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

FORM 10-Q

(Mark One)

☒ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended March 31, 2003

OR

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from _____ to _____ .

Commission file number: 001-15957

CAPSTONE TURBINE CORPORATION

(Exact name of Registrant as specified in its charter)

Delaware	**95-4180883**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

21211 Nordhoff Street, Chatsworth, California 91311
(Address of principal executive offices) (Zip code)

818-734-5300
(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 is an accelerated filer (as defined in Rule 12b-2 of the Securities Exchange Act of 1934). Yes ☒ No ☐

The number of outstanding shares of the registrant's common stock as of April 30, 2003 was 81,267,570.

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PART I — FINANCIAL INFORMATION

Item 1. ***Consolidated Financial Statements***

CAPSTONE TURBINE CORPORATION
CONSOLIDATED BALANCE SHEETS
(Unaudited)

	March 31, 2003	December 31, 2002
Assets		
Current Assets:		
Cash and cash equivalents	$ 132,584,000	$ 140,310,000
Accounts receivable, net of allowance for doubtful accounts and sales returns of $414,000 at March 31, 2003 and $194,000 at December 31, 2002	3,748,000	4,893,000
Inventory	12,121,000	9,124,000
Prepaid expenses and other current assets	1,341,000	2,331,000
Total current assets	149,794,000	156,658,000
Equipment and Leasehold Improvements:		
Machinery, equipment, and furniture	23,914,000	22,996,000
Leasehold improvements	8,480,000	8,480,000
Molds and tooling	4,365,000	4,350,000
	36,759,000	35,826,000
Less accumulated depreciation and amortization	16,857,000	15,346,000
Total equipment and leasehold improvements	19,902,000	20,480,000
Non-current Portion of Inventory	4,412,000	6,784,000
Deposits on Fixed Assets	73,000	708,000
Other Assets	505,000	532,000
Intangible Asset, Net	1,961,000	2,029,000
Total	$ 176,647,000	$ 187,191,000
Liabilities and Stockholders' Equity		
Current Liabilities:		
Accounts payable	$ 2,156,000	$ 4,321,000
Accrued salaries and wages	1,472,000	2,088,000
Other accrued liabilities	1,117,000	1,132,000
Accrued warranty reserve	6,657,000	6,913,000
Deferred revenue	1,253,000	734,000
Current portion of capital lease obligations	1,411,000	1,522,000
Total current liabilities	14,066,000	16,710,000
Long-Term Portion of Capital Lease Obligations	736,000	974,000
Other Long-Term Liabilities	1,277,000	1,325,000
Commitments and Contingencies	—	—
Stockholders' Equity:		
Common stock, $.001 par value; 415,000,000 shares authorized; 81,700,735 shares issued and 81,248,782 shares outstanding at March 31, 2003; 81,635,035 shares issued and 81,437,822 shares outstanding at December 31, 2002	82,000	82,000
Additional paid-in capital	527,188,000	526,952,000
Accumulated deficit	(366,281,000)	(358,646,000)
Less Treasury stock, at cost; 451,953 shares at March 31, 2003; 197,213 shares at December 31, 2002	(421,000)	(206,000)
Total stockholders' equity	160,568,000	168,182,000
Total	$ 176,647,000	$ 187,191,000

See accompanying notes to consolidated financial statements.

CAPSTONE TURBINE CORPORATION
CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended March 31,	
	2003	**2002**
Revenues	$ 2,782,000	$ 4,591,000
Cost of Goods Sold	4,956,000	7,549,000
Gross Loss	(2,174,000)	(2,958,000)
Operating Costs and Expenses:		
Research and development	1,006,000	1,439,000
Selling, general and administrative	4,821,000	8,360,000
Total operating costs and expenses	5,827,000	9,799,000
Loss from Operations	(8,001,000)	(12,757,000)
Interest Income	439,000	823,000
Interest Expense	(73,000)	(115,000)
Other Income	2,000	21,000
Loss Before Income Taxes	(7,633,000)	(12,028,000)
Provision for Income Taxes	2,000	2,000
Net Loss	$ (7,635,000)	$(12,030,000)
Weighted Average Common Shares Outstanding	81,410,614	77,387,574
Net Loss Per Share of Common Stock — Basic and Diluted	$ (0.09)	$ (0.16)

See accompanying notes to consolidated financial statements.

CAPSTONE TURBINE CORPORATION
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(Unaudited)

	Common Stock		Additional Paid In Capital	Accumulated Deficit	Treasury Stock	Total
	Shares Issued	Amount				
Three Months Ended March 31, 2002:						
Balance, January 1, 2002	77,207,383	$77,000	$521,668,000	$(284,291,000)	$ —	$237,454,000
Stock-based compensation	—	—	265,000	—	—	265,000
Exercise of stock options	200,173	—	80,000	—	—	80,000
Net loss	—	—	—	(12,030,000)	—	(12,030,000)
Balance, March 31, 2002	77,407,556	$77,000	$522,013,000	$(296,321,000)	$ —	$225,769,000
Three Months Ended March 31, 2003:						
Balance, January 1, 2003	81,635,035	$82,000	$526,952,000	$(358,646,000)	$(206,000)	$168,182,000
Stock-based compensation	—	—	214,000	—	—	214,000
Exercise of stock options	65,700	—	22,000	—	—	22,000
Purchase of treasury stock	—	—	—	—	(215,000)	(215,000)
Net loss	—	—	—	(7,635,000)	—	(7,635,000)
Balance, March 31, 2003	81,700,735	$82,000	$527,188,000	$(366,281,000)	$(421,000)	$160,568,000

See accompanying notes to consolidated financial statements.

CAPSTONE TURBINE CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Three Months Ended March 31,	
	2003	**2002**
Cash Flows from Operating Activities:		
Net loss	$ (7,635,000)	$ (12,030,000)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	1,573,000	3,083,000
Non-cash reversal of administrative expenses	(1,099,000)	—
Provision for doubtful accounts	220,000	125,000
Inventory write-down	243,000	472,000
Provision for warranty expenses	385,000	847,000
Loss on disposal of fixed assets	—	37,000
Non-employee stock-based compensation	4,000	—
Employee and director stock-based compensation	210,000	265,000
Changes in operating assets and liabilities:		
Accounts receivable	925,000	2,740,000
Inventory	(868,000)	941,000
Prepaid expenses and other assets	990,000	(275,000)
Accounts payable	(1,066,000)	(713,000)
Accrued salaries and wages	(625,000)	(152,000)
Other accrued liabilities	(54,000)	(823,000)
Accrued warranty reserve	(641,000)	(308,000)
Deferred revenue	519,000	(84,000)
Net cash used in operating activities	(6,919,000)	(5,875,000)
Cash Flows from Investing Activities:		
Acquisition of and deposits on fixed assets	(271,000)	(394,000)
Net cash used in investing activities	(271,000)	(394,000)
Cash Flows from Financing Activities:		
Purchase of treasury stock	(215,000)	—
Repayment of capital lease obligations	(343,000)	(315,000)
Exercise of stock options	22,000	80,000
Net cash used in financing activities	(536,000)	(235,000)
Net Decrease in Cash and Cash Equivalents	(7,726,000)	(6,504,000)
Cash and Cash Equivalents, Beginning of Period	140,310,000	170,868,000
Cash and Cash Equivalents, End of Period	$132,584,000	$164,364,000
Supplemental Disclosures of Cash Flow Information:		
Cash paid during the period for:		
Interest	$ 73,000	$ 115,000
Income taxes	$ 2,000	$ 2,000

See accompanying notes to consolidated financial statements.

CAPSTONE TURBINE CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. Business and Organization

Capstone Turbine Corporation (the "Company") develops, manufactures and sells microturbine generator sets for use in combined heat and power generation, resource recovery, hybrid electric vehicles and other power, heat and cooling applications in the markets for distributed power generation around the world. The Company was organized in 1988 and has been commercially producing its microturbine generators since 1998.

The Company has incurred significant operating losses since its inception. Management anticipates incurring additional losses until the Company can produce sufficient revenues to cover costs. To date, the Company has funded its activities primarily through private and public equity offerings.

2. Basis of Presentation

The accompanying unaudited financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("generally accepted accounting principles") for interim financial information and with the instructions to Form 10-Q and Regulation S-X promulgated under the Securities and Exchange Act of 1934. They do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. The balance sheet at December 31, 2002 was derived from audited financial statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2002. In the opinion of management the interim financial statements include all adjustments (consisting of normal recurring adjustments) necessary for a fair presentation of the financial condition, results of operations, stockholders' equity and cash flows for such periods. Results of operations for any interim period are not necessarily indicative of results for any other interim period or for the full year. These financial statements should be read in conjunction with the financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2002.

3. New Accounting Pronouncements

In January 2003, the Emerging Issues Task Force ("EITF") released EITF 00-21: "Accounting for Revenue Arrangements with Multiple Deliverables." EITF 00-21 clarifies the timing and recognition of revenue from certain transactions that include the delivery and performance of multiple products or services. EITF 00-21 is effective for revenue arrangements entered into in fiscal periods beginning after June 15, 2003. Alternatively, entities may elect to report the change in accounting as a cumulative-effect adjustment in accordance with APB Opinion 20, "Accounting Changes." If so elected, disclosure should be made in periods subsequent to the date of initial application of this consensus of the amount of the recognized revenue that was previously included in the cumulative-effect adjustments. The Company is currently reviewing the impact of EITF 00-21.

In December 2002, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 148, "Accounting for Stock-Based Compensation – Transition and Disclosure – an Amendment of SFAS No. 123." SFAS No. 148 amends SFAS No. 123, "Accounting for Stock-Based Compensation," to provide alternative methods of transition for a voluntary change to the fair value method of accounting for stock-based employee compensation. In addition, SFAS No. 148 amends the disclosure in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the methods used on reported results. The disclosure requirements apply to all companies for fiscal years ended after December 15, 2002. The Company accounts for its employee stock option plans under the intrinsic value method prescribed by Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" and related interpretations. The Company accounts for equity instruments issued to recipients other than employees using the fair value at the date of grant. The following table is presented in accordance with SFAS No. 148 and illustrates the effect on net loss and net loss per share if the Company had applied the fair value recognition provisions of SFAS No. 123.

	Three Months Ended March 31,	
	2003	2002
Net loss, as reported	$(7,635,000)	$(12,030,000)
Add: Stock-based employee and director compensation included in reported net loss	210,000	265,000
Deduct: Total stock-based employee and director compensation expense determined under fair value based method for all awards	(1,897,000)	(2,241,000)

CAPSTONE TURBINE CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS-(Continued)
(Unaudited)

	Three Months Ended March 31,	
	2003	2002
Pro forma net loss	$(9,322,000)	$(14,006,000)
Net loss per share – Basic and Diluted:		
As reported	$ (0.09)	$ (0.16)
Pro forma	$ (0.11)	$ (0.18)

In November 2002, FASB Interpretation ("FIN") No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others" was issued. FIN No. 45 elaborates on the disclosures to be made by a guarantor in its interim and annual financial statements about its obligations under certain guarantees that it has issued. FIN No. 45 also clarifies that a guarantor is required to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee. The initial recognition and initial measurement provisions of this Interpretation are applicable on a prospective basis to guarantees issued or modified after December 31, 2002. The Company did not issue any guarantees of indebtedness of others during the quarter ended March 31, 2003. Product warranties are excluded from the initial recognition and measurement provisions of FIN No. 45 but are subject to its disclosure requirements. The required disclosures and a roll-forward of product warranty liabilities are effective for financial statements of interim or annual periods ending after December 15, 2002. The Company disclosed its accounting policy on product warranty in its Annual Report on Form 10-K for the year ended December 31, 2002. The required tabular reconciliation of the changes in the aggregate product warranty liability for the quarter ended March 31, 2003 is disclosed in Note 8.

In July 2002, SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities," was issued by the FASB. SFAS No. 146 requires companies to recognize costs associated with exit or disposal activities when they are incurred rather than at the date of a commitment to an exit or disposal plan. Examples of costs covered by the standard include lease termination costs and certain employee severance costs that are associated with a restructuring, discontinued operation, plant closing, or other exit or disposal activity. SFAS No. 146 is to be applied prospectively to exit or disposal activities initiated after December 31, 2002. The adoption of SFAS No. 146 did not have a material impact on the Company's consolidated financial position or results of operations as it has not initiated any exit activities or disposal activities.

4. Segment Reporting

The Company is considered to be a single operating segment in conformity with SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information." The business activities of said operating segment are the development, manufacture and sale of turbine generator sets. Following is a breakdown by geographical area of the Company's revenues:

	Three Months Ended March 31,	
	2003	2002
North America:		
USA	$ 1,411,000	$ 948,000
Mexico	891,000	—
Others	36,000	191,000
Asia:		
Japan	78,000	1,800,000
Others	69,000	94,000
Europe	213,000	2,095,000
South America	4,000	32,000
Africa	80,000	(569,000)
Total	$ 2,782,000	$ 4,591,000

CAPSTONE TURBINE CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS-(Continued)
(Unaudited)

Revenues and margins for the three months ended March 31, 2002 were reported net of $569,000 and $79,000, respectively, that resulted from the repossession of 20 units of our C30 products from a distributor in Africa.

5. Inventory

Inventory is stated at the lower of standard cost (which approximates actual cost on the first-in, first-out method) or market and consists of the following:

	March 31, 2003	December 31, 2002
Raw materials	$12,724,000	$12,623,000
Work in process	2,271,000	1,831,000
Finished goods	1,538,000	1,454,000
Total	16,533,000	15,908,000
Less non-current portion	4,412,000	6,784,000
Current portion	$12,121,000	$ 9,124,000

The non-current portion of inventory represents that portion of the inventory in excess of amounts expected to be sold or used in the next twelve months.

6. Intangible Asset

The intangible asset represents the license granted to the Company to use a former supplier's intellectual property for the design and manufacture of licensed product for use in microturbines. Additional information is as follows:

	March 31, 2003	December 31, 2002
Gross carrying amount	$3,663,000	$3,663,000
Less accumulated amortization and impairment loss	1,702,000	1,634,000
Net	$1,961,000	$2,029,000

The intangible asset, which was acquired in 2000, is being amortized over its estimated useful life of ten years. The Company recorded $68,000 and $94,000 of amortization expense related to the manufacturing license for the quarters ended March 31, 2003 and 2002, respectively. The manufacturing license is scheduled to be fully amortized by 2010 with corresponding amortization estimated to be $199,000, $267,000, $267,000, $267,000, $267,000 and $694,000, for the remainder of 2003, calendar years 2004, 2005, 2006 and 2007, and thereafter, respectively.

7. Stock-Based Compensation

During 1999 and 2000, the Company issued common stock options at less than the fair value of its common stock. Accordingly, the Company recorded stock-based compensation expense based on the vesting of these grants as follows:

	Three Months Ended March 31,	
	2003	2002
Cost of goods sold	$ 9,000	$ 11,000
Research and development	59,000	69,000
Selling, general and administrative	142,000	185,000
Total employee and director stock-based compensation	$ 210,000	$ 265,000

As of March 31, 2003, the Company had $705,000 in deferred employee and director stock-based compensation, which will be amortized

through 2004 based on the vesting period.

On March 20, 2003, the Board of Directors approved an amendment to the 2000 Equity Incentive Plan (the "2000 Plan") to increase the number of shares of common stock available for grant by 2,500,000 shares. The grants under this increase shall be non-statutory stock options. As a result of this amendment, the 2000 Plan now provides for awards of up to 6,200,000 shares, plus the number of

CAPSTONE TURBINE CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS-(Continued)
(Unaudited)

shares previously authorized and remaining available under the 1993 Incentive Stock Plan (the "1993 Plan"), plus any shares covered by options granted under the 1993 Plan that are forfeited or expire unexercised.

8. Accrued Warranty Reserve

The following table represents the changes in the product warranty liability for the quarter ended March 31, 2003:

Balance at beginning of period	$6,913,000
Reductions for payments made in cash or in kind	(641,000)
Changes for accruals related to warranties issued during the period	148,000
Changes for accruals related to preexisting warranties	237,000
Balance at end of period	$6,657,000

9. Commitments and Contingencies

As of March 31, 2003, the Company had firm commitments to purchase inventories of approximately $4,300,000 and $2,400,000 for non-inventory items.

In December 2001, a purported shareholder class action lawsuit was filed in the United States District Court for the Southern District of New York against the Company, two of its officers, and the underwriters of our initial public offering. The suit purports to be a class action filed on behalf of purchasers of our common stock during the period from June 28, 2000 to December 6, 2000. An amended complaint was filed on April 19, 2002. No date has been set for the Company to respond to the complaint. Plaintiffs allege that the underwriter defendants agreed to allocate stock in the Company's June 28, 2000 initial public offering and November 16, 2000 secondary offering to certain investors in exchange for excessive and undisclosed commissions and agreements by those investors to make additional purchases of stock in the aftermarket at pre-determined prices. Plaintiffs allege that the prospectuses for these two public offerings were false and misleading in violation of the securities laws because they did not disclose these arrangements. The Company understands that over three hundred other issuers have been named as defendants in nearly identical lawsuits filed by some of the same plaintiffs' law firms. We intend to defend these actions vigorously. However, due to the inherent uncertainties of litigation, we cannot accurately predict the ultimate outcome of the litigation. Any unfavorable outcome of litigation could have a material adverse effect on the Company's financial position and results of operations.

10. Related Party Transactions

Mr. Eliot Protsch became a member of the Company's Board of Directors in April 2002 and became Chairman of the Company's Board of Directors in October 2002. Mr. Protsch is President of Alliant Energy-Interstate Power and Light and Executive Vice-President, Energy Delivery at Alliant Energy Corporation. Alliant Energy Resources, Inc., a subsidiary of Alliant Energy Corporation, is a distributor for the Company. Sales to Alliant Energy Resources, Inc. in the quarter ended March 31, 2003 were approximately $11,000. There were no sales to Alliant Energy Resources, Inc. in the quarter ended March 31, 2002.

11. Selling, General and Administrative Expenses

As a result of a settlement agreement with a professional services firm, liabilities for $1,099,000 of administrative expenses recorded in prior years were reversed in the first quarter of 2003.

12. Net Loss Per Common Share

Basic loss per common share is computed using the weighted-average number of common shares outstanding for the period. The impact of common stock options has not been included in the computation of diluted loss per share as their inclusion would have had an anti-dilutive effect on the per-share amounts for the periods presented; therefore, diluted loss per share is equal to basic loss per share.

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

The following discussion should be read in conjunction with the Financial Statements and Notes included in this Form 10-Q and within Capstone's Annual Report on Form 10-K for the year ended December 31, 2002. When used in the following discussion, the words "believes", "anticipates", "intends", "expects", "plans" and similar expressions are intended to identify forward-looking statements. Such statements are subject to certain risks and uncertainties, which could cause actual results to differ materially from those projected. These risks include those identified under "Other Information – Business Risks" in Item 5 of this Form 10-Q. Readers are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date hereof. We undertake no obligation to revise or update publicly any of the forward-looking statements after the filing of this Form 10-Q to conform such statements to actual results or to changes in our expectations.

Critical Accounting Policies

There were no material changes in the quarter ended March 31, 2003 relating to our critical accounting policies as previously discussed in Item 7 – "Management's Discussion and Analysis of Financial Condition and Results of Operations" included in our Annual Report on Form 10-K for the year ended December 31, 2002.

Results of Operations

Quarters Ended March 31, 2003 and 2002

Revenues. Revenues for the quarter ended March 31, 2003 decreased $1.8 million to $2.8 million from $4.6 million for the same period last year. Revenues from product shipments for the quarter decreased $2.4 million to $1.4 million from $3.8 million for the same period a year ago. During the quarter ended March 31, 2003, we shipped 1.3 megawatts, or 38 units, consisting of 32 units of our C30 products and 6 units of our C60 products. During the quarter ended March 31, 2002, we shipped 4.7 megawatts, or 127 units, consisting of 99 units of our C30 products and 28 units of our C60 products. Revenues from accessories, parts and service for the quarter ended March 31, 2003 increased $0.6 million to $1.4 million from $0.8 million for the same period last year.

During the quarter ended March 31, 2003, 50% of our revenues were to two customers in North America as compared to 75% to two customers, a European utility and Sumitomo Corporation in Japan, for the same period last year.

While our sales of products were low in the first quarter of 2003, we have entered the second quarter with 7 megawatts of orders scheduled for shipment mostly during the second and third quarters of 2003. These orders are not firm. The timing of shipments of these orders may also be changed. We expect our sales for the full year of 2003 will be about the same or lower than the sales of $19.5 million in 2002.

We currently believe that there close to 600 units in our distributors' inventories that are available for sale. These inventories, which are owned by our distributors, may adversely impact our sales opportunities in the future.

Gross Loss. Cost of goods sold includes direct material costs, production overhead, inventory charges and provision for estimated product warranty expenses. We had a gross loss of $2.2 million for the quarter ended March 31, 2003, compared to $3.0 million for the same period last year. The reduction in gross loss was primarily from increased sales of accessories, parts and service, and higher average selling prices of microturbines due to product configuration mix.

Our cost of goods sold has exceeded revenues each period. We expect this trend to continue until such time that we can sell a sufficient number of units to achieve a break-even margin. Despite our product and market advantages, the rate of adoption for our technology has been slower than initially anticipated. The present economic environment, with tight restrictions for capital expenditures, also makes it significantly more challenging. In our efforts to get to a higher rate of adoption and become profitable, we are working on three focus areas: specific vertical markets, lowering maintenance costs and new product development.

R&D Expenses. Research and development ("R&D") expenses include compensation, the engineering department overhead allocations for administration and facilities and material costs associated with development. R&D expenses were $1.0 million for the quarter ended March 31, 2003, compared to $1.4 million for the same period a year ago. R&D expenses are reported net of benefits from cost sharing programs. These benefits were $1.7 million for the quarter ended March 31, 2003 and $1.3 million for the same period last year. Our gross R&D spending was comparable between periods.

Selling, General, and Administrative Expenses. Selling, general, and administrative ("SG&A") expenses include compensation and related expenses in support of our general corporate functions, which include human resources, finance and accounting, shareholder relations, quality, information systems and legal services. SG&A expenses for the quarter ended March 31, 2003 decreased $3.6 million to $4.8 million, compared to $8.4 million for the same period last year. The decrease was due to several factors including:

- There was no amortization expense from marketing rights in the quarter ended March 31, 2003, compared to $1.3 million in the same period last year. The marketing rights were fully impaired during the second quarter of 2002.

- As a result of a settlement agreement with a professional services firm, liabilities for $1.1 million of administrative expenses recorded in prior years were reversed in the first quarter of 2003. We do not expect similar reversals of expenses in future periods.

- Spending was lower in 2003 as a result of our actions to reduce our cost structure, resize the business and lower our cash usage.

Interest Income. Interest income decreased $0.4 million to $0.4 million for the quarter ended March 31, 2003, compared to $0.8 million for the same period a year ago. The decrease was primarily attributable to the lower cash balances and lower interest rates. We expect decreasing cash balances from our use of funds will continue to diminish our interest income.

Liquidity and Capital Resources

Our cash requirements depend on many factors, including our product development activities and our commercialization efforts. While we are working to reduce our cash usage, we expect to continue to devote substantial capital resources to running our business, including continuing the development of our sales and marketing programs and continuing our R&D activities. We believe that our current cash balance of $132.6 million is sufficient to fund operating losses and our currently projected commitments to reach the point of cash flow positive. We have invested our cash in an institutional fund that invests in high quality short-term money market instruments to provide liquidity for operations and for capital preservation.

We used cash of $7.7 million during the quarter ended March 31, 2003, compared to $6.5 million for the same period last year.

Our net cash used in operations, excluding working capital, was $6.1 million for the quarter ended March 31, 2003, compared to $7.2 million for the same period last year. This decrease of $1.1 million was primarily from a lower net loss. We used cash for working capital of $0.8 million for the quarter ended March 31, 2003, compared to generating a source of cash from working capital of $1.3 million for the same period last year. This increase of $2.1 million was largely due to this year's first quarter having lower collections of accounts receivable as a result of lower sales, and higher inventory purchases.

Accounts receivable decreased $1.2 million to $3.7 million as of March 31, 2003 from $4.9 million as of December 31, 2002. The decrease was due to lower sales in the first quarter of 2003 compared to sales in the fourth quarter of 2002.

Total inventory increased $0.6 million to $16.5 million as of March 31, 2003 from $15.9 million as of December 31, 2002. At March 31, 2003, non-current inventory of $4.4 million represents that portion of the inventory in excess of amounts expected to be sold or used in the next twelve months. The increase in total inventory was due to inventory purchases under firm contracts with our suppliers. As of March 31, 2003, the Company had firm commitments to purchase inventories of approximately $4.3 million and $2.4 million for non-inventory items.

Net cash used in investing activities for acquisition of fixed assets was $0.3 million for the quarter ended March 31, 2003, compared to $0.4 million for the same period last year.

Our net cash used in financing activities of $0.5 million for the quarter, compared to $0.2 million for the same period a year ago primarily due to purchase of treasury stock of $0.2 million this year. In October 2002, the Company's Board of Directors approved a stock repurchase program under which the Company may purchase up to $10 million of the Company's common stock. The Company could purchase shares from time to time through open market and privately negotiated transactions at prices deemed appropriate by management. The program has no termination date. Since the inception of the program, we have repurchased 451,953 shares for an aggregate price of $0.4 million

There have been no material changes in the Company's remaining commitments under non-cancelable operating leases and capital leases as disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2002.

Impact of Recently Issued Accounting Standards

In January 2003, the Emerging Issues Task Force (EITF) released EITF 00-21: "Accounting for Revenue Arrangements with Multiple Deliverables." EITF 00-21 clarifies the timing and recognition of revenue from certain transactions that include the delivery and performance of multiple products or services. EITF 00-21 is effective for revenue arrangements entered into in fiscal periods beginning after June 15, 2003. Alternatively, entities may elect to report the change in accounting as a cumulative-effect adjustment in accordance with APB Opinion 20, "Accounting Changes". If so elected, disclosure should be made in periods subsequent to the date of initial application of this consensus of the amount of the recognized revenue that was previously included in the cumulative-effect adjustments. We are currently reviewing the impact of this EITF.

Item 3. Qualitative and Quantitative Disclosures About Market Risk

No material changes have occurred in the quantitative and qualitative market risk disclosure of the Company as presented in its Annual Report on Form 10-K for the year ended December 31, 2002.

Item 4. ***Controls and Procedures***

(a) Evaluation of disclosure controls and procedures.

Our Chief Executive Officer and our Chief Financial Officer evaluated our "disclosure controls and procedures" (as defined in Rule 13a-14(c) of the Securities Exchange Act of 1934 (the "Exchange Act")) as of a date within 90 days before the filing date of this quarterly report. They concluded that as of the evaluation date, our disclosure controls and procedures are effective to ensure that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission ("SEC") rules and forms.

(b) Changes in internal controls

Subsequent to the date of their evaluation, there were no significant changes in our internal controls or in other factors that could significantly affect these controls. There were no significant deficiencies or material weaknesses in our internal controls so no corrective actions were taken.

PART II — OTHER INFORMATION

Item 1. ***Legal Proceedings***

There have been no material developments since the quarter ended December 31, 2002.

Item 5. ***Other Information-Business Risks***

This document contains certain forward-looking statements (as such term is defined in Section 27A of the Securities Act of 1933, as amended (the "Securities Act") and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act")) pertaining to, among other things, Capstone's future results of operations, R&D activities, sales expectations, our ability to develop markets for our products, sources for parts, federal, state and local regulations, and general business, industry and economic conditions applicable to Capstone. These statements are based largely on Capstone's current expectations, estimates and forecasts and are subject to a number of risks and uncertainties. Actual results could differ materially from these forward-looking statements. Factors that can cause actual results to differ materially include, but are not limited to, those discussed below. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. The following factors should be considered in addition to the other information contained herein in evaluating Capstone and its business. We undertake no obligation to revise or update publicly any of the forward-looking statements after the filing of this Form 10-Q to conform such statements to actual results or to changes in our expectations except as required by law.

Investors should carefully consider the risks described below before making an investment decision. In addition, these risks are not the only ones facing our Company. Additional risks we are not presently aware of or that we currently believe are immaterial may also impair our business operations. Our business could be harmed by any of these risks. The trading price of our common stock has and could continue to decline due to any of these risks, and investors may lose all or part of their investment. In assessing these risks, investors should also refer to the other information contained or incorporated by reference in this Quarterly Report on Form 10-Q, or in our Annual Report on Form 10-K and other documents filed by us from time to time.

We have a limited operating history characterized by net losses, we anticipate continued losses and we may never become profitable.

Since inception through March 31, 2003, we generated cumulative operating losses of approximately $277 million. We expect this trend to continue until such time that we can sell a sufficient number of units to achieve profitability. We have only been commercially producing Capstone MicroTurbines since December 1998. Our business is such that we have relatively few customers and limited repeat business. While the Company commenced a program to decrease expenses, there can be no assurance that expenses have been, or will be, decreased sufficiently to have adequate cash resources to reach the point of profitability, that the Company will not increase expenses in the future, that the Company will maintain or increase net revenues or that the Company will ever become profitable. Even if we do achieve profitability, we may be unable to increase our sales and sustain or increase our profitability in the future.

Our success depends in significant part upon the service of management and key employees.

Our success depends in significant part upon the service of our executive officers, senior management, and sales and technical personnel. We have undergone numerous personnel changes in all levels of the organization. In particular, the Board is seeking a permanent CEO. Our inability to find an appropriate person for the CEO position may adversely impact the prospects for the Company. The failure of our personnel to execute our strategy, or our failure to retain management and personnel, could have a material adverse effect on our business. In addition, our interim CEO may make changes in management or our strategy that are not consistent with a new CEO's strategic plans. If we are unable to develop and implement our strategy in a timely manner, our market penetration may be negatively impacted, which could have a material adverse effect on our business and results of operations. Our success will be dependent on our continued ability to attract, retain and motivate highly skilled employees. There can be no assurance that we can do so.

Our internal control systems are highly dependent on detective controls performed by specific individuals in key positions at the Company. Detective controls are those designed to detect mistakes that have occurred and correct them. Loss of these key people

or our inability to replace them with similarly skilled individuals or new processes in a timely manner could adversely impact our internal control mechanisms.

We have reduced our personnel in order to reduce our operating costs. If we have terminated individuals whose skills we subsequently needed or if demand for our product significantly exceeds our expectations, our ability to generate revenues and maintain customer relationships could be adversely affected.

The economic downturn has made potential customers hesitant to make capital expenditures.

The global economic climate has made potential customers hesitant to make capital expenditures. As a result, we have seen reluctance on the part of customers to buy our products. As a result of the economic uncertainty and the desire by companies to tighten capital expenditures, along with fluctuations in energy prices, political disruptions or the risk of higher interest rates, we may not be able to sustain or expand our customer base and sales, which would negatively impact our financial position and results of operations. The impact of continued lower capital spending may result in increased risk of excess and obsolete inventories, excess facilities and manufacturing capacity and higher overhead costs as a percentage of revenues.

If we do not effectively implement our sales and marketing plans, our sales will not grow and our profitability will suffer.

Our sales and marketing efforts may not successfully compete against the more extensive and well-funded sales and marketing operations of our current and future competitors and therefore may not generate the net revenues anticipated. We market microturbine technology for use in stationary distributed power generation applications such as CHP, resource recovery and power quality and reliability as well as hybrid electric vehicles. We have decided to focus our resources on select vertical markets we believe have near term potential, such as those where we already have distributors. We may change our focus to other markets or applications in the future. There can be no assurance that our focus or our near term plans will be successful. If we are not able to successfully address markets for our products, we may not be able to grow our business, compete effectively or achieve profitability.

A sustainable market for microturbines may never develop or may take longer to develop than we anticipate, which would adversely impact our revenues and profitability.

Our products represent an emerging market, and we do not know whether our targeted customers will accept our technology or will purchase our products in sufficient quantities to grow our business. If a sustainable market fails to develop or develops more slowly than we anticipate, we may be unable to recover the losses we have incurred to develop our products, we may have further impairment of assets, we may be unable to meet our operational expenses and we may be unable to achieve profitability. The development of a sustainable market for our systems may be impacted by many factors including some that are out of our control. Examples include:

- the cost competitiveness of our microturbines;
- costs associated with the installation and commissioning of our microturbines by third parties;
- maintenance costs associated with our microturbines;
- the future costs and availability of fuels used by our microturbines;
- consumer reluctance to try a new product;
- consumer perceptions of our microturbines' safety and quality;
- regulatory requirements;
- economic downturns and reduction in capital spending; and
- the emergence of newer, more competitive technologies and products.

We have limited experience in international sales and may not succeed in growing our international sales.

We have limited experience in international sales and will depend on our international marketing partners for these sales. If a dispute arises between us and any of our partners, we may not achieve our desired sales results and we may be delayed or completely fail to penetrate some international markets, and our revenue and operations could be materially adversely affected. Any inability to obtain foreign regulatory approvals or quality standard certifications on a timely basis could negatively impact our business and results of operations. Also, as we seek to expand into the international markets, customers may have difficulty or be unable to integrate our products into their existing systems or may have difficulty meeting local standards. As a result, our products may require redesign. Any redesign of the product may delay sales or cause quality issues. In addition, we may be subject to a variety of other risks associated with international business, including:

- delays in establishing international distribution channels;
- difficulties in collecting international accounts receivables;
- difficulties in complying with foreign regulatory and commercial requirements;
- difficulties in recruiting and retaining individuals skilled in international business operations;
- increased costs associated with maintaining international marketing efforts;
- compliance with U.S. Department of Commerce export controls;
- increases in duty rates;
- the introduction of non-tariff trade barriers;
- fluctuations in currency exchange rates;
- global political and economic instability; and
- difficulties in enforcement of intellectual property rights.

Product quality expectations may not be met causing slower market acceptance.

As we improve the quality and lower the maintenance costs of our products, we may require engineering changes. Such improvement initiatives may render existing inventories obsolete or excessive. Despite our continuous quality improvement initiatives, if we do not meet customer expectations, we may experience slower market acceptance of our products. Any significant quality issues with our products could have a material adverse effect on our results of operations and financial position. Moreover, as we develop new configurations for our microturbines or as our customers place existing configurations in commercial use, we may experience product malfunctions that cause our products to perform below expectations. Any significant malfunctions could adversely affect our operating results and financial position and affect the marketability of our products.

We depend upon the development of new products and enhancements of existing products.

Our operating results may depend on our ability to develop and introduce new products, such as the C200 Microturbine, for existing and emerging markets and to reduce the costs to produce existing products. The success of new products is dependent on several factors, including proper new product definition, product cost, timely completion and introduction of new products, differentiation of new products from those of our competitors, meeting changing customer requirements, emerging industry standards and market acceptance of these products. The development of new, technologically advanced products is a complex and uncertain process requiring high levels of innovation, as well as the accurate anticipation of technological and market trends. There can be no assurance that we will successfully identify new product opportunities, develop and bring new products to market in a timely manner, and achieve market acceptance of our products, or that products and technologies developed by others will not render our products or technologies obsolete or noncompetitive.

A key element of the Company's strategy is the development of its C200 Microturbine planned for release in 2004. However, the Company has on occasion experienced delays in the introduction of new products and product enhancements. Such delays have, and any future delays could have, a material adverse effect on the Company's business, operating results and financial condition. Furthermore, from time to time, the Company may announce new products or product enhancements, capabilities or technologies that have the potential to replace the Company's existing product offerings and that may cause customers to defer purchasing existing Company products. Any failure to introduce new products or product enhancements on a timely basis, customer delays in purchasing products in anticipation of new product introductions or any inability of the Company to respond effectively to product announcements by competitors, technological changes or emerging industry standards could have a material adverse effect on the Company's business, operating results and financial condition.

We operate in a highly competitive market and may not be able to compete effectively due to factors affecting the market for our products.

The market for our products is highly competitive and is changing rapidly. We believe that the primary competitive factors affecting the market for our products include:

- operating efficiency;
- reliability;
- product quality and performance;
- life cycle costs;
- development of new products and features;
- quality and experience of sales, marketing and service organizations;
- availability and price of fuel;
- product price;
- emissions levels;
- name recognition; and
- quality of distribution channels.

Several of these factors are outside our control. We cannot assure you that we will be able to compete successfully in the future with respect to these or any other competitive factors.

In addition, competing technologies may get certain benefits, like governmental subsidies or promotion that we do not enjoy or do not benefit from to the same extent. This could enhance their abilities to fund research or penetrate markets.

Our competitors, who have significantly greater resources than we have, may be able to adapt more quickly to new or emerging technologies or to devote greater resources to the promotion and sale of their products, and we may be unable to compete effectively.

Our competitors include several well-established companies that have substantially greater resources than we have and worldwide presence. Ingersoll-Rand Company and Elliott Power Systems are competitors of Capstone that benefit from larger corporate resources, including technical and engineering resources, and who have microturbines in various stages of development and commercialization. Ingersoll-Rand Company has commercialized its first line of microturbine units and has announced that it will be commercializing its 250-kilowatt product in 2003 which will directly compete with our C200 product targeted for release in 2004. Many of these companies sell directly to end-users, which we believe may provide some competitive advantages over our sales strategy. Furthermore, many of these companies offer a more comprehensive solution to their customers.

In addition to these competitors, Turbec, a joint venture in Europe of AB Volvo and ABB Ltd., develops, produces and sells microturbines. Turbec's first product, a combined heat and power microturbine, is currently available. A number of other major automotive and industrial companies have in-house microturbine development efforts, including Ishikawajima-Harima Heavy Industries, Turbo Genset Inc., Toyota Motor Corporation and Kawasaki Heavy Industries. Furthermore, we believe that all of these companies will eventually have products that will compete with our microturbines. Some of our competitors are currently developing and testing larger microturbines than Capstone's current MicroTurbine products, ranging up to 280 kilowatts, and which may have longer useful lives than Capstone MicroTurbines.

Capstone MicroTurbines also compete with other existing technologies, including the electric utility grid, reciprocating engines, fuel cells and photovoltaic systems. Many of the competitors producing these technologies also have greater resources than we have. For instance, reciprocating engine generator sets are produced and sold by, among others, Caterpillar Inc., Interstate Companies, Cummins Inc., Yanmar, Hess and MAN. We cannot assure you that the market for distributed power generation products will not ultimately be dominated by technologies other than ours. Furthermore, electric utility companies may impose fees or other barriers that make microturbines less competitive.

Because of greater resources, some of our competitors may be able to adapt more quickly to new or emerging technologies and changes in customer requirements, to devote greater resources to the promotion and sale of their products than we can or introduce governmental regulations and policies to create competitive advantage vis-à-vis our products. We believe that developing and maintaining a competitive advantage will require continued investment by us in product development and quality, as well as attention to product performance, our product prices, our conformance to industry standards, manufacturing capability and sales and marketing.

Achieving projected development schedules has a significant impact on customer expectations and near-term sales of products for which products under development could serve as a substitute. For example, we have projected that the C200 product will be commercially available in 2004; we cannot assure that we will meet this development schedule and may suffer an adverse impact on revenues if we fail to meet this schedule. In addition, current and potential competitors have established or may in the future establish collaborative relationships among themselves or with third parties, including third parties with whom we have business relationships. Accordingly, new competitors or alliances may emerge and rapidly acquire significant market share.

There is no assurance that we will be able to successfully compete against either current or potential competitors or that competition will not have a material adverse effect on our business, operating results and financial condition.

Changes in government regulations and the electric utility industry restructuring may affect demand for our microturbines.

The market for electricity and generation products is heavily influenced by federal and state government regulations and policies. The deregulation and restructuring of the electric industry in the United States and elsewhere may aid the desirability of alternative power sources. However, problems associated with such deregulation and restructuring may cause rule changes that may reduce or eliminate advantages of such deregulation and restructuring. We cannot predict how the deregulation and the restructuring of the electric utility industry will ultimately affect the market for our microturbines. Additional competition from utilities and other power sources that may take advantage of these regulations could diminish the demand for our products. While we have seen some increase in government support for distributed power, we cannot assure that this support will continue or that it will be maintained in its current form or that it will have any near-term impact on our operating results. For example, the California Self Generation Program is due to expire in December 2004. Changes in regulatory standards or policies could reduce the level of investment in the research and development of alternative power sources, including microturbines. Any reduction or termination of such programs can increase the cost to our potential customers, making our systems less desirable and thereby harm our revenue and potential profitability.

We operate in a highly regulated business environment and changes in regulation could impose costs on us or make our products less economical.

Our products are subject to federal, state, local and foreign laws and regulations, governing, among other things, emissions to air as well as laws relating to occupational health and safety. Regulatory agencies may impose special requirements for implementation and operation of our products (*e.g.*, connection with the electric grid) or may significantly impact or even eliminate some of our target markets. We may incur material costs or liabilities in complying with government regulations. In addition, potentially significant expenditures could be required in order to comply with evolving environmental and health and safety laws, regulations and requirements that may be adopted or imposed in the future. For example, our current products do not comply with the

2007 proposed emission standards of the California Air Resources Board. Furthermore, our potential utility customers must comply with numerous laws and regulations. The deregulation of the utility industry may also create challenges for our marketing efforts. For example, as part of electric utility deregulation, federal, state and local governmental authorities may impose transitional charges or exit fees, which would make it less economical for some potential customers to switch to our products. Further, our ability to penetrate the Japanese market will depend on our receipt of approvals and changes to regulatory requirements surrounding power generation by Japanese regulators. We can provide no assurances that we will be able to obtain these approvals and changes in a timely manner, or at all.

Utility companies could place barriers to our entry into the marketplace and we may not be able to effectively sell our product.

Utility companies may charge additional fees to industrial customers who install on-site generation, thereby reducing the electricity they take from the utility, or for having the capacity to use power from the grid for back-up or standby purposes. For example, the New York Public Service Commission is currently in the process of adopting new standby charges. These types of fees or charges could increase the cost to our potential customers for using our systems and could make our systems less desirable, thereby harming our revenue and profitability potential. In addition, utility rate reductions can make our products less competitive which will have a material adverse effect on our operations. The California Public Utility Commission will be considering new rate proposals for investor owned utilities.

We may not be able to retain or develop additional strategic partners and distributors in our targeted markets, in which case our sales would not increase as expected.

In order to expand our customer base, we believe that we must enter into strategic sales and marketing alliances or similar collaborative relationships, in which we ally ourselves with companies that have particular expertise in or more extensive access to desirable markets. We believe that developing strategic partners in our targeted markets can improve the rate of adoption as well as reduce the direct financial burden of introducing a new technology and creating a new market. We may provide volume price discounts or otherwise incur significant costs that may reduce the potential profitability of these relationships. We may not be able to retain or develop appropriate distributors or strategic partners on a timely basis, and we cannot assure you that the partners with which we form alliances will focus adequate resources on selling our products or will be successful in selling them. In addition, some of the relationships may require that we grant exclusive distribution rights in defined territories. These exclusive distribution arrangements could result in us being unable to enter into other arrangements at a time when the distributor or partner with whom we form a relationship is not successful in selling our products or has reduced its commitment to market our products. We cannot assure you that we will be able to negotiate collaborative relationships on favorable terms or at all. The inability of the Company to develop strategic partners or a lack of success of our strategic partners in marketing our products may adversely affect our financial condition and results of operations.

We are subject to risks associated with our strategic alliance with United Technologies Corporation.

In October 2002, we entered into a strategic alliance with UTC through its UTC Power Division. The strategic alliance between UTC and Capstone is a ten-year agreement that involves the integration, marketing, sales and service of CHP solutions targeted for commercial buildings. The UTC Agreement provides for the combination of our microturbine products with their absorption chillers. We cannot assure that we can complete this integration in a cost effective manner or consistent with UTC's or our timing expectations. UTC will be the exclusive distributor for the combined Capstone MicroTurbines with UTC absorption chillers, but they will also be a non-exclusive distributor generally for Capstone MicroTurbines. The UTC Agreement is limited to North America and most of Europe. However, this alliance may not be successful and may create channel conflict with our other distributors. If this relationship fails to materialize as expected then this may impede our future growth and a sustainable market may fail to develop. Furthermore, although both parties have certain competitive restrictions, UTC may offer alternative solutions, designed by themselves or third parties. There can be no assurance that UTC will give a high priority to the marketing of the Company's products as compared to its other products or alternative solutions. Both UTC and Capstone have options to terminate the relationship if the other company fails to meet its development, product purchase or other goals in the UTC Agreement. There can be no assurance that the Company will retain its relationship with UTC. We do not expect short-term operating benefits from the UTC relationship but we have incurred and will incur short-term costs to create this alliance and fulfill our obligations under the UTC Agreement.

As part of the UTC Agreement, UTC purchased 3,994,817 shares of Capstone's common stock (the "UTC Shares") in October 2002 for an aggregate price of approximately $4.0 million. The UTC shares are subject to a lock-up period of nine months subject to certain exceptions provided for in the UTC Agreement. Any sale by UTC of the UTC Shares may be viewed by the

investing public as a drawback to the relationship that could have a material adverse effect on the Company's stock price and financial condition.

Our ability to identify and develop Authorized Service Providers ("ASPs") can significantly impact our success.

Our ability to identify and develop business relationships with ASPs who can provide quality, cost effective installations and service can significantly impact our success. We need to reduce the total installed cost of our microturbines to enhance market opportunities. Our inability to improve our ASPs' quality of installation and commissioning standards while reducing associated costs could affect the marketability of our products.

Our suppliers and manufacturers may not supply us with a sufficient amount of components or components of adequate quality, and we may not be able to produce our product.

Although we generally attempt to use standard parts and components for our products, some of our components are currently available only from a single source or limited sources. We may experience delays in production if we fail to identify alternative vendors, or any parts supply is interrupted, each of which could materially adversely affect our business and operations. In order to reduce manufacturing lead times and ensure adequate component supply, we enter into agreements with certain contract manufacturers and supply partners that allow them to procure inventory based upon criteria defined by us. If we fail to anticipate customer demand properly, an oversupply of parts could result in excess or obsolete inventories, which could adversely affect our business. A reduction or interruption in supply, a significant increase in price of one or more components or a decrease in demand of products could materially adversely affect our business and operations and could materially damage our customer relationships. Also, we cannot guarantee that any of the parts or components that we are obligated to purchase will be of adequate quality or that the prices we pay for the parts or components will not increase. Our inability to meet volume commitments with suppliers could affect the availability or pricing of our parts and components. Financial problems of contract manufacturers on whom we rely could limit our supply or increase our costs.

We may not achieve production cost reductions necessary to competitively price our product, which would impair our sales.

We believe that we will need to reduce the unit production cost of our products over time to maintain our ability to offer competitively priced products. Our ability to achieve cost reductions will depend on our ability to develop low cost design enhancements, to obtain necessary tooling and favorable vendor contracts, as well as to increase sales volumes so we can achieve economies of scale. We cannot assure you that we will be able to achieve any production cost reductions. Our failure to achieve such cost reductions could have a material adverse effect on our business and results of operations.

Our products involve a lengthy sales cycle and we may not anticipate sales levels appropriately, which could impair our profitability.

The sale of our products typically involves a significant commitment of capital by customers, with the attendant delays frequently associated with large capital expenditures. For these and other reasons, the sales cycle associated with our products is typically lengthy and subject to a number of significant risks over which we have little or no control. We expect to plan our production and inventory levels based on internal forecasts of customer demand, which is highly unpredictable and can fluctuate substantially. If sales in any period fall significantly below anticipated levels, our financial condition and results of operations could suffer. If demand in any period increases well above anticipated levels, we may have difficulties in responding, incur greater costs to respond, or be unable to fulfill the demand in sufficient time to retain the order. In addition, our operating expenses are based on anticipated sales levels, and a high percentage of our expenses are generally fixed in the short term. As a result of these factors, a small fluctuation in timing of sales can cause operating results to vary from period to period.

We may not effectively expand our production capabilities, which would negatively impact our sales.

We may experience unanticipated growth in our business operations, which may require expansion of our internal and external production capabilities. We may experience delays or problems in expanding production that could significantly impact our business. Several factors could delay or prevent production expansion, including our:

- inability to purchase parts or components in adequate quantities or sufficient quality;
- failure to increase our assembly and test operations;

- failure to hire and train additional personnel;
- failure to develop and implement manufacturing processes and equipment;
- inability to find and train proper partner companies with whom we can build product distribution, marketing, or development relationships; and
- inability to manufacture recuperator cores or air bearings on schedule, in quantities or with the quality that we require.

If we are unable to manufacture recuperator cores internally, our assembly and production of microturbines may suffer delays and interruptions.

Solar Turbines Incorporated ("Solar") was our sole supplier of recuperator cores, which are heat exchangers that preheat incoming air before it enters the combustion chamber and are an essential component of our microturbines. In 2001, we started to manufacture recuperator cores under contractual rights to use Solar's intellectual property. We cannot assure you that we will be able to successfully implement this technology in developing a sustainable manufacturing process at higher volumes. While on a demonstration basis, we have shown the ability to produce 50 cores in one week, this may not be sustainable as we are not experienced in manufacturing recuperator cores. Inherent in the manufacturing process are a number of risks. Manufacturing of the recuperator cores is a complex process requiring high levels of innovation and skill. At present, we are not aware of any other supplier that could produce these cores to our specifications within our time requirements. As a result of recent cost cutting measures, we have fewer people skilled in manufacturing recuperator cores. Our inability to manufacture recuperator cores could have a material adverse effect on the Company's operating results.

Our business is especially subject to the risk of earthquake.

Our Company and our manufacturing facilities are located in Southern California, a region known for seismic activity. A significant natural disaster, such as an earthquake, could have a material adverse impact on our business, operating results and financial condition.

We may not be able to effectively manage our growth or improve our operational, financial and management information systems, which would impair our profitability.

If we are successful in executing our business plan, we will experience growth in our business that could place a significant strain on our management and other resources. Our ability to manage our growth will require us to continue to improve our operational, financial and management information systems, to implement new systems and to motivate and effectively manage our employees. We cannot assure you that our management will be able to effectively manage this growth.

We depend on our intellectual property to make our products competitive and if we are unable to protect our intellectual property, our business will suffer.

We rely on a combination of patent, trade secret, copyright and trademark law, and nondisclosure agreements to establish and protect our intellectual property rights in our products. In particular, we believe that our patents and patents pending for our air-bearing systems, power electronics and controls and our combustion systems are key to our business. We believe that, due to the rapid pace of technological innovation in turbine products, our ability to establish and maintain a position among the technology leaders in the industry depends on both our patents and other intellectual property and the skills of our development personnel. We cannot assure you that any patent, trademark, copyright or license owned or held by us will not be invalidated, circumvented or challenged, that the rights granted thereunder will provide competitive advantages to us or that any of our future patent applications will be issued with the scope of the claims asserted by us, if at all. Further, we cannot assure you that third parties or competitors will not develop technologies that are similar or superior to our technology, including our air bearing technology, duplicate our technology or design around our patents. Also, another party may be able to reverse engineer our technology and discover our intellectual property and trade secrets. We may be subject to or may initiate proceedings in the U.S. Patent and Trademark Office, which can require significant financial and management resources or require us to develop a non-infringing technology or enter into royalty or license agreements. If we are found to infringe upon the intellectual property rights of others, we may not be able to produce our products or may have to enter into costly license agreements. In addition, the laws of foreign countries in which our products are or may be developed, manufactured or sold may not protect our products and intellectual property rights to the same extent as the laws of the United States.

Our inability to protect our intellectual property adequately could have a material adverse effect on our financial condition or results of operations.

Potential intellectual property, shareholder or other litigation may adversely impact our business.

Because of the nature of our business, we may face litigation relating to intellectual property matters, labor matters, product liability and shareholder disputes. For example, in December 2001, a purported shareholder class action lawsuit was filed in the United States District Court for the Southern District of New York against the Company, two of its officers, and the underwriters of our initial public offering. The suit purports to be a class action filed on behalf of purchasers of our common stock during the period from June 28, 2000 to December 6, 2000. An amended complaint was filed on April 19, 2002. No date has been set for the Company to respond to the complaint. Plaintiffs allege that the underwriter defendants agreed to allocate stock in the Company's June 28, 2000 initial public offering and November 16, 2000 secondary offering to certain investors in exchange for excessive and undisclosed commissions and agreements by those investors to make additional purchases of stock in the aftermarket at pre-determined prices. Plaintiffs allege that the prospectuses for these two public offerings were false and misleading in violation of the securities laws because they did not disclose these arrangements. The Company understands that over three hundred other issuers have been named as defendants in nearly identical lawsuits filed by some of the same plaintiffs' law firms. We intend to defend these actions vigorously. However, due to the inherent uncertainties of litigation, we cannot accurately predict the ultimate outcome of the litigation. Any unfavorable outcome of litigation could have a material adverse effect on the Company's financial position and results of operations.

Our intellectual property is one of our principal assets. A negative outcome in litigation relating to our intellectual property could have a material adverse effect on our business and operating results. An adverse judgment could negatively impact the price of our common stock and our ability to obtain future financing on favorable terms or at all. Any litigation could be costly, divert management attention or result in increased costs of doing business.

We may be unable to fund our future operating requirements, which could force us to curtail our operations.

We are a capital-intensive company and may need additional financing to fund our operations. Our future capital requirements will depend on many factors, including our ability to successfully market and sell our products. To the extent that the funds we now have on hand are insufficient to fund our future operating requirements, we will need to raise additional funds, through further public or private equity or debt financings. These financings may not be available or, if available, may be on terms that are not favorable to us and could result in further dilution to our stockholders. Downturns in worldwide capital markets may also impede our ability to raise additional capital on favorable terms or at all. If adequate capital were not available to us, we would likely be required to significantly curtail or possibly even cease our operations.

We may encounter greater business risks in the future as we manage cash resources differently. In 2002, we undertook efforts to lower our cash burn rate. As a result of those and ongoing efforts, we may not spend money in areas that ultimately prove important to the business. We may incur greater risks through lower spending rates for insurance, intellectual property protection, total employee compensation and other areas.

Termination of certain Supply and Distribution Agreements may require us to repurchase parts inventory.

We have certain Supply and Distribution Agreements and ASP agreements that upon termination under specified conditions require us to repurchase particular elements of their parts inventories. To date, these conditions have never arisen and we believe that the amounts of such inventories currently are not significant. It is possible, however, that in the future such conditions could occur that would require such repurchases. These repurchases could result in higher prices for the repurchased parts inventory than would otherwise be required to secure such quantities or could result in excess quantities of some parts inventory. In addition, certain ASP agreements require us to provide service to the customers of the ASP upon termination of the ASP agreement under specified conditions, until such time that we can identify and transfer the obligation to a new ASP. Since we do not have control over the terms of such third-party service agreements, we may be exposed to significant risks and expenses that we cannot adequately quantify. To date these conditions have not arisen, however, any significant exposure from such third-party service agreements in the future could have a material effect on our results of operations and financial position.

We face potentially significant fluctuations in operating results, which could impact our stock price.

As a result of variety of factors discussed herein, operating results for a particular quarter are difficult to predict. Given the continued uncertainty surrounding many variables that may impact the industry in which we operate, our visibility into future periods is limited. Our net sales may grow at a slower rate than experienced in the past periods and, in particular periods or overall, may decline. A number of factors could affect our operating results and thereby impact our stock price, including:

- the timing of the introduction or enhancement of products by us or our competitors;
- quality of installation and commissioning of our products by our ASPs and customers;
- our reliance on a small number of customers;
- the lack of order backlog;
- the size, timing, shipment and pricing of individual orders;
- market acceptance of new products;
- customers delaying orders of our products because of the anticipated release of new products by us or our competitors;
- changes in our operating expenses, the mix of products sold, or product pricing;
- the ability of our suppliers to deliver quality parts when we need them;
- development of our direct and indirect sales channels;
- change in management and loss of key personnel;
- political unrest or changes in the trade policies, tariffs or other regulations of countries in which we do business that could lower demand for our products;
- changes in environmental regulations; and
- changes in market prices for natural resources that could lower the desirability of our products.

Because we are in the early stages of selling our products, with relatively few customers, we expect our order flow to continue to be uneven from period to period. In addition, we do not have an established base of customers that we can rely on for repeat sales. Because a significant portion of our expenses is fixed, a small variation in the timing of recognition of revenue can cause significant variations in operating results from quarter to quarter. Any of the above factors could have a material adverse effect on our operations and financial results.

The market price of our common stock is highly volatile and may decline regardless of our operating performance.

The market price of our common stock is highly volatile. Many factors of this volatility are beyond our control. These factors may cause the market price of our common stock to decline, regardless of our operating performance. Factors that could cause fluctuation in our stock price may include, among other things:

- actual or anticipated variations in quarterly operating results;
- changes in financial estimates by securities analysts;
- conditions or trends in our industry or the overall economy;
- changes in the market valuations of other technology companies;

- the listing for trading of options on our common stock;
- announcements by us or our competitors of significant acquisitions, strategic partnerships, divestitures, joint ventures or other strategic initiatives;
- capital commitments;
- additions or departures of key personnel; and
- sales of common stock.

Our announced stock repurchase program may not produce benefits for stockholders.

Capstone may not purchase the approved maximum $10 million under the repurchase program announced in October 2002 or may not acquire shares at prices that later appear advantageous. We cannot assure stockholders that using cash for this purpose will result in short-term or long-term benefits for our stockholders.

Our NASDAQ National Market listing may be adversely affected if our stock price does not rise and we are unable to meet NASDAQ's listing requirements through other actions.

In order to continue to be listed on the NASDAQ National Market, we must meet specific quantitative standards, including a minimum bid price. On March 18, 2003, we received notice from the NASDAQ that the price of our stock had closed below the minimum $1.00 per share requirement for 30 consecutive trading days. Therefore, in accordance with Marketplace Rule 4450(e)(2), we will be provided until September 15, 2003 to regain compliance. In the event that we should fail to meet this listing requirement, we may appeal such determination, we may apply for listing on the NASDAQ SmallCap Market (where we may have up to an additional nine months to comply with the minimum bid price requirements for continued listing) or we may pursue alternative strategies to allow our common stock to continue to be listed. If we fail to meet the continuing listing standards for the NASDAQ National Market (and, should we be listed on the NASDAQ SmallCap Market, if we fail to meet the continuing listing standards for the NASDAQ SmallCap Market), our stock may be delisted. The delisting of our common stock would adversely affect the liquidity and trading price of our securities. In addition, it would make it difficult for investors to obtain accurate quotations of the share price of our common stock.

Item 6. ***Exhibits and Reports on Form 8-K:***

(a) *Index to Exhibits.*

The following exhibits are filed with, or incorporated by reference into, this Quarterly Report on Form 10-Q:

Exhibit Number	Description
3.1(2)	Second Amended and Restated Certificate of Incorporation of Capstone Turbine.
3.2(1)	Second Amended and Restated Bylaws of Capstone Turbine.
4.1(2)	Specimen stock certificate.
9.1(2)	Investors Rights Agreement.
9.2(2)	Amendment No. 1 to Investors Rights Agreement.
9.3(3)	Amendment No. 2 to Investors Rights Agreement.
9.4(3)	Amendment No. 3 to Investors Rights Agreement.
10.1(2)	Lease between Capstone Turbine and Northpark Industrial — Leahy Division LLC, dated December 1, 1999, for leased premises at 21211 Nordhoff Street, Chatsworth, California.
10.2(2)	1993 Incentive Stock Option Plan.
10.3(2)	Employee Stock Purchase Plan.
10.4(1)	Amended and Restated 2000 Equity Incentive Plan
10.5(4)	Transition Agreement, dated August 2, 2000, by and between Capstone Turbine and Solar Turbines Incorporated.
10.6(4)	Amended and Restated License Agreement, dated August 2, 2000, by and between Solar Turbines Incorporated and Capstone Turbine.
10.7(6)	Lease between Capstone Turbine and AMB Property, L.P., dated September 25, 2000, for leased premises at 16640 Stagg Street, Van Nuys, California.
10.8(6)	Lease between Capstone Turbine and AH Warner Center Properties, Limited Liability Company, dated February 16, 2001, for leased premises at 21700 Oxnard Street, Woodland Hills, California.
10.9(5)	Deferred Compensation Plan of Capstone Turbine
10.10(7)	Executive Incentive Compensation Plan
10.11 (7)	Change of Control Severance Plan
10.12 (8)	Transition Agreement and Mutual Release between Dr. Ake Almgren and Capstone Turbine Corporation dated October 31, 2002 and February 26, 2003
10.13 (8)	The Interim CEO Network Agreement between Emily Liggett and ICN dated November 21, 2002
10.14 (1)	Severance Pay Plan and First Amendment to the Severance Pay Plan
99.1 (1)	Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350

(1) Filed herewith.
(2) Incorporated by reference to Capstone Turbine's Registration Statement on Form S-1 (File No. 333-33024).
(3) Incorporated by reference to Capstone Turbine's Registration Statement on Form S-1 (File No. 333-48524).
(4) Incorporated by reference to Capstone Turbine's Current Report on Form 8-K filed on October 16, 2000.
(5) Incorporated by reference to Capstone Turbine's Registration Statement on Form S-8 (File No. 333-66390).
(6) Incorporated by reference to Capstone Turbine's Annual Report on Form 10-K for the year ended December 31, 2001 (File No. 001-15957).
(7) Incorporated by reference to Capstone Turbine's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2002 (File No. 001-15957).
(8) Incorporated by reference to Capstone Turbine's Annual Report on Form 10-K for the year ended December 31, 2002 (File No. 001-15957).

(b) *Reports on Form 8-K.*
None

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.

CAPSTONE TURBINE CORPORATION

Date: May 15, 2003 By: /s/ KAREN CLARK

Karen Clark
Senior Vice President,
Chief Financial Officer
(Principal Financial and Accounting Officer)

CERTIFICATION

I, Emily Liggett, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Capstone Turbine Corporation;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

   a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiary, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

   b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

   c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

   a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

   b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officer and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: May 15, 2003 By: /s/ EMILY LIGGETT

Emily Liggett
Interim Chief Executive Officer

CERTIFICATION

I, Karen Clark, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Capstone Turbine Corporation;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

   a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiary, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

   b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

   c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

   a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

   b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officer and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: May 15, 2003 By: /s/ KAREN CLARK

Karen Clark
Chief Financial Officer

EXHIBIT 3.2

SECOND AMENDED AND RESTATED BYLAWS OF

CAPSTONE TURBINE CORPORATION

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SECOND AMENDED AND RESTATED BYLAWS

OF

CAPSTONE TURBINE CORPORATION

ARTICLE I

OFFICES

Section 1. Registered Office. The registered office of Capstone Turbine Corporation (hereinafter, called the "corporation") shall be in the City of Dover, County of Kent, State of Delaware.

Section 2. Other Offices. The corporation may also have offices at such other places both within and without the State of Delaware as the Board of Directors may from time to time determine or the business of the corporation may require.

ARTICLE II

STOCKHOLDERS

Section 1. Place of Meetings. Meetings of stockholders shall be held at any place within or outside the State of Delaware designated by the board of directors. In the absence of any such designation, stockholders' meetings shall be held at the principal executive office of the corporation.

Section 2. Annual Meetings of Stockholders. The annual meeting of stockholders shall be held each year on a date and time designated by the board of directors. Any previously scheduled annual meeting of the stockholders may be postponed by resolution of the board of directors upon public notice given prior to the date previously scheduled for such annual meeting of the stockholders.

Section 3. Special Meetings. A special meeting of the stockholders may be called at any time by the chairman of the board of directors, or by a majority of the directors or by a committee of the board of directors which has been duly designated by the board of directors and whose powers and authority, as provided in a resolution of the board of directors, include the power to call such meetings, but such special meetings may not be called by any other person or persons. Any previously scheduled special meeting of the stockholders may be postponed by resolution of the board of directors upon public notice given prior to the date previously scheduled for such special meeting of the stockholders.

Section 4. Notice of Stockholders' Meetings. All notices of meetings of stockholders shall be sent or otherwise given in accordance with Section 5 of this Article II not less than ten (10) nor more than sixty (60) days before the date of the meeting being noticed. The notice shall

specify the place, date and hour of the meeting and in the case of a special meeting, the general nature of the business to be transacted.

Section 5. Manner of Giving Notice; Affidavit of Notice. If mailed, notice shall be deemed to have been given when deposited in the mail, postage prepaid, directed to the stockholder at his address appearing on the books of the corporation or given by the stockholder to the corporation for the purpose of notice. An affidavit of the mailing or other means of giving any notice of any stockholders' meeting shall be executed by the secretary, assistant secretary or any transfer agent of the corporation giving such notice, and shall be filed and maintained in the minute book of the corporation.

Section 6. Quorum. The presence in person or by proxy of the holders of a majority of the shares entitled to vote at any meeting of stockholders shall constitute a quorum for the transaction of business. The stockholders present at a duly called or held meeting at which a quorum is present may continue to do business until adjournment, notwithstanding the withdrawal of enough stockholders to leave less than a quorum, if any action taken (other than adjournment) is approved by at least a majority of the shares required to constitute a quorum.

Section 7. Adjourned Meeting and Notice Thereof. Any stockholders' meeting, annual or special, whether or not a quorum is present, may be adjourned from time to time by the chairman of the meeting, but in the absence of a quorum, no other business may be transacted at such meeting, except as provided in Section 6 of this Article II.

When any meeting of stockholders, either annual or special, is adjourned to another time or place, notice need not be given of the adjourned meeting if the time and place thereof are announced at a meeting at which the adjournment is taken, unless a new record date for the adjourned meeting is fixed, or unless the adjournment is for more than thirty (30) days from the date set for the original meeting. Notice of any such adjourned meeting, if required, shall be given to each stockholder of record entitled to vote at the adjourned meeting in accordance with the provisions of Sections 4 and 5 of this Article II. At any adjourned meeting the corporation may transact any business which might have been transacted at the original meeting.

Section 8. Voting. The stockholders entitled to vote at any meeting of stockholders shall be determined in accordance with the provisions of Section 11 of this Article II. Such vote may be by voice vote or by ballot, at the discretion of the chairman of the meeting. Any stockholder entitled to vote on any matter (other than the election of directors) may vote part of the shares in favor of the proposal and refrain from voting the remaining shares or vote them against the proposal; but, if the stockholder fails to specify the number of shares such stockholder is voting affirmatively, it will be conclusively presumed that the stockholder's approving vote is with respect to all shares such stockholder is entitled to vote. If a quorum is present, the affirmative

vote of the majority of the shares represented at the meeting and entitled to vote on any matter shall be the act of the stockholders, unless the vote of a greater number or voting by classes is required by the Delaware General Corporation Law or the certificate of incorporation or the certificate of determination of preferences as to any preferred stock.

At a stockholders' meeting involving the election of directors, no stockholder shall be entitled to cumulate (i.e., cast for any one or more candidates a number of votes greater than the number of the stockholders shares). The candidates receiving the highest number of votes, up to the number of directors to be elected, shall be elected.

Section 9. Waiver of Notice or Consent by Absent Stockholders. The transactions of any meeting of stockholders, either annual or special, however called and noticed, and wherever held, shall be as valid as though had at a meeting duly held after regular call and notice, if a quorum be present either in person or by proxy, and if, either before or after the meeting, each person entitled to vote, not present in person or by proxy, signs a written waiver of notice or a consent to the holding of the meeting, or an approval of the minutes thereof. The waiver of notice or consent need not specify either the business to be transacted or the purpose of any annual or special meeting of stockholders. All such waivers, consents or approvals shall be filed with the corporate records or made part of the minutes of the meeting.

Attendance of a person at a meeting shall also constitute a waiver of notice of such meeting, except when the person objects, at the beginning of the meeting, to the transaction of any business because the meeting is not lawfully called or convened, and except that attendance at a meeting is not a waiver of any right to object to the consideration of matters not included in the notice of the meeting if such objection is expressly made at the meeting.

Section 10. No Stockholder Action by Written Consent Without a Meeting. Stockholders may take action only at a regular or special meeting of stockholders.

Section 11. Record Date for Stockholder Notice and Voting. For purposes of determining the holders entitled to notice of any meeting or to vote, the board of directors may fix, in advance, a record date, which shall not be more than sixty (60) days nor less than ten (10) days prior to the date of any such meeting, and in such case only stockholders of record on the date so fixed are entitled to notice and to vote, notwithstanding any transfer of any shares on the books of the corporation after the record date fixed as aforesaid, except as otherwise provided in the Delaware General Corporation Law.

If the board of directors does not so fix a record date, the record date for determining stockholders entitled to notice of or to vote at a meeting of stockholders shall be at the close of business on the business day next preceding the day on which notice is given or, if notice is waived, at the close of business on the business day next preceding the day on which the meeting is held.

Section 12. Proxies. Every person entitled to vote for directors or on any other matter shall have the right to do so either in person or by one or more agents authorized by a written proxy signed by the person and filed with the secretary of the corporation. A validly executed proxy which does not state that it is irrevocable shall continue in full force and effect unless (i) revoked by the person executing it, prior to the vote pursuant thereto, by a writing delivered to the corporation stating that the proxy is revoked or by a subsequent proxy executed by, or attendance at the meeting and voting in person by, the person executing the proxy, or (ii) written notice of the death or incapacity of the maker of such proxy is received by the corporation before

the vote pursuant thereto is counted; provided, however, that no such proxy shall be valid after the expiration of one (1) year from the date of such proxy, unless otherwise provided in the proxy.

Section 13. Inspectors of Election; Opening and Closing the Polls. The board of directors by resolution shall appoint one or more inspectors, which inspector or inspectors may include individuals who serve the corporation in other capacities, including, without limitation, as officers, employees, agents or representatives, to act at the meetings of stockholders and make a written report thereof. One or more persons may be designated as alternate inspectors to replace any inspector who fails to act. If no inspector or alternate has been appointed to act or is able to act at a meeting of stockholders, the chairman of the meeting shall appoint one or more inspectors to act at the meeting. Each inspector, before discharging his or her duties, shall take and sign an oath faithfully to execute the duties of inspector with strict impartiality and according to the best of his or her ability. The inspectors shall have the duties prescribed by law.

The chairman of the meeting shall fix and announce at the meeting the date and time of the opening and the closing of the polls for each matter upon which the stockholders will vote at a meeting.

Section 14. Nomination and Stockholder Business Bylaw.

(A) Annual Meetings of Stockholders.

(1) Nominations of persons for election to the board of directors of the corporation and the proposal of business to be considered by the stockholders may be made at an annual meeting of stockholders (a) pursuant to the corporation's notice of meeting, (b) by or at the direction of the board of directors or (c) by any stockholder of the corporation who was a stockholder of record at the time of giving of notice provided for in this bylaw, who is entitled to vote at the meeting and who complies with the notice procedures set forth in this bylaw.

(2) For nominations or other business to be properly brought before an annual meeting by a stockholder pursuant to clause (c) of paragraph (A)(1) of this bylaw, the stockholder must have given timely notice thereof in writing to the secretary of the corporation and such other business must otherwise be a proper matter for stockholder action. To be timely, a stockholder's notice shall be delivered to the secretary at the principal executive offices of the corporation not less than the close of business on the 120th calendar day in advance of the first anniversary of the date the corporation's proxy statement was released to security holders in connection with the preceding year's annual meeting; provided, however, that if no annual meeting was held in the previous year or the date of the annual meeting has been changed by more than thirty (30) calendar days from the date contemplated at the time of the previous year's proxy statement, a proposal shall be received by the corporation no later than the close of business on the tenth day following the day on which notice of the date of the meeting was mailed or public announcement of the date of the meeting was made, whichever comes first. In no event shall the public announcement of an adjournment of an annual meeting commence a new time period for the giving of a stockholder's notice as described above. Such stockholder's notice shall set forth (a) as to each person whom the stockholder proposes to nominate for

election or reelection as a director all information relating to such person that is required to be disclosed in solicitations of proxies for election of directors in an election contest, or is otherwise required, in each case pursuant to applicable federal securities laws, including, without limitation, Regulation 14A under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and Rule 14a-11 thereunder (including such person's written consent to being named in the proxy statement as a nominee and to serving as a director if elected); (b) as to any other business that the stockholder proposes to bring before the meeting, a brief description of the business desired to be brought before the meeting, the reasons for conducting such business at the meeting and any material interest in such business of such stockholder and the beneficial owner, if any, on whose behalf the proposal is made; and (c) as to the stockholder giving the notice and the beneficial owner, if any, on whose behalf the nomination or proposal is made (i) the name and address of such stockholder, as they appear on the corporation's books, and of such beneficial owner and (ii) the class and number of shares of the corporation which are owned beneficially and of record by such stockholder and such beneficial owner.

(3) Notwithstanding anything in the second sentence of paragraph (A)(2) of this bylaw to the contrary, in the event that the number of directors to be elected to the board of directors of the corporation is increased and there is no public announcement by the corporation naming all of the nominees for director or specifying the size of the increased board of directors at least 70 days prior to the first anniversary of the date of the preceding years annual meeting, a stockholders notice required by this bylaw shall also be considered timely, but only with respect to nominees for any new positions created by such increase, if it shall be delivered to the secretary at the principal executive offices of the corporation not later than the close of business on the 10th day following the day on which such public announcement is first made by the corporation.

(B) Special Meetings of Stockholders. Only such business shall be conducted at a special meeting of stockholders as shall be brought before the meeting pursuant to the corporation's notice of meeting. A stockholder's nomination of one or more persons for election to the board of directors shall only be permitted to be made at a special meeting of stockholders if: (i) the corporation's notice of such meeting specified that directors are to be elected at such special meeting; (ii) such stockholder was a stockholder of record entitled to vote at the meeting at the time of giving of notice provided for in this bylaw; and (iii) if such stockholder complies with the notice procedures set forth in this bylaw. In the event the corporation calls a special meeting of stockholders for the purpose of electing one or more directors to the board of directors, any such stockholder may nominate a person or persons (as the case may be), for election to such position(s) as specified in the corporation's notice of meeting, if the stockholder's notice required by paragraph (A)(2) of this bylaw shall be delivered to the secretary at the principal executive offices of the corporation not earlier than the close of business on the 90th day prior to such special meeting and not later than the close of business on the later of the 60th day prior to such special meeting or the 10th day following the day on which public announcement is first made of the date of the special meeting and of the nominees proposed by the board of directors to be elected at such meeting. In no event shall the public announcement of an adjournment of a special meeting commence a new time period for the giving of a stockholder's notice as described above.

(C) General.

(1) Only such persons who are nominated in accordance with the procedures set forth in this bylaw shall be eligible to serve as directors. Except as otherwise provided by law, the certificate of incorporation or these bylaws, the chairman of the meeting shall have the power and authority to determine the procedures of a meeting of stockholders, including, without limitation, the authority to determine whether a nomination or any other business proposed to be brought before the meeting was made or proposed, as the case may be, in accordance with the procedures set forth in this bylaw and, if any proposed nomination or business is not in compliance with this bylaw, to declare that such defective proposal or nomination shall be disregarded.

(2) For purposes of this bylaw, "public announcement" shall mean disclosure in a press release reported by the Dow Jones News Service, Associated Press or comparable national news service or in a document publicly filed by the corporation with the Securities and Exchange Commission pursuant to Section 13, 14 or 15(d) of the Exchange Act.

(3) Notwithstanding the foregoing provisions of this bylaw, a stockholder shall also comply with all applicable requirements of the Exchange Act and the rules and regulations thereunder with respect to the matters set forth in this bylaw. Nothing in this bylaw shall be deemed to affect any rights (i) of stockholders to request inclusion of proposals in the corporation's proxy statement pursuant to Rule 14a-8 under the Exchange Act or (ii) of the holders of any series of preferred stock, if any, to elect directors under certain circumstances.

ARTICLE III

DIRECTORS

Section 1. Powers. Subject to the provisions of the Delaware General Corporation Law and any limitations in the certificate of incorporation and these bylaws relating to action required to be approved by the stockholders or by the outstanding shares, the business and affairs of the corporation shall be managed and all corporate powers shall be exercised by or under the direction of the board of directors.

Section 2. Number and Qualification of Directors. Until otherwise determined by resolution by the Board of Directors, the number of directors of the corporation shall be eight (8).

Section 3. Election and Term of Office of Directors. Directors shall be elected at the annual meeting of the stockholders. Each director, including a director elected to fill a vacancy, shall serve for a term ending on the next annual meeting following the annual meeting at which such director was elected and until a successor has been elected and qualified or the earlier of his resignation or removal.

Section 4. Vacancies. Vacancies in the board of directors may be filled by a majority of the remaining directors, though less than a quorum, or by a sole remaining director. Each

director elected to fill a vacancy shall hold office for the remainder of the term of the person whom he succeeds, and until a successor has been elected and qualified.

A vacancy or vacancies in the board of directors shall be deemed to exist in the case of the death, retirement, resignation or removal of any director, or if the board of directors by resolution declares vacant the office of a director who has been declared of unsound mind by an order of court or convicted of a felony, or if the authorized number of directors be increased, or if the stockholders fail at any meeting of stockholders at which any director or directors are elected, to elect the full authorized number of directors to be voted for at that meeting.

Any director may resign or voluntarily retire upon giving written notice to the chairman of the board, the president, the secretary or the board of directors. Such retirement or resignation shall be effective upon the giving of the notice, unless the notice specifies a later time for its effectiveness. If such retirement or resignation is effective at a future time, the board of directors may elect a successor to take office when the retirement or resignation becomes effective.

No reduction of the authorized number of directors shall have the effect of removing any director prior to the expiration of his term of office.

Section 5. Place of Meetings and Telephonic Meetings. Regular meetings of the board of directors may be held at any place within or without the State of Delaware that has been designated from time to time by resolution of the board. In the absence of such designation, regular meetings shall be held at the principal executive office of the corporation. Special meetings of the board shall be held at any place within or without the State of Delaware that has been designated in the notice of the meeting or, if not stated in the notice or there is no notice, at the principal executive office of the corporation. Any meeting, regular or special, may be held by conference telephone or similar communication equipment, so long as all directors participating in such meeting can hear one another, and all such directors shall be deemed to be present in person at such meeting.

Section 6. Annual Meetings. Immediately following each annual meeting of stockholders, the board of directors shall hold a regular meeting for the purpose of organization, any desired election of officers and transaction of other business. Notice of this meeting shall not be required.

Section 7. Other Regular Meetings. Other regular meetings of the board of directors shall be held at such time as shall from time to time be determined by the board of directors. Such regular meetings may be held without notice provided that notice of any change in the determination of time of such meeting

shall be sent to all of the directors. Notice of a change in the determination of the time shall be given to each director in the same manner as for special meetings of the board of directors.

Section 8. Special Meetings. Special meetings of the board of directors for any purpose or purposes may be called at any time by the chairman of the board or the president or any vice president or the secretary or any two directors.

Notice of the time and place of special meetings shall be delivered personally or by telephone to each director or sent by facsimile, first-class mail or telegram, charges prepaid, addressed to each director at his or her address as it is shown upon the records of the corporation. In case such notice is mailed, it shall be deposited in the United States mail at least four (4) days prior to the time of the holding of the meeting. In case such notice is delivered personally, by telephone, facsimile or telegram, it shall be delivered personally, or by telephone, by facsimile or to the telegraph company at least twenty-four (24) hours prior to the time of the holding of the meeting. Any oral notice given personally or by telephone may be communicated to either the director or to a person at the office of the director who the person giving the notice has reason to believe will promptly communicate it to the director. The notice need not specify the purpose of the meeting nor the place if the meeting is to be held at the principal executive office of the corporation.

Section 9. Quorum. A majority of the authorized number of directors shall constitute a quorum for the transaction of business, except to adjourn as hereinafter provided. Every act or decision done or made by a majority of the directors present at a meeting duly held at which a quorum is present shall be regarded as the act of the board of directors. A meeting at which a quorum is initially present may continue to transact business notwithstanding the withdrawal of directors, if any action taken is approved by at least a majority of the required quorum for such meeting.

Section 10. Waiver of Notice. The transactions of any meeting of the board of directors, however called and noticed or wherever held, shall be as valid as though had at a meeting duly held after regular call and notice if a quorum be present and if, either before or after the meeting, each of the directors not present signs a written waiver of notice, a consent to holding the meeting or an approval of the minutes thereof. The waiver of notice or consent need not specify the purpose of the meeting. All such waivers, consents and approvals shall be filed with the corporate records or made a part of the minutes of the meeting. Notice of a meeting shall also be deemed given to any director who attends the meeting without protesting, prior thereto or at its commencement, the lack of notice to such director.

Section 11. Adjournment. A majority of the directors present, whether or not constituting a quorum, may adjourn any meeting to another time and place.

Section 12. Notice of Adjournment. Notice of the time and place of an adjourned meeting need not be given, unless the meeting is adjourned for more than twenty-four (24) hours, in which case notice of such time and place shall be given prior to the time of the adjourned meeting, in the manner specified in Section 8 of this Article III, to the directors who were not present at the time of the adjournment.

Section 13. Action Without Meeting. Any action required or permitted to be taken by the board of directors may be taken without a meeting, if all members of the board shall individually or collectively consent in writing to such action. Such action by written consent shall have the same force and effect as a unanimous vote of the board of directors. Such written consent or consents shall be filed with the minutes of the proceedings of the board.

Section 14. Fees and Compensation of Directors. Directors and members of committees may receive such compensation, if any, for their services and such reimbursement of expenses, as may be fixed or determined by resolution of the board of directors. Nothing herein contained shall be construed to preclude any director from serving the corporation in any other capacity as an officer,

agent, employee, or otherwise, and receiving compensation for such services.

ARTICLE IV

COMMITTEES

Section 1. Committees of Directors. The board of directors may, by resolution adopted by a majority of the authorized number of directors, designate one or more committees, including an executive committee, each consisting of two or more directors, to serve at the pleasure of the board. The board may designate one or more directors as alternate members of any committee, who may replace any absent member at any meeting of the committee. Any such committee, to the extent provided in the resolution of the board, shall have all the authority of the board, except with respect to:

(a) the approval of any action which, under the General Corporation Law of Delaware, also requires the approval of the full board of directors, or the stockholders of the outstanding shares;

(b) the filling of vacancies on the board of directors or in any committee;

(c) the fixing of compensation of the directors for serving on the board or on any committee;

(d) the amendment or repeal of bylaws or the adoption of new bylaws;

(e) the amendment or repeal of any resolution of the board of directors which by its express terms is not so amendable or repealable;

(f) a distribution to the stockholders of the corporation, except at a rate or in a periodic amount or within a price range determined by the board of directors; or

(g) the appointment of any other committees of the board of directors or the members thereof.

Section 2. Meetings and Action of Committees. Meetings and action of committees shall be governed by, and held and taken in accordance with, the provisions of Article III of these bylaws, Sections 5 (place of meetings), 7 (regular meetings), 8 (special meetings and notice), 9 (quorum), 10 (waiver of notice), 11 (adjournment), 12 (notice of adjournment) and 13 (action without meetings), with such changes in the context of those bylaws as are necessary to substitute the committee and its members for the board of directors and its members, except that the time of regular meetings of committees may be determined by resolution of the board of directors as well as the committee, special meetings of committees may also be called by resolution of the board

of directors, and notice of special meetings of committees shall also be given to all alternate members, who shall have the right to attend all meetings of the committee. The board of directors may adopt rules for the government of any committee not inconsistent with the provisions of these bylaws.

ARTICLE V

OFFICERS

Section 1. Officers. The officers of the corporation shall be chosen by the board of directors and shall include a chairman of the board or president, or both, a vice president, a secretary and a chief financial officer. The corporation may also have, at the discretion of the board of directors, a president, one or more additional vice presidents, one or more assistant secretaries, one or more assistant treasurers, and such other officers as may be held by the same person.

Section 2. Election of Officers. The officers of the corporation, except such officers as may be appointed in accordance with the provisions of Section 3 or Section 5 of this Article V, shall be chosen annually by the board

of directors, and each shall hold his office until he shall resign or be removed or otherwise disqualified to serve or his successor shall be appointed in accordance with the provisions of Section 3 of this Article V. Any number of officers may be elected and qualified.

Section 3. Subordinate Officers, etc. The board of directors may appoint, and may empower the chairman of the board to appoint, such other officers as the business of the corporation may require, each of whom shall hold office for such period, have such authority and perform such duties as are provided in the bylaws or as the board of directors may from time to time determine.

Section 4. Removal and Resignation of Officers. Any officer may be removed, either with or without cause, by the board of directors, at any regular or special meeting thereof, or, except in case of an officer chosen by the board of directors, by any officer upon whom such power of removal may be conferred by the board of directors.

Any officer may resign at any time by giving written notice to the corporation. Any such resignation shall take effect at the date of the receipt of such notice or at any later time specified therein; and, unless otherwise specified therein, the acceptance of such resignation shall not be necessary to make it effective.

Section 5. Vacancies in Office. A vacancy in any office because of death, resignation, removal, disqualification, or any other cause shall be filled in the manner prescribed in these bylaws for regular appointments to such office.

Section 6. Chairman of the Board. The chairman of the board shall preside at all meetings of the stockholders and of the board of directors. The chairman of the Board shall be responsible for the general management of the affairs of the corporation and shall perform all

duties incidental to his office which may be required by law and all such other duties as are properly required of him by the board of directors. Except where by law the signature of the president is required, the chairman of the board shall possess the same power as the president to sign all certificates, contracts, and other instruments of the corporation which may be authorized by the board of directors. He shall make reports to the board of directors and the stockholders, and shall perform all such other duties as are properly required of him by the board of directors. He shall see that all orders and resolutions of the board of directors and of any committee thereof are carried into effect.

Section 7. President. The president shall act in a general executive capacity and shall assist the chairman of the board in the administration and operation of the corporation's business and general supervision of its policies and affairs. The president shall, in the absence of or because of the inability to act of the chairman of the board, perform all duties of the chairman of the board and preside at all meetings of stockholders and of the board of directors. The president may sign, alone or with the secretary, or an assistant secretary, or any other proper officer of the corporation authorized by the board of directors, certificates, contracts, and other instruments of the corporation as authorized by the board of directors.

Section 8. Vice Presidents. In the absence or disability of the president, a vice president designated by the board of directors shall perform all the duties of the president, and when so acting shall have all the powers of, and be subject to all the restrictions upon, the president. The vice presidents shall have such other powers and perform such other duties as form time to time may be prescribed for them respectively by the board of directors or the bylaws.

Section 9. Secretary. The secretary shall keep or cause to be kept, at the principal executive office or such other place as the board of directors may order, a book of minutes of all meetings and actions of directors, committees of directors and stockholders, with the time and place of holding, whether regular or special, and, if special, how authorized, the notice thereof given, the names of those present at directors' and committee meetings, the number of shares present or represented at stockholders' meetings, and the proceedings thereof.

The secretary shall keep, or cause to be kept, at the principal executive office or at the office of the corporation's transfer agent or registrar, as determined by resolution of the board of directors, a stock register, or a duplicate register, showing the names of all stockholders and their addresses, the number and classes of shares held by each, the number and date of certificates issued for the same, and the number and date of cancellation of every certificate surrendered for cancellation.

The secretary shall give, or cause to be given, notice of all meetings of the stockholders and of the board of directors required by the bylaws or by law to be given, and he shall keep the seal of the corporation in safe custody, and shall have such other powers and perform such other duties as may be prescribed by the board of directors or by the bylaws.

Section 10. Chief Financial Officer. The chief financial officer shall keep and maintain, or cause to be kept and maintained, adequate and correct books and records of accounts

of the properties and business transactions of the corporation, including accounts of its assets, liabilities, receipts, disbursements, gains, losses, capital, retained earnings and shares. The books of account shall be open at all reasonable times to inspection by any director.

The chief financial officer shall deposit all monies and other valuables in the name and to the credit of the corporation with such depositories as may be designated by the board of directors. The chief financial officer shall disburse the funds of the corporation as may be ordered by the board of directors, shall render to the chairman of the board and directors, whenever they request it, an account of all of his transactions as chief financial officer and of the financial condition of the corporation, and shall have other powers and perform such other duties as may be prescribed by the board of directors or the bylaws.

Section 11. Assistant Secretaries and Assistant Treasurers. Any assistant secretary may perform any act within the power of the secretary, and any assistant treasurer may perform any act within the power of the chief financial officer, subject to any limitations which may be imposed in these bylaws or in board resolutions.

ARTICLE VI

INDEMNIFICATION OF DIRECTORS, OFFICERS, EMPLOYEES AND OTHER AGENTS

Section 1. Indemnification. The corporation shall indemnify, in the manner and to the full extent permitted by law, any person (or the estate of any person) who was or is a party to, or is threatened to be made a party to, any threatened, pending or completed action, suit or proceeding, whether or not by or in the right of the corporation, and whether civil, criminal, administrative, investigative or otherwise, by reason of the fact that such person is a director or officer of the corporation, and at the discretion of the board of directors may indemnify any person (or the estate of any person) who is such a party or threatened to be made such a party by reason of the fact that such person is or was an employee or agent of the corporation or is or was serving at the request of the corporation as a director, officer, employee or agent of another corporation, partnership, joint venture, trust or other enterprise. The corporation may, to the full extent permitted by law, purchase and maintain insurance on behalf of any such person against any liability which may be asserted against him and may enter into contracts providing for the indemnification of such person to the full extent permitted by law. To the full extent permitted by law, the indemnification provided herein shall include expenses (including attorneys' fees), judgments, fines and amounts paid in settlement, and, in the manner provided by law, any such expenses may be paid by the corporation in advance of the final disposition of such action, suit or proceeding. The indemnification provided herein shall not be deemed to limit the right of the corporation to indemnify any other person for any such expenses to the full extent permitted by law, nor shall it be deemed exclusive of any other rights to which any person seeking indemnification from the corporation may be entitled under any agreement, vote of stockholders or disinterested directors or otherwise, both as to action in his official capacity and as to action in

another capacity while holding such office.

For the purposes of this Article V1, references to "the corporation" shall include, in addition to the resulting corporation, any constituent corporation (including any constituent of a constituent) absorbed in a consolidation or merger which, if its separate existence had continued, would have had power and authority to indemnify its directors or officers so that any person who is or was a director or officer of such constituent corporation, or is or was serving at the request of such constituent corporation as a director or officer of another corporation, partnership, joint venture, trust or other enterprise, shall stand in the same position under the provisions of this Article VI with respect to the resulting or surviving corporation as he would have with respect to such constituent corporation if its separate existence had continued.

For purposes of this Article VI, references to "other enterprises" shall include employee benefit plans; references to "fines" shall include any excise taxes assessed on a person with respect to an employee benefit plan; and references to "serving at the request of the corporation" shall include service as a director or officer of the corporation which imposes duties on, or involves services by, such director or officer with respect to an employee benefit plan, its participants or beneficiaries; and a person who acted in good faith and in a manner he reasonably believed to be in the interest of the participants and beneficiaries of an employee benefit plan shall be deemed to have acted in a manner "not opposed to the best interests of the corporation" as referred to in this section.

ARTICLE VII

GENERAL CORPORATE MATTERS

Section 1. Record Date for Purposes Other Than Notice and Voting. For purposes of determining the stockholders entitled to receive payment of any dividend or other distribution or allotment of any rights or entitled to exercise any rights in respect of any other lawful action, the board of directors may fix, in advance, a record date, which date shall not precede the date upon which the resolution fixing the record date is adopted by the board of directors, and which shall not be more than sixty (60) nor less than ten (10) days prior to any such action, and in such case only stockholders of record on the date so fixed are entitled to receive the dividend, distribution or allotment of rights or to exercise the rights, as the case may be, notwithstanding any transfer of any shares on the books of the corporation after the record date fixed as aforesaid, except as otherwise provided in the Delaware General Corporation Law.

A determination of stockholders of record entitled to notice of or to vote at a meeting of stockholders shall apply to any adjournment of the meeting; provided, however, that the board of directors may fix a new record date for the adjourned meeting. In order that the corporation may determine the stockholders entitled to consent to corporate action in writing without a meeting, the board of directors may fix a record date which shall not be more than ten days after the date upon which the resolution fixing the record date is adopted by the board of directors.

Section 2. Checks, Drafts, Evidences of Indebtedness. All checks, drafts or other orders for payment of money, notes or other evidences of indebtedness, issued in the name of or

payable to the corporation shall be signed or endorsed by such person or persons and in such manner as, from time to time, shall be determined by resolution of the board of directors.

Section 3. Corporate Contracts and Instruments, How Executed. The board of directors, except as otherwise provided in these bylaws, may authorize any officer or officers, agent or agents, to enter into any contract or execute any instrument in the name of and on behalf of the corporation, and such authority may be general or confined to specific instances; and, unless so authorized or

ratified by the board of directors or within the agency power of an officer, no officer, agent or employee shall have any power or authority to bind the corporation by any contract or engagement or to pledge its credit or to render it liable for any purpose or to any amount.

Section 4. Stock Certificates. A certificate or certificates for shares of the capital stock of the corporation shall be issued to each stockholder when any such shares are fully paid. All certificates shall be signed in the name of the corporation by the chairman of the board or the president or vice president and by the chief financial officer, the treasurer or an assistant treasurer or the secretary or any assistant secretary, certifying the number of shares and the class or series of shares owned by the stockholder. Any or all of the signatures on the certificate may be facsimile. In case any officer, transfer agent or registrar who has signed or whose facsimile signature has been placed upon a certificate shall have ceased to be such officer, transfer agent or registrar before such certificate is issued, it may be issued by the corporation with the same effect as if such person were an officer, transfer agent or registrar at the date of issue.

Section 5. Lost Certificates. Except as hereinafter in this Section 5 provided, no new stock certificate shall be issued in lieu of an old certificate unless the latter is surrendered to the corporation and canceled at the same time. The board of directors may in case any stock certificate or certificate for any other security is lost, stolen or destroyed, authorize the issuance of a new certificate in lieu thereof, upon such terms and conditions as the board of directors may require, including provision for indemnification of the corporation secured by a bond or other adequate security sufficient to protect the corporation against any claim that may be made against it, including any expense or liability, on account of the alleged loss, theft or destruction of such certificate or the issuance of such new certificate.

Section 6. Representation of Stock of Other Corporations. The chairman of the board, the president, or any vice president, or any other person authorized by resolution of the board of directors by any of the foregoing designated officers, is authorized to vote on behalf of the corporation any and all stock of any other corporation or corporations, foreign or domestic, standing in the name of the corporation. The authority herein granted to said officers to vote or represent on behalf of the corporation any and all stock by the corporation in any other corporation or corporations may be exercised by any such officer in person or by any person authorized to do so by proxy duly executed by said officer.

Section 7. Construction and Definitions. Unless the context requires otherwise, the general provisions, rules of construction, and definitions in the Delaware General Corporation Law shall govern the construction of the bylaws. Without limiting the generality of the foregoing,

the singular number includes the plural, the plural number includes the singular, and the term "person" includes both a corporation and a natural person.

Section 8. Fiscal Year. The fiscal year of the corporation shall be fixed by resolution of the board of directors.

ARTICLE VIII

AMENDMENTS

Section 1. Amendment. The bylaws, or any of them, may be rescinded, altered, amended or repealed, and new bylaws may be made (i) by the board of directors, by vote of a majority of the number of directors then in office as directors, acting at any meeting of the board of directors, or (ii) by the stockholders, by the vote of the holders of sixty-six and two-thirds percent (66-2/3%) of the outstanding voting stock of the corporation, at any annual or special meeting of stockholders, provided that notice of such proposed amendment, modification, repeal or adoption is given in the notice of the annual or special meeting; provided, however, that the bylaws can only be amended if such amendment would not conflict with the certificate of incorporation. Any bylaw made or altered by the requisite number of stockholders may be altered or repealed by the board of directors or may be altered or repealed by the

requisite number of stockholders.

* * * *

CERTIFICATE OF SECRETARY

I, the undersigned, do hereby certify:

(a) That I am the duly elected and acting Secretary of Capstone Turbine Corporation, a Delaware corporation (the "Corporation"); and

(b) That the foregoing Second Amended and Restated Bylaws constitute the Second Amended and Restated Bylaws of the Corporation, as duly adopted by the Board of Directors of the Corporation at a meeting duly held on January 30, 2003.

IN WITNESS WHEREOF, I have hereunto subscribed my name as of this 14th day of February, 2003.

/s/ Susan Cayley
- ----------------
Susan Cayley,
Secretary

EXHIBIT 10.4

CAPSTONE TURBINE CORPORATION

AMENDED AND RESTATED 2000 EQUITY INCENTIVE PLAN

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CAPSTONE TURBINE CORPORATION

AMENDED AND RESTATED 2000 EQUITY INCENTIVE PLAN

1. Purposes of the Plan. The purposes of the Capstone Turbine Corporation Amended and Restated 2000 Equity Incentive Plan are to attract and retain the best available personnel for positions of substantial responsibility, to provide additional incentive to Employees, Directors and Consultants and to promote the success of the Company's business. Options granted under the Plan may be Incentive Stock Options or Non-Qualified Stock Options, as determined by the Administrator at the time of grant. Stock Purchase Rights and Stock Bonuses may also be granted under the Plan.

2. Definitions. As used herein, the following definitions shall apply:

(a) "Acquisition" means (i) any consolidation or merger of the Company with or into any other corporation or other entity or person in which the stockholders of the Company prior to such consolidation or merger own less than fifty percent (50%) of the Company's voting power immediately after such consolidation or merger, excluding any consolidation or merger effected exclusively to change the domicile of the Company; or (ii) a sale of all or substantially all of the assets of the Company.

(b) "Administrator" means the Board or the Committee responsible for conducting the general administration of the Plan, as applicable, in accordance with Section 4 hereof.

(c) "Applicable Laws" means the requirements relating to the administration of stock option plans under U.S. state corporate laws, U.S. federal and state securities laws, the Code, any stock exchange or quotation system on which the Common Stock is listed or quoted and the applicable laws of any foreign country or jurisdiction where Options, Stock Purchase Rights or Stock Bonuses are granted under the Plan.

(d) "Board" means the Board of Directors of the Company.

(e) "Cause" means (i) with respect to a Holder who is an Employee, and whose employment contract expressly provides for termination of such Holder in certain specified circumstances constituting "cause", those circumstances that constitute "cause" under such Holder's employment contract; (ii) with respect to a Holder who is an Employee, but who does not have an employment contract or whose employment contract does not expressly provide for termination of such Holder in certain specified circumstances constituting "cause", (A) the commission of any act by such Holder involving fraud, embezzlement or a felony, (B) the commission of any act by such Holder constituting financial dishonesty against the Company or its Parent or any of its Subsidiaries, (C) repeated and gross dereliction of duty to the Company or its Parent or any of its Subsidiaries to which such Holder's duties extend, (D) an act involving moral turpitude which (1) brings the Company or its Parent or any of its Subsidiaries into public

disrepute or disgrace, or (2) causes material injury to the customer relations, operations or the business prospects of the Company or its Parent or any of its Subsidiaries, (E) the breach by such Holder of any of such Holder's obligations under such Holder's employee or employment agreement with the Company or its Parent or any of its Subsidiaries, or (F) the refusal or failure of such Holder to follow the lawful directives of the Board, the President and Chief Executive Officer of the Company or his designee or such Holder's supervisor; and (iii) with respect to a Holder who is a Director, (A) the commission of any act by such Holder involving fraud, embezzlement or a felony, (B) the commission of any act by such Holder constituting financial dishonesty against the Company or its Parent or any of its Subsidiaries, (C) repeated and gross dereliction of duty to the Company or its Parent or any of its Subsidiaries to which such Holder's duties extend, (D) an act involving moral turpitude which (1) brings the Company or its Parent or any of its Subsidiaries into public disrepute or disgrace, or (2) causes material injury to the customer relations, operations or the business prospects of the Company or its Parent or any of its Subsidiaries.

(f) "Code" means the Internal Revenue Code of 1986, as amended, or any successor statute or statutes thereto. Reference to any particular Code section shall include any successor section.

(g) "Committee" means a committee appointed by the Board in accordance with Section 4 hereof.

(h) "Common Stock" means the Common Stock of the Company, par value $0.001 per share.

(i) "Company" means Capstone Turbine Corporation, a Delaware corporation.

(j) "Consultant" means any consultant or adviser if: (i) the consultant or adviser renders bona fide services to the Company; (ii) the services rendered by the consultant or adviser are not in connection with the offer or sale of securities in a capital-raising transaction and do not directly or indirectly promote or maintain a market for the Company's securities; and (iii) the consultant or adviser is a natural person who has contracted directly with the Company to render such services.

(k) "Director" means a member of the Board.

(l) "Employee" means any person, including an Officer or Director, who is an employee (as defined in accordance with Section 3401(c) of the Code) of the Company or any Parent or Subsidiary of the Company. A Service Provider shall not cease to be an Employee in the case of (i) any leave of absence approved by the Company or (ii) transfers between locations of the

Company or between the Company, its Parent, any Subsidiary, or any successor. For purposes of Incentive Stock Options, no such leave may exceed ninety (90) days, unless reemployment upon expiration of such leave is guaranteed by statute or contract. Neither service

as a Director nor payment of a director's fee by the Company shall be sufficient, by itself, to constitute "employment" by the Company.

(m) "Exchange Act" means the Securities Exchange Act of 1934, as amended, or any successor statute or statutes thereto. Reference to any particular Exchange Act section shall include any successor section.

(n) "Fair Market Value" means, as of any date, the value of a share of Common Stock determined as follows:

(i) If the Common Stock is listed on any established stock exchange or a national market system, including, without limitation, the Nasdaq National Market or The Nasdaq SmallCap Market of The Nasdaq Stock Market, its Fair Market Value shall be the closing sales price for a share of such stock (or the closing bid, if no sales were reported) as quoted on such exchange or system for the last market trading day prior to the time of determination, as reported in The Wall Street Journal or such other source as the Administrator deems reliable;

(ii) If the Common Stock is regularly quoted by a recognized securities dealer but selling prices are not reported, its Fair Market Value shall be the mean between the high bid and low asked prices for a share of the Common Stock on the last market trading day prior to the day of determination; or

(iii) In the absence of an established market for the Common Stock, the Fair Market Value thereof shall be determined in good faith by the Administrator.

(o) "Holder" means a person who has been granted or awarded an Option or Stock Purchase Right or who holds Shares acquired pursuant to the exercise of an Option or Stock Purchase Right or pursuant to a Stock Bonus.

(p) "Incentive Stock Option" means an Option intended to qualify as an incentive stock option within the meaning of Section 422 of the Code and which is designated as an Incentive Stock Option by the Administrator.

(q) "Independent Director" means a Director who is not an Employee of the Company.

(r) "Non-Qualified Stock Option" means an Option (or portion thereof) that is not designated as an Incentive Stock Option by the Administrator, or which is designated as an Incentive Stock Option by the Administrator but fails to qualify as an incentive stock option within the meaning of Section 422 of the Code.

(s) "Officer" means a person who is an officer of the Company within the meaning of Section 16 of the Exchange Act and the rules and regulations promulgated thereunder.

(t) "Option" means a stock option granted pursuant to the Plan.

(u) "Option Agreement" means a written agreement between the Company and a Holder evidencing the terms and conditions of an individual Option grant. The Option Agreement is subject to the terms and conditions of the Plan.

(v) "Option Exchange Program" means a program whereby outstanding Options are surrendered or cancelled in exchange for Options of the same type (which may have a lower exercise price or purchase price), of a different type and/or cash.

(w) "Parent" means any corporation, whether now or hereafter existing (other than the Company), in an unbroken chain of corporations ending with the Company if each of the corporations other than the last corporation in the unbroken chain owns stock possessing more than fifty percent of the total combined voting power of all classes of stock in one of the other corporations in such chain.

(x) "Plan" means the Capstone Turbine Corporation Amended and Restated 2000 Equity Incentive Plan.

(y) "Public Trading Date" means the first date upon which Common Stock of the Company is listed (or approved for listing) upon notice of issuance on any securities exchange or designated (or approved for designation) upon notice of issuance as a national market security on an interdealer quotation system.

(z) "Restricted Stock" means Shares acquired pursuant to the exercise of an unvested Option in accordance with Section 10(h) below or pursuant to a Stock Purchase Right granted under Section 14 below.

(aa) "Rule 16b-3" means that certain Rule 16b-3 under the Exchange Act, as such Rule may be amended from time to time.

(bb) "Section 16(b)" means Section 16(b) of the Exchange Act, as such Section may be amended from time to time.

(cc) "Securities Act" means the Securities Act of 1933, as amended, or any successor statute or statutes thereto. Reference to any particular Securities Act section shall include any successor section.

(dd) "Service Provider" means an Employee, Director or Consultant.

(ee) "Share" means a share of Common Stock, as adjusted in accordance with Section 15 below.

(ff) "Stock Bonus" means a grant of Common Stock granted pursuant to Section 14(e) of the Plan.

(gg) "Stock Purchase Right" means a right to purchase Common Stock pursuant to Section 14 below or the right to receive a bonus of Common Stock for past services.

(hh) "Subsidiary" means any corporation, whether now or hereafter existing (other than the Company), in an unbroken chain of corporations beginning with the Company if each of the corporations other than the last corporation in the unbroken chain owns stock possessing more than fifty percent of the total combined voting power of all classes of stock in one of the other corporations in such chain.

3. Stock Subject to the Plan. Subject to the provisions of Section 15 of the Plan, the shares of stock subject to Options, Stock Purchase Rights or Stock Bonuses shall be Common Stock, initially shares of the Company's Common Stock, par value $0.001 per share. Subject to the provisions of Section 15 of the Plan, the maximum aggregate number of Shares which may be issued upon exercise of such Options or Stock Purchase Rights or pursuant to such Stock Bonuses is six million two hundred thousand (6,200,000) Shares, plus the number of Shares previously authorized and remaining available under the Company's 1993 Stock Incentive Plan, as amended, as of the Public Trading Date, plus any Shares covered by options granted under the Company's 1993 Stock Incentive Plan that are forfeited or expire unexercised or otherwise become available after the Public Trading Date; provided, however, that the maximum aggregate number of Shares which may be issued upon exercise of Incentive Stock Options is three million seven hundred thousand (3,700,000) Shares. Shares issued upon exercise of Options or Stock Purchase Rights or pursuant to Stock Bonuses may be authorized but unissued, or reacquired Common Stock. If an Option or Stock Purchase Right expires or becomes unexercisable without having been exercised in full, or is surrendered pursuant to an Option Exchange Program, the unpurchased Shares which were subject thereto shall become available for future grant or

sale under the Plan (unless the Plan has terminated). Shares which are delivered by the Holder or withheld by the Company upon the exercise of an Option or Stock Purchase Right or in respect of a Stock Bonus under the Plan, in payment of the exercise price thereof or tax withholding thereon, may again be optioned, granted or awarded hereunder, subject to the limitations of this Section 3. If Shares of Restricted Stock are repurchased by the Company at their original purchase price, such Shares shall become available for future grant under the Plan. Notwithstanding the provisions of this Section 3, no Shares may again be optioned, granted or awarded if such action would cause an Incentive Stock Option to fail to qualify as an Incentive Stock Option under Code Section 422.

4. Administration of the Plan.

(a) Administrator. Unless and until the Board delegates administration to a Committee as set forth below, the Plan shall be administered by the Board. The Board may delegate administration of the Plan to a Committee or Committees of one or more members of the Board, and the term "Committee" shall apply to any person or persons to whom such authority has been delegated. If administration is delegated to a Committee, the Committee shall have, in connection with the administration of the Plan, the powers theretofore possessed by the Board, including the power to delegate to a subcommittee any of the administrative powers the

Committee is authorized to exercise (and references in this Plan to the Board shall thereafter be to the Committee or subcommittee), subject, however, to such resolutions, not inconsistent with the provisions of the Plan, as may be adopted from time to time by the Board. Notwithstanding the foregoing, however, from and after the Public Trading Date, a Committee of the Board shall administer the Plan and the Committee shall consist solely of two or more Independent Directors each of whom is both an "outside director," within the meaning of Section 162(m) of the Code, and a "non-employee director" within the meaning of Rule 16b-3. Within the scope of such authority, the Board or the Committee may (i) delegate to a committee of one or more members of the Board who are not Independent Directors the authority to grant awards under the Plan to eligible persons who are either (1) not then "covered employees," within the meaning of Section 162(m) of the Code and are not expected to be "covered employees" at the time of recognition of income resulting from such award or (2) not persons with respect to whom the Company wishes to comply with Section 162(m) of the Code and/or (ii) delegate to a committee of one or more members of the Board who are not "non-employee directors," within the meaning of Rule 16b-3, the authority to grant awards under the Plan to eligible persons who are not then subject to Section 16 of the Exchange Act. The Board may abolish the Committee at any time and revest in the Board the administration of the Plan. Appointment of Committee members shall be effective upon acceptance of appointment. Committee members may resign at any time by delivering written notice to the Board. Vacancies in the Committee may only be filled by the Board.

(b) Powers of the Administrator. Subject to the provisions of the Plan and the specific duties delegated by the Board to such Committee, and subject to the approval of any relevant authorities, the Administrator shall have the authority in its sole discretion:

(i) to determine the Fair Market Value;

(ii) to select the Service Providers to whom Options, Stock Purchase Rights, and Stock Bonuses may from time to time be granted hereunder;

(iii) to determine the number of Shares to be covered by each such award granted hereunder;

(iv) to approve forms of agreement for use under the Plan;

(v) to determine the terms and conditions of any award granted hereunder (such terms and conditions include, but are not limited to, the exercise price, the time or times when Options or Stock Purchase Rights may vest or be exercised (which may be based on performance criteria), any vesting acceleration or waiver of forfeiture restrictions, and any restriction or limitation regarding any award granted hereunder or the Common Stock relating

thereto, based in each case on such factors as the Administrator, in its sole discretion, shall determine);

(vi) to reduce the exercise price of any Option or Stock Purchase Right to the then current Fair Market Value if the Fair Market Value of the Common Stock covered by such Option or Stock Purchase Right shall have declined since the date the Option or Stock Purchase Right was granted;

(vii) to institute an Option Exchange Program;

(viii) to determine whether to offer to buyout a previously granted Option as provided in subsection 10(i) and to determine the terms and conditions of such offer and buyout (including whether payment is to be made in cash or Shares);

(ix) to prescribe, amend and rescind rules and regulations relating to the Plan, including rules and regulations relating to sub-plans established for the purpose of qualifying for preferred tax treatment under foreign tax laws;

(x) to allow Holders to satisfy withholding tax obligations by electing to have the Company withhold from the Shares to be issued upon exercise of an Option or Stock Purchase Right or pursuant to a Stock Bonus that number of Shares having a Fair Market Value equal to the minimum amount required to be withheld based on the statutory withholding rates for federal and state tax purposes that apply to supplemental taxable income. The Fair Market Value of the Shares to be withheld shall be determined on the date that the amount of tax to be withheld is to be determined. All elections by Holders to have Shares withheld for this purpose shall be made in such form and under such conditions as the Administrator may deem necessary or advisable;

(xi) to amend the Plan or any Option or Stock Purchase Right granted under the Plan as provided in Section 17; and

(xii) to construe and interpret the terms of the Plan and awards granted pursuant to the Plan and to exercise such powers and perform such acts as the Administrator deems necessary or desirable to promote the best interests of the Company which are not in conflict with the provisions of the Plan.

(c) Effect of Administrator's Decision. All decisions, determinations and interpretations of the Administrator shall be final and binding on all Holders.

5. Eligibility. Non-Qualified Stock Options, Stock Purchase Rights and Stock Bonuses may be granted to Service Providers. Incentive Stock Options may be granted only to Employees. If otherwise eligible, an Employee or Consultant who has been granted an Option, Stock Purchase Right or Stock Bonus may be granted additional Options, Stock Purchase Rights or Stock Bonuses. In addition to the foregoing, each Independent Director shall be eligible to be granted Options at the times and in the manner set forth in Section 12.

6. Limitations.

(a) Each Option shall be designated by the Administrator in the Option Agreement as either an Incentive Stock Option or a Non-Qualified Stock Option. However, notwithstanding such designations, to the extent that the aggregate Fair Market Value of Shares subject to a Holder's Incentive Stock Options and other incentive stock options granted by the Company, any Parent or Subsidiary, which become exercisable for the first time during any calendar year (under all plans of the Company or any Parent or Subsidiary) exceeds $100,000, such excess Options or other options shall be treated as Non-Qualified Stock Options.

For purposes of this Section 6(a), Incentive Stock Options shall be taken into account in the order in which they were granted, and the Fair Market Value of the Shares shall be determined as of the time of grant.

(b) None of the Plan, any Option, Stock Purchase Right or Stock Bonus shall confer upon a Holder any right with respect to continuing the Holder's employment or consulting relationship with the Company, nor shall they interfere in any way with the Holder's right or the Company's right to terminate such employment or consulting relationship at any time, with or without cause.

(c) No Service Provider shall be granted, in any calendar year, Options, Stock Purchase Rights or Stock Bonuses to acquire more than three million (3,000,000) Shares. The foregoing limitation shall be adjusted proportionately in connection with any change in the Company's capitalization as described in Section 15. For purposes of this Section 6(c), if an Option is canceled in the same calendar year it was granted (other than in connection with a transaction described in Section 15), the canceled Option will be counted against the limit set forth in this Section 6(c). For this purpose, if the exercise price of an Option is reduced, the transaction shall be treated as a cancellation of the Option and the grant of a new Option.

7. Term of Plan. The Plan shall become effective upon its initial adoption by the Board and shall continue in effect until it is terminated under Section 17 of the Plan. No Options, Stock Purchase Rights or Stock Bonuses may be issued under the Plan after the tenth (10th) anniversary of the earlier of (i) the date upon which the Plan is adopted by the Board or (ii) the date the Plan is approved by the stockholders.

8. Term of Option. The term of each Option shall be stated in the Option Agreement; provided, however, that the term shall be no more than ten (10) years from the date of grant thereof. In the case of an Incentive Stock Option granted to a Holder who, at the time the Option is granted, owns (or is treated as owning under Code Section 424) stock representing more than ten percent (10%) of the voting power of all classes of stock of the Company or any Parent or Subsidiary, the term of the Option shall be five (5) years from the date of grant or such shorter term as may be provided in the Option Agreement.

9. Option Exercise Price and Consideration.

(a) Except as provided in Section 13, the per share exercise price for the Shares to be issued upon exercise of an Option shall be such price as is determined by the Administrator, but shall be subject to the following:

(i) In the case of an Incentive Stock Option

(A) granted to an Employee who, at the time of grant of such Option, owns (or is treated as owning under Code Section 424) stock representing more than ten percent (10%) of the voting power of all classes of stock of the Company or any Parent or Subsidiary, the per Share exercise price shall be no less than one hundred ten percent (110%) of the Fair Market Value per Share on the date of grant.

(B) granted to any other Employee, the per Share exercise price shall be no less than one hundred percent (100%) of the Fair Market Value per Share on the date of grant.

(ii) In the case of a Non-Qualified Stock Option

(A) granted to a Service Provider who, at the time of grant of such Option, owns stock representing more than ten percent (10%) of the voting power of all classes of stock of the Company or any Parent or Subsidiary, the exercise price shall be no less than one hundred ten percent (110%) of the Fair Market Value per Share on the date of the grant.

(B) granted to any other Service Provider, the per Share exercise price shall be no less than eighty-five percent (85%) of the Fair Market Value per Share on the date of grant.

(iii) Notwithstanding the foregoing, Options may be granted with a per Share exercise price other than as required in this subsection (a) above pursuant to a merger or other corporate transaction.

(b) The consideration to be paid for the Shares to be issued

upon exercise of an Option, including the method of payment, shall be determined by the Administrator (and, in the case of an Incentive Stock Option, shall be determined at the time of grant). Such consideration may consist of (1) cash, (2) check, (3) with the consent of the Administrator, a full recourse promissory note bearing interest (at no less than such rate as shall then preclude the imputation of interest under the Code) and payable upon such terms as may be prescribed by the Administrator, (4) with the consent of the Administrator, other Shares which (x) in the case of Shares acquired from the Company, have been owned by the Holder for more than six (6) months on the date of surrender, and (y) have a Fair Market Value on the date of surrender equal to the aggregate exercise price of the

Shares as to which such Option shall be exercised, (5) with the consent of the Administrator, surrendered Shares then issuable upon exercise of the Option having a Fair Market Value on the date of exercise equal to the aggregate exercise price of the Option or exercised portion thereof, (6) with the consent of the Administrator, property of any kind which constitutes good and valuable consideration, (7) with the consent of the Administrator, delivery of a notice that the Holder has placed a market sell order with a broker with respect to Shares then issuable upon exercise of the Options and that the broker has been directed to pay a sufficient portion of the net proceeds of the sale to the Company in satisfaction of the Option exercise price, provided, that payment of such proceeds is then made to the Company upon settlement of such sale, or (8) with the consent of the Administrator, any combination of the foregoing methods of payment.

10. Exercise of Option.

(a) Vesting; Fractional Exercises. Except as provided in Section 13, Options granted hereunder shall be vested and exercisable according to the terms hereof at such times and under such conditions as determined by the Administrator and set forth in the Option Agreement; provided, however, that, except with regard to Options granted to Officers, Directors or Consultants, in no event shall an Option granted hereunder become vested and exercisable at a rate of less than twenty percent (20%) per year over five (5) years from the date the Option is granted, subject to reasonable conditions, such as continuing to be a Service Provider. An Option may not be exercised for a fraction of a Share.

(b) Deliveries upon Exercise. All or a portion of an exercisable Option shall be deemed exercised upon delivery of all of the following to the Secretary of the Company or his or her office:

(i) A written or electronic notice complying with the applicable rules established by the Administrator stating that the Option, or a portion thereof, is exercised. The notice shall be signed by the Holder or other person then entitled to exercise the Option or such portion of the Option;

(ii) Such representations and documents as the Administrator, in its sole discretion, deems necessary or advisable to effect compliance with Applicable Laws. The Administrator may, in its sole discretion, also take whatever additional actions it deems appropriate to effect such compliance, including, without limitation, placing legends on share certificates and issuing stop transfer notices to agents and registrars;

(iii) Upon the exercise of all or a portion of an unvested Option pursuant to Section 10(h), a Restricted Stock purchase agreement in a form determined by the Administrator and signed by the Holder or other person then entitled to exercise the Option or such portion of the Option; and

(iv) In the event that the Option shall be exercised pursuant to Section 10(f) by any person or persons other than the Holder, appropriate proof of the right of such person or persons to exercise the Option.

(c) Conditions to Delivery of Share Certificates. The Company shall not be required to issue or deliver any certificate or certificates for

Shares purchased upon the exercise of any Option or portion thereof prior to fulfillment of all of the following conditions:

(i) The admission of such Shares to listing on all stock exchanges on which such class of stock is then listed;

(ii) The completion of any registration or other qualification of such Shares under any state or federal law, or under the rulings or regulations of the Securities and Exchange Commission or any other governmental regulatory body which the Administrator shall, in its sole discretion, deem necessary or advisable;

(iii) The obtaining of any approval or other clearance from any state or federal governmental agency which the Administrator shall, in its sole discretion, determine to be necessary or advisable;

(iv) The lapse of such reasonable period of time following the exercise of the Option as the Administrator may establish from time to time for reasons of administrative convenience; and

(v) The receipt by the Company of full payment for such Shares, including payment of any applicable withholding tax, which in the sole discretion of the Administrator may be in the form of consideration used by the Holder to pay for such Shares under Section 9(b).

(d) Termination of Relationship as a Service Provider. If a Holder ceases to be a Service Provider other than by reason of the Holder's disability or death, such Holder may exercise his or her Option within such period of time as is specified in the Option Agreement to the extent that the Option is vested on the date of termination (but in no event later than the expiration of the term of the Option as set forth in the Option Agreement). In the absence of a specified time in the Option Agreement, the Option shall remain exercisable for three (3) months following the Holder's termination. If, on the date of termination, the Holder is not vested as to his or her entire Option, the Shares covered by the unvested portion of the Option immediately cease to be issuable under the Option and shall again become available for issuance under the Plan. If, after termination, the Holder does not exercise his or her Option within the time period specified herein, the Option shall terminate, and the Shares covered by such Option shall again become available for issuance under the Plan. If a Holder is terminated for Cause, the Option shall immediately terminate, and the Shares covered by such Option shall again become available for issuance under the Plan.

(e) Disability of Holder. If a Holder ceases to be a Service Provider as a result of the Holder's disability, the Holder may exercise his or her Option within such period of time as is specified in the Option Agreement to the extent the Option is vested on the date of termination (but in no event later than the expiration of the term of such Option as set forth in the

Option Agreement). In the absence of a specified time in the Option Agreement, the Option shall remain exercisable for twelve (12) months following the Holder's termination. If such disability is not a "disability" as such term is defined in Section 22(e)(3) of the Code, in the case of an Incentive Stock Option such Incentive Stock Option shall automatically cease to be treated as an Incentive Stock Option and shall be treated for tax purposes as a Non-Qualified Stock Option from and after the day which is three (3) months and one (1) day following such termination. If, on the date of termination, the Holder is not vested as to his or her entire Option, the Shares covered by the unvested portion of the Option shall immediately cease to be issuable under the Option and shall again become available for issuance under the Plan. If, after termination, the Holder does not exercise his or her Option within the time specified herein, the Option shall terminate, and the Shares covered by such Option shall again become available for issuance under the Plan.

(f) Death of Holder. If a Holder dies while a Service Provider, the Option may be exercised within such period of time as is specified in the Option Agreement (but in no event later than the expiration of the term of such Option as set forth in the Notice of Grant), by the Holder's estate or by a person who acquires the right to exercise the Option by bequest or

inheritance, but only to the extent that the Option is vested on the date of death. In the absence of a specified time in the Option Agreement, the Option shall remain exercisable for twelve (12) months following the Holder's termination. If, at the time of death, the Holder is not vested as to his or her entire Option, the Shares covered by the unvested portion of the Option shall immediately cease to be issuable under the Option and shall again become available for issuance under the Plan. The Option may be exercised by the executor or administrator of the Holder's estate or, if none, by the person(s) entitled to exercise the Option under the Holder's will or the laws of descent or distribution. If the Option is not so exercised within the time specified herein, the Option shall terminate, and the Shares covered by such Option shall again become available for issuance under the Plan. The Company shall notify the Holder's estate or the person who acquires the right to exercise the Option by bequest or inheritance of the existence of the Holder's outstanding Option and the date of the expiration of the term of such Option as soon after the death of the Holder as is practicable.

(g) Regulatory Extension. A Holder's Option Agreement may provide that if the exercise of the Option following the termination of the Holder's status as a Service Provider (other than upon the Holder's death or Disability) would be prohibited at any time solely because the issuance of shares would violate the registration requirements under the Securities Act, then the Option shall terminate on the earlier of (i) the expiration of the term of the Option set forth in Section 8 or (ii) the expiration of a period of three (3) months after the termination of the Holder's status as a Service Provider during which the exercise of the Option would not be in violation of such registration requirements.

(h) Early Exercisability. The Administrator may provide in the terms of a Holder's Option Agreement that the Holder may, at any time before the Holder's status as a Service Provider terminates, exercise the Option in whole or in part prior to the full vesting of the Option; provided, however, that subject to Section 22, Shares acquired upon exercise of an

Option which has not fully vested may be subject to any forfeiture, transfer or other restrictions as the Administrator may determine in its sole discretion.

(i) Buyout Provisions. The Administrator may at any time offer to buyout for a payment in cash or Shares, an Option previously granted, based on such terms and conditions as the Administrator shall establish and communicate to the Holder at the time that such offer is made.

11. Non-Transferability of Options and Stock Purchase Rights. Options and Stock Purchase Rights may not be sold, pledged, assigned, hypothecated, transferred, or disposed of in any manner other than by will or by the laws of descent or distribution and may be exercised, during the lifetime of the Holder, only by the Holder.

12. Granting of Options to Independent Directors.

(a) During the term of the Plan, a person who is an Independent Director as of the Public Trading Date, or a person who is initially elected to the Board following the Public Trading Date and who is an Independent Director at the time of such initial election, may be granted an Option to purchase twenty-one thousand six hundred (21,600) shares of Common Stock (subject to adjustment as provided in Section 15) on the Public Trading Date or such initial election, as applicable (each, an "Initial Option"). Members of the Board who are employees of the Company who subsequently retire from the Company and remain on the Board will not receive an Initial Option. The Initial Option grants authorized by this Section 12(a) shall be made by the Board.

13. Terms of Initial Options. The per Share price of each Initial Option granted to an Independent Director shall equal 100% of the Fair Market Value of a share of Common Stock on the date the Initial Option is granted; provided, however, that the per Share price of each Initial Option granted to an Independent Director on the date of the initial public offering of Common Stock shall equal the initial public offering price (net of underwriting discounts and commissions) per Share. Initial Options granted to Independent Directors shall become exercisable in cumulative annual installments of one third (1/3) of the Shares subject to such option on each of the yearly anniversaries of the date of

Initial Option grant, commencing with the first such anniversary, such that each Initial Option shall be one hundred percent (100%) vested on the third anniversary of its date of grant, subject to the Independent Director remaining a Director on each such date. Subject to Section 10, the term of each Initial Option granted to an Independent Director shall be ten (10) years from the date the Initial Option is granted. No portion of an Initial Option which is unexercisable at the time of an Independent Director's termination of membership on the Board shall thereafter become exercisable.

14. Stock Purchase Rights and Stock Bonuses.

(a) Rights to Purchase. Stock Purchase Rights may be issued either alone, in addition to, or in tandem with Options granted under the Plan and/or cash awards made outside

of the Plan. After the Administrator determines that it will offer Stock Purchase Rights under the Plan, it shall advise the offeree in writing of the terms, conditions and restrictions related to the offer, including the number of Shares that such person shall be entitled to purchase, the price to be paid, and the time within which such person must accept such offer. The offer shall be accepted by execution of a Restricted Stock purchase agreement in the form determined by the Administrator.

(b) Repurchase Right. Unless the Administrator determines otherwise, the Restricted Stock purchase agreement shall grant the Company the right to repurchase Shares acquired upon exercise of a Stock Purchase Right upon the termination of the purchaser's status as a Service Provider for any reason. Subject to Section 22, the purchase price for Shares repurchased by the Company pursuant to such repurchase right and the rate at which such repurchase right shall lapse shall be determined by the Administrator in its sole discretion, and shall be set forth in the Restricted Stock purchase agreement.

(c) Other Provisions. The Restricted Stock purchase agreement shall contain such other terms, provisions and conditions not inconsistent with the Plan as may be determined by the Administrator in its sole discretion.

(d) Rights as a Shareholder. Once the Stock Purchase Right is exercised, the purchaser shall have rights equivalent to those of a shareholder and shall be a shareholder when his or her purchase is entered upon the records of the duly authorized transfer agent of the Company. No adjustment shall be made for a dividend or other right for which the record date is prior to the date the Stock Purchase Right is exercised, except as provided in Section 15 of the Plan.

(e) Stock Bonuses. Notwithstanding any other provision of the Plan, the Administrator may grant Stock Bonuses, as compensation or as bonuses, to such Service Providers as the Administrator may select in its sole discretion from time to time. Such Stock Bonuses may be issued either alone, in addition to, or in tandem with Options or Stock Purchase Rights granted under the Plan and/or cash awards made outside of the Plan. After the Administrator determines that it will offer Stock Bonuses under the Plan, it shall advise the offeree in writing of the terms and conditions related to the offer, including the number of Shares that such person shall be entitled to receive, the price to be paid, if any, the time within which such person must accept such offer, and the manner of acceptance of such offer.

15. Adjustments upon Changes in Capitalization, Merger or Asset Sale.

(a) In the event that the Administrator determines that any dividend or other distribution (whether in the form of cash, Common Stock, other securities, or other property), recapitalization, reclassification, stock split, reverse stock split, reorganization, merger, consolidation, split-up, spin-off, combination, repurchase, liquidation, dissolution, or sale, transfer, exchange or other disposition of all or substantially all of the assets of the Company, or exchange of Common Stock or other securities of the Company, issuance of warrants or other

rights to purchase Common Stock or other securities of the Company, or other similar corporate transaction or event, in the Administrator's sole discretion, affects the Common Stock such that an adjustment is determined by the Administrator to be appropriate in order to prevent dilution or enlargement of the benefits or potential benefits intended to be made available under the Plan or with respect to any Option, Stock Purchase Right or Restricted Stock, then the Administrator shall, in such manner as it may deem equitable, adjust any or all of:

(i) the number and kind of shares of Common Stock (or other securities or property) with respect to which Options or Stock Purchase Rights may be granted or awarded (including, but not limited to, adjustments of the limitations in Section 3 on the maximum number and kind of shares which may be issued and adjustments of the maximum number of Shares that may be purchased by any Holder in any calendar year pursuant to Section 6(c));

(ii) the number and kind of shares of Common Stock (or other securities or property) subject to outstanding Options, Stock Purchase Rights or Restricted Stock; and

(iii) the grant or exercise price with respect to any Option or Stock Purchase Right.

(b) In the event of any transaction or event described in Section 15(a), the Administrator, in its sole discretion, and on such terms and conditions as it deems appropriate, either by the terms of the Option, Stock Purchase Right or Restricted Stock or by action taken prior to the occurrence of such transaction or event and either automatically or upon the Holder's request, is hereby authorized to take any one or more of the following actions whenever the Administrator determines that such action is appropriate in order to prevent dilution or enlargement of the benefits or potential benefits intended by the Company to be made available under the Plan or with respect to any Option, Stock Purchase Right or Restricted Stock granted or issued under the Plan or to facilitate such transaction or event:

(i) To provide for either the purchase of any such Option, Stock Purchase Right or Restricted Stock for an amount of cash equal to the amount that could have been obtained upon the exercise of such Option or Stock Purchase Right or realization of the Holder's rights had such Option, Stock Purchase Right or Restricted Stock been currently exercisable or payable or fully vested or the replacement of such Option, Stock Purchase Right or Restricted Stock with other rights or property selected by the Administrator in its sole discretion;

(ii) To provide that such Option or Stock Purchase Right shall be exercisable as to all shares covered thereby, notwithstanding anything to the contrary in the Plan or the provisions of such Option or Stock Purchase Right;

(iii) To provide that such Option, Stock Purchase Right or Restricted Stock be assumed by the successor or survivor corporation, or a parent or subsidiary thereof, or shall be substituted for by similar options, rights or awards covering the stock of the successor or survivor corporation, or a parent or subsidiary thereof, with appropriate adjustments as to the number and kind of shares and prices;

(iv) To make adjustments in the number and type of shares of Common Stock (or other securities or property) subject to outstanding Options and Stock Purchase Rights, and/or in the terms and conditions of (including the grant or exercise price), and the criteria included in, outstanding Options, Stock Purchase Rights or Restricted Stock or Options, Stock Purchase Rights or Restricted Stock which may be granted in the future; and

(v) To provide that immediately upon the consummation of such event, such Option or Stock Purchase Right shall not be exercisable and shall terminate; provided, that for a specified period of time prior to such event, such Option or Stock Purchase Right shall be exercisable as to all Shares covered thereby, and the restrictions imposed under an Option Agreement or

Restricted Stock purchase agreement upon some or all Shares may be terminated and, in the case of Restricted Stock, some or all shares of such Restricted Stock may cease to be subject to repurchase, notwithstanding anything to the contrary in the Plan or the provisions of such Option, Stock Purchase Right or Restricted Stock purchase agreement.

(c) Subject to Section 3, the Administrator may, in its sole discretion, include such further provisions and limitations in any Option, Stock Purchase Right, Restricted Stock agreement or certificate, as it may deem equitable and in the best interests of the Company.

(d) If the Company undergoes an Acquisition, then any surviving corporation or entity or acquiring corporation or entity, or affiliate of such corporation or entity, may assume any Options, Stock Purchase Rights or Restricted Stock outstanding under the Plan or may substitute similar stock awards (including an award to acquire the same consideration paid to the stockholders in the transaction described in this subsection 15(d)) for those outstanding under the Plan. In the event any surviving corporation or entity or acquiring corporation or entity in an Acquisition, or affiliate of such corporation or entity, does not assume such Options, Stock Purchase Rights or Restricted Stock or does not substitute similar stock awards for those outstanding under the Plan, then with respect to (i) Options, Stock Purchase Rights or Restricted Stock held by participants in the Plan whose status as a Service Provider has not terminated prior to such event, the vesting of such Options, Stock Purchase Rights or Restricted Stock (and, if applicable, the time during which such awards may be exercised) shall be accelerated and made fully exercisable and all restrictions thereon shall lapse at least ten (10) days prior to the closing of the Acquisition (and the Options or Stock Purchase Rights terminated if not exercised prior to the closing of such Acquisition), and (ii) any other Options or Stock Purchase Rights outstanding under the Plan, such Options or Stock Purchase rights shall be terminated if not exercised prior to the closing of the Acquisition.

(e) In the event the Company undergoes an Acquisition and any surviving corporation or entity or acquiring corporation or entity, or affiliate of such corporation or entity, does assume any Options, Stock Purchase Rights or Restricted Stock outstanding under the Plan (or substitutes similar stock awards, including an award to acquire the same consideration paid to the stockholders in the transaction described in this subsection 15(e), for those outstanding under the Plan), then, with respect to each stock award held by participants in the Plan then performing services as Employees or Directors, the vesting of each such stock award (and, if applicable, the time during which such stock award may be exercised) shall be accelerated and such stock award shall immediately become fully vested and exercisable, if any of the following events occurs within nine (9) months after the effective date of the Acquisition: (1) the Employee status or Director status, as applicable, of the participant holding such stock award is terminated by the Company without Cause; (2) the Employee holding such stock award terminates his or her Employee status due to the fact that the principal place of the performance of the responsibilities and duties of the Employee is changed to a location more than fifty (50) miles from such Employee's existing work location without the Employee's express consent (this clause (2) is not applicable to Directors); or (3) the Employee holding such stock award terminates his or her Employee status due to the fact that there is a material reduction in such Employee's responsibilities and duties without the Employee's express consent (this clause (3) is not applicable to Directors).

(f) The existence of the Plan, any Option Agreement or Restricted Stock purchase agreement and the Options or Stock Purchase Rights granted hereunder shall not affect or restrict in any way the right or power of the Company or the stockholders of the Company to make or authorize any adjustment, recapitalization, reorganization or other change in the Company's capital structure or its business, any merger or consolidation of the Company, any issue of stock or of options, warrants or rights to purchase stock or of bonds, debentures, preferred or prior preference stocks whose rights are superior to or affect the Common Stock or the rights thereof or which are convertible into or exchangeable for Common Stock, or the dissolution or liquidation of the Company, or any sale or transfer of all or any part of its assets or business, or any other corporate act or proceeding, whether of a

similar character or otherwise.

16. Time of Granting Options, Stock Purchase Rights and Stock Bonuses. The date of grant of an Option, Stock Purchase Right or Stock Bonus shall, for all purposes, be the date on which the Administrator makes the determination granting such Option, Stock Purchase Right or Stock Bonus, or such other date as is determined by the Administrator. Notice of the determination shall be given to each Employee or Consultant to whom an Option, Stock Purchase Right or Stock Bonus is so granted within a reasonable time after the date of such grant.

17. Amendment and Termination of the Plan.

(a) Amendment and Termination. The Board may at any time wholly or partially amend, alter, suspend or terminate the Plan. However, without approval of the Company's stockholders given within twelve (12) months before or after the action by the

Board, no action of the Board may, except as provided in Section 15, increase the limits imposed in Section 3 on the maximum number of Shares which may be issued under the Plan or extend the term of the Plan under Section 7.

(b) Stockholder Approval. The Board shall obtain stockholder approval of any Plan amendment to the extent necessary and desirable to comply with Applicable Laws.

(c) Effect of Amendment or Termination. No amendment, alteration, suspension or termination of the Plan shall impair the rights of any Holder, unless mutually agreed otherwise between the Holder and the Administrator, which agreement must be in writing and signed by the Holder and the Company. Termination of the Plan shall not affect the Administrator's ability to exercise the powers granted to it hereunder with respect to Options, Stock Purchase Rights, Stock Bonuses or Restricted Stock granted or awarded under the Plan prior to the date of such termination.

18. Stockholder Approval. The Capstone Turbine Corporation 2000 Equity Incentive Plan, as originally adopted, was submitted for the approval of the Company's stockholders and such approval was received within twelve (12) months after the date of the Board's initial adoption thereof. In addition, an amendment to increase the number of Shares authorized for issuance hereunder from 3,300,000 to 3,700,000 was approved by the Company's stockholders, and such amendment is incorporated herein.

19. Inability to Obtain Authority. The inability of the Company to obtain authority from any regulatory body having jurisdiction, which authority is deemed by the Company's counsel to be necessary to the lawful issuance and sale of any Shares hereunder, shall relieve the Company of any liability in respect of the failure to issue or sell such Shares as to which such requisite authority shall not have been obtained.

20. Reservation of Shares. The Company, during the term of this Plan, shall at all times reserve and keep available such number of Shares as shall be sufficient to satisfy the requirements of the Plan.

21. Information to Holders and Purchasers. Prior to the Public Trading Date and to the extent required by Section 260.140.46 of Title 10 of the California Code of Regulations, the Company shall provide to each Holder and to each individual who acquires Shares pursuant to the Plan, not less frequently than annually during the period such Holder or purchaser has one or more Options or Stock Purchase Rights outstanding, and, in the case of an individual who acquires Shares pursuant to the Plan, during the period such individual owns such Shares, copies of annual financial statements. Notwithstanding the preceding sentence, the Company shall not be required to provide such statements to key employees whose duties in connection with the Company assure their access to equivalent information.

22. Repurchase Provisions. The Administrator in its sole discretion may provide that the Company may repurchase Shares acquired upon exercise of an Option or Stock Purchase

Right upon the occurrence of certain specified events, including, without limitation, a Holder's termination as a Service Provider, divorce, bankruptcy or insolvency; provided, however, that any such repurchase right shall be set forth in the applicable Option Agreement or Restricted Stock purchase agreement or in another agreement referred to in such agreement and, provided, further, that to the extent required by Section 260.140.41 and Section 260.140.42 of Title 10 of the California Code of Regulations, any such repurchase right set forth in an Option or Stock Purchase Right granted prior to the Public Trading Date to a person who is not an Officer, Director or Consultant shall be upon the following terms: (i) if the repurchase option gives the Company the right to repurchase the shares upon termination as a Service Provider at not less than the Fair Market Value of the shares to be purchased on the date of termination of status as a Service Provider, then (A) the right to repurchase shall be exercised for cash or cancellation of purchase money indebtedness for the shares within ninety (90) days of termination of status as a Service Provider (or in the case of shares issued upon exercise of Options or Stock Purchase Rights after such date of termination, within ninety (90) days after the date of the exercise) or such longer period as may be agreed to by the Administrator and the Plan participant and (B) the right terminates when the shares become publicly traded; and (ii) if the repurchase option gives the Company the right to repurchase the Shares upon termination as a Service Provider at the original purchase price for such Shares, then (A) the right to repurchase at the original purchase price shall lapse at the rate of at least twenty percent (20%) of the shares per year over five (5) years from the date the Option or Stock Purchase Right is granted (without respect to the date the Option or Stock Purchase Right was exercised or became exercisable) and (B) the right to repurchase shall be exercised for cash or cancellation of purchase money indebtedness for the shares within ninety (90) days of termination of status as a Service Provider (or, in the case of shares issued upon exercise of Options or Stock Purchase Rights, after such date of termination, within ninety (90) days after the date of the exercise) or such longer period as may be agreed to by the Company and the Plan participant.

23. Investment Intent. The Company may require a Plan participant, as a condition of exercising or acquiring stock under any Option, Stock Purchase Right or Stock Bonus, (i) to give written assurances satisfactory to the Company as to the participant's knowledge and experience in financial and business matters and/or to employ a purchaser representative reasonably satisfactory to the Company who is knowledgeable and experienced in financial and business matters and that he or she is capable of evaluating, alone or together with the purchaser representative, the merits and risks of exercising the Option or Stock Purchase Right or accepting the Stock Bonus; and (ii) to give written assurances satisfactory to the Company stating that the participant is acquiring the stock subject to the Option, Stock Purchase Right or Stock Bonus for the participant's own account and not with any present intention of selling or otherwise distributing the stock. The foregoing requirements, and any assurances given pursuant to such requirements, shall be inoperative if (A) the issuance of the shares upon the exercise or acquisition of stock under the applicable Option, Stock Purchase Right or Stock Bonus has been registered under a then currently effective registration statement under the Securities Act or (B) as to any particular requirement, a determination is made by counsel for the Company that such requirement need not be met in the circumstances under the then applicable securities laws.

The Company may, upon advice of counsel to the Company, place legends on stock certificates issued under the Plan as such counsel deems necessary or appropriate in order to comply with applicable securities laws, including, but not limited to, legends restricting the transfer of the stock.

24. Governing Law. The validity and enforceability of this Plan shall be governed by and construed in accordance with the laws of the State of Delaware without regard to otherwise governing principles of conflicts of law.

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EXHIBIT 10.14

CAPSTONE TURBINE CORPORATION
SEVERANCE PAY PLAN AND
SUMMARY PLAN DESCRIPTION

ARTICLE I
INTRODUCTION

Capstone Turbine Corporation (the "Company") hereby establishes, effective as of May 1, 2002, the 2002 Capstone Turbine Corporation Severance Pay Plan (the "Plan"), to provide severance pay benefits for eligible employees whose employment is involuntarily terminated without cause, subject to the terms of the Plan. This document serves as both the Plan document and the summary plan description of the Plan. Except as provided in any individual written contracts, this Plan replaces and supercedes any formal or informal prior severance pay plan, program or arrangement that may have covered you previously as an employee of the Company. The purpose of this Plan is to assist associates in their transition to finding new employment, not to reward an employee for years of service. Benefits paid to an employee hereunder are not earned or otherwise accrued by an associate.

ARTICLE II
PARTICIPATION IN THE PLAN

Full-time employees employed by the Company are eligible to receive benefits under the Plan, subject to its terms (hereinafter referred to as "Eligible Employees"). For purposes herein, "full-time" employee means an employee regularly scheduled to work 30 hours per week. Individuals who work for the Company as a temporary, seasonal, intern, leased or independent contractor basis are expressly excluded from participation in this Plan. Executives of the Company who are covered by another plan or contract are also excluded from this Plan. Full-time employees employed by any Company subsidiary within the United States are also covered by this Plan.

ARTICLE III
BENEFIT ELIGIBILITY

An Eligible Employee is entitled to benefits under this Plan if, and only if, the Company without "Cause" terminates his/her employment. For purposes herein, "Cause" shall mean violation of company policy, fraud, willful malfeasance (or similar wrongful acts) and continuing (after notice) neglect of job duties. Notwithstanding the foregoing, no Eligible Employee shall be eligible for benefits where, as a result of a Change in Business, as hereinafter defined, he or she become employed or are offered employment by a different employer in substantially the same position as he or she had with the Company. A Change in Business means the sale or transfer of all or a portion of the assets or stock or a merger of Capstone or related companies, or the Company's cessation of conducting certain business activities that are formally or informally transferred to another organization. The Company has the sole and absolute discretion to determine when a reduction in force or job elimination has occurred and will notify you of such determination.

If your regular employment is terminated for any other reason, you will not be entitled to receive any of the benefits offered through this Plan. This means, for example, that if you voluntarily

resign, are terminated for Cause, then you will not be entitled to receive the benefits offered through this Plan.

Notwithstanding the foregoing, if you refuse a reasonable reassignment to another position with the Company, you will not be considered as terminated due to a reduction in force or job elimination, and will not eligible to receive any benefits under this Plan.

ARTICLE IV
SEVERANCE BENEFIT

If you are entitled to benefits under Article III, your severance benefits will

be determined under Section 4.01 or Section 4.02, subject to the forfeiture provisions of Section 4.09.

SECTION 4.01. MINIMUM BENEFIT – If you do not execute the General Release & Separation Agreement, as required in Section 4.04, you will receive two (2) weeks of severance pay.

SECTION 4.02. SEVERANCE BENEFIT FORMULA – If you execute the General Release & Separation Agreement, as required in Section 4.04, you will receive the greater of: (i) one (1) week of severance pay for each full year of service with the Company as an Eligible Employee (except for years of service for which severance benefits have previously been paid by Company) for the period ending on the date of your termination; or, (ii) four (4) weeks of severance pay.

SECTION 4.03. PAYMENT. Each week of severance pay equals the weekly compensation regularly paid to you at the time your employment terminates, excluding any overtime pay, bonuses and imputed income. The severance pay benefit will be paid in the same manner as the Company's regular payroll practices during the severance period. Employees will also be paid for any unused vacation time, as defined in the Company's vacation policy, determined as of the termination date, which payment shall be made no later than required by applicable state law.

The payment of benefits hereunder does not extend an individual's employment with the Company. Unless specifically provided for under the Plan or required by applicable law, all benefits cease as of your date of termination, including, but not limited to, healthcare, dental, life, long term disability insurance, holiday pay and vacation accrual.

SECTION 4.04. GENERAL RELEASE & SEPARATION AGREEMENT – To receive benefits under Section 4.02 of this Plan, you must sign a "General Release & Separation Agreement" in the form prescribed by the Plan Administrator. If you do not sign the "General Release & Separation Agreement," you will receive benefits under Section 4.01 of this Plan. The General Release & Separation Agreement will include a release and waiver satisfactory to Company, substantially in the form as Exhibit A.

SECTION 4.05. RETIREMENT PLANS – Participation in this Plan is not intended to alter any benefits you are entitled to receive under the Company's retirement plans. Those benefits will continue to be determined by the terms of those plans. For more information, please refer to the plan documents and summary plan descriptions for those plans.

SECTION 4.06. NON-ALIENATION OF BENEFIT – You may not, in any manner, sell, pledge, transfer, assign, encumber, or otherwise dispose of any severance pay benefit, either voluntarily or involuntarily, before you receive it, and any attempt to do so or to otherwise dispose of any right to benefits under this Plan will be void.

SECTION 4.07. APPLICATION FOR BENEFITS – To receive benefits under this Plan, you must notify the Vice President, Human Resources, by executing and delivering to him the "General Release & Separation Agreement" by no later than the end of the time period set forth in the General Release & Separation Agreement. If you do not receive a benefit to which you believe you are entitled, you may write to the Company at the address set forth in this document and state the benefit to which you believe you are entitled. This writing will be considered a claim for benefits described in the section of this Plan entitled "Claims Procedures."

SECTION 4.08. FORFEITURE. Notwithstanding anything to the contrary set forth herein, any and all remaining severance benefits shall be forfeited and cease immediately upon:

(1) Any breach of the terms set forth in the General Release & Separation Agreement;

(2) Your rejection of an offer of re-employment with the Company in the same or an equivalent position; or,

(3) Your acceptance of re-employment with the Company.

SECTION 4.09. NO DUPLICATION. An employee of the Company may not receive severance benefits under the Plan and another arrangement with the Company. Such an associate will only be entitled to the severance benefit that provides him with the greatest amount of severance pay.

ARTICLE V
PLAN ADMINISTRATOR

The Company is the administrator of the Plan and a named fiduciary within the meaning of the Employee Retirement Income Security Act of 1974, as amended ("ERISA"). As Plan administrator, the Company has discretionary authority to interpret, with discretionary authority, the provisions of the Plan and to resolve, with discretionary authority, all disputed questions of Plan interpretation, including eligibility, rights and status of participants.

ARTICLE VI
MISCELLANEOUS

SECTION 6.01. FUNDING OF PLAN – Payments under the Plan are made directly from the Company's general assets.

SECTION 6.02. CLAIMS PROCEDURES – If you make a claim for benefits and the Company denies the claim, in whole or in part, the Company will give you written notice of the denial within ninety (90) days after the date on which it received the claim. If special circumstances require extension of the ninety (90) day response period, the Company may extend the period for up to

ninety (90) additional days by notifying you, within the original ninety (90) day period, of the extension, the reason for it, and when you can expect a decision. The written notice of the denial of a claim will contain the following information:

(1) the specific reason or reasons for denial of the claim,

(2) specific reference to the provisions of the Plan on which the denial is based,

(3) a description of any additional material or information that you may need to prove the claim, with an explanation as to why the material or information is necessary, and

(4) an explanation of the right to appeal for review of the claim denial and the procedure for appeal.

If the Company denies your claim, in whole or in part, you have the right to appeal to the Company's Vice President – Human Resources for review of the denial. The following provisions apply to that right of appeal:

(1) The request for review must be filed with the Company within sixty (60) days following delivery to you of the written notice of denial of the claim.

(2) The request must be in writing signed by you or your authorized representative.

(3) You have the right, upon request, to review records and documents in the Company's possession relating to the claim.

(4) You may submit issues, arguments, and other comments in writing to the Company, with any documentary evidence in support of the claim.

(5) The Company's decision must be given to you in writing within sixty (60) days after receipt of your request for review. If special circumstances require extension of the sixty (60) day response period, the Company may extend the period for up to sixty (60) additional days by notifying you, within the original sixty (60) day period, of the extension, the reason for it, and when you can expect a decision. The decision on

review must state specific reasons for the decision, including specific reference to the Plan provision or provisions on which the decision is based.

SECTION 6.03. PARTICIPANTS' RIGHTS UNDER ERISA - The following lengthy statement concerning rights of participants under ERISA is required by regulations issued by the U.S. Department of Labor:

As a participant in the Plan you are entitled to certain rights and protections under ERISA. ERISA provides that all Plan participants shall be entitled to examine, without charge, at the Company's offices, all Plan documents, including copies of all documents filed by the Plan with the U.S. Department of Labor, such as annual reports and summary plan descriptions. All Plan

participants may obtain copies of all Plan documents and other Plan information upon written request to the Company. The Company may make a reasonable charge for the copies. Plan participants shall receive a summary of the Plan's annual financial report, if the Plan is required by law to file one. In that event, the Company is required by law to furnish each participant with a copy of the summary annual report.

In addition to creating rights for Plan participants, ERISA imposes obligations upon the persons who are responsible for the operation of the Plan. These persons are referred to as "fiduciaries" in the law. Fiduciaries must act solely in the interest of the Plan participants, and they must exercise prudence in the performance of their Plan duties. No one, including your Company, may fire you or discriminate against you to prevent you from obtaining a Plan benefit or exercising your rights under ERISA. If your claim for a Plan benefit is denied in whole or in part, you must receive a written explanation of the denial. You have the right to have the Plan review and reconsider your claim. Under ERISA, there are steps you can take to enforce these rights. For instance, if you request materials from the Plan and do not receive them within thirty (30) days, you may file suit in a federal court. In such a case, the court may require the Company to provide the materials and pay you up to $110.00 a day until you receive the materials, unless the materials were not sent because of reasons beyond the Company's control. If you have a claim for benefits that is denied or ignored, in whole or in part, you may file suit in a state or federal court. If it should happen that Plan fiduciaries misuse the Plan's money, of if you are discriminated against for asserting your rights, you may seek assistance from the U.S. Department of Labor, or you may file suit in a federal court. The court will decide who should pay court costs and legal fees. If you are successful, the court may order the person you have sued to pay these costs and fees. If you lose, the court may order you to pay these costs and fees - for example, if it finds your claim is frivolous. If you have any questions about your Plan, you should contact the Company. If you have any questions about this statement or about your rights under ERISA, you should contact the nearest Area Office of the Pension and Welfare Benefits Administration, U.S. Department of Labor listed in your telephone directory or the Division of Technical Assistance and Inquiries, Pension and Welfare Benefits Administration, U.S. Department of Labor, 200 Constitution Avenue, N.W., Washington, D.C. 20210.

SECTION 6.04. AMENDMENT AND TERMINATION - The Company has the right to amend or terminate the Plan at any time.

SECTION 6.05. SPECIFIC INFORMATION ABOUT THE PLAN -

Name of Plan:	*Capstone Turbine Corporation. Severance Pay Plan*
Plan Number:	*506*
Name, Address, and Telephone Number of Plan Sponsor:	*Capstone Turbine Corporation 21211 Nordhoff Street Chatsworth, CA 91311 818 734 5300*

Plan Sponsor's Federal Identification Number:	
Name, Address and Telephone Number of Plan Administrator:	*Capstone Turbine Corporation* *21211 Nordhoff Street* *Chatsworth, CA 91311* *818 734 5300*
Type of Plan:	*Welfare benefit plan providing severance pay benefits to all Eligible Associates.*
Agent for Service of Legal Process:	*General Counsel* *Capstone Turbine Corporation* *21211 Nordhoff Street* *Chatsworth, CA 91311*
Date of End of Plan Year:	*December 31*
Basis of Keeping Records:	*Plan Year*

IN WITNESS WHEREOF, Capstone Turbine Corporation has executed this Severance Pay Plan effective the 1st day of May, 2002.

Capstone Turbine Corporation

By: /s/ AKE ALMGREN

FIRST AMENDMENT TO THE
2002 CAPSTONE TURBINE CORPORATION
SEVERANCE PAY PLAN

The 2002 Capstone Turbine Corporation Severance Pay Plan (the "Plan") hereby is amended, effective February 4, 2003, to read as follows:

I.

Section 4.02 of the Plan is amended in its entirety to read as follows:

"SECTION 4.02. SEVERANCE BENEFIT FORMULA - If you execute the General Release & Separation Agreement, as required in Section 4.04, you will receive the following benefits:

(1) If at the time of termination of your employment with the Company, you are an employee of the Company other than a Director or Executive, you will receive one (1) week of severance pay for each full year of service with the Company as an Eligible Employee (except for years of service for which severance benefits have previously been paid by Company) for the period ending on the date of your termination; provided, however, that benefits payable under this Section 4.02(1) will not be less than four (4) weeks of severance pay, or more than twelve (12) weeks of severance pay;

(2) If at the time of termination of your employment with the Company, you are a Director of the Company, you will receive two (2) weeks of severance pay for each full year of service with the Company as an Eligible Employee (except for years of service for which severance benefits have previously been paid by Company) for the period ending on the date of your termination; provided, however, that benefits payable under this Section 4.02(2) will not be less than four (4) weeks of

severance pay, or more than twelve (12) weeks of severance pay;

(3) If at the time of termination of your employment with the Company, you are an Executive of the Company, you will receive twenty-six (26) weeks of severance pay.

For purposes of this Section 4.02, 'Executive' shall mean any employee of the Company who reports directly to the President and Chief Executive Officer of the Company, and 'Director' shall mean any employee of the Company who reports directly to an Executive of the Company and makes greater than or equal to Eighty-Five Thousand Dollars ($85,000) in annual base salary.

II.

In all other respects, the Plan will remain in full force and effect.

CAPSTONE TURBINE CORPORATION

By: /s/ EMILY M. LIGGETT
Title: Chief Operating Officer

Exhibit 99.1

CERTIFICATION OF CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER
PURSUANT TO
18 U.S.C. 1350
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

I, Emily Liggett, certify, pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report of Capstone Turbine Corporation on Form 10-Q for the quarterly period ended March 31, 2003 fully complies with the requirements of Section 13(a) and 15(d) of the Securities Exchange Act of 1934 and that information contained in such Form 10-Q fairly presents in all material respects the financial condition and results of operations of Capstone Turbine Corporation.

Date: May 15, 2003

By: /s/ EMILY LIGGETT
Emily Liggett
Interim Chief Executive Officer

I, Karen Clark, certify, pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report of Capstone Turbine Corporation on Form 10-Q for the quarterly period ended March 31, 2003 fully complies with the requirements of Section 13(a) and 15(d) of the Securities Exchange Act of 1934 and that information contained in such Form 10-Q fairly presents in all material respects the financial condition and results of operations of Capstone Turbine Corporation.

Date: May 15, 2003

By: /s/ KAREN CLARK
Karen Clark
Chief Financial Officer