SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)
[x] Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended June 30, 1998
[ ] 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: 000-23329

C3, Inc.

(Exact name of Registrant as specified in its charter)

North Carolina	56-1928817
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

3800 Gateway Boulevard, 310, Morrisville, N.C. 27560

(Address of principal executive offices)

919-468-0399

Registrant's telephone number, including area code

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes X No _

As of August 7, 1998 there were 6,942,166 shares of the Registrant's Common Stock, no par value per share, outstanding.

C3, Inc.
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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

C3, Inc.
(A Company In The Development Stage)
Condensed Balance Sheets

	June 30, 1998	December 31, 1997
	(Unaudited)	
ASSETS		
Current Assets:		
Cash and equivalents	$ 39,070,181	$ 43,980,385
Accounts receivable, net	126,649	4,298
Interest receivable	144,936	177,654
Inventories	1,298,470	278,602
Prepaid expenses and other assets	329,076	73,274
Total current assets	40,969,312	44,514,213
Equipment, net	2,296,034	214,990
Patent and license rights, net	201,489	143,886
Total assets	$ 43,466,835	$ 44,873,089
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable:		
Cree Research, Inc.	$ 2,444,832	$ 567,110
Other	474,478	237,186
Accrued expenses	192,090	
Deferred revenue	33,224	22,512

Total current liabilities	3,144,624	826,808
Commitments and Contingencies		
Shareholders' Equity:		
Common stock	47,785,931	47,743,431
Additional paid-in capital - stock options	1,737,082	1,632,804
Deficit accumulated during the development stage	(9,200,802)	(5,329,954)
Total shareholders' equity	40,322,211	44,046,281
Total liabilities and shareholders' equity	$ 43,466,835	$ 44,873,089

See notes to Condensed Financial Statements

C3, Inc.
(A Company In The Development Stage)
Condensed Statements Of Operations
(Unaudited)

	Three Months Ended June 30, 1998	Three Months Ended June 30, 1997	Six Months Ended June 30, 1998	Six Months Ended June 30, 1997	Cumulative For the Period June 28, 1995 to June 30, 1998
Net sales	$ 202,010	$ --	$ 452,565	$ --	$ 452,565
Cost of goods	135,476	--	290,552	--	290,552
Gross profit	66,534	--	162,013	--	162,013
Operating expenses:					
Marketing and sales	512,863	24,904	1,273,999	46,611	1,866,660
General and administrative	686,456	135,371	1,298,287	316,154	4,158,152
Research and development	1,088,331	251,307	2,410,843	452,571	4,764,004
Depreciation and amortization	28,418	4,095	43,917	6,649	74,487
Operating loss	(2,249,534)	(415,677)	(4,865,033)	(821,985)	(10,701,290)
Interest income, net	473,690	79,957	994,185	113,376	1,500,488
Net loss	$ (1,775,844)	$ (335,720)	$ (3,870,848)	$ (708,609)	$ (9,200,802)

Basic and diluted net loss per share	$ (0.26)	$ (0.15)	$ (0.56)	$ (0.31)	$ (3.00)
Weighted-average common shares, basic and diluted	6,941,315	2,261,102	6,939,904	2,261,102	3,068,197

See notes to Condensed Financial Statements.

C3, Inc.
(A Company In The Development Stage)
Condensed Statements Of Cash Flows
(Unaudited)

	Six Months Ended June 30, 1998	Six Months Ended June 30, 1997	Cumulative For The Period June 28, 1995 to June 30, 1998
OPERATING ACTIVITIES:			
Net loss	$(3,870,848)	$(708,609)	$ (9,200,802)
Adjustments:			
Depreciation and amortization	43,917	6,648	74,487
Compensation expense related to stock options	146,778	66,000	1,845,582
Change in operating assets and liabilities:			
Net change in assets	(1,365,303)	7,000	(1,899,131)
Net change in liabilities	485,078	97,019	1,311,886
Net cash used by operating activities	(4,560,378)	(531,942)	(7,867,978)
INVESTING ACTIVITIES:			
Purchase of equipment	(286,492)	(44,842)	(524,102)
Patent costs	(63,334)	(33,951)	(215,170)
Net cash used by investing activities	(349,826)	(78,793)	(739,272)
FINANCING ACTIVITIES:			
Proceeds from common stock offerings, net of costs	----	----	42,102,785
Proceeds from preferred stock offerings, net of costs	----	4,981,376	5,574,646
Net cash provided by financing activities	----	4,981,376	47,677,431
Net change in cash and equivalents	(4,910,204)	4,370,641	39,070,181
Cash and equivalents, beginning of period	43,980,385	1,167,458	----
Cash and equivalents, end of period	$39,070,181	$5,538,099	$39,070,181

See notes to Condensed Financial Statements.

C3, Inc.
(A Company In The Development Stage)
Notes To Condensed Financial Statements
(Unaudited)

1. BASIS OF PRESENTATION

The accompanying unaudited financial statements have been prepared in conformity with generally accepted accounting principles. However, certain information or footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed, or omitted, pursuant to the rules and regulations of the Securities and Exchange Commission. In the opinion of management, the financial statements include all normal recurring adjustments which are necessary for the fair presentation of the results of the interim periods presented. Interim results are not necessarily indicative of results for the fiscal year. Certain reclassifications have been made to prior year's financial statements to conform to the classifications used in fiscal 1998. These financial statements should be read in conjunction with the Company's audited financial statements for the year ended December 31, 1997, as set forth in the Company's Form 10-K, filed with the Securities and Exchange Commission on March 31, 1998.

Prior to July 1, 1998 C3, Inc. was a development stage company which devoted substantially all of its efforts to research and product development and development of its initial markets and did not, through June 30, 1998, generate significant revenues from its planned principal operations.

In preparing financial statements that conform with generally accepted accounting principles, management must make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and amounts of revenues and expenses reflected during the reporting period.
Actual results could differ from those estimates.

2. INVENTORIES

Inventories are stated at the lower of cost or market. Inventories consisted of the following:

	June 30, 1998	December 31, 1997
Raw materials	$ 84,641	-----
Work in process	281,739	$ 278,602
Finished goods	932,090	----
Total inventory	$1,298,470	$ 278,602

3. NON-CASH OPERATING EXPENSES

During the quarter ended June 30, 1998, in accordance with Accounting Principals Board Opinion No. 25, the Company recorded compensation expense of approximately $96,000 relating to stock options. Cumulatively for the period from June 28, 1995 (date of inception) to June 30, 1998, such compensation expense aggregated approximately $1,846,000. This compensation expense is recorded in general and administrative expense in the statements of operations.

4. NEWLY ISSUED ACCOUNTING PRONOUNCEMENTS

In June 1997, Statement of Financial Accounting Standards No. 130 ("FAS 130"), Comprehensive Income, was issued. This Statement establishes standards for reporting and display of comprehensive income and its components (revenues, expenses, gains and losses) in a full set of general-purpose financial statements. FAS 130 is effective for fiscal years beginning after December 15, 1997. Reclassification of financial statements for earlier periods is required. However, this Statement does not currently affect the Company's financial statements since it has no items of other comprehensive income in any period presented.

5. SUBSEQUENT EVENT

In July 1998, the Company entered into an Amended and Restated Development Agreement (the "Agreement") with its exclusive supplier, Cree Research, Inc. (Cree), which is focused on increasing the yield of usable material in each silicon carbide crystal manufactured by Cree for use by C3 in the production of lab-created moissanite gemstones. The companies have agreed on the definition of a "repeatable process" in the KLMN comparable diamond color range. In June 1998 Cree demonstrated its ability to meet that definition for 2-inch diameter crystals and has now begun to produce 2-inch crystals using that process. The Agreement establishes performance milestones for 1999 and contemplates that the Company and Cree will revise the performance milestones annually to provide both parties with more flexibility to pursue further color and yield improvements on both 2-inch and 3-inch diameter crystals. The 4-year Agreement replaces the June 1997 Development Agreement and the 1998 Supplemental Development Agreement between the parties and requires the Company to fund the program at $2.88 million annually. Either party may terminate the Agreement if Cree does not meet the annual performance milestones or if the Company and Cree do not mutually agree on the performance milestones for the ensuing year.

ITEM 2: MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 that relate to the Company's future plans, objectives, estimates and goals. These statements are subject to numerous risks and uncertainties, including macro and micro economic factors that affect businesses operating in the international economy, the Company's reliance on Cree Research, Inc. as a developer and supplier of silicon carbide crystals, the level of growth in domestic and international gemstone jewelry markets, the level of market acceptance of and demand for the Company's products, and the actions of existing and potential competitors. These and other risks and uncertainties are described under the heading "Business Risks" in the Company's Form 10-K for the year ended December 31, 1997, which was filed with the Securities and Exchange Commission on March 31, 1998. These risks and uncertainties could cause actual results and developments to be materially different from those expressed or implied by any of the forward-looking statements included herein.

OVERVIEW

Since its organization in June 1995, the Company has devoted its resources to funding research and development of colorless lab-created moissanite gemstones, market research, qualifying potential domestic retail jewelers and potential international distributors, developing consumer marketing campaigns and assembling a management team. The company has achieved significant objectives in each of these areas and has begun the market introduction of its lab-created moissanite gemstones. See "Item 5: Additional Information" for more detailed information on the Company's present distribution arrangements. The Company's lab-created moissanite gemstones are being marketed as an exclusive, new gemstone with properties, including brilliance, fire and hardness that rival diamonds, sapphires, emeralds and other fine gemstones. Nonetheless, the Company remains subject to the risks inherent in establishing a new business, including the risk that full-scale operations will not occur.

Based on progress in gemstone development and distribution arrangements, the Company has determined that as of July 1, 1998 it is no longer a development stage company for financial reporting purposes. As a result, future gemstone sales will be reported as sales in the operating statement rather than being netted against research and development expenses, as was the case for the first two quarters of 1998.

Building on the initial shipment of lab-created moissanite gemstones to retailers in Miami/Ft. Lauderdale and Atlanta during the second quarter of 1998, and the July 1998 launch of consumer-focused advertising and promotion activities in those areas, the Company will focus on the market introduction of its lab-created moissanite gemstones throughout the Southeastern states of North Carolina, South Carolina, Georgia and Florida for the remainder of 1998. The Company anticipates increased advertising campaigns and additional distribution arrangements in this region. The Company will continue limited distribution and promotional activities in domestic locations outside this region and will continue its international distribution efforts.

The Company expects its sales volumes to increase gradually as it increases production capacity and as the market introduction expands geographically. During this period the Company will incur increasing spending levels as it makes investments in receivables, inventory and manufacturing equipment, and as it increases advertising, marketing and manufacturing personnel expenditures. The Company expects to continue operating at a loss through at least the balance of 1998. Moreover, there can be no assurance

that the Company will ever achieve profitability or that if profitability is achieved, that such profitability can be sustained.

RESULTS OF OPERATIONS

THREE MONTHS ENDED JUNE 30, 1998 COMPARED WITH THREE MONTHS ENDED JUNE 30, 1997.

Net sales for the quarter ended June 30, 1998, were $202,010, which resulted entirely from sales of the Company's proprietary test instrument. In addition, the Company generated net sales of approximately $243,000 for gemstones, which have been netted against research and development expenses on the operating statement, because many of the gemstones were associated with the Company's research and development program. There were no sales for the second quarter of 1997.

Gross profit was $66,534 or 33% of net sales for the quarter ended June 30, 1998. Gross profit related entirely to sales of the Company's proprietary test instrument. These margins decreased slightly from the first quarter of 1998 due to the Company entering into volume distribution agreements for its testers. Gross margins will likely decrease through the remainder of 1998 as the Company enters into additional volume distribution agreements for testers, as it potentially experiences pricing pressures on its testers from the introduction of competitive test instruments, and as it increases sales of its moissanite gemstones which will have a lower initial gross margin as the Company and Cree work to improve yields from the crystal growth process.

Research and development expenses increased from $251,307 for the three months ended June 30, 1997 to $1,088,331 for the three months ended June 30, 1998. The increase was primarily attributable to development expenses incurred under the Company's June 1997 Development Agreement and January 1998 Supplemental Development Agreement with Cree Research, Inc. under which Cree has pursued development of a fully repeatable process for producing larger diameter SiC crystals in specified comparable diamond color grades. The increase was also due to increased expenditures for the Company's internal development of prototype gemstone pre-forming and faceting operations and compensation expense for Company research and development staff.

Marketing and sales expenses increased from $24,904 for the three months ended June 30, 1997 to $512,863 for the three months ended June 30, 1998. The increase was primarily due to compensation expense associated with the expansion of the Company's sales staff, increased market research expenditures, and the development of consumer advertising campaigns and marketing materials.

General and administrative expenses rose from $135,371 for the three months ended June 30, 1997 to $686,456 for the three months ended June 30, 1998. The increase primarily reflected compensation and other expenses related to additional staff, occupancy expenses, regulatory expenses, and investor relations.

Net interest income increased from $79,957 for the three months ended June 30, 1997 to $473,690 for the three months ended June 30, 1998. This increase resulted from higher interest income earned on higher cash balances due primarily to the investment of proceeds from the Company's initial public offering in November 1997.

SIX MONTHS ENDED JUNE 30, 1998 COMPARED WITH SIX MONTHS ENDED JUNE 30, 1997.

Net sales for the six months ended June 30, 1998, were $452,565, which resulted entirely from sales of the Company's proprietary test instrument. In addition, the Company generated net sales of approximately $324,000 for gemstones, which have been netted against research and development expenses on the operating statement, because many of the gemstones were associated with the Company's research and development program. There were no sales for the six months ended June 30, 1997.

Gross profit was $162,013 or 36% of net sales for the six months ended June 30, 1998. Gross profit related entirely to sales of the Company's proprietary test instrument. Gross margins will likely decrease through the remainder of 1998 as the Company enters into additional volume distribution agreements for its testers, as it potentially experiences pricing pressures on its testers from the introduction of competitive test instruments, and as it introduces its gemstones which will have a lower initial gross margin as the Company and Cree Research, Inc. work to improve yields from the crystal growth process.

Research and development expenses increased from $452,571 for the six months ended June 30, 1997 to $2,410,843 for the six months ended June 30, 1998. The increase was primarily attributable to development expenses incurred under the Company's June 1997 Development Agreement and January 1998 Supplemental Development Agreement with Cree Research, Inc. under which Cree has pursued development of a fully repeatable process for producing larger diameter SiC crystals in specified comparable diamond color grades. The increase was also due to increased expenditures for the Company's internal development of prototype gemstone pre-forming and faceting operations and compensation expense for Company research and development staff.

Marketing and sales expenses increased from $46,611 for the six months ended June 30, 1997 to $1,273,999 for the six months ended June 30, 1998. The increase was primarily due to compensation and travel expense, increased market research expenditures, development of consumer advertising campaigns, and jewelry industry focused advertising activities.

General and administrative expenses rose from $316,154 for the six months ended June 30, 1997 to $1,298,287 for the six months ended June 30, 1998. The increase primarily reflected compensation expense of additional staff, occupancy expenses, regulatory and investor relations, and franchise tax. In the first half of 1997, the Company had few paid employees.

Net interest income increased from $113,376 for the six months ended June 30, 1997 to $994,185 for the six months ended June 30, 1998. This increase resulted from higher interest income earned on higher cash balances due primarily to the investment of proceeds from the Company's initial public offering in November 1997.

LIQUIDITY AND CAPITAL RESOURCES

The Company has financed its operations primarily from the net proceeds of its initial public offering of common stock in November 1997 and, prior to such offering, from the net proceeds of private equity sales. The net proceeds from the initial public offering were $41,072,982. During the second quarter of 1998, the Company used $2,439,596 to fund operations and $213,166 to fund capital expenditures and patent expenses. At June 30, 1998, the Company had approximately $39 million of cash and equivalents and approximately $37.8 million of working capital. The Company anticipates that its existing capital resources will be adequate to satisfy its capital requirements for at least the next 12 months.

Due to developments in the Company's business, several balance sheet items changed during the quarter. Accounts receivable and inventories have increased significantly over December 1997 levels due to the introduction of moissanite gemstones and the moissanite/diamond test instrument. In addition, accrued expenses increased over fiscal year-end levels primarily as a result of payroll and benefit expenses.

In May 1998, the Company agreed to acquire approximately $3.4 million of crystal growth systems from Cree to provide additional production capacity for silicon carbide crystals. The Company will pay the purchase price of the systems on a monthly basis as the systems are manufactured. Once completed, the systems will remain at Cree where Cree will use them to produce SiC crystals for the Company. When the systems are fully depreciated, the Company is obligated to transfer title to Cree. The first of these systems will come on-line during August 1998 with the balance coming on line through the remainder of 1998. The Company intends to fund the purchase of these systems from its existing cash and equivalents.

In July 1998, the Company entered into an Amended and Restated Development Agreement (the "Agreement") with Cree whereby Cree is focusing its development efforts on increasing the yield of usable material in each silicon carbide crystal manufactured for use in producing moissanite gemstones. See Note 5 of the Condensed Financial Statements and Item 5 of Part II of this Quarterly Report. Under the Agreement, the Company is required to fund the development program at $2.88 million annually as long as Cree meets certain performance milestones. The Company has also entered into a number of agreements with specialty retail jewelry stores in the United States and with international distributors. See Item 5 of Part II of this Quarterly Report. To support this expansion of its distribution network, the Company has begun to build an inventory of moissanite gemstones and intends to significantly increase its advertising and marketing expenditures. The Company intends to fund these development activities, inventories and advertising and marketing expenditures from its existing cash and equivalents.

PART II - OTHER INFORMATION

ITEM 2: CHANGES IN SECURITIES AND USE OF PROCEEDS

On November 14, 1997, the Securities and Exchange Commission declared the Company's Registration Statement on Form S-1 (File No. 333-36809) to be effective. The net proceeds of this offering were $41,072,982. As of June 30, 1998, the Company had approximately $34,165,800 of the remaining net proceeds of the offering invested in money market accounts, debt instruments having an original maturity of three months or less and other highly liquid investments. Approximately $3,200,800 of the proceeds have been used in research and development, of which $91,200 was paid to officers, directors or shareholders owning more than ten percent of the Common Stock outstanding. The Company has also used approximately $2,279,900 to fund sales, marketing and administrative expenses, of which $116,000 was paid to officers, directors or shareholders owning more than ten percent of the Common Stock outstanding. The Company also expended approximately $1,090,100 to build inventory of its products. In addition, the Company spent $336,400 to acquire and install certain computerized wafering and preform development equipment and other equipment.

ITEM 4: SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

The Annual Meeting of Shareholders of C3, Inc. was held on June 23, 1998. At the meeting, the shareholders voted on the election of directors and the selection of independent auditors. The following eight nominees were elected to the Board of Directors: Jeff N. Hunter, Kurt Leutzinger, Kurt Nassau, Howard Rubin, Frederick A. Russ, Ollin B. Sykes, Richard G. Hartigan, Jr., and Joel N. Levy. Additionally, the appointment of Deloitte & Touche LLP as independent auditors for the Company for the fiscal year ending December 31, 1998 was ratified. The number of votes cast for, against or withheld, as well as the number of abstentions, for each proposal are as follows:

A. Election of Directors

	Votes	Votes

Director Nominee	For	Withheld
Jeff N. Hunter	4,021,545	14,000
Kurt Leutzinger	3,892,168	143,377
Kurt Nassau	4,018,545	17,000
Howard Rubin	4,021,545	14,000
Frederick A. Russ	4,021,545	14,000
Ollin B. Sykes	4,014,545	21,000
Richard G. Hartigan, Jr.	4,014,545	21,000
Joel N. Levy	4,021,545	14,000

B. Ratification of Deloitte & Touche LLP as auditors for fiscal year ending December 31, 1998

	Votes For	Votes Against	Abstentions
Ratification of Deloitte & Touche LLP	4,021,718	2,200	11,627

ITEM 5: OTHER INFORMATION

In June 1998, the Company announced two key management additions. Robert Thomas was appointed President and Chief Operating Officer and Dr. Mark Kellam was appointed Director of Technology. Mr. Thomas has more than 20 years of company operating experience, most recently with Morven Partners, one of the nations largest processors and distributors of raw and processed edible nuts. Dr. Kellam has more than 15 years of experience in semi-conductor manufacturing technology and specializes in optical properties of materials like silicon carbide.

The Company has entered into a number of agreements with specialty retail jewelry stores in its initial launch cities of Miami/Fort Lauderdale, Florida and Atlanta, Georgia as well as certain other locations in the United States. The initial consumer launch activities in Miami/Fort Lauderdale and Atlanta began in mid-July 1998. Additionally, the Company has entered into 6 international agreements for distribution of moissanite gemstones in 10 countries and various areas in the Caribbean. The international agreements require the purchase of an aggregate of approximately $9 million of moissanite gemstones through the year 2000, with approximately $850,000 of those purchases in 1998.

Additionally, in July 1998, the Company entered into an Amended and Restated Development Agreement (the "Agreement") with its exclusive supplier, Cree Research, Inc. (Cree), which is focused on increasing the yield of usable material in each silicon carbide crystal manufactured by Cree for use by C3 in the production of lab-created moissanite gemstones. The companies have agreed on the definition of a "repeatable process" in the KLMN comparable diamond color range. In June 1998 Cree demonstrated its ability to meet that definition for 2-inch diameter crystals and has now begun to produce 2-inch crystals using that process. The Agreement establishes performance milestones for 1999 and contemplates that the Company and Cree will revise the performance milestones annually to provide both parties with more flexibility to pursue further color and yield improvements on both 2-inch and 3-inch diameter crystals. The 4-year Agreement replaces the June 1997 Development Agreement and the 1998 Supplemental Development Agreement between the parties and requires the Company to fund the program at $2.88 million annually. Either party may terminate the Agreement if Cree does not meet the annual performance milestones or if the Company and Cree do not mutually agree on the performance milestones for the ensuing year.

Under certain conditions, shareholders may request the Company to include a proposal for action at a forthcoming meeting of the shareholders of the Company in the proxy materials of the Company for such meeting. All shareholder proposals intended to be presented at the 1999 Annual Meeting of the Shareholders of the Company must be received by the Company no later than January 22, 1999 for inclusion in the Proxy Statement and proxy card relating to such meeting. In addition, if a shareholder desires to make a proposal from the floor during the meeting and written notice of such proposal is not received by the Company at least sixty days prior to the meeting, the shareholder proposal will be considered untimely and the proxies appointed pursuant to the proxy cards will have discretionary authority to vote for or against that proposal at the meeting even though the proposal is not discussed in the Proxy Statement.

ITEM 6: EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

Exhibit 10.25 Amended and Restated Development Agreement, dated July 1, 1998 between Cree Research, Inc. and C3, Inc.*

Exhibit 10.26 Letter Agreement dated, July 14, 1998, between Cree Research, Inc. and C3, Inc.*

Exhibit 27.1 Financial Data Schedule

*The Company has requested that certain portions of this exhibit be given confidential treatment. An unredacted version of this Exhibit has been filed with the Commission.

(b) Report on Form 8-K

The Company did not file any reports on 8-K during the three months ended June 30, 1998.

SIGNATURES

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

C3, Inc.

Dated: August 7, 1998

/s/ Jeff N. Hunter
Jeff N. Hunter
Chief Executive Officer and Chairman of the Board and Director
(Principal Executive Officer)

Dated: August 7, 1998

/s/ Mark W. Hahn
Mark W. Hahn
Chief Financial Officer
(Principal Financial and Accounting Officer)

EXHIBIT 10.25

THE REGISTRANT HAS REQUESTED THAT CERTAIN PORTIONS OF THIS EXHIBIT BE GIVEN CONFIDENTIAL TREATMENT. AN UNREDACTED VERSION OF THIS EXHIBIT HAS BEEN FILED WITH THE COMMISSION.

AMENDED AND RESTATED DEVELOPMENT AGREEMENT
DATED JULY 1, 1998
BETWEEN C3, INC. AND CREE RESEARCH, INC.

REDACTED - - OMITTED MATERIAL HAS BEEN FILED SEPARATELY WITH THE COMMISSION AND IS NOTED HEREIN BY *****

AMENDED AND RESTATED DEVELOPMENT AGREEMENT

This AMENDED AND RESTATED DEVELOPMENT AGREEMENT (the "Agreement") is entered into effective as of the 1st day of July 1998 by and between Cree Research, Inc. ("Cree") and C3, Inc. ("C3").

Recitals

WHEREAS, Cree and C3 are parties to an Amended and Restated Exclusive Supply Agreement dated June 6, 1997 (the "Supply Agreement") wherein Cree and C3 agree, inter alia, for Cree to supply C3 certain silicon carbide ("SiC") material and C3 agrees to purchase certain SiC material as provided therein; and

WHEREAS, Cree and C3 are parties to a Development Agreement dated June 6, 1997 (the "Development Agreement"), and a Supplemental Development Agreement dated January 8, 1998 (the "Supplemental Development Agreement"), wherein Cree and C3 agree that Cree will perform certain research and development activities directed to improving the colorless material available for purchase under the Supply Agreement; and

WHEREAS, Cree and C3 desire to combine the Development Agreement and the Supplemental Development Agreement in a single agreement and to amend and restate the Development Agreement and the Supplemental Developmental Agreement, as set out herein; and

WHEREAS, the parties acknowledge that Cree has successfully developed a Repeatable Process (as defined in Section 1.2 of this Agreement) for producing 2" diameter SiC crystals with a ***** mm height of which *****% is in the comparable diamond color grade range of KLMN, or better, according to the standards generally accepted by the diamond industry for color using pregraded master color stones; and

WHEREAS, Cree and C3, in entering into this Agreement desire to improve and expand upon their relationship and intend to work together cooperatively with the objective of developing, as promptly as practicable, both the market for and commercially viable means of manufacturing improved colorless silicon carbide material suitable for gemstones, and with the specific development objectives of further increasing the usable volume of material per crystal and improving the repeatability of Cree's processes for producing such material;

NOW, THEREFORE, the parties hereto, in consideration of the foregoing premises and the covenants and undertakings herein contained, mutually agree as follows:

REDACTED - - OMITTED MATERIAL HAS BEEN FILED SEPARATELY WITH THE COMMISSION AND IS NOTED HEREIN BY *****

1. Duties of Cree

1.1 Cree agrees to use its best commercially reasonable efforts to develop a repeatable process, as defined in Section 1.2 (the "Repeatable Process"), for producing SiC boules which meet the specifications provided in Section 1.3 (the "Specifications") according to the proposal attached hereto as Exhibit A.

1.2 The process for producing SiC boules shall be considered a "Repeatable Process" when ***** crystal growers together can produce, in a period of ***** days, at least ***** percent (*****%) of the total produced that meet the Specifications.

1.3 As used in this Agreement, the term "Specifications" shall mean the applicable specifications referred to in the Specifications and Timetable Chart below for SiC boules. The specifications require only that each boule contain a certain volume of SiC material of which a specified percentage (the "Percentage") is in the comparable diamond color grade range of KLMN, or better, according to the standards generally accepted by the diamond industry for color using pregraded master color stones. While the specifications do not require the absence of inclusions, blemishes or other defects affecting clarity, Cree shall use its best commercially reasonable efforts to minimize such defects since such defects can have an impact on the final product. The parties acknowledge that initially C3 shall promptly provide feedback to Cree concerning the Percentage, but the parties shall cooperate to develop a mutually acceptable testing procedure for Cree to determine the Percentage prior to delivery of the SiC boules to C3. The volume specifications are expressed in terms of the diameter and height of each boule, but any equivalent volume is acceptable. The specifications change over time, as the Date column indicates.

Specifications and Timetable Chart

Date	Minimum Diameter	Minimum Height	%KLMN-Grade
6/30/1999	*****"	*****mm	*****%
6/30/2000	*	*	*
6/30/2001	*	*	*
6/30/2002	*	*	*

*Each twelve-month period beginning July 1, 1998 through the period beginning July 1, 2001 is referred to in this Agreement as a "Subject Year". For each Subject Year beginning July 1, 1999 through July 1, 2001, the specifications applicable to June 30 of such year will

be mutually agreed upon by the parties prior to July 1 of that Subject Year, subject to Section 3.2(ii) below.

For each of the specifications above, Cree will provide prompt notice to C3 when Cree has developed a Repeatable Process for producing boules meeting such specifications.

1.4 In seeking to achieve the Specifications targeted for June 30, 1999, Cree will use its best commercially reasonable efforts to develop: (i) by August 31, 1998, a process that yields at a minimum a volume of material, corresponding to a *****" diameter boule with a ***** mm height, of which *****% is in the comparable diamond color grade range of KLMN, or better, according to the standards generally accepted by the diamond industry for color using pregraded master color stones, and (ii) by February 28, 1999 a process that yields at a minimum a volume of material, corresponding to a *****" diameter boule with a ***** mm height, of which *****% is in the comparable diamond color grade range of KLMN, or better, according to the standards generally accepted by the diamond industry for color using pregraded master color stones.

1.5 C3 and Cree will cooperate in determining the goals and the scope of the activities to be performed by Cree to the extent the same are not specified in this Agreement. Cree will direct the development work and determine the specific tasks to be undertaken towards the goals stated in Section 1.1 or otherwise agreed upon by the parties. If C3 reasonably requests major changes in such goals or that Cree undertake specific development activities in order to meet development needs related to SiC crystal growth required by C3's business, the parties will in good faith negotiate and seek to agree in writing on appropriate modifications to the Specifications set forth in Section 1.3, and the target date for achieving the affected Specifications will in any event be extended not less than ***** months from the originally scheduled date.

1.6 Cree agrees to report to C3 the progress of the development services provided pursuant to this Agreement at monthly progress meetings. Any "Confidential Information" provided by Cree to C3 at such meetings or otherwise under this Agreement shall be subject to the terms of Section 5 of the Supply Agreement.

1.7 In April of each year, Cree and C3 shall consult on appropriate development goals for the following year. Before May 1 of each year, Cree shall submit to C3 a development plan for the next twelve months beginning July 1 which shall include a budget and a description of the scope of the activities to be undertaken. Plans submitted under this paragraph shall set forth Cree's then current expectations for carrying on development activities under this Agreement for the period covered by the plan, in the manner determined by Cree to maximize the development progress toward the year's goals. Cree may substitute resources and personnel from those set out in the development plans provided that Cree reasonably determines such substitutions are in the best

interest of maintaining or enhancing progress toward the then current development goals. If Cree succeeds in reaching goals more quickly than anticipated, Cree will consult with C3 to determine other development goals important to high yields of gemstone quality SiC material.

1.8 All SiC boules produced pursuant to this Agreement, including SiC boules that do not meet the Specifications but excluding *****, shall be the property of C3; provided that the seeds from all SiC boules produced shall remain the property of Cree and shall be removed and retained by Cree. Cree shall identify each boule produced by the crystal growth system in which it was grown, the date it was produced and its disposition and provide such information to C3. Crystal growth systems used in the development activities shall not be considered as "in use for production" for purposes of the Supply Agreement. All SiC boules delivered hereunder will be supplied "AS IS." EXCEPT AS PROVIDED ABOVE IN THIS PARAGRAPH WITIH RESPECT TO IDENTIFICATION OF BOULES, CREE MAKES NO WARRANTY OF ANY KIND WITH RESPECT TO ANY MATERIAL SUPPLIED HEREUNDER AND DISCLAIMS ANY IMPLIED WARRANTIES, INCLUDING ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR NONINFRINGEMENT OF PATENT OR SIMILAR RIGHTS.

1.9 Cree will use all commercially reasonable efforts to maximize the value obtained from costs incurred in performing development services under this Agreement. It is understood, however, that Cree is expected to incur costs such that C3 will provide the maximum funding permitted under this Agreement.

1.10 Cree is not obligated to contribute resources to the development services performed under this Agreement beyond those funded by C3, as provided in Section 2.1.

1.11 Cree provides no assurances that the development services performed under this Agreement will be successful.

2. Duties of C3

2.1 Subject to Sections 2.2 and 2.3, C3 shall pay to Cree each month a development fee equal to the sum of:

(i) The costs of materials and equipment used in the development activities undertaken pursuant to this Agreement (including the costs of operating such equipment; with such costs calculated in the same manner as "loaded manufacturing costs," but, without reduction for boules that do not meet the "minimum specifications," as provided in the Supply Agreement);

(ii) An amount equal to a *****% gross margin of the costs described in Section 2.1(i); and

(iii) All research and development labor costs and outside services costs directly incurred by Cree in providing development services pursuant to this Agreement; provided, that these costs shall be charged to C3 on the same basis as Cree charges similar costs in providing research services pursuant to contracts between Cree and the U.S. government, using allocations, conditions and calculations no less favorable to C3 than those available under any such contract of Cree (it being understood that reductions in costs from cost-sharing shall not be applicable and that such costs include certain overhead allocations).

2.2 Subject to Section 2.3 and notwithstanding Section 2.1, C3 shall pay to Cree each month this Agreement continues in effect a development fee equal to the lesser of:

(i) The fee calculated pursuant to Section 2.1; or

(ii) The total monthly development budget as set forth in the proposal attached hereto as Exhibit A.

2.3 If the fee calculated pursuant to Section 2.1 is less than the total monthly development budget as set forth in the proposal in Exhibit A, the difference will be carried forward and applied to the development budget for subsequent months.

2.4 Cree shall invoice amounts due from C3 under this Agreement, and such invoices shall be due and payable within thirty days.

2.5 C3 shall have the right, at its expense, to have an independent public accounting firm reasonably acceptable to Cree audit Cree's costs described in Sections 2.1(i) and 2.1(iii) (the "Audited Costs"). The audit shall be conducted during normal business hours and upon reasonable prior notice. The accounting firm conducting the audit shall be required to enter into a mutually acceptable nondisclosure agreement with Cree under which such firm will be obligated not to disclose any information obtained during the course of the audit, except that it may disclose to C3 its analysis of the correctness of the Audited Costs as calculated by Cree. The audit right under this paragraph may be exercised not more than once during any fiscal year of Cree and only with respect to costs applicable to the year preceding the request for an audit. Cree shall provide reasonable assistance to the public accounting firm including, but not limited to, providing a schedule of the Audited Costs (which shall provide reasonable detail as to the calculation of the Audited Costs, including but not limited to hours charged by person at billing rates applicable to each, total material costs, equipment charges and overhead charges, however such schedule shall not divulge any

proprietary or confidential information of Cree), supporting analyses and any supporting source documentation reasonably required by the public accounting firm. Such accounting firm will audit and report to C3 on the schedule of Audited Costs, but will not divulge to C3 any proprietary or confidential information (including but not limited to supporting schedules and source documents) disclosed during the audit process.

3. Term and Termination

3.1 Unless earlier terminated pursuant to Section 3.2 or Section 5.6, or unless extended by the mutual consent of the parties hereto, this Agreement shall terminate on June 30, 2002.

3.2 C3 shall have the option to terminate this Agreement prior to June 30, 2002 under the following conditions:

(i) If Cree does not develop by June 30 of each Subject Year a Repeatable Process for producing SiC boules that meet the mutually agreed Specifications for such Subject Year, C3 shall have the option of terminating this Agreement by giving notice to Cree; provided, that such termination option, if not sooner exercised by C3, shall expire at 11:59 p.m. eastern daylight savings time on the tenth day following the termination of the applicable deadline for establishing the Repeatable Process.

(ii) If the parties are unable to mutually agree in writing on the Specifications for a Subject Year by July 1 of such year as provided in Section 1.3, C3 shall have the option of terminating this Agreement, effective December 31 of that Subject Year, by giving notice to Cree; provided, that such termination option, if not sooner exercised by C3, shall expire at 11:59 p.m. eastern daylight savings time on August 1st of such Subject Year. If C3 exercises this termination option, Cree will continue its development work under this Agreement through the effective date of the termination.

If C3 exercises its option to terminate this Agreement pursuant to Section 3.2(i), Cree shall not be entitled to payment for any work done or any expenses incurred during the period from the time C3's option to terminate became exercisable to the time such option is exercised.

4. Intellectual Property

4.1 All inventions developed by Cree personnel in performing work under this Agreement shall be the sole property of Cree.

4.2 Except for inventions related to the bulk growth of silicon carbide or gallium nitride, C3 shall have a perpetual, irrevocable, royalty-free, exclusive (including exclusive of Cree) license to use, manufacture, sell and otherwise practice (including the right to sublicense) all inventions developed by Cree pursuant to this Agreement for all gemstone applications and applications for gemological instrumentation; provided that Cree shall have the right to use and practice the invention to manufacture or process material for C3 for the licensed applications. References in this Agreement to "gemstones" are understood to mean "gems" (and vice versa).

5. General

5.1 This Agreement shall not be amended, modified or altered except pursuant to a document signed by both parties.

5.2 This Agreement is made in and shall be construed in accordance with and governed by the laws of the State of North Carolina.

5.3 This Agreement shall inure to the benefit of and be binding upon the parties and their respective successors and permitted assigns.

5.4 The invalidity or uneforceability of any particular provision of this Agreement shall not affect the other provisions hereof, and this Agreement shall be construed in all respects as if such invalid or unenforceable provisions were omitted.

5.5 This Agreement may not be assigned by either party without the other party's prior written consent, which consent shall not be unreasonably withheld except that either party may, in its sole discretion, withhold consent to assignment of this Agreement to anyone other than a permitted assignee of all rights under the Supply Agreement. Any attempted assignment in violation of this Section 5.5 is void and shall constitute a breach of this Agreement.

5.6 In the event of a material breach by either party of any obligation under this Agreement to the other party, the other party may terminate this Agreement upon written notice if the breach is not cured within thirty (30) days after giving written notice to the party in breach, setting out the nature of the breach in reasonable detail; provided, however, that no cure period shall apply to a termination pursuant to the terms of this Agreement by C3 pursuant to Section 3.2 (it being understood that the grounds for termination specified in Section 3.2 do not constitute a breach) or in the event of a material breach by a party that has breached this Agreement and been given notice of similar material breaches on two prior occasions. In addition, this Agreement shall automatically terminate upon any termination of the Supply Agreement under Section 3.3 thereof.

5.7 Neither party shall issue any press release nor otherwise make any public announcement concerning this Agreement without the prior consent of the other party, except as may be required by law. The parties further agree that the terms of this Agreement shall be treated as Confidential Information of each other subject to Section 5 of the Supply Agreement; provided, however, that either party may, upon notice to the other, make such public disclosures regarding this Agreement as in the opinion of counsel for such party are required by applicable securities laws or regulations or other applicable law. Neither party shall use the name of the other party in any advertising, marketing or similar material without the other party's prior written consent.

5.8 The parties acknowledge and agree that in the event of a breach of the Agreement, in addition to any other rights and remedies available to it at law or otherwise, the parties shall be entitled to seek equitable relief in the form of a temporary restraining order ("TRO") from any court of competent jurisdiction; provided, however, that in the event a TRO is obtained, the parties shall request that any hearing on the merits of the dispute shall be stayed pending arbitration of the dispute as provided in this Section 5.8. In the event a party seeks a TRO or in the event of any other controversy or claim (including, without limitation, any claim based on negligence, misrepresentation, strict liability or other basis) arising out of or relating to this Agreement or its performance or breach, a party shall give the other party notice of the dispute, setting out the circumstance in reasonable detail, and requesting a meeting of the representatives of the parties to attempt to resolve the dispute or to reduce the scope of the issues subject to dispute. The chief operating officers of the parties, and such other representatives as each may desire to have attend, shall meet at a mutually agreeable time within five business days from the date the meeting request was received and shall hold such meeting at the offices of the party not requesting the same, or at some mutually agreeable alternative location. In the event the parties do not resolve the dispute at such meeting, or any mutually agreed upon adjournment thereof, the dispute shall be settled exclusively by arbitration in the City of Raleigh, North Carolina pursuant to the expedited procedures of the Commercial Arbitration Rules of the American Arbitration Association (other than notice requirements which shall be as provided in Section 5.9 below and the expedited procedures for selection of arbitrators which shall be as provided in Sections 14 and 15 of such Rules). There shall be three arbitrators, one selected by each of C3 and Cree and a third selected by the arbitrators selected by the parties. The arbitrators shall in no event make any damage award that contravenes Section 5.10 of this Agreement, but shall order the losing party to pay all of the charges of the American Arbitration Association for such arbitration and all of the prevailing party's costs of the arbitration, including reasonable attorneys' fees. The decision in such arbitration shall be final and binding and judgment on any award rendered therein may be entered in any court having jurisdiction.

5.9 All notices under this Agreement shall be in writing and addressed to the other party at the address shown below or to such other addresses as the party may hereafter designate by

notice under this Agreement. All notices so addressed shall be deemed given five (5) days after mailing if sent by certified mail, return receipt requested, postage prepaid, or when sent via facsimile if receipt is acknowledged in writing or otherwise when actually received.

5.10 In no event shall either party be liable to the other for incidental, consequential or special loss or damages of any kind, however caused, or any punitive damages.

5.11 This Agreement constitutes the complete and exclusive statement of the understanding and agreement of the parties with respect to the subject matter hereof and supersedes all prior written or oral agreements between the parties concerning such subject matter, including without limitation the Development Agreement dated June 7, 1997, the Supplemental Development Agreement dated January 8, 1998 and the letter agreement between the parties dated January 8, 1998, but excluding the letter agreements between the parties dated July 14, 1997, January 31, 1996, February 12, 1996, May 1, 1998 and July 14, 1998, the Assignment Agreement dated June 28, 1995 (as amended September 15, 1995), and the Amended and Restated Exclusive Supply Agreement dated June 6, 1997.

5.12 This Agreement shall be deemed the "Development Agreement" as such term is used in the Amended and Restated Exclusive Supply Agreement between the parties dated June 6, 1997, except that any notice given by Cree that it has developed a Repeatable Process for achieving the Specifications as defined in this Agreement shall not constitute the notice required by the last paragraph of Section 1.1 or by Section 2.4 of the Exclusive

Supply Agreement. The parties acknowledge and agree that the Repeatable Process developed by Cree, as described in the recitals to this Agreement, does not constitute a process contemplated by Section 1.1 or Section 2.4 of the Exclusive Supply Agreement and that the provisions of Section 2.4(b) and (c) of such agreement are not presently applicable.

IN WITNESS WHEREOF, the parties have executed this Agreement by and through their duly authorized representatives.

CREE RESEARCH, INC.	C3, INC.
By: /s/ Charles M. Swoboda	By: /s/ Robert S. Thomas
Charles M. Swoboda, Vice President and Chief Operating Officer	Robert S. Thomas President and Chief Operating Officer

Address for Notices:	Address for Notices:
Cree Research, Inc. 4600 Silicon Drive Durham, NC 27703 Attention: Chief Operating Officer Fax No. (919) 361-4630	C3, Inc. P.O. Box 13533 Research Triangle Park, NC 27709-3533 Attention: President Fax No. (919) 468-0486

EXHIBIT A

A Proposal Submitted to:

C3, Inc.
P.O. Box 13533
Research Triangle Park, NC 27009-3533

entitled:

Development of Large Volume Colorless Silicon Carbide Crystals and Repeatable Process for Manufacturing such Crystals

by:

Cree Research, Inc.
2810 Meridian Parkway
Durham, NC 27713
Tel: (919) 361-5709

12 Month Cost: $2,880,000

Company Proprietary "The information contained in this document is confidential and proprietary to Cree Research, Inc. and shall not be duplicated, used or disclosed--in whole or in part without the prior written consent of the Company."

A. Personnel

Dr. *****, ***** at Cree Research, has over 20 years of experience in materials research and development of elemental and compound semiconductors, ranging from silicon through gallium arsenide to silicon carbide. Dr. *****'s work in silicon carbide has focused primarily on the development of large diameter *****- and *****- SiC crystals and substrates for microwave and power device applications, with special emphasis on polytype uniformity, uniformity of electrical properties (conducting through semi-insulating), and low crystalline defect density. In addition to SiC, Dr. *****'s work covers materials problems related to the growth of silicon, III-V materials (GaAs, InP) for microlectronic device applications including microwave power MMICs, high voltage power switching infrared imaging, and VLSI. His experience in semiconductor crystal growth covers growth of silicon carbide by modified sublimation/physical vapor transport method; growth of silicon by Czochralski and floating zone techniques; and growth of GaAs and InP by high pressure liquid encapsulated Czochralski. D. ***** has authored or co-authored over 60 papers and presentations. Dr. ***** will be the Principal Investigator on this program and will devote *****% of his time to the effort.

Dr. *****, ***** at Cree Research, has over 17 years of experience in research related to silicon carbide, and is also *****. He has been co-Principal Investigator or Program Manager on all of Cree's funded research contracts (totaling >$25M). Dr. ***** has extensive experience in SiC crystal growth, thin film deposition, doping, and material characterization and developed the first commercially viable SiC boule growth process. Since joining Cree, he has increased the diameter of SiC bulk crystals from ***** mm to ***** mm, increased crystal thickness by *****% and improved the crystal quality by orders of magnitude. Much of the progress has been made possible by the combination of a $2M NIST Advanced Technology Program project which was completed in 1994 and an ongoing $6.8 M DARPA funded program on which he is PI. He was also co-PI on a $2.4 M ARPA contract which demonstrated the first SiC/AIGaN single crystal alloy, increased the brightness of SiC blue LEDs from 17uW to 35uW. He is Program Manager on another ARPA funded program which will soon lead to the release of a much brighter blue LED based on GaN grown on SiC substrates. In addition to the ONR funded programs at NCSU, Dr. ***** was co-PI on a National Science Foundation sponsored grant on diffusion on SiC as well as other grants related to SiC for structural applications. He was also co-PI and program manager on an SDIO funded program on the growth and characterization of GaN and AIN on SiC substrates. Dr. ***** is co- inventor of 7 issued U.S. patents, 2 pending U.S. patent applications, and 1 issued foreign patent and has 70 publications on SiC and other electronic materials.

Dr. *****, ***** at Cree Research is responsible for the development of silicon carbide bulk crystal growth processes. He has over 25 years of experience in research related to growth technology and characterization of wide bandgap semiconductor crystals and epitaxial layers

including SiC, AIN, SiC-AIN, and GaN. Before joining Cree Research in April 1993, he was a professor at *****, *****. He investigated thermodynamics and kinetics of crystal growth processes for SiC and SiC-AIN crystals, both pure and doped. Based on this research, he developed a new method for bulk SiC and SiC-AIN crystal growth with controlled polytype structures in 1976. This seeded sublimation method is the basis for all known SiC boule growth programs. He also was a consultant of the R&D team at ***** for GaN technology (GaN powder preparation and epitaxial growth by a sublimation method). In 1991-1993, he was Consultant-Professor of Siemens AG and *****, *****. Since joining Cree Research, he has increased the diameter of SiC bulk crystals and has determined the primary reasons for formation of micropipe defects in SiC boules. He has 21 patents and his results are published in more than 100 articles and 5 books/monographs.

Dr. *****, ***** at Cree, has over 9 years of experience in the SiC field. His initial work began with UHV ion-assisted e-beam deposition processes and surface analytical studies on the interfacial chemistry of various materials grown on SiC. Traveling abroad as a visiting scientist in Sweden, he conducted materials studies on SiC for power device work sponsored by ABB. His research there focused on high resolution X-ray analysis of SiC bulk material and growth of CVD films. Upon returning to the U.S. he worked as a SiC crystal growth research scientist at Westinghouse Electric Corporation's Science and Technology Center. In October of 1995 he joined Cree Research as a crystal growth scientist and manager of their crystal growth department, where he has worked between development and production to successfully guide the Crystal Growth and Wafering Departments through a 300% expansion and an order of magnitude improvement in production material quality. Dr. ***** has authored or co-authored over 20 articles and presentations.

Dr. *****, ***** at Cree Research, has spent the past 6 years investigating optical and electrical processes in silicon carbide and other related wide bandgap materials using techniques such as: Fourier transform infrared spectroscopy, optical absorption, deep level transient spectroscopy, Hall effect, and thermally stimulated current. His initial work at Carnegie Mellon University, performed under an Air Force Fellowship, focused on the impact that impurities have on the optical and electronic properties of SiC. Immediately before his arrival at Cree Research, he spent 18 months working under a National Research Council post-doctoral fellowship at the Air Force Wright Labs, where, in addition to his interests in SiC, he examined the surface kinetics of III- N growth. Dr. ***** has authored or co-authored 16 papers and presentations. Dr. ***** will devote *****% of his time to this effort.

B. Budget

NOTE: CREE RESERVES THE RIGHT TO ADJUST THE SPENDING AS IT DEEMS APPROPRIATE IN ORDER TO MEET THE OBJECTIVES OF THE DEVELOPMENT PROGRAM AND WITHIN THE TOTAL AMOUNT OF THE BUDGET.

REDACTED - - OMITTED MATERIAL HAS BEEN FILED SEPARATELY WITH THE COMMISSION AND IS NOTED HEREIN BY *****

		Monthly
Equipment Costs		
Crystal Growers (*****)		$*****
Powder System (*****)		$*****
People Costs		
C3 Focused Team	$*****	
Cree Resources	*****	
Other Processing		
Analytical	$*****	
Wafering	$*****	
Polishing	$*****	
Total	$240,000	

Equipment - The equipment is outlined above and the cost reflects a *****% margin.

C3 Focused Team - This team will be led by Dr. *****, who reports to Dr. *****, who will supervise these efforts. The team will include a *****, *****, *****, and *****.

Cree Resources - These resources will support the C3 development effort on a part time basis. This team will work under the direction of Dr. ***** and include Dr. *****, Dr. *****, Dr.***** and other Cree resources as required.

EXHIBIT 10.26

THE REGISTRANT HAS REQUESTED THAT CERTAIN PORTIONS OF THIS EXHIBIT BE GIVEN CONFIDENTIAL TREATMENT. AN UNREDACTED VERSION OF THIS EXHIBIT HAS BEEN FILED WITH THE COMMISSION.

LETTER AGREEMENT
DATED JULY 14, 1998
BETWEEN C3, INC. AND CREE RESEARCH, INC.

REDACTED - - OMITTED MATERIAL HAS BEEN FILED SEPARATELY WITH THE COMMISSION AND IS NOTED HEREIN BY *****

July 14, 1998

Robert S. Thomas
President
C3 Inc.
P.O. Box 13533
Research Triangle Park, NC 27709-3533

This letter, if accepted by C3, will serve as an agreement between Cree and C3 to the following terms, effective as of July 1, 1998.

1. Cree agrees to supply production crystals and C3 agrees to purchase production crystals according to the terms outlined in this letter agreement for a period of one year.

2. C3 will purchase the output of crystal growers according to the following schedule:

DATE	# OF CRYSTAL GROWTH SYSTEMS
July 1, 1998 - July 31, 1998	*****
August 1, 1998 - September 15, 1998	*****
September 15, 1998 - October 31, 1998	*****
November 1, 1998 - June 30, 1999	*****

3. C3 must give Cree at least ***** days notice to delay the schedule outline in Section 2. Any delay in the schedule outlined in section 2 greater than ***** weeks by either party will give the other party the right to require the parties to re-negotiate in good faith the pricing schedule outlined in Exhibit A.

4. Cree will supply crystals from the systems outlined in Section 2 according to the pricing schedule outlined in Exhibit A.

5. C3 may switch growers from 2" to 3" diameter crystals provided it gives Cree at least ***** days notice and such additional time as reasonably required to address any conversion and ramp-up issues. Pricing for 3" production crystals will be mutually agreed upon by Cree and C3 prior to conversion.

REDACTED - - OMITTED MATERIAL HAS BEEN FILED SEPARATELY WITH THE COMMISSION AND IS NOTED HEREIN BY *****

6. The ***** crystal growth systems outlined in section 2 in excess of ***** systems are being paid for by C3 under the payment terms outlined in the letter agreement dated May 1, 1998. The systems are being built as new for use by Cree on behalf of C3.

7. As used in Exhibit A, 'usable material' means KLMN grade material ***** as previously defined by both parties. Any discrepancies in usable material will be mutually resolved by Cree and C3. All grading will be concluded in a timely manner consistent with past practice.

8. Except as provided above, purchases will be subject to the terms and conditions of the June 6, 1997 Amended and Restated Exclusive Supply Agreement (the "Supply Agreement').

9. The parties will negotiate in good faith a mutually acceptable definition of "Repeatable Process," as applied to the production of 2" and 3" crystals, to be used for purposes of Sections 1.1 and 2.4 of the Supply Agreement from and after July 1, 1999. No agreement regarding the definition will be effective until reduced to writing and signed on behalf of both parties. The existing provisions of the Supply Agreement will remain in effect until the parties mutually agree otherwise in writing. Neither party will have any liability as a result of failure to reach agreement.

10. If the parties do not agree in writing, prior to July 1, 1999, on a mutually acceptable definition of "Repeatable Process" for purposes of Sections 1.1 and 2.4 of the Supply Agreement, the pricing specified in this letter agreement for the second calendar quarter of 1999, will remain in effect for an additional six months, through December 31, 1999 (the "Extension Period"), provided that: (a) C3 purchases the output of at least ***** crystal growers during Extension Period; and (b) the Amended and Restated Development Agreement between the parties dated as of July 1, 1998 remains in effect during the Extension Period and C3's funding obligation under the agreement has not been reduced.

11. If the parties do not agree in writing, prior to January 1, 2000, on a mutually acceptable definition of "Repeatable Process" for purposes of Sections 1.1 and 2.4 of the Supply Agreement, then unless otherwise agreed in writing by the parties C3 will purchase from Cree, and Cree will sell to C3, material in accordance with the pricing and other terms and conditions set forth in the Supply Agreement and no minimum specifications shall be applicable to such material.

12. The contents of this letter shall be considered 'Confidential Information' of each party subject to the provisions of Section 5 of the Supply Agreement.

If acceptable, please sign below and date to indicate C3's binding agreement to these terms.

REDACTED - - OMITTED MATERIAL HAS BEEN FILED SEPARATELY WITH THE COMMISSION AND IS NOTED HEREIN BY *****

CREE RESEARCH, INC.

By: /s/Charles M. Swoboda
Charles M. Swoboda
Vice President & COO

C3, INC.

By: /s/Robert S. Thomas
Robert S. Thomas
President and COO

REDACTED - - OMITTED MATERIAL HAS BEEN FILED SEPARATELY WITH THE COMMISSION AND IS NOTED HEREIN BY *****

Exhibit A

2" Crystal Pricing Schedule

C3 Crystal Price
July 98 through October 98

Usable Material Range		Price
>=	<	
*****		$ *****
*****	*****	$ *****
*****	*****	$ *****
*****	*****	$ *****
*****	*****	$ *****
*****	*****	$ *****
*****	*****	$ *****
*****	*****	$ *****
	*****	$ *****

C3 Crystal Price
November 98 through February 99

Usable Material Range		Price
>=	<	
*****		$ *****

*****	*****	$ *****
*****	*****	$ *****
*****	*****	$ *****
*****	*****	$ *****
*****	*****	$ *****
*****	*****	$ *****
*****	*****	$ *****
	*****	$ *****

REDACTED - - OMITTED MATERIAL HAS BEEN FILED SEPARATELY WITH THE COMMISSION AND IS NOTED HEREIN BY *****

C3 Crystal Price
March 99 through June 99

Usable Material Range >=	<	Price
*****		$ *****
*****	*****	$ *****
*****	*****	$ *****
*****	*****	$ *****
*****	*****	$ *****
*****	*****	$ *****
*****	*****	$ *****
*****	*****	$ *****
	*****	$ *****

NOTE: THE UNITS FOR USABLE MATERIAL IS MM.

<ARTICLE> 5
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This Schedule Contains Summary Financial Information Extracted From The Condensed Balance Sheet As Of June 30, 1998 And The Condensed Statement Of Operations For The Six Months Ended June 30, 1998 And Is Qualified In Its Entirety By Reference To Such Financial Statements.
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<MULTIPLIER> 1

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<OTHER-SE>	(7,463,720)
<TOTAL-LIABILITY-AND-EQUITY>	43,466,835
<SALES>	452,565
<TOTAL-REVENUES>	452,565
<CGS>	290,552
<TOTAL-COSTS>	290,552
<OTHER-EXPENSES>	0
<LOSS-PROVISION>	0
<INTEREST-EXPENSE>	0
<INCOME-PRETAX>	(3,870,848)
<INCOME-TAX>	0
<INCOME-CONTINUING>	(3,870,848)
<DISCONTINUED>	0
<EXTRAORDINARY>	0
<CHANGES>	0
<NET-INCOME>	(3,870,848)
<EPS-PRIMARY>	(.56)
<EPS-DILUTED>	(.56)