CLEARONE INC
Form 10-Q
August 09, 2018

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UNITED STATES

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, 2018
or
[ ] **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period _______ to _______

Commission file number:**001-33660**

CLEARONE, INC.

(Exact name of registrant as specified in its charter)

Utah	**87-0398877**
(State or other jurisdiction of incorporation or organization)	(I.R.S. employer identification number)
5225 Wiley Post Way, Suite 500, Salt Lake City, Utah	**84116**
(Address of principal executive offices)	(Zip Code)

+1 (801) 975-7200
(Registrant's telephone number, including area code)

Indicate by check 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 [ ]

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes [X] No [ ]

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

Larger Accelerated Filer [ ]	Accelerated Filer [X]
Non-Accelerated Filer [ ] (Do not check if a smaller reporting company)	Smaller Reporting Company [ ]
Emerging growth company [ ]	

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. [ ]

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 number of shares of ClearOne common stock outstanding as of August 6, 2018 was 8,306,735.

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CLEARONE, INC.

QUARTERLY REPORT ON FORM 10-Q FOR THE QUARTER ENDED JUNE 30, 2018

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PART I - FINANCIAL INFORMATION

Item 1. FINANCIAL STATEMENTS

CLEARONE, INC.

UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS

(Dollars in thousands, except par value)

	June 30, 2018	December 31, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	$4,079	$ 5,571
Marketable securities	2,852	2,689
Receivables, net of allowance for doubtful accounts of $527 and $472, respectively	5,139	7,794
Inventories, net	14,380	14,415
Distributor channel inventories	—	1,555
Prepaid expenses and other assets	2,339	1,862
Total current assets	28,789	33,886
Long-term marketable securities	6,391	10,349
Long-term inventories, net	8,351	8,708
Property and equipment, net	1,423	1,549
Intangibles, net	8,511	6,543
Deferred income taxes	7,458	6,531
Other assets	318	311
Total assets	$61,241	$ 67,877
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$3,528	$ 4,122
Accrued liabilities	1,844	1,843
Deferred product revenue	258	4,635
Total current liabilities	5,630	10,600
Deferred rent	138	103
Other long-term liabilities	686	607
Total liabilities	6,454	11,310

Shareholders' equity:

Common stock, par value $0.001, 50,000,000 shares authorized, 8,306,935 and 8,319,022 shares issued and outstanding	8	8
Additional paid-in capital	47,750	47,464
Accumulated other comprehensive loss	(174)	(65)
Retained earnings	7,203	9,160
Total shareholders' equity	54,787	56,567
Total liabilities and shareholders' equity	$61,241	$ 67,877

See accompanying notes

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UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND

COMPREHENSIVE LOSS

(Dollars in thousands, except per share amounts)

	Three months ended June 30,		**Six months ended June 30,**	
	2018	**2017**	**2018**	**2017**
Revenue	$6,971	$10,311	$14,260	$21,989
Cost of goods sold	3,721	4,242	6,911	9,242
Gross profit	3,250	6,069	7,349	12,747
Operating expenses:				
Sales and marketing	2,760	2,646	5,628	5,387
Research and product development	1,920	2,322	3,976	4,679
General and administrative	1,542	2,210	3,159	4,316
Total operating expenses	6,222	7,178	12,763	14,382
Operating loss	(2,972)	(1,109)	(5,414)	(1,635)
Other income, net	49	84	73	186
Loss before income taxes	(2,923)	(1,025)	(5,341)	(1,449)
Benefit from income taxes	(760)	(205)	(1,332)	(161)
Net loss	$(2,163)	$(820)	$(4,009)	$(1,288)
Basic weighted average shares outstanding	8,301,094	8,638,091	8,304,093	8,702,743
Diluted weighted average shares outstanding	8,301,094	8,638,091	8,304,093	8,702,743
Basic loss per share	$(0.26)	$(0.09)	$(0.48)	$(0.15)
Diluted loss per share	$(0.26)	$(0.09)	$(0.48)	$(0.15)
Comprehensive loss:				
Net loss	$(2,163)	$(820)	$(4,009)	$(1,288)
Unrealized gain (loss) on available-for-sale securities, net of tax	(1)	20	(71)	58
Change in foreign currency translation adjustment	(60)	52	(38)	64
Comprehensive loss	$(2,224)	$(748)	$(4,118)	$(1,166)

See accompanying notes

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UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands, except per share amounts)

	Six months ended June 30, 2018	2017
Cash flows from operating activities:		
Net loss	$(4,009)	$(1,288)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization expense	769	779
Amortization of deferred rent	1	(35)
Stock-based compensation expense	266	340
Provision for doubtful accounts, net	59	6
Change of inventory to net realizable value	425	55
Deferred income taxes	(927)	—
Changes in operating assets and liabilities:		
Receivables	2,585	280
Inventories	(33)	(5,801)
Prepaid expenses and other assets	54	(190)
Accounts payable	(595)	1,429
Accrued liabilities	38	253
Income taxes payable	(540)	(393)
Deferred product revenue	(37)	(85)
Other long-term liabilities	79	-
Net cash used in operating activities	(1,865)	(4,650)
Cash flows from investing activities:		
Purchase of property and equipment	(130)	(404)
Purchase of intangibles	(98)	(127)
Capitalized patent defense costs	(2,383)	—
Proceeds from maturities and sales of marketable securities	5,128	3,631
Purchases of marketable securities	(1,403)	(3,051)
Net cash provided by investing activities	1,114	49
Cash flows from financing activities:		
Net proceeds from equity-based compensation programs	20	82
Dividend payments	(583)	(1,051)
Repurchase and cancellation of stock	(147)	(3,210)
Net cash used in financing activities	(710)	(4,179)
Effect of exchange rate changes on cash and cash equivalents	(31)	47
Net decrease in cash and cash equivalents	(1,492)	(8,733)
Cash and cash equivalents at the beginning of the period	5,571	12,100

Cash and cash equivalents at the end of the period	$4,079	$3,367

See accompanying notes

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UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands, except per share amounts)

The following is a summary of supplemental cash flow activities:

	Six months ended June 30,	
	2018	**2017**
Cash paid for income taxes	$11	$ 6

See accompanying notes

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited - Dollars in thousands, except per share amounts)

1. Business Description, Basis of Presentation and Significant Accounting Policies

Business Description:

ClearOne, Inc., together with its subsidiaries (collectively, “ClearOne” or the “Company”), is a global market leader enabling conferencing, collaboration, and network streaming solutions. The performance and simplicity of our advanced, comprehensive solutions offer unprecedented levels of functionality, reliability and scalability.

Basis of Presentation:

The fiscal year for ClearOne is the 12 months ending on December 31. The consolidated financial statements include the accounts of ClearOne and its subsidiaries. All significant inter-company accounts and transactions have been eliminated.

These accompanying interim unaudited condensed consolidated financial statements have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”) and are not audited. Certain information and footnote disclosures that are usually included in financial statements prepared in accordance with generally accepted accounting principles in the United States (“GAAP”) have been either condensed or omitted in accordance with SEC rules and regulations. The accompanying condensed consolidated financial statements contain all adjustments, consisting of normal recurring accruals, necessary for a fair presentation of our financial position as of June 30, 2018 and December 31, 2017, the results of operations for the three and six months ended June 30, 2018 and 2017, and the cash flows for the six months ended June 30, 2018 and 2017. The results of operations for the three and six months ended June 30, 2018 and 2017 are not necessarily indicative of the results for a full-year period. These interim unaudited condensed consolidated financial statements should be read in conjunction with the financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2017 filed with the SEC.

Significant Accounting Policies:

The significant accounting policies were described in Note 1 to the audited consolidated financial statements included in the Company's annual report on Form 10-K for the year ended December 31, 2017. There have been no changes to these policies during the six months ended June 30, 2018 that are of significance or potential significance to the Company except for the change in revenue recognition policy described below.

Adoption of New Revenue Standard: On January 1, 2018, as required, the Company adopted ASU No. 2014-09 - Revenue from Contracts with Customers (Topic 606) ("ASU 2014-09"), ASU No. 2015-14 - Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date ("ASU 2015-14"), ASU No. 2016-08 - Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations ("ASU 2016-08"), ASU No. 2016-10 - Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing ("ASU 2016-10"), ASU No. 2016-12 - Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients ("ASU 2016-12") and ASU No. 2016-20 - Technical Corrections and Improvements to Topic 606, Revenue from Contracts with Customers" ("ASU 2016-20") (collectively "the New Revenue Standard"). To conform to the New Revenue Standard, the Company modified its revenue recognition policy as described further below.

Change in Accounting Policy: On January 1, 2018, the Company adopted the New Revenue Standard using the modified retrospective method, applying the guidance to all open contracts and recognized an adjustment to increase retained earnings by $2,783, reduce deferred product revenue by $4,338 and reduce distributor channel inventories by $1,555 as of that date. The comparative financial information has not been restated and continues to be presented under the accounting standards in effect for the respective periods. The Company applied the practical expedient and has not disclosed the revenue allocated to future shipments of partially completed contracts.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited - Dollars in thousands, except per share amounts)

Prior to our change in accounting policy, revenue from product sales to distributors was not recognized until the return privilege had expired or until it can be determined with reasonable certainty that the return privilege had expired, which approximated when the product was sold-through to customers of our distributors (dealers, system integrators, value-added resellers, and end-users), rather than when the product was initially shipped to a distributor. At each quarter-end, we evaluated the inventory in the distribution channel through information provided by our distributors. The level of inventory in the channel fluctuated up or down each quarter based upon our distributors' individual operations. Accordingly, each quarter-end deferral of revenue and associated cost of goods sold were calculated and recorded based upon the actual channel inventory reported at quarter-end. Further, with respect to distributors and other channel partners not reporting the channel inventory, the revenue and associated cost of goods sold were deferred until we received payment for the product sales made to such distributors or channel partners.

After the change in the accounting policy, substantially all of the Company's revenue is recognized following the transfer of control of the products to the customer, which typically occurs upon shipment or delivery depending on the terms of the underlying contracts. During the three months ended June 30, 2018, revenue increased by $271 and during the six months ended June 30, 2018 revenue decreased by $581 due to the impact of the adoption of the New Revenue Standard.

Revenue Recognition Policy: The Company generates revenue from sales of its audio and video conferencing equipment to distributors, system integrators and value-added resellers. The Company also generates revenue, to a much lesser extent, from sale of software and licenses to distributors, system integrators, value-added resellers and end-users. The Company recognizes revenue when it satisfies a performance obligation in an amount reflecting the consideration to which it expects to be entitled. For sales agreements, the Company has identified the promise to transfer products, each of which are distinct, to be the performance obligation. The Company applies a five-step approach in determining the amount and timing of revenue to be recognized: (1) identifying the contract with a customer, (2) identifying the performance obligations in the contract, (3) determining the transaction price, (4) allocating the transaction price to the performance obligations in the contract and (5) recognizing revenue when the performance obligation is satisfied. Substantially all of the Company's revenue is recognized at the time control of the products transfers to the customer.

Sales agreements with customers are renewable periodically and contain terms and conditions with respect to payment, delivery, warranty and supply, but typically do not require mandatory purchase commitments. In the absence of a sales agreement, the Company's standard terms and conditions at the time of acceptance of purchase orders apply. The Company considers the customer purchase orders, governed by sales agreements or the Company's standard terms and conditions, to be the contract with the customer. The Company evaluates certain factors including the customer's ability to pay (or credit risk).

In determining the transaction price, the Company evaluates whether the price is subject to refund or adjustment to determine the net consideration to which the Company expects to be entitled. Sales to distributors, are typically made pursuant to agreements that provide return rights with respect to discontinued or slow-moving products, referred to as stock rotation. Sales to distributors can also be subject to price adjustment on certain products, primarily for distributors with drop-shipping rights. Although payment terms vary, most distributor agreements require payment within 45 days of invoicing.

The Company recognizes revenue when it satisfies a performance obligation. The Company recognizes revenue from sales agreements upon transferring control of a product to the customer. This typically occurs when products are shipped or delivered, depending on the delivery terms, or when products that are consigned at customer locations are sold to dealers or end users. Revenue recognized during the three and six months ended June 30, 2018 for equipment sales was $6,803 and $13,900, respectively, and for software, licenses, etc. was $168 and $360, respectively. Sales returns and allowances are estimated based on historical experience. Provisions for discounts and rebates to customers, estimated returns and allowances, ship and credit claims and other adjustments are provided for in the same period the related revenues are recognized, and are netted against revenues. For returns, the Company recognizes a related asset for the right to recover returned products with a corresponding reduction to cost of goods sold. The Company reviews warranty and related claims activity and records provisions, as necessary.

Frequently, the Company receives orders with multiple delivery dates that may extend across reporting periods. Since each delivery constitutes a performance obligation, the Company allocates the transaction price of the contract to each performance obligation based on the stand-alone selling price of the products. The Company invoices the customer for each delivery upon shipment and recognizes revenues in accordance with delivery terms. Although payment terms vary, distributors typically pay within 45 days of invoicing and dealers pay within 30 days of invoicing. As scheduled delivery dates are within one year, revenue allocated to future shipments of partially completed contracts are not disclosed.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited - Dollars in thousands, except per share amounts)

The Company has elected to record freight and handling costs associated with outbound freight after control over a product has transferred to a customer as a fulfillment cost and include it in cost of revenues. Taxes assessed by government authorities on revenue-producing transactions, including value-added and excise taxes, are presented on a net basis (excluded from revenues) in the Consolidated Statements of Operations and Comprehensive Income.

Recent Accounting Pronouncements:

In February 2016, the FASB released ASU No. 2016-02, Leases (Topic 842) to bring transparency to lessee balance sheets. The ASU will require organizations that lease assets (lessees) to recognize assets and liabilities on the balance sheet for the rights and obligations created by all leases with terms of more than 12 months. The standard will apply to both types of leases-capital (or finance) leases and operating leases. Previously, GAAP has required only capital leases to be recognized on lessee balance sheets. The standard is effective for fiscal years beginning after December 15, 2018 and interim periods within fiscal years beginning after December 15, 2018. Early application will be permitted for all organizations. The Company has not yet selected a transition method and is currently evaluating the effect that the updated standard will have on the consolidated financial statements.

In August 2016, the FASB released ASU No. 2016-15, Classification of Certain Cash Receipts and Cash Payments, which addresses eight specific cash flow issues with the objective of reducing the existing diversity in practice. ASU 2016-15 became effective for the Company on January 1, 2018. ASU 2016-15 had no material impact on our consolidated financial statements.

In May 2017, the FASB issued ASU No. 2017-09, Compensation-Stock Compensation (Topic 718): Scope of Modification Accounting. The new guidance provides clarity and reduces both (1) diversity in practice and (2) cost and complexity when applying the guidance in Topic 718, Compensation-Stock Compensation, to a change to the terms or conditions of a share-based payment award. The accounting standard update became effective for the Company on January 1, 2018. ASU 2017-09 did not have any material impact on our consolidated financial statements.

2. Revenue Information

The following table disaggregates the Company’s revenue into primary product groups:

	Three months ended **June 30, 2018**	**Six months ended** **June 30, 2018**
Professional audio products	$ 4,871	$ 9,804
Unified Communications end points	977	2,013
Video products	1,123	2,443
	$ 6,971	$ 14,260

The following table disaggregates the Company's revenue into major regions:

	Three months ended **June 30, 2018**	**Six months ended** **June 30, 2018**
North and South America	$ 4,110	$ 8,456
Asia (including Middle East) and Australia	1,861	3,899
Europe and Africa	1,000	1,905
	$ 6,971	$ 14,260

3. Earnings (Loss) Per Share

Earnings (loss) per common share is computed based on the weighted-average number of common shares outstanding and, when appropriate, dilutive potential common stock outstanding during the period. Stock options are considered to be potential common stock. The computation of diluted earnings (loss) per share does not assume exercise or conversion of securities that would have an anti-dilutive effect.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited - Dollars in thousands, except per share amounts)

Basic earnings (loss) per common share is the amount of net earnings (loss) for the period available to each weighted-average share of common stock outstanding during the reporting period. Diluted earnings (loss) per common share is the amount of earnings (loss) for the period available to each weighted-average share of common stock outstanding during the reporting period and to each share of potential common stock outstanding during the period, unless inclusion of potential common stock would have an anti-dilutive effect.

The following table sets forth the computation of basic and diluted earnings (loss) per common share:

	Three months ended June 30,		Six months ended June 30,	
	2018	**2017**	**2018**	**2017**
Numerator:				
Net loss	$(2,163)	$(820)	$(4,009)	$(1,288)
Denominator:				
Basic weighted average shares outstanding	8,301,094	8,638,091	8,304,093	8,702,743
Dilutive common stock equivalents using treasury stock method	—	—	—	—
Diluted weighted average shares outstanding	8,301,094	8,638,091	8,304,093	8,702,743
Basic loss per common share	$(0.26)	$(0.09)	$(0.48)	$(0.15)
Diluted loss per common share	$(0.26)	$(0.09)	$(0.48)	$(0.15)
Weighted average options outstanding	724,373	869,838	736,160	858,845
Anti-dilutive options not included in the computations	724,373	869,838	736,160	858,845

4. Marketable Securities

The Company has classified its marketable securities as available-for-sale securities. These securities are carried at estimated fair value with unrealized holding gains and losses included in accumulated other comprehensive income (loss) in stockholders’ equity until realized. Gains and losses on marketable security transactions are reported on the specific-identification method. Dividend and interest income are recognized when earned.

The amortized cost, gross unrealized holding gains, gross unrealized holding losses, and fair value for available-for-sale securities by major security type and class of securities at June 30, 2018 and December 31, 2017 were as follows:

	Amortized cost	Gross unrealized holding gains	Gross unrealized holding losses	Estimated fair value
June 30, 2018				
Available-for-sale securities:				
Corporate bonds and notes	$ 4,857	$ —	$ (62)	$ 4,795
Municipal bonds	4,491	—	(43)	4,448
Total available-for-sale securities	$ 9,348	$ —	$ (105)	$ 9,243

	Amortized cost	Gross unrealized holding gains	Gross unrealized holding losses	Estimated fair value
December 31, 2017				
Available-for-sale securities:				
Corporate bonds and notes	$ 8,458	$ 19	$ (49)	$ 8,428
Municipal bonds	4,637	1	(28)	4,610
Total available-for-sale securities	$ 13,095	$ 20	$ (77)	$ 13,038

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited - Dollars in thousands, except per share amounts)

Maturities of marketable securities classified as available-for-sale securities were as follows at June 30, 2018:

	Amortized cost	Estimated fair value
June 30, 2018		
Due within one year	$ 2,862	$ 2,852
Due after one year through five years	6,332	6,239
Due after five years	154	152
Total available-for-sale securities	$ 9,348	$ 9,243

Debt securities in an unrealized loss position as of June 30, 2018 were not deemed impaired at acquisition and subsequent declines in fair value are not deemed attributed to declines in credit quality. Management believes that it is more likely than not that the securities will receive a full recovery of par value, although there can be no assurance that such recovery will occur. The available-for-sale marketable securities with continuous gross unrealized loss position for less than 12 months and 12 months or greater and their related fair values were as follows:

(In thousands)	Less than 12 months		More than 12 months		Total	
	Estimated fair value	Gross unrealized holding losses	Estimated fair value	Gross unrealized holding losses	Estimated fair value	Gross unrealized holding losses
As of June 30, 2018						
Corporate bonds and notes	$2,672	$ (24)	$1,866	$ (38)	$4,538	$ (62)
Municipal bonds	3,325	(32)	919	(11)	4,244	(43)
Total	$5,997	$ (56)	$2,785	$ (49)	$8,782	$ (105)

(In thousands)	Less than 12 months		More than 12 months		Total	
	Estimated	Gross unrealized	Estimated	Gross unrealized	Estimated	Gross unrealized

	fair value	holding losses	fair value	holding losses	fair value	holding losses
As of December 31, 2017						
Corporate bonds and notes	$3,799	$ (20)	$2,125	$ (30)	$5,924	$ (50)
Municipal bonds	3,341	(18)	657	(9)	3,998	(27)
Total	$7,140	$ (38)	$2,782	$ (39)	$9,922	$ (77)

5. Intangible Assets

Intangible assets as of June 30, 2018 and December 31, 2017 consisted of the following:

	Estimated useful lives (years)	June 30, 2018	December 31, 2017
Tradename	5 to 7	$555	$ 555
Patents and technological know-how	10 to 17	11,059	8,578
Proprietary software	3 to 15	2,981	2,981
Other	3 to 5	323	323
Total intangible assets		14,918	12,437
Accumulated amortization		(6,407)	(5,894)
Total intangible assets, net		$8,511	$ 6,543

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited - Dollars in thousands, except per share amounts)

The amortization of intangible assets for the three and six months ended June 30, 2018 and 2017 was as follows:

	Three months ended June 30,		**Six months ended June 30,**	
	2018	**2017**	**2018**	**2017**
Amortization of intangible assets	$(265)	$(231)	$(513)	$(468)

The estimated future amortization expense of intangible assets is as follows:

Years ending December 31,	**Amount**
2018 (Remainder)	$ 537
2019	1,010
2020	831
2021	831
2022	831
Thereafter	4,471
Total	$ 8,511

6. Inventories

Inventories, net of reserves, as of June 30, 2018 and December 31, 2017 consisted of the following:

	As of June 30, 2018	**December 31, 2017**
Current:		
Raw materials	$2,580	$ 197
Finished goods	11,799	14,218
	$14,380	$ 14,415

Long-term:		
Raw materials	$2,022	$ 2,682
Finished goods	6,329	6,026
	$8,351	$ 8,708

Long-term inventory represents inventory held in excess of our current (next 12 months) requirements based on our recent sales and forecasted level of sales. We expect to sell the above inventory, net of reserves, at or above the stated cost and believe that no loss will be incurred on its sale, although there can be no assurance of the timing or amount of any sales.

Current finished goods did not include distributor channel inventories in the amounts of approximately $1,555 as of December 31, 2017. Distributor channel inventories represented inventories at distributors and other customers where revenue recognition criteria had not yet been achieved.

Net loss incurred on valuation of inventory at lower of cost or net realizable value and write-off of obsolete inventory during the three and six months ended June 30, 2018 was $170 and $425, respectively. During the three months and six months ended June 30, 2017 net loss incurred on valuation of inventory at lower of cost or net realizable value and write-off of obsolete inventory was $55 and $21, respectively.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited - Dollars in thousands, except per share amounts)

7. Share-based Compensation

Employee Stock Option Plans

The Company's share-based incentive plans offering stock options are offered under the Company's 2007 Equity Incentive Plan (the "2007 Plan"), which was restated and approved by the shareholders on December 12, 2015. Provisions of the restated 2007 Plan include the granting of up to 2,000,000 incentive and non-qualified stock options, stock appreciation rights, restricted stock and restricted stock units. Options may be granted to employees, officers, non-employee directors and other service providers and may be granted upon such terms as the Compensation Committee of the Board of Directors determines in their sole discretion. As of June 30, 2018, there were 716,855 options outstanding under the 2007 Plan. As of June 30, 2018, the 2007 Plan had 777,839 authorized unissued options.

A summary of the stock option activity under the Company's plans for the six months ended June 30, 2018 is as follows:

	Number of shares	Weighted average exercise price
Options outstanding at beginning of year	764,430	$ 8.78
Granted	—	—
Less:		
Exercised	—	—
Forfeited prior to vesting	(22,290)	11.00
Canceled or expired	(25,285)	11.07
Options outstanding at June 30, 2018	716,855	8.63
Options exercisable at end of June 30, 2018	581,127	$ 8.13

As of June 30, 2018, the total remaining unrecognized compensation cost related to non-vested stock options, net of forfeitures, was approximately $495, which will be recognized over a weighted average period of 1.41 years.

Share-based compensation expense has been recorded as follows:

	Three months ended June 30,		Six months ended June 30,	
	2018	2017	2018	2017
Cost of goods sold	$4	$7	$9	$14
Sales and marketing	10	15	20	29
Research and product development	27	37	57	76
General and administrative	88	110	180	221
	$129	$169	$266	$340

8. Shareholders' Equity

Stock Repurchase Program

On March 9, 2016, the Board of Directors of the Company authorized the repurchase of up to $10,000 of the Company's outstanding shares of common stock under a stock repurchase program. In connection with the repurchase authorization, the Company was authorized to complete the repurchase through open market transactions or through an accelerated share repurchase program, in each case to be executed at management's discretion based on business and market conditions, stock price, trading restrictions, acquisition activity and other factors. The transactions effectuated to date occurred in open market purchases.

On March 1, 2017, the Board of Directors of the Company renewed and extended the repurchase program for up to an additional $10,000 of common stock over the next twelve months. In connection with the repurchase extension authorization, the Company was authorized to complete the repurchase through open market transactions or through an accelerated share repurchase program, in each case to be executed at management's discretion based on business and market conditions, stock price, trading restrictions, acquisition activity and other factors. The transactions effectuated to date occurred in open market purchases.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited - Dollars in thousands, except per share amounts)

Upon expiry of this repurchase program in March 2018, the program was not renewed again.

Cash Dividends

On February 21, 2018, the Company declared a cash dividend of $0.07 per share of ClearOne common stock. The dividend was paid on March 21, 2018 to shareholders of record as of March 7, 2018. On June 13, 2018, the Company announced the suspension of its dividend program.

9. Fair Value Measurements

The fair value of the Company's financial instruments reflects the amounts that the Company estimates it will receive in connection with the sale of an asset or pay in connection with the transfer of a liability in an orderly transaction between market participants at the measurement date (exit price). The fair value hierarchy prioritizes the use of inputs used in valuation techniques into the following three levels:

Level 1 - Quoted prices in active markets for identical assets and liabilities.

Level 2 - Observable inputs other than quoted prices in active markets for identical assets and liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. This category generally includes U.S. Government and agency securities; municipal securities; mutual funds and securities sold and not yet settled.

Level 3 - Unobservable inputs.

The substantial majority of the Company's financial instruments are valued using observable inputs. The following table sets forth the fair value of the financial instruments re-measured by the Company as of June 30, 2018 and December 31, 2017:

	Level 1		**Level 2**	**Level 3**		**Total**
June 30, 2018						
Corporate bonds and notes	$	-	$4,795	$	-	$4,795
Municipal bonds		-	4,448		-	4,448
Total	$	-	$9,243	$	-	$9,243

	Level 1		**Level 2**	**Level 3**		**Total**
December 31, 2017						
Corporate bonds and notes	$	-	$8,428	$	-	$8,428
Municipal bonds		-	4,610		-	4,610
Total	$	-	$13,038	$	-	$13,038

10. Income Taxes

The Company's forecasted effective tax benefit rate at June 30, 2018 is 26.8%, a 16% increase from the 10.8% effective tax rate recorded at December 31, 2017. The 16% increase is primarily due to the enactment in 2017 of the Tax Cuts and Jobs act, which resulted in a lower corporate tax rate and a revaluation of the Company's net deferred tax assets. The forecasted effective tax benefit rate of 26.8% excludes jurisdictions for which no benefit from forecasted current year losses is anticipated. Including losses from such jurisdictions results in a forecasted effective tax benefit rate of 26.0%. Our forecasted effective tax rate could fluctuate significantly on a quarterly basis and could change, to the extent that earnings in countries with tax rates that differ from that of the U.S. differ from amounts anticipated at June 30, 2018.

After a discrete tax expense of $64, the effective tax benefit rate for the quarter ended June 30, 2018 is 24.9%. The discrete tax expense of $64 is primarily attributable to changes in income tax reserves related to an income tax audit in Hong Kong.

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Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This report on Form 10-Q includes "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). All statements in this report, other than statements of historical fact, are forward-looking statements for purposes of these provisions, including any projections of earnings, revenues or other financial items, any statements of the plans and objectives of management for future operations, any statements concerning proposed new products or services, any statements regarding future economic conditions or performance, and any statements of assumptions underlying any of the foregoing. All forward-looking statements included in this report are made as of the date hereof and are based on information available to us as of such date. We assume no obligation to update any forward-looking statement. In some cases, forward-looking statements can be identified by the use of terminology such as "may," "will," "expects," "plans," "anticipates," "intends," "believes," "estimates," "potential," or "continue," or the negative thereof or other comparable terminology. Although we believe that the expectations reflected in the forward-looking statements contained herein are based upon reasonable assumptions at the time made, there can be no assurance that any such expectations or any forward-looking statement will prove to be correct. Our actual results will vary, and may vary materially, from those projected or assumed in the forward-looking statements. Future financial condition and results of operations, as well as any forward-looking statements, are subject to inherent risks and uncertainties, many of which we cannot predict with accuracy and some of which we might not anticipate, including, without limitation, product recalls and product liability claims; infringement of our technology or assertion that our technology infringes the rights of other parties; termination of supplier relationships, or failure of suppliers to perform; inability to successfully manage growth; delays in obtaining regulatory approvals or the failure to maintain such approvals; concentration of our revenue among a few customers, products or procedures; development of new products and technology that could render our products obsolete; market acceptance of new products; introduction of products in a timely fashion; price and product competition, availability of labor and materials, cost increases, and fluctuations in and obsolescence of inventory; volatility of the market price of our common stock; foreign currency fluctuations; changes in key personnel; work stoppage or transportation risks; integration of business acquisitions; and other factors referred to in our reports filed with the SEC, including our Annual Report on Form 10-K for the year ended December 31, 2017. All subsequent forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by these cautionary statements. Additional factors that may have a direct bearing on our operating results are discussed in Part I, Item 1A "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2017.

BUSINESS OVERVIEW

ClearOne is a global market leader enabling conferencing, collaboration, and network streaming solutions. The performance and simplicity of our advanced, comprehensive solutions offer unprecedented levels of functionality, reliability and scalability.

We derive most of our revenue from professional audio conferencing products by promoting our products in the professional audio-visual channel. We have extended our total addressable market from installed audio conferencing market to adjacent complementary markets – microphones, video collaboration and networked audio and video streaming. We have achieved this through strategic technological acquisitions as well as by internal product development.

In June 2018, at our industry's largest trade show in North America, we introduced new audio products including significant additions to our CONVERGE® 2 audio conferencing platform, ceiling microphone array product line, and wireless microphone systems in the newly FCC allocated 537-563 MHz range. We also introduced new video solutions including economical new SKUs to our VIEW® AV Networking platform and a second-generation video cloud solution, COLLABORATE® Space. During the six months ended June 30, 2018 seven more patents related to video synchronization, speech technology, integrated microphone array and ceiling or wall tile, echo cancellation with beamforming microphone array, audio distribution over local area networks, and USB to Bluetooth audio bridging were issued to us. While focusing on strategic innovation that we believe will strengthen our competitive position, and accelerated product development, we have also planned and initiated a company-wide cost cutting programs. We also continued our vigorous litigation efforts to stop infringement of two of our strategic patents.

Overall revenue declined in the three and six months ended June 30, 2018 when compared to the three months and six months ended June 30, 2017, with declines seen in all product categories. Our gross profit margin decreased to 47% during the three months ended June 30, 2018 from 59% for the three months ended June 30, 2017. Gross profit margin decreased primarily due to an increase in inventory obsolescence costs, a decline in licensing revenues and due to reduced overhead absorption into inventory as we continue to reduce our net spend on inventory. Our gross profit margin decreased to 52% during the six months ended June 30, 2018 from 58% for the six months ended June 30, 2017. Gross profit margin decrease was primarily due to an increase in inventory obsolescence costs, a decline in licensing revenues and due to reduced overhead absorption into inventory. The proportion of overhead costs absorbed into inventory has declined due to a sharp decline in our inventory purchasing activity causing increased amounts of overhead costs to be expensed.

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Industry conditions

We operate in a very dynamic and highly competitive industry which is dominated on the one hand by a few players with respect to certain products like traditional video conferencing appliances while on the other influenced heavily by a fragmented reseller market consisting of numerous regional and local players. The industry is also characterized by the influx of venture capitalist funded start-ups and private companies keen to win market share even at the expense of mounting financial losses.

Economic conditions, challenges and risks

The audio-visual products market is characterized by intense competition and rapidly evolving technology. Our competitors vary within each product category. The adoption of Beamforming Microphone Array 2, along with Converge Pro 2, our new platform for professional audio conferencing, remains challenged in large part because of our competitors' product offering that directly infringes our strategic patents. The patent infringement also has had a material adverse effect on our revenue from ClearOne's other products like wireless microphones, ceiling microphones and video products.

Our revenues in the near term may be materially adversely affected by the resignation of a large US distributor in June 2018.

Our strength in professional audio visual space is largely due to our industry leading conferencing technologies and the full suite of professional microphone products, especially Beamforming Microphone Arrays. Despite our strong leadership position in the professional audio communications products market, we face challenges to revenue growth due to the infringement of our patents by competitors, the limited size of the market and pricing pressures from new competitors attracted to the commercial market.

During 2018, revenue from our video products has generally shown lesser decline than revenue from audio conferencing products. However, this is not an identifiable trend given the continuing change in the competitive landscape and also the uncertainty relating to revenue from our core product set due to patent infringement and ensuing litigation. We face intense competition in this market from well-established market leaders as well as emerging players rich with marketing funds. We expect our strategy of combining Spontania, our cloud-based video conferencing product, Collaborate, our appliance-based media collaboration product and our high-end audio conferencing technology to distinguish us from our competitors' product offerings.

We derive a large portion of our revenue (about 48%) from international operations and expect this trend to continue in the future. Most of our revenue from outside the U.S. is billed in US Dollars and is not exposed to any significant currency risk.

A detailed discussion of our results of operations follows below.

Results of Operations for the three and six months ended June 30, 2018

The following table sets forth certain items from our unaudited condensed consolidated statements of operations (dollars in thousands) for the three and six months ended June 30, 2018 ("2018-Q2") ("2018-H1") and 2017 ("2017-Q2") ("2017-H1"), respectively, together with the percentage of total revenue which each such item represents:

	Three months ended June 30,			Six months ended June 30,		
	2018	**2017**	**Percentage Change 2018 vs. 2017**	**2018**	**2017**	**Percentage Change 2018 vs. 2017**
Revenue	$6,971	$10,311	(32)%	$14,260	21,989	(35)%
Cost of goods sold	3,721	4,242	(12)%	6,911	9,242	(25)%
Gross profit	3,250	6,069	(46)%	7,349	12,747	(42)%
Sales and marketing	2,760	2,646	4%	5,628	5,387	4%
Research and product development	1,920	2,322	(17)%	3,976	4,679	(15)%
General and administrative	1,542	2,210	(30)%	3,159	4,316	(27)%
Operating loss	(2,972)	(1,109)	(168)%	(5,414)	(1,635)	(231)%
Other income	49	84	(42)%	73	186	(61)%
Loss before income taxes	(2,923)	(1,025)	(185)%	(5,341)	(1,449)	(269)%
Provision for (benefit from) income taxes	(760)	(205)	(271)%	(1,332)	(161)	(727)%
Net loss	$(2,163)	$(820)	(164)%	$(4,009)	$(1,288)	(211)%

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Revenue

Our revenue decreased by $3.3 million, or 32%, to $7.0 million in 2018-Q2 compared to $10.3 million in 2017-Q2. All product categories witnessed revenue declines with revenue declines of 35%, 15% and 30% for professional audio conferencing, unified communication end points and video products, respectively. The decline in revenue from professional audio conferencing products was mostly due to slower adoption of our Converge Pro 2 platform, largely caused by our competitors' product offering that we believe directly infringes our strategic patents and due to a decline in licensing revenue. The share of professional audio communications products (which includes microphone products but not premium products) in our product mix declined from 73% in 2017-Q2 to 70% in 2018-Q2. Share of video products revenue during 2018-Q2 remained the same at 16% compared to 2017-Q2 and share of UC end points revenue increased from 11% in 2017-Q2 to 14% in 2018-Q2. During 2018-Q2, revenue declined across all regions except China and Latin America. The revenue declines for Asia Pacific including Middle East, Europe and Africa, and Americas were 16%, 10% and 41%, respectively.

Costs of Goods Sold and Gross Profit

Cost of goods sold ("COGS") includes expenses associated with finished goods purchased from outsourced manufacturers, the manufacture of our products (including material and direct labor), our manufacturing and operations organization, property and equipment depreciation, warranty expense, freight expense, royalty payments, and the allocation of overhead expenses.

Our gross profit for 2018-Q2 was approximately $3.3 million or 47% compared to approximately $6.1 million, or 59%, for 2017-Q2. Gross margin for 2018-Q2 declined due to an increase in inventory obsolescence costs, a decline in licensing revenues and reduced overhead absorption into inventory. The proportion of overheads absorbed into inventory has declined due to a sharp decline in our inventory purchasing activity causing increased amounts of overheads to be expensed as against being carried with our inventory. Even though the total overhead spending has not increased, the combination of lower revenues and lower absorption has caused gross margin as a percentage of revenue to decline.

Our gross profit for 2018-H1 was approximately $7.3 million or 52% compared to approximately $12.7 million, or 58%, for 2017-H1. Gross margin for 2018-H1 declined due to increased inventory obsolescence costs, a decline in licensing revenues and due to lower absorption of overheads into inventory.

Our profitability in the near-term continues to depend significantly on our revenues from professional audio conferencing products. We hold long-term inventory and if we are unable to sell our long-term inventory, our profitability might be affected by inventory write-offs and price mark-downs. Our long-term inventory includes approximately $2.7 million of wireless microphones related finished goods and assemblies, $2.7 million of Converge Pro 2 products and about $1.1 million of raw materials that will be used for manufacturing professional audio conferencing products. Any business changes that are adverse to these product lines could potentially impact our ability to sell these long-term inventory in addition to our current inventory.

Operating Expenses

Operating expenses include sales and marketing ("S&M") expenses, research and product development ("R&D") expenses and general and administrative ("G&A") expenses. Total operating expenses were $6.2 million for 2018-Q2 compared to $7.2 million for 2017-Q2. Total operating expenses for 2018-H1 were $12.8 million compared to $14.4 million for 2017-H1. The following contains a more detailed discussion of expenses related to sales and marketing, research and product development, general and administrative, and other items.

Sales and Marketing - S&M expenses include selling, customer service, and marketing expenses such as employee-related costs, allocations of overhead expenses, trade shows, and other advertising and selling expenses.

S&M expenses for 2018-Q2 increased to $2.8 million from $2.6 million for 2017-Q2. The increase was mainly due to an increase in employee related costs partially offset by a decline in tradeshow related expenses. S&M expenses for 2018-H1 increased to $5.6 million from $5.4 million for 2017-H1. The increase was mainly due to an increase in employee related costs including commissions and an increase in marketing expenses.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Research and Product Development - R&D expenses include research and development, product line management, engineering services, and test and application expenses, including employee related costs, outside services, expensed materials, depreciation, and an allocation of overhead expenses.

R&D expenses were approximately $1.9 million for 2018-Q2, as compared to $2.3 million for 2017-Q2. The decrease was primarily due to reductions in project related expenses and employee costs related to salaries and benefits. R&D expenses were approximately $4.0 million for 2018-H1, as compared to $4.7 million for 2017-H1. The decrease was primarily due to reductions in project related expenses and employee costs related to salaries and benefits.

General and Administrative - G&A expenses include employee-related costs, professional service fees, allocations of overhead expenses, litigation costs, and corporate administrative costs, including costs related to finance and human resources.

G&A expenses decreased approximately 30% to $1.5 million for 2018-Q2 compared with approximately $2.2 million in 2017-Q2. The reduction was primarily due to the decrease in legal costs and employee costs related to salaries and benefits. Legal expenses in 2018-Q2 reduced mostly because of capitalization of legal costs related to our defense of strategic patents from infringement amounting to $1.1 million. No legal expenses were capitalized in 2017-Q2.

G&A expenses in 2018-H1 was $3.2 million compared to $4.3 million in 2017-H1. The decline of approximately 27% was primarily due to the decrease in legal costs and employee costs related to salaries and benefits. Legal expenses in 2018-H1 reduced mostly because of capitalization of legal costs related to our defense of strategic patents from infringement amounting to $2.4 million. No legal expenses were capitalized in 2017-H1.

Other income (expense), net

Other income (expense), net, includes interest income, interest expense, and foreign currency changes.

Other income reduced in 2018-Q2 and 2018-H1 due to reduction in interest income caused by decline in the investment holdings and due to higher realized losses on liquidated investments.

Provision for income taxes

During the six months ended June 30, 2018, we accrued income taxes at the forecasted effective tax benefit rate of 26.8% as compared to the forecasted effective tax rate of 127% used during the six months ended June 30, 2017. The 100.2% decrease in the forecasted effective tax rate was primarily due to the reduction in U.S. federal corporate tax rates as a result of the enactment of the Tax Cuts and Jobs Act and losses in certain foreign jurisdictions which cannot be benefited, which had a greater impact on the effective rate in 2017 due to differences in forecasted income as compared to 2018. In addition, a discrete tax expense of $64 thousand is primarily attributable to changes in income tax reserves related to an income tax audit in Hong Kong.

LIQUIDITY AND CAPITAL RESOURCES

As of June 30, 2018, our cash and cash equivalents were approximately $4.1 compared to $5.6 million as of December 31, 2017. Our working capital was $23.2 million and $23.3 million as of June 30, 2018 and December 31, 2017, respectively.

Net cash used in operating activities was approximately $1.9 million for the six months ended June 30, 2018, a decrease of cash used of approximately $2.8 million from $4.7 million of cash used in operating activities in the six months ended June 30, 2018. The decrease in cash used was primarily due to an increase in cash inflows due to change in operating assets and liabilities of $6.1 million partially offset by an increase in net loss by $2.7 million and decrease in non-cash charges of $0.6 million.

Net cash provided by investing activities was $1.1 million for the six months ended June 30, 2018 compared to net cash flows provided by investing activities of $49 thousand during the six months ended June 30, 2018, an increase in cash provided of $1.1 million. The increase was primarily due to an increase in proceeds from marketable securities net of purchases of approximately $3.1 million, partially offset by $2.4 million in capitalization of patent defense costs.

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Capitalization of patent defense costs. We capitalize external legal costs incurred in the defense of our patents when we believe that a significant, discernible increase in value will result from the defense and a successful outcome of the legal action is probable. When we capitalize patent defense costs we amortize the costs over the remaining estimated useful life of the patent, which is 15 to 17 years. During the six months ended June 30, 2018 we spent $2.4 million of legal costs related to the defense of our patents and capitalized the entire amount.

Net cash used in financing activities was approximately $0.7 million during the six months ended June 30, 2018, which consisted of cash outflows of $0.1 million on repurchase and cancellation of stock and $0.6 million for dividend payments. Net cash used in financing activities was approximately $4.2 million during the six months ended June 30, 2017, which consisted of cash outflows of $3.2 million on repurchase and cancellation of stock and stock options and $1.1 million for dividend payments.

We are currently pursuing all available legal remedies to defend our strategic patents from infringement. We have already incurred approximately $6.2 million from 2016 through June 30, 2018 towards this litigation and may be required to incur more to continue to enforce our patents. We have been actively engaged in preserving cash by suspending our dividend program, allowing the share repurchase program to expire and implementing company-wide cost reduction measures. In addition, we expect to generate additional cash as our inventory levels are brought down to historical levels. We also believe, although there can be no assurance, that the measures taken by us will yield higher revenues in the future. We believe all of these and effective management of working capital will provide the liquidity needed to meet our short-term and long-term operating requirements and finance our growth plans. We also believe that our strong portfolio of intellectual property and our solid brand equity in the market will enable us to raise additional capital if and when needed to meet our short and long-term financing needs, although there can be no assurance that we would be able to do so on terms that are acceptable to us or at all. In addition to capital expenditures, we may use cash in the near future for selective infusions of technology, sales and marketing, infrastructure, and other investments to fuel our growth.

At June 30, 2018, we had open purchase orders related to our electronics manufacturing service providers of approximately $2.0 million, primarily related to inventory purchases.

At June 30, 2018, we had inventory totaling $22.7 million, of which non-current inventory accounted for $8.4 million. This compares to total inventories of $24.7 million and non-current inventory of $8.7 million as of December 31, 2017. Our non-current inventory includes approximately $2.7 million of wireless microphones related finished goods and assemblies, $2.7 million of Converge Pro 2 products and about $1.1 million of raw materials that will be used for manufacturing professional audio conferencing products. Any business changes that are adverse to these product lines could potentially impact our ability to sell these long-term inventory in addition to our current inventory.

OFF-BALANCE SHEET ARRANGEMENTS

We have no off-balance-sheet arrangements that have or are reasonably likely to have a current or future material effect on our financial condition, changes in financial conditions, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources, results of operations or liquidity.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our discussion and analysis of our results of operations and financial position are based upon our unaudited consolidated financial statements included under Item 1 of this Form 10-Q, which have been prepared in conformity with accounting principles generally accepted in the United States. We review the accounting policies used in reporting our financial results on a regular basis. We believe certain of our accounting policies are critical to understanding our financial position and results of operations. Except with respect to our revenue recognition practices included in Note 1. “Business Description, Basis of Presentation and Significant Accounting Policies” under Item 1 of this Form 10-Q, there have been no changes to the critical accounting policies as explained in our 2017 Form 10-K.

RECENT ACCOUNTING PRONOUNCEMENTS

For a discussion of recent accounting pronouncements, see Note 3: “Recent Accounting Pronouncements” in the notes to our unaudited consolidated financial statements included under Item 1 of this Form 10-Q.

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not applicable.

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ITEM 4. CONTROLS AND PROCEDURES

An evaluation of the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act) as of June 30, 2018 was performed under the supervision and with the participation of our management, including our Chief Executive Officer and our Principal Financial and Accounting Officer. Based upon this evaluation, our Chief Executive Officer and Senior Vice President of Finance concluded that, as of the end of the period covered by this Quarterly Report, our disclosure controls and procedures were not effective at a reasonable assurance level as of June 30, 2018 due to the material weakness in internal control over financial reporting as described below.

Management identified a material weakness in the operating effectiveness of internal control over financial reporting relating to the accurate and timely reporting of its financial results and disclosures and its testing and assessment of the design and effectiveness of internal controls over financial reporting in a timely manner.

To address the material weakness, management is working with our third party internal controls consultant to assist with the implementation of a remediation plan which will supplement the existing controls. The remediation plan will include an assessment of personnel levels and responsibilities, additional training of financial reporting personnel and ability to handle new requirements and projects on a timely basis with respect to the preparation of the consolidated financial statements and public company reporting requirements and timelines. The material weakness will be fully remediated when, in the opinion of management, the control processes have been operating for a sufficient period of time to provide reasonable assurance as to their effectiveness. The remediation and ultimate resolution of the material weakness will be reviewed with the Audit Committee of the Board of Directors.

Except as noted above, there has been no change in the Company's internal control over financial reporting as of June 30, 2018, that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1. LEGAL PROCEEDINGS

There have been no material developments in the legal proceedings described in our Annual Report on Form 10-K for the year ended December 31, 2017.

Item 1A. RISK FACTORS

There have been no material changes to the risk factors included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2017.

Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

(a) None.

(b) Not applicable.

(c) None.

Item 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

Item 4. MINE SAFETY DISCLOSURES

Not applicable.

Item 5. OTHER INFORMATION

Not applicable.

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Item 6. EXHIBITS

Exhibit No.	Title of Document
31.1	Section 302 Certification of Chief Executive Officer (filed herewith)
31.2	Section 302 Certification of Principal Financial Officer (filed herewith)
32.1	Section 906 Certification of Chief Executive Officer (filed herewith)
32.2	Section 906 Certification of Principal Financial Officer (filed herewith)
101.INS	XBRL Instance Document (filed herewith)
101.SCH	XBRL Taxonomy Extension Schema (filed herewith)
101.CAL	XBRL Taxonomy Extension Calculation Linkbase (filed herewith)
101.DEF	XBRL Taxonomy Extension Definitions Linkbase (filed herewith)
101.LAB	XBRL Taxonomy Extension Label Linkbase (filed herewith)
101.PRE	XBRL Taxonomy Extension Presentation Linkbase (filed herewith)

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SIGNATURES

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

	ClearOne, Inc.,
	(Registrant)
	By: */s/ Zeynep Hakimoglu* Zeynep Hakimoglu
August 9, 2018	President, Chief Executive Officer and Chairman of the Board
	(Principal Executive Officer)
	By: */s/ Narsi Narayanan* Narsi Narayanan
August 9, 2018	Senior Vice President of Finance
	(Principal Accounting and Principal Financial Officer)