for this Wave Hub project, and the project has been approved for over £40 million of funding for construction of the Wave Hub infrastructure by SWRDA. Construction contracts have been awarded and SWRDA expects installation during 2010. We are in the planning and development stage for our part of the project, and we are seeking funding for the 5MW power station.

In October 2008, we signed an exclusive agreement with a consortium of three Japanese companies to develop a demonstration wave power station in Japan. The Japanese consortium comprises Idemitsu Kosan Co., Mitsui Engineering & Shipbuilding Co. (MES), and Japan Wind Development Co. We are presently working with MES to identify prospective sites for the wave power station.

In December 2008, we announced a Joint Development Agreement with Leighton Contractors Pty. Ltd. (Leighton) for the development of wave power projects off the east and south coasts of Australia. Over the past 50 years, Leighton has played an active role in building Australia s ports and marin