TESLA MOTORS INC
Form 10-K
February 26, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2014

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: 001-34756

Tesla Motors, Inc.

(Exact name of registrant as specified in its charter)

Delaware	91-2197729
(State or other jurisdiction of	(I.R.S. Employer
incorporation or organization)	Identification No.)
3500 Deer Creek Road	94304

Palo Alto, California
(Address of principal executive offices) (Zip Code)

(650) 681-5000

(Registrant's telephone number, including area code)

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

Title of each class	Name of each exchange on which registered
Common Stock, $0.001 par value	The NASDAQ Stock Market LLC

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

None

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

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

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 ("Exchange Act") 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 x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ¨

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

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

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

The aggregate market value of voting stock held by non-affiliates of the registrant, as of June 30, 2014, the last day of registrant's most recently completed second fiscal quarter, was $22,968,512,773 (based on the closing price for shares of the registrant's Common Stock as reported by the NASDAQ Global Select Market on June 30, 2014). Shares of Common Stock held by each executive officer, director, and holder of 5% or more of the outstanding Common Stock have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

As of January 31, 2015, there were 125,762,835 shares of the registrant's Common Stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's Proxy Statement for the 2015 Annual Meeting of Stockholders are incorporated herein by reference in Part III of this Annual Report on Form 10-K to the extent stated herein. Such proxy statement will be filed with the Securities and Exchange Commission within 120 days of the registrant's fiscal year ended December 31, 2014.

TESLA MOTORS, INC.

ANNUAL REPORT ON FORM 10-K FOR THE YEAR ENDED DECEMBER 31, 2014

INDEX

		Page
PART I.		
Item 1.	Business	4
Item 1A.	Risk Factors	15
Item 1B.	Unresolved Staff Comments	42
Item 2.	Properties	42
Item 3.	Legal Proceedings	43
Item 4.	Mine Safety Disclosures	43
PART II.		
Item 5.	Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	44
Item 6.	Selected Financial Data	46
Item 7.	Management's Discussion and Analysis of Financial Condition and Results of Operations	47
Item 7A.	Quantitative and Qualitative Disclosures About Market Risk	59
Item 8.	Financial Statements and Supplementary Data	60
Item 9.	Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	90
Item 9A.	Controls and Procedures	90
Item 9B.	Other Information	91
PART III.		
Item 10.	Directors, Executive Officers and Corporate Governance	91
Item 11.	Executive Compensation	91
Item 12.	Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	91
Item 13.	Certain Relationships and Related Transactions, and Director Independence	91
Item 14.	Principal Accountant Fees and Services	91
PART IV.		
Item 15.	Exhibits and Financial Statement Schedules	92
Signatures		98

2

Forward-Looking Statements

The discussions in this Annual Report on Form 10-K contain forward-looking statements reflecting our current expectations that involve risks and uncertainties. These forward-looking statements include, but are not limited to, statements concerning our strategy, future operations, future financial position, future revenues, projected costs, profitability, expected cost reductions, capital adequacy, expectations regarding demand and acceptance for our technologies, growth opportunities and trends in the market in which we operate, prospects and plans and objectives of management. The words “anticipates”, “believes”, “estimates”, “expects”, “intends”, “may”, “plans”, “projects”, “will”, “wo similar expressions are intended to identify forward-looking statements, although not all forward-looking statements contain these identifying words. We may not actually achieve the plans, intentions or expectations disclosed in our forward-looking statements and you should not place undue reliance on our forward-looking statements. Actual results or events could differ materially from the plans, intentions and expectations disclosed in the forward-looking statements that we make. These forward-looking statements involve risks and uncertainties that could cause our actual results to differ materially from those in the forward-looking statements, including, without limitation, the risks set forth in Part I, Item 1A, “Risk Factors” in this Annual Report on Form 10-K and in our other filings with the Securities and Exchange Commission. We do not assume any obligation to update any forward-looking statements.

PART I

ITEM 1. BUSINESS

Overview

We design, develop, manufacture and sell high-performance fully electric vehicles, advanced electric vehicle powertrain components and stationary energy storage systems. We have established our own network of sales and service centers and Supercharger stations globally to accelerate the widespread adoption of electric vehicles. We believe our vehicles, electric vehicle engineering expertise, and business model differentiates us from incumbent automobile manufacturers.

We are currently producing and selling our second vehicle, the Model S sedan. Model S is a four door, five-passenger premium sedan that offers exceptional performance, functionality and attractive styling. Model S inherited many of the electric powertrain innovations we introduced with our first vehicle, the Tesla Roadster. We commenced deliveries of Model S in June 2012 and as of December 31, 2014 we have delivered almost 57,000 Model S vehicles worldwide. Since its launch, Model S has won several awards, including the prestigious Motor Trend Car of the Year for 2013. Surveys by Consumer Reports gave Model S the highest customer satisfaction score of any car in the world in 2013 and gave Tesla Service the best overall satisfaction rating in the entire automotive industry in 2015. Model S also earned the highest safety rating in the United States by the National Highway Traffic Safety Administration. We have continued to improve Model S by introducing performance, all-wheel drive dual motor, autopilot options, and free over-the-air software updates.

We anticipate commencing customer shipments of our third vehicle, the Model X crossover, in the third quarter of 2015. This unique vehicle has been designed to fill the niche between the roominess of a minivan and the style of an SUV, while having high performance features such as our all-wheel drive dual motor system and fast 0 to 60 miles per hour acceleration. After the Model X, our goal is to introduce the Model 3, a lower priced sedan designed for the mass market, in 2017.

The commercial production of fully electric vehicles that meets consumers' range and performance expectations requires substantial design, engineering, and integration work on almost every system of our vehicles. Our design and vehicle engineering capabilities, combined with the technical advancements of our powertrain system, have enabled us to design and develop electric vehicles that we believe overcome the design, styling, and performance issues that have historically limited broad consumer adoption of electric vehicles. As a result, we believe our customers enjoy several benefits, including:

- Long Range and Recharging Flexibility. Our vehicles offer ranges that are over double the range of any other commercially available electric vehicle. In addition, our vehicles incorporate our proprietary on-board charging system, permitting recharging from almost any available electrical outlet. Model S also offers fast charging capability from our Supercharger network. We believe the long-range and charging flexibility of our vehicles will help reduce consumer anxiety over range, alleviate the need for expensive, large-scale charging infrastructure, and differentiate our vehicles as compared to those of our competitors.
- Energy Efficiency and Cost of Ownership. We believe our vehicles offer consumers an attractive cost of ownership when compared to similar internal combustion engine or hybrid electric vehicles. Using only an electric powertrain enables us to create a lighter, more energy efficient vehicle that is mechanically simpler than currently available hybrid or internal combustion engine vehicles. We currently estimate that the cost to fuel our vehicles is approximately one-fourth that of comparable internal combustion vehicles in the United States, and even less internationally where gasoline prices are typically higher. We also expect our electric vehicles will have lower

relative maintenance costs than hybrid, plug-in hybrid, or internal combustion engine vehicles due to fewer moving parts and the absence of certain components, including oil, oil filters, spark plugs and engine valves. Additionally, government incentives that are currently available can reduce the cost of ownership even further.

- High-Performance Without Compromised Design or Functionality. We believe our vehicles deliver unparalleled driving experiences with instantaneous and sustained acceleration through an extended range of speed. In addition, our Model S seats five adults, provides best in class storage in the trunk and hood while offering design and performance comparable to, or better than, other premium sedans.

We sell our vehicles through our own sales and service network which we are continuing to grow globally. We believe the benefits we receive from distribution ownership will enable us to improve the speed of product development and improve the capital efficiency of our business. We are also continuing to build our network of Superchargers in the United States, Europe and Asia to provide properly equipped Model S vehicle owners as well as future Tesla vehicle owners with fast and free charging to enable convenient long distance travel.

In addition to developing our own vehicles, we have developed and currently sell and service full electric powertrain systems and components to other automobile manufacturers. We also produce and sell stationary energy storage products for use in homes, commercial sites, and utilities. The applications for these battery systems include backup power, peak demand reduction, demand response, and wholesale electric market services.

We manufacture our products primarily at our facilities in Fremont, California, Lathrop, California and Tilburg, Netherlands. We are developing the Tesla Gigafactory, a facility where we intend to work together with our suppliers to integrate battery precursor material, cell, module and battery pack production at a site near Reno, Nevada. We plan to use the battery packs manufactured at the Gigafactory for our vehicles, starting initially for Model S and Model X in 2016, and later for our Model 3 vehicle, as well as for stationary storage applications.

Our Vehicles and Products

We currently design, develop, manufacture and sell fully electric vehicles and electric powertrain components. We are currently selling primarily the Model S.

Model S

Model S is a fully electric, four-door, five-adult passenger sedan that offers compelling range and performance with zero tailpipe emissions. We began customer deliveries in June 2012. As of December 31, 2014, we had delivered almost 57,000 Model S vehicles.

Model S offers a range on a single charge of up to 265 miles as determined using the United States EPA's combined two-cycle city/highway test. To complement this range, we also offer the capability to fast charge Model S at our Supercharger facilities. In addition, we designed Model S to incorporate a modular battery pack in the floor of the vehicle, enabling it to be rapidly swapped out at certain of our service centers and specialized commercial battery exchange facilities that we anticipate may be available in the future.

The 60 kWh and 85 kWh battery pack versions of Model S have an effective base price of $62,400, and $72,400, respectively, in the United States, assuming and after giving effect to the continuation of a United States federal tax credit of $7,500 for the purchase of alternative fuel vehicles. We offer performance and all-wheel drive dual motor system options with our 85 kWh Model S. The performance version of our All-Wheel Drive Dual Motor Model S accelerates from 0 to 60 miles per hour in 3.2 seconds, making it the quickest sedan in the world according to Motor Trend magazine.

We believe Model S offers a unique combination of functionality, convenience, safety and styling without compromising performance and energy efficiency. With the battery pack in the floor of the vehicle and the motor and gearbox in line with the rear axle, our single motor Model S provides best in class storage space of 31.6 cubic feet, including storage under both the tailgate and the hood. By way of comparison, this storage space exceeds the approximately 14 cubic feet of storage available in the 2015 BMW 5 Series sedan and the approximately 18 cubic feet of storage available in the 2015 Cadillac XTS. In addition, we have designed Model S to include a third row with two rear-facing child seats, allowing us to offer seating for five adults and two children. Model S is also available with premium luxury features, including a 17 inch touch screen driver interface and our advanced autopilot system. Our autopilot system, which is being progressively enabled over time through over-the-air software updates, includes both safety features such as collision warning systems and automatic braking and convenience features such as traffic aware cruise control. Model S also offers advanced wireless connectivity, such as 3G connectivity, and driver customization of the infotainment and climate control systems of the vehicle. We believe the combination of performance, safety, styling, convenience and energy efficiency of Model S positions it as a compelling alternative to other vehicles in the luxury and performance segments.

We have designed Model S to provide a lower cost of ownership as compared to other vehicles in its class. We consider the purchase price, cost of fuel and the cost of maintenance over a six year ownership period in this calculation. We assume comparable residual values, warranties, insurance costs and promotions and assume that currently available consumer incentives are still available at the time of a Model S purchase. In addition to the

competitive pricing of Model S relative to other premium vehicles, we estimate that customers of electric vehicles will enjoy lower fuel costs. For example, assuming an average of 15,000 miles driven per year, an average electricity cost of 12.1 cents per kilowatt-hour and an average gasoline price of $2.83 per gallon over the full ownership of the vehicle which were the average electricity cost and premium gasoline price in the United States, respectively, for December 2014, and based on our estimate of the energy efficiency of Model S, we estimate that our Model S could save approximately $1,600 per year less in fuel costs than a comparable premium internal combustion engine sedan. In international markets, where gasoline prices can be 2-3 times those of the United States, the savings are greater.

We have designed Model S with an adaptable platform architecture and common electric powertrain that we intend to leverage to create future electric vehicle models, including our Model X. In particular, by designing our electric powertrain within the chassis to accommodate different vehicle body styles, we believe that we can save significant time in future vehicle development. In addition, we believe our strategy of using currently available battery cells will enable us to leverage improvements in cell chemistries and rapidly introduce planned vehicles with different range options.

Model X

Our Model X crossover is the first vehicle we intend to develop by leveraging the Model S platform. This unique vehicle has been designed to offer the space and functionality of a sport utility vehicle while having high performance features such as our fully electric, all-wheel drive dual motor system. Model X will seat seven adults and incorporate a unique falcon wing door system for superior access to the second and third seating rows. We anticipate that the pricing of Model X will be similar to a comparably equipped Model S. We currently intend to begin customer deliveries of Model X in the third quarter of 2015. After its initial launch in the United States, Model X will be sold in all the markets where Model S is available including in Asia and Europe.

Model 3

We have also publicly announced our intent to develop a third generation electric vehicle, called Model 3, to be produced at the Tesla Factory. We intend to offer this vehicle at a lower price point and expect to produce it at higher volumes than our Model S. We expect that this vehicle will be introduced in 2017.

The Tesla Roadster

Our first vehicle, the Tesla Roadster, is the first high-performance electric sports car. It can accelerate from zero to 60 miles per hour in as little as 3.7 seconds and has a maximum speed of approximately 120 miles per hour. The Tesla Roadster also has a range of 245 miles on a single charge, as determined using the United States EPA's combined two-cycle city/highway test. We have sold approximately 2,500 Tesla Roadsters to customers in over 30 countries, predominately in North America and Europe. We concluded the production run of the Tesla Roadster in January 2012.

Stationary Energy Storage Applications

Using the energy management technologies and manufacturing processes developed for our vehicle powertrain systems, we have developed stationary energy storage products for use in homes, commercial sites and utilities. The applications for these battery systems include backup power, peak demand reduction, demand response and wholesale electric market services. We began selling our home systems in 2013 and our commercial and utility systems in 2014. We plan to ramp sales of these products in 2015.

Powertrain Development and Sales

In addition to our own vehicles, we also design, develop, manufacture and sell advanced electric vehicle powertrain components to other automotive manufacturers. We have provided development services and full powertrain systems and components to Daimler for its Smart fortwo, A-Class, and B-Class electric vehicles and to Toyota for use in its RAV4 EV. We are continuing to supply production parts for the Daimler B class electric vehicle.

Technology

We believe the core competencies of our company are powertrain engineering, vehicle engineering and innovative manufacturing. Our core intellectual property is contained within our electric powertrain and the ability to design a vehicle which capitalizes on the uniqueness of an electric powertrain. Our electric powertrain consists of the following: battery pack, power electronics, motor, gearbox and the control software which enables the components to operate as a system. We designed each of these major elements for our Tesla Roadster and Model S and plan to use much of this technology in Model X, Model 3, our future electric vehicles and powertrain components that we build for other manufacturers. Our powertrain and battery pack have a modular design, enabling future generations of electric vehicles and our stationary storage applications to incorporate a significant amount of this technology.

Further, our powertrain is very compact and contains far fewer moving parts than the internal combustion powertrain. These features enable us to adapt it for a variety of applications, including our future vehicles and any powertrain components we build for other manufacturers.

Battery Pack

We design our battery packs to achieve high energy density at a low cost while also maintaining safety, reliability and long life. For example, we have designed our Model S battery packs to store 85 kilowatt hours of useful energy and offer a warranty of unlimited miles over eight years. Our proprietary technology includes cooling systems, safety systems, charge balancing systems, battery engineering for vibration and environmental durability, robotic manufacturing processes, customized motor design and the software and electronics management systems necessary to manage battery and vehicle performance under demanding real-life driving conditions. We have significant experience and expertise in the safety and management systems needed to work with lithium-ion cells in the demanding automotive environment. We believe these advancements have enabled us to produce a battery pack at a low cost per kilowatt-hour.

We have designed our battery pack system to permit flexibility with respect to battery cell chemistry, form factor and vendor. In so doing, we believe that we can leverage the substantial battery cell investments and advancements being made globally by battery cell manufacturers and ourselves to continue to improve the cost per kilowatt-hour of our battery pack. We maintain an internal battery cell testing lab and an extensive performance database of the many available lithium-ion cell vendors and chemistry types. We intend to incorporate the battery cells that provide the best value and performance possible into our battery packs, and we expect this to continue over time as battery cells continue to improve in energy storage capacity, longevity, power delivery and cost. We believe this flexibility will enable us to continue to evaluate new battery cells as they become commercially viable, and thereby optimize battery pack system performance and cost for our current and future vehicles. In addition, we are designing the cell manufacturing equipment for the Tesla Gigafactory to enable flexibility in terms of battery chemistry and form factor. We believe our ability to change battery cell chemistries and vendors while retaining our existing investments in software, electronics, manufacturing equipment, testing and vehicle packaging, will enable us to quickly deploy various battery cells into our products and leverage the latest advancements in battery cell technology.

The range of our electric vehicles on a single charge declines principally as a function of usage, time and charging patterns. Customers' use of their Tesla vehicle as well as the frequency with which they charge the battery of their Tesla vehicle can result in additional deterioration of the battery's ability to hold a charge. For example, we currently expect that the Tesla Roadster battery pack will retain approximately 70% of its ability to hold its initial charge after approximately 100,000 miles or seven years, which will result in a decrease to the vehicle's initial range. In comparison with the Roadster battery pack, preliminary internal testing and customer results of Model S to date suggest that the retention rate of the Model S battery pack is greater, due to improvements at the battery cell and pack level. In addition, based on internal testing, we estimate that the Model S would have an approximate 5-10% reduction in range when operated continuously in 0°C temperatures.

To date, we have tested hundreds of battery cells of different chemistries, form factors and designs. Based on this evaluation, we are presently using lithium-ion battery cells based on the 18650 form factor in all of our battery packs. We intend to use the same battery cell form factor in Model X and entered into a supply agreement with Panasonic Corporation (Panasonic) for the use of Panasonic's battery cells in Model S and Model X. We expect these battery cells to exhibit better performance and longer lifetimes than the battery cells used in the Tesla Roadster.

Power Electronics

The power electronics in our electric powertrain govern the flow of electrical current throughout the car, primarily the current that flows into and out of the battery pack. The power electronics have two primary functions, the control of torque generation in the motor while driving and the control of energy delivery back into the battery pack while charging.

The first function is accomplished through the drive inverter, which converts direct current (DC) from the battery pack into alternating current (AC) to drive our three-phase induction motors. The drive inverter also converts the AC generated by regenerative braking back into DC for electrical storage in the battery pack. The drive inverter performs this function by using a high-performance digital signal processor which runs some of the most complicated and detailed software in the vehicle. In so doing, the drive inverter is directly responsible for the performance, high efficiency and overall driving experience of the vehicle.

The second function, charging the battery pack, is accomplished by the charger, which converts alternating current (usually from a wall outlet or other electricity source) into direct current that can be accepted by the battery. Tesla vehicles can recharge on a variety of AC electrical sources, from a common outlet to a high power circuit of up to 22kW, which provides faster recharging. Vehicles in both the United States and Europe come with the Tesla Mobile Connector which enables charging from a variety of different outlets. In other markets, Tesla offers a Tesla Wall

Connector that can be hardwired at a wide range of power levels to suit the electrical capabilities of the charging location.

The most common home charging system uses a standard high power and Mobile Connector to charge overnight. On the road, customers can also charge using our Supercharger network or at a variety of destinations that have deployed our charging equipment. In addition, Model S vehicles can also charge at a variety of public charging stations around the world, either natively or through a suite of adapters. This flexibility in charging provides customers with additional mobility, while also allowing them to conveniently charge the vehicle overnight at home.

Vehicle Control and Infotainment Software

The performance and safety systems of our vehicles and their battery packs require sophisticated control software. There are numerous processors in our vehicles to control these functions, and we write custom firmware for many of these processors. The flow of electricity between the battery pack and the motor must be tightly controlled in order to deliver the performance and behavior expected in the vehicle. For example, software algorithms enable the vehicle to mimic the “creep” feeling which drivers expect from an internal combustion engine vehicle without having to apply pressure on the accelerator. Similar algorithms control traction, vehicle stability and the sustained acceleration and regenerative braking of the vehicle. Software also is used extensively to monitor the charge state of each of the cells of the battery pack and to manage all of its safety systems. Drivers use the information and control systems in our vehicles to optimize performance, customize vehicle behavior, manage charging modes and times and control all infotainment functions. We develop almost all of this software, including most of the user interfaces, internally. We are also developing expertise in vehicle autopilot systems, including road tracking, lane changing, automated parking, driver warning systems and automated braking functions.

Vehicle Design and Engineering

In addition to the design, development and production of the powertrain, we have created significant in-house capabilities in the design and engineering of electric vehicles and electric vehicle components and systems. We design and engineer bodies, chassis, interiors, heating and cooling and low voltage electrical systems in house and to a lesser extent in conjunction with our suppliers. Our team has core competencies in computer aided design and crash test simulations which we expect to reduce the product development time of new models.

Several traditional automotive subsystems required substantial redesign and custom optimization to integrate with the powertrain of an electric vehicle. For example, we redesigned the heating, ventilation and air conditioning (HVAC) system to integrate with the battery thermal management system and to operate without the energy generated from an internal combustion engine. We have developed expertise in integrating these components with the high-voltage power source in the vehicle and in designing components that significantly reduce their load on the vehicle battery pack, thereby maximizing the available range of the vehicle.

Additionally, our team has expertise in lightweight materials, a very important characteristic for electric vehicles given the impact of mass on range. Model S is built with a lightweight aluminum body and chassis which incorporates a variety of materials and production methods that help optimize the weight of the vehicle.

Sales and Marketing

Company-Owned Stores and Galleries

We market and sell cars directly to consumers through an international network of company-owned stores and galleries. Our Tesla stores and galleries are highly visible, premium outlets in major metropolitan markets, some of which combine retail sales and service. We have also found that opening a service center in a new geographic area can increase demand. As a result, we have complemented our store strategy with sales facilities and personnel in service centers to more rapidly expand our retail footprint. We refer to these as “Service Plus” locations. Including all of our sales, Service Plus and service facilities, we operated 159 locations around the world as of December 31, 2014.

We believe that by owning our own sales and service network we can offer a compelling customer experience while achieving operating efficiencies and capturing sales and service revenues incumbent automobile manufacturers do not enjoy in the traditional franchised distribution and service model. Our customers deal directly with our own Tesla-employed sales and service staff, creating what we believe is a differentiated buying experience from the buying

experience consumers have with franchised automobile dealers and service centers. We believe we will also be able to better control costs of inventory, manage warranty service and pricing, maintain and strengthen the Tesla brand, and obtain rapid customer feedback. Further, we believe that by owning our sales network we will avoid the conflict of interest in the traditional dealership structure inherent to most incumbent automobile manufacturers where the sale of warranty parts and repairs by a dealer are a key source of revenue and profit for the dealer but often are an expense for the vehicle manufacturer.

Tesla Supercharger Network

We are building a network of up to 120 kW fast charging equipment, each called a Tesla Supercharger, throughout North America, Europe and Asia for fast charging of Model S and future Tesla vehicles. Our Supercharger network is a strategic corporate initiative designed to remove a barrier to the broader adoption of electric vehicles caused by the perception of limited vehicle range and to provide free charging access to Tesla's existing customers. The Tesla Supercharger is an industrial grade, high speed charger designed to replenish 170 miles of range in the battery pack in as little as 30 minutes. Supercharger stations typically have between four to ten Superchargers and are strategically placed primarily along well-travelled highways to allow Model S owners to enjoy long distance travel with convenient, minimal stops. We currently have 380 Supercharger stations open in North America, Europe, and Asia. Access to the Supercharger network is currently available free of charge to owners of Model S vehicles with the 85 kWh battery pack options and when purchased as an upfront option for 60 kWh. We are planning to methodically expand the Supercharger network over the next few years in the United States, Europe and Asia.

Destination Charging

We are working with a wide variety of locations, including hotels and popular destinations, to offer an additional charging option for our customers. These destination charging partners deploy our wall connectors and provide charging free of charge to Model S owners. Almost 1,000 locations in Asia and North America currently have 1,800 Tesla wall connectors installed. We plan to expand the Destination Charging program into Europe in Q2 of this year.

Orders and Reservations

We typically carry a very limited inventory of our Model S vehicles at our Tesla stores. The vast majority of our customers customize their vehicle by placing an order with us. We require a $2,500 payment to begin production for these, which is collected once the customer has selected the vehicle specifications and has entered into a purchase agreement. In certain markets, we require additional payments a few weeks prior to delivery. We require all remaining payment of the purchase price of the vehicle upon delivery of the vehicle to the customer.

For Model X, which is currently not in production, we require an initial refundable reservation payment of at least $5,000. Reservation payments and deposits are used by us to fund, in part, our working capital requirements and help us to align production with demand.

Marketing

Our principal marketing goals are to:

- generate demand for our vehicles and drive leads to our sales teams;
- build long-term brand awareness and manage corporate reputation;
- manage our existing customer base to create loyalty and customer referrals; and
- enable customer input into the product development process.

Historically, we have been able to generate significant media coverage of our company and our vehicles, and we believe we will continue to do so. To date, media coverage and word of mouth have been the primary drivers of our sales leads and have helped us achieve sales without traditional advertising and at relatively low marketing costs.

Our marketing efforts include events where our vehicles are displayed and demonstrated. These events range from widely attended public events, such as the Detroit, Los Angeles, and Frankfurt auto shows, to smaller events oriented towards sales, such as private drive events.

Service and Warranty

Service

We provide service for our electric vehicles at our company-owned service centers, at our Service Plus locations or, in certain areas for an additional charge, through Tesla Ranger mobile technicians who provide services that do not require a vehicle lift. We own and operate 95 service locations as of December 31, 2014. We are continuing our plan to build a number of additional service centers in several markets worldwide.

Model S is designed with the capability to wirelessly upload the data to us via an on-board GSM system, allowing us to diagnose and remedy many problems before ever looking at the vehicle. When maintenance or service is required, a customer can schedule service by contacting one of our Tesla service centers. Our Tesla Rangers, or mobile service team, can also perform an array of services that do not require a vehicle lift from the convenience of a customer's home or other remote location.

We believe that our company-owned service centers enable our technicians to work closely with our engineers and research and development teams in Silicon Valley to identify problems, find solutions, and incorporate improvements faster than incumbent automobile manufacturers.

New Vehicle Limited Warranty, Maintenance and Extended Service Plans

For our Model S customers, we provide a four year or 50,000 mile New Vehicle Limited Warranty with every Model S, subject to separate limited warranties for the supplemental restraint system and battery. During the third quarter of 2014, we extended the warranty on our Model S drive unit to eight years from four. The New Vehicle Limited Warranty also covers the battery for a period of eight years or 125,000 miles or unlimited miles, depending on the size of the vehicle's battery, although the battery's charging capacity is not covered.

In addition to the New Vehicle Limited Warranty, we offer a comprehensive maintenance program for Model S, which includes plans covering maintenance for up to eight years or up to 100,000 miles and an Extended Service Plan. The maintenance plans cover annual inspections, 24 hour roadside assistance and the replacement of wear and tear parts, excluding tires and the battery, with either a fixed fee per visit for Tesla Ranger service or unlimited Tesla Ranger visits for a higher initial purchase price. The Extended Service Plan covers the repair or replacement of Model S parts for an additional four years or up to an additional 50,000 miles after the New Vehicle Limited Warranty.

For our Roadster customers, we provided a three year or 36,000 mile New Vehicle Limited Warranty with every Tesla Roadster, which we extended to four years or 50,000 miles for the purchasers of our 2008 Tesla Roadster. Customers have the opportunity to purchase an Extended Service Plan for the period after the end of the New Vehicle Limited Warranty to cover the repair or replacement of Roadster parts for up to an additional three years or 36,000 miles, provided they are purchased within a specified period of time. We have previously provided our Tesla Roadster customers with a battery replacement option to replace the battery in their vehicles at any time after the expiration of the New Vehicle Limited Warranty but before the tenth anniversary of the purchase date of their vehicles.

Our New Vehicle Limited Warranties and Extended Service plans are subject to certain limitations, exclusions or separate warranties, including certain wear items, such as tires, brake pads, paint and general appearance, and battery performance, and are intended to cover parts and labor to repair defects in material or workmanship in the body, chassis, suspension, interior, electronic systems, battery, powertrain and brake system. In addition, all plans must be purchased within a specified period of time after vehicle purchase.

Financial Services

We offer loans and leases in North America, Europe and Asia primarily through various financial institutions. We also offer leases directly through our captive finance company in 37 states, the District of Columbia and in 4 provinces of Canada. Certain of our loan programs provide customers with a resale value guarantee under which those customers have the option of selling their vehicle back to us during the period of 36 to 39 months following delivery for a pre-determined resale value. This structure allows the customer to enjoy the benefits of Model S ownership without concern for its resale value. We introduced this program in North America in 2013 and expanded it to selected European markets in 2014. In certain markets, we also offer buy back guarantees to financial institutions which obligate us to repurchase, and the institution to sell us, the vehicles for a pre-determined price. We intend to broaden our financial services offerings during the next few years.

Manufacturing

We conduct our powertrain and vehicle manufacturing and assembly operations at our facilities in Fremont, California; Lathrop, California; and Tilburg, Netherlands. We are also building a cell and battery manufacturing

facility, the Tesla Gigafactory, outside of Reno, Nevada.

The Tesla Factory in Fremont, CA and Manufacturing in Lathrop, CA

We manufacture Model S and certain components that are critical to our intellectual property and quality standards for Model S at the Tesla Factory. The Tesla Factory contains several manufacturing operations, including stamping, machining, casting, plastics, body assembly, paint operations, final vehicle assembly and end-of-line testing. In addition, we manufacture lithium-ion battery packs, electric motors, gearboxes and components both for our vehicles and for our original equipment manufacturer customers at the Tesla Factory. Several major component systems of our vehicles are purchased from suppliers; however we have a high level of vertical integration in our manufacturing processes at the Tesla Factory. We recently commenced production and machining of various aluminum components at our facility in Lathrop, California.

We continue to increase our production capacity at the Tesla Factory with the goal of producing Model S, Model X and Model 3 at this location. In 2015, we intend to create a new body shop line to prepare for the expanded production of both Model S and Model X. We are also finishing the construction of a new high volume paint shop, to be used for Model S, Model X and Model 3.

The Netherlands

Our European headquarters is located in Amsterdam, Netherlands and houses our sales, service, and administrative functions. We also have operations in Tilburg, Netherlands for final assembly, testing and quality control for vehicles ultimately delivered into the European Union. The Tilburg facility also serves as a pan-European parts warehouse, remanufacturing site and customer service center.

The Tesla Gigafactory outside of Reno, Nevada

We are developing the Tesla Gigafactory as a facility where we work together with our suppliers to integrate battery precursor material, cell, module and battery pack production in one location. We plan to use the battery packs manufactured at the Gigafactory for our vehicles and for our stationary storage applications. We broke ground on the Gigafactory in June 2014 and currently expect to produce cells at this site beginning in 2016 for use initially in Model S and Model X. The Gigafactory is currently expected to attain full production capacity in 2020, which is anticipated to be sufficient for the production of approximately 500,000 vehicles annually as well as for the production of our stationary storage applications. By the time the Gigafactory reaches full, annualized production in 2020, we expect battery pack production capacity to reach 50 GWh. Of this, we expect to build 35 GWh of cell production capacity at the Gigafactory and purchase 15 GWh of cells from other manufacturers, potentially including Panasonic.

We believe that the Gigafactory will allow us to achieve a major reduction in the cost of our battery packs of greater than 30% on a per kWh basis by the end of the first year of volume production of Model 3. The total capital expenditures associated with the Gigafactory through 2020 are expected to be $4-$5 billion, of which approximately $2 billion is expected to come from Tesla. Panasonic has agreed to partner with us on the Gigafactory with investments in production equipment that it will use to manufacture and supply us with battery cells. We have agreed to prepare and provide the land, buildings and utilities, invest in production equipment for battery module and pack production and be responsible for the overall management. We expect to announce other partners as construction progresses.

Supply Chain

Model S uses over 3,000 purchased parts which we source globally from over 350 suppliers, the majority of whom are currently our single source suppliers for these components. We have developed close relationships with several key suppliers particularly in the procurement of cells and certain other key system parts. While we obtain components from multiple sources whenever possible, similar to other automobile manufacturers, many of the components used in our vehicles are purchased by us from a single source. In addition, while several sources of the battery cell we have selected for our battery packs are available, we have currently fully qualified only one cell. We expect to fully qualify additional cells from other manufacturers in 2015.

We use various raw materials in our business including aluminum, steel, cobalt, nickel and copper. The prices for these raw materials fluctuate depending on market conditions and global demand for these materials. We believe that we have adequate supplies or sources of availability of the raw materials necessary to meet our manufacturing and supply requirements. There are always risks and uncertainties, however, with respect to the supply of raw materials that could impact their availability in sufficient quantities or reasonable prices to meet our needs.

Quality Control

Our quality control efforts are divided between product quality and supplier quality, both of which are focused on designing and producing products and processes with high levels of reliability. Our product quality engineers work with our engineering team and our suppliers to help ensure that the product designs meet functional specifications and

durability requirements. Our supplier quality engineers work with our suppliers to ensure that their processes and systems are capable of delivering the parts we need at the required quality level, on time, and on budget.

Customers and Selected Relationships

We currently sell our cars primarily to individual customers. We have strategic or commercial relationships with Panasonic, Daimler, and Toyota.

Panasonic

Panasonic supplies us with battery cells for our battery packs and has partnered with us on the construction of the Gigafactory. In January 2010, we announced that we were collaborating with Panasonic on the development of next-generation electric vehicle cells based on the 18650 form factor and nickel-based lithium ion chemistry. In October 2011, we finalized a supply agreement for these battery cells. In October 2013, we entered into an amendment to the supply agreement to, among other things, provide for the long-term preferential prices and a minimum of 1.8 billion lithium-ion battery cells that we intend to purchase from Panasonic from 2014 through 2017. In July 2014, Panasonic agreed to partner with us on the Gigafactory.

Daimler AG

Beginning in 2008, we commenced efforts on a powertrain development arrangement with Daimler. Since that time, we have developed and produced powertrain components for Daimler for the Smart fortwo electric drive program, the A-Class electric vehicle program and the B-Class electric vehicle program. We started to supply production parts for the B-Class electric vehicle program in 2014 and expect to continue to supply parts under this program for the next few years.

Toyota Motor Corporation

In May 2010, we and Toyota announced our intention to cooperate on the development of electric vehicles, and for us to receive Toyota's support with sourcing parts and production and engineering expertise for Model S. Since that time, we have developed and produced a validated powertrain system, including a battery, power electronics module, motor, gearbox and associated software, which was integrated into an electric vehicle version of the Toyota RAV4. We began delivery of these systems to Toyota for installation into the Toyota RAV4 EV in the first half of 2012. During the third quarter of 2014, we completed the RAV4 EV program.

Governmental Programs, Incentives and Regulations

Full Repayment of United States Department of Energy Loans

In May 2013, we paid $451.8 million to settle all outstanding loan amounts due under a loan facility we had entered into with the Federal Financing Bank (FFB) and the United States Department of Energy (DOE), under the DOE's Advanced Technology Vehicles Manufacturing Loan Program, as set forth in Section 136 of the Energy Independence and Security Act of 2007 (ATVM Program). We refer to the loan facility with the DOE as the DOE Loan Facility.

Under the DOE Loan Facility, the FFB had made available to us two multi-draw term loan facilities in an aggregate principal amount of $465.0 million beginning on January 20, 2010. As of August 31, 2012, we had fully drawn down the aforementioned facilities. On May 22, 2013, we paid $451.8 million to fully retire our obligations under the DOE Loan Facility.

In connection with the closing of the DOE Loan Facility, we had also issued a warrant to the DOE to purchase up to 9,255,035 shares of our Series E convertible preferred stock at an exercise price of $2.51 per share. Upon the completion of our initial public offering on July 2, 2010, this preferred stock warrant became a warrant to purchase up to 3,090,111 shares of common stock at an exercise price of $7.54 per share. As a result of our repayment of all outstanding principal and interest under the DOE Loan Facility and the termination of the DOE Loan Facility in May 2013, the DOE warrant expired. Additionally, we amortized all remaining unamortized debt issuance costs related to the DOE Loan Facility.

California Alternative Energy and Advanced Transportation Financing Authority Tax Incentives

In December 2009, we finalized an arrangement with the California Alternative Energy and Advanced Transportation Financing Authority (CAEATFA) that resulted in an exemption from California state sales and use taxes for the purchase of $320 million of manufacturing equipment. As the equipment purchased would otherwise have been subject to California state sales and use tax, we believe this incentive resulted in tax savings by us of approximately $31 million over the period starting in December 2009 and ending in December 2013. The equipment purchases were used for three purposes: (i) to establish our production facility for Model S in California, (ii) to upgrade our Palo Alto powertrain production facility, and (iii) to expand our Tesla Roadster assembly operations at our Menlo Park facility. We exhausted all funds from the December 2009 approved exemption from California state sales and use taxes for

$320 million of manufacturing equipment in December 2013.

In January 2012, we finalized an additional agreement with CAEATFA for an exclusion from California state sales and use taxes for the purchase of up to $292 million of manufacturing equipment. To the extent all of this equipment is purchased and would otherwise be subject to California state sales or use tax, we believe this incentive would result in tax savings by us of up to approximately $24 million over the period starting in December 2011 and ending in December 2015. The equipment purchased under this exclusion may only be used for two purposes: (i) to develop Model X and its production capacity in California and (ii) to further upgrade our powertrain production facilities in California. We have not yet exhausted the $292 million in funds approved by CAEATFA in 2012.

In December 2013, we finalized a third agreement with CAEATFA that will result in an exclusion from California state sales and use taxes for an additional $415 million of manufacturing equipment. To the extent all of this equipment is purchased and would otherwise be subject to California state sales or use tax, we believe this 2013 incentive would result in tax savings by us of up to approximately $35 million over the period starting in December 2013 and ending in December 2016. The equipment purchased under this exclusion may only be used for three purposes: (i) to expand Model S manufacturing capacity in California; (ii) to expand electric vehicle powertrain production in California; and (iii) future Model S electric vehicle development.

Regulatory Credits

In connection with the production, delivery, and placement into service of our zero emission vehicles in global markets, we have earned and will continue to earn various tradable regulatory credits that can be sold to other manufacturers.

Under California's Zero-Emission Vehicle Regulations and those of states that have adopted the California standards, vehicle manufacturers are required to ensure that a portion of the vehicles delivered for sale in those states during each model year are zero-emission vehicles and partial zero-emission vehicles. Currently, the states of Arizona, California, Connecticut, Maine, Maryland, Massachusetts, New Jersey, New Mexico, New York, Oregon, Rhode Island and Vermont have such laws in effect. These laws provide that a manufacturer may earn credits, referred to as ZEV credits, if they produce more zero-emission vehicles than the minimum quantity required by those laws. Those manufacturers with a surplus of credits may sell the excess credits to other manufacturers who can then apply such credits to comply with the regulatory requirements, including making up for deficits. As a manufacturer solely of zero-emission vehicles, we have no minimum requirement, and therefore earn ZEV credits on each vehicle delivered and placed into service in such states. We have entered into agreements with other automobile manufacturers to sell the ZEV credits that we earn. Recently, California passed amendments to the ZEV mandate that would require, starting in 2018, all large-volume manufacturers (those manufacturers selling 20,000 or more vehicles in California in 2018) to increase the number of zero emission vehicles sold, such that 15.4% of each manufacturers' fleet must be made of zero emission vehicles by 2025. All states that have adopted the California program will amend their programs to conform to the new California standards.

Additionally, under the Environmental Protection Agency's (EPA) national greenhouse gas (GHG) emission standards and similar standards adopted by the Canadian government, car and truck manufacturers are required to meet fleet-wide average carbon dioxide emissions standards. Manufacturers who fail to meet such standards have a deficit in their emission profile. Manufacturers whose fleet wide average performs better than such standards may earn credits. Manufacturers may sell excess credits to other manufacturers, who can use the credits to comply with these regulatory requirements. As a manufacturer solely of zero emission vehicles, we earn the full amount of GHG credits established by the standards on each vehicle sold. We have contracted with another automobile manufacturer to sell all earned credits.

Under the National Highway Traffic Safety Administration's (NHTSA) Corporate Average Fuel Economy (CAFE) standards, car and truck manufacturers are required to meet fleet-wide average fuel economy standards. Manufacturers that fail to meet such standards have a deficit in their fuel economy profile. Manufacturers whose fleet-wide average performs better than such standards may earn credits. Manufacturers may sell excess credits to other manufacturers, who can use such credits to comply with these regulatory requirements. We have entered into agreements to sell the credits that we earn.

Regulation—Vehicle Safety and Testing

Our vehicles are subject to, and comply with or are otherwise exempt from, numerous regulatory requirements established by NHTSA, including all applicable United States Federal Motor Vehicle Safety Standards (FMVSS). The Model S fully complies with all FMVSSs without the need for any exemptions. The Roadster complies with or is exempt from all FMVSS.

As a manufacturer, we must self-certify that our vehicles meet all applicable FMVSS, as well as the NHTSA bumper standard, or otherwise are exempt, before the vehicles can be imported or sold in the United States. Numerous FMVSS apply to our vehicles, such as crash-worthiness requirements, crash avoidance requirements, and electric vehicle requirements. We are also required to comply with other federal laws administered by NHTSA, including the

CAFE standards, Theft Prevention Act requirements, consumer information labeling requirements, Early Warning Reporting requirements regarding warranty claims, field reports, death and injury reports and foreign recalls, and owner's manual requirements.

The Automobile Information and Disclosure Act requires manufacturers of motor vehicles to disclose certain information regarding the manufacturer's suggested retail price, optional equipment and pricing. In addition, the Act allows inclusion of city and highway fuel economy ratings, as determined by EPA, as well as crash test ratings as determined by NHTSA if such tests are conducted.

Our vehicles sold in outside of the U.S. are subject to foreign safety testing regulations. Many of those regulations are different from the federal motor vehicle safety standards applicable in the United States and may require redesign and/or retesting.

Regulation—EPA Emissions & Certificate of Conformity

The Clean Air Act requires that we obtain both an EPA-issued Certificate of Conformity and a California Air Resources Board (CARB)-issued Executive Order with respect to emissions for our vehicles. The Certificate of Conformity is required for vehicles sold in states covered by the Clean Air Act's standards and both the Certificate of Conformity and the Executive Order are required for vehicles sold in states that have sought and received a waiver from the EPA to utilize California standards. The California standards for emissions control for certain regulated pollutants for new vehicles and engines sold in California are set by CARB. States that have adopted the California standards as approved by EPA also recognize the Executive Order for sales of vehicles.

Regulation—Battery Safety and Testing

Our battery pack conforms to mandatory regulations that govern transport of “dangerous goods”, defined to include lithium-ion batteries, which may present a risk in transportation. The governing regulations, issued by the Pipeline and Hazardous Materials Safety Administration (PHMSA), are based on the United Nations (UN) Recommendations and Model Regulations on the Transport of Dangerous Goods, as well as related UN Manual Tests and Criteria. The regulations vary by mode of shipping transportation, such as by ocean vessel, rail, truck, or air. We have completed the applicable transportation tests for our prototype and production battery packs, demonstrating our compliance with the UN Manual of Tests and Criteria. We also subject our battery packs to the appropriate tests specified in the Society of Automotive Engineers (SAE) J2464 and J2929 standards, which incorporate tests such as immersion, humidity, and exposure to fire.

We use lithium metal oxide cells in our high voltage battery packs. The cells do not contain any lead, mercury, cadmium, other hazardous materials, heavy metals, or toxic materials. Our battery packs include certain packaging materials that contain trace amounts of hazardous chemicals whose use, storage, and disposal is regulated under federal law. We currently have an agreement with a third party battery recycling company to recycle our battery packs. If a customer wishes to dispose of a battery pack from one of our vehicles, we anticipate accepting the depleted battery from the customer without any additional charge.

Automobile Manufacturer and Dealer Regulation

State laws regulate the manufacture, distribution, and sale of automobiles, and generally require motor vehicle manufacturers and dealers to be licensed in order to sell vehicles directly to consumers in the state. As we open additional Tesla stores and service centers, we secure dealer licenses (or their equivalent) and engage in sales activities to sell our vehicles directly to consumers. A few states, such as Texas and Michigan, do not permit automobile manufacturers to be licensed as dealers or to act in the capacity of a dealer, or otherwise restrict a manufacturer’s ability to deliver or service vehicles. To sell vehicles to residents of states where we are not licensed as a dealer, we must generally conduct the sale out of the state via the internet, phone or mail. In such states, we have opened “galleries” that serve an educational purpose and are not retail locations.

As we expand our retail footprint in the United States, some automobile dealer trade associations have both challenged the legality of our operations in court and used administrative and legislative processes to attempt to prohibit or limit our ability to operate existing stores or expand to new locations. Although we have thus far prevailed in every lawsuit brought by dealer associations, we expect that the dealer associations will continue to mount challenges to our business model. In addition, we expect the dealer associations to actively lobbying state Governors and legislators to interpret existing laws or enact new laws in ways not favorable to Tesla’s ownership and operation of its own retail and service locations.

While we have analyzed the principal laws in the US, EU, China, Japan, UK, and Australia relating to our distribution model and believe we comply with such laws, we have not performed a complete analysis of all jurisdictions in which we may sell vehicles. Accordingly, there may be laws in certain jurisdictions that may restrict our sales and service operations.

Competition

The worldwide automotive market, particularly for alternative fuel vehicles, is highly competitive today and we expect it will become even more so in the future as we introduce additional, lower priced vehicles such as our Model 3. We believe the impact of new regulatory requirements for occupant safety and vehicle emissions, technological advances in powertrain and consumer electronics components, and shifting customer needs and expectations are

causing the industry to evolve in the direction of electric-based vehicles. We believe the primary competitive factors in our markets include but are not limited to:

- technological innovation;
- product quality and safety;
- service options;
- product performance;
- design and styling;
- brand perception;
- product price; and
- manufacturing efficiency.

We believe that our vehicles compete in the market both based on their traditional segment classification as well as based on their propulsion technology. For example, Model S competes primarily in the extremely competitive premium sedan market with internal combustion vehicles from more established automobile manufacturers, including Audi, BMW, Lexus and Mercedes. Our vehicles also compete with vehicles propelled by alternative fuels, principally electricity.

Many established and new automobile manufacturers have entered or have announced plans to enter the alternative fuel vehicle market. BMW, Daimler, Nissan, Fiat, Ford and Mitsubishi, among others, have electric vehicles available today. Moreover, Porsche, Lexus, Audi, Volkswagen and Volvo are also developing electric vehicles. Electric vehicles have also already been brought to market in China and other foreign countries and we expect a number of those manufacturers to enter the United States market as well. In addition, several manufacturers, including General Motors, Toyota, Ford, and Honda, are each selling hybrid vehicles, and certain of these manufacturers have announced plug-in versions of their hybrid vehicles.

Most of our current and potential competitors have significantly greater resources than we do, may be able to devote greater resources to the manufacture, sale and support of their products, and have other advantages. We believe our exclusive focus on electric vehicles and electric vehicle components, as well as our history of vehicle development and production, however, are the basis on which we can compete in the global automotive market in spite of the challenges posed by our competition.

Intellectual Property

As part of our business, we seek to protect our intellectual property rights in various ways, including through trademarks, copyrights, trade secrets, including know-how, patents, patent applications, employee and third party nondisclosure agreements, intellectual property licenses and other contractual rights. Additionally, consistent with our mission to accelerate the advent of sustainable transport, we announced a patent policy in which we irrevocably pledged that we will not initiate a lawsuit against any party for infringing our patents through activity relating to electric vehicles or related equipment for so long as such party is acting in good faith. We made this pledge in order to encourage the advancement of a common, rapidly-evolving platform for electric vehicles, thereby benefiting ourselves, other companies making electric vehicles, and the world.

Segment Information

We have determined that we operate as one reportable segment, which is the design, development, manufacturing and sales of electric vehicles and electric powertrain components. For information regarding financial data by geographic areas, see Note 10 to our Consolidated Financial Statements included in this Annual Report on Form 10-K under Item 8. Financial Statements and Supplementary Data.

Employees

As of December 31, 2014, we had 10,161 full-time employees. To date, we have not experienced any work stoppages, and we consider our relationship with our employees to be good.

Available Information

We file or furnish periodic reports and amendments thereto, including our Annual Reports on Form 10-K, our Quarterly Reports on Form 10-Q and Current Reports on Form 8-K; proxy statements and other information with the Securities and Exchange Commission (SEC). Such reports, amendments, proxy statements and other information may be obtained by visiting the Public Reference Room of the SEC at 100 F Street, NE, Washington, D.C. 20549. Information on the operation of the Public Reference Room can be obtained by calling the SEC at 1-800-SEC-0330. In addition, the SEC maintains a website (www.sec.gov) that contains reports, proxy and information statements, and other information regarding issuers that file electronically. Our reports, amendments thereto, proxy statements and other information are also made available, free of charge, on our investor relations website at ir.teslamotors.com as soon as reasonably practicable after we electronically file or furnish such information with the SEC. The information posted on our website is not incorporated by reference into this Annual Report on Form 10-K.

ITEM 1A. RISK FACTORS

You should carefully consider the risks described below together with the other information set forth in this report, which could materially affect our business, financial condition and future results. The risks described below are not the only risks facing our company. Risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and operating results.

Risks Related to Our Business and Industry

We may experience significant delays or other complications in the design, manufacture, launch and production ramp of Model X, as well as future vehicles such as Model 3, which could harm our brand, business, prospects, financial condition and operating results.

We may experience significant delays or other complications in bringing new vehicles to market. For example, while we expect Model X deliveries to start in the third quarter of 2015, refinements resulting from ongoing development and extensive testing of this vehicle could result in delays in its introduction. Complications could also arise from other factors, including the expansion of our production capacity required to bring Model X to market, finalization of it supply chain, and completion of regulatory approvals. Ahead of the Model X launch, we plan to expand capacity in several areas for our current and future vehicles, including installing a state of the art, highly automated casting and machining operation for various aluminum components for our vehicles, increasing production on our new drive unit line, installing a new robotic body assembly shop for Model X production and commissioning a new paint facility. Our suppliers may not be able to provide components in a timely manner, at an acceptable price or in the necessary quantities. Finally, we will also need to do extensive testing to ensure that Model X is in compliance with applicable NHTSA safety regulations and obtain EPA and CARB certification to emission regulations prior to beginning volume production and delivery of the vehicles.

We, as well as other automobile manufacturers, have experienced delays or other complications in connection with new vehicle models. In 2012, we experienced delays in the production ramp of Model S and in 2014, we delayed the start of production ramp of All-Wheel Drive Dual Motor Model S. Any significant delay or other complication in the development, manufacture, launch and production ramp of Model X or our future vehicles, including complications associated with expanding our production capacity, supply chain or regulatory approvals, could materially damage our brand, business, prospects, financial condition and operating results.

Our long-term success will be dependent upon our ability to design, build and achieve market acceptance of new vehicle models, specifically Model S and new vehicle models such as Model X and Model 3.

Our long-term success is dependent on market acceptance of the Model S sedan and future electric vehicles we introduce. In the United States, there is no guarantee that Model S will continue to be successfully accepted by the general public, especially in the long-term. As we expand in Europe and Asia, there is no guarantee that customers in these markets will embrace our vehicles and if they do not, demand for our vehicles could be lower than our expectations.

Moreover, there can be no assurance that we will be able to design future electric vehicles that will meet the expectations of our customers or that our future models, including the Model X crossover, will become commercially viable. To date, we have publicly revealed only an early prototype of the Model X. Work continues on the finalization of Model X with Beta Model X vehicles undergoing extensive testing. To the extent that we are not able to build Model X in accordance with the expectations created by the early prototype and our announced specifications and schedule, customers may cancel their reservations, our future sales could be harmed and investors may lose confidence in us.

In addition, we have also announced our intent to develop Model 3 which we expect to produce at the Tesla Factory after the introduction of Model X. We intend to offer this vehicle at a lower price point and expect to produce it at higher volumes than our Model S. Importantly, we anticipate producing Model 3 for the mass market and thus we will need a high-volume supply of lithium-ion cells at reasonable prices.

While we intend each of our production vehicles and their variants to meet a distinct segment of the automotive market, our vehicles may end up competing with each other which may delay sales and associated revenue to future periods. Also, if we fail to accurately anticipate demand for each of our vehicles, this could result in inefficient expenditures and production delays. Furthermore, historically, automobile customers have come to expect new and improved vehicle models to be introduced frequently. In order to meet these expectations, we may be required to introduce on a regular basis new vehicle models as well as enhanced versions of existing vehicle models. As automotive technologies change, including those specific to electric vehicles, we anticipate our customers will expect us to upgrade or adapt our vehicles and introduce new models in order to continue to provide vehicles with the latest technology. To date, we have limited experience simultaneously designing, testing, manufacturing, upgrading, adapting and selling our electric vehicles as well as limited experience allocating our available resources among the design and production of multiple vehicles.

We may be unable to increase production and deliveries of Model S in line with our plans, both of which could harm our business and prospects.

Since we began manufacturing and delivering Model S in 2012, we have significantly increased production and deliveries, and our plans call for an even greater increase in production and deliveries going forward. As part of this effort, we recently completed a new final assembly line and added more automation to our body shop at the Fremont factory, are installing a highly automated casting and machining operation for various aluminum components and are finishing the construction of a new high volume paint shop. Our ability to further ramp-up high volume Model S production, including for the All-Wheel Drive Dual Motor Model S, which we recently began producing for the first time, will depend upon a number of factors, including our ability to use these new manufacturing processes as planned while maintaining our desired quality levels, our suppliers' ability to deliver quality parts to us in a timely manner, and efficiently making design changes to ensure consistently high quality. To produce a vehicle that meets our quality standards requires us to carefully analyze each step of our production plan, improve the efficiency of our manufacturing processes and continue to train our employees. Our suppliers also must produce new products in sufficient quantities and quality to meet our demand. Certain suppliers have experienced delays in meeting our demand or have sought to renegotiate the terms of the supply arrangements, and we continue to focus on supplier capabilities and constraints. Any disruption in increasing our production level of Model S in line with our plans could materially damage our brand, business, prospects, financial condition and operating results.

In addition, for Model S we have introduced a number of new manufacturing technologies and techniques, such as aluminum spot welding systems, which have not been widely adopted in the automotive industry; and the Model S has a number of new and unique design features, such as a 17 inch display screen, retractable exterior door handles, and all-new dual motor and autopilot hardware, each of which poses unique manufacturing challenges. Model S production and deliveries will continue to require significant resources and we may experience unexpected delays or difficulties that could harm our ability to maintain full manufacturing capacity for Model S, or cause us to miss planned production targets, any of which could have a material adverse effect on our financial condition and operating results. Additionally, sustaining high volume production and doing so in a manner that avoids significant cost overruns, including as a result of factors beyond our control such as problems with suppliers and vendors, may be difficult.

Concurrent with the significant increase in our planned production levels, we will also need to continue to significantly increase our deliveries of Model S vehicles. We have limited experience in delivering a high volume of Model S vehicles, and, in particular, to locations outside of the United States. We may face difficulties meeting our delivery and growth plans in Asia and the right hand drive markets we have entered, which may impact our ability to achieve our worldwide delivery goals. If we are unable to ramp up to meet our delivery goals globally to match our production rate of Model S, this could result in negative publicity, damage our brand and have a material adverse effect on our business, prospects, financial condition and operating results.

Our ability to grow volume production and deliveries for Model S is subject to certain risks and uncertainties, including:

- that our suppliers will be able and willing to deliver components on a timely basis and in the necessary quantities, quality and at acceptable prices to produce Model S in volume and reach our financial targets;
- that we will be able to complete any necessary adjustments to the vehicle design or manufacturing processes of Model S in a timely manner that meets our production plan and allows for high quality vehicles;
- that we will be able to fully ramp production of All-Wheel Drive Dual Motor Model S to keep up with demand;
- that we will be able to ramp sales of Model S throughout Asia, pursuant to our current timeline;
- that we will be able to adequately respond in a timely manner to any problems that may arise with our vehicles;
- that we will be able to schedule and complete deliveries at our planned higher volume production levels;

that the equipment or tooling which we have purchased or which we select, including those that are part of our higher capacity production line that recently became operational, will be able to accurately manufacture the vehicle within specified design tolerances, and will not suffer from unexpected breakdowns or damage which could negatively affect the rate needed to produce vehicles in volume;

that we will be able to comply with environmental, workplace safety, customs and similar regulations required to operate our manufacturing facilities;

that we will be able to maintain and improve quality controls as we transition to a higher level of in-house manufacturing process; and

that the information technology systems that we are currently expanding and improving upon will be effective to manage higher volume production.

Finally, detailed long-term testing of quality, reliability and durability of Model S is ongoing and any negative results from such testing could cause production or delivery delays, cost increases, or lower quality of our Model S vehicles.

Problems or delays in bringing the Gigafactory online and operating it in line with our expectations could negatively affect us.

To lower the cost of cell production and produce cells in volume to allow us to grow quickly, we intend to integrate the production of lithium-ion cells and finished battery packs for our vehicles at our new Gigafactory. Our Gigafactory plan, however, is at an early stage. While we recently entered into various formal agreements with Panasonic on the Gigafactory, we have very little experience in building a factory of the size and scope planned for the Gigafactory, and no experience directly in the production of lithium-ion cells. In addition, to date we have not finalized agreements with additional Gigafactory partners that will be co-located at the Gigafactory. Also, the cost of building and operating the Gigafactory could exceed our current expectations and the Gigafactory may take longer to bring online than we anticipate. If we are unable to build the Gigafactory in a timely manner to produce high volumes of quality lithium-ion cells at reasonable prices, then our ability to supply battery packs to our vehicles, including Model 3, according to our schedule and/or at a price that allows us to sell them profitably and in the quantities we estimate could be constrained. Any such problems or delays with Gigafactory could negatively affect our brand and harm our business, prospects, financial condition and operating results.

If our vehicles or vehicles that contain our powertrains fail to perform as expected, or if we suffer product recalls, our ability to develop, market and sell our electric vehicles could be harmed.

Our vehicles or vehicles that contain our powertrains such as the Toyota RAV4 EV or the Mercedes-Benz B-Class EV may contain defects in design and manufacture that may cause them not to perform as expected or that may require repair. For example, our vehicles are highly dependent on software to operate. Software products are inherently complex and often contain defects and errors when first introduced, and changes to software may have unexpected effects. Model S issues experienced by customers include those related to the software for the 17 inch display screen, the panoramic roof and the 12 volt battery. Although we attempt to remedy the Model S issues experienced by our customers in a rapid manner, such efforts may not be timely or up to the satisfaction of our customers.

While we have performed extensive internal testing, we currently have a limited frame of reference by which to evaluate the long-term performance of our battery packs, powertrains and vehicles. Specifically, we have only a limited amount of data by which to evaluate Model S, upon which our business prospects depend, due to the fact that we only recently began production in June 2012. There can be no assurance that we will be able to detect and fix any defects in the vehicles prior to their sale to consumers.

We have experienced product recalls, including in May 2009, October 2010, and June 2013, all of which were unrelated to our electric powertrain. In May 2009, we initiated a product recall after we determined that a condition caused by insufficient torqueing of the rear inner hub flange bolt existed in some of our Tesla Roadsters, as a result of a missed process during the manufacture of the Tesla Roadster glider, which is the partially assembled Tesla Roadster that does not contain our electric powertrain. In October 2010, we initiated a product recall for some of our Tesla Roadsters after the 12 volt, low voltage auxiliary cable in a single vehicle chafed against the edge of a carbon fiber panel in the vehicle causing a short, smoke and possible fire behind the right front headlamp of the vehicle. In June 2013, we initiated a recall of slightly more than a thousand Model S vehicles to inspect and repair rear seat strikers that may have been compromised during the assembly process. Rear seat strikers are used to retain the rear seat backs in an upright position. Failure of this component may have resulted in the collapse of the rear seat back during a crash. Although the cost of this recall was not material, and limited to a small number of total Model S's produced, we may experience additional recalls in the future, which could adversely affect our brand in our target markets, as well as our business, prospects and results of operations.

In January 2014 we implemented a firmware update to address issues with certain Universal Mobile Connector NEMA 14-50 adapters, which are part of the charging units and are not part of the vehicles themselves, potentially

overheating during charging. We further announced that we would provide upgraded NEMA 14-50 adapters to our customers as an additional safeguard. If such measures do not adequately address the underlying concerns, our business, prospects and results of operations could be harmed.

Our electric vehicles may not perform consistent with customers' expectations or consistent with other vehicles currently available. For example, our electric vehicles may not have the durability or longevity of current vehicles, and may not be as easy to repair as other vehicles currently on the market. Additionally, while Model S recently achieved an overall five star safety rating by NHTSA, there is no guarantee that future model years or variants or other Tesla vehicles will also attain such safety ratings, and any such rating is not a guarantee of safe product design or that any individual vehicle will be free of any defect or failure.

Any product defects or any other failure of our performance electric vehicles to perform as expected could harm our reputation and result in adverse publicity, lost revenue, delivery delays, product recalls, product liability claims, harm to our brand and reputation, and significant warranty and other expenses, and could have a material adverse impact on our business, financial condition, operating results and prospects.

We are dependent on our suppliers, the majority of which are single source suppliers, and the inability of these suppliers to continue to deliver, or their refusal to deliver, necessary components of our vehicles in a timely manner at prices, quality levels, and volumes acceptable to us would have a material adverse effect on our financial condition and operating results.

Model S contains numerous purchased parts which we source globally from over 300 direct suppliers, the majority of whom are currently single source suppliers for these components. We expect that Model X will be sourced in an approximately similar manner. While we obtain components from multiple sources whenever possible, similar to other automobile manufacturers, the majority of the components used in our vehicles are purchased by us from single sources. To date we have not qualified alternative sources for most of the single sourced components used in our vehicles and we do not maintain long-term agreements with a number of our suppliers.

While we believe that we may be able to establish alternate supply relationships and can obtain or engineer replacement components for our single source components, we may be unable to do so in the short term, or at all, at prices or costs that are favorable to us. In particular, while we believe that we will be able to secure alternate sources of supply for most of our single sourced components in a relatively short time frame, qualifying alternate suppliers or developing our own replacements for certain highly customized components of our vehicles may be time consuming, costly and may force us to make additional modifications to a vehicle's design.

This limited supply chain exposes us to multiple potential sources of delivery failure or component shortages for our vehicles, as well as for our powertrain component sales activities. For example, earthquakes similar to the one that occurred in Japan in March 2011 or labor issues such as work stoppages or strikes at the ports on the west coast could negatively impact our supply chain. We have in the past experienced source disruptions in our supply chains, including those relating to our slower-than-anticipated ramp in our Model S production goals for 2012. We may experience additional delays in the future with respect to Model S, Model X and any other future vehicle we may produce.

In addition, because we have written agreements in place with the majority, but not all, of our suppliers, this may create uncertainty regarding a supplier's obligations to us, including but not limited to, those regarding warranty and product liability. Changes in business conditions, wars, governmental changes and other factors beyond our control or which we do not presently anticipate, could also affect our suppliers' ability to deliver components to us on a timely basis. Furthermore, if we experience significantly increased demand, or need to replace certain existing suppliers, there can be no assurance that additional supplies of component parts will be available when required on terms that are favorable to us, at all, or that any supplier would allocate sufficient supplies to us in order to meet our requirements or fill our orders in a timely manner. In the past, we have replaced certain suppliers because of their failure to provide components that met our quality control standards. The loss of any single or limited source supplier or the disruption in the supply of components from these suppliers could lead to delays in vehicle deliveries to our customers, which could hurt our relationships with our customers and also materially and adversely affect our financial condition and operating results.

Changes in our supply chain have resulted in the past, and may result in the future, in increased cost and delay. We have also experienced cost increases from certain of our suppliers in order to meet our quality targets and development timelines as well as due to design changes that we made, and we may experience similar cost increases in the future. Additionally, we are negotiating with existing suppliers for cost reductions, seeking new and less expensive suppliers for certain parts, and attempting to redesign certain parts to make them cheaper to produce. If we are unsuccessful in our efforts to control and reduce supplier costs, our operating results will suffer. Additionally, cost reduction efforts may interrupt or harm our normal production processes, thereby harming vehicle quality or reducing Model S production output.

Furthermore, a failure by our suppliers to provide the components in a timely manner or at the level of quality necessary to manufacture our performance electric vehicles could prevent us from fulfilling customer orders in a timely fashion which could result in negative publicity, damage our brand and have a material adverse effect on our business, prospects, financial condition and operating results.

Finally, in October 2013, we entered into an amendment to our existing supply agreement with Panasonic Corporation in order to address our anticipated short- to medium-term lithium-ion battery cell needs. While we expect that this supply agreement, as amended, will provide us with sufficient cells for the next few years, we may not be able to meet our long-term needs, including for Model 3 and other programs we may introduce, without securing additional suppliers or other sources for cells. We have recently signed an agreement with Panasonic to be our partner in the Gigafactory and be responsible for, among other things, manufacturing cells from there for use in our products. If we encounter unexpected difficulties with our current suppliers, including Panasonic, and if we are unable to fill these needs from other suppliers, we could experience production delays, which could have a material adverse effect on our financial condition and operating results.

Our future growth is dependent upon consumers' willingness to adopt electric vehicles.

Our growth is highly dependent upon the adoption by consumers of, and we are subject to an elevated risk of any reduced demand for, alternative fuel vehicles in general and electric vehicles in particular. If the market for electric vehicles in North America, Europe and Asia does not develop as we expect, or develops more slowly than we expect, our business, prospects, financial condition and operating results will be harmed. The market for alternative fuel vehicles is relatively new, rapidly evolving, characterized by rapidly changing technologies, price competition, additional competitors, evolving government regulation and industry standards, frequent new vehicle announcements and changing consumer demands and behaviors.

Other factors that may influence the adoption of alternative fuel vehicles, and specifically electric vehicles, include:

- perceptions about electric vehicle quality, safety (in particular with respect to lithium-ion battery packs), design, performance and cost, especially if adverse events or accidents occur that are linked to the quality or safety of electric vehicles, such as those related to the Chevrolet Volt battery pack fires or incidents involving Model S;
- perceptions about vehicle safety in general, in particular safety issues that may be attributed to the use of advanced technology, including vehicle electronics and regenerative braking systems;
- negative perceptions of electric vehicles, such as that they are more expensive than non-electric vehicles and are only affordable with government subsidies;
- the limited range over which electric vehicles may be driven on a single battery charge and the effects of weather on this range;
- the decline of an electric vehicle's range resulting from deterioration over time in the battery's ability to hold a charge;
- varied calculations for driving ranges achievable by EVs, which is inherently difficult given numerous factors affecting battery range;
- concerns about electric grid capacity and reliability, which could derail our past and present efforts to promote electric vehicles as a practical solution to vehicles which require gasoline;
- concerns by potential customers that if their battery pack is not charged properly, it may become unusable and may need to be replaced;
- the availability of alternative fuel vehicles, including plug-in hybrid electric vehicles;
- improvements in the fuel economy of the internal combustion engine;
- the availability of service for electric vehicles;
- consumers' desire and ability to purchase a luxury automobile or one that is perceived as exclusive;
- the environmental consciousness of consumers;
- volatility in the cost of oil and gasoline;
- consumers' perceptions of the dependency of the United States on oil from unstable or hostile countries;
- government regulations and economic incentives promoting fuel efficiency and alternate forms of energy as well as tax and other governmental incentives to purchase and operate electric vehicles;
- access to charging facilities, standardization of electric vehicle charging systems and consumers' perceptions about convenience and cost to charge an electric vehicle; and
- perceptions about and the actual cost of alternative fuel.

In addition, reports have suggested the potential for extreme temperatures to affect the range or performance of electric vehicles, and based on our own internal testing, we estimate that our vehicles may experience a material reduction in range when operated in extremely cold temperatures. To the extent customers have concerns about such reductions or third party reports which suggest reductions in range greater than our estimates gain widespread acceptance, our ability to market and sell our vehicles, particularly in colder climates, may be adversely impacted.

Additionally, we will become subject to regulations that require us to alter the design of our vehicles, which could negatively impact consumer interest in our vehicles. For example, our electric vehicles make less noise than internal combustion vehicles. Due to concerns about quiet vehicles and vision impaired pedestrians, in January 2011, Congress passed and the President signed the Pedestrian Safety Enhancement Act of 2010. The new law requires NHTSA to establish minimum sounds for electric vehicles and hybrid electric vehicles when travelling at low speeds. NHTSA issued a notice of proposed rulemaking in 2013 and plans to finalize a rule as soon as sometime in 2015 with a potential effective date for implementation as early as 2018. This will begin a three year phase-in schedule for establishing these minimum sounds in all electric and hybrid electric vehicles. Adding this artificial noise may cause current or potential customers not to purchase our electric vehicles, which would materially and adversely affect our business, operating results, financial condition and prospects.

If we fail to manage future growth effectively as we rapidly grow our company, especially internationally, we may not be able to produce, market, sell and service our vehicles successfully.

Any failure to manage our growth effectively could materially and adversely affect our business, prospects, operating results and financial condition. We continue to expand our operations significantly in North America as well as in Europe and Asia. Our future operating results depend to a large extent on our ability to manage this expansion and growth successfully. Risks that we face in undertaking this global expansion include:

- finding and training new personnel, especially in new markets such as Europe and Asia;
- controlling expenses and investments in anticipation of expanded operations;
- establishing or expanding sales, service and Supercharger facilities in a timely manner;
- adapting our products to meet local requirements in countries around the world; and
- implementing and enhancing manufacturing, logistics and administrative infrastructure, systems and processes.

We intend to continue to hire a significant number of additional personnel, including manufacturing personnel, design personnel, engineers and service technicians. Because our high-performance vehicles are based on a different technology platform than traditional internal combustion engines, we may not be able to hire individuals with sufficient training in electric vehicles, and we will need to expend significant time and expense training the employees we do hire. Competition for individuals with experience designing, manufacturing and servicing electric vehicles is intense, and we may not be able to attract, assimilate, train or retain additional highly qualified personnel in the future, the failure of which could seriously harm our business, prospects, operating results and financial condition.

If we are unable to adequately reduce the manufacturing costs of Model S, control manufacturing costs for Model X or otherwise control the costs associated with operating our business, our financial condition and operating results will suffer.

Our production costs for Model S were high initially due to start-up costs at the Tesla Factory, manufacturing inefficiencies including low absorption of fixed manufacturing costs, higher logistics costs due to the immaturity of our supply chain, and higher initial prices for component parts during the initial period after the launch and ramp of Model S. As we have gradually ramped production of Model S, manufacturing costs per vehicle have decreased. While we expect further cost reductions to be realized by both us and our suppliers during the next several quarters, there is no guarantee we will be able to achieve sufficient cost savings to reach our gross margin and profitability goals.

We incur significant costs related to procuring the raw materials required to manufacture our high-performance electric cars, assembling vehicles and compensating our personnel. We may also incur substantial costs or cost overruns in increasing the production capability of Model S and powertrain manufacturing facilities and the recent launch in Asia. Furthermore, if we are unable to produce Model X pursuant to our plan due to cost overruns or other unexpected costs, we may not be able to meet our gross margin targets.

Furthermore, many of the factors that impact our operating costs are beyond our control. For example, the costs of our raw materials and components, such as lithium-ion battery cells or aluminum used to produce body panels, could increase due to shortages as global demand for these products increases. Indeed, if the popularity of electric vehicles exceeds current expectations without significant expansion in battery cell production capacity and advancements in battery cell technology, shortages could occur which would result in increased material costs to us or potentially limit our ability to expand production. Additionally, we may be required to incur substantial marketing costs and expenses to promote our vehicles, including through the use of traditional media such as television, radio and print, even though our marketing expenses to date have been relatively limited as we have to date relied upon unconventional marketing efforts. If we are unable to keep our operating costs aligned with the level of revenues we generate, our operating results, business and prospects will be harmed.

We may fail to meet our publicly announced guidance or other expectations about our business, which would cause our stock price to decline.

We occasionally provide guidance regarding our expected financial and business performance, such as projections regarding the number of vehicles we hope to sell, produce or deliver in future periods and anticipated future revenues, gross margins, profitability and cash flows. Correctly identifying the key factors affecting business conditions and predicting future events is inherently an uncertain process. Our guidance is based in part on assumptions which include, but are not limited to, assumptions regarding:

- our ability to achieve anticipated production and sales volumes and projected average sales prices for Model S and Model X in North America, Europe and Asia;
- supplier and commodity-related costs; and
- planned cost reductions.

Such guidance may not always be accurate or may vary from actual results due to our inability to meet our assumptions and the impact on our financial performance that could occur as a result of the various risks and uncertainties to our business as set forth in these risk factors, or because of the way that applicable accounting rules require us to treat new product and service offerings that we may offer. We offer no assurance that such guidance will ultimately be accurate, and investors should treat any such guidance with appropriate caution. If we fail to meet our guidance or if we find it necessary to revise such guidance, even if such failure or revision is seemingly insignificant, investors and analysts may lose confidence in us and the market value of our common stock could be materially and adversely affected.

Our vehicles make use of lithium-ion battery cells, which have been observed to catch fire or vent smoke and flame, and such events have raised concerns, and future events may lead to additional concerns, about the batteries used in automotive applications.

The battery pack in our vehicles and the battery packs that we sell to Toyota and Daimler make use of lithium-ion cells. On rare occasions, lithium-ion cells can rapidly release the energy they contain by venting smoke and flames in a manner that can ignite nearby materials as well as other lithium-ion cells. Extremely rare incidents of laptop computers, cell phones and electric vehicle battery packs catching fire have focused consumer attention on the safety of these cells.

These events have raised concerns about the batteries used in automotive applications. To address these questions and concerns, a number of cell manufacturers are pursuing alternative lithium-ion battery cell chemistries to improve safety. We have designed the battery pack to passively contain any single cell’s release of energy without spreading to neighboring cells. However, we have delivered only a limited number of our vehicles to customers and have limited field experience with them. We have also only delivered a limited number of battery packs to Toyota and Daimler. Accordingly, there can be no assurance that a field or testing failure of our vehicles or other battery packs that we produce will not occur, which could damage the vehicle or lead to personal injury or death and may subject us to lawsuits. We may have to recall our vehicles or participate in a recall of a vehicle that contains our battery packs, and redesign our battery packs, which would be time consuming and expensive. Also, negative public perceptions regarding the suitability of lithium-ion cells for automotive applications or any future incident involving lithium-ion cells such as a vehicle or other fire, even if such incident does not involve us, could seriously harm our business.

In addition, we store a significant number of lithium-ion cells at our manufacturing facility. Any mishandling of battery cells may cause disruption to the operation of our facilities. While we have implemented safety procedures related to the handling of the cells, there can be no assurance that a safety issue or fire related to the cells would not disrupt our operations. Such damage or injury would likely lead to adverse publicity and potentially a safety recall. Moreover, any failure of a competitor’s electric vehicle, especially those that use a high volume of commodity cells

similar to Tesla's vehicles, may cause indirect adverse publicity for us and our electric vehicles. Such adverse publicity would negatively affect our brand and harm our business, prospects, financial condition and operating results.

We have a history of losses and have to deliver significant cost reductions to achieve sustained, long-term profitability and long-term commercial success.

We have had net losses on a GAAP basis in each quarter since our inception, except for the first quarter of 2013. Even if we are able to continue to increase Model S production and sales and begin to produce and sell Model X and future vehicles, there can be no assurance that we will be profitable. In order to achieve profitability as well as long-term commercial success, we must continue to achieve our planned cost reductions, control our operational costs while producing quality vehicles, increase our production rate, maintain strong demand in North America, and grow demand abroad in Europe and Asia. Failure to do one or more of these things could prevent us from achieving sustained, long-term profitability.

Foreign currency movements relative to the U.S. dollar could harm our financial results.

Our revenues and costs denominated in foreign currencies are not completely matched. As we have increased Model S deliveries in markets outside of the United States, we have much higher revenues than costs denominated in other currencies such as the euro, Norwegian kroner, and Chinese yuan. The recent strengthening of the U.S. dollar therefore has reduced, and any further strengthening of the U.S. dollar would tend to further reduce, our revenues as measured in U.S. dollars. In addition, a portion of our costs and expenses have been, and we anticipate will continue to be, denominated in foreign currencies, including the Japanese yen. If we do not have fully offsetting revenues in these currencies and if the value of the U.S. dollar depreciates significantly against these currencies, our costs as measured in U.S. dollars as a percent of our revenues will correspondingly increase and our margins will suffer. As a result, our operating results could be adversely affected.

The introduction of our resale value guarantee and leasing programs may result in lower revenues and profits and exposes us to resale risk to the extent many customers elect to return their vehicles to us and the residual values are lower than our estimates.

In 2013 we began offering a resale value guarantee to all customers who purchased a Model S in the United States and Canada and financed their vehicle through one of our specified commercial banking partners. In April and October of 2014, we started offering leasing to business customers and individual customers, respectively, including through Tesla Finance, our captive finance company. Both the resale value guarantee program and leasing offered through Tesla Finance generate lower revenues in the period the car is delivered as compared to cash purchases and both expose us to the risk that any vehicles repurchased or returned to us under the programs may be resold by us for prices less than we estimate.

Under the resale value guarantee program, Model S customers have the option of selling their vehicle back to us during the period of 36 to 39 months following delivery for a pre-determined resale value. As a result of this resale value guarantee and customers having the option of selling their vehicles to us, we apply lease accounting to such purchases, which defers the recognition of the associated revenues over time instead of full recognition at vehicle delivery. Although the resale value guarantee does not impact our cash flows and liquidity at the time of vehicle delivery, a significant uptake under this program could have a significant adverse impact on our near term GAAP revenues and operating results.

Under the leasing program offered through Tesla Finance, we lease vehicles directly to customers. Customers have the option of purchasing their vehicles at the stated value in the leasing contract or returning their vehicles to us. We apply lease accounting to such purchases. Unlike the resale value guarantee program, we may receive only a very small portion of the price of the vehicle from our customers at the time of purchase, and instead will receive a stream of lease payments. To the extent we expand this program and are unable to secure appropriate financing, our cash flow and liquidity, as well as our near term GAAP revenues and operating results, could be negatively impacted. Furthermore, we are exposed to credit risk that customers may not pay their lease payments on time and according to the terms of our leasing contracts.

Under both programs, we are exposed to the risk that the vehicles' resale value may be lower than our estimates and the volume of vehicles returned to us may be higher than our estimates, which could impact our future cash flows and/or profitability. Currently, there is only a very limited secondary market for our electric vehicles on which to base our estimates, and such a secondary market may not develop in the future. Our residual value and return volume estimates could prove to be incorrect, either of which could harm our financial condition and operating results.

Increases in costs, disruption of supply or shortage of raw materials, in particular lithium-ion cells, could harm our business.

We may experience increases in the cost or a sustained interruption in the supply or shortage of raw materials. Any such increase or supply interruption could materially and negatively impact our business, prospects, financial condition and operating results. We use various raw materials in our business including aluminum, steel, nickel and copper. The prices for these raw materials fluctuate depending on market conditions and global demand for these materials and could adversely affect our business and operating results. For instance, we are exposed to multiple risks relating to lithium-ion cells. These risks include:

- the inability or unwillingness of current battery manufacturers to build or operate battery cell manufacturing plants to supply the numbers of lithium-ion cells required to support the growth of the electric or plug-in hybrid vehicle industry as demand for such cells increases;
- disruption in the supply of cells due to quality issues or recalls by battery cell manufacturers;
- an increase in the cost of raw materials, such as nickel used in lithium-ion cells, or aluminum used in the body of Model S; and
- fluctuations in the value of the Japanese yen against the U.S. dollar as our battery cell purchases are currently denominated in Japanese yen.

Our business is dependent on the continued supply of battery cells for our vehicles' battery packs as well as for the battery packs we produce for other automobile manufacturers. While we believe several sources of the battery cells are available for such battery packs, we have fully qualified only one supplier for the cells used in such battery packs and have very limited flexibility in changing cell suppliers. Any disruption in the supply of battery cells from such vendors could disrupt production of our vehicles and of the battery packs we produce for other automobile manufacturers until such time as a different supplier is fully qualified. Furthermore, fluctuations or shortages in petroleum and other economic conditions may cause us to experience significant increases in freight charges and raw material costs. Substantial increases in the prices for our raw materials or prices charged to us, such as those charged by our battery cell manufacturers, would increase our operating costs, and could reduce our margins if we cannot recoup the increased costs through increased electric vehicle prices. There can be no assurance that we will be able to recoup increasing costs of raw materials by increasing vehicle prices. Any attempts to increase vehicle prices in response to increased raw material costs could be viewed negatively by our customers, result in cancellations of vehicle orders and reservations and could materially and adversely affect our brand, image, business, prospects and operating results.

Our success could be harmed by negative publicity regarding our company or our products, particularly Model S.

Occasionally, third parties evaluate or publish stories regarding our vehicles. For example, in 2013 the New York Times published a negative review of the Model S and our Supercharger network on a route from Washington, D.C. to Boston. The story created a negative public perception about Model S, its capabilities and the Supercharger network. To the extent that negative comments about us or our products are believed by the public, this may cause current or potential customers not to purchase our electric vehicles, including Model S and Model X, which can materially and adversely affect our business, operating results, financial conditions and prospects.

Our distribution model is different from the predominant current distribution model for automobile manufacturers, which makes evaluating our business, operating results and future prospects difficult.

Our distribution model is not common in the automobile industry today, particularly in the United States. We plan to continue to sell our performance electric vehicles in company-owned Tesla stores and over the internet. While we believe our approach is important to the success of our technology and vehicles, this model of vehicle distribution is relatively new and unproven, especially in the United States, and subjects us to substantial risk as it requires, in the aggregate, a significant expenditure and provides for slower expansion of our distribution and sales systems than may be possible by utilizing a more traditional dealer franchise system. For example, we do not utilize long-established sales channels developed through a franchise system to increase our sales volume, which may harm our business, prospects, financial condition and operating results. Moreover, we compete with companies with well-established distribution channels.

We have opened Tesla stores in North America, Europe and the Asia Pacific Region, many of which have been open for only a short period of time. We have relatively limited experience distributing and selling our performance vehicles through our Tesla stores, especially in Asia. Our success will depend in large part on our ability to effectively develop our own sales channels and marketing strategies. Implementing our business model is subject to numerous significant challenges, including obtaining permits and approvals from local and state authorities, and we may not be successful in addressing these challenges. The concept and layout of our interactive stores, which are typically located in high profile retail centers, is different than what has previously been used in automotive sales. We do not know whether our store strategy will continue to be successful. We may incur additional costs in order to improve or change our retail strategy.

Other aspects of our distribution model also differ from those used by traditional automobile manufacturers. For example, we do not anticipate that we will ever carry a significant amount of vehicle inventory at our stores and

customers may need to wait up to a few months from the time they place an order until the time they receive their vehicle. This type of custom manufacturing is unusual in the premium sedan market in the United States and it is unproven whether the average customer will be willing to wait this amount of time for such a vehicle. If customers do not embrace this ordering and retail experience, our business will be harmed.

We may become subject to product liability claims, which could harm our financial condition and liquidity if we are not able to successfully defend or insure against such claims.

We may become subject to product liability claims, which could harm our business, prospects, operating results and financial condition. The automobile industry experiences significant product liability claims and we face inherent risk of exposure to claims in the event our vehicles do not perform as expected or malfunction resulting in personal injury or death. Our risks in this area are particularly pronounced given the limited number of vehicles delivered to date and limited field experience of those vehicles. A successful product liability claim against us could require us to pay a substantial monetary award. Moreover, a product liability claim could generate substantial negative publicity about our vehicles and business and inhibit or prevent commercialization of other future vehicle candidates which would have material adverse effect on our brand, business, prospects and operating results. We self-insure against the risk of product liability claims, meaning that any product liability claims will have to be paid from company funds, not by insurance. Any lawsuit seeking significant monetary damages may have a material adverse effect on our reputation, business and financial condition. We may not be able to secure additional product liability insurance coverage on commercially acceptable terms or at reasonable costs when needed, particularly if we do face liability for our products and are forced to make a claim under such a policy.

We are currently expanding and improving our information technology systems. If these implementations are not successful, our business and operations could be disrupted and our operating results could be harmed.

We are currently expanding and improving our information technology systems, including implementing new internally developed systems, to assist us in the management of our business. In particular, our volume production of Model S necessitates continued development, maintenance and improvement of our information technology systems in the U.S. and abroad, which include product data management, procurement, inventory management, production planning and execution, sales, service and logistics, dealer management, financial, tax and regulatory compliance systems. These systems support our operations and enable us to produce Model S and future vehicles like Model X in volume. The implementation, maintenance and improvement of these systems require significant management time, support and cost. Moreover, there are inherent risks associated with developing, improving and expanding our core systems as well as implementing new systems, including the disruption of our data management, procurement, manufacturing execution, finance, supply chain and sales and service processes. These risks may affect our ability to manage our data and inventory, procure parts or supplies or manufacture, sell, deliver and service vehicles, or achieve and maintain compliance with, or realize available benefits under, tax laws and other applicable regulations.

We cannot be sure that these expanded systems or their required functionality will be effectively implemented or sufficiently maintained. If we do not successfully implement, improve or maintain these systems, our operations may be disrupted, our ability to accurately and/or timely report our financial results could be impaired; and deficiencies may arise in our internal control over financial reporting, which may impact our ability to certify our financial results. If these systems or their functionality do not operate as we expect them to, we may be required to expend significant resources to make corrections or find alternative sources for performing these functions.

We may not realize the benefits of our Supercharger network, which could harm our business, brand and operating results.

We continue to deploy Tesla Superchargers in the United States, Europe and Asia. Tesla Superchargers are a network of charging stations designed to provide fast-charge capability to owners of Model S vehicles with the Supercharging option. We intend to expand the Tesla Supercharger network throughout the U.S., Canada, Europe and Asia, but we may be unable to do so due to a number of factors, including the inability to secure, or delays in securing, suitable locations and permits, problems negotiating leases with landowners or obtaining required permits for such locations, difficulties in interfacing with the infrastructures of various utility companies and greater than expected costs and

difficulties of installing, maintaining and operating the network.

We may also be unable to expand the Supercharger network as fast as we intend or as the public expects, or to place the charging stations in places our customers believe to be optimal. Furthermore, even where Superchargers exist, the increasing number of Model S vehicles as well as future vehicles such as Model X may oversaturate the available charging bays at such Superchargers, leading to increased wait times and dissatisfaction for customers. In addition, as we have announced that we will not be charging our customers to access this network in addition to what they have already paid for their vehicles, any significant unexpected costs that we encounter will entirely be borne by us and may harm our operating results. Although our Supercharger network is intended to address customer concerns regarding long-distance travel, this network may not result in increased reservations or sales of Model S or future vehicles like Model X. If our Supercharger network is not expanded as currently planned or as quickly as planned, we may not realize the benefits of our Supercharger network and our business and operating results could be materially affected.

If we are unable to design, develop, market and sell new electric vehicles that address additional market opportunities, our business, prospects and operating results will suffer.

We may not be able to successfully develop new electric vehicles, address new market segments or develop a significantly broader customer base. In 2012, we publicly revealed an early prototype of the Model X crossover as the first vehicle we intend to develop by leveraging the Model S platform and are currently testing our Beta Model X vehicles. We have also announced our intent to develop Model 3 based on a smaller platform than the Model S which we expect to produce at the Tesla Factory after the introduction of Model X. Model 3 is currently planned to be a lower cost, smaller sedan designed for the mass market. Therefore, we intend to manufacture Model 3 in significantly higher volumes than Model S and there can be no assurance we can successfully scale our business accordingly. In addition, we have not yet finalized the design, engineering or component sourcing plans for Model 3 and there are no assurances that we will be able to bring this vehicle to market at the price point and in the volume that we currently intend, if at all. The market for vehicles in the price range we expect for Model 3 is much more competitive than for Model S and Model X, and therefore margins are likely to be lower compared to Model S and Model X margins. Our efforts to manufacture and sell a sufficiently profitable Model 3 may not be as successful, and therefore our business, prospects and operating results may suffer. Our failure to address additional market opportunities would harm our business, prospects, financial condition and operating results.

The automotive market is highly competitive, and we may not be successful in competing in this industry. We currently face competition from new and established competitors and expect to face competition from others in the future.

The worldwide automotive market, particularly for alternative fuel vehicles, is highly competitive today and we expect it will become even more so in the future. Other automobile manufacturers entered the electric vehicle market at the end of 2010 and we expect additional competitors to enter this market. With respect to Model S, we face competition from existing and future automobile manufacturers in the extremely competitive premium sedan market, including Audi, BMW, Lexus and Mercedes.

Many established and new automobile manufacturers have entered or have announced plans to enter the alternative fuel vehicle market. BMW, Daimler, Nissan, Fiat, Ford and Mitsubishi, among others, have electric vehicles available today. Moreover, Porsche, Lexus, Audi, Volkswagen and Volvo are also developing electric vehicles. In addition, several manufacturers, including General Motors, Toyota, Ford, and Honda, are each selling hybrid vehicles, and certain of these manufacturers have announced plug-in versions of their hybrid vehicles. For example, in December 2010, General Motors introduced the Chevrolet Volt, which is a plug-in hybrid vehicle that operates purely on electric power for a limited number of miles, at which time an internal combustion engine engages to recharge the battery pack.

Moreover, it has been reported that many of the other large OEMs, such as Daimler, Lexus and Audi, are also developing electric vehicles. Several new start-ups have also entered or announced plans to enter the market for performance electric vehicles. Finally, electric vehicles have already been brought to market in China and other foreign countries and we expect a number of those manufacturers to enter the United States market as well.

Most of our current and potential competitors have significantly greater financial, technical, manufacturing, marketing and other resources than we do and may be able to devote greater resources to the design, development, manufacturing, distribution, promotion, sale and support of their products. Virtually all of our competitors have more extensive customer bases and broader customer and industry relationships than we do. In addition, almost all of these companies have longer operating histories and greater name recognition than we do. Our competitors may be in a stronger position to respond quickly to new technologies and may be able to design, develop, market and sell their products more effectively. Additionally, we have not in the past, and do not currently, offer customary discounts on

our vehicles like most of our competitors do.

We expect competition in our industry to intensify in the future in light of increased demand for alternative fuel vehicles, continuing globalization and consolidation in the worldwide automotive industry. Factors affecting competition include product quality and features, innovation and development time, pricing, reliability, safety, fuel economy, customer service and financing terms. Increased competition may lead to lower vehicle unit sales and increased inventory, which may result in a further downward price pressure and adversely affect our business, financial condition, operating results and prospects. Our ability to successfully compete in our industry will be fundamental to our future success in existing and new markets and our market share. There can be no assurances that we will be able to compete successfully in our markets. If our competitors introduce new cars or services that compete with or surpass the quality, price or performance of our cars or services, we may be unable to satisfy existing customers or attract new customers at the prices and levels that would allow us to generate attractive rates of return on our investment. Increased competition could result in price reductions and revenue shortfalls, loss of customers and loss of market share, which could harm our business, prospects, financial condition and operating results.

Demand in the automobile industry is volatile, which may lead to lower vehicle unit sales and adversely affect our operating results.

Volatility of demand in the automobile industry may materially and adversely affect our business, prospects, operating results and financial condition. The markets in which we currently compete and plan to compete in the future have been subject to considerable volatility in demand in recent periods. Demand for automobile sales depends to a large extent on general, economic, political and social conditions in a given market and the introduction of new vehicles and technologies. As a low volume producer, we have less financial resources than more established automobile manufacturers to withstand changes in the market and disruptions in demand. As our business grows, economic conditions and trends in other countries and regions where we currently or will sell our electric vehicles, such as Europe and Asia, will impact our business, prospects and operating results as well. Demand for our electric vehicles may also be affected by factors directly impacting automobile price or the cost of purchasing and operating automobiles, such as sales and financing incentives, prices of raw materials and parts and components, cost of fuel and governmental regulations, including tariffs, import regulation and other taxes. Volatility in demand may lead to lower vehicle unit sales and increased inventory, which may result in further downward price pressure and adversely affect our business, prospects, financial condition and operating results. These effects may have a more pronounced impact on our business given our relatively smaller scale and financial resources as compared to many incumbent automobile manufacturers.

If we are unable to establish and maintain confidence in our long-term business prospects among consumers, analysts and within our industry, then our financial condition, operating results, business prospects and stock price may suffer materially.

Our vehicles are highly technical products that require maintenance and support. If we were to cease or cut back operations, even years from now, buyers of our vehicles from years earlier might have much more difficulty in maintaining their vehicles and obtaining satisfactory support. As a result, consumers may be less likely to purchase our vehicles now if they are not convinced that our business will succeed or that our operations will continue for many years. Similarly, suppliers and other third parties will be less likely to invest time and resources in developing business relationships with us if they are not convinced that our business will succeed. If we are required to curtail our expansion plans in the future as we have done in the past, this may result in negative perceptions regarding our long-term business prospects and may lead to cancellations of Model S or Model X orders and reservations.

Accordingly, in order to build and maintain our business, we must maintain confidence among customers, suppliers, analysts and other parties in our liquidity and long-term business prospects. In contrast to some more established automakers, we believe that, in our case, the task of maintaining such confidence may be particularly complicated by factors such as the following:

- our limited operating history;
- unfamiliarity with or uncertainty about Model X and future Tesla vehicles;
- uncertainty about the long-term marketplace acceptance of alternative fuel vehicles generally, or electric vehicles specifically;
- the perceived prospect that we will need ongoing infusions of external capital to fund our planned operations;
- the size of our expansion plans in comparison to our existing capital base and scope and history of operations; and
- the prospect or actual emergence of direct, sustained competitive pressure from more established automakers, which may be more likely if our initial efforts are perceived to be commercially successful.

Many of these factors are largely outside our control, and any negative perceptions about our long-term business prospects, even if exaggerated or unfounded, would likely harm our business and make it more difficult to raise additional funds when needed.

We have limited experience servicing our vehicles, especially in certain regions outside of the United States, and we are using a different service model from the one typically used in the industry. If we are unable to address the service requirements of our existing and future customers, our business will be materially and adversely affected.

If we are unable to successfully address the service requirements of our existing and future customers and meet customer expectations regarding service, our business and prospects will be materially and adversely affected. We have limited experience servicing our vehicles, especially in Europe and Asia. Servicing electric vehicles is different than servicing vehicles with internal combustion engines and requires specialized skills, including high voltage training and servicing techniques. If we are unable to satisfactorily service our customers and the various service related issues that they are facing and may face in the future, our ability to generate customer loyalty, grow our business and sell additional vehicles could be impaired.

We service our performance electric vehicles through our company-owned Tesla service centers, certain of our stores, and through our mobile service technicians known as the Tesla Rangers. However, certain service centers have been open for short periods, such as those outside of the United States, and to date we have only limited experience servicing our performance vehicles at these locations. We will need to open new standalone service centers in locations around the world and hire and train significant numbers of new employees to staff these service centers and act as Tesla Rangers in order to successfully maintain our fleet of delivered performance electric vehicles. We only implemented our Tesla Rangers program in October 2009 and have limited experience in deploying them to service our customers' vehicles. There can be no assurance that these service arrangements or our limited experience servicing our vehicles will adequately address the service requirements of our customers to their satisfaction, or that we will have sufficient resources to meet these service requirements in a timely manner as the volume of vehicles we are able to deliver annually increases.

We do not expect to be able to open Tesla service centers in all the geographic areas in which our existing and potential customers may reside. In order to address the service needs of customers who are not in geographical proximity to our service centers, we plan to either transport those vehicles to the nearest Tesla store or service center for servicing or deploy our mobile Tesla Rangers to service the vehicles at the customer's location. These special arrangements may be expensive and we may not be able to recoup the costs of providing these services to our customers. In addition, a number of potential customers may choose not to purchase our vehicles because of the lack of a more widespread service network. If we do not adequately address our customers' service needs, our brand and reputation will be adversely affected, which in turn, could have a material and adverse impact on our business, financial condition, operating results and prospects.

Traditional automobile manufacturers in the United States do not provide maintenance and repair services directly. Consumers must rather service their vehicles through franchised dealerships or through third party maintenance service providers. We do not have any such arrangements with third party service providers and it is unclear when or even whether such third party service providers will be able to acquire the expertise to service our vehicles. At this point, we anticipate that we will be providing substantially all of the service for our vehicles for the foreseeable future. As our vehicles are placed in more locations, we may encounter negative reactions from our consumers who are frustrated that they cannot use local service stations to the same extent as they have with their conventional automobiles and this frustration may result in negative publicity and reduced sales, thereby harming our business and prospects.

In addition, the motor vehicle industry laws in many states require that service facilities be available with respect to vehicles physically sold from locations in the state. Whether these laws would also require that service facilities be available with respect to vehicles sold over the internet to consumers in a state in which we have no physical presence is uncertain. While we believe our Tesla Ranger program and our practice of transporting customers' vehicles to our nearest Tesla service center would satisfy regulators in these circumstances, without seeking formal regulatory guidance, there are no assurances that regulators will not attempt to require that we provide physical service facilities in their states. Further, certain state franchise laws which prohibit manufacturers from being licensed as a dealer or acting in the capacity of dealer also restrict manufacturers from providing vehicle service. If issues arise in connection with these laws, certain aspects of Tesla's service program would need to be restructured to comply with state law, which may harm our business.

We may not succeed in maintaining and strengthening the Tesla brand, which would materially and adversely affect customer acceptance of our vehicles and components and our business, revenues and prospects.

Our business and prospects are heavily dependent on our ability to develop, maintain and strengthen the Tesla brand. Any failure to develop, maintain and strengthen our brand may materially and adversely affect our ability to sell the Model S, Model X, Model 3 and other future planned electric vehicles, and sell our electric powertrain components. If

we do not continue to establish, maintain and strengthen our brand, we may lose the opportunity to build a critical mass of customers. Promoting and positioning our brand will likely depend significantly on our ability to provide high quality electric cars and maintenance and repair services, and we have very limited experience in these areas. Any problems associated with the Toyota RAV4 EV and Mercedes-Benz B-Class EV, both of which use a Tesla powertrain, or the Model X may hurt the Tesla brand.

In addition, we expect that our ability to develop, maintain and strengthen the Tesla brand will also depend heavily on the success of our marketing efforts. To date, we have limited experience with marketing activities as we have relied primarily on the internet, word of mouth and attendance at industry trade shows to promote our brand. To further promote our brand, we may be required to change our marketing practices, which could result in substantially increased advertising expenses, including the need to use traditional media such as television, radio and print. The automobile industry is intensely competitive, and we may not be successful in building, maintaining and strengthening our brand. Many of our current and potential competitors, particularly automobile manufacturers headquartered in Detroit, Japan and the European Union, have greater name recognition, broader customer relationships and substantially greater marketing resources than we do. If we do not develop and maintain a strong brand, our business, prospects, financial condition and operating results will be materially and adversely impacted.

If our vehicle owners customize our vehicles or change the charging infrastructure with aftermarket products, the vehicle may not operate properly, which could harm our business.

Automobile enthusiasts may seek to “hack” our vehicles to modify its performance which could compromise vehicle safety systems. Also, we are aware of customers who have customized their vehicles with after-market parts that may compromise driver safety. For example, some customers have installed seats that elevate the driver such that airbag and other safety systems could be compromised. Other customers have changed wheels and tires, while others have installed large speaker systems that may impact the electrical systems of the vehicle. We have not tested, nor do we endorse, such changes or products. In addition, customer use of improper external cabling or unsafe charging outlets can expose our customers to injury from high voltage electricity. Such unauthorized modifications could reduce the safety of our vehicles and any injuries resulting from such modifications could result in adverse publicity which would negatively affect our brand and harm our business, prospects, financial condition and operating results.

Our plan to expand our network of Tesla stores, service centers and Superchargers will require significant cash investments and management resources and may not meet our expectations with respect to additional sales of our electric vehicles. In addition, we may not be able to open stores or service centers in certain states or Superchargers in desired locations.

Our plan to expand our network of Tesla stores, service centers and Superchargers will require significant cash investments and management resources and may not meet our expectations with respect to additional sales of our electric vehicles. This ongoing global expansion may not have the desired effect of increasing sales and expanding our brand presence to the degree we are anticipating. Furthermore, there can be no assurances that we will be able to expand on the budget or timeline we have established. We will also need to ensure we are in compliance with any regulatory requirements applicable to the sale and service of our vehicles in those jurisdictions, which could take considerable time and expense. If we experience any delays in expanding our network of Tesla stores, service centers and Superchargers, this could lead to a decrease in sales of our vehicles and could negatively impact our business, prospects, financial condition and operating results. We have opened Tesla stores and service centers in major metropolitan areas throughout North America, Europe and Asia, and we plan to open additional stores and service centers worldwide to support our ongoing worldwide Model S rollout. We have also rapidly expanded our Supercharger network in the U.S., Europe and China. However, we may not be able to expand at a sufficient rate and our planned expansion will require significant cash investment and management resources, as well as efficiency in the execution of establishing these locations and in hiring and training the necessary employees to effectively sell and service our vehicles.

Furthermore, certain states and foreign jurisdictions may have permit requirements, franchise dealer laws or similar laws or regulations that may preclude or restrict our ability to open stores or sell vehicles out of such states and jurisdictions. Any such prohibition or restriction may lead to decreased sales in such jurisdictions, which could harm our business, prospects and operating results. See Risk Factor “We may face regulatory limitations on our ability to sell vehicles directly or over the internet which could materially and adversely affect our ability to sell our electric vehicles.” Additionally, we may face potential difficulties in finding suitable Supercharger sites in desired locations, negotiating leases or obtaining required permits for such locations.

We face risks associated with our international operations and expansion, including unfavorable regulatory, political, tax and labor conditions and establishing ourselves in new markets, all of which could harm our business.

We face various risks associated with our international operations and expansion. We currently have international operations and subsidiaries in various countries and jurisdictions in Europe and Asia that are subject to the legal, political, regulatory and social requirements and economic conditions in these jurisdictions. Additionally, as part of our growth strategy, we will continue to expand our sales, maintenance, repair and Supercharger services

internationally, particularly in China. However, we have limited experience to date selling and servicing our vehicles internationally, as well as limited experience installing and operating Superchargers internationally, and international expansion requires us to make significant expenditures, including the establishment of local operating entities, hiring of local employees and establishing facilities in advance of generating any revenue. We are subject to a number of risks associated with international business activities that may increase our costs, impact our ability to sell our electric vehicles and require significant management attention. These risks include:

- conforming our vehicles to various international regulatory and safety requirements where our vehicles are sold, or homologation;
- difficulty in establishing, staffing and managing foreign operations;
- difficulties attracting customers in new jurisdictions;
- foreign government taxes, regulations and permit requirements, including foreign taxes that we may not be able to offset against taxes imposed upon us in the United States, and foreign tax and other laws limiting our ability to repatriate funds to the United States;
- fluctuations in foreign currency exchange rates and interest rates, including risks related to any interest rate swap or other hedging activities we undertake;

our ability to enforce our contractual and intellectual property rights, especially in those foreign countries that do not respect and protect intellectual property rights to the same extent as do the United States, Japan and European countries, which increases the risk of unauthorized, and uncompensated, use of our technology;
United States and foreign government trade restrictions, customs regulations, tariffs and price or exchange controls;
foreign labor laws, regulations and restrictions;
preferences of foreign nations for domestically produced vehicles;
changes in diplomatic and trade relationships;
political instability, natural disasters, war or events of terrorism; and
the strength of international economies.

Additionally, as we have expanded into new international markets, we have faced challenges with ensuring that our charging equipment works successfully with the charging infrastructure in such markets. For example, we have encountered such challenges in Norway and China. If customers experience problems with the way our charging equipment works with the local charging infrastructure, or we are unable to adapt our equipment to resolve such problems, then the viability and acceptance of our vehicles in such markets could be materially and adversely affected.

If we fail to successfully address these risks, our business, prospects, operating results and financial condition could be materially harmed.

Developments in alternative technologies or improvements in the internal combustion engine may materially adversely affect the demand for our electric vehicles.

Significant developments in alternative technologies, such as advanced diesel, ethanol, hydrogen, fuel cells or compressed natural gas, or improvements in the fuel economy of the internal combustion engine, may materially and adversely affect our business and prospects in ways we do not currently anticipate. Any failure by us to develop new or enhanced technologies or processes, or to react to changes in existing technologies, could materially delay our development and introduction of new and enhanced electric vehicles, which could result in the loss of competitiveness of our vehicles, decreased revenue and a loss of market share to competitors.

The unavailability, reduction or elimination of, or uncertainty regarding, government and economic incentives in the U.S. and abroad could have a material adverse effect on our business, financial condition, operating results and prospects.

Any reduction or elimination of government and economic incentives due to policy changes the reduced need for such incentives as the customer base of our electric vehicles expands, fiscal tightening or other reasons may result in the diminished competitiveness of the alternative fuel vehicle industry generally or our electric vehicles in particular. Such reduction or elimination of incentives could materially and adversely affect our growth as well because our business, prospects, financial condition and operating results, as our growth depends, in part, on the availability and amounts of government incentives. For example, we currently benefit from certain exemptions in the United States, such as the California state sales and use taxes. Similarly, government programs in Europe favor the purchase of electric vehicles, including through disincentives that discourage the use of gas-powered vehicles. In Norway, for example, the purchase of electric vehicles is not currently subject to import taxes, taxes on non-recurring vehicle fees, the 25% value added tax or the purchase taxes that apply to the purchase of gas-powered vehicles. If such government programs are reduced or eliminated, or the available benefits thereunder are exhausted earlier than anticipated, sales of all electric vehicles, including our Model S, could be adversely affected. In addition, customers in certain markets may delay taking delivery of their Tesla vehicles if they believe that certain electric vehicle incentives will be available at a later date, which may negatively affect our ability to achieve our planned delivery targets.

Our strategic relationships with third parties, such as Panasonic, are subject to various risks which could adversely affect our business and future prospects.

Our strategic relationships third parties, such as Panasonic which supplies us with battery cells for use in Model S and Model X and is our partner in the Gigafactory, pose various risks to us, including potential loss of access to important technology and vehicle parts, potential loss of business and adverse publicity. In addition, these third parties may not perform as expected under our agreements with them, such as with respect to vehicle parts quality of timeliness, and we may have disagreements or disputes with these third parties. The occurrence of any of the foregoing could adversely affect our business, prospects, financial condition and operating results.

The operation of our vehicles is different from internal combustion engine vehicles and our customers may experience difficulty operating them properly, including difficulty transitioning between different methods of braking.

We have designed our vehicles to minimize inconvenience and inadvertent driver damage to the powertrain. In certain instances, these protections may cause the vehicle to behave in ways that are unfamiliar to drivers of internal combustion vehicles. For example, we employ regenerative braking to recharge the battery pack in most modes of vehicle operation. Our customers may become accustomed to using this regenerative braking instead of the wheel brakes to slow the vehicle. However, when the vehicle is at maximum charge, the regenerative braking is not needed and is not employed by the vehicle. Accordingly, our customers may have difficulty shifting between different methods of braking. In addition, we use safety mechanisms to limit motor torque when the powertrain system reaches elevated temperatures. In such instances, the vehicle's acceleration and speed will decrease. Finally, if the driver permits the battery pack to substantially deplete its charge, the vehicle will progressively limit motor torque and speed to preserve the charge that remains. The vehicle will lose speed and ultimately coast to a stop. Despite several warnings about an imminent loss of charge, the ultimate loss of speed may be unexpected.

There can be no assurance that our customers will operate the vehicles properly, especially in these situations. Any accidents resulting from such failure to operate our vehicles properly could harm our brand and reputation, result in adverse publicity and product liability claims, and have a material adverse effect on our business, prospects, financial condition and operating results. In addition, if consumers dislike these features, they may choose not to buy additional cars from us, which could also harm our business and prospects.

If we are unable to keep up with advances in electric vehicle technology, we may suffer a decline in our competitive position.

We may be unable to keep up with changes in electric vehicle technology and, as a result, may suffer a decline in our competitive position. Any failure to keep up with advances in electric vehicle technology would result in a decline in our competitive position which would materially and adversely affect our business, prospects, operating results and financial condition. Our research and development efforts may not be sufficient to adapt to changes in electric vehicle technology. As technologies change, we plan to upgrade or adapt our vehicles and introduce new models in order to continue to provide vehicles with the latest technology, in particular battery cell technology. However, our vehicles may not compete effectively with alternative vehicles if we are not able to source and integrate the latest technology into our vehicles. For example, we do not currently manufacture battery cells, which makes us dependent upon other suppliers of battery cell technology for our battery packs.

If we are unable to attract and/or retain key employees and hire qualified management, technical, vehicle engineering and manufacturing personnel, our ability to compete could be harmed and our stock price may decline.

The loss of the services of any of our key employees could disrupt our operations, delay the development and introduction of our vehicles and services, and negatively impact our business, prospects and operating results as well as cause our stock price to decline. In particular, we are highly dependent on the services of Elon Musk, our Chief Executive Officer, Product Architect and Chairman of our Board of Directors, and JB Straubel, our Chief Technical Officer. None of our key employees is bound by an employment agreement for any specific term. There can be no assurance that we will be able to successfully attract and retain senior leadership necessary to grow our business. Our future success depends upon our ability to attract and retain our executive officers and other key technology, sales, marketing, engineering, manufacturing and support personnel and any failure to do so could adversely impact our business, prospects, financial condition and operating results. We have in the past and may in the future experience difficulty in retaining members of our senior management team as well as technical, vehicle engineering and manufacturing personnel due to various factors, such as a very competitive labor market for talented individuals with automotive experience. In addition, we do not have "key person" life insurance policies covering any of our officers or

other key employees.

Currently in Northern California, there is increasing competition for talented individuals with the specialized knowledge of electric vehicles, software engineers, manufacturing engineers and other skilled employees and this competition affects both our ability to retain key employees and hire new ones. Our continued success depends upon our continued ability to hire new employees in a timely manner and retain current employees. Additionally, we compete with many mature and prosperous companies in Northern California that have far greater financial resources than we do and thus can offer current or perspective employees more lucrative incentive packages than we can. Any difficulties in retaining current employees or recruiting new ones would have an adverse effect on our performance.

We are highly dependent on the services of Elon Musk, our Chief Executive Officer.

We are highly dependent on the services of Elon Musk, our Chief Executive Officer, Product Architect, Chairman of our Board of Directors and largest stockholder. Although Mr. Musk spends significant time with Tesla and is highly active in our management, he does not devote his full time and attention to Tesla. Mr. Musk also currently serves as Chief Executive Officer and Chief Technical Officer of Space Exploration Technologies, a developer and manufacturer of space launch vehicles, and Chairman of SolarCity, a solar equipment installation company.

We are subject to various environmental and safety laws and regulations that could impose substantial costs upon us and negatively impact our ability to operate our manufacturing facilities.

As an automobile manufacturer, we are subject to national, state, provincial and/or local environmental, health and safety laws and regulations, including laws relating to the use, handling, storage, disposal and human exposure to hazardous materials, both in the United States and abroad. Environmental and health and safety laws and regulations can be complex, and we expect that our business and operations will be affected by new, or future amendments to, such laws that may require us to change our operations, potentially resulting in a material adverse effect on our business. These laws can give rise to liability for administrative oversight costs, cleanup costs, property damage, bodily injury and associated fines and penalties. Capital and operating expenses needed to comply with environmental, health and safety laws and regulations can be significant, and violations of those laws may result in substantial fines and penalties, third party damages, suspension of production or a cessation of our operations. These expenses could have a material adverse effect on our financial condition or operating results.

Contamination at properties formerly owned or operated by us, as well as at properties we will own and operate, and properties to which hazardous substances were sent by us, may result in liability for us under environmental laws and regulations, including, but not limited to the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA). The government can impose liability on us under CERCLA for the full amount of remediation-related costs of a contaminated site without regard to fault. Such costs can include those associated with the investigation and cleanup of contaminated soil, ground water and buildings as well as to reverse impacts to human health and damages to natural resources.

We may also face unexpected delays in obtaining the necessary permits and approvals required by environmental laws in connection with our manufacturing facilities that could require significant time and financial resources and negatively impact our ability to operate these facilities, which would adversely impact our business prospects and operating results. As the owner of the Tesla Factory and surrounding land, we may be responsible under federal and state laws and regulations for the entire investigation and remediation of any environmental contamination at the Tesla Factory, whether it occurred before or after the date we purchased the property. When Tesla purchased the property, the previous owner and operator of the Tesla Factory, New United Motor Manufacturing, Inc. (NUMMI), identified environmental conditions at the Tesla Factory that could adversely affect soil and groundwater, and agreed to remediate these conditions. Although NUMMI stated that it fully documented and managed all environmental issues at the Tesla Factory, we cannot determine with certainty the truth of this statement, nor the total costs to remediate any pre-existing contamination that may eventually be found. We have reached an agreement with NUMMI under which, over a ten year period, we will pay the first $15.0 million of any costs of any governmentally-required remediation activities for contamination that existed prior to the closing of the purchase for any known or unknown environmental conditions (Remediation Activities), and NUMMI has agreed to pay the next $15.0 million for such Remediation Activities. Our agreement provides, in part, that NUMMI will pay up to the first $15.0 million on our behalf if such expenses are incurred in the first four years of our agreement, subject to our reimbursement of such costs on the fourth anniversary date of the closing.

On either the ten-year anniversary of the closing or whenever $30.0 million has been spent on Remediation Activities, whichever comes first, NUMMI’s liability to us with respect to Remediation Activities ceases, and we are responsible for any and all environmental conditions at the Fremont site. At that point in time, we have agreed to indemnify, defend, and hold harmless NUMMI from all liability, including attorney fees, or any costs or penalties it may incur arising out of or in connection with any claim relating to environmental conditions and we have released NUMMI for any known or unknown claims except for NUMMI’s obligations for representations and warranties under the agreement.

There are no assurances that NUMMI will perform its obligations under our agreement and NUMMI's failure to perform would require us to undertake these obligations at a potentially significant cost. Such performance may also adversely affect the production capacity of, and our ability to operate, the Tesla Factory. Any Remediation Activities or other environmental conditions at the Fremont site could harm our operations and the future use and value of the Fremont site and could delay our production plans for Model S.

Our business may be adversely affected by union activities.

Although none of our employees are currently represented by a labor union, it is common throughout the automobile industry generally for many employees at automobile companies to belong to a union, which can result in higher employee costs and increased risk of work stoppages. Our employees may join or seek recognition to form a labor union, or we may be required to become a union signatory. Our automobile production facility in Fremont, California was purchased from NUMMI. Prior employees of NUMMI were union members and our future work force at this facility may be inclined to vote in favor of forming a labor union. We also own and operate another component manufacturing facility in Lathrop, California. Furthermore, we are directly or indirectly dependent upon companies with unionized work forces, such as parts suppliers and trucking and freight companies, and work stoppages or strikes organized by such unions could have a material adverse impact on our business, financial condition or operating results. If a work stoppage occurs, it could delay the manufacture and sale of our performance electric vehicles and have a material adverse effect on our business, prospects, operating results or financial condition. The mere fact that our labor force could be unionized may harm our reputation in the eyes of some investors and thereby negatively affect our stock price. Consequently, the unionization of our labor force could negatively impact the company's health.

We are subject to substantial regulation, which is evolving, and unfavorable changes or failure by us to comply with these regulations could substantially harm our business and operating results.

The production and sale of motor vehicles, in general and specifically related to electric vehicles, are subject to substantial regulation under international, federal, state, and local laws. We have incurred, and expect to continue to incur, significant costs in complying with these regulations.

Regulations related to the electric vehicle industry and alternative energy are currently evolving and we face risks associated with changes to these regulations. In the United States, the following are examples of regulatory and statutory issues facing us:

- the imposition of a carbon tax or the introduction of a cap-and-trade system on electric utilities could increase the cost of electricity;
- increasingly stringent Clean Air Act emission regulations affecting power plants used to generate electricity could increase the cost of electricity;
- changes to the regulations governing the assembly and transportation of lithium-ion battery packs, such as the UN Recommendations of the Safe Transport of Dangerous Goods Model Regulations or regulations adopted by the U.S. Pipeline and Hazardous Materials Safety Administration (PHMSA) could increase the cost of lithium-ion battery packs or restrict their transport;
- the amendment or rescission of the federal law and regulations mandating increased fuel economy in the United States, referred to as the Corporate Average Fuel Economy (CAFE) standards, could reduce new business opportunities for our powertrain sales and development activities;
- the amendment or rescission of federal greenhouse gas tailpipe emission regulations administered by EPA under the authority of the Clean Air Act could reduce new business opportunities for our powertrain sales and development activities;
- the amendment or rescission of California's zero emission vehicle (ZEV) regulations administered by the California Air Resources Board under the California Health & Safety Code could reduce new business opportunities for our powertrain sales and development activities, as well as our ability to monetize ZEV credits not only in California, but also in the eleven additional states that have adopted the California program;
- increased sensitivity by regulators to the needs of established automobile manufacturers with large employment bases, high fixed costs and business models based on the internal combustion engine could lead them to pass regulations that could reduce the compliance costs of such established manufacturers or mitigate the effects of government efforts to promote alternative fuel vehicles;
- changes to the vehicle-specific Federal Motor Vehicle Safety Standards, which govern how all motor vehicles are made within the United States, could result in costly changes to how current vehicles are produced; and
- changes to regulations governing the export of our products could increase our delivery costs to outside the United States or force us to charge consumers in such jurisdictions a higher price for our vehicles.

In addition, as the automotive industry moves towards greater use of electronics in vehicle systems, NHTSA and other regulatory bodies may regulate these electronic systems more stringently, particularly as concerns about distracted driving increase. Such concerns could affect use of electronic systems in Model S, such as the 17 inch display screen, which could reduce the appeal of Model S or require adjustments to the display screen's functionality.

As we are currently delivering vehicles in Europe and Asia, we are subject to laws and regulations applicable to the import, sale and service of automobiles in those regions. For example, we are required to meet vehicle-specific safety standards that are often materially different from U.S. requirements, thus resulting in additional investment into the vehicles and systems to ensure regulatory compliance. Unlike in the U.S. where we self-certify our vehicles' compliance with standards, we must obtain advanced approval from regulatory agencies regarding the proper certification or homologation of our vehicles to enter into these markets. This process necessitates that foreign regulatory officials review and certify our vehicles prior to market entry. In addition, we must comply with regulations

applicable to vehicles after they enter the market, including foreign reporting requirements and recall management systems.

To the extent U.S. or international laws change, some or all of our vehicles may not comply with any new applicable international, federal, state or local laws, which would have an adverse effect on our business. Compliance with changing regulations could be burdensome, time consuming, and expensive. To the extent compliance with new regulations is cost prohibitive, our business, prospects, financial condition and operating results will be adversely affected.

We retain certain personal information about our customers and may be subject to various privacy and consumer protection laws.

Our collection, use, retention, security and transfer of personal information of our customers is subject to federal, state, and international laws. These laws continue to be enacted and may be inconsistent from jurisdiction to jurisdiction. Complying with changing international laws may cause us to incur substantial costs, expose us to legal liability or require us to change our business practices. Our privacy policy is posted on our website, and any failure by us or our vendor or other business partners to comply with it or with federal, state or international privacy, data protection or security laws or regulations could result in regulatory or litigation-related actions against us, legal liability, fines, damages and other costs. Although we take steps to protect the security of our customers' personal information, we may be required to expend significant resources to comply with data breach requirements if third parties improperly obtain and use the personal information of our customers or we otherwise experience a data loss with respect to customers' personal information. A major breach of our network security and systems could have serious negative consequences for our businesses and future prospects, including possible fines, penalties and damages, reduced customer demand for our vehicles, and harm to our reputation and brand.

We may be compelled to undertake product recalls or take other actions, which could adversely affect our brand image and financial performance.

Any product recall in the future may result in adverse publicity, damage our brand and adversely affect our business, prospects, operating results and financial condition. We previously experienced product recalls in May 2009, October 2010 and June 2013, none of which was related to our electric powertrain. In April 2009, we determined that a condition caused by insufficient torqueing of the rear inner hub flange bolt existed in some of our Tesla Roadsters, as a result of a missed process during the manufacture of the Tesla Roadster glider. In October 2010, we initiated a product recall after the 12 volt, low voltage auxiliary cable in a single vehicle chafed against the edge of a carbon fiber panel in the vehicle causing a short, smoke and possible fire behind the right front headlamp of the vehicle. In June 2013, we initiated a recall of slightly more than one thousand Model S vehicles to inspect and repair rear seat strikers that may have been compromised during the assembly process. Rear seat strikers are used to retain the rear seat backs in an upright position. Failure of this component may have resulted in collapse of the rear seat back during a crash. Finally, in January 2014, we implemented a firmware update to address issues with certain Universal Mobile Connector NEMA 14-50 adapters, which are part of the charging units and are not part of the vehicles themselves, potentially overheating during charging. In the future, we may at various times, voluntarily or involuntarily, initiate a recall if any of our vehicles, including Model S, or our electric powertrain components prove to be defective or noncompliant with applicable federal motor vehicle safety standards. Such recalls, voluntary or involuntary, involve significant expense and diversion of management attention and other resources, and could adversely affect our brand image in our target markets, as well as our business, prospects, financial condition and results of operations.

Our current and future warranty reserves may be insufficient to cover future warranty claims which could adversely affect our financial performance.

If our warranty reserves are inadequate to cover future warranty claims on our vehicles, our business, prospects, financial condition and operating results could be materially and adversely affected. Warranty reserves include management's best estimate of the projected costs to repair or to replace items under warranty. These estimates are based on actual claims incurred to-date and an estimate of the nature, frequency and costs of future claims. These estimates are inherently uncertain and changes to our historical or projected experience may cause material changes to our warranty reserves in the future. Subject to separate limited warranties for the supplemental restraint system and battery, we provide a four year or 50,000 mile New Vehicle Limited Warranty for the purchasers of Model S. The New Vehicle Limited Warranty for Model S also covers the drive unit for eight years and the battery for a period of eight years or 125,000 miles or unlimited miles, depending on the size of the vehicle's battery; although the battery's

charging capacity is not covered under the New Vehicle Limited Warranty or any Extended Service plan.

In addition, customers have the opportunity to purchase an Extended Service plan for the period after the end of the New Vehicle Limited Warranty for Model S to cover additional services for an additional four years or 50,000 miles, provided it is purchased within a specified period of time. The New Vehicle Limited Warranty and Extended Service plans for the Tesla Roadster and Model S are subject to certain limitations, exclusions or separate warranties, including certain wear items, such as tires, brake pads, paint and general appearance, and battery performance, and is intended to cover parts and labor to repair defects in material or workmanship in the vehicle including the body, chassis, suspension, interior, electronic systems, powertrain and brake system. We have previously provided our Tesla Roadster customers with a battery replacement option to replace the battery in their vehicles at any time after the expiration of the New Vehicle Limited Warranty but before the tenth anniversary of the purchase date of their vehicles. Additionally, in 2013, as part of our ongoing efforts to improve the customer ownership experience, we expanded the battery pack warranty and also eliminated the annual service requirement that was needed to keep the New Vehicle Limited Warranty in effect. Should this change in warranty coverage lead to an increase in warranty claims, we may need to record additional warranty reserves which would negatively affect our profitability.

Our insurance strategy may not be adequate to protect us from all business risks.

We may be subject, in the ordinary course of business, to losses resulting from products liability, accidents, acts of God and other claims against us, for which we may have no insurance coverage. While we currently maintain general liability, automobile, property, workers' compensation, and directors' and officers' insurance policies, as a general matter, we do not maintain as much insurance coverage as many other companies do, and in some cases, we do not maintain any at all. Additionally, the policies that we do have may include significant deductibles, and we cannot be certain that our insurance coverage will be sufficient to cover all future claims against us. A loss that is uninsured or which exceeds policy limits may require us to pay substantial amounts, which could adversely affect our financial condition and operating results.

Our financial results may vary significantly from period-to-period due fluctuations in our operating costs and the seasonality of our business.

We expect our period-to-period operating results to vary based on our operating costs which we anticipate will increase significantly in future periods as we, among other things, design, develop and manufacture Model X and future products, increase the production capacity at our manufacturing facilities to produce vehicles at higher volumes, develop the Gigafactory, open new Tesla service centers with maintenance and repair capabilities, open new Supercharger locations, increase our sales and marketing activities, and increase our general and administrative functions to support our growing operations. As a result of these factors, we believe that quarter-to-quarter comparisons of our operating results, especially in the short-term, are not necessarily meaningful and that these comparisons cannot be relied upon as indicators of future performance. Moreover, our operating results may not meet expectations of equity research analysts or investors. If any of this occurs, the trading price of our common stock could fall substantially, either suddenly or over time.

Additionally, sales of new cars in the automobile industry typically decline over the winter season and are generally higher during the spring and summer months. We anticipate that our sales of Model S and future models may have similar seasonality, but our limited operating history makes it difficult for us to judge the exact nature or extent of the seasonality of our business. Our operating results could also suffer if we do not achieve revenue consistent with our expectations for this seasonal demand because many of our expenses are based on anticipated levels of annual revenue.

Unauthorized control or manipulation of our vehicles' systems may cause them to operate improperly or not at all, or compromise their safety and data security, which could result in loss of confidence in us and our vehicles and harm our business.

There have been reports of vehicles of other automobile manufacturers being "hacked" to grant access and operation of the vehicles to unauthorized persons and would-be thieves. Our vehicles, and in particular Model S, are technologically advanced machines requiring the interoperation of numerous complex and evolving hardware and software systems. Subject to our customers' ability to opt out pursuant to our privacy policy, Model S is designed with built-in data connectivity to accept and install periodic remote updates from us to improve or update the functionality of these systems. Although we have designed, implemented and tested security measures to prevent unauthorized access to our vehicles and their systems, our information technology networks and communications with our vehicles may be vulnerable to interception, manipulation, damage, disruptions or shutdowns due to attacks by hackers or breaches due to errors by personnel who have access to our networks and systems. Any such attacks or breaches could result in unexpected control of or changes to our vehicles' functionality, user interface and performance characteristics. Hackers may also use similar means to gain access to data stored in or generated by the vehicle, such as its current geographical position, previous and stored destination address history and web browser "favorites." Any such unauthorized control of vehicles or access to or loss of information could result in legal claims or proceedings

and negative publicity, which would negatively affect our brand and harm our business, prospects, financial condition and operating results.

The range and power of our electric vehicles on a single charge declines over time, and this may negatively influence potential customers' decisions whether to purchase our vehicles.

The range and power of our electric vehicles on a single charge declines principally as a function of usage, time and charging patterns as well as other factors. How a customer uses their Tesla vehicle, the frequency of recharging the battery pack at a low state of charge and the means of charging can result in additional deterioration of the battery pack's ability to hold a charge over the long term. For example, we currently expect that our battery pack for the Tesla Roadster will retain approximately 70% of its ability to hold its initial charge after approximately 100,000 miles or seven years, which will result in a decrease to the vehicle's initial range and power. Preliminary internal testing and customer results of Model S to date suggest that deterioration of the Model S battery pack to be less than the Roadster, however, such battery pack deterioration and the related decrease in range and power over time as well as any perceived deterioration or fluctuation in range may negatively influence potential customer decisions whether to purchase our vehicles, which may harm our ability to market and sell our vehicles.

We may need or want to raise additional funds and these funds may not be available to us when we need them. If we cannot raise additional funds when we need or want them, our operations and prospects could be negatively affected.

The design, manufacture, sale and servicing of automobiles is a capital intensive business. We expect that our principal sources of liquidity will provide us adequate liquidity based on our current plans. However, until we are consistently generating positive free cash flows, if the costs for developing and manufacturing Model X exceed our expectations or if we incur any significant unplanned expenses or embark on or accelerate new significant strategic investments, such as the Gigafactory, we may need to raise additional funds through the issuance of equity, equity-related or debt securities or through obtaining credit from government or financial institutions. This capital will be necessary to fund our ongoing operations, continue research and development projects, including those for our planned Model X crossover and Model 3 vehicle, establish sales and service centers, build and deploy Superchargers and to make the investments in tooling and manufacturing capital required to introduce Model X. We cannot be certain that additional funds will be available to us on favorable terms when required, or at all. If we cannot raise additional funds when we need them, our financial condition, results of operations, business and prospects could be materially adversely affected.

If we fail to effectively manage the residual, financing and credit risks for our recently launched Model S leasing program, our business may suffer.

We recently introduced a leasing program in the United States and Canada through our captive finance company, Tesla Finance. The profitability of the leasing program depends on our ability to accurately project residual values, secure adequate financing and/or business partners to fund and grow this program, and manage customer credit risk. If actual residual values of Model S vehicles are below our estimates, we may suffer lower profitability or potentially have losses. If we are unable to adequately fund our leasing program with either internal funds or external financing sources, we may be unable to grow our sales. Additionally, if we do not properly screen customers for ability to pay their leases on time, we may be exposed to excessive credit risks and associated losses. Furthermore, if our leasing business grows substantially, our business may suffer if we cannot effectively manage the greater levels of residual and credit risks resulting from growth. Finally, if we do not successfully monitor and comply with federal and state financial regulations and consumer protection laws governing lease transactions, we may become subject to enforcement actions or penalties, either of which may harm our business.

Any failure to execute on the Daimler B-Class EV program could hurt our reputation as well as our profitability on this program.

We have worked with Daimler to develop a full electric powertrain for a Daimler Mercedes-Benz B-Class EV vehicle. We have substantially completed our development services under this B-Class program and commenced production of electric powertrains and battery packs for Daimler. The supply agreement for these products contemplates customary obligations of us such as timely deliveries, warranty and product defect obligations. If we fail to meet these obligations, or if we exceed our current cost projections for producing these products, our profitability on this program will suffer and this could have a negative impact on our operating results.

We may face regulatory limitations on our ability to sell vehicles directly or over the internet which could materially and adversely affect our ability to sell our electric vehicles.

We sell our vehicles from our Tesla stores as well as over the internet. We may not be able to sell our vehicles through this sales model in each state in the United States as many states have laws that may be interpreted to prohibit internet sales by manufacturers to residents of the state or to impose other limitations on this sales model, including laws that prohibit manufacturers from selling vehicles directly to consumers without the use of an independent dealership or without a physical presence in the state. In certain states in which we are not able to obtain dealer licenses, we have

worked with state regulators to open galleries, which are locations where potential customers can view our vehicles but are not full retail locations. It is possible that a state regulator could later determine that the activities at our gallery constitute unlicensed sales of motor vehicles.

In many states, the application of state motor vehicle laws to our specific sales model is largely untested under state motor vehicle industry laws and is being determined by a fact specific analysis of numerous factors, including whether we have a physical presence or employees in the applicable state, whether we advertise or conduct other activities in the applicable state, how the sale transaction is structured, the volume of sales into the state, and whether the state in question prohibits manufacturers from acting as dealers. As a result of the fact specific and largely untested nature of these issues, and the fact that applying these laws intended for the traditional automobile distribution model to our sales model allows for some interpretation and discretion by the regulators, the manner in which the applicable authorities are applying their state laws to our distribution model continues to be difficult to predict. Laws in some states have limited our ability to obtain dealer licenses from state motor vehicle regulators and may continue to do so.

In addition, decisions by regulators permitting us to sell vehicles may be subject to challenges as to whether such decisions comply with applicable state motor vehicle industry laws. For example, vehicle dealer associations in New York, Ohio and Massachusetts have filed lawsuits to revoke dealer licenses issued to us. These lawsuits have been dismissed, and in one recent court decision, the Supreme Court of Massachusetts held that state franchise laws like the one in Massachusetts do not restrict a manufacturer, like Tesla, that does not use franchised dealers from selling its vehicles directly to consumers. Such results have reinforced our continuing belief that state laws were not designed to prevent our distribution model. Similar lawsuits have been filed in Georgia and Missouri. Possible additional challenges in other states, if successful, could restrict or prohibit our ability to sell our vehicles to residents in such states. In some states, there have also been regulatory and legislative efforts by vehicle dealer associations to propose bills and regulations that, if enacted, would prevent us from obtaining dealer licenses in their states given our current sales model. Such events recently occurred in New Jersey, where the Motor Vehicle Commission, at the behest of the local automobile dealer lobby, passed a new regulation which purported to invalidate our sales licenses in the state, and in Michigan, where the state's automobile dealer association managed to add language into an unrelated bill that had the effect of impairing our right to sell vehicles through Tesla stores in Michigan. We have brought a lawsuit in New Jersey to invalidate that regulation, which we believe to be unlawful, and we are evaluating legislative and litigation solutions to remedy the situation in Michigan. Other states, such as New York, Ohio and Pennsylvania, have passed legislation that clarifies our ability to operate, but at the same time limits the number of dealer licenses we can obtain or stores that we can operate.

We are also registered as both a motor vehicle manufacturer and dealer in Canada, Australia, and Japan, and have obtained licenses to sell vehicles in other places such as Hong Kong and China. Furthermore, while we have performed an analysis of the principal laws in the European Union relating to our distribution model and believe we comply with such laws, we have not performed a complete analysis in all foreign jurisdictions in which we may sell vehicles. Accordingly, there may be laws in jurisdictions we have not yet entered or laws we are unaware of in jurisdictions we have entered that may restrict our sales or other business practices. Even for those jurisdictions we have analyzed, the laws in this area can be complex, difficult to interpret and may change over time.

We may need to defend ourselves against patent or trademark infringement claims, which may be time-consuming and would cause us to incur substantial costs.

Companies, organizations or individuals, including our competitors, may hold or obtain patents, trademarks or other proprietary rights that would prevent, limit or interfere with our ability to make, use, develop, sell or market our vehicles or components, which could make it more difficult for us to operate our business. From time to time, we may receive communications from holders of patents or trademarks regarding their proprietary rights. Companies holding patents or other intellectual property rights may bring suits alleging infringement of such rights or otherwise assert their rights and urge us to take licenses. In addition, if we are determined to have infringed upon a third party's intellectual property rights, we may be required to do one or more of the following:

- cease selling, incorporating or using vehicles or offering goods or services that incorporate or use the challenged intellectual property;
- pay substantial damages;
- obtain a license from the holder of the infringed intellectual property right, which license may not be available on reasonable terms or at all;
- redesign our vehicles or other goods or services; or
- establish and maintain alternative branding for our products and services.

In the event of a successful claim of infringement against us and our failure or inability to obtain a license to the infringed technology or other intellectual property right, our business, prospects, operating results and financial condition could be materially adversely affected. In addition, any litigation or claims, whether or not valid, could result in substantial costs and diversion of resources and management attention.

We may also face claims that our use of technology licensed or otherwise obtained from a third party infringes the rights of others. In such cases, we may seek indemnification from our licensors/suppliers under our contracts with them. However, indemnification may be unavailable or insufficient to cover our costs and losses, depending on our use of the technology, whether we choose to retain control over conduct of the litigation, and other factors.

Our patent applications may not result in issued patents, which may have a material adverse effect on our ability to prevent others from interfering with our commercialization of our products.

The status of patents involves complex legal and factual questions and the breadth and effectiveness of patented claims is uncertain. We cannot be certain that we are the first creator of inventions covered by pending patent applications or the first to file patent applications on these inventions, nor can we be certain that our pending patent applications will result in issued patents or that any of our issued patents will afford sufficient protection against someone creating a knockoff of our products, or as a defense against a competitor who claims that we are infringing its patents. In addition, patent applications filed in foreign countries are subject to laws, rules and procedures that differ from those of the United States, and thus we cannot be certain that foreign patent applications related to issued U.S. patents will result in issued patents in those foreign jurisdictions. In addition, others may obtain patents that we need to license or design around, either of which would increase costs and may adversely affect our business, prospects, financial condition and operating results.

Our trademark applications in certain countries remain subject to outstanding opposition proceedings.

We currently sell and market our products and services in various countries under our Tesla marks. We have filed trademark applications for our Tesla marks and opposition proceedings to trademark applications of third parties in various countries in which we currently sell and plan to sell our products and services. Certain of our trademark applications are subject to outstanding opposition proceedings brought by owners or applicants alleging prior applications for or use of similar marks. If we cannot resolve these oppositions and thereby secure registered rights in these countries, our ability to challenge third party users of the Tesla marks will be reduced and the value of the marks representing our exclusive brand name in these countries will be diluted. In addition, there is a risk that the prior rights owners could in the future take actions to challenge our use of the Tesla marks in these countries. Such actions could have a severe impact on our position in these countries and may inhibit our ability to use the Tesla marks in these countries. If we were prevented from using the Tesla marks in any or all of these countries, we would need to expend significant additional financial and marketing resources on establishing an alternative brand identity in these markets.

Our facilities or operations could be damaged or adversely affected as a result of disasters or unpredictable events.

Our corporate headquarters in Palo Alto, Tesla Factory in Fremont and additional component manufacturing facilities in Lathrop are located in Northern California, a region known for seismic activity. If major disasters such as earthquakes, fires, floods, hurricanes, wars, terrorist attacks, computer viruses, pandemics or other events occur, or our information system or communications network breaks down or operates improperly, our headquarters and production facilities may be seriously damaged, or we may have to stop or delay production and shipment of our products. In addition, our lease for our Palo Alto facility permits the landlord to terminate the lease following a casualty event if the needed repairs are in excess of certain thresholds and we do not agree to pay for any uninsured amounts. We may incur expenses relating to such damages, which could have a material adverse impact on our business, operating results and financial condition.

If our suppliers fail to use ethical business practices and comply with applicable laws and regulations, our brand image could be harmed due to negative publicity.

Our core values, which include developing the highest quality electric vehicles while operating with integrity, are an important component of our brand image, which makes our reputation particularly sensitive to allegations of unethical business practices. We do not control our independent suppliers or their business practices. Accordingly, we cannot guarantee their compliance with ethical business practices, such as environmental responsibility, fair wage practices, appropriate sourcing of raw materials, and compliance with child labor laws, among others. A lack of demonstrated compliance could lead us to seek alternative suppliers, which could increase our costs and result in delayed delivery of

our products, product shortages or other disruptions of our operations.

Violation of labor or other laws by our suppliers or the divergence of an independent supplier's labor or other practices from those generally accepted as ethical in the United States or other markets in which we do business could also attract negative publicity for us and our brand. This could diminish the value of our brand image and reduce demand for our performance electric vehicles if, as a result of such violation, we were to attract negative publicity. If we, or other manufacturers in our industry, encounter similar problems in the future, it could harm our brand image, business, prospects, financial condition and operating results.

Servicing our convertible senior notes requires a significant amount of cash, and we may not have sufficient cash flow from our business to pay our substantial debt.

We incurred $660.0 million, $920.0 million and $1.38 billion, respectively, in aggregate principal amount of senior indebtedness when we issued pursuant to registered public offerings 1.50% convertible senior notes due 2018 (2018 Notes) in 2013, and 0.25% convertible senior notes due 2019 (2019 Notes) and 1.25% convertible senior notes due 2021 (2021 Notes) in 2014. Our ability to make scheduled payments of the principal when due, to make quarterly interest payments or to make payments upon conversion or to refinance the Notes, depends on our future performance, which is subject to economic, financial, competitive and other factors beyond our control. Our business may not continue to generate cash flow from operations in the future sufficient to satisfy our obligations under the Notes and any future indebtedness we may incur and to make necessary capital expenditures. If we are unable to generate such cash flow, we may be required to adopt one or more alternatives, such as reducing or delaying investments or capital expenditures, selling assets, refinancing or obtaining additional equity capital on terms that may be onerous or highly dilutive. Our ability to refinance the Notes or future indebtedness will depend on the capital markets and our financial condition at such time. We may not be able to engage in any of these activities or engage in these activities on desirable terms, which could result in a default on the Notes or future indebtedness.

Pursuant to their terms, holders may convert their Notes at their option at any time prior to the final three-month period of the scheduled term of the respective Notes only under certain circumstances. For example, holders may generally convert their Notes at their option during a quarter (and only during such quarter), commencing with the fourth quarter of 2013 in the case of the 2018 Notes and the third quarter of 2014 in the case of the 2019 Notes and the 2021 Notes, if the last reported sale price of our common stock for at least 20 trading days (whether or not consecutive) during a period of 30 consecutive trading days ending on the last trading day of the immediately preceding quarter is greater than or equal to 130% of the conversion price for such series of Notes on each applicable trading day. As a result of this conversion feature, the 2018 Notes have been convertible at their holders' option during each quarter commencing with the fourth quarter of 2013, except the first quarter of 2014. Neither this nor any other conversion feature has been met with respect to the 2019 Notes and 2021 Notes, and consequently the 2019 Notes and 2021 have not been convertible at their holders' option Upon conversion of the Notes, we will be obligated to make cash payments in respect of the principal amounts thereof, and we may also have to deliver cash and, if applicable, shares of our common stock, in respect of such Notes. Any conversion of the Notes prior to their maturity, or acceleration of the repayment of the Notes or future indebtedness after any applicable notice or grace periods could have a material adverse effect on our business, results of operations and financial condition.

In addition, holders of the Notes will have the right to require us to purchase their Notes upon the occurrence of a fundamental change at a purchase price equal to 100% of the principal amount of the Notes, plus accrued and unpaid interest, if any, to, but not including, the fundamental change purchase date. However, we may not have enough available cash or be able to obtain financing at the time we are required to make purchases of Notes surrendered therefor or Notes being converted. In addition, our ability to purchase the Notes or to pay cash upon conversions of the Notes may be limited by law, by regulatory authority or by agreements governing our future indebtedness. Our failure to purchase Notes at a time when the purchase is required by the indenture or to pay cash payable on future conversions of the Notes as required by the indenture would constitute a default under the indenture. If the repayment of the related indebtedness were to be accelerated after any applicable notice or grace periods, we may not have sufficient funds to repay the indebtedness and purchase the Notes or make cash payments upon conversions thereof.

We may still incur substantially more debt or take other actions, which would intensify the risks discussed above.

We and our subsidiaries are not restricted under the terms of the indenture governing the Notes, or the indenture, from incurring additional debt, securing existing or future debt, recapitalizing our debt or taking a number of other actions that are not limited by the terms of the indenture that could have the effect of diminishing our ability to make

payments on the Notes when due.

The classification of our Notes may have a material effect on our reported financial results.

As described in the Risk Factor “Servicing our convertible senior notes requires a significant amount of cash, and we may not have sufficient cash flow from our business to pay our substantial debt,” Notes have been historically, and may become in the future, convertible at the option of their holders prior to their scheduled terms under certain circumstances. Even if holders do not elect to convert their Notes, the Notes become convertible prior to their scheduled maturity dates, we would be required to reclassify such Notes and the related debt issuance costs as current liabilities and certain portions of our equity outside of equity to mezzanine equity, which would have an adverse impact on our reported financial results for such quarter, and could have an adverse impact on the market price of our common stock.

Risks Related to the Ownership of our Common Stock

Concentration of ownership among our existing executive officers, directors and their affiliates may prevent new investors from influencing significant corporate decisions.

As of December 31, 2014, our executive officers, directors and their affiliates beneficially owned, in the aggregate, approximately 28.0% of our outstanding shares of common stock. In particular, Elon Musk, our Chief Executive Officer, Product Architect and Chairman of our Board of Directors, beneficially owned approximately 26.7% of our outstanding shares of common stock as of December 31, 2014. As a result, these stockholders will be able to exercise a significant level of control over all matters requiring stockholder approval, including the election of directors, amendment of our certificate of incorporation and approval of significant corporate transactions. This control could have the effect of delaying or preventing a change of control of our company or changes in management and will make the approval of certain transactions difficult or impossible without the support of these stockholders.

The trading price of our common stock is likely to continue to be volatile.

Our shares of common stock began trading on the Nasdaq Global Select Market in 2010 and, therefore, the trading history for our common stock has been limited. In addition, the trading price of our common stock has been highly volatile and could continue to be subject to wide fluctuations in response to various factors, some of which are beyond our control. Our common stock has experienced an intra-day trading high of $291.42 per share and a low of $177.22 per share over the last 52 weeks.

In addition, the stock market in general, and the market for technology companies in particular, has experienced extreme price and volume fluctuations that have often been unrelated or disproportionate to the operating performance of those companies. Broad market and industry factors may seriously affect the market price of companies' stock, including ours, regardless of actual operating performance. These fluctuations may be even more pronounced in the trading market for our stock during the period following a securities offering. In addition, in the past, following periods of volatility in the overall market and the market price of a particular company's securities, securities class action litigation has often been instituted against these companies. For example, a shareholder litigation like this was filed against us in 2013. While the trial court recently dismissed the plaintiffs' complaint with prejudice, this litigation (if the trial court's order is successfully appealed) or others like it could result in substantial costs and a diversion of our management's attention and resources.

A substantial portion of our total outstanding shares are held by a small number of insiders and investors and may be sold in the near future. The large number of shares eligible for public sale or subject to rights requiring us to register them for public sale could depress the market price of our common stock.

The market price of our common stock could decline as a result of sales of a large number of shares of our common stock in the market in the future, and the perception that these sales could occur may also depress the market price of our common stock. Stockholders owning a substantial portion of our total outstanding shares are entitled, under contracts providing for registration rights, to require us to register shares of our common stock owned by them for public sale in the United States, subject to the restrictions of Rule 144. In addition, we have registered shares previously issued or reserved for future issuance under our equity compensation plans and agreements, a portion of which are related to outstanding option awards. Subject to the satisfaction of applicable exercise periods and the shares of common stock issued upon exercise of outstanding options will be available for immediate resale in the United States in the open market. Sales of our common stock as restrictions end or pursuant to registration rights may make it more difficult for us to sell equity securities in the future at a time and at a price that we deem appropriate. These sales also could cause our stock price to fall and make it more difficult to sell shares of our common stock.

Conversion of the Notes may dilute the ownership interest of existing stockholders, including holders who had previously converted their Notes, or may otherwise depress the price of our common stock.

The conversion of some or all of the Notes will dilute the ownership interests of existing stockholders to the extent we deliver shares upon conversion of any of the Notes. As described in the Risk Factor “Servicing our convertible senior notes requires a significant amount of cash, and we may not have sufficient cash flow from our business to pay our substantial debt,” Notes have been historically, and may become in the future, convertible at the option of their holders prior to their scheduled terms under certain circumstances. Any sales in the public market of the common stock issuable upon such conversion could adversely affect prevailing market prices of our common stock. In addition, the existence of the Notes may encourage short selling by market participants because the conversion of the Notes could be used to satisfy short positions, or anticipated conversion of the Notes into shares of our common stock could depress the price of our common stock.

The convertible note hedge and warrant transactions we entered into in connection with the issuance of Notes may affect the value of the Notes and our common stock.

In connection with each issuance of the Notes, we entered into convertible note hedge transactions with the hedge counterparties. The convertible note hedge transactions cover, subject to customary anti-dilution adjustments, the number of shares of our common stock that initially underlay the applicable Notes. The convertible note hedge transactions are expected to reduce the potential dilution and/or offset potential cash payments we are required to make in excess of the principal amount upon conversion of the applicable Notes. We also entered into warrant transactions with the hedge counterparties relating to the same number of shares of our common stock, subject to customary anti-dilution adjustments. However, the warrant transactions could separately have a dilutive effect on our common stock to the extent that the market price per share of our common stock exceeds the applicable strike price of the warrants on the applicable expiration dates.

In addition, the hedge counterparties or their affiliates may modify their hedge positions by entering into or unwinding various derivatives with respect to our common stock and/or purchasing or selling our common stock or other securities of ours in secondary market transactions prior to the maturity of the applicable Notes (and are likely to do so during any observation period related to a conversion of Notes). This activity could also cause or prevent an increase or a decrease in the market price of our common stock or the Notes.

We do not make any representation or prediction as to the direction or magnitude of any potential effect that the transactions described above may have on the prices of the Notes or the shares of our common stock. In addition, we do not make any representation that the hedge counterparties have engaged or will engage in these transactions or that these transactions, once commenced, will not be discontinued without notice.

Mr. Musk borrowed funds from affiliates of certain underwriters in our public offerings and/or private placements and has pledged shares of our common stock to secure these borrowings. The forced sale of these shares pursuant to a margin call could cause our stock price to decline and negatively impact our business.

Beginning in June 2011, banking institutions that are affiliated with certain underwriters of our completed public offerings of common stock and Notes made extensions of credit to Elon Musk and the Elon Musk Revocable Trust dated July 22, 2003, or the Trust, a portion of which Mr. Musk used to purchase shares of common stock in our public offering in May 2013 and private placements in June 2011 and June 2013. Interest on such loans accrues at market rates and the banking institutions received customary fees and expense reimbursements in connection with these loans.

We are not a party to these loans, which are full recourse against Mr. Musk and the Trust and are secured by pledges of a portion of the Tesla common stock currently owned by Mr. Musk and the Trust and other shares of capital stock of unrelated entities owned by Mr. Musk and the Trust. The terms of these loans were negotiated directly between Mr. Musk and the applicable banking institutions.

If the price of our common stock declines, Mr. Musk may be forced by one or more of the banking institutions to provide additional collateral for the loans or to sell shares of Tesla common stock in order to remain within the margin limitations imposed under the terms of his loans. The loans between these banking institutions on the one hand, and Mr. Musk and the Trust on the other hand, prohibit the non-pledged shares currently owned by Mr. Musk and the Trust from being pledged to secure any other loans. These factors may limit Mr. Musk’s ability to either pledge additional shares of Tesla common stock or sell shares of Tesla common stock as a means to avoid or satisfy a margin call with respect to his pledged Tesla common stock in the event of a decline in our stock price that is large enough to trigger a margin call. Any sales of common stock following a margin call that is not satisfied may cause the price of our common stock to decline further.

Anti-takeover provisions contained in our certificate of incorporation and bylaws, the provisions of Delaware law, and the terms of our convertible notes could impair a takeover attempt.

Our certificate of incorporation, bylaws, Delaware law and the terms of our Notes contain provisions which could have the effect of rendering more difficult, delaying or preventing an acquisition deemed undesirable by our board of directors. Our corporate governance documents include provisions:

- creating a classified board of directors whose members serve staggered three-year terms;
- authorizing “blank check” preferred stock, which could be issued by the board without stockholder approval and may contain voting, liquidation, dividend and other rights superior to our common stock;
- limiting the liability of, and providing indemnification to, our directors and officers;
- limiting the ability of our stockholders to call and bring business before special meetings;
- requiring advance notice of stockholder proposals for business to be conducted at meetings of our stockholders and for nominations of candidates for election to our board of directors;

controlling the procedures for the conduct and scheduling of board and stockholder meetings; and
providing the board of directors with the express power to postpone previously scheduled annual meetings and to cancel previously scheduled special meetings.

These provisions, alone or together, could delay or prevent hostile takeovers and changes in control or changes in our management.

As a Delaware corporation, we are also subject to provisions of Delaware law, including Section 203 of the Delaware General Corporation law, which prevents some stockholders holding more than 15% of our outstanding common stock from engaging in certain business combinations without approval of the holders of substantially all of our outstanding common stock.

Any provision of our certificate of incorporation or bylaws or Delaware law that has the effect of delaying or deterring a change in control could limit the opportunity for our stockholders to receive a premium for their shares of our common stock, and could also affect the price that some investors are willing to pay for our common stock.

In addition, the terms of the convertible notes require us to repurchase the convertible notes in the event of a fundamental change. A takeover of our company would trigger an option of the holders of the convertible notes to require us to repurchase the convertible notes. This may have the effect of delaying or preventing a takeover of our company that would otherwise be beneficial to our stockholders or investors in the convertible notes.

The fundamental change repurchase feature of the Notes may delay or prevent an otherwise beneficial attempt to take over our company.

The terms of the Notes require us to repurchase the Notes in the event of a fundamental change. A takeover of our company would trigger options by the respective holders of the applicable Notes to require us to repurchase such Notes. This may have the effect of delaying or preventing a takeover of our company that would otherwise be beneficial to our stockholders or investors in the Notes.

If securities or industry analysts publishing research or reports about us, our business or our market change their recommendations regarding our stock adversely or cease to publish research or reports about us, our stock price and trading volume could decline.

The trading market for our common stock will be influenced by the research and reports that industry or securities analysts may publish about us, our business, our market or our competitors. If any of the analysts who may cover us change their recommendation regarding our stock adversely, or provide more favorable relative recommendations about our competitors, our stock price would likely decline. If any analyst who may cover us were to cease coverage of our company or fail to regularly publish reports on us, we could lose visibility in the financial markets, which in turn could cause our stock price or trading volume to decline.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

The following table sets forth the location, approximate size and primary use of our principal leased and owned facilities:

Location	Approximate Size (Building) in Square Feet	Primary Use	Lease Expiration Date
Fremont, California	5,400,000	Manufacturing, administration, engineering services, parts warehousing, and vehicle service	Owned building
Palo Alto, California	350,000	Corporate headquarters, administration, engineering services and powertrain development services	January 2020
Tilburg, Netherlands	203,772	Administration, engineering services, powertrain development services, parts warehousing, final vehicle assembly and vehicle service	November 2023
Lathrop, California	430,770	Manufacturing	Owned building (1)
Amsterdam, Netherlands	71,142	Administration	February 2024
Hawthorne, California	132,250	Vehicle engineering and design services	December 2022
Maidenhead, United Kingdom	8,870	Administration, sales, service and marketing services	November 2015
Beijing, China	8,190	Administration, sales and marketing services	November 2017

(1) As of December 31, 2014, the Lathrop property was subject to a lease agreement. In January 2015, Tesla exercised its option to purchase the Lathrop property under the terms of the lease agreement.

In addition to the properties included in the table above, we also lease a number of properties in North America, Europe and Asia for our retail and service locations as well as Supercharger sites.

We currently intend to add new facilities or expand our existing facilities as we add employees and expand our network of stores and galleries, service locations and Supercharger sites. We believe that suitable additional or alternative space will be available in the future on commercially reasonable terms to accommodate our foreseeable future expansion.

ITEM 3. LEGAL PROCEEDINGS

See Item 8 of Part II, Financial Statements and Supplementary Data—Note 11—Commitments and Contingencies.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Market Information

Our common stock has traded on The NASDAQ Global Select Market under the symbol "TSLA" since it began trading on June 29, 2010. Our initial public offering was priced at $17.00 per share on June 28, 2010. The following table sets forth, for the time period indicated, the high and low closing sales price of our common stock as reported on The NASDAQ Global Select Market.

	2014		2013	
	High	Low	High	Low
First Quarter	$254.84	$139.34	$39.48	$32.91
Second Quarter	240.06	178.59	110.33	40.50
Third Quarter	286.04	215.40	193.37	109.05
Fourth Quarter	260.62	197.81	193.00	120.50

Holders

As of January 31, 2015, there were 769 holders of record of our common stock. A substantially greater number of holders of our common stock are "street name" or beneficial holders, whose shares are held by banks, brokers and other financial institutions.

Dividend Policy

We have never declared or paid cash dividends on our common stock. We currently do not anticipate paying any cash dividends in the foreseeable future. Any future determination to declare cash dividends will be made at the discretion of our board of directors, subject to applicable laws, and will depend on our financial condition, results of operations, capital requirements, general business conditions and other factors that our board of directors may deem relevant.

Stock Performance Graph

This performance graph shall not be deemed "filed" for purposes of Section 18 of the Securities Exchange Act of 1934, as amended (the Exchange Act), or incorporated by reference into any filing of Tesla Motors, Inc. under the Securities Act of 1933, as amended, or the Exchange Act, except as shall be expressly set forth by specific reference in such filing.

The following graph shows a comparison from June 29, 2010 through December 31, 2014, of the cumulative total return for our common stock, the NASDAQ Composite Index, and a group of all public companies sharing the same SIC code as us which is SIC code 3711, “Motor Vehicles and Passenger Car Bodies” (Motor Vehicles and Passenger Car Bodies Public Company Group). Such returns are based on historical results and are not intended to suggest future performance. Data for The NASDAQ Composite Index and the Motor Vehicles and Passenger Car Bodies Public Company Group assumes an investment of $100 on June 29, 2010 and reinvestment of dividends. We have never declared or paid cash dividends on our capital stock nor do we anticipate paying any such cash dividends in the foreseeable future.

Unregistered Sales of Equity Securities

None.

Purchases of Equity Securities by the Issuer and Affiliated Purchasers

None.

ITEM 6. SELECTED CONSOLIDATED FINANCIAL DATA

The following selected consolidated financial data should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our consolidated financial statements and the related notes included elsewhere in this Annual Report on Form 10-K.

	Year Ended December 31,				
	2014	2013	2012	2011	2010
	(in thousands, except share and per share data)				
Consolidated Statements of Operations Data:					
Total revenues	$3,198,356	$2,013,496	$413,256	$204,242	$116,744
Gross profit	881,671	456,262	30,067	61,595	30,731
Loss from operations	(186,689)	(61,283)	(394,283)	(251,488)	(146,838)
Net loss	$(294,040)	$(74,014)	$(396,213)	$(254,411)	$(154,328)
Net loss per share of common stock, basic and diluted (1)	$(2.36)	$(0.62)	$(3.69)	$(2.53)	$(3.04)
Weighted average shares used in computing net loss per share of common stock, basic and diluted (1)	124,573,415	119,421,414	107,349,188	100,388,815	50,718,302

(1) Diluted net loss per share of common stock is computed excluding common stock subject to repurchase, and, if dilutive, potential shares of common stock outstanding during the period. Potential shares of common stock consist of stock options to purchase shares of our common stock, the conversion of our convertible senior notes (using the treasury stock method), warrants to purchase shares of our common stock issued in connection with our 2018 Notes, 2019 Notes, and 2021 Notes (using the treasury stock method), warrants to purchase shares of our convertible preferred stock (using the treasury stock method) and the conversion of our convertible preferred stock and convertible notes payable (using the if-converted method). For purposes of these calculations, potential shares of common stock have been excluded from the calculation of diluted net loss per share of common stock as their effect is antidilutive since we generated a net loss in each period.

	As of December 31,				
	2014	2013	2012	2011	2010
Consolidated Balance Sheet Data:					
Working capital (deficit)	$1,091,491	$590,779	$(14,340)	$181,499	$150,321
Total assets	5,849,251	2,416,930	1,114,190	713,448	386,082
Total long-term obligations (1)(2)	2,772,179	1,074,650	450,382	298,064	93,469

(1) In May 2013, we issued $660.0 million aggregate principal amount of 2018 Notes in a public offering. In accordance with accounting guidance on embedded conversion features, we valued and bifurcated the conversion option associated with the 2018 Notes from the host debt instrument and initially recorded the conversion option of $82.8 million in equity. During the fourth quarter of 2014, the closing price of our common stock exceeded 130%

of the applicable conversion price of our 2018 Notes on at least 20 of the last 30 consecutive trading days of the quarter; therefore, holders of 2018 Notes may convert their notes during the first quarter of 2015. As such, we classified the $601.6 million carrying value of our 2018 Notes as current liabilities on our condensed consolidated balance sheet as of December 31, 2014.

In March 2014, we issued $800.0 million principal amount of 0.25% convertible senior notes due 2019 (2019 Notes) and $1.20 billion principal amount of 1.25% convertible senior notes due 2021 (2021 Notes) in a public offering. In April 2014, we issued an additional $120.0 million aggregate principal amount of 2019 Notes and $180.0 million aggregate principal amount of 2021 Notes, pursuant to the exercise in full of the overallotment options of the underwriters of our March 2014 public offering. In accordance with accounting guidance on embedded conversion features, we valued and bifurcated the conversion option associated with the notes from the host debt instrument and recorded the conversion option of $188.1 million for the 2019 Notes and $369.4 million for the 2021 Notes in stockholders' equity.

(2) As of August 31, 2012, we had fully drawn down our $465.0 million under our DOE loan facility. In May 2013, we used a portion of the Notes offering proceeds to repay all outstanding loan amounts under the DOE Loan Facility.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis should be read in conjunction with our consolidated financial statements and the related notes that appear elsewhere in this Annual Report on Form 10-K.

Overview and 2014 Highlights

We design, develop, manufacture and sell high-performance fully electric vehicles, advanced electric vehicle powertrain components and stationary energy storage applications. We are currently producing and selling our second vehicle, the Model S sedan. Model S is a four door, five-passenger premium sedan that offers exceptional performance, functionality and attractive styling. The Model S inherited many of the electric powertrain innovations we introduced with our first vehicle, the Tesla Roadster. We commenced deliveries of Model S in June 2012 and have delivered 56,768 vehicles through December 31, 2014. We recently announced the availability of our All-Wheel Drive Dual Motor Model S and began delivery, starting with a performance-optimized version, in December 2014.

We are continuing to develop our Model X crossover vehicle and intend to commence customer deliveries in the third quarter of 2015. After the Model X, our goal is to introduce Model 3, a lower priced sedan designed for the mass market, in 2017.

Our primary source of revenue is from the sale of our vehicles. During the year ended December 31, 2014, we recognized total revenues of $3.20 billion, an increase of $1.19 billion over total revenues of $2.01 billion for the year ended December 31, 2013, primarily driven by growth of Model S deliveries worldwide.

Gross margin for the year ended December 31, 2014 was 27.6%, a significant increase from 22.7% for the year ended December 31, 2013. Higher vehicle production volume, supply chain efficiencies and component cost reductions, partially offset by one-time manufacturing inefficiencies associated with transitioning to our new final assembly line and introduction of All-Wheel Drive Dual Motor Model S, contributed to higher gross margin in 2014.

Research and development (R&D) expenses for the year ended December 31, 2014 were $464.7 million, an increase from $232.0 million for the year ended December 31, 2013. R&D expenses in 2014 reflected our engineering work on Model X as well as development work on our dual motor powertrain and other development programs including localization efforts for foreign markets. R&D expenses in 2013 reflected our activities on manufacturing process improvements, Model S cost reductions, the right-hand drive Model S and localization efforts for foreign markets, as well as development work on Model X.

During 2014, we significantly increased our sales and service footprint worldwide, entered several new markets including China, as well as accelerated the rollout of our Supercharging network. With the continued global expansion of our customer support infrastructure and the business in general in 2014, selling, general and administrative expenses were $603.7 million for the year ended December 31, 2014, compared to $285.6 million for the year ended December 31, 2013.

Management Opportunities, Challenges and Risks

Orders, Production and Deliveries

Our orders for Model S in 2014 significantly increased from the prior year as we expanded our operations internationally and introduced Model S product enhancements. In October 2014, we revealed our All-Wheel Drive Dual Motor Model S and our Autopilot system. This version of Model S proved very popular, leading to over 10,000 unfulfilled orders as of January 1, 2015. We expect that demand for Model S will continue to increase worldwide as more people drive and become aware of our vehicles, as we grow our customer support infrastructure, and as we broaden the appeal of our products.

As of December 31, 2014, we had received almost 20,000 reservations for Model X in advance of its planned introduction later this year. We are continuing to test the Beta Model X prototypes, and plan to begin building and testing a small fleet of release candidate Model X vehicles later in the first quarter of 2015. Our ability to launch the Model X program on time and cost efficiently is dependent upon a variety of factors, including completion of production tooling, supplier readiness, engineering completion and the successful completion of our validation testing.

In order to meet this anticipated demand for both Model S and Model X, we are executing a plan to increase our combined Model S and Model X production capacity to over 2,000 units per week by the end of 2015. In August 2014, we began our production ramp by transitioning to our new final assembly line and upgrading our body center. We are planning further investments in production capacity during 2015, including building a new paint shop and a new body shop for Model X. We expect our annual production will increase by over 50% each year for the next several years.

Our recent production capacity expansion contributed to several weeks of production in excess of 1,000 vehicles per week during the last few months of 2014. However, the changeover to our new final assembly line during the third quarter of 2014 and the introduction of All-Wheel Drive Dual Motor Model S onto this line during the fourth quarter of 2014 took longer than we expected. Consequently, we delivered fewer vehicles than we had planned in 2014. During 2015, we plan to achieve significant efficiencies in Model S production and begin production of Model X with the intent of achieving a significantly faster initial production ramp than we achieved with Model S. Any unexpected issues with the expansion of our production capacity or the launch and ramp of Model X production could affect our ability to meet future delivery targets.

In addition to expanding our production, we expect to continue to lower the cost of manufacturing our vehicles and improve our gross margin. Significant cost improvements for Model S were achieved in 2013 and 2014, including part cost reductions as well as manufacturing efficiencies. We expect that this trend will continue as we execute on our roadmap. We expect that such improvements, when combined with a favorable mix of vehicles, will allow us to achieve a 30% gross margin on Model S by the end of 2015, assuming no further deterioration in foreign currencies. However, we expect these cost improvements will be partially offset by production inefficiencies during the introduction of Model X. During our product introductions in 2014, we incurred manufacturing inefficiencies which negatively impacted our gross margin. When we introduce Model X, we expect that both production inefficiencies and supply chain inefficiencies typical of a new product introduction will suppress Model X margins for at least a few quarters after its introduction. If we are not able to achieve the planned cost reductions from our various cost savings and process improvement initiatives or introduce Model X efficiently, our ability to reach our gross margin goals would be negatively affected.

We expect to deliver approximately 55,000 Model S and X vehicles worldwide in 2015, approximately 74% more deliveries than we achieved in 2014. To support this growth, we plan to continue to expand our Supercharger, stores and service infrastructure worldwide as well as to provide better service in areas with a high concentration of Model S customers. As we now offer Model S in countries throughout North America, Europe and Asia, our expansion will primarily occur in geographic areas in which we already have a presence. Based on our current projections, we expect our long-term sales outside of North America will increase to almost half of our worldwide automotive sales. Despite initial challenges in China, we plan to continue to invest in our infrastructure in China as we believe that the country could be one of our largest markets within a few years. However, as compared to markets in the United States and Europe, we have relatively limited experience in Asian markets; thus, we may face continuing difficulties meeting our future expansion plans in Asia.

Trends in Capital Expenditures and Operating Expenses

Our capital expenditures and operating expenses significantly increased in 2014. As we continue to invest in the long term growth of Tesla, capital spending and operating expenses will continue to increase, but at a more moderate pace than in 2014. During 2015, capital expenditures are expected to be about $1.5 billion as we expand production capacity, complete Model X development, and invest in the Gigafactory, our stores and service centers. We also plan to grow our Supercharger network by over 50% this year as well as continue other product development programs, including Model 3.

Our operating expenses will continue to grow in 2015, but at less than half the pace of growth in 2014, or approximately 45% to 50% annualized. Our R&D expenses in particular will continue to increase as we complete the development, validation, and testing of Model X and accelerate design and engineering work on Model 3. Growth of sales, general and administrative expenses will be more modest as we will be particularly focused on increasing operational efficiency while we continue to expand our customer and corporate infrastructure. Over time, we expect overall operating expenses to decrease as a percentage of revenue.

As of December 31, 2014 and 2013 the net book value of our Supercharger network was $107.8 million and $25.6 million and currently includes 380 locations globally. We plan to continue investing in our Supercharger network for the foreseeable future, including in North America, Europe and Asia and expect such spending to be approximately 5% of total capital spending over the next 12 months. We allocate Supercharger related expenses to cost of revenues automotive sales and selling, general, and administrative expenses. These costs were immaterial for all periods presented.

Customer Financing Options

We offer loans and leases in North America, Europe and Asia primarily through various financial institutions. In 2013, we began offering a resale value guarantee in connection with certain loans offered by financial institutions and have since provided this guarantee to approximately 10,400 Model S customers. Model S deliveries with the resale value guarantee currently do not impact our cash flows and liquidity, since we receive the full amount of cash for the vehicle sales price at delivery. However, this program requires the deferral of revenues and costs into future periods under lease accounting. Although lease accounting will continue to impact our revenues and operating results as this and similar programs initially ramp up, as time passes, the amortization of existing deferred revenues and costs will begin to partially offset this adverse impact. Furthermore, while we do not assume any credit risk related to the customer, we are exposed to the risk that the vehicles' resale value may be lower than our estimates and the volume of vehicles returned to us may be higher than our estimates which could adversely impact our gross margin.

We currently offer leases in the U.S. directly from Tesla Finance, our captive financing entity, as well as through a bank partner. Leasing through Tesla Finance is now available in 37 states, the District of Columbia and in 4 provinces of Canada. We leased approximately 1,150 vehicles through Tesla Finance during 2014 and about approximately 200 vehicles through our banking partner. Leasing through both Tesla Finance and our banking partner exposes us to residual value risk and will adversely impact our near-term revenues and operating results by requiring the deferral of revenues and costs into future periods under lease accounting. In addition, for leases offered directly from Tesla Finance (but not for those offered through our bank partner), we will not receive the full amount of the cash for the vehicle price at delivery and will assume customer credit risk. We expect to increase our leasing activities during 2015.

We have set the residual values given to our customers under our resale value guarantee program at what we estimate will be the trade-in value of these vehicles at the end of the term of the option. Based on current market demand for our cars, we estimate the resale prices for our vehicles will continue to be above our resale value guarantee amounts. Should market values or customer demand decrease, these estimates may be impacted materially.

The Tesla Gigafactory

We are developing the Tesla Gigafactory, a facility where we intend to work together with our suppliers to integrate battery precursor material, cell, module and battery pack production in one location. In June 2014, we broke ground on the Gigafactory outside of Reno, Nevada. Construction continued during the end of 2014 at an accelerated pace with first cells expected to be produced in 2016 for use in Model S and Model X.

While our plan is to produce lithium-ion cells and finished battery packs at the Gigafactory, our plans for such production are at a very early stage. We have no experience in the production of lithium-ion cells, and accordingly we intend to engage partners with significant experience in cell production. We recently formalized our agreement with Panasonic to partner on the Gigafactory. Panasonic will invest in production equipment that it will use to manufacture and supply us with battery cells. We will prepare and provide the land, buildings and utilities for the Gigafactory, invest in production equipment for battery module and pack production and be responsible for the overall management of the Gigafactory. We anticipate bringing on additional partners for the Gigafactory to create a fully integrated industrial complex. Although planning discussions with production and supply chain partners continue to progress well, to date we have not formalized any agreements with any other partners. In addition, the cost of building and operating the Gigafactory could exceed our current expectations and the Gigafactory may take longer to bring online than we anticipate.

Critical Accounting Policies and Estimates

Our consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States. The preparation of these consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, costs and expenses and related disclosures. We base our estimates on historical experience, as appropriate, and on various other assumptions that we believe to be reasonable under the circumstances. Changes in the accounting estimates are reasonably likely to occur from period to period. Accordingly, actual results could differ significantly from the estimates made by our management. We evaluate our estimates and assumptions on an ongoing basis. To the extent that there are material differences between

these estimates and actual results, our future financial statement presentation, financial condition, results of operations and cash flows will be affected. We believe that the following critical accounting policies involve a greater degree of judgment and complexity than our other accounting policies. Accordingly, these are the policies we believe are the most critical to understanding and evaluating our consolidated financial condition and results of operations.

Revenue Recognition

Automotive Sales

We recognize automotive sales revenue from sales of Model S, including vehicle options, accessories and destination charges, vehicle service and sales of regulatory credits, such as ZEV and greenhouse gas emission (GHG) credits. We also recognize automotive sales revenue from the sales of electric vehicle powertrain components and systems, such as battery packs and drive units, to other manufacturers. Revenue is recognized when (i) persuasive evidence of an arrangement exists; (ii) delivery has occurred and there are no uncertainties regarding customer acceptance; (iii) fees are fixed or determinable; and (iv) collection is reasonably assured.

Car sales include certain standard features and customer selected options and configurations that meet the definition of a deliverable under multiple-element accounting guidance, including internet connectivity, Supercharging access, and specified software updates for cars equipped with Autopilot hardware. These deliverables are valued on a stand-alone basis and we recognize their related revenue over our performance period which is generally the eight-year life of the car or, for software upgrades, as they are delivered. If we sell a derivable separately, we use that pricing to determine its fair value; otherwise, we use our best estimated selling price by considering third party pricing of similar options, costs used to develop and deliver the service, and other information which may be available.

Resale Value Guarantee

We offer a resale value guarantee program to customers who purchase a Model S and finance their vehicle through one of our commercial banking partners in the US, Canada and Europe. Under this program, Model S customers have the option of selling their vehicle back to us during the period from 36 to 39 months after delivery for a specified value determined at time of purchase. Because we offer a resale value guarantee, we account for these transactions as operating leases. Accordingly, we recognize revenue attributable to the lease on a straight-line basis over the guarantee period to automotive sales revenue. Similarly, we capitalize the cost of the leased vehicle and depreciate its value, less expected salvage value, to cost of automotive sales over the same period.

At the end of the guarantee period, which is the earlier of 39 months or the pay-off date of the initial loan, the resale value guarantee and deferred revenue balances are settled to automotive sales revenue and the net book value of the leased vehicle is expensed to costs of automotive sales if our customer retains ownership of the car. In cases where a customer returns the vehicle back to us between months 36 and 39, we issue a check to the customer in the amount of the resale value guarantee and settle any remaining deferred revenue balance to automotive sales revenue.

At least annually, we assess the estimated market values of vehicles under our resale value guarantee program. As we accumulate more data related to the resale values of Model S, there may be significant changes to their estimated values.

Maintenance and Service Plans

We offer a prepaid maintenance program for Model S, which includes plans covering maintenance for up to eight years or up to 100,000 miles, provided these services are purchased within a specified period of time. The maintenance plans cover annual inspections and the replacement of wear and tear parts, excluding tires and the battery, with either a fixed fee per visit for Tesla Ranger service or unlimited Tesla Ranger visits for a higher initial purchase price. Payments collected in advance of the performance of service are initially recorded in deferred revenues on the consolidated balance sheets and recognized in automotive sales as we fulfill our performance obligations.

We also offer an extended service plan, which covers the repair or replacement of Model S parts for an additional four years or up to an additional 50,000 miles, after the end of our initial New Vehicle Limited Warranty, provided they are purchased within a specified period of time. For customers that are not covered by our New Vehicle Limited Warranties or our extended service plans, we offer Tesla Ranger service at a higher cost. Payments collected in advance of the performance of service are initially recorded in deferred revenues on the consolidated balance sheets and recognized in automotive sales ratably over the service coverage periods.

We provided Tesla Roadster customers with the opportunity to purchase an extended warranty plan for the period after the end of our initial New Vehicle Limited Warranty to cover additional services for an additional three years or 36,000 miles. We refer to this program as our Extended Service plan. Amounts collected on these sales are initially recorded in deferred revenues on the consolidated balance sheets and recognized in automotive sales over the extended warranty period.

Additionally, we have previously provided customers of our Tesla Roadsters with a one-time option to replace the battery packs in their vehicles at any time after the expiration of the New Vehicle Limited Warranty but before the tenth anniversary of the purchase date of their vehicles. We refer to this program as our Battery Replacement program. Amounts collected on these sales are initially recorded in deferred revenues on the consolidated balance sheets and recognized in automotive sales as we fulfill our obligation to replace the battery packs.

Inventory Valuation

We value our inventories at the lower of cost or market. Cost is computed using standard cost, which approximates actual cost on a first-in, first-out basis. We record inventory write-downs for estimated obsolescence or unmarketable inventories based upon assumptions about future demand forecasts. If our inventory on hand is in excess of our future demand forecast, the excess amounts are written off.

We also review inventory to determine whether its carrying value exceeds the net amount realizable upon the ultimate sale of the inventory. This requires us to determine the estimated selling price of our vehicles less the estimated cost to convert inventory on hand into a finished product.

Once inventory is written-down, a new, lower-cost basis for that inventory is established and subsequent changes in facts and circumstances do not result in the restoration or increase in that newly established cost basis.

Should our estimates of future selling prices or production costs change, material changes to these reserves may be required. A small change in our estimates may result in a material charge to our reported financial results.

Warranties

We provide a warranty on all vehicles, production powertrain components and systems sales, and we accrue warranty reserves upon delivery to customer. Warranty reserves include management's best estimate of the projected costs to repair or to replace any items under warranty. These estimates are based on actual claims incurred to-date and an estimate of the nature, frequency and costs of future claims. We review our reserves at least quarterly to ensure that our accruals are adequate in meeting expected future warranty obligations, and we will adjust our estimates as needed. These estimates are inherently uncertain and changes to our historical or projected experience may cause material changes to our warranty reserves in the future. The portion of the warranty provision expected to be incurred within 12 months is classified as current within accrued liabilities, while the remaining amount is classified as long-term within other long-term liabilities. During the third quarter of 2014, we extended the warranty on our Model S drive unit to eight years from four and reassessed our overall powertrain and vehicle warranty reserves which resulted in an additional charge of approximately $14.0 million.

Our warranty reserves do not include projected warranty costs associated with our operating lease vehicles, including those sold with resale value or similar guarantee terms. In such cases actual warranty costs are expensed as incurred and are recorded as a component of cost of revenues.

Valuation of Stock-Based Awards

Stock-Based Compensation

We use the fair value method of accounting for our stock options and restricted stock units (RSUs) granted to employees and our Employee Stock Purchase Plan (ESPP) to measure the cost of employee services received in exchange for the stock-based awards. The fair value of stock options and ESPP are estimated on the grant date and offering date using the Black-Scholes option-pricing model. The fair value of RSUs is measured on the grant date based on the closing fair market value of our common stock. The resulting cost is recognized over the period during which an employee is required to provide service in exchange for the awards, usually the vesting period which is generally four years for stock options and RSUs and six months for the ESPP. Stock-based compensation expense is recognized on a straight-line basis, net of estimated forfeitures.

The Black-Scholes option-pricing model requires inputs such as the risk-free interest rate, expected term and expected volatility. Further, the forfeiture rate also affects the amount of aggregate compensation. These inputs are subjective and generally require significant judgment.

We estimate our forfeiture rate based on an analysis of our actual forfeiture experience and will continue to evaluate the appropriateness of the forfeiture rate based on actual forfeiture experience, analysis of employee turnover behavior and other factors. Quarterly changes in the estimated forfeiture rate can have a significant effect on reported stock-based compensation expense, as the cumulative effect of adjusting the rate for all expense amortization is recognized in the period the forfeiture estimate is changed. If a revised forfeiture rate is higher than the previously estimated forfeiture rate, an adjustment is made that will result in a decrease to the stock-based compensation expense recognized in the consolidated financial statements. If a revised forfeiture rate is lower than the previously estimated forfeiture rate, an adjustment is made that will result in an increase to the stock-based compensation expense recognized in the consolidated financial statements.

As we accumulate additional employee stock-based awards data over time and as we incorporate market data related to our common stock, we may calculate significantly different volatilities, expected lives and forfeiture rates, which could materially impact the valuation of our stock-based awards and the stock-based compensation expense that we will recognize in future periods. Stock-based compensation expense is recorded in our cost of revenues, research and

development expenses, and selling, general and administrative expenses.

In August 2012, our Board of Directors granted 5,274,901 stock options to our CEO (2012 CEO Grant). The 2012 CEO Grant consists of ten vesting tranches with a vesting schedule based entirely on the attainment of both performance conditions and market conditions, assuming continued employment and service to us through each vesting date.

Each of the vesting tranches requires a combination of one of the ten pre-determined performance milestones outlined below and an incremental increase in our market capitalization of $4.0 billion, as compared to the initial market capitalization of $3.2 billion measured at the time of the 2012 CEO Grant.

- Successful completion of the Model X Alpha Prototype;
- Successful completion of the Model X Beta Prototype;
- Completion of the first Model X Production Vehicle;
- Successful completion of the Model 3 Alpha Prototype;
- Successful completion of the Model 3 Beta Prototype;

· Completion of the first Model 3 Production Vehicle;
· Gross margin of 30% or more for four consecutive quarters;
· Aggregate vehicle production of 100,000 vehicles;
· Aggregate vehicle production of 200,000 vehicles; and
· Aggregate vehicle production of 300,000 vehicles.

The term of the 2012 CEO Grant is ten years, so any tranches that remain unvested at the expiration of the 2012 CEO Grant will be forfeited. In addition, unvested options will be forfeited if our CEO is no longer in that role, whether for cause or otherwise.

We measured the fair value of the 2012 CEO Grant using a Monte Carlo simulation approach with the following assumptions: risk-free interest rate of 1.65%, expected term of ten years, expected volatility of 55% and dividend yield of 0%.

Stock-based compensation expense associated with the 2012 CEO Grant is recognized for each pair of performance and market conditions over the longer of the expected achievement period of the performance and market conditions, beginning at the point in time that the relevant performance condition is considered probable of being met.

As of December 31, 2014, the market conditions for six vesting tranches and the following performance milestone were achieved and approved by our Board of Directors:

· Successful completion of the Model X Alpha Prototype.

As of December 31, 2014, the following performance milestone was achieved and subject to our Board of Directors' approval at the upcoming board meeting:

· Successful completion of the Model X Beta Prototype;

As of December 31, 2014 the following three performance milestones were considered probable of achievement:

· Completion of the first Model X Production Vehicle;
· Successful completion of the Model 3 Alpha Prototype; and
· Aggregate vehicle production of 100,000 vehicles.

As the above three performance milestones were considered probable of achievement, we recorded stock-based compensation expense of $25.0 million, $14.5 million and $1.3 million for the years ended December 31, 2014, 2013 and 2012, respectively.

Additionally, no cash compensation has ever been received by our CEO for his services to the Company.

Income Taxes

We record our provision for income taxes in our consolidated statements of operations by estimating our taxes in each of the jurisdictions in which we operate. We estimate our actual current tax exposure together with assessing temporary differences arising from differing treatment of items recognized for financial reporting versus tax return purposes. In general, deferred tax assets represent future tax benefits to be received when certain expenses previously recognized in our consolidated statements of operations become deductible expenses under applicable income tax laws, or loss or credit carryforwards are utilized. Valuation allowances are recorded when necessary to reduce deferred tax assets to the amount expected to be realized.

Significant management judgment is required in determining our provision for income taxes, our deferred tax assets and liabilities and any valuation allowance recorded against our net deferred tax assets. We make these estimates and judgments about our future taxable income that are based on assumptions that are consistent with our future plans. As

of December 31, 2014, we had recorded a full valuation allowance on our net U.S. deferred tax assets because we expect that it is more likely than not that our U.S. deferred tax assets will not be realized in the foreseeable future. Should the actual amounts differ from our estimates, the amount of our valuation allowance could be materially impacted.

Furthermore, significant judgment is required in evaluating our tax positions. In the ordinary course of business, there are many transactions and calculations for which the ultimate tax settlement is uncertain. As a result, we recognize the effect of this uncertainty on our tax attributes based on our estimates of the eventual outcome. These effects are recognized when, despite our belief that our tax return positions are supportable, we believe that it is more likely than not that those positions may not be fully sustained upon review by tax authorities. We are required to file income tax returns in the United States and various foreign jurisdictions, which requires us to interpret the applicable tax laws and regulations in effect in such jurisdictions. Such returns are subject to audit by the various federal, state and foreign taxing authorities, who may disagree with respect to our tax positions. We believe that our accounting consideration is adequate for all open audit years based on our assessment of many factors, including past experience and interpretations of tax law. We review and update our estimates in light of changing facts and circumstances, such as the closing of a tax audit, the lapse of a statute of limitations or a material change in estimate. To the extent that the final tax outcome of these matters differs from our expectations, such differences may impact income tax expense in the period in which such determination is made. The eventual impact on our income tax expense depends in part if we still have a valuation allowance recorded against our deferred tax assets in the period that such determination is made.

Results of Operations

Revenues

Automotive Sales

Automotive sales, which include vehicle, options and related sales, and powertrain component and related sales, consisted of the following for the periods presented (in thousands):

	Year Ended December 31,		
	2014	2013	2012
Vehicle, options and related sales	$3,079,415	$1,952,684	$354,344
Powertrain component and related sales	113,308	45,102	31,355
Total automotive sales	$3,192,723	$1,997,786	$385,699

Vehicle, options and related sales primarily represent revenues related to deliveries of Model S, including vehicle options, accessories and destination charges, vehicle service and sales of regulatory credits to other automotive manufacturers. Powertrain component and related sales represent the sales of electric vehicle powertrain components and systems, such as battery packs and drive units, to other manufacturers.

Vehicle, options and related sales during the years ended December 31, 2014, 2013, and 2012 were $3.08 billion, $1.95 billion, and $354 million. The significant increases in vehicle, options and related sales was primarily driven by the ramp in Model S deliveries, including the commencement of deliveries to Europe in August 2013 and China in April 2014. Deliveries of Model S vehicles were 31,655 in 2014, 22,477 in 2013, and 2,636 in 2012 following the commencement of our Model S deliveries in June 2012. The increase also resulted from higher sales of regulatory credits year-over-year. During the years ended December 31, 2014, 2013, and 2012 regulatory credit sales were $216.3 million, $194.4 million, and $40.5 million.

In April 2013, we launched our resale value guarantee program. During the year ending December 31, 2014, we delivered 5,224 cars and recognized $128.2 million revenue under this program. During 2013 we delivered 5,179 under this program and recognized $29.1 million of revenue. As of December 31, 2014, we recorded $373.5 million in deferred revenues and $487.9 million in resale value guarantee related to Model S deliveries with the resale value guarantee. As of December 31, 2013, we recorded $230.9 million in deferred revenues and $236.3 million in resale value guarantee related to Model S deliveries with the resale value guarantee

Powertrain component and related sales for the periods presented were related to powertrain component sales to Daimler under the Mercedes-Benz B-Class Electric Drive program which commenced in April 2014 and to Toyota under the RAV4 EV program. Powertrain component and related sales for the years ended December 31, 2014, 2013 and 2012 were $113.3 million, $45.1 million and $31.4 million. During the third quarter of 2014, we completed the RAV4 EV program.

Development Services

Development services represent arrangements where we develop electric vehicle powertrain components and systems for other automotive manufacturers, including the design and development of battery packs, drive units and chargers to meet customers' specifications. We provided development services to Daimler and Toyota to assist in the development of electric powertrains for the Mercedes Benz B-Class EV and the Toyota RAV4. During the years ended December 31, 2014, 2013 and 2012, we recognized revenue under these arrangement in the amounts of $5.6 million, $15.7 million, $27.6 million. We do not expect any significant development services in future periods.

Beginning in the first quarter of 2015, we will change the caption of this to be Services and Other Revenue. This will include other revenues related to powertrain component sales to Daimler and other OEMs, vehicle service and sales from used Model S cars.

Cost of Revenues and Gross Profit

Cost of revenues includes cost of automotive sales and costs related to our development services.

Cost of automotive sales for the year ended December 31, 2014, 2013, and 2012 were $2.31 billion, $1.54 billion, and $371.7 million. Cost of automotive sales includes direct parts, material and labor costs, manufacturing overhead, including amortized tooling costs, royalty fees, shipping and logistic costs and reserves for estimated warranty expenses. Cost of automotive sales also includes adjustments to warranty expense, charges to write down the carrying value of our inventory when it exceeds its estimated net realizable value and to provide for obsolete and on-hand inventory in excess of forecasted demand and charges related to write down of fixed assets no longer in use for the production of Model S or our powertrain component sales. The increase in cost of automotive sales was driven primarily by the ramp in Model S deliveries.

In the years ended December 31, 2014 and 2013 we recognized $66.1 million and $19.4 million, respectively, in cost of automotive sales related to vehicle depreciation for cars accounted for as operating leases. For cars accounted for as leases our warranty reserves do not include projected warranty costs as such actual warranty costs are expensed as incurred. For the years ended December 31, 2014 and 2013, warranty costs incurred for our lease vehicles were $7.0 million and $1.6 million.

Gross profit for the years ended December 31, 2014, 2013, and 2012 were $881.7 million, $456.3 million and $30.1 million Gross margin for the years ended December 31, 2014, 2013, and 2012 were 27.6%, 22.7%, and 7.3%. The increase in gross profit from 2013 to 2014 was primarily due to manufacturing and supply chain efficiencies as well as component cost reductions and higher regulatory credit sales, partially offset by one-time manufacturing inefficiencies associated with transitioning to our new final assembly line and launch of All-Wheel Drive Dual Motor Model S. The increase in gross profit from 2012 to 2013 was primarily due to higher vehicle production volumes, cost reduction efforts including process efficiencies in manufacturing and supply chain, design improvements, as well as reduction of waste in the supply chain.

Research and Development Expenses

Research and development (R&D) expenses consist primarily of personnel costs for our teams in engineering and research, supply chain, quality, manufacturing engineering and manufacturing test organizations, prototyping expense, contract and professional services and amortized equipment expense. Overhead costs related to the Tesla Factory prior to the start of production of Model S are also included in R&D expenses. Also included in R&D expenses are development services costs that we incur, if any, prior to the finalization of agreements with our development services customers as reaching a final agreement and revenue recognition is not assured. Development services costs incurred

after the finalization of an agreement are recorded in cost of revenues.

R&D expenses for the year ended December 31, 2014 were $464.7 million, an increase from $232.0 million for the year ended December 31, 2013. The increase in R&D expenses consisted primarily of an $85.3 million increase in employee compensation expenses, a $60.7 million increase in expensed materials primarily to support our Model X, dual motor powertrain and right-hand drive Model S development, a $50.9 million increase in costs related to Model X, dual motor powertrain and right-hand drive Model S engineering, design and testing activities, a $28.1 million increase in stock-based compensation expense related to increased headcount and increasing values of awards granted, a $4.1 million increase in office, information technology and facilities-related costs and a $3.3 million increase in shipping charges for Model X, dual motor powertrain and right-hand drive Model S development.

R&D expenses for the year ended December 31, 2013 were $232.0 million, a decrease from $274.0 million for the year ended December 31, 2012. R&D expenses decreased due to significant development, prototyping and testing expenses related to the Model S launch in 2012, partially offset by an increase in similar costs in 2013 for Model X and right-hand drive Model S and other programs. The $42.0 million decrease in R&D expenses during the year ended December 31, 2013 consisted primarily of an $18.2 million decrease in expensed materials, an $8.5 million decrease in employee compensation expenses, a $7.8 million decrease in costs related to Model S engineering, design and testing activities, a $6.6 million decrease in shipping charges for Model S prototype materials and a $4.9 million decrease in office, information technology and facilities-related costs. The decrease was partially offset by a $5.0 million increase in stock-based compensation expense related to a larger number of outstanding equity awards due to additional headcount and generally an increasing common stock valuation applied to new grants.

Selling, General and Administrative Expenses

Selling, general and administrative (SG&A) expenses consist primarily of personnel and facilities costs related to our Tesla stores, marketing, sales, executive, finance, human resources, information technology and legal organizations, as well as litigation settlements and fees for professional and contract services.

SG&A expenses for the year ended December 31, 2014 were $603.7 million, an increase from $285.6 million for the year ended December 31, 2013. SG&A expenses increased primarily from higher headcount and costs to support an expanded retail, service and Supercharger footprint as well as the general growth of the business. The $318.1 million increase in our SG&A expenses consisted primarily of a $141.1 million increase in employee compensation expenses related to higher sales and marketing headcount to support sales activities worldwide and higher general and administrative headcount to support the expansion of the business, a $135.9 million increase in office, information technology and facilities-related costs to support the growth of our business as well as sales and marketing activities to handle our expanding market presence, a $35.8 million increase in stock-based compensation expense related to additional headcount and increasing value of awards granted and a $27.2 million increase in professional and outside services costs.

SG&A expenses for the year ended December 31, 2013 were $285.6 million, an increase from $150.4 million for the year ended December 31, 2012. SG&A expenses increased primarily from higher headcount and costs to support an expanded retail, service and Supercharger footprint as well as the general growth of the business. The $135.2 million increase in our SG&A expenses during the year ended December 31, 2013 consisted primarily of a $62.8 million increase in employee compensation expenses related to higher sales and marketing headcount to support sales activities worldwide and higher general and administrative headcount to support the expansion of the business, a $36.8 million increase in office, information technology and facilities-related costs to support the growth of our business as well as sales and marketing activities to handle our expanding market presence, a $17.8 million increase in stock-based compensation expense related to additional headcount and increasing value of awards granted and a $17.2 million increase in professional and outside services costs.

Interest Expense

Interest expense for the years ended December 31, 2014, 2013, and 2012 was $100.9 million, $32.9 million and $0.3 million. The increase in interest expense from 2013 to 2014 was due to the issuance of $920.0 million aggregate principal amount of 2019 Notes and $1.38 billion aggregate principal amount of 2021 Notes during the first half of 2014. The increase in interest expense from 2012 to 2013 was due to $17.8 million of interest expense incurred upon repayment of the Department of Energy (DOE) loan in May 2013 for early repayment fees, accrued interest and the amortization of the remaining loan origination costs as well as interest associated with the $660.0 million aggregate principal amount of 2018 Notes issued in May 2013.

Other Income (Expense), Net

Other income (expense), net, consists primarily of the change in the fair value of our DOE common stock warrant liability and foreign exchange gains and losses related to our foreign currency-denominated assets and liabilities. We expect our foreign exchange gains and losses will vary depending upon movements in the underlying exchange rates. Prior to the expiration of the DOE warrant in May 2013, the DOE warrant had been carried at its estimated fair value with changes in its fair value reflected in other income (expense), net.

Other income (expense), net, for the years ended December 31, 2014, 2013 and 2012 was $1.8 million, $22.6 million and ($1.8) million. The other income, net of $22.6 million in 2013 was primarily due to the reduction in fair value of our DOE common stock warrant liability of $10.7 million during the year. In March 2013, we entered into a fourth

amendment to the DOE Loan Facility which, among other things, accelerated the maturity date of our DOE loans to December 15, 2017; therefore, the DOE warrant was no longer expected to vest. The other income, net, also includes the favorable foreign currency exchange impact from our foreign currency-denominated liabilities during the year ended December 31, 2013, especially related to the Japanese yen.

Provision for Income Taxes

Our provision for income taxes for the years ended December 31, 2014, 2013, and 2012 was $9.4 million, $2.6 million, and $0.1 million. The increases in the provision for income taxes were due primarily to the increase in taxable income in our international jurisdictions, following the commencement of European Model S deliveries in August 2013 and Model S deliveries in Asia in April 2014.

Liquidity and Capital Resources

As of December 31, 2014, we had $1.91 billion in principal sources of liquidity available from our cash and cash equivalents including $1.27 billion of money market funds. Amounts held in foreign currencies had a US dollar equivalent of $315 million as of December 31, 2014, and consisted primarily of Chinese yuan, Japanese yen, euro and Norwegian krone.

Sources of cash are predominately from our deliveries of Model S, as well as customer deposits for Model S and Model X, sales of regulatory credits, cash from the provision of development services, and sales of powertrain components and systems. We expect that our current sources of liquidity, including cash and cash equivalents, together with our current projections of cash flow from operating activities, will provide us with adequate liquidity over the next 12 months based on our current plans. These cash flows enable us to fund our ongoing operations, research and development projects for our planned Model X, Model 3, and certain other future products; purchase tooling and manufacturing equipment required to introduce Model X and to continue to ramp up production of Model S; construct our Gigafactory; and establish and expand our stores, service centers and Supercharger network. We currently anticipate making aggregate capital expenditures of about $1.5 billion over the next 12 months.

When market conditions are favorable, we may evaluate alternatives to pursue liquidity options to fund capital intensive initiatives. Should prevailing economic, financial, business or other factors adversely affect our ability to meet our operating cash requirements, we could be required to obtain funding though traditional or alternative sources of financing. We cannot be certain that additional funds would be available to us on favorable terms when required, or at all.

Summary of Cash Flows

	Year Ended December 31,		
	2014	2013	2012
Net cash provided by (used in) operating activities	$(57,337)	$264,804	$(263,815)
Net cash used in investing activities	(990,444)	(249,417)	(206,930)
Net cash provided by financing activities	2,143,130	635,422	419,635

Cash Flows from Operating Activities

Our cash flows from operating activities are significantly affected by our cash investments to support the growth of our business in areas such as manufacturing, research and development and selling, general and administrative. Our operating cash flows are also affected by our working capital needs to support growth and fluctuations in inventory, personnel related expenditures, accounts payable and other current assets and liabilities.

Our operating cash inflows include cash from sales of our Model S, customer deposits for Model S and Model X, sales of regulatory credits, cash from the provision of development services, and sales of powertrain components and systems. These cash inflows are offset by payments we make to our suppliers for production materials and parts used in our manufacturing process, employee compensation, operating leases and interest expense on our financings.

Cash provided by (used in) operating activities was ($57.3) million, $264.8 million and ($263.8) million in 2014, 2013 and 2012. The decrease in operating cash flows in 2014 as compared to 2013 was due to an increase in finished goods inventory primarily due to cars whose delivery slipped from Q4 of 2014 to the following year, an increase in raw

material inventory balances at year end necessary to meet our planned production requirements for Model S in Q1 of the following year, higher operating expenses in R&D and SG&A, and use of cash for vehicles directly leased by us, partially offset by increased cash receipts from customer payments on vehicle sales, including an increase in customer deposits.

The increase in operating cash flows in 2013 as compared to 2012 was due to an increase in cash receipts from customer payments on vehicles deliveries, including for cars sold under our Resale Value Guarantee program, increased regulatory credits sold and increased customer deposits from orders for Model S and X. This was partially offset by an increase in inventory balances at year-end necessary to meet our planned production requirements for Model S in Q1 of the following year.

Customer Deposits

We collect deposits from customers at the time they place an order for a vehicle and, in some locations, at certain additional milestones up to the point of delivery. Customer deposit amounts and timing vary depending on the vehicle model and country of delivery. Customer deposits related to Model X still represent fully refundable reservations. Amounts are included in current liabilities until refunded or until they are applied to a customer’s purchase balance at time of delivery. As of December 31, 2014, we held $257.6 million in customer deposits.

Cash Flows from Investing Activities

Cash flows from investing activities primarily relate to capital expenditures to support our growth in operations, including investments in Model S manufacturing equipment and tooling and our stores, service centers and Supercharger network infrastructure. Cash used in investing activities was $990.4 million, $249.4 million and $206.9 million in 2014, 2013 and 2012. Cash flows from investing activities and variability between each year related primarily to capital expenditures, which were $969.9 million, $264.2 million, and $239.2 million in 2014, 2013, and 2012. Expenditures in all years consisted primarily of purchases of capital equipment, tooling, and facilities to support our Model S and Model X manufacturing.

In 2014, we began construction of our Gigafactory facility in Nevada. Tesla's contribution to total capital expenditures are expected to be about $2.0 billion over the next 5 years. In 2014, we used cash of $62.2 million towards the construction of the first stage of this project and expect to spend up to $300 million over the next 12 months.

Cash Flows from Financing Activities

Net cash provided by financing activities was $2.14 billion, $635.4 million, and $419.6 million in 2014, 2013 and 2012, respectively. The increase in cash provided from financing in 2014 and compared to 2013 was primarily due to $2.1 billion net proceeds from the issuance of our 2019 and 2021 Notes, including the associated hedge and warrant transactions, representing a $1.5 billion increase in debt financing as compared to 2013. Cash flows from financing in 2013 that did not recur in 2014 included proceeds of $415.0 million from the issuance of common stock in public and private offerings and $452.3 million used to repay our DOE loans.

The increase in cash provided from financing in 2013 and compared to 2012 was primarily due to $585.9 million net proceeds from the issuance of our 2018 Notes, including the associated hedge and warrant transactions, and a $193.5 million increase in proceeds from public and private equity issuances. In 2013 we used $452.3 million to repay our DOA loans as compared to proceeds of $188.8 million received during 2012 under these loans.

0.25% and 1.25% Convertible Senior Notes and Bond Hedge and Warrant Transactions

In 2014, we issued $920.0 million principal amount of 0.25% convertible senior notes due 2019 (2019 Notes) and $1.38 billion principal amount of 1.25% convertible senior notes due 2021 (2021 Notes) in a public offering. The total net proceeds from these offerings, after deducting transaction costs, were approximately 905.8 million from 2019 Notes and $1.36 billion from 2021 Notes, respectively. The interest rates are fixed at 0.25% and 1.25% per annum for the 2019 and 2021 Notes, respectively, and are payable semi-annually in arrears on March 1 and September 1 of each year, commencing on September 1, 2014.

In connection with the offering of these notes in 2014, we purchased a convertible note hedges for $603.4 million and sold warrants $389.2 million. Taken together, the purchase of the convertible note hedges and the sale of warrants are intended to offset any actual dilution from the conversion of the 2019 Notes and 2021 Notes.

During the fourth quarter of 2014, the closing price of our common stock did not meet or exceed 130% of the applicable conversion price of our 2019 Notes and 2021 Notes on at least 20 of the last 30 consecutive trading days of the quarter; furthermore, no other conditions allowing holders of these notes to convert have been met as of December 31, 2014. Therefore, the 2019 Notes and 2021 Notes are not convertible during the first quarter of 2015 and are classified as long-term debt. Should the closing price conditions be met in the first quarter of 2015 or a future quarter, the Notes will be convertible at their holders' option during the immediately following quarter.

1.50% Convertible Senior Notes and Bond Hedge and Warrant Transactions

In May 2013, we issued $660.0 million aggregate principal amount of 1.50% convertible senior notes due 2018 (the Notes) in a public offering. The net proceeds from the offering, after deducting transaction costs, were approximately $648.0 million. The interest under the Notes is fixed at 1.50% per annum and is payable semi-annually in arrears on June 1 and December 1 of each year, commencing on December 1, 2013.

In connection with the offering of the 2018 Notes, we purchased a convertible note hedge for $177.5 million and sold warrants for $120.3 million. Taken together, the purchase of the convertible note hedges and the sale of warrants are intended to offset any actual dilution from the conversion of the 2018 Notes.

During the fourth quarter of 2014, the closing price of our common stock exceeded 130% of the applicable conversion price of our 2018 Notes on at least 20 of the last 30 consecutive trading days of the quarter; therefore, holders of 2018 Notes may convert their notes during the first quarter of 2015. Upon conversion of 2018 Notes, we will be obligated to pay cash for the principal amount of the converted notes and we may also have to deliver shares of our common stock in respect of such converted notes. Any conversion of the notes prior to their maturity or acceleration of the repayment of the notes could have a material adverse effect on our cash flows, business, results of operations and financial condition. Should the closing price conditions be met in the first quarter of 2015 or a future quarter, 2018 Notes will be convertible at their holders' option during the immediately following quarter. Under current market conditions, we do not expect the 2018 Notes will be converted in the short term.

For more information on the 2018 Notes, 2019 Notes, and 2021 Notes see Item 8. of Part II, Financial Statements and Supplementary Data, Note 6 - Convertible Notes and Long-Term Debt Obligation to our Consolidated Financial Statements included in this Annual Report on Form 10-K.

Common Stock Offering and Concurrent Private Placement

Concurrent with the execution of the Notes and related transactions in May 2013, we also completed a public offering of common stock and sold a total of 3,902,862 shares of our common stock for total cash proceeds of approximately $355.1 million (which includes 487,857 shares or $45.0 million sold to our Chief Executive Officer (CEO)), net of underwriting discounts and offering costs. We also sold 596,272 shares of our common stock to our CEO and received total cash proceeds of $55.0 million in a private placement at the public offering price.

Contractual Obligations

We are party to contractual obligations involving commitments to make payments to third parties, including certain debt financing arrangements and leases, primarily for stores, service centers, certain manufacturing and corporate offices. These also include, as part of our normal business practices, contracts with suppliers for purchases of certain raw materials, components, and services to facilitate adequate supply of these materials and services and capacity reservation contracts. We have the following contractual obligations, including firm purchase obligations. A purchase obligation is defined as an agreement to purchase goods or services that is enforceable and legally binding on us and that specifies all significant terms. For obligations with cancellation provisions, the amounts included in the table below were limited to the non-cancelable portion of the agreement terms. The expected timing of payments of the obligations in the preceding table is estimated based on current information. Timing of payments and actual amounts paid may be different, depending on the time of receipt of goods or services, or changes to agreed-upon amounts for some obligations. Open purchase orders are generally cancellable in full or in part at our discretion and are therefore not considered firm purchase obligations.

The following table sets forth, as of December 31, 2014 certain significant obligations that will affect our future liquidity (in thousands):

	Year Ended December 31,					
	Total	2015	2016	2017	2018	2019 and thereafter
Operating lease obligations	$406,783	$56,522	$60,136	$56,566	$48,959	$184,600
Capital lease obligations, including interest	22,420	10,153	8,112	3,592	563	
Purchase obligations [(1)(2)]	562,976	529,551	20,055	13,370	—	—

2018 Notes, including interest [3]	694,400	694,400	—	—	—	—
2019 Notes, including interest	930,350	2,300	2,300	2,300	2,300	921,150
2021 Notes, including interest	1,492,125	17,250	17,250	17,250	17,250	1,423,125
Total	$4,109,054	$1,310,176	$107,853	$93,078	$69,072	$2,528,875

(1) Amounts do not include future cash payments for purchase obligations which were recorded in Accounts payable or Accrued liabilities at December 31, 2014.

(2) These totals represent aggregate purchase commitments with all vendors. Some of the commitments included are our agreements with Panasonic Corporation, to the extent quantities and timing of such purchases are fixed. Should we terminate the Panasonic contracts prior to purchasing certain minimum quantities, we would owe an additional $81 million under the terms of the agreement as of December 31, 2014.

(3) During the fourth quarter of 2014, the closing price of our common stock exceeded 130% of the applicable conversion price of our 2018 Notes on at least 20 of the last 30 consecutive trading days of the quarter; therefore, holders of 2018 Notes may convert their notes during the first quarter of 2015. As such, we classified the $601.6 million carrying value of our 2018 Notes as current liabilities on our condensed consolidated balance sheet as of December 31, 2014 and have included related contractual payments in the 2015 category in the table above.

In connection with our Tesla Factory located in Fremont, California, we are obligated to pay for the remediation of certain environmental conditions existing at the time we purchased the property from New United Motor Manufacturing, Inc. (NUMMI). As of December 31, 2014 and 2013, we accrued a total of $4.0 million and $5.5 million, respectively, related to these environmental liabilities. NUMMI is responsible for remediation costs between $15 million and $30 million for up to 10 years from the closing date.

Off-Balance Sheet Arrangements

During the periods presented, we did not have relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Foreign Currency Risk

Our revenues and costs denominated in foreign currencies are not completely matched. We commenced deliveries of Model S in June 2012 to customers in North America and to European customers in August 2013. We recently introduced Model S to China, Hong Kong, Japan, and Australia. Through December 31, 2014, a majority of our revenues have been denominated in U.S. dollars. However, we have materially greater revenues than expenses denominated in the Chinese yuan and Norwegian krona, and materially greater expenses than revenues denominated in the Japanese yen. December 31, 2014. Accordingly, if the value of the U.S. dollar depreciates significantly against currencies where we have a net short exposure, our costs as measured in U.S. dollars as a percent of our revenues will correspondingly increase which may adversely impact our operating results. Conversely, as the value of the U.S. dollar appreciates significantly against currencies where revenues exceed expenses, our revenues as measured in U.S. dollars may be reduced.

As a result of a favorable foreign currency exchange impact from foreign currency-denominated liabilities, especially related to the Japanese yen, we recorded gains of $2.0 million on foreign exchange transactions in other income (expense), net, for the year ended December 31, 2014.

Interest Rate Risk

We had cash and cash equivalents totaling $1.91 billion as of December 31, 2014. A significant portion of our cash and cash equivalents were invested in money market funds. Cash and cash equivalents are held for working capital purposes. We do not enter into investments for trading or speculative purposes. We believe that we do not have any material exposure to changes in the fair value as a result of changes in interest rates due to the short term nature of our cash equivalents.

As of December 31, 2014, we had $2.96 billion aggregate principal amount of convertible senior notes outstanding and capital lease obligations of $21.8 million, all of which are fixed rate instruments. Therefore, our results of operations are not subject to fluctuations in interest rates.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Index to Consolidated Financial Statements

	Page
Report of Independent Registered Public Accounting Firm	61
Consolidated Balance Sheets	62
Consolidated Statements of Operations	63
Consolidated Statements of Comprehensive Loss	64
Consolidated Statements of Stockholders' Equity	65
Consolidated Statements of Cash Flows	66
Notes to Consolidated Financial Statements	67

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of Tesla Motors, Inc.

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, of comprehensive loss, of stockholders' equity and of cash flows present fairly, in all material respects, the financial position of Tesla Motors, Inc. and its subsidiaries at December 31, 2014 and 2013, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2014 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2014, based on criteria established in Internal Control - Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in Management's Report on Internal Control over Financial Reporting appearing under Item 9A. Our responsibility is to express opinions on these financial statements and on the Company's internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ PricewaterhouseCoopers LLP

San Jose, California

February 26, 2015

Tesla Motors, Inc.

Consolidated Balance Sheets

(in thousands, except share and per share data)

	December 31, 2014	December 31, 2013
Assets		
Current assets		
Cash and cash equivalents	$1,905,713	$845,889
Restricted cash and marketable securities	17,947	3,012
Accounts receivable	226,604	49,109
Inventory	953,675	340,355
Prepaid expenses and other current assets	94,718	27,574
Total current assets	3,198,657	1,265,939
Operating lease vehicles, net	766,744	382,425
Property, plant and equipment, net	1,829,267	738,494
Restricted cash	11,374	6,435
Other assets	43,209	23,637
Total assets	$5,849,251	$2,416,930
Liabilities and Stockholders' Equity		
Current liabilities		
Accounts payable	$777,946	$303,969
Accrued liabilities	268,884	108,252
Deferred revenue	191,651	91,882
Capital lease obligations, current portion	9,532	7,722
Customer deposits	257,587	163,153
Convertible senior notes	601,566	182
Total current liabilities	2,107,166	675,160
Capital lease obligations, less current portion	12,267	12,855
Deferred revenue, less current portion	292,271	181,180
Convertible senior notes, less current portion	1,806,518	586,119
Resale value guarantee	487,879	236,299
Other long-term liabilities	173,244	58,197
Total liabilities	4,879,345	1,749,810
Commitments and contingencies (Note 11)		
Convertible senior notes (Notes 6)	58,196	—
Stockholders' equity:		
Preferred stock; $0.001 par value; 100,000,000 shares authorized; no shares issued and outstanding	—	—
Common stock; $0.001 par value; 2,000,000,000 shares authorized as of	126	123

December 31, 2014 and 2013, respectively; 125,687,607 and 123,090,990 shares issued and outstanding as of December 31, 2014 and 2013, respectively		
Additional paid-in capital	2,345,266	1,806,617
Accumulated deficit	(1,433,682)	(1,139,620)
Total stockholders' equity	911,710	667,120
Total liabilities and stockholders' equity	$5,849,251	$2,416,930

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

Tesla Motors, Inc.

Consolidated Statements of Operations

(in thousands, except share and per share data)

	Year Ended December 31,		
	2014	2013	2012
Revenues			
Automotive sales	$3,192,723	$1,997,786	$385,699
Development services	5,633	15,710	27,557
Total revenues	3,198,356	2,013,496	413,256
Cost of revenues			
Automotive sales	2,310,011	1,543,878	371,658
Development services	6,674	13,356	11,531
Total cost of revenues	2,316,685	1,557,234	383,189
Gross profit	881,671	456,262	30,067
Operating expenses			
Research and development	464,700	231,976	273,978
Selling, general and administrative	603,660	285,569	150,372
Total operating expenses	1,068,360	517,545	424,350
Loss from operations	(186,689)	(61,283)	(394,283)
Interest income	1,126	189	288
Interest expense	(100,886)	(32,934)	(254)
Other income (expense), net	1,813	22,602	(1,828)
Loss before income taxes	(284,636)	(71,426)	(396,077)
Provision for income taxes	9,404	2,588	136
Net loss	$(294,040)	$(74,014)	$(396,213)
Net loss per share of common stock, basic and diluted	$(2.36)	$(0.62)	$(3.69)
Weighted average shares used in computing net loss per share of common stock, basic and diluted	124,539,343	119,421,414	107,349,188

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

Tesla Motors, Inc.

Consolidated Statements of Comprehensive Loss

(in thousands)

	Year Ended December 31,		
	2014	2013	2012
Net loss	$(294,040)	$(74,014)	$(396,213)
Other comprehensive income (loss), net of tax:			
Unrealized net loss on short-term marketable securities	(22)	—	—
Reclassification adjustment for gain included in net loss	—	—	3
Other comprehensive income (loss)	(22)	—	3
Comprehensive loss	$(294,062)	$(74,014)	$(396,210)

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

Tesla Motors, Inc.

Consolidated Statements of Stockholders' Equity

(in thousands, except share and per share data)

	Common Stock		Additional Paid-In	Accumulated	Accumulated Other Comprehensive	Total Stockholders'
	Shares	Amount	Capital	Deficit	Loss	Equity
Balance as of December 31, 2011	104,530,305	$ 104	$893,337	$(669,393)	$ (3)	$ 224,045
Issuance of common stock in October 2012 public offering at $28.25 per share, net of issuance costs of $584	7,964,601	8	221,483	—	—	221,491
Issuance of common stock upon exercise of stock options, net of repurchases	1,345,842	2	16,498	—	—	16,500
Issuance of common stock under employee stock purchase plan	373,526	1	8,388	—	—	8,389
Stock-based compensation	—	—	50,485	—	—	50,485
Comprehensive loss:						
Net loss	—	—	—	(396,213)	—	(396,213)
Unrealized loss on short-term marketable securities, net	—	—	—	—	3	3
Total comprehensive loss	—	—	—	—	—	(396,210)
Balance as of December 31, 2012	114,214,274	115	1,190,191	(1,065,606)	—	124,700
Issuance of common stock in May 2013 public offering at $92.20 per share, net of issuance costs of $6,367	3,902,862	3	353,629	—	—	353,632
Issuance of common stock in May 2013 concurrent private placements at $92.20 per share	596,272	1	55,000	—	—	55,001
Conversion feature of convertible senior notes due 2018	—	—	82,842	—	—	82,842
Purchase of bond hedges	—	—	(177,540)	—	—	(177,540)
Sales of warrant	—	—	120,318	—	—	120,318
	3,852,673	3	82,570	—	—	82,573

Issuance of common stock upon exercise of stock options						
Issuance of common stock upon release of restricted stock units, net of shares withheld for employee taxes	6,166	—	(1,116)	—	—	(1,116)
Issuance of common stock under employee stock purchase plan	518,743	1	13,848	—	—	13,849
Stock-based compensation	—	—	86,875	—	—	86,875
Net loss	—	—	—	(74,014)	—	(74,014)
Balance as of December 31, 2013	123,090,990	123	1,806,617	(1,139,620)	—	667,120
Conversion feature of convertible senior notes due 2019 and 2021	—	—	548,603	—	—	548,603
Purchase of bond hedges	—	—	(603,428)	—	—	(603,428)
Sales of warrant	—	—	389,160	—	—	389,160
Reclass from equity to mezzanine equity	—	—	(58,199)	—	—	(58,199)
Issuance of common stock upon exercise of stock options	2,266,698	2	72,053	—	—	72,055
Issuance of common stock upon release of restricted stock units, net of shares withheld for employee taxes	166,319	1	(190)	—	—	(189)
Issuance of common stock under employee stock purchase plan	163,600	—	28,571	—	—	28,571
Stock-based compensation	—	—	162,079	—	—	162,079
Comprehensive loss:						
Net loss				(294,040)		(294,040)
Unrealized gain on short-term marketable securities, net	—	—	—	—	(22)	(22)
Total comprehensive loss						(294,062)
Balance as of December 31, 2014	125,687,607	$ 126	$2,345,266	$(1,433,660)	$ (22)	$ 911,710

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

Tesla Motors, Inc.

Consolidated Statements of Cash Flows

(in thousands)

	Year Ended December 31,		
	2014	2013	2012
Cash Flows From Operating Activities			
Net loss	$(294,040)	$(74,014)	$(396,213)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:			
Depreciation and amortization	231,931	106,083	28,825
Stock-based compensation	156,496	80,737	50,145
Amortization of discount on convertible debt	69,734	9,143	—
Inventory write-downs	15,609	8,918	4,929
Amortization of Department of Energy (DOE) loan origination costs	—	5,558	—
Change in fair value of DOE warrant liability	—	(10,692)	1,854
Fixed asset disposal	14,178	1,796	154
Other non-cash operating activities	7,471	1,815	1,406
Foreign currency transaction (gain) loss	(1,891)	(13,498)	143
Changes in operating assets and liabilities			
Accounts receivable	(183,658)	(21,705)	(17,303)
Inventories and operating lease vehicles	(1,050,264)	(460,561)	(194,726)
Prepaid expenses and other current assets	(60,637)	(17,533)	1,121
Other assets	(4,493)	(434)	(482)
Accounts payable	252,781	20,995	189,944
Accrued liabilities	162,075	66,418	9,603
Deferred revenue	209,681	268,098	(526)
Customer deposits	106,230	24,354	47,056
Resale value guarantee	249,492	236,299	—
Other long-term liabilities	61,968	33,027	10,255
Net cash provided by (used in) operating activities	(57,337)	264,804	(263,815)
Cash Flows From Investing Activities			
Purchases of property and equipment excluding capital leases	(969,885)	(264,224)	(239,228)
Withdrawals out of our dedicated DOE account, net	—	14,752	8,620
(Increase) decrease in other restricted cash	(3,849)	55	(1,330)
Purchases of short-term marketable securities	(205,841)	—	(14,992)
Maturities of short-term marketable securities	189,131	—	40,000
Net cash used in investing activities	(990,444)	(249,417)	(206,930)
Cash Flows From Financing Activities			
Proceeds from issuance of convertible debt	2,300,000	660,000	—
Proceeds from issuance of common stock in public offering	—	360,000	221,496
Proceeds from issuance of warrants	389,160	120,318	—

Proceeds from exercise of stock options and other stock issuances	100,455	95,307	24,885
Proceeds from issuance of common stock in private placement	—	55,000	—
Principal payments on DOE loans	—	(452,337)	(12,710)
Purchase of convertible note hedges	(603,428)	(177,540)	—
Common stock and convertible debt issuance costs	(35,149)	(16,901)	—
Principal payments on capital leases and other debt	(11,179)	(8,425)	(2,832)
Collateralized lease borrowing	3,271	—	—
Proceeds from DOE loans	—	—	188,796
Net cash provided by financing activities	2,143,130	635,422	419,635
Effect of exchange rate changes on cash and cash equivalents	(35,525)	(6,810)	(2,266)
Net increase (decrease) in cash and cash equivalents	1,059,824	643,999	(53,376)
Cash and cash equivalents at beginning of period	845,889	201,890	255,266
Cash and cash equivalents at end of period	$1,905,713	$845,889	$201,890
Supplemental Disclosures			
Interest paid	$20,539	$9,041	$6,938
Income taxes paid	3,120	257	117
Supplemental noncash investing activities			
Acquisition of property and equipment included in accounts payable and accrued liabilities	254,393	38,789	44,890
Estimated fair market value of facilities under build-to-suit lease	50,076	—	—

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

Tesla Motors, Inc.

Notes to Consolidated Financial Statements

1. Overview of the Company

Tesla Motors, Inc. (Tesla, we, us or our) was incorporated in the state of Delaware on July 1, 2003. We design, develop, manufacture and sell high-performance fully electric vehicles and advanced electric vehicle powertrain components. We have wholly-owned subsidiaries in North America, Europe and Asia. The primary purpose of these subsidiaries is to market, manufacture, sell and/or service our vehicles.

2. Summary of Significant Accounting Policies

Basis of Consolidation

The consolidated financial statements include the accounts of Tesla and its wholly owned subsidiaries. All significant inter-company transactions and balances have been eliminated in consolidation.

During the year ended December 31, 2014, we began separately presenting the effect of exchange rate changes on our cash and cash equivalents in our consolidated statements of cash flows due to our growing operations in foreign currency environments. Prior period amounts have been reclassified to conform to the current period presentation.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent liabilities at the date of the financial statements, and reported amounts of expenses during the reporting period, including revenue recognition, residual value of operating lease vehicles, inventory valuation, warranties, fair value of financial instruments, valuation allowances for deferred tax assets, uncertain tax positions, and stock-based compensation. Given the inherent uncertainty of these estimates, actual results could differ from those estimates.

Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board issued an accounting update which amends the existing accounting standards for revenue recognition. The new guidance provides a unified model to determine when and how revenue is recognized. Under the new model, revenue is recognized as goods or services are delivered in an amount that reflects the consideration we expect to collect. The guidance is effective for fiscal years beginning after December 15, 2016; early adoption is prohibited. The new standard is required to be applied retrospectively to each prior reporting period presented or retrospectively with the cumulative effect of initially applying it recognized at the date of initial application. We have not yet selected a transition method and are currently evaluating the impact of

adopting this guidance on our consolidated financial statements.

Revenue Recognition

We recognize revenues from sales of Model S and the Tesla Roadster, including vehicle options and accessories, vehicle service and sales of regulatory credits, such as zero emission vehicle (ZEV),greenhouse gas emission (GHG) credits, and CAFE credits, as well as sales of electric vehicle powertrain components and systems, such as battery packs and drive units and sales of services related to the development of these systems. We recognize revenue when: (i) persuasive evidence of an arrangement exists; (ii) delivery has occurred and there are no uncertainties regarding customer acceptance; (iii) fees are fixed or determinable; and (iv) collection is reasonably assured.

For multiple deliverable revenue arrangements, we allocate revenue to each element based on a selling price hierarchy. The selling price for a deliverable is based on its vendor specific objective evidence (VSOE) if available, third party evidence (TPE) if VSOE is not available, or estimated selling price if neither VSOE nor TPE is available.

Automotive Sales

We recognize automotive sales revenue from sales of Model S, including vehicle options, accessories and destination charges, vehicle service. We also recognize automotive sales revenue from the sales of electric vehicle powertrain components and systems, such as battery packs and drive units, to other manufacturers. Revenue is recognized when (i) persuasive evidence of an arrangement exists; (ii) delivery has occurred and there are no uncertainties regarding customer acceptance; (iii) fees are fixed or determinable; and (iv) collection is reasonably assured.

Car sales include certain standard features and customer selected options and configurations that meet the definition of a deliverable under multiple-element accounting guidance, including internet connectivity, Supercharging access, and specified software updates for cars equipped with Autopilot hardware. These deliverables are valued on a stand-alone basis and we recognize their related revenue over our performance period which is generally the eight-year life of the car or, for software upgrades, as they are delivered. If we sell a derivable separately, we use that pricing to determine its fair value; otherwise, we use our best estimated selling price by considering third party pricing of similar options, costs used to develop and deliver the service, and other information which may be available.

As of December 31, 2014, we had deferred $25.6 million related to access to our Supercharger network and $14.4 million related to connectivity.

At the time of revenue recognition, we record a reserve against revenue for estimated future product returns. Such estimates are based on historical experience and are immaterial in all periods presented.

Resale Value Guarantee

We offer a resale value guarantee program to customers who purchase a Model S and finance their vehicle through one of our commercial banking partners in the US, Canada and Europe. Under this program, Model S customers have the option of selling their vehicle back to us during the period from 36 to 39 months after delivery for a specified value determined at time of purchase. Because we offer a resale value guarantee, we account for these transactions as operating leases. Accordingly, we recognize revenue attributable to the lease on a straight-line basis over the guarantee period to automotive sales revenue. Similarly, we capitalize the cost of the leased vehicle and depreciate its value, less expected salvage value, to cost of automotive sales over the same period.

At the end of the guarantee period, which is the earlier of 39 months or the pay-off date of the initial loan, the resale value guarantee and deferred revenue balances are settled to automotive sales revenue and the net book value of the leased vehicle is expensed to costs of automotive sales if our customer retains ownership of the car. In cases where a customer returns the vehicle back to us between months 36 and 39, we issue a check to the customer in the amount of the resale value guarantee and settle any remaining deferred revenue balance to automotive sales revenue.

At least annually, we assess the estimated market values of vehicles under our resale value guarantee program. As we accumulate more data related to the resale values of Model S, there may be significant changes to their estimated values.

Beginning in 2014, Tesla began offering resale value guarantees in connection with automobile sales to certain financing institutions. As Tesla has guaranteed the value of these vehicles and as the vehicles are expected to be leased to end-customers, we account for them as collateralized borrowings. At December 31, 2014, we have $19.6 million of such borrowings recorded in resale value guarantee liability of which a portion will be accreted to revenue and a portion may be distributed to the financing institutions should we decide to repurchase the vehicles at the end of the term or should the financing institution sell the car to a third party and receive proceeds less than the value we have guaranteed. The maximum cash payment to re-purchase these vehicles under these arrangements at December 31, 2014, is $11.2 million. Cash received upon the sale of such cars is classified as collateralized lease borrowing within cash flows from financing activities in our Consolidated Statement of Cash Flows.

Account activity related to our resale value guarantee program consisted of the following for the period presented (in thousands):

	Year ended December 31, 2014	Year ended December 31, 2013
Operating lease vehicles under the resale value guarantee program—beginning of period	$376,979	$—
Increase in operating lease vehicles under the resale value guarantee program	380,627	396,361
Depreciation expense recorded in cost of automotive sales	63,105	17,171
Additional depreciation expense recorded in cost of automotive sales as a result of early cancellation of resale value guarantee	9,911	2,211
Operating lease vehicles under the resale value guarantee program—end of period	$684,590	$376,979
Deferred revenue related to the resale value guarantee program—beginning of period	$230,856	$—
Increase in deferred revenue related to Model S deliveries with resale value guarantee	278,397	259,962
Amortization of deferred revenue recorded in automotive sales	118,567	27,654
Additional revenue recorded in automotive sales as a result of early cancellation of resale value guarantee	9,590	1,452
Deferred revenue related to the resale value guarantee program—end of period	$381,096	$230,856
Resale value guarantee liability—beginning of period	$236,298	$—
Increase in resale value guarantee	260,138	237,620
Additional revenue recorded in automotive sales as a result of early cancellation of resale value guarantee	8,557	1,322
Resale value guarantee liability—end of period	$487,879	$236,298

Model S Leasing Program

In April 2014, we began offering a leasing program in the United States and Canada for Model S. Qualifying customers are permitted to lease a Model S for 36 months, after which time they have the option of either returning

the vehicle to us or purchasing it for a pre-determined residual value. We account for these leasing transactions as operating leases and accordingly, we recognize leasing revenues over the contractual term of the individual leases and depreciate the cost of the respective operating lease vehicles less expected salvage value to cost of automotive sales over the same period. As of December 31, 2014, we had deferred $9.4 million of lease-related upfront payments which will be recognized on a straight-line basis over the contractual term of the individual leases. Lease revenues are recorded in automotive sales and for the year ended December 31, 2014, we recognized $4.4 million.

Regulatory Credits Sales

California and certain other states have laws in place requiring vehicle manufacturers to ensure that a portion of the vehicles delivered for sale in that state during each model year are zero emission vehicles. These laws and regulations provide that a manufacturer of zero emission vehicles may earn regulatory credits, and may sell excess credits to other manufacturers who apply such credits to comply with these regulatory requirements. Similar regulations exist at the federal level that require compliance related to GHG emissions and also allow for the sale of excess credits by one manufacturer to other manufacturers. As a manufacturer solely of zero emission vehicles, we have earned emission credits, such as ZEV and GHG credits on vehicles, and we expect to continue to earn these credits in the future. We enter into contractual agreements with third parties to purchase our regulatory credits.

We recognize revenue on the sale of these credits at the time legal title to the credits is transferred to the purchasing party. Revenue from the sale of regulatory credits totaled $216.3 million, $194.4 million, and $40.5 million for the years ended December 31, 2014, 2013 and 2012, respectively.

Maintenance and Service Plans

We offer a prepaid maintenance program for Model S, which includes plans covering maintenance for up to eight years or up to 100,000 miles, provided these services are purchased within a specified period of time. The maintenance plans cover annual inspections and the replacement of wear and tear parts, excluding tires and the battery, with either a fixed fee per visit for Tesla Ranger service or unlimited Tesla Ranger visits for a higher initial purchase price. Payments collected in advance of the performance of service are initially recorded in deferred revenues on the consolidated balance sheets and recognized in automotive sales as we fulfill our performance obligations.

We also offer an extended service plan, which covers the repair or replacement of Model S parts for an additional four years or up to an additional 50,000 miles, after the end of our initial New Vehicle Limited Warranty, provided they are purchased within a specified period of time. For customers that are not covered by our New Vehicle Limited Warranties or our extended service plans, we offer Tesla Ranger service at a higher cost. Payments collected in advance of the performance of service are initially recorded in deferred revenues on the consolidated balance sheets and recognized in automotive sales ratably over the service coverage periods.

As of December 31, 2014 and 2013, we had deferred $39.7 million and $24.9 million, respectively, related to our maintenance and service plans. During the years ended December 31, 2014 and 2013, we recognized revenue of $3.0 million and $0.6 million related to these plans, respectively.

We provided Tesla Roadster customers with the opportunity to purchase an extended warranty plan for the period after the end of our initial New Vehicle Limited Warranty to cover additional services for an additional three years or 36,000 miles. We refer to this program as our Extended Service plan. Amounts collected on these sales are initially recorded in deferred revenues on the consolidated balance sheets and recognized in automotive sales over the extended warranty period. As of December 31, 2014 and 2013, we had deferred $0.7 million and $1.4 million, respectively. During the years ended December 31, 2014 and 2013, we recognized revenue of $0.5 million and $0.4 million related to this program, respectively.

Additionally, we have previously provided customers of our Tesla Roadsters with a one-time option to replace the battery packs in their vehicles at any time after the expiration of the New Vehicle Limited Warranty but before the tenth anniversary of the purchase date of their vehicles. We refer to this program as our Battery Replacement program. Amounts collected on these sales are initially recorded in deferred revenues on the consolidated balance sheets and recognized in automotive sales as we fulfill our obligation to replace the battery packs. As of December 31, 2014 and 2013, we had deferred $1.3 million and $1.3 million, respectively, related to the Battery Replacement program and have not yet recognized any related revenues.

Development Services Revenue

Revenue from development services arrangements consist of revenue earned from the development of electric vehicle powertrain components and systems for other automobile manufacturers, including the design and development of battery packs, drive units and sample vehicles to meet a customer’s specifications. Revenue is recognized as the performance requirements of each development arrangement are met and collection is reasonably assured. Where development arrangements include substantive at- risk milestones, revenue is recognized based upon the achievement of the contractually-defined milestones. Amounts collected in advance of meeting all of the revenue recognition criteria are not recognized in the consolidated statement of operations and are instead recorded as deferred revenue on the consolidated balance sheets. Costs of development services are expensed as incurred. When development services arrangements have multiple elements, we evaluate the separability of the various deliverables to ensure appropriate revenue recognition. Costs of development services incurred in periods prior to the finalization of an agreement are

recorded as research and development expenses; once an agreement is finalized, these costs are recorded in cost of revenues.

Cash and Cash Equivalents

All highly liquid investments with an original maturity of three months or less at the date of purchase are considered to be cash equivalents. We currently invest excess cash primarily in money market funds.

Marketable Securities

Marketable securities have historically been comprised of commercial paper and corporate debt and are all designated as available-for-sale and reported at estimated fair value, with unrealized gains and losses recorded in accumulated other comprehensive loss which is included within stockholders' equity. Realized gains and losses on the sale of available-for-sale marketable securities are recorded in other income (expense), net. The cost of available-for-sale marketable securities sold is based on the specific identification method. Interest, dividends, amortization and accretion of purchase premiums and discounts on our marketable securities are included in other income (expense), net. Available-for-sale marketable securities with maturities greater than three months at the date of purchase and remaining maturities of one year or less are classified as short-term marketable securities. Where temporary declines in fair value exist, we have the ability and the intent to hold these securities for a period of time sufficient to allow for any anticipated recovery in fair value.

When held, we regularly review all of our marketable securities for other-than-temporary declines in fair value. The review includes but is not limited to (i) the consideration of the cause of the impairment, (ii) the creditworthiness of the security issuers, (iii) the length of time a security is in an unrealized loss position, and (iv) our ability to hold the security for a period of time sufficient to allow for any anticipated recovery in fair value.

Restricted Cash and Deposits

We maintain certain cash amounts restricted as to withdrawal or use. We maintained total restricted cash of $29.3 million and $9.4 million as of December 31, 2014 and 2013, respectively. Current and noncurrent restricted cash as of December 31, 2013 was comprised primarily of security deposits held by vendors as part of the vendors' standard credit policies, security deposits related to lease agreements and equipment financing, and certain refundable customer deposits segregated in accordance with state consumer protection regulations.

Accounts Receivable and Allowance for Doubtful Accounts

Accounts receivable primarily include amounts related to sales of powertrain systems, receivables from financial institutions and leasing companies offering various financing products to our customers, and regulatory credits to other automotive manufacturers (OEMs). In circumstances where we are aware of a specific customer's inability to meet its financial obligations to us, we provide an allowance against amounts receivable to reduce the net recognized receivable to the amount we reasonably believe will be collected.

We typically do not carry accounts receivable related to our vehicle and related sales as customer payments are due prior to vehicle delivery, except for the amounts due from commercial financial institutions for approved financing arrangements between our customers and the financial institutions.

Concentration of Risk

Credit Risk

Financial instruments that potentially subject us to a concentration of credit risk consist of cash, cash equivalents, restricted cash and accounts receivable. Our cash equivalents are primarily invested in money market funds with high credit quality financial institutions in the United States. At times, these deposits and securities may be in excess of insured limits. We invest cash not required for use in operations in high credit quality securities based on our investment policy. Our investment policy provides guidelines and limits regarding credit quality, investment concentration, investment type, and maturity that we believe will provide liquidity while reducing risk of loss of capital. Our investments are currently of a short-term nature and include commercial paper and U.S. treasury bills.

As of December 31, 2014 and 2013, our accounts receivable were derived primarily from sales of regulatory credits, as well as funds to be received from financial institutions and leasing companies offering various financing products to our customers, the development and sales of powertrain components and systems to OEMs. Accounts receivable also included amounts to be received from commercial financial institutions for approved financing arrangements between our customers and financial institutions.

The following summarizes the accounts receivable from our OEM customers in excess of 10% of our total accounts receivable:

	December 31, 2014	December 31, 2013
Customer A	19 %	—
Customer B	14 %	30 %
Customer C	13 %	4 %

Supply Risk

Although there may be multiple suppliers available, many of the components used in our vehicles are purchased by us from a single source. If these single source suppliers fail to satisfy our requirements on a timely basis at competitive prices, we could suffer manufacturing delays, a possible loss of revenues, or incur higher cost of sales, any of which could adversely affect our operating results.

Inventories and Inventory Valuation

Inventories are stated at the lower of cost or market. Cost is computed using standard cost, which approximates actual cost on a first-in, first-out basis. We record inventory write-downs based on reviews for excess and obsolescence determined primarily by future demand forecasts. We also adjust the carrying value of our inventories when we believe that the net realizable value is less than the carrying value. These write-downs are measured as the difference between the cost of the inventory, including estimated costs to complete, and estimated selling prices. Once inventory is written down, a new, lower-cost basis for that inventory is established, and subsequent changes in facts and circumstances do not result in the restoration or increase in that newly established cost basis.

Property, Plant and Equipment

Property, plant and equipment are recognized at cost less accumulated depreciation. Depreciation is generally computed using the straight-line method over the estimated useful lives of the related assets as follows:

Machinery, equipment and office furniture	3 to 12 years
Building and building improvements	30 years
Computer equipment and software	3 years

Depreciation for tooling is computed using the units-of-production method whereby capitalized costs are amortized over the total estimated productive life of the related assets. As of December 31, 2014, the estimated productive life for tooling was 200,000 vehicles based on our current estimates of production.

Leasehold improvements are amortized on a straight-line basis over the shorter of their estimated useful lives or the term of the related lease.

Upon the retirement or sale of our property, plant and equipment, the cost and related accumulated depreciation are removed from the balance sheet and the resulting gain or loss is reflected in operations. Maintenance and repair expenditures are expensed as incurred, while major improvements that increase functionality of the asset are capitalized and depreciated ratably to expense over the identified useful life. Land is not depreciated.

Interest expense on outstanding debt is capitalized during the period of significant capital asset construction. Capitalized interest on construction in progress is included in property, plant and equipment, and is amortized over the life of the related assets.

Operating Lease Vehicles

Vehicles delivered under our resale value guarantee program, vehicles that are leased as part of our leasing program as well as any vehicles that are sold with a significant buy-back guarantee are classified as operating lease vehicles as the

related revenue transactions are treated as operating leases. Operating lease vehicles are recorded at cost less accumulated depreciation. Depreciation is computed using the straight-line method over the expected operating lease term. The total cost of operating lease vehicles recorded in the consolidated balance sheets as of December 31, 2014 and 2013 was $849.8 million and $401.9 million. Accumulated depreciation related to leased vehicles as of December 31, 2014 and 2013 was $83.1 million and $19.5 million.

Long-lived Assets

We evaluate our long-lived assets, including intangible assets, for indicators of possible impairment when events or changes in circumstances indicate the carrying amount of an asset (or asset group) may not be recoverable. Impairment exists if the carrying amounts of such assets exceed the estimates of future net undiscounted cash flows expected to be generated by such assets. Should impairment exist, the impairment loss would be measured based on the excess carrying value of the asset over the asset's estimated fair value. As of December 31, 2014 and 2013, we did not record any material impairment losses on our long-lived assets.

Research and Development Costs

Research and development costs are expensed as incurred. Research and development expenses consist primarily of payroll, benefits and stock-based compensation of those employees engaged in research, design and development activities, costs related to design tools, license expenses related to intellectual property, supplies and services, depreciation and other occupancy costs.

Advertising and Promotion Costs

Advertising and sales promotion costs are expensed as incurred. During the years ended December 31, 2014, 2013 and 2012, advertising, promotion and related marketing expenses were $48.9 million, $9.0 million and $3.9 million, respectively.

Shipping and Handling Costs

Amounts billed to customers related to shipping and handling are classified as revenue, and related shipping and handling costs are included in cost of revenues.

Income Taxes

Income taxes are computed using the asset and liability method, under which deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to affect taxable income. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized.

We record liabilities related to uncertain tax positions when, despite our belief that our tax return positions are supportable, we believe that it is more likely than not that those positions may not be fully sustained upon review by tax authorities. Accrued interest and penalties related to unrecognized tax benefits are classified as income tax expense.

Stock-based Compensation

We recognize compensation expense for costs related to all share-based payments, including stock options, restricted stock units (RSUs) and our employee stock purchase plan (the ESPP). The fair value of stock options and the ESPP are estimated on the grant date and offering date using an option pricing model, respectively. The fair value of RSUs is measured on the grant date based on the closing fair market value of our common stock. Stock-based compensation expense is recognized on a straight-line basis over the requisite service period, net of estimated forfeitures.

We account for equity instruments issued to non-employees based on the fair value of the awards. The fair value of the awards granted to non-employees is re-measured as the awards vest and the resulting change in fair value, if any, is recognized in the consolidated statements of operations during the period the related services are rendered.

For performance-based awards, stock-based compensation expense is recognized over the expected performance achievement period of individual performance milestones when the achievement of each individual performance milestone becomes probable.

For performance-based awards with a vesting schedule based entirely on the attainment of both performance and market conditions, the stock-based compensation expense is recognized for each pair of performance and market conditions over the longer of the expected achievement period of the performance and market conditions, beginning at the point in time that the relevant performance condition is considered probable of being met (see Note 8).

Foreign Currency Remeasurement and Transactions

For each of our foreign subsidiaries, the functional currency is the U.S. dollar. For these foreign subsidiaries, monetary assets and liabilities denominated in non-U.S. currencies are re-measured to U.S. dollars using current exchange rates in effect at the balance sheet date. Non-monetary assets and liabilities denominated in non-U.S.

currencies are maintained at historical U.S. dollar exchange rates. Revenues and expenses are re-measured at average U.S. dollar monthly rates.

Foreign currency transaction gains and losses are a result of the effect of exchange rate changes on transactions denominated in currencies other than the functional currency. Transaction gains and losses are recognized in other income (expense), net, in the consolidated statements of operations. For the year ended December 31, 2014 and 2013, we recorded foreign currency transaction gains of $2.0 million and $11.9 million, respectively. For the year ended December 2012, transaction gains and losses were not significant.

Beginning January 1, 2015, the functional currency of each of our foreign subsidiaries changed to their local country's currency. This change was based on the culmination of facts and circumstances that have developed as we expanded our foreign operations over the past year. The adjustment attributable to the current rate translation of non-monetary assets as of the date of the change will be included in accumulated other comprehensive income in the Company's quarterly report on Form 10-Q for the period ending March 31, 2015.

Comprehensive Loss

Comprehensive loss is comprised of net loss and other comprehensive income (loss). Other comprehensive income (loss) consists of unrealized gains and losses on our available-for-sale marketable securities that have been excluded from the determination of net loss.

Warranties

We provide a warranty on all vehicle, production powertrain components and systems sales, and we accrue warranty reserves at the time a vehicle or production powertrain component or system is delivered to the customer. Warranty reserves include management's best estimate of the projected costs to repair or to replace any items under warranty, based on actual warranty experience as it becomes available and other known factors that may impact our evaluation of historical data. For new vehicles, warranty reserves are based on management's best estimate of projected warranty experience until adequate historical data is accumulated. Our warranty reserves do not include projected warranty costs associated with our resale value guarantee vehicles as such actual warranty costs are expensed as incurred. For the year ended December 31, 2014, warranty costs incurred for our resale value guarantee vehicles was $6.9 million. We may have material changes as we accumulate more actual data and experience. We review our reserves at least quarterly to ensure that our accruals are adequate in meeting expected future warranty obligations, and we will adjust our estimates as needed. Warranty expense is recorded as a component of cost of revenues in the consolidated statements of operations. The portion of the warranty provision which is expected to be incurred within 12 months from the balance sheet date is classified as current, while the remaining amount is classified as long-term.

We began recording warranty reserves with the commencement of Tesla Roadster sales in 2008. Initially, Tesla Roadsters were sold with a warranty of three years or 36,000 miles, which we extended to four years or 50,000 miles for the purchasers of our 2008 Tesla Roadster. Tesla Roadster customers had the opportunity to purchase an Extended Service plan for the period after the end of the New Vehicle Limited Warranty to cover additional services for an additional three years or 36,000 miles, provided they are purchased within a specified period of time.

In June 2012, we commenced deliveries of Model S. For our Model S customers, we provide a four year or 50,000 miles New Vehicle Limited Warranty, subject to separate limited warranties for the supplemental restraint system and battery. During the third quarter of 2014, we extended the warranty on our Model S drive unit to eight years from four. The New Vehicle Limited Warranty also covers the battery for a period of eight years or 125,000 miles or unlimited miles, depending on the size of the vehicle's battery, although the battery's charging capacity is not covered. Model S customers also have the opportunity to purchase an Extended Service plan for the period after the end of the New Vehicle Limited Warranty to cover additional services for an additional four years or 50,000 miles, provided they are purchased within a specified period of time. The battery pack's charging capacity is not covered under the New Vehicle Limited Warranty or any Extended Service plan.

As of December 31, 2014 and 2013 the current portion of our accrued warranty was $32.3 million and $19.9 million, which was recorded in accrued liabilities in our Consolidated Balance Sheets. As of December 31, 2014 and 2013 the non-current portion of our accrued warranty was $96.7 million and $33.3 million, which was recorded in other long-term liabilities in our Consolidated Balance Sheets.

Accrued warranty activity consisted of the following for the periods presented (in thousands):

	Year Ended December 31,		
	2014	2013	2012
Accrued warranty—beginning of period	$53,182	$13,013	$6,315
Warranty costs incurred	(39,903)	(19,160)	(3,424)
Net changes in liability for pre-existing warranties, including expirations	18,599	(2,072)	—
Provision for warranty	97,165	61,401	10,122
Accrued warranty—end of period	$129,043	$53,182	$13,013

Environmental Liabilities

We are subject to federal and state laws and regulations for the protection of the environment, including those related to the discharge of hazardous materials and remediation of contaminated sites. We accrue for environmental liabilities in the period in which it is probable a liability exists and the amount of such loss can be reasonably estimated. We assess adequacy of our accrued liabilities for remediation of any environmental contamination at least quarterly and adjust our estimates as appropriate. As of December 31, 2014 and 2013, we accrued $4.0 million and $5.5 million related to environmental liabilities (see Note 11).

Net Loss per Share of Common Stock

Our basic and diluted net loss per share of common stock is calculated by dividing net loss by the weighted-average shares of common stock outstanding for the period. Potentially dilutive shares, which are based on the number of shares underlying outstanding stock options and warrants as well as our Notes, are not included when their effect is antidilutive.

The following table presents the potential weighted common shares outstanding that were excluded from the computation of basic and diluted net loss per share of common stock for the periods, related to the following securities:

	Year Ended December 31,		
	2014	2013	2012
Stock options	260,852	13,881,355	25,007,776
Convertible senior notes	2,344,998	411,560	—
Warrants issued May 2013	921,985	—	—
Employee stock purchase plan	23,859	23,296	59,763
Restricted stock units	88,213	224	—
DOE warrant	—	1,061,439	2,342,353

Since we expect to settle the principal amount of our outstanding convertible senior notes in cash, we use the treasury stock method for calculating any potential dilutive effect of the conversion spread on diluted net income per share, if applicable. The conversion spread will have a dilutive impact on diluted net income per share of common stock when the average market price of our common stock for a given period exceeds the conversion price of $124.52, $359.87, and $359.87 per share for the convertible senior notes due 2018 Notes, 2019 Notes and 2021 Notes, respectively.

3. Balance Sheet Components

Inventory

As of December 31, 2014 and 2013, our inventory consisted of the following (in thousands):

	December 31, 2014	December 31, 2013
Raw materials	$392,292	$184,665
Work in process	56,114	42,500
Finished goods	397,318	69,324
Service parts	107,951	43,866
Total	$953,675	$340,355

Finished goods inventory includes vehicles made to fulfill customer orders which have not been delivered and a smaller portion of vehicles available for immediate sale at our retail and service center locations. In addition, we also maintain vehicles used for marketing purposes and service loaners until they are sold to customers.

We write down inventory as a result of excess and obsolete inventories, or when we believe that the net realizable value of inventories is less than the carrying value. During the years ended December 31, 2014, 2013 and 2012, we recorded write-downs of $15.6 million, $8.9 million and $5.0 million, respectively, in cost of automotive sales.

Property, Plant and Equipment

As of December 31, 2014 and 2013, our property, plant and equipment, net, consisted of the following (in thousands):

	December 31, 2014	December 31, 2013
Machinery, equipment and office furniture	$720,746	$322,394
Tooling	295,906	230,385
Leasehold improvements	230,270	94,763
Building and building improvements	154,362	67,707
Land	49,478	45,020
Computer equipment and software	98,970	42,073
Construction in progress	572,125	76,294
	2,121,857	878,636
Less: Accumulated depreciation and amortization	(292,590)	(140,142)
Total	$1,829,267	$738,494

Construction in progress is comprised primarily of assets related to the manufacturing of our Model S, including building improvements at our Tesla Factory in Fremont, California as well as tooling and manufacturing equipment and capitalized interest expense. Depreciation of construction in progress begins when the assets are ready for their intended use. Interest expense on outstanding debt is capitalized during the period of significant capital asset construction. Capitalized interest on construction in progress is included in property, plant and equipment, and is amortized over the life of the related assets. During the years ended December 31, 2014 and 2013, we capitalized $12.8 million and $3.5 million of interest expense, respectively.

We are sometimes involved in construction at our leased facilities. In accordance with Accounting Standards Codification 840, Leases, for build-to-suit lease arrangements where we are involved in the construction of structural improvements prior to the commencement of the lease or take some level of construction risk, we are considered the owner of the assets during the construction period. Accordingly, upon commencement of our construction activities, we record a construction in progress asset and a corresponding financing liability. As of December 31, 2014, the table above includes $52.4 million of build-to-suit assets. Corresponding financing obligations of $21.0 million and $31.4 million are recorded in accrued liabilities and other long-term liabilities. Once the construction is completed, if the lease meets certain “sale-leaseback” criteria, we will remove the asset and related financial obligation from the balance sheet and treat the building lease as an operating lease. If upon completion of construction, the project does not meet the “sale-leaseback” criteria, the leased property will be treated as a capital lease for financial reporting purposes.

Depreciation and amortization expense during the years ended December 31, 2014, 2013 and 2012 were $155.9 million, $83.9 million and $25.3 million, respectively. Total property and equipment assets under capital lease as of December 31, 2014 and 2013 were $33.4 million and $23.3 million, respectively. Accumulated depreciation related to assets under capital lease as of these dates were $12.8 million and $5.0 million, respectively.

We have acquired land for the site of our Gigafactory and have begun initial construction activities on the site and have incurred $106.6 million of costs as of December 31, 2014.

Accrued Liabilities

As of December 31, 2014 and 2013, our accrued liabilities consisted of the following (in thousands):

	December 31, 2014	December 31, 2013
Taxes payable	$71,229	$38,067
Accrued purchases	68,547	19,023
Payroll and related costs	54,492	26,535
Accrued warranty, current portion	32,321	19,917
Build to suit finance obligation, current portion	21,030	—
Accrued interest	7,222	741
Environmental liabilities, current portion	3,573	2,132
Other	10,470	1,837
Total	$268,884	$108,252

4. Fair Value of Financial Instruments

The carrying values of our financial instruments including cash equivalents, marketable securities, accounts receivable and accounts payable approximate their fair value due to their short-term nature. As a basis for determining the fair value of certain of our assets and liabilities, we established a three-tier fair value hierarchy which prioritizes the inputs used in measuring fair value as follows: (Level I) observable inputs such as quoted prices in active markets; (Level II) inputs other than the quoted prices in active markets that are observable either directly or indirectly; and (Level III) unobservable inputs in which there is little or no market data which requires us to develop our own assumptions. This hierarchy requires us to use observable market data, when available, and to minimize the use of unobservable inputs when determining fair value. Our financial assets that are measured at fair value on a recurring basis consist of cash equivalents and marketable securities. Our restricted short-term marketable securities are classified within Level I of the fair value hierarchy.

All of our cash equivalents and current restricted cash, which are comprised primarily of money market funds, are classified within Level I of the fair value hierarchy because they are valued using quoted market prices or market prices for similar securities.

As of December 31, 2014 and 2013, the fair value hierarchy for our financial assets and financial liabilities that are carried at fair value was as follows (in thousands):

	December 31, 2014				December 31, 2013			
	Fair Value	Level I	Level II	Level III	Fair Value	Level I	Level II	Level III
Money market funds	$1,275,346	$1,275,346	$ —	$ —	$460,313	$460,313	$ —	$ —
U.S. treasury bills	16,673	16,673	—	—	—	—	—	—
Total	$1,292,019	$1,292,019	$ —	$ —	$460,313	$460,313	$ —	$ —

Our available-for-sale marketable securities classified by security type as of December 31, 2014 consisted of the following (in thousands):

	Year Ended December 31, 2014			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. treasury bills	$16,695	$ —	$ (22)	$16,673

The changes in the fair value of our common stock warrant liability were as follows (in thousands):

	Year Ended December 31, 2013
Fair value, beginning of period	$ 10,692
Change in fair value	(10,692)
Fair value, end of period	$ —

The estimated fair value of our 2018 Notes based on a market approach was approximately $1.22 billion (par value $659.8 million) as of December 31, 2014 and $914.9 million (par value of $660.0 million) as of December 31, 2013, respectively, and represent a Level II valuation. The estimated fair value of our 2019 Notes and 2021 Notes based on a market approach was approximately $852.2 million (par value $920.0 million) and $1.25 billion (par value of $1.38 billion) as of December 31, 2014, respectively, and represents a Level II valuation. When determining the estimated fair value of our long-term debt, we used a commonly accepted valuation methodology and market-based risk measurements that are indirectly observable, such as credit risk.

5. Customer Deposits

We collect deposits from customers at the time they place an order for a vehicle and, in some locations, at certain additional milestones up to the point of delivery. Customer deposit amounts and timing vary depending on the vehicle model and country of delivery. Customer deposits related to Model X still represent fully refundable reservations. Amounts are included in current liabilities until refunded or until they are applied to a customer’s purchase balance at time of delivery.

As of December 31, 2014 and 2013, we held $257.6 million and $163.2 million, respectively, in customer deposits.

6. Convertible Notes and Long-term Debt Obligations

0.25% and 1.25% Convertible Senior Notes and Bond Hedge and Warrant Transactions

In March 2014, we issued $800.0 million principal amount of 0.25% convertible senior notes due 2019 (2019 Notes) and $1.20 billion principal amount of 1.25% convertible senior notes due 2021 (2021 Notes) in a public offering. In April 2014, we issued an additional $120.0 million aggregate principal amount of 2019 Notes and $180.0 million aggregate principal amount of 2021 Notes, pursuant to the exercise in full of the overallotment options of the underwriters of our March 2014 public offering. The total net proceeds from these offerings, after deducting transaction costs, were approximately $905.8 million from 2019 Notes and $1.36 billion from 2021 Notes, respectively. We incurred $14.2 million and $21.4 million, respectively, of debt issuance costs in connection with the 2019 Notes and the 2021 Notes, which we initially recorded in other assets and are amortizing to interest expense using the effective interest method over the contractual terms of these notes. The interest rates are fixed at 0.25% and 1.25% per annum and are payable semi-annually in arrears on March 1 and September 1 of each year, commencing on September 1, 2014. During the year ended December 31, 2014, we recognized $3.2 million of interest expense, related to the amortization of debt issuance costs and $16.2 million of accrued coupon interest expense.

Each $1,000 of principal of these notes will initially be convertible into 2.7788 shares of our common stock, which is equivalent to an initial conversion price of approximately $359.87 per share, subject to adjustment upon the occurrence of specified events. Holders of these notes may convert their Notes at their option on or after December 1, 2018 for the 2019 Notes and on or after December 1, 2020 for the 2021 Notes. Further, holders of these notes may convert their notes at their option prior to the respective dates above, only under the following circumstances: (1) during any fiscal quarter beginning after the fiscal quarter ending June 30, 2014, if the last reported sale price of our common stock for at least 20 trading days (whether or not consecutive) during the last 30 consecutive trading days of immediately preceding fiscal quarter is greater than or equal to 130% of the conversion price of the applicable notes on each applicable trading day; (2) during the five business day period following any five consecutive trading day period in which the trading price for the applicable notes is less than 98% of the average of the closing sale price of our common stock for each day during such five trading day period; or (3) if we make specified distributions to holders of our common stock or if specified corporate transactions occur. Upon conversion of the 2019 Notes, we would pay or deliver as applicable, cash, shares of our common stock or a combination of cash and shares of our common stock, at our election. Upon conversion of the 2021 Notes, we would pay the holders in cash for the principal amount and, if applicable, shares of our common stock (subject to our right to deliver cash in lieu of all or a portion of such shares of our common stock) based on a daily conversion value. If a fundamental change occurs prior to the maturity date, holders of these notes may require us to repurchase all or a portion of their notes for cash at a repurchase price equal to 100% of the principal amount of the notes, plus any accrued and unpaid interest. In addition, if specific corporate events occur prior to the applicable maturity date, we will increase the conversion rate for a holder who elects to convert their notes in connection with such a corporate event in certain circumstances. During the fourth quarter of 2014, the closing price of our common stock did not meet or exceed 130% of the applicable conversion price of our 2019 Notes and 2021 Notes on at least 20 of the last 30 consecutive trading days of the quarter; furthermore, no other conditions allowing holders of these notes to convert have been met as of December 31, 2014. Therefore, the 2019 Notes and 2021 Notes are not convertible during the first quarter of 2015 and are classified as long-term debt. Should the closing price conditions be met in the first quarter of 2015 or a future quarter, the Notes will be convertible at their holders' option during the immediately following quarter. As of December 31, 2014, the if-converted value of the 2019 Notes and 2021 Notes did not exceed the principal value of those Notes.

In accordance with accounting guidance on embedded conversion features, we valued and bifurcated the conversion option associated with the notes from the respective host debt instrument and initially recorded the conversion option of $188.1 million for the 2019 Notes and $369.4 million for the 2021 Notes in stockholders' equity. The resulting debt discounts on the 2019 Notes and 2021 Notes are being amortized to interest expense at an effective interest rate of 4.89% and 5.96%, respectively, over the contractual terms of the notes. During the year ended December 31, 2014, we recognized $64.0 million of interest expense related to the amortization of the debt discount. As of December 31, 2014, the net carrying value of 2019 Notes and 2021 Notes was $759.9 million and $1.05 billion, respectively. The remaining bond discounts of the 2019 Notes and 2021 Notes of $160.1 million and $333.4 million will be amortized over their remaining lives of approximately 3.9 years and 5.9 years.

In connection with the offering of these notes in March 2014, we entered into convertible note hedge transactions whereby we have the option to purchase initially (subject to adjustment for certain specified events) a total of approximately 5.6 million shares of our common stock at a price of approximately $359.87 per share. The total cost of the convertible note hedge transactions was $524.7 million. In addition, we sold warrants whereby the holders of the warrants have the option to purchase initially (subject to adjustment for certain specified events) a total of approximately 2.2 million shares of our common stock at a price of $512.66 for the 2019 Notes and a total of approximately 3.3 million shares of our common stock at a price of $560.64 per share for 2021 Notes. We received $338.4 million in cash proceeds from the sale of these warrants. Similarly, in connection with the issuance of additional notes in April 2014, we entered into convertible note hedge transactions and paid an aggregate $78.7 million. In addition, we sold warrants to purchase (subject to adjustment for certain specified events) a total of approximately 0.3 million shares of our common stock at a strike price of $512.66 per share for the warrants relating to 2019 Notes, and a total of approximately 0.5 million shares of our common stock at a strike price of $560.64 per share for the warrants relating to 2021 Notes. We received aggregate proceeds of approximately $50.8 million from the sale of the warrants. Taken together, the purchase of the convertible note hedges and the sale of warrants are intended to offset any actual dilution from the conversion of these notes and to effectively increase the overall conversion price from $359.87 to $512.66 per share in the case of warrants relating to 2019 Notes and from $359.87 to $560.64 in the case of warrants relating to 2021 Notes. As these transactions meet certain accounting criteria, the convertible note hedges and warrants are recorded in stockholders' equity and are not accounted for as derivatives. The net cost incurred in connection with the convertible note hedge and warrant transactions was recorded as a reduction to additional paid-in capital on the consolidated balance sheet as of December 31, 2014.

1.50% Convertible Senior Notes and Bond Hedge and Warrant Transactions

In May 2013, we issued $660.0 million aggregate principal amount of 2018 Notes in a public offering. The net proceeds from the offering, after deducting transaction costs, were approximately $648.0 million. We incurred $12.0 million of debt issuance costs in connection with the issuance of the 2018 Notes which we recorded in other assets and are amortizing to interest expense using the effective interest method over the contractual term of the 2018 Notes. The interest under the 2018 Notes is fixed at 1.50% per annum and is payable semi-annually in arrears on June 1 and December 1 of each year, commencing on December 1, 2013. During the years ended December 31, 2014 and 2013, we recognized $2.0 million and $1.2 million, respectively, of interest expense related to the amortization of debt issuance costs and $9.8 million and $5.9 million, respectively, of coupon interest expense.

Each $1,000 of principal of the 2018 Notes will initially be convertible into 8.0306 shares of our common stock, which is equivalent to an initial conversion price of approximately $124.52 per share, subject to adjustment upon the occurrence of specified events. Holders of the 2018 Notes may convert their 2018 Notes at their option on or after March 1, 2018. Further, holders of the 2018 Notes may convert their 2018 Notes at their option prior to March 1, 2018, only under the following circumstances: (1) during any fiscal quarter beginning after the fiscal quarter ending September 30, 2013, if the last reported sale price of our common stock for at least 20 trading days (whether or not consecutive) during the last 30 consecutive trading days of the immediately preceding fiscal quarter is greater than or equal to 130% of the conversion price on each applicable trading day; (2) during the five business day period following any five consecutive trading day period in which the trading price for the 2018 Notes is less than 98% of the average of the closing sale price of our common stock for each day during such five trading day period; or (3) if we make specified distributions to holders of our common stock or if specified corporate transactions occur. Upon conversion, we would pay the holders in cash for the principal amount of the 2018 Notes and, if applicable, shares of our common stock (subject to our right to deliver cash in lieu of all or a portion of such shares of our common stock) based on a calculated daily conversion value. If a fundamental change occurs prior to the maturity date, holders of the 2018 Notes may require us to repurchase all or a portion of their 2018 Notes for cash at a repurchase price equal to

100% of the principal amount of the 2018 Notes, plus any accrued and unpaid interest. In addition, if specific corporate events occur prior to the maturity date, we will increase the conversion rate for a holder who elects to convert its 2018 Notes in connection with such a corporate event in certain circumstances.

In accordance with accounting guidance on embedded conversion features, we valued and bifurcated the conversion option associated with the 2018 Notes from the host debt instrument and recorded the conversion option of $82.8 million in stockholders' equity. The resulting debt discount on the 2018 Notes is being amortized to interest expense at an effective interest rate of 4.29% over the contractual term of the 2018 Notes. During the years ended December 31, 2014 and 2013, we recognized $15.5 million and $9.1 million, respectively, of interest expense related to the amortization of the debt discount. As of December 31, 2014, the net carrying value of the 2018 Notes was $601.6 million. The remaining bond discounts of the 2018 Notes of $58.2 million will be amortized over its remaining life of approximately 3.2 years.

In connection with the offering of the 2018 Notes, we entered into convertible note hedge transactions whereby we have the option to purchase initially (subject to certain specified events) a total of approximately 5.3 million shares of our common stock at a price of approximately $124.52 per share. The cost of the convertible note hedge transactions was $177.5 million. In addition, we sold warrants whereby the holders of the warrants have the option to purchase initially (subject to certain specified events) a total of approximately 5.3 million shares of our common stock at a price of $184.48 per share. We received $120.3 million in cash proceeds from the sale of these warrants. Taken together, the purchase of the convertible note hedges and the sale of warrants are intended to offset any actual dilution from the conversion of the 2018 Notes and to effectively increase the overall conversion price from $124.52 to $184.48 per share. As these transactions meet certain accounting criteria, the convertible note hedges and warrants are recorded in stockholders' equity and are not accounted for as derivatives. The net cost incurred in connection with the convertible note hedge and warrant transactions was recorded as a reduction to additional paid-in capital on the consolidated balance sheet as of December 31, 2014.

During the fourth quarter of 2014, the closing price of our common stock exceeded 130% of the applicable conversion price of our 2018 Notes on at least 20 of the last 30 consecutive trading days of the quarter; therefore, holders of 2018 Notes may convert their notes during the first quarter of 2015. As such, we classified the $601.6 million carrying value of our 2018 Notes as current liabilities and classified $58.2 million, representing the difference between the aggregate principal of our 2018 Notes of $659.8 million and the carrying value of 2018 Notes, as mezzanine equity on our consolidated balance sheet as of December 31, 2014. Similarly, debt issuance costs were classified as other current assets as of December 31, 2014. Should the closing price conditions be met in the first quarter of 2015 or a future quarter, 2018 Notes will be convertible at their holders' option during the immediately following quarter. As of December 31, 2014, the if-converted value of the 2018 Notes exceeded the aggregate principal amount by $518.7 million.

Contractual Obligations

As of December 31, 2014, aggregate future principal payments for our convertible senior notes were as follows (in thousands):

Years ending December 31,	
2015	$659,795
2016	—
2017	—
2018	—
2019	920,000
Thereafter	1,380,000
Total	$2,959,795

During the fourth quarter of 2014, the closing price of our common stock exceeded 130% of the applicable conversion price of our 2018 Notes on at least 20 of the last 30 consecutive trading days of the quarter; therefore, holders of 2018 Notes may convert their notes during the first quarter of 2015. As such, we have included the principal payment of the 2018 Notes in the 2015 category in the table above.

Full Repayment of Department of Energy Loan Facility

In May 2013, in connection with the closing of our offerings of common stock and Notes, we paid $451.8 million to settle all outstanding loan amounts of $441.0 million, including principal and interest, as well as an early repayment penalty of $10.8 million which was recorded in interest expense for the year ended December 31, 2013. Upon termination of the DOE Loan Facility, $29.3 million held in this dedicated account was released by the DOE.

On January 20, 2010, we entered into a loan facility with the Federal Financing Bank (FFB), and the DOE, pursuant to the Advanced Technology Vehicles Manufacturing (ATVM) Incentive Program. This loan facility was amended in June 2011 to expand our cash investment options, in February 2012 to modify the timing of certain future financial covenants and funding of the debt service reserve account, and in June and December 2012 to allow us to affect certain initiatives in our business plan. In September 2012, we entered into an amendment with the DOE to remove our obligation to comply with the current ratio financial covenant as of September 30, 2012 and amend the timing of pre-funding the principal payment due in June 2013. We entered into another amendment with the DOE in March 2013 that, among other things, modified certain future financial covenants, accelerated the maturity date of the DOE Loan Facility to December 15, 2017, created an obligation to repay approximately 1.0% of the outstanding principal under the DOE Loan Facility on or before June 15, 2013, and created additional contingent obligations based on excess cash flows that may result in accelerated repayment of the DOE Loan Facility starting in 2015. The original amortization schedule for the DOE Loan Facility was not affected by this amendment, and so the debt service payments remained the same until the new maturity date when all outstanding loans under the DOE Loan Facility were to be repaid. We refer to the loan facility with the DOE, as amended, as the DOE Loan Facility. Under the DOE Loan Facility, the FFB made available to us two multi-draw term loan facilities in an aggregate principal amount of $465.0 million. As of August 31, 2012, we had fully drawn down the aforementioned facilities.

All outstanding amounts under the DOE Loan Facility were repayable in quarterly installments, which commenced on December 15, 2012 and would be due on the maturity date of December 15, 2017. All obligations under the DOE Loan Facility were secured by substantially all of our property.

The DOE Loan Facility documents contained customary covenants that included, among others, a requirement that the projects be conducted in accordance with the business plan for such project, compliance with all requirements of the ATVM Program, and limitations on our and our subsidiaries' ability to incur indebtedness, incur liens, make investments or loans, enter into mergers or acquisitions, dispose of assets, pay dividends or make distributions on capital stock, pay indebtedness, pay management, advisory or similar fees to affiliates, enter into certain affiliate transactions, enter into new lines of business, and enter into certain restrictive agreements, in each case subject to customary exceptions. The DOE Loan Facility documents also contained customary financial covenants requiring us to maintain a minimum ratio of current assets to current liabilities, and (i) a limit on capital expenditures, (ii) from December 31, 2013, a maximum leverage ratio, a minimum interest coverage ratio, a minimum fixed charge coverage ratio, and (iii) from March 31, 2014, a maximum ratio of total liabilities to shareholder equity. We were in compliance with our current applicable financial covenants as of March 31, 2013. The DOE Loan Facility documents also contained customary events of default, subject in some cases to customary cure periods for certain defaults. In addition, events of default included a failure of Elon Musk, our Chief Executive Officer (CEO), and certain of his affiliates, at any time prior to one year after we would complete the project relating to the Model S Facility, to own at least 65% of capital stock held by Mr. Musk and such affiliates as of the date of the DOE Loan Facility. As part of the amendment to the DOE Loan Facility in March 2013, we agreed to, among other things, (i) make an early payment of approximately 1.0% of the outstanding principal under the DOE Loan Facility on or before June 15, 2013, (ii) make additional quarterly prepayments equal to: 20% of our excess cash flow for each quarter of fiscal 2015; and 35% of our excess cash flow for each quarter of fiscal 2016 and 2017.

Under the DOE Loan Facility, we had agreed to pre-fund a dedicated debt service reserve account with our planned loan repayments as required by the DOE loan facility. As of December 31, 2012, $14.9 million was held in this dedicated account and classified this cash as current restricted cash on the consolidated balance sheet.

DOE Warrant Expiration

In connection with the closing of the DOE Loan Facility, we issued in January 2010 a warrant to the DOE to purchase up to 9,255,035 shares of our Series E convertible preferred stock at an exercise price of $2.51 per share. Upon the completion of our initial public offering on July 2, 2010, this preferred stock warrant became a warrant to purchase up to 3,090,111 shares of common stock at an exercise price of $7.54 per share. Since the number of shares ultimately issuable under the warrants would vary depending on the average outstanding balance of the loan during the contractual vesting period, and decisions to prepay would be influenced by our future stock price as well as the interest rates on our loans in relation to market interest rates, we had historically measured the fair value of the warrant using a Monte Carlo simulation approach. The Monte Carlo approach simulates and captures the optimal decisions to be made between prepaying the DOE loan and the cancellation of the DOE warrant. For the purposes of the simulation, the optimal decision represents the scenario with the lowest economic cost to us. The total warrant value would then be calculated as the average warrant payoff across all simulated paths discounted to our valuation date. The prepayment feature which allowed us to prepay the DOE Loan Facility, and consequently affected the number of shares ultimately issuable under the DOE warrant, was determined to represent an embedded derivative. This embedded derivative was inherently valued and accounted for as part of the warrant liability on our consolidated balance sheets. Changes to the fair value of the embedded derivative were reflected as part of the warrant liability re-measurement to fair value at each balance sheet reporting date. The warrant was recorded at its estimated fair value with changes in its fair value reflected in other income (expense), net, until its expiration or vesting. As of

December 31, 2012, the fair value of the DOE warrant was $10.7 million. During the year ended December 31, 2012, we recognized expense for the change in the fair value of the DOE warrant in the amount of $1.9 million through other income (expense), net, in the consolidated statements of operations. The fair value of the warrant at issuance was $6.3 million, and along with the DOE Loan Facility fee of $0.5 million and other debt issuance costs of $0.9 million, represented a cost of closing the loan facility and was being amortized to interest expense over the expected term of the DOE Loan Facility. During the year ended December 31, 2012, we amortized $0.6 million to interest expense, respectively.

As a result of our repayment of all outstanding principal and interest under the DOE Loan Facility and the termination of the DOE Loan Facility in May 2013, the DOE warrant expired. As such, we recognized other income for the change in the fair value of the DOE warrant in the amount of $10.7 million for the year ended December 31, 2013. Additionally, we amortized all remaining unamortized debt issuance costs of $5.8 million related to the DOE Loan Facility to interest expense for the year ended December 31, 2013.

7. Common Stock

In October 2012, we completed a follow-on offering of common stock in which we sold a total of 7,964,601 shares of our common stock and received cash proceeds of $222.1 million (which included 35,398 shares or $1.0 million sold to our CEO) from this transaction, net of underwriting discounts and offering costs.

In May 2013, we completed a public offering of common stock and sold a total of 3,902,862 shares of our common stock for total cash proceeds of approximately $355.1 million (which included 487,857 shares or $45.0 million sold to our CEO), net of underwriting discounts and offering costs. We also sold 596,272 shares of our common stock to our CEO and received total cash proceeds of $55.0 million in a private placement at the public offering price. Concurrent with these equity transactions, we also issued $660.0 million principal amount of 1.50% convertible senior notes in a public offering and received total cash proceeds of approximately $648.0 million, net of underwriting discounts and offering costs (see Note 6).

8. Equity Incentive Plans

In July 2003, we adopted the 2003 Equity Incentive Plan. Concurrent with the effectiveness of our registration statement on Form S-1 on June 28, 2010, we adopted the 2010 Equity Incentive Plan (the Plan) and all remaining common shares reserved for future grant or issuance under the 2003 Equity Incentive Plan were added to the 2010 Equity Incentive Plan. The Plan provides for the granting of stock options, RSUs and stock purchase rights to our employees, directors and consultants. Options granted under the Plan may be either incentive options or nonqualified stock options. Incentive stock options may be granted only to our employees including officers and directors. Nonqualified stock options and stock purchase rights may be granted to our employees and consultants. Generally, our stock options and RSUs vest over four years and are exercisable over a period not to exceed the contractual term of ten years from the date the stock options are granted. Continued vesting typically terminates when the employment or consulting relationship ends. As of December 31, 2014, 22,853,070 shares of common stock were reserved for issuance under the Plan.

The following table summarizes stock option and RSU activity under the Plan:

		Outstanding Stock Options		Outstanding RSUs	
	Shares Available for Grant	Number of Options	Weighted Average Exercise Price	Number of RSUs	Weighted Average Grant Date Fair Value
Balance, December 31, 2011	9,919,107	15,806,663	$ 13.35	—	$ —
Additional options reserved	1,064,046	—	—	—	—
Granted	(11,854,941)	11,854,941	31.18	—	—
Exercised		(1,312,439)	12.52	—	—
Cancelled	1,341,319	(1,341,389)	25.51	—	—
Balance, December 31, 2012	469,531	25,007,776	21.20	—	—
Additional options reserved	3,426,428	—		—	—
Granted	(3,345,899)	2,643,821	74.17	702,078	155.51
Exercised	—	(3,852,673)	21.42	—	—

Cancelled	1,170,445	(1,157,982)	36.47	(12,463)	154.92
Released	—	—	—	(12,031)	160.98
Balance, December 31, 2013	1,720,505	22,640,942	26.70	677,584	155.41
Additional options reserved	3,077,274	—		—	—
Granted	(2,525,246)	1,432,171	181.56	1,093,075	223.66
Exercised	—	(2,266,697)	31.80	—	—
Cancelled	556,765	(433,456)	56.25	(123,309)	187.90
Released	—	—	—	(167,240)	155.70
Traded for taxes	6,786	—	—	—	—
Balance, December 31, 2014	2,836,084	21,372,960	$ 35.93	1,480,110	$ 203.08

Additional information regarding all stock options outstanding and exercisable as of December 31, 2014 is summarized below:

	Options Outstanding			Options Exercisable		
Range of Exercise Price	Number	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (in years)	Number	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (in years)
$2.70 - $6.15	329,072	$ 3.13		327,696	$ 3.13	
$6.63 - $6.63	7,030,489	6.63		7,029,293	6.63	
$9.96 - $28.45	2,183,386	23.87		1,779,133	23.19	
$29.12 - $31.07	1,105,021	30.00		606,484	30.00	
$31.17 - $31.17	5,611,130	31.17		663,860	31.17	
$31.49 - $38.42	2,376,417	33.25		1,167,109	32.82	
$39.10 - $179.72	2,140,496	111.51		379,519	94.50	
$184.67 - $259.32	498,658	233.06		84	198.09	
$259.94 - $259.94	72,333	259.94		4,332	259.94	
$282.11 - $282.11	25,958	282.11		—	—	
	21,372,960	35.93	5.48	11,957,510	12.37	3.63

Additional information regarding all stock options outstanding and exercisable as of December 31, 2013 is summarized below:

	Options Outstanding			Options Exercisable		
Range of Exercise Price	Number	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (in years)	Number	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (in years)
$0.15 - $6.15	523,182	$ 3.16		516,728	$ 3.16	
$6.63 - $6.63	7,096,725	6.63		7,093,020	6.63	
$9.96 - $28.35	2,266,058	22.08		1,302,499	19.70	
$28.43 - $31.07	2,136,721	29.48		864,050	29.24	
$31.07 - $31.07	5,715,734	31.17		91,541	31.17	
$31.49 - $34.00	2,288,998	32.07		707,052	31.98	
$34.57 - $141.60	2,266,350	60.57		127,674	45.62	
$144.70 - $147.38	252,945	147.31		11,542	147.38	
$160.70 - $160.70	18,975	160.70		—	—	
$179.72 - $179.72	75,254	179.72		—	—	
	22,640,942	26.70	6.37	10,714,106	12.37	4.01

The aggregate intrinsic value represents the total pretax intrinsic value (i.e., the difference between our common stock price and the exercise price, multiplied by the number of in-the-money options) that would have been received by the option holders had all option holders exercised their options. The aggregate intrinsic value of options outstanding as of December 31, 2014 and 2013 was $4.00 billion and $2.80 billion, respectively. The intrinsic value of options exercisable was $2.46 billion and $1.48 billion, and the intrinsic value of options vested and expected to vest was $4.00 billion and $2.80 billion as of December 31, 2014 and 2013, respectively. The total intrinsic value of options exercised was $446.9 million and $294.0 million for the years ended December 31, 2014 and 2013, respectively. The aggregate intrinsic value of RSUs outstanding as of December 31, 2014 was $329.2 million.

Fair Value Adoption

We utilize the fair value method in recognizing stock-based compensation expense. Under the fair value method, we estimated the fair value of each option award and the ESPP on the grant date generally using the Black-Scholes option pricing model and the weighted average assumptions noted in the following table.

	Year Ended December 31,		
	2014	2013	2012
Risk-free interest rate:			
Stock options	1.9%	1.3 %	1.0 %
ESPP	0.1%	0.1 %	0.2 %
Expected term (in years):			
Stock options	6.0	6.1	5.9
ESPP	0.5	0.5	0.5
Expected volatility:			
Stock options	55 %	57 %	63 %
ESPP	46 %	43 %	51 %
Dividend yield:			
Stock options	0.0%	0.0 %	0.0 %
ESPP	0.0%	0.0 %	0.0 %

The risk-free interest rate that we use is based on the United States Treasury yield in effect at the time of grant for zero coupon United States Treasury notes with maturities approximating each grant's expected life. Given our limited history with employee grants, we use the "simplified" method in estimating the expected term for our employee grants. The "simplified" method, as permitted by the SEC, is calculated as the average of the time-to-vesting and the contractual life of the options.

Our expected volatility is derived from our implied volatility on publicly traded options of our common stock and the historical volatilities of several unrelated public companies within industries related to our business, including the automotive OEM, automotive retail, automotive parts and battery technology industries, because we have limited trading history on our common stock. When making the selections of our peer companies within industries related to our business to be used in the volatility calculation, we also considered the stage of development, size and financial leverage of potential comparable companies. Our historical volatility and implied volatility are weighted based on certain qualitative factors and combined to produce a single volatility factor.

The weighted-average grant-date fair value for option awards granted during the years ended December 31, 2014, 2013 and 2012 was $94.01, $40.72 and $16.37 per share, respectively. The weighted-average grant-date fair value for ESPP granted during the years ended December 31, 2014, 2013 and 2012 was $74.07, $19.22 and $8.99 per share, respectively. The fair value of RSUs is measured on the grant date based on the closing fair market value of our common stock.

Performance-Based Stock Options

In December 2009, our Board of Directors approved an option grant to our CEO representing 4% of our fully-diluted share base prior to such grant as of the grant date, or 3,355,986 stock options, with 1/4th of the shares vesting immediately, and 1/36th of the remaining shares scheduled to vest each month over three years, assuming continued employment through each vesting date in recognition of his and our company's achievements and to create incentives for future success. In addition, to create incentives for the attainment of clear performance objectives around a key element of our business plan— the successful launch and commercialization of Model S—the Board of Directors approved an additional option grant to our CEO totaling an additional 4% of our fully-diluted shares prior to such grant as of the grant date, or 3,355,986 stock options, with a vesting schedule based entirely on the attainment of performance objectives as follows, assuming our CEO's continued employment and service to us through each vesting date:

- 1/4th of the shares subject to the option are scheduled to vest upon the successful completion of Model S Engineering Prototype;
- 1/4th of the shares subject to the option are scheduled to vest upon the successful completion of Model S Validation Prototype;
- 1/4th of the shares subject to the option are scheduled to vest upon the completion of the first Model S Production Vehicle; and
- 1/4th of the shares subject to the option are scheduled to vest upon the completion of the 10,000th Model S Production Vehicle.

Through December 31, 2013, all performance milestones were achieved. Stock-based compensation expense related to this grant to our CEO was $0.4 million and $4.2 million for the years ended December 31, 2013 and 2012, respectively.

Our Board of Directors also approved option grants in June and September 2010 to purchase our common stock of 666,300 and 20,000, respectively, to various members of our senior management with a vesting schedule based entirely on the attainment of the same performance objectives as those outlined for our CEO above. Through December 31, 2013, all performance milestones were achieved. During the years ended December 31, 2013 and 2012, we recognized $0.8 million and $1.4 million, respectively, of stock-based compensation expense related to the attainment of these performance objectives.

In August 2012, our Board of Directors granted 5,274,901 stock options to our CEO (2012 CEO Grant). The 2012 CEO Grant consists of ten vesting tranches with a vesting schedule based entirely on the attainment of both performance conditions and market conditions, assuming continued employment and service to us through each vesting date.

Each of the vesting tranches requires a combination of one of the ten pre-determined performance milestones outlined below and an incremental increase in our market capitalization of $4.0 billion, as compared to the initial market capitalization of $3.2 billion measured at the time of the 2012 CEO Grant.

Successful completion of the Model X Alpha Prototype;
Successful completion of the Model X Beta Prototype;
Completion of the first Model X Production Vehicle;
Successful completion of the Model 3 Alpha Prototype;
Successful completion of the Model 3 Beta Prototype;
Completion of the first Model 3 Production Vehicle;
Gross margin of 30% or more for four consecutive quarters;
Aggregate vehicle production of 100,000 vehicles;
Aggregate vehicle production of 200,000 vehicles; and
Aggregate vehicle production of 300,000 vehicles.

The term of the 2012 CEO Grant is ten years, so any tranches that remain unvested at the expiration of the 2012 CEO Grant will be forfeited. In addition, unvested options will be forfeited if our CEO is no longer in that role, whether for cause or otherwise.

We measured the fair value of the 2012 CEO Grant using a Monte Carlo simulation approach with the following assumptions: risk-free interest rate of 1.65%, expected term of ten years, expected volatility of 55% and dividend yield of 0%.

Stock-based compensation expense associated with the 2012 CEO Grant is recognized for each pair of performance and market conditions over the longer of the expected achievement period of the performance and market conditions, beginning at the point in time that the relevant performance condition is considered probable of being met.

As of December 31, 2014, the market conditions for six vesting tranches and the following performance milestone were achieved and approved by our Board of Directors:

Successful completion of the Model X Alpha Prototype.

As of December 31, 2014, the following performance milestone was achieved and subject to our Board of Directors' approval at the upcoming board meeting:

Successful completion of the Model X Beta Prototype;

As of December 31, 2014, the following three performance milestones were considered probable of achievement:

- Completion of the first Model X Production Vehicle;
- Successful completion of the Model 3 Alpha Prototype; and
- Aggregate vehicle production of 100,000 vehicles.

As the above three performance milestones were considered probable of achievement, we recorded stock-based compensation expense of $25.0 million, $14.5 million and $1.3 million for the years ended December 31, 2014, 2013 and 2012. No cash compensation has ever been received by our CEO for his services to the company.

In January 2014, to create incentives for continued long term success beyond the Model S program and to closely align executive pay with our stockholders' interests in the achievement of significant milestones by our company, the Compensation Committee of our Board of Directors granted stock options to certain employees to purchase 782,500 shares of our common stock. Each such grant consists of four vesting tranches with a vesting schedule based entirely on the attainment of future performance milestones, assuming continued employment and service to us through each vesting date.

- 1/4th of the shares subject to the options are scheduled to vest upon completion of the first Model X Production Vehicle;
- 1/4th of the shares subject to the options are scheduled to vest upon achieving aggregate vehicle production of 100,000 vehicles in a trailing 12-month period;
- 1/4th of the shares subject to the options are scheduled to vest upon completion of the first Model 3 Production Vehicle; and
- 1/4th of the shares subject to the options are scheduled to vest upon achievement of annualized gross margin of greater than 30.0% in any three years.

As of December 31, 2014, the following performance milestone was considered probable of achievement.

- Completion of the first Model X Production Vehicle.

As the above performance milestone was considered probable of achievement, we recorded stock-based compensation expense of $10.7 million for the year ended December 31, 2014.

Summary Stock Based Compensation Information

The following table summarizes the stock-based compensation expense by line item in the consolidated statements of operations (in thousands):

	Year Ended December 31,		
	2014	2013	2012
Cost of sales	$17,454	$9,071	$2,194
Research and development	62,601	35,494	26,580
Selling, general and administrative	76,441	39,090	21,371
Total	$156,496	$83,655	$50,145

We realized no income tax benefit from stock option exercises in each of the periods presented due to recurring losses and valuation allowances.

As of December 31, 2014, we had $412.7 million of total unrecognized compensation expense, net, of estimated forfeitures, that will be recognized over a weighted-average period of 5.0 years.

Employee Stock Purchase Plan

Employees are eligible to purchase common stock through payroll deductions of up to 15% of their eligible compensation, subject to any plan limitations. The purchase price of the shares on each purchase date is equal to 85% of the lower of the fair market value of our common stock on the first and last trading days of each six-month offering period. During the years ended December 31, 2014, 2013 and 2012, 163,600, 518,743 and 373,526 shares were issued under the ESPP for $28.6 million, $13.8 million and $8.4 million, respectively. A total of 3,615,749 shares of

common stock have been reserved for issuance under the ESPP, and there were 2,336,422 shares available for issuance under the ESPP as of December 31, 2014.

9. Income Taxes

A provision for income taxes of $9.4 million, $2.6 million and $0.1 million has been recognized for the years ended December 31, 2014, 2013 and 2012, respectively, related primarily to our subsidiaries located outside of the United States. Our loss before provision for income taxes for the years ended December 31, 2014, 2013 and 2012 were as follows (in thousands):

	Year Ended December 31,		
	2014	2013	2012
Domestic	$60,451	$75,279	$396,549
International	224,185	(3,853)	(472)
Loss before income taxes	$284,636	$71,426	$396,077

The components of the provision for income taxes for the years ended December 31, 2014, 2013 and 2012, consisted of the following (in thousands):

	Year Ended December 31,		
	2014	2013	2012
Current:			
Federal	$—	$—	$—
State	257	178	23
Foreign	9,203	2,349	282
Total current	9,460	2,527	305
Deferred:			
Federal	—	—	—
State	—	—	—
Foreign	(56)	61	(169)
Total deferred	(56)	61	(169)
Total provision for income taxes	$9,404	$2,588	$136

Deferred tax assets (liabilities) as of December 31, 2014 and 2013 consisted of the following (in thousands):

	December 31, 2014	December 31, 2013
Deferred tax assets:		
Net operating loss carry-forwards	$276,916	$341,172
Research and development credits	46,486	32,175
Other tax credits	12,750	166
Deferred revenue	75,823	42,491
Inventory and warranty reserves	53,546	23,260
Depreciation and amortization	68	68
Stock-based compensation	50,918	27,663
Convertible debt	45,118	22,930
Accruals and others	49,225	21,795
Total deferred tax assets	610,850	511,720
Valuation allowance	(524,394)	(472,375)
Deferred tax assets, net of valuation allowance	86,456	39,345
Deferred tax liabilities:		
Depreciation and amortization	(86,298)	(39,244)
Total deferred tax liabilities	(86,298)	(39,244)
Deferred tax assets, net of valuation allowance and deferred tax liabilities	$158	$101

Reconciliation of statutory federal income taxes to our effective taxes for the years ended December 31, 2014, 2013 and 2012 is as follows (in thousands):

	Year Ended December 31,		
	2014	2013	2012
Tax at statutory federal rate	$(99,622)	$(25,001)	$(134,702)
State tax, net of federal benefit	257	178	(12,580)
Nondeductible expenses	15,238	733	9,897
Foreign income rate differential	86,734	(253)	262
U.S. tax credits	(26,895)	(6,682)	(2,785)
Other reconciling items	877	1,317	525
Change in valuation allowance	32,815	32,296	139,519
Provision for income taxes	$9,404	$2,588	$136

Management believes that based on the available information, it is more likely than not that the U.S. deferred tax assets will not be realized, such that a full valuation allowance is required against all U.S. deferred tax assets. The Company has net $0.3 million of deferred tax assets in foreign jurisdictions which it believes are more-likely-than-not to be fully realized given the expectation of future earnings in these jurisdictions.

As of December 31, 2014, we had approximately $1.34 billion of federal and $991.8 million of state net operating loss carry-forwards available to offset future taxable income, which will begin to expire for federal in 2024 and 2019 for state purposes. As of December 31, 2014, the portion of net operating loss carryforwards related to stock options is approximately $590.0 million and $307.6 million for federal and state purposes, respectively, of which the tax benefits will be credited to additional paid-in capital when realized. Additionally, we have research and development tax credits of approximately $33.8 million and $36.6 million for federal and state income tax purposes, respectively. If not utilized, the federal carry-forwards will expire in various amounts beginning in 2019. However, the state credits can be carried forward indefinitely.

No deferred tax liability has been recognized for the remittance of any undistributed foreign earnings to the United States since the Company has no material amount of undistributed foreign earnings outside of our U.S. tax jurisdiction as of December 31, 2014.

Federal and state laws can impose substantial restrictions on the utilization of net operating loss and tax credit carry-forwards in the event of an “ownership change,” as defined in Section 382 of the Internal Revenue Code. We determined that no significant limitation would be placed on the utilization of our net operating loss and tax credit carry-forwards due to any prior ownership changes.

Uncertain Tax Positions

The aggregate changes in the balance of our gross unrecognized tax benefits during the years ended December 31, 2014, 2013 and 2012 were as follows (in thousands):

December 31, 2011	$17,430
Increases in balances related to tax positions taken during current year	640
December 31, 2012	18,070
Decreases in balances related to prior year tax positions	(7,802)
Increases in balances related to current year tax positions	3,102
December 31, 2013	13,370
Increase in balances related to prior year tax positions	56
Increases in balances related to current year tax positions	27,951
December 31, 2014	$41,377

Accrued interest and penalties related to unrecognized tax benefits are classified as income tax expense and was immaterial. As of December 31, 2014, unrecognized tax benefits of $39.1 million, if recognized, would not affect our effective tax rate as the tax benefits would increase a deferred tax asset which is currently fully offset with a full valuation allowance. We do not anticipate that the amount of existing unrecognized tax benefits will significantly increase or decrease within the next 12 months. We file income tax returns in the United States, California, various states and foreign jurisdictions. Tax years 2003 to 2013 remain subject to examination for federal purposes, and tax years 2003 to 2013 remain subject to examination for California purposes. All net operating losses and tax credits generated to date are subject to adjustment for U.S. federal and California purposes. Tax years 2007 to 2013 remain open for examination in other U.S. state and foreign jurisdictions.

10. Information about Geographic Areas

We operate as one reportable segment which is the design, development, manufacturing and sales of electric vehicles and electric vehicle powertrain components.

The following tables set forth total revenues and long-lived assets by geographic area (in thousands).

Total Revenues

	Year Ended December 31,		
	2014	2013	2012
United States	$1,471,643	$1,479,166	$344,877
China	477,082	—	—
Norway	412,198	217,070	4,298
Other	837,433	317,260	64,081
Total	$3,198,356	$2,013,496	$413,256

Long-lived Assets

	December 31, 2014	December 31, 2013
United States	$2,452,219	$1,091,487
International	143,792	29,432
Total	$2,596,011	$1,120,919

11. Commitments and Contingencies

Operating Leases

Our corporate headquarters and powertrain production operations are based in Palo Alto, California where we have leased a facility consisting of 350,000 square feet. This lease expires in January 2020. We lease a 203,772 square feet manufacturing facility in Tilburg, Netherlands through November 2023. We also lease a number of properties in North America, Europe and Asia for our office, retail and service locations as well as Supercharger sites under non-cancelable operating leases with various expiration dates through March 2028.

Included within Operating Leases commitments in the table below are payments due under operating leases that have been accounted for as build-to-suit arrangements and are included in property, plant, and equipment in our Consolidated Balance Sheets.

Rent expense for the years ended December 31, 2014, 2013 and 2012 was $46.3 million, $21.5 million and $12.1 million, respectively.

Capital Leases

We have entered into various agreements to lease equipment under capital leases over terms between 36 and 60 months. The equipment under the leases are collateral for the lease obligations and are included within property, plant and equipment, net, on the consolidated balance sheets under the categories of computer equipment and software and office furniture and equipment.

Future minimum commitments for leases as of December 31, 2014 are as follows (in thousands):

	Operating Leases	Capital Leases
2015	$56,522	$10,153
2016	60,136	8,112
2017	56,566	3,592
2018	48,959	563
2019 and thereafter	184,600	—
Total minimum lease payments	$406,783	22,420
Less: Amounts representing interest not yet incurred		621
Present value of capital lease obligations		21,799
Less: Current portion		9,532
Long-term portion of capital lease obligations		$12,267

Environmental Liabilities

In connection with our Tesla Factory located in Fremont, California, we are obligated to pay for the remediation of certain environmental conditions existing at the time we purchased the property from New United Motor Manufacturing, Inc. (NUMMI). Tesla is responsible for the first $15 million of remediation costs and any costs in excess of $30 million or costs incurred after the ten-year anniversary of closing. NUMMI is responsible for remediation costs between $15 million and $30 million for up to 10 years from the closing date. Through December 31, 2014, we have paid $3.1 million for remediation costs incurred related to the Fremont facility. As of December 31, 2014 and 2013, we accrued a total of $4.0 million and $5.5 million related to these environmental liabilities.

Legal Proceedings

From time to time, we are subject to various legal proceedings that arise from the normal course of business activities. In addition, from time to time, third parties may assert intellectual property infringement claims against us in the form of letters and other forms of communication. If an unfavorable ruling were to occur, there exists the possibility of a material adverse impact on our results of operations, prospects, cash flows, financial position and brand.

In November 2013, a putative securities class action lawsuit was filed against Tesla in U.S. District Court, Northern District of California, alleging violations of, and seeking remedies pursuant to, Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Rule 10b-5. The complaint, made claims against Tesla and its CEO, Elon Musk, sought damages and attorney's fees on the basis of allegations that, among other things, Tesla and Mr. Musk made false and/or misleading representations and omissions, including with respect to the safety of Model S. This case was brought on behalf of a putative class consisting of certain persons who purchased Tesla's securities between August 19, 2013 and November 17, 2013. On September 26, 2014, the trial court, upon the motion of Tesla and Mr. Musk, dismissed the complaint with prejudice, and indicated that a formal written order will be forthcoming. Following the trial court's decision, Tesla and Mr. Musk brought a motion for sanctions against the plaintiffs, and that motion is currently pending. The plaintiffs have also appealed from the trial court's order, and that appeal is pending, as well.

12. Quarterly Results of Operations (Unaudited)

The following table includes selected quarterly results of operations data for the years ended December 31, 2014 and 2013 (in thousands, except per share data):

	Three months ended			
	March 31	June 30	September 30	December 31
2014				
Total revenues	$620,542	$769,349	$851,804	$956,661
Gross profit	155,128	212,995	251,851	261,697
Net loss	(49,800)	(61,902)	(74,708)	(107,630)
Net loss per share, basic	(0.40)	(0.50)	(0.60)	(0.86)
Net income (loss) per share, diluted	(0.40)	(0.50)	(0.60)	(0.86)
2013				
Total revenues	$561,792	$405,139	$431,346	$615,219
Gross profit	96,320	100,483	102,868	156,590
Net income (loss)	11,248	(30,502)	(38,496)	(16,264)
Net income (loss) per share, basic	0.10	(0.26)	(0.32)	(0.13)
Net income (loss) per share, diluted	0.00	(0.26)	(0.32)	(0.13)

Net loss per share, basic and diluted for the four quarters of each fiscal year may not sum to the total for the fiscal year because of the different numbers of shares outstanding during each period.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

Not applicable.

ITEM 9A. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We conducted an evaluation as of December 31, 2014, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as of December 31, 2014, our disclosure controls and procedures were effective to provide reasonable assurance.

Management’s Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is a process designed by, or under the supervision of, our Chief Executive Officer and Chief Financial Officer to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that (1) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of our assets; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with authorizations of our management and directors; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on the financial statements.

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on criteria established in “Internal Control—Integrated Framework (2013)” issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Our management concluded that our internal control over financial reporting was effective as of December 31, 2014.

Our independent registered public accounting firm, PricewaterhouseCoopers LLP, has audited the effectiveness of our internal control over financial reporting as of December 31, 2014 as stated in their report which is included herein.

Limitations on the Effectiveness of Controls

Because of inherent limitations, internal control over financial reporting may not prevent or detect misstatements and projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Changes in Internal Control over Financial Reporting

There was no change in our internal control over financial reporting which occurred during the fourth fiscal quarter of the year ended December 31, 2014 which has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

ITEM 9B. OTHER INFORMATION

None

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The information required by this Item 10 of Form 10-K will be included in our 2015 Proxy Statement to be filed with the SEC in connection with the solicitation of proxies for our 2015 Annual Meeting of Stockholders (2015 Proxy Statement) and is incorporated herein by reference. The 2015 Proxy Statement will be filed with the SEC within 120 days after the end of the fiscal year to which this report relates.

ITEM 11. EXECUTIVE COMPENSATION

The information required by this Item 11 of Form 10-K will be included in our 2015 Proxy Statement and is incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information required by this Item 12 of Form 10-K will be included in our 2015 Proxy Statement and is incorporated herein by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

The information required by this Item 13 of Form 10-K will be included in our 2015 Proxy Statement and is incorporated herein by reference.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The information required by this Item 14 of Form 10-K will be included in our 2015 Proxy Statement and is incorporated herein by reference.

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

1. Financial Statements. See “Index to Consolidated Financial Statements” in Part II, Item 8 of this Annual Report on Form 10-K.
2. All financial statement schedules have been omitted, since the required information is not applicable or is not present in amounts sufficient to require submission of the schedule, or because the information required is included in the consolidated financial statements and notes thereto.
3. Exhibits. The exhibits listed in the accompanying “Index to Exhibits” are filed or incorporated by reference as part of this Annual Report on Form 10-K.

INDEX TO EXHIBITS

Exhibit Number	Exhibit Description	Incorporated by Reference Form	File No.	Exhibit	Filing Date	Filed Herewith
3.1	Amended and Restated Certificate of Incorporation of the Registrant	S-1	333-164593	3.1	January 29, 2010	
3.2	Amended and Restated Bylaws of the Registrant	8-K	333-164593	3.2	June 8, 2012	
				4.1	May 27, 2010	
4.1	Specimen common stock certificate of the Registrant	S-1/A	333-164593			
4.2	Fifth Amended and Restated Investors' Rights Agreement, dated as of August 31, 2009, between Registrant and certain holders of the Registrant's capital stock named therein	S-1	333-164593	4.2	January 29, 2010	
4.2A	Amendment to Fifth Amended and Restated Investors' Rights Agreement, dated as of May 20, 2010, between Registrant and certain holders of the Registrant's capital stock named therein	S-1/A	333-164593	4.2A	May 27, 2010	
4.2B	Amendment to Fifth Amended and Restated Investors' Rights Agreement between Registrant, Toyota Motor Corporation and certain holders of the Registrant's capital stock named therein	S-1/A	333-164593	4.2B	May 27, 2010	
4.2C	Amendment to Fifth Amended and Restated Investor's Rights Agreement, dated as of June 14, 2010, between Registrant and certain holders of the Registrant's capital stock named therein	S-1/A	333-164593	4.2C	June 15, 2010	
4.2D		8-K	001-34756	4.1		

	Amendment to Fifth Amended and Restated Investor's Rights Agreement, dated as of November 2, 2010, between Registrant and certain holders of the Registrant's capital stock named therein				November 4, 2010
4.2E	Waiver to Fifth Amended and Restated Investor's Rights Agreement, dated as of May 25, 2011, between Registrant and certain holders of the Registrant's capital stock named therein	S-1/A	333-174466	4.2E	June 2, 2011
4.2F	Amendment to Fifth Amended and Restated Investor's Rights Agreement, dated as of May 30, 2011, between Registrant and certain holders of the Registrant's capital stock named therein	8-K	001-34756	4.1	June 1, 2011
4.2G	Sixth Amendment to Fifth Amended and Restated Investors' Rights Agreement, dated as of May 15, 2013 among the Registrant, the Elon Musk Revocable Trust dated July 22, 2003 and certain other holders of the capital stock of the Registrant named therein.	8-K	001-34756	4.1	May 20, 2013

Exhibit Number	Exhibit Description	Incorporated by Reference Form	File No.	Exhibit	Filing Date	Filed Herewith
4.2H	Waiver to Fifth Amended and Restated Investor's Rights Agreement, dated as of May 14, 2013, between the Registrant and certain holders of the capital stock of the Registrant named therein.	8-K	001-34756	4.2	May 20, 2013	
4.3	Indenture, dated as of May 22, 2013, by and between the Registrant and U.S. Bank National Association.	8-K	001-34756	4.1	May 22, 2013	
4.4	First Supplemental Indenture, dated as of May 22, 2013, by and between the Registrant and U.S. Bank National Association.	8-K	001-34756	4.2	May 22, 2013	
4.5	Form of 1.50% Convertible Senior Note Due June 1, 2018 (included in Exhibit 4.4).	8-K	001-34756	4.3	May 22, 2013	
4.6	Second Supplemental Indenture, dated as of March 5, 2014, by and between the Registrant and U.S. Bank National Association.	8-K	001-34756	4.2	March 5, 2014	
4.7	Form of 0.25% Convertible Senior Note Due March 1, 2019 (included in Exhibit 4.6).	8-K	001-34756	4.3	March 5, 2014	
4.8	Third Supplemental Indenture, dated as of March 5, 2014, by and between the Registrant and U.S. Bank National Association.	8-K	001-34756	4.4	March 5, 2014	
4.9	Form of 1.25% Convertible Senior Note Due March 1, 2021 (included in Exhibit 4.8).	8-K	001-34756	4.5	March 5, 2014	
10.1**	Form of Indemnification Agreement between the Registrant and its directors and officers	S-1/A	333-164593	10.1	June 15, 2010	
10.2**	2003 Equity Incentive Plan	S-1/A	333-164593	10.2		

					May 27, 2010
10.3**	Form of Stock Option Agreement under 2003 Equity Incentive Plan	S-1	333-164593	10.3	January 29, 2010
10.3A**	Grant Notice and Stock Option Agreement between the Registrant and Elon Musk	S-1/A	333-164593	10.3A	March 29, 2010
10.4**	Amended and Restated 2010 Equity Incentive Plan, effective as of April 10, 2014	14A	333-164593	Appendix A	April 24, 2014
10.5**	Form of Stock Option Agreement under 2010 Equity Incentive Plan	S-1/A	333-164593	10.5	March 29, 2010
10.6**	Form of Restricted Stock Unit Award Agreement under 2010 Equity Incentive Plan	S-1/A	333-164593	10.6	March 29, 2010

Exhibit Number	Exhibit Description	Incorporated by Reference Form	File No.	Exhibit	Filing Date	Filed Herewith
10.7**	2010 Employee Stock Purchase Plan	S-1/A	333-164593	10.7	May 27, 2010	
10.8**	Form of Purchase Agreement under 2010 Employee Stock Purchase Plan	S-1/A	333-164593	10.8	June 15, 2010	
10.9**	Offer Letter between the Registrant and Elon Musk dated October 13, 2008	S-1	333-164593	10.9	January 29, 2010	
10.10**	Offer Letter between the Registrant and Deepak Ahuja dated June 13, 2008, and amended June 4, 2009	S-1	333-164593	10.10	January 29, 2010	
10.11**	Relocation Agreement between the Registrant and Deepak Ahuja effective October 31, 2008 and amended June 4, 2009	S-1	333-164593	10.11	January 29, 2010	
10.12**	Offer Letter between the Registrant and Jeffrey B. Straubel dated May 6, 2004	S-1	333-164593	10.12	January 29, 2010	
10.13	Commercial Lease between the Registrant and The Board of Trustees of The Leland Stanford Jr. University dated August 6, 2009	S-1	333-164593	10.22	January 29, 2010	
10.14†	ZEV Credits Agreement between American Honda Motor Co., Inc. and the Registrant dated February 12, 2009	S-1/A	333-164593	10.32	May 27, 2010	
10.14A	Addendum to ZEV Credits Agreement between American Honda Motor Co., Inc. and the Registrant dated February 20, 2009	S-1/A	333-164593	10.32A	May 27, 2010	
10.14B†	Supplemental ZEV Credits Agreement between American Honda Motor Co., Inc. and the Registrant dated March 20, 2009	S-1/A	333-164593	10.32B	May 27, 2010	

10.14C†	Second Supplemental ZEV Credits Agreement between American Honda Motor Co., Inc. and the Registrant dated February 8, 2010	S-1/A	333-164593	10.32C	May 27, 2010
10.15†	Supply Agreement by and among Panasonic Industrial Company, Panasonic Corporation, acting through Energy Company, and the Registrant dated July 21, 2009	S-1	333-164593	10.33	January 29, 2010
10.16	Settlement Agreement between the Registrant and entities affiliated with Valor Equity Partners dated May 20, 2010	S-1/A	333-164593	10.44	May 27, 2010
10.17	Letter Agreement between the Registrant and New United Motor Manufacturing, Inc. dated May 26, 2010	S-1/A	333-164593	10.45	May 27, 2010
10.17A	Amendment No. 1 to the Letter Agreement between the Registrant and New United Motor Manufacturing, Inc. dated June 15, 2010	10-Q	001-34756	10.3	November 12, 2010
10.17B	Amendment No. 2 to the Letter Agreement between the Registrant and New United Motor Manufacturing, Inc. dated October 1, 2010	10-Q	001-34756	10.4	November 12, 2010

Exhibit Number	Exhibit Description	Incorporated by Reference Form	File No.	Exhibit	Filing Date	Filed Herewith
10.17C	Amendment No. 3 to the Letter Agreement between the Registrant and New United Motor Manufacturing, Inc. dated October 8, 2010	10-Q	001-34756	10.5	November 12, 2010	
10.17D	Amendment No. 4 to the Letter Agreement between the Registrant and New United Motor Manufacturing, Inc. dated October 13, 2010	10-Q	001-34756	10.6	November 12, 2010	
10.17E	Amendment No. 5 to the Letter Agreement between the Registrant and New United Motor Manufacturing, Inc. dated October 15, 2010	10-Q	001-34756	10.7	November 12, 2010	
10.17F†	Amendment No. 6 to the Letter Agreement between the Registrant and New United Motor Manufacturing, Inc. dated October 19, 2010	10-Q	001-34756	10.8	November 12, 2010	
10.18	Sale and Purchase Agreement between Registrant and New United Motor Manufacturing, Inc., dated August 13, 2010	10-Q	001-34756	10.1	November 12, 2010	
10.18A	Addendum No. 1to the Sale and Purchase Agreement between Registrant and New United Motor Manufacturing, Inc., dated September 23, 2010	10-Q	001-34756	10.2	November 12, 2010	
10.19†	Phase 1 Contract Services Agreement between Registrant and Toyota Motor Corporation dated October 6, 2010	10-K	001-34756	10.47	March 3, 2011	
10.20†	Supply and Services Agreement between Toyota Motor Engineering & Manufacturing North America, Inc. and the Registrant dated July 15, 2011	10-Q	001-34756	10.1	November 14, 2011	
10.21†	Supply Agreement between Panasonic Corporation and the Registrant dated October 5, 2011	10-K	-001-34756	10.50	February 27, 2012	

10.21A†	Amendment No. 1 to Supply Agreement between Panasonic Corporation and the Registrant dated October 29, 2013	10-K	001-34756	10.35A	February 26, 2014
10.22	Form of Call Option Confirmation relating to 1.50% Convertible Senior Note Due June 1, 2018.	8-K	001-34756	10.1	May 22, 2013
10.23	Form of Warrant Confirmation relating to 1.50% Convertible Senior Note Due June 1, 2018.	8-K	001-34756	10.2	May 22, 2013
10.24	Indemnification Agreement, dated as of February 27, 2014, by and between the Registrant and J.P. Morgan Securities LLC.	8-K	001-34756	10.1	March 5, 2014
10.25	Form of Call Option Confirmation relating to 0.25% Convertible Senior Notes Due March 1, 2019.	8-K	001-34756	10.2	March 5, 2014

Exhibit Number	Exhibit Description	Incorporated by Reference Form	File No.	Exhibit	Filing Date	Filed Herewith
10.26	Form of Call Option Confirmation relating to 1.25% Convertible Senior Notes Due March 1, 2021.	8-K	001-34756	10.3	March 5, 2014	
10.27	Form of Warrant Confirmation relating to 0.25% Convertible Senior Notes Due March 1, 2019.	8-K	001-34756	10.4	March 5, 2014	
10.28	Form of Warrant Confirmation relating to 1.25% Convertible Senior Notes Due March 1, 2021.	8-K	001-34756	10.5	March 5, 2014	
10.29	Agreement between Panasonic Corporation and the Registrant dated July 31, 2014.	10-Q	001-34756	10.1	November 7, 2014	
10.30 †	General Terms and Conditions between Panasonic Corporation and the Registrant dated October 1, 2014.	10-Q	001-34756	10.2	November 7, 2014	
10.31 †	Production Pricing Agreement between Panasonic Corporation and the Registrant dated October 1, 2014.	10-Q	001-34756	10.3	November 7, 2014	
10.32 †	Investment Letter Agreement between Panasonic Corporation and the Registrant dated October 1, 2014.	10-Q	001-34756	10.4	November 7, 2014	
12.1	Statement regarding Computation of Ratio of Earnings to Fixed Charges	—	—	—	—	X
23.1	Consent of PricewaterhouseCoopers, Independent Registered Public Accounting Firm	—	—	—	—	X
31.1	Rule 13a-14(a) / 15(d)-14(a) Certification of Principal Executive Officer	—	—	—	—	X
31.2						

	Rule 13a-14(a) / 15(d)-14(a) Certification of Principal Financial Officer	—	—	—	—
32.1*	Section 1350 Certifications				
101.INS	XBRL Instance Document				
101.SCH	XBRL Taxonomy Extension Schema Document				
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.				
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document				
101.LAB	XBRL Taxonomy Extension Label Linkbase Document				
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document				

*Furnished herewith

**Indicates a management contract or compensatory plan or arrangement.

†Confidential treatment has been requested for portions of this exhibit

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

Tesla Motors, Inc.

Date: February 26, 2015 /s/ Elon Musk
Elon Musk
Chief Executive Officer
(Principal Executive Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
/s/ Elon Musk Elon Musk	Chief Executive Officer and Director (Principal Executive Officer)	February 26, 2015
/s/ Deepak Ahuja Deepak Ahuja	Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)	February 26, 2015
/s/ Brad Buss Brad Buss	Director	February 26, 2015
/s/ Robyn Denholm Robyn Denholm	Director	February 26, 2015
/s/ Ira Ehrenpreis Ira Ehrenpreis	Director	February 26, 2015
/s/ Antonio Gracias Antonio Gracias	Director	February 26, 2015
/s/ Stephen Jurvetson Stephen Jurvetson	Director	February 26, 2015
/s/ Kimbal Musk Kimbal Musk	Director	February 26, 2015