CLEARONE INC
Form 10-K
April 20, 2018

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

(Mark One)

[X]	**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
	For the fiscal year ended December 31, 2017
[ ]	**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
	For the transition period from _________ to _________

Commission file number 001-33660

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)

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

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

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

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

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

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

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. [X] Yes [ ] 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). [X] Yes [ ] No

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, 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 [ ]	Smaller Reporting Company [ ]
		(Do not check if a 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. [ ]

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Indicate by check mark whether the registrant is a shell Company (as defined in Rule 12b-2 of the Act). [ ] Yes [X] No

The aggregate market value of the shares of voting common stock held by non-affiliates was approximately $51.2 million at June 30, 2017 **,** (the Company's most recently completed second fiscal quarter), based on the $9.43 closing price for the Company's common stock on the NASDAQ Capital Market on such date. For purposes of this computation, all officers, directors, and 10% beneficial owners of the registrant are deemed to be affiliates. Such determination should not be deemed to be an admission that such officers, directors, or 10% beneficial owners are, in fact, affiliates of the registrant.

The number of shares of ClearOne common stock outstanding as of April 20, 2018 was 8,301,473.

DOCUMENTS INCORPORATED BY REFERENCE

Information required by Part III is incorporated by reference from registrant's proxy statement for the 2017 annual meeting of shareholders or an amendment to this Annual Report on Form 10-K, which will be filed with the Securities and Exchange Commission within 120 days after the end of its fiscal year ended December 31, 2017.

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CLEARONE, INC.

ANNUAL REPORT ON FORM 10-K FOR THE YEAR ENDED DECEMBER 31, 2017

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This report contains forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. These statements reflect our views with respect to future events based upon information available to us at this time. These forward-looking statements are subject to uncertainties and other factors that could cause actual results to differ materially from these statements. Forward-looking statements are typically identified by the use of the words "believe," "may," "could," "will," "should," "expect," "anticipate," "estimate," "project," "propose," "plan," "intend," and similar words expressions. Examples of forward-looking statements are statements that describe the proposed development, manufacturing, and sale of our products; statements that describe expectations regarding pricing trends, the markets for our products, our anticipated capital expenditures, our cost reduction and operational restructuring initiatives, and future impact of regulatory developments; statements with regard to the nature and extent of competition we may face in the future; statements with respect to the anticipated sources of and need for future financing; and statements with respect to future strategic plans, goals, and objectives and forecasts of future growth and value. Forward-looking statements are contained in this report under "Business" included in Item 1 of Part I, and "Management's Discussion and Analysis of Financial Condition and Results of Operations" included in Item 7 of Part II of this Annual Report on Form 10-K. The forward-looking statements are based on present circumstances and on our predictions respecting events that have not occurred, that may not occur, or that may occur with different consequences and timing than those now assumed or anticipated. Actual events or results may differ materially from those discussed in the forward-looking statements as a result of various factors, including the risk factors discussed in this report under the caption "Item 1A Risk Factors." These cautionary statements are intended to be applicable to all related forward-looking statements wherever they appear in this report. The cautionary statements contained or referred to in this report should also be considered in connection with any subsequent written or oral forward-looking statements that may be issued by us or persons acting on our behalf. Any forward-looking statements are made only as of the date of this report and we assume no obligation to update forward-looking statements to reflect subsequent events or circumstances.

PART I

References in this Annual Report on Form 10-K to "ClearOne," "we," "us," "CLRO" or "the Company" refer to ClearOne, Inc a Utah corporation, and, unless the context otherwise requires or is otherwise expressly stated, its subsidiaries.

ITEM 1. BUSINESS

GENERAL

ClearOne (the Company) was formed as a Utah corporation in 1983 organized under the laws of the State of Utah. The Company is headquartered in Salt Lake City, Utah, with locations in Gainesville, Florida; Austin, Texas; Corvallis, Oregon; Hong Kong; India, Israel, Spain and United Arab Emirates.

We are a global company that designs, develops and sells conferencing, collaboration and network streaming solutions for voice and visual communications. The performance and simplicity of our advanced comprehensive solutions offer unprecedented levels of functionality, reliability and scalability.

We design, develop, market, and service a comprehensive line of high-quality conferencing and collaboration products for personal use, as well as traditional tabletop, mid-tier premium and higher-end professional products for large, medium and small businesses. We occupy the number one global market share position, with more than 50% market share in the professional audio conferencing market for our products used by large businesses and organizations such as enterprise, healthcare, education and distance learning, government, legal and finance. Our solutions save organizations time and money by creating a natural environment for collaboration and communication.

We have an established history of product innovation and plan to continue to apply our expertise in audio, video and network engineering to develop and introduce innovative new products and enhance our existing products. Our end-users range from some of the world’s largest and most prestigious companies and institutions to small and medium-sized businesses, higher education and government organizations, as well as individual consumers. We sell our commercial products to these end-users primarily through a global network of independent distributors who, in turn, sell our products to dealers, systems integrators and other value-added resellers.

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ITEM 1-BUSINESS

Acquisitions

We believe that attractive acquisition opportunities may arise in the future. We intend to pursue strategic acquisition opportunities that would grow our customer base, expand our product lines, enhance our manufacturing and technical expertise, or otherwise complement our business or further our strategic goals.

Company Information

Our website address is www.clearone.com. Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and any amendments to such reports are available, free of charge, on our website in the "Investor Relations" section under "Company." These reports are made available as soon as reasonably practicable after we file such material with, or furnish it to, the SEC.

For a discussion of certain risks applicable to our business, results of operations, financial position, and liquidity, see the risk factors described in "Item 1A, Risk Factors" below.

Our Business Strategy

We currently participate in the following markets:

Professional audio visual, including audio conferencing, web conferencing and video conferencing and collaboration;
Professional microphones which includes our patented beamforming microphones, ceiling microphones and wireless microphones;
Media collaboration including interactive whiteboarding, webinar, wireless sharing and training tools;
Network streaming which includes audio and video networking, media streaming and video walls; and
Unified communications, including telephony.

Our business goals are to:

- Maintain our leading global market share in professional audio conferencing products for large businesses and organizations;
- Position ClearOne as the preferred AV channel partner uniquely offering a complete value-chain of natively integrated solutions from audio to video maximizing AV partner profitability;
- Extend total addressable market from installed audio beachhead to adjacent complementary markets – microphones, video collaboration and networked audio and video streaming;
- Continue to leverage the video conferencing, collaboration and network streaming technologies to enlarge our current market share;
- Focus on the small and medium business (SMB) market with scaled, lower cost and less complex products and solutions;
- Capitalize on the growing influence of information technology channels in the audio-visual market and introduce more products to these channels;
- Capitalize on emerging market trends as audio visual, information technology, and digital signage converge to meet enterprise and commercial multimedia needs and the users shift from high-priced systems to low cost appliances and cloud solutions;
- Leverage software-based platforms to provide disruptive cloud and networked video conferencing, collaboration and streaming solutions that complement our audio solutions;
- Expand and strengthen our sales channels;
- Consider disciplined strategic acquisitions

We will continue to focus on our core strengths, which include the following:

- Providing a superior conferencing and collaboration experience;
- Delivering the complete value chain for audio visual communication;
- Significantly impacting network streaming and control;
- Offering greater innovation, interoperability and value to our customers and partners;
- Leveraging and extending ClearOne technology, leadership and innovation;
- Leveraging our strong domestic and international channels to distribute new products; and
- Strengthening existing customer and partner relationships through dedicated support.

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ITEM 1- BUSINESS

PRODUCTS

Our products can be broadly categorized into the following:

- Professional audio conferencing including professional microphones
- Visual communication products including media collaboration and network streaming
- Unified communications audio end points

PROFESSIONAL AUDIO CONFERENCING INCLUDING MICROPHONES

Our full range of professional audio communication products includes (i) professional conferencing and sound-reinforcement products used in enterprise, healthcare, education and distance learning, government, legal and finance organizations, (ii) mid-tier premium conferencing products for smaller rooms and small and medium businesses which interface with video and web conferencing systems, and (iii) professional microphones used in various applications.

Our professional audio communication products, including premium conferencing and professional microphones, contributed 73%, 78% and 80% of our consolidated revenue in 2017, 2016 and 2015, respectively.

Our professional audio communication products and unified communications audio end points feature our proprietary HDConference®, Distributed Echo Cancellation® and noise cancellation technologies to enhance communication during a conference call by eliminating echo and background noise. Most of our products also feature some of our other HDConference proprietary audio processing technologies such as adaptive modeling and first-microphone priority, which combine to deliver clear, crisp and full-duplex audio. These technologies enable natural and fatigue-free communication between distant conferencing participants.

Professional Conferencing, Sound Reinforcement

We occupy the number one position in the global professional audio conferencing market with more than 50% of the total global market share. We have been developing high-end, professional conferencing products since 1991 and believe we have established strong brand recognition for these products worldwide. Our professional conferencing products include the CONVERGE® Pro 2, CONVERGE Pro and CONVERGE SR product lines.

Our flagship CONVERGE Pro 2 and CONVERGE Pro product lines lead our professionally installed audio products line. The CONVERGE Pro product line includes the CONVERGE Pro 880, CONVERGE Pro 880T, CONVERGE Pro 880TA, CONVERGE Pro 840T, CONVERGE Pro 8i, CONVERGE Pro TH20 and CONVERGE Pro VH20, and CONVERGE SR product line including CONVERGE SR1212 and SR1212A which together offer various levels of integration and features to allow a commercial system integrator to optimize a system to fit diverse conferencing applications and environments.

We started shipping some of the SKUs of the next generation of CONVERGE Pro products broadly called as CONVERGE Pro 2 at the end of 2016. We added more SKUs to CONVERGE Pro 2 line which now includes CONVERGE Pro 2 128, CONVERGE Pro 2 128D, CONVERGE Pro 2 128T, CONVERGE Pro 2 128TD, CONVERGE Pro 2 128V, CONVERGE Pro 2 128VD, CONVERGE Pro 2 120, CONVERGE Pro 2 012, CONVERGE Pro 2 48T, CONVERGE Pro 2 48V, CONVERGE Pro 2 128SR and CONVERGE Pro 2 128SRD. We have been shipping all SKUs in the CONVERGE Pro 2 line of products in 2017.

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ITEM 1 - BUSINESS

CONVERGE Pro 2's broad DSP platform satisfies clients' diverse audio needs with these features:

- The very latest and most powerful audio DSP algorithms, including acoustic echo cancellation, noise cancellation, feedback elimination, gain and level control, and microphone gating;
- More microphone inputs to supply greater flexibility;
- Integration of VoIP or telephony, USB, and Dante™ for maximum functionality;
- A new expansion bus that delivers increased audio-channel scalability to support large audio projects;
- New native interface that enables daisy-chaining for any combination of ClearOne peripheral devices, such as the new Beamforming Microphone Array 2, USB Expander unit, GPIO Expander unit and/or the new DIALOG® 20 Wireless Microphone system; and
- New software that includes both a traditional matrix view and the unique ClearOne FlowView™.

CONVERGE Pro 2 line of products is ably supported by a touch panel controller, a GPIO expansion box and a USB expansion box. CONVERGE Pro 2 VoIP SKUs are certified to interoperate with Cisco, Avaya and ShoreTel SIP based VoIP systems. It also interoperates with Microsoft Skype for Business.

Mid-Tier Premium Conferencing

Our INTERACT® product line is a mid-tier, lower cost, conferencing product line designed to meet the needs of our larger customers with smaller conferencing rooms as well as small and medium businesses. The INTERACT product series is comprised of the INTERACT AT and the INTERACT Pro. Both systems can be easily connected to enterprise telephones, analog POTS lines, existing HD video codecs and soft video clients. These INTERACT systems also include a USB audio interface to connect to PCs, laptops and tablets, as well as to rich multimedia devices, such as video or web conferencing systems and emerging unified communication systems for enhanced collaboration.

Professional Microphones: Beamforming Microphone Array

The ClearOne Beamforming Microphone Array is the Pro-Audio industry's first professional-grade microphone array with Beamforming and smart beam selection and ClearOne's next-generation Acoustic Echo Cancellation. The ultra-sleek design fits into any conferencing environment and delivers the clearest audio pickup available. The 24 microphone element industry-leading Beamforming Microphone Array has focused acoustic beams, digital signal processing, smart beam selection, and acoustic echo canceling to produce the clearest and most intelligible conferencing sound possible. ClearOne began shipping the Beamforming Microphone Array in March 2013. During the first quarter of 2014, we began shipping the Beamforming Microphone Array, including table, wall and ceiling applications, in black to increase market compatibility. This product works with CONVERGE Pro 880, CONVERGE Pro 880T, CONVERGE Pro 880TA and CONVERGE Pro 840T.

Beamforming Microphone Array 2, the next generation Beamforming Microphone Arrays started shipping in the last quarter of 2017. The Beamforming Microphone Array 2 affirms ClearOne's clear industry leadership in delivering:

Significantly enhanced and new echo cancellation, using direction of arrival determination for demanding acoustic environments;
Faster convergence and better adaptation to changes in room acoustics, such as ambient noise from chairs moving, doors closing, chatter in the background, or any spikes in sound that alter the path of the audio, using separate acoustic echo cancellation for each fixed beam and inhibiting beam selection when the far end is active;
Dramatically better mic pickup, including using an augmenting microphone signal, sharpening the capability to detect softer voices;
Natural and clearly intelligible audio, even when two people speak at once; and
Zero consumption of analog mic inputs in the CONVERGE Pro 2 suite of DSP mixers.

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Professional Microphones: Ceiling Microphone Array

The ClearOne Ceiling Microphone Array enhances almost any professional conferencing application which demands high-quality audio. The Ceiling Microphone Array is easily installed and combines affordability with exceptional audio quality. With three wide-range microphones mounted together into a single unit array, the Ceiling Microphone Array provides the rich sound of three individual unidirectional microphones while maintaining full 360-degree coverage.

Professional Microphones: Wireless Microphones

In 2013 ClearOne introduced WS800 Wireless Microphone Systems, including four new models of wireless microphones/transmitters (Tabletop/boundary, Gooseneck, Handheld, Bodypack) and a base-station receiver with either 4 or 8 channels, which connect to professional audio mixers. Since the Sabine acquisition in 2014, our portfolio of wireless microphone systems was enhanced by the introduction of digital compressed versions, Dante standard compatible versions and more frequency ranges catering to various international markets.

During 2017, we started shipping DIALOG® 20, the two-channel wireless microphone system. Leveraging the full power of ClearOne's robust, adaptive frequency-hopping "spread" spectrum technology within the 2.4 GHz unlicensed spectrum, DIALOG 20 has several advantages over fixed-frequency transmission. DIALOG 20 incorporates flexible features and multiple options usually available only in much larger systems. While DIALOG 20 works seamlessly with all commercially available mixers, it boasts additional features when natively interfacing with our new CONVERGE Pro 2 or new Beamforming Microphone Array 2.

UNIFIED COMMUNICATIONS AUDIO END POINTS

Our unified communications audio end points include (i) traditional tabletop conferencing phones used in conference rooms and offices and (ii) affordable personal conferencing products that can be used with PCs, laptops, tablets, smartphones, and other portable devices. Our unified communications audio end points contributed approximately 9%, 11% and 13% of our consolidated revenue in 2017, 2016 and 2015, respectively.

Tabletop Conferencing

Our MAX® product line is comprised of the following product families: MAX EX and MAXAttach® wired conference phones; MAX Wireless and MAXAttach Wireless; and MAX IP and MAXAttach IP tabletop conferencing phones. Designed for use in executive offices or small conference rooms with multiple participants, MAX Wireless can be moved from room to room within 150 feet of its base station. MAXAttach Wireless was the industry's first and remains the only dual-phone, completely wireless solution. This system gives customers tremendous flexibility in covering larger conference room areas. MAX EX and MAXAttach wired phones can be daisy chained together, up to a total of four phones. This provides even distribution of microphones, loudspeakers, and controls for better sound quality and improved user access in medium to large conference rooms. In addition, all MAXAttach wired phones can be used separately when they are not needed in a daisy-chain configuration. MAX IP and MAXAttach IP are VoIP tabletop conference phones which are based on the industry-standard SIP signaling protocol. These phones can also be daisy-chained together, up to a total of four phones.

Speakerphone

Our CHAT® product line includes affordable and stylish personal speakerphones and USB headsets. CHAT speakerphones provide full-duplex and rich full bandwidth frequency response for superior audio clarity. CHAT products are designed for a wide variety of applications and devices (fixed or portable) for greatly enhanced collaboration wherever and whenever needed. CHAT speakerphones are offered either as personal speakerphones under CHAT 50, CHAT 60 or CHAT 70 SKUs or as group speakerphones under CHAT 150, CHAT 160 and CHAT 170 SKUs.

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CHAT 50/60/70 personal speakerphones are approximately the size of a deck of cards, and connect to PCs and MACs for rich, clear, hands-free audio and playback. CHAT 150 group speakerphones are designed for small group use. These can also connect many of the same devices and applications as the CHAT personal speakerphones but feature three microphones in larger design for use by a larger number of participants. CHAT 150/160/170 group speakerphones have the ability to add high-quality, full-duplex speakerphones to user enterprise telephone handsets such as Avaya and Cisco. CHAT group speakerphones make it possible to introduce rich, crystal clear conferencing capability without the need for introducing a separate traditional conference phone. CHATAttach® is comprised of two CHAT 150 group speakerphones which can be daisy-chained together to function as a single conferencing system for much larger coverage than a single CHAT 150.

VISUAL COMMUNICATIONS

Our visual communication products include media collaboration and network streaming products. Our visual communication products contributed 18%, 11% and 7% of our consolidated revenue in 2017, 2016 and 2015, respectively.

Media Collaboration:

Our Media Collaboration suite of products is led by our comprehensive portfolio of industry-leading COLLABORATE® branded HD videoconferencing solutions.

COLLABORATE Pro 300: includes video appliance, UNITE® 150 camera, CHAT® 150C speakerphone and 90-days subscription to Spontania cloud video, audio and web conferencing, SIP/H.323 video conferencing, in-room wireless presentation and optional Skype® for Business native integration. This solution is targeted for huddle and small-size rooms.

COLLABORATE Pro 600: includes video appliance, UNITE 200 camera, CHATAttach® 150 speakerphones, and 90-days subscription to Spontania cloud video, audio and web conferencing, SIP/H.323 video conferencing with 4-way built-in MCU, in-room wireless presentation, optional Skype for Business native integration, capture recording and streaming. This solution is targeted at medium-size rooms.

COLLABORATE Pro 900: includes video appliance, UNITE 200 camera, CONVERGE® Pro installed audio endpoint, Beamforming Microphone Array and 90-days subscription to Spontania cloud video, audio and web conferencing, SIP/H.323 video conferencing with 4-way built-in MCU, multi-user in-room wireless presentation, optional Skype for Business native integration, capture recording and streaming. This solution is targeted at medium and large-size rooms.

Our Media Collaboration series also includes Spontania cloud video, audio and web conferencing service that can be deployed on-premises or in the cloud. Spontania offers all sort of collaboration tools such as screen sharing, application sharing, whiteboard, annotation over presentation, recording, hand-raise and chat. The service is targeted for any workspace including mobile, desktop and rooms of any size; and multiple use cases including meetings, classrooms and training sessions.

Bring your own video and web conferencing – COLLABORATE Versa 150 includes USB PTZ camera, speakerphone and central hub that connects the laptop to the meeting room peripherals via single USB 3.0 connectivity. COLLABORATE Versa 150, compatible with Cisco WebEx, Google Hangouts, Microsoft Skype for Business and more, is also bundled with 90-days free subscription of Spontania cloud video, audio and web conferencing. This solution is targeted at huddle spaces and medium conference rooms.

UNITE 200/150 is a professional-grade PTZ camera series supporting USB, HDMI and IP connectivity. It delivers 1080p HD resolution, 12X optical zoom and is compatible with PC-based and Pro-AV applications, supporting wide range of meeting spaces.

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Network Media Streaming and Digital Signage:

Our network media streaming products are primarily sold under VIEW™ and VIEW Pro brands deliver the ultimate IP A/V experience by streaming time sensitive high definition audio and video and control over TCP/IP networks. By combining audio and/or video content, meta-data and control signals into one digital stream in harmony with industry standards, its distributed, edge of the network architecture allows the hardware and the processing power to be distributed across any existing TCP/IP network. This leverages many of the advantages of using TCP/IP over traditional analog systems and other centrally controlled IP-based systems. The ClearOne VIEW and VIEW Pro products are powered by ClearOne's patented StreamNet® technology. A user can activate and control a single audio source or combination of audio sources, video sources, security systems, HVAC systems, lighting, and other room or facility monitoring functions such as paging or security access by just a single touch to its attractive touch screens. Alternatively, any PC, laptop, tablet, iPod, or other device with a built-in web browser with Flash can control the equipment connected to the system. The VIEW and VIEW Pro systems have no limits on the numbers of sources, displays, or amplifiers in a project and can be used in venues from high-end residential homes to large-scale commercial projects. The number of devices could be determined by the network bandwidth availability, number of media streams and its bandwidth requirements.

Converting an audio or video signal to TCP/IP preserves the digital quality of the signal across the network. Unlike analog systems, which lose quality over long distances, TCP/IP packets are decoded to retain the same digital quality as contained when they were encoded. The addition of Digital Encoder and Digital Decoder products with DVI/HDMI input and output enhances the flexibility of complete AV distribution system and makes it as easy to use as analog devices.

VIEW Pro solution provides 1080p60, H.264 high definition HDMI video-audio, 4:4:4 true-color, 24 bit per pixel video output. It comes with dual inputs encoder, single input encoder and single output decoder with balanced audio, general purpose control ports and clock synchronized video output. VIEW Pro system also provides PANORAMA™ , a multi-view video composition and video-wall software application using its built-in video processing engine, without using external expensive hardware video processors. This continues to be truly differentiated in the professional market by offering complete AV streaming and distribution systems that can scale to fulfill projects of any size and complexity, from light commercial to the very largest environments. VIEW Pro products include E110 and E120 encoders and D110, D210 and D310 decoders. VIEW Pro solution also comes with multiple license options including audio mixing, video composition, video wall, multicast RTSP and local playback.

During the second quarter of 2016, we introduced the new VIEW CONSOLE configuration management software. This software gives integrators a comprehensive platform from which to configure, manage, monitor, and control VIEW system installation using an easy, modern interface. The new toolset, which spotlights the latest in advanced software development technologies, works across ClearOne's full line of VIEW/VIEW Pro products. In 2017, we released an updated version of VIEW CONSOLE and PANORAMA software applications.

At the end of May 2016, we introduced a new flexible and single-channel-priced VIEW® Pro E110 Encoder — designed for single-media input settings. E110 Encoder delivers high-quality video with configurable 4:4:4 and 4:2:0 color sampling; standards-based streaming formats; 1080p60, H.264-based, high-profile encoding with lossless compression; very low end-to-end latency; and full HDCP support. We also introduced the innovative new entry-level VIEW Pro D310 Decoder featuring all the basic functionality to fully satisfy simple applications while delivering superb price-to-performance value. D310 Decoder features convenience in its small footprint and easy mounting behind any display. It delivers full-screen, single-image video; high-quality video with 4:2:0 video color sampling; and 1080p60, H.264-based high-profile decoding with lossless compression.

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MARKETING AND SALES

We primarily use a two-tier channel model through which we sell our commercial products to a worldwide network of independent professional audiovisual, information technology and telecommunications distributors, who then sell our products to independent systems integrators, dealers, and value-added resellers, who in turn work directly with the end-users of our products for product fulfillment and installation, if needed. Our products are also specified and recommended by professional audio-video consultants. We also sell our commercial products directly to certain dealers, systems integrators, value-added resellers, and end-users.

Our product sales generated in the United States and outside the United States for the years ended December 31 are as follows:

Revenue in millions	2017		2016		2015	
	Revenue	%	Revenue	%	Revenue	%
In the United States	$24.6	59 %	$31.8	65 %	$39.6	68 %
Outside United States	$17.2	41 %	$16.8	35 %	$18.2	32 %
	$41.8	100%	$48.6	100%	$57.8	100%

We sell directly to our distributors, resellers and end-users in approximately 61 countries worldwide. We anticipate that the portion of our total product revenue from international sales will continue to be a significant portion of our total revenue as we further enhance our focus on developing new products, establishing new channel partners, strengthening our presence in key growth areas, complying with regional environmental regulatory standards, and improving product localization with country-specific product documentation and marketing materials.

Distributors, Resellers and Independent Integrators

We sold our products directly to approximately 378 distributors and direct resellers throughout the world during 2017. Distributors and resellers purchase our products at a discount from list price and resell them worldwide to hundreds of independent systems integrators, telephony value-added resellers, IT value-added resellers, and PC dealers on a non-exclusive basis. Our distributors maintain their own inventory and accounts receivable and are required to provide technical and non-technical support for our products to the next level of distribution participants. We work with our distributors and resellers to establish appropriate inventory stocking levels. We also work with our distributors and resellers to maintain relationships with our existing systems integrators, dealers, and other value-added resellers.

While dealers, resellers, and system integrators all sell our products directly to the end-users, system integrators typically add significant value to each sale by combining our products with products from other manufacturers as part of an integrated system solution. Commercial dealers and value-added resellers usually purchase our products from distributors and may bundle our products with products from other manufacturers for resale to the end-user. We maintain close working relationships with all our reseller partners and offer them education and training on all of our products.

Marketing

Much of our marketing effort is conducted in conjunction with our channel partners who provide leverage for us in reaching existing and prospective customers worldwide. We also regularly attend industry forums and exhibit our products at multiple regional and international trade shows, often with our channel partners. These trade shows provide exposure for our brand and products to a wide audience. We market our ClearOne-branded commercial products on our website www.clearone.com. We also conduct public relations initiatives to get press coverage and product reviews in industry and non-industry publications alike.

Customers

We do not get comprehensive reports from our distributors and resellers that identify our end-users. As a result, we do not know whether any end-user accounted for more than 10 percent of our total revenue during any of the periods reported in this Annual Report. However, revenues included sales to Starin Marketing, which represented approximately 16% of consolidated revenue during the year ended December 31, 2017 with no other customer accounting for more that 10 percent. During the year ended December 31, 2016 sales to Starin Marketing represented approximately 16.3% of consolidated revenue with no other customer accounting for more that 10 percent. During the year ended December 31, 2015 sales to Starin Marketing and VSO represented approximately 14.2% and 10.4% of consolidated revenue with no other customer accounting for more that 10 percent.

As discussed above, distributors facilitate product sales to a large number of independent systems integrators, dealers, and value-added resellers, and subsequently to their end-users. The loss of one or more distributors could reduce revenue and have a material adverse effect on our business and results of operations. Our shipped orders on which we had not recognized revenue were $4.6 million and $3.9 million as of December 31, 2017 and 2016, respectively. We had a backlog of unshipped orders of approximately $0.2 million and $0.6 million as of December 31, 2017 and 2016, respectively.

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ITEM 1 - BUSINESS

Competition

The audio-visual product markets are characterized by intense competition, rapidly evolving technology, and increased business consolidation. We compete with businesses having substantially greater financial, research and product development, manufacturing, marketing, and other resources. If we are not able to continually design, manufacture, and successfully market new or enhanced products or services that are comparable or superior to those provided by our competitors and at comparable or better prices, we could experience pricing pressures and reduced sales, gross profit margins, profits, and market share, each of which could have a materially adverse effect on our business. Our competitors vary within each product category. We believe we are able to differentiate ourselves and therefore successfully compete as a result of the high audio quality of our products resulting from a combination of proprietary and highly advanced audio signal processing technologies and networking technology in the form of trade secrets and patented intellectual property, technical and channel support services, and the strength of our channels and brands. It is critical for our success to be able to defend our intellectual property including trademarks, trade secrets and patents from our competitors who have far more resources.

We believe the principal factors driving sales are the following:

Quality, features and functionality, and ease of use of the products;
Broad and deep global channel partnerships;
Significant established history of successful worldwide installations for diverse vertical markets;
Brand name recognition and acceptance;
Quality of customer and partner sales and technical support services; and
Effective sales and marketing.

In the professional audio conferencing system and sound reinforcement markets our main competitors include AcousticMagic, AMX Harman, Audio Technica, Biamp, BOSE, Crestron, Extron, BSS Harman, Peavey, Phoenix Audio, Polycom, QSC, Shure, Symetrix, Vaddio and Yamaha and their original equipment manufacturing (OEM) partners, along with several other companies potentially poised to enter the market. We occupy the number one position in the global professional audio conferencing market with more than 50% of the global market share.

In the professional microphones market, our primary competitors include AKG, Audio Technica, Audix, Avlex/Mipro, Beyerdynamic, Biamp, Clock Audio, Lectrosonics, Nureva, Mediavision/Taiden, Polycom, Phoenix Audio, Sennheiser, Shure, TeachLogic, TOA, Yamaha/Revolabs and Vaddio and their OEM partners.

In the traditional tabletop conferencing market, we face significant competition from Avaya/Konftel, Phoenix Audio, Polycom and Yamaha, and especially from their OEM partnerships. A significant portion of the tabletop market is covered by sales through OEM partnerships. While we believe MAX products have unique features and superior quality, our limited OEM partnerships and pricing pressures from higher volume competitors limit our ability to expand our existing share of this market.

Our primary competitors in the personal conferencing market are GN Netcom (Jabra), Logitech, Phoenix Audio, Plantronics, Polycom, Sennheiser and Yamaha and their OEM partners.

Our video conferencing products face tremendous competition from well established players as well as emerging players, including Acano, Adobe Connect, Amazon Chime, Avaya (Radvision), Aver, Barco, Blackboard Collaborate, Blue Jeans, Christie Digital, Cisco, Citrix, Fuze, Huawei, IDK AV, InFocus, Kramer, LifeSize, Magor, Pexip, Polycom, Microsoft Skype for Business, Starleaf, Telylabs, UNIFY, Videxio, Vidyo, Yealink, Zoom, ZTE, Highfive, Google, Tixeo and Owl Labs. We believe the migration of video conferencing from hardware-based codecs to software-based codecs provides an opportunity for us to differentiate our products and gain market share.

Our network streaming products which includes digital signage products face intense competition from a few well-established corporations of diversified capabilities and strengths, including AMX, Atlona, Aurora Multimedia, Barco, Biamp, Broadsign, Cisco, Christie Digital, Crestron, Extron, Gefen, Goopie, Haivision, Hall Research, IDK AV, Infocus (Jupiter), Key Digital, Kramer, Liberty AV, Magenta Research, Matrox, Mediasite, Ncast, RGB Spectrum, Scala, Spinetix, SVSi, voLANte, Tightrope, Teracue, tvONE, UCView, VBrick, Visionary Solutions, Visix, WyreStorm and ZeeVee. We believe that our software based patented technology delivers superior audio and video streaming performance and flexibility and provides us with a competitive edge over other industry players.

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ITEM 1 - BUSINESS

Regulatory Environment

Regulations regarding product safety, product operational agency compliance, the materials used in manufacturing, the process of disposing of electronic equipment and the efficient use of energy may require extensive lead-time to obtain regulatory approvals of new products in both domestic and international markets. Such regulations may impact our ability to expand our sales in a timely and cost-effective manner and, as a result, our business could be harmed.

Sources and Availability of Raw Materials

We manufacture our products through electronics manufacturing services (“EMS”) providers, who are generally responsible for sourcing and procuring required raw materials and components. Most of the components that our EMS providers require for manufacturing our products are readily available from a number of sources. During 2017, we witnessed a significant tightening of the electronics market with demand for electronic products especially for memories and processors far exceeding the supply caused price increases and longer fulfillment cycles.

We continually work with our EMS providers to seek alternative sources for all our components and raw material requirements to ensure higher quality and better pricing. Most of our EMS providers and their vendors are duly qualified by our corporate quality assurance process. We work with our EMS providers to ensure that raw materials and components conform to our specifications.

Manufacturing

Currently, all of our products are manufactured by EMS providers. Our primary EMS provider is Flextronics. The digital signage products are assembled in our Salt Lake City, Utah facility.

Seasonality

We do not recognize a consistent pattern between the quarters to identify seasonality.

Research and Product Development

We are committed to research and product development and view our continued investment in research and product development as a key ingredient to our long-term business success. Our research and product development expenditures were approximately $9.3 million, $8.6 million and $8.3 million, during the years ended December 31, 2017, 2016 and 2015, respectively.

Our core competencies in research and product development include (a) many audio technologies, including acoustic echo cancellation, noise cancellation and other advanced adaptive digital signal processing technologies, (b) networking and multimedia streaming technologies, and (c) video technologies. We also have expertise in wireless technologies, VoIP, software and network application, and digital signage system development. We believe that continued investment in our core technological competencies is vital to developing new products and to enhancing existing products.

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ITEM 1 - BUSINESS

Intellectual Property and Other Proprietary Rights

We believe that our success depends in part on our ability to protect our proprietary rights. We rely on a combination of patent, copyright, trademark, and trade secret laws and confidentiality agreements and processes to protect our proprietary rights.

As of December 31, 2017, we had approximately 87 patents and 21 pending patent applications, including foreign counterpart patents and foreign applications. Our patents and pending patent applications cover a wide range of our products and services including, but not limited to acoustic echo cancellation, beamforming microphone arrays, systems that enable streaming media over IP networks, algorithms for video processing, wireless conferencing systems, spatial audio, and technologies for the Internet of Things. The durations of our patents are determined by the laws of the country of issuance. For the U.S., patents may be 17 years from the date of issuance of the patent or 20 years from the date of its filing, depending upon when the patent application was filed. In addition, we hold numerous trademarks, both in the U.S. and in other countries. The laws of foreign countries may not protect our intellectual property to the same degree as the laws of the United States.

We will obtain patents and other intellectual property rights used in connection with our business when practicable and appropriate. Our intellectual property policy is to protect our products, technology and processes by asserting our intellectual property rights where appropriate and prudent. From time to time, assertions of infringement of certain patents or other intellectual property rights of others have been made against us. In addition, certain pending claims against a competitor are in various stages of litigation. See Part I, Item 3. Legal Proceedings and Note 8 – Commitments and Contingencies of the Notes to Consolidated Financial Statements (Part II, Item 8) for information regarding current legal proceedings involving our intellectual property rights.

We are dependent on our intellectual property. If we are not able to protect our proprietary rights or if those rights are invalidated or circumvented, our business may be adversely affected. We may be subject to litigation and infringement claims, which could cause us to incur significant expenses or prevent us from selling our products or services. For more information concerning the risks related to patents, trademarks, and other intellectual property, please see “Risk Factors-Risks Related to our Business.”

We generally require our employees, certain customers and partners to enter into confidentiality and non-disclosure agreements before we disclose any confidential aspect of our technology, services, or business. In addition, our employees are required to assign to us any proprietary information, inventions, or other technology created during the term of their employment with us. However, these precautions may not be sufficient to protect us from misappropriation or infringement of our intellectual property.

On April 25, 2017, the Company was awarded a new patent, U.S. Patent No. 9,635,186 (the “186 Patent”), which relates to a system and method involving the combination of echo cancellation and beamforming microphone arrays. Also on April 25, 2017, the Company filed a lawsuit in the U.S. Federal District Court in the District of Utah against three parties—Shure, Inc. (“Shure”), Biamp Systems Corporation (“Biamp”), and QSC Audio Products, LLC (“QSC,” together with Shure and Biamp, collectively, the “Defendants”), alleging that the Defendants were jointly and indirectly infringing the newly issued ‘186 Patent (the “Infringement Action”). On that same day, Shure filed a separate action in the U.S. Federal District Court in the Northern District of Illinois (the “Illinois Action”) requesting a declaratory judgment as to the invalidity or non-infringement with respect to the ‘186 Patent. The Illinois Action also seeks the same declaratory judgment with respect to another Company patent, United States Patent No. 9,264,553 (the “553 Patent”), and which has not been asserted by the Company against any defendant and has been submitted to the USPTO for reissue. In early 2018, Shure added a claim that the ‘186 Patent is unenforceable.

ITEM 1A - RISK FACTORS

ITEM 1A. RISK FACTORS

Investors should carefully consider the risks described below. The risks described below are not the only ones we face and there are risks that we are not presently aware of or that we currently believe are immaterial that may also impair our business operations. Any of these risks could harm our business. The trading price of our common stock could decline significantly due to any of these risks, and investors may lose all or part of their investment. In assessing these risks, investors should also refer to the other information contained or incorporated by reference in this annual report on Form 10-K, including our consolidated financial statements and related notes.

Risks Relating to Our Business

A material weakness has been identified in our internal control over financial reporting. If we fail to remediate and maintain effective internal control over financial reporting, we may be unable to report our financial results accurately on a timely basis, investors could lose confidence in our reported financial information, the trading price of our common shares could decline and our access to the capital markets or other financing sources could become limited.

In connection with the audit of our consolidated financial statements as of December 31, 2017, our independent registered public accounting firm identified deficiencies in our system of internal control over financial reporting that it considered to be a material weakness in the operation of certain of our controls that would have prevented and detected a misstatement on a timely basis, and therefore, affected our ability to ensure timely and accurate reporting of our financial condition and results of operations. The Public Company Accounting Oversight Board's Auditing Standard No. 5 defines a material weakness as a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of annual or interim financial statements will not be prevented or detected on a timely basis. The identified material weakness related to our lack of formally designed processes and controls to prevent or mitigate the risk of material errors from occurring within our consolidated financial statements. See Part II, Item 9A, “Controls and Procedures.”

We have initiated remedial measures, however there can be no assurance that these actions, as well as further actions we may take, will allow us to remediate this material weakness and provide a solid foundation to meet our reporting obligations under the Exchange Act. If we fail to implement and maintain effective internal control over financial reporting (including appropriately and effectively remediating this material weakness), or if additional material weaknesses in our internal control over financial reporting are discovered or occur in the future, our consolidated financial statements may contain material misstatements, and we could be required to restate our financial results. In addition, if we are unable to successfully remediate this material weakness and if we are unable to produce accurate and timely financial statements, our stock price may be materially adversely affected and we may be unable to maintain compliance with applicable stock exchange listing requirements.

We face intense competition in all markets for our products and services and our operating results will be adversely affected if we cannot compete effectively against other companies.

The markets for our products and services are characterized by intense competition, pricing pressures and rapid technological change. Our competitive landscape continues to rapidly evolve, in particular with respect to our video-related services and products, as we move into new markets for video collaboration such as mobile, social and cloud-delivered video. We compete with businesses having substantially greater financial, research and product development, manufacturing, marketing, and other resources than we do. If we are not able to continually design, manufacture, and successfully introduce new or enhanced products or services that are comparable or superior to those provided by our competitors and at comparable or better prices, we could experience pricing pressures and reduced sales, gross profit margins, profits, and market share, each of which could have a materially adverse effect on our business.

Difficulties in estimating customer demand in our products segment could harm our profit margins.

Orders from our distributors and other distribution participants are based on demand from end-users. Prospective end-user demand is difficult to measure. This means that our revenue during any fiscal quarter could be adversely impacted by low end-user demand, which could in turn negatively affect orders we receive from distributors and dealers. Our expectations for both short and long-term future net revenues are based on our own estimates of future demand. Revenue for any particular time period is difficult to predict with any degree of certainty. We typically ship products within a short time after we receive an order; consequently, unshipped backlog has not historically been a good indicator of future revenue. We believe that the level of backlog is dependent in part on our ability to forecast revenue mix and plan our manufacturing accordingly. A significant portion of our customers’ orders are received during the last month of the quarter. We budget the amount of our expenses based on our revenue estimates. If our estimates of sales are not accurate and we experience unforeseen variability in our revenue and operating results, we may be unable to adjust our expense levels accordingly and our gross profit and results of operations will be adversely affected. Higher inventory levels or stock shortages may also result from difficulties in estimating customer demand.

If we are unable to protect our intellectual property rights or have insufficient proprietary rights, our business would be materially impaired.

We currently rely primarily on a combination of trade secrets, copyrights, trademarks, patents, patents pending, and nondisclosure agreements to establish and protect our proprietary rights in our products. Our success is dependent in part on obtaining, maintaining and enforcing our intellectual property rights If we are unable to obtain, maintain and enforce intellectual property legal protection covering our products, then no assurances can be given that others will not independently develop technologies similar to ours, or duplicate or design around aspects of our technology. In addition, we cannot assure that any patent or registered trademark owned by us will not be invalidated, circumvented or challenged, or that the rights granted thereunder will provide competitive advantages to us. Costly litigation may be necessary to enforce our intellectual property rights. We believe our products and other proprietary rights do not infringe upon any proprietary rights of third parties; however, we cannot ensure that third parties will not assert infringement claims in the future. We currently hold only a limited number of patents. To the extent that we have patentable technology that is material to our business and for which we have not filed patent applications, others may be able to use such technology or even gain priority over us by patenting such technology themselves, which could have a material adverse effect on our business. With respect to any patent application we have filed, we cannot ensure that a patent will be awarded.

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ITEM 1A - RISK FACTORS

We are currently subject to patent litigation, including claims challenging the validity and enforceability of some of our patents, which could cause us to incur significant expenses or prevent us from protecting our products or services against competing products.

Our industry is characterized by vigorous protection of intellectual property rights. We have initiated litigation to enforce our intellectual property rights, which has resulted in our adversaries in such litigation challenging the validity, scope, and/or enforceability of our intellectual property. Irrespective of the merits of these claims, any resulting litigation could be costly and time consuming and could divert the attention of management and key personnel from other business issues. The complexity of the technology involved and the uncertainty of intellectual property litigation increase these risks. See Part I, Item 3. Legal Proceedings and Note 8 – Commitments and Contingencies of the Notes to Consolidated Financial Statements (Part II, Item 8) for information regarding current legal proceedings involving our intellectual property rights.

Our sales depend to a certain extent on government funding and regulation.

In the audio conferencing products market, the revenue generated from sales of our audio conferencing products for distance learning and courtroom facilities depends on government funding. In the event government funding for such initiatives was reduced or became unavailable, our sales could be negatively impacted. Additionally, many of our products are subject to governmental regulations. New regulations could impact sales in a materially adverse manner.

Environmental laws and regulations subject us to a number of risks and could result in significant costs and impact on revenue.

Regulations regarding the materials used in manufacturing, the process of disposing of electronic equipment and the efficient use of energy require us to take additional time to obtain regulatory approvals of new products in international markets. Such regulations may impact our ability to expand our sales in a timely and cost-effective manner and, as a result, our business could be harmed.

Our profitability may be adversely affected by our continuing dependence on our distribution channels.

We market our products primarily through a network of distributors who in turn sell our products to value-added resellers. All of our agreements with such distributors and other distribution participants are non-exclusive, terminable at will by both party, and generally short-term. No assurances can be given that any or all such distributors or other distribution participants will continue their relationship with us. Distributors and, to a lesser extent, value-added resellers cannot easily be replaced and any loss of revenues from these and other sources or our inability to reduce expenses to compensate for such loss of revenue could adversely affect our net revenue and profit margins.

Although we rely on our distribution channels to sell our products, our distributors and other distribution participants are not obligated to devote any specified amount of time, resources, or efforts to the marketing of our products, or to sell a specified number of our products. There are no prohibitions on distributors or other resellers offering products that are competitive with our products, and some do offer competitive products. The support of our products by distributors and other distribution participants may depend on the competitive strength of our products and the price incentives we offer for their support. If our distributors and other distribution participants are not committed to our products, our revenue and profit margins may be adversely affected.

Additionally, we offer our distributors price protection on their inventory of our products. If we reduce the list price of our products, we will compensate our distributors for the respective products that remain in their inventory on the date the price adjustment becomes effective, provided that they have been providing inventory reports consistently and the inventory was bought within the six months preceding the price adjustment date. Our net revenue and profit margins could be adversely affected if we reduce product prices significantly or distributors happen to have significant on-hand inventory of the affected product at the time of a price reduction. Further, if we do not have sufficient cash resources to compensate distributors on terms satisfactory to them or us, our price protection obligations may prevent us from reacting quickly to changing market conditions.

Product development delays or defects could harm our competitive position and reduce our revenue.

We have in the past experienced, and may again experience, technical difficulties and delays with the development and introduction of new products. Many of the products we develop contain sophisticated and complicated circuitry, software and components and utilize manufacturing techniques involving new technologies. Potential difficulties in the development process that we may experience include the following: (a) meeting required specifications and regulatory standards; (b) hiring and keeping a sufficient number of skilled developers; (c) meeting market expectations for performance; (d) obtaining prototype products at anticipated cost levels; (e) having the ability to identify problems or product defects in the development cycle; and (f) achieving necessary manufacturing efficiencies.

Once new products reach the market, they may have defects, or may be met by unanticipated new competitive products, which could adversely affect market acceptance of these products and our reputation. If we are not able to manage and minimize such potential difficulties, our business and results of operations could be negatively affected.

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ITEM 1A - RISK FACTORS

We depend on an outsourced manufacturing strategy, and any disruption in outsourced services could negatively impact our product availability and revenues.

We outsource the manufacturing of all of our products except digital signage and wireless microphone products to electronics manufacturing services (“EMS”) providers located outside the U.S. If any of these EMS providers experience (i) difficulties in obtaining sufficient supplies of components, (ii) component prices significantly exceeding anticipated costs, (iii) an interruption in their operations, or (iv) otherwise suffers capacity constraints, we could experience a delay in production and shipping of these products, which would have a negative impact on our revenue. Should there be any disruption in services due to natural disaster, economic or political difficulties, transportation restrictions, acts of terror, quarantines or other restrictions associated with infectious diseases, or other similar events, or any other reason, such disruption could have a material adverse effect on our business. Operating in the international outsourcing environment exposes us to certain inherent risks, including unexpected changes in regulatory requirements and tariffs, and potentially adverse tax consequences, which could materially affect our results of operations. Currently, we have no second source of manufacturing for a large portion of our products.

Switching from one EMS provider to another is an expensive, difficult and a time-consuming process, with serious risks to our ability to successfully transfer our manufacturing operations. Our operations, and consequently our revenues and profitability, could be materially adversely affected if we are forced to switch from any of our EMS providers to another EMS provider due to any of a number of factors, including financial difficulties faced by the manufacturer, disagreements in pricing negotiations between us and the manufacturer or organizational changes in the manufacturer.

The cost of delivered product from our EMS providers is a direct function of their ability to buy components at a competitive price and to realize efficiencies and economies of scale within their overall business structures. If they are unsuccessful in driving efficient cost models, our delivered costs could rise, affecting our profitability and ability to compete. In addition, if the EMS providers are unable to achieve greater operational efficiencies, delivery schedules for new product development and current product delivery could be negatively impacted.

EMS providers often require long range forecasts to help them plan their operations as well as to allocate their resources. We are tied to these forecasts through contracts as well as to maintain harmony in business relationships. Our ability to react to actual demand from our customers and order optimum levels of inventory is severely limited due to these forecasts provided to the EMS providers. Our inability to accurately forecast our future demands could lead to either excess inventory causing potential inventory obsolescence and cashflow problems or shortage in inventory causing potential loss of revenue.

Recent regulatory requirements regarding the use of “conflict minerals” could affect the sourcing and availability of raw materials to our EMS providers in the manufacture of certain of our products. We may be subject to costs associated with the new regulations, including for the diligence pertaining to the presence of any conflict minerals used in our products and the cost of remediation and other changes to products, processes, or sources of supply as a consequence of such verification activities. The impact of the regulations may result in a limited pool of suppliers who provide conflict free minerals, and we cannot assure you that we will be able to obtain products in sufficient quantities, at competitive prices, or at all. We may face reputational challenges with our customers and other stakeholders if we are unable to sufficiently verify the origins for the metals used in the products we sell. As a result, we may not be able to obtain the materials necessary to manufacture our products, which could force us to cease production or search for alternative supply sources, possibly at a higher cost. Such disruptions may have a material adverse effect on our business, financial condition, results of operations and cash flows.

Global economic conditions have adversely affected our business in the past and could adversely affect our revenues and harm our business in the future.

Adverse economic conditions worldwide have contributed to slowdowns in the communications industry and have caused a negative impact on the specific segments and markets in which we operate. Adverse changes in general global economic conditions can result in reductions in capital expenditures by end-user customers for our products, longer sales cycles, the deferral or delay of purchase commitments for our products and increased competition. These factors have adversely impacted our operating results in prior periods and could also impact us again in the future. Global economic concerns, such as the varying pace of global economic recovery, European and domestic debt and budget issues, the slowdown in economic growth in large emerging markets such as China and India, and international currency fluctuations, may continue to create uncertainty and unpredictability in the global and national economy. A global economic downturn would negatively impact technology spending for our products and services and could materially adversely affect our business, operating results and financial condition. Further, global economic conditions may result in a tightening in the credit markets, low liquidity levels in many financial markets, decrease in customer demand and ability to pay obligations, and extreme volatility in credit, equity, foreign currency and fixed income markets.

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ITEM 1A - RISK FACTORS

Such adverse economic conditions could negatively impact our business, particularly our revenue potential, potentially causing losses on investments and the collectability of our accounts receivable. These factors potentially include: the inability of our customers to obtain credit to finance purchases of our products and services, customer or partner insolvencies or bankruptcies, decreased customer confidence to make purchasing decisions resulting in delays in their purchasing decisions, decreased customer demand or demand for lower-end products, or decreased customer ability to pay their obligations when they become due to us.

We are a smaller Company than some of our competitors and may be more susceptible to market fluctuations, other adverse events, increased costs and less favorable purchasing terms.

Since we are a relatively small Company, there is a risk that we may be more susceptible to market fluctuations and other adverse events. In particular, we may be more susceptible to reductions in government and corporate spending from our government and enterprise customers. We may also experience increased costs and less favorable terms from our suppliers than some of our larger competitors who may have greater leverage in their purchasing spend. Any of these outcomes could result in loss of sales or our products being more costly to manufacture and thus less competitive. Any such unfavorable market fluctuations, reductions in customer spending or increased manufacturing costs could have a negative impact on our business and results of operations.

Difficulties in integrating past or future acquisitions could adversely affect our business.

Any acquisition involves numerous risks and challenges, including difficulties and time involved in integrating the operations, technologies and products of the acquired companies, entering new business or product lines, the diversion of our management’s attention from other business concerns, geographic dispersion of operations, generating market demand for expanded product lines and the potential loss of key customers or employees of an acquired Company. Failure to achieve the anticipated benefits of these and any future acquisitions or to successfully integrate the operations of these or any other companies or assets we acquire, could also harm our business, results of operations and cash flows. Additionally, we cannot assure you that we will not incur material charges in future periods to reflect additional costs associated with these acquisitions or any future acquisitions we may make.

Profitability could be negatively impacted if we do not adequately forecast the demand for our products and are unable to monetize our long-term inventories.

We hold approximately $8.7 million in long-term inventories. There can be no assurance that we will be able to successfully anticipate changing consumer preferences and product trends or economic conditions and, as a result, we may not successfully monetize our long-term inventory. Inventory levels in excess of consumer demand may result in inventory write-downs and the sale of excess inventory at discounted prices, which could have an adverse effect on the image and reputation of our brands and negatively impact profitability.

Conditions in Israel and the Middle East may affect the operations of our subsidiary in Israel.

We have a subsidiary located in Israel in connection with the acquisition of the assets of VCON Video Conferencing, Ltd and the subsequent establishment of a predominantly research and development team. Political, economic, security and military conditions in the Middle East in general, and in Israel in particular, directly affect our Israeli subsidiary's operations. Since the establishment of the State of Israel in 1948, a number of armed conflicts have taken place between Israel and its Arab neighbors and a state of hostility, varying in degree and intensity, has led to security and economic problems for Israel. Despite negotiations to effect peace between Israel and its Arab neighbors, the future of these peace efforts is uncertain.

Recent social unrest in various countries in the Middle East have led to severe political instability in those countries. This continuing instability may lead to deterioration of the political and trade relationships that exist between the State of Israel and these countries. In addition, this instability may affect the economy in the Middle East as well as the global economy and marketplace. Any armed conflicts or political instability in the region, including acts of terrorism or any other hostilities involving or threatening Israel, would likely negatively affect business conditions and could make it more difficult for us to conduct our operations in Israel, which could increase our costs and adversely affect our financial results.

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ITEM 1A - RISK FACTORS

Conditions in China, India, Spain and United Arab Emirates may affect our operations.

We have different teams working outside the U.S. in China, India, Spain and United Arab Emirates offering various services including research and development, sales and marketing, and manufacturing operations support. Our ability to operate the company smoothly may be affected significantly if either one or more of these countries are adversely impacted by political, economic, security and military conditions in these countries.

Product obsolescence could harm demand for our products and could adversely affect our revenue and our results of operations.

Our industry is subject to technological innovations that could render existing technologies in our products obsolete and thereby decrease market demand for such products. If any of our products becomes slow-moving or obsolete and the recorded value of our inventory is greater than its market value, we will be required to write down the value of our inventory to its fair market value, which would adversely affect our results of operations. In limited circumstances, we are required to purchase components that our outsourced manufacturers use to produce and assemble our products. Should technological innovations render these components obsolete, we will be required to write down the value of this inventory, which could adversely affect our results of operations.

International sales account for a significant portion of our net revenue and risks inherent in international sales could harm our business.

International sales represent a significant portion of our total product revenue. We anticipate that the portion of our total product revenue from international sales will continue to increase as we further enhance our focus on developing new products for new markets, establishing new distribution partners, strengthening our presence in emerging economies, and improving product localization with country-specific product documentation and marketing materials. Our international business is subject to the financial and operating risks of conducting business internationally, including the following:

unexpected changes in, or the imposition of, additional legislative or regulatory requirements;
unique or more onerous environmental regulations;
fluctuating exchange rates;
tariffs and other barriers;
difficulties in staffing and managing foreign sales operations;
import and export restrictions;

greater difficulties in accounts receivable collection and longer payment cycles;
potentially adverse tax consequences;
potential hostilities and changes in diplomatic and trade relationships; and
disruption in services due to natural disaster, economic or political difficulties, transportation, quarantines or other restrictions associated with infectious diseases.

We may not be able to hire and retain qualified key and highly-skilled technical employees, which could affect our ability to compete effectively and may cause our revenue and profitability to decline.

We depend on our ability to hire and retain qualified key and highly skilled employees to manage, research and develop, market, and service new and existing products. Competition for such key and highly-skilled employees is intense, and we may not be successful in attracting or retaining such personnel. To succeed, we must hire and retain employees who are highly skilled in the rapidly changing communications and Internet technologies. Individuals who have the skills and can perform the services we need to provide our products and services are in great demand. Because the competition for qualified employees in our industry is intense, hiring and retaining employees with the skills we need is both time-consuming and expensive. We may not be able to hire enough skilled employees or retain the employees we do hire. In addition, provisions of the Sarbanes-Oxley Act of 2002 and related rules of the SEC impose heightened personal liability on some of our key employees. The threat of such liability could make it more difficult to identify, hire and retain qualified key and highly-skilled employees. We have relied on our ability to grant stock options as a means of recruiting and retaining key employees. Accounting regulations requiring the expensing of stock options will impair our future ability to provide these incentives without incurring associated compensation costs. If we are unable to hire and retain employees with the skills we seek, our ability to sell our existing products, systems, or services or to develop new products, systems, or services could be hindered with a consequent adverse effect on our business, results of operations, financial position, or liquidity. In addition, given the current political climate regarding the U.S. immigration laws, we may not be able attract highly-skilled technical employees from abroad.

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ITEM 1A - RISK FACTORS

We rely on third-party technology and license agreements, the loss of any of which could negatively impact our business.

We have licensing agreements with various suppliers for software and hardware incorporated into our products. These third-party licenses may not continue to be available to us on commercially reasonable terms, if at all. The termination or impairment of these licenses could result in delays of current product shipments or delays or reductions in new product introductions until equivalent designs can be developed, licensed, and integrated, if at all possible, which would have a material adverse effect on our business.

We may have difficulty in collecting outstanding receivables.

We grant credit to substantially all of our customers without requiring collateral. In times of economic uncertainty, the risks relating to the granting of such credit will typically increase. Although we monitor and mitigate the risks associated with our credit policies, we cannot ensure that such mitigation will be effective. We have experienced losses due to customers failing to meet their obligations. Future losses could be significant and, if incurred, could harm our business and have a material adverse effect on our operating results and financial position.

Interruptions to our business could adversely affect our operations.

As with any Company, our operations are at risk of being interrupted by earthquake, fire, flood, and other natural and human-caused disasters, including disease and terrorist attacks. Our operations are also at risk of power loss, telecommunications failure, human error, physical or electronic security breaches and computer viruses (which could leave us vulnerable to the loss of confidential proprietary information as well as disruption of our business activities) and other infrastructure and technology-based problems. To help guard against such risks, we carry business interruption loss insurance to help compensate us for losses that may occur, but we cannot assure that such coverage would protect us from all such possible losses.

Changes in tax laws and uncertainties in the interpretation and application of the 2017 Tax Cuts and Job Act could materially affect our financial position, results of operations and cash flows.

In December 2017, the U.S. government enacted comprehensive income tax legislation commonly referred to as the Tax Cuts and Jobs Act (the "2017 Tax Act"). The 2017 Tax Act makes broad and complex changes to the Internal Revenue Code of 1986, as amended (the "Code"), including, among other changes, significant changes to the U.S. corporate tax rate and certain other changes to the Code that impact the taxation of corporations. In certain instances the 2017 Tax Act requires complex computations to be performed that generally were not previously required by the Code and the regulations promulgated thereunder; significant judgments to be made in interpreting the provisions of the 2017 Tax Act significant estimates to be made in certain calculations; and the preparation and analysis of information generally not previously relevant or regularly produced. The U.S. Treasury Department, the Internal Revenue Service ("IRS"), and other standard-setting bodies could interpret or issue guidance on how provisions of the 2017 Tax Act will be applied or otherwise administered that differs from our interpretation. As we complete our analysis of the 2017 Tax Act, collect and prepare necessary data, and interpret any additional guidance, we may make adjustments to provisional amounts that we have recorded that may materially impact our provision for income taxes in the period in which the adjustments are made. Additionally, there is risk relating to assumptions regarding the outcome of tax matters, based in whole or in part upon consultation with outside advisors; risk relating to potential unfavorable decisions in tax proceedings; and risks regarding changes in, and/or interpretations of federal and state income tax laws. Any such changes, interpretations or alternative outcomes could result in more unpredictability and variability to our future effective tax rates.

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ITEM 1A - RISK FACTORS

We may not be able to hire and retain qualified key and highly-skilled technical employees, which could affect our ability to compete effectively and may cause our revenue and profitability to decline.

We depend on our ability to hire and retain qualified key and highly skilled employees to manage, research and develop, market, and service new and existing products. Competition for such key and highly-skilled employees is intense, and we may not be successful in attracting or retaining such personnel. To succeed, we must hire and retain employees who are highly skilled in the rapidly changing communications and Internet technologies. Individuals who have the skills and can perform the services we need to provide our products and services are in great demand. Because the competition for qualified employees in our industry is intense, hiring and retaining employees with the skills we need is both time-consuming and expensive. We may not be able to hire enough skilled employees or retain the employees we do hire. In addition, provisions of the Sarbanes-Oxley Act of 2002 and related rules of the SEC impose heightened personal liability on some of our key employees. The threat of such liability could make it more difficult to identify, hire and retain qualified key and highly-skilled employees. We have relied on our ability to grant stock options as a means of recruiting and retaining key employees. Accounting regulations requiring the expensing of stock options will impair our future ability to provide these incentives without incurring associated compensation costs. If we are unable to hire and retain employees with the skills we seek, our ability to sell our existing products, systems, or services or to develop new products, systems, or services could be hindered with a consequent adverse effect on our business, results of operations, financial position, or liquidity.

Security breaches and other disruptions could compromise our information and expose us to liability, which would cause our business and reputation to suffer.

In the ordinary course of our business, we collect and store sensitive data, including intellectual property, our proprietary business information and that of our employees, customers, licensors, vendors and business partners, including personally identifiable information of our customers and employees, in our data centers and on our networks. Despite our security measures, our information technology and infrastructure may be vulnerable to attacks by hackers or breached due to employee error, malfeasance or other disruptions. Security breaches have occurred with increased frequency and sophistication in recent years. Any such breach could compromise our networks and the information stored there could be accessed, publicly disclosed, lost or stolen. Any such access, disclosure or other loss of information could result in legal claims or proceedings, liability under laws that protect the privacy of personal information, disrupt our operations, and damage our reputation, which could adversely affect our business.

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ITEM 1A - RISK FACTORS

Risks Relating to Share Ownership

Our stock price fluctuates as a result of the conduct of our business and stock market fluctuations.

The market price of our common stock has experienced significant fluctuations and may continue to fluctuate significantly. The market price of our common stock may be significantly affected by a variety of factors, including the following:

- statements or changes in opinions, ratings, or earnings estimates made by brokerage firms or industry analysts relating to the market in which we do business or relating to us specifically;
- disparity between our reported results and the projections of analysts;
- the shift in sales mix of products that we currently sell to a sales mix of lower-gross profit product offerings;
- the level and mix of inventory held by our distributors;
- the announcement of new products or product enhancements by us or our competitors;
- technological innovations by us or our competitors;
- success in meeting targeted availability dates for new or redesigned products;
- the ability to profitably and efficiently manage our supply of products and key components;
- the ability to maintain profitable relationships with our customers;
- the ability to maintain an appropriate cost structure;
- quarterly variations in our results of operations;
- general consumer confidence or market conditions, or market conditions specific to technology industry;
- domestic and international economic conditions;
- unexpected changes in regulatory requirements and tariffs;
- our ability to report financial information in a timely manner;
- the markets in which our stock is traded;
- our ability to integrate the companies we have acquired; and
- our ability to successfully utilize our cash reserves resulting from the settlement of litigation and arbitration matters.

Rights to acquire our common stock could result in dilution to other holders of our common stock.

As of December 31, 2017, there were outstanding options to acquire approximately 764,430 shares of our common stock at a weighted average exercise price of $8.78 per share. During the terms of these options, the holders thereof will have the opportunity to profit from an increase in the market price of the common stock. The existence of these options may adversely affect the terms on which we can obtain additional financing, and the holders of these options can be expected to exercise such options at a time when we, in all likelihood, would be able to obtain additional capital by offering shares of our common stock on terms more favorable to us than those provided by the exercise of these options.

The sale of additional shares of our common stock could have a negative effect on the market price of our common stock.

The sale of substantial amounts of our common stock in the public market could adversely affect prevailing market prices and could impair our ability to raise capital through the sale of our equity securities. Most shares of common stock currently outstanding are eligible for sale in the public market, subject in certain cases to compliance with the requirements of Rule 144 under the securities laws. Shares issued upon the exercise of stock options granted under our stock option plan generally will be eligible for sale in the public market. We also have the authority to issue additional shares of common stock and shares of one or more series of preferred stock. The issuance of such shares could dilute the voting power of the currently outstanding shares of our common stock and could dilute earnings per share.

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ITEM 1A - RISK FACTORS

If equity research analysts do not publish research or reports about our business or if they issue unfavorable commentary or downgrade our common stock, the price of our common stock could decline.

The liquidity of the trading market for our common stock may be affected in part by the research and reports that equity research analysts publish about us and our business. We do not control the opinions of these analysts. The price of our stock could decline if one or more equity analysts downgrade our stock or if those analysts issue other unfavorable commentary or cease publishing reports about us or our business.

Write off of capitalized legal expenses related to our defense of patents could negatively impact our net income and stockholders' equity.

Our intangible assets include capitalized legal expenses net of amortization of $2.3 million related to our defense of patents from infringement by our competitors. Legal expenses have been capitalized upon satisfaction of two conditions: (a) a determination being made that a successful defense of this litigation is probable, and (b) that the monetary benefits arising out of such successful defense will be in excess of the costs for the defense. If either one of these conditions fail to be satisfied in the future, the carrying amount in the books may have to be written off either completely or partially. There can be no assurance that we will be successful in the defense of these litigation claims, in whole or in part.

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ITEM 1B. UNRESOLVED STAFF COMMENTS

Not applicable.

ITEM 2. PROPERTIES

We occupy a 5,000 square-foot facility in Gainesville, Florida under the terms of an operating lease that expires in February 2021 with the possibility of renewing the lease for 10 more years. The Gainesville facility was used primarily to support out research and development activities.

We lease a 4,700 square-foot office facility in Hod Hasharon, Israel under the terms of an operating lease expiring in December 2019 which serves to support our research and development activities. Upon expiration, we will have the option to extend the lease for two additional years.

We currently occupy a 31,000 square-foot facility in Salt Lake City, Utah under the terms of an operating lease expiring in May 2019, which supports our principal administrative, sales, marketing, customer support, and research and product development activities.

We occupy a 10,700 square-foot warehouse in Shenzhen, China under the terms of an operating lease expiring in September 2019, which serves as our primary inventory fulfillment and repair center.

We occupy a 7,070 square-foot facility in Austin, Texas - under the terms of an operating lease expiring in October 2019. This facility support our administrative, sales, marketing, customer support, and research and development activities.

We occupy a 40,000 square-foot warehouse in Salt Lake City, Utah under the terms of an operating lease expiring in December 2021, which serves as our primary inventory fulfillment and repair center. This facility also serves as our assembly workshop for digital signage products.

We believe our current facilities are adequate to meet our needs for the foreseeable future and that suitable additional or alternative space will be available in the future on commercially reasonable terms as needed.

ITEM 3. LEGAL PROCEEDINGS

See Note 8 – Commitments and Contingencies of the Notes to Consolidated Financial Statements (Part II, Item 8) for information regarding legal proceedings in which we are involved, which is incorporated in this Item 3 by reference.

ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable.

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PART II

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

Market Information

Our common stock is traded on the NASDAQ Capital Market under the symbol CLRO. On March 30, 2018, there were 8,301,473 shares of our common stock issued and outstanding held by approximately 323 shareholders of record. Each broker dealer or a clearing corporation that holds shares for customers is counted as a single shareholder of record.

The high and low common stock sales prices per share were as follows:

	First Quarter	**Second Quarter**	**Third Quarter**	**Fourth Quarter**	**Full Year**
2017					
High	$ 12.60	$ 11.10	$ 10.10	$ 9.00	$12.60
Low	9.70	9.25	7.40	6.70	6.70
2016					
High	$ 13.15	$ 11.68	$ 12.36	$ 11.40	$13.15
Low	10.60	10.21	10.32	10.40	10.21

Dividends

During 2017 and 2016, our Board of Directors declared the following dividends:

Declaration Date	**Record Date**	**Payment Date**	**Dividend per share**	**Dividends (S thousands)**
February 25, 2016	March 07, 2016	March 18, 2016	0.050	459
May 17, 2016	June 01, 2016	June 15, 2016	0.050	465

August 02, 2016	August 17, 2016	August 31, 2016	0.050	449
November 01, 2016	November 16, 2016	November 30, 2016	0.050	444
January 31, 2017	February 15, 2017	March 1, 2017	0.050	439
May 4, 2017	May 17, 2017	May 31, 2017	0.070	612
August 7, 2017	August 22, 2017	September 7, 2017	0.070	599
November 8, 2017	November 22, 2017	December 6, 2017	0.070	589

In addition, on March 1, 2017, our Board of Directors authorized an increase in our quarterly dividend from $0.05 per share to $0.07 per share beginning with the second quarter dividend in 2017.

Issuer Purchases of Equity Securities

In May 2012, our Board of Directors authorized a stock repurchase program authorizing the Company to repurchase up to $2 million of our outstanding common stock. On July 30, 2012, the Board of Directors increased the repurchase amount to $3 million from the original $2 million. On February 20, 2013, the Board of Directors again increased the repurchase amount to $10 million from $3 million. On December 2, 2014, ClearOne, Inc. issued a press release announcing the declaration of future cash dividends by the Company’s Board of Directors and reported the discontinuance of this stock repurchase program. At the time of the discontinuance of this stock repurchase program, the Company had repurchased approximately $5.4 million of the Company’s stock.

On March 9, 2016, the Board of Directors of the Company authorized the repurchase of up to $10 million of the Company’s outstanding shares of common stock under a new 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 repurchase program may be suspended or discontinued at any time without prior notice. The transactions effectuated to date occurred in open market purchases.

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On March 1, 2017, the Board of Directors of the Company renewed and extended the repurchase program until March 8, 2018 for up to an additional $10 million 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 repurchase program may be suspended or discontinued at any time without prior notice. The transactions effectuated to date occurred in open market purchases.

During the three months ended December 31, 2017 we acquired the following shares of common stock under the current stock repurchase program:

Period	**(a) Total Number of Shares Purchased**	**(b) Average Price Paid per Share**	**(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs**	**(d) Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (in $ millions)**
October 2017	19,460	$ 7.47	19,460	$ 6.5
November 2017	29,855	7.01	29,855	6.3
December 2017	69,229	8.88	69,229	5.7
Total	118,544	8.18	118,544	

From March 11, 2016 to March 17, 2017, the Company offered to repurchase eligible vested options to purchase shares under the 1998 Plan and the 2007 Plan from employees and directors. The Company repurchased delivered options at a repurchase price equal to the difference between the closing market price on the date of the employee's communication of accepting the repurchase offer and the exercise price of such employee's delivered options, subject to applicable withholding taxes and charges. The Company repurchased 225,542 stock options from employees and directors between March 11, 2016 and March 17, 2017 at an average purchase price of $7.77. The repurchase program expired on March 8, 2018 and the Board of Directors determined not to renew or extend it at that time.

ITEM 6. SELECTED CONSOLIDATED FINANCIAL DATA

Selected Financials

(Dollar in thousands, except per share data)

Year Ended December 31,	2017	2016	2015	2014	2013
Revenue	$41,804	$48,637	$57,796	$57,909	$49,592
Gross profit	24,009	29,487	36,719	35,323	29,897
Operating income/(loss)	(16,193)	3,566	10,292	7,975	7,622
Net income/(loss)	(14,172)	2,444	6,776	5,596	5,179
Diluted earnings/(loss) per share	(1.65)	0.26	0.71	0.58	0.55
Cash dividends declared per share	0.26	0.20	0.155	0.10	0.00
Cash, cash equivalents, and short-term investments	8,260	17,130	20,573	14,434	20,392
Working capital	23,286	30,819	36,539	30,202	39,417
Total assets	67,877	88,124	93,529	88,860	81,061
Long-term obligations	710	1,354	1,353	2,089	2,077
Stockholders' equity	56,567	77,449	82,569	76,016	70,335

	Quarterly Data for 2017			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Revenue	$11,678	$10,311	$10,560	$9,255
Gross profit	6,678	6,069	6,509	4,753
Net loss	(469)	(820)	(9,276)	(3,607)
Diluted loss per common share	(0.05)	(0.09)	(1.09)	(0.43)

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	Quarterly Data for 2016			
	First Quarter	**Second Quarter**	**Third Quarter**	**Fourth Quarter**
Revenue	$ 13,033	$ 11,966	$ 12,908	$ 10,730
Gross profit	8,465	7,664	7,668	5,590
Net income (loss)	1,368	955	1,209	(1,088)
Diluted earnings(loss) per common share	0.14	0.10	0.13	(0.12)

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

The following discussion should be read in conjunction with our consolidated financial statements and related notes included in this report, as well as our other filings with the SEC. This discussion contains forward-looking statements based on current expectations that involve risks and uncertainties, such as our plans, objectives, expectations, and intentions, as set forth under "Disclosure Regarding Forward-Looking Statements." Our actual results and the timing of events could differ materially from those anticipated in these forward-looking statements as a result of various factors, including those set forth in the following discussion and under the caption "Risk Factors" in Item 1A and elsewhere in this report.

OVERVIEW

ClearOne is a global Company that designs, develops and sells conferencing, collaboration, and network streaming solutions for voice and visual communications. The performance and simplicity of our advanced, comprehensive solutions offer a high level 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.

During 2017, we devoted most of our attention to the transition of our flagship professional audio conferencing products from CONVERGE Pro and Beamforming Microphone Array platform to CONVERGE Pro 2, our full line of next-gen DSP conferencing platform and Beamforming Microphone Array 2 platform. A number of CONVERGE Pro 2 SKUs were introduced and shipped during 2017 along with accessories like touch panel controllers, GPIO expansion box and USB expansion box. On the operations side, we successfully transitioned the manufacture of our professional audio conferencing products by our Electronics Manufacturer Services provider in the US to outside the US. On the sales and marketing front, our initiatives included focusing on smaller regional arenas, adding headcount to the sales team for increased feet on the street, and bringing on new regional channel partners to boost sales opportunity funnels.

Overall revenue declined in 2017 despite a significant increase in revenue from video products. The declines in revenue from professional audio products and unified communications end points more than offset the increase in revenue from video products. Our revenue decline in professional audio products reflects the challenges in transition to the next generation professional audio conferencing platform, and the on-going harm of infringement of ClearOne's patents to our professional audio conferencing products.

Our gross profit margin decreased in 2017 to 57% compared to 61% in 2016 primarily due to the reduced margins associated with CONVERGE Pro 1 consequent to price reductions announced in the fourth quarter of 2016. Net income decreased from $2.4 million in 2016 to a loss of $14.2 million in 2017. Net loss in 2017 was primarily due to $13.5 million in impairment of goodwill and intangible assets.

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. Our professional audio communication products, which contribute the most to our revenue, continues to be ahead of the competition despite the reduction in revenues through our transition from the CP1 platform to the next generation CP2 platform. Our strength in this space is largely due to our fully integrated suite of products consisting of DSP mixers, wide range of professional microphone products and video collaboration products. Despite our strong leadership position in the professional audio communications products market, we face challenges to revenue growth due to the limited size of the market and pricing pressures from new competitors attracted to the commercial market due to higher margins.

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

Revenue from our video products in the overall revenue mix has been improving on the back of a strong growth for our media collaboration products in 2017. 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 continue to generate high growth in revenue. We believe we are also well positioned to capitalize on the continuing migration away from the traditional hardware-based video conferencing systems to software-based video conferencing applications.

We derive a major portion of our revenue (approximately 39% for the year ended December 31, 2017) 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. However, we are exposed to foreign exchange risk if the US dollar is strong against other currencies as it will make U.S. Dollar denominated prices of our products less competitive.

Deferred Revenue

Each quarter-end, we evaluate the inventory in the distribution channel through information provided by certain of our distributors. The level of inventory in the channel fluctuates up or down each quarter based upon our distributors' individual operations. Accordingly, each quarter-end revenue deferral is calculated and recorded based upon the underlying channel inventory at quarter-end. Deferred revenue increased by $0.7 million to $4.6 million in 2017, due to higher orders placed in December. In 2016 deferred revenue decreased by $0.7 million from $4.6 million at the end of 2015 to $3.9 million at the end of 2016.

DISCUSSION OF RESULTS OF OPERATIONS

The following table sets forth certain items from our consolidated statements of operations for the years ended December 31, 2017, 2016 and 2015, together with the percentage change each item represents. Throughout this discussion, we compare results of operations for the year ended December 31, 2017 ("2017") to the year ended December 31, 2016 ("2016" or "the comparable period") and to the year ended December 31, 2015 ("2015" or "the comparable period").

(In thousands, except percentages)	2017	2016	2015	Percentage Change 2017 vs 2016		Percentage Change 2016 vs 2015	
Revenue	$41,804	$48,637	$57,796	-14	%	-16	%
Cost of goods sold	17,795	19,150	21,077	-7	%	-9	%
Gross profit	24,009	29,487	36,719	-19	%	-20	%
Sales and marketing	10,996	10,032	10,646	10	%	-6	%
Research and product development	9,342	8,564	8,318	9	%	3	%
General and administrative	7,161	7,325	7,493	-2	%	-2	%
Impairment of intangible assets	769	-	-	100	%	-	%
Impairment of goodwill	12,724	-	-	100	%	-	%
Legal settlement	790	-	-	-100	%	_	%
Operating expenses	40,202	25,921	26,457	55	%	-2	%
Operating income/(loss)	(16,193)	3,566	10,262	-554	%	-65	%
Income/(loss) before income taxes	(15,893)	3,878	10,551	-510	%	-63	%
Provision for/(benefit from) income taxes	(1,721)	1,434	3775	-220	%	-62	%
Net income/(loss)	(14,172)	2,444	6,776	-680	%	-64	%

Revenue

Our revenue decreased to $41.8 million in 2017 compared to $48.6 million in 2016. The 38% increase in revenue from video products was more than offset by a 19% decline in professional audio conferencing revenue and a 27% decline in revenue from unified communication end points. Premium products consisting of Interact AT line of products declined the most while media collaboration products increased the most. The decline in revenue from professional audio conferencing products was mostly due to price reductions to CONVERGE Pro 1 platform in the fourth quarter of 2016, delay in transitioning to the next generation professional audio conferencing platform, and the on-going harm of infringement of ClearOne’s patents to our professional audio conferencing products. The share of professional audio communications products (which includes microphone products but not premium products) in our product mix declined from 77% in 2016 to 72% in 2017. Share of video products in the revenue mix increased from 11% in 2016 to 17% in 2017. The increase in revenue from video products was due to the success of media collaboration products, especially Unite camera, and increasing acceptance of View Pro in major projects, especially in Asia and Middle East. Share of UC end points declined marginally from 12% in 2016 to 11% in 2017.

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

During 2017, revenue declined across all major markets except India, Middle East, China and parts of Europe. The decline was pronounced in the USA, Canada, South Asia, Korea and Northern Europe. Asia Pacific including Middle East increased by 18%, Europe and Africa declined by 12% and Americas declined by about 23%. The revenue decline was primarily caused by the delay in the transition to our next generation audio platform, CONVERGE Pro 2 and Beamforming Microphone Array 2 combined with price reduction effected to Converge Pro 1 platform in 2016 and the on-going harm of infringement of ClearOne's patents to our professional audio conferencing products. We believe, although there can be no assurance, that we will return to growth path when the transition from CONVERGE Pro 1 platform to CONVERGE Pro 2 platform is complete which we anticipate may happen in the next 12 months.

Our revenue decreased to $48.6 million in 2016 compared to $57.8 million in 2015. The 40% increase in revenue from video products was more than offset by a 19% decline in professional audio conferencing revenue and a 23% decline in revenue from unified communication end points. Tabletop audio conferencing products declined the most while media collaboration products increased the most. The decline in revenue from professional audio conferencing products was mostly due to overall weakness in the economy, decline in orders due to transition from CONVERGE Pro 1 to CONVERGE Pro 2 and reductions in CONVERGE Pro 1 pricing in the last quarter of 2016. The share of professional audio communications products (which includes microphone products but not premium products) in our product mix declined from 80% in 2015 to 77% in 2016. Share of video products in the revenue mix increased from 6.5% in 2015 to 11% in 2016. The increase in revenue from video products was due to the success of Unite camera, favorable reception to the new Collaborate SKUs containing integrated audio solutions and increasing acceptance of View Pro in major projects. Share of UC end points declined marginally from 13% in 2016 to 12% in 2015.

Cost 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 during 2017 was approximately $24.0 million or 57% compared to approximately $29.5 million or 61% in 2016. Gross margin declined mainly due to the price reductions made to CONVERGE Pro 1 products in the fourth quarter of 2016 and the decline in higher margin professional audio conferencing products in the mix

Our gross profit during 2016 was approximately $29.5 million or 61% compared to approximately $36.7 million or 64% in 2015. This increase in margin was mainly due to favorable change in product mix and contribution of licensing fees to the revenue.

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.

Operating Expenses and Profits (Losses)

Operating income/(loss), or income/(loss from operations, is the surplus or deficit after operating expenses are deducted from gross profits. 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 $40.2 million in 2017, which included $13.5 million in impairment of goodwill and intangible assets, compared to $25.9 million in 2016 and $26.5 million in 2014. The following contains a more detailed discussion of expenses related to sales and marketing, research and product development, general and administrative, and other items.

<u>**Sales and Marketing**</u> S&M expenses include sales, 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 in 2017 increased by 10% from $10.0 million in 2016 to $11 million in 2017 mainly due to an augmentation in headcount and employee-related salaries, and benefits.

S&M expenses in 2016 declined by 6% from $10.6 million in 2015 to $10.0 million in 2016 mainly due to reductions in commissions paid to independent agents and reductions in employee-related salaries, benefits.

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 increased during 2017 to $9.3 million from $8.6 million in 2016. The increase was primarily due to an increase in R&D project costs and employee-related costs partially offset by a reduction in overhead allocated to R&D.

R&D expenses increased marginally during 2016 to $8.6 million from $8.3 million in 2015. The increase was primarily due to an increase in R&D project costs and employee-related costs partially offset by a reduction in overhead allocated to R&D.

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 were approximately $7.2 million in 2017 compared with approximately $7.3 million in 2016. G&A expenses was practically unchanged with main expenses relating to audit, accounting fees and legal expenses.

G&A expenses were approximately $7.3 million in 2016 compared with approximately $7.5 million in 2015. The decrease in G&A expenses was primarily due to a reduction in audit and accounting fees and employee-related costs partially offset by an increase in legal expenses, especially in the fourth quarter.

Impairment of Goodwill and Intangibles

We recognized impairment of goodwill of $12.7 million and intangibles of $0.7 million during the twelve months ended December 31, 2017. There were no such impairment charges during the years ended December 31, 2016 and 2015. The analysis for impairment was mainly triggered due to the decrease of our market capitalization. We recorded impairment charges upon determination that the carrying value of certain intangibles and goodwill is in excess of the implied fair value of such assets.

Provision for income taxes

The tax benefit of $1.7 million during 2017 was primarily the result of the tax benefit on current year losses, offset by additional tax expense related to the impact of the tax rate change on net deferred tax assets. This compared to tax expense of $1.4 million during 2016, which was primarily the result of tax on current year income. This increase in tax benefit of $3.1 million resulted primarily from changing from income in 2016 to losses in 2017.

The tax expense of $1.4 million during 2016 was primarily the result of tax on current year income. This compared to tax expense of $3.8 million during 2015, also primarily the result of tax on current year income. This decrease of $2.4 million resulted primarily from a decrease in the overall pre-tax income for the period, as well as reduced R&D tax credit utilization.

LIQUIDITY, CAPITAL RESOURCES AND FINANCIAL POSITION

As of December 31, 2017, our cash and cash equivalents were approximately $5.6 million compared to $12.1 million as of December 31, 2016. Our working capital was $23.3 million and $30.8 million as of December 31, 2017 and 2016, respectively.

Net cash flows used by operating activities were approximately $9.3 million during 2017, a decrease of approximately $17.1 million from $7.8 million provided by operating activities in 2016. The decrease was primarily due to reduction in net income of $16.6 million and an increase in inventory of $12.6 million partially offset by an increase in non-cash charges of $11.6 million consisting mostly of impairment charges.

Net cash flows provided by investing activities were $10.2 million during 2017 compared to net cash flows used in investing activities of $0.9 million during 2016, an increase of $11.1 million during 2017. The increase was primarily due to an increase in net sales of marketable securities of $13.4 million partially offset by $2.3 million of capitalized patent defense costs.

Net cash used in financing activities increased in 2017 by $0.7 million primarily due to a decrease in payments for stock repurchases and cancellation of stock options of $2.4 million offset by an increase in dividend payments of $0.4 million and an increase in proceeds from equity-based compensation programs and related tax benefits of $1.3 million.

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

Net cash flows provided by operating activities were approximately $7.8 million during 2016, an increase of approximately $0.2 million from $7.6 million provided by operating activities in 2015. The increase was primarily due to increase in cash inflows due to change in operating assets and liabilities of $4.8 million mostly offset by a decrease in non-cash charges of $0.2 million and a reduction in net income of $4.3 million.

Net cash flows used in investing activities were $0.9 million during 2016 compared to net cash flows used in investing activities of $0.6 million during 2015, an increase of $0.3 million during 2016. The increase was primarily due to an increase of $0.5 million in purchases of property, plant and equipment and intangibles partially offset by a reduction in net purchases of marketable securities. Net cash used in financing activities increased in 2016 by $7.3 million primarily due to payments for stock repurchases and cancellation of stock options of $7.8 million and increased dividend payments of $0.4 million partially offset by increased proceeds from equity-based compensation programs and related tax benefits of $1.0 million. Please refer to Note 3 - Business Combinations, Goodwill and Intangibles in the Notes to Consolidated Financial Statements (Part IV) for details on the Company's acquisitions.

Net cash used in financing activities in 2016 consisted of proceeds received from the exercise of stock options amounting to $0.5 million and associated tax benefits of $41 thousand, offset by cash dividends of $1.4 million. Net cash used in financing activities in 2015 consisted of proceeds from the exercise of stock options totaling $1.3 million and associated tax benefits totaling $0.2 million, offset by the acquisition of outstanding stock totaling $2.6 million under the stock repurchase program.

We believe that future income from operations 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 financial position and sound business structure will enable us to raise additional capital if and when needed to meet our short and long-term financing needs. 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, as well as acquisitions that may strategically fit our business and are accretive to our performance. We also intend to use cash to pay quarterly cash dividends and repurchase stock under our repurchase program expired in March 2018.

At December 31, 2017, we had open purchase orders related to our electronics manufacturing service providers of approximately $3.4 million, primarily related to inventory purchases.

At December 31, 2017, we had inventory totaling $23.1 million, of which non-current inventory accounted for $8.7 million. This compares to total inventories of $13.0 million and non-current inventory of $1.7 million as of December 31, 2016.

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 consolidated financial statements, which have been prepared in conformity with U.S. generally accepted accounting principles. We review the accounting policies used in reporting our financial results on a regular basis. The preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. We evaluate our assumptions and estimates on an ongoing basis and may employ outside experts to assist in our evaluations. We believe that the estimates we use are reasonable; however, actual results could differ from those estimates. Our significant accounting policies are described in Note 1 - Business Description, Basis of Presentation and Significant Accounting Policies to the Consolidated Financial Statements included in Part IV of this report. We believe the following critical accounting policies identify our most critical accounting policies, which are the policies that are both important to the representation of our financial condition and results and require our most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain.

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

Revenue and Associated Allowances for Revenue Adjustments and Doubtful Accounts

Included in continuing operations is product revenue, primarily from product sales to distributors, dealers, and end-users. Product revenue is recognized when (i) the products are shipped and any right of return expires, (ii) persuasive evidence of an arrangement exists, (iii) the price is fixed and determinable, and (iv) collection is reasonably assured.

We provide a right of return on product sales to certain distributors under a product rotation program. Under this seldom-used program, once a quarter, a distributor is allowed to return products purchased during the prior quarter for a total value generally not exceeding 15% of the distributor’s net purchases during the preceding quarter. The distributor is, however, required to place a new purchase order for an amount not less than the value of products returned under the stock rotation program. When products are returned, the associated revenue, cost of goods sold, inventory and accounts receivable originally recorded are reversed. When the new order is placed, the revenue, associated cost of goods sold, inventory and accounts receivable are recorded and the product revenue is subject to the deferral analysis described below. In a small number of cases, the distributors are also permitted to return the products for other business reasons.

Revenue from product sales to distributors is not recognized until the return privilege has expired or until it can be determined with reasonable certainty that the return privilege has expired, which approximates when the product is sold-through to customers of our distributors (dealers, system integrators, value-added resellers, and end-users), rather than when the product is initially shipped to a distributor. At each quarter-end, we evaluate the inventory in the distribution channel through information provided by our distributors. The level of inventory in the channel will fluctuate up-ward or down-ward each quarter based upon our distributors’ individual operations. Accordingly, each quarter-end deferral of revenue and associated cost of goods sold are 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 are deferred until we receive payment for the product sales made to such distributors or channel partners.

The accuracy of the deferred revenue and costs depend to a large extent on the accuracy of the inventory reports provided by our distributors and other resellers, and any material error in those reports would affect our revenue deferral. However, we believe that the controls we have in place, including periodic physical inventory verifications and analytical reviews, would help us identify and prevent any material errors in such reports. As part of these controls, we sample test the inventory of a limited number of distributors on an annual basis, most recently in the fourth quarter of 2017, to verify inventory levels reported.

The amount of deferred cost of goods sold was included in distributor channel inventories. The following table details the amount of deferred revenue, cost of goods sold, and gross profit:

	As of December 31,		
	2017	**2016**	**2015**
Deferred revenue	$4,635	$3,882	$4,549
Deferred cost of goods sold	1,555	1,530	1,628
Deferred gross profit	$3,080	$2,352	$2,921

We offer rebates and market development funds to certain of our distributors, dealers/resellers, and end-users based upon volume of product purchased by them. We record rebates quarterly as a reduction of revenue in accordance with GAAP.

We offer credit terms on the sale of our products to a majority of our channel partners and perform ongoing credit evaluations of our customers' financial condition. We maintain an allowance for doubtful accounts for estimated losses resulting from the inability or unwillingness of our channel partners to make required payments based upon our historical collection experience and expected collectability of all accounts receivable. Our actual bad debts in future periods may differ from our current estimates and the differences may be material, which may have an adverse impact on our future accounts receivable and cash position.

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

Impairment of Goodwill and Intangible Assets

We perform impairment tests of goodwill and intangible assets with indefinite useful lives on an annual basis in the fourth fiscal quarter, or sooner if a triggering event occurs suggesting possible impairment of the values of these assets. Impairment testing for these assets involves a two-step process. In the first step, the fair value of the reporting unit holding the assets is compared to its carrying amount. If the carrying amount of the reporting unit exceeds its fair value, the second step of the impairment test is performed to measure the amount of the impairment loss, if any. In the second step, the fair value of the reporting unit is allocated to all of its assets and liabilities, including intangible assets and liabilities not recorded on the balance sheet. The excess, if any, of the fair value of the reporting unit over the sum of the fair values allocated to identified assets and liabilities is the value of goodwill to be compared to its carrying value.

Based on the third quarter results of the Company’s recent impairment analysis triggered by the fall in the Company’s stock price and recent financial results, the Company determined that goodwill and an intangible asset consisting of customer relationships were impaired and recognized a charge of $12.7 million towards goodwill impairment and $0.7 million towards the intangible asset impairment for the three and nine months ended September 30, 2017.

Impairment of Long-Lived Assets

We assess the impairment of long-lived assets, such as property and equipment and definite-lived intangible assets subject to amortization, whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset or asset group to estimated future undiscounted net cash flows of the related asset or group of assets over their remaining lives. If the carrying amount of an asset exceeds its estimated future undiscounted cash flows, an impairment charge is recognized for the amount by which the carrying amount exceeds the estimated fair value of the asset. Impairment of long-lived assets is assessed at the lowest levels for which there are identifiable cash flows that are independent of other groups of assets. The impairment of long-lived assets requires judgments and estimates. If circumstances change, such estimates could also change. Assets held for sale are reported at the lower of the carrying amount or fair value, less the estimated costs to sell.

Accounting for Income Taxes

We are subject to income taxes in both the United States and in certain non-U.S. jurisdictions. We estimate our current tax position together with our future tax consequences attributable to temporary differences resulting from differing treatment of items, such as deferred revenue, depreciation, and other reserves for tax and accounting purposes. These temporary differences result in deferred tax assets and liabilities. We must then assess the likelihood that our deferred tax assets will be recovered from future taxable income, prior year carryback, or future reversals of existing taxable temporary differences. To the extent we believe that recovery is not more likely than not, we establish a valuation allowance against these deferred tax assets. Significant judgment is required in determining our provision for income taxes, our deferred tax assets and liabilities, and any valuation allowance recorded against our deferred tax assets.

To the extent we establish a valuation allowance in a period, we must include and expense the allowance within the tax provision in the consolidated statement of operations. In accordance with ASC Topic 740, “Accounting for Income Taxes”, we analyzed our valuation allowance at December 31, 2017 and determined that based upon available evidence it is more likely than not that certain of our deferred tax assets related to foreign net operating loss carryovers, foreign intangible assets, state R&D tax credit carryovers, and capital loss carryovers will not be realized and, accordingly, we have recorded a valuation allowance against these deferred tax assets in the amount of $2.2 million. Please refer to Note 12 - Income Taxes in the Notes to Consolidated Financial Statements for additional information.

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

We perform a quarterly analysis of obsolete and slow-moving inventory to determine if any inventory needs to be written down. In general, we write-down our excess and obsolete inventory by an amount that is equal to the difference between the cost of the inventory and its estimated market value if market value is less than cost, based upon assumptions about future product life-cycles, product demand, shelf life of the product, inter-changeability of the product and market conditions. Those items that are found to have a supply in excess of our estimated current demand are considered to be slow-moving or obsolete and classified as long-term. An appropriate reserve is made to write down the value of that inventory to its expected realizable value. These charges are recorded in cost of goods sold. The reserve against slow-moving or obsolete inventory is increased or reduced based on several factors which, among other things, require us to make an estimate of a product's life-cycle, potential demand and our ability to sell these products at estimated price levels. While we make considerable efforts to calculate reasonable estimates of these variables, actual results may vary. If there were to be a sudden and significant decrease in demand for our products, or if there were a higher incidence of inventory obsolescence because of changing technology and customer requirements, we could be required to increase our inventory allowances, and our gross profit could be adversely affected.

Share-Based Payments

We estimate the fair value of stock options using the Black-Scholes option pricing model, which requires certain estimates, including an expected forfeiture rate and expected term of options granted. We also make decisions regarding the method of calculating expected volatilities and the risk-free interest rate used in the option-pricing model. The resulting calculated fair value of stock options is recognized as compensation expense over the requisite service period, which is generally the vesting period. When there are changes to the assumptions used in the option-pricing model, including fluctuations in the market price of our common stock, there will be variations in the calculated fair value of our future stock option awards, which results in variation in the compensation cost recognized.

IMPACT OF RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

For descriptions of recently issued accounting standards, see Note 1. Business Description, Basis of Presentation and Significant Accounting Policies of our Notes to Consolidated Financial Statements.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk represents the risk of changes in the value of a financial instrument, derivative or non-derivative, caused by fluctuations in interest rates, foreign exchange rates, and equity prices. Changes in these factors could cause fluctuations in the results of our operations and cash flows. In the ordinary course of business, we are exposed to foreign currency and interest rate risks. These risks primarily relate to the sale of products and services to foreign customers and changes in interest rates on any interest-bearing investments or notes receivable, notes payable, or capital leases.

Financial instruments which potentially expose us to concentrations of credit risk primarily consist of cash and cash equivalents, short-term and long-term investments, accounts receivable and unbilled accounts receivable.

Our fixed-income portfolio consisting primarily of investment-grade securities is managed by professional money managers. Our investment securities also consist of triple-A rated short-term money market funds that typically invest in U.S. Treasury, U.S. government agency, and highly rated corporate securities. Since these funds are managed in a manner designed to preserve capital we do not expect any material changes in market values, as a result of increase or decrease in interest rates.

We believe that our credit policies reflect normal industry terms and business risk. We do not anticipate non-performance by the counterparties and, accordingly, do not require collateral. Credit losses and write-offs of accounts receivable balances have historically not been material to our financial statements and have not exceeded our expectations.

We did not have any notes payable and capital lease obligations as of December 31, 2017. Accordingly, we do not have significant exposure to changing interest rates. We have not undertaken any additional actions to cover market interest rate market risk and are not a party to any other interest rate market risk management activities. We do not purchase or hold any derivative financial instruments.

Although we enter into non-US Dollar transactions, foreign currency exposures arising from these transactions are not material.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Financial statements and supplementary data required by this are included herein as a separate section of this Form 10-K, beginning on page F-1, and are incorporated in this Item 8 by reference.

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

None.

ITEM 9A. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures designed to ensure that information required to be disclosed in our reports filed under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), is recorded, processed, summarized, and reported within the required time periods, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Senior Vice President of Finance, as appropriate, to allow for timely decisions regarding required disclosure. As required by Rule 13a-15 under the Exchange Act, we have completed an evaluation, under the supervision and with the participation of our management, including the Chief Executive Officer and the Senior Vice President of Finance, of the effectiveness and the design and operation of our disclosure controls and procedures as of December 31, 2017. Our disclosure controls and procedures are designed to provide reasonable assurance of achieving their objectives. 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 Annual Report, our disclosure controls and procedures were not effective at a reasonable assurance level as of December 31, 2017 due to the material weakness in internal control over financial reporting as described below. Despite the existence of this material weakness, the Company believes the financial information presented herein is materially correct and in accordance with generally accepted accounting principles in the United States of America, and do not contain any untrue statement of a material fact or omit to state a material fact required to be stated or that is necessary to make a statement not misleading in light of the circumstances under which it was made. The consolidated financial statements together with the other financial information included in the consolidated financial statements and this Annual Report on Form 10-K fairly present, in all material respects, the financial condition, financial performance and cash flows of the Company for the year ended December 31, 2017.

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The effectiveness of any system of disclosure controls and procedures is subject to certain limitations, including the exercise of judgment in designing, implementing, and evaluating the controls and procedures, the assumptions used in identifying the likelihood of future events, and the inability to eliminate improper conduct completely. A controls system, no matter how well designed and operated, cannot provide absolute assurance that the objectives of the controls system are met, and no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within a Company have been detected. As a result, there can be no assurance that our disclosure controls and procedures will detect all errors or fraud.

Management's Annual Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act. Our internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with United States generally accepted accounting principles.

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

Our management conducted an evaluation of the effectiveness of our internal control over financial reporting as of December 31, 2017 based on the framework set forth in *Internal Control - Integrated Framework* (2013 framework) issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Public Company Accounting Oversight Board's Auditing Standard No. 5 defines a material weakness as a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of annual or interim financial statements will not be prevented or detected on a timely basis. 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 for the fiscal year ended December 31, 2017 and its testing and assessment of the design and effectiveness of internal controls over financial reporting in a timely manner. This material weakness was identified prior to the issuance of our consolidated financial statements for the year ended December 31, 2017, and could result in material misstatements in the Company's annual or interim consolidated financial statements that would not be prevented or detected.

As a result of the material weakness described above, management concluded that our internal control over financial reporting was not effective as of December 31, 2017. The effectiveness of our internal control over financial reporting as of December 31, 2017 has been audited by Tanner, LLC, our independent registered public accounting firm, as stated in their report appearing on page F-1.

Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting that occurred during the fourth fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Remediation Activities

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.

ITEM 9B. OTHER INFORMATION

None.

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PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The information required by this item is incorporated herein by reference to the definitive proxy statement for our 2017 annual meeting of shareholders or an amendment to this Annual Report on Form 10-K, which will be filed with the Securities and Exchange Commission within 120 days after the end of our fiscal year covered by this Annual Report on form 10-K.

ITEM 11. EXECUTIVE COMPENSATION

The information required by this item is incorporated herein by reference to the definitive proxy statement for our 2017 annual meeting of shareholders or an amendment to this Annual Report on Form 10-K, which will be filed with the Securities and Exchange Commission within 120 days after the end of our fiscal year covered by this Annual Report on form 10-K.

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

The information required by this item is incorporated herein by reference to the definitive proxy statement for our 2017 annual meeting of shareholders or an amendment to this Annual Report on Form 10-K, which will be filed with the Securities and Exchange Commission within 120 days after the end of our fiscal year covered by this Annual Report on form 10-K.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE

The information required by this item is incorporated herein by reference to the definitive proxy statement for our 2017 annual meeting of shareholders or an amendment to this Annual Report on Form 10-K, which will be filed with the Securities and Exchange Commission within 120 days after the end of our fiscal year covered by this Annual Report on form 10-K.

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

The information required by this item is incorporated herein by reference to the definitive proxy statement for our 2017 annual meeting of shareholders or an amendment to this Annual Report on Form 10-K, which will be filed with the Securities and Exchange Commission within 120 days after the end of our fiscal year covered by this Annual Report on form 10-K.

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PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES

1. Financial Statements: Financial statements set forth under Part II, Item 8 of this Annual Report on Form 10-K are filed in a separate section of this Form 10-K. See the “Index to Consolidated Financial Statements”.

2. Financial Statement Schedules: All schedules are omitted since they either are not required, not applicable or the information is presented in the accompanying consolidated financial statements and notes thereto.

3. Exhibits: The exhibits listed under the Index of exhibits in the next page are filed or incorporated by reference as part of this Form 10-K.

ITEM 16. FORM 10-K SUMMARY

Not applicable.

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INDEX TO EXHIBITS

Exhibit Number	Exhibit Description	Form	Exhibit Incorporated Herein by Reference	Filing Date
2.1	Agreement and Plan of Merger, dated as of November 3, 2009, by and among ClearOne Communications, Inc., Alta-Wasatch Acquisition Corporation, NetStreams, Inc., Austin Ventures VIII, L.P., and Kevin A. Reinis.	8-K	2.2	11/09/09
3.1	Amended and Restated Articles of Incorporation of ClearOne, Inc.	10-K	3.1	03/25/13
3.2	Bylaws	10-K	3.2	03/31/11
10.1	1997 Employee Stock Purchase Plan	S-8	4.9	10/06/06
10.2	1998 Stock Option Plan	S-8	4.8	10/06/06
10.3	2007 Equity Incentive Plan	S-8	4.7	01/22/08
10.4	ClearOne, Inc. Equity Incentive Plan	S-8	4.8	01/26/16
10.5	Amendment No. 1 to the ClearOne, Inc. Equity Incentive Plan	S-8	4.11	06/30/15
10.6	ClearOne, Inc. Employee Stock Purchase Plan	S-8	4.3	06/30/15
10.7	Office Lease between Edgewater Corporate Park, LLC and ClearOne Communications, Inc. dated June 5, 2006	10-K	10.19	09/14/06
10.8	Stock Purchase Agreement Between ClearOne, Inc. and Doran M. Oster Dated March 4, 2014 for the Sabine Acquisition.	10-K	10.7	03/20/14
10.9	Manufacturing Services Agreement between Flextronics Industrial, Ltd. and ClearOne Communications, Inc. dated November 3, 2008	10-K	10.21	10/13/09
10.10	Framework Agreement between ClearOne, Inc. and Dialcom Networks S.L., dated December 20, 2013	8-K	10.1	04/07/14
10.11	Amendment to Framework Agreement between ClearOne, Inc. and Dialcom Networks S.L., dated March 31, 2014	8-K	10.2	04/07/14
10.12	Purchase Agreement between ClearOne, Inc. and Dialcom Networks S.L., dated March 31, 2014	10-Q	10.3	05/14/14
10.13	Form of Offer to Repurchase Eligible Options for Cash	10-Q	10.1	05/10/16
14.1	Code of Ethics, approved by the Board of Directors on August 23, 2006	10-K	14.1	09/14/06
21.1†	Subsidiaries of the registrant			
23.1†	Consent of Tanner LLC, Independent Registered Public Accounting Firm			
31.1†	Section 302 Certification of Chief Executive Officer			
31.2†	Section 302 Certification of Chief Financial Officer			
32.1†	Section 906 Certification of Chief Executive Officer			
32.2†	Section 906 Certification of Chief Financial Officer			
101.INS‡	XBRL Instance Document			
101.SCH‡	XBRL Taxonomy Extension Schema			
101.CAL‡	XBRL Taxonomy Extension Calculation Linkbase			
101.DEF‡	XBRL Taxonomy Extension Definitions Linkbase			
101.LAB‡	XBRL Taxonomy Extension Label Linkbase			

101.PRE‡ XBRL Taxonomy Extension Presentation Linkbase

* Constitutes a management contract or compensatory plan or arrangement.

† Filed herewith

‡ Information furnished herewith shall not be deemed to be "filed" for the purposes of Section 18 of the 1934 Act

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SIGNATURES

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

CLEARONE, INC.

Registrant

/s/ Zeynep Hakimoglu
Zeynep Hakimoglu
President, Chief Executive Officer and Chairman of the Board
April 20, 2018

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

/s/ Zeynep Hakimoglu
Zeynep Hakimoglu
President, Chief Executive Officer and Chairman of the Board
(principal executive officer)
April 20, 2018

/s/ Narsi Narayanan
Narsi Narayanan
Senior Vice President of Finance
(principal accounting and principal financial officer)
April 20, 2018

/s/ Brad R. Baldwin
Brad R. Baldwin
Director
April 20, 2018

/s/ Larry R. Hendricks
Larry R. Hendricks
Director
April 20, 2018

/s/ Eric L. Robinson
Eric L. Robinson
Director
April 20, 2018

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CLEARONE, INC.

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Stockholders and Board of Directors
ClearOne, Inc.

Opinion on the Consolidated Financial Statements

We have audited the accompanying consolidated balance sheets of ClearOne, Inc. and subsidiaries (collectively, ClearOne) as of December 31, 2017 and 2016, and the related consolidated statements of operations and comprehensive income (loss), shareholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2017, and the related notes to the consolidated financial statements (collectively referred to as the "consolidated financial statements"). In our opinion, the consolidated financial statements referred to above present fairly, in all material aspects, the financial position of ClearOne as of December 31, 2017 and 2016, and the results of its operations and its cash flows for each of the years in the three-year period ended December 31, 2017, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) ("PCAOB"), the Company's internal control over financial reporting as of December 31, 2017, based on criteria established in *Internal Control – Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission, and our report dated April XX, 2018 expressed an adverse opinion on the effectiveness of the Company's internal control over financial reporting.

Basis for Opinion

These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that our audits provide a reasonable basis for our opinion.

We have served as the Company's auditor since October 14, 2015.

/s/ TANNER LLC

Salt Lake City, Utah
April 20, 2018

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Stockholders and Board of Directors
ClearOne, Inc.

Opinion on Internal Control Over Financial Reporting

We have audited ClearOne, Inc. and subsidiaries' (the "Company") internal control over financial reporting as of December 31, 2017, based on criteria established in *Internal Control – Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. In our opinion, because of the effect of the material weakness noted below, the Company did not maintain, in all material respects, effective internal control over financial reporting as of December 31, 2017, based on criteria established in *Internal Control – Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) ("PCAOB"), the consolidated balance sheets of the Company as of December 31, 2017 and 2016, the related consolidated statements of operations, comprehensive income (loss), stockholders' equity and cash flows for the each of the years in the three-year period ended December 31, 2017, and the related notes to the consolidated financial statements (collectively referred to as the "consolidated financial statements"), and our report dated April 20, 2018 expressed an unqualified opinion on those consolidated financial statements.

A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the Company's annual or interim financial statements will not be prevented or detected on a timely basis. A material weakness related to the accurate and timely reporting of its financial results and disclosures for the fiscal year ended December 31, 2017 and its testing and assessment of the design and effectiveness of internal controls over financial reporting in a timely manner has been identified and included in management's assessment. The material weakness was considered in determining the nature, timing, and extent of audit tests applied in our audit of the 2017 consolidated financial statements, and this report does not affect our report on those consolidated financial statements.

Basis for Opinion

The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Annual Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

Definition and Limitations of Internal Control Over Financial Reporting

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

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

/s/ TANNER LLC

Salt Lake City, Utah
April 20, 2018

CLEARONE, INC.

CONSOLIDATED BALANCE SHEETS

(Dollars in thousands, except par value)

	December 31, 2017	December 31, 2016
ASSETS		
Current assets:		
Cash and cash equivalents	$ 5,571	$ 12,100
Marketable securities	2,689	5,030
Receivables, net of allowance for doubtful accounts of $472 and $187, as of December 31, 2017 and 2016 respectively	7,794	7,461
Inventories	14,415	11,377
Distributor channel inventories	1,555	1,530
Prepaid expenses and other assets	1,862	2,642
Total current assets	33,886	40,140
Long-term marketable securities	10,349	21,365
Long-term inventories, net	8,708	1,664
Property and equipment, net	1,549	1,513
Intangible assets, net	6,543	5,677
Goodwill	—	12,724
Deferred income taxes	6,531	4,654
Other assets	311	387
Total assets	$ 67,877	$ 88,124
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 4,122	$ 3,545
Accrued liabilities	1,843	1,894
Deferred product revenue	4,635	3,882
Total current liabilities	10,600	9,321
Deferred rent	103	103
Other long-term liabilities	607	1,251
Total liabilities	11,310	10,675
Shareholders' equity:		
Common stock, par value $0.001, 50,000,000 shares authorized, 8,319,022 and 8,812,644 shares issued and outstanding as of December 31, 2017 and 2016 respectively	8	9
Additional paid-in capital	47,464	46,669
Accumulated other comprehensive loss	(65)	(205)
Retained earnings	9,160	30,976
Total shareholders' equity	56,567	77,449
Total liabilities and shareholders' equity	$ 67,877	$ 88,124

See accompanying notes

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CLEARONE, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)

(Dollars in thousands, except per share amounts)

	Year ended December 31,		
	2017	**2016**	**2015**
Revenue	$*41,804*	$*48,637*	$*57,796*
Cost of goods sold	*17,795*	*19,150*	*21,077*
Gross profit	*24,009*	*29,487*	*36,719*
Operating expenses:			
Sales and marketing	*10,996*	*10,032*	*10,646*
Research and product development	*9,342*	*8,584*	*8,318*
General and administrative	*7,161*	*7,325*	*7,493*
Impairment of an intangible asset	*769*	—	—
Impairment of goodwill	*12,724*	—	—
Legal settlement	*(790*)	—	—
Total operating expenses	*40,202*	*25,921*	*26,457*
Operating income/(loss)	*(16,193*)	*3,566*	*10,262*
Other income, net	*300*	*312*	*289*
Income/(loss) before income taxes	*(15,893*)	*3,878*	*10,551*
Benefit from/(provision for) income taxes	*1,721*	*(1,434*)	*(3,775*)
Net income/(loss)	$*(14,172*)	$*2,444*	$*6,776*
Basic earnings/(loss) per common share	$*(1.65*)	$*0.27*	$*0.74*
Diluted earnings/(loss) per common share	$*(1.65*)	$*0.26*	$*0.71*
Basic weighted average shares outstanding	*8,576,588*	*9,021,980*	*9,127,385*
Diluted weighted average shares outstanding	*8,576,588*	*9,306,034*	*9,594,659*
Comprehensive income:			
Net income/(loss)	$*(14,172*)	$*2,444*	$*6,776*
Other comprehensive income:			
Unrealized gain (loss) on available-for-sale securities, net of tax	*36*	*(1*)	*(81*)
Change in foreign currency translation adjustment	*104*	*(38*)	*(77*)
Comprehensive income/(loss)	$*(14,032*)	$*2,405*	$*6,618*

See accompanying notes

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CLEARONE, INC.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(Dollars in thousands, except per share data)

	Common Stock		Additional Paid-in	Accumulated Other Comprehensive Income (Loss)	Retained	Total Shareholders'
	Shares	**Amount**	**Capital**		**Earnings**	**Equity**
Balances at December 31, 2014	9,097,827	9	44,939	(8)	31,076	76,016
Exercise of stock options	56,143	-	308	-	-	308
Cash dividends, $0.155 per share	-	-	-	-	(1,417)	(1,417)
Tax benefit - stock option exercises	-	-	41	-	-	41
Stock-based compensation expense	15,005	-	848	-	-	848
Proceeds from employee stock purchase plan	14,982	-	155	-	-	155
Unrealized loss on available-for-sale securities, net of tax	-	-	-	(81)	-	(81)
Foreign currency translation adjustment	-	-	-	(77)	-	(77)
Net income	-	-	-	-	6,776	6,776
Balances at December 31, 2015	9,183,957	9	46,291	(166)	36,435	82,569
Exercise of stock options	149,315	-	686	-		686
Repurchased and cancellation of stock options	-	-	(1,752)	-	-	(1,752)
Stock repurchased	(542,259)	-	-	-	(6,086)	(6,086)
Cash dividends, $0.20 per share	-	-	-	-	(1,817)	(1,817)
Stock-based compensation expense	12,491	-	667	-	-	667
Tax benefit - stock option exercises	-	-	690	-	-	690
Proceeds from employee stock purchase plan	9,140	-	87	-	-	87
Unrealized loss on available-for-sale securities, net of tax	-	-	-	(1)	-	(1)
Foreign currency translation adjustment	-	-	-	(38)	-	(38)
Net income	-	-	-	-	2,444	2,444
Balances at December 31, 2016	8,812,644	9	46,669	(205)	30,976	77,449
Exercise of stock options	45,260	-	64	-	-	64
Stock repurchased	(551,936)	(1)	-	-	(5,118)	(5,119)
Restricted stock granted	5,000	-	-	-	-	-
Cash dividends, $0.26 per share	-	-	-	-	(2,239)	(2,239)

Stock-based compensation expense	-	-	665	-	-	665
Cancellation of restricted stock and stock options	(1,056)	-		-	(287)	(287)
Proceeds from employee stock purchase plan	9,110	-	66	-	-	66
Unrealized loss on available-for-sale securities, net of tax	-	-	-	36	-	36
Foreign currency translation adjustment	-	-	-	104	-	104
Net loss	-	-	-	-	(14,172)	(14,172)
Balances at December 31, 2017	8,319,022	$ 8	$ 47,464	$ (65)	$ 9,160	$ 56,567

See accompanying notes

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CLEARONE, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year ended December 31,		
	2017	**2016**	**2015**
Cash flows from operating activities:			
Net income	$(14,172)	$2,444	$6,776
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization expense	1,531	1,873	2,058
Impairment of goodwill and intangible assets	13,493	-	-
Amortization of deferred rent	(44)	(73)	(95)
Stock-based compensation expense	665	667	848
Provision for (recoveries of) doubtful accounts, net	252	132	(4)
Write-down of inventory to net realizable value	649	653	496
Loss on disposal of assets	7	54	7
Tax benefit from exercise of stock options	-	(690)	(41)
Deferred income taxes	(1,877)	439	(4)
Changes in operating assets and liabilities:			
Receivables	(526)	1,085	1,201
Inventories	(10,756)	1,869	(2,249)
Prepaid expenses and other assets	9	(209)	824
Accounts payable	572	733	(242)
Accrued liabilities	(23)	(319)	(1,219)
Income taxes payable	853	(207)	323
Deferred product revenue	740	(665)	(447)
Other long-term liabilities	(644)	48	(638)
Net cash provided/(used) by operating activities	(9,271)	7,834	7,594
Cash flows from investing activities:			
Capitalized patent defense costs	(2,289)	-	-
Purchase of property and equipment	(638)	(730)	(359)
Purchase of intangible assets	(278)	(161)	-
Proceeds from maturities and sales of marketable securities	17,640	9,795	7,341
Purchase of marketable securities	(4,248)	(9,826)	(7,630)
Net cash used/(provided) in investing activities	10,187	(922)	(648)
Cash flows from financing activities:			
Net proceeds from equity-based compensation programs	130	773	463
Repurchase and cancellation of stock options	(287)	(1,752)	-
Tax benefits from equity-based compensation programs	-	690	41
Dividend payments	(2,239)	(1,817)	(1,417)
Payments for stock repurchases	(5,119)	(6,086)	-
Net cash used in financing activities	(7,515)	(8,192)	(913)

Effect of exchange rate changes on cash and cash equivalents	*70*	*(32)*	*(61)*
Net increase (decrease) in cash and cash equivalents	*(6,529)*	*(1,312)*	*5,972*
Cash and cash equivalents at the beginning of the year	*12,100*	*13,412*	*7,440*
Cash and cash equivalents at the end of the year	$*5,571*	$*12,100*	$*13,412*

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CLEARONE, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year ended December 31,		
	2017	**2016**	**2015**
Supplemental disclosure of cash flow information:			
Cash paid for income taxes	$*6*	$*1,154*	$*3,730*

See accompanying notes

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CLEARONE, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except share and 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 Company that designs, develops and sells conferencing, collaboration, network streaming and digital signage solutions for audio and visual communications. The performance and simplicity of our advanced comprehensive solutions offer unprecedented levels of functionality, reliability, and scalability.

Basis of Presentation:

Fiscal Year – This report on Form *10*-K includes consolidated balance sheets for the years ended *December 31, 2017* and *2016* and the related consolidated statements of operations and comprehensive income/(loss), cash flows, and shareholders' equity for each of the years *2017, 2016* and *2015.*

Consolidation – These consolidated financial statements include the financial statements of ClearOne, Inc. and its wholly owned subsidiaries. All inter-Company accounts and transactions have been eliminated in consolidation. Certain prior year amounts have been reclassified to conform to the current year presentation.

Use of Estimates – The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of sales and expenses during the reporting periods. Key estimates in the accompanying consolidated financial statements include, among others, revenue recognition, allowances for doubtful accounts and product returns, provisions for obsolete inventory, potential impairment of goodwill and of long-lived assets, and deferred income tax asset valuation allowances. Actual results could differ materially from these estimates.

Foreign Currency Translation – We are exposed to foreign currency exchange risk through our foreign subsidiaries. Other than our Spain subsidiary, our foreign subsidiaries are U.S. dollar functional, for which gains and losses arising from remeasurement are included in earnings. Our Spain subsidiary is Euro functional, for which gains and losses arising from translation are included in accumulated other comprehensive income or loss. We translate and remeasure foreign assets and liabilities at exchange rates in effect at the balance sheet dates. We translate revenue and expenses using average rates during the year.

Concentration Risk – We depend on an outsourced manufacturing strategy for our products. We outsource the manufacture of all of our products (except digital signage products) to *third* party manufacturers located in both the U.S. and Asia. If any of these manufacturers experience difficulties in obtaining sufficient supplies of components, component prices significantly exceeding the anticipated costs, an interruption in their operations, or otherwise suffer capacity constraints, we would experience a delay in production and shipping of these products, which would have a negative impact on our revenues. Should there be any disruption in services due to natural disaster, economic or political difficulties, transportation restrictions, acts of terror, quarantine or other restrictions associated with infectious diseases, or other similar events, or any other reason, such disruption *may* have a material adverse effect on our business. Operating in the international environment exposes us to certain inherent risks, including unexpected changes in regulatory requirements and tariffs, and potentially adverse tax consequences, which could materially affect our results of operations. Currently, we have *no second* source of manufacturing for a portion of our products.

Significant Accounting Policies:

Cash Equivalents – The Company considers all highly-liquid investments with a maturity of *three* months or less, when purchased, to be cash equivalents. The Company places its temporary cash investments with high-quality financial institutions. At times, such investments *may* be in excess of the Federal Deposit Insurance Corporation insurance limits.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except share and per share amounts)

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 shareholders' 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.

A decline in the market value of any available-for-sale security below cost that is deemed other than temporary results in a charge to earnings and establishes a new cost basis for the security. Losses are charged against "Other income" when a decline in fair value is determined to be other than temporary. We review several factors to determine whether a loss is other than temporary. These factors include, but are *not* limited to: (i) the extent to which the fair value is less than cost and the cause for the fair value decline, (ii) the financial condition and near term prospects of the issuer, (iii) the length of time a security is in an unrealized loss position and (iv) our ability to hold the security for a period of time sufficient to allow for any anticipated recovery in fair value. There were *no* other-than-temporary impairments recognized during the years ended *December 31, 2017, 2016* and *2015.*

Accounts Receivable – Accounts receivable are recorded at the invoiced amount. Generally, credit is granted to customers on a short-term basis without requiring collateral, and as such, these accounts receivable, do *not* bear interest, although a finance charge *may* be applied to such receivables that are past due. The Company extends credit to customers who it believes have the financial strength to pay. The Company has in place credit policies and procedures, an approval process for sales returns and credit memos, and processes for managing and monitoring channel inventory levels.

The allowance for doubtful accounts is the Company's best estimate of the amount of probable credit losses in the Company's existing accounts receivable. Management regularly analyzes accounts receivable including current aging, historical write-off experience, customer concentrations, customer creditworthiness, and current economic trends when evaluating the adequacy of the allowance for doubtful accounts. We review customer accounts quarterly by *first* assessing accounts with aging over a specific duration and balance over a specific amount. We review all other balances on a pooled basis based on past collection experience. Accounts identified in our customer-level review as exceeding certain thresholds are assessed for potential allowance adjustment if we conclude the financial condition of that customer has deteriorated, adversely affecting their ability to make payments. Delinquent account balances are written off if the Company determines that the likelihood of collection is *not* probable. If the assumptions that are used to determine the allowance for doubtful accounts change , the Company *may* have to provide for a greater level of expense in future periods or reverse amounts provided in prior periods.

The Company's allowance for doubtful accounts activity for the years ended as follows:

	Year Ended December 31,		
	2017	**2016**	**2015**
Balance at beginning of the year	$*187*	$*54*	$*58*
Allowance increase (decrease)	*287*	*148*	*36*
Write offs , net of recoveries	*(2*)	*(15*)	*(40*)
Balance at end of the year	$*472*	$*187*	$*54*

Inventories – Inventories are valued at the lower of cost or market, with cost computed on a *first*-in, *first*-out ("FIFO") basis. In addition to the price of the product purchased, the cost of inventory includes the Company's internal manufacturing costs, including warehousing, engineering, material purchasing, quality and product planning expenses and applicable overhead, *not* in excess of estimated realizable value. Consideration is given to obsolescence, excessive levels, deterioration, direct selling expenses, and other factors in evaluating net realizable value.

Distributor channel inventories include products that have been delivered to customers for which revenue recognition criteria have *not* been met.

The inventory also includes advance replacement units (valued at cost) provided by the Company to end-users to service defective products under warranty. The value of advance replacement units included in the inventory was *$76* and *$21,* as of *December 31, 2017* and *2016,* respectively.

The inventory consists of current inventory of $14,415 and long-term inventory of $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.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except share and per share amounts)

Property and Equipment – Property and equipment are stated at cost less accumulated depreciation and amortization. Expenditures that materially increase values or capacities or extend useful lives of property and equipment are capitalized. Routine maintenance, repairs, and renewal costs are expensed as incurred. Gains or losses from the sale, trade-in, or retirement of property and equipment are recorded in current operations and the related book value of the property is removed from property and equipment accounts and the related accumulated depreciation and amortization accounts. Estimated useful lives are generally *two* to *ten* years. Depreciation and amortization are calculated over the estimated useful lives of the respective assets using the straight-line method. Leasehold improvement amortization is computed using the straight-line method over the shorter of the lease term or the estimated useful life of the related assets.

Goodwill and Intangible Assets – Intangible assets acquired in a purchase business combination are amortized over their useful lives unless these lives are determined to be indefinite. Intangible assets are carried at cost, less accumulated amortization. Amortization is computed over the estimated useful lives of the respective assets, which are generally *three* to *ten* years. Goodwill represents the excess of costs over the fair value of net assets of businesses acquired. Goodwill and intangible assets acquired in a purchase business combination and determined to have an indefinite useful life are *not* amortized.

Impairment of Goodwill - Goodwill is measured as the excess of the cost of acquisition over the sum of the amounts assigned to tangible and identifiable intangible assets acquired less liabilities assumed. In accordance with the provisions of FASB ASC Topic *350, Intangibles – Goodwill and Other* the Company performs impairment tests of goodwill on an annual basis in the *fourth* fiscal quarter, or sooner if a triggering event occurs suggesting possible impairment of the values of these assets.

We assess the recoverability of our *one* reporting unit's carrying value of goodwill by making a qualitative or quantitative assessment. If we begin with a qualitative assessment and are able to support the conclusion that it is *not* more likely than *not* that the fair value of the Company is less than its carrying value, we are *not* required to perform the *two*-step impairment test. Otherwise, using the two–step approach is required (See Note *3* – Business Combinations, Goodwill and Intangibles). ClearOne and all of its subsidiaries are considered as *one* reporting unit for this purpose.

In the *first* step of the goodwill impairment test, we compare the carrying value the Company, including its recorded goodwill, to the estimated fair value. We estimate the fair value using an equity-value based methodology. The principal method used is an equity-value based method in which the Company's market-cap is compared to the net book value. This value is then compared to total net assets. If the fair value of the Company exceeds its carrying value, the goodwill is *not* impaired and *no* further review is required. However, if the fair value of the reporting unit is less than its carrying value, we perform the *second* step of the goodwill impairment test to determine the amount of the impairment charge, if any.

The *second* step involves a hypothetical allocation of the fair value of the Company to its net tangible and intangible assets (excluding goodwill) as if the business unit were newly acquired, which results in an implied fair value of goodwill. The amount of the impairment charge is the excess of the recorded goodwill over the implied fair value of goodwill.

During the *third* quarter ended *September 30, 2017,* we recorded *$12,724,* or the entire value of goodwill, as an impairment charge.

Impairment of Long-Lived Assets - Long-lived assets, such as property, equipment, and definite-lived intangible assets subject to depreciation and amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying value of an asset *may not* be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset or asset group to estimated future undiscounted net cash flows of the related asset or group of assets over their remaining lives. If the carrying amount of an asset exceeds its estimated future undiscounted cash flows, an impairment charge is recognized for the amount by which the carrying amount exceeds the estimated fair value of the asset. Impairment of long-lived assets is assessed at the lowest levels for which there are identifiable cash flows that are independent of other groups of assets. The impairment of long-lived assets requires judgments and estimates. If circumstances change, such estimates could also change. Assets held for sale are reported at the lower of the carrying amount or fair value, less the estimated costs to sell.

During the *twelve* months ended *December 31, 2017* we recorded *$769* as a charge for impairment of an intangible asset consisting of customer relationships.

Revenue Recognition – Product revenue is recognized when (i) the products are shipped, (ii) persuasive evidence of an arrangement exists, (iii) the price is fixed and determinable, and (iv) collection is reasonably assured.

The Company provides a right of return on product sales to certain distributors and other resellers under a product rotation program. Under this seldom-used program, once a quarter, a distributor or reseller is allowed to return products purchased during the prior *180* days for a total value generally *not* exceeding *15%* of the distributor's or reseller's net purchases during the preceding quarter. The distributor or reseller is, however, required to place a new purchase order for an amount *not* less than the value of products returned under the stock rotation program. When products are returned, the associated revenue, cost of goods sold, inventory and accounts receivable originally recorded are reversed. When the new order is fulfilled, the revenue, associated cost of goods sold, inventory and accounts receivable are recorded and the product revenue is subject to the deferral analysis described below. In a small number of cases, the distributors are also permitted to return products for other business reasons.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except share and per share amounts)

Revenue from product sales to distributors is *not* recognized until the return privilege has expired or until it can be determined with reasonable certainty that the return privilege has expired, which approximates when product is sold-through to customers of the Company's distributors (dealers, system integrators, value-added resellers, and end-users) rather than when the product is initially shipped to a distributor. At each quarter-end, the Company evaluates the inventory in the channel through information provided by our distributors. The level of inventory in the channel will fluctuate up-ward or down-ward each quarter, based upon its distributors' individual operations. Accordingly, at each quarter-end, the deferral for revenue and associated cost of goods sold are 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 are deferred until the Company receives payment for the product sales made to such distributors or channel partners.

The amount of deferred cost of goods sold is included in distributor channel inventories.

The details of deferred revenue and associated cost of goods sold and gross profit are as follows:

	As of December 31,	
	2017	**2016**
Deferred revenue	$*4,635*	$*3,882*
Deferred cost of goods sold	*1,555*	*1,530*
Deferred gross profit	$*3,080*	$*2,352*

The Company offers rebates and market development funds to certain of its distributors, dealers/resellers, and end-users based upon the volume of product purchased by them. The Company records rebates as a reduction of revenue in accordance with GAAP.

The Company provides, at its discretion, advance replacement units to end-users on defective units of certain products under warranty. Since the purpose of these units is *not* revenue generating, the Company tracks the units due from the end-user, until the defective unit has been returned. Any amount due from the customer upon failure to return the products is accounted as receivable only after establishing customer's failure to return the products. The inventory due from the customer is accounted at cost or market value whichever is lower.

Sales and Similar Taxes - Taxes collected from customers and remitted to government authorities are reported on a net basis and thus are excluded from revenues.

Shipping and Handling Costs – Shipping and handling billed to customers is recorded as revenue. Shipping and handling costs are included in cost of goods sold.

Warranty Costs – The Company accrues for warranty costs based on estimated warranty return rates and estimated costs to repair. These reserve costs are classified as accrued liabilities on the consolidated balance sheets. Factors that affect the Company's warranty liability include the number of units sold, historical and anticipated rates of warranty returns, and repair cost. The Company reviews the adequacy of its recorded warranty accrual on a quarterly basis.

The details of changes in the Company's warranty accrual are as follows:

	Year Ended December 31,		
	2017	**2016**	**2015**
Balance at the beginning of year	$*246*	$*288*	$*331*
Accruals/additions	*399*	*361*	*442*
Usage/claims	*(400*)	*(403*)	*(485*)
Balance at end of year	$*245*	$*246*	$*288*

Advertising – The Company expenses advertising costs as incurred. Advertising costs consist of trade shows, magazine advertisements, and other forms of media. Advertising expenses for the years ended *December 31, 2017, 2016* and *2015* totaled *$1,079, $836,* and *$728,* respectively, and are included under the caption "Sales and Marketing".

Research and Product Development Costs – The Company expenses research and product development costs as incurred.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except share and per share amounts)

Income Taxes – The Company uses the asset and liability method of accounting for income taxes. Under the asset and liability method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, and operating loss and tax credit carry-forwards. These temporary differences will result in deductible or taxable amounts in future years when the reported amounts of the assets or liabilities are recovered or settled. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance is provided when it is more likely than *not* that some or all of the deferred tax assets *may not* be realized. The Company evaluates the realizability of its net deferred tax assets on a quarterly basis and valuation allowances are provided, as necessary. Adjustments to the valuation allowance increase or decrease the Company's income tax provision or benefit. As of *December 31, 2017* and *2016,* the Company had a valuation allowance of *$2,236* and *$1,404,* respectively against foreign net operating losses, foreign intangible assets, capital losses carryforwards, and state research and development credits.

On *December 22, 2017,* the U.S. government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act (the "Tax Act"). The Tax Act, which is generally effective for tax years beginning on *January 1, 2018,* makes broad and complex changes to the U.S. tax code, including, but *not* limited to, (*1*) reducing the U.S. federal corporate tax rate from *35* percent to *21* percent; (*2*) eliminating the corporate alternative minimum tax (AMT); (*3*) bonus depreciation that will allow for full expensing of qualified property; (*4*) creating a new limitation on deductible interest expense; (*5*) the repeal of the domestic production activity deduction; (*6*) the creation of the base erosion anti-abuse tax (BEAT), a new minimum tax; (*7*) a general elimination of U.S. federal income taxes on dividends from foreign subsidiaries and imposing a *one*-time repatriation tax on deemed repatriated earnings and profits of U.S.-owned foreign subsidiaries (the Transition Tax); (*8*) a new provision designed to tax global intangible low-taxed income (GILTI), which allows for the possibility of using foreign tax credits (FTCs) and a deduction of up to *50* percent to offset the income tax liability (subject to some limitations); and (*9*) changing rules related to uses and limitation of net operating loss carryforwards created in tax years beginning after *December 31, 2017.*

Shortly after enactment, the Securities and Exchange Commission issued Staff Accounting Bulletin *No. 118* ("SAB *118"*) which provided US GAAP guidance on the accounting for the Act's impact at *December 31, 2017.* A reporting entity *may* recognize provisional amounts, where the necessary information is *not* available, prepared or analyzed (including computations) in reasonable detail or where additional guidance is needed from the taxing authority to determine the appropriate application of the Act. A reporting entity's provisional impact analysis *may* be adjusted within the *12*-month measurement period provided for under SAB *118.*

The Transition Tax is based on the Company's post-*1986* earnings and profits (E&P) of U.S.-owned foreign subsidiaries for which the Company had previously deferred U.S. income taxes. Due to the aggregate loss position of these subsidiaries, the Company estimates that the Transition Tax will *not* result in additional U.S. tax.

The reduction in the corporate tax rate to *21* percent due to the Tax Act is effective *January 1, 2018.* Consequently, the Company has recorded a decrease related to the net deferred tax assets of approximately *$3.3* million with a corresponding net adjustment to deferred income tax expense of approximately *$3.3* million for the year ended *December 31, 2017.*

The impact of the Tax Act *may* differ from amounts currently recorded, possibly materially, during the *12*-month measurement period due to, among other things, further refinement of the Company's calculations, changes in interpretations and assumptions the Company has made, guidance that *may* be issued and actions the Company *may* take as a result of the Tax Act.

The Company follows the provisions contained in ASC Topic *740, Income Taxes.* The Company recognizes the tax benefit from an uncertain tax position only if it is at least more likely than *not* that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position.

Judgment is required in determining the provision for income taxes and related accruals, deferred tax assets and liabilities. In the ordinary course of business, there are transactions and calculations where the ultimate tax outcome is uncertain. Additionally, the Company’s tax returns are subject to audit by various tax authorities. Although the Company believes that its estimates are reasonable, actual results could differ from these estimates.

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Earnings Per Share – The following table sets forth the computation of basic and diluted earnings per common share:

	Year Ended December 31,		
	2017	**2016**	**2015**
Numerator:			
Net income/(loss)	$(14,172)	$2,444	$6,776
Denominator:			
Basic weighted average shares	8,576,588	9,021,980	9,127,385
Dilutive common stock equivalents using treasury stock method	-	284,054	467,274
Diluted weighted average shares	8,576,588	9,306,034	9,594,659
Basic earnings per common share:	$(1.65)	$0.27	$0.74
Diluted earnings per common share:	$(1.65)	$0.26	$0.71
Weighted average options outstanding	815,870	885,163	1,053,785
Anti-dilutive options not included in the computation	815,870	323,644	177,125

Share-Based Payment – We estimate the fair value of stock options using the Black-Scholes option-pricing model, which requires certain estimates, including an expected forfeiture rate and expected term of options granted. We also make decisions regarding the method of calculating expected volatilities and the risk-free interest rate used in the option-pricing model. The resulting calculated fair value of stock options is recognized as compensation expense over the requisite service period, which is generally the vesting period. When there are changes to the assumptions used in the option-pricing model, including fluctuations in the market price of our common stock, there will be variations in the calculated fair value of our future stock option awards, which results in variation in the compensation cost recognized.

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Recent Accounting Pronouncements - Recent Accounting Standards *Not* Yet Effective as of Fiscal Year End. In *May 2014,* the FASB issued ASU *2014-09,* Revenue from Contracts with Customers (Topic *606*), requiring an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The updated standard will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective and permits the use of either a full retrospective or retrospective with cumulative effect transition method. Early adoption is permitted. The updated standard becomes effective for the Company on *January 1, 2018.* The Company expects to adopt this accounting standard update on a modified retrospective basis in the *first* quarter of fiscal *2018,* and it is currently evaluating the impact of this accounting standard update on the consolidated financial statements.

In *February 2016,* the FASB issued 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 *March 2016,* the FASB issued ASU *No. 2016-09,* Compensation - Stock Compensation: Improvements to Employee Share-Based Payment Accounting. The standard is intended to simplify several areas of accounting for share-based compensation arrangements, including the income tax impact, classification on the statement of cash flows and forfeitures. ASU *2016-09* was effective for the Company on *January 1, 2017.* As a result of the adoption of ASU *2016-09,* excess tax benefits or deficiencies related to stock-based compensation are now reflected in the Consolidated Statements of Operations as a component of the provision for income taxes, whereas they previously were recognized in additional paid-in capital. In addition, our Consolidated Statements of Cash Flows will now present, on a prospective basis, excess tax benefits as an operating activity. Finally, we have elected to account for forfeitures as they occur, rather than estimate expected forfeitures.

In *August 2016,* the FASB issued 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* is effective for the Company beginning *January 1, 2018* and the Company is currently evaluating the impact that ASU *2016-15* will have on the 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 will be effective for The Company beginning *January 1, 2018* on a prospective basis, and early adoption is permitted. 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.

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2. 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 shareholders’ 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 security at *December 31, 2017* and *2016* were as follows:

	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*
December 31, 2016				
Available-for-sale securities:				
Corporate bonds and notes	$ *20,028*	$ *64*	$ *(122*)	$ *19,970*
Municipal bonds	*6,463*	*6*	*(44*)	*6,425*
Total available-for-sale securities	$ *26,491*	$ *70*	$ *(166*)	$ *26,395*

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Maturities of marketable securities classified as available-for-sale securities were as follows at *December 31, 2017:*

	Amortized cost	Estimated fair value
Due within one year	$ *2,688*	$ *2,688*
Due after one year through five years	*10,408*	*10,350*
Total available-for-sale securities	$ *13,096*	$ *13,038*

Debt securities in an unrealized loss position as of *December 31, 2017* 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. The available-for-sale marketable securities in a gross unrealized loss position as of *December 31, 2017* are summarized as follows:

	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 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*)
	$*7,140*	$ *(38*)	$*2,782*	$ *(39*)	$*9,922*	$ *(77*)

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3. Business Combinations, Goodwill and Intangible Assets

Goodwill impairment

There was a decrease in goodwill during the *twelve* months ended from *$12,724* as of *December 31, 2016* to *$0* as of *December 31, 2017* due to the impairment of goodwill. During the *third* quarter ended *September 30, 2017,* there was a decrease in the Company's market capitalization which was determined to be a triggering event for potential goodwill impairment. Accordingly, the Company performed a goodwill impairment analysis. The Company utilized the market capitalization to estimate the fair value. Our total stockholders' equity exceeded the estimated fair value. The failure of step *one* of the goodwill impairment test triggered a step *two* impairment test. As a result of step *two* of the impairment test, the Company determined the implied fair value of goodwill and concluded that the carrying value of goodwill exceeded its implied fair value as of *September 30, 2017.* Accordingly, an impairment charge of *$12,724,* which represents a full impairment charge, was recognized in the *third* quarter ended *September 30, 2017.*

Intangible Assets

Intangible assets as of *December 31, 2017,* and *2016* consisted of the following:

	Estimated useful lives (in years)	**As of December 31,**	
		2017	**2016**
Tradename	*5 to 7*	$*555*	$*555*
Patents and technological know-how	*10*	*8,578*	*6,010*
Proprietary software	*3 to 15*	*2,981*	*4,341*
Other	*3 to 5*	*323*	*324*
Total intangible assets, gross		*12,437*	*11,230*
Accumulated amortization		*(5,894*)	*(5,553*)
Total intangible assets, net		$*6,543*	$*5,677*

During the years ended *December 31, 2017, 2016* and *2015,* amortization of these intangible assets were *$932, $1,121,* and $*1,258* respectively.

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

Years ending December 31,	
2018	$*935*
2019	*831*
2020	*652*
2021	*652*
2022	*652*
Thereafter	*2,821*
Total	$*6,543*

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4. Inventories

Inventories, net of reserves, consisted of the following:

	As of December 31,	
	2017	2016
Current:		
Raw materials	$*197*	$*2,291*
Finished goods	*14,218*	*9,086*
Total	$*14,415*	$*11,377*
Long-term:		
Raw materials	$*2,682*	$*599*
Finished goods	*6,026*	*1,065*
Total	$*8,708*	$*1,664*

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 have developed programs to reduce the inventory to normal operating levels in the near future. 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.

Current finished goods do *not* include distributor channel inventories in the amounts of approximately *$1,555* and *$1,530* as of *December 31, 2017* and *2016,* respectively. Distributor channel inventories represent inventory at distributors and other customers where revenue recognition criteria have *not* been achieved.

The losses incurred on valuation of inventory at the lower of cost or market value and write-off of obsolete inventory amounted to *$649, $653* and *$496* during the years ended *December 31, 2017, 2016* and *2015,* respectively.

5. Property and Equipment

Major classifications of property and equipment and estimated useful lives were as follows:

	Estimated useful lives in years	As of December 31, 2017	2016
Office furniture and equipment	*3 to 10*	$*4,904*	$*4,835*
Leasehold improvements	*1 to 6*	*1,509*	*1,495*
Vehicles	*5 to 10*	*160*	-
Manufacturing and test equipment	*2 to 10*	*2,577*	*2,537*
		9,150	*8,867*
Accumulated depreciation and amortization		*(7,601*)	*(7,354*)
Property and equipment, net		$*1,549*	$*1,513*

Depreciation expense on property and equipment for the years ended *December 31, 2017, 2016* and *2015* was *$599, $723,* and *$801,* respectively. During the *twelve* months ended December *31, 2017* we recorded *$128* thousand for the disposal of fixed assets consisting of software, manufacturing equipment and furniture.

6. Leases and Deferred Rent

Rent expense is recognized on a straight-line basis over the period of the lease taking into account future rent escalation and holiday periods. Rent expense was *$999, $1,099* and *$1,420,* including amortization of deferred rent of *$44, $73,* and *$95* for the years ended *December 31, 2017, 2016* and *2015,* respectively.

We occupy a *5,000* square-foot facility in Gainesville, Florida under the terms of an operating lease that expires in *February 2021* with the possibility of renewing the lease for *10* more years. The Gainesville facility was used primarily to support our research and development activities.

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We lease a *4,700* square-foot office facility in Hod Hasharon, Israel under the terms of an operating lease expiring in *December 2019* which serves to support our research and development activities. Upon expiration, we will have the option to extend the lease for *two* additional years.

We currently occupy a *31,000* square-foot facility in Salt Lake City, Utah under the terms of an operating lease expiring in *May 2019,* which supports our principal administrative, sales, marketing, customer support, and research and product development activities.

We occupy a *10,700* square-foot warehouse in Shenzhen, China under the terms of an operating lease expiring in *September 2019,* which serves as our primary inventory fulfillment and repair center for Asia.

We occupy a *7,070* square-foot facility in Austin, Texas - under the terms of an operating lease expiring in *October 2019.* This facility support our administrative, sales, marketing, customer support, and research and development activities.

We occupy a *40,000* square-foot warehouse in Salt Lake City, Utah under the terms of an operating lease expiring in *April 2025,* which serves as our primary inventory fulfillment and repair center. This facility also serves as our assembly workshop for digital signage products.

Future minimum lease payments under non-cancellable operating leases with initial terms of *one* year or more are as follows:

Years ending December 31,	
2018	$ *762*
2019	*412*
2020	*182*
2021	*187*
2022	*193*

Thereafter	*472*
Total minimum lease payments	$*2,208*

7. Accrued Liabilities

Accrued liabilities consist of the following:

	As of December 31, 2017	2016
Accrued salaries and other compensation	$*1,072*	$*1,098*
Sales and marketing programs	*435*	*319*
Product warranty	*245*	*246*
Other accrued liabilities	*91*	*231*
Total	$*1,843*	$*1,894*

8. Commitments and Contingencies

We establish contingent liabilities when a particular contingency is both probable and estimable. The Company is *not* aware of any pending claims or assessments, other than as described below, which *may* have a material adverse impact on the Company's financial position or results of operations.

Outsource Manufacturers. We have manufacturing agreements with electronics manufacturing service ("EMS") providers related to the outsourced manufacturing of our products. Certain manufacturing agreements establish annual volume commitments. We are also obligated to repurchase Company-forecasted but unused materials. The Company has non-cancellable, non-returnable, and long-lead time commitments with its EMS providers and certain suppliers for inventory components that will be used in production. The Company's purchase commitments under such agreements is approximately *$3,402* as of *December 31, 2017.*

Uncertain Tax Positions. As further discussed in Note *12,* we had *$652* of uncertain tax positions as of *December 31, 2017.* Due to the inherent uncertainty of the underlying tax positions, it is *not* possible to forecast the payment of this liability to any particular year.

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Legal Proceedings.

Intellectual Property Litigation

On *April 25, 2017,* the Company was awarded a new patent, U.S. Patent *No. 9,635,186* (the *"186* Patent"), which relates to a system and method involving the combination of echo cancellation and beamforming microphone arrays. Also on *April 25, 2017,* the Company filed a lawsuit in the U.S. Federal District Court in the District of Utah against *three* parties—Shure, Inc. ("Shure"), Biamp Systems Corporation ("Biamp"), and QSC Audio Products, LLC ("QSC," together with Shure and Biamp, collectively, the "Defendants"), alleging that the Defendants were jointly and indirectly infringing the newly issued *'186* Patent (the "Infringement Action"). On that same day, Shure filed a separate action in the U.S. Federal District Court in the Northern District of Illinois (the "Illinois Action") requesting a declaratory judgment as to the invalidity or non-infringement with respect to the *'186* Patent. The Illinois Action also seeks the same declaratory judgment with respect to another Company patent, United States Patent *No. 9,264,553* (the *"553* Patent"), and which has *not* been asserted by the Company against any defendant and has been submitted to the USPTO for reissue. In early *2018,* Shure added a claim that the *'186* Patent is unenforceable.

On *May 22, 2017,* the U.S. Supreme Court issued its opinion in the TC Heartland LLC v. Kraft Foods Group Brands LLC, *No. 16–341.* That opinion changed the law on permissible venues for patent litigation from any district in which there was personal jurisdiction over a defendant to only districts in which a defendant was incorporated or had a regular and established place of business. Given that *none* of the Defendants were incorporated or had a regular and established place of business in the District of Utah, on *May 30, 2017,* the Company filed an answer to the Illinois Action and counterclaims substantially the same as those in the Company's Infringement Action, joining Biamp and QSC as counter-defendants with Shure in such counterclaims in the Illinois Action, and on *May 31, 2017,* the Company voluntarily dismissed the Infringement Action in Utah without prejudice. On *November 14, 2017* the U.S. Federal District Court in the Northern District of Illinois granted Biamp's and QSC's motions to dismiss for lack of appropriate venue and followed up with a written opinion on *March 16, 2018* consistent with its minute order on *November 14, 2017.* Also on *March 16,* the Court granted the Company's motion to dismiss Shure's declaratory judgment claim for noninfringement of the *'553* Patent.

On *July 14, 2017,* Shure filed a petition with Patent Trial and Appeals Board ("PTAB") for inter partes review against the *'553* Patent. On *January 29, 2018,* PTAB decided to institute inter partes review.

On *August 6, 2017,* the Company filed a motion seeking a preliminary injunction to enjoin the defendants from continuing to infringe on the Company's *'186* Patent. On *March 16, 2018* the Court denied the Company's motion for preliminary injunction.

On *November 7, 2017,* the U.S. Patent and Trademark Office awarded the Company U.S. Patent *No. 9,813,806* ("the *'806* Patent"). On *February 6, 2018,* the Company filed a motion for leave to file a Second Amended Counterclaim adding the *'806* Patent to the case. The Court granted the motion the next day. On *April 17,* the Company filed a motion for preliminary injunction to enjoin Shure from continuing to infringe the Company's *'806* Patent.

The Company intends to continue to vigorously enforce and defend its intellectual property rights in the Illinois Action.

During *twelve* months ended *December 31, 2016* and *2016,* the Company recorded *$408* and *$1,111* respectively, of pretax gross expenses related to this intellectual property litigation to prevent infringement of the Company's patents. In addition, the Company also capitalized *$2,289* of litigation expenses related to this matter during the *twelve* months ended *December 31, 2017.*

<u>Former Employee Litigation</u>

On or about *October 24, 2016,* the Company received written notice from the United States Department of Labor, Occupational Health and Safety Administration ("OSHA") that a complaint had been filed against it by a former employee. Among other things, the former employee's OSHA complaint alleged harassment, retaliation, and violations of *18* U.S.C.A. Section *1514A,* et seq. (the "Sarbanes-Oxley Act"), arising out of the termination of his employment with the Company on or about *August 17, 2016 (*the "OSHA Complaint"). By letter dated *March 2, 2017,* the Company received notice that the same former employee who initiated the OSHA Complaint filed a complaint with the Utah Labor Commission, Anti-Discrimination & Labor Division ("UALD"), alleging that the employee's termination was discriminatory based upon a disability or, in the alternative, retaliatory for substantially the same reasons alleged in the OSHA Complaint. The charge was also forwarded to the United States Equal Employment and Opportunity Commission ("EEOC") and was also recognized as a charge under the EEOC's federal jurisdiction.

Following negotiations between the parties, the parties executed a settlement agreement on *December 7, 2017 (*"the Agreement") with respect to the OSHA Complaint. Per the terms of the Agreement, the Company's signing of the Agreement in *no* way constitutes an admission of a violation of any law or regulation enforced by OSHA. Around the same time in *December 2017,* the parties executed a side settlement agreement by which the former employee acknowledged that he does *not* believe that the Company engaged in activities which would be construed as violations of securities-related laws and agreed to withdraw his charge against the Company from the UALD and the EEOC. The charge was effectively withdrawn on *December 6, 2017.*

During the *twelve* months ended *December 31, 2016* and *2017,* the Company recorded *$927* and *$152* respectively, of pretax gross expenses and settlement costs related to the defense of the OSHA Complaint and review of the allegations underlying the former employee's OSHA complaint. The amount recorded in *2017* is net of recoveries from the insurance company towards this matter.

The Company maintains an Employment Practices Liability policy with Chubb/Federal Insurance Company (the "EPL Policy"). Based on the allegations contained in the OSHA Complaint, the Company has tendered a claim for coverage under the EPL Policy.

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In addition, the Company is also involved from time to time in various claims and legal proceedings which arise in the normal course of our business. Such matters are subject to many uncertainties and outcomes that are *not* predictable. However, based on the information available to us, we do *not* believe any such other proceedings will have a material adverse effect on our business, results of operations, financial position, or liquidity.

Conclusion

We believe there are *no* other items that will have a material adverse impact on the Company's financial position or results of operations. Legal proceedings are subject to all of the risks and uncertainties of legal proceedings and there can be *no* assurance as to the probable result of any legal proceedings.

The Company believes it has adequately accrued for the aforementioned contingent liabilities. If adverse outcomes were to occur, our financial position, results of operations and cash flows could be negatively affected materially for the period in which the adverse outcomes are known.

9. **Share-Based Payments**

Employee Stock Option Plans

The Company's share-based incentive plans offering stock options primarily consists of *two* plans. Under both plans, *one* new share is issued for each stock option exercised. The plans are described below.

The Company's *1998* Incentive Plan (the *"1998* Plan") was the Company's primary plan through *November 2007.* Under this plan shares of common stock was made available for issuance to employees and directors. Through *December 1999, 1,066,000* options were granted that would cliff vest after *9.8* years; however, such vesting was accelerated for *637,089* of these options upon meeting certain earnings per share goals through the fiscal year ended *June 30, 2003.* Subsequent to *December 1999* and through *June 2002, 1,248,250* options were granted that would cliff vest after *6.0* years; however, such vesting was accelerated for *300,494* of these options upon meeting certain earnings per share goals through the fiscal year ended *June 30, 2005.*

The Company's *2007* Equity Incentive Plan (the *"2007* Plan") was restated and approved by the shareholders on *December 12, 2016.* 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.

Of the options granted subsequent to *June 2002,* all vesting schedules are based on *3* or *4*-year vesting schedules, with either *one-third* or *one-fourth* vesting on the *first* anniversary and the remaining options vesting ratably over the remainder of the vesting term. Generally, directors and officers have *3*-year vesting schedules and all other employees have *4*-year vesting schedules. Additionally, in the event of a change in control or the occurrence of a corporate transaction, the Company's Board of Directors has the authority to elect that all unvested options shall vest and become exercisable immediately prior to the event or closing of the transaction. All options outstanding as of *December 31, 2017* had contractual lives of *ten* years.

Under the *1998* Plan, *2,500,000* shares were authorized for grant. As of *December 31, 2017,* there were *no* options outstanding under the *1998* Plan.

As of *December 31, 2017,* there were *764,430* options outstanding under the *2007* Plan. As of *December 31, 2017,* the *2007* Plan had *774,456* authorized unissued options, while there were *no* options remaining that could be granted under the *1998* Plan.

The Company uses judgment in determining the fair value of the share-based payments on the date of grant using an option-pricing model with assumptions regarding a number of highly complex and subjective variables. These variables include, but are *not* limited to, the risk-free interest rate of the awards, the expected life of the awards, the expected volatility over the term of the awards, and the expected dividends of the awards. The Company uses the Black-Scholes option pricing model to determine the fair value of share-based payments granted under the guidelines of ASC Topic *718.*

In applying the Black-Scholes methodology to the options granted, the Company used the following assumptions:

	Year ended December 31,		
	2017	**2016**	**2015**
Risk-free interest rate, average	*2.21* %	*1.52* %	*2.00* %
Expected option life, average (in years)	*7.9*	*6.1*	*6.1*
Expected price volatility, average	*40.71*%	*43.75*%	*44.30*%
Expected dividend yield	*2.83* %	*1.71* %	*1.10* %

The risk-free interest rate is determined using the U.S. Treasury rate in effect as of the date of the grant, based on the expected life of the stock option. The expected life of the stock option is determined using historical data.

The expected price volatility is determined using a weighted average of daily historical volatility of the Company's stock price over the corresponding expected option life.

Under guidelines of ASC Topic *718,* the Company recognizes the associated compensation cost for only those awards expected to vest on a straight-line basis over the underlying requisite service period. The Company estimated the forfeiture rates based on its historical experience and expectations about future forfeitures.

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The following table shows the stock option activity:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value
As of December 31, 2014	*1,040,081*	$ *5.65*	*5.60*	$ *4,286*
Granted	*56,666*	*13.03*		
Reinstated	*4,583*	*4.47*		
Expired and canceled	*(1,000*)	*3.42*		
Forfeited prior to vesting	*(15,252*)	*7.85*		
Exercised	*(56,143*)	*5.51*		
As of December 31, 2015	*1,028,935*	$ *6.03*	*4.73*	$ *7,104*
Granted	*217,700*	*11.73*		
Expired and canceled	*(4,186*)	*12.03*		
Forfeited prior to vesting	*(17,360*)	*10.67*		
Exercised	*(374,857*)	*4.46*		
As of December 31, 2016	*850,232*	$ *8.06*	*5.78*	$ *3,001*
Granted	*105,000*	*9.90*		
Expired and canceled	*(3,144*)	*10.29*		
Forfeited prior to vesting	*(8,996*)	*11.01*		
Exercised	*(178,662*)	*5.90*		
As of December 31, 2017	*764,430*	$ *8.78*	*6.48*	$ *1,038*
Vested and Expected to Vest at December 31, 2015	*1,028,935*	$ *6.03*	*4.73*	$ *7,104*
Vested at December 31, 2015	*820,022*	$ *5.10*	*3.74*	$ *6,419*
Vested and Expected to Vest at December 31, 2016	*850,232*	$ *8.06*	*5.78*	$ *3,001*
Vested at December 31, 2016	*552,097*	$ *6.33*	*4.09*	$ *2,843*
Vested and Expected to Vest at December 31, 2017	*764,430*	$ *8.78*	*6.48*	$ *1,038*
Vested at December 31, 2017	*529,669*	$ *7.89*	*5.50*	$ *1,033*

The weighted average per share fair value of options granted during the years ending *December 31, 2017, 2016* and *2015* was *$3.31, $4.27,* and $ *5.27* respectively. The total intrinsic value of options exercised during the years ended *December 31, 2017, 2016* and *2015* was *$646, $2,824,* and *$404* respectively.

The total pre-tax compensation cost related to stock options recognized during the years ended *December 31, 2017, 2016,* and *2015* was *$665, $667* and *$848,* respectively. Tax benefit from compensation cost related to stock options during the years ended *December 31, 2017, 2016* and *2015* was *$0, $107* and *$41,* respectively. As of *December 31, 2017,* the total compensation cost related to stock options *not* yet recognized and before the effect of any forfeitures was *$829,* which is expected to be recognized over approximately the next *1.80* years on a straight-line basis.

Employee Stock Purchase Plan

During *2017,* the Company issued shares to employees under the Company's *2016* Employee Stock Purchase Plan (the "ESPP"). The ESPP was approved by the Company's shareholders on *December 12, 2016.* As of *December 31, 2017, 466,783* of the originally approved *500,000* shares were available for offerings under the ESPP. Offering periods under the ESPP commence on each *Jan 1* and *July 1,* and continue for a duration of *six* months. The ESPP is available to all employees who do *not* own, or are deemed to own, shares of stock making up an excess of *5%* of the combined voting power of the Company, its parent or subsidiary.

During each offering period, each eligible employee *may* purchase shares under the ESPP after authorizing payroll deductions. Under the ESPP, each employee *may* purchase up to the lesser of *2,500* shares or *$25* of fair market value (based on the established purchase price) of the Company's stock for each offering period. Unless the employee has previously withdrawn from the offering, his or her accumulated payroll deductions will be used to purchase common stock on the last business day of the period at a price equal to *85%* (or a *15%* discount) of the fair market value of the common stock on the *first* or last day of the offering period, whichever is lower.

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Shares purchased and compensation expense associated with Employee Stock Purchase Plans were as follows:

	2017	**2016**	**2015**
Shares purchased under ESPP plans	*9,110*	*9,140*	*14,982*
Plan compensation expense	$*13*	$*18*	$*31*

Stock Repurchase Program and Cash Dividends

In *May 2012,* our Board of Directors authorized a stock repurchase program to purchase the Company's common stock in the open market. A total of *272,767* shares costing *$2,598* were purchased under this program during the year ended *December 31, 2014.* The cost of shares purchased were recorded as a reduction to shareholders' equity. On *December 2, 2016,* the Company announced the discontinuance of the stock repurchase program along with the initiation of a cash dividend plan.

On *March 9, 2016,* the Board of Directors of the Company authorized the repurchase of up to *$10* million of the Company's outstanding shares of common stock under a new 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 repurchase program *may* be suspended or discontinued at any time without prior notice. 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* million 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 repurchase program *may* be suspended or discontinued at any time without prior notice. The transactions effectuated to date occurred in open market purchases. This program terminated in March 2018.

During the *twelve* months ended *December 31, 2017,* we acquired the following shares of common stock under the stock repurchase program authorized by the Board of Directors in March 2016 and renewed and extended in March 2017:

$ in thousands except per share price	**Total Number of Shares Purchased (a)**	**Average Price Paid per Share (b)**	**Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (c)**	**Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs ($ thousands) (d)**
January 1 to March 31	*78,956*	$ *11.75*	*78,956*	$ *9.9*
April 1 to June 30	*214,866*	*9.91*	*214,866*	*7.7*
July 1 to September 30	*139,570*	*7.84*	*139,570*	*6.6*
October 1 to December 31	*118,544*	*8.18*	*118,544*	*5.7*
Total	*551,936*	$ *9.28*	*551,936*	

From *March 11, 2016* to *March 17, 2016,* the Company offered to repurchase eligible vested options to purchase shares under the *1998* Plan and the *2007* Plan from employees and directors. The Company repurchased delivered options at a repurchase price equal to the difference between the closing market price on the date of the employee's communication of accepting the repurchase offer and the exercise price of such employee's delivered options, subject to applicable withholding taxes and charges. The Company repurchased *225,542* stock options from employees and directors at an average purchase price of *$7.77.*

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10. Significant Customers

Sales to significant customers that represented more than *10* percent of total revenues are as follows:

	Year ended December 31,		
	2017	**2016**	**2015**
Customer A	*16.1%*	*16.3%*	*14.2%*
Customer B	- %*	- %*	*10.4%*
Total	*16.1%*	*16.3%*	*24.6%*

* Sales did *not* exceed *10%* of the revenue.

The following table summarizes the percentage of total gross accounts receivable from significant customers:

	As of December 31,	
	2017	**2016**
Customer A	*20.3%*	*13.4%*
Customer B	*11.0%*	*11.7%*
Total	*31.3%*	*25.1%*

These customers facilitate product sales to a large number of end-users, *none* of which is known to account for more than *10* percent of the Company's revenue from product sales. Nevertheless, the loss of *one* or more of these customers could reduce revenue and have a material adverse effect on the Company's business and results of operations.

11. 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 quoted prices in active markets or based on other observable inputs. The following tables set forth the fair value of the financial instruments re-measured by the Company as of *December 31, 2017* and *2016:*

	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*
December 31, 2016				
Corporate bonds and notes	$ —	$*19,970*	$ —	$*19,970*
Municipal bonds	—	*6,425*	—	*6,425*
Total	$ —	$*26,395*	$ —	$*26,395*

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12. Income Taxes

Consolidated income before taxes for domestic and foreign operations consisted of the following:

	Year ended December 31,		
	2017	**2016**	**2015**
Domestic	$*(12,630)*	$*6,332*	$*13,295*
Foreign	*(3,263)*	*(2,454)*	*(2,744)*
Total	$*(15,893)*	$*3,878*	$*10,551*

The Company's (provision) for income taxes consisted of the following:

	Year ended December 31,		
	2017	**2016**	**2015**
Current:			
Federal	$*577*	$*(593)*	$*(3,386)*
State	*(66)*	*63*	*(344)*
Foreign	*(682)*	*(37)*	-
Total current	*(171)*	*(567)*	*(3,730)*
Deferred:			
Federal	*1,497*	*(633)*	*(220)*
State	*480*	*(17)*	*(10)*
Foreign	*748*	*115*	*470*
Total	*2,725*	*(535)*	*240*
Change in valuation allowance	*(833)*	*(332)*	*(285)*
Total deferred	*1,892*	*(867)*	*(45)*
Benefit/(provision) for income taxes	$*1,721*	$*(1,434)*	$*(3,775)*

The income tax benefit (provision) differs from that computed at the federal statutory corporate income tax rate as follows:

	Year ended December 31,		
	2017	2016	2015
Tax benefit (provision) at federal statutory rate	$5,403	$(1,318)	$(3,587)
State income tax benefit (provision), net of federal benefit	439	(148)	(408)
Research and development tax credits	411	423	456
Subpart F inclusion	(370)	-	-
Foreign earnings or losses taxed at different rates	(540)	(292)	(231)
Tax rate change	(3,161)	-	-
Other	372	233	280
Change in valuation allowance	(833)	(332)	(285)
Tax benefit (provision)	$1,721	$(1,434)	$(3,775)

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The tax effects of significant temporary differences representing net deferred tax assets and liabilities consisted of the following:

	2017	**2016**
Deferred revenue	$*738*	$*845*
Basis difference in intangible assets	*3,403*	*(56*)
Inventory reserve	*2,089*	*2,650*
Net operating loss carryforwards	*1,627*	*1,391*
Research and development tax credits	*163*	*88*
Accrued expenses	*75*	*92*
Stock-based compensation	*327*	*584*
Allowance for sales returns and doubtful accounts	*119*	*70*
Difference in property and equipment basis	*(212*)	*(350*)
Other	*438*	*743*
Total net deferred income tax asset	*8,767*	*6,057*
Less: Valuation allowance	*(2,236*)	*(1,403*)
Net deferred income tax asset (liability)	$*6,531*	$*4,654*

The Company has *not* provided for U.S. deferred income taxes or foreign withholding taxes on undistributed earnings of its non-U.S. subsidiaries since these earnings are intended to be reinvested indefinitely, in accordance with guidelines contained in ASC Topic *740, Accounting for Income Taxes*. It is *not* practical to estimate the amount of additional taxes that might be payable on such undistributed earnings.

In accordance with ASC Topic *740,* the Company analyzed its valuation allowance at *December 31, 2017* and determined that, based upon available evidence, it is more likely than *not* that certain of its deferred tax assets *may not* be realized and, as such, has established a valuation allowance against certain deferred tax assets. These deferred tax assets include foreign net operating loss carryforwards, foreign intangible assets, state R&D tax credit carryforwards, and capital loss carryforwards.

The Company has federal net operating loss (“NOL”) carryforwards of approximately *$692* (pre-tax), and Spain NOL carryforwards of approximately *$5,805.* The federal NOL carryforwards will begin to expire in *2029.* The Spain NOL carryforward does *not* expire.

Effective *July 1, 2007,* the Company adopted the accounting standards related to uncertain tax positions. This standard requires that tax positions be assessed using a *two*-step process. A tax position is recognized if it meets a "more likely than *not"* threshold, and is measured at the largest amount of benefit that is greater than *50* percent likely of being realized. Uncertain tax positions must be reviewed at each balance sheet date. Liabilities recorded as a result of this analysis must generally be recorded separately from any current or deferred income tax accounts.

The total amount of unrecognized tax benefits at *December 31, 2017* and *2016,* that would favorably impact our effective tax rate if recognized was *$647* and *$588,* respectively. As of *December 31, 2017* and *2016,* we accrued *$14* and *$87,* respectively, in interest and penalties related to unrecognized tax benefits. We account for interest expense and penalties for unrecognized tax benefits as part of our income tax provision.

Although we believe our estimates are reasonable, we can make *no* assurance that the final tax outcome of these matters will *not* be different from that which we have reflected in our historical income tax provisions and accruals. Such difference could have a material impact on our income tax provision and operating results in the period in which we make such determination.

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A reconciliation of the beginning and ending amount of liabilities associated with uncertain tax positions is as follows:

	Year ended December 31,	
	2017	**2016**
Balance - beginning of year	$*1,189*	$*1,126*
Additions based on tax positions related to the current year	*67*	*16*
Additions for tax positions of prior years	*520*	*47*
Reductions for tax positions of prior years	-	-
Settlements	*(165*)	-
Lapse in statutes of limitations	*(959*)	-
Uncertain tax positions, ending balance	$*652*	$*1,189*

The Company's U.S. federal income tax returns for *2014* through *2017* are subject to examination. The Company also files in various state and foreign jurisdictions. With few exceptions, the Company is *no* longer subject to federal, state, or non-U.S. income tax examinations by tax authorities for years prior to *2014.* The Company completed its audit by the Internal Revenue Service ("IRS") for its *2012* and *2013* tax returns in *2017.* As a result of the audit by the IRS, there were *no* material adjustments made to the Company's tax return.

The Inland Revenue Department of Hong Kong, a Special Administrative Region (the "IRD"), commenced an examination of the Company's Hong Kong profits tax returns for *2009* through *2011* in the *fourth* quarter of *2012,* which was completed subsequent to *December 31, 2017.* As a result of the audit, there were *no* material changes to the Company's financial position. During the next *twelve* months, it is reasonably possible that the amount of the Company's unrecognized income tax benefits could change significantly. These changes could be the result of our ongoing tax audits or the settlement of outstanding audit issues. However, due to the issues being examined, at the current time, an estimate of the range of reasonably possible outcomes cannot be made, beyond amounts currently accrued.

13. Geographic Sales Information

The United States was the only country to contribute more than *10* percent of total revenues in each fiscal year. The Company's revenues are substantially denominated in U.S. dollars and are summarized geographically as follows:

	Year ended December 31,		
	2017	**2016**	**2015**
United States	$*24,569*	$*31,838*	$*39,563*
All other countries	*17,235*	*16,799*	*18,233*
Total	$*41,804*	$*48,637*	$*57,796*

***14.* Subsequent Events**

On *February 21, 2018,* the Company declared a stock dividend of *$0.07* per share of ClearOne common stock payable on *March 21, 2018* to shareholders of record on *March 7, 2018.*

In *March 2018,* the Company did *not* renew its common stock repurchase program.